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THE THURSDAY REPORT

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Re: The Easter Report

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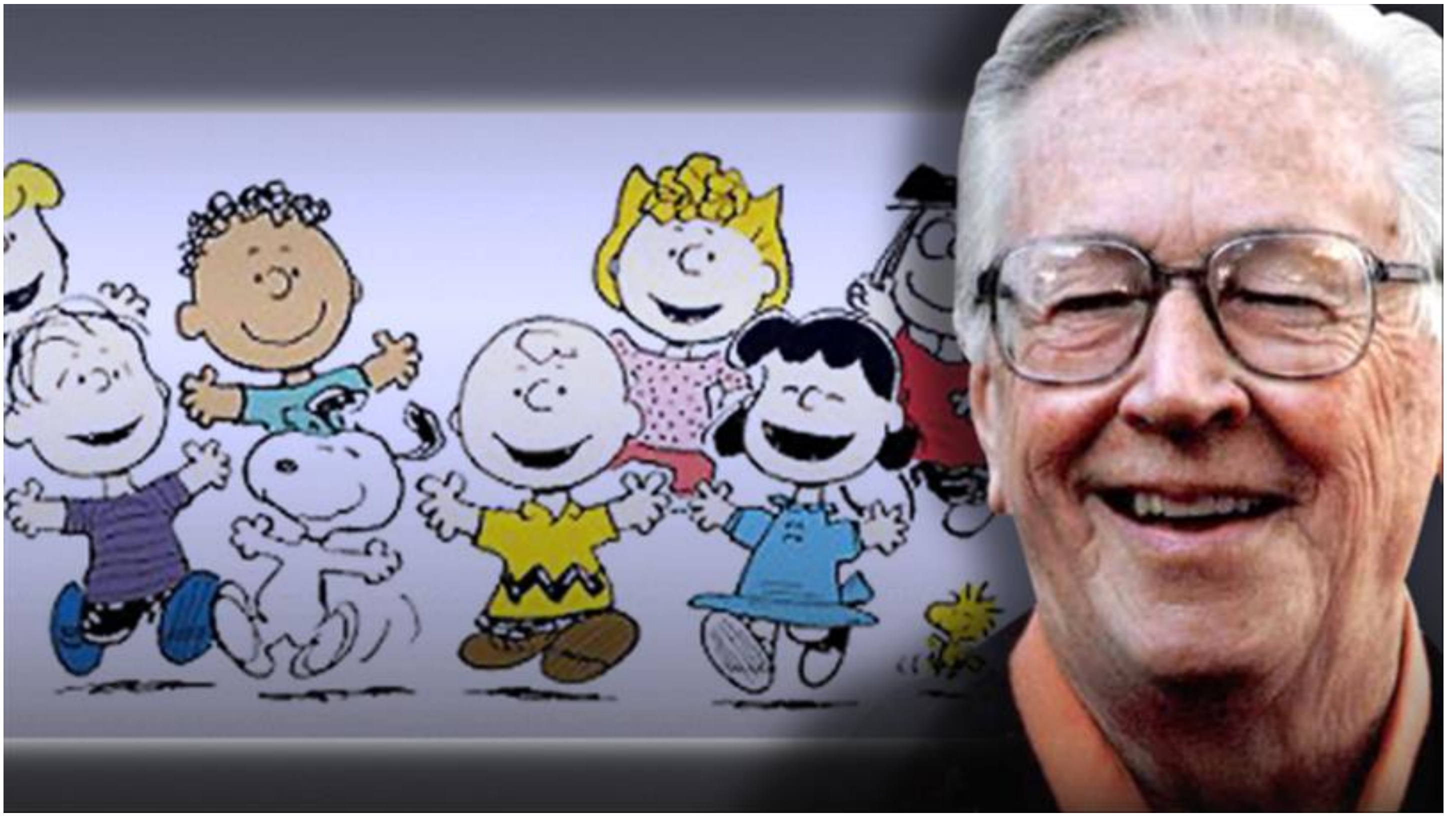
We welcome contributions for future Thursday Report topics. If you are interested in making a contribution as a guest writer, please email Alan at agassman@gassmanpa.com

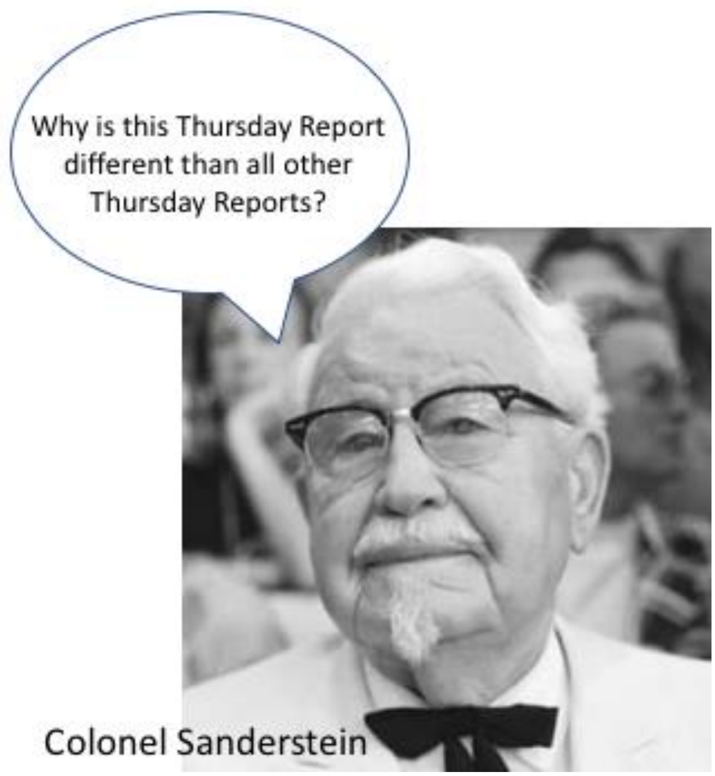
This week marks the beginning of spring and as Robin Williams once said, "Spring is nature's way of saying, Let's party!" However, for us Floridians it also means you can run, you can hide, but the pollen will find you.

Quote of the Week



All you need is love…But a little chocolate now and then doesn't hurt

-Charles M. Schulz



ABA Webinar Clarifies Issues but Provides Unpleasant Surprises for Tax Practitioners

By Alan Gassman and Brandon Ketron

EXECUTIVE SUMMARY:
On April 4, 2019 an ABA Webinar entitled *Recent 199A Guidance: Hear from Practicing Experts and Government Officials* was presented by LISI commentator, Steve Gorin and Bob Keebler along with Treasury Department attorneys Audrey Ellis and Wendy Kribell, to review many Section 199A issues.

The discussion included some very important points that all practitioners who are navigating under Section 199A should be aware of, including which attribution rules apply under the related party provisions, how an aggregation election made by an S-corporation or entity taxed as a partnership can be damaging to partners and shareholders, if and when taxpayers would ever be required to keep separate books and records when SSTB and non-SSTB activities are conducted under a single taxable entity, and whether beneficiaries who receive distributions from a complex trust can qualify for the Section 199A deduction with respect to SSTB or low wage / UBIA income when the Grantor of the Trust is a high income bracket taxpayer.

LISI commentators, Alan Gassman and Brandon Ketron, thank the presenters of this excellent Webinar for their hard work and commentary, and have summarized what was discussed and expounded thereon for LISI readers.

FACTS:
Section 199A of the Internal Revenue Code was enacted effective January 1, 2018 to enable individual taxpayers and certain trusts and estates to receive a deduction equal to up to 20% of "Qualified Business Income."

Qualified Business Income received from a Specified Service Trade or Business ("SSTB") or an entity that does not have sufficient wages or unadjusted basis ("UBIA") from Qualified Property will not qualify for the deduction if received by high income bracket taxpayers.

The April 4, 2019 Webinar, which follows issuance of January 18, 2019 Final Regulations and February 4, 2019 Corrected Final Regulations along with Steve Gorin's amazing 1,900 page white paper on corporate and business planning that includes hundreds of pages of discussion of Section 199A are significant game changers for a great many advisors who have Section 199A issues and decisions to make. It was pointed out early in the Webinar that the statements made by the IRS lawyers were their own personal opinion, and not the official position of the IRS, although it is clear that IRS personnel will be guided to some extent by these comments, and that they were provided in order to enable tax advisors to understand how the statute works.

The basic items of discussion under the Webinar, and covered in this newsletter, are as follows:

1. Income distributed from a complex trust to a beneficiary will be aggregated with the income of the Grantor for purposes of measuring the $157,500/$315,000 exemption.

2. An entity level aggregation election can cause harm to individual partners or S-corporation owners.

3. The related party rules will include not only Sections 267(b) and 707(b), as explicitly mentioned in the Final Regulations, but will also include Section 267(c), by reason of specific incorporation under subsection 267(b)(1) and Section 267(c).

4. The Internal Revenue Code Section 3121(d) "Statutory Employee" Rule that applies to life insurance agents will not prevent life insurance agents or agencies from being considered to be independent contractors if the other employee versus independent contractor tests are met, and compensation paid to independent contractor life insurance agents can be considered as wages under the 20% wage test if the life insurance agent is properly characterized as an employee under the employee versus independent contractor rules.

COMMENT:

Confusion will continue to exist with respect to the definition of "active trade or business" and what activities can be grouped together to determine whether the cumulative level of activity will be considered sufficient for this purpose.

This is completely different than the question of what trades and businesses can be aggregated for purposes of cumulatively applying wages and the unadjusted basis (UBIA) of property to determine if high income taxpayers can receive a deduction.

On the question of if an when different trades or businesses can be aggregated to determine whether the level of activity is sufficient to satisfy the "active trade or business" requirement, the following rules apply:

1. A landlord, who is the owner or is considered as related to the owner or owners of an active trade or business, will be considered to be active and will therefore, pass the Section 162 test even if it is a triple net lease, although the rent income will be considered to be SSTB income if the rental income is from a related SSTB and the taxpayer will not qualify for the deduction if income exceeds the $157,500/$315,000 thresholds as adjusted for inflation.

2. A single or married taxpayer, S corporation, or partnership that owns multiple commercial or residential properties directly, or through one or more disregarded LLCs, cannot group residential and commercial properties together under the Aggregation Rule for purposes of applying the Wage/QP Test, according to Example 17 of Section 1.199A-4(b) to the Final Regulations, which provides as follows:

(17) Example 17 to paragraph (d). (i) Facts. S, an S corporation owns 100% of the interests in a residential condominium building and 100% of the interests in a commercial rental office building. Both building operations share centralized accounting, legal, and human resource functions.

(ii) Analysis. S owns more than 50% of each trade or business thereby satisfying paragraph (b)(1)(i) of this section. Although both businesses share significant centralized business elements, S cannot show that another factor under paragraph
(b)(1)(v) of this section is present because the two building operations are not of the same type of property. S must treat the residential condominium building and the commercial rental office building as separate trades or businesses for purposes of
applying §1.199A-1(d).

An exception to this may apply under sub-Section 1.199A-4(b)(v)(B) and (C) if the residential and commercial properties are integrated, such as if a building is shared by the trades or businesses, the trades or businesses share significant centralized business elements (i.e. personnel, accounting, or information technology resources), or if the trades or businesses are operated in coordination with, or reliance upon, one or more of the businesses in the aggregated group. An example of this may include a store on the first floor and an apartment on the second floor that are normally rented out together to the store owner or a residential apartment building that has a floor of commercial businesses that primarily services the residents of the building.

3. When the same taxpayers own multiple S corporations or partnerships that have exact or similar common ownership and separate rental properties or other businesses, these S corporations or

partnerships cannot be aggregated to determine whether the level of activity reaches the definition of an active trade or business, even if they can be aggregated for wage and qualified property measurement purposes.

Separate or "Separable" Books and Records Requirement

The Treasury Department and IRS have indicated by statements in the Preamble that separate trades or businesses must at a minimum meet the requirements to be permitted to maintain separate books and records, even though separate books and records may not actually have to be kept, separate books and records in order to allow non-SSTB SSTB services to not be considered as SSTB services where more than 10% of income under an entity comes from SSTB service.

Although not specifically mentioned in the statute or the Final Regulations, the examples seem to indicate that the only safe way to assure that taxable income attributable to Non-SSTB income will be considered separate from SSTB income under the same taxable entity will be for taxpayers to maintain separate books and records for non-SSTB services when revenues from an SSTB activity in the same entity exceed 10% of an entity's gross revenues if revenues are less than $25,000,000, or 5% of revenues if revenues exceed $25,000,000, although having "separable" books and records should be sufficient.

Many believe that the drafters of the Regulations thought that the Section 446 regulations required separate books and records, but then discovered that this was not the case, and did not see the change to the language of the Preamble to the Final Regulations when they were re-issued on February 4th, which points out that the Internal Revenue Code Section 446 Regulations provide that "no trade or business is considered separate and distinct unless a complete and separable set of books and records is kept for that trade or business," as per the following language:

The Treasury Department and the IRS also believe that multiple trades or businesses will generally not exist within an entity unless different methods of accounting could be used for each trade or business under §1.446 1(d). Section 1.446- 1(d) explains that no trade or business is considered separate and distinct unless a complete and separable set of books and records is kept for that trade or business. Further, trades or businesses will not be considered separate and distinct if, by reason of maintaining different methods of accounting, there is a creation or shifting of profits and losses between the businesses of the taxpayer so that income of the taxpayer is not clearly reflected.

Although this cannot be cited as authority and was only explained in the recent ABA webinar with two Treasury officials (it was mentioned that their statements were their own personal views and not the views of the Treasury or the IRS) Audrey Ellis of the Office of Tax Policy of the Treasury apologized for the confusion and stated that separate books and records do not actually have to be created as long as they are separable, meaning that an accountant would be able to use the records kept to create separate books and records in the future to verify the allocation of income and expenses that is used. As a practical matter, it seems that until further guidance is issued, taxpayers will be safer maintaining separate books and records so that it is clear that the identities of SSTB and Non-SSTB income are separate and well organized.

It is noteworthy that the example in the Final Regulations further mentions that the non-SSTB activity has separate employees that are not affiliated with the SSTB activity, and that the taxpayer has treated the activities as a separate trade or business in all respects, although these additional formalities do not appear to be required under the Section 446 Regulations cited above.

Complex Trust Anti- Abuse Rules

The Proposed Regulations had unusual language which provided that certain trusts would be "disrespected" for Section 199A purposes if they were established for the purpose of avoiding tax under Section 199A. The Final Regulations clarify that the anti-abuse rule is designed to "thwart the creation of even one single trust with a principal purpose of avoiding, or using more than one, threshold amount."

The Final Regulations indicate that if the trust is created or funded for "a principal purpose" of avoiding tax under Section 199A, then the trust income will be aggregated with the grantor or other trusts from which it was funded for purposes of determining the threshold amount for calculating the Section 199A deduction.

Specifically, the Regulation reads as follows:

Anti-abuse rule for creation of a trust to avoid exceeding the threshold amount. A trust formed or funded with a principal purpose of avoiding, or of using more than one, threshold amount for purposes of calculating the deduction under Section 199A will not be respected as a separate trust entity for purposes of determining the threshold amount for purposes of Section 199A.

The Final Regulations provide no examples and give no further guidance with respect to this, and many experts do not believe that the above language will cause income distributed by a Complex Trust to a low-income beneficiary to not qualify as being under the $157,500 threshold, notwithstanding the following:

In an April 4, 2019 ABA webinar with two Treasury officials , an example was discussed where a mother had gifted part ownership in a business earning $400,000 of income to her son so that the mother was then considered to have $200,000 of income and the son was considered to have $200,000 of income. The example explained that the gift was directly to the son, solely for the purposes of qualifying income for the Section 199A deduction, and that there is no anti-abuse rule to prevent this type of planning. The example then explained that if the gift of the 50% interest in the business was to a Complex Trust for the benefit of the son and the trust was established for the purpose of avoiding tax under Section 199A, then the trust would be disregarded for purposes of determining the threshold and the $200,000 of income allocated to the trust would be aggregated with the Grantor of the trust (the mother), so that the mother would be considered to have $400,000 of Section 199A income. As a result of this, none of the mother's income would be eligible for the Section 199A deduction. The trust would still be taxed on the $200,000 of income, or on the income that was not distributed out to the beneficiaries, and the Treasury officials declined to comment on whether or not the income of the trust, or income distributed from the trust would be able to take the Section 199A deduction.

As a result of the above, more tax planners will recommend the use of a Section 678 trust, which enables all of the income earned by the trust to be taxed as if it was actually earned by an individual who had the right to make a withdrawal of all principal or income from the trust.

Aggregation

The Final Regulations also give partnerships, S corporations or other entities (referred to in the Final Regulations as Relevant Pass Through Entities, or RPEs) owning multiple trades or businesses by direct ownership or subsidiaries the ability to make an aggregation election at the entity level, if the requirements for aggregation are met by the RPE. The election made by the RPE should be carefully considered, because it will be binding upon all of the individual owners of the RPE. Although individual owners include trades or businesses that are aggregated by the RPE, such owners can aggregate additional trades or businesses with the RPE's aggregation, assuming that the other requirements for aggregation are met.

While making such an election may simplify tax reporting for the partners or S-corporation owners, it can also cause loss of Section 199A tax savings by eliminating aggregation options that an individual partner or S-corporation owner would otherwise have.

For example, if Taxpayer A has a food business and also owns 60% of a partnership that operates both a movie theater and a food business, then Taxpayer A may aggregate his personally owned food business with the food business of the partnership, due to the fact that they are the same type of products and services and share centralized business elements. On the other hand, [i]f the partnership makes an aggregation election to combine the movie theater with the partnership's food business (since they are operated in coordination with each other and share centralized business elements), then the individually owned food service cannot be aggregated with the combined movie theater and food business due to the fact that the individually owned food business is not considered the same type of product or service as the combined movie theater and food operations, and therefore the requirements for aggregation cannot be met.

This is illustrated in the following example contained in the Final Regulations:

(i) Facts:
PRS1, a partnership, directly operates a food service trade or business and owns 60% of PRS2, which directly operates a movie theater trade or business and a food service trade or business. PRS2's movie theater and food service businesses operate in coordination with, or reliance upon, one another and share a centralized human resources department, payroll, and accounting department. PRS1's and PRS2's food service businesses provide products and services that are the same and share centralized purchasing and shipping to obtain volume discounts.

(ii) Analysis:

PRS2 may aggregate its movie theater and food service businesses. Paragraph (b)(1)(v) of this Section is satisfied because the businesses operate in coordination with one another and share centralized business elements. If PRS does aggregate the two businesses, PRS1 may not aggregate its food service business with PRS2's aggregated trades or businesses. Because PRS1 owns more than 50% of PRS2, thereby satisfying paragraph (b)(1)(i) of this section, PRS1 may aggregate its food service businesses with PRS2's food service business if PRS2 has not aggregated its movie theater and food service businesses. Paragraph (b)(1)(v) of this Section is satisfied because the businesses provide the same products and services and share centralized business elements. Under either alternative, PRS1's food service business and PRS2's movie theater cannot be aggregated because there are no factors in paragraph (b)(1)(v) of this Section present between the businesses.

Lawyers who are drafting or updating entity agreements may wish to prohibit the entity from making an aggregation election without the consent of all or substantially all of the owners, or may alternatively specifically provide that no officer, manager or director will have a fiduciary duty to aggregate or not aggregate.

Related Party Attribution Rules

The Section 267(b) and Section 707(b) ownership attribution rules are used and ownership by spouses, as well as children, grandchildren, parents, and siblings, can be attributed to each other. Under the Proposed Regulations, siblings would not have been considered as having been related.
In addition, the constructive attribution rules in Section 267(c) and the other provisions of Section 267 regarding attribution will also apply to determine whether the 50% common ownership test is met, although most advisors were not aware of this until it was clarified as a part of the April 4, 2019 ABA Webinar. The inclusion of Section 267(c) causes ownership of family members in all entities, and ownership of corporate stock (but not partnership interests) by partners of the taxpayer to be considered as constructively owned by the taxpayer (so that the rules will now apply to potentially cause individuals who own minority interests in a corporation to be considered as related to other entities by reason of the existence of a partnership with another shareholder when they would otherwise not be considered as related because now the individual is considered to constructively own the stock of his or her partner). In addition, ownership by partnerships, corporations, estates, and trusts will be attributed to the individual partner, stockholder, or beneficiary for purposes of applying the attribution rules.

Treatment of Life Insurance Agents

The webinar also mentioned that life insurance agents who are Independent Contractors are treated differently under the employment tax rules, pursuant to Internal Code Section 3121(d) and Treasury Regulation 31.3121(d)-1(d)(3)(ii), (and as verified by Revenue Ruling 69-287 and Private Letter Ruling 9242003), which defines certain Independent Contractors as “Statutory Employees” for the purposes of assuring that employers withhold Social Security and Medicare taxes on their own compensation.

Under this statute, a full-time life insurance sales agent who is otherwise treated as an Independent Contractor will be subject to this definition and these requirements, if his or her principal business activity is selling life insurance or annuity contracts, or both, primarily for one life insurance company, and all three of the following conditions are met:

1. The service contract states or implies that substantially all of the services are to be performed personally by the individual.

2. The individual does not have a substantial investment in the equipment and property used to perform the services (other than his or her automobile or other "transportation facilities."

3. The services are performed on a continuing basis for the same employer.

If the life insurance sales person is an Independent Contractor under the normal tests, then his or her income will qualify for the Section 199A deduction as non-SSTB income, as long as it is appropriately documented as being separate and apart from income derived as an employee, and any income derived from being an investment broker or advisor, which is an SSTB activity. These separate or separable books and records requirement discussed above will apply under those circumstances.

<u>Conclusion</u>

The new views described above came as a surprise to many of us and show that the process of writing and understanding complex and voluminous regulations on short notice is an inexact science at best. Hopefully some of these views will change over time after consideration that the actual language of the Final Regulations does not seem to support all of these positions.

Separating Out the Aggregation Rules Under Section 199A

By: Alan Gassman and Brandon Ketron

IRC Section 199A provides a tax deduction of up to 20% on Qualified Business Income, which is the income that an individual taxpayer, trust or estate receives by reason of ownership and operation of a trade or business that is owned individually, under a disregarded LLC, or by an entity taxed as a S-corporation or a partnership.

Many complicated rules apply under Section 199A, and the complexity is increased when a high earner taxpayer (an individual or trust with more than $157,500 or a married couple with more than $315,000 of taxable income, as adjusted for inflation) because qualified business income from a Specified Service Trade or Business or from any trade or business that does not pay sufficient wages and/or have sufficient "unadjusted basis" in the trade or business will be limited as to deductibility.

In many situations, individual taxpayers and trusts are involved with multiple trades and businesses, which may be aggregated in order to qualify for deductibility that would otherwise not apply.

There are multiple types of Aggregation that can apply, and they are easy to confuse:

1. Active Trade or Business Test. An individual, trust, S-corporation or partnership may own multiple trades or businesses or have multiple rental properties or other activities that would not be considered

to be active or entrepreneurial enough to qualify separately as a "trade or business," but which may meet the definition of an "active trade or business" when considered as a group.

Under this "Aggregation" rule, the question is whether the separate items or activities all belong to the same individual or entity.

Whether a trade or business exists is measured at the individual level or at the Relevant Pass Through Entity (RPE) level.

For example, an individual or trust may own 10 LLCs that are each disregarded for income tax purposes, so that the individual or trust is considered to own 10 rental properties.

The individual or the trustee of the trust may spend 10 hours a year on average with respect to rental services, and may have an employee and also one or two contractors who themselves spend 20 hours a year on average on each property.

If this were one or two properties, the IRS might not consider this to be sufficient to be considered a "trade or business," but in the aggregate with 10 properties combined at the individual level this may well surpass what is needed to establish an active trade or business under these rules.

On the other hand, if the individual or trust owns 10 separate S-corporations or partnerships which each owns and operates a separate property, then these cannot be aggregated for purposes of determining whether the properties and activities are considered to be active trades or businesses, simply because the Final Regulations issued by the Internal Revenue Service on February 4th do not permit this.

If instead the 10 separate S-Corporations or partnerships were placed under a single holding company, either as disregarded single member LLCs or Qualified Subchapter S Subsidiaries (Q-Subs), all of the activities of the partnership could be aggregated, or combined, to determine if a trade or business exists.

2. Other Rules. Other rules also apply with respect to if and when separate items and activities can be aggregated to see if the Active Trade or Business test has been met:

A. Safe Harbor for Non-Triple Net Leases. IRS Notice 2019-7 provides a safe harbor for when a landlord who has an active (not triple net) lease arrangement can be sure of being considered to be an active trade or business. This Proposed Revenue Procedure requires at least 250 hours per year of activity by the landlord and agents of the landlord, which must be contemporaneously memorialized and fall into categories of functions that would not include buying and selling the rental properties, travel to or from the rental properties, or reviewing financial statements.

Most advisors feel that the Proposed Revenue Procedure is not helpful, because virtually any taxpayer that would qualify under the Revenue Procedure would have qualified without its assistance.

B. Residential and Commercial Property Can Normally Not Be Aggregated. Residential and commercial property cannot be aggregated for purposes of determining whether there is an active trade or business; therefore, residential and commercial property must be tested separately to determine if the 250 hour required under the safe harbor is met. It is unclear if residential and commercial property may be combined if they are significantly interrelated, such as if a store and the apartment above the store are rented to the same tenant, or a building has both retail and commercial space and his wholly owned by the landlord. The Notice simply states that commercial and residential property may not be part of the same enterprise and the authors are not aware of any other guidance on this issue.

C. Similar Properties Under Revenue Notice 2019-7. IRS Notice 2019-7 provides that taxpayers can either treat each non-triple net lease property owned by an individual or RPE separately or treat all similar properties as s single enterprise. The Notice does not discuss what is considered to be similar property, with the exception of stating that residential and commercial property cannot be treated as part of the same enterprise. As a result, it appears that all rental activity related to residential properties held by an individual or a RPE and all rental activity related commercial properties held by an individual or a RPE can be aggregated to determine if the 250 hour safe harbor is met.

3. Triple Net Leases With Related Party Tenants May Be Considered As Active. A related rule that is worthy of mention is that a triple net lease can be considered to be an active trade or business if the tenant is an active trade or business and is considered to be commonly owned under the applicable attribution rules. This rule does not apply if the tenant is a C corporation. Therefore the tenant must be a commonly controlled RPE or individual sole proprietor for this to apply.

4. Combining Wages and Qualified Properties. Unrelated to whether an activity is an active trade or business, taxpayers may elect to aggregate commonly controlled entities for purposes of combining the Wages and Qualified Property of each entity in applying the Wage/Qualified Property Test if the following requirements are met:

A. The same person or group of persons directly or indirectly own 50% or more of each trade or business. For purposes of determining ownership, ownership by spouses, as well as children, grandchildren, parents, brothers, and sisters can be attributed to each other;

B. The ownership existed for a majority of the tax year;

C. The items must be reported on returns within the same taxable year;

D. None of the businesses can be a Specified Service Trade or Business; and

E. The aggregated trades or business must also satisfy at least two of the following requirements:

i. The trade or businesses provide products or services that are the same or customarily offered together;

ii. The trade or businesses share facilities or significant centralized business elements such as personnel, accounting, legal, manufacturing, purchasing, human resources, or information technology resources; and

iii. The trades or businesses are operated in coordination with, or reliance upon, one or more of the businesses in the aggregated group (for example, supply chains interdependencies).

A series of eighteen well-written examples, which can be found below, provide detailed guidance on the aggregation provisions. In addition, Example 11 demonstrates that a taxpayer owning less than 50% of multiple entities can elect to aggregate her interests therein, as long as there are other common taxpayers who own more than 50% of each entity. The minority owner can elect to aggregate even if the other owners do not.

Aggregation will allow wages and Qualified Property to be considered as paid for all of the entities, so that the deduction can be taken for income received from a partnership, S corporation or proprietorship that has little or no wages or Qualified Property if another entity has sufficient wages and Qualified Property for both its own income and the income of affiliates. The examples point out that losses from any entity that could be aggregated must be netted against the aggregate profits of other applicable entities, if any aggregation occurs.

The examples indicate that ownership of a sailboat racing team and a marina by separate companies would not be aggregated, but that ownership of a trucking company that delivers lumber and other supplies in one company, operation of a lumber yard in another company, and operation of a construction business that presumably uses lumber and other supplies, can be aggregated.

A new example added in the Final Regulations states that residential and commercial property rental activities cannot be aggregated together for purposes of satisfying the Wage/Qualified Property Test, due to the fact that residential and commercial property are not the same type of property and do not otherwise satisfy two of the three aggregation requirements. If a high-income Taxpayer has rental income from both residential property and commercial property that is considered to be a trade or business, then the residential rental activity and the commercial rental activity must be separately tested to see if both satisfy the wage/Qualified Property Test.

Once a taxpayer chooses to aggregate two or more trades or businesses, they must be consistently reported and aggregated for all subsequent taxable years, unless there is a change in facts and circumstance so that a taxpayer's prior aggregation no longer qualifies for aggregation.

The Final Regulations also give partnerships, S corporations or other entities (referred to in the Final Regulations as Relevant Pass Through Entities, or RPEs) owning multiple trades or businesses by direct ownership or subsidiaries the ability to make an aggregation election at the entity level, if the requirements for aggregation are met by the RPE. The election made by the RPE should be carefully considered, because it will be binding upon all of the individual owners of the RPE. Although individual owners include trades or businesses that are aggregated by the RPE, such owners can aggregate additional trades or businesses with the RPE's aggregation, assuming that the other requirements for aggregation are met.

While making such an election can simplify tax reporting for the partners or S corporation owners, it can also cause loss of Section 199A tax savings by eliminating aggregation options that an individual partner or S corporation owner would otherwise have.

Under one Example in the Final Regulations, Taxpayer A has a food business and also owns 60% of a partnership that operates both a movie theater and a food business. Taxpayer A may aggregate his personally owned food business with the food business of the partnership, due to the fact that they are the same type of products and services and share centralized business elements. On the other hand, if the partnership makes an aggregation election to combine the movie theater with the partnership's food business (since they are operated in coordination with each other and share centralized business elements), then the individually owned food service cannot be aggregated with the combined movie theater and food business due to the fact that the individually owned food business is not considered the same type of product or service as the combined movie theater and food operations, and therefore the requirements for aggregation cannot be met.

Lawyers who are drafting or updating entity arrangements may wish to have the documents prohibit the entity from making an aggregation election without the consent of all, or substantially all, of the owners or may additionally provide that no officer, manager, or director will have a fiduciary duty to aggregate or to not aggregate.

The implications of all of this to professional advisers can be daunting. In some instances, modeling the various options may be the only way to determine what the actual impact of various decisions might be. Practitioners should be cautious about providing conclusions to clients with specificity without the opportunity to perform the appropriate analysis. The costs of the level of detailed analysis that might be necessary in many instances will often be material.



When Trades or Businesses are Considered "Separable"Under Section 199A

by Alan Gassman, Brandon Ketron and Kelsey Weiss

In order to be considered a separate trade or business, the Section 199A Regulations point to regulations issued under Internal Revenue Code Section 446 which provide that no trade or business will be considered separate unless a complete and "separable" set of books and records can be maintained. Under Section 446 of the Internal Revenue Code, a taxpayer may use separate accounting methods for multiple Trades of Businesses. Alternatively, a taxpayer with a single Trade or Business may only use one method for accounting. This requirement has been highlighted by several court decisions.

In some cases, it can be fairly easy to determine whether the IRS will consider two businesses as separate and distinct if the two trades or business are in completely different lines of business. For example, in the 1928 case of Stern, the petitioners were partners under the firm name of Stern Brothers that carried on two businesses – one business operated two retail stores and the other business bought and sold coal lands. The Board of Tax Appeals held that the businesses were separate distinct by reasoning that the two businesses were "wholly different in character."

The determination can be much more difficult, however, when the businesses are similar or different divisions operate primarily for the purposes of transactions between the divisions.

In Peterson Produce Co., the District Court determined that the corporate taxpayer was unsuccessful in attempting to use difference accounting methods for different divisions of the corporation. The taxpayer used the accrual method for the feed and hatchery divisions of the poultry corporation and the cash method for the broiler division. The District Court reasoned that the broiler division was not a separate and distinct business from the feed and hatchery divisions. In this case, the feed and hatchery divisions operated almost solely to transfer feed and young chickens to the broiler division at cost. Although the general ledger accounts of the three divisions could be separated, the original and daily entries could not be physically separated. Therefore, the court determined that the separate books and records kept by the taxpayer were not adequate. The Court held that the three divisions were functionally integrated.

On the other hand, the Tax Court came to the opposite conclusion in Rocco, Inc. even though the corporation in Rocco was essentially trying to accomplish the same objective as the corporation in Peterson Produce. In Rocco, the corporate taxpayer created a distinct new corporation to run the turkey broiler division completely separate from the chicken broiler division even. Even though the two divisions transacted with each other, The Tax Court determined that the turkey broiler division and the chicken broiler division were distinct and separate because each business was conducted through a separate and individual entity.

These decisions have lead tax and legal professionals to conclude that entity structure can be very important in determined whether a particular activity can be included as part of a trade or business and multiple entities can result in multiple trades or business.

In an April 11, 2019 Webinar, Attorney and Author Steve Gorin had some practical insights on the matter. As states by Mr. Gorin:

"As a matter of sound bookkeeping and sound business practices, I highly recommend keeping a separate set of books and records for each business. I would also suggest having separate bank accounts for each separate business to help you track your accounting for each business… You have to be able to show that these really are separate businesses – they may have some interdependencies, but they are being run separately."

Mr. Gorin also provided the following practical example: "If I were going to try to establish my title company as a separate business [from my law firm], I would advertise to the real estate community the ability of my separate title company to provide services for their real estate needs that are completely independent of my law firm services."

Defining a "Primary Purpose" Under Section 199A

by Alan Gassman Brandon Ketron and Kelsey Weiss

Summary Points

Treasury Regulation 1.199A-6(d)(3)(vii) provides that "a trust formed or funded with a principal purpose of avoiding, or using more than one, threshold amount for purposes of calculating the deduction under Section 199A will not be respected as a separate trust entity for purposes of determining the threshold amount for purposes of Section 199A."

The term "a primary purpose" is an interesting choice of words, since the word "a" denotes that there can be multiple "primary purposes," while the word "primary" indicates that this would have to be the main purpose, or that there might be equally ranked "primary purposes."

These words have been used in other Internal Revenue Code Sections and Federal Statutes, and have been the subject of decisions by the U.S. Supreme Court, the Tax Court, and multiple Circuit Courts of Appeals

The majority of case law and regulations seem to define this term as being singular, meaning there can be only one principal purpose. Therefore, "if the purpose to evade or avoid Federal income tax exceeds in importance any other purpose, it is the principal purpose." In determining the purpose, "entire circumstances in which the transaction or course of conduct occurred, in connection with the tax result," is to be considered. In cases where multiple purposes are apparent, it might be "appropriate to aggregate all tax avoidance purposes and compare them with the aggregate business purposes for the acquisition."

An excellent article which reviews these decisions can be read to conclude that the IRS would have to prove that no other purpose was more important than the objective of avoiding tax under Code Section 199A in order for the "a primary purpose" test to be met.

Once the IRS makes the determination that an acquisition was made with the principal purpose to evade tax, the determination is presumed correct and the burden then shifts to the taxpayer to show otherwise.

For example, the vast majority of estate and trust planning performed by the authors will involve trusts that will benefit descendants and never be paid outright to them. Many of these trusts are formed after the death of a parent, for the primary purpose of providing lifetime creditor, estate tax, divorce and unwise decision protection for a child and the descendants of a child, which has nothing to do with Section 199A income tax savings.

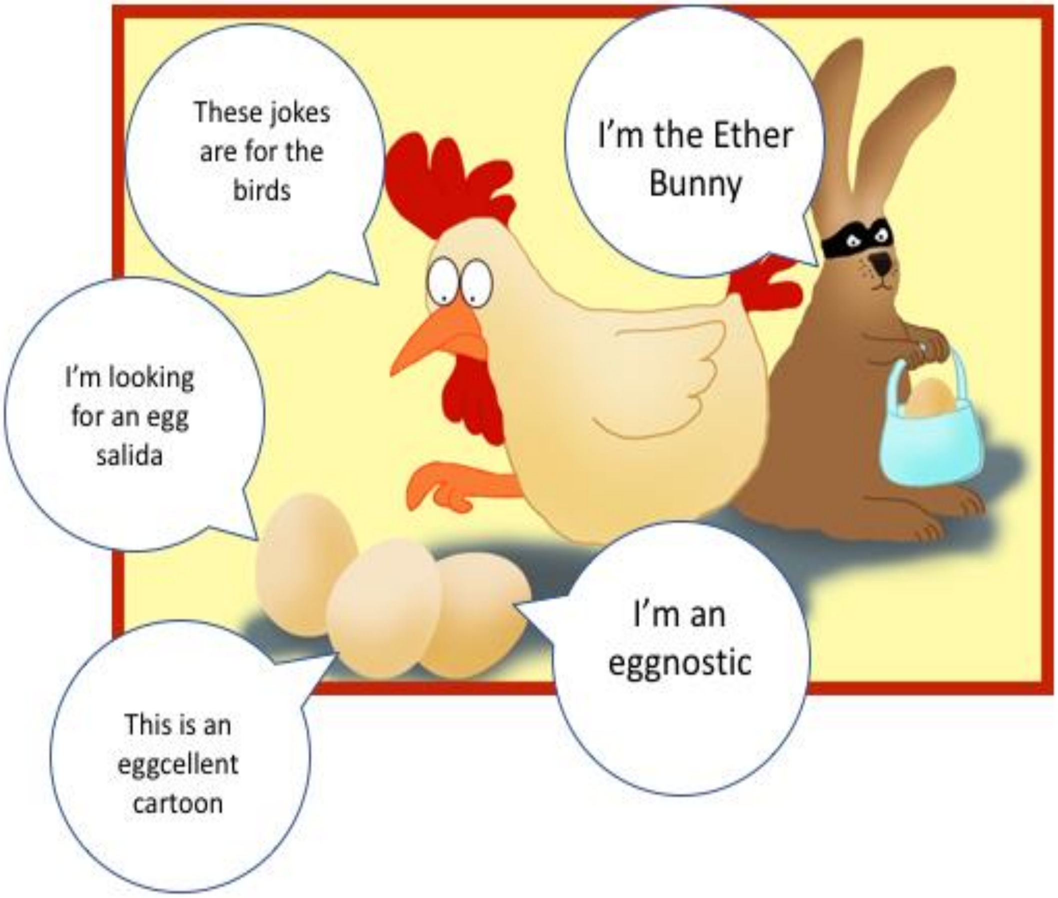
Quite often, clients form such trusts during their lifetime to facilitate avoidance of federal estate tax, and to protect assets going to descendants from potential future creditors of the parent.

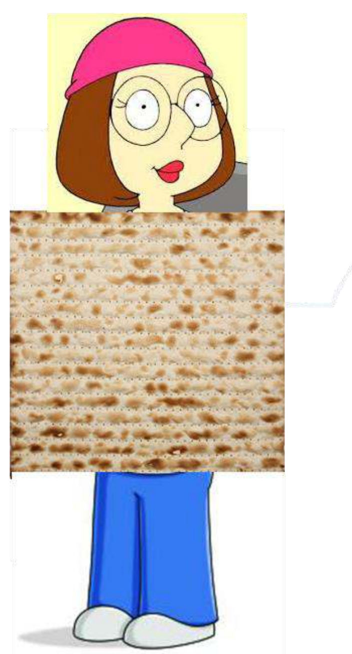
These trusts have been formed routinely by the authors for decades, and the authors will not stop forming these trusts, even if establishing them would cause loss of income tax savings under Code Section 199A.

But, if and when such a trust is formed, if an "incidental benefit" is to save income taxes under Section 199A, would that be "a primary purpose?"

The answer to this question will be based upon the facts and circumstances of each situation, but the fact that a trust is formed and may save tax money under Section 199A will not make it automatically considered to have been established for "a primary purpose" of avoiding such tax.

Humor-or something similar…





Un-leavened Meg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GASSMAN, CROTTY
& DENICOLO, P.A.
ATTORNEYS AT LAW
ALAN S. GASSMAN
KENNETH J. CROTTY
CHRISTOPHER J. DENICOLO
EMIL G. PRATESI
BRANDON L. KETRON
THE SMART
CLOCK WAS
AHEAD OF
IT'S TIME


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ALAN S. GASSMAN
KENNETH J. CROTTY
CHRISTOPHER J. DENICOLO
EMIL G. PRATESI
BRANDON L. KETRON
YOU BUTTER
CHECK YOUR
CHOLESTEROL

Calendar of Events

Newly announced events in RED

EVENT	DATE/TIME	DESC.	REGISTRATION
University of North Carolina Tax Institute	April 25-26, 2019	Creative Planning with Section 199A After the New Regulations	Contact: Agassman@gassmanpa.com
Parametric Advisor Forum	Wednesday, May 1, 2019 Grand Bohemian Hotel – Orlando, 325 S Orange Ave, Orlando, FL 32801	TBD	Contact: Agassman@gassmanpa.com
Leimberg Information Services Webinar	May 2, 2019 3:00 PM – 4:30 PM	Avoiding Estate and Trust Litigation and Disputes	Contact: Agassman@gassmanpa.com
FSU FICPA Accounting Conference	May 6 – 8, 2019, Tallahassee, FL	Alan will be speaking on the new 199A finalized regulations	Contact: Agassman@gassmanpa.com
Tampa General Hospital Lecture Series	May 10, 2019	Contract Negotiations	Contact: Agassman@gassmanpa.com

FICPA Mega CPE Conference for the TCJA	June 10 – 13, 2019	Alan will be speaking on the new 199A finalized regulations		Contact: Agassman@gassmanpa.com
MER Conference Internal Medicine for Primary Care	June 13 – 16, 2019, Chicago, IL	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
Maui Mastermind Wealth Summit Bonus Webinar	June 20, 2019. 3:00 PM	Legal Protection Package: Nuts and Bolts of Estate Planning, Personal Creditor and Estate Tax		Please Click HERE
Maui Mastermind Financial Pillar Super Course	June 22-23, 2019	Hilton-Atlanta Airport	Crucial Legal and Tax Principals for Accumulating Wealth	Please Click HERE
45th Annual Notre Dame Tax Institute	September 26-27, 2019	South Bend, Indiana	Alan's topic will be, "Application of Section 199A and its interaction with other Prominent Tax Laws to Real Estate Investors, Developers and Others"	Contact: Agassman@gassmanpa.com
FICPA Accounting and Tax Conference	October 24, 2019	Estero, FL	TBD	Contact: Agassman@gassmanpa.com
Special Asset Protection Presentation	Friday, October 25, 2019	University of Miami Law School	Advanced Asset Protection Workshop with Les Share	Contact: Agassman@gassmanpa.com
Maui Mastermind Wealth Summit	November 3-8, 2019	Wailea Beach Resort,	Essential Aspects and Decisions for Your	Please Click HERE

		Maui	Remarkable Financial Future	
Certified Contractors Network Presentation	January 4, 2020 - Orlando	Orlando, FL	Creditor Protection for the Intelligent Construction Family – It Wasn't Raining When Noah Built the Ark	Contact: Agassman@gassmanpa.com
Venice Estate Planning Council Presentation Hosted by Community Foundation of Sarasota County	Tuesday, January 21, 2020, Venice then Sarasota, FL	For the Venice Estate Planning Council and Sponsored by the Community Foundation of Sarasota County, Alan will be conducting a morning presentation, "Innovative Charitable Techniques, Asset Protection Strategies You Didn't Know and Creative Planning Under Section 199A" He will be answering questions (and telling many bad jokes) for VIPS at the hosted luncheon and will be the dinner speaker to finish the event off. Starting in Venice, these events will conclude in Sarasota.		Contact: Barbie Gonzalez: BGonzalez@CFSarasota.org