Current Federal Tax Developments

Week of January 6, 2020

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CURRENT FEDERAL TAX DEVELOPMENTS
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SECTION: LEGISLATION
SECURE ACT, EXTENDERS AND REPEAL OF CERTAIN ACA TAXES ENACTED AS PART OF YEAR END APPROPRIATIONS ACT

Citation: Further Consolidated Appropriations Act, 2020 (HR 1865), 12/20/19

In the last few weeks of 2019 Congress produced its most significant tax package of the year as part of the Further Consolidated Appropriations Act, 2020 (HR 1865).[1] The President signed the Act into law on December 20, 2019. The Act includes primarily appropriations provisions for various federal agencies, but it has significant tax provisions in the following Divisions:

- **Division N – Health and Human Services Extenders, Title I-Health and Human Services Extenders, Subtitle E – Revenue Provisions:** This portion of the Act repeals three taxes originally enacted as part of the Patient Protection and Affordable Care Act but which had not yet gone into force.

- **Division O – Setting Every Community Up for Retirement Enhancement (SECURE):** The bill that passed the House earlier this year dealing with various retirement provisions, including major changes to required distributions for inherited IRAs, delayed required beginning date for required minimum distributions, other provisions affecting qualified retirement plans, expansion of items §529 plan distributions can be used for as education expenses and returning to the pre-TCJA version of the Kiddie Tax.

- **Division Q – Revenue Provisions (Taxpayer Certainty and Disaster Tax Relief Act of 2019):** The largest portion of this section of the Act contains extenders, some retroactive, of various provisions that had expired or were scheduled to expire, including the ability to treat certain private mortgage insurance as interest on acquisition debt, the nonbusiness energy credit and many others. As well the bill adds disaster relief provisions for disasters taking place in 2018, 2019 and the very early portion of 2020 and retroactively repeals the rule treating transportation benefits provided to employees of a tax exempt entity as unrelated business income (a portion of the "parking lot tax" provision added by the Tax Cuts and Jobs Act).

Our weekly podcast for December 23 will give an overview of this Act and we are working on a four hour continuing education session to be given on this topic at the Arizona Society of CPA's offices on January 8 that will also be webcast. The session

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[1] HR 1865, Further Consolidated Appropriations Act, 2020, Signed into law December 20, 2019, https://www.congress.gov/116/bills/hr1865/BILLS-116hr1865enr.pdf (retrieved December 22, 2019)

has tentatively been scheduled to begin at 8:00 Mountain Standard Time that morning, with details to be available early the week of December 23.

SECTION: 183
SUCCESSFUL ATTORNEY FOUND TO HAVE PROFIT MOTIVE IN MAKING FILM DOCUMENTING HISTORY OF ORGANIZATION HER HUSBAND HAD PREVIOUSLY BEEN INVOLVED IN

Citation: Storey v. Commissioner, TC Memo 2012-115, 4/19/12

This particular case was one mentioned by Tony Nitti in the over two hour BKD Simply Tax podcast with Damien Martin that was released on December 26, 2019[2] *where Tony discussed his top 10 tax cases for 2019. If you haven't listened to this two hour discussion of cases, their importance in learning tax law, and how Tony deals with reading the number of cases he does, be sure to listen to the program. You won't be disappointed.*

I had written on the topic, a case that involved a local attorney here in Phoenix, for Nichols Patrick in April of 2012 prior to the establishment of this website. Because, as Tony notes, this is an especially useful case to understand hobby loss rules and we don't have a lot going on at the end of the year, I've decided to publish this on the website here at year end.

The IRS decided that an attorney who was claiming deductions relating to a documentary she was filming was not engaged in the activity for a profit, and sought to disallow her losses. Fortunately for the taxpayer, the Tax Court, in the case of *Storey v. Commissioner*, TC Memo 2012-115,[3] decided that in fact, her large losses did not indicate that she did not intend to eventually make a profit from the activity.

The case attracted the IRS's interest for a number of reasons that often cause the IRS to question the profit motive of the taxpayer. The taxpayer was a successful attorney in practice in Phoenix specializing in natural resource and water rights law. Her income for the year in question from her law practice was in excess of $1 million. Her husband had participated with Up With People as a teenager and Ms. Storey decided to film a documentary, titled "Smile 'Til It Hurts," that outlined the history of that organization.

The taxpayer had incurred six straight years of losses from the activity. The years before the court were 2006, 2007 and 2008 and, in fact, the taxpayer had received no

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[2] Simply Tax Episode 83: *Top 10 Tax Cases of 2019 with Tony Nitti*, December 26, 2019, https://www.bkd.com/podcast/2019/12/simply-tax-episode-83-top-10-tax-cases-2019-tony-nitti

[3] *Storey v. Commissioner*, TC Memo 2012-115, https://www.ustaxcourt.gov/UstcInOp/OpinionViewer.aspx?ID=10049

income from the film and had received none until she received a $250 screening fee in March 2010 from a film festival.

Thus, the IRS theory was that the taxpayer was clearly "really" a lawyer and thus, in their view, wasn't truly a filmmaker. Rather the IRS believed she was pursuing the activity due to personal reasons related to her husband's prior connection to the subject of her activity. Her "true" business of being an attorney provided an income that was sufficient that, in the IRS's view, she could pursue an expensive hobby that had no real hope of making money.

However, in this case there were other factors that lead the Court to find that Ms. Storey had a profit motive in pursuing the activity. As is normal in such cases, the Court looked to the nine factors outlined in Reg. §1.183-2(b) to analyze whether a true profit motive existed:

- The manner in which the taxpayer carried on the activity,
- The expertise of the taxpayer or his or her advisers
- The time and effort expended by the taxpayer in carrying on the activity,
- The expectation that the assets used in the activity may appreciate in value,
- The success of the taxpayer in carrying on other similar or dissimilar activities,
- The taxpayer's history of income or loss with respect to the activity,
- The amount of occasional profits, if any, which are earned,
- The financial status of the taxpayer, and
- Whether elements of personal pleasure or recreation are involved.

The taxpayer had conducted the activity in a businesslike manner. She formed a business entity (a single member LLC) to operate the business, it maintained its own books handled by a bookkeeper Ms. Storey hired and regularly consulted with, she prepared a business plan, made changes to her production and plans over time based on information received, took steps to protect her reputation as a filmmaker and she marketed the film.

The Court rejected the IRS view that the project was really conducted primarily as a "tribute" to the taxpayer's husband, noting:

> We specifically note our disagreement with respondent's assertion that Smile 'Til It Hurts was an exploration of William Storey's youth, rather than an undertaking for profit. William Storey's history in Up With People, which had been previously unknown to petitioner, certainly piqued her interest. His contacts and access to members of Up With People also facilitated her project. His appearance in the film is a small percentage of the total movie time, although compelling. His relationship to petitioner is not mentioned or otherwise noticeable in Smile 'Til It Hurts. We find that Smile 'Til It Hurts is not a tribute to

> or memoir about William Storey, as respondent argues. Instead, we find that petitioner's efforts to make Smile 'Til It Hurts a financial success show a profit objective and that this factor favors petitioner.

The taxpayer retained experts in the industry with which she consulted during her work, actions consistent with the actions a person looking to make a profitable film would take.

The Court very specifically disagreed with the IRS's assertion that because Ms. Storey was a successful partner in a law firm her film-making activity could not rise to the level of a full trade or business. The Court noted that while she billed 30-35 hours a week on legal matters, she used other time to pursue the filmmaking, and specifically noted that a taxpayer may engage in more than one trade or business at a time.

The Court found the fourth factor (expectation that property will rise in value) not useful in this case, since it was essentially just looking at the overall issue—the film was the asset that might rise in value, but essentially it would do that if this was a profitable activity. So the question was not one independent of Ms. Storey's intention to operate a profitable venture.

The Court found that the taxpayer had been a successful attorney and had prior experience in the arts, producing musicals for a nonprofit organization from 1998 through 2003 and had received commissions for her bronze work. These factors favored the taxpayer.

The Court found that the taxpayer was still in the expected "start-up" phase for a documentary filmmaker and thus it put little value on the fact that she had incurred substantial losses and had only insignificant income. The film was not concluded until the end of the final year under examination and it could not produce significant income until that point in time.

The Court agreed with the IRS that the fact that Ms. Storey's income from the law practice would allow her to pay for an expensive hobby and still maintain her expected lifestyle, finding that this factor favored the government—that is, Ms. Storey did not need this activity to generate a profit. The Court also agreed that Ms. Storey clearly enjoyed filmmaking and, specifically, sharing the story of Up With People. However, the Court did not find that these two factors meant that the operation could not have operated with a view towards making a profit.

Ultimately the Court concluded:

> After considering all the facts and circumstances, we find that petitioner has shown that she engaged in her filmmaking activity for profit. We recognize some factors in this case that indicate the absence of a profit motive: petitioner has a history of losses, earns significant income from other sources and appears to enjoy filmmaking. These factors, however, are outweighed by the facts demonstrating that petitioner did engage in film production for profit. In addition to petitioner's testimony, which we found to be credible and forthright, the record shows an intent and effort by petitioner to engage in and continue in the filmmaking field with the purpose of producing income. We conclude that, during the years in issue, petitioner engaged

> in the filmmaking activity with the dominant objective and intent of realizing a profit.

The case was one that attracted the attention of the documentary filmmaking community, with the Court receiving amicus briefs from organizations related to such filmmaking in support of Ms. Storey.

While the case was resolved in favor of the taxpayer, advisers should note that Ms. Storey, as an attorney, was probably more apt than many taxpayers in similar situations to maintain excellent documentation and books—that is, she had significant and well-documented independent evidence of actions that corroborated her assertion that the activity had been conducted for a profit. The case may not have turned out so well had the taxpayer kept sloppy records or operated less formally.

SECTION: 199A
§199A DEDUCTION WILL NOT BE INCLUDED IN SUBSTITUTE FOR RETURN PREPARED BY IRS

Citation: SBSE-04-1219-0054, 12/9/19

In a memorandum that will likely not surprise anyone, the IRS Small Business/Self-Employed Division has issued a memorandum providing guidance that the deduction under §199A will not be included in substitutes for returns (SFRs) prepared under IRC §6020(b).[4]

IRC §6020 grants the IRS authority to prepare substitute tax returns under various conditions. The provision provides:

> **(a) Preparation of return by Secretary**
>
> If any person shall fail to make a return required by this title or by regulations prescribed thereunder, but shall consent to disclose all information necessary for the preparation thereof, then, and in that case, the Secretary may prepare such return, which, being signed by such person, may be received by the Secretary as the return of such person.
>
> **(b) Execution of return by Secretary**
>
> > **(1) Authority of Secretary to execute return**
> >
> > If any person fails to make any return required by any internal revenue law or regulation made thereunder at the time prescribed therefor, or makes, willfully or otherwise, a false or fraudulent return, the Secretary shall make such return from

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[4] SBSE-04-1219-0054, December 9, 2019, https://www.irs.gov/pub/foia/ig/sbse/sbse-04-1219-0054.pdf

> his own knowledge and from such information as he can obtain through testimony or otherwise.
>
> **(2) Status of returns**
>
> Any return so made and subscribed by the Secretary shall be prima facie good and sufficient for all legal purposes.

The qualified business income deduction under IRC §199A provides a 20% deduction related to amounts of qualified business income. The question the memorandum seeks to answer is whether, in preparing such a substitute return, the IRS should include a §199A deduction if the substitute return includes income that appears to be qualified business income.

The memorandum answers that question with a simple no. The memorandum provides the following justification for its position:

> Depending on the taxpayer's taxable income, the QBI deduction is subject to multiple limitations including the type of trade or business, the amount of W-2 wages paid by the trade or business, and the unadjusted basis immediately after acquisition (UBIA) of qualified property held by the trade or business. Additionally, a qualified business loss or qualified publicly traded partnership loss carried forward from prior years must be considered. Therefore, while a taxpayer may be entitled to claim a QBI deduction on a filed return, the Service will not allow the QBI deduction on an SFR prepared under IRC section 6020(b).[5]

The memorandum notes that taxpayers are allowed to file a delinquent return claiming the §199A deduction in response to the substitute return. As the memorandum notes:

> If a taxpayer subsequently files a delinquent tax return that includes a QBI deduction, the Service will consider the deduction following the same policies for other items included on the filed return.[6]

When the IRS prepares an SFR, the agency will generally assume all facts that aren't known for certain by the agency will work to the taxpayer's detriment. It is not surprising that even though it may be very likely the taxpayer would qualify for a §199A deduction, the agency is not going to place that deduction on the SFR it prepares. It is up to the taxpayer to respond and present the evidence that the taxpayer does qualify for this tax benefit.

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[5] SBSE-04-1219-0054, p. 1

[6] SBSE-04-1219-0054, p. 1

SECTION: 274
AUTO MILEAGE RATES FOR 2020 ISSUED BY IRS

Citation: Notice 2020-05, 12/31/19

On the last day of 2019, the IRS released the updated auto mileage rates for 2020 in Notice 2020-05.[7]

The standard mileage rates for 2020 are:

- Business use: 57.5 cents per mile;
- Charitable mileage rate: 14 cents per mile; and
- Medical care and limited cases where moving expenses are still deductible: 17 cents per mile.

The basis reduction amounts for taxpayers using the standard business mileage rates are:

- 27 cents per mile for 2020;
- 26 cents per mile for 2019;
- 25 cents per mile for 2018;
- 25 cents per mile for 2017; and
- 24 cents per mile for 2016.

The maximum automobile cost for purposes of computing the allowance under a fixed and variable rate allowance (FAVR) plan is $50,400 for automobiles (including trucks and vans) for 2020.

For purposes of the fleet-valuation rule found in Reg. §1.61-21(d)(5)(v) and the vehicle cents per mile rule found at Reg. §1.61-21(e) the maximum fair market value of automobiles (including trucks and vans) is $50,400 for 2020.

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[7] Notice 2020-05, December 31, 2019, https://www.irs.gov/pub/irs-drop/n-20-05.pdf (retrieved December 31, 2019)

SECTION: 501
CHARITIES GIVEN GUIDANCE ON RESPONSIBILITIES WHEN RECEIVING DONATION OF VIRTUAL CURRENCY

Citation: "Frequently Asked Questions on Virtual Currency Transactions," IRS website, 12/31/19

The IRS quietly added more guidance in the virtual currency arena to their frequently asked questions (FAQ), this time adding new questions and answers related to how charities should deal with the receipt of a virtual currency donation, as well as how the donor deals with the donation.[8]

Two questions related to the donor had previously been in the FAQ. To provide a complete discussion, we'll cover those two first.

The first question deals with the donation of virtual currency from the viewpoint of the donor concerned he/she may have to recognize income due to disposing of the virtual currency by making a donation. Question 33 provides:

> **Q33. If I donate virtual currency to a charity, will I have to recognize income, gain, or loss?**
>
> A33. If you donate virtual currency to a charitable organization described in Internal Revenue Code Section 170(c), you will not recognize income, gain, or loss from the donation. For more information on charitable contributions, see Publication 526, Charitable Contributions.

This is consistent with the IRS view that cryptocurrency is a capital asset in the hands of the taxpayer. A donation of the asset is not considered to be a sale or exchange of the asset—after all, nothing except a "good feeling" is received by the donor, or what is received is of relatively minor value. If that wasn't the case, we'd likely be looking at a part-sale, part-gift situation at best.

Question 34 confirms that virtual currency is treated as just another capital asset for donation purposes:

> **Q34. How do I calculate my charitable contribution deduction when I donate virtual currency?**
>
> A34. Your charitable contribution deduction is generally equal to the fair market value of the virtual currency at the time of the donation if you have held the virtual currency for more than one year. If you have

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[8] "Frequently Asked Questions on Virtual Currency Transactions," IRS website, December 31, 2019 revision, https://www.irs.gov/individuals/international-taxpayers/frequently-asked-questions-on-virtual-currency-transactions (retrieved January 1, 2020)

> held the virtual currency for one year or less at the time of the donation, your deduction is the lesser of your basis in the virtual currency or the virtual currency's fair market value at the time of the contribution. For more information on charitable contribution deductions, see Publication 526, Charitable Contributions.

Next we turn to the charity itself—what are the charity's responsibilities when it receives virtual currency as a contribution?

The charity is receiving a non-cash contribution, and that contribution may very well be worth more than $5,000 and likely even more often worth more than $250. The IRS provides the following description of the charity's responsibilities when dealing with donor notification:

> **Q35. When my charitable organization accepts virtual currency donations, what are my donor acknowledgment responsibilities? (12/2019)**
>
> A35. A charitable organization can assist a donor by providing the contemporaneous written acknowledgment that the donor must obtain if claiming a deduction of $250 or more for the virtual currency donation. See Publication 1771, *Charitable Contributions Substantiation and Disclosure Requirements* (PDF), for more information.
>
> A charitable organization is generally required to sign the donor's Form 8283, *Noncash Charitable Contributions*, acknowledging receipt of charitable deduction property if the donor is claiming a deduction of more than $5,000 and if the donor presents the Form 8283 to the organization for signature to substantiate the tax deduction. The signature of the donee on Form 8283 does not represent concurrence in the appraised value of the contributed property. The signature represents acknowledgement of receipt of the property described in Form 8283 on the date specified and that the donee understands the information reporting requirements imposed by section 6050L on dispositions of the donated property (see discussion of Form 8282 in FAQ 36). See Form 8283 instructions for more information. (12/2019)

But the charity's responsibilities do not end there. The IRS goes on to describe the charity's responsibilities when reporting to the IRS when it receives a donation of virtual currency:

> **Q36. When my charitable organization accepts virtual currency donations, what are my IRS reporting requirements? (12/2019)**
>
> A36. A charitable organization that receives virtual currency should treat the donation as a noncash contribution. See Publication 526, *Charitable Contributions,* for more information. Tax-exempt charity responsibilities include the following:

- Charities report non-cash contributions on a Form 990-series annual return and its associated Schedule M, if applicable. Refer to the Form 990 and Schedule M instructions for more information.

- Charities must file Form 8282, *Donee Information Return*, if they sell, exchange or otherwise dispose of charitable deduction property (or any portion thereof) - such as the sale of virtual currency for real currency as described in FAQ #4 - within three years after the date they originally received the property and give the original donor a copy of the form. See the instructions on Form 8282 for more information. (12/2019)

SECTION: 1366
TAXPAYER NOT ALLOWED TO ASSERT SUBSTANCE OVER FORM, NO DEBT BASIS FOR LOANS FROM RELATED CORPORATION

Citation: Messina et ux. et al. v. Commissioner, Case No. 18-70186, CA9, 12/27/19

The Ninth Circuit Court of Appeals affirmed the Tax Court's 2017 decision in the case of *Messina et ux. et al. v. Commissioner.*[9] The appellate decision explains why the IRS is allowed to argue substance over form for a transaction, but that argument will not generally be helpful for the taxpayer—as it failed to be in this case.

In 2017 we had previously written about this case when the Tax Court decision came down.[10] In that article we summarized the facts of the case as follows:

> In this situation, the controlling shareholders of an S corporation formed another S corporation that loaned funds to a qualified S corporation subsidiary (QSUB) of the first S corporation. The shareholders then attempted to claim losses from the first S corporation by using those loans as additional basis in the corporation—a position the IRS and, ultimately, the Tax Court disagreed with.
>
> The second S corporation was formed on the advice of the taxpayers' counsel in order to work around a problem. The loan was to be used to refinance third party debt to the QSUB. However, by terms of the

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[9] *Messina et ux. et al. v. Commissioner*, Case No. 18-70186, CA9, 12/27/2019, http://cdn.ca9.uscourts.gov/datastore/memoranda/2019/12/27/18-70186.pdf

[10] Ed Zollars, "Loans from Related Corporations Did Not Give Shareholders Basis for Losses," *Current Federal Tax Developments,* October 31, 2017, https://www.currentfederaltaxdevelopments.com/blog/2017/10/31/loans-from-related-corporations-did-not-shareholders-basis-for-losses

> agreement with other creditors (who had sold the business to the S corporation originally), any amounts borrowed from the shareholders of the S corporation had to be subordinated to the original owner's debts. The attorney advised the taxpayers by using a new S corporation, no subordination of the new debt would be required.[11]

As we noted at the time, the Tax Court found that such debt from a related party did not give the shareholders basis—they couldn't ignore the existence of the lending corporation and treat the debt as coming directly from the shareholders.

The taxpayers appealed this decision, and the Ninth Circuit has rendered its decision, agreeing with the Tax Court that the taxpayers could not ignore the corporation that they had voluntarily formed to hold the loans.

The taxpayers argued that the substance of the transaction was a loan from them to the S corporation from which they wished to claim a loss, and that the court should respect this substance. But the Ninth Circuit rejects the idea that a *taxpayer* can argue substance over form when the form of the transaction is created by the taxpayer:

> We have not held that the "substance over form" doctrine is available to a taxpayer as well as the government. Indeed, we have previously rejected the notion that the taxpayer can "escape the tax consequences of a business arrangement which he made upon the asserted ground that the arrangement was fictional." *Maletis v. United States*, 200 F.2d 97, 98 (9th Cir. 1952) (quoting *Love v. United States*, 96 F. Supp. 919, 921 (Ct. Cl. 1951)).[12]

The government is allowed to argue substance over form for the simple reason that the government was not involved in deciding the form of the transaction. The taxpayer, on the other hand, was free to choose whatever form he/she wished and, in this case, the taxpayers did not choose to structure this as a loan directly from the taxpayers to the S corporation.

But even when the form over substance doctrine is available to a party, the party still needs to show that the form does not correspond to the substance of the arrangement—and the panel notes that that was not the case here. The panel continues:

> As the Tax Court properly held, the form of the loan acquisition in this case "corresponds to its substance" and should therefore "be respected for Federal tax purposes as it was implemented." *Messina v. Comm'r*, T.C. Memo. 2017-213, 2017 WL 4973291, at *16 (2017).

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[11] Ed Zollars, "Loans from Related Corporations Did Not Give Shareholders Basis for Losses," *Current Federal Tax Developments,* October 31, 2017, https://www.currentfederaltaxdevelopments.com/blog/2017/10/31/loans-from-related-corporations-did-not-shareholders-basis-for-losses

[12] *Messina et ux. et al. v. Commissioner*, p. 3

> KMGI's purchase of the third-party loan directly, rather than through Kirkland and Messina, was motivated by a number of non-tax business and regulatory considerations. In all circumstances except their tax returns, Taxpayers treated KMGI as an independent entity that was to acquire the third-party loan and serve as Club One's creditor. They reaped several benefits from doing so, including avoidance of a foreclosure on the casino that they co-own through Club One and a call on the personal guaranties that they signed in connection with the third-party loan. In addition, KMGI served business functions, including: being able to apply for the Gambling Commission's permission to acquire the loan; purchasing the loan from the third party potentially to maintain the loan's seniority to Club One's other obligations; receiving loan payments from Club One; and returning capital contributions to Kirkland and Messina. Thus, even if the "substance over form" doctrine were available to Taxpayers, it does not alter the outcome here[13]

Since debts have to come directly from the shareholders to the corporation to be basis for loss deductions to the shareholders, these debts fail to qualify to create basis. Thus, the Tax Court correctly denied the taxpayers the losses they claimed that depended on this debt basis.

SECTION: 1400Z-1
FINAL REGULATIONS ON QUALIFIED OPPORTUNITY ZONE FUNDS RELEASED BY IRS

Citation: IRS release of TD 9889 and FAQ, 12/19/19

The final regulations dealing with Qualified Opportunity Zone Funds have been released by the IRS.[14] Note that the copy released by the IRS has the following caveat:

> This document will be submitted to the Office of the Federal Register (OFR) for publication. The version of the final rule released today may vary slightly from the published document if minor editorial changes are made during the OFR review process. The document published in the Federal Register will be the official document.[15]

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[13] *Messina et ux. et al. v. Commissioner*, pp. 3-4

[14] IRS release of TD 9889, released by Department of Treasury on December 19, 2019, https://www.irs.gov/pub/irs-drop/td-9889.pdf (retrieved December 22, 2019)

[15] IRS release of TD 9889, p. 1

The IRS also released a five page frequently asked questions (FAQ) document on the final regulations.[16] One major change found in the final regulations is highlighted early in the FAQ relates to business gains:

> *Sales of business property* — The proposed regulations only permitted the amount of an investor's gains from the sale of business property that were greater than the investor's losses from such sales to be invested in QOFs, and required the 180-day investment period to begin on the last day of the investor's tax year. The final regulations allow a taxpayer to invest the entire amount of gains from such sales without regard to losses and change the beginning of the investment period from the end of the year to the date of the sale of each asset.[17]

Also highlighted is a modification on the timing of the beginning of the 180-day period for gains flowing to a partner from a partnership:

> *Partnership gain* — Partners in a partnership, shareholders of an S corporation, and beneficiaries of estates and non-grantor trusts have the option to start the 180-day investment period on the due date of the entity's tax return, not including any extensions. This change addresses taxpayer concerns about potentially missing investment opportunities due to an owner of a business entity receiving a late Schedule K-1 (or other form) from the entity.[18]

The FAQ highlights a clarification for reinvestment of mutual fund (registered investment company or RIC) and REIT gains:

> *Investment of Regulated Investment Company (RIC) and Real Estate Investment Trust (REIT) gains* — The rules clarify that the 180-day investment period generally starts at the close of the shareholder's tax year and provides that gains can, at the shareholder's option, also be invested based on the 180-day investment period starting when the shareholder receives capital gains dividends from a RIC or REIT.[19]

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[16] *Final Regulations on Opportunity Zones: Frequently Asked Questions*, Department of the Treasury, December 19, 2019, https://home.treasury.gov/system/files/136/Treasury-Opportunity-Zone-Final-Regulations-FAQ-12-19-19.docx (retrieved December 22, 2019)

[17] *Final Regulations on Opportunity Zones: Frequently Asked Questions*, p. 1

[18] *Final Regulations on Opportunity Zones: Frequently Asked Questions*, p. 1

[19] *Final Regulations on Opportunity Zones: Frequently Asked Questions*, p. 1

As well, a taxpayer friendly clarification on the impact on installment sales is also found in the FAQ:

> *Installment sales* — The rules clarify that gains from installment sales are able to be invested when received, even if the initial installment payment was made before 2018.[20]

The FAQ also highlights a taxpayer-friendly change in the final regulations regarding which gains can be excluded from income once the 10-year period has expired:

> *Sales of property by a Qualified Opportunity Zone Business (QOZB)* — In the proposed regulations, an investor could only elect to exclude gains from the sale of qualifying investments or property sold by a QOF operating in partnership or S Corporation form, but not property sold by a subsidiary entity. The final regulations provide that capital gains from the sale of property by a QOZB that is held by such a QOF may also be excluded from income as long as the investor's qualifying investment in the QOF has been held for 10 years. However, the amount of gain from such a QOF's or its QOZBs' asset sales that an investor in the QOF may elect to exclude each year will reduce the amount of the investor's interest in the QOF that remains a qualifying investment.[21]

The FAQ also highlights the ability to exclude certain other gains under the final regulations.

> *Applicability to other gains* — The final rules clarify that the exclusion is available to other gains, such as distributions by a corporation to shareholders or a partnership to a partner, that are treated as gains from the sale or exchange of property (other than inventory) for Federal income tax purposes.[22]

The FAQ concludes with two other sections based on the following questions:

- How does a Fund determine levels of new investment in a Qualified Opportunity Zone?
- How can large C Corporations invest in Opportunity Zones?

[20] *Final Regulations on Opportunity Zones: Frequently Asked Questions*, p. 1

[21] *Final Regulations on Opportunity Zones: Frequently Asked Questions*, p. 2

[22] *Final Regulations on Opportunity Zones: Frequently Asked Questions*, p. 2

SECTION: 3405
RULES ISSUED FOR 2020 FOR WITHHOLDING TAXES ON PENSION AND ANNUITY PAYMENTS

Citation: Notice 2020-03, 12/18/19

With the changes made to the Form W-4 for 2020, the IRS has issued Notice 2020-03[23] to give instructions on how to deal with withholding on periodic payments for pensions, annuities and certain other deferred income under IRC §3405(a).

The Notice explains the problem as follows:

> Prior to the 2020 calendar year, information requested on Form W-4P regarding withholding from periodic payments generally paralleled the information requested on Form W-4 for withholding from wages. The Form W-4 for the 2020 calendar year (which has been renamed the Form W-4, Employee's Withholding Certificate) has been redesigned to increase transparency and accuracy of the withholding system. Beginning in calendar year 2020, employers are required to use the redesigned form for all new employees and employees hired prior to 2020 who wish to adjust their withholding. As a result, information requested on the 2020 Form W-4 no longer parallels information requested on Form W-4P for withholding from periodic payments. Among other changes, the redesigned Form W-4 requests the employee's filing status, rather than marital status, and no longer requests the number of withholding allowances the employee is claiming. The 2020 Form W-4 also includes a new method by which an employee may request withholding using higher withholding rate tables. Importantly, the Treasury Department and the IRS have designed the withholding tables and computational procedures in the 2020 *Publication 15-T, Federal Income Tax Withholding Methods*, to work with both a 2019 or earlier Form W-4 and the redesigned 2020 Form W-4. Therefore, for purposes of withholding from periodic payments under § 3405(a), the IRS plans to provide in the 2020 *Publication 15-A, Employer's Supplemental Tax Guide*, that the 2020 Form W-4P will work with certain withholding tables and computational procedures in the 2020 Publication 15-T that are applicable to a 2019 or earlier Form W-4.[24]

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[23] Notice 2020-03, December 18, 2019, https://www.irs.gov/pub/irs-drop/n-20-03.pdf, retrieved December 18, 2019

[24] Notice 2020-03, pp. 2-3

As well, current Temporary Regulations provide that if no Form W-4P is filed by a recipient of such periodic payments, tax is to be withheld based on the rates for a married person claiming three withholding allowances.[25]

The information requested on the Form W-4P will continue to parallel that asked for on 2019 and earlier Forms W-4, rather than the information on the 2020 Form W-4.[26] The Notice explains:

> Payees of periodic payments may use either the worksheets to Form W-4P or the Tax Withholding Estimator (www.irs.gov/W4App) to assist in determining their entries on the 2020 Form W-4P. As explained in Section II of this notice, certain withholding tables and computational procedures in the 2020 Publication 15-T that are applicable to a 2019 or earlier Form W-4 will also work with the 2020 Form W-4P.[27]

The Notice provides the following information on the computation of withholding amounts on such payments for 2020 payments:

> For the 2020 calendar year, the rules for withholding from periodic payments under § 3405(a) when no withholding certificate has been furnished will continue to parallel the rules for prior years. Therefore, for 2020, the default rate of withholding from periodic payments under § 3405(a) will be based on treating the payee as a married individual claiming three withholding allowances and applying that status to the applicable withholding tables and related computational procedures in the 2020 *Publication 15-T*. The IRS plans to provide in the 2020 *Publication 15-A* that this default rate of withholding will work with certain withholding tables and computational procedures in the 2020 *Publication 15-T* that are applicable to a 2019 or earlier Form W-4.[28]

Treasury and the IRS indicate that they are considering what changes should be adopted for years after 2020, including whether the default rate for these withholdings should be changed in 2021 and later years.[29]

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[25] Temporary Reg. §35.3405-1T, Q&As A-10, B-3 and B-4

[26] Notice 2020-30, p. 4

[27] Notice 2020-30, p. 4

[28] Notice 2020-03, pp. 4-5

[29] Notice 2020-03, p. 5