Recent Developments in Federal Income Taxation

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First Wednesday Tax Update
February 5, 2020

1

To obtain today's outline and slides:
https://tinyurl.com/outline0220

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2

Disaster-Related Tax Provisions of the 2020 Consolidated Appropriations Act

- 40% credit (max. $2,400) for qualified wages paid to each employee while employer is inoperable in disaster area (item F.4, p.4)
- Access to retirement funds for those in disaster areas (item B.6, p.6)
  - Penalty-free withdrawals of up to $100,000
  - Income from withdrawals can be reported ratably over three years
  - Amounts withdrawn can be recontributed within three years and treated as tax-free rollovers
- Deduction of casualty losses in disaster areas (item D.4, p.9)
  - Deductible to extent the loss exceeds $500 with no 10% threshold
  - Deduction is available regardless of whether taxpayer itemizes
- Use of prior-year earned income for EITC and CTC (item D.5, p.10)
- Deduction of charitable contributions for relief efforts in disaster areas up to 100% of AGI (item B.1, p.19)
- Mandatory 60-day extension of certain deadlines in disaster areas (item E.1, p.21)

3

3

Retroactive Extension of Deductions and Credits 2020 Consolidated Appropriations Act

- § 179D deduction for cost of energy efficient commercial building property. (item D.1, p.2)
  - Generally, improvements to reduce energy and power costs with respect to interior lighting systems, heating, cooling, ventilation, and hot water systems of a commercial building by 50 percent or more compared to certain standards.
  - Had expired for property placed in service after December 31, 2017
  - Deduction now is available for property placed in service before January 1, 2021
- 3-year recovery period for racehorses (item E.1, p.3)
  - Had expired for racehorses placed in service after December 31, 2017
  - Now applies to racehorses placed in service before January 1, 2021
- 7-year recovery period for motorsports entertainment complexes (item E.2, p.3)
  - Had expired for property placed in service after December 31, 2017
  - Now applies to property placed in service before January 1, 2021

4

4

Retroactive Extension of Deductions and Credits 2020 Consolidated Appropriations Act

- Three-year credit of $500 for small employers that implement automatic contribution arrangements- new Code § 45T (item F.1, p.3)
  - Applies to taxable years beginning after December 31, 2019
- § 45L credit of $2,000 or $1,000 (depending on the projected level of fuel consumption) an eligible contractor can claim for each qualified new energy efficient home constructed (item F.2, p.3)
  - Had expired for homes acquired after December 31, 2017
  - Now applies to homes acquired before January 1, 2021
- § 45S credit extended through December 31, 2020
  - Available to an "eligible employer" that pays at least 50% of normal wages to "qualifying employees" during periods in which the employees are on family and medical leave.
  - Credit ranges from 12.5% to 25% of wages paid

5

5

Increase in Age for RMDs to 72 *Outline: item B.2, page 5*

- A provision of the SECURE Act, Division O, Title I, § 114 of the 2020 Further Consolidated Appropriations Act, amended Code § 401(a)(9)(C)(i)(I)
- Increases the age at which required minimum distributions (RMDs) from a qualified plan (including IRAs) must begin from 70-½ to 72.
- RMDs now must begin by April 1 of the calendar year following the later of:
  - Calendar year in which the employee attains age 72, or
  - In the case of an employer plan, the calendar year in which the employee retires (does not apply to a 5-percent owner (as defined in § 416))
- Applies to distributions required to be made after December 31, 2019, with respect to individuals who attain age 70-½ after that date.

6

6

No More Stretch RMDs from Non-Spousal Inherited Retirement Accounts
Outline: item B.3, page 6

- A provision of the SECURE Act, Division O, Title IV, § 401 of the 2020 Further Consolidated Appropriations Act, amended Code § 401(a)(9)(E)
- Modifies the required minimum distribution (RMD) rules for inherited retirement accounts (defined contribution plans and IRAs).
- Requires all funds to be distributed by the end of the 10th calendar year following the year of death.
  - There is no requirement to withdraw any minimum amount before that date.
- Current rules, which permit taking RMDs over many years, continue to apply to certain designated beneficiaries, including surviving spouses, children of the participant who have not reached the age of majority, and those not more than 10 years younger than the deceased individual.
- Applies to distributions with respect to those who die after 12/31/19.

7

7

Penalty-Free Withdrawals for Birth or Adoption
Outline: item B.4, page 6

- A provision of the SECURE Act, Division O, Title I, § 113 of the 2020 Further Consolidated Appropriations Act, added Code § 72(t)(2)(H)
- Permits penalty-free withdrawals from "applicable eligible retirement plans" for a "qualified birth or adoption distribution."
- A "qualified birth or adoption distribution" is:
  - "any distribution from an applicable eligible retirement plan to an individual if made during the 1-year period beginning on the date on which a child of the individual is born or on which the legal adoption by the individual of an eligible adoptee is finalized."
  - Must include child's name, age, and taxpayer identification number of on the return.
  - Maximum penalty-free distribution is $5,000 per individual per birth or adoption.
- Applies to distributions made after Dec. 31, 2019.

8

8

Income from Graduate Fellowships is Compensation for Purposes of IRA Contributions
Outline: item D.1, page 8

- A provision of the SECURE Act, Division O, Title I, § 106 of the 2020 Further Consolidated Appropriations Act, amended Code § 219(f)(1)
- Provides that amounts paid to an individual to aid in the pursuit of graduate or postdoctoral study and included in the individual's gross income are now treated as compensation for purposes of the limit on contributing to an IRA.
  - Would include taxable stipends and non-tuition fellowship payments received by graduate and postdoctoral students.
- Applies to taxable years beginning after December 31, 2019.

9

9

No More Age Limit for IRA Contributions
Outline: item D.2, page 8

- A provision of the SECURE Act, Division O, Title I, § 107 of the 2020 Further Consolidated Appropriations Act, repealed Code § 219(d)(1)
- Eliminates the age restriction (formerly 70-1/2) for contributions to a traditional IRA.
- Also amends § 408(d)(8)(A), which allows taxpayers who are age 70-½ or older to make tax-free distributions to a charity from an IRA of up to $100,000 per year.
  - The change reduces a taxpayer's ability to take such tax-free distributions for charity by the amount of deductible IRA contributions made after age 70-½.
  - The reduction appears to apply on a year-by-year basis.
- Changes apply to contributions and distributions made for taxable years beginning after December 31, 2019.

10

10

Exclusion for Cancellation of Qualified Principal Residence Indebtedness

Outline: item B.1, page 8

- A provision of the Taxpayer Certainty and Disaster Tax Relief Act of 2019, Division Q, Title I, § 101 of the 2020 Further Consolidated Appropriations Act, extended Code § 108(a)(1)(E)
- Permits taxpayers to exclude from gross income the discharge of qualified principal residence indebtedness.
- Is in effect for 2018, 2019, and 2020.
  - The exclusion had expired after 2017.
  - Amendment of 2018 returns might be necessary

11

11

Medical Expense Deduction

Outline: item D.1, page 9

- Prior to 2017 TCJA, medical expenses generally were deductible only to the extent they exceeded 10% of a taxpayer's AGI
  - For taxable years beginning after 2012 and ending before 2017, this threshold was reduced to 7.5% if the taxpayer or the taxpayer's spouse had attained age 65 by the close of the year.
- TCJA:
  - Amended § 213(f) to provide that the 7.5% threshold applies to <u>all</u> taxpayers for calendar years 2017 and 2018.
  - The 7.5% threshold applies for purposes of both the regular tax and the AMT.
- A provision of the Taxpayer Certainty and Disaster Tax Relief Act of 2019, Division Q, Title I, § 103 of the 2020 Further Consolidated Appropriations Act, extended the 7.5% threshold for 2019 and 2020.

12

12

Deduction of Mortgage Insurance Premiums
Outline: item D.2, page 9

- A provision of the Taxpayer Certainty and Disaster Tax Relief Act of 2019, Division Q, Title I, § 102 of the 2020 Further Consolidated Appropriations Act, extended Code § 163(h)(3)(E)
- Permits taxpayers to treat mortgage insurance premiums paid in connection with acquisition indebtedness as deductible qualified residence interest.
- Is in effect for 2018, 2019, and 2020.
  - This provision had expired after 2017.
  - Amendment of 2018 returns might be necessary

13

13

Above-the-Line Deduction of Qualified Tuition
Outline: item D.3, page 9

- A provision of the Taxpayer Certainty and Disaster Tax Relief Act of 2019, Division Q, Title I, § 104 of the 2020 Further Consolidated Appropriations Act, extended Code § 222
- Permits an above-the-line deduction for *qualified tuition and related expenses* for higher education of the taxpayer, the taxpayer's spouse, or dependents.
  - Limit is \$0, \$2,000, or \$4,000, depending on the taxpayer's adjusted gross income
- Is in effect for 2018, 2019, and 2020.
  - This provision had expired after 2017.
  - Amendment of 2018 returns might be necessary

14

14

529 Accounts
Outline: item F.1, page 11

- A provision of the SECURE Act, Division O, Title 3, § 302 of the 2020 Further Consolidated Appropriations Act, added Code § 529(c)(8)-(9)
- Section 529(c)(8) permits tax-free distributions from § 529 accounts to pay:
  - "expenses for fees, books, supplies, and equipment required for the participation of a designated beneficiary in an apprenticeship program" registered under the National Apprenticeship Act.
- Section 529(c)(9) permits *an aggregate of $10,000* of tax-free distributions from § 529 accounts to pay:
  - "principal or interest on any qualified education loan (as defined in section 221(d)) of the designated beneficiary or a sibling of the designated beneficiary."
- Applies to distributions occurring after 2018

15

15

Negative Tax Capital Accounts of Partners
Outline: item G.1, page 11

- The 2018 Instructions for Form 1065 and accompanying Schedule K-1 required a partnership that does not report tax basis capital accounts to its partners to report, on line 20 of Schedule K-1 (Form 1065) using code AH, the amount of a partner's *tax basis capital* both at the beginning of the year and at the end of the year if either amount is negative.
- Notice 2019-20 2019-14 I.R.B. 927 (3/7/19), and FAQ on IRS website provide guidance on tax capital accounts.
- Draft 2019 Form 1065 and Schedule K-1 *required* partnerships to report *tax capital accounts* on Schedule K-1 (item b, page 13)
  - Several other significant changes
- Notice 2019-66, 2019-52 I.R.B. 1509 (12/9/19): defers requirement of tax basis capital accounts to partnership tax years beginning after 2019 (item c, page 14)

16

16

Repeal of Increase to UBTI
Outline: item A.1.d, page 18

- The 2017 TCJA enacted § 512(a)(7), which increased the UBTI of tax-exempt organizations that provided qualified transportation fringe benefits that would be nondeductible by a taxable employers.
- A provision of the Taxpayer Certainty and Disaster Tax Relief Act of 2019, Division Q, Title III, § 302 of the 2020 Further Consolidated Appropriations Act, repealed Code § 512(a)(7)
- Repeal is effective retroactively, i.e., as if the provision had never been enacted.
- Refund of UBIT paid for 2018?

17

17

Kestin v. Commissioner, 153 T.C. No. 2 (8/29/19)
Outline: item A.1, page 20

- Held that filing an amended return on Form 1040X and then submitting to the IRS six photocopies of the same amended return results in only one $5,000 frivolous return penalty, not six more penalties.

18

18

Repeal of Certain Excise Taxes
2020 Further Consolidated Appropriations Act

- Cadillac tax imposed by § 4980*I* repealed for taxable years beginning after December 31, 2019 (item C.1, p.23)
- Medical device tax of § 4191 repealed for sales of medical devices after December 31, 2019 (item C.2, p.23)

19

19