TAX UPDATES 2019

Overview **Page**

Overview	Page
• DUE DATES FOR 2018 FILING SEASON	1
• TAX CUTS AND JOBS ACT LAW (TJCA) FIGURES FOR 2018	1
• EXEMPTION OF $0 UNDER TCJA	4
• FORM 1040 WITH MULTIPLE SCHEDULES	4
• INVALID ITINs AND SSNs ASSIGNED AFTER APRIL 15	5
• SSN IS REQUIRED FOR ALL QUALIFYING CHILDREN	6
• PENALIZATION OF PROFESSIONAL RULES OF CONDUCT	6
• ITINS REQUIRED TO BE RENEWED BEFORE 2018 ENDS	7
• FUTA RATE REDUCED FOR CALIFORNIA LOAN REPAID IN 2018	8
• CREDIT REPORTING COMPANIES NOT ALLOWED TO CHARGE FOR FREEZING AND UNFREEZING SERVICES	8
• CALIFORNIA ADJUSTED REFUNDS WILL NOT BE MAILED OUT IN CHECKS IF DIRECT DEPOSIT WAS SELECTED	8
• THE WAYFAIR DECISION	9
• THE DYNAMEX DECISION	10

INCOME TAX DUE DATE FOR 2018 FILING SEASON.

The due date for the individual income tax returns will be April 15, 2019. This is the last day for filing federal income tax returns and extension requests this 2018 tax season. In case of living in Maine or Massachusetts, taxpayers will be able to file and pay their taxes until April 17, 2019, since Patriot's day (a legal holiday in these states) falls on Monday, April 15, and the Emancipation Day holiday falls on Tuesday, April 16, 2019.

TAX CUTS AND JOBS ACT LAW FIGURES FOR 2018.

Earn Income Credit

EITC AMOUNT AND LIMITS FOR 2018				
Income Qualification Item	**No Children**	**With 1 Child**	**With 2 Children**	**With 3+ Children**
1. Max. amount of EITC	$529	$3,526	$5,828	$6,557
2. Earned Income (lower limit) required to get maximum credit	$6,920	$10,370	$14,570	$14,570

EITC AMOUNT AND LIMITS FOR 2018				
Income Qualification Item	**No Children**	**With 1 Child**	**With 2 Children**	**With 3+ Children**
3. Phaseout Threshold Amount Begins **(for Single, SS, or Head of Household)**	$8,650	$19,030	$19,030	$19,030
4. Phaseout Amount When Credit Ends **(for Single, SS, or Head of Household)**	$15,570	$41,094	$46,703	$50,162
5. Phaseout Threshold Amount Begins **(for Married Filing Jointly)**	$14,450	$24,820	$24,820	$24,820
6. Phaseout Amount When Credit Ends **(for Married Filing Jointly)**	$21,370	$46,884	$52,493	$55,592

Tax Income Brackets

Under the **Tax Cuts and Jobs Act,** there are seven tax rates that will be applied to the 2018 ordinary income (see the following tables).

***New Tax Rates*.** The proposal creates four tax rates and new rate for unmarried individuals:

Tax Rate	**Married Filing Jointly and Qualifying widow(er)**	**Married filing separately**	**Single**	**Head of Household**
	Taxable Income up to			
10%	19,050	9,525	9,525	13,600
12%	77,400	38,700	38,700	51,800
22%	165,000	82,500	82,500	82,500
24%	315,000	157,500	157,500	157,500
32%	400,000	200,000	200,000	200,000
35%	600,000	300,000	500,000	500,000
37%	Over 600,000	Over 300,000	Over 500,000	Over 500,000

Qualifying dividends and Net Capital Gain Brackets

For 2018, the qualified dividends and net capital gain are subject to 0%, 15%, and 20 %, or the combination of these (see the following table). These rates do not apply to long term gains subject to the 28% rate or the 25% rate for unrecaptured real estate depreciation.

Tax Rate	Married Filing Jointly and Qualifying widow(er)	Married filing separately	Single	Head of Household
	If taxable income is			
0%	$1 - $77,200	$1 - $38,600	$1 - $38,600	1 - 51,700
15%	$77,201 - $479,000	$38,601 – $239,500	$38,601 - $425,800	51,701 - 452,400
20%	Over $479,000	Over $239,500	Over $425,800	Over 452,400

Other figures

Standard Deductions

$12,000	Single / Married filing separately.
$18,000	Head of Household.
$24,000	Married filing jointly / Qualifying widow(er)

Personal and dependent exemptions

Eliminated	From 2018 trough 2025

Child Tax Credit

$2,000	Per qualifying child
$1,400	Refundable portion

EXEMPTION OF $0 UNDER TCJA WILL NOT BE USED FOR DEPENDENCY REQUIREMENTS.

Under 26 U.S. Code §152(d)(1)(B), a qualifying relative includes an individual "whose gross income for the calendar year in which such taxable year begins is less than the exemption amount."

There is no personal exemption amount anymore, and it is pretty impossible to have income less than zero. As a result, the IRS proposed regulations will make it clear that the reduction of the personal exemption amount to zero will not be taken into account to figure dependency for purposes of the $500 credit.

Similarly, the reduction of the personal exemption amount will not be taken into account to figure dependency as it relates to head of household status.

Instead, the exemption amount for the application of these provisions will be treated as $4,150, as adjusted for inflation, for years in which the exemption amount is zero (2018 through 2025). According to the IRS, this interpretation is consistent with 26 U.S. Code §151(d)(5), which states that "[f]or purposes of any other provision of this title, the reduction of the exemption amount to zero under subparagraph (A) shall not be taken into account in determining whether a deduction is allowed or allowable, or whether a taxpayer is entitled to a deduction, under this section."

ONLY ONE FORM 1040 WITH MULTIPLE SCHEDULES.

The IRS is working on a draft version of the 2018 Form 1040, *U.S. Individual Income Tax Return*, that reduces the size of the form to two half-pages in length and eliminates more than 50 lines, compared to the 2017 version of the form. The draft form moves many items that in the past have appeared on the face of the 1040 to various new schedules. The new 1040 – about half the size of the current version -- would replace the current Form 1040 as well as the Form 1040A and the Form 1040EZ.

The 2018 draft form, uses the first page to gather information about the taxpayer and any dependents and for the taxpayer's signature. The second page gathers information on the taxpayer's income, deductions (including a new line for the Sec. 199A qualified business income deduction), credits, and taxes paid. Many of the items reported on the 1040 will be calculated on various new schedules. These schedules include:

- Schedule 1, *Additional Income and Adjustments to Income*, includes items from lines 10 through 37 of the 2017 Form 1040, such as business income, capital gains or losses, and adjustments including educator expenses and student loan interest expense.

- Schedule 2, *Tax*, includes items from lines 44 through 47 of the 2017 Form 1040, such as the tax on a child's unearned income (commonly called the kiddie tax), the alternative minimum tax (ATM), and any excess premium tax credit that must be repaid.

- Schedule 3, *Nonrefundable Credits*, includes items from lines 48 through 55 of the 2017 Form 1040, such as the foreign tax credit, the credit for child and dependent child care, the education credit, and the residential energy credit.

- Schedule 4, *Other Taxes*, includes items from 57 through 63 of the 2017 Form 1040, such as household employment taxes, the health care individual responsibility payment for 2018 only; the net investment income tax, and the additional Medicare tax. It also includes a new line for reporting the Sec. 965 net tax liability installment from Form 965-A — a form that does not yet exist.

- Schedule 5, *Other Payments and Refundable Credits*, includes items from lines 65 through 74 of the 2017 Form 1040, such as estimated tax payments, the net premium tax credit, and amounts paid with an extension request.

- Schedule 6, *Foreign Address and Third Party Designee*, provides taxpayers who have a foreign address a place to list their country, province, and postal code (formerly these appeared on page 1 of the 1040) and provides all taxpayers with a place to list information for a third-party designee who can discuss the return with the IRS.

The form will keep some of the existing schedules. These include Schedule A, *Itemized Deductions*, Schedule C, *Profit or Loss From Business*, Schedule D, *Capital Gains and Losses*, Schedule E, *Supplemental Income and Loss*, Schedule F, *Profit or Loss From Farming*, Schedule H, *Household Employment Taxes*, Schedule SE, *Self-Employment Tax*, and Schedule 8812, *Child Tax Credit*.

REMINDER ITINs AND SSNs ASSIGNED AFTER APRIL 15 ARE NOT VALID FOR ANY PREVIOUS YEAR.

Under Protecting Americans from Tax Hikes (PATH), taxpayers were required to have their identification number assigned before the due date of the original income tax return. Under the TCJA, the same principle will apply with the only difference that a SSN is required for dependents claiming the Child or Additional Child Tax Credit.

The provision denies to any taxpayer the EITC, the Child Tax Credit, the Additional Child Tax Credit and the American opportunity tax credit, with respect to any taxable year for which such taxpayer has a taxpayer identification number that has been issued after the due date for filing the return for such taxable year. In other words, taxpayers who got their identification number after April 15, will not qualify for those credits for any previous year. If taxpayer is filing the original income tax return for 2017 with an ITIN application in May of 2018, the IRS will deny any credit mentioned before because taxpayer did not have an identification number assigned before the due date. The same principle applies to amended returns.

Example. *Luis is filing his original income tax return for 2017 in May of 2018; he did not have ITIN in 2017. Luis is filing his tax return with the Form W7,* Application for IRS Individual Taxpayer Identification Number. *The income tax includes two children who are U.S. citizens; one of them is age 6 and the other age 8. The IRS will deny the Child Tax Credit because Luis did not have his ITIN or SSN assigned before April 15, 2018.*

Similarly, a qualifying child (in the case of the EITC and child credit) or a student (in the case of the American opportunity credit) is not taken into account with respect to any taxable year for which such child or student is associated with a taxpayer identification number that has been issued after the due date for filing the return for such taxable year.

REMINDER UNDER NEW TCJA, THE SSN IS REQUIRED FOR ALL QUALIFYING CHILDREN CLAIMING CTC AND ACTC. TAXPAYERS ARE NOT REQUIRED TO HAVE SSN, YET.

In order to claim the credit Child Tax Credit or the Additional Child Tax Credit, each child’s SSN is now required under the TCJA. Other forms of taxpayer identification, such as an ITIN or ATIN, no longer suffice. SSNs are only available to U.S. citizens, aliens who are lawfully admitted into the U.S. for permanent residence or work, and other aliens who can lawfully work in the U.S. Although there is no express requirement that a taxpayer claiming the credit for himself or herself be a U.S. citizen or resident, as a practical matter, taxpayers with questionable citizenship or residency status will likely be hesitant to claim the credit. This does not mean that they cannot file and get the credit.

IRS PENALIZES DEBT RELIEF FIRM FOR MISREPRESENTATION UNDER CIRCULAR 230.

The IRS Office of Professional Responsibility (OPR) set a monetary penalty to a tax practitioner for violating professional rules of conduct set forth in Circular 230. His firm also accepted responsibility for knowing the practitioner engaged in misconduct in attracting clients with outstanding collection issues.

The practitioner agreed to five years of probation and a 12-month suspension of practice before the IRS if the probation is violated. The firm agreed to a monetary penalty based on a percentage of the gross income from the misconduct.

"Monetary penalties are generally not part of Circular 230 cases but in this situation, we concluded it provided a way to limit the practitioner's ability to profit from his misconduct," said Stephen Whitlock, Director of OPR. "A five-year probationary period with the threat of losing practice privileges before the IRS should send a strong warning to anyone tempted to mislead taxpayers with false claims."

Circular 230 prohibits tax practitioners from using public or private communication that contains false, fraudulent, coercive, misleading or deceptive statements. It also prohibits practitioners from using false or misleading solicitations to procure business.

In this case, the practitioner created false advertising designed to mislead potential clients to believe the firm successfully helped thousands of taxpayers and employed multiple attorneys, enrolled agents, CPAs and former IRS employees. In fact, the practitioner is an enrolled agent and the only Circular 230 practitioner at the firm.

The false advertising was also intended to mislead potential clients to believe that hiring a private firm was virtually their only hope of resolving their tax issues due to alleged widespread misconduct by IRS employees. The advertising also falsely inflated the chances of tax relief for clients by inflating the percentage of clients receiving offers in compromise (OIC) and claiming none of these OICs were above a small percentage of outstanding taxes due.

Settlement agreements are common in Circular 230 cases when the practitioner acknowledges a violation and commits to tangible actions to prevent future violations. The level of sanction imposed in this case reflects the practitioner's cooperation with OPR's inquiry and corrective action taken by the practitioner. The settlement agreement includes authorization for disclosures made in this press release.

In general, only attorneys, CPAs, EAs, enrolled actuaries and enrolled retirement plan agents may represent clients in proceedings before the IRS.

ITINS REQUIRED TO BE RENEWED BEFORE 2018 ENDS.

ITINs that have not been used on a federal tax return at least once in the last three consecutive years will expire Dec. 31, 2018. In addition, ITINs with middle digits 73, 74, 75, 76, 77, 81 or 82 will also expire at the end of the year. These affected taxpayers who expect to file a tax return in 2019 must submit a renewal application before December 31, 2018.

<u>ITIN that expired already in 2017</u>. ITINs with middle digits of 70, 71, 72, 78, 79 or 80 have previously expired. Taxpayers with these ITINs can still renew at any time.

Spouses or dependents residing inside the United States should renew their ITINs. However, spouses and dependents residing outside the United States do not need to renew their ITINs unless they anticipate being claimed for a tax benefit (for example, after they move to the United States) or if they file their own tax return. That's because the deduction for personal exemptions is suspended for tax years 2018 through 2025 by the TCJA.

Taxpayers with an ITIN that has middle digits 73, 74, 75, 76, 77, 81 or 82, as well as all previously expired ITINs, have the option to renew ITINs for their entire family at the same time. Those who have received a renewal letter from the IRS can choose to renew the family's ITINs together, even if family members have an ITIN with middle digits that have not been identified for expiration. Family members include the tax filer, spouse and any dependents claimed on the tax return.

The IRS no longer accepts passports that do not have a date of entry into the U.S. as a stand-alone identification document for dependents from a country other than Canada or Mexico, or dependents of U.S. military personnel overseas. The dependent's passport must have a date of entry stamp, otherwise the following additional documents to prove U.S. residency are required:

- U.S. medical records for dependents under age 6,
- U.S. school records for dependents under age 18, and
- U.S. school records (if a student), rental statements, bank statements or utility bills listing the applicant's name and U.S. address, if over age 18.

FUTA RATE REDUCED FOR CALIFORNIA LOAN REPAID IN 2018.

The US Department of Labor's FY 2018 Unemployment Insurance Outlook Midsession Review indicates that the states (California and the Virgin Islands) that are currently borrowing from the federal government are expected to repay their loan balances by the end of fiscal year 2018.

If California does not borrow in 2018, the federal unemployment insurance (FUTA) tax rate will return to normal (a net 0.6%) for calendar year 2018 for California employers. Much of what EDD collects from employers in UI contributions is collected in the first part of the year. As of May 11, 2018, the trust fund had a positive balance of approximately $3.2 billion. Therefore, based on the EDD's forecast, and provided that California does not require additional federal loans to pay benefits, employers should see their FUTA taxes return to the minimum allowed for calendar year 2018.

Beginning on January 26, 2009, California borrowed from the federal government to pay UI benefits. As of December 8, 2017, California had an outstanding federal UI loan balance of $870,349,347. Because the state did not repay all its federal UI loans by November 10, 2017, employers experienced a 2.1% FUTA credit reduction for calendar year 2017 (for a total FUTA rate of 2.7%), that was paid with the employers' fourth quarter 2017 FUTA tax deposit, which was due on January 31, 2018.

CREDIT REPORTING COMPANIES NOT ALLOWED TO CHARGE FOR FREEZING AND UNFREEZING SERVICES.

Credit reporting companies such as Equifax, Experian, and TransUnion are required to let consumers freeze and unfreeze their credit files free of charge.

The provision is part of a bipartisan bill signed Thursday by President Donald Trump that rolls back certain Dodd-Frank financial rules that Congress approved after the 2008 financial crisis. Before, consumers could pay up to $10 to freeze their credit reports, depending on where they live.

Along with the free credit freezes are some other benefits. Consumers now have the right to place a fraud alert on their credit file at no cost for one year. In addition, victims of identity theft are entitled to an extended fraud alert lasting seven years.

Each credit reporting agency is required to create a web page that allows consumers to request security freezes and fraud alerts, and opt out of the use of their information by companies marketing credit or insurance products.

CALIFORNIA ADJUSTED REFUNDS WILL NOT BE MAILED OUT IN CHECKS IF DIRECT DEPOSIT WAS SELECTED.

Historically, when the FTB made an adjustment to a refund requested in the form of a direct deposit, the FTB would issue a paper check and mail a notice explaining why the tax return was changed. This often resulted in a delay in receiving the refund.

Beginning July 2018, in most cases, if there is a change made to a refund, the taxpayer will still receive their refund via direct deposit. Only the notice explaining the change will be mailed. Because it is possible that the revised refund will be deposited prior to the notice explaining the change arriving in the mail, taxpayers must wait for the notice before calling about their refund.

The notice explaining the change will also be available in MyFTB. If a taxpayer requested the refund be deposited into 2 separate accounts, the FTB will adjust the deposit using these rules:

- If the adjustment results in a **reduced** refund, the FTB will deduct the difference from the second account. If the difference exceeds the amount requested for the second account, the FTB will deduct the remainder from the first account.
- If the adjustment results in an **increased** refund, the FTB will add the difference into the second account.

As a reminder, increased refund amounts to specific account types may need the client's attention.

- If the refund was deposited in an account that has a contribution limit, the taxpayer may need to arrange to withdraw the excess contributions.
- If the refund was deducted as a contribution to a tax-favored account (such as an IRA or 401K), the taxpayer may need to file an amended return.

THE WAYFAIR DECISION. ONLINE SALES TAX, NO BUSINESS OFFICE IS REQUIRED.

In 2018, in a five-to-four decision, the Supreme Court has ruled that states can make online businesses collect sales taxes even if they don't have a physical presence in that state.

This new ruling overturns a decision from the Court in 1992 (Quill Corp. v. North Dakota) that paved the way for the explosion of online retail in the United States. This decision ruled that companies need to have at least some physical connection with a state for that state to require that company to pay taxes.

Decision to charge sales tax to online sales rest on each state. While the ruling opens the door for states to collect taxes from online businesses, there are some significant outstanding questions regarding this decision. For instance, the court did not rule out the possibility that states may not collect taxes on all online purchases, given the negligible size of some transactions. And the court didn't say whether states could retroactively seek sales taxes. That's a big issue, considering that e-commerce sales in the U.S. were $435.5 billion in 2016, versus $180 billion in mail-order sales in 1992 when the court issued its first ruling on interstate sales and taxes.

Some states may adopt laws that emulate South Dakota's in every respect. Other states may adopt laws that adopt only some of the features, and that would likely be subject to further litigation. Some states may not act until their next regular legislative session, while others may never act.

Congress may act to establish a minimum standard for states that wish to collect sales tax on interstate sales. A federal standard would create certainty for sellers and consumers and ensure that every state meets certain simplification guidelines.

No big change on the e-commerce for big companies. The Act covers only sellers that, on an annual basis, deliver more than $100,000 of goods or services into the State or engage in 200 or more separate transactions for the delivery of goods or services into the State.

For most large online retailers (including Amazon — the country's largest), the decision will have little impact, since they've been voluntarily paying state sales taxes for years. Instead, the burden will be on earlier-stage companies that do not have the same sort of scale and which will be facing more operational costs as a result.

If states simplify their tax systems as set out by Wayfair, there will likely be only small changes in the e-commerce landscape. Sellers may need to monitor their new compliance requirements and seek a new software solution, but these costs can be minimized if states provide the necessary simplifications and protections. However, if some states ignore the features of the South Dakota law in crafting their own laws, and put crushing burdens on interstate sellers, there will be more litigation and a higher potential for action by Congress.

THE DYNAMEX DECISION. A CALIFORNIA DECISION OVER EMPLOYEE OR INDEPENDENT CONTRACTOR CLASSIFICATION.

On April 30, 2018, The California Supreme Court issued a landmark decision in the matter of Dynamex Operations West, Inc. v. Superior Court of Los Angeles. The California Supreme Court reinterpreted and rejected the Borello test for determining whether workers should be classified as either employees or independent contractors.

The court's opinion in Dynamex v. Superior Court of Los Angeles County has a lot of trucking companies in panic mode, scrambling to figure out how the ruling will affect their operations. The ruling could also have a profound impact on many companies like Uber, Lyft, Instacart, and others that provide on-demand services.

All workers are employees. In particular, the Court embraced a standard *presuming* that all workers are employees instead of contractors, and placed the burden on any entity classifying an individual as an independent contractor of establishing that such classification is proper under the newly adopted "ABC test".

The ABC Test. The Dynamex court rejected the Borello test and replaced it with the so-called ABC test that several states have adopted. Under the ABC test, a worker will be deemed to have been "suffered or permitted to work," and thus, an employee for wage order purposes, unless the putative employer proves:

A. that the worker is free from the control and direction of the hiring entity in connection with the performance of the work, both under the contract for the performance of the work and in fact;

B. that the worker performs work that is outside the usual course of the hiring entity's business; and
C. that the worker is customarily engaged in an independently established trade, occupation, or business of the same nature as the work performed.

Note that each of these requirements needs to be met in order for the presumption that a worker is an employee to be rebutted, and for a court to recognize that a worker has been properly classified as an independent contractor.

The court noted that in many states a common element of the ABC test "provide[s] that a hiring entity may satisfy part B by establishing either (1) that the work provided is outside the usual course of the business for which the work is performed, or (2) that the work performed is outside all the places of business of the hiring entity." (Emphasis added)

However, the court deliberately removed the latter element from part B of its new standard, which will make it difficult to classify an individual as an independent contractor unless that person has essentially no connection to the employer's business. In other words, employers in California that rely on independent contractors are about to discover that the California supreme court may have just put their business model in jeopardy.

What Does the Dynamex Decision Mean for Businesses? The question of whether an individual worker should be classified as an employee or independent contractor has considerable significance for workers, businesses, and the public generally. If a worker is classified as an employee, the employer bears the responsibility of paying Social Security and payroll taxes, unemployment insurance taxes and state employment taxes, providing worker's compensation insurance, and of course, complying with the endless labyrinth of state and federal statutes governing the wages, hours, and working conditions of employees.

Indeed, many businesses, particularly those operating in the "gig economy," are fundamentally premised on the use of independent contractors. In light of this case, any businesses operating in California that treat workers as independent contractors should confer with their legal counsel to review the relationship under the "ABC test" and determine whether any or all such workers should be reclassified. Barbers, tattoos and other companies are worried.