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FROM THE CHAIR

A Time to Reflect

By Karen L. Hawkins, Hawkins Law, Yachats, OR

In my first Chair’s letter last August, I wrote:

The Tax Section has been (and continues to be), for me, a major source of academic improvement, skill development, and strong personal bonding. It is no exaggeration to say that I am who, and where, I am today because of my 39-year engagement with the Section of Taxation and its members. In 2009, I was eager to give back to the Section in payment for all the benefits I had received as a member. My enthusiasm in that regard has not wavered with the passage of time. It is this history and relationships that I think of as I prepare to assume the Chair position in August.

Well, the Fat Lady is about to sing on my year as Chair. I’m told this is a time to reflect and assess.

First, given unforeseen interventions, on August 7th, I will have completed what I set out to do in August 2008: lead the Section of Taxation as its Chair. I highly recommend a less circuitous route for anyone interested in doing the same.

Second, I did not think it was possible, but I am even more impressed with Tax Section members every year. Our committees are loaded with talented, bright, enthusiastic people ready to step up and help on a moment’s notice. In light of the passage of the Tax Act of 2017, late in the year, there were, and continue to be, calls for comments, feedback, and informal observations throughout the public and private sectors. Numerous of our committees have done yeopersons’ work in responding to the numerous requests from Treasury and IRS on various aspects of the new legislation—all in a timely manner. The comments have been exceptionally well-received and continue to solidify the Section’s status as the premier professional tax organization in the U.S. Since last August, 28 formal comments have been submitted to Treasury and IRS on the Tax Act as well as other matters. All are accessible here. Further, informal participation in IRS focus groups has made the Section’s position known on important tax administration issues. Our courtesy calls with Treasury and the IRS resulted in needed adjustments to estate tax administration issues and in the Appeals process. None of this activity would have been possible without the corps of volunteers within the Section making their repeated contributions. I am proud to have led the Section during this time.

Third, the Tax Section has the best administrative staff on the planet! I know this has been a regular mantra of mine, but I mean it. Every member of the staff gives 110%. Our live meetings have been artfully orchestrated by Haydee Moore, Director of Meetings, and her staff, with able assistance from the entire Section staff who pitch in behind the scenes as well as onsite to ensure events run smoothly at every
venue. My decision to increase webinar offerings to members (helped along a bit by the 2017 Act) was made technically and administratively possible by Chris Tank, Director of CLE, and his staff. To date, the Section has offered 18 paid or free webinars on a myriad of technical and practice-oriented topics with a viewership pushing 3,500. Council’s decision to shift The Tax Lawyer editorial collaboration to Northwestern University Pritzker School of Law’s Tax LL.M. Program has been undergoing a smooth summer transition under the watchful eye of Anne Dunn, former Director of Publications, and her staff. Several other Section publications in print and digital format were released this year as well. Anne, who retired at the end of March, has remained with us as a consultant through the end of August. Her contributions over the years have been invaluable, and she will be missed. Megan Newman joined us late last year as the Section’s Chief Counsel, a position consolidated from the legislative counsel and pro bono counsel positions of prior years. As such, her challenge has been to juggle multiple disparate projects on an on-going basis. She assists with nearly every aspect of Section activity from comment letters to pro bono projects. I couldn’t be happier with her responsiveness or her enthusiasm. Arnyae Neal also joined us late last year to tackle the Section’s essential membership and marketing needs, and we have already benefitted from her talents in increased attendance at our meetings. One of the least sexy, but most critical, aspects of Section business is managing the finances. Real time information is critical in the decision-making required for all aspects of Section activities. Ty Hansen, our steadfast Associate Director, works diligently to provide the officers with the information they need to make timely financial choices. Oversight of this phenomenal staff falls to John Thorner, Executive Director. John, who joined us in May 2017, encountered a steep learning curve (we are an eccentric group, after all) but has risen to the occasion and is playing a key role in the Section’s many activities. It has been an honor and a privilege to work with such talented and dedicated people.

Fourth, the Section Vice-Chairs ROCK! I cannot say enough about the support I have received from the Section’s six Vice-Chairs. Bahar Schippel, Vice-Chair (Pro Bono and Outreach), has worked hard to get the Section to the next level in its pro bono commitments by launching the Elder Tax Law Initiative, in addition to maintaining our many other on-going pro bono opportunities. Fred Murray, Vice-Chair (CLE), has done a stellar job of overseeing the Section’s phenomenally successful webinar series and generally overseeing all the Section’s many other CLE offerings. Scott Michel, Vice-Chair (Committee Operations), streamlined the Committee governance process to facilitate more active, meaningful involvement among Council Directors and the committees they oversee. He also accommodated my desire to eliminate the Incoming Chair/Vice-Chairs’ Breakfast Meeting traditionally held at 7:30 am during Section Meetings—an ungodly hour for those of us travelling from the west coast—in favor of adopting more modern methods of communications with the committees. Thank you, Scott! Julie Divola, Vice-Chair (Publications), worked tirelessly to bring about our new contractual relationship with Northwestern University for editorial support of The Tax Lawyer. The fruits of her labor will be seen in the Fall edition of our journal. Julian Kim, Vice-Chair (Government Relations), in addition to shepherding all the Section’s many timely comments through the COGS process, oversaw the arrangements and agenda for our government courtesy calls last fall which resulted in productive and continuing dialogue with Treasury and the IRS on a number of tax administration issues. Last, but certainly not least, Chuck Rettig, despite the distractions of being nominated to be Commissioner of the Internal Revenue Service, stayed the course as Vice-Chair (Administration), working to put a revised investment policy in place and creating an Investment Advisory Committee to support the VCA’s responsibility for sound fiscal management of the Section. I am indebted to each of these individuals beyond measure for ensuring that I not only survived my year as Chair, but that I actually enjoyed myself in the process!

Fifth, Council Directors play an invaluable role in the overall well-being of this volunteer organization. There are 15 Council Directors who rotate in/out in classes of five every three years. Each has responsibility for overseeing the smooth running of multiple substantive committees. I want to thank the class of 2018 as
they rotate off Council (hopefully to play some other meaningful role in Section administration) for their enthusiasm, support, commitment and tolerance during my year as Chair: Carol Tello, Tom Greenaway, John Bergner, Roberta Mann and Gary Wilcox.

Sixth, our two members of the House of Delegates, Dick Lipton and Armando Gomez, are invaluable in ways too numerous to describe in this letter. Their continued involvement and support are critical to the future of the Tax Section. Thank you both, gentlemen.

Last, I want to acknowledge Eric Solomon's role as Chair-Elect during this past year. While we collaborated on many issues as a team, I especially appreciate his responsiveness to my request for an updated Diversity and Inclusion Plan for the Section which, along with his establishment of a new Committee on Diversity and Inclusion in the Profession, ensures the Section’s long-standing commitment is properly documented and viable well into the future.

A year serving as Chair of this Section seemed like a long time in August of 2017. Now as I approach August of 2018, I feel there is so much I won't have time to finish (or start). That's why succession is so important. Building on the positive legacies of those who came before you ensures those coming behind you will do the same. As I said in my first letter:

Every chair wants to leave a legacy of some sort. And unquestionably each has. I don't want to fumble my opportunity. Of course, much of what happens during my year as Chair will not be in my control. External forces: tax legislation, government allocation of resources, and unanticipated political events will all, no doubt, impact my personal agenda as well as the Section’s activities and involvement.

In retrospect, we have been nimble, responsive, thoughtful, relevant and timely. I am very proud about how the Section has performed over the past year. I hope many of you feel the same.
FROM THE CHAIR-ELECT

The Coming Year

By Eric Solomon, Ernst & Young LLP, Washington, DC

It is an honor for me to be the next Chair of the Tax Section, and a privilege to have the opportunity to serve our members, the tax community and the public.

We operate in an evolving environment that requires us to recognize and anticipate change and adapt to it. The Tax Section is not immune from the need to see the trends and proactively respond to them. We need to be constantly evaluating our offerings and operations to improve them in light of the shifting needs of our stakeholders. With this in mind, as Chair I wish to continue and enhance the programs and initiatives of my predecessors, at the same time taking steps to position the Tax Section to thrive in the future.

With the assistance and support of an excellent team of Section Officers, Council, Committee Chairs and Tax Section staff, I look forward to focusing on the following areas in the coming year.

Pro Bono & Public Service

One of the most important contributions of the Tax Section is pro bono services. These activities include: (1) the Elder Tax Law Initiative, started by our current Chair Karen Hawkins, which provides tax assistance to this growing share of our population; (2) the Adopt-A-Base program, led by Wells Hall, which helps military personnel prepare their tax returns; (3) the Partnering for Pro Bono program, in which volunteer attorneys work with low-income taxpayer clinics; (4) the Calendar Call program, in which volunteer attorneys provide national coverage at Tax Court calendar calls; (5) the Volunteer Income Tax Assistance (VITA) program, where practitioners help prepare tax returns for low-income taxpayers; (6) pro bono CLE webinars, where experienced low-income tax practitioners share their knowledge and experience; and (7) assistance to victims of natural disasters, where volunteers advise affected individuals regarding the tax implications of their losses.

These programs were recently highlighted at the Welcome Reception at the May meeting of the Tax Section in Washington, DC. Under the energetic leadership of Bahar Schippel, Vice Chair for Pro Bono and Outreach, the Tax Section endeavors to help low-income individuals understand and comply with their tax obligations, as well as to resolve their tax difficulties. The Tax Section provides opportunities for attorneys interested in pro bono work by encouraging them to participate in these programs as well as pro bono programs in their communities.
In addition, through the Tax Assistance Public Service (TAPS) fund, members of the Tax Section support the Christine Brunswick Public Service Fellowship Program, which enables new tax lawyers to spend two years providing services to low-income taxpayers.

I express my gratitude and respect for those members who contribute their time or resources to pro bono efforts and encourage all members to contribute in some manner. Interested persons can volunteer by contacting Bahar Schippel (bschippel@swlaw.com), or Meg Newman, the Tax Section's General Counsel (megan.newman@americanbar.org).

**Continuing Legal Education**

One of the greatest strengths of the Tax Section is its continuing education offerings provided in many forms, including at the three annual meetings, other conferences, and webinars. The three annual meetings are an excellent forum for Tax Section committees to present insightful panels about the tax law, especially now after the enactment of the 2017 Tax Act. Under the leadership of Fred Murray, Vice Chair for Continuing Legal Education, the Tax Section is also hosting numerous timely and informative webinars.

The Tax Section's programs will be a timely and informative source of education about the forthcoming regulatory and other guidance interpreting the 2017 Tax Act. I am sure you will want to attend our Fall Tax Meeting with the Real Property, Trust and Estate Law (RPTE) Section in Atlanta, GA, on October 4-6, 2018, at which you will hear from fellow practitioners and government officials about the latest developments.

**Government Relations**

The Treasury Department actively seeks comments on issues requiring regulatory and other published guidance. Enactment of the 2017 Tax Act provides a special opportunity for the Tax Section to assist in the rulemaking process by submitting comment letters on various issues in the domestic and international tax areas. The Tax Section will also communicate with government officials through periodic meetings with Treasury’s Office of Tax Policy, the IRS, and Hill staff. Under the leadership of incoming Vice Chair for Government Relations Eric Sloan, Tax Section committees will be preparing comment letters that will assist the Treasury Department in identifying and addressing the numerous issues arising from the 2017 legislation.

**Diversity and Inclusion**

The Tax Section is committed to diversity and inclusion. At the 2015 May meeting of the Tax Section, Tax Section Officers and Council approved a Diversity and Inclusion (D&I) Plan, which was prepared by a task force chaired by our next Chair-Elect, Tom Callahan. As stated in the D&I Plan, the plan seeks to encourage full and equal participation in the Tax Section by lawyers and law students with diverse backgrounds and perspectives, including individuals of color, women, members of the LGBTQ+ community, Native Americans, individuals of diverse national or religious backgrounds, individuals of diverse ethnic or cultural heritages, individuals with disabilities, military veterans, and individuals of diverse ages and professional experiences.

Last year, Chair Karen Hawkins initiated a project, led by me, to update the D&I Plan. As a result of this review, changes were proposed and approved by Section Officers and Council at the 2018 May meeting of the Tax Section. As additional best practices are identified and lessons are learned, the Tax Section will continue to evaluate the D&I Plan to ensure its effectiveness. The updated D&I Plan can be found on the Tax Section website.
As the Tax Section continues to implement actions in its D&I Plan, we must also be mindful of other negative practices, attitudes, and behaviors that are contrary to the welcoming environment we strive to achieve. The Tax Section embraces ABA policy that verbal, sexual, or physical harassment of any kind that disrupts another person’s duties or job performance or that creates an intimidating, offensive, abusive or hostile work environment is unacceptable.

Leadership Team

The Tax Section has an excellent leadership team for 2018-2019. Tom Callahan, who has devoted many years to the Tax Section, is the Chair-Elect. Bahar Schippel returns for another year as Vice Chair for Pro Bono and Outreach, and Fred Murray returns for another year as Vice Chair for Continuing Legal Education.

I look forward to working with Larry Campagna as the new Vice Chair for Administration, Megan Brackney as the new Vice Chair for Committee Operations, Eric Sloan as the new Vice Chair for Government Relations, and Keith Fogg as the new Vice Chair for Publications.

I want to express my special thanks to the outgoing Vice Chairs. Julie Divola, outgoing Vice Chair for Publications, negotiated an agreement whereby Northwestern University has succeeded Georgetown University as the collaborating partner in the publication of *The Tax Lawyer*. Julie was ably assisted by Anne Dunn of the Tax Section staff. Under the leadership of Scott Michel, outgoing Vice Chair for Committee Operations, the Tax Section has improved various aspects of committee governance. Under Julian Kim, outgoing Vice Chair for Government Relations, the Tax Section has submitted numerous comment letters to the government and has held successful meetings with Treasury’s Office of Tax Policy and the IRS.

The Tax Section’s Council members for the 2018-2019 year include Gregg Barton, Adam Cohen, Michael Desmond, Sheri Dillon, Catherine Engell, Diana Erbsen, Mary Foster, George Hani, Anthony Infanti, Ronald Levitt, Peter Lowy, Chris Rizek, Julie Sassenrath, David Wheat and Melissa Wiley. Katherine David will continue as Secretary and Robb Longman as Assistant Secretary. I look forward to the active engagement of Council members in Tax Section matters and with their assigned committees. I also wish to acknowledge the efforts of all the committees and their officers, who are responsible for so much of the work for which the Tax Section is recognized.

In addition, I want to extend special thanks to Bill Caudill, former Chair of the Tax Section, as well as Chuck Rettig (outgoing Vice Chair for Administration), Scott Michel, and Ty Hansen. During his chairmanship, Bill formed a working group with these individuals to take immediate and effective steps to address the worsening financial situation of the Tax Section. Karen Hawkins has continued the focus on improving the Tax Section’s financial status and I am committed to this task as well. It is essential for us to control expenses and seek additional ways to increase revenue. We will do our utmost to provide the best services to our members, the tax community and the public in a fiscally prudent manner.

Finally, I would like to recognize the support and counsel of Dick Lipton and Armando Gomez in their role as Section Delegates to the ABA House of Delegates. They are the eyes and ears of the Tax Section regarding the Section’s relationship with the larger ABA, which like the Tax Section is changing as circumstances require.

Staff Team

The Tax Section is supported by a talented staff. The success of Tax Section operations, especially the annual meetings, is largely because of the efforts of the Tax Section staff. We are grateful for the work of
John Thorner (Executive Director), Ty Hansen (Associate Director), Haydee Moore (Director of Meetings), Chris Tank (Director of CLE), Meg Newman (General Counsel), and Arnyae Neal (Director of Membership and Marketing).

I want to express my particular thanks to Anne Dunn (Director of Publishing), who has done such a tremendous job regarding all the Tax Section’s publications for many years. Anne is retiring from the Tax Section. We will greatly miss her professionalism, knowledge, and experience. We wish her all the best in her future endeavors.

**Closing Thoughts**

Like all incoming Chairs of the Tax Section, I am daunted to follow so many dedicated and effective previous Chairs. My task is particularly difficult because I follow Karen Hawkins, who has given so much to the Tax Section and the tax system for so many years. As I said at the Plenary Luncheon at the May Meeting, Karen has displayed her commitment in many ways, including her commitment to pro bono, her commitment to diversity and inclusion, her commitment to serving small firms and solo practitioners, and her commitment to the tax system, particularly in her government service as head of the IRS Office of Professional Responsibility and in her many roles for the Tax Section.

I am honored to be Chair-Elect of the Tax Section and I look forward to the opportunities and challenges of the role. I know we will work together to maintain the highest level of service to our members, the tax community and the public.
Interview with Steven M. Rosenthal

By Thomas D. Greenaway, KPMG LLP, Boston, MA

Editor’s Note: Steven M. Rosenthal is a long-time participant in the Washington D.C. tax community in both public and private roles. He is currently a senior fellow in the Urban-Brookings Tax Policy Center where his research and writing focus primarily on business tax issues.

Q Steve, welcome and thank you for taking the time to speak with Tax Times. Many of our readers are curious about how people decide on tax careers, so can you tell us how you came into tax?

A Well, I arrived at tax in a linear fashion. I grew up in San Diego, California, where I attended public schools and then the University of California at Berkeley. I majored in math and economics, but I was always interested in public service, in making a difference. After I finished college, I moved from California to Washington, D.C., where I worked as a research assistant in President Carter’s White House. That was a fascinating year in which I got to observe economists, lawyers, and other professionals. I was planning to be an economist, but I saw lawyers doing a lot of important things. After my year in D.C., I studied economics and public policy at Harvard, but I decided to go to law school. At Harvard, I explored fields of economics that had an overlay with law, in order to select a field of law that played to some of my analytical strengths. I studied public finance at Harvard with a couple of brilliant economists, Marty Feldstein and Alan Auerbach. I discovered that we order much of our social and economic relations through the tax law. I easily concluded this was the field for me!

The next step was to begin law school at Berkeley. At the same time, I started working as a legal research assistant for the IRS Appeals Office in San Francisco—and worked there for three years. The Appeals Officers hired me before I knew any tax law, but they taught me. There wasn’t too much tax at Berkeley.

After I finished law school, I decided to pursue tax law in D.C. I started out in private practice. One of the nice things about practicing tax in D.C. is that you can simply change a subway stop and change your practice, like working in the government. And the nature of tax practice in D.C. differs from anywhere else. It focuses on the industry of the town: the government.
Q Steve, you’ve worked in a number of different settings. Can you help us compare practicing tax in an accounting firm and practicing tax at a law firm?

A Oh, sure. I started with a big law firm in D.C, Wilmer, Cutler & Pickering. After a few years there, I had an opportunity to work for the Joint Committee on Taxation of the U.S. Congress. I helped develop and draft tax legislation for six years. That was long enough; I was ready to return to practice. At the time—this was the mid-1990s—the accounting firms were aggressively expanding and KPMG made me a very attractive offer: a short path to partnership; the chance to practice in a field that I really enjoyed, financial transactions and financial services; and the ability to stay in D.C., without having to move to New York. At KPMG I was the National Director, Technical, for the Financial Services Practice for several years. Slowly, though, my role evolved and shifted as KPMG changed its priorities. I was assigned to working on tax advantaged products, which I didn’t really care for. Basically, I reviewed and helped deliver tax shelters to the field. I eventually resigned and returned to law practice, working as a partner at Miller & Chevalier and, later, at Ropes & Gray, before joining the Tax Policy Center.

Comparing the accounting and law firms is interesting. When I started at KPMG, I had not really met many accountants: I’d just known a lot of lawyers. The accountants were truly outstanding professionals, brilliant and dedicated. Many of them came from the hinterlands of the country, from schools I’d never heard of—they got to the national office through hard work and real talent. Even in the field, the accountants I saw were exceptionally engaged in the work and in trying to improve themselves. The accountants and lawyers were interchangeable.

But the major drawback I saw at accounting firms is their large size. There’s a real separation of the management of the firm from the partners, the professionals, and the staff. Decisions are made—like in a large corporation—to shift the ship, and everybody on the ship must drift in the same direction. During the 90s when I was at KPMG, management decided to shift towards delivering more tax-advantaged products. I disagreed with that direction. It’s not that I thought that tax planning is inherently wrong. I think that clients are entitled to plan their affairs and to take advantage of transactions that are properly structured and have economic substance. I just saw too many aggressive transactions that, in my judgment, crossed the line.

So I returned to private law practice. My law practice focused on helping individual clients—and I largely controlled how to help them—and what advice to offer.

During that time, I always harbored the interest of returning to public service. I expected to have a chance in the start of the Obama administration, but I had registered as a lobbyist on a small matter that disqualified me for a couple of years. So I decided to leave practice—I had done it for long enough and had made enough money—to go to a think tank to cool my heels while my lobbying ban expired. It turned out that the work here at the Tax Policy Center was fascinating, and the opportunities to contribute to the public debate are great. So that’s what I’ve been doing for the last seven years. It’s a nice situation but a different career path than most tax lawyers take.

Q How are things different for you now that you’re at a think tank versus a law firm or an accounting firm?

A Well, most importantly, my output is different. I write blogs and articles—and I tweet @stevertax. I spend a lot of time educating the press, who are very bright but don’t know tax. I help legislative and executive branch staff informally—who tap my expertise on topics. I have a lot of professional freedom and
a lot of ability to express my views based on what I think is good tax policy without advocating any cause, or advancing any client interest. I don’t bill hours very closely. Before your readership decides that this sounds like the ideal path, I have to caution that there’s very little money in it. It is, however, fulfilling.

Q Didn’t you play a role in the changes to the D.C. tax code?

A I did. As I said, I’ve been here at the Tax Policy Center for about seven years, but in the middle of those years, I split my time with the D.C. Tax Revision Commission (as Staff Director) and the Tax Policy Center. The D.C. Tax Revision Commission prepared a package of recommendations for the D.C. Council, which were adopted almost completely over time. I was the lead technical resource, coordinating more than a dozen consultants. I also had seen the tax legislative process from the Hill. Tony Williams, the Chair of our commission and a former mayor of Washington D.C., leaned on me heavily for both substantive ideas and processes, how to pull a package together. The experience was fascinating. We found that middle-class residents were paying a disproportionate tax burden compared to high-income and low-income taxpayers. D.C.’s business taxes were high, both regionally and nationally. The tax base was very narrow. There were all sorts of problems because not-for-profits were exempt, government institutions were exempt, and commuters were exempt. We had to create a package to solve all of those problems—and we did. We created a package that followed pretty much the recipe of the 1986 federal tax reform—a broader base, lower rates, fewer loopholes. We got support from across the political spectrum. The Tax Foundation, a right-leaning group, applauded our work, as did Grover Norquist. The Institute for Tax and Economic Policy, a left-leaning group, applauded our work, as did the D.C. Fiscal Policy Institute. We worked for a year and a half and saw our recommendations enacted into law within a year. It was good work that everybody liked.

Q Now that you have the benefit of a few years to see the law after it was enacted and as it played out, is it still working?

A Yes. I think D.C.’s experience turned out really well. I think everyone is really happy. The economy is vibrant. There’s great business growth. We have seen the middle-class tax relief materialize. I think some of the middle-class flight to the suburbs was reduced. A remaining problem for D.C., and a problem that plagues other cities, like Seattle and Silicon Valley and San Francisco, is that sometimes success creates additional problems. So, we see in D.C. displacement of some lower-income workers and public servants. That’s a real challenge, as is homelessness. The larger question is how do you work to make a city vibrant without leaving behind the residents who can’t keep up economically and get displaced? By and large, I’d say the D.C. tax experience worked, but there still are some issues.

Q You have been an interested observer in the work that Congress and Treasury have done and continue to do around tax reform. What are your thoughts on the 2017 federal tax legislation that we’re all now working with?

A Well, the good news is that there was, in fact, major tax legislation, which had been stymied in Congress for many, many years, if not decades. The bad news is the tax legislation fell short in several respects, both as a matter of process and substance.

The process, which I think contributes to some of the substantive shortcomings, was a very hastily thrown-together bill. There had been years of hearings to complain about the prior law. But Congress held no hearings on the structural solutions and changes that were part of the tax bill, like international tax reform or the pass-through business tax reform. To get enacted, the bill was raced through Congress without much
input from the minority party or from impartial outsiders. Unlike the ’86 act, and unlike our work in the D.C. government, there was no consensus behind this tax bill. It was passed on a strictly partisan basis. If the parties change, the tax law will change. And the consequence is two-fold: one, there are a lot of shortcomings in the legislation and two, the tax legislation is unstable.

I think the bill failed substantively on the ways we usually evaluate tax bills—on efficiency, simplicity and fairness. For example, the pass-through provisions are a complete mess. Those provisions will not be efficient, they will not be simple, and I don’t think they are fair because by and large the relief is targeted at the very top end. Another major component to the bill, lower corporate tax rates, may have been desirable, but the right approach is what we did in D.C. to bring down tax rates and to close loopholes. There wasn’t much closing loopholes. The international tax changes were original and potentially helpful. But they were passed in haste and given very little review, so they suffer from a lot of problems. I think even Chairman Brady acknowledges that the international tax reform effort fell short.

There are a lot of technical problems in the bill, which will require a major technical corrections bill. Moreover, the complexity added to the Code is going to be hard for taxpayers and the IRS to cope with. The bill is also unstable because the individual tax relief is temporary and the business tax relief is permanent. So the individual tax relief will need to be revisited.

Finally and most importantly, we use tax law to raise the funds to pay for the services that we all demand. By cutting taxes so substantially in this last tax bill, we were left with a large shortfall at a time when the services that we need will be increasing as our population ages. The CBO’s estimates of the deficits added by the new tax legislation have become significantly bigger, increasing from $1.5 trillion at passage to $2 trillion now. There is not a chance that the tax bill pays for itself. How are we going to pay for future services? Will we slash the social safety nets, like Medicare and Social Security, for our elderly? Those difficult decisions have been kicked down the road.

Q Steve, you and I have talked over the years about bar associations and the important work they do. I know you’ve been a long-time member and a leader in the ABA Tax Section and the D.C. Bar. Do you have any thoughts on how these organizations can grow and thrive and succeed both now and in the future?

A Let me start by saying these associations are phenomenally helpful for practitioners who want to develop their technical skill sets as well as their network of professional relationships. I have called upon former colleagues from the ABA and the D.C. Bar to help with problems frequently, both when I was in practice and since coming to the Tax Policy Center. In my judgment, bar associations should be oriented towards helping practitioners with technical aspects of their work and with building networks of professional colleagues.

I think bar associations should also be governed transparently and inclusively. They should not be clubby or insular. There’s a natural tendency for the leadership of any large organization to become insulated. That, I think, presents an ongoing struggle for the ABA and the D.C. Bar: how to make sure that the bar continues to be open and inclusive.

For young lawyers, to break through requires showing up. I remember when I first joined the ABA I would attend these fascinating meetings and I’d hang out afterwards to listen to the panelists continue their talk after their presentation. Then they’d wander off to dinner, and I was not included. I wondered, how can I be included? What do I need to do? There are ways to get yourself involved by working on comments and speaking up more often and the like. But it turns out that just the passage of time and effort brings you into
the process. 20 years later, when I attended ABA meetings, everyone stopped and said “hi” to me. But I remember the start of my career, so I have always tried when I go to bar meetings to stop and engage young people and meet with any young person that wants to meet for coffee or talk about practice over lunch. I think the bar associations are a great facilitator.

Q Steve, any advice for other ways tax professionals can make a difference?

A I’m a big proponent for the idea that part of a person’s professional fulfillment should be public contributions. Working in the government is one way to contribute. Bar associations and working on comments to the government are another way to contribute. What I’m doing now at a think tank is yet another way. For lawyers who don’t have the financial wherewithal to go into government and want to stay in practice and are looking for ways to contribute, I encourage them to get involved in bar associations and to do pro bono work, whether it’s tax litigation or even pro bono tax policy work. Anyone interested could reach out and speak to me, new lawyers or retiring lawyers, and I’d be eager to have their help and help them contribute to the public debate.

We’re living in really challenging times now. My fundamental view on formulating good public policy is transparency in the process and basing decisions on the evidence. That’s hard to do now, when our society seems to have such difficulty distinguishing fact from fiction. One way to help is what I’m doing now, trying to be an honest broker in the public exchange of ideas. Anyone else who’s interested in doing something like I am doing, I encourage them to try.

Q Well, thank you, Steve, that’s inspirational stuff. We very much appreciate your time.

A Sure. Thank you for allowing me to share my thoughts.
Farewell Physical Presence: Was the U.S. Supreme Court’s Decision Way Off, or Way . . . Fair?

By Jennifer Weidler Karpchuk, Chamberlain Hrdlicka, Philadelphia, PA

Must a taxpayer have physical presence to be subjected to sales tax collection obligations in a state, or is such a requirement antiquated and unrepresentative of the virtual world in which we live? That is the issue the U.S. Supreme Court grappled with in South Dakota v. Wayfair.\(^1\) State and local tax practitioners debated the issues in the case for months leading up to the U.S. Supreme Court’s June 21, 2018, monumental decision overturning 50 years of precedent. With a 5-4 decision and a lively oral argument, there is no doubt that the Justices were engaging in some heated debate of their own. At oral argument, Justice Breyer summed up the complex polarity well.

> When I read your briefs, I thought absolutely right. And then I read through the other briefs and I thought absolutely right. And you cannot both be absolutely right.\(^2\)

Justice Breyer would end up joining the dissent; what he and three other Justices ultimately viewed as the “absolutely right” outcome, the majority found to be absolutely wrong.

The majority’s opinion came down to the idea of fairness and of righting the wrongs created by the Court’s prior “physical presence” decisions—but did it achieve that goal? The majority asserts that “Quill created an inefficient ‘online sales tax loophole’ that gives out-of-state businesses an advantage.”\(^3\) It goes on to classify the physical presence requirement as “unfair and unjust.”

> It is unfair and unjust to those competitors, both local and out of State, who must remit the tax; to the consumers who pay the tax; and to the States that seek fair enforcement of the sales tax, a tax many States for many years have considered an indispensable source for raising revenue.\(^4\)

Nevertheless, as the majority opinion later concedes, the issue really lies in the use tax system. That system is problematic because it relies upon individuals to document and remit tax on purchases for which they did not pay sales tax. It is based upon an honor system that does not work either because individuals purposefully underreport their unverifiable use tax obligations for the year, or because they are genuinely ignorant to whether they owe the tax and, if so, on what.

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3. Wayfair (slip op., at 9).
4. Id. at 16.
Yet, even before the internet, this “loophole” was (and is) being utilized by businesses—and not just for online sellers. For instance, in Delaware—a state without a sales tax—businesses advertise the state as the “home of tax-free shopping.” When individuals make purchases in Delaware from Pennsylvania, New Jersey, or other states, they are supposed to report that use tax to their respective state. The fact that they do not do so is not necessarily a “loophole,” but rather a flaw in the use tax system. Moreover, the majority’s assertion that *Quill* essentially resulted in a “judicially created tax shelter”\(^5\) is a bit extreme: no one would suggest that a brick-and-mortar business’s decision to locate in Delaware instead of Pennsylvania to avoid collecting the sales tax is a “tax shelter.” How can it be a tax shelter when the onus remains on the consumer to report the use tax?

Another consideration is whether the decision has created a new and unintended “loophole” for foreign companies—i.e., those outside of the United States. The same argument can now be made that foreign companies may have the advantage of not collecting sales tax and thereby have the ability to sell their goods at a lower price. While the requirement to collect and remit sales taxes to states with economic nexus laws should apply to both domestic and foreign companies, the ability of states to actually enforce and collect that obligation from foreign companies with no U.S. presence is, in practice, quite doubtful. The *Wayfair* Court explains that the physical presence rule creates an incentive to avoid physical presence in multiple states. Does its elimination of the physical presence standard now create an incentive to avoid physical presence in the United States altogether?

Finally, the state involved in the *Wayfair* litigation was South Dakota. South Dakota is one of the twenty-three member states of the Streamlined Sales and Use Tax Agreement, which—as the Court points out—standardizes taxes to reduce administrative and compliance costs. Some of the largest states, however, are non-members, including Pennsylvania, California, and New York. Might the Court’s decision result in remote sellers purposefully avoiding states that are not member states because the cost of compliance is too high in a non-streamlined state? Possibly. However, those non-member states are states with some of the largest populations and, conceivably, part of the remote seller’s largest market. Thus, this will result in compliance costs and potential audits in each jurisdiction—and failure to comply or errors in application of the law can result in hefty penalties. Further, those compliance costs may put small businesses out of business altogether—arguably to the benefit of large businesses. Appropriately, this is the dissent’s chief concern and criticism of the majority’s decision. Chief Justice Roberts, writing the dissent, notes that the Court “breezily disregards the costs that its decision will impose on retailers” and that “[t]he burden will fall disproportionately on small businesses.”\(^6\) Small businesses in particular will need to consider how to address the issues that *Wayfair* has created for them, specifically.

While the Court may have eliminated some perceived unfairness with its decision, it may have inadvertently created new levels of inequity. But the fact remains that whether right or wrong, fair or unfair, we must all now live in the post-*Wayfair* era and bid adieu to 50 years of physical presence. ■

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5 Id. at 13.
6 Id. (Slip. diss. at 5-6).
U.S. Tax Court’s Opinion Reversed in Altera by Ninth Circuit Court of Appeals

On July 24, the Ninth Circuit Court of Appeals, in *Altera Corp. v. Comm’r*, reversed the Tax Court’s *Altera* ruling that the Treasury’s section 482 transfer-pricing regulations on cost-sharing arrangements was “arbitrary and capricious” under the Administrative Procedure Act. The 2-1 decision found that the agency had followed proper procedures and was not arbitrary and capricious under the APA standard of review. “[T]he dispute here is not truly whether stock-based compensation is a cost but whether Altera—rather than the Commissioner—may decide how to apportion that cost between related entities.” It went on to defer to the agency’s interpretation under *Chevron*. Judge Kathleen M. O’Malley, sitting by designation from the U.S. Court of Appeals for the Federal Circuit, dissented from the reversal.

This was an important case with a long list of interested parties represented in Amicus Curiae briefs, including academics, the Chamber of Commerce, Amazon, Cisco Systems, the Software and Information Industry Association, National Association of Manufacturers, and others. The decision at least temporarily dashes the hopes of those planning further regulatory challenges based on the *Altera* success.

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2. *Altera Corp. v. Comm’r*, at 35.
PRACTICE POINT

How the Byrd Rule Might Have Killed the 2017 Tax Bill . . . and Why It Didn’t

By George K. Yin, Edwin S. Cohen Distinguished Professor of Law and Taxation, University of Virginia, Charlottesville, VA

During debate on the 2017 tax bill that was once slated to become the “Tax Cuts and Jobs Act,” the number of stories referencing an arcane budget law known as the “Byrd rule” skyrocketed in publications as diverse as the New York Times and the weekly trade magazine, Tax Notes. Many of the references, however, dealt with minor effects of the rule, such as its role in removing the bill’s short title from the final legislation. This article briefly describes a much more important and little-known aspect of this little-known rule that might have—and perhaps should have—killed the bill altogether.

Preventing Out-Year Deficit Increases

The Byrd rule potentially prevents Senate consideration of any part of a reconciliation bill or conference report that is considered to be “extraneous” to the underlying bill. The rule creates a point of order that may be raised by any Senator against any provision in such legislation. If the point of order is sustained and not waived by at least three-fifths of the Senate, the offending provision must be removed from the bill.

An “extraneous” provision includes one that would increase the deficit in any fiscal year—sometimes termed an “out-year”—after the budget period covered by the reconciliation bill. This part of the rule arose in 1987 when reconciliation bills were still used only for deficit reduction purposes. Some Senators tried to elude the deficit reduction objective by including provisions that raised revenue during the period covered by the bill (thus helping to meet the bill’s deficit reduction target) but lost revenue in an out-year. The Senate curbed this practice by generally defining as extraneous any provision increasing the deficit in an out-year.

Yet the single biggest tax cut included in the 2017 tax legislation—the dramatic lowering of the corporate tax rate—was not sunset. That provision was estimated to lose about $1.35 trillion during the legislation’s ten-year budget period (2018-2027) and, because it was enacted as a “permanent” provision, will continue
to increase the deficit after 2027. So how did it escape a Byrd rule objection? Before answering, let us consider one other important piece of background information.

**Suppose an objection had been raised and sustained against the corporate tax rate cut included in the 2017 conference report. At that point, the only option would have been for the Senate and House to vote up or down on the legislation without the corporate rate cut.**

**Objections to Provisions in Conference Reports**

A Byrd rule point of order can be raised during the Senate’s consideration of a conference report of a reconciliation bill. But a conference report—the product of a conference committee’s compromise of differences in House and Senate bills on a piece of legislation—is a special class of legislation. To achieve finality in the legislative process, a conference report is generally subject to only an up-or-down vote in the House and Senate. No more amendments are allowed, or else the process would be endless.

So what happens if a Byrd objection is sustained against a provision in a conference report being considered by the Senate? In that instance, the law permits the conference bill to be amended by removing the offending provision but making no other change. The conference bill without the offending provision is then considered by the Senate and, if approved, sent back to the House for its up-or-down vote.

Now put those two pieces of information together. Suppose an objection had been raised and sustained against the corporate tax rate cut included in the 2017 conference report. At that point, the only option would have been for the Senate and House to vote up or down on the legislation without the corporate rate cut.

What would have happened? I believe support for the entire bill would have collapsed. Without the corporate rate cut, few members of Congress would have supported the corporate tax base broadeners remaining in the bill, such as repeal of former section 199. Support for the international tax changes would also probably have disappeared. Finally, there would have been little reason to make most of the other changes in the bill, including enactment of new section 199A and the tax cuts for individuals. This possible scenario shows the potential significance of the Byrd rule. A single objection permitted by the rule, if sustained and supported by at least 41 Senators, could have scuttled—without use of the filibuster—a major policy initiative of a majority in Congress.

The timing of the objection would have been crucial. Many stories in the media and among Hill observers dealt with the possible role of the Byrd rule during the Senate’s consideration of its own bill. But the same objection raised and sustained at that stage of the legislative process would not have had the same effect because the Senate could have amended its bill. The obvious change would have been to sunset the corporate rate cut after ten years. Supporters would not have liked that change, but it surely would have been better than no corporate rate cut at all. Only if the Byrd objection had been raised at the conference stage—when it would have been too late to make any other amendment—could it have had its dramatic effect of killing the bill.

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So—why wasn’t an objection raised against the corporate tax rate cut in the conference report? And if it was raised, why wasn’t it sustained?

**Out-Year Deficit Increases Determined on a “Net” Basis**

Part of the answer is that a Byrd rule violation is determined on a “net” basis. If the amount a provision increases the deficit in an out-year is offset by enough deficit reduction in that year from other provisions, then there is no violation.

When the Senate considered its bill, supporters worked to ensure that it would be Byrd-compliant. The major change made to the House bill was to sunset the tax cuts for individuals after 2025 to eliminate their revenue loss in the out-years. But supporters made other changes as well, including a curious one to delay a House provision requiring amortization over five years of certain previously deductible R&E expenditures. The House had proposed making it effective beginning in 2023 but the Senate proposed to delay it until 2026, with the following budgetary consequence to the Senate bill:

| Selected Revenue Effects of 2017 Tax Legislation (Senate Bill) (billions of dollars) |
|---------------------------------|-----------------|-----------------|-----------------|-----------------|
| Provision                       | 2018-2024       | 2025            | 2026            | 2027            | after 2027      |
| corporate tax rate cut          | . . .           | -157            | -163            | -171            | greater losses  |
| amortization of R&E expenditures| . . .           | -0-             | +26             | +36             | smaller gains   |
| . . .                            | . . .           | . . .           | . . .           | . . .           | . . .           |
| Net total                       | . . .           | -156            | -59             | +34             | ??             |

Source: Jt. Comm. on Tax’n, Estimated Revenue Effects of the “Tax Cuts and Jobs Act,” as passed by the Senate on Dec. 2, 2017, JCX-63-17, items II.A.1, II.C.9, and net total.

The Senate may have delayed the R&E provision at the insistence of the affected taxpayers. But, as the table shows, delay also had an important budgetary effect by helping to make the overall Senate bill a revenue raiser in 2027. Without the estimated $36 billion produced by the R&E provision in that year, the overall bill would have resulted in a small revenue loss in 2027.

But what did the bill’s budget effect in 2027—the last year of the bill’s budget period—have to do with the Byrd rule, which is concerned with budget effects in years after that period (i.e., after 2027)? One explanation is that it supported a possible claim that since the bill reduced the deficit in 2027, it would do likewise in every year after 2027 (and hence not violate the Byrd rule).

At least one news report bought this claim.7 Tax professionals, however, know that it is not necessarily true. The budget effect of some provisions changes and even reverses from one year to the next.

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Indeed, the R&E change was one such provision. The revenue estimate of the provision in the House bill showed that its second year would be its peak year for raising revenue. After that year, more of the revenue gain from amortizing (and not deducting) new expenditures would be offset by revenue loss from the continued amortization of prior expenditures, thereby causing the provision to produce less than $36 billion per year of net revenue gain after its second year (i.e., after 2027 in the Senate bill). The last column in the table identifies this effect, leaving uncertainty as to the budget impact of the entire bill in the out-years.

Congress changed these and other provisions in the conference report, but this example reveals an important omission in the analysis of the bill. Since the corporate rate cut will increase the deficit in the out-years, the only way it can avoid being a Byrd violation is if there are sufficient offsets, but do we know the budget effect of the entire bill after 2027?

But aren’t these simply questions to be resolved by budget economists? After all, there were other provisions in the final bill, including repeal of the Affordable Care Act’s individual mandate penalty and especially the change in inflation indexing, that could be expected to reduce the deficit in years after 2027. Maybe their budget effect would more than offset the out-year deficit increases produced by the rest of the bill. There are, however, at least two problems with that answer.

Determining Byrd Rule Compliance

One problem is practical. Estimated budget effects of proposed legislation are measured against a baseline of what would have transpired had there been no change in law. The JCT relies upon baseline parameters provided by the CBO, but the CBO generally doesn’t provide such parameters beyond ten years. In general, if there is no baseline, there can be no estimates, and if there are no estimates, there is no way to determine if a Byrd rule violation has been avoided.

A panelist at a recent tax conference stated that, notwithstanding the absence of this information, the JCT had estimated that the inflation indexing change would raise a large amount of revenue during the first ten out-years (2028-2037). This estimate—not found by me on any of the pertinent congressional websites—would not be dispositive of the Byrd rule question, which requires an estimate of the budget consequences of the entire bill for a potentially unlimited number of future years. One out-year estimate that is publicly available is a statement from the CBO and JCT—in response to a different congressional budget law requirement—that the bill “would not increase on-budget deficits by more than $5 billion in any of the

8 See Jt. Comm. on Tax’n, Estimated Revenue Effects of H.R. 1, the “Tax Cuts and Jobs Act,” as ordered reported by the Committee on Ways and Means on Nov. 9, 2017, JCX-54-17, item II.E.15.
9 See JCX-67-17, supra n. 5, item III.A.3.
four consecutive 10-year periods beginning in 2028.”10 This statement is obviously also not dispositive of the Byrd question.

But there is a more fundamental problem with determining compliance with the Byrd rule. As illustrated by the foregoing CBO and JCT statement, skilled economists may be able to make reasonable assumptions to support estimates of long-term budget consequences. But the Byrd rule doesn’t require reliance on such economists. Rather, the law specifies that all budget determinations are to be made by the House and Senate budget committees, meaning, effectively, the chairs of those committees.11 Those chairs may—but apparently need not—seek out the professional expertise I have described.

We know this because of one final part of the story. In 2006, the Senate was considering a reconciliation bill that extended the reduced tax rates for dividends and long-term capital gain. The bill covered only five years, and the estimates for the years after the budget period—in this case, years 6-10—showed that it lost revenue. In other words, the bill was clearly in violation of the Byrd rule.

Congress overcame this problem by adding to the bill a provision allowing more taxpayers to convert their regular IRAs to Roth IRAs. The JCT estimated that conversion would produce enough additional revenue in years 6-10 to offset the revenue loss from the bill in those years.12 But the JCT also estimated that over ten years, the conversion provision would lose revenue.13 Despite this, and despite protests from members of the minority party in Congress, the Senate budget committee chair refused to certify that the bill as amended still violated the Byrd rule.14 In other words, the addition of a new tax cut to a bill already in violation of the Byrd rule because of its revenue loss miraculously eliminated the problem. The budget committee chair, who had carefully cultivated a reputation of fiscal responsibility over the years, flinched when he finally had an opportunity to act on his purported beliefs.

Conclusion

So there you have it. A determination of a Byrd rule violation requires analysis by those with budget estimating expertise, yet the law does not mandate that consultation. The rule is therefore an example of a potentially powerful tool that can be incapacitated by the way it is implemented. It is an all too familiar phenomenon in Congress. If the reconciliation process is now to be used principally to enable thin majorities in Congress to pass important legislative priorities—without regard to the budget effect of the legislation—it is not likely that a senior member of such a majority, such as a budget committee chair, will thwart that goal by requiring strict compliance with the Byrd rule.

Should Congress ever decide to take deficit reduction seriously—and is it not finally about time?—it would be a simple fix to make the Byrd rule administrable and consequential by requiring reliance on specific, published analysis provided by the CBO or JCT. Until then, the Byrd rule may be just another legislative frill—often a nuisance, and maybe sometimes a blessing, but never anything that would prevent a congressional majority from getting its way.

10 See CBO letter to Hon. Kevin Brady, Chair, House Ways & Means Committee (Dec. 15, 2017).
14 See id. at 8018-8019 (statement of Sen. Gregg (R.-N.H.)). For more detail on this episode, see Yin, supra n. 4, at 221-24.
PRACTICE POINT

Executive Compensation for Tax-Exempt Entities After Tax Reform

By Katila Howard, Foster Swift Collins & Smith P.C., Lansing, MI

I. Background

While the 2017 tax legislation did not produce all of the changes some had predicted, new rules governing excessive compensation for tax-exempt entities will substantially alter the landscape of executive compensation. Deferred compensation and other executive compensation arrangements for tax-exempt entities differ from those established for taxable for-profit entities. Tax consequences account for some of this difference as for-profit entities cannot deduct a compensation expense until the benefit is paid. Alternatively, the compensation deduction is of little consideration to a tax-exempt entity so it can incentivize the use of deferred compensation arrangements in certain circumstances. Generally, tax-exempt entities were not subject to compensation limitations, but were limited under the private inurement doctrine and section 4598 if compensation was excessive.

Nevertheless, tax-exempt entities must adhere to deferred compensation rules, reasonable compensation rules, and the private inurement doctrine. Tax-exempt entities must be mindful of deferred compensation requirements under The Employee Retirement Income Security Act of 1974 (ERISA) and the Internal Revenue Code when designing executive compensation plans. Previously, tax-exempt entities were not subject to excise taxes on executive compensation arrangements. After the 2017 tax legislation, however, tax-exempt entities are subject to a golden parachute and excise tax regime similar to those in sections 280G and 162(m) (irrespective of any organizational change in control), which prohibit deductions for excess parachute payments by public companies.

II. Private Inurement Doctrine

Private inurement is prohibited under the Code and regulations. To maintain its tax-exempt status, tax-exempt entities must be organized and operated exclusively for charitable purposes. “An organization is not operated exclusively for one or more exempt purposes if its net earnings inure in whole or in part to the benefit of private shareholders or individuals.”1 Accordingly, a tax-exempt entity is not organized and operated exclusively for charitable purposes if the exempt entity’s net earnings inure to the benefit of any private shareholder or individual.2

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1 Prop. Treas. Reg. § 1.501(c)(3)-1(c)(2).
2 I.R.C. § 501(c)(3).
A private shareholder or individual means a person who has a personal and private interest in the activities of the entity. A person includes an individual, trust, estate, partnership, association, company, or corporation. Thus, excessive compensation violates the prohibition on private inurement. However, the prohibition on private inurement only applies to transactions involving individuals receiving a benefit as a result of their position of control or influence over the tax-exempt entity, such as shareholders, directors, officers or major contributors.

Nevertheless, if the tax-exempt entity is receiving fair market value for the goods, services or other consideration in the transaction, then the prohibition against inurement does not apply. Further, there is no safe harbor for de minimis inurement. While a small amount of inurement can jeopardize a tax-exempt entity’s status, a compensation arrangement with a person who has a private interest will not constitute private inurement if the compensation is reasonable relative to the services provided to the tax-exempt entity.

III. Reasonable Compensation Rules

The compensation provided by a tax-exempt entity is not considered “excessive” if it is “reasonable.” Reasonable compensation is the value that would ordinarily be paid for like services by like entities under similar circumstances. Reasonable compensation rules apply to the aggregate of all compensation received by the executive.

In 1996, Congress enacted the Taxpayer Bill of Rights 2, which included Section 4958. That section imposes intermediate sanctions on prohibited private inurement by establishing a series of excise taxes, commonly referred to as intermediate sanctions penalties, on disqualified persons who enter into excess benefit transactions with tax-exempt entities. A disqualified person is generally a person, at any time during the five-year period ending on the date of the transaction, in a position to exercise substantial influence over the affairs of the applicable tax-exempt entity. Additionally, a disqualified person includes certain family members of a disqualified person, and 35% controlled entities of a disqualified person.

An excess benefit is the amount by which the value of the economic benefit provided by an applicable tax-exempt entity, directly or indirectly, to or for the use of any disqualified person exceeds the value of the consideration (including the performance of services) received for providing such benefit.

Pursuant to section 4958, an excess benefit transaction will trigger: (1) a tax of 25% of the excess benefit on each disqualified person who receives an excess benefit; (2) a tax equal to 10% of the excess benefit (up to $20,000 per person) on those involved in approving the excess benefit; and (3) a tax of 200% on the recipient if the excess benefit transaction is not corrected by a certain date.

Under section 4958, an exempt entity may establish a rebuttable presumption of reasonableness for compensation or that a transfer of property or the right to use property is presumed to be at fair market value.

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3 Prop. Treas. Reg. § 1.501(a)-1(c)
4 I.R.C. § 7701.
5 Id.
7 Id.
8 I.R.C. § 4958(c)(1)(A)-(B).
9 I.R.C. § 4958(a)-(b).
Deferred compensation arrangements of tax-exempt entities must account for ERISA as well as Code sections 409A and 457.

with respect to the specific transaction. Once the rebuttable presumption is established, the burden of establishing that the transaction results in an excess benefit shifts to the Service. The rebuttable presumption may be established if pursuant to regulations the tax-exempt entity has an informed independent body approve compensation arrangements and contemporaneously documents decisions.10 Nevertheless, a compensation arrangement that qualifies for the presumption of reasonableness under section 4958 continues to be subject to excise tax under section 4960.

In addition to the tax penalties, the Service may revoke a tax-exempt entity’s exemption status for an excess benefit transaction. There are correction rules, however, which require undoing the excess benefit transaction (to the extent possible) by making a payment in cash or cash equivalents equal to the correction amount to the applicable tax-exempt entity.

IV. Deferred Compensation Rules

Deferred compensation arrangements of tax-exempt entities must account for ERISA as well as Code sections 409A and 457. Deferred compensation structured as a top hat plan avoids ERISA funding and other requirements. Generally, ERISA requires that pension benefit plans, which include many deferred compensation arrangements, be funded.11 However, funding a plan that only covers a small number of individuals can have unfavorable tax consequences under section 402(b). One solution to this problem is to structure the arrangement as a top hat plan. Top hat plans are also exempt from ERISA's participation, vesting, and fiduciary responsibility requirements.12 Additionally, top hat plans are exempt from Form 5500 reporting and ERISA disclosure requirements as long as the sponsor files a one-time notice with the Department of Labor.13

Further, deferred compensation arrangements of tax-exempt entities must account for sections 457 and 409A. Section 457 governs the tax treatment of the deferred compensation paid by state and local governmental employers as well as tax-exempt entities. It does not apply to tax-favored plans under sections 401(a), 403, the portion of plans that consist of a transfer of property under section 83, the portion of plans that consist of a section 402(b) trust, qualified governmental excess benefit arrangements, and applicable employment retention plans. The tax treatment under section 457 is dependent on whether an arrangement qualifies as a 457(b) plan or a 457(f) plan.

Generally, 457(b) plans are eligible deferred compensation plans that are designed as defined contribution arrangements due to nature of the requirements. 457(f) plans encompass all other deferred compensation arrangements of governmental and tax-exempt employers that do not meet the requirements under section 457(b). As such, 457(f) plans are referred to as ineligible deferred compensation plans. Section 457(f)

10 Treas. Reg. § 53.4958-6(a).
11 ERISA §§ 302 through 308 govern funding of defined benefit pension plans. (Also see 26 U.S.C. § 412, §430, §431, and §432.) Funding requirements for single-employer plans were amended by §§101 to 116 of the Pension Protection Act of 2006. Funding requirements for multiemployer DB plans were amended by §§ 201 to 221 of the Pension Protection Act of 2006.
12 ERISA §§ 201(2), 301(a)(3), 401(a)(1) (29 U.S.C. §§ 1051(2), 1081(a)(3), 1101(a)(1)).
13 29 C.F.R. § 2520.104-23.
imposes income taxes on all nonqualified deferred compensation when amounts are no longer subject to a substantial risk of forfeiture, with the exception of amounts disbursed under a 457(b) plan.

Eligible plans under section 457(b) are not subject to the requirements of section 409A. However, section 409A applies to 457(f) plans, in addition to section 457(f), to the extent any plan provides for the deferral of compensation within the meaning of section 409A. Amounts included as income under either section 457(b) or section 457(f) are counted as remuneration in determining whether the excise tax on excess compensation applies.

Section 409A covers nonqualified deferred compensation arrangements that permit an employee to defer income recognition and income taxation on amounts earned, but paid in a subsequent year. It does not apply, however, to tax-qualified retirement plans such as 401(k) plans, 403(b) plans, 457(b) plans or similar tax-favored plans, although these plans similarly delay taxation on compensation. Under section 409A, a nonqualified deferred compensation arrangement must meet (1) distribution, (2) acceleration, and (3) election requirements both in form and in operation unless an exception applies. Failure to comply with the requirements of the provision causes the compensation at issue to be immediately included as income, even if not yet payable under the deferred compensation arrangement, and subjects the compensation to an additional 20% tax, plus an additional excise tax imposed, equal to the IRS underpayment rate plus 1%. It is important to note that while both sections 457 and 409A impose taxes on nonqualified deferred compensation arrangements when there is no longer a substantial risk of forfeiture, the definition of the phrase differs in the two sections.

V. Tax Reform

The 2017 tax legislation added section 4960 (the “Tax on Excess Tax-Exempt Organization Executive Compensation”). This section imposes a new excise tax on “excessive” compensation paid by tax-exempt entities for taxable years beginning after December 31, 2017. It applies to:

(i) farmers' cooperatives under section 521(b)(1);
(ii) political organizations under section 527;
(iii) governmental entities under section 115(1) and organizations under section 501(a);
(iv) and organizations under section 401(a).

Note the tax is imposed on the entity, not the employee.

14 I.R.C. § 409A (d)(2)(B); Reg. §1.409A-1(a)(2)(vii). See Notice 2005-58 (until further guidance is issued, federal credit unions may treat nonqualified deferred compensation plans as eligible §457(b) plans).
20 I.R.C. § 4960(c)(1).
Under this new provision, tax-exempt entities are subject to a 21% excise tax (the new corporate tax rate) on any remuneration paid to covered employees in excess of $1 million.\(^{21}\) This excise tax equals 21% of the sum of:

(i) compensation paid by the entity to any covered employee in excess of $1 million;

(ii) all forms of deferred compensation; and

(iii) excess parachute payments to covered employees triggered by separation from employment, to the extent that the total parachute payments exceed three times the five-year average total compensation.\(^{22}\)

A covered employee is any current or former employee who is one of the five highest-compensated employees for the current year or any prior tax year beginning after December 31, 2016.\(^{23}\) Section 4960 applies to any such employee, even if the employee is not an officer. Once an employee is a covered employee, the employee will always be a covered employee.

An exception is provided for remuneration attributable to medical services of certain qualified medical professionals.\(^{24}\) Remuneration means wages under section 3401(a). Remuneration paid to a licensed medical professional which directly relates to the performance of medical or veterinary services are not taken into account. Thus, qualified medical professionals such as doctors, nurses, and veterinarians are not considered covered employees.

Remuneration is treated as paid when there is not a substantial risk of forfeiture of the right to payment.\(^{25}\) Payments from a 457(f) plan are included in the year vested.\(^{26}\) Designated Roth contributions are excluded.\(^{27}\) Remuneration includes not only remuneration by the tax-exempt entity itself, but also by related persons, which includes persons or governmental entities that:

(i) control or are controlled by the organization;

(ii) are controlled by one or more persons that control the organization; or

(iii) are supporting organizations or supported organizations for the taxable year with respect to the organization.

However, if the related organization is subject to the section 162(m) limit on deductible compensation and the remuneration is not deductible under that section, then the deduction is also disallowed under section 4960. Further, a related entity is liable for its proportion of the excise tax from the remuneration paid to the covered employee.

\(^{21}\) I.R.C. § 4960(a).

\(^{22}\) I.R.C. § 4960(a)(1)-(2).

\(^{23}\) I.R.C. § 4960(c)(2)(A)-(B).

\(^{24}\) I.R.C. § 4960(c)(3)(B).

\(^{25}\) I.R.C. § 4960(a)(2).

\(^{26}\) Id.

\(^{27}\) I.R.C. § 4960(a)(1), I.R.C. § 4960(c)(2).
This section also defines an excess parachute payment as an amount equal to the excess of any parachute payment over the employee’s base amount.28 The base amount is equal to the employee’s trailing five-year average W-2 compensation before the date of the employee’s separation from employment. An amount would be a parachute payment if it is contingent on the employee’s separation from employment and the present value of the compensation equals or exceeds three times the employee’s base amount.29

The excess parachute payments under section 4960 operate in a manner similar to the golden parachute rules under section 280G, although the golden parachute rules are not tied to a change in control and also do not apply to employees who are not highly compensated employees. However, parachute payments do not include payments under a qualified retirement plan, a simplified employee pension plan, a simple retirement account, a tax-deferred annuity, or an eligible deferred compensation plan of a state or local government or tax-exempt entity.30

VI. Recommendations

Entities subject to section 4960 should identify their five highest compensated employees starting with the first year beginning after December 31, 2016, and maintain a cumulative list of all such employees for each year thereafter. Additionally, entities should track the total amount of remuneration being paid. After December 31, 2017, these employees—as well as the five highest compensated employees in 2018—will be the covered employees for the first tax year in which the excise tax applies.

Entities should review covered employees’ compensation arrangements to determine whether the excise tax may apply. The review should consider annual base salary, long-term incentive programs, taxable benefits, employment agreements, deferred compensation plans, severance arrangements, and change in control agreements. Following the assessment, entities may need to amend existing employment and other agreements to address the impact of the excise tax. Entities will also need to assess the impact of the excise tax on recently terminated covered employees to determine the impact on payments to such covered employees.

Future planning techniques may include accelerating amounts of taxable compensation within one or more years prior to separation from service from the tax-exempt entity to boost the base amount. Another planning strategy for tax-exempt entities involves using restrictive covenants, such as covenants not to compete, as conditions of severance payments. If permitted under state law, a valid and enforceable covenant not to compete could prohibit the classification of the severance payment as a parachute payment. This strategy is regularly used to mitigate the adverse tax consequences of section 280G. Note, however, any severance payment would be characterized as reasonable compensation and counted toward the $1 million limit.

28 I.R.C. § 4960(c)(5)(A).
29 I.R.C. § 4960(c)(5)(B)(i).
30 I.R.C. § 4960(c)(5)(C)(i)-(iv).
VII. Conclusion

From a tax policy perspective, the excise tax creates tax equity between tax-exempt entities and taxable entities because the section 4960 provisions parallel the golden parachute and excise tax regime provisions under sections 280G and 162(m). Tax-exempt entities must account for the new excise tax and consider the tax and fiscal ramifications. Additionally, this process can be onerous for larger tax-exempt entities with multiple entities as the section applies on an entity-by-entity basis.

Tax-exempt entities will need to be creative in attracting quality candidates because section 4960 substantially impacts executive compensation practices in this sector. Historically, tax-exempt entities have competed with for-profit entities for talent. Section 4960 may be a disadvantage to tax-exempt entities as these entities may now face new challenges and increased costs in designing competitive executive compensation packages. Tax-exempt entities may be forced to choose between incurring the excise tax liability for offering competitive compensation packages or risk being unable to attract and retain quality talent with reduced compensation packages for executives.

Tax-exempt entities may have to juggle additional payroll expenses and simultaneously navigate new procedures as this new provision modifies regulations that have governed this sector for nearly two decades. While tax-exempt entities need to offer competitive compensation, the distinction between reasonable compensation and excessive compensation can be difficult to discern. Until the Service promulgates regulations and other guidance under the new law, the impact on executive compensation for tax-exempt entities will remain uncertain.

Further, since sections 4958 and 4960 operate independently, tax-exempt entities must account for both regimes: a compensation arrangement can trigger the excise tax on excess benefit transfer under section 4958 and the excise tax on excessive executive compensation under section 4960. We will likely see regulations clarifying ambiguities of section 4960 and interpreting provisions applicable to public universities, credit unions, medical/veterinarian professionals, and 457(f) plans.
Section 1202: A Big Deal for Small Business

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Section 1202 was enacted in 1993 as an incentive for taxpayers to start and invest in certain small businesses. Currently, the statute provides an exclusion from income for any gain from the sale or exchange of “qualified small business stock” (QSBS) acquired after the effective date of the statute and held for more than five years. However, the amount of gain that is excludible from income depends on when the QSBS was originally issued. The gain exclusion is 50% for QSBS issued before February 18, 2009, and 75% for QSBS issued between February 18, 2009 and September 27, 2010. The Creating Small Business Jobs Act of 2010 increased the exclusion to 100% of the total gain for all QSBS issued after September 27, 2010.

Despite this additional incentive, many businesses shied away from planning for QSBS because only the stock of C corporations qualified. Unless business founders had planned from inception to use the sale of stock as an exit strategy, founders were reluctant to voluntarily impose “double taxation” (i.e., income taxes at both the corporate level and the shareholder level) on the corporation’s taxable income.

Planning for QSBS became important for many more enterprise founders due to the reduction of the corporate rate to 21% under the 2017 tax legislation. Now is the ideal time to review the fundamentals of QSBS treatment and the particulars of section 1202.

I. Overview of Section 1202

A. Basic Mechanics

Section 1202 allows a taxpayer to exclude 100% of the eligible gain realized from the sale or exchange of QSBS issued after September 27, 2010 and held for more than five years. QSBS must be issued by a

1 The views expressed are those of the author and do not necessarily reflect the views of Ernst & Young LLP or any other member firm of the global Ernst & Young organization.
3 § 1202(a)(1). This assumes the taxpayer holds no offsetting position, such as a short sale, put option, hedge, or the like. See § 1202(j).
4 See P.L. 103-66, § 13113(a); P.L. 111-5, § 1241(b).
5 § 1202(a)(4).
6 § 1202(c)(1).
8 § 1202(a)(1), as modified by § 1202(a)(4).
“qualified small business” and generally be acquired by the taxpayer at original issuance, either in exchange for cash or other property (not including stock) or as compensation for services rendered to the corporation (other than services an underwriter of the stock).9

B. Limitations on Gain Exclusion

The statute limits the per-issuer amount that can be excluded to “eligible gain,” which is the greater of:

1) $10 million reduced by any amount the taxpayer excluded from sales or exchanges of QSBS from the same issuer in prior years, or

2) 10 times the aggregate adjusted basis of the QSBS issued by the corporation disposed of by the taxpayer during the taxable year, as measured on the original issue date.10

Because the limitation references the higher amount of the two measurements, the potential total gain excluded from gross income may exceed $10 million. Because a corporation qualifying for the provision could have up to $50 million in assets upon inception,11 the maximum amount of gain eligible for exclusion could reach $500 million under the ten-times-basis limitation.

C. The “Qualified Small Business”

A “qualified small business” is a domestic C corporation (C-Corp) that meets three threshold requirements:12

1) The aggregate gross assets of the corporation, including any predecessor corporation, did not exceed $50 million at all times on or after August 10, 1993, and prior to issuance.

2) The aggregate gross assets of the corporation immediately after issuance (including amounts received upon issuance) did not exceed $50 million.

3) The corporation agrees to submit reports to the Secretary and its shareholders as the Secretary may require.

Upon satisfying these requirements, the corporation must also satisfy the “active business” test to be eligible for QSBS treatment. The active business test provides:13

1) The corporation uses at least 80% of its assets (as measured by fair market value) in the active conduct of a “qualified trade or business” (the “80% test”); and

2) The corporation is a C-Corp that is not a domestic international sales corporation (DISC) or former DISC, regulated investment company (RIC), real estate investment trust, real estate mortgage investment conduit, or cooperative.

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9 § 1202(c)(1). An exception described further herein exists for certain conversions and non-recognition transactions.
10 § 1202(b)(1). For taxpayers filing separately, the limitation in (1) is $5 million instead of $10 million. §1202(b)(3)(A).
11 § 1202(d)(1)(A).
12 § 1202(d)(1).
13 § 1202(e)(1); § 1202(e)(4).
A “qualified trade or business” is defined in section 1202(e)(3). This definition gained significant attention when the 2017 tax legislation “borrowed” and modified part of it to define and limit businesses eligible to take the deduction for qualified business income under the new section 199A.

For purposes of the 80% test, assets used in the active conduct of a qualified trade or business include (1) assets used in startup activities, research and development, and in-house research;\(^\text{14}\) (2) assets held for reasonably required working capital needs;\(^\text{15}\) (3) assets held for investment that are reasonably expected to be used within two years to finance research and development or increases in the working capital needs of the business, limited to 50% of the corporation's total assets after the corporation has existed for two years;\(^\text{16}\) and (3) computer software rights leading to the production of section 543(d)(1) royalties.\(^\text{17}\)

**D. Defining a “Qualified Trade or Business”**

A “qualified trade or business” (QTB) is defined in section 1202(e)(3). This definition gained significant attention when the 2017 tax legislation “borrowed” and modified part of it to define and limit businesses eligible to take the deduction for qualified business income (QBI) under the new section 199A.\(^\text{18}\) Rather than identifying what a QTB is, section 1202(e)(3) sets forth what a QTB is *not*, namely:

1. Any trade or business involving the performance of services in the fields of health, law, engineering, architecture, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, or any trade or business in which the principal asset of such trade or business is the reputation or skill of one or more of its employees;
2. Any banking, insurance, financing, leasing, investing, or similar business;
3. Any farming business (including the business of raising or harvesting trees);
4. Any business involving the production or extraction of products of a character with respect to which a deduction is allowable under section 613 or section 613A (i.e., oil or gas properties subject to depletion); and
5. Any business of operating a hotel, motel, restaurant, or similar business.

Beyond this statutory description, scant guidance exists – perhaps because of the relative obscurity of the QSBS statute – to help taxpayers determine whether an activity is a QTB. Two private letter rulings and one tax court case comment on the subject. In PLR 201436001, a pharmaceutical research and clinical testing company was a QTB because it did not “offer value to customers primarily in the form of services ... [or] individual expertise.” Likewise, in PLR 201717010, a health care technology company providing

\(^{14}\) § 1202(e)(2).
\(^{15}\) § 1202(e)(6)(A).
\(^{16}\) § 1202(e)(6)(B).
\(^{17}\) § 1202(e)(8).
\(^{18}\) P.L. 115-97, § 11011(a).
laboratory reports was a QTB because the company never offered a patient a “diagnosis or treatment recommendation,” but rather only issued the reports. In Owen v. Commissioner, the Tax Court concluded that a corporation’s principal asset did not include the reputation or skill of one or more employees even though the court acknowledged that the success of the corporation was attributable to its owners.\textsuperscript{19} Otherwise, practitioners may need to look to other guidance defining these terms, such as section 448 and the regulations thereunder.

**E. Holding QSBS in a Pass-Thru Entity**

Section 1202(g) permits taxpayers to hold QSBS through any partnership, subchapter S corporation, RIC, or common trust fund.\textsuperscript{20} Generally, however, a transfer of originally issued QSBS to a pass-thru entity will cause the QSBS to cease to be treated as QSBS.\textsuperscript{21} For example, if QSBS is transferred to a partnership in exchange for a partnership interest, gain realized on the disposition of the stock by the partnership would not be eligible for exclusion under section 1202(a).

Any QSBS held via pass-thru entity will enjoy the same treatment as QSBS held directly to the extent the pass-thru entity meets all requirements otherwise applicable to an individual holder of QSBS.\textsuperscript{22} Taxpayers must hold the interest in the pass-thru entity for at least five years, as well; for instance, a taxpayer may not acquire an interest in a partnership that has held QSBS for ten years, then sell the interest two days later and receive QSBS treatment.\textsuperscript{23} Disallowance of QSBS treatment would likewise apply if the aforementioned hypothetical taxpayer received a distributive share of partnership income attributable to the sale of QSBS shortly after acquisition of a partnership interest.

**F. Allowable Transfers and Entity Conversions**

Section 1202(h) allows for transferees to receive QSBS that retains its character as QSBS in certain permitted transfers. The list of permitted transfers generally reflects a policy of blessing certain QSBS dispositions that provide for carry-over basis treatment. For instance, if a taxpayer holds QSBS through a tax partnership from first issuance, distribution of the QSBS from the partnership to the taxpayer in a non-recognition transaction will allow the taxpayer to tack the partnership’s QSBS eligibility and holding period to her own.\textsuperscript{24} If a taxpayer gifts or bequeaths QSBS, the recipient of the QSBS will also be allowed to tack QSBS eligibility and holding period.\textsuperscript{25}

Tax-deferred incorporations and reorganizations enjoy similar treatment: any successor stock received in exchange for QSBS will also retain its character and holding period.\textsuperscript{26} If a taxpayer holds QSBS and exchanges it for non-QSBS in a section 351 or section 368 transaction, the non-QSBS received will be treated as QSBS to the extent of the built-in gain on the date of the reorganization.\textsuperscript{27}

\textsuperscript{19} T.C. Memo 2012-21.
\textsuperscript{20} § 1202(g)(4).
\textsuperscript{21} § 1202(h).
\textsuperscript{22} § 1202(g)(2).
\textsuperscript{23} § 1202(g)(3).
\textsuperscript{24} § 1202(h)(2)(C).
\textsuperscript{25} § 1202(h)(2)(A), (B).
\textsuperscript{26} § 1202(h)(4).
\textsuperscript{27} Note this applies to section 351 transactions only to the extent the corporation issuing the non-QSBS has section 368(c) control of the corporation originally issuing the QSBS. § 1202(h)(4)(D).
For example, assume Acme Corp. issues QSBS to Tom Taxpayer in 2012, and Tom Taxpayer has a basis of $1 per share. In 2018, after meeting all applicable requirements imposed by section 1202 for the entirety of Tom Taxpayer's holding period, Acme Corp. merges with Widget Corp. Assume that the adjusted basis of Acme Corp. stock in the hands of Tom Taxpayer remains $1, but Widget Corp. values Acme Corp.'s shares at $11 per share. Unlike Acme Corp., the stock of Widget Corp. is non-QSBS. Under section 1202(h)(4)(B), the Widget Corp. stock that Tom Taxpayer received in exchange for his Acme Corp. stock is treated as QSBS to the extent of the $10-per-share built-in gain at the time of the merger. If Tom Taxpayer sells his Widget Corp. stock when it appreciates to $26 per share, he will enjoy a section 1202(a) exclusion for $10 per share of his gain but will not be able to apply section 1202(a) to the remaining $15 per share of his gain.

G. Section 1045: QSBS Rollovers

Section 1045 allows a taxpayer to “roll over” gain on the disposition of QSBS into QSBS of a different issuer, provided the QSBS is held for more than six months prior to disposition and the rollover occurs within 60 days. If the taxpayer does not purchase “replacement” QSBS with a fair market value equal to or greater than the “relinquished” QSBS, the taxpayer will recognize “boot” in the form of capital gain, similar to the treatment of a section 1031 exchange. For purposes of determining the five-year QSBS holding period, the taxpayer’s holding period in the “relinquished” QSBS will count toward the holding period of the “replacement” QSBS.

For example, assume Tina Taxpayer has a $100,000 adjusted basis and a three-year holding period in her Acme Corp. QSBS. Tina then sells her Acme Corp. QSBS for $1 million. Within 60 days of her original sale, Tina purchases Widget Corp. QSBS for $850,000. Tina takes a $100,000 carry-over basis in her Widget Corp. QSBS and recognizes $150,000 of capital gain. To avoid recognition of capital gain entirely, Tina could have reinvested the remaining $150,000 into Widget Corp. QSBS or the QSBS of a different issuer. Tina’s three-year holding period in the Acme Corp. QSBS carries over to her new Widget Corp. QSBS. Thus, Tina would only need to hold her Widget Corp. QSBS for two additional years to qualify for gain exclusion from the sale or exchange of the Widget Corp. QSBS.

II. Traps for the Unwary

A. Put Options as Dispute Resolution

Section 1202(j) prohibits the application of Section 1202(a) to exclude gain from the sale of QSBS from a taxpayer’s gross income if the taxpayer holds an “offsetting short position” with respect to the QSBS. Although the statute was clearly designed for taxpayers who actively seek out strategies to mitigate their economic risk of loss for QSBS holdings, no statutory or regulatory exception exists for the common dispute resolution strategy of allowing shareholders to possess a put option for their stock that would allow the shareholder to exit by compelling a sale to either another shareholder or the corporation itself. Practitioners who are not mindful of section 1202(j) could inadvertently trigger its application by attempting in good faith to set up a method for the corporation to avoid a crippling impasse between its principals.

28 § 1045(a)(1).
29 § 1045(b)(5); see § 1202(f)(2).
B. Failure to Monitor Assets or Spend Working Capital

As described above, section 1202(e) measures the “active business requirement” by examining how the corporation uses its assets. Section 1202(e)(1)(A) requires the corporation to use 80% of its assets in the active conduct of a qualified trade or business. While section 1202(e) provides a list of exceptions, failure to meet the requirements of section 1202(e) could result in a tax disaster. Corrective action may cure such a failure, but any rescue attempt must be completed quickly to allow the taxpayer to meet the “substantially all” requirement in section 1202(c)(2)(A). Because no bright-line standard exists for measuring “substantially all of the taxpayer’s holding period” for QSBS, time is of the essence for taxpayers and their advisors to discover and remedy any facts or circumstances causing less than 80% of assets to be used in a qualified trade or business.

III. Interplay with the 2017 Tax Legislation

The 2017 tax legislation cut the statutory income tax rate on C-Corps from 35% (the maximum rate in a graduated rate provision) to a 21% flat rate, making the C-Corp a significantly more attractive choice of entity. Other changes in the tax act also favored C-Corps, such as the limitation on a non-corporate taxpayer’s deduction for state and local income, property, and sales/use taxes, which is not applicable to C-Corps. The introduction of tax incentives for investment in qualified opportunity zones (QOZs) might be the second most important aspect of the 2017 tax legislation to favor planning for QSBS treatment. In brief, Congress provided for the deferral and partial forgiveness of capital gain that is reinvested into a QOZ and the exclusion from gross income of all subsequent appreciation, provided certain conditions have been met. Depending on Treasury’s reconciliation of the incentives in section 1202 with the incentives in section 1400Z-2, seizing the tax advantages of QSBS could become even more compelling if the QOZs also satisfy the requirements to be treated as QOZ stock. In that case, adroit tax planning could result in the permanent exclusion from taxation of gain on the sale of the QOZ, provided forthcoming regulations do not prohibit the technique. The overlap of the QSBS and QOZ systems will require detailed rules, which are unlikely to be a part of the initial wave of QOZ guidance expected in the coming months.

IV. Conclusion

Section 1202 did not receive much attention from the tax community at large because of the relative unattractiveness of C-Corps, but with the passage of the 2017 tax legislation, now is the ideal time for practitioners to review the inner workings of the statute. Despite existing statutory and administrative ambiguity, taxpayers can obtain significant benefits from issuing QSBS, especially if they work closely with their tax advisors to avoid traps for the unwary. In the current environment, the cost-benefit analysis in the choice of entity decision will favor C-Corps more frequently when QSBS treatment applies. Although

30 P.L. 115-97, § 13001(a).
31 Id. at § 11042.
32 Id. at § 13823. While a complete discussion of QOZ is beyond the scope of this article, readers should familiarize themselves with the concept because of its seismic effect on a wide variety of taxpayers. See generally §§ 1400Z-1, 1400Z-2.
33 Id. A QOZ is a population census tract located in a low-income community that is designated as a qualified opportunity zone. Section 1400Z-1(a).
34 At first blush, § 1202 does not appear to conflict with the congressional intent of §§ 1400Z-1 and 1400Z-2. If this hypothesis proves correct, Treasury could actually adopt the opposite approach and bless the complete exclusion of the deferred capital gain from income and the complete exclusion of any subsequent appreciation from gross income if the QOZ investment is in the form of QSBS, despite the mandate of § 1400Z-2(b)(1)(B) that any deferred capital gain be recognized by December 31, 2026, regardless of whether a realization or recognition event has occurred.
shareholders, accountants, and lawyers will need to jointly navigate the setup and operation of a corporation issuing QSBS, the reward at the end of the journey is well worth the complexity, and the tax advantages may become even more enticing if Treasury promulgates taxpayer-favorable regulations under section 1400Z-2.
PRACTICE POINT

Wives Need Their Own Lawyers When Their Husbands Are Accused of Tax Evasion and Other White-Collar Crimes

By Guinevere Moore and Jenny Johnson Ware, Johnson Moore LLC, Chicago, IL

The Sixth Amendment guarantees the right to conflict-free counsel in a criminal case. In addition to the obvious question of whether an attorney can represent co-defendants in a white-collar criminal case, there is the less obvious question of whether the attorney owes a professional duty to non-clients: the criminal defendant's spouse and children. Whether an attorney owes a professional duty to a non-client, including the spouse of a client, depends on the state where the representation takes place. Moreover, the question of whether an attorney-client relationship has formed is fact-specific and an attorney, through direct or indirect communications with the spouse or representations made to prosecutors, courts or others, may create an implied representation of the spouse without ever explaining the actual or potential conflicts of interest to the defendant and his spouse or receiving an informed waiver of those conflicts.

Attorneys who represent defendants in white-collar criminal cases should recommend that their clients’ spouses, referred to throughout this article as “White-Collar Wives,” obtain their own counsel as soon as possible. Far too often, attorneys who represent clients in tax evasion and other white-collar criminal cases do not think about the conflicts that could arise between spouses during the life of a white-collar case, or equally as important, how the collateral consequences of a white-collar conviction such as forfeiture, restitution, and civil tax assessments will impact the defendant’s spouse and family. As illustrated by the

1 See, e.g., United States v. Carona-Vicenty, 842 F.3d 766, 771-72 (1st Cir. 2016) (“A lawyer can represent multiple defendants, but not if the joint representation gives rise to a conflict of interests adversely affecting the lawyer's performance—for then there would be a Sixth Amendment violation.”) (internal quotations and citations omitted).
2 Compare Massachusetts, where attorneys have a professional duty to nonclients where the attorney knew, or should have reasonably foreseen, that the nonclient would rely on the attorney's services, International Strategies Group, Ltd. v. Greenberg Traurig, LLP, 482 F.3d 1 (1st Cir. 2007), with Illinois, where a duty is owed to a nonclient when the intent of the client to benefit the nonclient is the primary purpose of the representation. Oakland Police & Fire Retirement System v. Mayer Brown, LLP, 861 F.3d 644 (7th Cir. 2017).
3 Parker v. Carnahan, 772 S.W.2d 151, 157 (Tex. App. Texarkana 1989, writ denied) (plaintiff's husband was represented by attorneys in criminal tax evasion case based on jointly filed tax returns, plaintiff met and discussed her case with attorneys, and attorneys advised her to sign late-filed tax returns, fact issue on whether attorneys were negligent in failing to advise plaintiff that they were not representing her interests).
4 We refer to the white-collar defendants in this article as men and their spouses as “White-Collar Wives” because a significantly higher proportion of men than women are convicted of white-collar crimes. See, e.g., National Incident Based Reporting System (NIBRS) 2016 data, sex of offenders by category. The advice obviously applies to spouses of criminal defendants equally regardless of gender.
Second Circuit’s recent opinion in United States v. Daugerdas, White-Collar Wives have important due process and other property rights separate and apart from the defendant. White-Collar Wives who wait too long to get their own attorney—or even worse, never do get their own attorney—risk forfeiting these due process and other property rights entirely, along with the increased risk of being civilly responsible for a tax bill that they didn’t have a hand in generating. Money spent protecting and preserving her assets, as well as protecting her from collateral consequences of her husband’s trial, is just as important and well-spent as the money spent on her husband’s defense.

Eleanor Daugerdas: A Case-Study for White-Collar Wives

Paul Daugerdas is currently serving a 15-year prison sentence for tax evasion, mail fraud, and conspiracy to defraud the IRS, among other things. When he was arrested, Paul’s assets were seized pursuant to a post-indictment restraining order, as is common in white-collar criminal cases. Asset seizure is a precursor to forfeiture. Assets are typically seized based on probable cause to believe that property is subject to forfeiture and generally (although not always) must be seized pursuant to a judicial warrant.

Proceeds of most crimes—but not all—are subject to forfeiture. For example, section 891 of the federal money laundering and asset forfeiture statutes authorizes forfeiture of property derived from proceeds of over 200 crimes, including fraud, bribery, embezzlement, and theft. Asset forfeiture is designed to remove all profit from criminal acts, and to restore as much property as possible to victims of crime. Property may be subject to forfeiture if the government can trace the seized property directly to the offense giving rise to the forfeiture. Once Paul Daugerdas committed mail fraud, the government’s interest in the proceeds of that mail fraud arose and attached to the money he gained because of the mail fraud.

Following a lengthy jury trial, Paul Daugerdas was found guilty, but won a new trial due to juror misconduct. A second trial again resulted in conviction, and the Court entered an order for criminal forfeiture in the amount of $164,737,500 and an order for restitution in the amount of $371,006,397 against Paul.

When property subject to forfeiture is insufficient to satisfy the forfeiture order against the defendant, courts may order other property of the defendant to satisfy the forfeiture order, “up the value of the missing

9 United States v. Daugerdas, 837 F.3d 212, 231 (2d Cir. 2016).
10 United States v. Daugerdas, 867 F. Supp.2d 455 (S.D.N.Y. June 4, 2012), vacated and remanded sub nom., United States v. Parse, 789 F.3d 83 (2d Cir. 2015) (reversing and remanding for new trial). The fact that Paul had two trials is significant because Paul sought access to restrained funds to pay legal bills for his second trial. After a new trial was ordered but before the new trial began, Paul moved to vacate or modify the post-indictment order restraining his assets, arguing that unless the assets seized and held by the government were released, he would be unable to afford counsel, thus depriving him of his Sixth Amendment right to counsel. United States v. Daugerdas, No. S3 09 Cr. 581 (WHP), 2012 WL 5835203 (S.D.N.Y. Nov. 7, 2012). Although a defendant may be entitled to an adversarial, post-restraint, pretrial hearing to test the finding of probable cause to restrain assets, the defendant must demonstrate that “(1) that the restrained assets are necessary to pay for private counsel, and (2) that the assets were improperly seized.” Id., citing United States v. Monsanto, 624 F.2d 1186, 1203 (2d 1991) (en banc). Noting that his conviction was overturned due to juror misconduct and not insufficiency of evidence, the court found Daugerdas failed to meet the required elements for a Monsanto hearing and denied his motion. In his motion, Paul made many of the same commingling arguments that his wife, Eleanor, raised later.
White-Collar Wives have important due process and other property rights separate and apart from the defendant. White-Collar Wives who wait too long to get their own attorney—or even worse, never do get their own attorney—risk forfeiting these due process and other property rights entirely, along with the increased risk of being civilly responsible for a tax bill that they didn’t have a hand in generating.

proceeds.” This is known as “substitute property.”\(^\text{12}\) While the government’s interest in proceeds of fraud (and other crimes subject to forfeiture) vests as soon as the proceeds of a forfeiture crime exist,\(^\text{14}\) the same is not necessarily true of substitute property. The “relation-back” doctrine that applies to proceeds of fraud does not apply the same way to substitute property, insofar as a third party’s interest in substitute property may supersede the government’s interest.\(^\text{15}\)

Paul’s wife, Eleanor Daugerdas, filed a petition in response to the forfeiture order, arguing that certain accounts in her name and the name of an investment company she owns should not be subject to forfeiture.\(^\text{16}\) Eleanor’s petition, filed almost five years after Paul’s arrest and when the property was seized, requested that property in various accounts in various financial institutions be excluded from the forfeiture order.\(^\text{17}\)

Eleanor argued that she had a right to keep the accounts because they were substitute property, that her rights attached to the substitute property before the government’s, and accordingly her interest in the substitute property required that it be returned to her instead of forfeited.\(^\text{18}\) The crux of her argument is that not all of the proceeds in the bank accounts that were ordered to be forfeited could be traced back to the proceeds of fraud, and to the extent that they couldn’t be traced back, her interest in that “substitute property” trumped the government’s interest and that property could not be used to satisfy Paul’s in personam forfeiture obligations.\(^\text{19}\) Eleanor’s accounts were traceable to Paul’s fraud, but Eleanor maintained that Paul’s “tainted income” (which was indisputably subject to forfeiture upon his conviction for fraud) was “untraceably commingled with other non-tainted funds of [Paul’s law firm] while still in the law firm’s accounts.”\(^\text{20}\) The district court granted the government’s motion to dismiss Eleanor’s petition, finding that even if she could plead additional facts, she lacked standing to petition for the property.

The Second Circuit vacated the district court’s order and remanded the case for further proceedings, finding that while Eleanor had not sufficiently pleaded facts to state a claim to the property at issue, she has “significant constitutional rights potentially at stake” and “has a due process right to be heard” on her claim to the property.\(^\text{21}\) “[I]f Eleanor’s interest in Paul’s untainted property . . . vested before, and is therefore superior to, the government’s interest,” then due process requires that she be allowed to petition the court

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\(^{12}\) United States v. Daugerdas, 2018 WL 2944310, at *1. Criminal forfeiture is often characterized as part of the sentence in a criminal case, and is in personam against the defendant, compared with an in rem action against the property itself in civil forfeiture. \(\text{Id.}\)

\(^{13}\) 21 U.S.C. § 853(p).

\(^{14}\) 21 U.S.C. § 853(c).

\(^{15}\) United States v. Daugerdas, 2018 WL 2944310, at *6-8.

\(^{16}\) United States v. Daugerdas, Case No 1:09-cr-00581-LTS, Docket No. 853. Eleanor owned the investment company as a result of an assignment from Paul approximately seven years before he was indicted. \(\text{Id.}\) at ¶3.

\(^{17}\) United States v. Daugerdas, Case No 1:09-cr-00581-LTS, Docket No. 853.


\(^{19}\) \(\text{Id.}\)

\(^{20}\) \(\text{Id.}\) at *3.

\(^{21}\) \(\text{Id.}\) at *9, 17 n.7.
Accordingly. Although Eleanor has been given another chance to show she is entitled to funds in her accounts, it will be difficult for her to gather and present evidence sufficient to prove that her accounts contain “untainted property” now, over nine years from when the property was seized. While it is true that Eleanor could not have brought her petition under section 853(n) until after the forfeiture order was entered, as she did, there are other steps she could have taken earlier to protect her interests.

For example, Eleanor and any White-Collar Wife whose property is seized pursuant to a post-indictment restraining order may file a Motion for Return of Property under Rule 41(g) of the Federal Rules of Criminal Procedure, long before a petition for determination of third-party interests can be filed under section 853(n). Rule 41(g) provides that a “person aggrieved by an unlawful search and seizure of property or by a deprivation of property may move for the property’s return.” The motion is to be filed in the district court where the property was seized, and “the court must receive evidence on any factual issue necessary to decide the motion.” In other words, even if the search was legal, a person who is deprived of her property may use a motion for return of property to ask for it back.

Filing a motion for return of property as early as possible in the criminal proceedings may reduce the amount ultimately due to the government because white-collar crimes have tax implications. All income, whether legal or illegal, must be reported to the Service. When someone is convicted of a white-collar crime, the next step is often an increase in tax due to the failure to report and pay tax on the proceeds of the crime. In addition to having to pay tax on the previously unreported income, someone convicted of a white-collar crime may also be responsible for a 75% fraud penalty on the amount of tax that was not reported due to the illegal activity. If property that is seized is not ultimately forfeited, it can be applied to a tax or other civil liability as of the date that the motion for return of property should have been granted. Because of the onerous penalties and interest that apply to unpaid tax liabilities, the sooner payments are applied, the better.

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[A]ny White-Collar Wife whose property is seized pursuant to a post-indictment restraining order may file a Motion for Return of Property under Rule 41(g) of the Federal Rules of Criminal Procedure, long before a petition for determination of third-party interests can be filed under section 853(n).

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22 Id. at *9.
23 Fed. R. Crim. P. 41(g).
24 Rutkin v. United States, 343 U.S. 130, 137 (1952) (“An unlawful gain, as well as a lawful one, constitutes taxable income when its recipient has such control over it that, as a practical matter, he derives readily realizable economic value from it.”).
25 See, e.g., Crouse v. Commissioner, T.C. Memo 2011-97 (holding “embezzled funds are includable in gross income for the year in which those funds are embezzled”).
26 I.R.C. § 6663; Wright v. Commissioner, T.C. Memo 2000-336 (holding taxpayer who concealed his receipt of embezzled funds was responsible for increase in tax due to embezzled funds as well as 75% fraud penalty on the increase in tax). “Convictions for such crimes are highly probative of petitioner’s intent to evade taxes because the activities involve perjury, deceit, breach of fiduciary duty, and concealment of criminal proceeds.” Id.
27 In re Search of 2847 East Higgins Road, Elk Grove Village, Illinois, 390 F.3d 964, 965-66 (7th Cir. 2004) (hereinafter, East Higgins Road).
28 See, e.g., IRC §§ 6601, 6662.
In *East Higgins Road*, the owner of seized cash filed a motion for return of property. The government argued that the cash was proceeds of tax evasion, but conceded that it was otherwise lawfully earned income. The Court of Appeals for the Seventh Circuit found that income earned from a lawful business is not the fruit of a crime—and therefore is not subject to forfeiture—even if the recipient failed to pay tax on that income. In that case, the taxpayer had directed the government to apply the seized cash to payment of his tax liabilities rather than return it to him shortly after the seizure. As a result, the court did not order the physical return of the cash, but rather found that the funds should be applied to the taxpayer’s tax liabilities “as of the date that a motion for return of property should have been granted.” If the funds had been subject to forfeiture, they essentially would have vanished into thin air because forfeited funds do not reduce tax liabilities or any other liabilities. Instead, by filing a motion for return of property, the taxpayer succeeded not only in getting the funds applied to his tax liabilities, but also in erasing significant penalties and interest that had accrued while the motion was being litigated. White-Collar Wives who have grounds to file a similar motion may net similar benefits.

Together with other accounts she claims should not be subject to forfeiture, Eleanor’s petition, filed in August of 2014, requests that a Goldman Sachs trading account number 4XDG (titled in her name and part of the post-indictment asset seizure) be returned to her. The fact that this account was owned by Eleanor and titled in her name was known early in the criminal proceedings. The government explained in a letter to the Court that it “conferred with counsel for the defendant, Paul M. Daugerdas, who expressed a preference for maintaining the status quo.” It isn’t clear from the docket entry whether Paul’s attorneys consulted Eleanor, as well as Paul, to understand her “preference” along with his, whether Paul’s attorneys were considering what was best for Eleanor or what was best for Paul, or whether Eleanor received the legal advice she needed to make an educated decision to give up her right to seek return of those funds at that point in time.

The amounts Eleanor alleged were deposited in her accounts prior to Paul’s indictment, which she argues in her petition belong to her, are in excess of $30 million. The petition alleges that $1 million alone was deposited into her Goldman Sachs account over a year before the indictment. Even if all of Paul’s accounts and assets were forfeited, if Eleanor had filed a successful motion for return of property with regard to that one account in 2009, she would be in a materially different position than she is today. This is not to say that Eleanor should have filed a motion for return of property back in 2009. There are many very good reasons why an attorney representing a White-Collar Wife would decide not to file a motion for return of property. Above all, no amount of property being returned is worth being indicted as a co-conspirator, and if there is any risk that asserting ownership over property would lead to that result, then it is not worth trying to get the property returned. But it is important for each White-Collar Wife in this position to make an informed and reasoned decision together with an experienced attorney who is looking out only for her interests.

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29 **East Higgins Road**, 390 F.3d 964.
30 Id. at 965-66.
31 Id.
32 Id. at 966.
33 Id. at 966.
35 Id.
Kathleen Manafort, the wife of recently indicted white-collar defendant Paul Manafort, presents another example of the unique problems White-Collar Wives face. Paul Manafort has been indicted for crimes that are subject to forfeiture. The indictments specify assets that are allegedly subject to forfeiture as the fruits of specific alleged crimes, and also declare an intent to seek forfeiture of substitute assets, as in Daugerdas. The government has alleged that foreign financial accounts that should have been, but were not, reported to the government are subject to forfeiture. Although Kathleen Manafort is not named in the indictment, her property is included in the list of “records to be seized” on the search and seizure warrant authorized by the court, including any and all foreign financial records.

United States persons who have a direct or indirect interest in foreign financial accounts over a certain amount must report those accounts to the government. Penalties for the failure to do so include significant monetary penalties and up to five years in prison. An attorney representing Kathleen Manafort would need to carefully weigh whether Kathleen has a separate interest in property that was seized, including bank records or bank accounts, before acting. Without question, the primary goal would be to protect Kathleen: arguing that she had an interest in undisclosed foreign financial accounts could potentially expose her to criminal charges and significant civil penalties. On the other hand, if domestic financial accounts of Kathleen’s were seized that contain funds that do not have anything to do with her husband’s allegedly illegal activity, then she may be able to bring a motion for return of property for those funds.

In addition to the issues surrounding asset seizure and forfeiture, White-Collar Wives face significant collateral consequences from their husbands’ battles with the government over funding costs of defense, plea negotiations, the financial statements that must be provided as part of a pre-sentencing investigation, civil tax issues that necessarily follow a conviction for a white-collar crime, and restitution for unpaid taxes. It is well settled that when a defendant pleads guilty to tax evasion and enters into a restitution agreement with the U.S. government, that agreement does not “preclude the IRS from assessing tax liabilities and civil penalties that differ from the restitution for the same period.” White-Collar Wives will have different defenses than their husbands to additional assessments, even if they filed tax returns jointly. In addition, an “innocent spouse” may be granted relief from joint and several liability of a portion of the tax allocable to the other spouse. This defense, however, often creates a clear conflict between the two spouses.

Given the rights and defenses available to White-Collar Wives that are not available to defendants, and the significant collateral consequences that families face when a family member is charged with a white-collar crime, white-collar attorneys should counsel their clients regarding the significant benefits of separate representation for their spouses. Particularly where, as in Daugerdas, assets that belong to the White-Collar Wife are seized and forfeited along with the defendant’s assets, attorneys who are engaged to represent the husband may not be able to advise the wife about her potential rights due to a conflict of interest. If

43 Cantrell v. Commissioner, T.C. Memo 2017-20 at *17.
44 I.R.C. § 6013.
45 I.R.C. § 6015.
46 Dorchester Industries Inc. v. Commissioner, 108 T.C. 320, 339 (1997) (stating that “one spouse’s claim that she (he) is an innocent spouse can present a conflict of interest to counsel trying to represent both spouses”).
47 ABA Rules of Professional Conduct, Rule 1.7.
a spouse does not obtain her own counsel, attorneys representing the defendant should not speak on the spouse's behalf with the government or with the court for fear of creating an implied representation without getting a formal waiver of the potential conflict of interest.
PRO BONO MATTERS

#CripTheCode¹ to Enable Work

By Francine J. Lipman, William S. Boyd Professor of Law, William S. Boyd School of Law, University of Nevada, Las Vegas, Las Vegas, NV, and James E. Williamson, Professor of Accountancy, Charles W. Lamden School of Accountancy, Fowler College of Business, San Diego State University, San Diego, CA

Until the spirit of love for our fellow men, regardless of race, color or creed, shall fill the world, making real in our lives and our deeds the actuality of human brotherhood, until the great mass of the people shall be filled with the sense of responsibility for each other’s welfare, social justice can never be attained.

—Helen Keller

I. What Would Helen Do?

Helen Keller was born on a sultry summer day in 1880 on her family’s cotton plantation in Tuscumbia, Alabama. Helen was her young mother Kate’s first child, but the third child and first daughter of Helen’s beloved father, Confederate Captain Arthur. Kate Adams Keller was a voracious reader with a razor-sharp mind, memory and intellect. Captain Arthur managed the local newspaper and routinely ran for local public offices. Curly, golden-locked Helen was the stand-out star of the large extended Keller family including many house and field servants and their children. Baby Helen was talking and walking before she even celebrated her first birthday. In the always active Alabama household Helen continued to thrive until just before her

¹ We derived #CripTheCode from the #CripTheVote nonpartisan campaign that was started by the Disability Visibility project on Twitter to engage voters with disabilities and encourage a national conversation about disability rights. The term Crip is used intentionally. "Crip" is considered to be an inclusive term, representing all disabilities: people with vastly divergent physical and psychological differences. Crip represents the contemporary disability rights wave and is an ‘insider’ term for disability culture. Not to be confused with a gang name, the term Crip within the disability community reflects the political reclaiming of the historically derogatory term ‘cripple,’ which not only diminished the person to an image of ugliness but also excluded those with non-physical disabilities from the disability community. To identify as a Crip or with the Crip community means you identify as a member of the disability community or as an Ally to the disability community, and that you recognize a distinct disability culture. As a Crip, you are also fighting to challenge and reclaim the negative words and terminology historically used to objectify and pathologize the minds, bodies and souls of disabled individuals. Finally, the term Crip extends beyond the inclusion of all disabilities and encompasses members of other diverse groups historically invisible and ignored, such as disabled persons of color, disabled members with LGBTQI identities, those who are both disabled and linguistically diverse, and many other intersecting identities.

Breaking Silences, Demanding Crip Justice Conferences, Wright State University (Sept. 2017).
family celebrated her second birthday when a ravaging high fever turned Helen’s world forever dark and silent.

At the end of the 19th century, people with disabilities were legally sterilized, institutionalized, and denied the right to marry or even be in public. Schools systematically excluded children with disabilities except for a few visionary facilities that served individuals who were blind and/or deaf. Despite overwhelming discrimination and a dearth of resources, Helen excelled because of her unique and fortunate circumstances and undeniable genius. With the able assistance of her parents and others including her exceptionally gifted teacher, Annie Sullivan, Helen graduated cum laude from Radcliffe College at age 24 and authored more than a dozen books and countless articles in her 80 years.

Like her father, Heller was engaged in politics from an early age, vehemently supporting racial equality and peaceful conflict resolution while opposing violence and war. Helen travelled the globe and found her voice by lecturing worldwide as a bold and relentless advocate for the poor, people of color, and people with disabilities, especially those who were blind. For more than five decades, Helen Keller testified before the U.S. Congress championing disability rights including equal education opportunities, job and teacher training, uniform and affordable reading materials and accessible public transportation.

In 1944, a spry, engaged and active 64-year-old Helen Keller testified before the U.S. House Committee on Labor. She described the need for increased financial resources for people of color, those without access to an education, and for blind and deaf individuals. At the time, she argued that blind individuals had to incur “unaided peculiar expenses which lack of sight” entailed. “For instance they must pay a guide or a reader at the sacrifice of other precious necessaries.” She testified that most blind individuals “cannot afford Braille writers or typewriters.” Then she asked the committee members to imagine themselves in the dark “unable to send a written message to a son or a brother overseas.”

Seventy-four years later, Helen Keller would be deeply disappointed to learn that blind individuals in the United States continue to suffer “unaided peculiar expenses,” sky-high unemployment rates and workplace discrimination. The National Federation of the Blind (NFB) reports that nearly 72% of blind Americans are unemployed or underemployed and more than 30% are living in poverty. The high rates of under- and unemployment and lack of livable incomes are due, among other reasons, to the fact that current opportunities for education and employment demand access to technology. Unfortunately, access to technology is expensive, with costs ranging from $1,000 up to $6,000. For example, a screen reader is $900, a Braille note taker is $5,495, a refreshable Braille display is $2,795, and a moderately priced Braille embosser is $3,695. Most blind Americans do not have the financial resources needed to purchase this or similar equipment. These financial barriers disable rather than enable work, education and training leading to prohibitive under- and unemployment rates, inadequate education and skills, and isolation from political, social and other community activities.

For a discussion of disability rights now and then, see Rhonda Neuhaus and Cindy Smith, Disability Rights Through the Mid-20th Century, 31 American Bar Association GP-Solo (Nov./Dec. 2014) noting that:

The laws of a nation reflect societal values. Historically, the laws of the United States devalued persons with disabilities as society as a whole viewed such persons as a group of people to be pitied, ridiculed, rejected, and feared, or as objects of fascination. Persons with disabilities were seen as objects of charity or welfare or as needing to be subjected to medical treatment or cure. As a result of these views, persons with disabilities were denied basic human rights (as is quite frequently still the case today).

Id.
II. Enabling Work through the Tax Code

A. An Act Whose Time Has Come

Fortunately, Kimie Beverly Eacobacci, NFB's government affairs specialist and a former student at University of Nevada, William S. Boyd School of Law, has been working with members of Congress on a bipartisan, bicameral bill to mitigate these financial barriers. The Access Technology Affordability Act of 2017 (the Act) (H.R. 1734/S.732) provides a refundable tax credit to offset out-of-pocket expenses of up to $2,500 for “qualified access technology” (QAT) for qualifying blind individuals for consecutive three-year periods. Thus, the credit is not a financial advantage, but merely reimburses blind individuals for any out-of-pocket costs for their employment and educational barriers not otherwise covered by insurance, employers or educational institutions. For purposes of the credit, QAT means hardware, software, or other information technology the primary function of which is to convert or adapt information that is visually represented into forms or formats useable by blind individuals. Blind individuals are defined by using the definition used for the additional standard deduction amount for blindness under section 63(f)(4). Therefore, individuals are “blind if their central visual acuity does not exceed 20/200 in their better eye with correcting lenses, or if their visual acuity is greater than 20/200 but is accompanied by a limitation in the fields of vision such that the widest diameter of the visual field subtends an angle no greater than 20 degrees.”

The credit is targeted to low- and middle-income blind individuals and their families so it phases out $100 for every $1,000 (or part thereof) over $75,000 of modified adjusted gross income ($150,000 for joint tax returns). Both the credit amount and the phase-out thresholds are indexed annually for inflation so that they remain consistent over time. By empowering blind individuals with a reimbursement of their employment-related expenses, the credit enables them to buy, own, and use technology that will enable them to work and engage in a fuller and richer life.

B. Examples of Taxpayers Who Would Benefit from—and Benefit Society Under—the Act

John is a blind Vietnam War veteran. John’s only income is $1,200 that he receives each month from the Veterans Administration (VA) in non-taxable compensation for his service-related disabilities. John does not receive any VA benefit for his loss of eyesight because this condition developed after he had completed his military service. In 2018, John purchased QAT for $1,500; in 2019 he paid $750 to update his QAT; in 2020, John, again, spent $750 to update and repair his QAT. John will spend $3,000 out-of-pocket on QAT from 2018 through 2020, but would receive only $2,500 in tax credits over this three-year period because of the overall limitation under the Act.

Because John’s income does not exceed the modified adjusted gross income limitation (MAGI) for single individuals of $75,000, he is entitled to refundable credits of $1,500 in 2018, $750 in 2019, but only $250 in 2020 (the credit is limited to $2,500 in any consecutive three-year period). However, to receive the credit John must file a federal income tax return even if he is not otherwise required to file.
Because the credit amount and thresholds are indexed for inflation, amounts for years subsequent to its enactment could be higher than those amounts shown above and in the following examples.

**Alejandro is a blind individual under the Act** and prior to 2021 was working at his cousin’s restaurant. Although Alejandro had successfully completed a two-year community college certificate in business before his eyesight failed, his cousin paid him only the minimum wage for his work in 2018.

In 2018, Alejandro acquired QAT that allowed him to finish his four-year degree in accounting and successfully pass the CPA examination. After graduation in June of 2020, Alejandro was hired by an international accounting firm and with his wages from the restaurant had MAGI of $76,000 for that year. During 2021, his first full year as a professional accountant, Alejandro earned $80,000.

Alejandro paid $1,500 for QAT in 2018; in 2019 he paid $500 to update his QAT; in 2020 Alejandro purchased an upgraded QAT system for $750; and in 2021 he paid $500 to upgrade the new system.

Although Alejandro continued to work at his cousin's restaurant while he pursued his accounting degree, his MAGI in 2018 and 2019 did not exceed the threshold for single individuals of $75,000. Therefore, he was entitled to refundable credits of $1,500 and $500, respectively, in 2018 and 2019. However, because his MAGI in 2020 exceeded the $75,000 limit by $1,000, $100 of his total allowable three-year credit was phased out. Alejandro’s allowable refundable credit in 2020 was only $400 ($2,500 - $100 = $2,400) and ($2,400 - $1,500 - $500 = $400). Alejandro received only a $400 credit for the $750 of QAT he purchased in 2020 because of the $2,500 three-year limitation reduced as a result of his $76,000 income level ($1,000 above the MAGI threshold for single individuals of $75,000) down to $2,400.

In 2021 Alejandro will receive a tax credit of $500 for buying the upgrade for his QAT. Because his MAGI is $80,000, $500 of his consecutive three-year $2,500 QAT credit limit is reduced to $2,000 ($80,000 - $75,000 = $5,000) / $1,000 = 5) x $100 = $500]. Moreover, because this is the first year of a new three-year period, Alejandro is entitled to a credit for the entire $500 that he spent in 2021. Any subsequent purchases will be subject to the overall cap of $2,500 reduced by any phase-out for MAGI above the relevant threshold less the $500 of credit already received.

**Lakshmi is a single blind parent** and one of her two dependent daughters that live with her is also blind. During 2018-2020, Lakshmi pursues a technical degree at a local community college and also supports her family by working at the Center for the Blind, earning $35,000 per year. In 2018, Lakshmi purchases a QAT system for $3,500 to be used at home by her and her daughter to help them with their work and educational activities. In 2019, Lakshmi pays $1,000 to update the system and in 2020, she spends another $1,500 to update the QAT system again.

As long as Lakshmi does not earn more than $75,000, she is entitled to a refundable credit of $3,500 in 2018. Her 2019 refundable credit will be $1,000 [$5,000 ($2,500 x 2) - $3,500 = $1,500, but up to the amount of QAT purchased for the year or $1,000]. Her $1,500 of QAT expenses in 2020 will generate a limited refundable credit of only $500 ($5,000 – $3,500 – $1,000 = $500). In any consecutive three-year period, the credit is limited to $2,500 per qualified blind taxpayer including any qualifying blind dependents (here, $2,500 x 2 = $5,000).

**Alexander and Eliza are married blind individuals.** They have been married for ten years and have one dependent daughter who is also blind. Alexander is a stay-at-home dad. Eliza is an executive administrator at the Center for the Blind and earns $180,000 per year. In 2018, Alexander and Eliza purchase a QAT
system for their home for $3,500; in 2019 they pay $200 to update the system; and in 2020 they purchase an upgraded replacement QAT system for $6,000.

Even though Alexander and Eliza’s MAGI is greater than $150,000, they can claim the entire $3,500 of purchased QAT as a refundable credit in 2018. Their credit in 2018 is $3,500 \(\left[\frac{\$7,500}{3 \times \$2,500}\right]\) reduced by the phase-out of $3,000 = $4,500, but limited to annual QAT purchases of $3,500. The credit limitation is reduced by $100 for each $1,000 or fraction thereof in excess of $150,000 MAGI or $3,000 (30 x $100). In 2019, they will be entitled to a $200 credit for updating the QAT system ($4,500 - $3,500 = $1,000 up to the $200 of annual QAT purchases).

Assuming the same income level for 2020, credit for the $6,000 replacement system that they purchase in 2020 will be limited because of their MAGI and the overall three-year limitation. The total credit for the three-year consecutive period cannot exceed $7,500 ($2,500 x 3 qualified blind individuals). In addition, Alexander and Eliza’s total three-year QAT credit is limited by their MAGI in excess of $150,000, to $4,500 ($7,500 – $3,000). Therefore, they would only be entitled to claim $800 ($4,500 - $3,500 - $200 = $800) of the $6,000 QAT purchase in 2020.

If Alexander and Eliza had waited to purchase the new system in 2021 (the start of a new three-year period), assuming the same level of MAGI they would have been able to claim a credit of up to $4,500 of QAT reimbursement ($7,500 - $3,000).

**Marco and Dave are both blind.** In 2018, they each purchase $2,000 of QAT. In 2018, Marco worked as a lawyer for the Center for the Blind and earned $85,000. As an assistant professor Dave earned $65,000. Marco and Dave file 2018 tax returns as single individuals. Dave’s MAGI does not exceed the limit, therefore he receives a credit for the entire $2,000 paid for his QAT system. Marco’s QAT credit is partially phased out to a $1,500 credit. [$2,500 – $1,000 \(\left[\frac{\$85,000 – \$75,000}{\$1,000}\right]= 10\) 10 x $100].

If Dave and Marco had married before the end of 2018 and filed a joint tax return they would be entitled to a full reimbursement of their $4,000 QAT expenditures in 2018 ($85,000 + $65,000 = $150,000, thus they do not exceed the $150,000 MAGI limit for a married couple and their credit would not be reduced).

As these examples demonstrate, the credit will reimburse out-of-pocket expenses for QAT for low- and middle income blind taxpayers up to $2,500 per qualifying individual for each three-year consecutive period. Given barriers to education and work, the average annual household income for visually impaired individuals is less than $40,000. As a result, most blind individuals will qualify for full reimbursements up to the $2,500 three-year limitation. Hopefully, in time, these reimbursements will help to mitigate work and education barriers and thus increase self-confidence, skill sets, job opportunities and household income levels.

**III. #CripJustice**

Almost 75 years after Helen Keller had the foresight and tenacity to testify before members of Congress for reimbursements for “unaided peculiar necessities” for the blind, this Act is more than ripe. Helen said she longed “to accomplish a great and noble task, but it is my chief duty to accomplish small tasks as if they were great and noble.” This Act would enable countless small tasks that may well coalesce to be as great and noble as Helen Keller.
YOUNG LAWYERS CORNER

Save the Date: 18th Annual Law Student Tax Challenge (2018-2019)

An alternative to traditional moot court competitions, the Law Student Tax Challenge asks two-person teams of students to solve a cutting-edge and complex business problem that might arise in everyday tax practice. Teams are initially evaluated on two criteria: a memorandum to a senior partner and a letter to a client explaining the result. Based on the written work product, six teams from the J.D. Division and four teams from the LL.M. Division receive a free trip (including airfare and accommodations for two nights) to the Section of Taxation 2019 Midyear Meeting, January 17-19, in New Orleans, LA, where each team will defend its submission before a panel of judges representing the country's top tax practitioners and government officials, including Tax Court judges.

The competition, sponsored by the Young Lawyers Forum, is a great way for law students to showcase their knowledge in a real-world setting and gain valuable exposure to the tax law community. On average, more than 60 teams compete in the J.D. Division and more than 40 teams compete in the LL.M. Division.

**IMPORTANT DATES**

- **Problem Release Date:** September 4, 2018, released by 5pm ET
- **Submission Deadline:** November 6, 2018, by or before 5pm ET
- **Notification of Semifinalists and Finalists:** December 18, 2018
- **Semifinal and Final Oral Defense Rounds:** January 18, 2019, in New Orleans, LA
TAX Bits

You’ll Never Pay Too Much

By Robert S. Steinberg, Law Offices of Robert S. Steinberg, Palmetto Bay, FL

(To tune of, “You’ll Never Walk Alone,” by Richard Rodgers and Oscar Hammerstein II, from the 1945 Broadway musical show Carousel.1)

When you fear a tax storm,
When those ill-winds blow,
Looming tax-clouds can give a big fright.

You’d be wise to consult
With a Tax-Law Pro
So you’ll not worry sleepless all night.

Tax law has no heart.
Tax lawyers are smart.
And they come through in the clutch.

Tax law, tax law—
The tax lawyers know.
So, you’ll never pay too much.
You’ll never pay too much.

1 For the original Carousel version with Shirley Jones (skip to 3:32), https://www.youtube.com/watch?v=B7YhWlzdc-g; for the tune as performed by Gerry & the Pacemakers, https://www.youtube.com/watch?v=jahLGeX1hPM; for the tune as performed by Elvis Presley, https://www.youtube.com/watch?v=E4IgITXHDg; for the tune as performed by Frank Sinatra, https://www.youtube.com/watch?v=QrGHJbIXCs.
Government Submissions Boxscore

Government submissions are a key component of the Section’s government relations activities. Since August 15, 2017, the Section has coordinated the following government submissions. The full archive is available to the public on the website: http://www.americanbar.org/groups/taxation/policy.html.

SUBMISSIONS AND COMMENTS ON GOVERNMENT REGULATIONS, ADMINISTRATIVE RULINGS, BLANKET AUTHORITY and ABA POLICY

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The technical comments and blanket authority submissions listed in this index represent the views of the ABA Section of Taxation. They have not been approved by the ABA Board of Governors or the ABA House of Delegates and should not be construed as representing the policy of the ABA.
SECTION NEWS & ANNOUNCEMENTS

2018-2019 John S. Nolan Fellowships

The American Bar Association Section of Taxation announced the recipients of the 2018-2019 John S. Nolan Fellowships during the Section’s May Meeting in Washington, D.C. Nolan Fellows are young tax lawyers who are actively involved in the Section, have demonstrated leadership qualities, and commitment to the Section’s mission.

The six 2018-2019 Nolan Fellows are:

- Giselle Alexander, Dickinson Wright, Phoenix, AZ;
- James Creech, Law Offices of James Creech, San Francisco, CA;
- Yongo Ding, Miller & Chevalier, Washington, DC;
- Frank DiPietro, Indiana Legal Services, Bloomington, IN;
- Jeffrey Dirmann, Agostino & Associates, Hackensack, NJ;
- Anne Gordon, PWC, McLean, VA.

“We are pleased to announce these young lawyers as our Nolan Fellows for 2018-2019,” said Karen L. Hawkins, Chair of the Section of Taxation. “Nolan Fellows are young lawyers and those new to tax practice who have demonstrated exceptional leadership ability and a commitment to the Tax Section mission. We hope they will remain active with the Tax Section for many years to come.”

The one-year fellowship includes waiver of meeting registration fees and assistance with travel to Section meetings. For more information about the Nolan Fellowship program, visit the Section website, http://www.americanbar.org/groups/taxation/awards/nolans.html.
SECTION NEWS & ANNOUNCEMENTS

Accepting Applications for the 2019-2021 Christine A. Brunswick Public Service Fellowship

The American Bar Association Section of Taxation is pleased to announce that it is now accepting applications for its Christine A. Brunswick Public Service Fellowship program class of 2019-2021. Developed in 2008, the Fellowship program seeks to address the growing need for tax legal assistance and to foster a greater interest in tax-focused public service through funding and other support to young lawyers engaged in tax work for underserved communities.

The deadline for applications is November 16, 2018. Visit the Christine A. Brunswick Public Service Fellowship page for more information about the award criteria and to download the application form.

ABA Section of Taxation’s End-of-Summer Book Sale

Save this summer on the ABA Section of Taxation’s bestselling titles! Use promo code TXSUMMER18 at checkout to save 15%. Visit www.ambar.org/taxpubs to see the Section’s complete catalog of tax titles. Sale on Section publications ends August 31, 2018.

TaxIQ: Access Materials from Past Section Meetings

TaxIQ offers online access to the latest committee program materials presented at Tax Section Meetings. Using either our static, Section-hosted website—TaxIQ—or a searchable database powered by Westlaw, access is only a few clicks away.

Access to these databases are an exclusive benefit of membership in the Section of Taxation. Click here to access the Westlaw and TaxIQ databases. You will be prompted to log into the websites, so please have your ABA-associated email address and password handy.

Audio Edition of The Tax Lawyer Available from ModioLegal

How much is an hour of your desk-time worth? Listen to the same content as the print edition of The Tax Lawyer without forgoing billable time – approximately 40 hours of content per year!
The Tax Lawyer – Spring 2018 Issue Is Available

The Spring 2018 Issue of The Tax Lawyer, the nation's premier, peer-reviewed tax law journal, is now available. The Tax Lawyer is published quarterly as a service to members of the Tax Section. Click here to read or download the complete issue.

2018 Erwin N. Griswold Lecture Before the American College of Tax Counsel

Martin J. McMahon, Jr., Tax Policy Elegy

Articles


Bradley T. Borden & Sang Hee Lee, Quantitative Prediction Model of Tax Law's Substantial Authority

Fred B. Brown, Proposing a Single, Simpler Test for Cash Equivalency

Philip G. Cohen, The Fact of the Liability Requirement in the All Events Test—Flying Lessons over the Dark Clouds of General Dynamics from a Giant Eagle

Eric A. San Juan, The Distributive State and the Function of Tax Expenditures

Bruce A. McGovern & Cassady V. Brewer, Recent Developments in Federal Income Taxation: The Year 2017

The Practical Tax Lawyer – August 2018 Issue Is Available

Produced in cooperation with the Tax Section and published by ALI-CLE, The Practical Tax Lawyer offers concise, practice-oriented articles to assist lawyers with all aspects of tax practice. The articles are written by practitioners and are reviewed by an expert board of editorial advisors who are members of the ABA Tax Section and are appointed by the Section. Published four times yearly, each issue of The Practical Tax Lawyer brings you pragmatic, nuts-and-bolts advice on how to solve your clients’ tax problems. The new issue features the following articles

Theodore M. David, Learn To Love the IRS


Sarah-Jane Morin, Tax Aspects of Cryptocurrency with a focus on the Tax Aspects of Initial Coin Offerings

William Prescott and Mark Altierei, Professional Practice Transitions, Section 197, and the Anti-Churning Rules

Dale Spradling, The Nuts and Bolts of an Offer in Compromise

John Cunningham, Advising Clients under Section 199A—A Revolutionary New Field of Tax and Legal Practice

Index to volumes 30, 31, and 32 (2016-2018)

For more information, visit PTL's webpage: https://www.ali-cle.org//index.cfm?fuseaction=publications.periodical&pub=PTL.
Support the Section’s Public Service Efforts with a Contribution to the TAPS Endowment

Through the Tax Assistance Public Service (TAPS) endowment fund, the Section of Taxation seeks to provide stable, long-term funding for its tax-related public service programs. The TAPS endowment fund will primarily support the Christine A. Brunswick Public Service Fellowship program. The Public Service Fellowship program provides two-year fellowships for recent law school graduates working for non-profit organizations offering tax-related legal assistance to underserved communities. Consider giving to the TAPS endowment fund today. Your generous support will help ensure that the Section can continue its mission to provide legal assistance to those in need.

Get Involved in ATT

ABA Tax Times (ATT) is looking for volunteers to join its ranks as associate editors to assist in writing and acquiring articles for publication. This opportunity is open to Section members with significant writing or publication experience, a genuine interest in helping ATT attract great content, and a willingness to commit to at least one article a year. You can find more information about our submission guidelines here. If you are interested in a regular writing and editing opportunity with ATT, contact Linda M. Beale, Supervising Editor, at lbeale@wayne.edu.
### Section CLE Calendar

**www.americanbar.org/groups/taxation/events_cle.html**

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SECTION EVENTS & PROMOTIONS

ABA Section of Taxation CLE Products

Listen at your convenience to high-quality tax law CLE on a variety of topics. ABA CLE downloads are generally accepted in the following MCLE jurisdictions: AK, AR, CA, CO, GA, HI, IL, MO, MT, NV, NM, NY, ND, OR, TX, UT, VT, WV. Recordings and course materials from the following recent Tax Section webinars and more are available at www.shopABA.org.

- The 2017 Tax Act and Its Impact on Corporate Transactions
- Nuts & Bolts Collections Part II: Next Steps in Assisting Pro Bono Clients with Collections Matters
- Tax Planning for Law Firms under the 2017 Tax Act
- What Tax Reform Means for Affiliated and Related Corporations
- Nuts & Bolts Collections Workshop: A Guide to Assisting Pro Bono Clients with Collection Matters
- Tax Reform and Implications for Financial Transactions
- C Corporation or Pass Through? Analyzing the Decision in the Wake of the 2017 Tax Act
- Keepin' It Real: Limitations on 1031 Exchanges Under the New Tax Act
- U.S. Tax Reform: Are You and Your Clients Prepared?
- Changes to S Corporation, Partnership and LLC Taxation under the Tax Cuts and Jobs Act
- Captives and Pooling After Avrahami
- Cloud Computing: Current Sales Tax Issues
- Dawn of a New Era – the New Partnership Audit Rules Will Soon Be Upon Us
- The Ethical Duty of Technology Competence
- The Nuts and Bolts of Consolidated Return Regulations
- Common Cross-Border Issues in M&A and Tax Planning
SECTION EVENTS & PROMOTIONS

Sponsorship Opportunities

ENHANCE YOUR VISIBILITY. GROW YOUR NETWORK. EXPAND YOUR REACH.

ABA Section of Taxation Sponsorship Provides Invaluable Returns.

ABA Section of Taxation Meetings are the premier venues for tax practitioners and government guests to connect on the latest developments in tax law and practice. Section Meetings draw up to 2,000 tax practitioners from across the U.S. and internationally. With over 150 panel discussions presented over two days by the country’s leading tax attorneys, government officials, and policy makers, Section Meetings are your opportunity to maximize your organization’s visibility and build relationships with key figures in the world of tax law.

The Section of Taxation is the largest, most prestigious group of tax lawyers in the country, serving nearly 16,000 members and the public at large.

• Over 10,000 Section members are in private practice
• 1,100 members are in-house counsel
• 32% of meeting attendees represent government
• 25% come from firms of over 100 attorneys
• 23% come from firms of 1-20 attorneys

Sponsorship Opportunities are now available for the following meetings:

| October 4 - 6, 2018 | FALL TAX MEETING  
Cosponsored by the ABA Sections of Taxation and  
Real Property Trust & Estate Law, Trust & Estate Division | Hyatt Regency – Atlanta, GA |
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For additional information on the above conferences or any of our other conferences, please visit [http://www.americanbar.org/groups/taxation/sponsorship.html](http://www.americanbar.org/groups/taxation/sponsorship.html) or contact our Sponsorship Team at taxmem@americanbar.org or at 202/662-8680.
Thank You To Our International Tax Planning Strategies Conference Sponsors!

**18th Annual US-Europe Tax Planning Strategies Conference**

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**EXHIBITORS**

**11th Annual US-Latin America Tax Planning Strategies Conference**

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