S Corporation Association Update
August 28, 2019

S-Corp Update Contents

1. Tax Affecting S-Corps

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For those not in the business valuation business, the term "tax affecting" might be a new one. But in the S corporation world, the term is rife with controversy. The question is, when valuing an S corporation for gift and estate tax purposes, do you discount it for the taxes the S corporation's owners will have to pay? The business community says yes, the IRS (ridiculously) says no, and recent court rulings have gone in several different directions.

So the S-Corp world cheered last week when the Tax Court ruled in favor of an Oregon timber company and against the IRS. You can read the full decision here. The key graph in our opinion is this:

> *We find on the record before us that [the company valuation expert] has more accurately taken into account the tax consequences of SJTC's flowthrough status for purposes of estimating what a willing buyer and willing seller might conclude regarding its value. His adjustments include a reduction in the total tax burden by imputing the burden of the current tax that an owner might owe on the entity's earnings and the benefit of a future dividend tax avoided that an owner might enjoy…. [The company's] tax-affecting may not be exact, but it is more complete and more convincing than [the IRS'] zero tax rate.*

Not convinced that this is a big deal? The valuation difference was $140 million (IRS) verses $21 million (company). Not all that was due to tax affecting, but much of it was. That's a lot of timber.

2. GILTI Notice Big Win for S-CORPs

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Final GILTI regulations issued by Treasury in July would have imposed two layers of tax on numerous S corporations with overseas subsidiaries, as the rules created a mismatch between income attributed to the parent S corporation and income and taxes paid by the S corporation's owners.

S-CORP highlighted the challenge in a July 29th letter to Treasury. As the letter states:

> *The final GILTI regulations released on June 14 completely change the manner in which S Corporations are required to attribute their GILTI income. While the proposed rules took an*

entity-level approach for determining GILTI income of a CFC owned through an S corporation, the final rules treat the individual shareholders, not the S corporation, as the owner of the foreign shares for purposes of attributing the GILTI income.

This about face has put S corporations with CFCs in an extremely difficult position. With just a few weeks left to finalize their federal returns, they are being asked to work through an entirely new and, and in many cases extremely unfavorable, set of rules.

Well, good news! The folks at Tax Policy heard our concerns and last week issued Notice 2019-46, which provides S corporations with tangible relief by allowing them to file their 2018 taxes using either the proposed or the final rules. Filing taxes using the proposed rules should allow S corporations to avoid the mismatch, and ultimately, the double tax that could have occurred under the final rules. This solution applies to 2018 only, so S-CORP will continue to work to find solutions for these businesses in future tax years.

3. Treasury on 199A Guardrails

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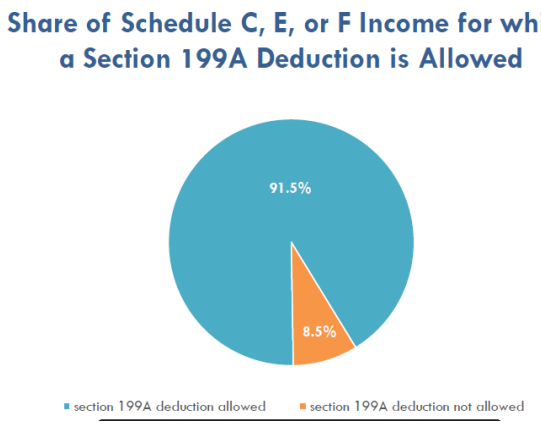
Remember this JCT chart from earlier this year? It garnered lots of attention and called into question how the 199A pass-through deduction was structured. If only 9 percent of all pass-through income was disqualified from getting the deduction, what was the point of having all those complicated rules?



We wondered about the estimate at the time, as it didn't comport with our member's experience. In our S-CORP survey this year, only half of our members expected to get the full deduction, while rest expected just a partial deduction or no deduction at all. How was it possible the excluded income of all those firms is only 9 percent of the total?

Read the entire post here.

4. S-CORP in the News

Passthrough Entity Tax Prompts Massachusetts Draft Directive -- Tax Notes, Aug. 23, 2019

Massachusetts is seeking input on a draft directive that would allow resident taxpayers a credit for their distributive share of taxes paid by passthrough entities under a 2018 Connecticut law.

Under a working draft directive released August 21, individuals and "other chapter 62 taxpayers" who are both Massachusetts residents and members of a passthrough entity subject to Connecticut's new passthrough entity tax are eligible for an income tax credit under chapter 62, section 6(a) of Massachusetts general laws for their distributive share of the entity's tax payment.

Connecticut enacted in 2018 a mandatory entity-level income tax on the net receipts of passthrough entities and an offsetting individual income tax credit for the entity's members. The legislation was a workaround to the Tax Cuts and Jobs Act's $10,000 cap on individual state and local tax deductions.

Brian Reardon, president of the S Corporation Association, praised the Massachusetts draft directive. "A key step to achieving SALT parity is for states like [Massachusetts] to recognize the tax credits and income exclusions of the states, like [Connecticut], enacting SALT reforms," Reardon told Tax Notes in an August 22 email. "The more states that do this, the sooner we can get full reform enacted here in D.C."

"Now if [Massachusetts] would just adopt their own SALT parity bill, all those S corporations up on Route 128 would have more money to invest and create jobs!" he added…

Citing Wisconsin as an example, Thomas J. Nichols of Meissner Tierney Fisher & Nichols SC told Tax Notes that "there are a number of states that have for years allowed their residents a credit for out-of-state income taxes paid at the corporate level (as well as composite and other taxes paid at the individual level)." The S Corporation Association has been circulating a March 2019 memo, authored by Nichols, that offers in part a legal analysis of Wisconsin's own entity-level SALT cap workaround.

The public comment period for Massachusetts's directive is open through September 13.

5. Social Media Update

@SCorpAssn, @MainStEmployers