Taxation & Representation, March 19, 2019
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Client Alert

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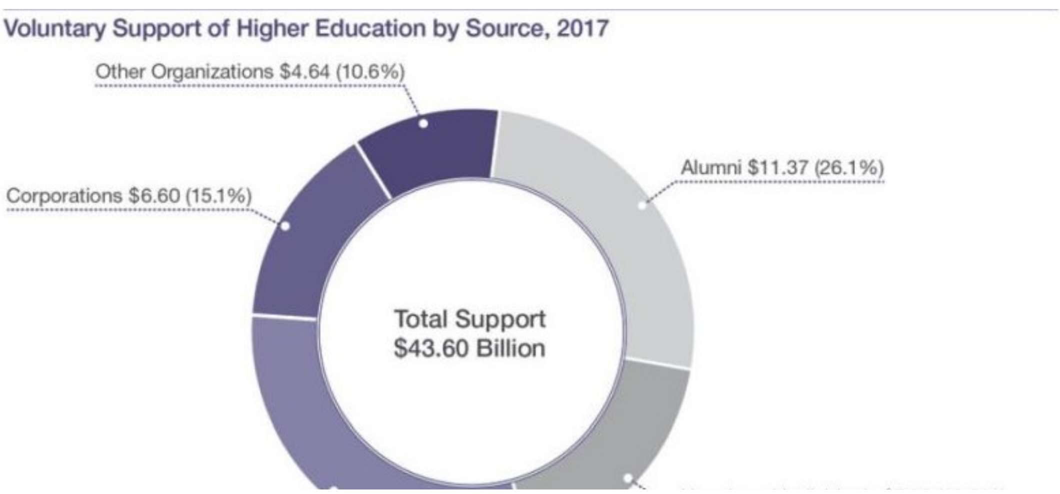

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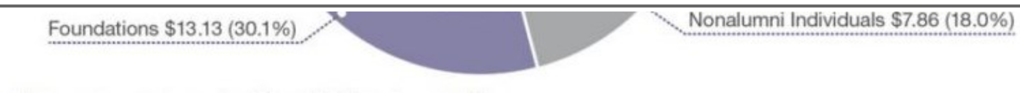

Source: Council for Advancement and Support of Education

$43,060,000,000: The amount of donations that higher-education institutions received in 2017. That's a lot of zeros. Even for Felicity Huffman.

As the nation is gripped by a Bernie Madoff-esque college cheating scandal, taxes—or more specifically, tax deductions—play a central role in the scheme.

Just in case our readers have been too preoccupied by **Treasury Secretary Steven Mnuchin's testimony** before Congress to follow along, here's a quick recap of the college cheating scam.

On Tuesday, March 12, federal prosecutors charged William Singer, founder of college preparatory business Edge College and Career Network, and its charity arm, Key Worldwide Foundation, with racketeering conspiracy; conspiracy to launder money; conspiracy to defraud the United States and obstruction of justice. Singer plead guilty to all charges and has been cooperating with investigators since February. About 50 parents have also been charged as part of the cheating scandal.

How did the scam work? Wealthy parents made over $25 million in payments to Singer to guarantee placement at selective universities for their children. Singer helped fake SAT scores and created photo shopped images and fraudulent recommendations falsely portraying children as student-athletes. Payments to Singer were disguised as charitable contributions to a nonprofit organization—the Key Worldwide Foundation. As a result, not only did parents secure admittance for their children at prestigious universities, but they also walked away with large tax breaks for these donations.

While payments to Singer were illegal and should not have been deductible, tax deductions for legal donations made to higher-education institutions are allowed. In fact, according to the Council for Advancement's annual survey, higher-education institutions raised $43.6 billion in 2018, which account for about 10 percent of overall charitable contributions. According to the **Joint Committee on Taxation**, tax breaks for donations to higher-education institutions will cost taxpayers about $46.2 billion between 2017-2021.

Singer's cheating scam may have been illegal, but there are several legal ways that wealthy students can gain a leg up during the admissions process. To address these concerns, on March 13, Senate Finance Committee Ranking Member Ron Wyden (D-OR) announced plans to introduce legislation that would end the tax benefit for donations made to colleges and universities before or during the enrollment of children of the donor's family. Wyden noted that while people attempt to distinguish Singer's crimes from "payoffs in the form of buildings or stadiums to secure access for the undeserving, it is all part of the same corrupt system."

Wealthier private colleges and universities with large endowments took a hit under the *Tax Cuts and Jobs Act* (P.L. 115-97), which subjects these institutions to a 1.4 percent tax on net investment income if they have at least 500 full-time students and investments assets of $500,000 per full-time student, similar to the excise tax on private foundations. Watch out—Congress is on the hunt for infrastructure pay-fors!

LEGISLATIVE LOWDOWN

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Extenders: Contenders or Pretenders? On Tuesday, March 12, the House Ways and Means Subcommittee on Select Revenue Measures **discussed temporary tax provisions** with a number of academics and practitioners weighing in on potential legislation. Republicans and Democrats agreed that extenders are capable of incentivizing positive behavior, such as energy conservation. However, there was disagreement among the panelists on whether or not the temporary tax provisions should be made permanent. Kyle Pomerleau of the Tax Foundation argued that temporary tax laws should be avoided as they create uncertainty for businesses, while Pam Olson of PricewaterhouseCoopers said the temporary nature of the provisions allows lawmakers the opportunity to evaluate the effectiveness of the breaks. For a deeper dive into the specifics, check out the Joint Committee on Taxation's **comprehensive breakdown** of the temporary tax breaks.

After the hearing, Subcommittee Chair Mike Thompson (D-CA) acknowledged the uncertainty created by temporary provisions and expressed the need to pass legislation as quickly as possible. The ranking member of the full committee, Rep. Kevin Brady (R-TX), agreed. Building off **draft legislation** he authored at the end of 2018, Brady has continued working on a bill to make some of the temporary provisions permanent, while allowing others to sunset. His bill is expected to parallel with the *Tax Extender and Disaster Relief Act* (**S.617**), introduced by Senate Finance Committee Chair Chuck Grassley (R-IA) and Ranking Member Ron Wyden (D-OR) last month.

Despite support from these heavyweight tax writers, some hurdles remain for extenders. The pay-as-you-go requirement put in place by House Democrats may make restoring the extenders without offsets challenging, unless the rule is waived. There has also been talk among congressional staffers that more progressive policies might find their way into extenders legislation in order to entice Democratic members on the far left to get on board. If these policies, such as an expansion of the Earned Income Tax Credit or the Child Tax Credit, make it into the package, the chances of Senate approval will decrease.

Better Later Than Never. After declining an earlier invitation to testify, Treasury Secretary Steven Mnuchin testified before the House and Senate tax writing committees to discuss the president's fiscal year 2020 budget proposal—"**A Budget for a Better America: Promises Kept. Taxpayers First.**" Well, at least that was the idea. Instead, lawmakers used the opportunity to once again debate the *Tax Cuts and Jobs Act (TCJA)* (P.L.115-97), with Republicans offering arguments that tax reform led to economic growth for all Americans and is leading to a record low unemployment for working class Americans, and Democrats saying wealthy individuals and corporations have benefited at the expense of the middle-class and poor.

During the House Ways and Means Committee hearing, Democrats used the opportunity to discuss President Trump's tax returns, multiemployer pension plans and penalty relief for filers who under-withheld taxes.

In the Senate Finance Committee hearing, lawmakers primarily battled over the impact of the TCJA with surprisingly little discussion of the president's budget proposal.

In both hearings, Republicans and Democrats agreed on one thing: the positive effects of Opportunity Zones, a provision that offers tax benefits for investments in certain economically depressed areas. Mnuchin said the Treasury Department is currently coordinating with the Office of Information and Regulatory Affairs (OIRA) to release additional guidance as soon as possible on the popular provision. Both parties also agreed on a need for infrastructure legislation; how to pay for the package remains a sticking point.

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Democrats Budge on Budget. Both Republicans and Democrats are engaging in intraparty battles over a host of issues, including the budget. Traditionally, the budget offers the controlling party a chance to outline its broader agenda. However, Democrats, now in control of the House, worry that voting on the budget resolution may simply expose the Democratic internal divide—something Speaker Nancy Pelosi (D-CA) wants to avoid. Internal fights over provisions like the Green New Deal and Medicare for All would expend enormous amounts of political capital but have no concrete outcomes. To avoid airing dirty laundry, Democrats will likely not schedule a vote in the full House of Representatives after releasing their budget draft in the coming weeks.

House Budget Committee Chair John Yarmuth (D-KY) agrees that avoiding the tension would be wise, saying "we're still proceeding as if we're going to do one, but we're also considering other options because we don't know if we can get 218 votes for anything." Some Democratic staffers agree the political messaging exercise would only accentuate the divergence within the party if brought to a vote.

Carried Off Into the Sunset. Sen. Tammy Baldwin (D-WI) and Rep. Bill Pascrell (D-NJ) re-introduced legislation last week that would end the carried-interest tax break to investment fund managers. The tax break allows some investment managers to tax portions of their income at the 23.8 percent top capital gains rate, rather than the top ordinary income rate of 37 percent. Democrats argue the tax break is an unfair practice because it allows wealthy fund managers to pay lower tax rates than middle-income workers. It is worth noting that President Trump also supported eliminating the carried-interest tax break while he was a presidential candidate. However, his signature tax law, the *Tax Cuts and Jobs Act* (P.L. 115-97), merely required fund managers hold onto their investments for three years, instead of one, to qualify for the lower rates.

So It Begins. Rep. Lloyd Doggett (D-TX) and Sen. Sheldon Whitehouse (D-RI) announced the introduction of two bills on Wednesday that would effectively repeal some provisions of the *Tax Cuts and Jobs Act* (P.L. 115-97). The first bill, the *No Tax Breaks for Outsourcing Act*, would stop companies from paying lower tax rates when income is earned offshore rather than within the U.S. The second bill, the *Stop Tax Haven Abuse Act*, would prevent companies from diverting profits to lower tax countries that the legislation labels as tax havens. The two lawmakers argue that both provisions encourage business outsourcing through tax inversion practices. The House Ways and Means Committee announced plans to hold hearings reviewing how *TCJA* has impacted the way U.S. companies pay tax globally, but has yet to announce any formal dates.

1111 CONSTITUTION

Budget Conscious. Early last week, President Trump released text for his 2020 budget, entitled "A Budget for a Better America: Promises Kept. Taxpayers First." The budget proposes $11.5 million in funding for the Internal Revenue Service (IRS), a small increase from the $11.3 million appropriated in the current fiscal year, which ends on Sept. 30. The budget would require social security numbers to be provided to claim the Earned Income Tax Credit. After the budget's release, the National Treasury Employees Union noted that the $200 million increase was insufficient to make up for $845 million in lost funding over the last decade which was cut by Republicans when the IRS was caught targeting conservative organizations. Further, the budget provides $50 billion in tax credits for the next decade for private education options. This was also quickly criticized by the Institute on Taxation and Economic Policy.

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Refunds, Refunds, Come Get Your Refunds. The Internal Revenue Service (IRS) announced that over 1.2 million taxpayers who did not file their 2015 Form 1040 have a month to claim nearly $1.4 billion in refunds. According to IRS Commissioner Chuck Rettig, “students, part-time workers and many others may have overlooked filing for 2015. And there’s no penalty for filing a late return if you’re due a refund.” Those who did not file 2015 tax returns have until April 15 to postmark their refund claim, with filers in Maine and Massachusetts having a slightly later deadline of April 17. All refunds not collected by then will become property of the Treasury Department. For 2015 filings, the IRS estimates that outstanding refunds have a median value of $879. Taxpayers who have not yet submitted their returns could also be missing out on $6,242 from the Earned Income Tax Credit (EITC). There is no penalty for filing late returns, but the refund may be withheld if an individual's tax returns from 2016 or 2017 have not been filed. Students and part-time workers are among the most likely to have forgotten to file their tax returns.

GLOBAL GETDOWN

Storming the Bastille. In light of France’s decision to institute an online digital revenue tax, senior Treasury Department officials began brainstorming ways to combat the effects. Chip Harter, the deputy assistant secretary for international tax affairs, spoke to reporters in Paris on March 12 and said the “United States opposes any digital services tax proposals” that have been pursued unilaterally. Instead, Harter stressed that any forthcoming proposal will be evaluated on the merits of unfairly discriminating against U.S. businesses “under trade, agreements, WTO, [and] treaties.”

On March 2, France became the first country to formally introduce legislation taxing top tech companies with expansive digital footprints in their country. The three percent tax would specifically apply to companies that generate over $850 million in annual revenue, with at least $28.3 million of that amount attributable to France. Among the 30 global companies that are subject to the tax are Facebook, Apple, Google, and Amazon. As a result, several U.S. officials have criticized the measure as an explicit attack on American tech giants. France may have started a trend as several European countries quickly expressed plans to institute their own version of the digital revenue tax. France’s digital tax comes after failed efforts by the EU to implement a European wide digital tax.

2020 VISION

Beto’s In. Shortly after entering the 2020 Democratic primary on Thursday, former U.S. representative Beto O'Rourke laid out his broad tax priorities. Pointing to the $2 trillion in lost revenues, O'Rourke criticized the *Tax Cuts and Jobs Act (TCJA)* (P.L.115-97) as "one of the most irresponsible things that the country has ever done." He argued that growing income inequality demands corporations and wealthy individuals pay a larger share of taxes. However, O'Rourke did not provide any detail about the extent and level of these tax hikes. He suggested new revenue from tax increases should be spent on public needs, such as Medicare for

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All, or used to address the $21 trillion national debt. O'Rourke has not released a detailed tax plan yet.

Taxing Giants. During the South by Southwest (SXSW) festival in Austin last week, presidential hopeful Sen. Amy Klobuchar (D-MN) floated a potential idea for taxing corporations that profit from the data they mine from consumers. With the growing number of presidential hopefuls, the Minnesota senator has tried to establish herself a consumer protection champion. During the conversation Sen. Klobuchar noted her distrust of big technology companies and added that their number one priority should be protecting people's safety and privacy. It is worth noting that Austin is home to Whole Foods, a subsidiary of Amazon.

REGWATCH

Carbon Capture Guidance. A Trump administration official revealed last week that the Treasury Department is crafting regulations on the carbon capture tax credit under section 45Q of the Internal Revenue Code. Last February, Congress raised the value for the carbon tax credit and expanded the number of companies that can qualify for the credit. Since then, lawmakers have accused the administration of moving too slowly in producing guidance. The Undersecretary of Energy, Mark Menezes, said the Department of Energy will soon be consulting with the Treasury Department on the formation of the regulations, and he urged industry professionals to participate in the comment period process.

Under the Feb. 2018 *Bipartisan Budget Act* (**P.L.115-123**), the tax credit was increased from $10 per ton of carbon stored to $35 and set aside $75 million for the credits. In order to qualify for the credit, companies need to begin projects before Jan. 1, 2024. However, because the Internal Revenue Service (IRS) could potentially take another year to release the guidance, taxpayers may be reluctant to begin projects until they know more.

In the Senate Finance Committee hearing on Thursday, Sen. Sheldon Whitehouse (D-RI) questioned Treasury Secretary Steven Mnuchin about the progress of the carbon capture guidance, saying that industry and academics are ready to make the most of the new rule but have been inhibited by doing so because of the lack of direction from the Treasury Department. Mnuchin stated he would look into the issue and is happy to coordinate further with congressional staff to move the process along.

AT A GLANCE

- **You Down with OPP'T (Zones)?** The Office of Management and Budget (OMB) last week started its internal review process for a set of proposed rules for tax-advantaged investments in opportunity zones. The proposed rules would determine what types of property are eligible as qualified opportunity zone business property, and would further define the steps that must be taken for a business to be eligible as a qualified opportunity zone business.
- **JCT Analysis on Passthroughs.** The Joint Committee on Taxation released on Wednesday a report on Section 199A deductions for qualified business income. The report can be found **here**.

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- **Consumer Financial Protect This.** Sen. Elizabeth Warren (D-MA) told Consumer Financial Protection Bureau Director Kathy Kraninger last week that she should "do [her] job or resign." Warren was particularly concerned with a seeming lack of consistency at the agency and for consumer protection settlements being "1/25th the size" of those by former director Richard Cordray.

BROWNSTEIN BOOKSHELF

- **Gas Tax Laboratories.** As Congress figures out how to fund the quickly deteriorating Highway Trust Fund and generate cash for an infrastructure overhaul, the ***Wall Street Journal*** provides an update on the latest state, Ohio, to advocate for a gas tax increase and takes a look at other laboratories of democracy considering similar measures.
- **States Receive March Madness Slam Dunk** With upwards of $8.5 billion in legal and illegal sports wages expected during this year's college basketball "March Madness" tournament, states could expect a mad amount of cash from tax revenues. Read more **here.**
- **In the Zone.** While a new tranche of opportunity zone regulations are on the horizon, the *New York Times* **outlines** how investors are itching for new guidance on which investments qualify for tax benefits.

REGULATION STATION

INTERNATIONAL

Regulation	Latest Action	Regulation Link	Comment Countdown	Brownstein Commentary
Sec. 965 Transition Tax	Feb. 5, 2019 **Final Regulations**	84 FR 1838	Deadline Passed Oct. 9	
Certain Hybrid Arrangements	Dec. 28, 2018	REG-104352-18	Deadline Passed Feb. 26	
BEAT (Sec. 59A)	Dec. 21, 2018	REG-104259-18	Deadline Passed Feb. 19	
Foreign Tax Credit	Dec. 7, 2018	REG-105600-18	Deadline Passed Feb. 5	
Sec. 956	Nov. 5, 2018	REG-114540-18	Deadline Passed Dec. 5	
GILTI	Oct. 10, 2018	REG-104390-18	Deadline Passed Nov. 26	
GILTI	Sept. 13, 2018	Rev. Proc. 2018-48	N/A	

199A

Regulation	Latest Action	Regulation Link	Comment Countdown	Brownstein Commentary

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Qualified Business Income Deduction (Sec. 199A)	Feb. 8, 2018	REG-134652-18	21 Days	
Qualified Business Income Deduction (Sec. 199A)	Feb. 8, 2019 **Final Regulations**	84 FR 2952	Deadline Passed Oct. 1	
W-2 Wages for Qualified Business Income Deduction (Sec. 199A)	Jan. 18, 2019	Rev. Proc. 2019-11	N/A	
Trade or Business Safe Harbor: Rental Real Estate (Sec. 199A)	Jan. 18, 2019	Notice 2019-07	N/A	Washington Update

DOMESTIC BUSINESS

Regulation	Latest Action	Regulation Link	Comment Countdown	Brownstein Commentary
Interest Expense Deduction	Dec. 28, 2018	REG-106089-18	Deadline Passed Feb. 26	
Opportunity Zones	Oct. 29, 2018	REG-115420-18	Deadline Passed Dec. 28	
Debt-Equity Documentation (Sec. 385)	Sept. 24, 2018	REG-130244-17	Deadline Passed Dec. 24	
Sec. 162(m)	Aug. 21, 2018	Notice 2018-68	N/A	Washington Update
Full Expensing	Aug. 3, 2018	REG-104397-18	Deadline Passed Oct. 9	
Carried Interest	March 1, 2018	Notice 2018-18	N/A	

EXEMPT ORGANIZATIONS

Regulation	Latest Action	Regulation Link	Comment Countdown	Brownstein Commentary
Excise Tax on Executive Compensation	Dec. 31, 2018	Notice 2019-09	N/A	
UBIT (Sec. 512(a)(7))	Dec. 10, 2018	Notice 2018-99	N/A	
UBIT (Sec. 512(a)(6))	Aug. 21, 2018	Notice 2018-67	N/A	Washington Update

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Higher Education Excise Tax	June 8, 2018	Notice 2018-55	Deadline Passed Sept. 6	

OTHER

Regulation	Latest Action	Regulation Link	Comment Countdown	Brownstein Commentary
Estate and Gift Taxes	Nov. 23, 2018	REG-106706-18	Deadline Passed Feb. 21	
Sec. 451(b) Market Discount Guidance	Sept. 27, 2018	Notice 2018-80	N/A	Washington Update
Safe Harbor of Eligible Rollover Distributions	Sept. 20, 2018	Notice 2018-74	N/A	Washington Update
SALT	Aug. 27, 2018	REG-112176-18	Deadline Passed Oct. 11	Washington Update
Education Savings	July 30, 2018	Notice 2018-58	N/A	Washington Update
Health Savings Accounts	March 5, 2018	Rev. Proc. 2018-18 Rev. Proc. 2018-27	N/A	

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