

## Upcoming Events

### NATP National Conference

Anaheim CA, Anaheim Marriott

August 6-9, 2018

See Pg 6 for NY Chapter Meet & Greet

### NATP Tax Forums

Atlantic City NJ, Harrah's

September 20-21, 2018

Las Vegas NV, Planet Hollywood

September 25-26, 2018

Indianapolis IN, Crowne Plaza

Downtown

October 17-18, 2018

## The NY Chapter Summer Series

The Summer of Tax Reform!

Day One: **NATP New York Chapter Summer of Tax Reform: Individuals and Trusts**

Day Two: **NATP New York Chapter Summer of Tax Reform: Tax Reform for Small Businesses**

See Page 8 for in depth details on topics, locations

# E-News

New York Chapter of NATP  
Monthly Newsletter

July 2018

## Are you going to conference in Anaheim?

If you will be attending to the National Conference in Anaheim be sure to look for chapter board members Matt Hall, CPA, Kathryn Keane, EA, Secretary Christina Parisi and Chapter President Ed Arcara, CPA. We are planning a meet and greet for New York chapter members, watch the bulletin boards for date, time and location. Safe travels, looking forward to seeing many of you there!



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## This Month's Issue

- Case Study
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- TCJA: The Empire (State) Strikes Back
- Summer Series Topics & Dates

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# Case Study:

## Taxation of Personal Services Income Received by Non-US/Foreign Person from the U.S.

This article is the second in the series of articles that discusses foreign-related issues - foreign information reporting, application for ITIN, foreign versus U.S. status, foreign vs. U.S. source income, and myriad foreign issues.

This second part discusses the taxation of personal services income, received by a non-US/foreign person (an entity or an individual), for services performed in the US. For this purpose following is assumed.

- The performer of services is a nonresident alien<sup>1</sup>, a foreign corporation<sup>2</sup> or a foreign partnership<sup>3</sup> as referenced under IRC sections 861, 864, 871, 882, 884, 1441, 1442, or 1446, to the extent these code sections are applicable to the taxation of personal services income and/or the tax rates applicable to the same.
- For the sake of simplicity, this article collectively refers foreign partnership, foreign corporation, or a nonresident alien individual as non-US/foreign person, or if the context requires otherwise, specifically as foreign corporation, foreign partnership, or non-US/foreign individual.
- The services are considered performed in the US, sourced in the US, and therefore unless statutory exception or treaty exemption applies, taxed in the US.
- If the services are performed by an individual, this individual is not from Mexico, Canada, or Puerto Rico. (special rules apply to individuals from these countries).
- The performance of personal services does not include pay for teaching, scholarships and fellowship grants, or payment under exchange or training programs, or other grants, prizes and awards (a somewhat similar but a separate set of rules apply to these).

The reason for these assumptions is that many of these are topics by themselves that require a more comprehensive analysis. In another part of this series I may discuss these topics separately.

When reviewing taxability of income from performance of personal services in the US by a non-US/foreign person, the questions to review include:

- Who is performing these services?
  - An individual, or an entity?
- If an entity is performing these services
  - Is it a partnership, or a corporation, or a disregarded entity?
  - Is the performance of services characterized as a US effectively connected taxable income (USECTI) or is it a non-effectively connected income?
- If an individual is performing these services,
  - Is this performance as an employee or as an independent contractor?
  - Is the performance of services in the course of a trade or business of this individual?
  - What is the visa status of this individual?
  - How long is the individual in the US for this purpose?
  - What is the amount of compensation received?
  - Is there a tax treaty that changes the applicable tax?

First the general rules. The income from the performance of personal services is taxed in the jurisdiction where it is considered sourced. The place of payment, the place of residence of the payer, or the place where the contract to perform such services is entered is irrelevant for this purpose. As such only if the services are performed by a non-US/foreign person, in the US, that it is considered sourced in the US<sup>4</sup>. A de minimis exception to this general rule provides that the performance of services is not considered US source if, (1) the services are performed by a non-US/foreign person who is

present in the US for a period that does not exceed 90 days during the tax year, (2) with the total pay not exceeding \$3,000, and (3) the performance of services is under a contract with (a) a nonresident alien individual, foreign partnership, or foreign corporation, neither of whom are engaged in a trade or business in the United States; or (b) a U.S. citizen or resident alien individual, a domestic partnership, or a domestic corporation, if the labor or services are performed for an office or place of business maintained in a foreign country or in a possession of the United States by this individual, partnership, or corporation<sup>5</sup>. Note that even if each of the conditions set out in the preceding paragraph are satisfied but if the total pay is more than \$3,000, the total amount paid is considered income from sourced in the US.

Once it is ascertained that the performance of personal services by the non-US/foreign person is sourced to the US, the answers to the questions in the preceding paragraph are crucial to the determination of,

- the applicable US tax rate, that is 30%, or a graduated tax rate, or a reduced rate/no tax under an applicable tax treaty,
- the time at which this tax becomes payable and who pays this tax, that is thru the payments of quarterly estimates by the non-US/foreign person, or thru withholdings by the payer, and/or upon filing of the tax return by the non-US/foreign person, and
- the amount subject to tax, that is net income after all allowable deductions or gross income without any deductions.

Let us begin. In general, when we talk about the payment for performance of personal services, we think of an individual working as an employee or as an independent contractor. However, personal services can be performed by a foreign partnership or a foreign corporation. A clear understanding of who - an individual or an entity - is performing services is necessary to decide who pays the tax, how, and how much.

<sup>1</sup> IRC Sec. 7701(b)(1)(B) Individuals who are not US citizens and who do not meet either the green card test or the substantial presence test for resident alien status are considered nonresident aliens.

<sup>2</sup> IRC Sec. 7701(a)(4) and (5). A foreign corporation is a corporation that is neither created nor organized in the US or under the law of the US or of any State. Special

definition applies to corporation created or organized in Guam, American Samoa, the Northern Mariana Islands, or the Virgin Islands or under the law of any of those US possessions.

<sup>3</sup> IRC Sec. 7701(a)(4) and (5). Broadly speaking, a foreign partnership is a partnership that is neither created nor organized in the US or under the law of the

US or of any State, unless the Secretary provides otherwise by regulations. Under certain circumstances a domestic partnership may be treated as foreign. This article is not intended to review these complex situations.

<sup>4</sup> IRC Section 861(a)(3)

<sup>5</sup> IRC Section 861(a)(3)

1. ***Performance of Services By a foreign corporation:***

Generally, one is not likely to view an entity as providing personal services but view it as being in a trade or business in the US<sup>6</sup> and as such receiving a US effectively connected taxable income (US ECTI). Broadly speaking, the factors to consider in determining if an item of income is treated as an effectively connected or not include (a) whether the income is from assets used in, or held for use in, the conduct of the trade or business, or (b) whether the activities of that trade or business were a material factor in the realization of the income<sup>7</sup>.

2.

If the income of the foreign corporation is US ECTI it is taxed at a graduated rate applicable to corporations<sup>8</sup>. The foreign corporation will file the tax return for its tax year and pay the tax in the US on a net basis (that is after deduction of all allowable expenses under the US tax code)<sup>9</sup>. The foreign corporation may need to make estimated tax payments under normal rules applicable to the US corporations. In order to prevent the payor from withholding at 30% on this income, the foreign corporation must provide Form W-8ECI (Certificate of Foreign Person's Claim that Income is Effectively Connected With the Conduct of a Trade or Business in the United States) to the payor. If, however the foreign corporation is claiming exemption from any withholding due to treaty provision, the payor is not provided a Form W-8ECI but a Form 8233 (Exemption from Withholding on Compensation for Independent (and Certain Dependent)<sup>10</sup> is provided instead. Once the necessary form is received, the payer of the personal services income has no obligation to withhold any tax from the payment due to the foreign corporation.

If, however, the foreign corporation is considered not receiving a USECTI", or meets each of the following, the payor must withhold 30% of the gross payment of the personal service income. These conditions include:

- The foreign corporation qualifies as a personal holding corporation for income tax purposes<sup>11</sup>.
- The foreign corporation receives amounts under a contract for personal services of an individual whom the corporation has no right to designate.
- 25% or more in value of the outstanding stock of the foreign corporation at some time during the tax year is owned, directly or indirectly, by or for an individual who has performed, is to perform, or may be designated as the one to perform, the services called for under the contract<sup>12</sup>.

If taxed at 30%, this rate applies to the gross amount. No deduction is allowed. The payor reports and remits the 30% tax to the IRS using Form 1042 (Annual Withholding Tax Return for U.S. Source Income of Foreign Persons). Additionally, Form 1042-S (Foreign Person's U.S Source Income Subject to Withholding), is filed by the payor, with the IRS and a copy provided to the foreign corporation.

Whatever be the tax rate, 30% or graduated, the applicable tax treaty may reduce the applicable tax rate or exempt the personal services income from any US tax. Some of these treaty related matters are discussed in greater depth below under Item 3 (Performance of Personal Services by an Individual).

This indeed is a highly simplistic view of the taxation of income of a foreign corporation from the performance of personal services. More complex analysis may be necessary, for example if the foreign corporation has US offices or

employees, has a US subsidiary or other associated entity in the US, or nexus is created in a State in the course of performance of services, or is considered a controlled foreign corporation. In addition the foreign corporation may be subject to a 30% branch profits tax on the after-tax earnings of the corporation's US trade or business if certain conditions are met<sup>13</sup>. In conclusion, when an entity is providing personal services additional analysis is necessary.

3. ***Performance of Personal Services By a foreign partnership:***

Similar to a foreign corporation, generally one is not likely to view a partnership as providing personal services but view it as being in a trade or business in the US<sup>14</sup> and receiving US effectively connected taxable income ("USECTI"). Broadly speaking, the factors to consider in determining if an item of income is treated as an effectively connected or not include (a) whether the income is from assets used in, or held for use in, the conduct of the trade or business, or (b) whether the activities of that trade or business were a material factor in the realization of the income<sup>15</sup>.

Normally it will be a bit odd for a foreign partnership to directly (as opposed to through another US partnership or US corporation that it owns) provide personal services in the US. If, however the foreign partnership provides personal services directly, the discussion will be the same as above under "*Performance of Services By a foreign corporation*".

There is another unique wrinkle however with respect to foreign partnerships that have non-US/foreign persons as partners (as opposed US persons). Under section 1446, a partnership, with US effectively connected taxable income is required to withhold tax, at the highest marginal tax rate applicable to the individuals, on the distributive share of the ultimate individual foreign partner's partnership income. The

<sup>6</sup> IRC Reg. Sec. 1.864-2(b)(1)The term engaged in trade or business in the US does not include performance of personal services (i) for a nonresident individual, foreign partnership, foreign corporation, not engaged in trade or business within the US at any time during the taxable year, or (ii) for an office or place of business maintained in a foreign country or in a possession of the United States by an individual who is a citizen or resident of the US or by a domestic partnership, or a domestic corporation, by a nonresident individual who is temporarily present in the US for a period or periods not exceeding a total of 90 days during the taxable year and whose compensation for such services does not exceed in the aggregate gross amount of \$3,000.

<sup>7</sup> IRC Section 864(c)(2)

<sup>8</sup> IRC Section 882(a)

<sup>9</sup> IRC Section 882

<sup>10</sup> See instructions to Form W08ECI - Who must provide Form W-8ECI

<sup>11</sup> A personal holding company is the one that meets both the income and the stock ownership tests. (1) The Income test is met if at least 60% of the corporation's adjusted ordinary gross income for tax year after certain adjustments consists of dividends, interest, rent, royalties, annuities, amounts received from personal services contract, and income from estates and trusts. (2) The stock ownership test is met if at any time during the last half of the tax year of the corporation, 50% in value of the corporation's outstanding stock is held directly or indirectly by 5 or fewer individuals. IRC Sections 541, 542, and 544.

<sup>12</sup> IRC Section 543(a)(7)

<sup>13</sup> IRC Section 884.

<sup>14</sup> IRC Reg. Sec. 1.864-2(b)(1)The term engaged in trade or business in the US does not include performance of personal services (i) for a nonresident individual, foreign partnership, foreign corporation, not engaged in trade or business within the US at any time during the taxable year, or (ii) for an office or place of business maintained in a foreign country or in a possession of the United States by an individual who is a citizen or resident of the US or by a domestic partnership, or a domestic corporation, by a nonresident individual who is temporarily present in the US for a period or periods not exceeding a total of 90 days during the taxable year and whose compensation for such services does not exceed in the aggregate gross amount of \$3,000.

<sup>15</sup> IRC Section 864(c)(2)

tax is remitted by the partnership to the IRS using Forms 8804 and 8805. If the aggregate section 1446 tax on the US ECTI is \$500 or more, the partnership is required to make estimated tax payments due by 15<sup>th</sup> day of the 4<sup>th</sup>, 6<sup>th</sup>, 9<sup>th</sup>, and 12<sup>th</sup> months of the partnership's tax year. A copy of the Form 8805 is provided to the foreign partner. The foreign partner can then file his/her personal tax return in the US to seek refund of tax that is more than his/her marginal tax rate<sup>16</sup>. A foreign partner is not likely to have a taxpayer identification number to enable him/her to file a tax return in the US. The foreign partner must in that case apply for an ITIN using Form W-7, contemporaneous with the filing of his/her tax return on Form 1040NR. The tax withheld by the partnership is considered distribution by the partnership to the partner<sup>17</sup>.

Once again, this too is a highly simplistic view of otherwise a complex situation. A more complex analysis may become necessary if the foreign partnership conducts business thru another partnership, or another entity, or nexus is created in a State in the course of the conduct of the business. The review of the nationality of the partners will also be necessary. If the partners are all US residents or US citizens, the above withholding provisions or need to provide W-8ECI may not arise. Instead, a Form W-8 identifying partners as US residents/citizens can obviate the need to make any tax withholding.

4. ***Performance of Personal Services By an Individual:*** The taxability of income for the performance of personal services by an individual is governed by IRC Section 871 and associated withholding provisions are under section 1441. The tax rate and the applicable withholding provisions depend on whether the income is for
- independent personal services, or
  - dependent personal services.

Independent personal services is the term commonly used in the tax treaties. Basically, it is the performance of personal services by a non-US/foreign individual in his/her capacity as an independent contractor as opposed to as an employee. When the performance of personal services is as an employee, it is known as an income from dependent personal services.

***Independent personal services income:***

The income from the performance of independent personal services by a non-US/foreign individual, unless the tax treaty applies, and unless it is pursuant to a trade or business of the non-US/foreign individual, is taxed at 30%<sup>18</sup> and subject to withholding by the payer under IRC Section 1441. If the income from the performance of independent personal services is considered from a trade or business carried out in the US, it is taxed at a graduated tax rate applicable to individuals<sup>19</sup>. The tax is applied to net income after allowing all applicable deductions.

If taxed at 30%, this rate applies to the gross amount. No deduction is allowed. The payor reports and remits the 30% tax to the IRS using Form 1042 (Annual Withholding Tax Return for U.S. Source Income of Foreign Persons). Additionally, Form 1042-S (Foreign Person's U.S Source Income Subject to Withholding), is filed by the payor, with the IRS and a copy provided to the non-US/foreign individual. The code 17 is used, on Form 1042-S, to report this income. The non-US/foreign individual is next required to file his/her tax return for the tax year.

If considered trade or business<sup>20</sup> and therefore taxed at graduated tax rate, the taxpayer is required to file his/her tax return for the tax year and remit the tax to the IRS. The non-US/foreign individual may be required to make estimated tax payments under normal rules applicable to the US residents/citizens. In order to prevent the payor from

withholding at 30% on this income, the non-US/foreign individual must provide to the payor, a Form W-8ECI (Certificate of Foreign Person's Claim that Income is Effectively Connected With the Conduct of a Trade of Business in the United States). In the event, the non-US/foreign individual is claiming exemption from withholding due to treaty provision, the payor is not provided Form W-8ECI, but the payor is provided Form 8233 (Exemption from Withholding on Compensation for Independent (and Certain Dependent)<sup>21</sup>. Once the necessary form is received, the payor of the personal services income has no obligation to withhold any tax.

Whatever be the tax rate 30% or graduated, under the tax treaty between the US and the country of residence of the non-US/foreign individual, the applicable tax rate may be modified. A careful review of the applicable treaty is necessary before one determines the income subject to tax. This is because each country's tax treaty defines various terms, that permit reduced or no tax, quite differently. Some tax treaties treat the pay for independent personal services performed in the United States as business income and tax the same under the treaty provisions applicable to business profits.

Other tax treaties may exempt the independent personal services income from tax, if the non-US/foreign individual performs the services during a period he/she is temporarily present in the US (typically not more than 183 days), and such person is a resident of the treaty country.

The publication 901 provides a country specific overview of treaty provisions applicable to personal services income. While publication 901 is a good start to understand the applicability of the treaty to a given situation, it is no substitute to reading the relevant provisions of the treaty itself.

<sup>16</sup> Note that special rules apply to the foreign partners of a publicly traded partnership

<sup>17</sup> If the income is considered not US effectively connected 30% tax rate applies to distributive share of the partner's FDAP income. FDAP stands for fixed, determinable and annual periodic payment. Typical examples of FDAP income include interest, dividend, ren, royalty, personal services income, etc. The partnership is required to withhold and remit this tax using Form 1042, 1042-S.

<sup>18</sup> IRC Section 871(a)(1)

<sup>19</sup> IRC Section 871(b)

<sup>20</sup> IRC Reg. Sec. 1.864-2(b)(1) The term engaged in trade or business in the US does not include performance of personal services (i) for a nonresident individual, foreign partnership, foreign corporation, not engaged in trade or business within the US at any time during the taxable year, or (ii) for an office or place of business maintained in a foreign country or in a possession of the United States by an individual who is a citizen or resident of the US or by a domestic partnership, or a

domestic corporation, by a nonresident individual who is temporarily present in the US for a period or periods not exceeding a total of 90 days during the taxable year and whose compensation for such services does not exceed in the aggregate gross amount of \$3,000.

<sup>21</sup> See instructions to Form W-8ECI - Who must provide Form W-8ECI

In order to avail of the lower tax treaty rate or benefit of a treaty provision, the non-US/foreign individual must provide to the payor, Form 8233 [Exemption from Withholding on Compensation for Independent (and Certain Dependent) Personal Services of a Nonresident Alien Individual]. The non-US/foreign individual is also required to file (except under some very narrow exceptions), Form 8833 Treaty-Based Return Position Disclosure Under Section 6114 or 7701(b), together with his/her tax return.

Despite the available treaty provision, the payor may under certain circumstances withhold at 30% rate because the factors on which the treaty exemption is based may not be determinable until after the close of the tax year or at the time the payment is being made. For example, if at the time of payment of the personal services income, the parties are uncertain as to the term of the contract - less than or more than 183 days. The payor may withhold 30% despite the exemption/reduced rate claimed by the non-US/foreign individual. The non-US/foreign individual can recover the over withheld tax upon filing his tax return.

The above discussion related to the independent personal services income may become irrelevant if the final payment exemption under IRC Reg, Sec. 1.1441-4(b) applies. Subject to the approval from the IRS, meeting certain procedural requirements, and if the amount of the payment sought to be exempt from withholding is not more than \$5,000, the final or the last payment of compensation for personal services income may be exempt from withholding provisions of section 1441, either totally or partially.

*Dependent personal services income:*

The examples of dependent personal services income include salaries, wages, bonuses, or any other pay for personal services (“wages”). Subject to certain treaty exemptions or statutory exceptions, such income is subject to withholding at a graduated tax rate applicable to individuals and not at the 30% withholding rate.

The tax is withheld by the employer, each pay period, in a manner that is similar to the withholding on the payment of

wages to a US person. The non-US/foreign individual performing dependent personal services provides to the employer, a Form W-4 (Employee’s Withholding Certificate). The employer/payor reports wages to the employee on Form W-2 and pay/deposit taxes due by filing Form 941 and 940. Essentially the procedure for the payment of dependent personal services income to a non-US/foreign individual is similar to that applicable to the US resident/citizen.

As stated before, the tax treaty of some countries may exempt the wages paid for dependent personal services provided by the non-US/foreign individual in the US. A careful review of the applicable treaty is necessary before the payor may decide to apply reduced tax rate or not withhold any tax. This is because each country’s tax treaty defines various terms permitting reduced or no tax quite differently. Under some treaties the pay for dependent personal services is exempt from tax in the US if both the employer and the employee are treaty country residents and the non-US/foreign individual performs the services while temporarily living in the United States (usually for not more than 183 days).

The tax treaties of some other countries provide an exemption if the employer is a resident of any foreign country, the non-US/foreign employee is a resident of the treaty country, and the services are performed while the non-US/foreign employee is temporarily in the US.

The publication 901 provides a country specific overview of treaty provisions applicable to personal services income. While publication 901 is a good start to understand the applicability of the treaty to a given situation, it is no substitute to reading the relevant provisions of the treaty itself.

To avail of the lower tax treaty rate or benefit of a treaty provision, the non-US/foreign individual must provide to the payor, Form 8233 -Exemption from withholding on compensation for independent (and certain dependent) personal services of a nonresident alien individual. While in general the non-US/foreign employee is issued a W-2

evidencing payment of income and withholding, if a treaty provision is invoked, a Form 1042-S (Foreign Person’s U.S Source Income Subject to Withholding), is filed by the payor, with the IRS and a copy provided to the non-US/foreign individual. The code 18 is used, on Form 1042-S, to report this income. A W-2 may additionally be issued by the payor if the personal services income is subject to State tax. The non-US/foreign individual is next required to file his/her tax return together with Form 8833 [Treaty-Based Return Position Disclosure Under Section 6114 or 7701(b)].

Besides exemption under the applicable tax treaty, the Internal Revenue Code provides limited exemption under which the dependent or independent personal services income of a non-US/foreign individual is either not taxed in the US or is considered not sourced to the US and therefore not taxable in the US. For example,

- The following income is not sourced to the US and therefore not taxable in the US.
  - If the services are performed by a non-US/foreign individual who is present in the US for a period that does not exceed 90 days during the tax year, with the total pay not exceeding \$3,000, and the performance of services under a contract with (a) a nonresident alien individual, foreign partnership, or foreign corporation, neither of whom are engaged in a trade or business in the United States; or (b) a U.S. citizen or resident alien individual, a domestic partnership, or a domestic corporation, if the labor or services are performed for an office or place of business maintained in a foreign country or in a possession of the United States by this individual, partnership, or corporation<sup>22</sup>. Note that even if each of the conditions set out in the preceding paragraph are satisfied but if the total pay is more than \$3,000, the total amount paid is considered income from sources in the US and is subject to tax at graduated rate or if applicable at the treaty rate.
  - If the labor or services are performed by a non-US/foreign individual in connection with the individual’s temporary presence in the US as a regular member of the crew of a foreign vessel engaged in transportation between the US and a foreign country or a possession of the US, the

<sup>22</sup> IRC Section 861(a)(3)

compensation for such labor or service is deemed non-US source and therefore not taxable in the US<sup>23</sup>.

- The following income is exempted from US tax:
  - The compensation paid to “F”, “J”, or “Q” visa holders, by a foreign employer, for the period these visa holders are temporarily present in the US, is exempt from US income tax<sup>24</sup>. Typically, these visa holders comprise of students, scholars, trainees, teachers, researchers, research assistants, professors, specialists or leaders in specialized knowledge fields.
  - The compensation for personal services paid to certain residents of Mexico, Canada, or Puerto Rico may also not be subject to US tax. As mentioned earlier, there are many nuances to this exception and is not discussed here further.

5. ***By a Disregarded Entity:*** If services are performed by a disregarded entity, a further analysis as to the location (US or foreign) and status (corporation, partnership, or an individual) of the 100% owner needs to be looked at first. Depending on these findings any or none of the discussion may become applicable and a further analysis is necessary.

Finally, the taxation, reporting, and withholding of US source personal services income payable to a non-US/foreign person spans over a complex web of rules involving several code sections, review of treaty provisions of the country where the service provider is the resident as well as an if and then analysis of various factors. When we add to this mix (a) the nature of the services provided, that is as a teacher, or as a student, or as a researcher, (b) the visa status of the individual in the US, (c) the length of intended stay versus the length of the actual stay, and (b) the type of payment received, that is, pure wages, payment to a permanent establishment in the US, or scholarship, grant, award, or prize, or winning, the things get complicated very quickly. While many factors in seeking services from a foreigner may not be in the hands of the receiver of the personal services, in order to derive the best tax situation (for the receiver and the performer of the personal services) it is essential that the rules related to taxation of personal services income are not only

reviewed carefully but complied with quite carefully. The non-withholding of required tax, or non-filing of the required tax form to report the income and the tax withheld, are quite hefty, ranging from few hundred to a few thousand dollars depending on the type of violation.

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Marcum LLP ([www.marcumllp.com](http://www.marcumllp.com)) is a national accounting and advisory services firm with offices in major business markets throughout the U.S., as well as Grand Cayman, China, and Ireland.

## Want to join the NY Chapter Board?

By Matt Hall

At our Annual meeting this Fall we will have elections for chapter board members. We need volunteers to help run the chapter and keep providing the education that we all need to keep current. If you are interested in joining the board or want more information, please contact President Ed Arcara at (716) 884-2492.

## NY Chapter Meet & Greet!

2018 NATP National Conference & Expo  
Chris Bertuglia

Every year NATP hosts a 4-day National Conference where you can choose from various courses and earn up to 28 CPE. Attending the National Conference is a great way to learn from the high-quality courses given as well as network with other professionals. Throughout the conference, you can visit the expo hall where there are numerous vendors who will be giving out information on items from professional software to office supplies.

The NY Chapter will be hosting its annual meet and greet right after the charity event on Tuesday August 7<sup>th</sup>. The NY Chapter’s Board of Directors would like to show our appreciation to all NY members. Join us for a drink and some appetizers! It will be a great way for us to meet you and for you to meet other NY members!

Be sure to look out for our flyers when you get to the conference. We will be posting our location for the meet and greet.

<sup>23</sup> IRC Section 861(a)(3)

<sup>24</sup> IRC Section 872(b)(3)

# TCJA: THE EMPIRE (STATE) STRIKES BACK

By Michael Novick, EA

Many commentators agree that the Tax Cuts and Jobs Act of 2017 included more sweeping changes than any other tax law since the Tax Reform Act of 1986. This article is going to focus on one change that will significantly affect many New York taxpayers, the limitation on the deduction of state and local taxes (SALT).

As we know, taxpayers were previously able to deduct the full amount (subject to the Pease Limitation) of state and local income and property taxes paid during the year.

Good news: the Pease Limitation has been repealed. This means that there will be no phase out of itemized deductions for “high” income taxpayers (which in operation really wasn’t all that high at all)

Bad news: Under TCJA, SALT deductions will now be limited to \$10,000. That’s a TOTAL of \$10,000, not even \$10,000 per category.

In my practice, I have multiple clients who reside in New York State (some also within New York City) and have annual income in excess of \$2,000,000. Each of them owns a home or multiple homes.

Let’s examine a real life situation with a client whose W-2 showed wages of \$3,000,000 with \$450,000 of state and local withholding. In addition, the client owns a home and pays annual real estate tax of \$30,000.

In 2017, the full \$480,000 was deductible (subject to partial phase out) on Schedule A.

Fast forward one year to 2018. The taxpayer can now deduct only \$10,000.

You don’t have to be a mathematician to realize that even with a reduced tax rate, this client is facing a 2018 federal tax increase of more than \$150,000.

This article will examine New York State’s budgetary and judicial attempts to work around or offset the SALT limitation:

- Employer Compensation Expense Tax
- Charitable Gifts Trust Fund and
- Joining with neighboring states to file suit against the federal government

## EMPLOYER COMPENSATION EXPENSE TAX (ECET):

Under new Article 24, an employer can make an annual election to pay a tax on the payroll expense to certain “covered employees” earning more than \$40,000 per year. The tax rate will be 1.5% in 2019, 3% in 2020 and 5% in 2021 and later years.

An electing employer would only be subject to the tax to the extent that a covered employee’s calendar payroll expense exceeds \$40,000. Assume that in 2019, Employer X paid wages of \$100,000 to covered employee Y. X will pay \$900 (\$60,000 excess wage above \$40,000 x 1.5% rate)

On the personal side, the covered employee will get a credit against their New York State personal income tax liability.

Accordingly, the ECET shifts the burden from the individual to the employer. The individual would only be able to deduct the capped maximum. By contrast, the employer’s deduction would not be limited because the tax represents an ordinary and necessary business expense.

That sounds pretty good, doesn’t it? Unfortunately, there are some real world drawbacks including increased administrative payroll costs to the employer. Only time will tell as to the effectiveness of this program.

## CHARITABLE GIFTS TRUST FUND:

The 2018/19 fiscal year budget also created the Charitable Gifts Trust Fund which would provide individual taxpayers with a credit against New York State income tax liability. The credit would be equal to 85% of the contributions made to the fund in the preceding year.

How does this benefit individual taxpayers? Since charitable donations are (basically) unlimited on the federal return, the tax payment would be effectively converted to a contribution which is not affected by the TCJA cap.

The Budget also provides localities with the option to create similar funds for an individual’s real estate tax liabilities.

This sounds like a no brainer but there’s always a catch. The Service has issued guidance that is based on the doctrine of Substance over Form. In other words, the Service’s position is that a tax is a tax, regardless of how you label it.

## JUDICIAL:

Earlier this month, New York State Attorney General Barbara D. Underwood filed a lawsuit (joined by the Attorneys General of Connecticut, Maryland and New Jersey) against the federal government. The suit alleges that the SALT limitation is unconstitutional for the following reasons:

- The limitation was enacted to target New York State and similarly situated states;
- The limitation interferes with a state’s right to make its own fiscal decisions; and
- The limitation disproportionately harms taxpayers in these states.

It is well established that there’s no divine right to any tax deduction. The Legislature is solely responsible for creating, limiting or eliminating them.

Indeed, the deduction for state and local income tax has been the subject of extensive and sometimes heated debate for years (because some states such as New York have high income taxes, others have low rates and still others have no tax at all). Unfortunately, TCJA represents the first time that Congress has chosen to act.

As stated above, the lawsuit specifically cites the disproportionate effect of this provision. However, that can be said about almost any law (and not just taxes).

Some people talk about the unfairness and even the retaliatory nature of this change. As tax professionals, we recognize that equity is not always present in the legislative process. As a corollary, inequity, by itself, is not sufficient to strike down a law as unconstitutional.

One final point: Over the past (approximately) 15 years, many middle class New York taxpayers have enjoyed little to no benefit to SALT deductions because the entire tax section of Schedule A is disallowed in the Alternative Minimum Tax computation.

We could be in for a long ride. Stay tuned.

# Summer Series Dates/Locations

## Summer of Tax Reform: Individuals and Trusts (8CE)

8:00 am - 5:00 pm

Tax Reform changed the face of the tax world. This hands-on seminar looks at how tax reform impacts the 1040 as well as presenting an overview of Trusts. The session will cover the changes to Schedule A, the expanded Child Tax Credit, new Family Tax Credit, changes to 529 and the how the world turned upside down.

### At the end of this session, attendees will be able to:

- Recognize the new Standard Deductions and Tax Rates
- Distinguish between Qualified Child and Qualified Relative
- Calculate the 2018 federal state and local tax deduction.
- Discuss the impact of items no longer deductible on the Schedule A
- Calculate the new Kiddie Tax
- Determine the expanded Child Tax Credit
- Understand the new Family Tax Credit
- Advise clients on the expanded uses of 529 funds, including rollover to ABLE
- Understand why clients form Trust
- Recognize the different types of Trusts utilized by clients
- Determine when a Trust tax return is due

## Summer of Tax Reform: Tax Reform for Small Businesses (8CE)

8:00 am - 5:00 pm

Tax Reform for Small Businesses Tax Reform radically changes how our small business clients will move forward. This session will review how Tax Reform will be implemented among our Schedule C filers as well as entity members and corporations.

### At the end of this session, attendees will be able to:

- Recognize when the Small Business Deduction is available
- Calculate the Small Business Deduction
- Discuss the Small Business Accounting Method expansion
- Utilize Bonus Depreciation, Section 179
- Discuss the new Paid Family/Medical Leave credit
- Recognize the revised NOL provisions
- Discuss the previously available tax breaks no longer available

### Register Online:

<https://www.natptax.com/Chapters/Pages/NewYorkChapterEducation.aspx>

**By Phone:** Call Member Services (800) 558-3402 Ex 3

Mail/Fax Registration forms available at the end of newsletter

## Locations:

Aug. 2-3, 2018

[del Lago Resort & Casino](#)

1133 State Route 414

Waterloo, NY 13165

Room Rate Code: NYNATP

Aug. 20-21, 2018

[Hilton Garden Inn Melville](#)

1575 Round Swamp Rd

Plainview, NY 11803

Room Rate Code: NYNATP

Aug. 22-23, 2018

[Adria Hotel & Conference Center](#)

221-17 Northern Blvd

Bayside, NY 11361

Room Rate Code: NYNATP

Aug. 27-28, 2018

[Hampton Inn Tarrytown](#)

200 West Main St

Elmsford, NY 10523

Room Rate Code: NYNATP

Aug. 29-30, 2018

[Courtyard Albany Airport](#)

168 Wolf Road

Albany, NY 12205

Room Rate Code: NYNATP

## Tax Season Issues?

Did you have a taxpayer who asked a tricky tax question that you just couldn't answer?

Did you encounter a tax issue not common in your practice and need some guidance?

Send them to the NYS Chapter!

For the past three years, we have gathered your questions and sticky situations into our Tax Season Issues Module for our Fall Series and it has been a HUGE hit!

For this coming year we would love to keep Tax Season Issues fresh and exciting for our seminars, but we can't do it without your help!

Send your "Tax Season Issues" to Rick Rottkamp at [rh1040@aol.com](mailto:rh1040@aol.com)

You may just find the answer in our 2018 Fall Seminar!

## NY Chapter Founders Award

Ralph Sommers  
2013

Wendy C. Loomis  
2014

Karl Herba  
2015

Dwayne "Rocky" Rhodes  
2016

Kathryn M. Keane  
2017



## Newsletter Committee:

Kathryn M. Keane, EA  
Christina Parisi &  
Tricia Santana

## Purchasing a Quickfinder?

Will you be buying a Quickfinder for the coming season? The NY Chapter receives a donation for each book ordered when you use the Association Code below, mention NATP or use the Special Order Form provided at:

<http://newyorknatp.com/quickfinder-purchase/>

Quickfinder Association Code Q680

***You also receive a discount when you mention our codes!***

***The NY Chapter THANKS YOU FOR YOUR SUPPORT!!***



**NATP New York Chapter  
Summer of Tax Reform:  
Tax Reform for Small Businesses**

8:00 am – 5:00 pm

Name: \_\_\_\_\_ Member ID#: \_\_\_\_\_

Designation(s): \_\_\_\_\_ License #: \_\_\_\_\_ PTIN #: \_\_\_\_\_

Address: \_\_\_\_\_

City: \_\_\_\_\_ State: \_\_\_\_\_ Zip: \_\_\_\_\_

Email: \_\_\_\_\_ Phone: \_\_\_\_\_

Emergency Contact Name & Phone Number \_\_\_\_\_

Check here if the above address should be your main mailing address.

<b>Registration Fees</b>	<b>Member</b>	<b>Non-Member</b>
Early Bird <i>(ends 8 days prior to seminar)</i>	\$225	\$250
Standard	\$250	\$275
Guest Meal Ticket	\$25	
Paper Materials	\$20	

*Registration includes  
E-Materials  
and  
Lunch*

Location – Please check the box in front of the location you wish to attend.		
<input type="checkbox"/>	Plainview – Hilton Garden Inn - Melville	Aug. 21, 2018
<input type="checkbox"/>	Bayside – Adria Hotel & Conf. Center - Queens	Aug. 23, 2018
<input type="checkbox"/>	Elmsford – Hampton Inn – Tarrytown	Aug. 28, 2018
<input type="checkbox"/>	Albany – Courtyard - Albany Airport	Aug. 30, 2018
<input type="checkbox"/>		

Payment Method: Credit Card or Checks made payable to NATP

Name as it appears on CC: \_\_\_\_\_

CC #: \_\_\_\_\_ Exp. Date: \_\_\_\_\_ CVV # \_\_\_\_\_

Signature: \_\_\_\_\_

**How To Register:**

**Mail To:** NATP, PO Box 8002 Appleton, WI 54912-8002

**Phone:** 800.558.3402, Ext. 3

**Fax:** 800.747.0001

**Online:** <https://www.natptax.com/Chapters/Pages/NewYorkChapterEducation.aspx>

Cancellation Policy: Cancellations must be submitted to NATP no later than 8 days prior to the seminar to receive a refund. Cancellation is subject to a \$25 fee.



**NATP New York Chapter  
Summer of Tax Reform:  
Individuals and Trusts**

8:00 am – 5:00 pm

Name: \_\_\_\_\_ Member ID#: \_\_\_\_\_  
 Designation(s): \_\_\_\_\_ License #: \_\_\_\_\_ PTIN #: \_\_\_\_\_  
 Address: \_\_\_\_\_  
 City: \_\_\_\_\_ State: \_\_\_\_\_ Zip: \_\_\_\_\_  
 Email: \_\_\_\_\_ Phone: \_\_\_\_\_  
 Emergency Contact Name & Phone Number \_\_\_\_\_

Check here if the above address should be your main mailing address.

Registration Fees	Member	Non-Member
Early Bird <i>(ends 8 days prior to seminar)</i>	\$225	\$250
Standard	\$250	\$275
Guest Meal Ticket	\$25	
Paper Materials	\$20	

*Registration includes  
E-Materials  
and  
Lunch*

Location – Please check the box in front of the location you wish to attend.		
<input type="checkbox"/>	Plainview – Hilton Garden Inn - Melville	Aug. 20, 2018
<input type="checkbox"/>	Bayside – Adria Hotel & Conf. Center - Queens	Aug. 22, 2018
<input type="checkbox"/>	Elmsford – Hampton Inn – Tarrytown	Aug. 27, 2018
<input type="checkbox"/>	Albany – Courtyard - Albany Airport	Aug. 29, 2018
<input type="checkbox"/>		

Payment Method: Credit Card or Checks made payable to NATP

Name as it appears on CC: \_\_\_\_\_

CC #: \_\_\_\_\_ Exp. Date: \_\_\_\_\_ CVV # \_\_\_\_\_

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# QUICKFINDER HANDBOOKS AND QUICK REFERENCE GUIDES

TAX PREPARATION TOOLS	BEST VALUE			BEST VALUE			ORDER TOTAL	BEST VALUE			ORDER TOTAL
	Standard Binding	ProView eBook	3-Ring Binder	Standard Binding	ProView eBook	3-Ring Binder		Standard Binding	ProView eBook	3-Ring Binder	
	LIST PRICE			ORDER QUANTITY				TOTAL PRODUCT ORDER \$			
	A	B	C	D	E	F		COLUMN A X COLUMN D	COLUMN B X COLUMN E	COLUMN C X COLUMN F	
EXAMPLE PRODUCT	\$55	\$51	\$58	2	5	6	13	\$110	\$255	\$348	\$713
1040 Quickfinder Handbook	\$55	\$51	\$58					\$	\$	\$	\$
Small Business Quickfinder Handbook	\$55	\$51	\$58					\$	\$	\$	\$
Premium Quickfinder Handbook	\$77	\$73	\$80					\$	\$	\$	\$
All States Quickfinder Handbook	\$85	\$81	N/A			N/A		\$	\$	N/A	\$
Individuals – Special Tax Situations Quickfinder Handbook	\$55	\$51	N/A			N/A		\$	\$	N/A	\$
Depreciation Quickfinder Handbook	\$55	\$51	N/A			N/A		\$	\$	N/A	\$
Laminated Tax Tables for Individual Returns	\$16	\$12	N/A			N/A		\$	\$	N/A	\$
Laminated Tax Tables for Business Returns	\$16	\$12	N/A			N/A		\$	\$	N/A	\$
TAX PLANNING TOOLS											
Health Care Reform Quickfinder Handbook	\$55	\$51	N/A			N/A		\$	\$	N/A	\$
Quickfinder Annual Tax Update	\$55	\$51	N/A			N/A		\$	\$	N/A	\$
Tax Planning for Individuals Quickfinder Handbook	\$55	\$51	N/A			N/A	N/A	\$	\$	N/A	\$
Social Security and Medicare Quickfinder Handbook	\$55	\$51	N/A			N/A	N/A	\$	\$	N/A	\$
IRA and Retirement Plan Quickfinder Handbook	\$55	\$51	N/A			N/A	N/A	\$	\$	N/A	\$
Quickfinder Tax Tips Newsletter**	\$71	\$68	N/A			N/A	N/A	\$	\$	N/A	\$
<b>QUICKFINDER ORDER TOTALS</b>											
								\$	\$	\$	\$

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5	Calculate Quickfinder order total – Add amounts from steps 2, 3, and 4.	\$

Order Quantity	ORDER by 9/30/18 Save up to 25%*
1	5%
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6 – 10	-20%
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7	Grand total	\$ =

## New from Quickfinder: Tax Reform Essentials Library

Sorting through the implications of tax reform for your clients may seem like an uphill battle, but it doesn't have to be an insurmountable task if you have the right tools. The key tax reform resources for tax professionals in this library are the tools to save you time and your clients tax dollars now, in planning 2018 transactions, and throughout the next tax season when complying with the many changes first effective this year under the Tax Cuts and Jobs Act (TCJA). These Quickfinder Handbooks incorporate the TCJA changes into the timeless, concise and easy-to-use Quickfinder format that our customers have trusted since 1973. Learn more at [tax.tr.com/qfbundles](http://tax.tr.com/qfbundles)

\* Savings of up to 25% applies to new orders placed by September 30, 2018. Savings promotion excludes PPC, RIA, Checkpoint and Checkpoint Learning CPE and may not be combined with any other offers.