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DEAN DORTON ALLEN FORD, PLLC

NEWSLETTER

FALL 2018

Some Good News About the New Qualified Business Income Deduction

In our last newsletter, the Summer 2018 Edition, we introduced readers in an article titled "Basics of a New Deduction" to the qualified business income (QBI) deduction, a principal feature of the Tax Cuts and Jobs Act. The IRS now has issued proposed regulations interpreting many provisions of the statute.

You may remember the 20% QBI deduction is unavailable, if taxable income exceeds specified threshold amounts, for certain businesses (called "specified service businesses"). A type of business the statute lists as a specified service business is one in which the principal business asset is the reputation and skill of one or more employees or owners. A plain reading of this suggests that many, if not most, service businesses, along with some producers or sellers of property, would not qualify for the deduction. However, the good news is the proposed regulations have taken a very narrow view of what fits within the definition of a business in which the principal asset is the reputation and skill of one or more employees or owners. The businesses that may be disqualified from the deduction under this provision are limited to only:

- A business in which a person receives pay for endorsing products or services
- A business in which a person licenses or receives pay for the use of an individual's image, likeness, name, signature, voice, trademark, or any other symbols associated with the individual's identity
- Receiving pay for appearing at an event or on radio, TV, or another media format

So, it now seems that many businesses which tax professionals thought would not qualify instead will qualify for the QBI deduction.

Remember, type of business does not matter if income thresholds ($157,500 for individuals, trusts, and estates, and $315,000 for married individuals filing jointly) are not exceeded.

We welcome your questions about how the QBI deduction may impact you.

Doug Dean, *ddean@deandorton.com*

Inside

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If you're interested in receiving our quarterly newsletters digitally via email, please contact Carrie Asalon at **casalon@deandorton.com**.

Task Force to Study Kentucky's Tax Expenditures and Make Recommendations

Leaders of Kentucky's General Assembly formed a legislative task force to determine what tax exemptions or other "tax expenditures" the legislature should consider modifying or repealing in its 2019 Session. The Task Force began meeting in June and its report is due December 30, 2018.

What's a tax expenditure?
The Office of the State Budget Director estimates the Commonwealth's tax expenditures on a biennial basis. The Office describes a tax expenditure as "the estimated amount of revenue loss resulting from an exemption, exclusion, or deduction from the base of a tax, a credit against the tax, a deferral of a tax, or a preferential tax rate." Sales tax exemptions are the most commonly discussed tax expenditures.

What are the largest sales tax expenditures?
Six of the top 10 expenditures are sales tax exemptions. They are as follows:

Specific Expenditure	Tax Expenditure Amount
Prescription medicines, prosthetic devices, and physical aids	$612,000,000
Food items	$490,000,000
Nonprofit educational, qualified nonprofit organizations, charitable and religious institutions, historical sites	$423,000,000
Residential utilities	$300,000,000
State, cities, counties, and special districts	$265,000,000
Livestock, poultry, ratite birds, llama, alpaca, aquatic organisms, buffalo, cervids, embryos and semen, farm work stock and feed, seeds, and fertilizers	$170,000,000

These items make up over $2.2 billion of the estimated $3.3 billion in sales tax expenditures. While it is easy to talk about tax exemptions and a need to repeal them, the conversation gets much more difficult when the actual items at issue are examined. It will be interesting to see what recommendations, if any, the Task Force makes.

Erica Horn, *ehorn@deandorton.com*

Firm Launches Wealth Management Services

To provide existing and future clients a broader array of services, Dean Dorton announces the launch of a wholly-owned subsidiary, Dean Dorton Wealth Management, LLC. As an independent registered investment advisor, Dean Dorton Wealth Management offers retirement planning, investment consulting, portfolio management, and a host of other holistic financial planning services.

Dean Dorton Wealth Management is led by David Parks, who has a long history with Dean Dorton. As a CPA who also is accredited in business valuation, David has over 30 years of experience in providing tax, business valuation, and other consulting services to individuals and businesses. David Bundy, Dean Dorton CEO, also serves as a senior advisor in the wealth management practice. As a member of the BAM Alliance (a national network of independent wealth management firms), Dean Dorton Wealth Management has access to a vast array of resources and expertise to enable the firm to effectively and efficiently serve its clients.

Dean Dorton Wealth Management stands ready to help individuals, families, qualified retirement plans, trusts, foundations, endowments, and closely-held businesses manage their wealth.

Please contact David Parks (*dparks@deandortonwealth.com* or (859) 425-7782), or visit *deandortonwealth.com* for more information.

Social Security Status Update

We all likely have heard or read that Social Security will "go broke" sometime in the not-too-distant future absent changes to benefits, funding, or both. A recent Congressional Research Service (CRS) report provides us with a current projection of Social Security's financial situation.

Social Security includes the Old-Age and Survivors Trust Fund and the Disability Insurance Trust Fund. Social Security benefits are currently funded from three sources: current period payroll and self-employment taxes (87.7%), interest on U.S. Treasury obligations resulting from investment of accumulated system surpluses (8.5%), and income taxes on Social Security benefits (3.8%). The interest income portion has enabled the system's total revenue to fund benefits fully since 1982. However, starting this year, benefits are projected to exceed total revenue from all sources. When this happens, the investment of surplus funds is diminished, reducing future interest income.

Assuming no changes in laws governing revenues and benefits, the CRS projects full depletion of investment assets in 2034. Does this mean the system then will be "broke?" No, system revenues other than interest would continue. The CRS projects that revenue at that time would fund 79% of projected benefits.

So, assuming the CRS's projections turn out to be accurate, a 21% reduction of benefits in 2034 would retain the system's solvency for at least the short term.

What if, instead of a benefits reduction, a tax increase would be enacted in 2034? The projections show the tax rate would need to increase from the current 12.4% to 15.7% in 2034. Funding also could be enhanced by increasing the age for full retirement benefits (currently age 67) and by raising—or even eliminating—the cap on income subject to tax.

Of course, a combination of funding increases and benefit reductions also could put the Social Security system on sounder financial footing.

Your guess about whether Congress will act to deal with the expected underfunding problem before crisis time, when something simply must be done, is as good as ours. The need for a solution does not seem to be a current priority. The longer Congress waits to act, the more severe the changes will need to be.

Jon Tennent, *jtennent@deandorton.com*
Doug Dean, *ddean@deandorton.com*

Remote Retailers Beware! The Ramifications of the Supreme Court's Decision in *Wayfair*

The United States Supreme Court recently issued its opinion in *South Dakota v. Wayfair, Inc., et al*. While the decision's effect on internet retailers has dominated the headlines, *Wayfair* has implications for nearly every industry.

Pre-*Wayfair*, sellers without a "physical presence" in a state into which they are shipping products to purchasers could not be required to collect and remit that state's sales tax. The Court struck down this "physical presence" standard, holding that South Dakota's "economic nexus" statute was constitutionally sound. South Dakota's law requires sellers with 200 or more transactions or more than $100,000 in sales for delivery into South Dakota to collect and remit South Dakota's sales tax.

Wayfair paves the way for state "economic nexus" laws, which affect more than just internet retailers. These laws affect all sellers without a physical presence in a state ("remote sellers") that make sales into the state in excess of the state's sales threshold. In addition to South Dakota, over 20 other states have some type of "economic nexus" law in place. Many states also impose notice and reporting requirements, which require remote sellers that don't collect the state's sales tax to report to the state certain information on their customers. Often, these requirements are triggered at much lower thresholds, as low as $10,000 of sales into some states.

States are rapidly changing their laws. Businesses that make sales into other states without having a physical presence in those states need to acquaint themselves with the various states' sales tax laws applicable to remote sellers and develop systems to track number of sales transactions and dollar value of sales volume by state.

Our state and local tax personnel are able to assist businesses comply with the changing sales tax environment resulting from the *Wayfair* decision.

Maddie Schueler, *mschueler@deandorton.com*

Dean Dorton: Your Information Security Office

Many organizations struggle with hiring and retaining information security professionals. Offering a long-term career path for these individuals can be challenging. A recent report indicated there is a negative unemployment rate in the cybersecurity field.

Security compliance requirements are increasingly complex. Cyber threats continue to evolve, and many organizations are not well-prepared to handle sophisticated cyberattacks. Organizations that host or maintain valuable information, such as Personally Identifiable Information (PII) or Personal Health Information (PHI), often are specifically targeted by cyber criminals for financial gain. Considering the average cost of a data breach is $3.96 million[1], information security is a key business risk.

In response to the growing risk, our firm has added a dedicated team of cybersecurity professionals to assist our clients. As part of our new cybersecurity services, we have added a service called **Dean Dorton Information Security Office**. Our unique approach to cybersecurity challenges involves understanding your organization's specific information security needs through a **Security Program Maturity Review** and tailoring recommendations based on your organization's specific risk tolerance. This process will lead to a **Security Roadmap** developed in collaboration with your team and supported by best practices and industry specific experience.

Finally, the roadmap will lead to your ongoing **Program Management** plan. Dean Dorton's Information Security Office provides a team of experienced information security professionals who can augment your organization's information security team or take the lead in designing, implementing, and maintaining a strong information security program on your behalf.

Dean Dorton's Information Security Office also offers a variety of services to assist as little as organizations want or as much as they need to continuously strengthen their information security program.

Gui Cozzi, who has 20 years of experience working in cybersecurity, has joined Dean Dorton to lead the firm's cybersecurity group. Prior to joining Dean Dorton, he served in various information security leadership roles, including implementing the Security Risk Management program for one of the nation's largest health systems, leading teams of cybersecurity consultants, and serving as Chief Information Security Officer for organizations in various industries.

Visit *deandortoncyber.com* to learn more.

Jason Miller, *jmiller@ddaftech.com*

[1]Source: 2018 Cost of a Data Breach Study (IBM Security / Ponemon Institute)

New Rules for Auditing Partnership Tax Returns

Over time the IRS has struggled with how best to efficiently conduct audits of partnership income tax returns. Various approaches have been tried, and significant changes have now become effective. Even though the first partnership tax returns for which the new audit rules will apply will be for 2018 tax returns, not due to be filed until 2019, partnerships will need to deal with a couple of important matters before their 2018 returns are filed.

First, the appointment of a Partnership Representative, a new position, is required. The Partnership Representative will serve as the audit contact and will have the authority to bind the partnership and its partners to audit adjustments. Given the power the Partnership Representative will have under the new rules, careful attention needs to be given to whom the partnership designates. The partnership may want to include procedures or contractual limitations on the power of the Partnership Representative in its partnership or operating agreement.

Certain partnerships will be able to elect to "opt-out" of the new rules. A partnership will qualify for this election if the partnership has (1) 100 or fewer partners and (2) only partners who are individuals, corporations (including S corporations), and estates of deceased partners. Partnerships with trusts (even grantor trusts), other partnerships, or disregarded LLCs as partners will not qualify for this election. The opt-out election must be made annually on a timely filed tax return. For partnerships qualifying to opt-out, we believe that will be the preferred course of action in most cases.

A partnership is required to either disclose the Partnership Representative or make the opt-out election on its 2018 partnership tax return. We strongly encourage persons who manage tax partnerships to address the new rules with their tax professionals before the upcoming tax filing season.

Matthew Smith, *msmith@deandorton.com*

Firm News

INSIDE Public Accounting Top 200
Dean Dorton has once again been named a Top 200 firm, based on U.S. net revenue, by *INSIDE Public Accounting*. We were ranked #116, making this the third consecutive year of being listed among the largest accounting firms in the country.

IGNITE Leadership Conference
Earlier this summer, Dean Dorton hosted the IGNITE Leadership Conference, a two-day interactive program for today's college accounting students looking to become tomorrow's leaders. Twenty-five students from eight colleges in the region gathered in Lexington on July 19-20 to gain hands-on experience through case study simulations; learn CPA exam tips; get to know Dean Dorton, our services, and our industry expertise; and meet members of our team, ranging from interns to partners. For a full recap of this inaugural event, visit *deandorton.com/ignite*.

People News

We welcome the following new team members:

Gui Cozzi joined our Technology team in Lexington. He has held various technology and cybersecurity roles since 1999. Gui earned his Bachelor degree in Business Management and Master degree in Business Administration from Western Governors University in Salt Lake City, Utah.

Aaron Hubbs joined our Technology team in Lexington. Aaron earned his Bachelor degree in Network Security and Electronics from Eastern Kentucky University. While in school, he worked as a computer technician, and he has management experience in the fast food restaurant industry.

Katie Hunt joined our Marketing team in Lexington. Katie recently earned her Bachelor degree in Integrated Strategic Communication from the University of Kentucky. While in college, she had work experience with a student newspaper, a magazine, a nonprofit foundation, and a community services organization.

Austin McQueen joined our Technology team in Lexington. While in college, he gained technology work experience with the Owsley County School System and the Owsley County Public Library. Austin earned his Bachelor degree in Network Security and Electronics from Eastern Kentucky University.

Tabitha Schmaltz joined our Technology team and works from her home office in Arizona. She most recently worked as a Business Outsourcing and Strategy Manager for a large Western U.S. regional CPA firm. Tabitha earned her Bachelor degree in Business Administration from Arizona State University and her Master degree in Accounting from Grand Canyon University in Phoenix, Arizona.

Maddie Schueler joined our Tax team in Louisville. Maddie recently earned her Master of Laws in Taxation from Georgetown University in Washington, D.C. She earned her Juris Doctor from the University of Louisville and her Bachelor degree from the University of Missouri. She has four years of experience working with the law firm Stoll Keenon Ogden in its Lexington office.

Corey Shell rejoined our Technology team in Lexington. He has nine years of technology-related work experience. Corey earned his Bachelor degree in Business Information Systems from Indiana Wesleyan University and his Master degree in Information Security and Assurance from Western Governors University in Salt Lake City, Utah.

Jacob Singleton joined our Technology team in Lexington. He has served as a computer support specialist, computer technician, and help desk coordinator since 2011. Jacob holds a Bachelor degree in Business and Technology from Eastern Kentucky University.

Alyssa Yozwiak, a CPA, joined our Tax team in Lexington. She has nine years of tax experience. Alyssa earned her Bachelor degree in Accounting from Miami University in Oxford, Ohio and her Master degree in Accounting from John Carroll University in University Heights, Ohio.

Michael Dilly, **Matthew Schwartz**, and **Chee Yin** are beginning their careers with our firm. Michael earned his Bachelor degree in Business Administration and Master degree in Accounting from the University of Kentucky. Matthew earned his Bachelor degrees in Business Administration and Accounting and Management Information Systems from Berea College. Chee Yin received her Bachelor degree in Biochemistry from Nanjing University, Master degree in Chemistry from Clarkson University, and Master degree in Accounting from the University of Kentucky.

Interns rejoining us are **Brooklin Hinz** and **Mary Maze**, University of Kentucky students.

We recognize the following activities and accomplishments of our team members:

Emily Anderson, **Joey George**, **Tori Lindon**, and **Dome Vongvises** successfully completed the CPA exam. Congratulations to each of them.

Danielle Langdon of our Healthcare Consulting team earned her Certified Documentation Expert Outpatient credential, which validates her expertise in reviewing healthcare outpatient documentation for accuracy to support coding, quality measures, and clinical requirements.

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People News (continued)

Daniel Paz of our Technology team earned his VMware Certified Professional 6.5 certification, which validates that he has the skills required to successfully install, deploy, scale, and manage VMware vSphere 6.5 environments.

Jay Swacker of our Healthcare Consulting team received his certification in Healthcare Compliance.

Christie Atzinger of our Healthcare Consulting team earned her Certified Professional Coder (CPC) designation from the American Academy of Professional Coders.

Lance Mann was selected for Louisville Business First's Forty Under 40 program, which honors Louisville-area professionals who are making an impact on their workplace and community.

Elizabeth Leatherman was elected as Treasurer of the Bluegrass Estate Planning Council.

Natalie Schuler was elected to the Bluegrass Estate Planning Council's board of directors.

Erica Horn and **Mike Harbold** spoke at the Kentucky Chamber of Commerce's Navigating Sales and Use Tax in Kentucky seminar.

Jason Miller and **Brittany Neaves** presented at the Institute for Higher Education Compliance at Thomas More College.

Kevin Cornwell presented on cybersecurity at the KyCPA Next 2018 Manufacturing Conference. He also presented on information technology policies and cybersecurity at Information Technology Mangers Association TechCon, and presented on ransomware at the Hospitality Financial and Technical Professionals annual convention.

Erica Horn moderated the Greater Louisville Inc. Issues & Influencers Conference; presented on tax reform at the Kentucky Chamber of Commerce's Sales & Use Tax Conference; led Dean Dorton's webinar for higher education institutions on changes to Kentucky's sales and use taxes; presented on nonprofits and sales taxes at a Kentucky Nonprofit Network webinar; and presented on Kentucky sales tax changes at multiple chambers of commerce, Kentucky Occupational License Fee Administrators, and Women's Accounting and Finance Alliance.

Erica Horn and **Jen Shah** presented on federal and state tax reform at a Commerce Lexington seminar.

Jen Shah presented on federal and state tax reform updates for horse and farm owners in Saratoga Springs, New York.

Shawn Stevison presented at the Healthcare Financial Management Association 2018 Conference, and she presented on the Office of Inspector General Work Plan Update at the Association of Healthcare Internal Auditors (AHIA) Annual Conference in San Diego.

Megan Crane was selected to join the Leadership Lexington class of 2018-2019.

Elizabeth Woodward is teaching the 2018 Annual Professional Ethics Update throughout the state for the Kentucky Society of CPAs. At the recent KyCPA Forensic Accounting, Business Valuation, and Litigation Conference, Elizabeth presented on professional ethics and on expert witness testimony.