

SUMMER 2019

Opportunity Zones: Tax Deferral and Savings Potential

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Investors and others who realize significant capital gains may benefit from the Opportunity Zone program created by the Tax Cuts and Jobs Act at the end of 2017. The program provides favorable tax treatment for certain investments in "Opportunity Zones," economically-distressed communities across the country. Opportunity Zones, nominated by state governors and certified by the U.S. Department of Treasury, cover portions of all fifty states, the District of Columbia, and five U.S. territories. Kentucky has 144 Opportunity Zones located in 84 counties.

How does the Opportunity Zone program work? A taxpayer who has realized a capital gain, such as gain from the sale of stock or land, can defer tax on that gain through the end of 2026 if the gain (not the proceeds) is invested in a "Qualified Opportunity Fund" (QOF) within 180 days of realization. A QOF is a partnership or a corporation created for investing in eligible property located in one or more Opportunity Zones. A QOF must hold at least 90% of its assets in a qualified Opportunity Zone business or property. To become a QOF, an eligible partnership or corporation self-certifies by filing Form 8996 with its federal income tax return.

Taxpayers who invest capital gains in a QOF elect to defer recognizing the gain on the tax return on which the gain would have been recognized had the investment in the QOF not been made. The deferred gain must be recognized on the earlier of the date on which the QOF investment is sold or December 31, 2026. Investments held for a required period of time qualify for additional tax benefits. If the investment in the QOF is held by the taxpayer for at least five years (meaning the gain must be invested by the end of 2021), the basis of the investment is increased by 10% of the deferred gain, resulting in a 10% reduction in the gain that will be recognized not later than the end of 2026. If the investment is held more than seven years (meaning the gain must be invested by the end of 2019), the basis of the investment is increased by an additional 5% of the deferred gain, resulting in an overall 15% reduction of the deferred gain.

Further, in addition to the deferral and potential reduction in the original gain invested in a QOF, a taxpayer can permanently exclude the gain on the QOF investment if the investment is held for at least ten years. Thus, if a taxpayer originally invested \$100 of capital gain in a QOF, held that investment for at least ten years, and then sold the investment for \$150, the taxpayer could also exclude the \$50 gain on the QOF investment from tax.

This article highlights basic features of the Opportunity Zone program. Although the potential benefits of an Opportunity Zone investment may seem somewhat straightforward, the underlying requirements are quite complex. For more information, please contact your Dean Dorton tax advisor.

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Notable 2019 Changes to Kentucky's Tax Law

The General Assembly made changes to Kentucky's tax law during its 2019 session, albeit not the type of wholesale changes made in 2018. The most significant sales tax changes and several income tax changes are described below.

Sales Tax

Between legislative sessions, three main problems were identified as a result of sales tax changes made in 2018. Recall that legislators imposed, for the first time, sales tax on eleven services: landscaping, janitorial, small animal veterinarian, pet care, industrial laundry, non-coin-operated laundry and dry cleaning, linen supply, indoor skin tanning, non-medical diet and weight reducing, limousine services (if a driver is provided), and extended warranties. During the 2019 session, changes were enacted to address the problems identified.

Problem 1 – de minimis receipts: The new sales tax on services applied to all sales, even if total sales were insignificant. This meant if Tommy the Teenager mowed lawns during the summer, Tommy was expected to collect and remit on the first dollar paid to him, even if his total receipts from lawn mowing totaled a small amount.

Solution – \$6,000 threshold: Retroactive to January 1, 2018, gross receipts less than \$6,000 during a calendar year from sales of taxable services are exempt from sales tax. All gross receipts over \$6,000 are taxable and will be taxable in subsequent years.

Problem 2 – double taxation: Some service providers, for example, landscapers and janitorial businesses, were not permitted to provide companies who did subcontracting work for them with a resale certificate. As a result, sales tax had to be charged twice: once by the subcontractor and once by the business providing the services to the end user. This is not good tax policy.

Solution – resale certificates permitted: Beginning July 1, 2019, service providers may issue a resale certificate if they purchase a service they subsequently resell. An example involves a janitorial service that subcontracts with a window washing company. Beginning July 1, the janitorial service will provide a resale certificate to the window washing company, and the window washing company will not have to charge sales tax on its services to the janitorial service. While the janitorial service will still have to charge its customer sales tax, now sales tax is only being charged once.

Problem 3 – sales tax on nonprofits: The expansion of the law required nonprofit organizations to collect sales tax on admission tickets and fundraising sales.

Solution – exempt from tax nonprofit admissions and most fundraising: Effective March 26, 2019, admissions sold by nonprofit organizations and the vast majority of fundraising event sales are exempt from sales tax. Additional information regarding the impact of these changes on nonprofit organizations is available on our website.

Three additional changes include: no sales tax on veterinarian services for "poultry;" narrowing the definition of "admission" to exclude fishing tournaments, fees paid for boat slips, and unarmed combat shows; and requiring marketplace providers (Amazon, for example) to collect and remit sales tax on behalf of vendors selling from their platforms.

Income Tax

The General Assembly also made several income tax changes with varying levels of impact. The following four changes have broad applicability: (1) increasing from \$25,000 to \$100,000 Kentucky's version of the Internal Revenue Code's Section 179 expense, which allows immediate expensing of capital purchases (effective for purchases made on or after January 1, 2020); (2) allowing a deduction for investment interest expense; (3) allowing a deduction for wagering losses; and (4) conforming Kentucky's estimated tax filing rules to those of the IRS. Now, taxpayers will have only one set of rules for both federal and state estimated income tax payments. With the exception of the changes to the expensing deduction for capital purchases, the changes are effective for tax years beginning on or after January 1, 2019. Additionally, for those sections of the Internal Revenue Code to which Kentucky conforms, the state will now conform to the Code as of December 31, 2018. Other changes made relate to the filing methodology for C corporations and taxation of financial institutions and savings and loan associations.

Since the 2019 Session adjourned, there has not been any chatter about more changes in 2020, but one never knows. We welcome your questions about these changes.

Erica Horn, ehorn@deandorton.com

The Future Home of Accounting: The Cloud

Dean Dorton's Accounting and Financial Outsourcing team (AFO) leverages cloud technology to provide accounting solutions to our clients. We utilize various software applications that work in harmony to give our clients the data they need to operate their businesses. Our cloud-based approach allows us to offer a broader array of solutions that many businesses would not be able to access otherwise.

The term "cloud" often has a negative connotation. Sometimes it means a storm is coming. Our parents, teachers, or even employers may have said to us "get your head out of the clouds." On the other hand, we now can associate "cloud" with "access," a more positive connotation. Cloud-based services provide online access to resources that are managed by a third party rather than by the user. Consider cloud-based storage, which is access to remote digital storage, or cloud computing, which is access to remote computing resources.

Outsourced cloud services allow user access anywhere an internet connection exists. These services allow users to avoid significant capital investment, lengthy implementations, and long-term contracts often found in traditional applications. A worldwide survey conducted by Deloitte in 2018 found that 93% of organizations are considering or are already using outsourced cloud services.

You may be using a cloud-based outsourced service and not realize it. Cloud technology has created a landscape in which almost anything can be a service. Examples include software as a service (Google Apps), transportation as a service (Uber), entertainment as a service (Netflix), and now accounting as a service (Dean Dorton AFO).

So what would an outsourced cloud-based accounting solution look like? Dean Dorton AFO utilizes Sage Intacct as the hub of the cloud accounting solution. With Sage Intacct as the general ledger, we find cloud-based tools that streamline and

automate the accounting needs of our clients in a synchronized manner. We call this combination of tools a "tech stack." A typical tech stack for an AFO client includes:

- Sage Intacct – general ledger, invoicing, and financial reporting tool
- A bill pay service to automate the collection of invoices, accounts payable management, and recording of expenses
- A tool to reconcile corporate credit cards
- A payroll provider
- A tool to facilitate employee expense reimbursement

The AFO team works with our clients to develop a workflow for each step within the accounting process. We facilitate strong internal controls, eliminate or reduce risks associated with employee turnover, ensure software is up-to-date, and manage security over accounting data. Additionally, when partnered with AFO services, tax professionals can provide tax planning opportunities throughout the year.

Decision makers and advisors have access to dashboards, key performance indicators, and customized reports within Sage Intacct, all of which can be accessed through a PC, smartphone, or tablet. Decision makers have the ability to drill into a financial dashboard or report to gain insight at the transaction level. This puts instant decision-making power into the hands of management 365 days a year without having an accountant on the payroll.

If you would like to consider the benefits and costs of a cloud-based accounting and financial management system for your organization, please email or call me, as the head of our AFO services team, or contact your Dean Dorton service provider, who can connect us.

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Recent Firm Accolades

Dean Dorton Among Top Firms to Watch

We were recently listed as a Top Firm in the Southeast by Accounting Today, a national publication.

Kentucky's Best Bets

Business growth throughout Kentucky is critical to the continued expansion of Kentucky's economy and vital to job creation throughout the Commonwealth. In conjunction with The Lane Report, Dean Dorton recognized the distinct and esteemed companies that are impacting Kentucky's economic development through Best Bets 2018. The Best Bets list of eight winning companies was based on several metrics, including, but not limited to, revenues over the last three years, employee investment, and reinvestment in the company. The list of winners can be found at www.kybestbets.com/best-bets-winners.

Just the Facts, Ma'am

Some readers may remember the old television series "Dragnet," the main character in which was Sergeant Joe Friday. Every episode it seemed that Sgt. Friday, when interviewing a talkative lady about a crime, would interrupt and say "just the facts, ma'am."

We recently reviewed a publication, "USAFacts 2018 Annual Report: Our Nation, in Numbers," published by USAFacts Institute, founded in 2017 by Steve Ballmer, former CEO of Microsoft. The organization's mission is "to provide Americans with a portrait of the US population, government finances, and the outcomes of government activities." The report's data comes solely from official government sources, presented, the organization asserts, with no partisan agenda or commercial motive. You can find the report at USAFacts.org.

In today's political climate, it may seem to be very hard and frequently frustrating to find data presented objectively and without suspicion that it is distorted for political purposes. If, indeed, the data in USAFacts 2018 Annual Report can be trusted to be what the organization claims it to be, it will be welcomed by those who seek reliable information, "just the facts."

We cannot begin to summarize the full report, but will share some of the information presented.

Population

The report's headline under the topic of population is: "We're getting more diverse, older, and more educated." From 1980 to 2016 the Hispanic population in the U.S. has gone from 6.4% to 17.8% of our population. White, non-Hispanic has decreased from 80% to 61.3% over the same period.

The median age of our population increased to 37.9 from 30 over that period. Those age 65 and over increased from 11.3% to 15.2% of our total population, while those under age 18 decreased to 22.8% from 28.1% of our population. The multiple of this latter group (under 18) to the former (65 and over) declined from 2.5 to 1.5.

Adults age 25 and over who have at least some college experience increased to 60% in 2016 from 46% in 1990, and individuals who did not finish high school decreased from 25% in 1990 to 12% in 2016. [Author's comment: While the report shows we are becoming more educated, many of us may question whether we are becoming better educated.]

Government Revenue

Total government (federal, state, and local) revenue for 2015 (the last year for which complete information was available when data for the report was compiled) was \$5.2 trillion. The largest component was individual income tax at 37%, followed by payroll-related taxes (Social Security, Medicare, and unemployment insurance) at 21%. Other taxes which were significant components of the total include property taxes (9%), corporate income taxes (8%), sales taxes (7%), and excise taxes (5%, including taxes on specific items such as gasoline and tobacco). Note that corporate income tax is not synonymous with business income tax, as income tax on most closely-held businesses is paid at the owner rather than at the entity level. Thus, individual income tax is paid on some business, as well as other forms, of income.

Government Spending

Total government spending (again including federal, state, and local) for 2015 was \$5.7 trillion. USAFacts breaks spending down into the four missions laid out in the Preamble to the U.S. Constitution (and listed below along with each category's percentage of the total):

- Establish justice and ensure domestic tranquility (encompassing physical safety, protection from business or financial crime, and child social services) 7%
- Provide for common defense (encompassing national defense and veterans affairs, foreign affairs and aid, and immigration and border security) 14%
- Promote general welfare (encompassing investments in infrastructure, research and development, transfers to citizens, and government-run businesses, such as the post office and airports) 23%
- Secure the blessings of liberty to ourselves and our posterity (encompassing education, Social Security, Medicare, debt service, and promotion of agriculture and energy) 53%

In case you are "auditing" our math, the other 3% is for general government administration. Spending on Social Security and Medicare made up 25% of total government spending.

The report contains a wealth of other information as it goes deeper into data that can be useful in gaining a better understanding of changes in our domestic society and finances.

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Have You Heard About the Endow Kentucky Tax Credit?

The Endow Kentucky Tax Credit Program offers individuals and businesses an opportunity to receive a state tax credit against Kentucky income tax after making a contribution to permanent endowment funds at qualified community foundations. The state makes total credits of \$1,000,000 available to taxpayers on **July 1** each year. Taxpayers are eligible to receive up to a 20% income tax credit (not to exceed \$10,000) per year. A tax credit, as opposed to a deduction, lowers your tax bill dollar-for-dollar regardless of your tax bracket. Any amount of credit that a taxpayer is not able to use during a particular year can be carried forward up to five years for use in a subsequent year.

If tax credit applications result in an oversubscription, the credit grants are scaled down pro rata. After the donor receives notice of the tax credit amount granted, the donor has a specified time period within which to fund the endowment.

Submitting the application and being awarded a credit does not obligate one to fund the endowment. Of course, without funding no credit is allowable.

Your local community foundation likely has a list of a number of endowments already established for the benefit of specified charitable organizations, or you can work with the foundation to add your favorite charity or charities to the list.

Taxpayers must complete and submit an application for the credit to the Department of Revenue to obtain preliminary authorization for the credit. With the July 1 deadline approaching, the time is now to contact us or your local community foundation to learn more about the credit and the application process.

Erica Horn, ehorn@deandorton.com

People News

We welcome the following new team members:

Kim Arthur joined our Administrative team in Louisville as a front desk coordinator. She has 14 years of customer service experience. Kim studied Business Administration at Jefferson Community College and Indiana Wesleyan College.

Adam Carby joined our Technology team in Lexington, after gaining eight years of IT experience. Adam earned his Associates degree in System, Networking, and LAN/WAN Management from the University of Phoenix.

Michael Gilliam joined our Technology team in Lexington. He has 12 years of cybersecurity experience, split between security operations and conducting technical security assessments and penetration tests. Michael earned his Bachelor degree in Telecommunications Systems – Management Network Security from Murray State University.

Phil Hardin joined our Accounting & Financial Outsourcing team in Louisville. He is starting his accounting career with us, after earning his Bachelor degree in Finance and Accounting from the University of Kentucky.

Tina Hart joined our internal accounting team in Lexington as a billing specialist. She has had diverse work experience, including the last nine years in accounting and clerical roles. Tina earned her Bachelor degree in Psychology from Eastern Kentucky University.

Cody Higdon joined our Technology team in Louisville. He held various technology roles while completing his Bachelor degree in Computer Information Systems from the University of Louisville.

Claudia Gonzalez joined our Office Services team full-time in Lexington, after being with the firm on a temporary basis during tax busy season. She earned her Bachelor degree in Broadcast Journalism from the University of Kentucky.

Amy Justice joined our Technology team in Lexington. She has 10 years of IT experience, most recently serving as an IT auditor and security consultant. Amy earned her Bachelor degree in Assets Protection: Computer Information Securities from Eastern Kentucky University.

Jamie Lee, a CPA, rejoined us in our Accounting & Financial Outsourcing team in Lexington, after spending three years in a corporate financial management and accounting role. Jamie was with Dean Dorton for nearly five years previously. She earned her Bachelor degree in International Business Administration from Ewha Womans University in Seoul, South Korea, and Master degrees in Accounting and Taxation from State University of New York.

Tom Major, a CPA, joined our Technology team and works from his home office in Arkansas. He has more than 30 years of experience in various accounting and technology roles, including as the owner of his own software implementation firm and serving as Chief Financial Officer at a technology company in Little Rock. Tom earned his Bachelor degree in Business and Economics, with an Accounting minor, from Hendrix College in Conway, Arkansas.

Jake McLees joined our Office Services team full-time in Lexington, after assisting the firm during tax busy season. Jake earned his Bachelor degree in English from the University of Kentucky.

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People News (continued)

Jodie Muller joined our Accounting and Financial Outsourcing team in Lexington. She is starting her accounting career with us, after earning her Associates degree in Business Administration from Midway College and her Bachelor degree in Public Accounting from Eastern Kentucky University.

Hannah Reed joined our Accounting and Financial Outsourcing team in Lexington. Hannah has over two years of accounting experience, most recently serving as an accounting clerk for a skilled nursing center. Hannah earned her Bachelor degree in Financial Management from Western Kentucky University, and she is pursuing a Master degree in Organizational Communication from Murray State University.

Candice Shaw joined our Healthcare Solutions team in Louisville, after gaining over 10 years of medical office work experience. Candice earned her Associate degree in Health Information Technology from the National College of Business and Technology.

Shyla Thomas joined our Office Services team in Louisville. She has 12 years of experience serving as an Executive Assistant.

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

Jim Stubanas and **Ian D'Amelio** achieved Sage Intacct's Certified Implementation Specialist designation.

Jim Major, **Ian D'Amelio**, and **Jim Stubanas** successfully passed the Sage Intacct Implementation Consultant's exam.

Jason Whitaker completed the Aruba Networks ACCP ClearPass Professional technical certification.

Elizabeth Woodward is serving as President of the KyCPA, the statewide society for CPAs in Kentucky.

Cameron Sallee joined the Arbor Youth Services Board of Directors.

Jen Shah hosted a webinar with the National Thoroughbred Racing Association (NTRA), focusing on key federal tax reform items for horse and farm owners.

Erica Horn participated on a panel about careers in tax for the University of Kentucky Tax Law Society and presented on "What Business Lawyers Need to Know About the New Kentucky Tax Laws" at the Business Associations Law Institute.

Kevin Cornwell, Gui Cozzi, Megan Crane, Erica Horn, Simon Keemer, Jason Miller, David Parks, David Richard, and **Maddie Schueler** presented at Dean Dorton's annual Higher Education Training Day.

Jim Norton was a lead in a regional theater musical production in Raleigh, North Carolina.

Ryan Walker presented on "Transformative Technology" at the Institute of Management Accountants (IMA) Louisville Chapter's Spring 2019 Conference.

Ryan Walker and **Simon Keemer** conducted Dean Dorton's Revenue Recognition Roundtable for accounting and financial professionals in Lexington.