Lally&Co.
CPAs and Business Advisors

The Evergreen

Quarterly Journal for Clients & Friends

Spring 2016 – Volume XVIII

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The Evergreen. Always Growing.

Like the evergreen oak tree, Lally & Co. is always growing. With the support and loyalty of our clients and friends we have grown into a firm of 40 individuals serving clients in many diverse fields. Our growth gives us the ability to better serve our clients and provide effective solutions to their needs. If you have questions about your business or personal tax situation, please contact us. We welcome your call and are always looking for ways to better serve you.

Contact our office or visit our website for more information.

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Dear Clients and Friends,

Spring has arrived and with that came the end of another "busy" season. We would like to extend our sincere gratitude for the trust you have invested in us. Our clients and referral sources are the reason we had one of our busiest and most successful tax seasons. It would not have happened without each of you.

As you read through *The Evergreen*, please do not hesitate to contact us if you have questions regarding an article or regarding your business or personal tax situation. We would be happy to hear from you! This and past issues of *The Evergreen* are available on our website at http://lallycpas.com/newsletters/.

Congress Takes First Steps to Tax Reform

Tax reform continues to be highly touted in Congress as lawmakers from both parties call for simplification of countless complex rules, overhaul of tax rates, and more. At times this year, President Obama and Congressional Republicans seem far apart on a way forward, but at similar times in the past, agreements have quickly and often surprisingly emerged, most recently in the Protecting Americans from Tax Hikes Act of 2015 (PATH Act). As the November elections approach more closely every passing day, lawmakers from both parties and the President have a short window to agree on tax legislation. The weeks leading up to Congress' summer recess may be decisive.

PATH Act as path forward

The scope of the PATH Act surprised many Hill observers. Instead of merely extending the so-called tax extenders (including the state and local sales tax deduction, research tax credit, teachers' classroom expense deduction), Congress voted to make permanent many of the incentives. Although there had been hearings and discussions about permanently extending some of the incentives, the prospect of getting a bill through Congress and to the President's desk seemed remote right up to December. Behind the scenes negotiations between the White House and Congressional Republicans resulted in the largest tax bill since the American Tax Relief Act of 2012. The PATH Act went far beyond the extenders. It made changes to the rules for IRS administration, real estate investment trusts (REITs), how the Tax Court works, and more.

Passage of the PATH Act shows that another tax bill, possibly an even larger tax reform package, could make it out of Congress before year-end. Speaking in Washington, D.C. earlier this year, Senate Finance Committee (SFC) ranking member Ron Wyden, D-Oregon, suggested such an outcome. "Against all odds, Democrats and Republicans reached a bipartisan agreement on the PATH Act," Wyden said. "The December agreement leading to passage of the PATH Act worked out because of the

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Firm Announcements

Amanda R. Donolo joined our Administrative Staff in January 2016

Christian J. Crabtree became engaged to Joyce Tedrick in May 2016

Lindsey M. Burchell, CPA marries Markus Buchanan in May 2016

Important Dates

June 15, 2016 – 2016 2nd Quarter Estimated Payments Due

June 30, 2016 – Form 114, Report of Foreign Bank and Financial Accounts Due

approach members took to the negotiations." Wyden predicted that lawmakers would use the PATH Act as a "blueprint for broader reform."

Everything on the table

Almost everything in the Tax Code appears to be on the table at this time. House Ways and Means Chair Kevin Brady, R-Texas, who is a leading proponent of tax reform in the House, has said as much. "Not all deductions and exclusions will stay; not all will go. The question to ask is: how will these policies drive economic growth?" Among the provisions/ideas being discussed by legislators are:

- Consolidation of the individual income tax rates
- Enhancing incentives for lower and middle income taxpayers
- Revising/repealing some of the tax measures under the Affordable Care Act
- Lowering the U.S. corporate tax rate
- Consolidating education tax incentives
- Eliminating/consolidating some energy tax breaks
- Repealing the alternative minimum tax (AMT)
- Tweaking the child tax credit, earned income tax credit, child and dependent care credit

International tax reform

Reforming the rules for international taxation, such as the complex rules for corporate inversions, transfer pricing, and more, has been of special interest this year to the House Ways and Means Committee. One unanswered question is whether international tax reform can move forward by itself or if proponents need to add "sweeteners" such as expanded tax breaks for lower and middle income taxpayers to win support in Congress. Some lawmakers want to link international tax reform to a cut in the U.S. corporate tax rate. How to pay for any rate cuts also is generating questions and few answers. President Obama has proposed to tighten the international tax rules and use the expected revenue to pay for infrastructure projects, along with reducing the corporate tax rate.

Energy tax measures

Before Congress' summer recess, a package of energy tax breaks could be approved by the House and Senate. Many of these are temporary incentives that were not included in the PATH Act, such as the special credits for fuel cell vehicles. There appears to be bipartisan support to make permanent some, if not all, of these tax breaks. SFC ranking member Wyden is spearheading the movement to win passage of these energy tax incentives, seeking to attach them to a bipartisan aviation bill.

FBAR, Form 8938 Filings Increase as Taxpayers Become More Aware of Reporting Requirements

Six years ago, Congress passed the Foreign Account Tax Compliance Act (FATCA), which set in motion a wave of new reporting and disclosure requirements by individuals, foreign financial institutions, and others. In response, the IRS created a host of new rules and regulations; and new forms for these reporting requirements. One key FATCA form – Form 8938, Statement of Specified Foreign Financial Assets – has seen usage steadily increase since passage of FATCA, the IRS recently reported. At the same time, more individuals are filing a related form – FinCEN Form 114, Report of Foreign Bank and Financial Accounts (known as the

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FBAR), which reached a record high in 2015.

Two key forms

FATCA generally requires U.S. citizens, resident aliens and certain non-resident aliens to report specified foreign financial assets on Form 8938 if the aggregate value of those assets exceeds certain thresholds. Examples of financial accounts include: savings, deposit, checking, and brokerage accounts held with a bank or broker-dealer. And, to the extent held for investment and not held in a financial account, individuals must report stock or securities issued by someone who is not a U.S. person, any other interest in a foreign entity, and any financial instrument or contract held for investment with an issuer or counterpart that is not a U.S. person. Examples of these assets that must be reported if not held in an account include (but are not limited to) stock or securities issued by a foreign corporation; a note, bond or debenture issued by a foreign person; a partnership interest in a foreign partnership; and any interest in a foreign-issued insurance contract or annuity with a cash-surrender value. Reporting thresholds vary based on whether a taxpayer files a joint income tax return or lives abroad.

Individuals with an interest in, or signature or other authority over foreign financial accounts whose aggregate value exceeded $10,000 have a separate reporting requirement. This requirement is satisfied by filing the FBAR. The FBAR is filed through the BSA E-Filing System (with Treasury's Financial Crimes Enforcement Network (FinCEN).

Note that the Treasury's Financial Crimes Enforcement Network (FinCEN) has proposed revisions to the rules for filing FBARs. The revisions generally would apply to financial professionals who file FBARs due to their employment responsibilities.

Increase in filings

According to the IRS, taxpayers filed more than 300,000 Forms 8938 with their returns in tax year (TY) 2014. The number of filings was approximately the same as in 2014 but up from 200,000 filing for TY 2011, which was the first year for filing Form 8938. Form 8938 is filed with the taxpayer's annual return.

FinCEN received 1,163,229 FBARs in 2015, representing an eight percent increase compared to 2014. During the past five years, the number of FBAR filings has increased on average by 17 percent each year, the IRS reported.

IRS investigations

Since passage of FATCA, the IRS has stepped up investigations into reports of undisclosed foreign accounts. The IRS often uses its summons authority to discover foreign accounts and the federal courts have upheld the agency's authority when challenged by taxpayers.

On February 29, 2016, the First Circuit Court of Appeals found that foreign bank account records fell within the required records exception to the Fifth Amendment. The First Circuit joined seven other circuits in holding that the required records exception applies.

The Court found that the Bank Secrecy Act requires individuals engaged in foreign banking to file reports and maintain certain records. These records must be retained for a certain time and must be available for inspection. The required records doctrine prevents individuals, who possess records the government requires to be maintained as a result of voluntary participation in certain regulated activities, from asserting their Fifth Amendment privilege.

What is the Roth IRA Contribution Limit for 2016?

Individuals may contribute up to $5,500 to a Traditional or a Roth IRA for 2016. This is the same limit as 2015. An individual age 50 and older can make a catch-up contribution of an additional $1,000 for the year. The contribution is limited to the taxpayer's taxable compensation for the year, minus contributions to all non-Roth IRAs.

Taxpayers can contribute to a Roth IRA as long as the taxpayer's adjusted gross income for the year is less than:

- $193,000 for married filing jointly or qualifying widow(er),
- $131,000 for single, head of household, or married filing separately and you did not live with your spouse at any time during the year, and
- $10,000 for married filing separately and you lived with your spouse at any time during the year.

Unlike Traditional IRAs, the owner of a Roth IRA can make contributions to the IRA after turning age 70 ½ and does not have to begin taking contributions at that age. The mandatory distribution rules for Traditional IRAs that normally begin at age 70 ½ do not apply until the owner dies.

Although contributions to a Roth IRA are not deductible, income accumulates tax-free and "qualified" distributions will also be tax-free, if certain conditions are satisfied:

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- The distribution must be made after the owner turns 59 ½, unless the owner is disabled or the payment is made to a beneficiary after the owner's death; and
- The amount contributed must be held in the Roth IRA for at least five years.

Taxpayers can also roll over benefits from an eligible retirement plan to a Roth IRA, without the rollover being counted against the annual contribution limit, provided the payment from the retirement plan is an eligible rollover distribution. The retirement plan can be a qualified plan, 401(k) plan, tax-sheltered annuity, or governmental deferred contribution plan. The payment will still be taxable, since contributions to a Roth IRA are not deductible and must be made with after-tax dollars.

Filing Season Closes; Cybersecurity and Customer Service Top Priorities for IRS

The 2016 filing season has closed with renewed emphasis on cybersecurity, tax-related identity theft and customer service. Despite nearly constant attack by cybercriminals, the IRS reported that taxpayer information remains secure. The agency also continued to intercept thousands of bogus returns and prevent the issuance of fraudulent refunds.

Cybersecurity

Concerns about cybersecurity and the confidentiality of taxpayer information were paramount during the filing season. According to the IRS, its basic systems are attacked "millions of times" every day by cybercriminals looking for weaknesses. In April, IRS Commissioner John Koskinen told Congress that the agency's basic systems are secure. However, cybercriminals did breach its Get Transcript app in 2015 and other applications are under constant probing and attack by cybercriminals.

Koskinen assured Congress that the agency is beefing up its cybersecurity staffing. The IRS has hired 55 new cybersecurity experts. However, he acknowledged that the agency's cybersecurity head has left and the position is open. This has drawn criticism from lawmakers who have questioned why such an important job is open. Koskinen said that the lengthy government hiring process is a deterrent to hiring cybersecurity professionals and urged Congress to reinstate the agency's fast-track hiring process.

Identity theft

Closely related to cybersecurity is tax-related identity theft. The breach of the Get Transcript app in 2015 resulted in $50 million in fraudulent refunds paid to cybercriminals, according to a government watchdog.

Because the filing season has just ended, final statistics will not be released until later this year. However, interim statistics give a snapshot of the vastness of the problem of tax-related identity theft. As of March 5, 2016, the IRS had successfully prevented the issuance of some $180 million in fraudulent refunds.

To help prevent tax-related identity theft, the IRS has enhanced its return processing filters. Many of these enhancements, the IRS has explained, are invisible to taxpayers. Other enhancements have been made working with return preparers and tax software providers.

Customer service

The IRS's level of customer service hit historic lows during the 2015 filing season. Almost two-thirds of all calls to the IRS went unanswered and the agency disconnected millions of callers (so-called "courtesy disconnects.") There were also long lines for in-person assistance at IRS service centers nationwide. The IRS blamed the poor customer service on budget cuts and its inability to hire more employees to answer taxpayer questions.

In December 2015, Congress gave the IRS an additional $290 million and instructed the agency to use the money to improve customer service, along with boosting cybersecurity and combating identity theft. Koskinen told Congress in April that the agency spent more than $100 million of the $290 million on customer service. As a result, the agency's level of customer service reached as high as 65 percent during the filing season. However, that level will fall to around 50 percent for all of 2016, Koskinen said. The additional employees hired during the filing season were merely temporary employees and their employment ended with the close of the filing season, Koskinen explained.

Return processing

The IRS expects to receive some 150.6 million returns this filing season. That number includes an estimated 13.5 million returns on extension. Taxpayers on extension have until October 17, 2016 to file.

Don't Overlook New-For-2016 Enhancements to Certain Tax Incentives

Passage of the "Tax Extenders" undeniably provided one of the major headlines – and tax benefits – to come out of the Protecting Americans from Tax Hikes Act of 2015 (PATH Act), signed into law on December 18, 2015. Although these tax extenders

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(over 50 of them in all) were largely made retroactive to January 1, 2015, valuable enhancements to some of these tax benefits were not made retroactive. Rather, these enhancements were made effective only starting January 1, 2016. As a result, individuals and businesses alike should treat these enhancements as brand-new tax breaks, taking a close look at whether one or several of them may apply. Here's a list to consider as 2016 tax planning gets underway now that tax filing-season has ended:

Section 179 expensing. The PATH Act permanently extended the Code Section 179 dollar of investment limitations at the higher $500,000 and $2 million, levels, which are adjusted for inflation for tax years beginning after 2015 (it is $500,000 and $2,010,000 for 2016). In addition, starting only in 2016, the $250,000 limitation on the amount of section 179 property that can be attributable to qualified real property has been eliminated. Further, for tax years beginning after 2015, the Code Section 179 expense deduction is now allowed for air conditioning and heating units.

Bonus depreciation. In addition to the big news that the PATH Act extended Code Section 168(k) bonus depreciation to apply to most qualifying property placed in service before January 1, 2020, it made a number of modifications, including:

- replacement of the bonus allowance for qualified leasehold improvement property with a bonus allowance for additions and improvements to the interior of any nonresidential real property, effective for property placed in service after 2015; and
- allowance to farmers of a 50 percent deduction in place of bonus depreciation on certain trees, vines, and plants in the year of planting or grafting rather than the placed-in-service year, effective for planting and grafting after 2015.

Section 181 expensing. Special Section 181 expensing for qualified film and television productions is extended for two years to apply to qualified film and television productions commencing before January 1, 2017. However, the expensing rule is also expanded to apply to qualified live theatrical productions commencing after December 31, 2015.

WOTC. The Work Opportunity Tax Credit (WOTC) has been extended five years through December 31, 2019. In addition, the credit has been expanded and made available to employers who hire individuals who are qualified long-term unemployment recipients who begin work for the employer after December 31, 2015.

Research credit. The PATH Act permanently extended the research credit that applies to amounts paid or incurred after December 31, 2014. However, a new allowance of the research credit against alternative minimum tax liability applies to credits determined for tax years beginning after December 31, 2015. In addition, a new payroll tax credit associated with the research credit applies only to tax years beginning after December 31, 2015 (Act Sec. 121(d) (3) of the PATH Act).

Military differential pay. The PATH Act extended the employer tax credit for differential wage payments made to qualified employees on active military duty has been made permanent and applies to payments made after December 31, 2014. Effective only for tax years beginning after December 31, 2015, however, the credit may be claimed by all employers regardless of the average number of individuals employed during the tax year. The credit is also no longer limited to eligible small business employers with less than 50 employees.

Teachers' classroom expense deduction. The PATH Act permanently extended the above-the-line deduction for elementary and secondary school teachers' classroom expenses. Additionally, for tax years after 2015, the Act includes "professional development expenses" within the scope of the deduction. These expenses include courses related to the curriculum in which the educator provides instruction.

Nonbusiness energy property credit. The PATH Act extended the nonrefundable nonbusiness energy property credit allowed to individuals under Code Sec. 25C for two years, making it available for qualified energy improvements and property placed in service before January 1, 2017. For property placed in service after December 31, 2015, the standards for energy efficient building envelope components are modified to meet new conservation criteria.

Are Contributions to Foreign Charities Tax-Deductible?

Social media has helped to make our world smaller and when natural disasters and tragedies occur we want to help with contributions of money and/or other types of aid. At home, countless charitable organizations are providing all types of help and generally, your contributions to U.S. charities are tax-deductible. Contributions to foreign charities generally are not tax-deductible; however, special rules apply to charitable organizations in Canada, Israel and Mexico.

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First, let's take a brief look at some of the rules for U.S. charities. A charitable deduction is allowed only for a gift of money or property made to or for the use of an organization that meets qualification requirements. Charitable contributions of $250 or more must be substantiated by a contemporaneous written acknowledgment from the charitable organization to be deductible.

It is not enough that a domestic charity is "tax-exempt." The charitable organization must be qualified at the time of the contribution. It is the organization's responsibility to ensure that its character, purposes, activities, and method of operation satisfy the qualification requirements, so donors have assurance that their contributions are tax-deductible at the time made.

While a domestic charity can use contributions abroad, it cannot merely transfer them to a foreign charity. Contributions generally are deductible only if it can be shown, among other requirements, the domestic charitable organization is not serving as an agent for, or conduit of, a foreign charitable organization.

Special rules apply to charitable organizations in Canada, Israel and Mexico. Contributions to certain Canadian charitable organizations covered under an income tax treaty with Canada may be tax-deductible. Generally, the taxpayer must have income from sources in Canada.

The U.S.-Israel income tax treaty provides that a contribution to an Israeli charitable organization is deductible if and to the extent the contribution would have been treated as a charitable contribution if the organization had been created or organized under U.S. law. Among other requirements, the taxpayer must have income from sources in Israel.

The same approach applies to contributions to Mexican charitable organizations. Under the U.S.-Mexico income tax treaty, a contribution to a Mexican charitable organization may be deductible, but only if and to the extent the contribution would have been treated as a charitable contribution to a public charity created or organized under U.S. law. Among other requirements, the taxpayer must have income sources in Mexico.

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