Tax Compliance

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June 8, 2022

Learning Objectives – after this presentation you will have a better understanding of compliance issues related to:

1. Remote Employees
2. Donor Advised Funds (DAFs)
3. Alternative Investments and Added Reporting Requirements
4. Cryptocurrency
5. Political vs Lobbying vs Education

1

Remote Employees

Polling question

Do you have employees who work remotely?

- Yes
- No

If yes, does your organization have a policy in place to ensure you know where remote employees are physically located?

- Yes
- No
- Unknown

Hiring Employees to Work in Another State

- Factors to consider may include:
  - Recruitment, morale, retention
  - Is attracting the best talent worth the burden of compliance?
  - Roles and responsibilities of employees, such as soliciting contributions
  - Permanent vs temporary

Remote Employees

- Usually withholding depends on location of where the work is performed, rather than where the employer is located
- Variations:
  - Threshold requirements
    - Day count
    - Income
  - Convenience of the employer
  - Reciprocity
  - Residency in more than one state

Remote Employees Could Create Nexus and Require:

1. Withholding, state and local
2. State unemployment insurance
3. Income or franchise taxes
4. Sales and use tax
5. State charity filings
6. Tax exempt status
7. Secretary of State annual filings

Remote Employees

States with no income tax

AK FL NV SD

TN TX WA WY

Taxes only interest and dividends

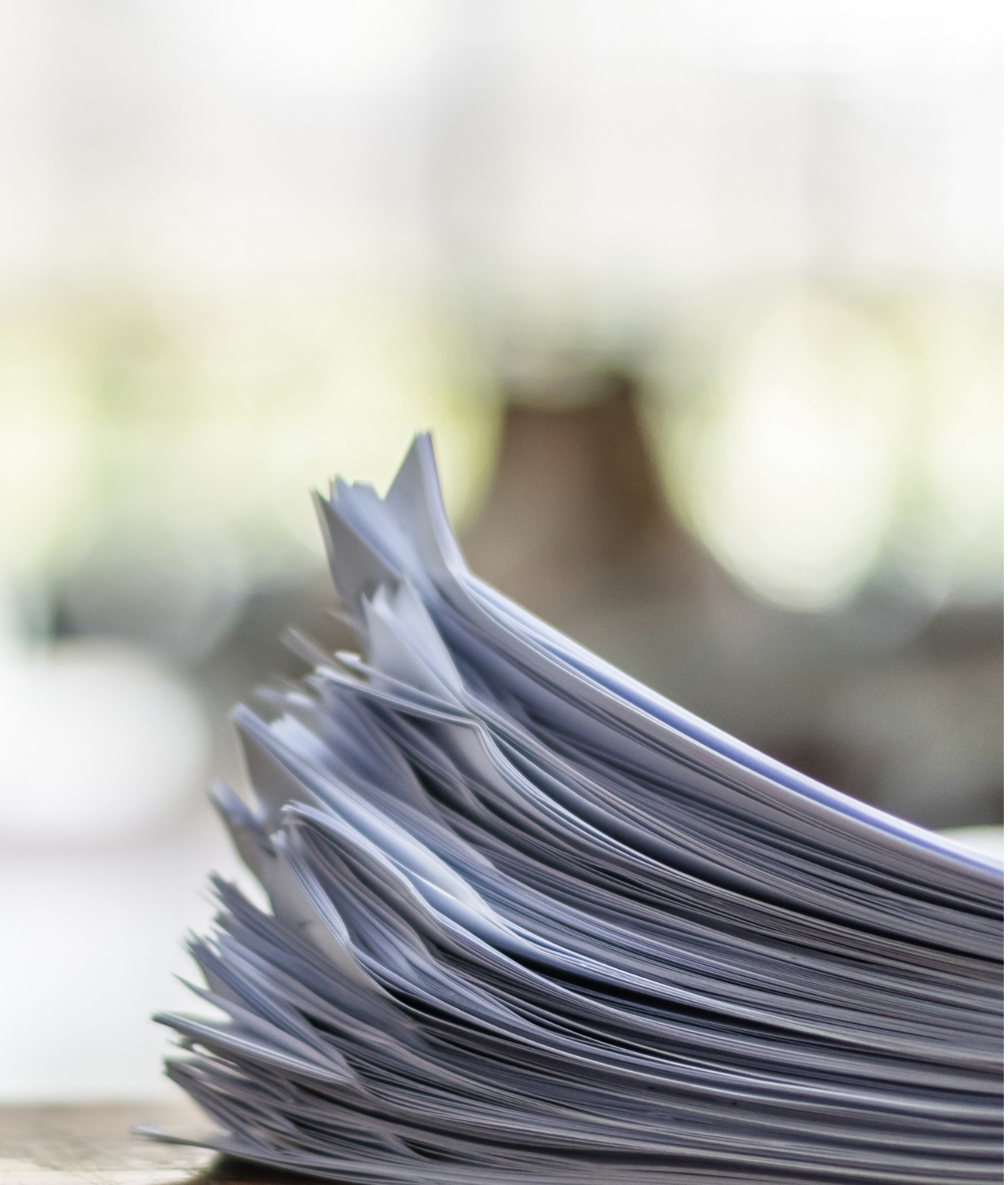
NH

States that base on where employer is located

NY NJ DE

NE CT PA

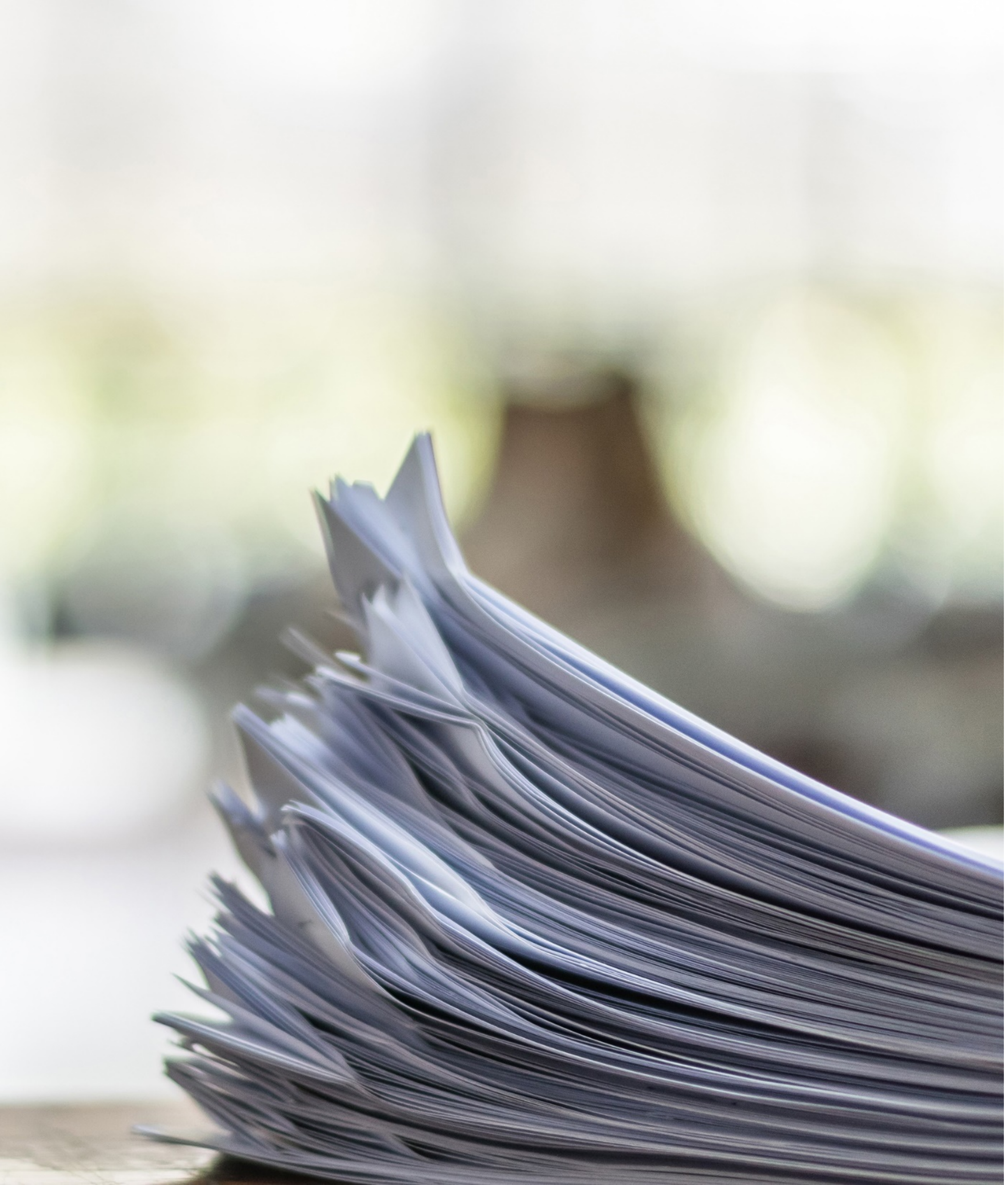
Mobile Workforce State Income Tax Simplification Act of 2021 not yet passed—tax in state of employee's residence and where employee is present and performing duties for more than 30 days



Other Issues Requiring Attention for Remote Employees in Another State

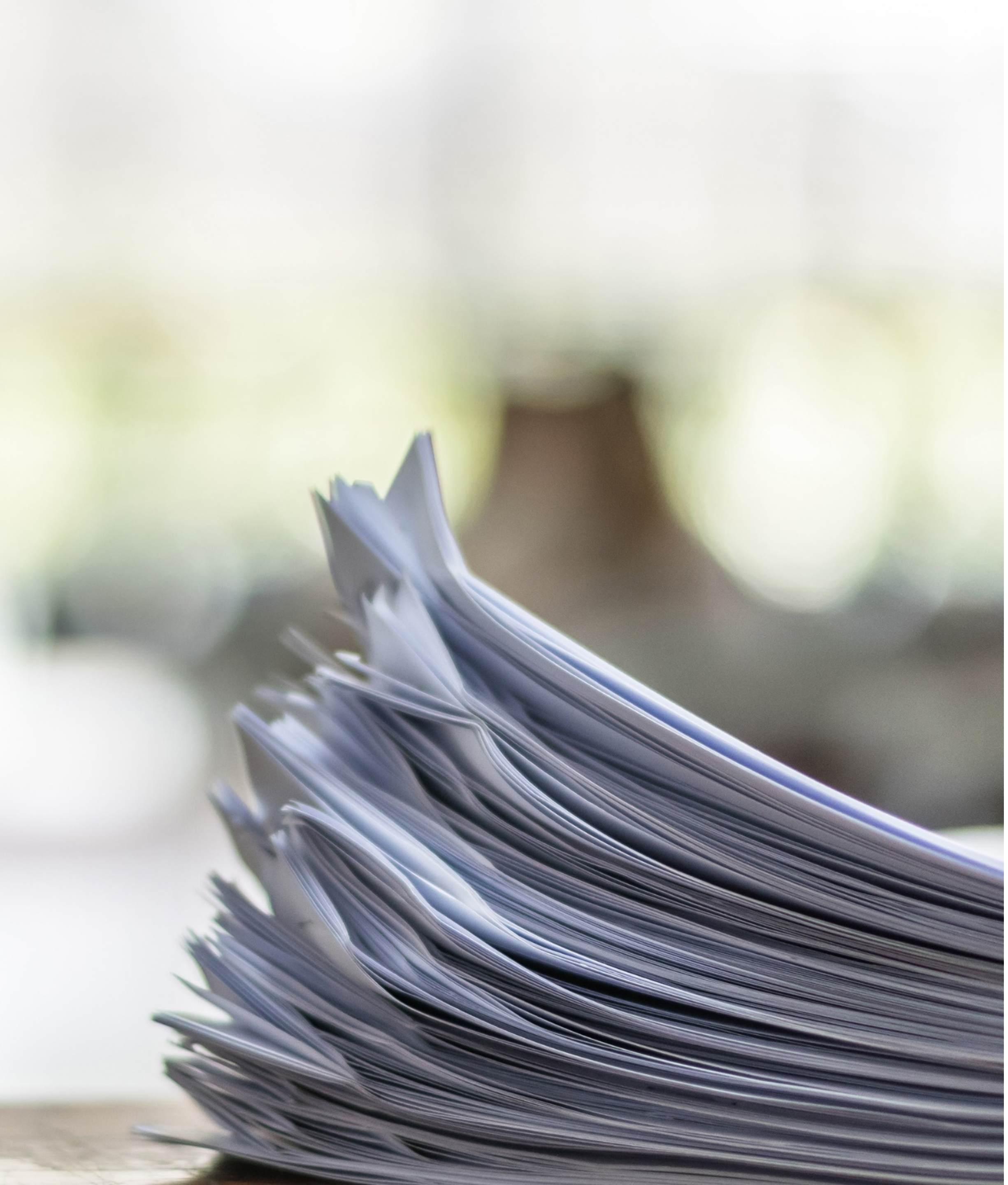
- Minimum wage and overtime pay, meal breaks
- Paid family leave and paid sick leave
- Disability benefits
- Workers' compensation
- Healthcare plans and other benefits coverage
- Antidiscrimination laws and equal pay
- OSHA reporting

May depend on number of days employee works in the state



Best Practice: Create a Policy

- Identify and compile the various state/local employment and tax law rules
- Quantify the potential financial and administrative costs
- Evaluate: does attracting the best and brightest, regardless of location, outweigh the additional tax, administrative cost, and risk of tax assessment (including interest and penalties) for failing to properly comply?



Best Practice: Create a Policy

Craft and communicate a policy (**including employee certification of work location, change**) so that all employees are treated fairly and relevant employment laws are properly followed.

2

Donor Advised Funds (DAFs)

What is a Donor Advised Fund?

- Investment vehicle through which donors can optimize tax benefits from charitable donations.
- Sponsored by 501(c)(3) public charities, Community Foundations
- Allows donors to make an irrevocable contribution, receive an immediate tax deduction, and then recommend grants from the fund over time.
- Grants are given over time to IRS-qualified 501(c)(3) public charities.

Assets generally accepted include

- *Cash equivalents*
- *Publicly traded securities*
- *Certain restricted, controlled, or lock-up stock*
- *Mutual fund shares*
- *Bitcoin and other cryptocurrencies*
- *Private equity and hedge fund interests*
- *Real estate*
- Certain complex assets, such as privately held *C-corp* and *S-corp* shares

What is a donor-advised fund?

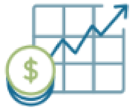
A simple, flexible and tax-efficient way to give to your favorite charities.

A donor-advised fund is like a charitable investment account, for the sole purpose of supporting charitable organizations you care about. When you contribute cash, securities or other assets to a donor-advised fund at a public charity, like Fidelity Charitable, you are generally eligible to take an immediate tax deduction. Then those funds can be invested for tax-free growth and you can recommend grants to virtually any IRS-qualified public charity.

When you give, you want your charitable donations to be as effective as possible. Donor-advised funds are the fastest-growing charitable giving vehicle in the United States because they are one of the easiest and most tax-advantageous ways to give to charity. Let's take an in-depth look at how a donor-advised fund works.

How a donor-advised fund works

MAKE A DONATION



GROW THE BALANCE

SUPPORT CHARITIES

DAFs' Growth Through the Years

- DAFs were formally recognized as a legal entity in 2006.
- Steady growth in both contributions and total assets through every year.

TABLE 1: DONOR-ADVISED FUND METRIC OVERVIEW ($ BILLIONS EXCEPT AS NOTED)

	2019	2020	Percentage change
Total Grants	$27.29	$34.67	27.0%
Total Contributions	$39.69	$47.85	20.6%
Charitable Assets	$145.49	$159.83	9.9%
Payout Rate*	22.3%	23.8%	6.9%
Number of DAF Accounts	864,187	1,005,099	16.3%
Average Size of DAF Account ($)	$168,355	$159,019	-5.5%

Advantages of a DAF

- Immediate tax deduction without deciding which charity will receive the funds
- Funds remain in the DAF and grow tax-free until donor decides to use them
- Ease of donating appreciated assets or cryptocurrency
- Allows donor to sustain their giving throughout their retirement

Disadvantages of a DAF

- DAF not legally required to spend the funds and can hold as long as desired.
- DAF has final say in what happens to the funds, not donor.
- Some DAFs contain hidden fees assessed by mutual funds in which donations are invested, in addition to the upfront charges.

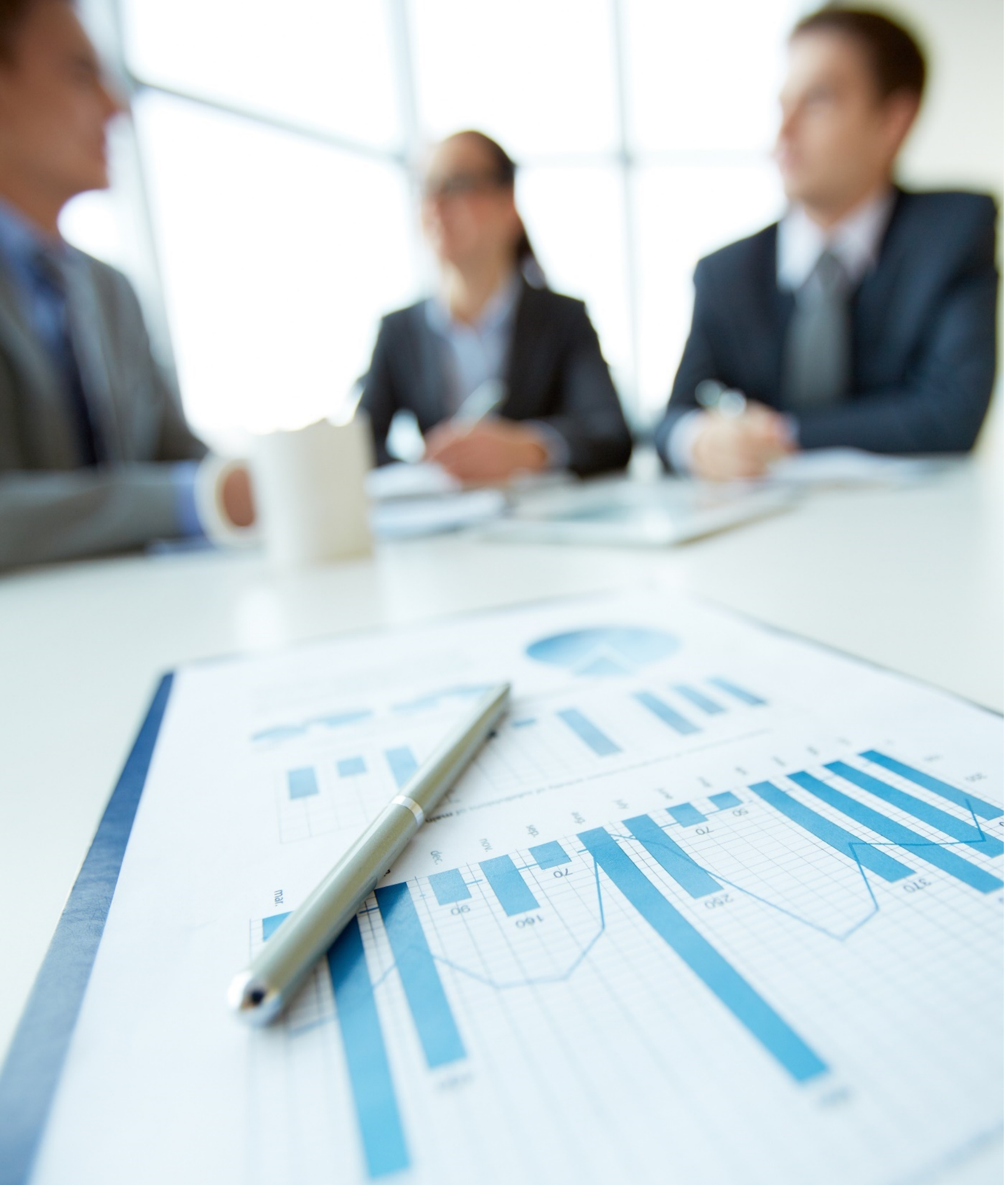
Many believe that giving directly to the organizations would yield larger overall contributions.

Concerns with DAFs

1. Is more money going into DAFs than grants coming out of them?
2. How much of the grants paid out by the DAFs are actually donor-designated?
3. Transparency – Donors will remain anonymous by contributing through DAFs, instead of donating directly to the organization.

How Much of the Grants Paid Out by the DAFs are Actually Donor-Designated?

- Donors can make recommendations on organizations to awards grants to, but DAFs are not required to follow their recommendations.
- Are there a large number of donors who are inactive when it comes to designating charities?
- What happens to a donor’s funds after they die?



Transparency

- By donating through a DAF, it allows the donor to remain anonymous.
- Can create donor-advised "dark money."
- Most DAFs are required to donate to only an IRS-qualified 501(c)(3) public charity.
- Fidelity and Schwab recently banned gifts from DAFs to NRA-Affiliated Charities.
- Their reasoning behind the ban was suspending grants to 501(c)(3) organizations that are under investigation, until the investigation concludes and the organization retains its 501(c)(3) status.

Proposed Regulation of Donor Advised Funds

The Accelerating Charitable Efforts Act (the ACE Act):

- Sponsored by Sen. Angus King (I -ME) and Sen. Chuck Grassley (R-IA), introduced in June 2021 but not yet passed into law
- 15 Year DAF: funds must be distributed by the DAF within 15 years of the donation (or pay 50% tax on undistributed funds)
- 15 Year DAF: tax deduction for nonpublicly-traded assets contributed to DAF not allowed until DAF sells the assets, and donation deduction = cash received in sale

Proposed Regulation of Donor Advised Funds

The Accelerating Charitable Efforts Act (the ACE Act):

- 50 Year Nonqualified DAF: Aligned Benefit Rule – No income tax deduction until the donated funds are distributed to charity
- 50 Year Nonqualified DAF: All funds required to be paid out to charity no later than 50 years after their donation (or pay 50% tax on undistributed funds)
- 50 Year Nonqualified DAF: No deduction allowed for donation to DAF (other than cash) until the DAF sells the property for cash

Proposed Regulation of Donor Advised Funds

The Accelerating Charitable Efforts Act (the ACE Act):

- Community Foundations (CF): Donors can contribute up to $1 million in DAF funds to a CF without being subject to payout rules
- CF DAF: Amounts exceeding $1 million require 5% annual payout or all distributions paid out within 15 years of donation
- Qualified CF – no larger than 4 states and at least 25% of assets are in non-DAFs
- Effective for contributions made after date of enactment

Proposed Regulation of Donor Advised Funds

The Accelerating Charitable Efforts Act (the ACE Act):

- Private Foundations: cannot meet payout rules through
  - salaries or travel expenses paid to a donor’s family members
  - **Or through distributions to DAFs** unless funds paid out of the DAF by the end of the following year

- Effective for distributions made after December 31, 2021 (note the date is the same in the House version)

Proposed Regulation of Donor Advised Funds

The Accelerating Charitable Efforts Act (the ACE Act):

- Public Support Tests and DAFs:
  - DAF considered to be one person, not a publicly supported org
  - DAF donor identified and treated as the donor rather than the DAF
- Effective for tax years beginning after enactment
- Exemption from investment income excise tax for PFs
  - Making significant qualifying distributions of 7% or more
  - New PF with life duration of 25 years or less
- Effective for tax years beginning after enactment

Proposed Regulation of Donor Advised Funds

Biden administration’s fiscal 2023 budget (Green Book):

- Proposal to prevent Private Foundations (PF) from using DAFs to meet minimum distribution requirements
- (1) Funds put into a DAF by a PF must be expended by the end of the following taxable year
- (2) PF must maintain adequate records or other evidence showing that the DAF has made a qualified distribution within the required time frame
- Effective after date of enactment

Proposed Regulation of Donor Advised Funds

Biden administration’s fiscal 2023 budget (Green Book):

- Reasoning for change: use of DAFs by a PF subverts the goal behind requiring minimum distributions

- Reasoning against change: PF might use a DAF when it wants to use a local community foundation's expertise to more effectively and efficiently determine how to meet local needs of that community

3

Alternative Investments and Added Reporting Requirements

Alternative Investments

- Investments outside of standard assets such as traditional stock and bonds
- Diversify portfolios and offer potential for higher rates of return
- Typically organized as corporations and partnerships; many are foreign in locales such as Cayman Islands with favorable tax laws
- Probable complex reporting requirements:
  - U.S. based
  - Foreign based
- READ the fine print in the offering documents very carefully, ask questions before making the investment

Alternative Investments

U.S. Based

- UBI probable – inquire before making investment
- Multiple state filings if UBI
- Net Operating Losses (NOLs) – cannot use in future if no filing done in year generated, offset only this activity
- Cost/benefit analysis must be done, determine appetite for risk
- Additional expense for tax filings must be considered when considering initial purchase; what is ROR after this expense?

Alternative Investments

Foreign Based

- Foreign reporting required, severe penalties if overlooked
  - **Form 990, Schedule F –** foreign investments exceed $100,000
  - **Form 926 –** invest $100,000 or more in 12-month period into corporation
  - **Form 8865 –** invest $100,000 or more in 12-month period into partnership
  - **Form 5471 –** required if own 10% or more of foreign corporation
  - **Form 3520 –** ownership in foreign trust
  - **FinCEN Form 114 –** report of foreign bank and financial accounts
  - Penalty $10,000 or more for each missed form
- Additional expense for tax filings must be considered when considering initial purchase; what is ROR after this expense?

Polling question

Does your organization accept donations of **Cryptocurrency?**

- Yes
- No
- Unknown

Does your organization accept donations of **Nonfungible Tokens (NFTs)?**

- Yes
- No
- Unknown

4

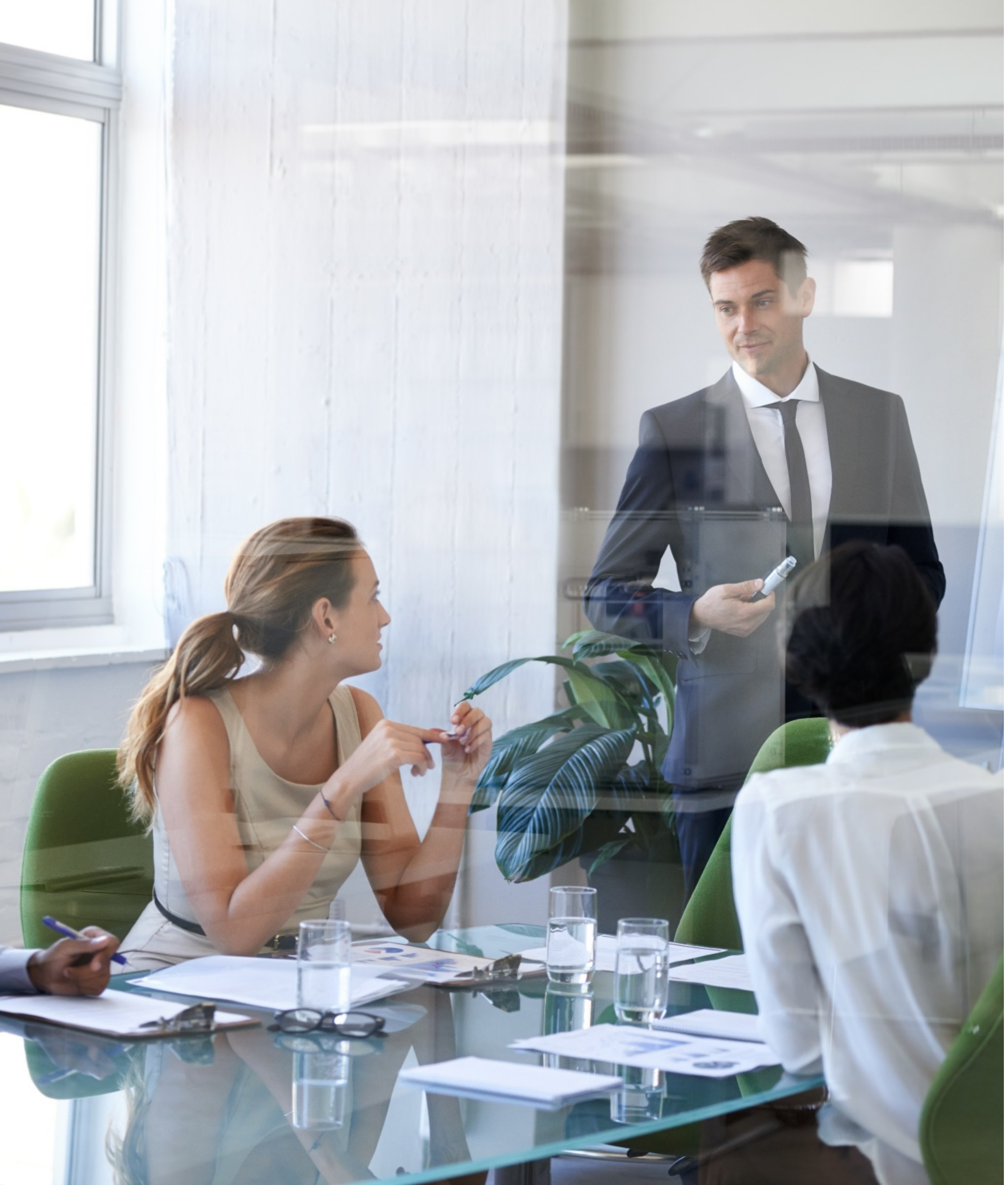
Cryptocurrency

Cryptocurrency

- Digital asset with no physical form (Bitcoin, Ethereum)
- Not issued by a central bank
- Held in a digital wallet, local and web-based versions, require password
- Regulations are minimal to date though anticipated soon
- Value based on supply and demand, volatile
- Has its own trading platforms (i.e., Crypto.com)

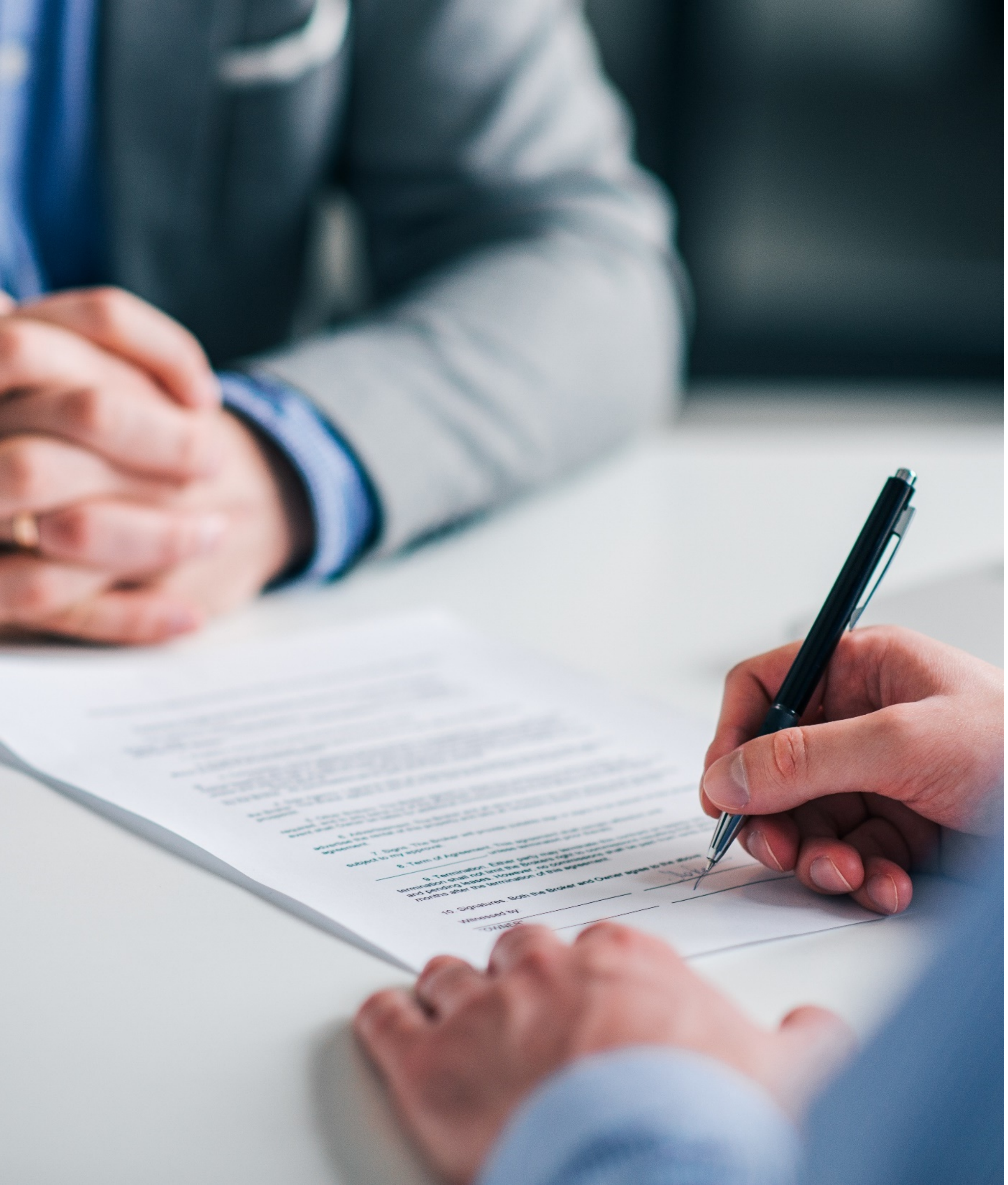
Cryptocurrency vs Nonfungible Tokens (NFTs)

- Cryptocurrency – type of virtual currency that uses cryptography to secure transactions that are digitally recorded on a distributed ledger (blockchain)
- NFT – unique digital assets that take various forms (artwork, music, in-game items)
- NFT – Purpose and function distinct from a "currency"
- If using cryptocurrency to buy NFTs, gain/loss on the cryptocurrency is recognized on the NFT purchase (Gain/loss = FMV of NFT less basis of cryptocurrency)



Can EOs accept as a donation?

- Yes – IRS considers cryptocurrency to be **noncash property**
- Internal controls must be in place to ensure security
- Review and update gift acceptance policy:
  - Willing to accept cryptocurrency?
  - Intend to hold or sell upon acceptance?
- Back-end support available (i.e., The Giving Block)
- Some EOs resisting as seen as predatory and believes contributes to global warming



Gift Acknowledgement

- Required for donations valued at $250 or more
- Noncash property = description only, no value on acknowledgement
- Form 8283 – EO signs Part V if value > $5,000
- Form 8283 – donor may need appraisal
- Form 8282 – if sold within 3 years

Recording Cryptocurrency

- Books – balance sheet = intangible asset
- Form 990 – noncash contribution revenue:
  - Schedule B
  - Schedule M
- Generates capitals gains/losses when sold

5

Political vs Lobbying vs Education

Polling question

What Internal Revenue Code Section is your organization exempt under? Select as many that apply if you represent multiple organizations.

- 501(c)(3)
- 501(c)(4)
- 501(c)(5)
- 501(c)(6)
- Other

Education Vs Lobbying Vs Political Activities

What is considered education?

- **Education = Advocacy**
- Stakeholders can make their voices heard through education, as long as it doesn't take a specific position.
- Examples:
  - Telling members of congress how grants helped constituents.
  - Inviting members of congress to visit your organization.
- If you attempt to influence legislation, you have crossed into lobbying.

Education Vs Lobbying Vs Political Activities

What is considered lobbying?

- **Lobbying = Legislation**
- Two types:
  - Direct Lobbying Communication: Direct communication with legislative member and refers to specific legislation and reflects a view on that legislation
  - Grassroots Lobbying: Attempt to influence legislation by affecting the opinions on the general public
    - Must include a call to action from the public
- Refer to specific legislation, and express a position on that legislation

Education Vs Lobbying Vs Political Activities

What are political activities?

- **Political Activities = People**
- Political activities are actions that support or oppose any candidate for an elected office.
  - Attempts to influence elections.
  - Applies to any federal, state, or local election.

501(c)(3) vs 501(c)(4) vs 527

501(c)(3)

Charitable

Donations are tax deductible

501(c)(4)

Social welfare

Donations are NOT tax deductible

527

Political Action Committee

Supporting or opposing candidates for political offices – donations are NOT tax deductible

501(c)(3) vs 501(c)(4) vs 527

Who can do what?

Education is acceptable for all organizations!

501(c)(3)

- Lobbying is allowed as long it is not "substantial"
- Substantial Test: Time and expenditures. Be careful.
- Section 501(h) election: quantifies "substantial"
  - 20% of first $500,000 of budget.
  - 15% of the next $500,000 up to $1 million.
- Political activities strictly forbidden by 501(c)(3)

501(c)(4)

- Unlimited lobbying as long as the issues relate to the exempt purpose.
  - Limited political activities (cannot be the primary activities)

527 Organizations

- Unlimited support of politicians.
- 501(c)(3) cannot make contributions to these organizations. 501(c)(4) organizations must file Form 1120 POL if they make a contribution.

Thank you

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