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IRS Increases Tangible Property Expensing Threshold For Taxpayers Without AFS

IR-2015-133, Notice 2015-82

In much-anticipated news, the IRS has announced an increase in the de minimis safe harbor limit under the "repair regs" for taxpayers without an applicable financial statement (AFS). The new $2,500 threshold takes effect starting with tax year 2016. The IRS also provided audit protection to qualified taxpayers by not challenging use of the new $2,500 threshold in tax years prior to 2016.

- ***Take Away.*** "The $2,500 amount is reasonable and will reduce the administrative burden on small businesses," Melissa Labant, CPA, director of tax advocacy, American Institute of Certified Public Accountants (AICPA), told Wolters Kluwer. "The AICPA is appreciative that the IRS listened to concerns from small businesses and tax professionals. This is an example of where the process worked," Labant added.
- ***Comment.*** For taxpayers with an AFS, the de minimis threshold under the repair regs is unchanged and remains $5,000.

Background

The repair regs provide a de minimis safe harbor election. Under the repair regs, the de minimis threshold amounts are $5,000 for taxpayers with an AFS and $500 for taxpayers without an AFS. The election is not a change in method of accounting, requiring the filing of Form 3115, Application for Change in Method of Accounting.

- ***Comment.*** On its website, the IRS explained that taxpayers should not file Form 3115, Application for Change in Method of Accounting, to use the de minimis safe harbor for a particular tax year, and should not file a Form 3115 to change the amount the taxpayer deducts under the taxpayer's book policy. Similarly, taxpayers should not file a Form 3115 to stop applying the de minimis safe harbor for a subsequent tax year.

The IRS explained that the de minimis safe harbor was intended as an "administrative convenience" so taxpayers could deduct small dollar expenditures for the acquisition or production of new property or for the improvement of existing property. However, the $500 threshold for taxpayers without an AFS generated controversy, with many small businesses and professional associations calling for an increase. The IRS requested comments about the threshold amount in Rev. Proc. 2015-20. The IRS reported that it received more than 150 comments.

Many small businesses and tax professionals cautioned that the $500 limitation was too low to effectively reduce the administrative burden of complying with the capitalization requirement for small businesses that frequently purchase tangible property in their trades and businesses. Commentators also expressed concern about the disparate treatment of taxpayers with an AFS compared to taxpayers without an AFS. For many small businesses, obtain-

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IRS Upgrades FATCA Online Registration System

IR-2015-131

Enhancements and upgrades have been made to the Foreign Account Tax Compliance Act (FATCA) Online Registration System, the IRS has announced. The changes will enable sponsoring entities to register their sponsored entities to obtain a global intermediary identification number (GIIN), among other upgrades.

- ***Take Away.*** IRS Commissioner John Koskinen characterized the registration system as the "backbone" of FATCA. "These upgrades improve the FATCA process, enabling the registration of sponsored entities and making it easier for registrants to use. Working with financial institutions and through intergovernmental agreements, our progress against undisclosed foreign accounts continues," Koskinen said.

Background

FATCA generally requires withholding agents to withhold tax on certain payments to foreign financial institutions that do not agree to report certain information to the IRS about their U.S. accounts. Financial institutions (FIs) may report information about account holders through the IRS's FATCA Registration System. FIs also receive a GIIN, which they use for identification purposes with withholding agents and tax administrators.

Enhancements

FATCA, the IRS explained, requires certain sponsored entities to have their own GIIN for reporting and withholding purposes by December 31, 2016. The FATCA Online Registration System has been upgraded to enable sponsoring entities to add their sponsored entities and, if applicable, to add sponsored subsidiary branches. These entities can be added either individually or by submitting a file containing information for multiple entities, the IRS explained.

The IRS also reported that new registration questions have been added, such as asking foreign financial institutions to indicate their tax identification number in their country or jurisdiction, if they have one. Other registration questions relate to identifying the common parent entity of an affiliated group. Additionally, certain FIs also can now change their "Financial Institution Type" and member financial institutions can now transfer to another affiliated group without having to cancel their current agreement and re-register.

FFI list

The IRS posts a list of all foreign financial institutions (FFIs) that have submitted a registration and have been assigned a GIIN at the time the list was compiled. The list is accessible on the IRS website. Several enhancements have been made to the list, the agency reported on its website. Additional sponsored entities and sponsored subsidiary branches appear on the list. Updated financial institution names for branches, which includes the financial institution's name under which the branch is listed, also has been added.

Reference: TRC FILEBUS: 9,108.

Threshold

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ing an AFS is cost prohibitive and does not adequately justify the substantially lower de minimis ceiling, commentators observed.

Increase in threshold

In response to concerns raised by small businesses and tax professionals, the IRS has decided to increase the de minimis threshold for taxpayers without an AFS. The threshold rises from $500 to $2,500 for costs incurred during tax years beginning on or after January 1, 2016. The IRS explained that it took this action in light of the many comments, recognizing that one goal of the repair regs is to reduce administrative burdens.

- ***Comment.*** The $2,500 amount is not indexed for inflation, Labant noted. As a result, the benefit of the safe harbor will erode with time.

Audit protection

For tax years beginning before January 1, 2016, the IRS will not raise on examination the issue of whether a taxpayer without an AFS can utilize the de minimis safe harbor for an amount not to exceed $2,500 per invoice (or per item as substantiated by invoice), if the taxpayer otherwise satisfies the requirements of Reg. §1.263(a)-1(f)(1)(ii). If the taxpayer's use of the de minimis safe harbor is an issue under consideration in examination, appeals, or before the Tax Court in a tax year that begins after December 31, 2011, and ends before January 1, 2016, the issue relates to the qualification under the safe harbor of an amount (or amounts) that does not exceed $2,500 per invoice (or per item as substantiated by invoice), and the taxpayer otherwise satisfies the requirements of Reg. §1.263(a)-1(f)(1)(ii), then the IRS will not further pursue the issue.

References: FED ¶¶46,469, 46,470; TRC BUSEXP: 9,104.15.

REFERENCE KEY

FED references are to ***Standard Federal Tax Reporter***
USTC references are to ***U.S. Tax Cases***
Dec references are to ***Tax Court Reports***
TRC references are to ***Tax Research Consultant***

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Wolters Kluwer Computes 2016 Luxury Vehicle Limits, Fringe Benefit Caps

Based on inflation factors now available, Wolters Kluwer has projected the annual "luxury vehicle" depreciation caps for use in connection with vehicles first placed in service in calendar year 2016. Also computed are the maximum fair market values (FMVs) to be used in 2016 to determine availability of the cents-per-mile method in determining the fringe benefit value of the personal use of employer-provided vehicles.

- ***Take Away.*** Overall, the CPI-U for new cars decreased from last year but rounding rules kept the depreciation caps the same. The price of trucks and vans, however, increased and did so sufficiently to push all but the third-year depreciation cap slightly higher. Computations under Code Sec. 280F call for use of the "new cars" and "new trucks" components of the October 2015 Consumer Price Index, Urban (CPI-U) that were released by the Bureau of Labor Statistics on November 17, 2015.
- ***Comment.*** Enhanced first year vehicle write-offs due to bonus depreciation—a significant benefit to most businesses—will not be available for 2015 or 2016, unless Congress extends bonus depreciation, which expired at the 50 percent level after December 31, 2014 (except for certain transportation and longer-lived property, which runs through 2015).

2016 vehicle depreciation caps

The projected luxury auto depreciation limits under Code Sec. 280F for passenger automobiles placed in service in 2016 are:

- $3,160 for the first year, the same as for 2015 ($11,160 for 2016, same as for 2015, only if Congress extends bonus depreciation into 2015 and 2016);
- $5,100 for the second tax year, the same as for 2015;
- $3,050 for the third tax year, the same as for 2015; and
- $1,875 for each tax year thereafter, the same as for 2015.

Trucks and vans

The projected maximum depreciation limits under Code Sec. 280F for trucks and vans first placed in service during the 2016 calendar year are:

- $3,560 for 2016, up from $3,460 for 2015 ($11,560 for 2016 if bonus depreciation is extended);
- $5,700 for the second tax year, up from $5,600 for 2015;
- $3,350 for the third tax year, the same as for 2015; and
- $2,075 for each tax year thereafter, up from $1,975 for 2015.

Cents-per-mile valuation

One permitted method that an employer can use to value the personal use of an employer-provided automobile is the standard mileage allowance rate, which for 2015 is 57.5 cents-per-mile for business-related travel (the 2016 mileage rate is expected to be announced sometime in mid-December 2015), but only if the vehicle's FMV does not exceed certain amounts. The maximum FMVs for use of the vehicle cents-per-mile valuation rule in 2016, as projected, will be:

- $15,900 for a passenger automobile (down from $16,000 for 2015);
- $17,700 for a truck or van, which includes minivans and SUVs built on a truck chassis (up from $17,500 in 2015); and
- $21,200 for a fleet passenger automobile (down from $21,300 for 2015) and $23,100 for a fleet truck or van (up from $22,900 for 2015).

Reference: TRC DEPR: 3,504.05.

IRS Rejects Portion Of Taxpayer's Losses Claimed Under Repair Regs For Dispositions Of Structural Components

FAA 20154601F

The IRS, in field attorney advice (FAA), has rejected part of a taxpayer's claimed losses under Code Sec. 168 and the "repair regs" from the disposition of building structural components. The IRS concluded that the taxpayer's statistical study used by the taxpayer to estimate its loses incorrectly applied the proposed regs under Code Sec. 168.

- ***Take Away.*** The repair regs change prior law and provide a substantial benefit to taxpayers by allowing them to write off the remaining cost of building structural components (BSCs) when they are replaced, rather than having to continue to depreciate their cost. The FAA demonstrates, however, that it may not be so easy to satisfy the IRS when a taxpayer uses a statistical sample to calculate its losses.

Background

The taxpayer operated its business at several locations using both owned and leased facilities. Prior to the IRS's proposal and adoption of the repair regs, the taxpayer capitalized and depreciated building structural components (BSCs) as fixed assets under Code Sec. 168(a). Whenever the taxpayer disposed of BSCs, it continued to depreciate them under existing loss, and did not recognize a loss.

The taxpayer filed Form 3115, Change in Accounting Method, to adopt the accounting method for disposing of BSCs under the 2013 proposed regs for Code Sec. 168. The taxpayer used a statistical study to identify assets that it had disposed of but was still depreciating, and determined the percentage of sampled records showing a loss that could be written off.

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IRS Rejects Taxpayer's Claim For Interest On Additional Overpayment Portion Attributable To NOL

TAM 201548019

The IRS has determined in technical advice that a taxpayer was entitled to overpayment interest on a portion of an overassessment of tax. However, interest on the overpayment was allowable only until the due date of the return for the year that the taxpayer claimed a net operating loss (NOL) carryback.

- ***Take Away.*** The taxpayer claimed that interest was due until the IRS paid a tentative refund on an NOL carryback. The IRS concluded that interest was not owed after the due date of the return on which the NOL was claimed (the "loss return year").

Background

The taxpayer filed a return for Tax Year 1 and timely paid the tax by the due date of the return (Date 1). The taxpayer claimed an NOL for Tax Year 2. The taxpayer carried the NOL back to Tax Year 1 and filed a tentative refund claim on Date 4. The IRS issued a refund of Amount 1. No overpayment interest was paid because the refund was paid within 45 days.

The IRS subsequently disallowed most of the NOL and assessed, on Date 3, an underpayment of Amount 2. On the same day, the IRS made an adjustment to the return for Tax Year 1 that reduced the tax due on the original return, resulting in an overpayment of Amount 3. The Amount 3 overpayment exceeded the Amount 2 underpayment by Amount 4. (Thus, Amount 2 plus Amount 4 equaled Amount 3.)

The IRS paid interest on Amount 2, computed from Date 1 (the filing and payment due date for Tax Year 1) until Date 2 (the due date for Tax Year 2, the year that supposedly generated the NOL). The IRS paid interest on Amount 4 from Date 1 to Date 4 (the date of the tentative refund). The taxpayer claims that the interest on Amount 2 should also be computed from Date 1 to Date 4.

- ***Comment.*** Code Sec. 6611(b) determines the period for interest on overpayments. For a credit, interest runs from the date of the overpayment to the due date of the amount against which the credit is taken (Code Sec. 6611(b)(1)). This is usually the last day for the payment of tax, without extensions. For a refund, interest runs from the date of the overpayment to a date preceding the date of the refund check by no more than 30 days (Code Sec. 6611(b)(2)).

IRS analysis

The IRS looked to dictionary definitions "credit" and "refund." A credit is a deduction from an amount otherwise due. Since the IRS deducted the Amount 2 underpayment from the Amount 3 overpayment (and refunded the excess, Amount 4, with interest), Amount 2 was an amount credited.

A refund is an amount of money returned, to balance an account. The overpayment equal to Amount 2 was not returned to the taxpayer. Thus, the due date for interest was the unextended due date of the return on which the tax must be reported.

Reference: TRC PENALTY: 9,100.

Structural Components

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The taxpayer relied on its case histories for fixed assets, including asset location, description, tax life, depreciation, placed-in-service date, and net tax value. The taxpayer did not use multiple asset accounts and excluded assets with a recovery period under 15 years and nonbuilding-related assets. The cost histories were the sole source of information about disposed of assets.

Law

The final repair regs under Code Sec. 168 apply to tax years beginning on or after January 1, 2014. Taxpayers may rely on the proposed regs under Code Sec. 168 for years beginning on or after January 1, 2012. The IRS agreed that the taxpayer was entitled to rely on the proposed regs.

Under the proposed regs, a taxpayer can claim a loss when it disposes of a depreciable asset that it has not fully depreciated. The taxpayer can make a late partial disposition election for tax years 2012-2014 by filing Form 3115.

The proposed regs only apply to MACRS depreciable property. Buildings and their structural components are assets. A taxpayer disposes of an asset when it permanently withdraws the asset from use in its trade or business. A taxpayer that disposes of part of an asset can use any reasonable method to determine the basis of the disposed of portion.

IRS analysis

The IRS concluded that the taxpayer's study overstated its losses because it incorrectly applied the proposed regs and because taxpayer's records do not fully substantiate the reported losses. The IRS identified the following problems:

- The case histories included assets depreciated under the pre-MACRS method; no loss can be recognized on the disposal of those assets.
- A loss cannot be claimed unless an asset is disposed of; many of the new assets were for an expansion or addition to existing assets, not a disposition.
- When a disposed of asset is replaced, the old and new assets should be in the same location and of the same type; many assets did not meet these requirements.
- A taxpayer cannot claim a loss unless it has basis remaining at the time of disposition; many of the cost histories do not identify any basis.
- A taxpayer can use the FIFO method to identify assets, but the old and new assets must have the same recovery period.

Reference: TRC DEPR: 15,210.

Chief Counsel Reviews When Employers May Exclude From Income Cost Of Health Insurance Coverage

CCA 201547006

IRS Chief Counsel has reaffirmed that an employer may exclude from an employee's gross income payments for the cost of health insurance coverage provided through his or her spouse's group health plan but only to the extent the spouse has paid for all or part of the coverage on an after-tax basis and not through salary-reduction under a Code Sec. 125 cafeteria plan. Chief Counsel reviewed a number of scenarios.

- ***Take Away.*** Employers can contribute to accident or health plans in different ways. The employer may pay the premium on a policy of accident or health insurance. It may contribute to a separate trust or fund that provides accident or health benefits directly or through insurance to the employees. The employer also may reimburse employees who are not covered by group insurance for all or part of the expense of their own policies.

Background

Scenario #1. Anita and Barry are married. Anita does not participate in her employer's group health plan. Barry participates in his employer's group health plan. This plan requires an employee participating in the plan to make either an after-tax contribution of $100 per month for self-only insured coverage or an after-tax contribution of $175 per month for other than self-only insured coverage. Barry elects other than self-only coverage to cover both him and Anita. Anita substantiates to her employer that Barry has $175 per month deducted from his pay on an after-tax basis, $75 of which represents the cost of Anita's insured coverage. Anita's employer pays her $75 per month in addition to her other compensation.

Cafeteria plan. The facts are the same as in scenario #1 except that Barry makes the contribution to his employer's plan by salary reduction through his employer's Code Sec. 125 cafeteria plan.

Chief Counsel's analysis

Chief Counsel first observed that Code Sec. 106 provides that gross income of an employee does not include employer-provided coverage under an accident or health plan. Code Sec. 125 allows an employer to establish a cafeteria plan that permits an employee to choose among two or more benefits, consisting of cash (generally, salary) and qualified benefits, including accident or health coverage. The amount of an employee's salary reduction applied to purchase coverage is not included in gross income.

In Scenario #1, Chief Counsel determined that the amounts are excluded from Anita's gross income under Code Sec. 106 because her employer is paying the premium (or a portion of the premium) on a group health plan covering one or more employees, the employee's spouse and dependents, or by contributing to a separate trust or fund, which provides accident or health benefits directly or through insurance to one or more employees, the employee's spouse and dependents. The payments are also excluded from FICA and FUTA taxes, and federal income tax withholding.

In the cafeteria plan scenario, Chief Counsel determined that the amount paid for insured health coverage by Barry through salary-reduction under a cafeteria plan has been excluded from his gross income. An employer may not exclude from gross income under Code Sec. 106 an amount paid to an employee for insured health coverage that has already been excluded from gross income as employer-provided coverage (including salary-reduction amounts under a cafeteria plan). Chief Counsel determined the arrangement under which Anita's employer makes payments to Anita fails to be a health plan. No amounts paid under the arrangement to any participant would be excluded from gross income and the amounts are also subject to FICA and FUTA taxes, and federal income tax withholding.

Reference: TRC INDIV: 33,408

IRS Launches Form W-2 Verification Code Pilot Program For 2016 Filing Season

For the 2016 filing season, the IRS has announced a new pilot program to test whether requiring certain employees to enter a verification code displayed on their Forms W-2 onto their e-filed tax returns will be helpful in curbing identity theft. The test will not apply to paper-filed tax returns.

Verification code. Certain payroll service providers have agreed to participate in this test for 2016. Participants will randomly include a 16-digit code on a limited number of the Form W-2 statements (copies B and C) issued to employees. These employees, when preparing their e-filed tax returns (or having them prepared), will be prompted by their tax return software to enter the verification code. The objective of this test, the IRS explained, is to verify that the data on the Form W-2 copies submitted to the IRS by taxpayers and the data reported on their e-filed returns is accurate.

- ***Comment.*** Presumably identity thieves would not have access to the taxpayer's genuine W-2 statement.

The IRS indicated that tax preparation software will not always request the code. For purposes of the test, omitted and incorrect W-2 Verification Codes will not delay the processing of a tax return, the IRS stated.

Some Forms W-2 will have a "Verification Code" box that is blank. Taxpayers with blank boxes do not need to enter any data into their tax software, the IRS explained.

www.irs.gov.

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Chief Counsel Determines Civil Tax Issues For Taxpayer Convicted Of Filing False Or Fraudulent Returns

CCA 201545016

IRS Chief Counsel has addressed several civil tax issues involving false tax returns, the filing of which resulted in criminal charges against the taxpayer. The issues addressed include the validity of the returns; the imposition of tax, additions, and penalties; and the application of collateral estoppel.

- ***Take Away.*** The CCA demonstrates that the taxpayer's actions involving the filing of return must be taken at face value and analyzed under civil tax provisions. The fact that the taxpayer pled guilty to filing a false return does not automatically negate the taxpayer's actions.

Background

A taxpayer filed purported tax returns for several years. The returns reported false original issue discount (OID) income and withholdings. The taxpayer attached false Forms 1099-OID. The taxpayer was charged with filing a false, fictitious, or fraudulent for each year. The taxpayer pled guilty to the charge for one tax year and was sentenced to jail time.

The taxpayer had struck out the "under penalties of perjury" portion of each return filed on paper. For one return, the IRS assessed tax, based on the purported returns, additions to tax, and interest. The IRS did not credit the taxpayer for the withholdings and did not issue the claimed refund. The IRS did not process other returns filed on paper.

The taxpayer also e-filed a return that reported false income, withholdings, and a refund. The IRS redetermined the correct tax for the year, applied a portion of an overpayment to the taxpayer's liability, and froze the remainder.

Issues

Chief Counsel came to the following conclusions:

1. The paper returns were not valid, because the taxpayer struck out the "penalties of perjury" references. The e-filed return was valid.
2. The IRS can abate tax assessments or the excessive portion of the assessments for several unidentified tax years. The assessment period of limitations is open for several years; for one year, it is open only if the IRS can establish that the return was fraudulent. For all the years, the IRS must follow deficiency procedures in making assessments.
3. The IRS calculated the amount of the fraud penalty for a particular year.
4. The taxpayer's guilty plea does not collaterally estop the taxpayer from litigating Code Sec. 6651(f) additions to tax for a fraudulent failure to file or the Code Sec. 6663 fraud penalty.
5. Neither treating the returns as valid or as invalid is more consistent (or inconsistent) with the positions taken in the criminal prosecution.

Chief Counsel's analysis

Issue 1. For the tax year that the taxpayer did not strike out "under penalties of perjury," the return is valid if it satisfies a four-part test: there is sufficient data to calculate tax liability; the document purports to be a return; there is an honest and reasonable attempt to satisfy the tax law; and the taxpayer executes the penalties of perjury statement. The taxpayer's return satisfies this test and is valid. As long as the return "on its face plausibly purports to be in compliance," it can be a valid return, even if it is incorrect or fraudulent.

Issue 2. Where an assessment of tax exceeds the correct tax liability, the IRS can abate the assessment. Where the taxpayer reported false OID income, the assessment was excessive. Where the tax is abated, the IRS cannot reassess liability unless the applicable period of limitations is still open. The IRS should consider this before abating any assessment.

Issue 4. The civil fraud penalty requires that the taxpayer intended to evade a tax "believed to be owing." This element of intent does not appear to be a necessary element to the taxpayer's criminal conviction. Therefore, although taxpayer's plea may be relevant to the issue of fraud, it does not prevent the taxpayer from litigating the issue.

Reference: TRC PENALTY: 6,102

Fall 2015 SOI Bulletin Released; Partnerships, CFCs Show Gains

The latest IRS Statistics of Income Bulletin highlights partnerships and controlled foreign corporations (CFCs). Data shows that both entities continue to represent a growing share of the U.S. tax base.

Partnership returns (2013). The number of partnerships and partners in the U.S. continued to increase for tax year 2013. Partnerships filed over 3-million returns, representing more than 27 million partners. The real estate and leasing sector contained nearly half of all partnerships (49.8 percent) and just over a quarter of all partners (27.7 percent). Domestic limited liability companies (LLCs) made up the majority (at 66 percent) of all partnerships, surpassing all other entity types for the 12th consecutive year.

Controlled foreign corporations (2010). The number of foreign corporations controlled by U.S. multinational corporations decreased slightly in 2010, to 84,260. Despite the decrease, end-of-year assets ($15.9 trillion), total receipts ($6.2 trillion) and current earnings and profits (less deficit) before income taxes ($822 billion) all increased from tax year 2008.

IRS Fall 2015 Statistics of Income Bulletin (irs.gov).

Chief Counsel Nixes Deduction For Settlement Payment Related To Foreign Bribery Charges

LAFA 20154702F

IRS Chief Counsel, in Legal Advice Issued by Field Attorneys (LAFA), has determined that no business deduction could be taken for a settlement payment related to foreign bribery charges. Chief Counsel was not persuaded that the taxpayer's primary motive for the payment was to preserve its business reputation.

- ***Take Away.*** Code Sec. 162 generally allows taxpayers to deduct ordinary and necessary business expenses. However, Chief Counsel noted that no deduction is allowed under Code Sec. 162(a) for any fine or similar penalty paid to a foreign government and this encompasses an amount paid in settlement of an actual or potential liability for a civil or criminal fine or penalty.

Background

The taxpayer's former subsidiary did business in Country A. Country A claimed that the subsidiary had bribed government officials in exchange for contracts. An indictment was eventually brought by Country A against executives of the taxpayer and its subsidiary. The taxpayer requested a settlement and Country A agreed. The taxpayer paid a monetary amount to Country A. In turn, Country A ended all legal proceedings against the taxpayer and its subsidiary.

Chief Counsel's analysis

Chief Counsel determined that the settlement agreement between the taxpayer and Country A resolved all of the issues concerning the purported bribery. Chief Counsel further determined that the taxpayer's payment under the agreement was a fine or similar penalty paid for violation of law. The payment, Chief Counsel noted, was made to avoid any potential liability, regardless of the validity of the charges. Therefore, any deduction was barred by Code Sec. 162(f).

In defense of its deduction, the taxpayer claimed that its primary motive for the payment was to preserve its business reputation as well as to ensure continued business in Country A. However, Chief Counsel determined that the taxpayer's reliance on *Jenkins, TC Memo. 1983-667*, was misplaced. The business losses in *Jenkins* were properly deductible, unlike the amount paid by the taxpayer. The issue of protecting its reputation or its continued business, Chief Counsel determined, was incidental to the fact that the settlement resolved serious charges filed against it and its executives for alleged violations of Country A's laws.

Reference: TRC BUSEXP: 18,808.

TAX BRIEFS

Internal Revenue Service

The IRS did not abuse its discretion by retroactively revoking a favorable determination letter issued to a professional association's Employee Stock Ownership Plan (ESOP). The (ESOP) was not qualified under Code Sec. 401(a) and the related trust was not exempt Code Sec. 501(a) for the plan year at issue or any subsequent year because it failed to operate according to the plan document.

Fleming Cardiovascular, P.A., TC, Dec. 60,453(M), FED ¶48,163(M); TRC COMPEN: 21,050

Jurisdiction

The Tax Court lacked jurisdiction to determine a married couple's tax deficiency because their petition was not timely filed. The timely filing of a petition for redetermination is a jurisdictional prerequisite. Accordingly, the Tax Court's orders were vacated and the case remanded with instructions to dismiss the couple's petition for lack of jurisdiction.

Briley, CA-4, 2015-2 USTC ¶50,569; TRC LITIG: 6,106.05

Deductions

The IRS properly applied Code Sec. 482 to disallow a limited liability company's (LLC) losses attributable to a portfolio of nonperforming loans acquired from a Chinese asset-management company. The IRS properly reduced the LLC's basis in the loan portfolio.

Austin Investment Fund, LLC, DC D.C., 2015-2 USTC ¶50,574; TRC ACCTNG: 30,050

Liens and Levies

An individual's appeal of a Tax Court decision upholding a federal tax lien notice and imposing a penalty for raising frivolous arguments for purpose of delay was dismissed because the petition was filed in an improper venue. Moreover, a transfer of the case to the appropriate venue was not in the interests of justice.

A.S. Kanofsky, CA-4, 2015-2 USTC ¶50,570; TRC LITIG: 6,962

Refund Claims

The government was entitled to recover an erroneous refund paid to a married couple. The IRS Office of Appeals exceeded its authority when it issued the refund to the couple because the couple's refund request was untimely and the limitations period was not equitably tolled. In addition, the court could not abate the interest because only the IRS has the authority to abate interest on erroneous refunds.

Bates, DC Fla., 2015-2 USTC ¶50,575; TRC IRS: 33,312.10

Collection Due Process

The IRS was not entitled to summary adjudication of a challenge to a Collection Due Process (CDP) determination because there was a genuine issue of fact regarding the taxpayer's receipt of the deficiency notice. However, the IRS's assessments were valid because the IRS mailed deficiency notices for the tax years at issue to the taxpayer.

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Tax Briefs

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Concluding that an individual taxpayer's denial of receipt was insufficient to rebut the presumption when the taxpayer lacked documented and routinized procedures for handling mail, and could seldom offer any evidence other than mere denials, would in effect make the presumption conclusive, to the prejudice of the taxpayer's rights.

Garrett, TC, Dec. 60,457(M), FED ¶48,167(M); TRC IRS: 51,056.25

An IRS settlement officer did not abuse his discretion by including an individual's veteran disability benefits when calculating the taxpayer's ability to make installment agreement payments. The IRS's position was consistent with the requirement in the Internal Revenue Manual that amounts a taxpayer receives that are not includible in gross income may be included when determining ability to pay even if those benefits are not subject to levy under Code Sec. 6334.

Matthews, Jr., TC, Dec. 60,454(M), FED ¶48,164(M); TRC IRS: 51,062

Tax Assessments

A married couple's federal tax liabilities were reduced to judgment. The couple timely filed their tax returns for the tax years at issue but failed to pay the reported tax liability. Moreover, despite notice and demand for payment, the couple failed to pay their tax liabilities in full. Since the IRS established that the assessments were properly made and the liability had not been satisfied, the government was entitled to judgment in its favor.

O'Connor, DC Calif., 2015-2 USTC ¶50,577; TRC LITIG: 9,256

Deficiencies and Penalties

The CEO of a steel company was a responsible person liable for trust fund recovery penalties. There was sufficient evidence for the jury to find that the CEO was "responsible" within the meaning of Code Sec. 6672. There was also sufficient evidence for the jury to find that he acted willfully because he paid other creditors before the government.

Sananikone, CA-9, 2015-2 USTC ¶50,573; TRC PAYROLL: 6,306.05

The president and CEO of a construction company was liable for the trust fund recovery penalty and his wife's untimely injured spouse claim was properly dismissed for lack of subject matter jurisdiction. The husband willfully paid other creditors instead of remitting the trust fund taxes to the IRS and the wife failed to show she contributed to the overpayment and, therefore, was entitled to a refund.

L.D. Ruscitto, CA-3, 2015-2 USTC ¶50,572; TRC PAYROLL: 6,308

Withholding

A dentist and his various business entities were enjoined from failing to withhold and pay over federal employment taxes or dissipating assets. The government showed that it was likely to succeed on the merits; an injunction was in the public's interest; and necessary to prevent accumulation of additional tax debt.

Dental Care Associates of Spokane Valley, PS, DC Wash., 2015-2 USTC ¶50,576; TRC LITIG: 9,256

Tax Crimes

A tax preparer's conviction for willfully aiding and assisting in the preparation of fraudulent tax returns in violation of Code Sec. 7206(2) was affirmed. The district court's refusal to provide the individual's requested instruction did not affect the case's outcome.

Carter, CA-5, 2015-2 USTC ¶50,568; TRC IRS: 66,058.20

Frivolous Arguments

The appeals court lacked jurisdiction over a successful taxpayer's appeal. Further, the Tax Court properly denied the individual's motion to consolidate her frivolous-return penalty case with tax proceedings involving her husband. There was no evidence that the Tax Court abused its discretion by denying the motion to consolidate.

Kupersmit, CA-3, 2015-2 USTC ¶50,571; TRC LITIG: 6,662

Bankruptcy

After the Tax Court issued its ruling in T.G. Akey, 108 TCM 433, Dec. 60,051(M), TC Memo. 2014-211, the taxpayer notified the court he had filed for bankruptcy before the ruling was issued. The court then vacated that opinion and stayed the proceedings. Now that the automatic stay has terminated, the Tax Court has replaced TC Memo. 2014-211 with a new, unchanged opinion.

Akey, TC, Dec. 60,456(M); TRC BUSEXP: 15,050.

IRS Advises Tax Professionals To Check Electronic Filing Identification Number Status

In a Fact Sheet, the IRS has reminded tax professionals preparing for the 2016 filing season to review their Electronic Filing Identification Number (EFIN) status to insure its accuracy and security. EFINs are numbers issued by the IRS that enables authorized IRS e-file providers to file returns electronically. The IRS emphasized that EFINs are available only by accessing IRS e-services, and recipients must meet certain requirements, including a background check, in order to qualify.

The IRS recommended several steps that can be taken by professionals prior to and during the filing season, including: review the e-file application on e-services at *IRS.gov* before the filing season; ensure that proper individuals are identified on the EFIN application; identify one or more responsible officials; ensure that multiple offices that are transmitting returns from multiple locations have separate EFINs; and regularly check that the status of employees or contractors who may not be authorized to participate in IRS e-file.

- ***Comment.*** Participation requirements and necessary steps to obtain an EFIN are provided in IRS Publication 3112, IRS e-file Application and Participation. Rules and requirements for participation in IRS e-file are set out in IRS Publication 1345, Handbook for Authorized IRS e-file Providers of Individual Income Tax Returns.

FS-2015-27, FED ¶46,462; TRC FILEIND: 18,054.

PRACTITIONERS' CORNER

Foreign Information Returns, First-Time Abatement, And Accuracy-Related Penalties

Taxpayers who fail to report or who improperly report certain items can face stiff penalties under the Internal Revenue Code. For example, foreign information reporting by individuals has been required for a while, but concerns about tax avoidance involving offshore assets have focused a spotlight on both new and existing reporting requirements. For other failures or omissions involving improper reporting, accuracy-related penalties can mount up. At the same time, many penalties can be waived for "good behavior" by the taxpayer, but the requirements for waivers can differ, depending on the type of violation. This Practitioners' Corner looks at selected topics involving information reporting by individuals, penalties, and penalty waivers.

Foreign accounts

Since the enactment of the *Foreign Account Tax Compliance Act* (FATCA), taxpayers have had to comply with two reporting requirements for foreign assets and accounts: Form 8938, Statement of Specified Foreign Financial Assets; and FinCEN Form 114, Report of Foreign Bank and Financial Accounts (FBAR). These are separate requirements; the filing of one form does not qualify as compliance with the other form.

Code Sec. 6038D imposes a $10,000 penalty on individuals who fail to report specified foreign financial assets if the assets' aggregate value exceeds the applicable threshold ($50,000 for resident U.S. individuals). There is an exception to the filing penalty for "reasonable cause."

Title 31 similarly imposes a $10,000 penalty on a U.S. person who fails to file the FBAR, if the accounts' aggregate value exceeds $10,000. Current law requires that the FBAR be filed by June 30, to report for the prior calendar year, and does not provide for any extension for filing the FBAR for tax years beginning before January 1, 2016.

New law (the *Surface Transportation Act of 2015*) prescribes a filing deadline of April 15 for tax years beginning on or after January 1, 2016. Taxpayers may also obtain a six-month extension, and the IRS (which enforces the FinCEN requirements) has the authority to waive penalties for first-time filers. There is also an exception to the FBAR filing penalty for reasonable cause, provided the balance in the account is properly reported. For a willful failure, a person may be subject to a penalty of the greater of $100,000 or 50 percent of the balance in the account at the time of the violation.

- ***Comment.*** The IRS's Offshore Voluntary Disclosure Program provides a mechanism for nonfilers to become compliant, with the potential for reduced penalties.

"Taxpayers who fail to report or who improperly report certain items can face stiff penalties under the Internal Revenue Code."

Transfers of property abroad

The concern about property held abroad by U.S. taxpayers is also reflected in other filing requirements. Code Sec. 6038B requires U.S. persons to report certain transfers of property to non-U.S. persons and entities. Form 926 must be filed. U.S. transferors also must report a contribution to a foreign partnership on Form 8865. For both filing requirements, taxpayers can be penalized 10 percent of the fair market value of the property at the time of the transfer. The penalty is capped at $100,000, unless the failure to file was due to intentional disregard.

Sec. 6048 imposes reporting on U.S. persons who own and/or transfer property to a foreign trust. Form 3520 must be filed. Penalties are set at the greater of $10,000 or 35 percent of the "gross reportable amount" for each failure to file. Additional penalties can apply if the taxpayer fails to file with 90 days after notice of the need to file.

- ***Comment.*** For these reporting requirements, penalties can be imposed even if no income tax is due (unlike other penalties). Taxpayers can request abatement of the penalties for reasonable cause.

Other foreign information reporting

Under Code Sec. 6038, U.S. persons (U.S. citizens or residents) must file Form 5471, Information Return of U.S. Persons with Respect to Certain Foreign Corporations. The categories of persons required to file are extensive, but generally depend on either stock ownership or position held with the corporation or both. Under Code Sec. 6038A, U.S. corporations must file Form 5472, Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business, if the corporation engaged in a "reportable transaction" (not a tax shelter-type transaction).

A penalty of $10,000 can apply for each late or incomplete form. Penalties can increase up to $50,000 if the failure to report continues after notice of the need to file. Again, in both cases, penalties can apply if no income tax is due. Taxpayers can request waiver of penalties based on reasonable cause.

- ***Comment.*** Civil penalties for failing to file either Form 5471 or 5472 may

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WASHINGTON REPORT *by the Wolters Kluwer Washington News Bureau*

Congress returns for year-end tax work

Lawmakers have returned to Capitol Hill after their Thanksgiving recess with tax-related items high on the agenda. A conference agreement on a multi-year highway bill is being negotiated. The conference agreement could include some tax measures, such as authorizing the IRS to contract with private collection agencies to collect tax debts and denying or revoking U.S. passports to individuals with delinquent tax liabilities. House and Senate appropriators continue to negotiate a fiscal year (FY) budget for the IRS. A temporary funding bill is scheduled to expire in mid-December. Also on the agenda are the tax extenders. A tax extenders bill has been approved by the Senate Finance Committee and awaits action by the full Senate. Unless extended, a host of popular but temporary tax incentives will be unavailable for 2015.

Biofuel industry expresses concern about changes to extender

The U.S. biofuel industry recently expressed concern about possible changes to the biodiesel and renewable diesel blenders tax credit. In a letter to the House Ways and Means Committee and the Senate Finance Committee, the industry noted that since 2005 there has been a biodiesel and renewable diesel blenders tax credit of $1.00 for each gallon of biodiesel or renewable diesel used in a qualified mixture. This tax credit expired at the end of 2014. Pending legislation would extend biodiesel and renewable diesel tax credit for two years but, starting in 2016, convert the credit from one for blenders (those who make biodiesel mixtures) to one for those who produce biodiesel and renewable diesel. The credit would also be unavailable to imported biodiesel or renewable diesel. "Converting the tax credit to a producer's tax credit and denying its availability to imported fuels will benefit a small group of biodiesel producers and come at the expense of fuel retailers and consumers," the industry cautioned.

HHS proposes clarifications to individual mandate hardship exemption

The U.S. Department of Health and Human Services (HHS) has proposed to permit any applicant for insurance through the Health Insurance Marketplace, whose gross income is below the filing threshold, to qualify for a hardship exemption and claim the exemption through the tax filing process. Generally, hardship exemptions require an exemption certificate to be issued by the Marketplace. HHS also proposed to allow individuals eligible for services from an Indian health care provider to claim a hardship exemption through the tax filing process. Under the Affordable Care Act (ACA), all individuals must carry minimum essential health coverage or make a shared responsibility payment, unless exempt.

HHS also proposed to increase options for employees in the Small Business Health Options Program (SHOP). Under current regulations, employers participating in the federal SHOP Marketplace can offer their employees either one health plan and/or one dental plan, or all health and dental plans across one metal level (or actuarial value, for dental plans). Under the proposal, employers would be able to offer all plans across all levels of coverage from one insurance company.

TIGTA reviews penalties for failing to provide wage information

The Treasury Inspector General for Tax Administration (TIGTA) has found that the IRS did not always assess penalties against employers that failed to respond to the Service's requests to resolve discrepancies related to the wage information the employers reported to the Social Security Administration (SSA) and the IRS. The Combined Annual Wage Reporting (CAWR) Program ensures that employers submit Forms W-2 and W-3 to both the SSA and the IRS so that employees' Social Security accounts can be properly credited and the proper income and employment tax withholding amount can be collected from employers. "Discrepancies in the wages credited to an individual's Social Security account may affect the amount of Social Security benefits available to the employee upon retirement," Treasury Inspector General for Tax Administration J. Russell George said in a statement.

According to TIGTA, the IRS had not established a process to identify cases associated with the discrepancies and, as a result, the IRS did not correctly assess more than $200 million in penalties on 32 cases for tax year 2011. In addition, TIGTA reported that the IRS excluded 22,814 of 134,937 cases referred from the SSA. Of the 22,814 cases, the IRS indicated that 608 cases were erroneously excluded because of computer programming errors. As a result, the IRS did not assess more than $22 million in penalties.

Payment card reporting improvements could help reduce tax gap

The Treasury Inspector General for Tax Administration (TIGTA) found that improvements are needed by the IRS in the implementation of payment card reporting requirements. TIGTA discussed how the IRS uses Forms 1099-K, Payment Card and Third Party Network Transactions, to reduce the tax gap (the difference between what taxpayers owe and what they actually pay). According to TIGTA, the IRS recognized the challenges associated with using Forms 1099-K to identify noncompliance with income reporting and implemented initiatives to address these challenges.

In 2008, Congress passed and President Bush signed into law the *Housing and Economic Recovery Act of 2008.* The Act created Code Sec. 6050W, requiring information returns to be filed for reportable payment transactions. In response, the IRS developed Form 1099-K.

Some payers are not compliant with backup withholding requirements, TIGTA found. Its review of calendar year 2013 identified 10,216 Forms 1099-K with a missing Taxpayer Identification Number (TIN) and 2,933 Forms 1099-K for which the payee TIN was that of a deceased individual.

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also be abated under the IRS's "First Time Abate" (FTA) policy.

- ***Comment.*** An additional consequence is that if the taxpayer fails to provide information about certain cross-border transactions, the assessment period for the entire return stays open. However, if there is reasonable cause for the failure to file, the assessment period only stays open for the particular form itself.

First-time abatement

Under IRM 20.1.1.3.6.1, a penalty can be abated under FTA if the taxpayer is a first-time filer or if the taxpayer has been compliant in the prior three years and is current with federal tax filing and payment obligations. The IRM states that the taxpayer should be given the opportunity to get current, if needed. The compliance requirement applies for the same type of tax.

FTA relief may be available, for example, for penalties under Code Sections 6651 (individual's failure to file or pay); 6656 (failure to deposit taxes); 6698 (partnership failure to file); and 6699 (S corporation failure to file). Relief is not available or event-based filings, like Forms 706 (estate taxes) and 709 (gift taxes).

FTA relief can only be obtained once. Practitioners can request both FTA relief and reasonable cause relief. While the IRS suggests using FTA relief first, others recommend that practitioners seek reasonable cause relief first. This allows the taxpayer to reserve the use of FTA relief for a later situation that may not be as sympathetic and might not qualify for reasonable cause relief.

Reasonable cause

Many penalties can be waived for reasonable cause. Reasonable cause is determined by the facts and circumstances. Facts include the taxpayer's reason for missing a deadline, the taxpayer's compliance history, the elapsed time until compliance, and whether circumstances are beyond the taxpayer's control. Examples of reasons for failing to comply include reliance on professional advice, and an honest misunderstanding of the taxpayer's responsibilities.

Reasonable cause may vary, depending on the violation. For failures to file or to pay under Code Sec. 6651, one test is whether the taxpayer exercised ordinary business care and prudence. If the taxpayer paid the tax with a return on extension, there is a presumption that the taxpayer had reasonable cause. Facts and circumstances include examining the taxpayer's efforts to meet the obligation. For a failure to pay on time, factors could include whether the taxpayer's spending was reasonable or lavish, and whether the taxpayer's assets were liquid. Under Code Sec. 6724, information reporting penalties may be waived for reasonable cause for significant mitigating factors or because of events beyond the taxpayer's control, and the taxpayer acted in a responsible manner.

For some violations, the standard is stricter. For understatements stemming from a reportable transaction, a taxpayer has reasonable cause if the taxpayer had substantial authority for the position and a reasonable belief that the treatment on the return is "more likely than not" the proper treatment. However, relief for reasonable cause is not available if the transaction was not disclosed or if the transaction lacked economic substance.

Accuracy-related penalties

Accuracy-related penalties can be steep. Under Code Sec. 6662, they can amount to 20 percent of an underpayment that is attributable to negligence or disregard of rules or regulations, a substantial understatement of tax, a substantial valuation misstatement, or a substantial estate or gift tax valuation understatement. The penalties can increase to 40 percent for a disallowance of tax benefits because of a transaction that lacks economic substance, an undisclosed foreign financial asset understatement, or a gross valuation misstatement.

- ***Comment.*** Negligence is a failure to make a reasonable attempt to comply with the tax code; disregard means any careless, reckless, or intentional disregard.

Under Code Sec. 6662A, a 20-percent penalty can apply to a reportable transaction understatement. This penalty can rise to 30 percent if the relevant facts are not adequately disclosed.

- ***Comment.*** Only one of these penalties may apply; they are not stacked. If the taxpayer does not owe any taxes, there is no penalty.

Significantly, a penalty is waived under Code Sec. 6662 or 6662A if there was reasonable cause for the underpayment and the taxpayer acted in good faith. This penalty relief does not apply to transactions lacking economic substance. For a reportable transaction understatement, the taxpayer also must adequately disclose the relevant facts, there must be substantial authority for the treatment, and the taxpayer reasonably believed that the treatment was more likely than not justified.

A substantial understatement of income tax is the greater of $5,000 or 10 percent of the tax required to be shown. The amount of the understatement is reduced (and therefore may not be substantial) for the understatement amount stemming from the tax treatment of an item that is "adequately disclosed" and there was a reasonable basis for the tax treatment; or, if there was substantial authority for the taxpayer's treatment. However, these relief provisions do not apply if the item is attributable to a tax shelter, defined as an entity or arrangement with a significant purpose of avoiding or evading federal income taxes.

Adequate disclosure

Adequate disclosure is described in Reg. §1.6662-4(f). A taxpayer must disclose all relevant facts about the tax treatment of an item or a position. The disclosure must be made on Form 8275, Disclosure Statement, or Form 8275-R, Regulation Disclosure Statement, and must be attached to the return. Disclosure of an uncertain tax position on Schedule UTP will satisfy the requirement to file Form 8275 or 8275-R.

For some items, the IRS issues an annual revenue procedure that prescribes the circumstances for adequate disclosure in accordance with applicable forms and instructions. An item that is not listed in this revenue procedure must be disclosed on the Form 8275 or 8275-R.

- ***Comment.*** Rev. Proc. 2015-16 applies for 2014 income tax returns. For example, for personal taxes, taxpayers must supply all information required on Lines 5 through 9 of Schedule A and list the tax and amount paid on Line 8.

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COMPLIANCE CALENDAR

December 4
Employers deposit Social Security, Medicare, and withheld income tax for November 28, 29, 30, and December 1.

December 9
Employers deposit Social Security, Medicare, and withheld income tax for December 2, 3, and 4.

December 10
Employees who received $20 or more in tips during November report them to their employers using Form 4070.

December 11
Employers deposit Social Security, Medicare, and withheld income tax for December 5, 6, 7, and 8.

December 16
Employers deposit Social Security, Medicare, and withheld income tax for December 9, 10, and 11.

December 18
Employers deposit Social Security, Medicare, and withheld income tax for December 12, 13, 14, and 15.

TRC TEXT REFERENCE TABLE

The cross references at the end of the articles in Wolters Kluwer Federal Tax Weekly (FTW) are text references to Tax Research Consultant (TRC). The following is a table of TRC text references to developments reported in FTW since the last release of New Developments.

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CONFERENCES

December 8–9: The University of Cincinnati presents its 48th Annual Income Tax Conference in Cincinnati, Ohio. Expert practitioners and IRS speakers will cover the new legislative changes, business taxation, individual income tax issues, and more. For more information, or to register, visit *www.business.uc.edu/taxconference* or call (513) 558-1810.

December 11: Wolters Kluwer, presents a webinar "TIN Matching to Reduce Your B-Notices and Eliminate Proposed Penalties." Attendees will learn how to ensure proper compliance with W-9 checking as well as steps to ensure that a company's Forms 1099 include accurate information. For more information, visit *www.krm.com/cch* or call (800) 775-7654.

December 17: Wolters Kluwer, presents a webinar, "Using CCH® IntelliConnect to Conduct International Tax Research." For more information, visit *www.krm.com/cch* or call (800) 775-7654.

December 17–18: The George Washington University Law School presents its 28th Annual Institute on Current Issues in International Taxation in Washington, D.C. Senior government speakers and expert practitioners will discuss new challenges for multinational corporations regarding anti-base erosion and profit shifting measures, cross-border transactions, and foreign tax credits among other topics. For more information visit *www.tggroup.com/GWUIRSInstitute* or call (202) 492-8278.

January 28, 2016: The District of Columbia Bar Taxation Section hosts its program, "Top 10 Estate Planning Developments in 2015 and How They Impact Your Practice In 2016." For more information, visit *www.dcbar.org*.

January 28–30: The American Bar Association Section of Taxation hosts its 2016 Midyear Meeting in Los Angeles. Expert practitioners and IRS speakers will discuss the latest federal tax policies, initiatives, regulations, legislative forecasts and planning ideas. For more information, or to register, visit *americanbar.org*.