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IRS Nixes Proposed Regs On Optional Reporting By Charitable Organizations

NPRM REG-138344-13, Withdrawal

In response to concerns from some in Congress and the nonprofit community, the IRS has withdrawn proposed regs (NPRM REG-138344-13) providing an optional reporting procedure for donees to substantiate certain charitable contributions. The proposed regs would have implemented the statutory exception to the contemporaneous written acknowledgment requirement for substantiating charitable contribution deductions of $250 or more.

- ***Take Away.*** "The Treasury Department and the IRS wisely withdrew their proposed gift substantiation rules after hearing from almost 38,000 Americans who filed comments in opposition to the proposal," Tim Delaney, president and CEO, National Council on Nonprofits, told Wolters Kluwer. "Consultation in advance would have prevented this flawed rulemaking."
- ***Comment.*** In December 2015, the IRS issued a statement intended to clarify that the proposed regs would not impose mandatory changes to current rules on how charities substantiate contributions. "Charities could continue doing things as they do now." The statement apparently failed to assuage concerns about the proposed regs.

Background

Generally, taxpayers must obtain a contemporaneous written acknowledgment from the charitable organization indicating the amount of the cash and a description of any property contributed for any contribution of $250 or more (including contributions of cash or property). The acknowledgment must describe whether the charitable organization provided any goods or services in exchange for the gift and, if so, must provide a description and a good faith estimate of the value of those goods or services. One document from the charitable organization may satisfy both the written communication requirement for monetary gifts and the contemporaneous written acknowledgment requirement for all contributions of $250 or more.

In Code Sec. 170(f)(8)(D), Congress provided an exception to the contemporaneous written acknowledgment requirement. Generally, a contemporaneous written acknowledgment would not be required if the charitable organization files a return on a form and in accordance with regs as the IRS would issue.

The IRS issued proposed regs on the Code Sec. 170(f)(8)(D) exception in 2015. The proposed regs generally provided a method of information reporting for qualified contributions of $250 or more that would have included the donor's name, address, and taxpayer identification number/Social Security number ("Donee Report").

- ***Comment.*** According to the IRS, some taxpayers have taken the position that an amended Form 990, Return of Organization Exempt from Income Tax, constitutes permissible donee reporting under Code Sec. 170(f)(8)(D). The IRS disagreed. "Form

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IRS Clarifies Treatment Of Retroactive Increase In Excludable Transit Benefits For FICA Taxes And W-2 Reporting

Notice 2016-6

The IRS has clarified how employers should address the retroactive increase for periods after 2014 in the monthly exclusion for transit passes and van pooling benefits under the *Protecting Americans from Tax Hikes Act of 2015* (PATH Act). The IRS also provided a special administrative procedure for employers to make adjustments on their Forms 941, Employer's Quarterly Federal Tax Return, filed for the fourth quarter of 2015, and in filing Forms W-2, Wage and Tax Statement.

- ***Take Away.*** Before the year-end tax legislation, the adjusted maximum monthly excludable amount for 2015 for the aggregate of transportation in a commuter highway vehicle and any transit pass was $130; and the adjusted maximum monthly excludable amount for qualified parking was $250. The year-end tax legislation, however, retroactively enacted parity between the two amounts for the 2015 tax year. Therefore, the maximum monthly excludable amount for the period January 1, 2015, through December 31, 2015, is $250 for transit passes and van pool benefits and also $250 for qualified parking. For 2016, the monthly exclusion for each benefit is $255. However, there is no mandate that employers provide additional transit benefits to their employees for 2015.

Notice 2016-6

The IRS explained that any transit benefits (the aggregate benefit for transit passes and van pooling) provided in 2015 by an employer to an employee in excess of $130 and up to $250 is excluded from the employee's gross income and wages. (The Notice refers to this additional $120 as "excess transit benefits.") The exclusion applies whether the employer provided the transit benefits out of its own funds or whether the transit benefits were provided through salary reduction arrangements.

With regard to transit benefits provided pursuant to compensation reduction arrangements, the guidance clarifies that employees may not retroactively increase their compensation reduction for 2015 to take advantage of the increase in the excludable amount for transit benefits in 2015. In addition, employees may not reduce their compensation by more than $255 per month in 2016 to make up for any permissible reimbursement of transit benefits incurred in 2015.

Special procedure

Employers that treated "excess transit benefits" as taxable wages and that have not yet filed their fourth quarter Form 941 for 2015 should repay or reimburse their employees the over-collected FICA tax on the excess transit benefits for all four quarters of 2015, on or before filing the fourth quarter Form 941, the IRS explained.

The employer, in reporting amounts on its fourth quarter Form 941, may reduce the fourth quarter wages, tips and compensation reported on line 2; taxable Social Security wages reported on line 5a; and Medicare wages and tips reported on line 5c, and taxable wages and tips subject to Additional Medicare Tax withholding reported on line 5d by the excess transit benefits for all four quarters of 2015.

Employers that have filed the fourth quarter Form 941 must use normal procedures and must file Form 941-X, Adjusted Employer's Quarterly Federal Tax Return or Claim for Refund to make an adjustment or claim a refund for any quarter in 2015, the IRS explained. Similarly, employers that, on or before filing the fourth quarter Form 941, did not repay or reim-

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Regs Withdrawn

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990 is an unsuitable reporting method for this purpose and may not be used to effectuate donee reporting." The proposed regs, the IRS explained, were intended to end the use of Form 990 for this purported purpose.

Almost immediately after the proposed regs were released, concerns arose. Many charitable organizations expressed concerns about the information reporting requirements, particularly Social Security Numbers from donors. Legislation (Sen. 2370) to block the proposed regs was introduced in Congress.

Regs withdrawn

The IRS reported it received a substantial number of comments on the proposed regs, many expressing concern about safeguarding Social Security numbers and donors' privacy. The IRS decided to withdraw the proposed regs and not implement the statutory exception to the contemporaneous written acknowledgment requirement. The IRS emphasized that the exception under Code Sec. 170(f)(8)(D) remains unavailable unless and until final regs are issued prescribing the method for donee reporting.

References: FED ¶46,228; TRC INDIV: 51,454.10.

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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Tax Court Reversal: Taxpayers Can Claim Losses By Mark-to-Marking Currency Options Under Code Sec. 1256

Wright, CA-6, January 7, 2016

Reversing the Tax Court, the Sixth Circuit Court of Appeals has concluded that a foreign currency option involving a major currency (e.g. euros) qualified as a foreign currency contract under Code Sec. 1256. By following the mark-to-market rules that apply to Code Sec. 1256 contracts, the taxpayers could claim a substantial capital loss when they disposed of the option.

- ***Take Away.*** The Sixth Circuit relied on the plain language of the statute for its analysis. It noted that the Tax Court's reasoning may have been supported by sound tax policy but conflicted with the statute's plain language. Although the transaction was designed to generate a substantial tax loss at little economic risk, the concern for tax policy does not justify reforming the statutory language.

Background

The taxpayers, a married couple, decided to pursue an investment opportunity involving major-minor foreign currency options. Another company set up the transactions and acted as counterparty. The taxpayers purchased four offsetting options involving foreign currencies. They purchased a currency put option (giving the purchaser the right to sell currency) for a premium of $36 million; this gave them the right to sell 1.2 billion euros (a "major" currency traded through regulated futures contracts) for $1.26 billion. They also purchased a euro call option (giving the purchaser the right to buy currency) with mirror terms. The taxpayers also purchased similar put and call options in Danish krone, which they claimed is a minor currency.

Three days after the initial transactions, the taxpayers assigned the euro and krone put options to a charity (arranged by the counterparty). The taxpayers and the counterparty also closed old the euro and krone call options. If one option appreciated in value, the mirror option would decline in value. Shortly after purchase, the euro put option and the krone put option were each worth $33 million.

Taxpayer reporting

The taxpayers treated the transfer of the euro put options to charity as a disposition that triggered the mark-to-market rules for recognizing gain or loss under Code Sec. 1256. They thus recognized a $3 million short-term capital loss on their tax return.

- ***Comment.*** The other option transactions generated a small short-term loss (approximately $25,000) that they reported.

The IRS claimed that the currency options were not Section 1256 contracts and were not subject to the mark-to-market rules; thus, the taxpayers could not claim the $3 million loss.

Law

Under Code Sec. 1256, holders of certain derivative contracts must mark-to-market their "Section 1256 contracts" at the end of the year by treating them as having been sold at fair market value. The mark-to-market rules also apply to a termination or transfer during the year.

A foreign currency contract is a "Section 1256 contract." A foreign currency option allows the obligated party to settle the contract in cash, without delivering foreign currency. The taxpayers claimed that an over-the-counter option in a major currency is a foreign currency contract that can be marked-to-market.

Under the major-minor tax shelter, the taxpayer buys offsetting put and call options in both a major and a minor currency. By donating a depreciated option

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Transit Benefits

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burse employees who received excess transit benefits in 2015 must use Form 941-X.

Forms W-2

Employers that have not furnished 2015 Forms W-2 to their employees should take into account the increased exclusion for transit benefits in calculating the amount of wages reported in box 1, Wages, tips, other compensation; box 3, Social Security wages; and box 5, Medicare wages and tips, the IRS explained. Employers that have already filed 2015 Forms W-2 should file Form W-2c, Corrected Wage and Tax Statement.

References: FED ¶46,231; TRC COMPEN: 36,350.

Chief Counsel Will Assert Penalties Based On Disallowed Refundable Credits, Following Change In PATH Act

IRS Chief Counsel has advised its attorneys to calculate accuracy-related or fraud penalties under Code Secs. 6662 and 6663 by taking into account the amount of any disallowed refundable credits to determine the tax shown on the return. As a result, attorneys should not concede penalties under those provisions if the statutory notice of deficiency asserted penalties on those amounts, Chief Counsel explained.

PATH Act. The notice reverses the approach taken previously by Chief Counsel (CC-2014-007) and by the Tax Court in *Rand, 141 T.C. 376 (2013)*. Chief Counsel made the change because Sec. 209(a) of the *Protecting Americans from Tax Hikes Act of 2015* (PATH Act) amended Code Sec. 6664(a) to require that disallowed refundable tax credits be taken into account and can reduce the tax shown on the return below zero, for calculating the underpayment of tax subject to penalty. The change is effective for all returns filed after December 18, 2015, and all returns filed on or before that date for which the statute of limitations has not expired.

CC-2016-004; TRC PENALTY: 3,104.05.

IRS Provides Some Penalty Relief To Education Institutions For Missing TINs

Ann. 2016-3

Eligible educational institutions may qualify for penalty relief if they fail to include a student's correct taxpayer identification number (TIN) on Form 1098-T, Tuition Statement, for the 2015 calendar year. Relief is available from penalties under Code Sections 6721 and 6722 to eligible educational institutions.

- ***Take Away.*** The penalty relief applies only to eligible educational institutions. Relief is not available to insurers required to file Forms 1098-T under Code Sec. 6050S(a)(2) or to persons engaged in the business of servicing student loans and obligated under Code Sec. 6050S(a)(3) to report on Form 1098-E student loan interest aggregating $600 or more for a calendar year.

Background

Code Sec. 6050S(a)(1) generally requires eligible educational institutions to file Form 1098-T with the IRS and provide written statements to taxpayers relating to qualified tuition and related expenses paid to or billed by the institution. Eligible educational institutions must include the TIN of any individual who is enrolled at the institution.

A Code Sec. 6721 penalty may be imposed where an eligible educational institution fails to file correct and/or timely information returns with the IRS. A Code Sec. 6722 penalty may be imposed on an eligible educational institution that fails to provide correct and/or timely written statements to the student. Both penalties may be waived if failure was due to reasonable cause and not willful neglect.

Congress revised the penalty framework in the *Trade Preferences Extension Act of 2015.* A penalty under Code Sec. 6721 or Code Sec. 6722 may not be imposed on an eligible educational institution solely by reason of failing to include an individual's TIN on a Form 1098-T or related statement if the institution contemporaneously certifies that it has complied with IRS for obtaining the TIN. The 2015 Trade Act applies to returns required to be made and statements required to be provided after December 31, 2015.

Relief

The IRS reported that it is unable to make the necessary programming and related changes for the penalty provisions under the 2015 Trade Act for the 2015 calendar year. As a result, penalties under Code Sec. 6721 or 6722 will not be imposed against an eligible educational institution that timely files or furnishes 2015 Forms 1098-T or statements with missing or incorrect TINs during 2016.

- ***Comment.*** The IRS cautioned that the penalty relief does not apply to other failures by an eligible educational institution subject to Code Sec. 6721 or Code Sec. 6722 penalties.

References: FED ¶46,228; TRC PENALTY: 3,202.05.

Losses

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in the major currency, the taxpayer can claim a loss under Code Sec. 1256. Because the option in the minor currency is not a Section 1256 contract, the taxpayer does not have to recognize any gain until the option terminates.

Court's analysis

Under the taxpayer's interpretation of Code Sec 1256, the taxpayer can obtain a large tax loss with minimal economic risk, the Sixth Circuit noted. The IRS claimed that a foreign currency contract must require either delivery of currency or settlement of the contract in the foreign currency. The options did not do either.

However, the court observed, the plain language of Code Sec. 1256 treats a contract as a foreign currency contract as long as "the settlement of [the contract] depends" on the value of a foreign currency. Based on this plain language, the appeals court concluded that the taxpayers' options satisfied this requirement and were Section 1256 contracts.

- ***Comment.*** The Sixth Circuit noted that reforming the language might unintentionally permit other tax-avoidance schemes. Instead, the IRS can address the transaction either by issuing regs to exclude foreign currency options from Code Sec. 1256, or by challenging the transactions economic substance under Code Sec. 7701(o).

References: 2016-1 USTC ¶50,137; TRC SALES: 48,100.

IRS Updates Determination Letter/Ruling Procedures For Private Foundation Status

The IRS has issued its annual update to the procedures for the issuance of determinations and letter rulings for private foundation status, operating foundation status, and exempt operating foundation status under Code Secs. 509(a), 4942(j)(3), and 4940(d)(2). Language indicating that an organization could request a letter ruling from the Associate Chief Counsel (Tax Exempt and Government Entities (TE/GE)) that a given change in facts and circumstances will not adversely affect exempt status has been removed. Under Rev. Proc. 2016-3, Associate Chief Counsel (TE/GE) will not issue this type of letter ruling.

Rev. Proc. 2016-10; FED ¶46,229; TRC EXEMPT: 21,208.15.

Exchange Of Property Was Tax-Free Under Code Sec. 1031, Even Though Property Did Not Generate Profits

CCA 201601011

IRS Chief Counsel has determined that a company's exchange of aircraft was tax-free under Code Sec 1031 because the aircraft were held for productive use in a trade or business. The aircraft qualified because they were leased to a related company that operated and used the aircraft in a legitimate profit-making business.

- ***Take Away.*** Chief Counsel considered the overall legal structure of the business enterprise and concluded that assets maintained in a separate entity that did not generate a profit still qualified under Code Sec. 1031 as property held for productive use in a trade or business.

Background

Partnership P owns multiple aircraft that are leased to Partnership O. The aircraft are used by two of O's senior executives (A and B) for business and personal purposes. A and B own interests in O, and also own 100 percent of P.

P engaged in an exchange of aircraft. P leases the aircraft through "dry leases", under which the lessee provides the flight crew and other aircraft services. The lease payments for the relinquished aircraft approximated the planes' fair market rental value, while the lease payments for the replacement aircraft were below market. In both cases, the lease payments covered the aircrafts' carrying costs, but did not generate meaningful economic profit.

The IRS exam team claimed that the aircraft were not held for productive use in a trade or business, relying on Code Sec. 183. Exam also argued that the profit motive of one entity should not be attributed to a related entity.

Chief Counsel's analysis

Whether property is held for productive use under Code Sec. 1031 is a question of fact. While Code Sec. 183 limits deductions by an individual or S corporation engaging in an activity without a profit motive, the standards of Code Sec. 183 do not apply Code Sec. 1031 to determine whether property is held for productive use in a trade or business.

Many businesses hold property, especially aircraft, in a separate entity. Even though the property may not generate profit, the property is held for productive use in that business. Here, the aircraft are owned by P, a related entity, not by O, the entity that uses them. If O owned the aircraft, or was 100 percent owner of P, the exam team probably would not have raised the issue. Here, P's lack of intent to make an economic profit on the aircraft rental does not establish that the aircraft fail the productive use standard of Code Sec. 1031.

Were the IRS to disallow tax-free treatment under Code Sec. 1031, businesses would be forced to structure their transactions in inefficient and potentially risky ways to achieve Code Sec. 1031 treatment. For business and legal reasons, O has structured its affairs so that the aircraft are separately owned and then leased to O. On these facts, Chief Counsel concluded, the aircraft are held for productive use in a trade or business.

Reference:TRC PART: 39,206.10.

Tax Court Rejects Collateral Estoppel Argument Over Question Of Gifts

Blagaich, TC Memo. 2016-2

The Tax Court has rejected a taxpayer's argument that the IRS should be collaterally estopped from re-litigating the question of whether money and property she received from her ex-boyfriend was a gift. The IRS, the Tax Court held, was not a party to the litigation over this issue in a state court.

- ***Take Away.*** The taxpayer raised collateral estoppel as an affirmative defense. The taxpayer also raised the rescission doctrine to try to "turn back the clock."

Background

In 2010, the taxpayer and her boyfriend entered into a written agreement intended to confirm their commitment to each other. The agreement provided that the boyfriend would make an immediate payment of $400,000 to the taxpayer. Previously, the boyfriend had provided some $700,000 in cash and property to the taxpayer.

One year later, the boyfriend sent the taxpayer a notice of termination of their agreement. The now ex-boyfriend filed a civil suit seeking return of all the cash and property he had given to the taxpayer. The trial court found that some of the cash and property were gifts to the taxpayer.

The ex-boyfriend filed a Form 1099-MISC, Miscellaneous Income, reporting that he had paid the taxpayer over $700,000 in 2010. Post-trial a revised Form 1099-MISC was filed reflecting the court's decision that some of the $700,000 constituted gifts to the taxpayer.

Court's analysis

Collateral estoppel, the court explained, precludes parties (and their privies) from relitigating issues litigated and decided in a final prior judgment by a court of competent jurisdiction. Here, the IRS was not

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Tax Court Rejects Taxpayer's Attempts To Reduce Taxable Gain On Merger Transaction

Tseytin, TC Memo. 2015-247

The Tax Court has rejected a taxpayer's arguments for reducing the taxable gain recognized on a merger from $17.3 million to $9.1 million. The taxpayer was taxable on all the proceeds received for the stock transferred in the merger, and could not claim that an unrelated third party was taxable on a portion of the proceeds.

- ***Take Away.*** The taxpayer was not taxable on all the proceeds received, involving an exchange of stock for stock. He was taxable on the cash received as boot in the merger.

Background

The taxpayer owned 750 of the 1000 shares outstanding in a New Jersey corporation. These shares had a zero basis. An unrelated third party owned the other 250 shares. The taxpayer purchased the 250 shares for $14 million. He then merged the corporation into an unrelated Netherlands corporation, by transferring the 1,000 shares for approximately $54 million. He received cash of $23.1 million and shares in the Dutch company worth $30.8 million. Treating the 750 shares and the 250 shares as separate blocks of stock, the taxpayer realized a short-term capital loss of $527,000 on the 250 shares, and a long-term capital gain of $40.4 million on the 750 shares.

Taxpayer's tax returns

On his original tax return, the taxpayer treated the 1,000 shares of stock as one block of stock. He treated the $23.1 million cash payment as taxable, but reduced it by approximately $6 million, based on the cost for the 250 shares. Consequently, he reported taxable long-term gain or $17.1 million and tax due of $3.78 million.

The taxpayer then filed an amended return, treating the two groups of shares as separate blocks. On the 750 shares, he reported a long-term gain of $17.3 million; on the 250 shares, he reported a short-term loss of $8.2 million. He netted these amounts and reported a net long-term capital gain of $9.1 million and taxes due of $2.6 million.

The IRS treated the shares as two different blocks. It determined that the taxpayer realized long-term gain of $40.4 million on the 750 shares and should recognize taxable gain of $17.3 million from the receipt of cash. The taxpayer realized a short-term loss of $527,000 on the 250 shares. The recognized gain of $17.3 million could not be netted with the realized loss of $527,000. As a result, the taxpayer was liable for $3.81 million in taxes, a deficiency of $30,000 from the original return, and an accuracy-related penalty of $6,000.

Court's analysis

The Tax Court agreed with the IRS. It rejected the taxpayer's claim that he was not the true owner of the 250 shares and should not be taxed on the $14 million paid for those shares. Taxpayers cannot disregard a transaction's form of their own making unless there was some fraud or mistake. Thus, he was taxable on the portion of the cash boot allocable to those shares.

The court determined that the taxpayer cannot internally net gains and losses from different blocks of stock. Furthermore, losses realized on one block cannot be netted against gains realized and recognized from another block of stock. The court also agreed with the IRS that the taxpayer was liable for a penalty on his original return for treating the 1,000 shares as one block of stock.

References: Dec. 60,478(M); TRC CCORP: 12,202.05.

IP PIN Notices With Incorrect Tax Year Still Valid, IRS Instructs

The IRS has mailed Identity Protection Personal Identification Number (IP PIN) notices to taxpayers referencing the incorrect tax year. However, the IRS advised taxpayers that the IP PIN is valid for use in 2016.

Background. The IRS assigns IP PINs (a six-digit number) to eligible taxpayers. The IP PIN verifies a taxpayer's identity. The IRS generally provides IP PINs to individuals who reported that they are victims of identity theft, individuals identified by the agency as victims of identity theft, and individuals who participated in a pilot program.

Clarification. Notice CP01A, with a date of January 4, 2016, instruct taxpayers to use the IP PIN for filing 2014 returns. This is incorrect, the IRS cautioned. The IP PIN is valid for filing 2015 returns in 2016, the agency explained.

www.irs.gov; TRC FILEIND: 12,100.

Gifts

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a party to the state court action, nor was it a privy to a party or otherwise sufficiently connected to a party, the court found.

Generally, restoration under the rescission doctrine must be accomplished in the same tax year as the original transaction. According to the court, the taxpayer seemed to argue that the rescission doctrine may apply even when repayment of a gain does not formally occur in the year of receipt, but only if, before the end of the year, the taxpayer recognizes his or her liability under an existing and fixed obligation to repay the amount received and makes provisions for repayment. In this case, there appeared to be no requirement under the agreement for the taxpayer to return any of the money. The taxpayer took the $400,000 in 2010 without any limitations or restrictions. The taxpayer made no provisions to repay the money until three years later.

References: Dec. 60,503(M); TRC ACCTNG: 27,350

Contribution Of Value Of Unused Vacation Leave To 401(k) Plan Or HRA Treated As Employer Contributions; Not Taxable To Employees

LTR 201601012

The IRS has determined that a 401(k) plan and a health reimbursement arrangement (HRA) can be amended to allow employees to elect to contribute the value of unused vacation leave to either the 401(k) or the HRA plans. The amounts contributed will be treated as employer contributions and will not trigger taxation to the employee, under either Code Sec. 402(g) or Code Sec. 105(b) and 106.

- ***Take Away.*** Although employees must make an election so that unused amounts will be transferred, the IRS concluded that the contributions can be attributed to the employer. Therefore, they were not treated as elective employee contributions that are limited by Code Sec. 402(g)(1), and or as employee contributions to an HRA that would be taxable to the employee, instead of being tax-free payments by the employer for medical benefits.

Background

The taxpayer, an employer, maintains two plans, a 401(k) plan and an HRA plan that reimburses medical expenses of retirees. The 401(k) plan allows a participating employee to elect to have the employer make contributions to a trust on behalf of the employee. The HRA is funded through mandatory employee contributions from salary.

Employees also accrue a certain amount of vacation leave each year. Any unused leave cannot be carried over; amounts up to 21 days are forfeited; amounts over 21 days are paid out as regular wages. The taxpayer proposes to amend the two plans to allow each employee to make an irrevocable election to have the taxpayer contribute the dollar equivalent of the unused vacation (up to the 21-day limit) to either the 401(k) plan, the employee's retiree HRA, or to a combination of both. The employee must make the election before the start of the calendar year in which the leave is earned.

If an amount cannot be contributed to the 401(k) plan because of the Code Sec. 401(g) annual limits on contributions, the employer will contribute the excess amount to the retiree's HRA at the same time. If the employee fails to make the election, the unused vacation will be paid as an employer contribution to the 401(k) plan, and any excess will be contributed to the retiree HRA.

IRS's analysis

The IRS noted that unused vacation contributed to the 401(k) plan may only be made available to employees in the future. Employees cannot elect to have the amounts paid currently in cash or as another taxable benefit. Accordingly, the amendment will not cause the 401(k) plan to offer an additional cash or deferred arrangement, and the employer's contributions will not be considered an employee pre-tax contribution subject to the 401(g) limits.

Under Revenue Rulings 2002-41 and 2002-45, contributions to an HRA must be made solely by an employer and not under a salary reduction arrangement. Here, if the employee elects to have unused vacation contributed to the HRA, the amounts are paid solely by the employer and will only be used for retiree medical benefits, the IRS determined. Accordingly, the HRA plan satisfies the two revenue rulings, and the amounts are excludable from the gross income of retired employees under Code Secs. 105(b) and 106, the IRS concluded.

Reference:TRC RETIRE: 3,200.

Wolters Kluwer Projects 2016 Inflation-Adjusted Code Sec. 179 Limitations, Classroom Expense Cap

Based on required inflation-adjustment computations required under the *Protecting Americans from Tax Hikes Act of 2015* (PATH Act), Wolters Kluwer Tax & Accounting US has projected that Code Sec. 179's $500,000 expensing limitation will remain unchanged for 2016, but the overall $2-million investment will increase to $2,010,000 for 2016. The Code Sec. 62(a)(2)(D) classroom expense limit of $250 is projected to remain at the $250 level for the 2016 tax year. The IRS is expected to release official figures shortly.

- ***Comment.*** The PATH Act directs that the Code Sec. 179 limitations be adjusted for inflation for tax years beginning after 2015, subject to rounding. Code Sec. 179(b)(6)(B) requires such inflation adjustment to be based on the cost-of-living adjustment determined under Code Sec. 1(f)(3) for the calendar year in which the tax year begins, but substituting calendar year 2014 for calendar year 1992. It further directs that, when adjusting the dollar limitation or the investment limitation for inflation, the resulting amount must be rounded to the nearest multiple of $10,000. Code Sec. 62(d)(3) requires the same inflation adjustments with respect to the $250 cap on the classroom deduction, but with rounding to the nearest multiple of $50.

TAX BRIEFS

Collection Due Process

An IRS Appeals officer did not abuse his discretion by sustaining a proposed levy and rejecting an individual's offer in compromise or proposing an installment agreement amount. The individual's sought to compromise his tax liabilities and tax shelter promoter penalties; however, his offer did not address his outstanding criminal restitution. Moreover, after the individual rejected the Appeals officer's proposed installment amount, he never made a counteroffer. Therefore, sustaining the levy was not arbitrary, capricious or without sound basis in law.

Rebuck, TC, CCH Dec. 60,504(M), FED ¶47,919(M); TRC IRS: 51,056.15

An IRS settlement officer (SO) did not abuse her discretion by sustaining the filing of a Notice of Federal Tax Lien (NFTL) to collect an individual's outstanding tax liabilities or by rejecting a collection alternative. The taxpayer failed to submit any information to support a collection alternative. Therefore, the SO's rejection of a collection alternative was not arbitrary or capricious.

Baptiste, TC, CCH Dec. 60,505(M), FED ¶47,920(M); TRC IRS: 48,058.10

Practice and Procedure

The government was entitled to reduce an individual's outstanding tax liabilities to judgment, foreclose its tax liens and sell his real property to satisfy the liabilities. The government presented evidence of the individual's outstanding tax liabilities and the arguments the individual raised to disprove those liabilities did not present a genuine issue of material fact.

Short, DC N.C., 2016-1 USTC ¶50,133; TRC IRS: 45,158

Employment Taxes

A garment manufacturer and its temporary, nonresident former employees were not entitled to a refund of Federal Insurance Contributions Act (FICA) taxes and the manufacturer was required to repay an erroneously issued refund. FICA applies to all workers and their employers in the Commonwealth of the Northern Mariana Islands (CNMI) regardless of their citizenship.

F.L. Ai, CA-9, 2016-1 USTC ¶50,132; TRC INTL: 24,200

An individual who worked on advertisements and television commercials as a production assistant was an independent contractor. Production companies generally hired the individual to build sets and individual had a large degree of control as to how to accomplish the projects he was hired to do. The union contracts excluded fixed wages and working conditions from their coverage; these issues were expressly reserved to the workers.

Quintanilla, TC, CCH Dec. 60,506(M), FED ¶47,921(M); TRC COMPEN: 3,102

Losses

A married couple was not entitled to carry over a net operating loss (NOL) generated by the short sale of rental properties owned by their daughter because the loss was not theirs. They were not the real or beneficial owners of the properties that generated the loss and they failed to substantiate the amount claimed. A penalty for substantial understatement was imposed.

Ghafouri, TC, CCH Dec. 60,507(M), FED ¶47,922(M); TRC BUSEXP: 45,050

Summonses

A certified appraiser's petition to quash an IRS summons to produce documents was dismissed for lack of subject matter jurisdiction. The taxpayer failed to show a waiver of sovereign immunity. In addition, Code Sec. 7609(c)(2)(A) did not apply as the summons was unambiguously issued to the taxpayer with respect to his own liability.

Clower, DC Ga., 2016-1 USTC ¶50,135 TRC IRS: 21,104

Tax Crimes

An individual's sentence for mail and wire fraud and filing false tax returns was procedurally reasonable. The district court properly grouped the individual's tax offenses separately from the fraud offenses, the Eleventh Circuit held.

Doxie, CA-11, 2016-1 USTC ¶50,134; TRC IRS: 66,462

Banktruptcy

A bankruptcy court's decision that married debtors' tax liability was dischargeable in bankruptcy because their late-filed returns were "returns" under the Bankruptcy Code was vacated and remanded. The court did not apply the correct legal standard for assessing the honesty and reasonableness of the debtors' efforts to comply with the applicable tax law.

In re Martin, BAP-9, 2016-1 USTC ¶50,136; TRC IRS: 57,150

The government was not equitably estopped from collecting a married couple's delinquent tax liabilities for two tax years. The government's failure to include those two years in its proof of claim in the couple's bankruptcy proceeding as well as a stipulation entered into later stating that the only tax due and owing was a portion of different year's tax liability did not establish affirmative misconduct.

Burrell, CA-9, 2016-1 USTC ¶50,131; TRC LITIG: 9,256

IRS Announces Disaster Relief For Mississippi

The IRS has postponed certain deadlines and will abate certain penalties and interest for taxpayers who reside or have a business in the parts of Mississippi due to severe storms, tornadoes, straight-line winds and flooding that began on December 23, 2015. The counties of Benton, Coahoma, Marshall, Quitman and Tippah in Mississippi have been declared federal disaster areas.

IR-2016-2; FED ¶46,227; TRC FILEIND: 15,204.25.

PRACTITIONERS' CORNER

Sample Client Letter On 2015 Fourth Quarter Federal Tax Developments

The fourth quarter of 2015 brought many tax developments from Washington, the IRS and the courts. Wolters Kluwer has prepared a Fourth Quarter 2015 Federal Tax Developments client letter. Practitioners can email this letter to clients to alert them to some of these important recent developments.

This letter includes references to Federal Tax Weekly. Practitioners can refer to Federal Tax Weekly for more information about these developments, but should delete the references in their communications with clients.

Re: Important 2015 Fourth Quarter Federal Tax Developments

Dear Client:

During the fourth quarter of 2015, there were many important federal tax developments. This letter highlights some of the more significant developments for you. As always, contact our office if you have any questions.

Tax legislation

President Obama signed the *Protecting Americans from Tax Hikes Act of 2015* (PATH Act) and the *Consolidated Appropriations Act* in December. The PATH Act makes permanent a number of tax extenders for individuals and businesses. The PATH Act also extended other extenders (some through 2016 and some through 2019), revised some of the rules for real estate investment trusts (REITs), revised rules for the Tax Court, and more. The *Consolidated Appropriations Act* earmarked an additional $290 million to the IRS to improve customer service and cybersecurity, and better combat tax-related identity theft. *Federal Tax Weekly No. 52, December 31, 2015.*

Also in December, President Obama signed the *Fixing America's Surface Transportation* (FAST) Act, a multi-year highway and transportation spending bill. The FAST Act authorizes the federal government to deny or revoke a U.S. passport to individuals with "seriously delinquent tax debt," mandates that the IRS contracts with private collection agencies to collect some tax debts, extends highway taxes, and more. *Federal Tax Weekly No. 50, December 10, 2015.*

In November, President Obama signed the *Bipartisan Budget Act of 2015,* which repeals the TEFRA unified partnership audit rules and replaces them with streamlined procedures. The 2015 Budget Act also repeals automatic enrollment in certain employer-sponsored health plans and makes a number of pension-related changes. *Federal Tax Weekly No. 45, November 5, 2015.*

"The fourth quarter of 2015 brought many tax developments from Washington, the IRS and the courts."

Affordable Care Act

The PATH Act imposes a two-year moratorium (2016 and 2017) on the Affordable Care Act (ACA) excise tax on qualified medical devices. The *Consolidated Appropriations Act* provides for a two-year delay of the excise tax on high-cost employer-sponsored health coverage (known as "Cadillac plans") and also provides for a one-year moratorium (2017) on the ACA's health insurance provider fee. *Federal Tax Weekly No. 52, December 31, 2015.*

At year-end, the IRS announced an automatic extension of filing deadlines for certain 2015 information returns under the ACA. The extension affects Code Sec. 6055 reporting by insurers, self-insuring employers and other providers of minimum essential coverage and Code Sec. 6056 reporting by applicable large employers (ALEs). The IRS also provided transition relief for individuals who may be impacted by the extension. *Federal Tax Weekly No. 1, January 7, 2016.*

In October, President Obama signed into law the *Protecting Affordable Coverage for Employees Act* (PACE Act). The PACE Act amends the Public Health Service Act to redefine small employer as one with 50 or fewer employees for purposes of the small group health market. The PACE Act also gives states the option to expand the definition to include employers with up to 100 employees for purposes of the small group health market. *Federal Tax Weekly No. 42, October 15, 2015.*

2016 mileage rates

In December, the IRS issued the 2016 optional standard mileage rates used to calculate the deductible costs of operating an automobile for business, medical, moving and charitable purposes. The optional business standard mileage rate for 2016 is 54 cents per mile, a decrease of 3.5 cents compared to 2015. The optional standard mileage rate for medical and moving expenses for 2016 is 19 cents per mile, a decrease of four cents compared to 2015. The optional standard mileage rate for charitable expenses is set by statute and remains at 14 cents per mile. *Federal Tax Weekly No. 52, December 31, 2015.*

Inflation adjustments

In October, the IRS announced that personal and dependency exemptions will increase from $4,000 in 2015 to $4,050 for 2016. Standard deductions will remain the same for 2016, with the exception of the standard deduction for heads of household. For 2016, the amount of itemized deductions that can be claimed will begin to phase out for certain taxpayers whose income exceeds $311,300 (married joint filers); $285,350 (heads of household); $259,400 (single fil-

WASHINGTON REPORT *by the Wolters Kluwer Washington News Bureau*

Ryan highlights plans for 2016

House Speaker Paul Ryan, R-Wisc., said on January 7 that he wants 2016 to be a year of ideas. This means putting together a pro-growth agenda and putting it together quickly, Ryan said at his weekly news conference in Washington, D.C. However, he declined to give any specifics beyond mentioning "lower tax rates."

Ryan also lauded the House's passage on January 6 of the Restoring Americans' Healthcare Freedom Reconciliation Act of 2015 (H.R. 3762). The Senate previously approved the legislation. "If we elect a Republican president we can use this same path to repeal (the Affordable Care Act)," he said.

Brady discusses tax reform

House Ways and Means Committee Chair Kevin Brady, R-Texas, touched on international tax reform at an event in Washington, D.C. on January 11. "We want a fairer, flatter, simpler Tax Code," Brady said. Last year, Brady became chair of the House tax-writing committee after Rep. Paul Ryan, R-Wisc., was elected Speaker of the House. In 2015, Brady supported several permanent extensions of various tax extenders, some of which were made permanent in year-end tax legislation.

Obama vetoes bill repealing ACA

On January 8, President Obama vetoed the Restoring Americans' Healthcare Freedom Reconciliation Act of 2015 (H.R. 3762). The House had approved the bill along party-lines in early January; the Senate had approved the bill last year. In a statement, President Obama said that the bill "earned his veto because of the harm it would cause to the health and financial security of Americans."

IRS holds hearing on Code Sec. 2801 regs

Speakers at an IRS hearing on proposed regulations under Code Sec. 2801 told the IRS that the statute and proposed regs would unfairly and excessively impose heavy taxes on U.S. residents who move abroad. One speaker told the IRS that the statute goes beyond its stated Congressional purpose of retaining tax neutrality and should not be implemented by the IRS until Congress changes the law. Another speaker asked the IRS to use the regs to clarify the interaction between the statute and overlapping treaty provisions that could reduce the impact of the tax.

Code Sec. 2801 imposes a transfer tax on gifts and bequests from individuals who abandon U.S. citizenship or residency and later make a gift or bequest to a U.S. taxpayer. The tax is imposed at a 40 percent rate on the amount transferred. Unlike the estate tax, which currently exempts estates up to $5.43 million (indexed for inflation) from tax, there is no comparable exemption under Code Sec. 2801. Thus, if the transferor is a covered expatriate, the tax applies to any gift or bequest worth more than $14,000 (one gift tax exemption).

Watchdog reviews administration of Code Sec. 36B credit

The Inspector General for the U.S. Department of Health and Human Services (HHS) has issued a report on the administration of the Code Sec. 36B premium assistance tax credit by the Health Insurance Marketplaces. Individuals who enroll in coverage through the Marketplaces may qualify for the Code Sec. 36B credit to help offset the cost of coverage. Generally, individuals and families whose household income for the year is between 100 percent and 400 percent of the federal poverty line for their family size may be eligible for the credit. The credit may be paid in advance to insurers. The Marketplaces determine the amount of advance payments of the credit using the price of the second-lowest-priced silver-level plan available in the area in which the enrollees reside and the enrollees' reported income and family size. During the 2015 filing season, the IRS processed some 1.4 million tax returns that reported approximately $4.4 billion in Code Sec. 36B credits, which were either received in advance or claimed at the time of filing.

The HHS Inspector General met with insurers and officials of the Marketplaces. The HHS Inspector General also interviewed officials with the Treasury Inspector General for Tax Administration (TIGTA) to review how HHS and the IRS work together to administer the credit.

The HHS Inspector General discovered that HHS does not have a process in place to ensure that advance payments of the Code Sec. 36B credit are made only for enrollees who had paid their monthly premiums. HHS relied on insurers to verify that enrollees paid their monthly premiums and to attest that payment information that the insurer reported was accurate.

Swiss bank agrees to penalty

The U.S. Department of Justice (DOJ) announced on January 6 that Swiss Bank Union Bancaire Privee (UBP) has agreed to pay a penalty of $187 million under the Swiss Bank Program. The Swiss Bank Program is intended to provide a route for Swiss banks to resolve potential liabilities with the U.S. related to tax crimes, DOJ explained. Under the program, banks are required to, among other provisions, make a complete disclosure of cross-border activities, provide information on accounts in which U.S. taxpayers have an interest, and pay appropriate penalties.

"The agreement is a significant one," Richard Weber, chief, IRS Criminal Investigation, said in a statement. "UBP, as one of the largest private banks in Switzerland, had nearly 3,000 U.S.-related accounts," Weber reported. UBP mitigated its penalty by encouraging U.S. accountholders to come into compliance with their tax and disclosure obligations. "The agreement marks the final resolution with UBP, which acknowledges its role in conspiring with U.S. taxpayers to evade U.S. taxes through an array of sham entities, structured transactions, nominees, and bank services designed to disguise the true ownership of foreign accounts," Caroline Ciraolo, acting Assistant Attorney General, Tax Division, said in a statement.

Continued from page 21

ers); or $155,650 (married separate filers). *Federal Tax Weekly No. 44, October 29, 2015.*

The IRS also announced that many retirement plan contribution and benefit limit amounts will remain the same for 2016 as for 2015. The 2016 cost of living adjustments (COLAs) affect a wide range of retirement savings vehicles, including defined contribution plans, defined benefit plans, employee stock ownership plans (ESOPs), and individual retirement arrangements (IRAs). *Federal Tax Weekly No. 44, October 29, 2015.*

In October, the Social Security Administration (SSA) announced that the maximum amount of earnings subject to OASDI Social Security tax will remain at $118,500 for 2016, the same as for 2015. For 2016, the domestic employee coverage threshold, as adjusted for a slightly different inflation factor and subject to rounding, will be $2,000, up from $1,900 in 2015. *Federal Tax Weekly No. 43, October 22, 2015.*

Repair regs

The IRS announced in December 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. *Federal Tax Weekly No. 49, December 3, 2015.*

Restaurant/retail

In November, the IRS unveiled a safe harbor method for qualified taxpayers in the restaurant business or retail trades to use to determine if costs paid or incurred to refresh or remodel a qualified building are deductible or must be capitalized. The IRS also described how taxpayers may obtain automatic consent to change to the safe harbor method of accounting. *Federal Tax Weekly No. 48, November 27, 2015.*

International

The IRS issued in December proposed regulations that would require country-by-country (CbC) reporting by U.S.-owned multinational business enterprises (MNEs). Under CbC reporting, the multinational group would be required to provide a report on its business activity in each country where it owns and operates a business entity. *Federal Tax Weekly No. 52, December 31, 2015.*

In October, the IRS reported that disclosures under the Offshore Voluntary Compliance Program (OVDP) and the related Streamlined Filing Compliance Program continue to increase. The OVDP has generated some $8 billion, according to the IRS. *Federal Tax Weekly No. 43, October 22, 2015.*

In September, a federal district court denied a request for a preliminary injunction to prevent the IRS from enforcing the *Foreign Account Tax Compliance Act* (FATCA), the related intergovernmental agreements (IGAs) that supplant FATCA, and the Report of Foreign Bank and Financial Accounts (FBAR) requirement. The court held that the plaintiffs were unlikely to succeed on the merits, because they lacked standing and were not likely to suffer irreparable injury. *Crawford v. Treasury, DC-Ohio, Federal Tax Weekly No. 41, October 8, 2015.*

Same-sex marriage

In December, the IRS provided guidance to retirement plans and health and welfare plans on the Supreme Court's decision in *Obergefell, 2015-1* USTC *¶50,357.* The Supreme Court extended same-sex marriage nationwide. Because same-sex marriages have been recognized for federal tax law purposes since *Windsor, 2013-2* USTC *¶50,400,* the IRS explained that it does not anticipate any significant impact from Obergefell on the application of federal tax law to employee benefit plans. *Federal Tax Weekly No. 51, December 31, 2015; Federal Tax Weekly No. 44, October 29, 2015.*

Employment taxes

In December, the IRS launched a new initiative for employers that appear to have fallen behind in remitting payroll taxes. The "Early Interaction Initiative" is intended to help employers stay in compliance with their payment and reporting obligations. The IRS can impose the Trust Fund Recovery Penalty (TFRP) for willful failure to collect, account for, or pay over employment taxes. *Federal Tax Weekly No. 51, December 17, 2015.*

Tax-related identity theft

In November, the IRS announced that victims of identity theft and refund fraud may obtain copies of bogus returns filed under their names. Victims or their authorized representatives may request copies of fraudulent Forms 1040, 1040A, 1040EZ, 1040NR, or 1040NR-EZ. *Federal Tax Weekly No. 47, November 19, 2015.*

Audit coverage

The IRS reported that 146.8 million individual returns were filed and 1.23 million returns were audited, for an audit rate of 0.84 percent for fiscal year (FY) 2015. Field audits declined from 291,000 in FY 2014 to 267,000 in FY 2015, while correspondence audits increased from 951,000 to 961,000. Examination revenue fell from $12.5 billion in FY 2014 to $7.3 billion in FY 2015. *Federal Tax Weekly No. 46, November 12, 2015.*

Innocent spouse

In November, the IRS issued proposed regulations to revise the existing regulations under Code Sec. 6015, which governs relief from joint and several liability for innocent spouses. The proposed regulations would revise Reg. §1.6015-1 so that a requesting spouse does not need to indicate whether he or she is requesting innocent spouse relief under Code Sec. 6015(b), (c), or (f).*Federal Tax Weekly No. 48, November 27, 2015.*

ABLE accounts

The IRS announced in November some modifications to its proposed regulations on Achieving a Better Life Experience (ABLE) accounts. The year-end tax legislation also tweaked the rules for ABLE accounts. *Federal Tax Weekly No. 48, November 27, 2015; Federal Tax Weekly No. 52, December 31, 2015.*

If you have any questions about these or other federal tax developments, please contact our office.

Sincerely,

COMPLIANCE CALENDAR

January 15

Employers deposit Social Security, Medicare, and withheld income tax for January 9, 10, 11, and 12.

If the monthly deposit rule applies, employers deposit the tax for payments in December 2015.

January 19

The 2016 filing season opens.

January 21

Employers deposit Social Security, Medicare, and withheld income tax for January 13, 14, and 15

January 22

Employers deposit Social Security, Medicare, and withheld income tax for January 16, 17, 18, and 19.

January 27

Employers deposit Social Security, Medicare, and withheld income tax for January 20, 21, and 22.

January 29

Employers deposit Social Security, Medicare, and withheld income tax for January 23, 24, 25, and 26.

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.

ACCTNG 27,350	17	FILEBUS 9,108	574	IRS 12,200	3
ACCTNG 36,162.05	566	FILEIND 12,100	18	IRS 33,302.05	603
ACCTNG 36,162.05	613	FILEIND 15,204.25	20	IRS 60,050	590
BUSEXP 9,092	561	FILEIND 18,052	612	LITIG 6,100	7
BUSEXP 9,104.15	573	FILEIND 18,054	580	LITIG 6,130.35	564
BUSEXP 18,450	588	HEALTH 6,100	613	PART 39,2016.10	15
BUSEXP 18,458	6	HEALTH 6,104	1	PAYROLL 9,104	553
BUSEXP 18,808	579	HEALTH 6,106	599	PENALTY 3,052	611
BUSEXP 24,506.05	611	HEALTH 9,116	614	PENALTY 3,110.25	601
BUSEXP 30,104.05	589	HEALTH 18,000	556	PENALTY 3,202	16
BUSEXP 30,262.50	5	INDIV 6,368	2	PENALTY 3,260.15	589
CCORP 6,054	603	INDIV 33,408	577	PENALTY 9,100	576
DEPR 3,504.05	575	INDIV 51,050	587	PENALTY 9,152	615
DEPR 15,162.85	587	INDIV 51,454.10	13	REAL 12,500	563
DEPR 15,210	575	INDIV 60,054.10	592	RETIRE 9,050	597
ESTGIFT 3,068	602	INTL 18,150	612	RETIRE 51,102.05	602
EXEMPT 21,208.15	16	INTL 30,082.05	562	RETIRE 51,356	4
EXEMPT 21,210	614	INTL 33,054.25	593	SALES 9,104.10	600
FARM 21,176	8	INTLOUT 3,100	565	SALES 48,100	14
FILEBUS 9,104	601	IRS 9,302	3	SALES 51,056.15	588

FROM THE HELPLINE

The following questions have been answered recently by our "Wolters Kluwer Federal Tax Service" Helpline (1-800-344-3734).

Q Should bulk water sales by farmers to the oil & gas companies be reported on Schedule F and subject to Self-Employment Tax?

A The types of income reported on Schedule F generally only include income generated from farming activities. Certain types of income are specifically not reported on Schedule F including, but not limited to, income from the sale or exchange of business property which is generally reported on Form 4797 (*see TRC FARM: 3,150*). Also note that the sale of bulk water may fall under a State's sale and use tax rules or particular sales may be exempt from a State's sale and use taxes. The customer should take a look at the laws of the State where the taxpayer resides for further information.

Q What is the current limit on the Section 179 expensing deduction?

A The Section 179 allowance was scheduled to be reduced from $500,000 per year to $25,000 per year beginning in 2015. However, recent legislation (the *Protecting Americans from Tax Hikes Act of 2015* (PATH Act) made the $500,000 annual limit permanent. That new law also made the limit subject to an annual inflation adjustment starting for the 2016 tax year. Based upon the PATH Act's inflation factors and rounding conventions, Wolters Kluwer Tax & Accounting US projects that the $500,000 will remain at that level for 2016 (the corresponding $2 million level at which point the $500,000 phases-out, however, is projected to increase to $2,010,000 for 2016). Official figures have not yet been released. *See TRC DEPR:12,104.*