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Inside this Issue

IRS Touts Increase In Audits Of Higher Income Taxpayers

◆ *www.irs.gov, IRS news conference*

The IRS audited one in eight individuals with incomes over $1 million in fiscal year (FY) 2011, Deputy Commissioner for Services and Enforcement Steven Miller recently reported. While the overall audit coverage rate for individuals remained steady at just over one percent, the audit coverage rate for higher-income individuals experienced growth in FY 2011. Miller presented the IRS's fiscal year (FY) 2011 enforcement results during a telephone news conference with reporters.

■ ***CCH Take Away.*** "The trend in enforcement is clearly in the direction of increased enforcement dollars," Benson Goldstein, CPA, senior technical manager, American Institute of Certified Public Accountants (AICPA), told CCH. However, this trend could be slowed by IRS budget cuts. Congress appropriated $305 million less for the IRS in FY 2012 compared to FY 2011. During his news conference, Miller said that the IRS's FY 2012 budget reduction "will have an impact" but declined to provide details.

Individuals

The IRS selected 1,564,690 individual returns for examination in FY 2011 compared to 1,581,394 individual returns selected for examination in FY 2010, Miller said. Although there was a slight decline in the number of individual returns selected for audit in FY 2011, the overall audit coverage rate remained at 1.11 percent for FY 2011. The vast majority of individual audits were correspondence audits (1,173,069 in FY 2011), Miller said.

Higher income individuals. The audit coverage rate for individuals with incomes under $200,000 was 1.04 percent in FY 2010 and fell to 1.02 percent in FY 2011. However, the audit coverage rate for individuals with incomes $200,000 and higher increased from 3.10 percent in FY 2010 to 3.93 percent in FY 2011.

Significant gains in audit coverage came in audits of individuals with incomes $1 million or more, Miller reported. The audit coverage rate for those millionaires increased from 8.36 percent in FY 2010 to 12.48 percent in FY 2011.

■ ***Comment.*** Field audits of individuals with incomes $200,000 and higher increased from 58,521 in FY 2010 to 78,392 in FY 2011. Field audits of individuals with incomes $1 million and higher increased from 16,509 in FY 2010 to 20,475 in FY 2011.

Businesses

Examinations of business returns in FY 2011 decreased compared to FY 2010, Miller reported. Overall, the IRS examined 9,869,358 business returns (all types of businesses) in FY 2011. That number was 9,941,289 in FY 2010.

Corporations. Corporations with assets $10 million and higher had the highest audit coverage rate at 17.64 percent in FY 2011 (16.58 percent in FY 2010). Within the large corporation category,

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Route to: ______ ______ ______ ______ ______

Tax Gap Grows To $450 Billion; Compliance Rate Holds Steady

◆*IR-2012-4, FS-2012-6, www.irs.gov*

The "tax gap" climbed from $345 billion in Tax Year (TY) 2001 to $450 billion in TY 2006, the most recent year for which the necessary statistics were available, the IRS has reported. The growth in the tax gap over five years was concentrated in underreporting and underpayment, which jointly accounted for nine out of 10 tax gap dollars, according to the agency. The IRS also reported that despite the increase in the tax gap, the voluntary compliance rate for TY 2006 was statistically unchanged from TY 2001.

■ ***CCH Take Away.*** "It is too soon to measure new compliance efforts and new withholding and reporting rules put in place after the last round of tax gap figures were released," Dustin Stamper, manager, Washington National Tax Office, Grant Thornton, LLP, told CCH. "It will be a few years before we can gauge how well the government's response to the tax gap is working."

Background

The net tax gap, according to the IRS, is the amount of tax liability that is never collected. That is, the net tax gap consists of the amount of tax liability not paid on time (the gross tax gap) that is not collected subsequently, either voluntarily or as the result of enforcement activities. In TY 2001, the gross tax gap was $345 billion and the net tax gap was $290 billion. In TY 2006, the gross tax gap climbed to $450 billion and the net tax gap grew to $385 billion. The IRS reported that enforcement activities and late payments reduced the TY 2006 net tax gap by $65 billion, compared to $55 billion in TY 2001.

The overall voluntary compliance rate in TY 2006 was 83.1 percent compared to 83.7 percent in FY 2001. According to the IRS, the two rates are essentially the same because the TY 2006 rate is within the range of error of the TY 2001 rate.

■ ***Comment.*** The IRS explained that 2006 was the latest year in which all statistics that go into a tax gap computation were available, taking into account filing time, audit cycles and collection efforts. The IRS did not speculate on what an eventual examination of TY 2011 would reveal another five years from now. However, it did mention the attention that IRS Commissioner Shulman has given to the tax gap since taking office in 2008, emphasizing in FS-2012-6 that virtually all major initiatives launched by the IRS since then "have been designed to focus on the tax gap."

Underreporting

Underreporting of income remained the largest contributing factor to the tax gap, the IRS explained. Underreporting accounted for an estimated $376 billion (84 percent) of the $450 billion TY 2006 gross tax gap. Underreporting grew 32 percent between TY 2001 and TY 2006, the IRS reported.

Individuals. According to the IRS, individuals underreported by an estimated $235 billion in TY 2006 compared to $197 billion in 2001.

Corporations. The IRS estimated that the tax gap for large corporations (assets over $10 million) was $48 billion undererported in TY 2006 and $19 billion for small corporations in TY 2006.

Employment taxes. Underreporting of self-employment taxes contributed $57 billion to the TY 2006 tax gap, the IRS reported. Taxpayers underreported FICA taxes by $14 billion in TY 2006.

Nonpayment

Nonfiling made up $28 billion of the TY 2006 gross tax gap, the IRS explained. Nonfiling by individuals accounted for nearly 90 percent of all nonfiling in TY 2006.

Hill reaction

"In an era when we're squeezing the federal budget for every dollar of savings, we have to make every effort to recover these lost funds," Senate Finance Committee Chair Max Baucus, D-Montana, said in a statement. A spokesperson for House Ways and Means Chair Dave Camp, R-Mich., said that the tax gap study reinforced the need for tax reform.

Reference: TRC IRS: 15,054.

Audits

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the audit coverage rate was highest for corporations with assets $250 million or higher, Miller reported, at 27.6 percent for FY 2011. The audit coverage rate for small corporations (corporations with assets under $10 million) was 1.02 percent in FY 2011 compared to 0.94 percent in FY 2010.

Partnerships/S corps. The audit coverage rate for partnerships in FY 2011 was 0.40 percent, compared to 0.36 percent in FY 2010. The audit coverage rate also increased for S corps (0.42 percent in FY 2011 compared to 0.37 percent in FY 2010).

Reference: TRC INDIV: 36,056.

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Reference Key

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

IRS Reopens Offshore Voluntary Disclosure Program; Increases Highest Penalty

◆ *IR-2012-5*

The IRS has reopened the offshore voluntary disclosure program, which closed in 2011, to encourage taxpayers to disclose unreported foreign accounts. The revived program is open-ended but the IRS reserved the right to change the terms of the program at any time going forward. Additional details will be posted on the IRS website, the IRS advised.

■ ***CCH Take Away.*** IRS Commissioner Douglas Shulman announced the reopening of the offshore voluntary disclosure program by lauding the success of past programs. Shulman reported that the IRS has collected $4.4 billion from the 2009 and 2011 programs. Shulman predicted the IRS will collect additional revenue from the 2011 program as it processes cases.

Reopened program

The reopened program is similar to the 2011 program but there are some differences. The overall penalty framework requires individuals to pay a penalty of 27.5 percent of the highest aggregate balance in foreign bank accounts/entities or value of foreign assets during the eight full tax years prior to disclosure. The 2011 program imposed a penalty of 25 percent. Unchanged from the 2011 program are reduced penalties of 12.5 percent and five percent for qualified taxpayers, the IRS explained. Individuals who have made voluntary disclosures after the 2011 program ended will be able to be treated under the provisions of the revived program.

No deadline

The 2009 and 2011 programs were temporary and required taxpayers to request to participate by certain deadlines. The reopened program has no set deadline. However, the terms of the revived program could change at any point, the IRS cautioned. The IRS indicated it could increase penalties in the program for all or some taxpayers or defined classes of taxpayers; or it could decide to end the revived program entirely.

■ ***Comment.*** Shulman reported that the 2009 and 2011 programs have generated 33,000 voluntary disclosures to date.

TAD

In related news, the National Taxpayer Advocate recently has ordered the IRS Large Business & International and Small Business/Self-Employed Divisions in a Taxpayer Assistance Directive (TAD) to revoke a memorandum issued on March 1, 2011 to examiners of open cases in the 2009 offshore voluntary disclosure program. The memorandum directs examiners in certain listed categories of cases to stop using their discretion to determine whether to propose an offshore penalty less than 20 percent. According to the National Taxpayer Advocate, the IRS materially changed the terms of the 2009 offshore voluntary disclosure program after taxpayers applied to it in reliance on the original terms, resulting in the IRS treating similarly situated taxpayers differently.

Reference: FED ¶46,241; TRC FILEBUS: 9,104.

IRS Clarifies Form W-2 Reporting Of Employer-Provided Health Insurance/Updates FAQs

◆ *Notice 2012-9,www.irs.gov*

The IRS has issued interim guidance to clarify informational reporting by employers to employees on the cost of employer-provided health insurance. The IRS also updated existing frequently asked questions (FAQs) and posted new FAQs on its website.

■ ***CCH Take Away.*** "Including this information on Form W-2 has no impact on whether the coverage is taxable; it is for informational purposes only," Kimberly McCarthy, partner, Partridge, Snow and Hahn, LLP, Providence, R.I., told CCH "The employer generally must report the entire cost of coverage based on the information available as of December 31 of the calendar year. Any election or notification in the subsequent calendar year is not required to be included in the calculation, even if it has retroactive effect, " McCarthy explained.

Background

The Patient Protection and Affordable Care Act (PPACA) generally requires employers to disclose the aggregate cost of applicable employer-sponsored coverage on an employee's Form W-2 for tax years beginning on or after January 1, 2011. To give employers more time to update their payroll systems, the IRS made reporting optional for all employers in Notice 2010-69. Notice 2011-28 provided further relief for small employers.

Interim guidance

The interim guidance, the IRS explained, is generally applicable to 2012 Forms W-2 (forms that employers will provide to employees in 2013). Employers may rely on Notice 2012-9 if they voluntarily report the cost of coverage on 2011 Forms W-2, the IRS advised. The interim guidance describes employer-sponsored coverage, method of reporting, aggregate cost of coverage, and more.

■ ***Comment.*** "Notice 2012-9 adds important clarifications on a number of open issues, including the role of third party sick pay providers, and the proper treatment of excess 105(h) payments and employee assistance programs, which should help plan sponsors and insurers meet these interim 'Code DD' reporting requirements," Elizabeth Dold, principal, The Groom Law Group, Chartered, Washington, D.C., told CCH.

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IRS Proposes Revamping Equitable Innocent Spouse Rules

◆ *IR-2012-3, Notice 2012-8*

The IRS has proposed a revenue procedure to revise the threshold requirements for Code Sec. 6015(f) equitable innocent spouse relief. The agency also proposed streamlined equitable innocent spouse determinations. Additionally, IRS Chief Counsel instructed its attorneys to immediately follow the proposed revenue procedure.

■ ***CCH Take Away.*** "The revised factors were a longtime coming and level the playing field," David Sands, CPA, past chair, relations with the IRS committee, New York State Society of CPAs, told CCH. "The revised factors reflect the realities of life, looking at the true economics of a taxpayer's situation."

Background

There are different types of relief from joint and several liability for spouses who filed joint returns: Code Sec. 6015(b) innocent spouse relief; Code Sec. 6015(c) separation of liability relief; and Code Sec. 6015(f) equitable relief. Equitable relief under Code Sec. 6015(f) may apply when a taxpayer does not qualify for Code Sec. 6015(b) or 6015(c) relief.

■ ***Comment.*** The IRS Restructuring and Reform Act of 1998 did not specify a limitations period for Code Sec. 6015(f) equitable relief. However, the IRS imposed one by reg. The Tax Court struck down the reg in *Lantz,* CCH Dec. 57,784 and in *Mannella,* CCH Dec. 57,787. These decisions were reversed on appeal. A number of lawmakers also called on the IRS to remove the controversial reg, which the agency did in July 2011.

Proposals

A new revenue procedure, which would supersede Rev. Proc. 2003-62, would clarify application of the equitable factors to the determination, take into account abuse and financial control by the nonrequesting spouse, alter how economic hardship is evaluated, and make other changes, the IRS explained. The proposed changes would also apply to Code Sec. 66(c), which provides equitable relief for married individuals with community property income.

■ ***Comment.*** The IRS reported that it will apply the proposed procedures instead of Rev. Proc. 2003-62 in evaluating requests for equitable innocent spouse relief until the proposed rules are finalized. However, taxpayers may request that the IRS apply Rev. Proc. 2003-62.

Factors

The IRS considers all of the facts and circumstances to determine if a taxpayer qualifies for equitable innocent spouse relief. The IRS proposed to clarify that no one factor or a majority of factors necessarily controls the determination. The IRS also proposed to revise the economic hardship factor to provide minimum standards based on income, expenses and assets. Actual knowledge, the IRS explained, would no longer be weighed more heavily than other factors.

Abuse/financial control

Where a taxpayer has been abused by the nonrequesting spouse, the taxpayer may not have been able to challenge the treatment of items on the return or question the payment of taxes, the IRS reported. Lack of financial control may have a similar impact, the agency added. In response, the IRS proposed that abuse or lack of financial control may mitigate other factors that weigh against granting relief.

Streamlined decisions

If the taxpayer satisfies certain threshold criteria, the IRS proposed to consider a streamlined determination. Ineligibility for a streamlined determination would not impact a taxpayer's consideration for equitable innocent spouse relief, the agency explained.

Chief Counsel

IRS Chief Counsel instructed its attorneys, effective immediately, to no longer argue that equitable relief is not warranted based on factors in Rev. Proc. 2003-62. Instead, Chief Counsel attorneys will apply the revised factors in the proposed revenue procedure.

References: FED ¶¶46,236, 46,237; TRC INDIV: 18,058.

Employers

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Coverage

Applicable employer-sponsored coverage is coverage under any group health plan made available to the employee by an employer excluded from the employee's gross income under Code Sec. 106 or would be excluded if it were employer-provided coverage within the meaning of Code Sec. 106, the IRS explained. Notice 2012-9 describes types of coverage that are excluded from reporting.

■ ***Comment.*** "One of the most important clarifications of the new guidance is that the reporting requirement does not apply to contributions to HRAs, HSAs, MSAs, and FSAs funded solely by employee pre-tax salary contributions on the W-2," McCarthy noted.

Small employers

For 2012 Forms W-2 (and W-2s issued in later years unless and until further guidance is issued), an employer is not subject to reporting for any calendar year if the employer was required to file fewer than 250 Forms W-2 for the preceding calendar year, the IRS explained. Whether an employer is required to file fewer than 250 Forms W-2 for a calendar year is determined based on the Forms W-2 that it would be required to file if it filed Forms W-2 to report all wages paid by the employer and without regard to use of an agent under Code Sec. 3504, the IRS added.

Transition relief

The IRS cautioned that certain transition relief, such transition relief for some multiemployer plans and others, may be limited by future guidance. However, future guidance will not require reporting for 2012 Forms W-2 for small employers (W-2s provided to employees in 2013).

References: FED ¶46,228; TRC COMPEN: 45,236.05.

Chief Counsel Allows "Any Reasonable Method" For Applying Mortgage Interest Deduction Limits

◆ *CCA 201201017*

IRS Chief Counsel has approved the use of "any reasonable method" by a taxpayer to determine the amount of interest that can be deducted as qualified residence interest. Applied to situations in which the debt exceeds the $1 million or $100,000 statutory limits, reasonable methods include the simplified method and the "exact" method, as described in the regs, and a hybrid method described in Publication 936, Home Mortgage Interest Deduction.

■ ***CCH Take Away.*** Under Code Sec. 163(h), certain items of interest, such as credit card interest, are nondeductible personal interest. However, a deduction is allowed for "qualified residence interest" under Code Sec. 163(h)(3). The issue is how to determine the amount of deductible interest when the interest is paid on debt that exceeds the limits on residential debt, but part of which may be deducted as a business or investment expense or as part of another deductible activity.

Background

The Omnibus Budget Reconciliation Act of 1987 (OBRA) amended Code Sec. 163(h)(3) to allow a deduction for qualified residence interest for up to $1 million of acquisition debt and $100,000 of home equity debt. In the legislative history for OBRA, Congress stated that it expects the IRS to issue regs describing the proper method for allocating interest on excess amounts of debt (that exceed the $1 million and $100,000 limits). Until the IRS issued regs, Congress directed that taxpayers be allowed to use a "reasonable method."

The IRS issued temporary and proposed regs before OBRA, setting out the simplified and exact methods. The IRS stated that these methods still apply, if modified to reflect the new limits.

Methods

The simplified method multiplies the interest paid by a fraction equal to the debt limits divided by the sum of all the secured debts. Under this method, the interest on excess debt is treated as personal (nondeductible) interest.

The exact method compares the debt limit to the average balance of each debt. The debt limit is the lesser of the fair market value or the purchase price of the residence, reduced by prior debts. Thus, the interest paid is multiplied by a fraction equal to the debt limit for a particular debt, divided by the average balance of the debt. The interest on excess debt is deductible or nondeductible based on the use of the debt proceeds under interest tracing rules. There is a hybrid method in Pub. 936.

■ ***Comment.*** Taxpayers can also elect to treat debt secured by a qualified residence as not secured by the residence.

Chief Counsel's analysis

Chief Counsel determined that taxpayers can use any reasonable method to allocate debt that exceeds the limits, including the exact method, the simplified method, the Pub 936 method, and a reasonable approximation of those methods.

Regardless of the method used, the taxpayer may allocate amounts that exceed the limits, according to the use of the debt proceeds. Taxpayers can elect to treat the debt as not secured by a residence, but do not have to make the election. If an election is made, the entire debt is treated as not secured by the residence; if an election is not made, only the debt portion that exceeds the limits is traced according to the use of the proceeds, Chief Counsel determined.

Reference: TRC REAL: 6,056.15.

IRS Updates Determination Letter/Ruling Procedures On Organizations' Exempt Status

The IRS has updated the procedures governing IRS determination letters and rulings on the status of non-profit, charitable, and other exempt organizations under Code Sections. 501 and 521.

Rev. Proc. 2012-9 clarifies that Form 8718, User Fee for Exempt Organization Determination Letter Request, is not an application for a determination letter; hospital organizations under Code Sec. 501(r) must submit Form 1023, Application for Recognition of Exemption Under Section 501(c)(3); that the IRS may continue its existing practice whereby it may refuse to issue a group exemption letter; and that a determination letter or ruling recognizing exemption may be revoked or modified automatically, pursuant to Code Sec. 6033(j), if the organization fails to file a required annual return for three years in a row.

Rev. Proc. 2012-9; FED ¶46,238; TRC EXEMPT: 12,102.05.

IRS Updates Determination Letter Procedures For Private Foundation Status

The IRS has updated its procedures on the issuance of rulings and determination letters for private foundation status, operating foundation status, and exempt operating status under Code Sections 509(a), 4942(j)(3), and 4940(d)(2), respectively.

Section 7 of Rev. Proc. 2012-10 (formerly Section 6) has been slightly rewritten to account for the introduction of Form 8940, Request for Miscellaneous Determination Under Section 507, 509(a), 4940, 4942, 4945, and 6033 of the Internal Revenue Code, and the corresponding instructions. Form 8940 and instructions now address the list of information to be included with determination requests as well as the guidelines for filing Form 990 that were formerly outlined in Section 6 of Rev. Proc. 2011-10.

Rev. Proc. 2012-10; FED ¶46,239; TRC EXEMPT: 12,102.05.

IRS Explains 2011 Reporting For 2010 Conversions To Roth Accounts

◆ *www.irs.gov*

The IRS has provided guidance to taxpayers who transferred amounts to a Roth account in 2010 in a taxable transaction. Generally, these taxpayers must report half of the income in 2011 and half in 2012, unless the taxpayer elected to report the income in 2010.

■ ***CCH Take Away.*** 2010 was the first year that taxpayers could transfer funds from a traditional individual retirement account (IRA) to a Roth IRA without restriction. To encourage taxpayers to take advantage of this opportunity, Congress provided a special benefit for taxpayers who created Roth accounts in 2010 and made a taxable transfer to the account. Instead of having to report all the income in 2010, taxpayers could defer reporting the income until 2011 and 2012, a welcome benefit for taxpayers who transferred large amounts to their Roth accounts in 2010.

Scope

Amounts transferred into a Roth account from another retirement account are taxable, although they are not subject to the 10 percent tax on early withdrawals. Taxes apply to:

- Eligible rollovers from a retirement plan to a Roth IRA;
- Amounts transferred from a non-Roth IRA to a Roth IRA (a conversion); and
- An in-plan rollover of benefits in a retirement plan to a Roth account maintained by the same plan.

The IRS instructed that taxpayers engaging in one of these transactions during 2010 must report half of the taxable amount from the transfer on their 2011 tax return and half of the taxable amount in 2012, unless the taxpayer:

- Elected to include the taxable amount in income in 2010 (this election cannot be revoked after the due date for the 2010 tax return);
- Recharacterized the transfer to a Roth IRA as a traditional IRA (the deadline for recharacterizing a 2010 transfer was October 17, 2011; also, an in-plan Roth rollover cannot be recharacterized, the IRS advised); or
- Received a taxable distribution in 2010 or 2011 from the Roth IRA (in which case, the taxpayer would not report half of the income but would report a different amount on the 2011 return).

On their 2010 tax return, Form 8606, Nondeductible IRAs, taxpayers would have reported the transfer and either made the election to report it in 2010 or identified the 50 percent amounts reportable in 2011 and 2012.

2011 reporting

Assuming they did not receive a distribution in 2011, the IRS instructed taxpayers who made a transfer to a Roth account in 2010 to obtain the 50-percent amount from their 2010 return and include it on their 2011 Form 1040 under IRA distributions, and pensions and annuities.

If the taxpayer received a taxable distribution (of the converted amount) in 2010 from the Roth IRA, then in 2011 the taxpayer would report the smaller of:

- The 50-percent amount reported in 2010; or
- The remaining taxable amount from the 2010 transfer.

■ ***Example.*** Tyler transferred $30,000 from a traditional IRA to a Roth IRA in 2010. Later in 2010, Tyler received a $20,000 distribution. Tyler must include the $20,000 in income for 2010. The 50-percent amount that would have been reportable in 2011 is $15,000 (half of the $30,000 transfer). However, only $10,000 of the transfer remains to be taxed. Since this is smaller than $15,000, Tyler reports the remaining $10,000 in 2011, and does not report anything from the transfer in 2012.

If, instead, the taxpayer received a taxable distribution of the converted amount in 2011, then the taxpayer has to fill out Part III or Part IV of the 2011 Form 8606 to determine how much of the transferred amount to report in 2011 and 2012.

Reference: TRC RETIRE: 66,760.10.

IRS Releases Covered Compensation Tables For 2012 Plan Year

The IRS issued covered compensation tables under Code Sec. 401(l)(5)(E) for the 2012 plan year. Covered compensation sets an upper limit to the integration level of defined benefit excess benefit plans and to the amount of final average compensation used to compute the maximum offset allowance in an offset plan.

Covered compensation. Covered compensation for an employee is the average of the contribution and benefit bases in effect under the Social Security Act (SSA), for each year in the 35-year period ending with the year in which the employee reaches (or will reach) Social Security retirement age. A 35-year period is used for all individuals regardless of their year of birth.

■ ***Comment.*** The IRS therefore reported that for purposes of determining covered compensation for the 2012 year, the taxable wage base for both covered compensation and Social Security contribution purposes is $110,100. For 2011, the taxable wage base was $106,800.

Wage base. The taxable wage base is the contribution and benefit base under the SSA. For determining the amount of an employee's covered compensation, a plan may use the IRS tables developed by rounding the actual amounts of covered compensation for different years of birth.

Rev. Rul. 2012-5, FED ¶46,235; TRC RETIRE: 24,208.

Tax Briefs

Internal Revenue Service

The IRS has announced a change to Publication 1220, Specifications for Filing Forms 1097, 1098, 1099, 3921, 3922, 548 and W-2G Electronically. The IRS has changed Part C, section 6(14) Payee "B" record layout for Form 1099-K to delete the reference to Rev. Proc. 2004-43, related to Merchant Category Codes.

Announcement 2012-2, FED ¶46,240; TRC FILEBUS: 12,302.15.

Summons

An IRS summons directing an individual to produce documents related to an investigation of his tax liabilities was ordered enforced because the government established a *prima facie* case for enforcement under *Powell* that was not rebutted.

McNorton, DC Hawaii, 2012-1 USTC ¶50,127; TRC IRS: 21,300.

An individual's petition to quash an IRS summons was dismissed for failure to timely serve the government. Although the individual was given notice that her petition was subject to dismissal for lack of service, she did not show cause as to why she failed to effectuate timely service on the IRS.

Grove, DC Colo., 2012-1 USTC ¶50,126; TRC IRS: 21,056.15.

An IRS summons directing an individual to appear and produce documents related to an investigation of his tax liabilities was ordered enforced. The government established its *prima facie* case for enforcement under *Powell*, which the individual failed to rebut.

Gillies, DC Calif., 2012-1 USTC ¶50,125; TRC IRS: 21,300.

An IRS summons directing an individual to appear, testify and produce documents relevant to the IRS's efforts to collect a farm corporation's employment taxes was properly enforced. The government established its *prima facie* case for enforcement under *Powell*, which the individual failed to rebut.

Carranco, DC Calif., 2012-1 USTC ¶50,124; TRC IRS: 21,300.

A federal district court had jurisdiction to enforce an IRS administrative summons directing an individual to appear, testify and produce documents related to a civil investigation of his tax liabilities. The individual failed to rebut the government's *prima facie* case and his argument that the revenue agent lacked authority to issue the summons under Code Sec. 7608 was without merit because the IRS had instigated a civil investigation of the individual. Further, requiring the individual to comply with the summons would not deprive him of his constitutional rights under the Fourth and Fifth Amendments.

Lund, DC Ore., 2012-1 USTC ¶50,123; TRC IRS: 21,300.

Income

Individuals who were married during the tax year at issues were not entitled to reduce their income by cost of goods sold absent adequate substantiation and were denied relief from joint and several liability, except that an understatement of tax was allocated equally to each spouse; an accuracy-related penalty applied.

Gaitan, TC, CCH Dec. 58,904(M), FED ¶47,917(M); TRC INDIV: 18,058.

Deductions

An individual's expenses related to his writing a proposed book were not deductible because he was not in the trade or business of being a book author. Further, he did not establish a business purpose for each of his expenses. Although the denial of his expense deductions resulted in a substantial understatement of his income tax, he was not liable for an accuracy-related penalty because he relied on the

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Chief Counsel Limits Airline's Deduction To 50 Percent Of Cost Of In-Flight Meals To Crew

IRS Chief Counsel has concluded that meals provided by an airline to its crew members while they are working on a plane are only 50 percent deductible by the airline, under Code Sec. 274(n). The deduction is limited to 50 percent, rather than 100 percent, even though the meals are totally excluded from the employees' income under Code Sec. 119.

- ***CCH Take Away.*** Code Sec. 119 excludes meals from an employee's income if the meals are furnished for the convenience of the employer. Although this test was satisfied, Chief Counsel concluded that the meals had to be excluded under Code Sec. 132(e) as a de minimis fringe benefit, for the employer/airline to avoid the 50 percent limitation.

Background. The airline required the crew to stay on-board the airline before and after the flight for specified periods. The airline provided catered meals, prepared by a third party, for crew members on its planes, to eat while they are performing flight duties. The taxpayer took a full deduction for the meals.

Chief Counsel's analysis. Code Sec. 274(n) limits the deduction for food and beverages to 50 percent unless an exception applies. Code Sec. 274(n)(2)(B) allows a full deduction for food expenses that are excluded as de minimis fringe benefits under Code Sec. 132(e). Chief Counsel focused on Code Sec. 132(e)(2) and argued that it did not provide an exclusion for the airline meals. Therefore, the deduction was limited to 50 percent.

CCA 201151020, TRC COMPEN: 36,502.

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advice of his tax advisor in claiming the disallowed deductions.

Oros, TC, CCH Dec. 58,905(M), FED ¶47,918(M); TRC BUSEXP: 24,252.

An individual was not entitled to deduct expenses that he claimed on three separate Schedule C forms because he failed to substantiate these expense and his claim that his records were destroyed in a fire did not relieve him of this responsibility. He was liable for the addition to tax for failure to timely file a return and the accuracy-related penalty. He did not show reasonable cause or good faith for the underpayment.

Roumi, TC, CCH Dec. 58,903(M), FED ¶47,916(M); TRC BUSEXP: 24,502.

Three individual taxpayers were denied charitable contribution deductions for conservation easements granted to a charitable organization. The conservation easements were not granted in perpetuity; therefore, the taxpayers failed to meet the requirements of Reg. §1.170A-14(g)(6)(i), and the easements were not qualified conservation contributions.

Carpenter, TC, CCH Dec. 58,902(M), FED ¶47,915(M); TRC INDIV: 51,364.25.

Liens and Levies

A brother and sister's quiet title action challenging IRS liens placed on a property they held as nominees of their delinquent taxpayer parents was dismissed because they lacked standing to challenge the validity of the tax liens. The children failed to establish that they suffered the actual, particularized injury necessary to confer standing to challenge the IRS liens.

Adam, DC Calif., 2012-1 USTC ¶50,128; TRC IRS: 48,106.

The government was entitled to foreclose its tax liens upon the real property of an individual who was assessed the trust fund recovery penalty. The government previously obtained a judgment against the individual for the unpaid taxes and the tax liens were valid, attached to all of the individual's property and rights to property when he failed to pay and he failed to present any defense to the foreclosure.

Bibin, Jr., DC Mich., 2012-1 USTC ¶50,121; TRC IRS: 45,158.

Deficiencies and Penalties

Two LLCs taxed as partnerships were collaterally estopped from challenging the IRS's disallowance of deductions generated by BLIPS transactions because the LLCs' controlling managers had been convicted of tax evasion and conspiracy to evade taxes for their role in designing and selling the BLIPS. The LLCs were subject to negligence penalties under Code Sec. 6662 because their managers acted negligently by claiming deductions generated by the BLIPS; however, the gross valuation misstatement penalty was inapplicable because the underpayment was attributable to the invalid deductions, not an overvaluation of the assets.

Princeton Strategic Investment Fund, LLC, DC Calif., 2012-1 USTC ¶50,122; TRC PART: 60,550.

Bankruptcy

A debtor was not a responsible person under Code Sec. 6672 for the period after he took a job in the Middle East and relinquished control of their jointly owned corporation to his brother. The IRS's argument that the debtor remained a responsible person because he was not formally removed from the corporation's paperwork was rejected.

In re Hayes, BC-DC Mich., 2012-1 USTC ¶50,129; TRC PAYROLL: 6,256.

IRS Launches Video Taxpayer Assistance Pilot Program

The IRS has began a pilot program using two-way video to assist taxpayers with questions, the Treasury Department recently reported on its website. Taxpayers may communicate with IRS personnel through interactive video in select locations nationwide.

Two-way video, the Treasury Department explained, will be available in IRS offices in Jonesboro, Ark.; Fresno, Calif.; Laguna Niguel, Calif.; Colorado Springs, Colo.; Miami; Utica, N.Y.; Harrisburg, Pa.; Richmond, Va.; Bridgeport, W.Va.; and Rothschild, Wisc. Additionally, two-way video will be available in the offices of community organizations in Prescott, Ariz.; and Bellefonte, Pa. According to the Treasury Department, the pilot program may be expanded to more locations in the future.

www.treasury.gov.

Form 8937 Now Available For Corporations To Report Organizational Actions By January 17

The IRS recently released final Form 8937, Report of Organizational Actions Affecting Basis of Securities. Release of Form 8937 comes barely in time for corporations to file within the transition relief period on basis reporting provided in Notice 2011-18 (see the February 24, 2011 issue of this newsletter). Corporations must report any organizational action (such as a stock split, merger or acquisition), starting with 2011 actions, that affects the basis of stock. Notice 2011-18 had set a transitional deadline of January 17, 2012 for those corporations first coming under this requirement, irrespective of any earlier deadline.

■ ***Comment.*** As part of the new reporting system enacted under the Emergency Economic Stabilization Act of 2008, corporations that engage in an "organizational action" must file an information return with the IRS. Absent the transitional deadline of January 17, 2012, that report on Form 8937 must be filed within 45 days after the date of the action, or if earlier, by January 15 of the following year. Alternatively, the corporation can post the information on its primary web site by the filing date.

Form 8937 and Instructions, TRC FILEBUS: 9,380.