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# IRS Removes Covered Opinion Rules, Clarifies Other Provisions Of Circular 230

◆ *TD 9668*

The IRS has issued final regs under Circular 230, Rules of Practice, which eliminate the rules for covered opinions and make other changes. Under the final regs, all written tax advice is subject to one standard under Section 10.37 of Circular 230. The final regs also clarify written tax advice, competence, and more.

■ ***CCH Take Away.*** "Though we have not had the time to do a full analysis of the final Circular 230 regulations, we believe the regulations move in the right direction from a rule-based system to a principle-based system," Melanie Lauridsen, technical manager, American Institute of Certified Public Accountants (AICPA), told CCH. "A principle-based system will focus on removing bad apples, rather than catching persons who have tripped over the rules. We were very pleased to see that the final regulations are consistent with some of our recommendations/comments."

## Covered opinions

The former rules required practitioners providing a covered opinion to make certain disclosures. Additionally, certain relationships between the practitioner and a person promoting or marketing a tax shelter were required to be disclosed.

■ ***Comment.*** Since issuance of the covered opinion rules, disclaimers on emails and other practitioner communications have become commonplace. As the IRS observed, they often appear on communications which did not constitute taxpayer advice.

The final regs replace the covered opinion rules with principles to which all practitioners must adhere when rendering written advice. Section 10.37 provides that practitioners base all written advice on reasonable factual and legal assumptions, exercise reasonable reliance, and consider all relevant facts that the practitioner knows or reasonably should know. A practitioner must also use reasonable efforts to identify and ascertain the facts relevant to written advice on a federal tax matter.

The final regs, the IRS explained, do not impose a specific requirement for a practitioner to include in the written advice any particular piece of information or analysis. However, the IRS encouraged practitioners to describe all relevant facts, law, analysis, and assumptions in appropriate circumstances. Determination of whether a practitioner complied with the requirements of Section 10.37 will be based on all facts and circumstances, including whether it was appropriate to describe all relevant facts, law, analysis, and assumptions in a particular piece of written tax advice.

## Written tax advice

Some commentators asked the IRS to clarify that certain items would not be considered written tax advice. The IRS agreed. The final regs provide that submis-

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Route to: ____________ ____________ ____________ ____________ ____________

# Inherited IRA Not Exempt From Bankruptcy Estate, Supreme Court Rules

◆ *Clark v. Rameker, SCt., June 12, 2014*

In a unanimous decision, the U.S. Supreme Court has held that funds from an inherited IRA are not "retirement funds" exempt from the debtor's bankruptcy estate. Funds held in inherited IRAs are not objectively set aside for the purpose of retirement, the Court found.

■ ***CCH Take Away.*** "The decision narrowly reads the retirement funds exception to exclude inherited IRAs," Elizabeth Thomas Dold, The Groom Law Group, Chartered, Washington, D.C., told CCH. "Individuals concerned about their potential beneficiaries spending habits may want to focus more on this point when making rollover decisions. And, in any case, the case underscores the potential benefits of a surviving spouse's election to treat an IRA as his or her own."

■ ***Comment.*** The decision resolves a split among the Circuits. In *Chilton, 2012-1* USTC *¶50,250,* the Fifth Circuit found that inherited IRAs are retirement funds under Bankruptcy Code Sec. 522(d)(12). The Seventh Circuit reached the opposite conclusion in *Clark, 2013-1* USTC *¶50,389.*

## Background

In 2000, the taxpayer's mother created a traditional IRA and named her daughter as the sole beneficiary. After her mother's death in 2001, the taxpayer elected to take monthly distributions from the account. Nine years later, the taxpayer sought Chapter 7 bankruptcy protection. At that time, the inherited IRA contained approximately $300,000. The taxpayer argued that the inherited IRA constituted retirement funds and was exempt from the bankruptcy estate.

The bankruptcy court held that an inherited IRA does not represent retirement funds in the hands of the current owner and therefore is not exempt under Bankruptcy Code Sec. 522(d)(12). A federal district court reversed, finding that funds representing retirement funds in the decedent's hands must be treated the same way in successors' hands

The Seventh Circuit disagreed. An inherited IRA does not have the economic attributes of a retirement vehicle, because the money cannot be held in the account until the current owner's retirement, the Seventh Circuit explained.

## Court's decision

Justice Sotomayor delivered the Court's opinion. "The Bankruptcy Code does not define 'retirement funds,' so we give the term its ordinary meaning. Section 522(b)(3)(C)'s reference to 'retirement funds' is therefore properly understood to mean sums of money set aside for the day an individual stops working," Sotomayor wrote. The inquiry into whether a set of funds falls within this definition must be an objective one, Sotomayor added.

"Three legal characteristics of inherited IRAs lead us to conclude that funds held in such accounts are not objectively set aside for the purpose of retirement," Sotomayor continued. "First, the holder of an inherited IRA may never invest additional money in the account. Where inherited IRAs categorically prohibit contributions, the entire purpose of traditional and Roth IRAs is to provide tax incentives for accountholders to contribute regularly and over time to their retirement savings. Second, holders of inherited IRAs are required to withdraw money from such accounts, no matter how many years they may be from retirement. Finally, the holder of an inherited IRA may withdraw the entire balance of the account at any time, and for any purpose, without penalty."

"If an individual is allowed to exempt an inherited IRA from her bankruptcy estate, nothing about the inherited IRA's legal characteristics would prevent (or even discourage) the individual from using the entire balance of the account on a vacation home or sports car immediately after her bankruptcy proceedings are complete," Sotomayor noted. "Allowing that kind of exemption would convert the Bankruptcy Code's purposes of preserving debtors' ability to meet their basic needs and ensuring that they have a 'fresh start.'"

*References: 2014-1* USTC *¶50,317;*
*TRC RETIRE: 66,800.*

## Circular 230

*Continued from page 1*

sions on matters of general policy are not considered written tax advice on a federal tax matter for purposes of Section 10.37.

The final regs also clarify that continuing education presentations to an audience solely for the purpose of enhancing practitioners' professional knowledge on federal tax matters are not written advice for purposes of Section 10.37.

## Federal tax matter

The final regs define "federal tax matter." Under Section 10.37(d), a federal tax matter is any matter concerning the application or interpretation of (1) a revenue provision as defined in Code Sec. 6110(i)(1)(B), (2) any provision of law impacting a person's obligations under the internal revenue laws and regulations, including but not limited to the person's liability to pay tax or obligation to file returns, or (3) any other law or regulation administered by the IRS.

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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 Unveils "Taxpayer Bill Of Rights;" Revises Communications With Taxpayers

◆ *IR-2014-72, www.irs.gov*

After several years of discussion, the IRS has adopted a Taxpayer Bill of Rights (TBOR). The IRS also updated *Publication 1, Your Rights as a Taxpayer,* to reflect the newly-adopted Taxpayer Bill of Rights.

■ ***CCH Take Away.*** "The Taxpayer Bill of Rights will help to educate taxpayers about their rights and protections before the IRS," Bernadette Schopfer, CPA, a member of the Small Business Advisory Committee of the New York State Society of CPAs (NYSSCPA) told CCH. Individuals without the benefit of professional assistance are often intimidated by IRS communications. The IRS has indicated that it intends to highlight the Taxpayer Bill of Rights in its communications with taxpayers, Schopfer added.

■ ***Comment.*** "These are core concepts about which taxpayers should be aware. The new Taxpayer Bill of Rights summarizes these important protections in a clearer, more understandable format" IRS Commissioner John Koskinen said at a news conference in Washington, D.C., announcing the Taxpayer Bill of Rights.

## Background

Proposals for a Taxpayer Bill of Rights have been raised by National Taxpayer Advocate Nina Olson and in Congress. Earlier this year, Olson made adoption of a Taxpayer Bill of Rights her number one recommendation to Congress for action. In 2013, the House had passed the Taxpayer Bill of Rights Act (HR 2768), but the bill stalled in the Senate.

■ ***Comment.*** "Just as the U.S. Constitution's Bill of Rights is organized and presented in a manner that U.S. citizens and the government can understand and respect, a Taxpayer Bill of Rights would serve the same function in the realm of taxation," Olson told Congress.

## Taxpayer Bill of Rights

The Taxpayer Bill of Rights contains 10 provisions:

- (1) The Right to be Informed
- (2) The Right to Quality Service
- (3) The Right to Pay No More than the Correct Amount of Tax
- (4) The Right to Challenge the IRS's Position and Be Heard
- (5) The Right to Appeal an IRS Decision in an Independent Forum
- (6) The Right to Finality
- (7) The Right to Privacy
- (8) The Right to Confidentiality
- (9) The Right to Retain Representation
- (10) The Right to a Fair and Just Tax System

## Publication 1

*IRS Publication 1* provides brief explanations each of the rights. For example, *Publication 1* states that the Right to be Informed reflects that "Taxpayers have the right to know what they need to do to comply with the tax laws. They are entitled to clear explanations of the laws and IRS procedures in all tax forms, instructions, publications, notices, and correspondence. They have the right to be informed of IRS decisions about their tax accounts and to receive clear explanations of the outcomes."

The Right to Challenge the IRS's position and to be Heard reflects that "Taxpayers have the right to raise objections and provide additional documentation in response to formal IRS actions or proposed actions, to expect that the IRS will consider their timely objections and documentation promptly and fairly, and to receive a response if the IRS does not agree with their position." The Right to Retain Representation reflects that "Taxpayers have the right to retain an authorized representative of their choice to represent them in their dealings with

*Continued on page 4*

## Circular 230

*Continued from page 2*

### Competence

The proposed regs provided that a practitioner must possess the necessary competence to engage in practice before the IRS and that competent practice requires the appropriate level of knowledge, skill, thoroughness, and preparation necessary for the matter for which the practitioner is engaged. The IRS explained that the competence standard contemplates that practitioners may become competent in a variety of ways, including, among other things, consulting with experts in the relevant area and studying the relevant law.

### Compliance

The IRS reported that Circular 230's compliance measures have successfully encouraged firms to self-regulate. Firms must have procedures to ensure compliance with respect to a firm's tax return preparation practice (76 FR 32286). The IRS finalized these measures in TD 9668.

### Significant purpose standard

The IRS proposed to apply a heightened standard of review to determine if a practitioner has satisfied the written advice standards when the practitioner knows or has reason to know that the written advice will be used in promoting, marketing, or recommending an investment plan or arrangement a significant purpose of which is the avoidance or evasion of any tax. The final regs clarify that the IRS will apply a reasonable practitioner standard that considers all facts and circumstances with an emphasis given to the additional risk associated with the practitioner's lack of knowledge of the taxpayer's particular circumstances.

■ ***Comment.*** The final regs also address electronic negotiation of taxpayer refunds, expedited suspension procedures, and the IRS Office of Professional Responsibility.

*References: FED ¶47,024; TRC IRS: 3,200.*

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# IRS Determines Certain Stock Rights Exempt From Code Sec. 457A

◆ *Rev. Rul. 2014-18*

The IRS has clarified that certain stock rights granted by a Code Sec. 457A nonqualified entity would be treated as exempt from the Code Sec. 457A deferred compensation rules. The stock right must be exempt from Code Sec. 409A and the stock appreciation right at all times by its terms must be settled, and is in fact settled, in service recipient stock.

■ ***CCH Take Away.*** The *Emergency Economic Stabilization Act of 2008* created Code Sec. 457A intending to limit a taxpayer's ability to defer compensation paid by nonqualified entities (offshore hedge funds) to the extent the compensation is no longer subject to a substantial risk of forfeiture (vested). Since that time, taxpayers have questioned if cumulative incentive fees would be allowed. The IRS determined that cumulative incentive fees are permissible.

## Background

The service recipient is a foreign corporation and a nonqualified entity for purposes of Code Sec. 457A(b). The service provider is a limited liability company organized and treated as a partnership for U.S. income tax purposes (a typical hedge-fund structure). As incentive compensation for service provider, service recipient grants a nonstatutory stock option and a stock appreciation right (in each case, a stock right) to service provider, each with respect to a fixed number of common shares of service recipient, which qualify as service recipient stock (as defined under Reg. §1.409A-1(b)(5)(iii)). Each stock right has an exercise price per share that is not less than the fair market value of a common share of service recipient on the date of grant; the stock rights do not include any feature for the deferral of compensation and otherwise comply with the requirements under Reg. §1.409A-1(b)(5)(i)(A) or (B). The terms of the stock appreciation right at all times provide that it must be settled in service recipient stock, and the stock appreciation right is settled in service recipient stock.

## IRS analysis

The IRS explained that although stock appreciation rights are generally subject to Code Sec. 457A, a stock appreciation right that, as here, at all times by its terms must be settled, and is settled, in service recipient stock is functionally identical in all material respects to a nonstatutory stock option to purchase service recipient stock with a net exercise feature. The stock transfer under such an arrangement, like the stock transfer pursuant to the exercise of a nonstatutory stock option, is taxable under Code Sec. 83. Therefore, the IRS determined that a nonstatutory stock option exempt from Code Sec. 409A is exempt from Code Sec. 457A.

Additionally, a stock appreciation right exempt from Code Sec. 409A that at all times by its terms must be settled, and is settled, in service recipient stock is exempt from Code Sec. 457A. A stock appreciation right that may be or is settled other than in service recipient stock is not exempt from Code Sec. 457A, regardless of whether the stock appreciation right is a nonqualified deferred compensation plan for purposes of Code Sec. 409A.

Applying these principles, the IRS determined that neither stock right with respect to common shares of service recipient granted to service provider is a nonqualified deferred compensation plan for purposes of Code Sec. 457A(a) because each is either a nonstatutory stock option that meets the requirements of Reg. §1.409A-1(b)(5)(i)(A) or a stock appreciation right that meets the requirements of Reg. §1.409A-1(b)(5) (i)(B) and at all times by its terms must be settled, and is settled, in service recipient stock. The stock rights granted to service provider would be exempt from Code Sec. 457A.

*References: FED ¶46,361; TRC COMPEN: 15,352.*

## Taxpayer Bill of Rights

*Continued from page 4*

the IRS. Taxpayers have the right to seek assistance from a Low Income Taxpayer Clinic if they cannot afford representation."

■ ***Comment.*** "Our establishment of the Taxpayer Bill of Rights is a clear reminder that all of the IRS takes seriously our responsibility to treat taxpayers fairly," Koskinen said.

*Reference: TRC IRS: 3,058.*

## *House Approves Enhanced Small Business Expensing, S Corp Bills*

The House continues to move selected tax extenders. On June 12, the House approved bills to make permanent enhanced Code Sec. 179 expensing and incentives targeted to S corps. The bills face an uncertain future in the Senate and a veto threat by President Obama.

■ ***Comment.*** "The votes offered good news for both small businesses and S corporations, but there are still scores of other expired provisions that need action," Dustin Stamper, director, Washington National Tax Office, Grant Thornton, LLP, told CCH. "Ultimately, the House action does not change the outlook on the extenders very much. A resolution over all of the expired provisions is unlikely before late in year."

***Expensing.*** Enhanced small business expensing under Code Sec. 179 expired after 2013. The House approved America's Small Business Tax Relief Bill of 2014 (HR 4457) by a vote of 272 to 144. The bill would make permanent the expensing amount and investment threshold in effect for 2013 ($500,000 and $2 million, respectively). The expensing amount and investment limitation would be indexed for inflation after 2014.

***S corps.*** The House also approved the S Corporation Permanent Tax Relief Bill of 2014 (HR 4457) by a vote of 263 to 155. The bill makes permanent the reduced recognition period for built-in gains of S corps.

# IRS Clarifies Effect Of Sequestration On Section 1603 Grants, Tax Credits

◆ *Notice 2014-39*

The IRS has announced that Section 1603 grants made after October 1, 2013, and on or before September 30, 2014, for qualified energy projects are subject to a sequestration rate of 7.2 percent. The agency also clarified the relationship between sequestration and certain energy tax credits.

■ ***CCH Take Away.*** The Section 1603 program has expired. Qualified projects that started construction prior to the expiration of the provision may be eligible to receive grants. As of May 2014, Treasury reported that 96,675 projects have been funded with Section 1603 grants at a cost of $21.6 billion.

## Background

Under Code Sec. 45, taxpayers may claim the PTC for the production and sale of electricity from qualified renewable sources. Code Sec. 48 provides an investment tax credit (ITC) for qualified energy property. In 2009, the *American Recovery and Reinvestment Act* (ARRA) allowed taxpayers to claim an ITC in lieu of a PTC. ARRA also created the Section 1603 grant program, under which taxpayers may elect to receive a cash grant from Treasury in lieu of tax credits. The amount of the grant is the applicable percentage of the basis of the property (10 or 30 percent depending on the type of property). Qualifying technologies include biomass, fuel cells, solar, and wind energy projects.

## Sequestration

The *Budget Control Act of 2011* imposes across-the-board spending cuts (known as sequestration) on many federal agencies and programs, including the Section 1603 program. The IRS explained that due to sequestration, a Section 1603 grant made on or after October 1, 2013, and on or before September 30, 2014, is subject to a sequestration rate of 7.2 percent. Further, the IRS explained that taxpayers may not partition the basis of property for which they receive a Section 1603 grant and claim a tax credit under Code Sec. 45 or Code Sect. 48 with respect to any part of the basis of the same property. Taxpayers must reduce the basis of the specified energy property by 50 percent of the amount of the Section 1603 grant.

*References: FED ¶46,362; TRC BUSEXP: 54,558.*

# Fifth Circuit Upholds Tax Court's Valuation Of Conservation Easement On Remand, Vacates Gross Valuation Misstatement Penalty

◆ *Whitehouse Hotel Limited Partnership, CA-5*

The Fifth Circuit Court of Appeals has upheld the Tax Court's finding on remand that a limited partnership had overvalued the value of real estate property donated as a qualified conservation contribution. However, the Fifth Circuit vacated the gross valuation misstatement penalty. Although the partnership had misstated the value of the contribution deduction by more than 400 percent, it had conducted a good faith investigation to determine the value of the property to be donated, the court held.

■ ***CCH Take Away.*** The Fifth Circuit instructed the Tax Court to (1) reconsider all valuation methods, not just the comparable sales method; (2) determine the entire parcel's "highest and best use" for the purpose of determining its valuation; and (3) consider the effect of the easement on the second building, even if the easement itself did not directly burden that building under relevant state law. There was no dispute that the conservation easement was valid.

■ ***Comment.*** Code Sec. 6662(h)(2)(A)(i) provides that the IRS may impose a penalty of 40 percent of the underpayment of tax on a taxpayer that misstates a deduction by 400 percent or more. Code Sec. 6664(c)(3) provides a defense to this penalty for a taxpayer that can show it had reasonable cause for the underpayment and that it acted in good faith.

## Background

In 1995, a partnership acquired an historic building in New Orleans' French Quarter. The partnership donated a façade easement to a local nonprofit organization and claimed a charitable deduction for the façade easement.

The Tax Court initially valued the easement at $1.7 million. The Tax Court also found that the taxpayer had made a gross valuation misstatement of more than 400 percent of the value of the conservation contribution, thus justifying IRS's assessment of the Code Sec. 6662(a) penalty of 40 percent.

The taxpayer appealed to the Fifth Circuit, which remanded the case to the Tax Court. On remand the Tax Court restated its original conclusion that any restriction on a development (such as the second building) that is not expressly contained in an easement cannot be used in valuation of that easement. However, it enforced the Fifth Circuit's holding and found that some effect on the valuation of the entire parcel including the second building not subject to the easement must occur as a result of the easement on the first building.

## Court's analysis

The Fifth Circuit upheld the Tax Court's valuation of the deduction for the donation of a qualified conservation easement, finding that the partnership's claim that the Tax Court had ignored the Fifth Circuit's

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# Sixth Circuit Affirms Lessee May Deduct Portion Of Purchase Price Under Option-To-Buy As Payment For Unexpired Lease

◆ *ABC Beverage Corp., CA-6, June 13, 2014*

Affirming a federal district court, the Sixth Circuit Court of Appeals has found that a taxpayer may immediately deduct as a business expense a portion of the purchase price that represented a buy-out of its unexpired lease obligations. The taxpayer did not have to capitalize the entire purchase price.

- ***CCH Take Away.*** The court noted that it had already held that a lessee similar to the taxpayer in this case could claim the deduction (*Cleveland Allerton Hotel, Inc., 48-1 ustc ¶9218*). The court rejected the IRS's argument that intervening decisions by the Supreme Court and changes in the Tax Code required modification of the *Cleveland Allerton* decision

## Background

The taxpayer acquired a company that held a long-term lease on a manufacturing plant. The taxpayer determined that the rent exceeded the plant's fair market rental value and exercised its purchase option. Three appraisals concluded that the value of the property without the lease was $2.75 million. The taxpayer initially offered $9 million to purchase the property and eventually agreed to a purchase price of $11 million.

On its income tax return, the taxpayer capitalized $2.75 million as the cost of purchasing the property and claimed a business deduction of $6.25 million, representing the difference between the $2.75 million appraisal value of the property and the $9 million, representing the amount the taxpayer had calculated it would have to pay for the property with the lease. The IRS disallowed the refund.

## Court's analysis

In *Cleveland Allerton,* a hotel operated a business on leased property. The hotel determined that the rent was excessive. The hotel calculated that the value of the property without the lease was $200,000 and paid $441,250 to purchase the property and the lease. The Sixth Circuit allowed the $241,250 deduction. The court found that the lease for the hotel was a liability it sought to extinguish. In contrast, the lease in the hand of a third party would be an asset capable of producing income from rental payments.

In 1956, the Supreme Court decided *Millinery Center Building Corp.. 56-1* USTC *9391.* The Supreme Court upheld the denial of a deduction for a lease. The facts were similar to *Cleveland Allerton,* but the taxpayer did not show that the rent was burdensome. Here, the taxpayer showed that the rent was burdensome.

The court also found that Code Sec. 167(c)(2) was not a bar to the taxpayer's deduction. The phrase "acquired subject to a lease," in the provision is best understood to encompass only those acquisitions in which the lease continues after the purchase and property is not acquired subject to a lease if the purchase extinguishes the lease, the court found.

*References: 2014-1* USTC *¶50,320; TRC SALES: 24,354.10.*

## Easement

*Continued from page 5*

mandates on remand was without merit. The Tax Court followed the Fifth Circuit's directive, reconsidered its original decision, and included the second building in the valuation of the easements as instructed.

The Fifth Circuit did, however, vacate the Tax Court's decision to uphold the gross valuation misstatement penalty. The partnership had obtained and analyzed two qualified appraisals prior to submitting a professionally prepared tax return. Therefore, it had demonstrated a good-faith investigation as required under Code Sec. 6664(c)(3)(B), the Fifth Circuit concluded.

*References: 2014-1* USTC *¶50,316; TRC INDIV: 51,364.45.*

## *U.N. Employee's Income Does Not Qualify For Code Sec. 893 Exclusion*

The Tax Court has found that a Finnish citizen working for the United Nations (U.N.) held U.S. resident status and therefore owed taxes and accuracy related penalties for the 2004 through 2009 tax years resulting from unreported wages. The Tax Court found that by executing a U.S. Citizenship and Immigration Services (USCIS) Form I-508, Waiver of Rights, Privileges, Exemptions and Immunities, she had waived all rights, privileges, exemptions and immunities that would otherwise have accrued to her by reason of her occupational status. The waived exemptions included the Code Sec. 893 exemption from gross income of compensation received by an employee of a foreign government or international organization for official services.

***Court's analysis.*** The Tax Court rejected the taxpayer's argument that at the time she signed Form I-508, she did not understand the waiver or appreciate its effects. If lack of understanding due to a language barrier were sufficient to nullify an executed Form I-508, the waiver of exemptions "would become the exception rather than the rule," the court found. Furthermore, the taxpayer presented no statute or judicial precedent to support her argument that the court could cite.

The Tax Court also found that because the taxpayer was a U.S. permanent resident, her wages were not exempt from tax under the U.S.–Finland Tax Treaty. Neither were they exempt from tax under the Vienna Convention on Diplomatic Relations: the taxpayer failed to present evidence that she held diplomatic status or rank. Finally, her wages were not exempt under the *International Organizations Immunities Act.*

*Abrahamsen, 142 TC No. 22, CCH Dec. 59,930; TRC INTL: 12,150.*

# Tax Briefs

*Jurisdiction*

An individual's complaint seeking declaratory and injunctive relief, tax refund and damages for alleged violation of his constitutional rights by various IRS employees was dismissed for lack of subject matter jurisdiction and for failure to state a claim. No *Bivens* cause of action existed and he failed to exhaust his administrative remedies prior to bringing his action under Code Secs. 7422 and 7433.

*Rott v. Oklahoma Tax Commission, DC Okla., 2014-1 USTC ¶50,312; TRC LITIG: 9,254.05.*

*Tax Crimes*

An 18-month sentence imposed on an individual for preparing false income tax returns was vacated and remanded for resentencing because the district court committed procedural error when imposing the sentence. The district court was required to consider the proper facts when sentencing.

*Desrosiers, CA-3, 2014-1 USTC ¶50,314; TRC IRS: 66,462.05.*

*Deductions*

An individual who operated a landscaping business was allowed some claimed deductions and was denied others for lack of substantiation. He was denied a home office deduction for failure to show exclusive use of part of the home. The taxpayer's cancellation of indebtedness income was taxable. Finally, the taxpayer was subject to penalties for failure to file returns or pay taxes, and an accuracy-related penalty.

*Sievers, TC, CCH Dec. 59,937(M), FED ¶48,053(M); TRC SALES: 12,150.*

A married couple that owned an S corporation that constructed and refurbished houses was denied deductions for net operating losses (NOLs) and business expenses that were incurred by the corporation. Penalties for failure to keep books and records were imposed.

*Briley, TC, CCH Dec. 59,936(M), FED ¶48,052(M); TRC BUSEXP: 3,200.*

A physician was not entitled to a net operating loss carryforward for the tax year at issue and late-filing and negligence penalties were imposed. Other than his own testimony, the taxpayer failed to provide any evidence to substantiate the net operating loss.

*Coburn, TC, CCH Dec. 59,935(M), FED ¶48,051(M); TRC BUSEXP: 45,106.*

*Liens and Levies*

The Tax Court has remanded a case to IRS Appeals for further consideration of collection alternatives. The IRS had not requested financial information from a married couple before sustaining a tax lien and proposed levy under Code Secs. 6320 and 6330.

*Uribe, TC Memo. 2014-116; Dec. 59,938(M); TRC IRS: 48,202.05.*

*Refund Claims*

A federal district court lacked subject matter jurisdiction over an individual's untimely tax refund claims. Any recovery was time-barred under the three-year look-back rule in Code Sec. 6511(b)(2)(a) and he failed to show that he was financially disabled under Code Sec. 6511(h) during the applicable period.

*Meconi, DC Del., 2014-1 USTC ¶50,311; TRC IRS: 36,052.05.*

An individual's untimely filed refund claims were dismissed for lack of jurisdiction. The individual failed to file suit within two years from the mailing date of the IRS's first disallowance notice, which clearly instructed him to file suit within the two-year limitations period.

*Palm, Sr., FedCl, 2014-1 USTC ¶50,309; TRC LITIG: 9,052.*

*Tax Assessments*

The IRS failed to show the reasonableness of jeopardy assessments it made against a former state senator who had been convicted of tax fraud. Six months before the IRS made the jeopardy assessment it determined that one was not necessary to preserve its ability to collect the individual's tax liability. However, the IRS relied on the same information available then to justify the jeopardy assessment but failed to show what circumstances changed in the six-month period to make the jeopardy assessment necessary.

*Fumo, DC Pa., 2014-1 USTC ¶50,310; TRC IRS: 54,206.35.*

*Deficiencies and Penalties*

The IRS properly assessed a deficiency against individual taxpayers after refunding more than the amount to which they

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## *Supreme Court Declines Review Of Economic Substance Case*

The U.S. Supreme Court has denied a petition for review of *WFC Holdings Corporation, CA-8, 2013-2 USTC ¶50,485.* The Eighth Circuit Court of Appeals had upheld the IRS's denial of a tax refund claim based on capital losses from a transaction that lacked economic substance.

A financial institution entered into a lease restructuring transaction (LTR) designed and sold by an accounting firm. The scheme's purpose was to generate capital losses that would be used to offset income from capital gains. The Eighth Circuit found that the financial institution had failed to establish any motive for the transaction other than tax avoidance.

*WFC Holdings, Supreme Court Order List, June 9, 2014; TRC SALES: 3,154.*

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## Tax Briefs

*Continued from page 7*

were entitled. On their return, the taxpayers omitted gross Social Security benefits, but correctly entered taxable Social Security benefits. The IRS, incorrectly assuming that the amount entered was the amount of gross benefits, recalculated the taxpayers' tax liability and increased their refund over the correct amount. The excess amount refunded was classified as a "rebate refund" and was recoverable by the IRS through deficiency procedures.

*Thomas, TC, CCH Dec. 59,940(M), FED ¶48,056(M); TRC IRS: 27,050.*

The Court of Appeals for the Federal Circuit has found in a split opinion that a lawyer who served as the executor of his father's estate did not have reasonable cause to rely on the advice of a tax professional who said he could delay filing Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return, until resolution of litigation over the widow's rights under a pre-nuptial agreement.

*Liftin Est., CA-FC, 2014-1 USTC ¶60,678; TRC PENALTY: 3,060.10.*

The IRS was not entitled to increase a taxpayer's deficiency to recover a duplicate nonrebate refund; the Tax Court lacked jurisdiction over the issue. The second refund was a nonrebate refund and such refunds cannot be recovered using the deficiency procedures because of the definition of "deficiency" in Code Sec. 6211.

*YRC Regional Transport, Inc., TC, CCH Dec. 59,934(M), 2014FED ¶48,050(M); TRC IRS: 27,050*

### *Bankruptcy*

A Chapter 7 trustee's objection to a debtor's exemption of tax refunds attributable to the Earned Income Tax Credit (EIC) was rejected. Under state (Ohio) law, the EIC is a form of public assistance; therefore, the exemption statute protected the debtor's interest in the EIC, and did not allow proportional reduction of the exemption. However, the debtor could not exempt the nonrefundable portion of the Child Tax Credit (CTC) because the nonrefundable portion of the CTC was not part of the individual's refund and, therefore, was not property of the estate.

*In re Yost, BC-DC Ohio, 2014-1 USTC ¶50,313; TRC INDIV: 57,450.*

The IRS was entitled to relief from the automatic stay to offset a Chapter 13 debtor's prepetition tax liability with her postpetition tax refund. The confirmation of the plan did not defeat the IRS's nonbankruptcy right of setoff or force payment of an unauthorized refund while the debtor owed unpaid taxes.

*In re Pugh, BC-DC Wis., 2014-1 USTC ¶50,308; TRC IRS: 57,054.05.*

### *Alimony*

An individual was entitled to deduct only a portion of payments he made to his ex-spouse as alimony. The fact that the divorce court retroactively redesignated divorce-related payments as alimony, instead of child support, was disregarded for federal income tax purposes because the order changed the rights of parties or the legal status of the payments.

*Baur, TC, CCH Dec. 59,939(M), FED ¶48,055(M); TRC INDIV: 21,204.*

An individual was not entitled to an alimony deduction for amounts from a back pay award allocated to pay child support nor a deduction for disability benefits he was required to repay. He was liable for the accuracy-related penalty under Code Sec. 6662, because he failed to show reasonable cause and good faith.

*Farahani, TC, CCH Dec. 59,933(M), FED ¶48,049(M); TRC INDIV: 21,200.*

### *Retirement Plans*

For pension plan years beginning in June 2014, the IRS has released the 30-year Treasury bond weighted average interest rate, the permissible range of interest rates used to calculate current plan liability and to determine the required contribution under Code Sec. 412(l) for plan years through 2014, and the current corporate bond yield curve and related segment rates for the purpose of establishing a plan's funding target under Code Sec. 430(h)(2).

*Notice 2014-41, FED ¶46,364; TRC RETIRE: 15,304.10.*

### *Tax Credits*

The IRS has released the inflation adjustment factor for the credit for carbon dioxide ($CO_2$) sequestration under Code Sec. 45Q for 2014. The inflation adjustment factor is 1.0754, and the credit is $21.51 per metric ton of qualified $CO_2$ under Code Sec. 45Q(a)(1), and $10.75 per metric ton of qualified $CO_2$ under Code Sec. 45Q(a)(2). The aggregate amount of qualified $CO_2$ taken into account for purposes of Code Sec. 45Q was 27,114,815 metric tons based on the annual reports filed with the IRS as of June 1, 2014.

*Notice 2014-40, FED ¶46,363; TRC BUSEXP: 55,600.*

### *Civil Damages*

An exempt social-welfare organization was not entitled to statutory and punitive damages for the IRS's disclosure of its Schedule B donor information because it failed to show that the disclosure was willful or the result of gross negligence. The evidence showed only that an IRS agent carelessly sent a reporter an unredacted copy of the organization's Schedule B in response to a FOIA request and inadvertent disclosure does not amount to gross negligence.

*The National Organization for Marriage, Inc., DC Va., 2014-1 USTC ¶50,306; TRC IRS: 9,350.*

### *Like-Kind Exchanges*

An individual's sale of property and his subsequent purchase of unimproved land failed to qualify as a deferred exchange under Code Sec. 1031 because the qualified intermediary, the taxpayer's son, was a disqualified person. The taxpayer could not increase the basis in the property he sold by the amounts paid by him to spouses pursuant to divorce.

*Blangiardo, TC, CCH Dec. 59,932(M), FED ¶48,048(M); TRC SALES: 30,610.15.*

### *Innocent Spouse Relief*

An ex-wife was entitled to equitable innocent spouse relief from liability for a tax underpayment on a joint return. Six factors weighed in favor of relief, and the seventh (economic hardship) was neutral.

*Molinet, TC, CCH Dec. 59,931(M), FED ¶48,047(M); TRC INDIV: 18,058.15.*