Wolters Kluwer

SEPTEMBER 22, 2016
VOL. 103, ISSUE NO. 39, REPORT 39

STANDARD FEDERAL TAX REPORTS Taxes on Parade

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IRS Intends To Identify New Foreign Tax Credit "Splitter Arrangements"

Notice 2016-52

The IRS has announced that it plans to issue regs to address the separation of related income from foreign income taxes paid by a Code Sec. 902 corporation under a foreign-initiated tax adjustment. The regs will identify two new splitter arrangements: a splitter arrangement for ownership changes and a splitter arrangement for distributions.

- ***Take Away.*** "The notice looks to curb prospective tax planning undertaken to separate a foreign corporation's related earnings from future foreign-initiated tax adjustments in an effort to artificially inflate U.S. foreign tax credits, without repatriating the separated earnings," Cory Perry, international tax manager, Washington National Tax Office, Grant Thornton, LLP, told Wolters Kluwer. "Although the notice seems to target a small number of large U.S. multinationals effected by the highly politicized state aid investigations, its impact on foreign tax adjustments exceeding $10 million raises broader concerns for many multinationals subject to foreign tax redeterminations in prior years."

Background

Code Sec. 909(a) generally provides that if there is a foreign tax credit splitting event, with respect to foreign income tax paid or accrued, the tax will not be taken into account before the tax year in which the related income is taken into account by the taxpayer. If there is a foreign tax credit splitting event with respect to foreign income tax paid or accrued by a Code Sec. 902 corporation, Code Sec. 909(b) provides that the tax is not taken into account for purposes of Code Sec. 902 or Code Sec. 960, or for purposes of determining earnings or profits under Code Sec. 964(a), before the tax year in which the related income is taken into account by the Code Sec. 902 corporation or the domestic corporation that meets the ownership requirements of Code Sec. 902(a) or Code Sec. 902(b).

Under Code Sec. 905(c), certain foreign income taxes paid by a Code Sec. 902 corporation after the tax year to which the taxes relate generally are taken into account by adjusting Code Sec. 902 pools of post-1986 foreign income taxes in the tax year in which the taxes are paid, rather than accounting for the taxes in the prior tax year to which the taxes relate. The IRS reported that, in anticipation of a large foreign-initiated adjustment that relates to a prior tax year, a taxpayer may take steps to separate the additional payment of foreign income tax from the income to which it relates.

In response, the IRS determined that guidance is necessary. The guidance is intended to prevent the separation of creditable foreign taxes from related income generally by deferring the right to claim credits until the related income is included in U.S. taxable income, the agency explained.

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IRS Seeks Comments On Planned Changes To Determination Letter Program

Ann. 2016-32

In light of planned changes to the determination letter program, the IRS is requesting comments from stakeholders. The IRS identified a number of concerns raised by stakeholders.

- ***Take Away.*** "This gives us some insight on what's coming next," Elizabeth Thomas Dold, principal, The Groom Law Group, Washington, D.C., told Wolters Kluwer. "Requesting comments on how to simplify the qualified plan drafting process is a positive step, particularly since sanctions are in play if the IRS disagrees with the drafted language. Ideas such as incorporation by reference, sample or model IRS amendments, use of pre-approved plans (and how to retain reliance on the opinion/advisory letter), and eliminating inapplicable provisions are all on the table. "

Background

In Rev. Proc. 2016-37, the IRS announced that it intended to as of January 1, 2017, the five-year remedial amendment cycle system for individually designed plans, currently set forth in Rev. Proc. 2007-44. Effective January 1, 2017, a sponsor of an individually designed plan will be permitted to submit a determination letter application only for initial plan qualification, for qualification upon plan termination, and in certain other circumstances, as described in Rev. Proc. 2016-37.

Stakeholders' concerns

The IRS reported that stakeholders suggested that expanding the use of incorporation by reference could help plan sponsors avoid inadvertent errors in plan documents. The IRS requested comments on any additional qualification requirements that should be permitted to be incorporated by reference as well as suggested language.

Additionally, stakeholders expressed concerns about being required to include certain plan provisions or amendments in situations in which the provisions or amendments are not applicable, or not yet applicable, to their plans. The IRS also requested comments about these concerns.

The changes to the determination letter program may encourage some plan sponsors to transition from sponsoring an individually designed plan to using a pre-approved plan document, the IRS reported. The IRS requested comments on any impediments to that transition process.

References: FED ¶46,408; TRC RETIRE: 51,052.

Foreign

Continued from page 1

Notice 2016-52

Notice 2016-52 describes splitter arrangements arising from application of Code Sec. 905(c) to successor entities. The IRS explained that in this foreign-initiated adjustment splitter arrangement, changes in ownership structures result in a foreign tax credit splitting event. The regs will provide that a splitter arrangement arises when, as a result of a "covered transaction" a Code Sec. 902 corporation pays "covered taxes" during the tax or splitter year, the IRS explained.

Notice 2016-52 also describes splitter arrangements arising from distributions made before the payments of additional tax under foreign-initiated adjustments. The IRS explained that in this foreign-initiated splitter adjustment, distributions are used to move post-1986 undistributed earnings from one Code Sec. 902 corporation to another Code Sec. 902 corporation before the first Code Sec. 902 corporation makes a tax payment pursuant to a foreign-initiated adjustment. As a result, the earnings to which the tax payment relate are taken into account by the payor, but then are taken into account by a covered person that is a Code Sec. 902 corporation before the first Code Sec. 902 corporation pays the tax. The regs will provide that a splitter arrangement exists when a payor that is a Code Sec. 902 corporation pays covered taxes during a tax year and the payor or its predecessor has made a "covered distribution," the IRS explained.

Effective date

The IRS did not release a timetable for issuance of the regs. The regs, the IRS explained, will apply to foreign income taxes paid on or after September 15, 2016.

- ***Comment.*** The IRS added that no inference is intended from Notice 2016-52, describing the regs, as to the treatment of transactions described under current law. Further, no inference is intended as to whether (1) payments under a foreign-initiated adjustment qualify as payments of creditable tax, or (2) taxes paid by a U.S. person under a foreign-initiated adjustment to the tax liability of a Code Sec. 902 corporation are eligible for a Code Sec. 901 foreign tax credit.

References: FED ¶46,405; TRC INTLOUT: 3,300.

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***

STANDARD FEDERAL TAX REPORTS (USPS 518000) (ISSN 0162-3494), TOP Edition published weekly, except for the week of Christmas by Wolters Kluwer, 2700 Lake Cook Road, Riverwoods, IL 60015. Subscription rate $5,565 per year. Taxes on Parade sold separately, subscription rate $335 per year for the TOP Edition. Periodicals postage paid at Chicago, Illinois, and at additional mailing offices. **POSTMASTER:** SEND ADDRESS CHANGES TO STANDARD FEDERAL TAX REPORTS, 2700 LAKE COOK ROAD, RIVERWOODS, IL 60015. Printed in U.S.A.
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Eleventh Circuit Affirms Bulk Land Sale Generated Ordinary Income To Developer

Boree, CA-11, September 12, 2016

The Eleventh Circuit Court of Appeals has affirmed that taxpayers were liable for tax on ordinary income with respect to the bulk sale of a parcel of land following its development. The taxpayers were found to have acted as developers with respect to the land, and income attributed to the land was to reflect that position.

- ***Take Away.*** The taxpayers failed to act in accordance with their claimed intentions—that is, as investors. Given the facts and circumstances, the taxpayers' behaviors with respect to the bulk sale, like that of their behavior with that of other parcels of land they sold to individuals, were in line with that of a developer, and, therefore, the sale, resulted in ordinary income.

Background

The taxpayers owned a real estate business. The taxpayers acquired nearly 1,900 acres of vacant real property. The taxpayers engaged in development activities with respect to the property, to include submitting development plans, deducting business expenses related to the property, and selling several lots to buyers between 2002 and 2006. In 2007, the taxpayers sold its remaining lots, nearly 1,100 acres, in a bulk sale to a development company.

For the 2007 tax year, the taxpayers sought capital gains treatment with respect to the bulk sale. The IRS determined that the sale resulted in ordinary income. The taxpayers were also assessed accuracy-related penalties. The Tax Court ruled in favor of the IRS, finding that the sale resulted in ordinary income, as the property was held for sale in the ordinary course of business.

Circuit Court's analysis

The Eleventh Circuit affirmed the Tax Court's decision, finding that income from the taxpayers' bulk sale of property resulted in ordinary income. The appellate court was not persuaded that the later imposition of land use restrictions was so adverse that it led the taxpayers to hold the property for investment and not for sale, as the restrictions did not act as a bar of all development of the property. The court also gave weight to the taxpayers' continued requests for exceptions from the subsequent land use restrictions so that they could continue with their proposed subdivision.

Additionally, the court found that the Tax Court appropriately determined that the taxpayers continued to sell, or make attempts to sell, lots to individuals after the land use restrictions were in place, and deducted, as opposed to capitalized, expenses related to the property. This activity suggested that the taxpayers engaged in development activities even after the restrictions were imposed. Further, the court found that the Tax Court's determination that the sale of 600 acres, which equaled one-third of the property, amounted to "frequent and substantial" sales, regardless of the fact that the taxpayers sold fewer lots after the land restrictions were in place.

- ***Comment.*** The "frequency and substantiality" of sales is a factor used to determine whether property is being held as a capital asset. Frequent sales tend to suggest that property is not held for investment.

Also, the court noted the taxpayers' failure to distinguish the parcels of land that they intended to use for development purposes from those they intended to hold as investment property. In addition, the court found that the early maps and later plans for the property envisioned a project that included, and continued to include, the property in its entirety, further undermining the taxpayers' contentions that their primary purpose with respect to the property changed.

Penalties

However, the Eleventh Circuit found the imposition of accuracy-related penalties against the taxpayers improper, as they were able to establish the requisite reasonable cause and good faith. The taxpayers relied on the advice of an accounting firm in completing their returns. As such, it was not unreasonable for the taxpayers to both rely on the accountant's decision to claim business expense deductions and capital gain treatment for the same activity.

References: 2016-2 USTC ¶50,406; TRC SALES: 15,104.15.

Over- And Underpayment Interest Rates Remain Same For Fourth Quarter 2016

The IRS has announced that the interest rates on overpayments and underpayments of tax for the calendar quarter beginning October 1, 2016 will remain unchanged. The rates will be:

- 4 percent for overpayments, other than corporations;
- 3 percent for overpayments by corporations (except 1.5 percent of the portion of a corporate overpayment exceeding $10,000);
- 4 percent for underpayments (except large corporations); and
- 6 percent for large corporate underpayments.
- ***Comment.*** The Tax Code provides that the rate of interest on overpayments and underpayments of tax is to be determined on a quarterly basis. The interest rates for the second quarter of 2016 are computed from the federal short-term rate determined during July 2016, based on daily compounding.

IR-2016-121, Rev. Rul. 2016-23, FED ¶46,404; TRC PENALTY: 9,152.

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Merger Termination Fee Is Capital Loss As Opposed To Ordinary Loss, Chief Counsel Determines

FAA 20163701F

IRS Chief Counsel has concluded, through field attorney advice, that a break fee, paid on the termination of a merger agreement, gives rise to a capital loss under Code Sec. 1234A for the corporation that pays the fee. Therefore, the corporation is only entitled to a deduction to the extent of capital gains.

- ***Take Away.*** With the classification of break fees as capital losses and not ordinary losses, corporations must consider, pre-merger, the viability of any proposed merger. Capital losses, by their very nature, are more difficult for corporations to use than ordinary losses, as they can only be deducted to the extent of capital gain.

Background

Following a press release announcing the recommended combination with the target company, the taxpayer formed a new company to enable the merger. Key portions of the merger agreement outlined that shareholders of the taxpayer and the target would receive stock in the new company, that the taxpayer and the target would become subsidiaries of the new company, and that the merger could only go forward if the taxpayer board recommended it to its shareholders. In addition, the taxpayer was required to pay a break fee to the target if the taxpayer withdrew from the merger.

The taxpayer's board recommended the merger. However, before the merger could begin, the Treasury Department issued a notice that adversely affected the expected tax benefits of the proposed merger. The taxpayer withdrew its recommendation for the merger. In accordance with the merger agreement, the taxpayer paid a break fee to the target. The advice sought from the IRS was whether to treat the payment of the break fee as an ordinary loss, deductible in its entirety, or as a capital loss, only deductible to the extent of capital gain.

Applicable law

Code Sec. 1234A provides that the gain or loss attributable to the cancellation, lapse, expiration or the termination of a right or obligation with respect to property that is a capital asset in the hands of the taxpayer shall be treated as a gain or loss from the sale of ta capital asset. A capital asset is defined as any property that is held by the taxpayer, regardless of whether it is connected to the taxpayer's trade or business, unless it falls under an enumerated list of exceptions. Additionally, Code Sec. 1211 provides that in the case of a corporation, losses from sales or exchanges of capital assets are limited to gains from such sales or exchanges; however, excess capital loses may be carried over. Moreover, stock is considered a capital asset.

Chief Counsel's analysis

Chief Counsel determined that the break fee related to a contractual right and obligation concerning a capital asset—the targets right and obligation to acquire stock of the new corporation. In addition, the taxpayer had rights and obligations concerning the target's stock. Therefore, Chief Counsel reasoned, any gain or loss realized by the taxpayer on the termination of the contract, which provided rights and obligations with respect to stock, which is a capital asset, would be capital in nature. As such, Code Sec. 1234A applied and the taxpayer's loss attributed to paying the break fee was a capital loss.

Reference: TRC SALES: 15,054.65.

IRS's Debt Collection Program Needs Improvement, GAO Reports

The Government Accountability Office (GAO) has reported that the IRS should address its Field Collection program, as it lacks clearly defined and measurable objectives that support the program's mission. In addition, the GAO noted that the Field Collection program has provided insufficient guidance to group managers on the use of professional judgment in case selection.

Background. The GAO stated that the IRS Field Collection Program uses automated processes to categorize unpaid tax or unfiled tax return cases, after which group managers select the cases for debt collection. An integral part of the Field Collection program's mission is to apply the tax laws with integrity and fairness to all, the GAO reported.

Findings. The GAO stated that the lack of clearly defined and communicated objective negatively impacts aspects of the Field Collection case selection processes. These aspects include the IRS's ability to measure the program's performance, assess risks to the achievement of objectives, and assess the continued effectiveness of automated processes. In addition, although managers balance a number of considerations when selecting field collection cases, GAO reported that the lack of adequate procedures to guide group managers' use of judgement in selecting cases for collection support the achievement of the program's mission of applying the tax law with integrity and fairness to all.

Recommendations. The GAO recommended that the IRS develop, document and communicate Field Collection program and case selection objectives, including the role of fairness, in clear and measurable terms. In addition, the GAO recommended that the IRS develop, document, and communicate control procedures guidance for group managers to exercise professional judgment in case selection.

Tax Debt Collection: IRS Needs to Define Field Program Objectives and Assess Risks in Case Selection ; TRC IRS: 100.

Cattle Ranching Losses Attributable To Corporation, Not Individual Owners, Tax Court Finds

Barnhardt Ranch Co., TC Memo. 2016-170

The Tax Court has found that two brothers could not use net operating losses from cattle ranching to offset individual income. The taxpayers chose the corporate form for ranching and benefited from that choice. The taxpayers could not disregard that choice whenever it would be beneficial for tax purposes, the court held.

- ***Take Away.*** The IRS examined the taxpayers' returns several times before the present litigation. Each time, the reviews generated "no change" letters. The taxpayers relied, unsuccessfully, on these letters to avoid penalties in the present case.

Background

The taxpayers' father organized a domestic corporation under state (Texas) law. The corporation engaged in cattle ranching, oil field development and other activities. The father died in 2007 and the taxpayers took control of the corporation. The taxpayers served as officers of the corporation.

On their individual income tax returns, the taxpayers offset personal income with losses from the cattle operations. According to the IRS, the corporation managed the cattle business. The taxpayers argued that the corporation did not.

Court's analysis

The court first found that absent extraordinary circumstances a corporation's business is not attributable to its shareholders for tax purposes. Exceptions exist where the creation of the corporation was not followed by any business activity, the purpose of creating the corporation was not a business purpose, or the corporation was the agent of the taxpayers.

Here, the court found that the corporation identified its business activity and operations as "management of cattle ranch" on its federal income tax returns. The corporation bought and sold cattle, held a bank account, purchased and held titles to vehicles, leased ranch property, and held ranch and workers' compensation and employer's liability insurance policies. The corporation also paid for the services of a ranch manager and ranch hands, and it handled their employment tax and income tax documents.

The court further found that for tax purposes, the true owner of income-producing property is the one with beneficial ownership, rather than mere legal title. It is the ability to command the property or enjoy its economic benefits that marks a true owner, the court held.

In this case, the court found that the corporation had command over the cattle to the degree that it was the recognized seller and purchaser of this income-producing property. The corporation deposited all income from the cattle sales into its corporate account and directly paid cattle operation expenses from that account. The court concluded that the corporation was the owner of the cattle for federal tax purposes. As a separate taxable entity, the corporation was the taxpayer to which the net losses that stemmed from the cattle would be attributable.

Agency argument

The court also rejected the taxpayers' argument that the corporation functioned only as their agent and, therefore, the losses were attributable to them as individuals. The court acknowledged that generally, if a corporation is merely the shareholders' agent, then income or expenses generated by the corporation's assets would be income and expenses of the shareholders as principals. In this case, the corporation acted for its own account. The corporation incurred its own debts, entered into its own contracts with third parties for the purchase of goods and services, and bought and sold cattle in its own name; and not as an agent, the court concluded.

Penalties

The court also upheld the IRS's imposition of the penalties. The court found that the taxpayers did not act with reasonable cause and good faith. The court found that the prior IRS exams had reviewed activities in addition to cattle ranching and the taxpayers' reliance on the no-change letters was misplaced.

References: Dec. 60,693(M); TRC CCORP: 7,100.

System Outage Delays Filing Of Form 8976 For Some Organizations

The IRS has announced that a September 13, 2016 computer system outage delayed filing of Form 8976, Notice of Intent to Operate Under Section 501(c)(4), for some organizations. This outage delayed filings for entities that intend to operate as Code Sec. 501(c)(4) organizations.

Background. Year-end 2015 legislation generally requires an organization to notify the IRS of its intent to operate as a Code Sec. 501(c)(4) organization. The IRS has developed Form 8976 for organizations to provide this notification.

Form submission. Organizations unable to submit the Form 8976 as a result of the system outage should submit the form now, the IRS explained. The IRS has stated that it will take any system outages into consideration when evaluating the statutorily imposed penalties for late filing of the Form 8976, and added that it will work with any organization to ensure that it is not subjected to any penalties as a result of the system outage. Organizations that experienced difficulties in submitting Form 8976 should contact the IRS at (877) 829-5500.

TRC EXEMPT: 9,321.

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Receipts From Construction Activities Qualify As Domestic Production Gross Receipts

TAM 201638022

The IRS has concluded, in a technical advice memorandum, that a U.S. construction contractor's activities qualified as construction of real property. Therefore, gross receipts from the projects qualified as domestic production gross receipts (DPGR) under Code Sec. 199.

- ***Take Away.*** Since the Code Sec. 199 deduction became fully phased-in, there has been greater interest in the incentive, and thus in income classification as DPGR.

Background

The taxpayer was a national construction contractor. Although the taxpayer was engaged in a variety of construction business activities, it generally did not erect new structures. Many of the activities in which the taxpayer engaged amounted to renovations of major components and substantial structural parts of existing structures. At issue was whether the substantial renovations qualified as construction of real property so that gross receipts from the projects constituted DPGR.

Law

Under Code Sec. 199, DPGR includes the gross receipts of a taxpayer which are derived from, in the case of a taxpayer engaged in the active conduct of a construction trade or business, construction of real property performed in the United States by a taxpayer in the ordinary course of trade or business. In addition, DPGR includes compensation for the performance of construction services in the United States, as provided under Reg. §1.199(3)(m).

Reg. §1.199-3(m)(3) defines real property as buildings, to include items that are structural components of the buildings, inherently permanent structures, which is defined in § 1.263A-8(c)(3), other than machinery (including items that are components of inherently permanent structures), and inherently permanent land improvements. Reg. §1.263A-8(c)(3) defines inherently permanent structures to include property that is affixed to real property and that will ordinarily remain affixed for an indefinite period of time.

IRS analysis

The IRS concluded that the taxpayer's activities were construction of real property for purposes of Code Sec. 199. The structures themselves weighed hundreds, and some even thousands of tons and they required significant foundations and other groundwork, and concrete support beams and columns. Installations required construction machinery and equipment, which indicated that the structures were attachments to real property. Therefore, the IRS reasoned, the structures were inherently

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AFRs Issued For October 2016

Rev. Rul. 2016-25

The IRS has released the short-term, mid-term, and long-term applicable interest rates for October 2016.

Applicable Federal Rates (AFR) for October 2016

Short-Term	**Annual**	**Semiannual**	**Quarterly**	**Monthly**
AFR	.66%	.66%	.66%	.66%
110% AFR	.73%	.73%	.73%	.73%
120% AFR	.79%	.79%	.79%	.79%
130% AFR	.86%	.86%	.86%	.86%
Mid-Term				
AFR	1.29%	1.29%	1.29%	1.29%
110% AFR	1.43%	1.42%	1.42%	1.42%
120% AFR	1.56%	1.55%	1.55%	1.55%
130% AFR	1.69%	1.68%	1.68%	1.67%
150% AFR	1.95%	1.94%	1.94%	1.93%
175% AFR	2.27%	2.26%	2.25%	2.25%
Long-Term				
AFR	1.95%	1.94%	1.94%	1.93%
110% AFR	2.14%	2.13%	2.12%	2.12%
120% AFR	2.34%	2.33%	2.32%	2.32%
130% AFR	2.54%	2.52%	2.51%	2.51%

Adjusted AFRs for October 2016

	Annual	**Semiannual**	**Quarterly**	**Monthly**
Short-term adjusted AFR	.49%	.49%	.49%	.49%
Mid-term adjusted AFR	.96%	.96%	.96%	.96%
Long-term adjusted AFR	1.45%	1.44%	1.44%	1.44%

The Code Sec. 382 adjusted federal long-term rate is 1.45%; the long-term tax-exempt rate for ownership changes during the current month (the highest of the adjusted federal long-term rates for the current month and the prior two months) is 1.82%; the Code Sec. 42(b)(2) appropriate percentages for the 70% and 30% present value low-income housing credit are 7.37% and 3.16%, respectively, however, the appropriate percentage for non-federally subsidized new buildings placed in service after July 30, 2008, shall not be less than 9%; and the Code Sec. 7520 AFR for determining the present value of an annuity, an interest for life or a term of years, or a remainder or reversionary interest is 1.6%.

References: FED ¶46,409; TRC ACCTNG: 36,162.05.

TAX BRIEFS

Interest Rates

For pension plan years beginning in (month) 2016, the IRS has released the 30-year Treasury bond weighted average interest rate, the unadjusted segment rates, the adjusted rates and the minimum present value segment rates.

Notice 2016-54, FED ¶46,406; TRC RETIRE: 30,556

Deductions

A salesman, who primarily sold maintenance parts and electrical items to manufacturers, was not entitled to business expense deductions in excess of those allowed by the IRS. The taxpayer failed to substantiate any of his claimed deductions in excess of the amounts allowed by the IRS. The taxpayer was also liable for an accuracy-related penalty due to substantial understatement of tax. The record clearly showed that he did not act with reasonable cause and good faith.

Galbraith, TC, CCH Dec. 60,691(M), FED ¶48,107(M); TRC BUSEXP: 24,806

Liens and Levies

A bank was entitled to quiet title to a property on which it had a mortgage because the bank's second mortgage was a security interest under state (Alabama) law that was entitled to priority over an IRS tax lien.

Wells Fargo Bank, N.A., DC Ala., 2016-2 USTC ¶50,405; TRC IRS: 48,152

Refund Claims

A nonprofit medical college that received a refund of overpaid employment taxes was not entitled to interest at the noncorporate rate because it was a corporation. The court rejected the hospital's argument that the parenthetical in the flush language of Code Sec. 6621 incorporates the C corporation limitation of Code Sec. 6621(c)(3)(A) because that language more naturally refers only to the definition of tax period in Code Sec. 6621(c)(3)(B).

Medical College of Wisconsin Affiliate Hospitals, Inc., DC Wis., 2016-2 USTC ¶50,409; TRC PENALTY: 9,152

Tax Assessments

A pastor was not exempt from liability for federal income tax and self-employment taxes. The pastor did not remit income to the church pursuant to his vow of poverty; the payments the church made on his behalf served only to benefit the pastor by meeting his living expenses. Therefore, the payments were included in his gross income. Moreover, the individual did not timely file an application for exemption from self-employment for any of the tax years at issue. Therefore, the individual was liable for self-employment tax.

White, TC, CCH Dec. 60,690(M), FED ¶48,106(M); TRC COMPEN: 6,054.

An individual was denied dependent exemptions for his mother and two nephews; therefore, he was not entitled to file as head of household or to additional Child Tax Credit (CTC) or the Earned Income Credit (EIC). Since the nephews were not dependents, they were not qualifying children so the taxpayer was not entitled to additional CTC. The taxpayer was ineligible for an EIC because his income exceeded the maximum amount allowed for a taxpayer without any qualifying children. Finally, the taxpayer had no dependents during the tax year at issue; therefore, he was not entitled to head-of-household filing status.

Gomez, TC, CCH Dec. 60,696(M), FED ¶48,112(M); TRC FILEIND: 6,154.10

Deficiencies and Penalties

A retired teacher was liable for an accuracy-related penalty based on substantial understatement of income tax because she failed to report a portion of her retirement distributions on her tax return for the tax year at

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Developer

Continued from page 6

permanent because they were affixed to real property both as a result of their weight and their attachment, via welding, bolting or other affixation, to the concrete foundations and support beams and columns.

In addition, the IRS found the structures had useful lives that spanned several decades and would remain affixed to real property from the time of their installation to the end of their useful lives. As such, the IRS determined, the structures were inherently permanent because they were affixed to real property for an indefinite period of time.

Reference: TRC BUSEXP: 6,156.05.

Wolters Kluwer Projects Inflation-Adjusted Tax Brackets And Other Amounts for 2017

The Tax Code requires that federal income tax brackets and certain other figures be adjusted for inflation annually. Wolters Kluwer has projected the 2017 standard deduction, tax bracket amounts and other inflation-adjusted tax figures based on the relevant inflation data just released by the U.S. Department of Labor (DOL).

Key figures. Key projected inflation-adjusted tax amounts that have increased for 2017 include:

The personal exemption for 2017 will remain at $4,050 for 2017, just missing the next level up due to rounding.

The top 39.6 percent bracket start at over: $470,700 for married joint filers (up from $466,950); $444,550 for heads of household (up from $441,000); $418,400 for unmarried filers (up from $415,050); $235,350 for married separate filers (up from $233,476); and $12,500 for estates and trusts (up $12,400 from 2016);

Filers subject to the Alternative Minimum Tax (AMT) will see their exemption amounts increase: $84,500 for married joint filers (up from $83,800); $54,300 for unmarried filers (up from $53,900); $42,250 for married separate filers (up from $41,900); and $24,100 for estates and trusts (up from $23,900).

www.bls.gov/cpi.

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Tax Briefs

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issue. The taxpayer failed to show that her two financial advisers were sufficiently experienced in federal tax law to give her advice regarding the reporting requirements for the retirement distributions she received.

Perry, TC, CCH Dec. 60,695(M), FED ¶48,111(M); TRC PENALTY: 3,108.05

An individual was properly liable for taxes and penalties on income he received from selling nutritional supplements he created. Contrary to his argument, the money was not program income of a tax-exempt organization because no organization existed during the applicable tax years.

George, Jr., CA-1, 2016-2 USTC ¶50,408; TRC INDIV: 51,116

Alimony

A payment an individual received pursuant to a marital settlement agreement (MSA) was alimony, but she did not receive it in the year the IRS claimed. Also, the individual had a theft loss in the year she discovered the theft and was liable for late-filing and accuracy-related penalties for two of the three years at issue.

Leslie, TC, CCH Dec. 60,694(M), FED ¶48,110(M); TRC INDIV: 21,200

Innocent Spouse Relief

A financial management analyst was not entitled to innocent spouse relief for the two tax years at issue. The individual was not entitled to relief under Code Sec. 6015(b) because she knew of the erroneous Schedule C income and deductions related to her husband's law practice that caused the understatement of tax on the returns. Further, it was not inequitable to deny the individual equitable spouse relief.

Canty, TC, CCH Dec. 60,692(M), FED ¶48,108(M); TRC INDIV: 18,054.10

Tax Crimes

The government was not required to show probable cause in order to obtain an *ex parte* order directing the IRS to disclose certain tax return information in furtherance of a public corruption investigation to the Justice Department. The standard of proof under Code Sec. 6103 is "reasonable cause," which is a lesser burden of proof than probable cause. Therefore, the government need only make some rational showing, supported by reliable evidence, that a crime has been committed and that the tax return information may be relevant to that crime.

In the Matter of Application of the United States for Taxpayer Return Information, DC Ky., 2016-2 USTC ¶50,410; TRC IRS: 66,360.05

A vulnerable victim sentencing enhancement was properly imposed on a tax preparer who prepared fraudulent returns claiming false dependents. The test for applying the enhancement is the nexus between the victim's vulnerability and the crime's success, which test was met when the sentencing court found that the tax preparer had stolen children's personal information in order to file fraudulent tax returns.

Adeolu, CA-3, 2016-2 USTC ¶50,407; TRC IRS: 66,462.15

IRS Addresses Leave Donation To Help Louisiana Storm Victims

The IRS has announced that employees who participate in leave-based donation programs, established to provide relief to Louisiana storm victims, will not be subjected to tax on the donated leave. Employers will be permitted to deduct payments made under leave-sharing donation programs.

Leave-based donations. Employers may have adopted, or may be considering adopting, leave-based donation programs in an effort to provide a form of charitable relief for victims of the severe storms and flooding in Louisiana that began on August 11, 2016. Employees can elect to forgo vacation, sick, or personal leave in exchange for cash payments that the employer makes to Code Sec. 170(c) charitable organizations.

Guidance. The IRS will not assert that cash payments an employer makes to charitable organizations in exchange for vacation, sick or personal leave made by an employee constitute gross income or wages to the employee if the payments are: (1) made to the charitable organizations for the relief of victims of the Louisiana storms; and (2) paid to such organizations before January 1, 2018. Participating employees cannot claim a charitable contribution deduction under Code Sec. 170 for the value of the forgone leave. However, employers may deduct the amounts as business expenses, as the IRS will not assert that payments made under a leave-donation program are deductible as charitable contributions.

Notice 2016-55; FED ¶46,407; TRC INDIV: 51,056.

IRS To Cease Paper Return Processing At Three Locations

The processing of paper returns at three IRS campuses is scheduled to end in coming years, the agency has announced. The three affected locations are Covington, Ky., Fresno, Calif., and Austin, Texas.

- ***Comment.*** The IRS attributed the change to the growth of electronic filing.

Changes ahead. Paper return processing will cease in Covington in 2019. In 2021, paper return processing will cease in Fresno and in 2024 in Austin. After 2024, only two locations will process paper returns. The Kansas City, Mo., site will focus on individual returns, and the Ogden location will focus on business returns, the agency reported. According to the IRS, approximately 1,800 employees in Covington, 3,000 employees in Fresno and 2,400 employees in Austin will have their jobs phased-out.

Cost savings. The IRS projected the five-year cost savings from consolidation of processing will be approximately $266 million. Annual savings in subsequent years are projected to be roughly $53 million, the agency added.

- ***Comment.*** The National Treasury Employees Union (NTEU), which represents IRS employees, reported that other operations, including Accounts Management, Compliance, Call-Sites and Automated Collection System (ACS), will continue in the three locations.

IRS Statement, September 14, 2016;TRC IRS: 3,200.