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IRS Announces Per Diem Rates For Post-September 30 Travel

Notice 2016-58

The IRS has announced the special per diem rates that taxpayers can use to reimburse employees for expenses incurred during travel after September 30, 2016. The high-cost area per diem increases to $282 and the low-cost area per diem increases to $189, the IRS reported.

- ***Take Away.*** The IRS had historically issued revenue procedures providing rules for using per diem rates to substantiate the amount of an employee's expenses for lodging, meal and incidental expenses. However, in Rev. Proc. 2011-47, the IRS explained that it would no longer revise the annual revenue procedure, but instead would release an annual notice providing the specific per diem rates and the list of high-cost localities.

Per diem rates

The IRS-approved per diem rate for high-cost areas is $282. The IRS-approved per diem rate for all other areas is $189. The rates apply to per diem allowances paid for travel as of October 1, 2016. As in past years, the employee must still substantiate to the payer the elements of time, place, and business purpose.

Incidental expenses

In accordance with Rev. Proc. 2011-47, "incidental expenses" has the same meaning as in the federal travel regs. Federal travel regs issued by the General Services Administration (GSA) in 2011 describe incidental expenses as fees and tips given to porters, baggage carriers, bellhops, hotel maids, stewards or stewardesses and others on ships. Transportation between places of lodging or business and places where meals are taken, and the mailing cost associated with filing travel vouchers and payment of employer-sponsored charge card billings, are excluded from the GSA definition of incidental expenses.

The rate for the incidental expenses only deduction remains at $5 per day for post-September 30, 2016 travel. Those individuals who do not pay or incur meal expenses for a calendar day of travel away from home may deduct $5 per day for each day away from home.

Transportation industry

The special transportation industry meals and incidental expenses rate for taxpayers in the transportation industry is $63 for any locality of travel in the continental United States. The special transportation industry meals and incidental expense rate is $68 for any locality of travel outside the continental United States. These rates remained unchanged, the IRS reported.

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IRS Dials-Back Letter Rulings For Some RIC Determinations

NPRM REG-123600-16, Rev. Proc. 2016-50

The IRS will no longer issue rulings regarding regulated investment company (RIC) income and asset tests if the ruling will require a determination of whether a financial instrument or position is a security. At the same time, the IRS released proposed regs relating to the RIC income test and asset diversification requirements.

- ***Take Away.*** Rev. Proc. 2016-50 amends Rev. Proc. 2016-3, which identifies areas in which the IRS will not issue rulings or determinations, to reflect the change affecting RICs.

Background

Under Code Sec. 851(a), a domestic corporation registered under the *Investment Company Act of 1940* (1940 Act) at all times during the tax year as a management company, unit investment trust business or business development company, may qualify as a RIC. In Code Sec. 851(b)(2) is the income test, which requires that at least 90 percent of the corporation's gross income for the tax year be derived from dividends, interest, payments with respect to securities loans, gains from the sale or other disposition of stocks, securities or foreign currencies or other income related to investments in stock, securities or foreign currencies such as gains from options, futures, or forward contracts. Additionally, a corporation must satisfy the asset diversification requirements set forth in Code Sec. 851(b)(3) at the close of each quarter of the corporation's tax year to be treated as a RIC.

The IRS explained that the income test and the asset diversification requirements both use the term "securities." An asset is a security for purposes of either the income test or the asset diversification requirements if it is a security under the 1940 Act.

In Rev. Rul. 2006-1, the IRS determined that a derivative contract with respect to a commodity index is not a security for purposes of Code Sec. 851(b)(2). The IRS also determined that income from the contract was not qualifying other income for purposes of Code Sec. 851(b)(2). The IRS modified and clarified Rev. Proc. 2006-1 in Rev. Proc. 2006-31.

The agency explained that after issuance of Rev. Rul. 2006-1 and Rev. Rul. 2006-31, it received a number of private letter ruling requests concerning whether certain instruments that provided commodity exposure were securities for purposes of the income test and the asset diversification requirements. In 2011, the IRS announced it would not issue further private letter rulings addressing specific proposed RIC commodity-related investments while it reviewed the issues and considered guidance of broader applicability.

Rulings

The IRS may decline to issue a letter ruling or a determination letter when appropriate in the interest of sound tax administration, including resource constraints, or on other grounds. Here, the IRS will no longer issue letter rulings on questions relating to the treatment of a corporation as a RIC that require a determination of whether a financial instrument or position is a security.

More guidance

The IRS added that in certain cases, a U.S. person may be required under Code Sec. 951(a)(1)(A)(i) or Code Sec. 1293(a) to include in taxable income certain earnings of a foreign corporation in which the U.S. person holds an interest, without regard to whether the foreign corporation makes a corresponding distribution of cash or property to the U.S. person. The IRS has issued letter ruling that permit an inclusion under these Code provisions to qualify as "other income" derived with respect to a RIC's business of investing in currencies or 1940 Act stock or securities even in the absence of a distribution. The proposed regs specify that for purposes of Code Sec. 851(b)(2), an inclusion under Code Secs. 951(a)(1) or 1293(a) does not qualify as "other income" derived with respect to a RIC's business of investing in stock, securities or currencies, the IRS explained.

References: FED ¶¶46,417, 49,713; TRC RIC: 3,052.

Per Diems

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Effective date

Notice 2016-58 is effective for per diem allowances for lodging, meal and incidental expenses, or for meal and incidental expenses only, paid to any employee on or after October 1, 2016, for travel away from home on or after October 1, 2016. For purposes of computing the amount allowable as a deduction for travel away from home, Notice 2016-58 is effective for meal and incidental expenses or for incidental expenses only paid or incurred on or after October 1, 2016.

- ***Comment.*** For travel during the last three months of the calendar year, a payor must continue to use the same method (per diem method, or high-low method) for an employee as the payor used during the first nine months of the calendar year. The payor may use either the rates and high-cost localities in effect for the first nine months of the calendar year or the updated rates and high-cost localities in effect for the last three months of the calendar year as long as the payor uses the same rates and localities consistently for all employees reimbursed under the high-low method.

References: FED ¶46,414; TRC BUSEXP: 24,912.05.

REFERENCE KEY

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

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IRS Nonacquiesces In Customer Loyalty Program Decision Finding Liability Fixed Under All-Events Test

AOD 2016-003

The IRS has announced its nonacquiescence in an appellate decision finding that a taxpayer's accrued liabilities arising from a customer loyalty program were fixed for purposes of Code Sec. 461 when earned by customers. The Third Circuit Court of Appeals ruled in favor of the taxpayer in *Giant Eagle, 2016-1 ustc ¶50,274.*

- ***Take Away.*** The IRS had prevailed in the Tax Court. However, the Third Circuit, a 2-1 panel decision, reversed on appeal.

Background

The taxpayer, an accrual method taxpayer, operated a chain of supermarkets. Customers could enroll in a loyalty card program. Qualified purchases generated discounts on gasoline and other items sold by the taxpayer.

The taxpayer claimed a deduction for the discounts its customers had accumulated but, at year's end, had not yet applied to fuel purchases. The taxpayer argued that the discounts accumulated but not yet applied by year's end satisfied the all-events test because its liability became fixed on issuance of the discounts. The IRS and the Tax Court rejected the taxpayer's arguments. The Tax Court found that the taxpayer's liability became fixed only after customers applied the accumulated discounts to a fuel purchase. The taxpayer appealed to the Third Circuit.

- ***Comment.*** Under the all-events test, income is included in gross income when all the events have occurred that fix the taxpayer's right to receive the income and allow the amount of income to be determined with reasonable accuracy. On appeal, the sole issue was whether the fact of liability was fixed at year's end.

Third Circuit's ruling

The Third Circuit found that for purposes of the all- events test's fixed liability prong, it was irrelevant that neither the total amount of taxpayer's anticipated liability nor the identity of all the customers who eventually applied discounts toward gasoline purchases could be conclusively identified at year's end. The court acknowledged that there could be a remote and speculative possibility that the amount of the taxpayer's claimed deductions would overstate the value of the rewards its customers ultimately redeemed.

However, the Third Circuit found that the taxpayer had taken action to mitigate that risk. The taxpayer's method for calculating the deduction took into account the chance of non-redemption with reasonable accuracy, the court found. Therefore, the court concluded that the taxpayer could deduct to deduct its loyalty program liabilities.

Nonacquiescence

The IRS will not acquiesce in *Giant Eagle.* In reference to a Circuit Court decision, the IRS explained that nonacquiescence indicates that it will not follow the holding on a nationwide basis. However, the IRS will recognize the precedential impact of the decision on cases arising within the venue of the deciding circuit. The Third Circuit encompasses Delaware, New Jersey, Pennsylvania, and the U.S. Virgin Islands.

References: FED ¶46,421; TRC ACCTNG: 9,464.

IRS Updates Employee Plans Compliance Resolution System

Rev. Proc. 2016-51

The IRS has released guidance updating the Employee Plans Compliance Resolution System (EPCRS) for sponsors of retirement plans that are intended to satisfy the requirements of Code Secs. 401(a), 403(a), 403(b), 408(k), or 408(p), but who have not met the requirements for a period of time. The new procedures make changes to the Self-Correction Program (SCP), the Voluntary Correction Program (VCP), and the Audit Closing Agreement Program (Audit CAP).

- ***Take Away.*** "As anticipated. the updated guidance largely eliminates any reference to the determination letter program, but does provide some helpful changes to audit sanctions for nonamender failures to help with 'foot faults' with required IRS amendments," Elizabeth Thomas Dold, principal, The Groom Law Group, Washington, D.C., told Wolters Kluwer. "And plan sponsors of individually designed plans are still eligible to self-correct significant operational failures if they have a favorable determination letter (it does not need to be a current letter)," Dold noted.

Background

The EPCRS incorporates a system of corrections programs specifically meant for sponsors of retirement plans that have failed to meet any number of requirements under the retirement plan provisions of the code. The EPCRS uses three levels of corrections programs—the SCP, the VCP, and the Audit CAP.

Updates

In 2015, the IRS announced that it was implementing changes to its employee plans compliance determination letter program in 2017. The changes provide that

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IRS Issues Guidance On Making QTIP And Portability Elections

Rev. Proc. 2016-49

The IRS has issued guidance describing the relationship between the portability and the qualified terminable interest property (QTIP) elections. Rev. Proc. 2016-49 modifies and supersedes Rev. Proc. 2001-38.

- ***Take Away.*** The introduction of the portability of the deceased spouse's unused exemption (DSUE) amount generated some questions as to whether an estate could make the election for what would have been an unnecessary QTIP election to maximize the unused exclusion amount. The IRS determined that it is appropriate to provide procedures by which the agency will disregard an unnecessary QTIP election and treat the election as null and void, but only for estates in which the executor neither made nor was considered to have made the portability election. In estates in which the executor made the portability election, QTIP elections will not be treated as void, the IRS explained.

Background

Rev. Proc. 2001-38 provided a procedure by which the IRS would treat the QTIP election as null and void for estate, gift and generation-skipping transfer (GST) taxes if the election was unnecessary to reduce the estate tax liability to zero. When issued, the procedure provided relief to a surviving spouse where the decedent's estate received no benefit from a QTIP election. However, the amendment to Code Sec. 2010(c) affording estates the ability to make portability elections left estates and practitioners with the need for clarity.

Rev. Proc. 2016-49

Rev. Proc. 2016-49, the IRS explained, provides that a QTIP election will be treated as void if:

- The estate's federal estate tax liability was zero, regardless of the QTIP election, based on values as finally determined for federal estate tax purposes, thus making the QTIP election unnecessary to reduce the federal estate tax liability;
- The executor of the estate neither made nor was considered to have made the portability election as provided in Code Sec. 2010(c)(5)(A) and its regs; and
- The procedural requirements of Sec. 4.02 of Rev Proc 2016-49 are satisfied.
- ***Comment.*** Sec. 4.02 of Rev. Proc. 2016-49 provides that a taxpayer must submit the required information in connection with (a) a supplemental Form 706 filed for the estate of the predeceased spouse, (b) a Form 709 (United States Gift (and Generation-Skipping Transfer) Tax Return) filed by the surviving spouse, or (c) a Form 706 filed for the estate of the surviving spouse. The taxpayer must notify IRS that a QTIP election is within the scope of Rev Proc 2016-49, Sec. 3.01; identify the QTIP election that should be treated as void and provide an explanation of why the QTIP election falls within the scope of Rev Proc 2016-49, Sec. 3.01; and provide sufficient evidence that the QTIP election is within the scope of Rev Proc 2016-49, Sec. 3.01.

If a QTIP election falls within the scope of Rev. Proc. 2016-49, the IRS will disregard the QTIP election. Further, the IRS will treat the election as null and void for purposes of Code Sec. 2044(a), Code Sec. 2056(b)(7), Code Sec. 2519(a), and Code Sec. 2652.

- ***Comment.*** The property for which the QTIP election is disregarded under Rev. Proc. 2016-49 will not be included in the gross estate of the surviving spouse under Code Sec. 2044, and the spouse will not be treated as making a gift under Code Sec. 2519 if the spouse disposes of part or all of the income interest with respect to the property. The surviving spouse will not be treated as the transferor of the property for generation-skipping transfer tax purposes under Code Sec. 2652(a).

The IRS further explained that the QTIP election will not be treated as void if:

- A partial QTIP election was required with respect to a trust to reduce the estate tax liability and the executor made the election with respect to more trust property than was necessary to reduce the tax liability to zero;
- The QTIP election was stated in formulaic terms intended to reduce the estate tax to zero;
- The QTIP election was a protective election;
- The executor made a portability election even if the decedent's DSUE amount was zero; or
- The requirements of section 4.02 of the revenue procedure are not met.

Reference: TRC ESTGIFT: 42,262.

Employee Plans

Continued from page 459

determination letters will only be offered to plans on the commencement and termination of a plan. In addition, the Service is eliminating the staggered five-year remedial amendment cycle for individually designed plans.

Rev. Proc. 2016-51 outlines a number of other changes to the EPCRS. Audit CAP sanctions will no longer be a negotiated percentage of the maximum payment amount, but instead will be determined based on the facts and circumstances. However, the maximum payment amount is one such factor that may be considered in the determination. In addition, the sanction will not be generally be less than the VCP user fee applicable to the plan. Further, the sanction for failing to timely adopt a plan amendment that is corrected within three months after the expiration of the remedial amendment period has been reduced to $750, regardless of the number of plan participants. Also, beginning in 2017, all user fees and rules relating to user fees for VCP submissions will be published in the annual EP revenue procedure that sets forth user fees, including VCP user fees.

- ***Comment.*** The IRS has requested comments on the changes. The guidance is to take effect January 1, 2017.

References: FED ¶46,419; TRC RETIRE: 51,450.

IRS Releases Tax Exempt And Government Entities FY 2017 Work Plan

Tax Exempt and Government Entities FY 2017 Work Plan

The IRS recently released its Tax Exempt and Government Entities (TE/GE) FY 2017 Work Plan. The plan provides a review of results from initiatives in place in the last two years, as well as an overview of what TE/GE has planned for its initiatives in 2017.

- ***Take Away.*** The work plan provides a blueprint for FY 2017 for each of the TE/GE functions. According to the work plan, over the next year, TE/GE will operate on a standard rooted in transparency, efficiency, and effectiveness. The ultimate goal, as provided in the work plan, is to provide stakeholders with "a superior experience whenever TE/GE interacts with them."
- ***Comment.*** TE/GE Commissioner Sunita Lough, during a news conference with reporters, stressed the importance of transparency in facilitating compliance and resolving issues. "We will issue interim guidance sometime in October which will let the taxpayers know who are under audit the type of communication we will have so that we can resolve issues sooner," she stated.

Continuing initiatives

Lough stated that much of what is planned will be continuations of the initiatives started in the past two years. Lough noted that TE/GE will continue working to prevent erroneous revocations, as prevention reduces burdens to taxpayers and the service. In addition, TE/GE specifically indicated in its plan that in fiscal year 2017, it will continue to work on the following:

- In the exam area, TE/GE will continue to review how it identifies issues of noncompliance, select and classify returns based on robust filters and modeling, assign the next-best case to the field, and sharpen our information document request process. In addition, TE/GE will be working with other IRS areas including Research Applied Analytics and Statistics, Large Business and International, Small Business and Self Employed, and Criminal Investigation to use a data-driven decision-making process to more precisely focus case-selection.
- Having integrated the Knowledge Management and K-Nets into TE/GE operations, TE/GE will continue to develop resources, answer questions, conduct discussion forums and facilitate collaboration.
- Having successfully combined three case-closing functions into a single entity, TE/GE staff will be cross-trained accordingly.
- TE/GE will continue to monitor the success of Form 8038-CP, created to eliminate several costly filing errors, and make adjustments as necessary.

New developments

TE/GE will continue to work on ensuring that the return selection process is objective, Lough said, particularly in terms of making it more data driven in an effort to cut down on the subjectivity inherent in the process. The work plan also notes that TE/GE plans to develop a referral model that will aid in integrating the next best referral case into the work stream.

Tamera Ripperda, director of exempt organizations, stated that TE/GE is in the process of developing a plan for an ongoing rolling statistical sample of Code Sec. 501(c) organizations. This initiative will present a measure of the impact that the enforcement activity has on voluntary compliance of exempt organizations. "We worked with our research minds to develop a statistical sample approach that will give us a baseline of current compliance in order to then instruct us going forward on what impact our enforcement efforts have on that baseline compliance level."

Reference: TRC IRS: 3,108.

Agricultural Host Organization Fails To Qualify As Business League

The IRS has determined that an organization that was formed to provide an outlet for farmers, cheesemakers, bakers, and crafts people to sell their products did not meet the requirements for tax-exempt status. The organization applied under Code Sec. 501(c)(6). However, the IRS found that it did not operate as a business league.

- ***Comment.*** A business league is an association having some common business interest, the purpose of which is to promote such common interest and not to engage in a regular business of a kind ordinarily carried-on for profit.

Background. An organization was formed to organize and promote a weekly market for farmers and other agricultural producers. The organization provided an outlet for farmers, cheesemakers, bakers, and crafts people to sell their products. The organization maintained that its purpose was to provide a venue for open competition among its members without restriction or limitation on specific products.

IRS analysis. The IRS denied tax-exempt status under Code Sec. 501(c)(6) because the organization did not operate to improve the business conditions of one or more lines of businesses or of a certain area. The IRS determined that the organization provided services for the convenience of its members.

The IRS explained that activities should be directed to the improvement of business conditions of one or more lines of business as distinguished from the performance of particular services for individual persons. Accordingly, an organization whose purpose is to engage in a regular business of a kind ordinarily carried-on for profit, even though the business is conducted on a cooperative basis, is not a business league, the IRS concluded.

LTR 201639016; TRC EXEMPT: 9,102.

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Tax Court Allows Estate To Deduct Ponzi Losses Incurred By 99-Percent Owned LLC

Heller Est., 147 TC No. 11

In a case of first impression, the Tax Court found that an estate properly deducted theft losses from a Ponzi scheme. The theft loss had been incurred by a limited liability company (LLC), in which the estate held a 99 percent interest. As a result of the Ponzi scheme, the LLC's sole asset became worthless, the court found.

- ***Take Away.*** "The taxpayer received a wonderful and just result, largely because the Tax Court's view of Code Sec. 2054 is broader than a narrow state law view of what constitutes a theft. This case will be important going forward for future theft losses and may even allow claims for refunds when the statute of limitations remains open," Robert S. Keebler, Keebler and Associates, LLP, Green Bay, Wisc., observed.

Background

The decedent died in 2008. At the time of his death, the decedent owned a 99 percent interest in an LLC. The decedent's estate timely filed Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return. The Ponzi scheme was revealed after the decedent's death, during the settlement of his estate. The LLC's sole asset was its investment in the Ponzi scheme. After the Ponzi scheme collapsed, the LLC's sole asset became worthless.

The estate claimed a $5 million theft loss deduction relating to the Ponzi scheme. The IRS denied the theft loss deduction. According to the IRS, the estate was not entitled to a Code Sec. 2054 deduction because the estate did not incur a theft loss during its settlement.

- ***Comment.*** The IRS argued that under applicable state law the LLC and not the estate was the victim of the theft. The court found that Code Sec. 2054 allows for a broader nexus (i.e., between the theft and the incurred loss) than did the IRS's interpretation.

Court's analysis

The court first noted that the question of whether an estate is entitled to a Code Sec. 2054 theft loss deduction relating to property held by an LLC was an issue of first impression. According to the court, neither the regs nor legislative history relating to Code Sec. 2054 addressed this question.

The court found that the estate tax is imposed on the value of property transferred to beneficiaries. Code Sec. 2054 provides for a deduction for losses incurred during the settlement of an estate arising from theft. When the LLC lost its sole asset as a result of the Ponzi scheme, the estate, during its settlement, also incurred a loss because the value of its interest in the LLC decreased to zero, the court found.

Here, the nexus between the theft and the value of the estate's interest in the LLC was direct and indisputable, the court found. The estate's loss was directly related to the LLC interest, the worthlessness of which arose from the theft.

The court observed that its construction was in accordance with, and buttressed by, the purpose of the estate tax. While the estate tax is imposed on the value of property transferred to beneficiaries, estate tax deductions are designed to ensure that the tax is imposed on the net estate, which is really what of value passes from the dead to the living. Here, the theft extinguished the value of the estate's LLC interest, thereby diminishing the value of property available to the decedent's heirs. The court concluded that the estate's entitlement to a deduction under Code Sec. 2054 was consistent with the overall statutory scheme of the estate tax.

References: Dec. 60,703; TRC ESTGIFT: 39,350.

Loans From Qualified Plan Triggered Taxable Income, Tax Court Finds

Martinez, TC Memo. 2016-182

The Tax Court has upheld the IRS's determination that loans from a qualified plan were properly included in a taxpayer's income. The taxpayer failed to make the required repayments and did not satisfy any exceptions. The court also upheld the accuracy-related penalty.

- ***Take Away.*** The court noted that a plan participant's loan from a qualified plan is essentially a debt to him- or herself. The administrator has no personal recourse against the participant. The plan will deem the outstanding loan balance to be a distribution of funds, thereby reducing the amount available to the participant from his or account in the future, the court noted.

Background

In 2010, the taxpayer requested two loans from her qualified plan. The loans totaled approximately $33,000. Each loan agreement indicated that the loan was to be repaid in quarterly payments over a five-year period. The loan agreements also indicated that the funds were not to be used as a residential loan.

The taxpayer initially made repayments. Ultimately, the taxpayer stopped making payments and the loans were treated as in default. The balances were deemed taxable distributions. The taxpayer did not report income from the qualified plan distributions on her federal return.

Court's analysis

The court first found that generally distributions from a qualified plan are taxable to the recipient for the tax year of the distribution. The proceeds of a loan from a qualified plan to a participant are treated as, or deemed to be, a distribution and therefore generally included in income. However, there are exceptions, the court found.

In this case, the taxpayer did not satisfy any exception. The taxpayer had failed to make loan payments after May 2012 and

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IRS Expands Types Of Private Letter Rulings That Qualify For Reduced User Fees

Notice 2016-59

The IRS has issued guidance revising the requirements for obtaining a reduced user fee for substantially identical letter rulings found in section 15.07(2) of Rev. Proc. 2016-1. In addition, the, the guidance corrects the amount of the user fee for Foreign Insurance Excise Tax Waiver Agreements.

- ***Take Away.*** Within Notice 2016-59, the IRS has included substantially identical letter rulings requested by taxpayers who are parties engaged in the same transaction to the list of private letter rulings eligible for reduced user fees.

Background

In Rev. Proc. 2016-1, the IRS listed the requirements for reduced user fee for certain substantially identical letter rulings requested for multiple entities with a common member or sponsor, or multiple members of a common entity. The user fee for a letter ruling is $28,300, unless subject to a reduced fee. When the requirements are met, the user fee for subsequent substantially identical letter rulings is $2,700.

Revised requirements

Notice 2016-59 revises the requirements for the reduced user fee to now include substantially identical letter rulings requested by taxpayers who are parties engaged together in the same transaction. This additional basis will be included in Rev. Proc. 2017-1 when it is published in January 2017, the IRS reported. However, the IRS has rendered the change effective immediately to more properly reflect the IRS's actual costs in preparing letter rulings. Pending publication of Rev. Proc. 2017-1, taxpayers may rely on this guidance for purposes of requesting a reduced user fee as of September 27, 2016. Accordingly, this guidance is effective for letter ruling requests received on or after September 27 and requests pending with the IRS as of September 27.

More guidance

Additionally, Notice 2016-59 corrects an oversight of Rev. Proc. 2016-1. Rev. Proc. 2016-1 provided that the user fee for Foreign Insurance Excise Tax Waiver Agreements received on or after February 4, 2016 was decreased from $8,000 to $7,200. However, the decrease was inadvertently omitted from Rev. Proc. 2016-1. The new guidance corrects this oversight.

References: FED ¶46,418; TRC IRS: 12,220.60.

TAX BRIEFS

Internal Revenue Service

The IRS has announced plans to begin the private collection of certain overdue federal tax debts next spring and has selected four contractors to implement the new program. As a condition of receiving a contract, the agencies contracted must respect taxpayer rights.

IR-2016-125, FED ¶46,415; TRC IRS: 45,250

Deductions

An individual failed to obtain permission for his change of accounting method; therefore, he was not entitled to deduct additional legal fees that accrued during the tax year at issue. Since the taxpayer failed to obtain consent to change his accounting method, the IRS could require him to abandon his new accounting method and compute his income and expenses using the cash accounting method.

Mills, TC, CCH Dec. 60,706(M), FED ¶48,122(M); TRC ACCTNG: 21,102.05

False Tax Returns

The entry of a preliminary injunction against a tax return preparer was proper. The government's evidence established a widespread pattern of highly inaccurate returns being filed over several years by the individual and preparers in his offices based on practices that were, at best, grossly negligent and incompetent and, at worst, willful and predatory. This evidence was clearly sufficient to justify the court's use of injunctive relief to ensure the proper enforcement of the internal revenue laws.

Stinson, CA-11, 2016-2 USTC ¶50,417; TRC IRS: 6,200

Liens and Levies

An IRS Appeals officer (AO) did not abuse her discretion by sustaining a levy and a lien against the sole member of a limited liability company (LLC) for unpaid employment taxes. For employment taxes related to wages paid before January 1, 2009, the sole member of an LLC and the limited liability company itself are a single taxpayer liable for reporting and paying employment taxes.

Heber E. Costello, LLC, TC, CCH Dec. 60,710(M), FED ¶48,126(M); TRC IRS: 51,056.15

Refund Claims

A widow's claims for unlawful collection damages and declaratory judgment were dismissed; however, her claims for a tax refund and fees and costs were not. The individual was not a "taxpayer" for the purposes of Code Sec. 7433 because the IRS did not attempt to collect from her personally and she failed to exhaust her administrative remedies. However, the widow's refund claim fell within the waiver of sovereign immunity in Code Sec. 7422 and she exhausted all administrative remedies relating to the refund claim.

Garlovsky, DC Ill., 2016-2 USTC ¶50,421; TRC IRS: 33,150

A married couple's refund claims were dismissed for lack of jurisdiction because one

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Tax Briefs

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year was barred by the statute of limitations and the second year was barred by *res judicata*.

Tanne, DC Utah, 2016-2 USTC ¶50,420; TRC LITIG: 9,050

Interest Abatement

The IRS's denial of a married couple's interest abatement claim for two tax years was not an abuse of discretion. The taxpayers failed to prove that any managerial or ministerial act by the IRS caused an unreasonable error or delay.

Lesende, TC, CCH Dec. 60,704(M), FED ¶48,120(M); TRC IRS: 33,400

Deficiencies and Penalties

An individual who failed to report her unemployment compensation on her return was liable for a substantial understatement penalty. The taxpayer agreed that the unemployment compensation was taxable and that she failed to report it for the year at issue.

Hill, TC, CCH Dec. 60,707(M), FED ¶48,123(M);TRC COMPEN: 6,064

The IRS timely mailed a notice of deficiency to an individual and, therefore, appropriately assessed the related tax deficiencies. Contrary to the taxpayer's argument, the IRS was not required to use a U.S. Postal Service Form 3877 to prove the certified mailing because it used a comparable form that contained the same information.

Garrett, TC, CCH Dec. 60,705(M), FED ¶48,121(M); TRC IRS: 27,156

Tax Crimes

A corporate officer's post-trial motion for acquittal of tax evasion was granted because the government failed to show that she attempted to evade and defeat corporate income tax due and owing "by her." Because the government included the phrase "by her" in the superseding indictment, it was required to prove that she personally owed the corporate income taxes.

Stegman, DC Kan., 2016-2 USTC ¶50,418; TRC IRS: 66,052

The government was properly granted summary judgment in its action to collect a serial tax protestor's delinquent taxes. The individual's claim that under Code Sec. 6203 he was entitled to review IRS Forms RACS 006 and 025 was rejected. Neither the statute nor the regulation mandated the form in which the relevant information must be provided. Moreover, Form 4340 supplied all of the information to which the individual was entitled.

Miller, CA-7, 2016-2 USTC ¶50,416; TRC IRS: 27,202

Bankruptcy

A bankruptcy court's determination that taxes reported on a debtor's late-filed returns were not dischargeable as a matter of law was reversed and remanded. The bankruptcy court failed to consider whether the late-filed returns constituted an honest and reasonable attempt to comply with the tax laws even though the tax had already been assessed and the returns did not report additional liability.

J.R. Biggers, DC Tenn., 2016-2 USTC ¶50,419; TRC IRS: 57,056.05

Plan Loans

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repay these missed amounts within the permitted cure period. The court concluded that the taxpayer did not meet the exception under Code Sec. 72(p)(2). The distributions were taxable distributions as of November 2012, when the grace periods had expired and the taxpayer had defaulted.

The court also found that the taxpayer misinterpreted Code Sec. 72(p)(2)(B)(ii), which addresses an exception for home loans. The taxpayer had affirmed in the loan agreements that the loans were not to be used as residential loans. The court further found that the taxpayer was liable for the 10 percent additional tax on early distributions. The taxpayer did not argue that she satisfied any exception to the additional tax on early distributions.

Additionally, the court found that the taxpayer had also received a distribution for a qualified tuition plan that was not used for eligible educational expenses. Further the taxpayer had other unreported income from a life insurance policy.

Penalty

The court upheld the accuracy-related penalty. The court found that the taxpayer should have known when she stopped repaying the loans, which originated from tax-deferred accounts, that there would be tax consequences.

References: Dec. 60,708(M); TRC INDIV: 30,100.

Drought-Stricken Farmers And Ranchers Have Additional Time To Replace Livestock

The IRS has provided an extended period for farmers and ranchers, forced to sell livestock due to drought, to replace the livestock and defer tax on any gains from the forced sales. Farmers and ranchers whose drought sale replacement period was scheduled to expire on December 31, 2016, will now have until the end of their next tax year.

Background. If a sale or exchange of livestock is treated as an involuntary conversion and is solely on account of drought, flood, or other weather-related conditions, the replacement period ends four years after the close of the first tax year in which any part of the gain from the conversion is realized. Code Sec. 1033(e)(2)(B) authorizes the IRS to extend the replacement period.

Extension. The one-year extension of the replacement period generally applies to capital gains realized by eligible farmers and ranchers on sales of livestock held for draft, dairy or breeding purposes due to drought. Because the normal drought sale replacement period is four years, this extension immediately impacts drought sales that occurred during 2012, the IRS explained. Because of previous drought-related extensions affecting some of these localities, the replacement periods for some drought sales before 2012 are also affected.

- ***Comment.*** Sales of other livestock, such as those raised for slaughter or held for sporting purposes, and poultry are not eligible for the relief, the IRS explained.

IR-2016-127, Notice 2016-60; FED ¶46,420; TRC FARM: 3,206.10.

PRACTITIONERS' CORNER

Sample Client Letter On 2016 Third Quarter Federal Tax Developments

The third quarter of 2016 brought many tax developments from Washington, the IRS and the courts. Practitioners can email this letter to clients to alert them to some of these important recent developments.

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

Re: Important 2016 Third Quarter Federal Tax Developments

Dear Client

During the third quarter of 2016, there were many important federal tax developments. This letter highlights some of the more significant developments for you. As always, contact our office if you have any questions.

Tax legislation

After an extended summer recess, Congress returned to work after Labor Day. The House approved in September legislation (5523) to limit the IRS's authority in conducting civil asset seizures and forfeitures in so-called "structuring" cases. The House also approved legislation (HR 3957) to address the tax treatment of costs associated with certain citrus costs and legislation (HR 5946) to generally exempt the value of Olympic and Paralympic prizes and awards from federal taxation, subject to certain limitations. *Federal Tax Weekly No. 39, September 29, 2016; Federal Tax Weekly No. 36, September 8, 2016.*

Meanwhile, the Senate took the lead in passing a stop-gap spending bill to keep the federal government, including the IRS, open after the end of fiscal year (FY) 2016. The Continuing Resolution continues funding for the IRS and other federal agencies through mid-December. *Federal Tax Weekly No. 40, October 6, 2016.*

Affordable Care Act

The IRS issued proposed regulations clarifying certain provisions of the Code Sec. 5000A individual shared responsibility requirement and the Code Sec. 36B premium assistance tax credit. The regulations address, among other topics, opt-out payments, and benchmark plans. The IRS reiterated that coverage that provides only limited benefits is not minimum essential coverage for the *Affordable Care Act* (ACA). This includes coverage consisting solely of excepted benefits, such as stand-alone vision care or dental care; workers' compensation; and accident or disability coverage. *Federal Tax Weekly No. 28, July 14, 2016.*

"The third quarter of 2016 brought many tax developments from Washington, the IRS and the courts."

The IRS made some changes to forms for ACA-related reporting by applicable large employers and others. The changes affect Forms 1095-B and 1095-C, generally used by ALEs. *Federal Tax Weekly No. 29, September 29, 2016.*

Partnerships

The IRS issued temporary and proposed regulations in August that provide the time, form, and manner of election for a partnership to opt in to the new partnership audit regime under the *Bipartisan Budget Act of 2015* (BBA). The election is available for partnerships that want the new audit regime to apply to a return filed for a partnership tax year that begins before January 1, 2018. *Federal Tax Weekly No. 32, August 11, 2016.*

FACTA

The IRS announced in July that it will stop treating intergovernmental agreements (IGAs) as being in force and effect after December 31, 2016, unless the foreign jurisdiction that entered into the agreement explains why the jurisdiction has not yet brought the IGA into, provides a plan for bringing the IGA into effect, and demonstrates firm resolve to bring the IGA into effect. FFIs in jurisdictions with an IGA in effect will be required to register with the IRS under the Foreign Account Tax Compliance Act (FATCA), unless an exemption applies. *Federal Tax Weekly No. 31, August 4, 2016.*

Code Sec. 469

The IRS determined in August that it would not regroup taxpayer's interests in multiple activities as a single activity under the passive loss rules of Code Sec. 469, or otherwise challenge the taxpayer's grouping of activities. The IRS determined that there was more than one reasonable method for grouping taxpayer's activities. The taxpayer's choices did not show a tax avoidance purpose. Code Sec. 469 disallows losses from a passive activity, defined as a trade or business in which the taxpayer does not materially participate. *Federal Tax Weekly No. 34, August 25, 2016.*

The Court of Appeals for the Ninth Circuit found that a taxpayer's rental losses were not automatically nonpassive because of her status as a real estate professional *Gragg, 2016-2* USTC *¶50,370.* The court rejected the taxpayer's argument that she did not need to show material participation in the rental property. *Federal Tax Weekly No. 33, August 18, 2016.*

Code Sec. 199

The IRS has concluded, in a technical advice memorandum, that a U.S. construction con-

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WASHINGTON REPORT *by the Wolters Kluwer Washington News Bureau*

Obama signs stop-gap spending bill

President Obama signed a stop-gap spending bill on September 29 to avoid a shutdown of the IRS and the federal government after September 30. The stop-gap spending bill extends funding for the IRS and the federal government through mid-December. The bill includes language barring the IRS from issuing regs related to the political activities of exempt organizations.

The stop-gap spending bill was approved by the Senate on September 28 after lengthy negotiations over non-tax provisions. The House voted late on September 28 to approve the measure. Generally, funding is extended at current levels.

"I welcome the Senate's efforts to avert a government shutdown," Sen. Mark Warner, R-Va., said. "Is it perfect? No. Is it necessary? Yes," Sen. Barbara Mikulski, D-Md., said.

Lawmakers have now recessed until after the November elections. Funding for the IRS and other federal agencies for 2017 may be part of a year-end omnibus spending bill. In past years, year-end tax legislation has also included extensions of expiring tax incentives.

Senators introduce bipartisan legislation limiting IRS's forfeiture authority

Bipartisan legislation has been introduced in the Senate to require the IRS to show probable cause that funds relating to structuring transactions under the *Bank Secrecy Act* (BSA) originated from an illegal source or criminal activity before seizing taxpayers' assets. Introduction of the Restraining Excessive Seizure of Property through Exploitation of Civil Asset Forfeiture Tools (RESPECT) Bill follows legislation unanimously approved in the House last week. The Senate bill was introduced by Sens. Sherrod Brown, D-Ohio and Tim Scott, R-S.C.

"It all comes down to fairness," Scott said in a statement. "The IRS should not have the ability to seize property without first meeting a basic, set burden of proof." Current law provides no standard burden of proof the IRS must follow when seizing taxpayers' assets, according to Scott.

"This bill preserves the IRS' ability to go after criminals, while also protecting law-abiding business owners from having their property illegally seized, "Brown said. "The bill makes sure those who are found innocent can get their property back without having to jump through hoops,"" Brown added.

House bill. In the House, the bipartisan Clyde-Hirsch-Sowers RESPECT bill (HR 5523) was unanimously approved on September 22. The measure, introduced by Ways and Means Oversight Subcommittee Chairman Peter Roskam, R-Ill., and Rep. Joseph Crowley, D-N.Y., too, would limit the IRS's authority in conducting civil asset seizure and forfeiture relating to structuring.

The passage of HR 5523 followed a House Oversight Subcommittee hearing earlier this year that examined the IRS's former civil asset forfeiture procedure IRS Commissioner John Koskinen testified at the hearing that the agency's Criminal Investigations Division would no longer seize funds associated with legally sourced structuring activity. The House and Senate bills would essentially codify the IRS's current policy.

House exempts certain CO-OP participants from ACA's individual mandate

The House approved on September 27 the CO-OP Consumer Protection Bill of 2016 (HR 954). The legislation would exempt certain individuals from the Affordable Care Act's (ACA) individual shared responsibility requirement, also known as the individual mandate. The House Ways and Means Committee approved the measure earlier in September.

HR 954, sponsored by Rep. Adrian Smith, R-Neb., heads to the Senate for consideration. If enacted, certain individuals who had coverage under a terminated qualified health plan funded through the Consumer Operated and Oriented Plan (CO–OP) program may be eligible for an exemption from the individual mandate.

Individuals are required under the ACA to maintain minimum essential coverage or make a shared responsibility payment, unless exempt, the Joint Committee on Taxation (JCT) noted in its report on the measure (JCX-69-16). Exemptions under the ACA are available Medicare, Medicaid, TRICARE, and other types of coverage. The House bill would expand the roster of exemptions to include individuals affected by CO-OP terminations. If presented with HR 954, President Obama would veto the bill, according to a Statement of Administration Policy released September 27.

Senate Republicans seek withdrawal of Code Sec. 2704 proposed regs

A group of Senate Lawmakers have asked Treasury Secretary Jacob Lew not to move forward with Code Sec. 2704 proposed regulations, which were released in August (NPRM REG-163113-02). In a September 29 letter Senate Finance Committee (SFC) Chairman Orrin Hatch, R-Utah, SFC member Sen. John Thune, R-S.D., and a number of other Senate Republicans, expressed their concerns to Lew.

"The proposed regulations eliminate or greatly reduce the discounts for lack of control and lack of marketability for family farms and businesses and will thus discourage families from continuing to operate and build their businesses," the GOP lawmakers wrote. "If finalized in their current form, it will significantly increase the estate tax burden on family businesses."

The Obama administration, however, views the proposed regs differently. "It is common for wealthy taxpayers and their advisors to use certain aggressive tax planning tactics to artificially lower the taxable value of their transferred assets. By taking advantage of these tactics, certain taxpayers or their estates owning closely held businesses or other entities can end up paying less than they should in estate or gift taxes," Mark Mazur, Assistant Secretary for Tax Policy, said in August.

Practitioners' Corner

Continued from page 465

tractor'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. The IRS also determined that a taxpayer could not claim any portion of its gross receipts from the sale of its foreign-manufactured products that might be attributable to advertising from a catalogue it printed in the U.S. *Federal Tax Weekly No. 38, September 22, 2016; Federal Tax Weekly No. 27, July 7, 2016.*

Retirement savings

In August, the IRS unveiled a new self-certification procedure for taxpayers who inadvertently miss the 60-day time limit for certain retirement plan distribution rollovers. The IRS described a number of mitigating circumstances, including situations where an error was committed by the financial institution receiving the contribution or making the distribution or the distribution was deposited into and remained in an account that the taxpayer mistakenly thought was an eligible retirement plan. *Federal Tax Weekly No. 35, September 1, 2016.*

The IRS issued final regulations in September that allow qualified plans to facilitate the payment of benefits partly in the form of an annuity and partly as a single sum or other accelerated form. The final regulations generally track proposed regulations issued in 2012 with certain simplifications and clarifications. *Federal Tax Weekly No. 37, September 15, 2016.*

Installment agreements

The IRS proposed in August, in response to budgetary pressures, to overhaul user fees related to installment agreement fees. Under the proposal, the fee for entering into a regular installment agreement would be $225; the fee for entering into a direct debit installment agreement would be $107; the fee for entering into an online payment agreement would be $149; the fee for entering into a direct debit online payment agreement would be $31; and the fee for restructuring or reinstating an installment agreement would be $89. Special rules would apply for lower-income taxpayers. *Federal Tax Weekly No. 34, August 25, 2016.*

Education

The IRS announced in September that only one rollover from a single Coverdell education savings account per individual per year is allowed under Code Sec. 530(d)(5). This conclusion follows in line with the interpretation provided for the limitations on individual retirement arrangement rollovers from the 2014 decision reached by the Tax Court in *Bobrow , T.C. Memo. 2014-21,* the IRS explained. *Federal Tax Weekly No. 36, September 8, 2016.*

The IRS issued proposed regulations that provide detailed guidance to higher education institutions on how to report tuition and other qualified expenses on Form 1098-T, Tuition Statement. The proposed regulations also provide penalty relief for the institution's failure to provide the student's correct taxpayer identification number (TIN). Taxpayers use the information on Form 1098-T to claim education tax breaks. *Federal Tax Weekly No. 31, August 4, 2016.*

Corporations

In July, the IRS issued proposed regulations under Code Sec. 355 that tighten the requirements for corporations to spin off controlled corporations tax-free to their shareholders. Among other things, the regulations would impose new bright-line standards for triggering the device test and for satisfying the active trade or business (ATB) test. *Federal Tax Weekly No. 29, July 21, 2016.*

Individuals

Final regulations were issued in September to explain that marriage for federal tax purposes encompasses opposite-sex marriage and same-sex marriage. The final regulations generally track proposed regs issued after the Supreme Court's decision on same-sex marriage in *Obergefell, 2015-1* USTC *¶50,357.* In *Obergefell,* the Supreme Court held that the Fourteenth Amendment requires a state to license a marriage between two people of the same sex. Further, states must recognize a marriage between two people of the same sex when their marriage was lawfully licensed and performed out-of-state. *Federal Tax Weekly No. 36, September 8, 2016.*

Per diem rates

For post-September 30, 2016 travel, the IRS-approved per diem rate for high-cost areas is $282. For post-September 30, 2016 travel, the IRS-approved per diem rate for all other areas is $189. The rate for the incidental expenses only deduction is $5 per day for post-September 30, 2016 travel. *Federal Tax Weekly Issue No. 40, October 6, 2016.*

Tax administration

The IRS announced in September that private collection agencies will begin working some taxpayer accounts in spring 2017. Congress revived private tax collection in year-end 2015 legislation. *Federal Tax Weekly No. 39, September 29, 2016.*

The Treasury Inspector General for Tax Administration (TIGTA) reported in September that the IRS needs to improve its oversight of Roth IRA conversions. According to TIGTA, the IRS sometimes failed to follow processes that are designed to ensure accuracy in working Roth IRA conversion cases. *Federal Tax Weekly No. 29, September 29, 2016.*

The Tax Court held in July that when the date appearing on a levy notice is earlier than the date of mailing, the timeframe during which a taxpayer may request a collection due process (CDP) hearing is determined by reference to the date of mailing (*Weiss, Dec. 60,676*). The taxpayer unsuccessfully argued that the date appearing on the notice controlled. *Federal Tax Weekly No. 34, August 25, 2016.*

In July, National Taxpayer Advocate Nina Olson renewed her concerns about the IRS's "Future State" initiative. Olson told lawmakers that many taxpayers will not be able to interact with the IRS as envisioned in the Future State initiative because they lack internet access, cannot complete the authentication process, do not trust the security of the IRS systems, or prefer to speak with an IRS employee. *Federal Tax Weekly No. 28, July 14, 2016.*

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

Sincerely,

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COMPLIANCE CALENDAR

■ **October 7**
Employers deposit Social Security, Medicare, and withheld income tax for October 1, 2, 3, and 4.

■ **October 11**
Employees who received $20 or more in tips during September report them to their employers.

■ **October 13**
Employers deposit Social Security, Medicare, and withheld income tax for October 5, 6, and 7.

■ **October 14**
Employers deposit Social Security, Medicare, and withheld income tax for October 8, 9, 10 and 11.

TRC TEXT REFERENCE TABLE

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

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EXEMPT 9,321	437	IRS 42,120	364	RETIRE 66,760.10	449
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FILEBUS 6,140.40	451	IRS 45,152	352	RIC 3,052	458
FILEBUS 12,106	363	IRS 45,202	387	RIC 6,072.05	410
FILEIND 3,202	409	IRS 45,250	447	SALES 15,054.65	436
FILEIND 15,200	452	IRS 66,304	411	SALES 15,104.15	435
FILEIND 21,050	400	PART 60,060	426	SALES 30,604	375
HEALTH 3,102	392	PAYROLL 3,052.25	378	SALES 51,102.10	423

CONFERENCES

October 5: Wolters Kluwer presents its webinar, “Proving Material Participation for the Passive Loss Rules.” The program will cover the seven material participation tests found in the regulations, with a focus on the case law that has defined how to prove that one or more of the tests has been satisfied. For more information, visit *www.krm.com/cch* or call (800) 775-7654

October 12: The Tax Executives Institute hosts its 71st Annual Conference in Philadelphia. Industry experts will discuss tax administration, corporate tax planning, international tax transactions, and more. To register, visit *www.tei.org* or call (202) 638-5601.

October 20-21: ALI-CLE presents Employee Benefit Plans of Tax-Exempt and Governmental Employers in Washington, D.C. The conference will feature leading benefits professionals discussing the impact of the Department of Labor’s fiduciary rule on 403(b) plans, as well as the wind-down of the determination letter program and the issues that it raises. For more information, visit *www.ali-cle.org*.

October 23-26: Wolters Kluwer will host the CCH Connections: User Conference 2016, in Washington, D.C. The conference is designed to provide tax practitioners with the tools, resources and solutions you need to grow, manage and protect your business. To register, visit *CCHUserConference.com*.

October 23-28: New York University presents its 75th Institute on Federal Taxation in New York and again in San Diego on November 13-88. The six-day conference will address all major areas of taxation, including expert discussion of the latest technical, legislative, and planning developments. To register, call (212) 992-3320 or visit *www.scps.nyu.edu*.

November 2-3: The Union League of Philadelphia and the American Bar Association present their 27th annual tax conference in Philadelphia. The program will address the latest federal, state, and international developments and planning opportunities. For more information or to register, visit *www.americanbar.org*.