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STANDARD FEDERAL TAX REPORTS Taxes on Parade

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IRS Issues Final Regs For Defining Marriage Post-*Obergefell*

TD 9785

Final regs have been issued to reiterate that marriage for federal tax purposes encompasses opposite-sex marriage and same-sex marriage. The final regs generally track proposed regs issued after the Supreme Court's decision on same-sex marriage in *Obergefell, 2015-1* USTC *¶50,357*.

- ***Take Away.*** "The final regulations codify the Supreme Court's decisions in *Obergefell* and *Windsor* (consistent with (and replacing) Rev. Rul. 2013-17), clarify the treatment of common law and foreign marriages, and continue to exclude from the definition of marriage for tax purposes domestic partnerships and civil unions," Elizabeth Thomas Dold, principal, The Groom Law Group, Washington, D.C., told Wolters Kluwer.

Background

In *Windsor, 2013-2* USTC *¶50,400*, the Supreme Court struck down Section 3 of the *Defense of Marriage Act* (DOMA), which defined marriage for federal purposes as only the union between members of the opposite sex. After *Windsor,* the IRS announced in Rev. Proc. 2013-17 that it would take a place of celebration approach to same-sex marriage. The IRS also issued guidance for employee benefit plans and others to reflect *Windsor.*

Two years later, 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. The IRS subsequently issued proposed regs to reflect *Obergefell.*

Domestic marriages

For clarification, the final regs provide a general rule for recognizing a domestic marriage for federal tax purposes and a separate rule for recognizing foreign marriages for federal tax purposes. A marriage of two individuals is recognized for federal tax purposes if the marriage is recognized by the state, possession, or territory of the U.S. in which the marriage is entered into, regardless of the married couple's place of domicile.

Foreign marriages

To clarify how foreign marriages are recognized for federal tax law, the final regs provide a specific rule for foreign marriages. Two individuals entering into a relationship denominated as marriage under the laws of a foreign jurisdiction are married for federal tax purposes if the relationship would be recognized as marriage under the laws of at least one state, possession, or territory of the U.S.

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IRS Clarifies Definition Of Real Property For REITs

TD 9784

Final regs have been issued to clarify the definition of real property for purposes of real estate investment trusts (REITs). The final regs generally track proposed regs issued in 2014.

- ***Take Away.*** The IRS first issued guidance some 50 years ago, followed by letter rulings determining if certain assets qualified as real property for purposes of Code Sec. 856. The final regs, like the proposed regs, only apply under the REIT provisions in the Tax Code.

Background

At least 75 percent of a REIT's total assets must include real estate assets, cash and cash items, and government securities, as determined at the end of each quarter of the tax year. The proposed regs defined real property to include land, inherently permanent structures, and structural components. Land includes crops and other natural products until removed from the land. Real property interests also include certain intangible assets.

Final regs

Land. The final regs clarify that air space or water space superjacent to land each qualify as land even if the taxpayer owns only the air space or water space and does not own an interest in the underlying land.

Improvements to land. Some commentators recommended that clearing, grading, landscaping, and earthen dams be treated as improvements to land. To the extent these assets are distinct assets that have value apart from the land, a REIT must analyze these assets separately under the final regs, the IRS explained.

Inherently permanent structures. The IRS explained that inherent permanence alone is not a sufficient basis for a distinct asset to be treated as an inherently permanent structure. The IRS cited large, heavy machinery as an example. Machinery, including automated machinery that functions with little or no human involvement, does not qualify as real property for purposes of Code Sec. 856.

Buildings. The proposed regs provided that a building encloses a space within its walls and is covered by a roof, such as houses, hotels, warehouses, and barns. The final regs retain this definition. The IRS declined to adopt the definition of building used by appraisers, which focus on valuation, for REIT qualification purposes.

Structural component. In generally defining the term structural component, the proposed regulations stated, in part, that a structural component is any distinct asset that is a constituent part of and integrated into an IPS, serves the IPS in its passive function, and, even if capable of producing income other than consideration for the use or occupancy of space, does not produce or contribute to the production of such income. The IRS declined to expand this definition and the final regs retain the language used the proposed regs.

Intangible assets. The proposed regs provided that an intangible asset is real property or an interest in real property if the asset derives its value from real property or an interest in real property, is inseparable from that real property or interest in real property, and does not produce or contribute to the production of income other than consideration for the use or occupancy of space. The final regs clarify that intangible assets that are related to services and that are separable from the real property do not qualify as real property.

References: FED ¶47,043; TRC RIC: 6,072.05.

Marriage

Continued from page 1

Domestic partners

Some stakeholders recommended that regardless of whether a relationship is denominated as marriage, any relationship that has the same rights and responsibilities as marriage under state law should be treated as marriage for federal tax purposes. The IRS declined to take this approach. While some states have extend the rights and responsibilities of marriage to couples in registered domestic partnerships, civil unions, or other similar relationships, these states also retain marriage as a separately denominated legal relationship, the IRS observed. Registered domestic partnerships, civil unions, and similar formal relationships are not treated as marriage for federal tax purposes, the IRS explained.

- ***Comment.*** Registered domestic partners - same-sex couples and opposite-sex couples - may not file a federal return using a married filing separately or jointly filing status.

Other issues

Rev. Rul. 2013-17, the IRS explained, does not distinguish between civil marriages and common-law marriages of same-sex couples. Therefore, same-sex couples in common-law marriages may rely on Rev. Rul. 2013-17 for the purpose of filing original returns, amended returns, adjusted returns, or claims for credit or refund for any overpayment of tax resulting from the holdings of Rev. Rul. 2013-17 and the definitions in

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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 Closes CAP Program To New Applicants; Undertakes Comprehensive Assessment

www.irs.gov

The IRS has announced that no new taxpayers will be accepted into the Compliance Assurance Process (CAP) program for the 2017 application season. The agency explained in a posting on its website and in updated FAQs that it is undertaking a comprehensive assessment of the CAP program.

- ***Take Away.*** "The IRS's update of the CAP FAQs builds on its announcement by the Large Business and International Division (LB&I) earlier this spring that it would stop accepting new applicants to the CAP program, which is designed to be a 'real-time' audit program for large, generally compliant taxpayers. This latest announcement reflects the IRS's ongoing reorganization of LB&I and its constraint in maintaining programs like CAP, due to budgetary and staffing issues," Shamik Trivedi, Manager, Washington National Tax Office, Grant Thornton, told Wolters Kluwer.

Background

Under the CAP program, eligible corporations (those with at least $10 million in assets) work with the IRS to resolve potential issues on a return before the return is filed, allowing for the settlement of tax issues before filing. As a result, these taxpayers may be generally subject to shorter, narrower, and more focused post-filing examinations. A pilot program was introduced in 2005 and made permanent in 2011.At that time, the IRS expanded CAP to include the pre-CAP program and the CAP Maintenance program.

In the Pre-CAP phase, taxpayers work with the IRS in the traditional post-filing examination process to close examinations of filed tax returns with the goal of meeting the CAP selection criteria and progressing to the CAP phase. Taxpayers and the IRS develop an action plan to examine tax returns of the open years within an agreed upon timeframe.

In the CAP phase, taxpayers make open, comprehensive, and contemporaneous disclosures of their completed business transactions. Taxpayers must also disclose the steps within those transactions. Taxpayers who resolve all material items and positions taken with regard to transactions with the IRS are assured prior to the filing of their returns that the agency will accept their returns.

Taxpayers who continue to meet the CAP eligibility requirements and expectations, and have completed two full CAP cycles, may progress, if approved, to the Compliance Maintenance phase. In the Compliance Maintenance phase, the IRS reduces the level of review based on the complexity and number of issues, and the taxpayer's history of compliance, cooperation and transparency in the CAP.

Going forward

The CAP program will not accept new taxpayers for the 2017 application season, scheduled to begin this month. Only taxpayers currently in the CAP and CAP Maintenance phases may submit applications. Taxpayers currently in the CAP phase may be moved into the Compliance Maintenance phase, as appropriate.

Additionally, new pre-CAP applications will not be accepted. Current pre-CAP taxpayers may, however, remain in the pre-CAP phase.

Reference: TRC IRS: 15,106.05.

Marriage

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the final regs, provided the applicable limitations period has not expired.

Some stakeholders asked the IRS for clarification on state community-property laws. The IRS determined that the federal tax treatment of issues under community-property laws was outside the scope of the final regs.

Effective date

The final regs obsolete Rev. Rul. 2013-17 as of September 2, 2016. Taxpayers, the IRS added, may continue to rely on guidance related to the application of Rev. Rul. 2013-17 to employee benefit plans, including Notice 2013-61, Notice 2014-37, Notice 2014-19, Notice 2014-1, and Notice 2015-86 to the extent they are not modified, superseded, obsoleted, or clarified by subsequent guidance.

References: FED ¶47,044; TRC FILEIND: 3,202.

IRS Warns Of More Cyberattacks On Tax Professionals

Tax professionals need to be alert for cybercriminals attempting to remotely access their computer systems to file fraudulent returns, the IRS has cautioned. In recent weeks, the IRS has learned of an uptick in cyberattacks on tax professionals.

- ***Comment.*** Cyberattacks on tax professionals are not uncommon before important filing deadlines, the IRS noted. A similar increase in cyberattacks on tax professionals took place in April. The October 17 deadline for taxpayers on extension is fast approaching.

Cyberattacks. Cybercriminals use remote technology to access client data and e-file fraudulent returns. Refunds are directed to accounts created by the cybercriminals. The IRS urged tax professionals review their preparation software settings and immediately enact all security measures, especially those settings that require usernames and passwords to access the products.

Security measures. The IRS recommended that tax professionals strengthen passwords for both computer access and software access. Passwords should be a minimum eight digits with a mix of numbers, letters and special characters. Staff and personnel should be aware of the increase in cyberattacks, the IRS added.

IR-2016-119; TRC IRS: 66,304.

IRS Relaxes Retirement Plan Hardship Loan And Distribution Rules For Louisiana Flood Victims

IR-2016-115; Ann. 2016-30

The IRS has announced broad-based relief for Louisiana flood victims through liberalized plan loans and hardship distributions. The relief is aimed at individuals affected by of the storms and flooding that began on August 11, 2016.

- ***Take Away.*** The relief, which is aimed at affected individuals who have retirement assets in qualified employer plans, allows qualified employer retirement plans to make loans and hardship distributions to flood victims and their family members. Relief in the form of postponement of certain tax filing and payment/deposit deadlines, as well as claims for disaster-relief casualty losses, for Louisiana storm victims had been announced earlier *(see the August 25, 2016 issue of this newsletter for details)*.

Background

Qualified employer plans have expressed limitations on the permissibility of loans and distributions made from those plans. For Code Sec. 401(k) plans that are part of a profit-sharing or stock bonus plan, elective deferrals may be distributed in certain situations, with conditions of hardship being one of such situations. Similar rules exist with respect to elective deferrals under Code Sec. 403(b) plans. In addition, a Code Section 457(b) may not permit distributions before the occurrence of certain enumerated events, one being when the participant is faced with an unforeseeable emergency. Moreover, although certain other types of plans or accounts are not permitted to make in-service distributions, that is, distributions to a participant who is still an employee, even if there is a hardship, guidance may exist that affords employees with distributions, rules notwithstanding.

Further, Code Section 72(p) imposes certain requirements that so long as they are met, will not result in a plan loan being treated as a distribution under the plan. In order to make a loan or distribution, to include a hardship distribution, a plan must contain language authorizing the loan or distribution. Also, except to the extent a distribution consists of already-taxed amounts, the distribution will be includible in gross income and generally subject to the 10-percent additional tax under § 72(t). Similar rules relating to income inclusion and taxation apply to a distribution from an IRA.

Relief

With Ann. 2016-30, the IRS has stated that it will ease the rules under which employer-sponsored retirement plans make loans and hardship distributions to Louisiana storm victims. A qualified employer plan will not be treated as failing to satisfy any requirement of the tax code or accompanying regulations because the plan makes a loan or a hardship distribution to an employee or former employee for a need arising from the Louisiana storms and flooding.

The employee or former employee must have had a principal residence or place of employment on August 11, 2016 that was located in one of the parishes that have been identified as part of a covered disaster areas, or whose lineal ascendant or descendant, dependent, or spouse had a principal residence or place of employment in one of these parishes on that date. To qualify for the provided relief, a hardship loan or distribution must be made no later than January 17, 2017.

References: FED ¶46,399; TRC RETIRE: 9,354.

IRS To Notify New Victims Of Employment-Tax Identity Theft, TIGTA Reports

TIGTA Ref. No. 2016-40-065

The IRS plans to notify newly-discovered victims of employment-related identity theft starting January 2017, the Treasury Inspector General for Tax Administration (TIGTA) has reported. Initially, the IRS will not notify victims it identified prior to January 2017, but will determine if it is necessary or feasible to notify these victims once the program is underway, TIGTA added.

- ***Take Away.*** The Senate Finance Committee has approved legislation (Stolen Identity Refund Fraud Prevention Act, Sen. 3157) to require among other measures, victim notification of tax-related identity theft. The bill could go to the Senate floor before year-end.

Background

TIGTA explained that employment-related identity theft occurs when an identity thief uses the identity of an innocent taxpayer to gain employment. Taxpayers may first realize they are a victim of employment-related identity theft when they receive an IRS notice of a discrepancy in the income they reported on their tax return. The identification of the discrepancy is from the IRS's Automated Underreporter (AUR) Program match of taxpayer income reported on third-party information returns (for example, W-2, Wage and Income Statement) to amounts reported by taxpayers on their individual income tax returns.

In February 2011, the IRS began identifying e-filed tax returns with an individual taxpayer identification number (ITIN), but the Form W-2 attached to the tax return reported wages and withholding under a different taxpayer's Social Security number (SSN). The IRS refers to these filings as an ITIN/SSN mismatch., TIGTA explained.

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IRS Reports Increases In Individual Income, Deductions And AMT For 2014; Preliminary 2015 Stats Continue Trend

IR-2016-118

The IRS has released statistics on individual income tax returns filed in tax year (TY) 2014, the most recent full year for which data are available. The IRS highlighted changes in individual income, deductions, and the alternative minimum tax (AMT), all of which overall showed increases compared to TY 2013. Preliminary data through mid-July reflecting 2015 tax year returns that have been filed also indicated a repeat of that trend.

- ***Take Away.*** The latest information shows an economy recovering from the Great Recession. Unemployment compensation decreased 35.9 percent to $33.3 billion as the number of returns claiming unemployment fell 19.8 percent to 7.5 million. Capital gains continued to rise with the bull markets.

Income

Taxpayers filed 148.1 million individual income tax returns for TY 2014, reflecting an increase of 0.8 percent from the 146.9 million returns filed for TY 2013, the IRS reported. Total income reported on these returns reached $9.9 trillion, reflecting a 7.4-percent increase from TY 2013. The IRS attributed the growth in income to the increase in net capital gains (less losses) to $698.6 billion for TY 2014. Additionally salaries and wages, the largest component of total income increased 4.8 percent to $6.8 trillion for TY 2014.Adjusted gross income (AGI) rose 7.4 percent to $9.8 trillion TY 2014.

Deductions

Taxpayers claimed itemized deductions on 29.6 percent of all returns filed, the IRS reported. The average for total itemized deductions (after limitation) was $27,447 for TY 2014, compared to the $26,812 average total claimed for TY 2013. The largest itemized deduction for TY 2014 was taxes paid. In second and third place were interest paid, and charitable contributions, respectively. While taxes paid increased 2.8 percent over 2013, the deduction for charitable contributions rose 8.2 percent to $210.6 billion for TY 2014.

- ***Comment.*** Unlike the deductions for taxes paid and charitable contributions, the deduction for interest paid, the second largest itemized deduction, decreased 2.9 percent for TY 2014, likely because of mortgage availability and refinancing at lower rates .

AMT

The IRS reported that the AMT increased 4.4 percent to $28.6 billion for TY 2014. The number of returns with AMT liability also increased rising 8.5 percent to 4.3 million returns.

Higher-income taxpayers

Average tax rates increased as income rose for each AGI category from $20,000 up to $5 million or less, the IRS reported. The average tax rate peaked at 29.4 percent for returns in the AGI class $2 million under $5 million. For the classes above this level, the average tax rates declined to a low of 26.1 percent for taxpayers with AGI of $10 million or more. According to the IRS, the main reason for this decline was that individuals in the classes above $5 million or more tended to report a larger percentage of their AGI as long-term capital gains and qualified dividends, compared to individuals in the lower AGI classes.

Preliminary 2015 statistics

According to preliminary 2015 tax year statistics through mid-July 2016, representing 95 percent of all individuals expected to tile, trends ide ntified from 2014 tax year returns continued. As in 2014, individuals in the upper ranges of AGI had a much higher percentage of their income in capital gain: 19.1 percent for those in the $2-5 million AGI category; 25.7 percent for the $5-10 million AGI range; and 41/7 percent for those individuals with AGI of $10 million or more.

References: FED ¶46,400; TRC IRS: 12,350.

Identity Theft

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Once the e-filed tax returns are identified during processing, the IRS systemically places a code on the tax account of the innocent taxpayer whose SSN was used to commit employment-related identity theft. This code, TIGTA explained, keeps the innocent taxpayer from being selected by the AUR Program if an income discrepancy is identified when the AUR match is performed. However, a similar process has not been established to identify ITIN/SSN mismatches on paper-filed returns, TIGTA reported.

TIGTA's findings

During the period February 2011 to December 2015, the IRS flagged almost 1.1 million taxpayers who were victims of employment-related identity theft, TIGTA reported. The IRS had commenced a pilot notification initiative in 2014. However, TIGTA found that the pilot notification fell short. According to TIGTA, a statistical sample of cases revealed no record of the Social Security Administration (SSA) receiving notification of identity theft in 21 percent of the cases reviewed. Some 11 percent of cases were inaccurately processed by the IRS, TIGTA discovered.

IRS response

TIGTA recommended that the IRS all individuals identified as victims of employment-related identity theft.The IRS responded that programming changes will in January 2017 to notify taxpayers where the IRS has reason to believe they may be a victim of employment-related identity theft. Potential victims identified prior to 2017 may be notified. After the first year of this systemic notification, the IRS explained it will evaluate the results and determine an appropriate course of action with respect to the previously identified potential victims.

Reference: TRC IRS: 66,304.

Couple Responsible For Excess Contribution Tax After Failing To Timely Withdraw Prior Year's Excess Contribution

Wu, CA-7, August 29, 2016

The Seventh Circuit Court of Appeals has held that taxpayers, who contributed more than allowed to their individual retirement accounts and failed to timely withdraw the excess, were not entitled to a refund of the tax they were required to pay on the excess contributions. Under Code Sec. 408(d)(4), the taxpayers were required to withdraw the excess amount contributed in the same tax year as the contribution itself; otherwise, the taxpayers were required to withdraw the prior year's excess contribution before year end.

- ***Take Away.*** Unfortunately for the taxpayers, their interpretation of the provisions governing the excess contribution tax both ignored the language of Code Sec. 408(d)(4) and did not square with that of Code Sec. 4973(b). The taxpayers incorrectly attempted to have Code Sec. 408(d)(4) apply to distributions made outside of the year in which their excess contributions were made. There is some question as to whether the taxpayers would have been afforded some reprieve had they sought to have the excess amounts treated as if they had not been contributed, in line with relief afforded by Code Sec. 4973(b).

Background

The taxpayers, a married couple, each had an IRA in which they contributed $200,000 from the sale of their home in 2007. However, the maximum deduction allowed for IRA contributions in 2007 was $4,000. The taxpayers did not realize their mistake until March 2010, after which point they withdrew the excess contributions and earnings that corresponded with the excess contributions.

The taxpayers informed the IRS of their mistake and asked for a waiver of the excess contribution tax for tax years 2007 to 2009. After paying the applicable taxes and penalties for tax year 2009, the taxpayers requested a refund of the excess contribution taxes attributable to 2009, asserting that they had withdrawn the excess contributions and earnings from that excess before the filing deadline. The IRS denied both the waiver requests and the refund claims.

- ***Comment.*** When a taxpayer contributes more to an IRA than she is entitled, Code Sec. 4973(a) assesses a 6 percent excess contribution tax on the excess amount contributed for each year that the amount is held in the IRA. However, as per Code Sec. 4973(b), when the excess amounts are taken as a Code Sec. 408(d)(4) distribution from an IRA, the contribution will not be treated as a contribution; therefore, no excess contribution tax applies for that year.

District court

The taxpayers filed suit for refunds, contending that Code Sec. 4973(b) provided that they did not incur the excess contributions tax for tax year 2009 because they distributed the excess contributions and earnings before the filing deadline of April 15, 2010. The taxpayers argued that the language of Code Sec. 408(d)(1) meant that the excess contributions, for whatever year added to an IRA, are exempt from the annual tax on excess contributions in a later taxable year if a distribution is made during, or before a return is due for that later taxable year. However, the court held in favor of the government, finding that the contributions were excess contributions for each year they remained in the couple's IRAs. Therefore, the couple could avoid the excise tax if they withdrew the contributions before the filing date for their tax

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Coverdell Education Savings Account Rollovers Limited To One Per Year

The IRS has announced, via program manager technical advice memorandum (PMTA), 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.

Background. Code Sec. 408 governs distributions from IRAs. In *Bobrow,* the Tax Court held that Code Sec. 408(d)(3)(B) limits how often a taxpayer may elect to make a nontaxable rollover contribution. In addition, the court held that the one-year limitation referenced in the section applied to all IRAs maintained by the taxpayer.

Coverdell ESA limitations. Distributions from Coverdell ESAs are governed by Code Sec. 530(d). Generally, any amount distributed from a Coverdell ESA is includible in gross income by the distributee. The IRS found, that given the similarity between the languages of Code Secs. 408(d)(3)(B) and 530(d)(5), with respect to rollovers described in Code Sec. 530(d)(5), only one rollover per individual per year is permitted.

- ***Comment.*** A taxpayer can make only one rollover from a Coverdell ESA to another Coverdell ESA in any 12-month period regardless of the number of Coverdell ESAs the taxpayer owns, the IRS explained. However, a taxpayer can make unlimited transfers from one Coverdell ESA trustee directly to another Coverdell ESA trustee because such transfers are not considered to be distributions or rollovers.

PMTA 2016-10; TRC INDIV: 60,202.25.

CPA Not Entitled To Business Deductions Taken With Insufficient Substantiation; Penalties Assessed

Kilpatrick, TC Memo. 2016-166

The Tax Court has held that a taxpayer, who was a certified public accountant (CPA), was not entitled to deductions in excess of those allowed by the IRS, as he was not able to substantiate a number of his business expenses with adequate records, and others were determined to be nondeductible personal expenses. The court assessed the taxpayer accuracy-related penalties after failing to show that he had reasonable cause to make the underpayments for the years in issue, or that he acted in good faith in making those underpayments.

- ***Take Away.*** The Tax Court seemed to place some importance on the fact that the taxpayer in this instance was not an unsophisticated taxpayer, but rather that he was an experienced CPA. The taxpayer conceded at trial that he was not entitled to the itemized deductions he claimed, which amounted to negligence. This should serve as a cautionary tale that even tax professionals can stumble in claiming home business deductions.

Background

The taxpayer, a full time CPA for a firm, started a home CPA business. He claimed to have traveled 40,601 miles during 2009 for that business, miles that he attributed to "distributing advertising materials." In addition, the taxpayer also purchased antique furniture that he claimed as office furniture and internet service, as well as other purchases from an office supply vendor, and amounts paid for conferences, postage or telephone service. The taxpayer claimed itemized deductions totaling more than $73,000, in addition to business expense deductions and automobile expenses for the 2009 and 2010 tax years.

The IRS denied most of the taxpayer's itemized deductions and automobile expenses for the two tax years in issues; the IRS did allow some portion of the deductions, however, the amount was substantially less. In addition, the Agency rejected his deductions for office expenses and supplies in their entirety.

Court's analysis

Although the taxpayer provided receipts, bank statements, credit-card statements, invoices, check images, calendars, directions and copies of travel-reservation confirmations, the Tax Court held that none of the provided documentation adequately substantiated his claims for deductions. Specifically, the court found that the calendar and directions were prepared at least one year following the period that the taxpayer claimed to have used his vehicle for business travel; additionally, neither form of documentation outlined the amount of business travel, the dates of use, nor the business purpose behind that use. Accordingly, the court determined that the taxpayer was not entitled to any automobile deduction that exceeded the amount the IRS had allowed.

- ***Comment.*** The court ruled that the taxpayer's calendar and directions were insufficient to back his claims for deduction given the gaps of time between when the taxpayer stated that he traveled for business and the creation of the record provided.

In addition, the court held that the taxpayer was not entitled to depreciation deductions for the purchase of the antique furniture that he stated was office furniture because the furniture would retain its value, as is the nature of antiques. Additionally, the taxpayer was not able to deduct purchases from an office supply vendor or amounts paid for conferences, postage, internet service or telephone use, as the court agree with the IRS that these were personal expenses.

- ***Comment.*** The taxpayer incorrectly attempted to deduct amounts paid for the furniture under Code Sec. 162; however, the court noted that real or personal tangible property is a capital expenditure and not an ordinary expense.
- ***Comment.*** The court found that the taxpayer could have sought reimbursement for his conference expenses from his employer. In addition, he failed to substantiate the business use of his cellphone.

The court allowed the assessment of accuracy-related penalties against the taxpayer, attributing his underpayments for the tax years in issue to negligence. The taxpayer conceded at trial that he was not entitled to all his claimed deductions. In addition, although he was an experienced CPA, he failed to show he had reasonable cause or act in good faith with respect to any portion of the underpayment.

References: Dec. 60,687(M); TRC BUSEXP: 24,806.

Contributions

Continued from page 6

return for the tax year in which the excess contribution was made.

Circuit court

On appeal, the circuit court affirmed the district court decision. The court found that the taxpayers' interpretation of Code Sec. 408(d)(4), that the excess contributions, for whatever year added to an IRA, are exempt from the annual tax on excess contributions in a later taxable year if a distribution is made during, or before a return is due for that later taxable year, was incorrect. The court agreed with the government's position that the taxable year referred to in Code Sec. 408(d)(4) meant the taxable year in which the contribution was made into the IRA account. Therefore, the taxpayers were not entitled to relief, as they had not withdrawn the prior year's excess contribution before the end of that tax year.

References: 2016-2 USTC ¶50,396; TRC RETIRE: 66,350.

IRS Reminds Examiners Where To Focus When Auditing Foreign Housing Deduction

JTO/P/09_06_06_17

In an updated audit guide, the IRS has reminded examiners about key elements of claiming the foreign housing deduction. The audit guide is for use in cases where an examiner receives a case involving an individual who claimed the housing deduction under Code Sec. 911 on Form 2555, Foreign Earned Income, Part VI and IX. Examiners must determine if the taxpayer is entitled to the housing deduction.

- ***Take Away.*** The IRS outlined three general steps for examiners. First, the examiner must determine if the individual is a qualified individual; second, determine if the individual's housing expenses are deductible under Code Sec. 911; and third, determine if the individual's housing deduction was properly computed.

Qualified individuals

Only qualified individuals may claim the foreign housing exclusion. A qualified individual must be a bona fide resident or meet the physical presence test, must have a tax home in a foreign country, must have foreign earned income, and must make a valid election.

The IRS reminded examiners that the housing amount deductible under Code Sec. 911 cannot be more than an individual's foreign earned income from self-employment minus the total of the individual's foreign earned income exclusion, plus any amounts excluded under the foreign housing exclusion. A taxpayer, the IRS emphasized, cannot claim a double benefit by taking a credit that may be available under a treaty attributable to amounts excluded from gross income under Code Sec. 911(a).

Housing expenses

Individuals must have eligible housing expenses, the IRS reminded examiners. Eligible housing expenses are reasonable expenses paid or incurred in a foreign country for a qualified individual, his or her spouse, and his or her dependents. These expenses, the IRS explained, include rent, housing repairs (that are not capital expenditures), utilities (other than telephone charges), real and personal property insurance, occupancy taxes, nonrefundable fees for securing a lease-hold, expenses for renting furniture, and residential parking expenses, the agency noted. Eligible housing expenses do not include the cost of domestic help, the IRS added.

Reference: TRC EXPAT: 12,152.

TAX BRIEFS

Internal Revenue Service

The IRS has provided the domestic asset/liability percentages and domestic investment yields needed by foreign life insurance companies and foreign property and liability insurance companies to compute their minimum effectively connected net investment income under Code Sec. 842(b) for tax years beginning after December 31, 2014.

Rev. Proc. 2016-46, FED ¶46,401; TRC INTL: 3,400

Summons

An individual's attempt to quash a summons issued to her employer was dismissed. The summons was issued in aid of collecting the individual's tax liability. Therefore, she lacked standing to move to quash the summons and the court lacked subject matter jurisdiction over her claim.

Stenshoel-Sousa, DC Calif., 2016-2 USTC ¶50,395; TRC IRS: 21,106

A corporation was ordered to obey a summons issued to obtain information to aid in collecting a tax debtor's unpaid tax liability. The IRS set forth a *prima facie* case under *Powell* and the corporation failed to show abuse of process or bad faith.

Cade Corporation, DC Calif., 2016-2 USTC ¶50,394; TRC IRS: 21,054

Collection Due Process

The IRS Appeals office did not err in concluding that the IRS properly mailed deficiency notices to an individual's last known address. Further, even if the individual had rebutted the presumption of receipt, the individual was not entitled to have the deficiency notices set aside but was entitled to challenge the underlying tax liabilities at a CDP hearing. Since the individual was given the opportunity to challenge his tax liabilities but chose not to avail himself of it, he was not entitled to further relief.

Portwine, CA-10, 2016-2 USTC ¶50,393; TRC IRS: 51,056.20

Deficiencies and Penalties

The Tax Court did not clearly err by holding that a former bankruptcy attorney, who was the sole owner of an S corporation that liquidated video stores, improperly claimed carryover net operating loss (NOL) deductions for three years and was subject to a 20-percent penalty on the amount of the understatement for each of the years at issue. Despite having nearly an extra year to find documents for trial, the taxpayer never provided the returns that were the source of the net operating losses, nor did he provide any source documents that would provide direct evidence of the S corporation's purported losses.

Jasperson, CA-11, 2016-2 USTC ¶50,397; TRC BUSEXP: 45,150

Tax Crimes

A district court did not select the incorrect sentencing guideline for an individual's offense or err by failing to grant her a downward variance. In transmitting a fraudulent levy release, the individual not only attempted to evade the IRS's collection efforts, but sent it to a third party while pretending to act for the IRS. In addition, the court meaningfully considered the individual's request for a variance.

D. Cellucci, CA-3, 2016-2 USTC ¶50,392; TRC IRS: 51,064.30