SECTION: ERISA

ALTER EGO TEST FOR WITHDRAWAL LIABILITY REQUIRES SHOWING BOTH COMMON CONTROL AND USE OF SECOND EMPLOYER AS SHAM TO AVOID COLLECTIVE BARGAINING LIABILITY

Citation: Resilient Floor Covering Pension Fund v. M&M Installation, CA9 No. 09-17047, 12/22/10

The Ninth Circuit remanded to the District Court for reconsideration under different grounds whether a non-union employer could be charged a withdrawal liability due to a union pension plan when a union employer owned by the same parties as the non-union employer ceased operations. The Ninth Circuit disagreed with the test used by the District Court to find the non-union employer was the alter ego of the now defunct union employer.

The panel noted that the Ninth Circuit had previously outlined a two-part alter ego test. First, there must be shown to be common ownership, management, operations and labor relations. Neither party disputed this was true in the case of these two employers. The second test is whether the non-union firm is used in a “sham effort to avoid collective bargaining obligations.” The panel complains that the District Court replaced that test with one of whether recognizing the two employers as separate undermines the purposes of ERISA.

However the Court did not find that the second standard could not be satisfied in this case simply because the non-union employer existed first and the union employer was created later to allow the firm to bid on union contracts. The Court found it was possible a double-breasted operation, while not inherently illegal, could be used to avoid payment of a withdrawal liability. Such use would satisfy the second prong of the test.

The Court found there was some evidence that the non-union employer may have engaged in activities that effectively bankrupted the union employer, and that a determination of whether these actions were sufficient to meet the second test would be a matter for consideration of the District Court on remand.

The Court did comment, in an aside, that it was not clear that the alter ego doctrine or veil piercing is consistent with the statutory rule being applied under ERISA when withdrawal liability is at issue. Since neither party disputed that issue in their arguments, the panel accepted the position for this decision, but “suggested” that the District consider whether 29 USC §1392(c) is “intended to be the sole route of redress for evading or avoiding withdrawal liability.”

SECTION: ERISA
ENTITY FOUND TO BE ALTER EGO OF ORGANIZATION IT CONTROLLED, LIABLE FOR PLAN WITHDRAWAL LIABILITY

Citation: The Retirement Plan of the UNITE HERE National Retirement Fund v. Kombassan Holdings, CA2 No. 07-4143-cv, 12/21/10

A Turkish company was held to be the alter ego of a U.S. corporation that incurred withdrawal liability from an employee benefit plan, making the Turkish entity liability for the withdrawal liability of its now defunct related entity. The U.S. entity's shares had been assigned to four other entities when the stock was acquired by the Turkish entity. The assignment was undertaken primarily to get around Turkey's limits on foreign investments by Turkish entities without the Turkish government's approval.

The chairman of the Turkish company was also chairman of each of the four entities to which the shares were assigned, and that company maintained control of the four entities. The President of the U.S. operation looked to the Turkish effective parent as the controlling entity. The Turkish entity numerous times in the U.S. entity's bankruptcy case represented to the bankruptcy court that it had effective control of the U.S. entity.

The Turkish entity argued that the alter ego concept should not apply because the transfers were not undertaken to avoid ERISA liability, but rather for wholly unrelated reasons. As well, the entity was not a successor company formed with the intent of evading the U.S. entity's ERISA liabilities. However, the Second Circuit Court of Appeals held that these issues were not relevant—what was relevant was that the Turkish entity was that it was the actual, if not technically the legal, owner of the enterprise in question and directed its operations.

SECTION: 1
ADDITIONAL COST OF LIVING FIGURES FOR 2011, ADJUSTED FOR THE TAX RELIEF, UNEMPLOYMENT INSURANCE REAUTHORIZATION, AND JOB CREATION ACT OF 2010, RELEASED BY THE IRS

Citation: Revenue Procedure 2011-12, 12/23/10

The IRS released an additional set of inflation adjusted figures for 2011. The new release is in addition to adjustments announced in Rev. Proc. 2010-40, 2010-46 I.R.B. 663. These adjustments are primarily required due to the extension of certain provisions contained in the Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010.

The new notice contains the tax rate tables for 2011 for all filing statuses, adjusted to reflect the continuation of the 2010 rates contained in the tax act.

The earned income number that is used in computing the refundable child tax credit pursuant to §24(d)(1)(B)(i) remains at $3,000. As well, the maximum HOPE scholarship credit available under §25A(b)(1) remains at $2,500.

A minor adjustment is made in the phase-out levels for the Lifetime Learning Credit, with the adjustments beginning for taxpayers with modified adjusted gross income in excess of $51,000 ($102,000 for married couples filing a joint return). For 2010 the phase-out began at $50,000 and $100,000 respectively.

The limits for the earned income credit for 2011 are as follows:

	Number of Qualifying Children			
Item	**One**	**Two**	**Three or More**	**None**
Earned Income Amount	$9,100	$12,780	$12,780	$6,070
Maximum Amount of Credit	$3,094	$5,112	$5,751	$464
Threshold Phaseout Amount (Single, Surviving Spouse, or Head of Household)	$16,690	$16,690	$16,690	$7,590
Completed Phaseout Amount (Single, Surviving Spouse, or Head of Household)	$36,052	$40,964	$43,998	$13,660
Threshold Phaseout Amount (Married Filing Jointly)	$21,770	$21,770	$21,770	$12,670
Completed Phaseout Amount (Married Filing Jointly)	$41,132	$46,044	$49,078	$18,740

For 2011, the earned income credit will be disallowed under §32(i) for excess investment income if such income exceeds $3,150.

The standard deductions for 2011 will be:

Filing Status	Standard Deduction
Married Individuals Filing Joint Returns and Surviving Spouses	$11,600
Heads of Households	$8,500
Unmarried Individuals (other than Surviving Spouses and Heads of Households)	$5,800
Married Individuals Filing Separate Returns	$5,800

The standard deduction for a person eligible to be claimed as a dependent on another's tax return will be further limited to no more than the greater of $950 or the individual's earned income plus $300. The additional standard deduction for the aged or blind is increased to $1,150, with the amounts increased to $1,450 if the individual is unmarried and not also a surviving spouse.

The qualified transportation fringe monthly limitation for 2011 under §132(f)(2)(B) is set at $230.

The personal exemption for 2011 will be $3,700.

For tax years beginning in 2011, the maximum deduction for interest paid on student loans will be capped at $2,500, with the deduction phasing out as a taxpayer's modified adjusted gross income exceeds $60,000 ($120,000 for married couples filing a joint return). The entire deduction will be phased out for taxpayers with incomes above $75,000 ($150,000 for a married couple filing a joint return).

SECTION: 106
IRS ALLOWS USE OF FSA OR HRA DEBIT CARDS TO PURCHASE PRESCRIBED OVER-THE-COUNTER MEDICINES AND DRUGS FROM VENDORS MEETING SPECIFIC REQUIREMENTS

Citation: IRS Notice 2011-5, 12/23/10

The IRS modified the guidance originally published in Notice 2010-59 regarding the use of FSA and HRA debit cards for use for the purchase of over-the-counter medicines. The original notice prohibited such use entirely after January 15, 2011.

The guidance is modified to indicate that reimbursement is allowed for a drug that is a prescribed drug (determined without regard to whether such drug is available without a prescription) or is insulin.

Under the revised rules, the cards may continue to be used to purchase prescribed over-the-counter medicines if all of the following conditions are satisfied:

1. prior to purchase, (i) the prescription for the over-the-counter medicine or drug is presented (in any format) to the pharmacist; (ii) the over-the-counter medicine or drug is dispensed by the pharmacist in accordance with applicable law and regulations pertaining to the practice of pharmacy; and (iii) an Rx number is assigned;
2. the pharmacy or other vendor retains a record of the Rx number, the name of the purchaser (or the name of the person for whom the prescription applies), and the date and amount of the purchase in a manner that meets IRS recordkeeping requirements;
3. all of these records are available to the employer or its agent upon request;
4. the debit card system will not accept a charge for an over-the-counter medicine or drug unless an Rx number has been assigned; and
5. the requirements of previously issued Prop. Treas. Reg. § 1.125-6, Rev. Rul. 2003-43, 2003-1 C.B. 935; Notice 2006-69, 2006-2 C.B. 107; Notice 2007-2, 2007-1 C.B. 254; and Notice 2008-104, 2008-2 C.B. 1298 are followed.

The cards can also be used to purchase over-the-counter medicine or drugs that have been prescribed after January 15, 2011 at pharmacies for which 90% of the store's gross receipts for the prior tax year consisted of items which qualify for medical care under §213(d) even if they do not have an inventory information system in place.

For purchases at all others merchants not meeting either of the two above requirements, FSA or HRA debit cards may not be used to purchase over-the-counter medicines or drugs after January 15, 2011.

SECTION: 162
DUTY OF CONSISTENCY APPLIED TO PARTNERSHIP AND SETTLEMENT FUND WHERE RECEIVER CONTROLLED RETURNS OF BOTH

Citation: CCA 201052004, 12/30/10

The receiver appointed to handle the assets of a partnership that was found to have been involved in a Ponzi scheme ended up with a bit of a tax issue. The receiver established a settlement fund consisting of income generated from the partnership's remaining legitimate business activities and interest earned on that income.

The receiver also prepared and filed the income tax returns for the partnership. Those returns contained deductions for expenses incurred by the receiver in gathering and conserving the partnership's assets. However the returns did not contain the interest income on the settlement fund, apparently believing it should issue Forms 1099 to the investors who would receive settlement payments. Such 1099s were not actually ever issued so that that interest on the settlement fund was never reported to the IRS.

The receiver began making payments out of the settlement fund to investors. In the year following the start of payments to the investors, the receiver noticed the problem with the Form 1099s and contacted the IRS.

It was determined that, in fact, the receiver should have been filing Form 1120-SF (U.S. Income Tax Return for Settlement Funds) for each year the fund was in existence and the interest reported there. Such returns should have reported the interest income on the settlement fund and, had the returns be filed timely, a deduction would have been allowed for the expenses incurred by the receiver in gathering and conserving the partnership assets.

Complicating matters was the fact that the statute of limitations for assessing tax on the partnership returns for the years those expenses were incurred had expired—returns on which these same expenses had been deducted.

The IRS concluded that the duty of consistency doctrine applied in this case to prevent the deduction of those expenses on the 1120-SF for the years in question. The doctrine generally applies when the following three elements are present:

1. A representation has been made by the taxpayer in one year
2. The IRS has relied on that representation and
3. The taxpayer now seeks to change that representation at a later time when the statute of limitations bars an adjustment to the return for the earlier year

The receiver protested that denying those deductions would harm the investors, as the settlement fund would bear the entire burden, and, in any event, the partnership and the settlement fund were not the same taxpayer.

While agreeing these entities were two separate tax entities, the IRS pointed out that the duty of consistency doctrine can apply to related taxpayers. The IRS concluded that the fact that the receiver had control over both taxpayers was sufficient to cause the duty of consistency to apply.

SECTION: 165
COURT, FOLLOWING THE COHEN DOCTRINE, ALLOWS REDUCED AMOUNT OF MOVING EXPENSES AND CASUALTY LOSS

Citation: Zilberberg v. Commissioner, TC Memo 2011-5, 1/5/11

Mark Zilberberg's case gave the Tax Court cause to apply the doctrine first outlined many years ago in the 1930 case of entertainer George M. Cohan (39 F.2d 540). Mr. Zilberberg claimed a right to moving expenses of $5,000 and casualty losses of $36,350 for 2005.

In that year Mr. Zilberberg moved to Key West, Florida to take up employment. However his timing was a poor, as Key West was affected by four hurricanes that year, and as a result of Hurricane Wilma Mr. Zilberberg had water up to his chest for four days where he lived. He testified that this flooding ruined most everything that he owned.

Mr. Zilberberg had no records to back up either claimed deduction, apparently making rough estimates of the amounts he had paid. However before and during trial these estimates changed, creating some confusion about the exact amounts being claimed. The Court, while not accepting his testimony to support the full amounts he claimed, found he had clearly incurred expenses in moving to Key West to take up new employment and had suffered casualty losses.

As such, the Court allowed Mr. Zilberberg moving expenses of $3,000 and a casualty loss of $15,000. Aside from Mr. Zilberberg's rough estimates, he had made no other attempts to obtain additional documentation to back up his claim. The Court found that at least some of the reason for the lack of detail fell on Mr. Zilberberg, but a portion could also be attributed to the hurricane—so the Court effectively arrived at its own intermediate amounts.

SECTION: 179D
§179D DEDUCTION IS SUBJECT TO BASIS LIMITATION WHEN PASSED OUT FROM A PARTNERSHIP OR S CORPORATION

Citation: IRS Legal Memorandum AM2010-007, 12/23/10

Government entities that have energy efficient commercial building property that is installed on or in property the entity owns are able to allocate the §179D deduction to the person primarily responsible for designing the property. In this memorandum, the IRS considers the impact of transferring such a deduction to a partnership or S corporation.

The memorandum notes that many of the designers who receive this allocation of the §179D deductions from government entities operate as S corporations and partnerships. Because there's little need for capital in these service entities, they often distribute virtually all of their cash to the owners and have little in the way of assets. Thus the basis of the interests held by these owners often is relatively low.

The IRS has become aware that some partners and S corporation shareholders in this situation are taking the position that the §179D deduction does not reduce the basis of the owner's interest. The taxpayers argue that the deduction is a partner or shareholder level deduction rather than one of the entity, meaning it is not impacted by the limitation on deductions in excess of basis under §704(d) for a partnership or §1366(d) for an S corporation.

The IRS memorandum disagrees with this position. The memorandum points out that the governmental agency contracts with the partnership or S corporation and not the individual owners. Unlike the provisions found under §199(d)(1), there is no similar provision in §179D that causes the deduction to apply at the partner or shareholder level.

SECTION: 183
EVEN THOUGH TAXPAYERS HAD TEN YEARS OF LOSSES, COURT FOUND THEY OPERATED HORSE BREEDING BUSINESS WITH A VALID PROFIT MOTIVE

Citation: Frimml v. Commissioner, TC Summary Opinion 2010-176, 12/28/10

Once again the Tax Court was facing the question of whether a horse breeding operation that generated substantial and continuing losses (this time over ten years) was a hobby operation where losses would be disallowed under §183.

The Court found the taxpayers had generally conducted their horse breeding activity in a businesslike manner. The taxpayers adapted their plan over time to take into account changing circumstances and had identified potential sources of significant future revenue. The Court took special note of the taxpayer's well-reasoned justifications for decisions to heal one horse that had prospects, while putting down a different horse where they determined the cost to heal her leg exceeded the projected price in selling her. However the Court found these positives offset by their sloppy recordkeeping and limited advertising.

The taxpayers showed extensive knowledge and expertise in the area, a factor in their favor. The court also noted they spent substantial amounts of time devoted to the operation, even having one of them stay back from family events so that the horses were not left unattended—again, factors that indicate a true profit motive.

The real estate they had purchased to conduct the activity had appreciated in value, and they had a reasonable expectation one of their horses would appreciate in value, both of which justified their willingness to accept continued operating losses. This factor favored the taxpayers.

However the taxpayers had not previously profitably operated such an enterprise and converted it to profitable operations, a factor that favored the IRS.

The Court found that because this was a horse breeding operation, the years in question remained in the range of a reasonable start-up period when losses would be expected to be incurred, rendering the operating losses and lack of profit during these years a neutral factor.

While the taxpayers had salaries of over $90,000 a year, the Court did not find that they were using their salaries to support the horse business as a hobby. Finally, the taxpayers did not ride the horses in question, nor did they allow family and friends to ride them. Thus the activity did not appear to have significant elements of personal pleasure and recreation to the taxpayers, factors that indicated a profit motive.

Since most factors favored the taxpayers, the Court found that they had the required profit motive and allowed their losses for the years in question.

SECTION: 213
TAXPAYER ALLOWED TO DEDUCT MEDICAL EXPENSES AND TAXES PAID BY HER MOTHER ON HER BEHALF

Citation: Lang v. Commissioiner, TC Memo 2010-286, 12/30/10

Judith Lang's mother, Frances, paid Judith's medical expenses of $27,776 directly to the providers of the medical services. Frances also paid directly to the city government $5,508 of real estate taxes that were owed by Judith.

Judith claimed a deduction for both payments on her Schedule A for 2006. The IRS argued that Judith could not claim a deduction because she did not pay the expenses.

The Tax Court agreed with Judith that the proper way to view the transaction was as a gift to Judith followed by the payment of the expenses. That was true even though, for gift tax purposes, the payment was not treated as a taxable gift by operation of §2503(e)(1)'s exclusion of direct payment of medical expenses of the donee from gift taxation. The Tax Court noted that the gift tax consequences do not control the income tax treatment, and that it was proper to look at the substance of the transaction rather than the form.

The Court found similarly that substance should rule over form on the deduction of property taxes. The tax could only be deducted by Judith, as she was the only person who owed the tax.

Even though the Court applied substance over form in this case in favor of the taxpayer, that result is a bit unusual. However, unlike cases where taxpayer unsuccessfully attempt to argue substance over form, Judith was not in control of the form of these transactions—her mother was the person making the transactions. When the taxpayer is the person in charge of the form (or one of those involved in setting the form), the Tax Court is much less likely to accept a taxpayer argument to look at substance over form.

SECTION: 274
TAXPAYER WHO MAINTAINED LOG FOR 77% OF TRIPS ALLOWED FULL AMOUNT OF CLAIMED AUTO EXPENSES

Citation: Barajas v. Commissioner, TC Summary Opinion 2011-2, 1/5/11

It's not often we see the taxpayer win when the IRS attempts to disallow claimed auto expenses by pointing at §274(d)'s requirements—but in this case the IRS failed to prevail.

The Tax Court pointed out that the IRS's attempt to disallow Martin Barajas was based on imposing a standard for documenting deductible auto mileage that went beyond the IRS's own regulations under §274. Mr. Barajas had fully detailed logs for 77% of the trips that he claimed, so the IRS wished to disallow all of the mileage which was not accounted for in the logs.

Reg. §1.274-5T(c)(3)(ii)(A) requires only that the taxpayer maintain a log for a representative portion of the year, and the Court found that the IRS's own examples in those regulations of "acceptable" partial year logs involved logging of only ¼ of the year—far less than the 77% that Mr. Barajas had maintained. Independent evidence, in the form of ATM withdrawals, gas purchases, subcontractor invoices and cancelled checks showed that the taxpayer had taken the additional trips.

SECTION: 280A
MINIMAL USE OF AREA FOR PERSONAL PURPOSES DISQUALIFED AREA FROM INCLUSION AS PART OF OFFICE IN THE HOME

Citation: Rayden v. Commissioner, TC Memo 2011-1, 1/3/11

The Tax Court found it implausible that the taxpayers in question had truly used 70% of their personal residence exclusively for business purposes, and rather accepted the IRS's finding that only 43% of the residence met the requirements. The case serves to again remind us of just how little personal use is enough to eliminate a deduction for an office in the home.

The Court noted that even minimal personal use of an area disqualified it from meeting the exclusive use test found in IRC §280A(c)(1). The Court understood why the taxpayer believed that an area that used only minimally for personal use during the year and otherwise was used for business purposes should generate a deduction. However, that isn't the law.

Specifically the Court found that the taxpayer's concession that he and his family may have occasionally eaten in the breakfast area disqualified that area from meeting the exclusive use test. Similarly, use of the den, vestibule and adjoining bar one or two times a year by visiting family served to disqualify those areas. The dining room similarly failed to meet the test when the taxpayer conceded that one or two nights a year when his sons were in town the family would eat in that area.

The Court did note that disqualifying personal use did not extend to the use of a room solely as a passage to get from one nonbusiness location to another. So the mere fact that individuals had to pass through the living room to get from one room to another did not serve to disqualify that room from being treated as used exclusively for business.

SECTION: 401
ESOP DETERMINED TO FAIL TO QUALIFY AS A QUALIFIED PLAN FROM INCEPTION DUE TO DOCUMENT AND OPERATIONAL FAILURES

Citation: Michael C. Hollen, D.D.S., P.C. v. Commissioner, TC Memo 2011-2, 1/4/11

Qualified plans require careful adherence to specific requirements in order to maintain qualified status. The plan in this case failed on numerous counts and, as such, was held not to be a qualified plan dating all the way back to the plan's first year of October 31, 1987 through the current date.

In this case the plan in question was an ESOP maintained by one dentist professional corporation. The plan had 15 participants and/or beneficiaries as of its year ended December 31, 2002.

The first problem the Court addressed was the plan's failure to adopt plan amendments required by the Small Business Job Protection Act of 1996 and the IRS Restructuring and Reform Act of 1998. Such plan amendments were required to be effective as of various effective dates ranging from December 12, 1994 to January 1, 199.. Under Revenue Procedure 2001-55 the plan had until February 28, 2002 to make these amendments under the remedial amendment period.

The plan did adopt amendments well before that final date, adopting them on January 1, 2001. However the amendments did not contain language adopting the required retroactive effective dates, but rather were effective only beginning as of the adoption date. Thus the plan was not qualified since the amendments did not cover the entire remedial amendment period—so at this point the plan would have ceased to be qualified as of December 12, 1994. But the problems were to go back further than that.

The plan document properly required that plan benefits vest over a six year period, but the plan in operation did not follow that vesting schedule. The Court noted four employees that were shown with 0% vested benefits that were required to have currently some level of vested benefits ranging from 20% to 80%, one employee with a reflected vesting of 40% that should have been fully vested and one employee with vesting per the plan records of 20% that actually had no vested benefits. Thus, as the plan did not comply with vesting requirements under §411(a)(2)(B)(iii) and also failed to be operated in accordance with its own requirement, it was again found to fail qualification.

Yet another problem involved the plan's appraisal by a certified public accountant the plan engaged for 2001-2003. The CPA in question failed to sign the declarations that he held himself out to be an appraiser and required by Reg. §1.170A-13(c)(5)(i), one of the requirements to be a "qualified appraiser." As well, Reg. §1.170A-13(c)(ii)(F) and (5)(i)(B) require the appraiser to list his or her background, experience, education and membership in professional organizations, and that was also missing from the appraisals for the year in question. Thus, yet again the plan is found to not to be a qualified plan.

Finally, and probably the item that was truly fatal to the dentist's plan, there was a large dividend paid to the plan on its stock in 1989 of which the doctor was the principal beneficiary. The IRS treated the amount of that dividend allocated to the doctor as being, in effect, a disguised allocation to the dentist's account far in excess of the §415 limit of $30,000 in effect for the year in question. While generally dividend distributions on stock held by an ESOP are not treated as annual additions for §415 purposes, if the transfer is truly an attempt at an "end run" around the annual addition limits, the IRS has authority under Reg. §1.415(b)(2)(i) to reclassify the amounts as annual additions. The Court found the IRS did not abuse its discretion in this case, holding that the large distribution which was used to pay the loan the ESOP used to acquire the stock amounted to a wealth transfer primarily to the dentist.

Thus the plan failed to qualify at that point, and as the plan never took action to correct the failure, it remained disqualified through the dates involved in this case.

Finally, even though the issues noted did not affect years prior to 1989, the Court found the plan was not qualified prior to that point because there was no plan document presented for those earlier years.

The Court noted in the opinion that the taxpayer had failed to take advantage of the opportunity that the IRS had offered to correct these problems via the closing agreement program.

SECTION: 402
IRS DECLINES TO WAIVE WRERA AIRLINE EMPLOYEE ROTH ROLLOVER TIME LIMIT, ARGUES THE AGENCY LACKS THE AUTHORITY TO DO SO

Citation: PLR 201051027, 12/27/10

Prior to the addition of §402(c)(B) to the Internal Revenue Code, the IRS took the position it had no authority to waive the 60-day period for rolling a distribution from a qualified employer sponsored retirement plan to an IRA. The IRS returned to that position when a taxpayer attempted to get permission to make a late rollover to a Roth IRA of an amount received as a qualified airline employee of an amount received pursuant to an order of a federal bankruptcy court by the airline to offset the termination of the airlines' retirement plan.

Section 125 of the Worker, Retiree and Employee Recovery Act of 2008 (WRERA) allowed for such amounts to be rolled into a Roth IRA by such employees, but such a rollover had to take place no later than the later of 180 days after the enactment of WRERA or receipt of the distribution.

The taxpayer received a notice from the airline regarding his option to roll the balance into a Roth IRA and the deadline date that was applicable. However the taxpayer was extremely ill at the time, and was not able to review the notice until after the expiration of the deadline date.

The IRS ruled that while WRERA Section 125 provided that these distributions take on the character of a qualified rollover contribution, it did not actually make it into a §402 rollover contribution. As such, the IRS found that §402(c)(B) did not grant it the authority to extend the due date for this rollover, and there was no relief provision in WRERA itself granting the IRS such authority. The IRS declined to grant relief, arguing that no authority existed allowing it do so in this case.

SECTION: 419A
CONVERSION OF MULTIPLE EMPLOYER §419A PLAN TO SINGLE EMPLOYER ARRANGEMENT TRIGGERED IMMEDIATE INCOME RECOGNITION

Citation: Cadwell v. Commissioner, 136 TC No. 2, 1/3/11

The Tax Court took a look at the impact of a conversion of an employee benefit plan from a purported multiple employer plan to a single employer plan, specifically looking at the amount that must be treated as income (if any) by the employee in the situation. In this case, the individual was treated as an employee of his spouse's S corporation, a corporation that held an interest in a limited partnership.

The corporation had adopted a multiple employer plan that purportedly complied with the requirements of §419A(f)(6). The transaction was of a type that the IRS had identified as a listed transaction in Notice 95-34. Following the passage of the American Jobs Creation Act of 2004, where failing to include disclosure information related to listed transactions subjected the taxpayers to significant penalties, the plan was converted by its sponsor (a benefits consulting firm) into separate plans for each employer. The sponsor noted in its letter to the employers participating in the plan that this action was being taken specifically due the possibility that the transaction was a listed transaction subject to substantial penalties.

The IRS contended that in the year of the conversion of the plan the taxpayer had $102,039 of unreported income, consisting of $70,529 in fund value of the insurance policy, $18,000 of excess contributions to the plan and the cost of term insurance on the taxpayer's life for the year of $13,510. The Tax Court found first that following the conversion of the plan to a single employer there was no longer a substantial risk of forfeiture, as the conversion eliminated the chance that other employer's claims under the multi-employer plan could cause the assets to be used to pay those claims. The court found the taxpayer, as the sole listed officer of the corporation, had the right to terminate the plan at any time, thus eliminating the risk of forfeiture. The court determined its prior decision in Booth v. Commissioner was not applicable as the court held that deferred compensation was not an issue in this case, unlike Booth.

The Court also found the purported vesting restrictions were illusory under the facts of this case, since the taxpayer could terminate the plan at will and have the plan assets distributed to the corporation and any power to enforce restrictions against the taxpayer was in the hands of his spouse and children. As the employer was designated as the plan administrator and taxpayer controlled the employer completely, the taxpayer had no real restrictions on his access to the asset.

The fact that the employer never claimed a deduction for premiums paid to the plan also did not remove it from taxation, as the Court held that IRC §402(b)(1) does not condition inclusion in income on an employer level deduction being claimed. In accordance with Rev. Proc. 2005-25 the cash surrender value is ignored in computing the fair market value of the policy to determine the amount taxable to the taxpayer upon the conversion.

The Court also concluded that excess contributions to the plan and the value of the year's death benefit were also taxable to the taxpayer, since the taxpayer's relied on the same defense based on the illusory risk of forfeiture to argue against inclusion of either of these items in income.

SECTION: 451
IRS OFFERS OPTION EXPANDING CASES WHERE GIFT CARD REVENUE CAN BE DEFERRED AND WHERE ISSUANCE OF GIFT CARD TREATED AS AN EXPENSE OF A RETURN

Citation: Rev. Proc. 2011-17 and 2011-18, 1/5/11

The IRS issued a pair of revenue procedures impacting reporting income from the use of gift cards, allowing methods of reporting income that many taxpayers had already been using. Previously the IRS had indicated that these taxpayers could not defer any revenue to a later year (see TAM 200849015), nor treat the issuance of gift cards as an expense when given to a customer who returned an item.

Rev. Proc. 2011-17 deals with handling gift cards issued to customers in exchange for returned merchandise, while Rev. Proc. 2011-18 deals with the situation where a gift card is issued by one entity that sells gift cards redeemable through other entities via a gift card service agreement.

Entities that issue gift cards to customers when return merchandise will be able to treat the transaction as if the vendor had refunded cash to the customer, followed by the customer purchasing a gift card from the vendor. For accrual basis taxpayers, if the transaction qualifies for deferral under Reg. §1.451-5 and Rev. Proc. 2004-34 and the taxpayer uses that method of accounting for such sales, the revenue from the sale would not be recognized until the earlier of the date the customer redeemed the gift card for goods or services or the year following the year the gift card was issued.

Rev. Proc. 2011-18 serves to expand the scope of Rev. Proc. 2004-34 so that it can be used by entities that enter into a gift service card agreement. In such an arrangement 1) the taxpayer must be primarily liable to the customer or holder of the gift card for the value of the card until redemption or the expiration of the card and 2) the gift card must be redeemable by the taxpayer or any other entity that is legally obligated to the taxpayer to accept the card or one of the category of items listed in Rev. Proc. 2004-34.

Both Revenue Procedures contain provisions allowing for taxpayers to obtain automatic consent to change their methods of accounting to use these now permitted methods. As well, each procedure provides that the IRS will not challenge the use of such methods for years ended prior to December 31, 2010, and will not pursue the matter in any examination in progress where these issues are currently in question.

SECTION: 461
S CORPORATION SHOULD HAVE CLAIMED FULL DEDUCTION FOR PAYMENT MADE ON DISPUTED WAGES IN YEAR OF PAYMENT

Citation: Winter v. Commissioner, TC Memo 2010-287, 12/30/10

Judge Holmes was put in an unusual position—being assigned to decide issues that he had previously indicated the Court had no jurisdiction to decide (Winter v. Commissioner, 135 TC No. 12). So he begins his opinion by noting:

"I would have held that the Court lacks jurisdiction over these questions, but my colleagues, in a reviewed opinion, assured me, the parties, and the rest of the audience for our opinions that we did have jurisdiction in Winter v. Commissioner."

But given the assignment, Judge Holmes now wrestled with a case involving a shareholder employee of an S corporation who had a falling out with the corporation. The case becomes truly unusual because now the employee is arguing that the S Corporation return should have included additional deductions, forcing the Court to have to look through to the corporation's return to come to a conclusion in the matter.

In 2002 Mr. Winter received $5.5 million from the corporation that related to his employment agreement. However, in 2003 the corporation, asserting that Mr. Winter was terminated for cause, brought action to recover the portion of the compensation that represented the amount that would have been due for periods after Mr. Winter was terminated and stopped performing services.

As well, Mr. Winter claimed never to have received a K-1 from the S corporation, but computed his share of income based on financial reports of entity. A major difference between the financial reporting and the tax return was that the corporation deducted only $1.1 million of the $5.5 million, that portion applicable to 2002. Mr. Winter, now being shown the K-1, disputed the corporation's tax reporting, claiming the amount was a payment on a disputed liability, deductible under IRC §461(f).

The IRS countered that this could not be a disputed liability because no dispute existed at the time the corporation paid the amount due. However, Judge Holmes notes that the IRS's own regulations have an example where a vendor paid for product only to later find it was defective. The regulations held in that case the original payment was a payment of a contested liability. Judge Holmes held that the key was whether the amount was disputed at year end.

The Judge noted that if Mr. Winter had not been discharged for cause, the additional $4 million would have payable to him as damages under the contract. For purposes of applying the four tests for recognition under §461(f), the amount paid had to treated as if it was paid for what Mr. Winter alleged—the payout of his contract. If it had been paid to settle the balance due on Mr. Winter's contract, it would be in the nature of a severance payment. Since there was no future benefit the payor would receive, the amount would have been deductible in 2002 absent the dispute. Since the payor had turned over the cash to Mr. Winter, the amount was properly deductible in 2002—thus, Mr. Winter was correct that his Schedule K-1 was in error and should have reported a loss rather than the income shown.

The fact the S Corporation did not claim the loss isn't relevant—as Judge Holmes noted, "unless the Code explicitly allows a taxpayer to make an election, each of his expenses has a proper year for its deduction." Therefore, 2002 was the only year in which that deduction could be claimed—it's not an optional claim.

However the Court did not agree with Mr. Winter's argument that he only needed to recognize the $1.1 million, treating the additional $4 million of income as a loan. The Court found that Mr. Winter had not been given a "loan" but rather had unfettered use of the funds, subject to a contingent repayment obligation. Thus he was required to recognize the entire payment in 2002. If he later needed to repay the loan, he would receive a deduction in the year of repayment.

The Court also didn't accept Mr. Winter's claim that he should not be held subject to a negligence penalty for not attempting to obtain his K-1 or filing a Form 8082 since he had not hired professional help to prepare his return. The Court found that Mr. Winter was financially sophisticated enough to understand that tax and financial reporting income are often very different, admitted he knew a Form 8082 (flagging an inconsistent treatment) should have been filed, and that while hiring a professional wouldn't automatically protect a taxpayer from a negligence penalty, failing to hire one in this case was not going to be accepted as an excuse for failure to handle the matter properly.

SECTION: 701
VALUE OF TAX CREDITS INCLUDED IN ECONOMIC SUBSTANCE CALCULATION WHERE CONGRESS INTENDED CREDIT TO SUBSIDIZE OTHERWISE UNPROFITABLE ACTIVITIES

Citation: Historic Boardwalk Hall, LLC v. Commissioner, 136 TC No. 1, 1/3/11

The IRS challenged an arrangement between a state created entity and a corporation, charging that the partnership created was a sham and merely existed to sell a federal tax credit to the corporation. The partnership was created to restore a convention hall for use by the state agency. The particular hall being renovated would generally not, by itself, be expected to generate a profit, but the existence of that hall would increase the ability of the state agency to entice bookings into related facilities.

The hall in question was an old facility that had historical significance, thus the renovation would qualify generally for historic rehabilitation credits under IRC §47. The agency transferred the interests in that building to a partnership where a large corporation was given a 99.9 interest in the hall via a limited liability company. Pursuant to the operating agreement, the outside corporation would be required to make certain capital contributions to the partnership so long as certain goals were met. As well, under the operating agreement the corporation was an investor member, and the managing member of the LLC was designated as the state agency.

There were a set of agreements under which the state could force the corporation to sell its interest or the corporation could force the state to purchase its interest. The corporation would receive a 3% preferred return on its investment, and there were various agreements that served to effectively insure that the preferred return would eventually be realized, either through operations of the entity or via the purchase options. The LLC in fact operated at a loss each year.

The IRS argued the partnership had no realistic chance of a positive rate of return absent the value of the rehabilitation credits, thus the transaction was a sham that should be disregarded for federal tax purposes as lacking economic substance. The Tax Court, looking to prior rulings of the Third Circuit which would have jurisdiction over any appeal in this case, ruled that, in this case, the value of the rehabilitation credits were proper to consider in determining if there was economic substance to the transaction.

The Court decided that Congress's purpose in enacting §47 was to make restorations economically viable that otherwise would not have been, thus in this case it was proper to consider the value of those credits. As well, the Court found that while protections were put in place for the corporation with regard to the options to buy and sell and insurance against potential environmental hazards, the corporation still had real risk exposure—either due to the agency being unable to actually fund the buyout down the line or an environmental exposure being greater than the insured amounts.

The Court also rejected the IRS's attempts to disregard the partnership under the anti-abuse rules of Reg. §1.701-2(b). As the use of the credit in this fashion was in line with Congressional intent, the Court did not find that the structure violated the spirit of Subchapter K. The Court noted that this IRS attack failed for the same reason as the economic substance attack—the structure had Congressional blessing, being the type of transaction that Congress wished to encourage.

SECTION: 4980D
PHS §2716 NON-DISCRIMINATION PROVISIONS EFFECTIVE DATE DELAYED PENDING FURTHER GUIDANCE

Citation: Notice 2011-1, 12/22/10

One item in the Patient Protection and Affordable Care Act of 2010 that is in effect but for which no guidance had been provided is the provision found in §10101(d) of the Act that added §2716 to the Public Health Service Act. PHS §2716 provides that non-grandfathered insured group health plans must comply with the substantive nondiscrimination rules found in IRC §105(h) for self-insured plans, though not the tax rules that would apply to highly compensated individuals for self-insured plans that fail to comply with that provision.

Insured plans that fail to meet these requirements would be subject to an excise tax of $100 per day, a civil penalty of the same amount or a civil action under ERISA to enjoin provisions contrary to this rule or other equitable relief. On September 20, 2010 the IRS released Notice 2010-63 that asked for public comment on implementing this provision. The IRS noted that responses the agency received indicated a need for regulatory guidance, specifically explaining the application of PHS §2716(b)(1) that provides "rules similar to the rules contained in paragraphs (3), (4) and (8) of section 105(h) of such Code shall apply." Such guidance does not currently exist.

The notice indicates that the IRS, Department of Labor and Department of Health and Human Services will not require compliance with PHS §2716 nor will any sanctions apply until after regulatory guidance is issued. When such guidance is issued, the rules will not apply until plan years beginning a specified period after the release of the rules to allow time for plan sponsors to modify plans to comply with the regulations.

The notice requests comments on thirteen specific problem areas that the IRS believes specifically need to be resolved. Comments are due by March 11, 2011.

SECTION: 6011
IRS WILL NOT BE ABLE TO PROCESS CERTAIN RETURNS, INCLUDING ALL RETURNS WITH SCHEDULE A, UNTIL MID- TO LATE FEBRUARY

Citation: IRS News Release IR-2010-126, 12/23/10

The IRS announced that, due to the late 2010 passage of the Tax Relief, Unemployment Insurance Reauthorization and Job Creation Act of 2010, many taxpayers will not be able to file their 2010 tax forms until the middle or latter portion of February. Specifically impacted are any taxpayers who are claiming the higher education tuition and fees deduction, the educator expense deduction or, most significantly, any taxpayers itemizing deductions on Schedule A.

The IRS indicated that this processing delay will affect both paper and electronic returns and is asking taxpayers not to submit either type of return until the IRS announces it is ready to process such returns.

SECTION: 6011
DRAFT OF FORM RELEASED TO BE REQUIRED WHEN RETURN NOT PREPARED FOR EFILE BY PREPARER REQUIRED TO EFILE RETURNS IN 2011

Citation: Form 8948 (Draft), 12/21/10

The IRS has issued a draft of new Form 8948 which will be used to explain why a tax return is not being filed electronically. The form is only to be used by preparers who are required to file a return electronically for returns for which electronic filing is generally available.

The form contains check boxes that are to indicate the reason the return is not being filed electronically. The form contains additional options beyond those the IRS had already announced in Notice 2010-85 for what will apparently be exceptions from mandatory e-filing.

In addition to indicating a client has elected not to e-file the return or that the preparer has received a hardship waiver (two circumstances described in Notice 2010-85), the form also contains the following additional reasons for failing to electronically file a return prepared by a preparer otherwise required to e-file:

1. Conscientious objection on religious grounds to electronic filing
2. Return was rejected for e-file and the condition could not be resolved
3. The preparer's tax software does not support e-filing a particular form or schedule
4. The preparer is ineligible to e-file due to being a foreign preparer that does not have a social security number and works abroad
5. The preparer is under an IRS sanction that bars participation in the e-file program
6. Other circumstances that prevent electronic filing

If the preparer indicates that other circumstances prevented electronic filing, the preparer must describe those circumstances.

The form will not have to be submitted if the particular individual or trust return type is one for which the IRS does not currently provide for electronic filing. However it will be required in cases where the return is rejected and the issue cannot be corrected within the terms of the e-file program.

Such a case would exist when a return is rejected because a dependent has been rejected due to the dependent already being claimed on another return. Assuming the taxpayer whose return was rejected is the taxpayer who truly has the right to claim the dependent, the only option to file the original return to claim the exemption is to file the return on paper. In that case the Form 8948 would be used to explain the situation.

Preparers should be aware the form does not grant an absolute right to ignore the e-file requirements—proposed amendments to Circular 230 §10.51 would provide that willfully failing to e-file when required would be grounds for discipline against a tax preparer, including a potential suspension or disbarment from practice. These proposed amendments would also make preparation of a return practice before the IRS, so the effect of a suspension or disbarment would be the equivalent of a professional death penalty.

SECTION: 6011
IRS RELEASES EFILE HARDSHIP WAIVER FORM AND GUIDANCE

Citation: Form 8944, Annoucement 2010-96, 12/21/10

The IRS released the form that practitioners who wish to claim a hardship exception from electronic filing will be required to use to apply for such relief. The form in question is Form 8944. Applications will generally need to be made by April 1, 2011 to be exempted from the program for 2011.

The form lists as potential reasons for a hardship waiver bankruptcy, economic hardship, being in a Presidential Disaster Area or other hardships. For relief due to bankruptcy, the preparer must submit a copy of bankruptcy court documentation. Taxpayers asking for relief on economic grounds must submit two estimates of the costs to comply with the electronic filing mandate from third parties, outlining the costs for additional hardware, software or any other expenses. Failure to provide documentation in either case will result in a denial of the application.

For those located in a Presidentially declared disaster area, an explanation of the impact of the disaster on the preparer that affects his/her ability to electronically file returns must be included. Individuals asking for relief for other reasons must attach complete documentation of the nature of the hardship and how it affects the preparer's ability to comply with the electronic filing mandate.

For requests submitted after April 1, 2011 to be considered, the preparer must be filing due to unusual or unforeseen and unavoidable circumstances. Individuals filing a late application must detail these circumstances that justify the late consideration of their application.

Requests can be sent to the IRS either by mail or via fax.

SECTION: 6015
WIDOW WHO SIGNED JOINT RETURN FOLLOWING DEATH OF SPOUSE NOT GRANTED RELIEF AS SHE WAS AWARE TAX WOULD NOT BE PAID

Citation: Sommer v. Commissioner, TC Summary Opinion 2010-177,12/28/10

The Tax Court had previously ruled that the fact that a spouse was aware a tax was unlikely to be paid when signing the return did not automatically deny the spouse relief under §6015(f). But in the case of Harriet Sommer the Court found that her situation was one where her knowledge the tax wasn't going to be paid precluded relief on its own.

Harriet's husband was an attorney. For a number of years he had applied for extensions of time to file their tax return, would eventually file the return during the extension period without paying the tax and then finally would pay the tax. In 2005 Mr. Sommer received extra income and Mrs. Sommer testified that she requested he set aside ½ of the funds received to pay the tax, a request Mr. Sommer agreed to. Although he agreed to doing so, he apparently did not actually set aside the funds.

When April 15 rolled around in 2006 Mr. Sommer again requested an extension to file their return. However in June, before the return was filed, Mr. Sommer died. The return was completed by their preparer less than 2 weeks after Mr. Sommer's death and forwarded to Mrs. Sommer. She signed the return as surviving spouse, but did not pay any of $37,692 of tax shown as due on the return. She admitted she didn't think anything more about the return until the IRS contacted her.

Mrs. Sommer argued that she should be granted innocent spouse relief from the liability since the funds had not been set aside. The Court disagreed, noting that Mrs. Sommer took over responsibility for the filing on her husband's death and should have been aware by then that the funds were not set aside—she testified that he had left her only enough funds to pay for his funeral. She nevertheless elected to file a joint return with her deceased husband for that year.

It probably didn't help her case much that, after being contacted by the IRS with a threat to file a lien against her property, Mrs. Sommer came up with $25,000 from sources she didn't identify to partially pay the IRS. She also paid off the balance of the tax after refinancing her home. Prior to paying off the balance she had agreed to pay $600 a month on an installment agreement and she paid off all other creditors except for the mortgage—and, again, no explanation was given of how she was able to do this when, in this case, she argued paying the tax would create severe economic hardship for her.

SECTION: 6103
SB/SE FAST TRACK SETTLEMENT PILOT PROGRAM EXTENDED FOR TEST LOCATIONS

Citation: Announcement 2011-5, 12/30/10

The IRS announced the continuation of the Small Business/Self-Employed Fast Track Settlement pilot program in the test locations of Chicago, IL; Houston, TX; St. Paul, MN; Philadelphia, PA; central New Jersey; and San Diego, Laguna Niguel, and Riverside, CA. The program will be available in those cities until further notice and the IRS indicated that the program may be expanded nationwide in the future as determined by SB/SE and Appeals.

The notice contains additional information about the program which is used to resolve factual and legal issues, preferably before the issuance of a 30-day letter,

SECTION: 6109
RULES FOR PREPARATION UNDER SUPERVISION OF CPA AND FATPS, OTHER GUIDANCE FOR PTIN PROGRAM IN 2011

Citation: Notice 2011-6, 12/30/10

The IRS offered additional guidance as 2010 ended on the application of the PTIN rules for 2011. The notice creates some new categories of PTIN holding preparers, including carving out special treatment for individuals that work under the supervision of CPAs, EAs, attorneys or enrolled actuaries.

The notice begins by noting that those have applied for and been granted a PTIN, or renewed their PTIN, after September 28, 2010 will be treated as meeting the requirements under Reg. §1.6109-2 to have obtained a PTIN that qualifies one to prepare tax returns in 2011.

The IRS carves out a special rule for individuals who prepare returns under the supervision of a CPA, EA, attorney or enrolled actuary. These individuals will not be required to take the competency test, nor will they be subject to mandatory continuing professional education. These individuals will still need to obtain a PTIN, pay the user fees annually to obtain and renew that PTIN and pass the tax compliance and suitability checks. These individuals will not be able to sign a return, represent clients in any form before the IRS, nor hold themselves out to the IRS or the general public as a registered tax return preparer.

This “non-registered tax return preparer” individuals will have to meet the following requirements:

1. The individual must be 18 years of age or older;
2. The supervising CPA, EA, attorney or enrolled actuary must sign any returns or claims for refund prepared by this individual and
3. The individual must be employed at the CPA firm, law firm or "other recognized firm" of the preparer who signs the return.

CPA firms and law firms are defined by local law definitions authorizing practice in those licensed areas. The third category, the "other recognized firm," is a firm other than a CPA firm or law firm, must have one or more employees engaged in practice before the IRS and is 80% or more owned by one or more CPAs, EAs, attorneys, enrolled retirement plan agents or enrolled actuaries who are currently allowed to practice before the IRS.

An individual obtaining a PTIN under this rule must certify on the application that they will be preparing return solely under the supervision of one of the preparers noted above and may be required by the IRS to give a supervising preparer's PTIN or other number assigned by the IRS. If the individual is no longer supervised by that authorized preparer, the PTIN holder must notify the IRS of this fact and cease preparing returns. The IRS will retain the right to revoke the PTIN of this individual if the person willfully violates the rules found in Circular 230 or engages in disreputable conduct.

The IRS also has carved out an exception for preparers who do not prepare individual income tax returns. The IRS indicates that the initial competency exam will be limited to individual income tax issues. While the IRS anticipates adding additional examinations to cover other areas, for now the IRS will issue a PTIN to and exempt from the requirement to pass a competency examination individuals who:

1. Are 18 years of age or older;
2. The individual certifies that the individual does not prepare or assist in the preparation of any return currently covered by a competency exam

The individual will still need to apply for a PTIN and pay the fee annually, as well as pass the suitability and tax compliance check. For now these individuals will also be exempted from the continuing education requirements. However, they will not be allowed to represent to the public or the IRS that they are registered tax return preparers. The IRS retains the right to revoke PTINs issued under this provision for violations of rules or disreputable conduct.

Enrolled retirement plan agents and enrolled actuaries that obtain a PTIN under this provision will continue to be allowed to practice before the IRS in the limited areas provided under Circular 230 for those individuals.

The IRS also published a list of forms which will not be subject to the PTIN requirements of Reg. §1.6109-2. These forms are:

1. Form SS-4, Application for Employer Identification Number;
2. Form SS-8, Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding;
3. Form SS-16, Certificate of Election of Coverage under FICA;
4. Form W-2 series of returns;
5. Form W-7, Application for IRS Individual Taxpayer Identification Number;
6. Form W-8BEN, Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding;
7. Form 870, Waiver of Restrictions on Assessment and Collection of Deficiency in Tax and Acceptance of Overassessment;
8. Form 872, Consent to Extend the Time to Assess Tax;
9. Form 906, Closing Agreement On Final Determination Covering Specific Matters;
10. Form 1098 series;
11. Form 1099 series;
12. Form 2848, Power of Attorney and Declaration of Representative;
13. Form 3115, Application for Change in Accounting Method;
14. Form 4029, Application for Exemption From Social Security and Medicare Taxes and Waiver of Benefits;
15. Form 4361, Application for Exemption From Self-Employment Tax for Use by Ministers,Members of Religious Orders and Christian Science Practitioners;
16. Form 4419, Application for Filing Information Returns Electronically;
17. Form 5300, Application for Determination for Employee Benefit Plan;
18. Form 5307, Application for Determination for Adopters of Master or Prototype or Volume Submitter Plans;
19. Form 5310, Application for Determination for Terminating Plan;
20. Form 5500 series;
21. Form 8027, Employer's Annual Information Return of Tip Income and Allocated Tips;
22. Form 8288-A, Statement of Withholding on Dispositions by Foreign Persons of U.S. Real Property Interests;
23. Form 8288-B, Application for Withholding Certificate for Dispositions by Foreign Persons of U.S. Real Property Interests;
24. Form 8508, Request for Waiver From Filing Information Returns Electronically;
25. Form 8717 User Fee for Employee Plan Determination, Opinion, and Advisory Letter Request;
26. Form 8809, Application for Extension of Time to File Information Return;
27. Form 8821, Tax Information Authorization;
28. Form 8942, Application for Certification of Qualified Investments Eligible for Credits and Grants Under the Qualifying Therapeutic Discovery Project Program

This list is subject to revision by the IRS.

Since neither the competency examination nor the continuing education programs are ready at this time, the IRS has implemented interim rules. Under these interim rules, individuals will be given provisional PTINs. The IRS plans to issue provisional PTIN only through the date at which the competency examination is made available. The IRS indicates it expects the competency exam to be available sometime in the middle of 2011. Once that examination is available anyone not already possessing a provisional PTIN or otherwise exempted from the examination process will have to pass the examination to become a registered return preparer.

Individuals who obtain provisional PTINs prior to the availability of the examination will be allowed to prepare returns through December 31, 2013 so long as they continue to renew their PTINs during that period. Once the examination is available these individuals will be able to pay the fee and take the exam as often as it offered prior to December 31, 2013. Such individuals will need to pass the exam prior to that date to continue to prepare returns.

While these individuals will be allowed to prepare and sign returns for compensation and represent him/herself as authorized to practice before the IRS for preparing and filing tax returns and claims for refund. However the provisional PTIN holder will not be allowed to represent that he/she is a registered tax return preparer. Effectively, there will not be registered tax return preparers until the IRS releases the examination, the exam is administered and individuals pass the exam.

Individuals who have prepared returns will be allowed to exercise the limited represented of taxpayers before the IRS for returns that the individual prepared if the person was authorized under the regulations to prepare and sign the return for compensation, even if currently that person would not be authorized to do so. However this provision does not expand the rights of these individuals to the expanded representation available to CPAs, EAs, attorneys, enrolled retirement agents and enrolled actuaries.

The notice reiterates that no continuing education requirement will be imposed for the first year of registration which began on September 30, 2010.

SECTION: 6662
IRS OUTLINES ADEQUATE DISCLOSURE FOR PURPOSES OF §6662 AND §6694

Citation: Revenue Procedure 2011-13, 12/28/10

The IRS issued the annual return disclosure revenue procedure applicable for 2010 income tax returns. The document outlines disclosures made on the return that will be deemed to be adequate to escape the penalty for substantial understatement of tax without having to file a Form 8275 or 8275-R for positions that have, at a minimum, a reasonable basis. The requirements are listed generally by form and information type, and describe what items will and will not constitute adequate disclosure.

This year's version of the form added references to newly enacted §6662(i) (accuracy related penalty for nondisclosed noneconomic substance transactions) and §6662(j) (accuracy related penalty for undisclosed foreign asset understatements. The ruling also provides that a complete and accurate disclosure of a tax position on a corporation's Schedule UTP, Uncertain Tax Position Statement, will be treated as if the corporation filed a Form 8275 or Form 8275-R regarding the tax position. However, the converse is not true. The filing of a Form 8275 or Form 8275-R will not be treated as if the corporation filed a Schedule UTP.

The document outlines what the IRS expects of taxpayers when filling out tax returns forms to properly disclose items and should be reviewed by all individuals who are involved in the preparation of tax returns.

SECTION: 7123
IRS EXTENDS MEDIATION AND ARBITRATION TEST PROGRAM FOR OIC AND TRUST FUND CASES

Citation: Announcement 2011-6, 12/30/10

The IRS has extended the test of mediation and arbitration procedures on certain offer in compromise (OIC) and trust fund recovery penalty cases (TFRP) for an additional two years, through December 31, 2012. The program is still only available for taxpayers whose appeals are located at the

1. Atlanta, Georgia
2. Chicago, Illinois
3. Cincinnati, Ohio
4. Houston, Texas
5. Indianapolis, Indiana
6. Louisville, Kentucky
7. Phoenix, Arizona
8. San Francisco, California

The notice reserves to the IRS the right to expand the program to other cities. The IRS's announced plan is to use this testing period to determine necessary adjustments to the mediation and arbitration program, as well as to consider whether to make the arbitration component permanent.

The notice contains scope limitations on the entire program, as well as limitations applicable to only the OIC or TFRP program.

The notice lists the following issues as generally appropriate for mediation or arbitration in OIC cases:

1. The value of assets, including those held by a third party.
2. The value of dissipated assets and what amount should be included in the overall determination of reasonable collection potential.
3. A taxpayer's proportionate interest in jointly held assets.

4. Projections of future income based on calculations other than current income.
5. The calculation of a taxpayer's future ability to pay when living expenses are shared with a non-liable person.
6. Other factual determinations, such as whether a taxpayer's contributions into a retirement savings account are discretionary or mandatory as a condition of employment.

For TFRP cases, the notice lists the following issues as generally appropriate for mediation:

1. Whether a person was required to collect, truthfully account for, and pay over income, employment, or excise taxes.
2. Whether a responsible person willfully failed to collect or truthfully account for and pay over such tax, or willfully attempted in any manner to evade or defeat the payment of such tax.
3. Whether a taxpayer sufficiently designated a payment to the trust fund portion of the unpaid tax.
4. Whether the taxpayer provided sufficient corporate payroll records to establish that a corporate tax deposit was in the amount required by Treas. Reg. § 31.6302-1(c) and therefore was considered a designated payment to be applied to both the trust fund and non-trust fund portions of the employment taxes associated with that specific payroll.

Separately, the notice lists the following issues as generally appropriate for arbitration in a TFRP case:

1. Specific factual determinations concerning whether a person was required to collect, account for, and pay over income, employment, or excise taxes. Common factors include whether the taxpayer: was an officer, director, or shareholder of the corporation; had the authority to sign checks; exercised significant control over the corporation's financial affairs; had the authority to determine which creditors would be paid; was involved in payroll disbursements; had control over the voting stock of the corporation; was involved in making federal tax deposits; and had the ability to hire and fire employees.
2. Specific factual determinations concerning whether a responsible person willfully failed to collect or truthfully account for and pay over such tax, or willfully attempted in any manner to evade or defeat the payment of such tax. Common factors to be determined include: when the taxpayer became aware of the failure to pay over the withheld tax; whether the taxpayer had knowledge of payments to other creditors, including employees, after becoming aware of the failure to pay over the withheld tax; whether there were unencumbered funds available to satisfy pre-existing employment tax liabilities; and whether the taxpayer failed to use unencumbered funds to satisfy preexisting tax liabilities after becoming aware of such liabilities.
3. A factual determination of the amount designated by the taxpayer as a payment to the trust fund portion of the unpaid tax.
4. A factual determination whether the taxpayer provided sufficient corporate payroll records to establish that a corporate tax deposit was in the amount required by Treas. Reg. § 31.6302-1(c) and therefore was considered a designated payment to be applied to both the trust fund and non-trust fund portions of the employment taxes associated with that specific payroll.

SECTION: 7502
TIMELY MAILING RULE DOES NOT APPLY TO AMENDED RETURNS REPORTING TAX DUE, DOES APPLY TO AMENDED RETURNS ASKING FOR REFUND

Citation: CCA 201052003, 12/30/10

In a Chief Counsel Memorandum the IRS decided that the timely mailing rule of §7502 does not apply to amended tax returns reporting tax due, but does apply to amended returns that are claims for refund or credit.

The corporation in question had filed a Form 1120X that showed adjustments that both served to increase and decrease the tax due on its return. The amended return was mailed 3 years to the day after the original return had been filed on extension. The original return was mailed one day before the extended due date. The amended return showed an increase in tax due and the taxpayer sent payment along with the 1120X.

The IRS sent a letter stating that it could not assess the tax shown on the return because the statute of limitations on assessment had expired. The taxpayer protested that the return had been postmarked timely within the assessment period.

The memorandum concludes that the IRS letter was correct. IRC §7502(a)(1) covers "any return, claim, statement, or other document required to be filed" that is received by the IRS after the date prescribed for filing. The memorandum argues that an amended return reporting tax due is not required to be filed under any provision of the IRC, with the key issue being a requirement. As such, the timely mailing equals filing rule would not apply.

However, the memorandum points out that an amended return asking for a refund would be covered, arguing that IRC §6511 imposes a requirement to file such a claim and provides time limitations for the filing. While not discussed in the memorandum, the key difference is that it is the taxpayer that must act in a claim for refund and file a document, while it is the IRS that faces a time limitation in assessing tax.

The memorandum went on to conclude that because the timely mailing rule did not apply to the amended return showing a balance due, the statute for assessing tax by the IRS was not extended by sixty days under §6501(c)(7), as the statute expired prior to the filing of the document where the taxpayer indicated additional tax was due. Under §6401(a) the payment submitted with the amended return should be treated as an overpayment of tax, entitling the taxpayer to an offset or refund under IRC §6402(a).

As well, the IRS is not allowed to bifurcate the amended return into two parts, one representing the changes that increased taxes (which would not be timely filed) and one representing the changes that decreased taxes (a claim that would be covered by the timely mailing rule). The memorandum rules the IRS has to accept the amended return as a single package, as the amended return adjustments are simply "components of a single tax liability."