ROUNDUP OF RECENT TAX DEVELOPMENTS

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I. INDIVIDUALS

A. Student Loan Forgiveness Exclusion

1. American Rescue Plan Act of 2021 (*IRC §108(f)(5)*).

a. Excludes from gross income discharge of indebtedness income relating to student loan debt.

i. Including private student loans.

ii. Unless student is required to provide services to the discharging lender.

b. Effective for 2021-2025

B. Premium Tax Credit

1. Premium Tax Credit (PTC) (*IRC §36B*)

a. Refundable credit design to subsidize health insurance purchased through an Exchange.

b. Based on percentage of income the cost of premiums represents ranging from:

i. 2% of income for those below 133% of the federal poverty line, to

ii. 9.5% of income for those at 400% of the federal poverty line.

2. Advanced Premium Tax Credit (APTC)

   a. Taxpayer signs up for insurance through the exchange using prior year tax information.

   b. Exchange then pays an amount to the health insurance provider.

   c. Health insurance provider reduces the monthly health insurance premium paid by taxpayer.

   d. Advance received reduces the PTC allowed on the tax return.

3. American Rescue Plan Act of 2021.

   a. Changes the percentages to increase the affordability of health insurance for 2021 and 2022.

   b. Also makes the PTC available to taxpayers with income above 400% of the federal poverty line if cost of premiums would exceed 8.5% of household income.

   c. Extended for 3 years through 2025 by the Inflation Reduction Act of 2022.

C. COVID-19 Expenses and Preventive Care

1. Generally, an HDHP is not permitted to provide benefits until the minimum deductible for the year is met.

2. Section 223(c)(2)(C) contains an exception for preventive care.

3. Notice 2020-15 created an exception for testing and treatment related to COVID-19.

4. The COVID-19 emergency ended on May 11, 2023.

5. Notice 2023-37 indicates that Notice 2020-15 will continue to apply only for plan years ending on or before December 31, 2024.

D. Medical Expenses

1. New FAQs added to irs.gov on March 17, 2023

2. Background:

   a. Section 213 allows a deduction for medical expenses.

   b. Alternatively, may be paid or reimbursed from HSA, FSA, Archer MSA, or HRA.

3. Medical Expenses:

   a. Costs of diagnosis, cure, mitigation, treatment or prevention of disease.

   b. Payment for medical services rendered by physicians, surgeons, dentists, and other medical practitioners.

4. Includes:

   a. Costs of Equipment, supplies and diagnostic devices.

   b. Costs of medicines and drugs prescribed by a physician.

5. Examples of items added to FAQs that may be paid or reimbursed from an HAS, FSA, Archer MSA, or HRA:

   a. Dental, eye or physical exam.

   b. Program to treat a drug-related substance use disorder.

   c. Program to treat an alcohol use disorder.

d. Smoking cessation disorder.

e. Therapy if it is a treatment for a disease.

f. Nutritional counseling if it treats a specific disease diagnosed by a physician.

g. Weight-loss program if it treats a specific disease diagnosed by a physician.

6. Gym membership if sole purpose is:

a. To affect a structure of the body (e.g., physical therapy); or

b. To treat a specific disease (e.g., obesity).

c. Note: Cost of exercise to improve general health does not qualify.

7. Food or beverage, if:

a. Not for normal nutritional needs;

b. Alleviates or treats a disease; and

c. Substantiated by a physician.

8. Nutritional supplements if recommended to treat a specific medical condition diagnosed by a physician.

9. Nonprescription (over-the-counter) drugs & medications:

a. Except for insulin, not a deductible medical expense under Section 213.

b. But, may be paid or reimbursed by an HSA, FSA, Archer MSA, or HRA.

E. New TIP Reporting Program

1. Notice 2023-13

   a. Contains a proposed Revenue Procedure.

   b. Service Industry Tip Compliance Agreement (“SITCA”) Program.

2. Designed to take advantage of:

   a. Point-of-sale systems.

   b. Time and attendance systems.

   c. Electronic payment settlement methods.

3. Features:

   a. Replaces current programs.

   b. Requires an annual report.

   c. Protects employers from liability under the rules defining tips as part of an employee’s pay.

4. Effective:

   a. Voluntary

   b. Other programs would sunset at the end of the first full calendar year after the Revenue Procedure is published.

   c. Doesn’t affect the Gaming Industry Tip Compliance (“GITCA”) Program.

F. Taxation of State Payments.

1. Background

a. On February 10, 2023, the IRS issued news release IR-2023-23 providing guidance for the 2023 tax filing season on various kinds of state payments many of which were related to COVID-19.

b. The news release indicated that for 2022 only, the IRS wouldn't challenge the treatment of a 2022 payment on either an original or amended return.

2. Notice 2023-56:

a. Issued by the IRS in response to requests for additional information on payments made in 2023 and future years.

b. Indicates that, in general, state payments are taxable unless a specific exclusion applies.

c. Examples include state tax refunds, certain welfare payments, and certain disaster relief payments.

G. Supervisory Penalty Approval (REG-121709-19)

1. Background:

a. IRC §6751(b) requires the immediate supervisor of a revenue agent to approve the determination of a penalty.

b. IRC §6751(b)(2) exempts penalties automatically calculated by electronic means.

c. Courts have been inconsistent particularly with respect to the timing of the approval requirement.

2. Proposed regulations adopt three timing rules:

   a. For penalties appearing in a pre-assessment notice, must be no earlier than the date of the notice.

   b. For penalties raised in the Tax Court after a petition is filed, must be obtained before the court is asked to determine the penalty.

   c. For penalties assessed without prior opportunity for Tax Court review, may be any time before assessment.

H. Lookback Period for Refund Claims Extended.

1. Background:

   a. Refund claims must be filed by later of:

      i. Three years from when return filed; or

      ii. Two years from the time the tax was paid.

   b. Taxes are deemed to be paid when the return is filed.

2. Example: A taxpayer would have until April 15, 2023 or October 15, 2023 to file a refund claim on 2019 taxes depending on whether an extension was filed.

3. Problem:

   a. Notice 2020-23 postponed 2019 filing date to July 15, 2020.

   b. Notice 2021-21 postponed 2020 filing date to May 17, 2021.

   c. Both were “postponements,” not “extensions”.

4. <u>Note</u>: Relief under Notice 2023-21 is automatic (no form needs to be filed).

I. Direct-File Program (IR-2023-192).

1. Details of IRS' direct-file pilot program for the 2024 filing season.

a. Online, interview-based service giving taxpayers a free option to file their individual federal tax returns directly with the IRS.

b. Does not include state tax returns.

2. Limited by:

a. State where the taxpayer resides.

b. Small group of states with specified types of incomes, credits, and deductions.

3. Arizona, California, Massachusetts and New York are preparing to integrate their state taxes into the program.

4. At least nine other states that have no state income tax are partnering with the IRS.

J. FBAR Penalty (*Bittner*, U.S. Supreme Court, February 28, 2023)

1. Background:

a. A "Report of Foreign Bank and Financial Accounts" (FBAR) is required to be filed on or before June 30th of each year reporting foreign bank accounts held during the preceding calendar year.

b. Penalty for non-willful violations is $10,000.

c. Penalty for willful violations is greater of $100,000 or 50% of the account.

2. Facts:

   a. Taxpayer was born in Romania, became a naturalize citizen, went back to Romania in1990, and then returned to the U.S. in 2007.

   b. Unaware of the FBAR requirement until he returned.

   c. Hired a CPA and filed FBARs for 2007-2011.

   d. Penalties for years prior to 2007 were expired due to the statute of limitations.

   e. Reported all foreign bank accounts and balances.

3. IRS:

   a. Assessed $2.7 million in penalties.

   b. $10,000 for each individual account.

      i. 2007 – 61 accounts.

      ii. 2008 – 51 accounts.

      iii. 2009 – 53 accounts.

      iv. 2010 – 53 accounts.

      v. 2011 – 54 accounts.

4. Issue:

   a. Does FBAR penalty apply on an account-by-account basis (IRS and 5th Circuit); or

   b. On a report-by-report basis (Taxpayer).

5. U.S. Supreme Court:

   a. The FBAR penalty for a non-willful violation applies on a per-report basis.

   b. The penalty for willful violations applies on an account basis.

K. Bonuses & Commissions Not Self-Employment Income. (*Schmerling*, T.C. Summary 2023-14)

1. Facts:

   a. Taxpayer worked as an automobile salesman.

   b. Received W-2 for wages.

   c. Reported manufacturer performance bonus on a 1099.

   d. Reported commissions on sales of extended warranties on a 1099.

2. IRS:

   a. Recharacterized Schedule C gross receipts as "other income" on the 1040.

   b. Disallowed all expenses shown on Schedule C.

3. Court agreed with IRS:

   a. Bonus & commissions inextricably connected to his status as an employee.

L. Receipt of Partnership Units for Services. (*ES NPA Holding, LLC v. Comm'r*, T.C. Memo. 2023-55

1. Background:

   a. Under Code Sec. 721(a), no gain or loss is recognized to a partner in the case of a contribution of property to the partnership in exchange for an interest in the partnership.

   b. Reg. Sec. 1.721-1(b)(1) provides that the receipt of a partnership capital interest in exchange for services is taxable to the service provider as income under Code Sec. 61.

   c. In Rev. Proc. 93-27, the IRS stated that it will not treat the receipt of a profits interest as a taxable event.

   d. Rev. Proc. 93-27 defines a profits interest as a partnership interest "other than a capital interest."

   e. A capital interest is, in turn, an interest that would give the holder a share of the proceeds if the partnership's assets were sold at fair market value and then the proceeds were distributed in a complete liquidation of the partnership occurring immediately after the transaction.

2. Holding:

   a. The Tax Court held that a taxpayer did not have unreported income under Reg. Sec. 1.721-1(b) on its receipt of class C units in a partnership in exchange for cash and the performance of services because the taxpayer received a profits interest, rather than a capital interest, in the partnership, which is not treated as income under Rev. Proc. 93-27.

b. It was a profits interest because there would be no distribution to the holders of the class C units on a hypothetical liquidation of the partnership after all capital accounts were first satisfied in full in accordance with the partnership agreement.

M. Real Estate Professional (*Teague*, T.C. Summary 2023-16)

1. Facts:

a. Taxpayer deducted $23,967 in rental real estate losses on three cabins in Maine.

b. IRS determined that the taxpayer actively participated in a real estate activity.

c. But, only $1,540 was deductible because of income phase-out.

d. Taxpayer claimed he was a real estate professional and not subject to the phase-out.

2. Real estate professional:

a. Materially participate for more than 750 hours; and

b. More than ½ of personal services are in the real property trade or business in which the taxpayer material participates.

3. Taxpayer:

a. Regularly visited the cabins.

b. Licensed real estate agent.

c. Did not maintain records of time spent.

d. Employed full time for Comcast.

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4. Result:

   a. Taxpayer believed he only needed 750 hours.

   b. But, really needed more than 1,850, since that was the amount of time he testified that he worked for Comcast.

   c. Taxpayer was unable to carry that burden of proof.

N. Professional Gambler (*Mercier*, U.S. Tax Court, June 6, 2023).

1. Facts:

   a. Taxpayers lived in Nevada and claimed to have extensive knowledge in video poker.

   b. Husband had an appliance repair business.

   c. Wife was an accountant.

   d. Did not report gambling income from Form W-2G on return, because gambling losses couldn't be utilized on Schedule A since they were lower than standard deduction.

   e. Claimed "unfair".

   f. Despite filing a Schedule C for the appliance business, didn't attempt to offset gambling winnings with losses on Schedule C until Notice of Deficiency received.

2. Court:

   a. "Serious" about gambling, but not professionals.

   b. E.g., kept no records and instead just relied on third-party information from the Casinos.

3. Nine Factor Test.

   a. Business approach (e.g., records).

   b. Expertise.

   c. Time & effort.

   d. Expectation that assets used in the activity may increase in value.

   e. Success in non-gambling activities.

   f. History of winnings & losses.

   g. Amount of occasional profits from gambling.

   h. Taxpayer’s financial status.

   i. Evidence of personal pleasure or recreation.

O. Casualty Loss (*Richey*, T.C. Memo. 2023-43)

1. Facts:

   a. Taxpayers claimed a casualty loss deduction of $640,000 based upon a claim that the value of their second home declined from $2.6 million to $1.9 million due to generalized flooding caused by Winter Storm Stella in 2017.

2. Background:

   a. Section 165 permits a deduction for a nonbusiness loss.

   b. Casualty loss is calculated by the difference in FMV before and after the casualty.

c. Reg. §1.165-7(a)(2)(iii) allows cost of repairs to be used if appraisals are not available.

3. Court denied deduction:

a. Taxpayer claimed that photos showing the damage were deleted from his phone during a software update, and the photos he did have only showed ordinary construction activities.

b. Did not have appraisals, just MLS printouts from a real estate broker generated after the IRS audit began.

c. Claimed repairs were more in the nature of improvements, e.g., a deck and pool.

d. The construction permit indicated a second phase of repairs, but those costs had not been incurred yet.

e. The absence of any evidence of the home's condition prior to the storm made it impossible to determine the extent to which the expenses were for repairs.

f. There was no evidence as to whether the repairs/improvements would increase the FMV of the house.

g. There was no evidence of claims under the taxpayer's homeowner's insurance and the results.

P. Qualified Conservation Contribution (*Cattail Holdings, LLC*, T.C. Memo. 2023-17)

1. Background:

a. Taxpayer deeded a conservation easement.

b. Claimed a charitable contribution deduction.

c. Deed prohibited:

i. The extraction of minerals; or

ii. The transportation of same if it would interfere with the conservation purposes of the property "in the discretion of the Grantee".

2. Law:

a. A deduction for a charitable contribution is not allowed unless the entire interest in the property has been transferred.

b. Exceptions:

i. Remainder interest in a home or farm;

ii. CRAT or CRUT;

iii. Qualified conservation easement; or

iv. Undivided part of the taxpayer's entire interest.

c. IRC §170(h)(5)(B)(i) excludes deductions for conservation easements where there is a retention of a mineral interest and there may be extraction of minerals by any surface mining method.

3. Tax Court:

a. IRS argued that the deed gave the taxpayer a contingent right to engage in surface mining.

b. Court disagreed and found that the deed prohibits surface mining and the discretion only related to the transportation of minerals that would interfere with the conservation purposes of the property.

Q. Damages for Emotional Distress are Taxable. (*Montes*, U.S. Tax Court, June 29, 2023)

1. Background – IRC §104(a)(2):

   a. Excludes from gross income "any damages other than punitive damages received whether by suit or agreement and whether as lump sums or as periodic payment on account of personal, physical injuries or physical sickness."

2. Facts:

   a. Taxpayer worked for the San Francisco Fire Department.

   b. Filed a lawsuit for harassment and settled.

   c. Did not report the payment received upon the advice of her CPA.

   d. IRS issued a notice of deficiency.

3. Court:

   a. The complaint alleged discrimination and retaliation.

   b. The settlement agreement indicated that the payment was for general damages, including emotional distress and attorney's fees.

   c. No physical injuries were alleged.

   d. Payment must therefore be included in taxable income.

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R. Cascading Credits. (*Webber*, U.S. Tax Court, May 12, 2023)

1. Facts:

   a. Taxpayer routinely filed tax returns late, but just before the statute of limitations ran.

   b. Instead of requesting a refund, applied refund to following year tax as a credit elect.

   c. Objective seemed to be to prevent the IRS from auditing the return that produced the credit being carried forward.

2. IRS:

   a. Denied the cascade of credit claims.

   b. Proposed collection by levy.

   c. Taxpayer argued that no refunds had been received.

3. Court:

   a. IRS has the discretion to credit the overpayment or refund it.

   b. Taxpayer has the burden of showing that the IRS allowed the credit.

   c. If taxpayer can't, then he/she can claim an overpayment which opens the prior year to audit.

S. False Installment Agreement. (*Crandell*, U.S. Court of Appeals for the 5th Circuit, June 9, 2023)

1. Facts:

a. Taxpayer was a medical doctor.

b. Did not file returns or pay taxes from 2006 through 2012.

c. Contracted with two hospitals, so no taxes were withheld.

d. Eventually, the taxpayer worked with a tax preparation firm to file the returns, but even then did not pay off the tax liability.

e. Taxpayer, working with the tax preparation firm, submitted a Form 433-A, *Collection Information Statement for Wage Earners and Self-Employed Individuals*.

f. The Form 433-A contained incomplete and inaccurate information.

2. Result:

a. The taxpayer was indicted for submitting a fraudulent Form 433-A.

b. Found guilty of tax evasion under IRS §7201.

c. Sentenced to 33 months in jail and $972,493.86 of restitution.

d. Taxpayer appealed claiming that submitting a false Form 433-A cannot support a conviction for tax evasion, because it is just a payment plan and does not change the amount owed.

e. The Court of Appeals disagreed and affirmed the conviction.

T. "Newly Discovered Evidence" (*Thomas*, 160 T.C. No. 4, February 13, 2023).

1. Background:

   a. IRC §6015(e)(7) requires the Tax Court only to consider:

      i. The administrative record as of the time of the determination.

      ii. Any additional newly discovered or previously unavailable evidence.

2. Facts:

   a. Surviving spouse seeking relief from joint and several liability for deceased husband's taxes.

   b. Sought to exclude blog posts from evidence.

3. IRC §6015(b) – Innocent spouse relief:

   a. Joint return.

   b. Understatement of tax attributable to one of the spouses.

   c. The other spouse did not know, and had no reason to know, about the understatement.

   d. Inequitable to hold the other spouse liable for the tax.

   e. Innocent spouse relief elected no later than two years after the IRS has begun collection activities.

4. Court:

   a. Issue of first impression.

   b. Held that the blog posts were "newly discovered" – at least by the IRS – as of the time of the trial.

   c. Relevant because they provided information about the spouse's lifestyle, assets and business.

U. Exceptions to Notice Requirement for Summonses. (*Polselli*, U.S. Supreme Court, May 18, 2023)

1. Background – IRC §7609(c)(2)(D):

   a. IRS may issue a summons both to determine whether a taxpayer owes tax and to collect the tax.

   b. Notice is required if the purpose of the summons is to determine the liability of the taxpayer.

   c. Notice is not required if the purpose of the summons is to collect the tax.

2. Facts:

   a. Taxpayer underpaid taxes for multiple years.

   b. IRS assessed over $2 million in taxes and penalties.

   c. In connection with its collection efforts, the IRS sent a summons to a law firm where the taxpayer had been a client.

   d. Notice of the summons was not sent to the taxpayer.

3. Decision:

   a. The taxpayer claimed that he had to have a legal interest in the account or records sought by the summons in order for the notice exception to apply.

   b. The Supreme Court disagreed.

   c. Only three requirements must be met to exempt the IRS from providing notice:

      i. The summons is issued to help collection.

      ii. It helps collection of an actual assessment made or judgment rendered.

      iii. The assessment or judgment is against the person with respect to whose liability the summons is issued.

V. ACA Payments Get Priority in Bankruptcy. (*In re: Howard D. Juntoff, Debtor*, Nos. 1:19-bk-17032, July 31, 2023)

1. The Sixth Circuit Court of Appeals, joining the Third and Fourth circuits, affirmed a bankruptcy appellate panel decision that reversed a bankruptcy court and held that the shared responsibility payment under the Affordable Care Act is a tax measured by income that is entitled to priority status under the Bankruptcy Code.

II. BUSINESS

A. Limitation on Excess Business Losses of Non-Corporate Taxpayers. (*IRC* §461(l)

1. TCJA limited the deduction of non-corporate business losses in excess of $250,000 ($500,000 MJF), adjusted annually for inflation, for tax years beginning before 1/1/2026.

2. CARES Act temporarily suspended the limitation for 2018-2020.

3. ARP extends the limitation on excess business losses to tax years beginning before 1/1/2027.

4. Inflation Reduction Act of 2022 extends it further to tax years beginning after 2026 and before 2029.

5. An excess business loss is:

   a. The taxpayer's aggregate deductions for the tax year from the taxpayer's trades or businesses, determined without regard to whether or not such deductions are disallowed for such tax year under the excess business loss limitation; over

   b. The sum of –

      i. The taxpayer's aggregate gross income or gain for the tax year from such trades or businesses, plus

      ii. $250,000, adjusted annually for inflation in tax years after 2018.

   c. For 2021, the amount is $262,000 ($524,000 for joint returns).

   d. For 2022, the amount is $270,000 ($540,000 for joint returns).

   e. For 2023, the amount is $289,000 ($578,000 for joint returns).

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6. Example:

a. Facts: For 2022, Sam, a single taxpayer, has $1 million of gross income and $1.4 million of deductions from a retail business that is not a passive activity.

b. Question: What is his excess business loss?

c. Answer: His excess business loss is $138,000 ($1,400,000 – [$1,000,000 + $270,000]). Sam must treat his excess business loss of $130,000 as an NOL carryforward to 2023.

B. Employee Retention Credit

1. IR-2023-169:

a. Immediate moratorium on processing ERC claims at least through December 31, 2023.

b. Payouts will continue though, albeit at a slower pace.

c. Result of concern about "honest small business owners being scammed" by promotors claiming contingency fees, e.g., 25% of the refund.

d. Both specially trained auditors and IRS Criminal Investigation division are actively working to identify fraudsters.

2. OVERVIEW:

a. Eligibility:

i. A full or partial suspension of operations due to orders from an appropriate government authority during 2020 or the first three quarters of 2021.

ii. A significant decline in gross receipts during 2020 or a decline in gross receipts in the first three quarters of 2021.

(a). For 2020, less than 50% of gross receipts in same calendar quarter as 2019.

(b) For 2021, less than 80% of gross receipts in same calendar quarter as 2019.

iii. Qualification as a "recovery startup business" in the third or fourth quarter of 2021.

b. Wages Eligible:

i. Claimed on wages paid between March 13, 2020 and December 31, 2021.

(a) For 2020, 50% of qualified wages ($10,000 per employee for the year including health care expenses).

(b) For 2021, 70% of qualified wages ($10,000 per employee per calendar quarter including health care expenses).

ii. Claim the credit by amending affected Forms 941, Employer's Federal Quarterly Tax Returns.

c. Supply chain issues:

i. Example of an area of concern.

ii. Addressed in new FAQs added on July 28, 2023.

(a) Government order caused supplier to suspend operations;

(b) Could not obtain supplier's goods or materials elsewhere (regardless of cost); and

(c) Resulted in full or partial suspension of business operations.

C. Limited Partner Exception

1. Background:

a. IRC §1402(a)(13), enacted in 1977, generally excludes a limited partner's share of partnership income or loss from SECA tax.

b. The exclusion does not apply to guaranteed payments.

c. The IRS proposed regulations a couple of times, most recently in 1997, but they stalled when Congress imposed a temporary moratorium.

d. The 1997 proposed regulations were based on factors involving liability, management and participation.

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2. Developments:

   a. The courts have largely been left to sort out limited partner status.

   b. For example, in *Renkemeyer* attorneys who actively participated in an LLP were found not to be limited partners.

   c. In 2018, a SECA compliance program was launched focusing on partnerships operating in the asset management, financial services, private equity and hedge fund industries.

   d. A guidance project has now appeared on the 2023-2024 priority guidance plan released September 29, 2023.

D. Relief for S Corporations

1. Rev. Proc. 2022-19 details the areas in which the IRS will not ordinarily issue a PLR and, in doing so, amplifies and modifies Rev. Proc. 2022-3.

2. However, Rev. Proc. 2022-19 also allows S corporations and their shareholders to obtain relief in six frequently-encountered areas without requesting a private letter ruling.

3. The IRS identified these issues as not affecting the validity or continuation of a corporation's election to be treated as an S corporation or to treat its corporate subsidiary as a qualified subchapter S subsidiary (QSub).

4. Key areas include:

   a. The one class of stock requirement and governing provisions, including "principal purpose" conditions;

   b. Disproportionate distributions;

c. Certain inadvertent errors on or omissions from Forms 2553 (S election) or Form 8869 (QSub election), which Rev. Proc. 2013-130 and Rev. Proc. 2004-35 do not address;

d. Missing administrative acceptance letters for an S election or QSub election;

e. Federal income tax return filing inconsistent with an S election or a QSub election; and

f. Potential retroactive corrections of nonidentical governing provisions (e.g., rights to distributions or liquidation proceeds that are not identical among shareholders).

5. The appendices to Rev. Proc. 2022-19 provide a sample corporate governing provision statement and a sample shareholder statement.

6. An officer and affected shareholders must complete and sign these statements to rely on Rev. Proc. 2022-19 for relief related to retroactive corrections of nonidentical governing provisions.

7. Rev. Proc. 2022-19 is effective October 11, 2022 and includes a transition rule for pending PLRs.

E. Unannounced Revenue Agent Visits

1. IR-2023-133:

a. IRS announced that it is ending most unannounced visits to taxpayers by revenue agents.

b. Replaced by mailed letters to schedule visits.

c. Attributed to:

i. Safety concerns.

ii. Inflammatory rhetoric confusing taxpayers about visits by revenue agents.

F. Form 8300

1. IR-2023-157:

a. Starting January 1, 2024, businesses are required to e-file Form 8300, *Report of Cash Payments over $10,000*.

2. Exceptions:

a. Fewer than 10 information returns for the calendar year.

b. Can request a waiver for hardship by filing Form 8508, but the waiver applies to all information returns.

G. COD Income and the SMLLS (*Jacobowitz*, T.C. Memo. 2023-107)

1. Facts:

a. Taxpayer operated a business through an SMLLC.

b. Never filed a Form 8832, *Entity Classification Election*.

c. Secured a loan through a local bank.

d. Closed the business in 2008.

e. Bank sent the IRS a Form 1099-C, Cancellation of Debt, for 2016.

f. Taxpayer did not include any COD income on his 2016 Form 1040.

g. IRS issued a notice of deficiency.

2. Taxpayer:

a. Did not dispute debt.

b. Argued that under state law the members of an LLC are not personally liable for the debts of the LLC.

3. Court:

a. Disagreed.

b. Under the “check-the-box” regulations the LLC was a disregarded entity for tax purposes.

c. Thus, the taxpayer was obliged to report on his personal return any income or loss attributable to the LLC.

H. Cancellation of Nonrecourse Debt: (*Parker*, T.C. Memo. 2023-104).

1. Facts:

a. S corporation sold interest in real estate to unrelated third party.

b. Lender agreed to cancel nonrecourse debt owed by disregarded entities that the corporation controlled.

c. Instead, lender received partial payment from the buyer, new guarantees and an escrowed deed.

2. Taxpayer:

a. Argued that the nonrecourse debt was excludable cancellation of debt income under IRC §108(a)(12)(B) because the S corporation was insolvent.

3. Court:

a. Cancelled nonrecourse debt was gain realized on the sale.

b. Not excludable cancellation of debt income.

I. Accountable Plan: (*Simpson*, T.C. Memo. 2023-4)

1. Background.

a. Accountable plan.

i. Employee pays expense, submits receipt, and corporation reimburses.

ii. Excluded from employee's wages.

iii. Deductible by corporation.

b. No accountable plan.

i. Reimbursement is included in employee's wages.

ii. Employee treats reimbursement as an unreimbursed employee business expense subject to the 2% AGI limit on miscellaneous itemized deductions (which are not currently deductible).

2. Accountable plan (IRC §62(a)(2)(A)):

a. Reimbursement must be for business expense allowable as a deduction paid or incurred by the employee in connection with the performance of services as an employee of the employer.

b. Expense must be substantiated within a reasonable period of time.

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c. Reimbursement of travel & entertainment expenses must meet the strict substantiation requirements of IRC §274(d) and the regulations.

d. For other expenses, substantiation must be sufficient to identify the nature of the expense and how it is attributable to the employer's business.

e. Excess reimbursements must be returned to the employer within a reasonable period of time.

3. Facts:

a. Taxpayers operated a business out of their house.

b. Claimed to have an unwritten accountable plan.

c. IRS disagreed and claimed:

i. The reimbursements should be included in wages.

ii. The expenses should be treated as unreimbursed employee business expenses.

4. Court:

a. An accountable plan does not necessarily have to be in writing.

b. But, here there was no evidence that the corporation required any substantiation or that any excess amounts be returned.

c. Company was an S corporation, and reimbursements were indistinguishable from distributions.

J. Mileage Log (*Craddock*, T.C. Summary 2023-4)

1. Background:

   a. To substantiate vehicle expenses, IRC §274(d) requires:

      i. Amount of expense.

      ii. Time and place of expense or use of listed property.

      iii. Business purpose of expense or use.

      iv. Business relationship.

   b. Car & truck expenses also require a contemporaneous log, trip sheet or similar record, as well as corroborating documentary evidence.

2. Facts:

   a. In addition to the W-2 job, taxpayer had an unincorporated business making sales call.

   b. Typically drove his pick-up truck to work, and then left to conduct those sales calls.

   c. Provided a mileage log and bank statements identifying various expenses as for "tolls," "car parts," "fuel," and "insurance."

3. Court:

   a. Disallowed the deductions as not credible.

   b. Mileage log showed the taxpayer in one state when the bank statements showed him in another.

   c. No corroborating evidence provided other than the taxpayer's own testimony.

K. Income Statement Verified by CPA not Substantiation (*Barrios*, T.C. Memo. 2023-32).

1. Facts:

   a. Taxpayer did not file a 2011 tax return.

   b. IRS prepared a substitute return based upon information provided by third parties.

   c. Taxpayer petitioned the Tax Court and filed a return prepared by a CPA in 2018 while the case was pending.

   d. Return showed $7,565,528 in gross receipts, $6,266,451 for COGS, $1,257,618 for wages, $54,024 for insurance, $35,144 for depreciation, and $189,368 for miscellaneous expenses.

   e. Taxpayer primarily relied on a profit & loss statement reconstructed after litigation had begun.

   f. CPA supervised the preparation by discussing with the taxpayer's bookkeeper her general approach as to the inclusion and categorization of the 2011 expenses, and then spot-checking the work.

   g. Bookkeeper used QuickBooks for the reconstruction, but had no direct knowledge of the expenses.

   h. There was also some information from PayChex, Inc., but no testimony concerning the company's recordkeeping system.

2. Court:

a. Ruled that taxpayer failed to substantiate expenses in excess of the amounts allowed by the IRS.

b. Lack of documentary evidence.

c. Non-compelling nature of the CPA's testimony.

d. CPA's "confidence that these expenses are substantially correct" is insufficient to substantiate the nature, amount or purpose of the claimed deductions.

L. Small Business Stock Exclusion (Ltr. Rul. 202319013)

1. Background:

a. IRC §1202 excludes gain from the sale of qualified small business stock held for more than 5 years:

Stock Issuance Date	Exclusion
8/11/1993 to 2/18/2009	50%
2/19/2009 to 9/27/2010	75%
9/28/2010 -	100%

b. Must be a C corporation that satisfies the active business requirements of IRC §1202(e).

i. At least 80% of the assets are used in the active conduct of a qualified trade or business.

ii. “Qualified trade or business” does not include:

(a) Health, law, engineering, architecture, accounting, actuarial science, performing arts, athletics, financial services, brokerage services, or consulting.

(b) Trades or businesses where the principal asset is the reputation or skill of one or more of its employees.

2. Facts:

a. Enterprise cloud application services software company.

b. Employees had specialized technical skills and knowledge from training they received on the company’s proprietary processes.

c. Company could recruit and train new employees to provide substantially the same services using its proprietary processes.

3. IRS Ruled:

a. Principal asset was intellectual property, not the skill of one or more employees.

b. Qualifies for the IRC §1202 exclusion.

M. Taxation of Unrealized Income (*Moore v. United States*, U.S. Supreme Court Docket #22-800.

1. Issue:

a. Constitutionality of taxing the deemed repatriation of earnings under IRC §965 enacted by the TCJA of 2017.

2. Background:

   a. Taxpayer invested in an Indian company that was a controlled foreign corporation.

   b. IRC §965 deems the accumulated post-1986 deferred foreign income to be Subpart F income for 2017 or 2018, depending on its taxable year end.

3. Taxpayer's Argument:

   a. IRC §965 is an unapportioned direct tax that is not an income tax, thus violating the apportionment clause in the U.S. Constitution.

   b. Essentially, the argument is that a tax on unrealized income is unconstitutional.

4. Government's Argument:

   a. There is no blanket constitutional ban on Congress's disregarding corporate form to facilitate taxation of shareholders' income.

5. Ramifications:

   a. Subpart F.

   b. Tax on global intangible low-taxed income (GILTI).

   c. New book minimum tax.

   d. Mark-to-market for securities dealers.

   e. Constructive sales, such as equity swaps.

   f. Taxation of derivatives.

6. Revenue Effects:

   a. If GILTI is struck down, perhaps $350 billion over the next 10 years.

   b. Another $75 billion over the same period of Subpart F is repealed.

III. **<u>INFLATION REDUCTION ACT.</u>**

A. Inflation Reduction Act of 2022.

1. Many Tax Credits and Related Provisions:

   a. Clean Energy Tax Credits.

   b. Carbon Management.

   c. Residential Energy Efficiency.

   d. Offshore Wind and Oil & Gas Systems.

   e. Community Investment and Energy Justice.

   f. Investments in the Permitting Process.

   g. Clean Energy Financing.

   h. Agriculture & Forestry.

2. New Advanced Manufacturing Production Tax Credit (IRC §45X).

   a. Tax credit for the production of clean energy technology components that are produced in the United States or by a U.S. possession.

   b. Eligible components include solar components, wind turbine and offshore wind components, inverters, many battery components, and the critical minerals needed to produce these components.

   c. Begins to phase out in 2029 and phases out completely in 2032.

3. Extension of Energy Investment Tax Credit (IRC §48).

   a. Extends the existing energy investment tax credit for applicable energy projects.

   b. Ends in 2024 for most technologies and is replaced by the new tech-neutral Clean Electricity ITC (48E), which begins in 2025.

   c. Extends date of construction in most cases to 2024 and maintains a 10% or 30% credit.

4. New Clean Electricity Investment Tax Credit (IRC §48E).

   a. This newly established ITC replaces the Energy ITC once it phases out at the end of 2024.

   b. 48E is an emissions-based incentive that is neutral and flexible between clean electricity technologies.

   c. Taxpayers choose between a PTC (45Y) and an ITC (48E).

5. Clean Vehicle Credit (IRC §30D)

   a. Maintains the existing $7,500 consumer credit for the purchase of a qualified new clean vehicle, including electric vehicles, plug-in hybrids, and hydrogen fuel cell vehicles.

   b. Maximum of $80,000 per vehicle for vans, SUVs and pickups and $55,000 for other vehicles.

   c. Income eligibility limit of $150,000 or $300,000 for joint filers.

   d. Eliminates the previous manufacturer quota, which phased out the tax credit for manufacturers as they neared 200,000 clean vehicles sold.

6. New Previously Owned Clean Vehicle Credit (IRC §25E).

   a. Tax credit for the purchase of previously owned clean non-commercial vehicles, including electric vehicles and plug-in hybrids.

   b. Credit is equal to the lesser of $4,000 or 30% of the vehicle cost.

   c. Sets a maximum sale price of $25,000.

   d. Model must be at least 2 years older than the year of sale.

   e. Implements an income eligibility limit of $75,000 or $150,000 for joint filers.

B. Transferability of EV Credit at Point of Sale (REG-113064-23).

1. Under proposed regulations issued October 6, 2023, starting January 2024 qualified taxpayers will be able to transfer the Section 30D and section 25E tax credits, worth up to $7,000 for the purchase of a new electric vehicle and $4,500 for a used electric vehicle, respectively, directly to the car dealer at the point of sale.

2. "Allows consumers to reduce the up-front cost a clean vehicle, expanding consumer choices and helping car dealers expand their businesses".

3. Treat the transfer as being repaid by the consumer to the dealer as part of the purchase price of the vehicle, thereby not affecting the dealer's tax liability.

4. Consumers looking to take advantage of the credit must attest to being under the eligible income threshold.

5. Car dealers must register under a new website, the "IRS Energy Credits Online Portal," to take part in the program.

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C. Inflation Reduction Act of 2022.

1. New Commercial Clean Vehicle Credit (IRC §45W).

a. For class 1-3 (under 14,000 lbs.) vehicles for commercial use, creates a $7,500 tax credit tax for the purchase of electric vehicles or other qualified clean vehicles.

b. For class 4 and above (over 14,000 lbs.) vehicles for commercial use, increases the credit to $40,000.

2. Credit for Residential Clean Energy (IRC §25D).

a. Extends credit through 2034 for residential solar, wind, geothermal, and biomass fuel.

b. Maintains the previous credit rate but adjusts the project dates.

c. Applies a 30% credit for projects started between 2022 and 2032.

d. Credit decreases to 26% for projects started in 2033 and 22% for projects started in 2034.

e. Expands eligibility to battery storage technology.

3. Credit for Energy Efficiency Home Improvements (IRC §25C).

a. Extends credit for energy efficiency home improvements through 2032.

b. Increases credit from 10% to 30%.

c. Replaces lifetime cap on credits with a $1,200 annual credit limit, including $600 for windows and $500 for doors.

d. Increases limit to $2,000 for heat pumps and biomass stoves.

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e. Removes eligibility for roofs.

f. Updates language to reflect advances in energy efficiency.

g. Expands credit to cover the cost of home energy audits up to $150 and electrical panel upgrades up to $600.

4. Notice 2023-59:

a. Outlines requirements for claiming the IRC §25C home energy audit credit that are expected to be included in proposed regulations.

b. Examples of topics include:

i. Home energy audit.

ii. Qualified home energy auditor (not required for 2023).

iii. Qualified certification program.

iv. Written report.

v. Substantiation requirement.

5. Credit for builders of new energy-efficient homes (IRC §45L).

a. Eligible contractors who build or substantially reconstruct qualified new energy-efficient homes may be able to claim tax credits up to $5,000 per home.

b. Preliminary guidance may be found in Notice 2023-65.

6. Home Energy Performance-Based Whole House Rebates (HOMES).

   a. $4.3 billion through 2031 to DOE to help state energy offices implement a HOMES rebate program to provide rebates to homeowners and aggregators for whole-house energy saving retrofits.

   b. Additional funding can be provided to low- and moderate-income individuals, who earn less than 80% of the area median income.

7. High-Efficiency Electric Home Rebate Program.

   a. $4.5 billion through 2031 for grants from DOE to States and Tribes to implement a high-efficiency electric home rebate program.

   b. Provides up to $14,000 per household including $8,000 for heat pumps, $1,750 for heat pump water heaters, and $840 for electric stoves.

   c. Also includes rebates for improvements to electrical panels or wiring and home insulation or sealant.

   d. Eligible recipients must fall below 150% of the area median income.

D. New EV Tax Credit.

1. Example:

   a. Facts: The Inflation Reduction Act, which the President signed on August 16, 2022 created a $7,500 tax credit for consumers who buy new electric vehicles.

   b. Question: Do you qualify?

   c. Answer: Maybe!

2. The credit is non-refundable, so you need at least $7,500 in taxes.

3. Beginning in 2023:

   a. A tax credit isn't available to single individuals with modified adjusted gross income over $150,000.

   b. The cap is higher for others - $225,000 for heads of household and $300,000 for married couples who file a joint tax return.

   c. The test applies to income for the current or prior year, whichever is less.

   d. Sedans with a retail price of more than $55,000 aren't eligible, nor are vans, SUVs or trucks over $80,000.

4. A new requirement for final assembly in North America was added that took effect on August 16, 2022.

5. If you bought a new Chevy Bolt in 2022 – an EV made in the U.S. – it did not qualify for the Clean Vehicle Credit because of the old 200,000- vehicle cap on the credits; but if you waited until January 1, 2023, those old 200,000-vehicle limit rules disappeared and you could once again get that EV tax credit.

6. After 2023, vehicles will not qualify for the EV tax credit if any components in the battery are manufactured or assembled by a "foreign entity of concern" (e.g., Huawei in China).

7. About half the credit or $3,750 is based on where the battery components are made or assembled, e.g. –

   a. 40% for EVs that go on sale before 2024.

   b. 50% for EVs that go on sale in 2024.

   c. 60% for EVs that go on sale in 2025.

   d. 70% for EVs that go on sale in 2026.

   e. 80% for EVs that go on sale after December 31, 2026.

8. Just like battery components, the credit has requirements based on where the raw materials used in the battery come from that must be met to qualify for half of the credit or $3,750:

   a. 40% of "critical minerals" through end of 2023.

   b. 50% in 2024.

   c. 60% in 2025.

   d. 70% in 2026.

   e. 80% after 2026.

E. Reporting Rules for Clean Vehicle Credits.

1. Rev. Proc. 2022-42, released December 12, 2022:

a. Initial guidance on how auto manufacturers and dealers can qualify their cars available for clean vehicle credits.

b. Manufacturer's generally must enter into written agreements with the IRS agreeing to make periodic written reports with VIN numbers for each vehicle sole.

c. Seller's likewise must make reports about each sale in order for the new or used vehicles sold to be eligible for the tax incentives.

F. 2023 EV Credit Availability.

1. Notice 2023-1:

a. Guidance on what cars and trucks qualify for the new clean vehicle tax credits in 2023.

i. Includes only four manufacturers: Ford, Rivian, Stellantis, and Nissan.

b. Provides guidance on how it will calculate a vehicle's manufacturer's suggested retail price for purposes of qualifying for the credit.

c. Leaves open questions about how requirements for electric vehicle battery content will work.

2. Note: Notice 2023-9 provides additional guidance on the commercial clean vehicle credit.

G. Prevailing Wage and Apprenticeship Requirements. (Notice 2022-61)

1. Increased credit amounts and deductions may be available to certain taxpayers satisfying prevailing wage and apprenticeship requirements.

   a. Increased credits: IRC §30C, 45, 45Q, 45V, 45Y, 45Z, 48, 48C and 48E.

   b. Increased deductions: IRC §179D.

   c. Increased credits also available under IRC §45L and 45U if just a prevailing wage requirement is satisfied.

2. The prevailing wage requirement is met if laborers and mechanics are paid at rates not less than the prevailing rates for construction, alteration or repair of similar character in the locality where the facility is located as determined by the Secretary of Labor.

3. The apprenticeship requirement is met if the following percentage of total labor hours is performed by qualified apprentices:

   a. 10% if construction begins prior to 1/1/2023.

   b. 12.5% if construction begins after 12/31/2022 and before 1/1/2024.

   c. 15% if construction begins after 12/31/2023.

IV. **CORPORATE TRANSPARENCY ACT**

A. Corporate Transparency Act.

1. National Defense Authorization Act for Fiscal Year 2021 (NDAA).

2. NDAA included significant reforms to the U.S. anti-money laundering and countering the financing of terrorism regime.

3. Division F of the NDAA consists of the Anti-Money Laundering Act of 2020, which includes the Corporate Transparency Act (CTA).

4. Congress enacted the CTA to establish uniform beneficial ownership information reporting requirements to improve transparency for national security, intelligence, and law enforcement agencies in their efforts to detect and prevent money laundering and terrorist financing.

5. On September 29, 2022, the U.S. Department of the Treasury's Financial Crimes Enforcement Network (FinCEN) issued regulations regarding the beneficial ownership reporting requirements.

6. The final rulemaking is effective January 1, 2024.

7. Reporting companies created or registered before January 1, 2024, will have one year (until January 1, 2025) to file their initial reports.

8. Reporting companies created or registered after January 1, 2024, will have 30 days after creation or registration to file their initial reports.

9. FINCEN has issued a Notice of Proposed Rule Making that would extend the 30-day period to 90 days for new entities created in 2024.

10. Several Exemptions:

    a. Financial institutions or certain issuers of securities in heavily regulated industries (e.g., banks, credit unions, broker-dealers, money services businesses registered with FinCEN, and issuers registered with the U.S. Securities and Exchange Commission).

    b. "Large operating companies".

        i. Entity that employs more than 20 full time employees in the U.S.,

        ii. Has an operating presence at a physical office within the U.S., and

        iii. Filed a federal income tax or information return in the U.S. for the previous year demonstrating more than $5,000,000 in gross receipts or sales.

    c. Other types of legal entities, including certain trusts, will be excluded to the extent that they are not created by the filing of a document with a secretary of state or similar office.

11. A "reporting company" is a corporation, limited liability company, or other similar entity that is:

    a. Created by the filing of a document with a secretary of state or similar office, or

    b. Formed under the law of a foreign country and registered to do business in the U.S. by the filing of a document with a secretary of state or a similar office.

12. Note: There is no dollar minimum or profit motive requirement.

13. Examples:

    a. Single owner S corporation or single member LLC filing a Schedule C.

    b. A hobby that generates no profits if it is registered as an LLC for liability protection purposes.

14. A "beneficial owner" is an individual who, directly or indirectly, through any contract, arrangement, understanding, relationship, or otherwise:

    a. Exercises substantial control over the entity, or

    b. Owns or controls not less than 25 percent of the ownership interests of the entity.

15. Examples:

    a. Senior officer of the reporting company;

    b. Having authority over the appointment or removal of any senior officer or a majority of the board of directors (or similar body); or

    c. Directing, determining, or having substantial influence over important decisions made by the reporting company.

16. In addition to reporting information about itself and its beneficial owners, and entity created on or after January 1, 2024 must also report information about its “company applicants”.

    a. The individual who directly files the document that creates or first registers the reporting company.

    b. The individual primarily responsible for directing the filing of the relevant document.

    c. There can be up to two persons who qualify as company applicants.

17. Penalties for Noncompliance:

    a. Civil Penalties:

        i. Not more than $500 for each day that the violation continues.

    b. Criminal Penalties:

        i. Fines of not more than $10,000, and

        ii. Imprisonment for not more than two years, or both.

    c. Separate from the CTA, persons could face criminal liability under the federal criminal code, which prohibits knowingly and willfully providing false information or concealing a material fact to any of the three branches of the federal government.

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18. Example:

    a. Facts: You are the sole owner and the president of an LLC.

    b. Question: Are you the beneficial owner?

    c. Answer: You are the beneficial owner because you exercise substantial control as the senior officer, you own more than 25%, and no one else exercises substantial control.

19. Example:

    a. Facts: A, B and C own 50%, 40% and 10%, respectively, of a company, and D serves as president.

    b. Question: Who are the beneficial owners?

    c. Answer: A & B are beneficial owners because they own more than 25%. D is a beneficial owner because he exercises substantial control as a senior officer. C is not a beneficial owner.

20. Example:

    a. Facts: Four individuals each own 25% of a company, and four additional persons serve as CEO, CFO, COO and general counsel.

    b. Question: Who are the beneficial owners?

    c. Answer: All eight are beneficial owners,

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21. Example:

    a. Facts: Person A prepares and files a document through an online portal creating a new company.

    b. Question: Who is the company applicant?

    c. Answer: Person A

22. Example:

    a. Facts: Person A prepares a document creating a new company and directs person B to file it using an online portal.

    b. Question: Who is the company applicant?

    c. Answer: Persons A and B.

V. **RETIREMENT**

A. Proposed Regulations on RMD's (*REG-105954-20).*

1. Issued on February 3, 2022, under the SECURE Act.

2. Address two important issues relating to RMDs.

    a. Delay in RBD to age 72 (now age 73 for 2023 under SECURE 2.0.); and

    b. 10-year limit on RMDs after death.

3. Distributions taken in 2021 can be based on a "reasonable interpretation of the law".

4. Eligible Designated Beneficiary ("EDB").

   a. The participant's surviving spouse.

   b. The employee's child who has not yet reached the "age of majority".

   c. "Disabled".

   d. "Chronically ill".

   e. Not more than 10 years younger than the participant.

5. Death before RBD:

BENEFICIARY	DISTRIBUTION PERIOD
Not a "designated beneficiary"	5-year rule
Designated beneficiary, but not an EBD	10-year rule
EBD	Life Expectancy

6. Death after RBD:

BENEFICIARY	DISTRIBUTION PERIOD
Not a "designated beneficiary"	5-year rule
Designated beneficiary, but not an EBD	Life Expectancy for 10 years with balance distributed in 10th year
EBD	Life Expectancy

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7. "Age of Majority" – age 21.

8. "Disability".

   a. Unable to engage in substantial activity.

   b. A medically determinable physical or mental impairment that results in marked and severe functional limitations, and that can be expected to result in death or to be of long-continued and indefinite duration.

   c. Social Security Administration determination.

9. "Chronically ill".

   a. Unable to perform at least two activities of daily living (such as eating, toileting, and dressing) without substantial assistance for a lengthy, indefinite period.

   b. Plan receives documentation of that status by October 31 of the year following the year of the employee's death.

   c. *Note: The determination of disability or chronically ill is made as of the date the employee dies.*

10. Example:

   a. Facts: Ed names his nephew, Adam, as beneficiary of his 401(k) account. Ed dies March 2, 2023. Adam is involved in an accident September 15, 2023, and as a result is chronically ill.

   b. Question: Is Adam an EDB?

   c. Answer: Adam is not an EDB because he was not chronically ill when Ed died.

11. Example:

    a. Facts: Marie names her daughter, Donna, as beneficiary of her 403(b) account. When Marie dies at age 40, Donna is only 10 years old. At that time, she is not Disabled. However, five years later, Donna becomes disabled.

    b. Question: Is Donna an EDB?

    c. Answer: Donna is an EDB, because she is Marie's child who has not reached the age of majority. Ten years after Donna turns 21, the plan must distribute the entire account to Donna. Had she been disabled when Marie died, Donna would have been able to continue taking distributions throughout her life or life expectancy.

12. Trusts as Beneficiaries:

    a. Previously, the regulations treated a trust as being, at most, one designated beneficiary, with an age equal to that of the oldest beneficiary of the trust.

    b. In Private Letter Rulings, the IRS had allowed a more generous policy, particularly with regard to so-called "look-through" trusts.

    c. The Proposal codifies those trust rules, and thereby expands available estate planning techniques.

    d. If a trust satisfies the look-through rules, then the beneficiaries of the trust are considered designated beneficiaries.

13. Special Needs Trusts:

    a. SECURE Act 2.0 includes a clarification that a third-party special needs trust (e.g., a trust established by a parent for a child with a disability) may have a charitable organization as the remainder beneficiary.

    b. Concern was that it might preclude qualification for lifetime distributions to the disabled beneficiary of the SNT after the account holder's death.

    c. Effective starting in 2023.

14. 50% Penalty Tax Relief.

    a. Penalty applies if a participant or beneficiary does not take an RMD.

    b. RMD rules require the participant or his/her estate to take an RMD for the year of death in the same manner as if the participant lived until the end of the year – i.e., by December 31 of the year of death.

    c. Proposed regs would waive the penalty provided that the beneficiary takes the RMD no later than his or her tax return due date (with extensions).

    d. Note: SECURE 2.0 Act reduces the penalty to 25%. In addition, the penalty drops down to 10% if you take the necessary RMD by the end of the second year following the year it was due.

15. Effective date of the Proposed Regulations was January 1, 2022.

16. Notice 2022-53 provides that:

    a. The final RMD regulations will apply no earlier than 2023.

    b. A defined contribution plan will not be treated as having failed to satisfy the RMD rules under Code Section 4019(a)(9), as amended by the SECURE Act, merely because it did not make a "specified RMD".

    c. If a beneficiary did not take a "specified RMD" the IRS will not assert that the 50% excise tax applies, and will refund any excise tax that has already been paid for a missed RMD in 2021.

17. Notice 2023-54.

    a. Final regulations won't apply until 2024.

18. A "specified RMD" is defined as:

    a. Any distribution that would be required to be made in 2021 or 2022 under a plan or IRA if that distribution would be required to be made to:

        i. A designated beneficiary of an employee or IRA owner if the employee or IRA owner died in 2020 or 2021 and on or after their required beginning date, and the designated beneficiary is not an eligible designated beneficiary taking distributions under the life expectancy rule, or

        ii. A beneficiary of an eligible designated beneficiary if the eligible designated beneficiary died in 2020 or 2021 and they were taking distributions under the life expectancy rule.

B. Further Transition Relief:

1. Background:

a. Prior to SECURE 2.0, a person born in 1951 would attain age 72 in 2023, so 2023 RMD would due by April 1, 2024 and the 2024 RMD by December 31, 2024.

b. After SECURE 2.0, the person would attain age 73 in 2024, so 2024 RMD would due by April 1, 2025 and the 2025 RMD by December 31, 2025.

2. Notice 2023-54:

a. Any distributions made between January 1, 2023 and July 31, 2023 that were characterized as RMDs, but aren't under the new rules, could be rolled over by September 30, 2023.

C. ESOP Compliance Issues.

1. IR-2023-144, August 9, 2023.

a. Compliance issues with ESOPs identified by the IRS include:

i. Valuation issues with employee stock.

ii. Prohibited allocation of shares to disqualified persons.

iii. Failure to follow through with tax requirements for ESOP loans.

b. The IRS announcement provides examples of potentially abusive ESOP arrangements, including:

i. A business that creates a management S corporation whose stock is wholly owned by an ESOP for the sole purpose of diverting taxable business income to the ESOP.

ii. In this instance, the S corporation purports to have provided loans to the business owners in the amount of the business income to avoid taxation.

VI. **SECURE ACT 2.0.**

A. SECURE Act 2.0.

1. Included within the Consolidated Appropriations Act, 2023.

2. Called SECURE Act 2.0 because it builds on the changes made by the *Setting Every Community Up for Retirement Enhancement Act of 2019* (SECURE Act).

3. Originated as three separate bills:

a. SECURING A STRONG RETIREMENT ACT (H.R. 2954) passed by the House of Representatives on March 29, 2022.

b. RETIREMENT IMPROVEMENT AND SAVINGS ENHANCEMENT TO SUPPLEMENT HEALTHY INVESTMENTS FOR THE NEST EGG (RISE & SHINE) ACT (S. 435) approved by the Senate Health, Education, Labor, and Pensions Committee on June 15, 2022.

c. ENHANCING AMERICAN RETIREMENT NOW (EARN) ACT approved by the Senate Finance Committee on June 22, 2022.

B. SECURE Act 2.0: Retirement Plans.

1. Auto-enrollment.

   a. Mandatory for new plans starting in 2025.

   b. At least 3% of salary, no higher than 10%.

   c. Escalates at 1% per year of service up to a minimum of 10% and a maximum of 15%.

   d. An employee can opt out.

   e. Employers with 10 or fewer employees exempt.

2. The 10-50% nonrefundable saver's credit for contributions to retirement plans, IRAs and ABLE accounts is replaced.

   a. New 50% federal match of non-Roth contributions deposited into taxpayer's plan by Treasury.

   b. Phases out at certain income thresholds.

   c. Maximum $2,000.

   d. Effective after 12/31/2026.

3. Start-up Cost Credit for New Plan.

   a. Employers with 50 or few employees.

      i. Goes from 50% to 100% for 3 years.

      ii. Max $5,000 per year.

b. Employers with 51-100 employees.

i. 50%

ii. Max $5,000 per year.

c. Additional credit for up to $1,000 of employer matching.

4. SEP/SIMPLE Plans:

a. Employers may make additional discretionary contributions to SIMPLE plans.

i. Up to 10% of compensation.

ii. Maximum of $5,000 (indexed).

iii. Begins 2024.

b. Annual deferral and catch-up limits to SIMPLE plans increased by 10% starting in 2024 for employers with 25 or fewer employees.

c. Employers of domestic employees (e.g., nannies) may provide benefits under a SEP starting in 2023.

5. Long-term Part-Time Workers:

a. Employees working 500+ hours in 2 consecutive years must be eligible to defer.

b. Also applies to 403(b) plans.

c. Begins 2025.

d. Note: Under SECURE 1.0 there was a similar 3-year rule starting in 2024.

6. Pension-linked ("sidecar") emergency savings accounts:

   a. Employers may automatically opt NHCEs into emergency savings accounts.

   b. No more than 3% of salary.

   c. $2,500 cap.

   d. Contributions over limit can be stopped or directed to Roth account.

   e. Treated as Roth elective deferrals and may be matched up to the cap.

   f. Up to 4 no-fee, no-tax withdrawals available per year.

   g. Upon separation, account balance may be taken as cash or rolled into a Roth plan or IRA.

   h. Begins 2024.

7. Cash-out Distributions:

   a. Currently, plan sponsors may "cash-out" terminated participant balances under $5,000 and, unless the participant elects otherwise, rollover cash outs over $1,000 to an established IRA.

   b. Starting in 2024, $5,000 is increased to $7,000.

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c. An automatic portability provider ("APP") will be permitted to rollover an automatic cash out IRA established with a participant's prior employer-sponsored retirement plan into a subsequent eligible defined contribution employer-sponsored retirement plan, provided that:

i. The individual is an active participant in the subsequent plan;

ii. The participant was given notice and did not opt out of the transaction; and

iii. The APP acknowledges fiduciary status and meets certain other requirements.

8. Other retirement plan changes:

a. Employees making "qualified student loan payments" can have those payments matched in the retirement plan starting in 2024.

b. Catch-up contributions increase to $10,000 in 2025 for participants age 60-63.

c. 10% early distribution penalty waived for certain unforeseeable personal or family emergency expenses.

i. One distribution up to $1,000 per year.

ii. Option to repay within 3 years.

iii. Beings 2028.

d. Certain barriers to the availability of life annuities in qualified plans and IRAs eased starting in 2023.

e. Qualified longevity annuity contracts:

i. 25%df of account balance limit eliminated.

ii. Cap raised to $200,000.

iii. Begins immediately.

f. Starting in 2023r, new 401(k) plans sponsored by sole proprietors or single-member LLCs may allow certain deferral contributions up to the date of the employer's tax return filing date for the first year of the plan.

g.. Starting in 2024, discretionary plan amendments increasing benefits may be adopted by the due date of the employer's tax return.

h. Effective immediately, early distributions to terminally ill individuals are exempt from the 10% premature distribution penalty.

i. A surviving spouse is currently allowed to elect to treat a deceased IRA owner's IRA as the surviving spouse's own IRA for RMD purposes. Starting in 2024, this option is extended to qualified plans.

j. Starting 3 years after enactment, distributions up to $2,500 per year too pay premiums on long-term care insurance contracts are exempt from the 10% premature distribution penalty.

k. Roth IRAs are currently exempt from the RMD rules. Starting in 2024, this exemption is extended to Roth amounts in qualified plans.

l. Starting in 2023, a SEP and a SIMPLE IRA are permitted to be designated as Roth IRAs.

m. Plans may allow employees to designate employer matching or nonelective contributions as Roth contributions (effective immediately).

n. All catch-up contributions to qualified plans must be made on a Roth basis.

i. Exception for participants whose prior year wages do not exceed $145,000 (indexed).

ii. Not applicable to SIMPLE IRAs and SEP plans.

iii. This was one of the primary revenue raisers to get the Act within the 10-year budget window by which legislation is "scored" for cost purposes.

o. Notice 2023-62 indicates that the first two years after December 31, 2023 will be treated as an administrative transition period, so the foregoing requirement will apply beginning after December 31, 2025.

C. SECURE Act 2.0: Individual Retirement Accounts (IRA).

1. Required Minimum Distributions (RMDs):

a. Increase in required minimum distribution age:

i. Age 73 starting January 1, 2023

ii. Age 75 starting January 1, 2033.

b. Beginning in 2023, the penalty for not taking an RMD is reduced from 50% to 25%d, and decreased even further to 10% if corrected during a 2 year window.

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2. IRA charitable donations:

   a. Currently, individuals age 70-1/2 and older may transfer up to $100,000 per year from an IRA to a public charity or private operating foundation.

   b. Expanded to permit a one-time election to transfer up to $50,000 to a qualifying charitable remainder annuity trust, a charitable remainder unitrust, or a charitable gift annuity.

   c. The $50,000 and $100,000 limits will be indexed for inflation.

   d. Effective for taxable years ending after the date of enactment.

3. Other IRA changes:

   a. Catch-up limit for those age 50 and older is inflation indexed after December 31, 2023.

   b. Beneficiaries of 529 college savings accounts are permitted tax and penalty free rollovers of up to $35,000 over their lifetime to ROTH IRAs starting in 2024.

   c. Effective immediately, corrective distributions of excess contributions to an IRA are no longer subject to the 10% premature distribution penalty.

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VII. **ESTATE PLANNING**

A. Proposed Clawback Regs. (*REG-118913-21)*

1. TCJA doubled the estate and gift tax exemption from $5 million to $10 million, inflation adjusted until Jan. 1, 2026.

2. However, it wasn't clear under TCJA what happens if the taxpayer makes gifts while the higher exemption is in place and then dies after the higher exemption sunsets and the exemption is lower.

3. Reg. 20.2010-1(c)(1), published November 26, 2019, provided relief from the "clawback".

4. Proposed regs released April 26, 2022, would exclude certain transactions from the anti-clawback rules.

5. Proposed Regs would exclude:

a. Transfers where the donor retains a life estate or other powers or interests described in Section 2035 through 2038 and Sec. 2042, including gifts made within three years of death and life insurance policies with reversionary interests.

b. Enforceable gifts of promissory notes if the promissory note has not yet been paid.

c. Gifts of interests in family partnerships and LLCs under Sec. 2701 where the senior generation maintains a preferred equity interest.

d. Gifts of interest in trusts, including GRATs and QPRTs, subject to the special valuation rules of Sec. 2702.

e. The relinquishment of an interest involving any of the above transactions within eighteen months of the donor's death.

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6. Example:

   a. Facts: Rob makes a completed gift of a promissory note in the amount of $9,000,000 on January 1, 2023. The promissory note is Rob's only lifetime gift, and it remains unpaid as of the date of Rob's death on January 1, 2026, at which time the lifetime exemption amount for estate tax purposes has been adjusted to $6,800,000.

   b. Question: Is the note includible in Rob's estate?

   c. Answer: The note is treated as includible in Rob's gross estate, and the anti-clawback rules do not apply to the original gift of the note in 2023. As a result, Rob's estate tax is calculated using the reduced $6,800,000 lifetime exemption amount.

7. Two exceptions to the proposed regs:

   a. Transfers where the portion subject to gift tax is less than 5% of the total value of the transfer.

   b. Relinquishments of interests that are triggered by either the passage of time or the death of an individual if provided for in the terms of the original instrument effectuating the transfer.

B. Proposed Estate Administration Regulations.

1. Published June 28, 2022 under Section 2053: (87 Fed. Reg. 38331 (Federal Register: Guidance Under Section 2053 Regarding Deduction for Interest Expenses and Amounts Paid Under a Personal Guarantee, Certain Substantiation Requirements, and Applicability of Present Value Concepts)

a. Provide guidance on the use of present-valued principles in determining the amount deductible by an estate for funeral expenses, administration expenses and certain claims against the estate;

b. Provide guidance on the deductibility of interest expense accruing on tax and penalties owed by an estate and interest expense accruing on certain loan obligations incurred by an estate;

c. Amend and clarify the requirements for substantiating the value of a claim against an estate that's deductible in certain cases; and

d. Provide guidance on the deductibility of amounts paid under a decedent's personal guarantee.

C. Present Value Principles Used to Determining Amount Deductible Under Section 2053.

1. The Proposed Regulations:

a. Require calculating the present value of the amount of a deductible claim or expense that isn't paid or to be paid on or before the third anniversary of the decedent's date of death.

b. The discount rate to be used is the applicable federal rate determined under IRC Section 1274(d) for the month in which the decedent's date of death occurs, compounded annually.

c. Require a supporting statement to be filed with the Form 706 estate tax return showing any calculations of present value.

d. Provide that the expected date or dates of payment generally must be identified in a written appraisal document.

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D. Deductibility of Interest on Unpaid Estate Tax.

1. Background:

a. Section 2053(c)(1)(D) states that no deduction is allowed for interest payable under Section 6601 (underpayments) because of an election under Section 6166 to pay estate tax in installments.

b. Reg. §20.2053-3(a) permits the deduction of expenses actually and necessarily incurred in the administration of an estate.

c. Reg. §2053-1(b)(2) states that only expenses that are bona fide in nature are deductible.

2. Proposed Regulations under Section 2053: (REG-130975-08, June 28, 2022)

a. Allows "non-section 6166 interest" to be deducted as an administrative expense if it is "bona fide".

i. Section 6161 extension for reasonable cause.

ii. Section 6163 deferral when value of a remainder or reversionary interest is includible in the gross estate, but the value is not available.

iii. Underpayment of a tax or deficiency.

b. "Non-section 6166 interest" may also be deductible if it meets the "actually and necessarily incurred" test, but that depends on the facts and circumstances.

E. Interest on Graegin Loans.

1. A Graegin loan is a loan to the estate in order to facilitate the payment of estate taxes and other expenses of the administration of the estate, the interest of which is deductible under Section 2053(a)(2) of the Code (*Estate of Graegin v. Commissioner*, T.C. Memo. 1988-477).

2. The idea behind the Graegin loan is that the full amount of the interest that will be paid over term of the loan is taken as a current deduction, dollar for dollar, from the gross estate.

3. Example:

   a. If an estate borrows $10 million at 5% interest on a ten-year note, the loan can be structured with all principal and interest deferred until a balloon payment at the end of the term.

   b. Up front, the entire $5 million of interest ($10 million x 5% x 10 - $5 million) would be deductible from the gross estate, creating an estate tax savings of at least $2m (these loans by their terms cannot be prepaid (unless at that time all interest payable on the full note would be due).

4. The Proposed Regulations:

   a. Provide that interest expense is deductible *only if*, among other things, the loan's terms are actually and necessarily incurred in the administration of the decedent's estate and are essential to the proper settlement of the decedent's estate.

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b. Provide a nonexclusive list of factors to consider in determining whether interest expense payable pursuant to such a loan obligation of an estate satisfies the applicable requirements, e.g.:

i. Whether the loan obligation is entered into by the executor with a lender who isn't a substantial beneficiary of the decedent's estate (or an entity controlled by such a beneficiary) at a time when there's no available alternative to obtain the necessary liquid funds to satisfy estate obligations.

ii. If the loan obligation carried an extended loan term with a single balloon payment that doesn't correspond with the estate's ability to satisfy the loan.

c. In those cases, the interest accruing on the loan isn't necessarily incurred in the administration of the estate and therefore isn't deductible.

F. Substantiating Value of Claims Against Estate.

1. The proposed regulations revisit the "qualified appraiser" and "qualified appraisal" requirements in the context of valuing claims against an estate.

2. The proposed regulations require a written appraisal that adequately reflects the current value of the claim when the Form 706 estate tax return is being completed.

3. The current value of the claim should take into account post-death events occurring prior to the time a deduction is claimed, as well as those events reasonably anticipated to occur.

G. Claims Based on Decedent's Personal Guarantee.

1. Under the Proposed Regulations, claims based on a decedent's personal guarantee of another's debt must be:

   a. Bona fide, and

   b. In exchange for adequate and full consideration in money or money's worth (as opposed to gratuitous, even if enforceable under applicable state law).

2. In addition, the estate's right of contribution or reimbursement, if any, will reduce the amount deductible.

3. Test Provided Under the Proposed Regulations:

   a. A decedent's agreement to guarantee a bona fide debt of an entity in which the decedent had control (within the meaning of IRS Section 2701(b)(2)) at the time of the guarantee satisfies the requirement that the agreement be in exchange for adequate and full consideration in money or money's worth.

4. Alternative Test:

   a. If, at the time the guarantee is given, the maximum liability of the decedent under the guarantee didn't exceed the fair market value of the decedent's interest in the entity.

5. Potential Negative Inference:

   a. A decedent's personal guarantee in circumstances that fall outside these circumstances may not give rise to an estate tax deduction, even though the decedent may have had a substantial interest in the entity.

H. Intentionally Defective Grantor Trusts.

1. Background. (Revenue Ruling 2023-02)

a. Establishing an IDGT requires the grantor to settle an irrevocable trust in which the grantor retains certain powers that cause the trust to be treated as a grantor trust for income tax purposes.

b. A grantor trust is not treated as an entity separate from the grantor for income tax purposes and, therefore the trust's income is taxed to the grantor.

c. For estate and gift tax purposes, however, the trust is treated as an entity separate from the grantor.

2. Revenue Ruling 2023-02:

a. There is no basis step-up for assets in IDGT if the assets are not included in the grantor's gross estate upon his or her death.

I. Buy-Sell Agreements & Life Insurance. (*Connelly*, 8th Circuit Court of Appeals, June 2, 2023)

1. Facts:

a. Mike & Tom Connelly were sole shareholders.

b. Buy-sell agreement provided two ways of determining stock value:

i. Certificate of Agreed Value.

ii. Appraisal.

c. Neither were utilized.

d. Company maintained $3.5 million in life insurance, and when Mike died it paid $3 million to his estate.

2. Estate's arguments:

   a. The price paid for Mike's shares was determined pursuant to the buy-sell agreement.

   b. The liability to Mike under the buy-sell agreement offsets the proceeds from the policy.

3. Court:

   a. The price was not determined under the buy-sell agreement.

   b. It was simply the result of an agreement between Tom and Mike's estate.

4. The court's math:

   a. The IRS valued the company at $3.86 million.

   b. Mike and Tom collectively owned 500 shares.

   c. Thus, the per share value was $7,720.

   d. After paying off Mike's estate, the company was still worth $3.86 million, but since Tom owned 114.1 shares those shares were now worth $33,800 each.

5. That didn't make sense to the court, so it ruled that the life insurance is included in the value of the corporation for purposes of determining the value of a decedent's stock.

J. Beneficiaries & Trustee Liable for Estate Taxes. (*United States v. Paulson*, No. 21-55197 (9th Cir. May 17, 2023)

1. Defendants, who had received estate property, were within the categories of persons listed in IRC §6324(a) and thus are liable for the unpaid estate taxes as beneficiaries and trustees.

2. §6324(a)(2) imposes personal liability for unpaid estate taxes on the categories of persons listed in the statute who have or receive estate property, either on the date of the decedent's death or at any time thereafter, subject to the applicable statute of limitations.

K. Assignment of Income/Gift Substantiation. (*Estate of Scott M. Hoensheid, et al. v. Commissioner*, TC. Memo 2023-24).

1. Facts:

   a. Donor donated a portion of the donor's stock in his family business to a donor advised fund at Fidelity.

   b. Shortly after the donation, an unrelated third party purchased the shares in the Company, including Fidelity's shares.

   c. The donor claimed a charitable deduction for the appraisal value of the stock on his income tax return and did not report any capital gains on the sale of the stock.

2. Court:

   a. Upheld the IRS' denial of the charitable deduction for the contribution of the stock to the donor advised fund.

   b. Held that the donor must include the capital gain from the sale of the stock in his taxable income notwithstanding the fact that the sale occurred after the date of the gift.

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3. Reasoning:

   a. Communications between the donor, the Company, the purchaser, the donor's counsel, the appraiser, and Fidelity, made it clear that the Company would be sold to a specific buyer shortly after the donation.

   b. The sale of the Company had progressed to the point that the sale was already a "practical certainty" by the date of the gift.

   c. Thus, the donor must recognize the capital gain on the sale after the date of the gift as if the donor had sold the shares before donating the shares to Fidelity.

   d. In addition, the appraiser was not a qualified appraiser meeting the requirements set forth in Treas. Reg. §1.170A-13.

4. Takeaways:

   a. Be careful of violating the assignment of income doctrine by making gifts through a prearranged transaction where a sale of the gifted interest is sufficiently imminent and practically certain.

   b. Keep in mind that the circumstances and timing of a sale transaction can be examined on audit, and if, like in *Hoensheid*, the gift is completed at a time when the donor's right to income has already become practically certain, the donor can incur capital gains tax on the sale.

   c. Donors and their advisors must ensure compliance with the requirements for qualified appraisals and qualified appraisers.

L. Statute of Limitations on Gifts. (*Schlapfer v. Commissioner* (T.C. Memo 2023-65))

1. Background:

a. IRC §2501(a)(1) imposes a tax on the transfer of property by gift.

b. Individuals who make a gift and are subject to the gift tax are required to file a gift tax return for the year of such transfer under IRC §6019.

c. Under IRC §6501(a), (c), the Commissioner generally has three years from the filing of a gift tax return to assess gift tax.

d. Under Treas. Regs. §301.6501(c)-1(f)(5), this applies even if the gift disclosed is ultimately determined to be an incomplete transfer.

e. However, IRC §6501(c)(9) provides that gift tax may be assessed at any time when a reportable gift wasn't reported.

f. Treas. Regs. §301.6501(c)-1(f)(2) says that this exception applies unless the gift has otherwise been "reported in a manner adequate to apprise the Internal Revenue Service of the nature of the gift and the basis for the value so reported."

2. Adequate Disclosure:

a. Treas. Regs. §301.6501(c)-1(f)(2) (the Adequate Disclosure Regulation (ADR)) provides, in relevant part, that transfers reported on a gift tax return will be considered adequately disclosed if the return (or an attached statement) provides the following:

i. A description of the transferred property and any consideration;

ii. The identity of, and relationships between, transferor and transferee; and

iii. A detailed description of the method used to determine the fair market value of the gift.

b. The IRS argued that strict compliance with the ADR was required for a gift to be deemed adequately disclosed, and that only the Form 709 should be considered.

3. Court:

a. The court held that the limitations period began with the filing of the Form 709 for 2006 (in 2013) and concluded before the IRS issued the notice of deficiency to Schlapfer in 2019.

b. The court based its conclusions on following:

i. The entirety of the disclosure packet should be considered.

ii. Substantial compliance with the ADR was sufficient.

M. Levy on Trust Bank Account. (*Marshall F. Newman et al. v. United States et al.*, No. 1:20-cv-10632 (D. Mass. 2023))

1. Facts:

a. Albert Todesca owed the IRS income taxes and trust fund recovery penalties (TFRP).

b. In 2011 his dad created a trust which, at his death, called for the equal division of the trust for the benefit of his two sons, Albert and Paul.

c. Father passed away in 2017 and the IRS issued a bank levy thereafter to the bank holding a money market account and a checking account in the trust's name.

d. The trust directed the trustee to distribute "so much of the annual net income in such amount or amounts or principal as the said Albert M. Todesca may, from time to time, request, or, in the absence of such request, so much thereof as the Trustee in his sole discretion shall deem necessary for the maintenance, support and general welfare of said, Albert M. Todesca".

2. Court:

a. Concluded that the taxpayer's right to demand distributions was a property right to which the federal tax lien attached.

b. Pointed out that the taxpayer's interest in the trust's principal and interest had pecuniary value and that the spendthrift provision didn't immunize it from the federal tax lien.

VIII. **MICHIGAN**

A. Phase-Out of Retirement Tax.

1. Background:

a. Signed into law on March 7, 2023.

b. Phases out the state's "retirement tax" over four years.

c. Allows taxpayers to choose between the current limitations on the deductibility of retirement and pension income or the limitations specified in the new law.

TAX YEAR	RETIREE DATE OF BIRTH	PHASE-IN SUBTRACTION
2023	Jan. 1, 1946 – Dec. 31, 1958	Up to 25%
2024	Jan. 1, 1946 – Dec. 31, 1962	Up to 50%
2025	Jan. 1, 1946 – Dec. 31, 1966	Up to 75%
2026	N/A	Up to 100%

2. 2023 Tax Year.

a. Those born in 1945 or before: There is no change. You can still deduct the full amount of the allowable deduction. For the 2023 tax year, it is $61,518 for single returns and $123,036 for joint returns.

b. Those born between 1946-1952: You can choose between the maximum deduction of:

i. $20,000 for single returns and $40,000 for joint returns (the previous provisions of the Income Tax Act of 1967), or

ii. Up to 25% of the maximum amount of the allowable deduction for those born in 1945 or before, which for the 2023 tax year would equal a deduction of $15,379.50 for a single return and $30,759 for a joint return.

c. Those born between 1953-1958 who are 67 years of age or older: You can choose between the maximum deduction of:

i. $20,000 for single returns and $40,000 for joint returns (the previous provisions of the Income Tax Act of 1967), or

ii. Up to 25% of the maximum amount of the allowable deduction for those born in 1945 or before, which for the 2023 tax year equals $15,379.50 for a single return and $30,759 for a joint return.

d. Those born between 1953-1958 who are 66 years of age or younger: You are not eligible for a deduction under the Income Tax Act of 1967 but do qualify under Public Act (PA) 4 of 2023 to deduct up to 25% of the maximum amount of the allowable deduction for those born in 1945 or before, which for the 2023 tax year equals $15,379.50 for a single return and $30,759 for a joint return.

e. Those born in 1959 and after: You are not eligible for a deduction in the 2023 tax year.

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B. Flow-Through Entity Tax.

1. Background:

a. Allows owners of Flow-Through Entities (S-Corporations & Partnerships) the option to pay and deduct their state and local income taxes at the business-entity level instead of individually.

b. Mirrors the so-called State and Local Tax (SALT) cap workaround enacted by several other states and is designed to avoid the $10,000 federal limit on individual itemized deductions for state and local taxes.

2. Developments:

a. Because of the reduction in the personal income tax rate for tax year 2023, the FTE tax rate is likewise reduced to 4.05% for all flow-through entities with tax years beginning in 2023.

b. According to a notice issued on April 14, 2023, taxpayer must apply for an extension of time to file its annual flow-through entity tax return, even if the taxpayer was granted an extension on their federal return.

C. Reporting Adjustments from Partnership Level Audits.

1. L. 2022, S248 (P.A. 148) ("2022 Public Act 148") (see *State Tax Update*, 07/21/2022), created Chapter 18 within Part 3 of the Income Tax Act.

2. Generally, Chapter 18 requires final federal adjustments that arise from a partnership level audit or administrative adjustment request subject to the federal Bipartisan Budget Act (BBA) of 2015 to be reported and paid in one of two ways:

a. The partnership may report adjustments to members, who must then separately report and pay their share of the applicable Michigan income tax due (i.e., the "push out" method) or,

b. The partnership may elect to report and pay any applicable Michigan income tax on behalf of its members (i.e., the "pay up method").

3. Reporting Deadlines:

a. A 90-day deadline:

i. For partnerships that "push out" adjustments, to report to each direct partner their share of the adjustments and, if applicable, pay any Michigan income tax on behalf of direct partners previously included on a composite return; and

ii. For all partnerships to report certain preliminary information about the adjustments to the Department if it will be making the "pay up" election.

b. A 180-day deadline:

i. For direct members of a partnership under the "push out" method, to report their share of adjustments to the Department and to pay the Michigan income tax owed on those adjustments; and

ii. For a partnership that made the "pay up" election, to pay the collective Michigan income tax owed on those adjustments.

4. Effective date: (Notice Regarding the Implementation of 2022 Public Act 148, Mich. Dept. Treas., 08/26/2022)

a. Chapter 18 is generally applicable for the reporting of certain federal adjustments for tax years beginning on and after January 1, 2018.

b. Because PA 148 was also given retroactive effect, Chapter 18 also applies to federal adjustments that have a "final determination date" both prior to and after its date of enactment.

c. The 90-day and 180-day deadlines referenced above were treated as beginning on January 1, 2023, for any federal adjustment subject to Chapter 18 that had a "final determination date" prior to that date.

5. Annual Report: (Michigan Treasury Update, Mich. Dept. Treas., 09/02/2023)

a. The Michigan Federal Adjustments Report ("FAR") for Partnerships and Other Flow-Through Entities

b. the FAR for partnerships is an interactive Excel document that collects the necessary information about adjustments and partners and reports the partnership's tax due or refund.

c. It is expected that completed reports will be uploaded through Michigan Treasury Online (MTO) beginning in 2024.

6. Payments or Refund Claims:

a. Under the "Pay Up" method, tax, penalty, and interest due from partnerships are paid using MTO.

b. Under the "Push-Out" method, partnerships are responsible for paying or seeking a refund on behalf of all partners that participated in a composite return (Form 807) filed for the reviewed tax year.

c. These partnerships should use Partnership Audit Adjustments Payment Voucher (Form 5839) to make payments.

7. Reporting obligations of partners:

   a. Partners (or embers of another flow-through entity in a tiered structure) that receive pushed-out Michigan adjustments from their partnership or other flow-through entity will have reporting obligations to Treasury.

   b. In addition, partners will pay tax, penalty and interest to Treasury or make a refund request, whichever is applicable.

   c. Information about these pushed-out adjustments comes from the partnership; there is no associated Treasury form.

   d. Partners should then fulfill their obligations to Treasury under the procedures specific to the partner's income tax.

   e. For a partner subject to the Corporate Income Tax (CIT), the partner should file an amended CIT return (Form 4892) for the reviewed tax year and pay tax or request a refund as they would for any other CIT amended return.

   f. For a partner subject to the individual income tax – including individuals, trusts, and estates and excluding anyone who participated in a composite return for the reviewed tax year – tax, penalty, and interest due should be paid using a paper check and the Form 5839 voucher.

D. Apportioning Income from an Asset Sale. (*Vectren Infrastructure Services Corp. v. Department of Treasury*, Mich. S. Ct., Dkt. No. 163742, 07/31/2023)

1. Background:

    a. Sale of a Michigan business (Vectren) to a Minnesota company (ML) structured as an asset sale.

    b. Issue involved the apportionment of the sales proceeds.

2. Supreme Court:

    a. To calculate the sales factor ML's total sales in Michigan during the tax year must be compared to ML's total sales "everywhere" during the tax year.

    b. "Sales" is defined as "stock in trade," property that can be inventoried, and services sold.

    c. It does not include the sale of a company.

    d. Therefore, while the asset-sale income generated from the sale of ML to Vectren is "business income" and includable in the tax base, it is inappropriate to include the asset sale in either the sales-factor numerator or denominator.

IX. **CITY OF DETROIT.**

A. Telecommuting. (City Income taxes and Telecommuting FAQ, Mich. Dept. Treas., 12/01/2022)

1. If a taxpayer is a Detroit resident, all income earned by that taxpayer is subject to Detroit tax, no matter where it is earned.

2. Wages earned by a nonresident of Detroit, who is working from home (telecommuting) at a location outside of the city is not taxable by Detroit.

3. Any wages earned by a nonresident while working within the City of Detroit are taxable.

4. If a taxpayer is a nonresident of Detroit and earned income while both in the city and outside the city, all wages earned while working in the City of Detroit are taxable.

5. Nonresidents should file using the City of Detroit Nonresident Income Tax Return (Form 5119), and include the City of Detroit Withholding Tax Schedule (Form 5121), and complete part 3.

6. Nonresidents should keep a work log of the days worked outside the city to help allocate telecommuting wages to nontaxable income.

7. Employers should provide employees with a letter, on company letterhead, stating the dates that employees were directed to work from home.

8. The employees are not required to submit the work log and employer letter with a city income tax return, but taxpayers should still retain the documents and may be required to furnish the documents upon request by a city tax administrator.

9. The stimulus payment is not considered income and therefore not included in a taxpayer's federal Adjusted Gross Income (AGI) which is used to determine taxable income for the City Resident Income Tax Return (Form 5118).

10. It should also not be included when calculating taxable income on the City of Detroit Nonresident Income Tax Return (Form 5119) or the City of Detroit Part-Year Resident Income Tax Return (Form 5120).

B. Electronic Payments. (News release, Mich. Dept. Treas., 02/07/2023)

1. City of Detroit individual income taxpayers can now pay by eCheck or debit or credit card their estimated payments, annual return payments, proposed tax due payments, 10-day demand payments, assessment payments or audit payments.

2. Payment of city income taxes by eCheck or with a debit or credit card must be made by the due date of the payment.

3. The State's eCheck system does not accept payments for Detroit property taxes and other fines.

4. Those looking to pay property taxes can continue to do so in-person, by mail or online.

C. Withholding. (News & Events Digest: August 2023, Mich. Dept. Treas., 08/31/2023

1. State law requires that a withholding employer in any city where the Michigan Department of Treasury (Treasury) administers taxes must file a return and pay the tax withheld for each calendar month by the end of the 15th day of the following month.

2. Effective January 1, 2024, employers will be required to file and pay their City of Detroit withholding tax monthly.

3. State law also requires employers to file an annual City of Detroit Income Withholding Reconciliation (Form 5321) before February 28 of the immediately following calendar year.

4. City Withholding Tax forms and documents will be updated to reflect the new monthly filings. The forms will only be available online or through applicable software vendors. Paper forms and booklets will no longer be printed and mailed to employers.

5. Treasury is working to implement an electronic payment system that will accept debit and credit cards or Automated Clearing House (ACH) or Electronic Fund Transfer (EFT) payments.

6. Debit and credit card payments will have a service fee, while ACH or EFT payments will not. Taxpayers interested in using a fee-free EFT payment method must submit a City of Detroit Electronic Funds Transfer Debit Applications, Account Update (Form 5473), which will be available by December 31, 2023.