33rd Annual

Tax Symposium

FALL 2024 ROUNDUP OF RECENT TAX DEVELOPMENTS

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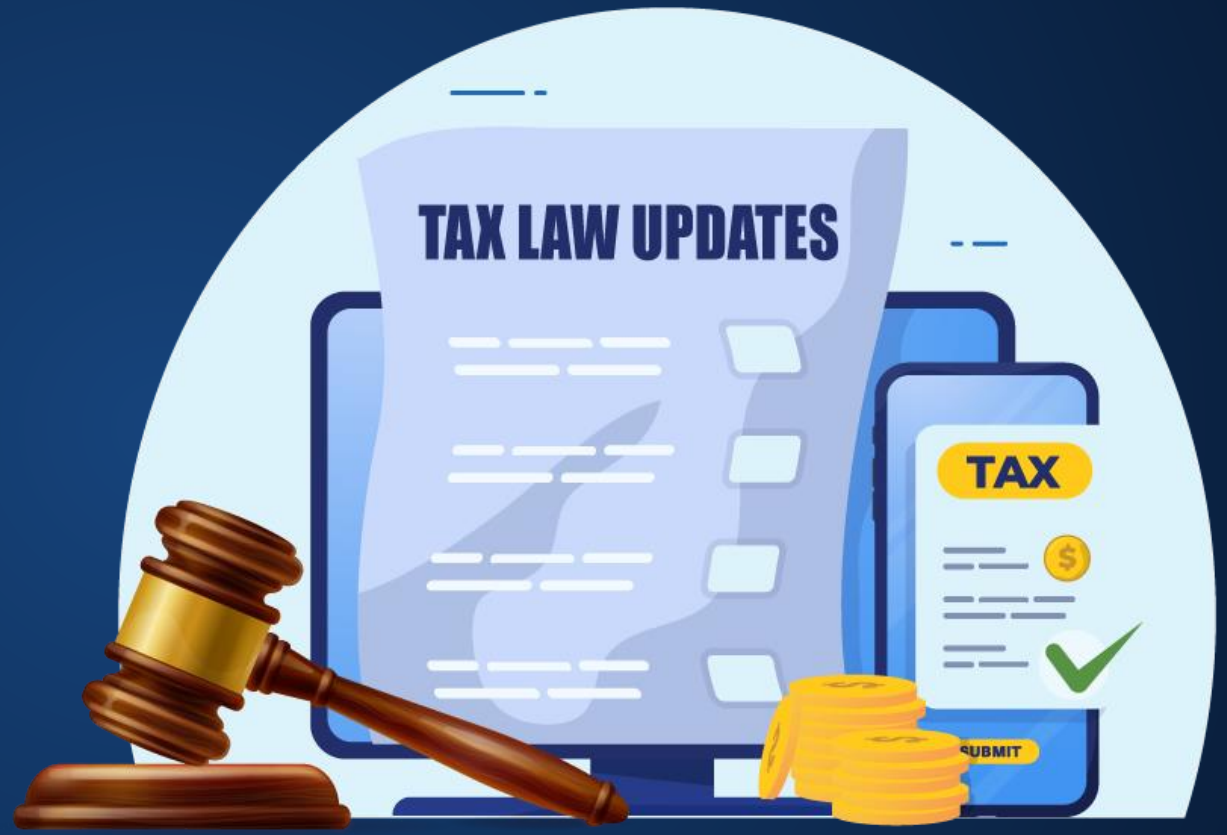
ROUNDUP OF RECENT TAX DEVELOPMENTS

- Individuals
- Business
- Inflation Reduction Act
- Retirement
- Estate Planning



INDIVIDUALS

IRS WIPES AWAY $1 BILLION IN PENALTIES

IRS announced December 19, 2023:

- $1 billion in automatic penalty relief to about 4.7 million taxpayers and businesses whose tax year 2020 and 2021 tax returns were affected by pandemic disruptions in notifications
- Although the IRS had paused much of its automated collection activity, failure-to-pay penalties continued to accrue over the past 22 months
- Taxpayers who already paid failure-to-pay penalties will also automatically be given a refund, or, if applicable, have that amount applied as a credit toward another existing tax liability

IRS WIPES AWAY $1 BILLION IN PENALTIES

IRS sent letters (LT38, *Reminder, Notice Resumption)* to affected taxpayers to:

- Remind taxpayers of their outstanding tax liability
- Inform them of the penalty relief
- Present different options for paying tax liabilities

IRS WIPES AWAY $1 BILLION IN PENALTIES

Caveats:

- Failure-to-pay penalties for relevant taxpayers resumed on April 1, 2024
- The relief is capped at taxpayers who were assessed less than $100,000 in tax

NEW INITIATIVES

IR-2024-46:

- IRS announced plans to begin dozens of audits on business aircraft involving personal use

IR-2024-56:

- New effort focused on high-income taxpayers who failed to file federal income tax returns
- More than 125,000 instances since 2017 identified

PREMIUM TAX CREDIT

IR-2024-54

Form 8962, Premium Tax Credit:

- Required to reconcile advance payments of the Premium Tax Credit

IRS Reminder:

- Electronically filed tax returns will be rejected if a Form 8962 is required, but the Form 8962 is not completed in the software and filed with the return
- To correct, must refile the complete return with the Form 8962 and attach a written explanation for its absence
- Previously, the IRS would correspond with the taxpayer instead of rejecting the electronically filed return

MEDICAL EXPENSES

IR-2024-65

- Reminder that personal expenses for general health and wellness are not deductible as medical expenses
- They are also not reimbursable from FSAs, HSAs, HRAs or MSAs
- Getting a note from a doctor does not make a wellness expense deductible

Example:

- Advertisement stating that pre-tax dollars from an FSA can be used to purchase health food sold by the company to control blood sugar
- Company, for a fee, will provide a “doctor’s note” that can be submitted to the FSA

DIGITAL ASSETS

Form 1099-DA, *Digital Asset Proceeds from Broker Transactions*

- Draft version of this new form released by IRS
- Intended for 2025 tax year
- Beginning in 2025, brokers are required to report proceeds digital asset sales
- Basis is also required to be reported, but brokers can check box 10a if it is unknown, or the digital assets were acquired prior to 1/1/2023 or sold prior to 1/1/2026
- Taxpayers may be required to recognize gain

DIRECT-FILE PROGRAM

IR-2024-151, May 30, 2024

- IRS has announced that it will make Direct File a permanent option starting with the 2025 tax season
- Inviting all states to partner with Direct File next year
- Based on survey data:
  - Taxpayers liked using Direct File
  - Direct File made filing easier
  - Direct File served as a catalyst for the IRS' digital transformation
  - Provided IRS with an opportunity to test customer service innovations on a larger scale

FREE FILE PROGRAM

IR-2024-145

- “Free File” is a partnership between the IRS and eight tax preparation software companies providing free online tax preparation and filing software on IRS.gov
- IRS has extended Free File through 2029
- This was its 22nd filing season
- Usage increased this year from 2.7 million tax returns to 2.9 million

CASES

WORKERS' COMPENSATION OFFSET

Ecret, T.C. Memo. 2024-23

Background:

- Workers' compensation is excludable under Section 104(a)(1)
- Up to 85% of Social Security is taxable under Section 86
- 42 U.S.C. Sec. 424a(a) limits combined workers' compensation and Social Security benefits to 80% of Average Current Earnings ("ACE")
- Under Section 86(d)(3), if a taxpayer's Social Security benefits are reduced by reason of the receipt of workers' compensation benefits, the term "Social Security benefit" includes the portion of the workers' compensation benefit equal to the amount of the reduction

WORKERS' COMPENSATION OFFSET

Facts:

- Taxpayer received $42,000 in workers' compensation
- Her ACE for the year was $48,708
- She was entitled to $19,866 in Social Security, but received only $6,120 due to the workers' compensation offset
- She argued that she should only be taxed on the Social Security

Result:

- Court disagreed holding that she was required to treat a portion of her otherwise excludable workers' compensation as taxable Social Security benefits

GAMBLING LOSS ALLOWED

Tolstov, T.C. Summary 2024-19

Cohan Rule (*Cohan v. Commr.*, 39 F.2d 540 (2d Cir. 1930)):

- Court should estimate deductions if taxpayer:
  - Demonstrates expense actually incurred
  - But, unable to substantiate amount
  - Provided that court has some reasonable evidentiary basis on which to base an estimate

GAMBLING LOSS ALLOWED

Facts:

- Compulsive slot machine gambler
- No log of gambling activities as required by Rev. Proc. 77-29
- Statement from casino showed “coin in” of $105,063
- Reported $61,929 of gambling winnings per Form W-2G received from casino
- Claimed $61,929 of gambling losses

GAMBLING LOSS ALLOWED

Court:

- Allowed $61,929 of gambling losses

Reasoning:

- Taxpayer exhausted $40,000 of equity in home
- Taxpayer had few other assets and no accessions to wealth
- “Virtual certainty” that taxpayer placed many losing bets
- Satisfied that taxpayer attempted in good faith to obtain substantiation from third parties

BUSINESS

NEW FORM 7217 FOR PARTNERSHIP DISTRIBUTIONS

Form 7217, Partner's Report of Property Distributed by a Partnership (IRC 732)

Background:

- Current distribution:
  - Does not completely retire a partner's interest in the partnership
  - Can reduce either the partner's capital account or partnership interest
  - Gain not recognized unless money is distributed
  - Gain recognized only if money distributed exceeds partner's adjusted basis in the partnership
  - Partner's basis in property received is same as partnership's adjusted basis in the property
  - Property's basis is limited to the partner's basis in the partnership reduced by any money received in the distribution

NEW FORM 7217 FOR PARTNERSHIP DISTRIBUTIONS

- Liquidating distribution:
  - Retires a partner's interest in the partnership
  - Includes a series of payments made as part of a liquidation
  - Gain recognized to the extent money distributed exceeds the partner's adjusted basis in his or her partnership interest
  - Loss recognized if cash, unrealized receivables or inventory received is less than the partner's adjusted basis
  - Cannot recognize a loss if any other property is received

NEW FORM 7217 FOR PARTNERSHIP DISTRIBUTIONS

Form 7217:

- Beginning for tax year 2024
- Must be filed by any partner receiving a distribution of property from a partnership in a liquidating or nonliquidating distribution in order to report the basis of the distributed property, including an adjustment required by IRC 732(a)(2) or (b)
- Must be filed regardless of whether there is an adjustment as a result of the distribution
- Not filed if only money or marketable securities treated as money is distributed
- Not filed to report a guaranteed payment under IRC 707
- Must be attached to the partner's tax return for the year the property is actually (not constructively) received

LIMITED PARTNER EXCEPTION TO SELF-EMPLOYMENT TAX

Soroban Capital Partners LP v. Commissioner, Docket Nos. 16217-22 and 16218-22

- On November 28, 2023, the U.S. Tax Court issued its opinion
- Held that a "functional analysis test" must be applied in determining whether the limited partner exception to the imposition of SECA tax under section 1402(a)(13) applies to limited partners
- Thus, a limited a partner in a limited partnership is not per se excluded from SECA tax

LIMITED PARTNER EXCEPTION TO SELF-EMPLOYMENT TAX

Soroban Capital Partners LP v. Commissioner, Docket Nos. 16217-22 and 16218-22 – Cont.

The IRS has asserted the following:

- The test is whether the Principals functioned like passive investors, not how their income stream was formalistically bifurcated
- The Principals functioned in the manner of self-employed persons, and receiving some of their income as guaranteed payments does not change that

INFORMATION RETURNS: SAFE HARBOR CORRECTION

TD 9984, December 19, 2023

IRC 6721 – Penalty for failure to file correct information return

- $250 for each return
- $100 if corrected by August 1st of the year
- $50 if corrected within 30 days after the required filing date
- Maximum penalty $3,000,000

INFORMATION RETURNS: SAFE HARBOR CORRECTION

Final Regulations – De Minimis Error Safe Harbor

- Number of returns limited to greater of 10 or ½ of 1%
- Considered de minimis if error is not more than $100 per statement
- In the case of tax withheld, the error can't be more than $25 per statement
- Applies only to information return accuracy penalties, and does not affect the requirement to pay and report all employment taxes

Exception:

- Person receiving the statement may elect out of the safe harbor and choose instead to receive a corrected statement
- Must elect out no later than 30 days after date statement is required to be provided or October 15th

FORM 8300, *REPORT OF CASH PAYMENTS OVER $10,000*

IR-2023-157:

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

Exceptions:

- Fewer than 10 information returns for the calendar year
- Can request a waiver for hardship by filing Form 8508, but the waiver applies to all information returns

BUSINESS TAX ACCOUNT

FS-2024-27, August 19, 2024

- Launched by IRS last fall with funding from the Inflation Reduction Act
- Goal:
  - ❑ Check tax history
  - ❑ Make payments
  - ❑ View notices
  - ❑ Authorize powers of attorney
  - ❑ Conduct other business with the IRS

BUSINESS TAX ACCOUNT

Who can use:

- Sole proprietor with an EIN
- Individual partner or shareholder with both:
  - Social Security number or individual tax i.d. (ITIN)
  - Schedule K-1
    - 2012-2023 for partners
    - 2006-2023 for shareholders

BUSINESS TAX ACCOUNT

Access coming to:

- LLC reporting business income on a Schedule C
- C and S corporations
- Partnerships
- Tax-exempt organizations
- Government agencies

MULTI-FACTOR AUTHENTICATION

IR-2024-201

- IRS reminder that multi-factor authentication (MFA) is now a federal requirement for tax professionals
- Requirement arises under Federal Trade Commission rules intended to protect client's sensitive information
- Must have:
  - Username
  - MFA
- Examples:
  - Token or random number sequence sent to cellphone
  - Fingerprint or facial scan

SECURITY PLAN

- Tax professionals are also required to have a written security plan (“WISP”)
- Required under the Gramm-Leach-Bliley Act
- IRS has published a sample template
- See, IRS Publication 5708 (Revised August 2024), *Creating a Written Information Security Plan for your Tax & Accounting Practice*

CASES

TAXATION OF UNREALIZED INCOME

Moore v. United States, U.S. Supreme Court Docket #22-800

Issue:

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

Background:

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

TAXATION OF UNREALIZED INCOME

Taxpayer's Argument:

- IRC §965 is an unapportioned direct tax that is not an income tax, thus violating the apportionment clause in the U.S. Constitution
- Essentially, the argument is that a tax on unrealized income is unconstitutional

Government's Argument:

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

TAXATION OF UNREALIZED INCOME

Ramifications:

- Subpart F
- Tax on global intangible low-taxed income (GILTI)
- New book minimum tax
- Mark-to-market for securities dealers
- Constructive sales, such as equity swaps
- Taxation of derivatives

Revenue Effects:

- If GILTI is struck down, perhaps $350 billion over the next 10 years
- Another $75 billion over the same period of Subpart F is repealed

Supreme Court's Decision:

- The mandatory repatriation tax does not exceed Congress' constitutional authority
- Article I of the Constitution authorizes direct taxes on persons and property, and indirect taxes on activities and transactions
- While direct taxes must be apportioned among the states according to population, indirect taxes only need to be "uniform throughout the United States"
- The holding is narrow and limited to pass-through entities
- It does not attempt to address whether realization is a constitutional requirement for an income tax

POWER OF FEDERAL AGENCIES

Loper Bright Enterprises v. Raimondo, 144 S. Ct. 2244 (2024)

Background:

- Magnuson-Stevens Act requires fisheries operating within 200 nautical miles off the U.S. coast to allow federal observers onboard its vessels to collect data for preventing overfishing
- The National Marine Fisheries Service adopted a rule requiring the fishing industry to pay the salaries of the observers
- A group of fisheries from New England are challenging the National Marine Fisheries Service's interpretation of the Magnuson-Stevens Act
- The Supreme Court previously ruled in *Chevron U.S.A., Inc. v. Natural Resources Defense Council*, Inc., 467 U.S. 837 (1984), that courts must defer to the authority of an administrative agency's interpretation of a statute whenever both the intent of Congress was ambiguous and the agency's interpretation is reasonable or permissible
- Lower courts upheld the agency action based on *Chevron*

POWER OF FEDERAL AGENCIES

Supreme Court Holding:

- Administrative Procedure Act requires courts to exercise their independent judgment in deciding whether an agency has acted within its statutory authority, and courts may not defer to an agency interpretation of the law simply because a statute is ambiguous
- Overrules *Chevron*
- Potentially wide-ranging consequences

DEADLINE TO SUE FOR HARM CAUSED BY AN AGENCY

Corner Post, Inc. v. Board of Governors of the Federal Reserve System, 603 U.S. ___ (2024)

Issue:

- Whether a challenge to the validity of a rule must be brought within six years of the rule's issuance—or instead within six years of when the rule first injures the particular plaintiff challenging the rule

Holding:

- The statute of limitations does not start running until the particular plaintiff has been harmed by the agency action

COST OF GOODS SOLD

Villa, T.C. Memo. 2023-15

Issue:

- To what extent must gross receipts be reduced by cost of goods sold?

Facts:

- Taxpayer built fences as a contractor
- Only included income reported to him on a 1099-MISC
- Used cash withdrawals for business and personal expenses
- Wanted to apply the ratio between COGS and gross receipts on a recent job to determine the COGS on his unreported income

COST OF GOODS SOLD

Law:

- While deductions from gross income (e.g., for ordinary and necessary business expenses) are a matter of legislative grace, the reduction of gross receipts by the cost of goods sold is mandatory under the Sixteenth Amendment (*Doyle v. Mitchell Bros*., 247 U.S. 179 (1918); Reg. 1.61-3(a))
- The "Cohan Rule" allows courts to estimate deductible expenses if there is a reasonable basis (*Cohan v. Commr*., 39 F.2d 540 (2d Cir. 1930))
- But, the court "bears heavily if it chooses upon the taxpayer whose inexactitude is of his own making"
- The rule doesn't apply to the strict substantiation requirements of Section 274(d), such as expenses for transportaton, lodging and meals
- The Tax Court has extended the rule to COGS

COST OF GOODS SOLD

Result:

- The court found the taxpayer's testimony credible regarding his other recent job
- However, that ratio doesn't apply to determining the portion of cash withdrawals used for personal expenses
- Moreover, some of the estimated COGS might have been included in the labor and expenses already allowed by the IRS
- As a result, the court only allowed 50% of the cash withdrawals as COGS

EMPLOYMENT TAXES

Taylor, T.C. Memo. 2024-33

Issue:

- Are poor math skills an excuse for failing to pay employment taxes?

Facts:

- Taxpayer was the CEO and sole shareholder of the company
- Delegated many business and financial responsibilities
- One such person, the company's CPA, embezzled $1-2 million

EMPLOYMENT TAXES

Law:

- Section 6672(a) provides that anyone who is required to collect and pay over any federal tax and who willfully fails to do so is liable for a penalty equal to the amount of the tax

Result:

- CEO liable
- According to the court, the issue is the taxpayer's authority to control the company's obligation to pay its employment taxes, not whether the CEO personally took responsibility
- Didn't help that the CEO used amounts recovered from an insurance company and a bank to pay personal expenses and a bonus, instead of the employment taxes

SHOEBOX OF RECEIPTS DOES NOT A DEDUCTION MAKE

Wright, T.C. Summary Opinion 2024-9, June 10, 2024

Background:

- Taxpayer owned an S corporation and several Schedule C businesses
- Challenged an audit in which the IRS allowed some deductions and disallowed others
- Taxpayer provided the court:
  - 44 exhibits containing 1,882 pages
  - Included copies of thousands of bills, receipts, etc.
  - Some contained adding machine tapes which didn't always add up
  - Separate deductions were taken in some cases for both the restaurant receipt and the credit card invoice

SHOEBOX OF RECEIPTS DOES NOT A DEDUCTION MAKE

Result:

- The court said it would not undertake the task of sorting through thousands of exhibits in an attempt to see whether the taxpayer providing adequate substantiation to counter the IRS' adjustments
- Court likened the taxpayer's approach to the "shoebox" method of attaching photocopies of receipts to numerous adding machine tapes without making any effort to link the items to a deductible trade or business expense that is in dispute

SUBSTANTIATING DEDUCTIONS

Patricia Marcello Anderson et al. v. Commissioner; T.C. Memo. 2024-95

Issue:

- Can accounting records (cash disbursements journals and account registers) be used to substantiate reported business expenses where evidence of actual payment is too voluminous to produce?

Facts:

- Taxpayers were self-employed, engaged in company management, commercial real estate, and the medical industry
- Failed to file returns for several years, so the IRS prepared substitute returns
- Taxpayer provided accounting records to evidence deductions, because the boxes containing the records of actual payment were claimed to be too voluminous to produce or tied up in other litigation

Result: Court disallowed the deductions

- Treating profit and loss statements without source documents is argument — not evidence
  - *See, e.g.*, *Barrios v. Commissioner*, T.C. Memo. 2023-32
- Because proper record keeping was feasible and, apparently, proper records were maintained, Court declined to exercise its authority under the *Cohan* doctrine, to estimate the taxpayer's expenditures.
  - *See Vanicek v. Commissioner*, 85 T.C. 731, 742-43 (1985) (citing *Cohan v. Commissioner*, 39 F.2d 540 (2d Cir. 1930))

SECOND CLASS OF STOCK

Maggard, T.C. Memo 2024-77

Facts:

- Taxpayer, an inventor, formed an S corporation with an investor
- Taxpayer owned 40% and the investor 60%
- The investor later sold 40% of his interest to one person, and 20% to another
- Those two persons began misappropriating funds by inflating their expense reimbursements and taking disproportionate distributions from the company's earnings
- Taxpayer sued for embezzlement claiming over $1 million in damages
- The case eventually settled

SECOND CLASS OF STOCK

Tax Court:

- Taxpayer filed a tax court petition claiming the unequal distributions had created a second class of stock revoking the S election

Result:

- The disproportionate distributions did not create a second class of stock
- Under the regulations, you look at the shareholders' rights under the corporation's governing documents, not what the shareholders actually do
- Taxpayer must include in income a proportionate share of the corporation's earnings despite the disproportionate distributions made to the two other shareholders

INFLATION REDUCTION ACT

New Consumer Clean Vehicle Credit (IRC §30D)

- 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
- Maximum of $80,000 per vehicle for vans, SUVs and pickups and $55,000 for other vehicles
- Income eligibility limit of $150,000 or $300,000 for joint filers
- Eliminates the previous manufacturer quota, which phased out the tax credit for manufacturers as they neared 200,000 clean vehicles sold

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

- Tax credit for the purchase of previously owned clean non-commercial vehicles, including electric vehicles and plug-in hybrids
- Credit is equal to the lesser of $4,000 or 30% of the vehicle cost
- Sets a maximum sale price of $25,000
- Model must be at least 2 years older than the year of sale
- Implements an income eligibility limit of $75,000 or $150,000 for joint filers

FINAL ELECTRIC VEHICLE REGULATIONS

IR-2024-131

May 6, 2024:

- Final regulations issued on tax credits under Section 30D for new clean vehicles and under Section 25E for previously owned clean vehicles
  - Includes rules for taxpayers transferring new or previously owned clean vehicle credits to dealers eligible to receive advance payments
  - Process for dealers to become eligible to receive advance payments
  - Rules for manufacturers to determine whether battery components and critical minerals are "foreign entity of concern" compliant

June 8, 2024:

- Rev. Proc. 2024-26, issued updating and expanding procedures for qualified manufacturer and seller reporting

TRANSFERABILITY OF OTHER CREDITS

IRC 6418; TD 9992, 4/30/2024

Background:

- For tax years beginning after December 31, 2022, taxpayers may elect under IRC 6418 to transfer eligible tax credits to an unrelated third party
- Under the election:
  - The transferee gets the credit
  - The amount received by the transferor is excludable from gross income
  - The election is made at the partnership or S corporation level
- Investors and developers are structuring and negotiating transactions to transfer energy tax credits

TRANSFERABILITY OF OTHER CREDITS

Eleven credits eligible:

- Credits for alternative fuel vehicle refueling property (Section 30C)
- Renewable electricity production credit (Section 45)
- Credit for carbon dioxide sequestration (Section 45Q)
- Zero-emission nuclear power production credit (Section 45U)
- Clean hydrogen production credit (Section 45V)
- Advanced manufacturing production credit (Section 45X)
- Clean energy production credit (Section 45Y)
- Clean fuel production credit (Section 45Z)
- Energy investment tax credit (Section 48)
- Qualifying advanced energy project credit (Section 48C)
- Clean electricity investment credit (Section 48E)

TRANSFERABILITY OF OTHER CREDITS

Final Regulations:

- Election must be made on an original (i.e., not amended) return filed by the due date, including extensions
- Once made, cannot be revoked
- IRS online pre-filing registration process required to get a registration number for the eligible credit property
- Recapture may apply if the qualifying energy asset is disposed of, sold, or ceases operations within the first five years after being placed in service
- A transferee claiming more credits than are allowable may be liable for a tax equal to the excess, plus 20%

CLEAN ENERGY TAX CREDIT SCAM

IR-2024-182

- IRS warned taxpayers on July 10, 2024, about falling victim to a new emerging scam involving buying clean energy tax credits
- Unscrupulous tax return preparers are targeting individual 1040 filers and having them improperly claim energy credits that offset income from other sources like wages, Social Security and retirement withdrawals
- Individuals purchasing tax credits are subject to the passive activity loss rules
- Thus, they can generally only use the purchased credits to offset income from a passive activity

RETIREMENT

OVERPAYMENTS FROM RETIREMENT PLANS

Notice 2024-77 (October 15, 2024)

Background:

- "Inadvertent benefit overpayment":
  - Exceeds amount allowed under the plan; or
  - Is made before allowed under the terms of the plan
- Does not include payments to disqualified persons
- SECURE 2.0 provides that inadvertent benefit overpayments will not cause a plan to lose its tax-qualification or fail ERISA
- Overpayment is treated as an eligible rollover distribution
- Plan must either seek recovery of the overpayment or reduce the individual's benefits

OVERPAYMENTS FROM RETIREMENT PLANS

Guidance:

- While a corrective payment generally is not required for an inadvertent benefit overpayment, other failures may occur as the result of an inadvertent benefit overpayment that could require a corrective payment – examples:
  - IRC Section 414(aa)(3) may require an employer to make a corrective payment to prevent or restore an impermissible forfeiture in accordance with IRC Section 411
  - If a failure under IRC Section 436 occurs due to an inadvertent benefit overpayment, the plan sponsor must make a corrective payment
- Rollovers
  - an individual who receives an inadvertent benefit overpayment and rolls over that overpayment pursuant to a direct or 60-day rollover will keep the tax-favored status of the overpayment for the portion of it for which a recoupment is not sought
  - The portion of an inadvertent benefit overpayment for which recoupment is sought that is not returned to the plan is not treated as an eligible rollover distribution

OVERPAYMENTS FROM RETIREMENT PLANS

Guidance – con't:

- Plan Amendments
  - A plan amendment to increase past benefit payments in a manner that results in a violation of IRC Section 401(a)(17) or 415 for a past year is not permitted.
  - However, an amendment to increase past benefits under IRC Section 414(aa)(1)(B) that results in a failure under IRC Section 436 for a past year is permitted if contributions are made in accordance with Rev. Proc. 2021-30 (i.e., EPCRS)
- A plan sponsor may self-correct an inadvertent benefit overpayment if certain requirements are met
- Bottom line: Employers do not have to make corrective contributions for overpayments in many situations that contributions were previously required

STUDENT LOAN PAYMENTS

Notice 2024-63

What:

- Employer match of a participant's qualified student loan payment (QSLP)
- 401(k) plans, 403(b) plans, SIMPLE IRA plans, government section 457(b) plans
- Not a plan contribution, although treated as a contribution for purposes of meeting the matching contribution rules

QSLP:

- Repayment of a qualified education loan incurred by the employee to pay qualified higher education expenses of the employee, spouse or dependents
- Doesn't exceed plan limitations when aggregated with other contributions
- Certified by the employee

CASES

SALE OF STOCK TO AN ESOP

Edward L. Berman et al. v. Commissioner, 163 T.C. No. 1 (July 16, 2024)

Issue:

- Whether gains from the sale of stock to an ESOP, deferred under IRC § 1042, can be recognized under the installment method after engaging in transactions that trigger gain recognition

Facts:

- In 2002, taxpayers sold stock to an ESOP and received promissory notes, thereby deferring the gains under IRC § 1042
- In 2003, they purchased Qualified Replacement Property (QRP) to defer recognition of the gains
- Later in 2003, they engaged in transactions using their QRP as collateral for loans, which were later deemed to be sales, requiring gain recognition under IRC § 1042(e)
- The IRS issued deficiency notices for 2003-2008, arguing the gains should be recognized in full for 2003
- Taxpayers argued for installment sale reporting under IRC § 453, claiming their gains should be recognized proportionally as payments were received

SALE OF STOCK TO AN ESOP

Result:

- Taxpayers made valid elections under IRC § 1042 to defer gains from the 2002 stock sales
- Gains recognized due to the 2003 sale of QRP are determined under the installment method as per IRC § 453
- The gains recognized in 2003 and 2004 are determined proportionally to the payments received in those years
- The IRS's position that § 1042(e) should exclusively determine gain recognition was rejected; the installment method applies unless affirmatively elected otherwise

ESTATE PLANNING

BASIS CONSISTENCY FINAL REGULATIONS

T.D. 9991 (September 17, 2024)

Consistent Basis Requirement under IRC 1014(f):

- Taxpayer's initial basis in property acquired from a decedent cannot exceed:
  - The property's final value for estate tax purposes; or
  - If no final value has been determined, then the basis is the property's reported value on the federal estate tax return or on Form 8971
- Requirement applies until the entire property is sold, exchanged, or otherwise disposed of in a recognition transaction for income tax purposes or the property becomes includible in another gross estate

BASIS CONSISTENCY FINAL REGULATIONS

Required Information Return:

- Form 8971
- Filed with IRS (and Schedule A with beneficiaries) on or before the earlier of:
  - 30 days after the due date of the estate tax return or
  - 30 days after the date on which the estate tax return is filed with the IRS
- If a beneficiary acquires property after the due date of the estate tax return, the Statement must be furnished to the beneficiary by January 31 of the year following the acquisition of that property
- Executors have a duty to supplement the Information Return or Statements upon the receipt, discovery, or acquisition of information that causes the information to be incorrect or incomplete

BASIS CONSISTENCY FINAL REGULATIONS

Penalties:

- May be imposed under:
  - Reg. §301.6721-1(h)(2)(xii) for filing an incorrect Information Return; and
  - Reg. §301.6722-1(e)(2)(xxxv) for filing incorrect Statements (i.e., Schedule A)
- In addition, an accuracy-related penalty can be imposed under Reg. §1.6662-9 on the portion of the underpayment of tax relating to property subject to the consistent basis requirement that is attributable to an inconsistent basis

BASIS CONSISTENCY FINAL REGULATIONS

Effective Date:

- Final Regs are effective for estate tax returns filed after September 17, 2024
- But, the basis consistency requirements in general apply to estate tax returns filed after July 31, 2015, which is the date Section 2004 of the Surface Transportation and Veterans Health Care Choice Improvement Act of 2015, Public Law 114-41, 129 Stat. 443, enacted sections 1014(f), 6035, 6662(b)(8), 6662(k), 6724(d)(1)(D), and 6724(d)(2)(II) of the Internal Revenue Code

CASES

TERMINATION OF QTIP RESULTS IN INADVERTENT GIFT

McDougall v. Commr., 163 T.C. No. 5 (Sept. 17, 2024)

Facts:

- Mrs. McDougall died in 2011
- Survived by husband and two children
- Estate plan directed majority of her estate to be held in a marital trust for her husband, for which a QTIP election was made
- On husband's death, remaining assets in marital trust would be distributed to children

TERMINATION OF QTIP RESULTS IN INADVERTENT GIFT

Facts – con't:

- Husband and two children executed a nonjudicial agreement to terminate the marital trust
  - As a result, the marital trust was distributed to husband
  - Husband then used those assets to make gifts to trusts for children's benefit
- Family filed gift tax returns taking the position that the gift of the remainder interest to the children was offset by the marital trust assets distributed to husband

TERMINATION OF QTIP RESULTS IN INADVERTENT GIFT

Tax Court:

- Under IRC 2519, the disposition of an income interest in a QTIP trust is treated as if the surviving spouse had made a deemed transfer of the entire remainder interest in the QTIP trust
- However, since husband retained all of the property in this case, there was no deemed transfer of the remainder interest in the QTIP trust
- On the other hand, since the children had a remainder interest prior to the termination of the QTIP trust, but not afterward, they made gratuitous transfers subject to gift tax

LAST MINUTE FLP DISREGARDED

Estate of Fields v. Comm'r (T.C. Memo. 2024-090)

Facts:

- Anne Fields inherited an oil business from her husband when he died in the 1960s and successfully managed it herself for years
- In 2011, she was diagnosed with Alzheimer's and shortly thereafter broke her hip and had multiple surgeries
- She had named her great nephew, Bryan, in whom she had great confidence, as executor of her estate and durable power of attorney
- In 2015, Bryan consulted an attorney pursuant to which he established two LLCs for Anne using his durable power of attorney naming himself as manager
- One LLC held cash, notes and collectible guitars, and the other held real estate
- Anne died one month later

LAST MINUTE FLP DISREGARDED

Tax Court:

- Anne didn't retain sufficient assets outside of the LLCs for her own support and the bequests under her will
- There was an implied agreement that the partnership would make distributions to Anne for her expenses and, after her death, to fulfill the bequests in her estate plan resulting in inclusion of the partnership assets in her estate pursuant to Section 2036(a)(1)
- She also retained the right to dissolve the partnership in conjunction with Bryan, giving her the right to designate the persons who would enjoy the property causing estate tax inclusion under Section 2036(2)

LAST MINUTE FLP DISREGARDED

Tax Court – con't.

- No evidence of any business purpose for the LLCs:
  - There was no change in her wealth or composition of the estate that would generate a non-tax reason for asset management
  - The assets transferred didn't require active management
  - The assets were all very different, with no obvious synergies from pooling them in a single entity
- The transfer of the assets to the LLC was not a bona fide sale for full consideration

LAST MINUTE FLP DISREGARDED

Tax Court – con't.

- Amount included in gross estate under Sections 2033, 2036 and 2043 determined using formula from Estate of Moore, T.C. Memo. 2020-40:

  1) Date-of-death value of consideration received from the transfer to the LLC that remained in Anne's estate (the LLC units), plus

  2) Date-of-death value of the LLC's assets included in her estate under Section 2036, less

  3) Value of the consideration received at the time of transfer to the LLC (the value of the LLC units received when the LLC was initially funded)

- #1 & 3 netted out in this case due to the absence of appreciation in the short period between when the LLC was formed and when Anne died

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Tax Symposium

THANK YOU

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