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IRS Reviews Individual Mandate, Exemptions And More For 2014 Tax Year Filing

◆ *Pub. 5187, Health Care Law: What's New for Individuals & Families*

As the filing season nears, the IRS has reminded taxpayers of the individual shared responsibility requirement under the *Patient Protection and Affordable Care Act* (PPACA). Individuals, unless exempt, must carry minimum essential health coverage or make a shared responsibility payment, applicable to tax years starting in 2014.

■ ***Take Away.*** "After having four years to implement the ACA, we are coming to the start of the filing season with many open questions about the law," Stephen Mankowski, CPA, Chair of the Tax Policy Committee and National Secretary for the National Conference of CPA Practitioners (NCCPAP), told Wolters Kluwer. "The greatest challenge for CPAs will be the exemptions to the individual shared responsibility requirement because they are so widespread," Mankowski predicted.

Minimum essential coverage

Minimum essential coverage is a health care plan or arrangement specifically identified in the PPACA as minimum essential coverage, the IRS explained. Employer-sponsored coverage under a group health plan (including self-insured plans) and individual market coverage, such as a qualified health plan purchased through the PPACA Marketplace, are treated as minimum essential coverage. Medicare, TRICARE and CHIP are generally treated as minimum essential coverage. Individuals who carry minimum essential coverage have been instructed by the IRS to check a box on their 2014 return.

■ ***Comment.*** Our organization has predicted problems with unscrupulous return preparers who will merely check the box for their clients, reporting coverage that the client actually does not have, Mankowski said.

Exemptions

Individuals may seek an exemption to the individual shared responsibility requirement. In some cases, exemptions are only available through the PPACA Marketplace. The IRS recommended that individuals make their requests to the Marketplace for an exemption as soon as possible. Other exemptions are claimed only on a tax return, and some exemptions may be obtained from the Marketplace or claimed on a return, the IRS explained.

An individual may qualify for an exemption if, among other reasons, household income is below the return filing threshold, the individual went without coverage for less than three consecutive months during the year, or the individual was a member of a health care sharing ministry. An individual may also seek an exemption based on hardship.

Payment

The IRS explained that for 2014, the individual shared responsibility payment is

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Route to: ____________ ____________ ____________ ____________ ____________

Tax Court Reversed; Foundation May Be Liable For Taxes As Transferee

◆ *Salus Mundi Foundation, CA-9, December 22, 2014*

Reversing the Tax Court, the Ninth Circuit Court of Appeals has found that a foundation may be liable for taxes under Code Sec. 6901 as the transferee of a transferee. The Ninth Circuit remanded the case to the Tax Court to determine whether the taxpayer actually was a transferee of a transferee, and whether the IRS satisfied the statute of limitations for assessing liability.

■ ***Take Away.*** The Ninth Circuit declined to recharacterize the transactions under federal law but still concluded that the transactions could be recast and collapsed under state law, because of the parties' constructive knowledge of the fraudulent tax avoidance scheme at the heart of the transaction.

Background

An individual set up a holding company that owned low-basis assets worth $319 million. Sale of the assets would have triggered tax liability of approximately $81 million. The holding company stock was transferred to a marital trust for the individual's wife. The wife wished to make cash gifts to her three children (by making gifts to their trusts).

To avoid the marital trust's tax liability from the sale of the assets, and to satisfy both seller and purchaser, the wife's advisors proposed an intermediary or Midco transaction, in which the marital trust (and a foundation also holding 1/3 of the stock) would sell stock for cash to a newly-formed intermediary, who would sell the assets (not the stock) to a purchaser. The marital trust would then make cash distributions to foundations benefitting the children. The intermediary would ordinarily be liable for taxes on the asset sale, but would claim sufficient tax losses to avoid the taxable gain.

Case history

The parties implemented a Midco transaction. The intermediary sold the assets and claimed offsetting losses. However, the Tax Court disallowed the losses as artificial, resulting from a Son-of-BOSS transaction.

The IRS attempted to collect taxes from the holding company, by recasting the stock sale as a sale of the company's assets, followed by a liquidating distribution to its shareholders (*Diebold, TC, 2010, CCH Dec. 58,374(M)*). Since the holding company no longer had any assets, the IRS attempted to collect from the shareholders as transferees under Code Sec. 6901.

The Tax Court, however, held that the shareholders lacked actual or constructive knowledge under state law of the tax avoidance scheme (*Salus Mundi, TC Memo. 2012-61, CCH Dec. 58,969(M)*). Since the shareholders were not liable as transferees, the children's foundations were not liable as transferees of a transferee. The IRS appealed.

Court's analysis

The application of transferee liability requires a two-prong test: is the party a transferee under federal tax law; and is the party substantively liable for the transferor's unpaid taxes under state law. The Ninth Circuit agreed with the taxpayer that the two prongs were separate; therefore, the IRS's recast of the transaction, to determine who is a transferee, does not apply to determine transferee liability under state law. However, the Second Circuit, in addressing the same facts, issues, and applicable law in a case involving another of the children's foundations, concluded that the holding company's shareholders had constructive knowledge of the tax avoidance scheme and were therefore liable under state law. The Second Circuit vacated the Tax Court's decision and remanded to the Tax Court the issues of the foundation's transferee status under federal law and the application of the statute of limitations.

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Affordable Care Act

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the greater of: one percent of household income that is above the tax return filing threshold for the individual's filing status; or the individual's flat dollar amount, which is $95 per adult and $47.50 per child, limited to a family maximum of $285, but capped at the cost of the national average premium for a bronze level health plan available through the Marketplace in 2014. For 2014, the annual national average premium for a bronze level health plan available through the Marketplace is $2,448 per individual ($204 per month per individual), but $12,240 for a family with five or more members ($1,020 per month for a family with five or more members).

Code Sec. 36B credit

Individuals who obtain health insurance coverage through the Marketplace may qualify for the Code Sec. 36B premium assistance tax credit. The IRS explained that to claim the credit, generally a taxpayer must have household income of at least 100 percent but not more than 400 percent of the Federal poverty line (FPL) for the family size, and cannot be claimed as a dependent.

Reference: TRC HEALTH: 3,000.

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Reference Key

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

IRS Issues Final Regs On PPACA Requirements For Tax-Exempt Hospitals, Including "CHNAs "/Financial Policies

◆ *TD 9708*

The IRS has issued final regs under Code Sec. 501(r) on the additional requirements for nonprofit hospitals to maintain their tax-exempt status under Code Sec. 501(c)(3). The regs address the requirements for hospitals to conduct a community health needs assessment (CHNA) every three years, to adopt an implementation strategy to meet these needs, and to adopt financial policies that benefit needy individuals.

■ ***Take Away.*** "The final regulations are well conceived and well written," Nancy Ortmeyer Kuhn, director, Jackson and Campbell, P.C., Washington, D.C., told Wolters Kluwer. "They follow the legislative intent and give hospitals the tools they need to objectively satisfy the CHNA and financial policy requirements. I was concerned that the regulations would include a lot of facts and circumstances tests that allow for subjective determinations by the IRS, but they didn't do that."

New requirements

The *Patient Protection and Affordable Care Act* (PPACA) imposed additional requirements on charitable hospitals to maintain their tax-exempt status. These requirements include conducting a CHNA; establishing and disclosing financial assistance policies (FAPs); limiting charges to needy individuals; and following reasonable billing and collection policies.

Effective dates

The CHNA requirement first applied to tax years beginning after March 23, 2012. The other requirements first applied to tax years beginning after March 23, 2010. The final regs generally will not take effect until the hospital's first tax year beginning after December 29, 2015. For tax years beginning on or before that date, a hospital may rely on a reasonable good faith interpretation of the statutory requirements. Complying with either the proposed regs or the final regs will satisfy the good faith requirement.

■ ***Comment.*** "The rules provide charitable hospitals with adequate time to fully update their policies and programming to implement the changes," McMahon said.

However, the regs on CHNA reporting violations and excise taxes, which merely clarified or confirmed requirements already in effect, apply December 29, 2014.

Financial assistance policies

One concern for hospitals was the requirement to adequately communicate their FAPs to patients. According to Treasury, the regs revise the notification requirements to protect patients while easing the burden on hospitals. General notifications must appear on bills and conspicuously in the hospital. However, individual notifications are only required when a hospital plans to use extraordinary collection actions such as reporting a debt to a credit bureau, selling the debt to a third party, or garnishing wages.

■ ***Comment.*** Kuhn expressed a concern that there are no minimum standards for financial assistance policies. "There is nothing in the statute or regulations," Kuhn said. "A hospital could provide a narrow standard. The requirements don't accomplish anything for middle-income people; hospitals can still bill at high rates and take aggressive financial collection actions. But you can't expect the IRS to draft regulations that are tougher than the statute."

Reporting and penalties

If a hospital fails to meet the consumer protection standards, the IRS could revoke

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Transferee

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In this case, the Ninth Circuit acceded to the Second Circuit's decision ("absent a strong reason to . . . create a direct conflict with other circuits"), and similarly remanded the case to the Tax Court to determine the same transferee and statute of limitations issues.

References: 2015-1 USTC ¶50,120; TRC IRS: 60,052.

IRS Extends Deadline For Withholding Entities To Apply Joint Account Options

In an email, the IRS announced that it has extended the deadline from June 30, 2014, to June 30, 2015 for qualified intermediaries (QIs), withholding foreign partnerships (WPs), and withholding foreign trusts (WTs) to apply the joint account option to a partnership or trust. The notification states that QIs, WPs, and WTs that have entered into an agreement with a partnership or trust to apply the joint account option may now continue to apply simplified joint account treatment until June 30, 2015.

Documentation. The email applies to entities that have entered into or that may apply to enter into the QI Agreement described in Rev. Proc. 2014-39, the WP Agreement described in Rev. Proc. 2014-47, or the WT Agreement also described in Rev. Proc. 2014-47. The email informs relevant withholding entities that the QI, WP and WT agreements are modified to allow the withholding entities to continue to document a joint account through June 30, 2015, consistent with the requirements in the prior QI, WP or WT agreements.

Withholding. The email also explained that a QI, WP or WT must withhold under Chapter 4 (FATCA) with respect to a partnership or trust if required (for example, if the withholding entity has actual knowledge that the partnership or trust is a nonparticipating foreign financial entity).

QI Joint Account Extension Email; TRC INTL: 33,054.25.

IRS Unveils Voluntary Closing Agreement Program For 501(c)(3) Bond Issuers Where Entity Loses Exempt Status

◆*Announcement 2015-02*

The IRS has unveiled a simplified process for issuers of qualified Code Sec. 501(c)(3) bonds to request a closing agreement where the borrower of the proceeds of the bonds had its exempt status revoked and then had it reinstated but not retroactively. Generally, bondholders will not be required to include interest on the bonds in gross income if they satisfy the simplified process.

■ ***Take Away.*** In Rev. Proc. 2011-36 the IRS provided procedures for reinstating the tax-exempt status of organizations that have had their tax-exempt status automatically revoked. A 501(c)(3) organization has its exempt status automatically revoked if it fails to file an annual return for three consecutive years.

Background

Under Code Sec. 145, interest on qualified Code Sec. 501(c)(3) bonds is generally exempt from tax. All the property financed with the net proceeds of the bonds must be owned by a 501(c)(3) organization or a state or local government entity, and the property financed with the net proceeds of the bonds must be used almost exclusively by 501(c)(3) organizations in their related trade or business or state or local government entities. If the 501(c)(3) organization fails to qualify as a tax-exempt organization while bonds are outstanding, the bonds fail to qualify under Code Sec. 145. A 501(c)(3) organization may seek retroactive reinstatement of its exempt status.

■ ***Comment.*** The IRS noted that often the effective date of a reinstated exemption will be the date that the organization's exemption application was submitted to the agency. However, organizations may choose to request that reinstatement be retroactive to the effective date of revocation.

Ann. 2015-02

The IRS explained that an issuer of may apply for a closing agreement under Ann. 2015-02 if certain requirements are satisfied: the 501(c)(3) has received prospective reinstatement of its exempt status; the organization's exempt status has not been previously revoked since the issue date of the bonds; and, the bonds are not under examination.

Issuers must request a closing agreement within 12 months of the date of the reinstatement letter, the IRS explained. If the reinstatement letter is dated before December 30, 2014, the issuer has 12 months from December 30, 2014 to submit a closing agreement, the IRS explained. The issuer also must pay the closing agreement amount for each bond issue covered by the closing agreement. A copy of the reinstatement letter also must be included with the request for a closing agreement.

References: FED ¶46,207;
TRC EXEMPT: 12,252.15.

IRS Wins Court Approval For John Doe Summonses In Offshore Investigation

The IRS has been authorized by a federal district court to serve John Doe summonses on eight entities in an investigation into a target that allegedly facilitated offshore tax evasion, the U.S. Department of Justice (DOJ) recently announced. DOJ reported that the entities were directed to produce records that will assist the IRS in identifying U.S. taxpayers who allegedly used the target's services.

Offshore entities. The IRS launched an investigation into the target. According to the government, some taxpayers allegedly had used the services of the target to establish, among other allegations, anonymous corporations and foundations in Panama as well as offshore entities. The taxpayers could allegedly control assets without appearing to own them.

■ ***Comment.*** "The IRS remains committed to continuing our priority efforts to stop offshore tax evasion wherever it is found," Commissioner John Koskinen said in a statement. "We have made tremendous progress in this area, working cooperatively with other agencies. The John Doe summons remains an important tool in our efforts to find international tax evaders and those who help them."

U.S. DOJ News Release, December 19, 2014.

Hospitals

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its tax-exempt status. If a hospital fails to properly conduct a CHNA and adopt an implementation strategy, a $50,000 excise tax will apply. If a hospital's failure is neither willful nor egregious, the hospital can correct and disclose the error. This will avoid revocation, but the excise tax will still apply to CHNA violations. The final regs also require that a hospital disclose its FAPs, its CHNA , and its implementation strategy for the CHNA.

■ ***Comment.*** "The CHNA and the FAP are both public documents," Kuhn said. "The information provided will assist the IRS and nonprofits involved in "policing" hospitals, to see if they are really charitable. Public involvement will help the IRS's enforcement efforts."

The regs impose an income tax on hospital organizations that operate more than one hospital facility with one of its facilities fails to satisfy Code Sec. 501(r). The overall organization would retain its tax-exempt status but would have to pay taxes on its income.

■ ***Comment.*** Kuhn said it is unusual for regs to impose a tax that is not in the statute.

References: FED ¶47,006;
TRC EXEMPT: 3,154.

IRS Releases 2015 Updates For Ruling Requests, Technical Advice, And No-Rule Procedures

◆ *Rev. Procs. 2015-1 through 2015-8*

The IRS has issued its annual revisions to the general procedures for ruling requests, technical advice memoranda (TAM), determination letters, and user fees, as well as areas on which the Associate Chief Counsel offices will not rule. The new and revised procedures are generally effective beginning January 2, 2015. Some updated user fees are effective February 2, 2015.

- ***Take Away.*** These procedures are updated annually by the IRS at the beginning of each calendar year. They are comprehensive and supersede the prior year's revenue procedures on these issues, including those announced throughout the past year.

Annual updates

The revenue procedures include the following guidance on:

- ***Rev. Proc. 2015-1:*** letter rulings, closing agreements, determination letters, information letters, and oral advice issued by the offices of the Associate Chief Counsel;
- ***Rev. Proc. 2015-2:*** technical advice issued by the offices of Associate Chief Counsel to a director or an appeals area director;
- ***Rev. Proc. 2015-3:*** areas for which the Associate Chief Counsel offices will not issue letter rulings or determination letters;
- ***Rev. Proc. 2015-4:*** general procedures for employee plans and exempt organizations letter rulings requests;
- ***Rev. Proc. 2015-5:*** procedures for applying for and for issuing determination letters on the exempt status under §501(c)(3) using Form 1023–EZ, Streamlined Application for Recognition of Exemption;
- ***Rev. Proc. 2015-6:*** determination letters on the qualified status of certain pension, profit-sharing, stock bonus, annuity and employee stock ownership plans (ESOPs) and on the status for exemption of any related trusts or custodial accounts under Code Sec. 501(a);
- ***Rev. Proc. 2015-7:*** subject areas on which the Associate Chief Counsel (International) will not issue advance letter rulings or determination letters without unique and compelling circumstances;
- ***Rev. Proc. 2015-8:*** user fees for advice on matters under the jurisdiction of the Commissioner, Tax Exempt and Government Entities Division.

Changes

Highlights among the changes that the IRS has made to its annual procedures include:

Rev. Proc. 2015-1. A new schedule of user fees is provided in Appendix A. The new user fee schedule is effective February 2, 2015.

Rev. Proc. 2015-2. The IRS updated Rev. Proc. 2015-2 to reflect that authority to issue TAMs on matters within the jurisdiction of the Commissioner, Tax Exempt and Government Entitles Division, has been delegated to Associate Chief Counsel.

Rev. Proc. 2015-3. The IRS revised its list of areas under the jurisdiction of the various offices of Associate Chief Counsel for which it will not issue advance letter rulings or determination letters. The IRS added a number of areas, including:

- Whether a plan is a governmental plan under Code Sec. 414(d);
- Whether a joint venture between a tax-exempt organization and a for-profit organization affects the organization's exempt status or results in unrelated business taxable income;
- Whether unrelated business taxable income tax issues arise when charitable lead trust assets are invested with charitable organizations; and
- Whether a compensation or property transaction satisfies the rebuttable presumption that the transaction is not an excess benefit transaction under Code Sec. 4958;

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IRS Reaffirms FATCA Requirement For Reporting Model 1 Foreign Financial Institution To Provide GIIN To Withholding Agent

The IRS, in a Q&A on its website, has reaffirmed the requirement under the *Foreign Account Tax Compliance Act* (FATCA) that a foreign financial institution (FFI) must provide a Global Intermediary Identification Number (GIIN) to a withholding agent for payments made on or after January 1, 2015. The withholding agent must have a withholding certificate that identifies the recipient of the payment (the payee) as a registered deemed-compliant FFI. Furthermore, the certificate must include a GIIN for the payee. These requirements must be met for the payee to avoid withholding on the payment.

Announcement 2014-38. The issue arose because Announcement 2014-38 allows a foreign jurisdiction to treat its intergovernmental agreement (IGA) with the U.S. as being in effect after December 31, 2014, even though the IGA is not yet in effect. Under a Model 1 IGA, an FFI may report account information to its own government. Since the IGA as treated as being in effect, the reporting Model I FFI must provide certain required information to the withholding agent, including the GIIN. A reporting Model I FFI that has not yet obtained a GIIN must inform its withholding agent that it has applied for the GIIN. This gives the withholding agent 90 days to verify the GIIN against the IRS list.

The IRS similarly affirmed that Announcement 2014-38 does not change the timing of any other due diligence or reporting requirements under FATCA.

FATCA General FAQs, IGA Registration Q&A-8 (December 22, 2014), www.irs.gov; TRC INTL: 36,052.

Tax Debts Not Discharged When Return Filed Late, Appeals Court Affirms

◆ *Mallo, CA-10, December 29, 2014*

The Tenth Circuit Court of Appeals has affirmed a federal district court decision that a debtor who obtained a general discharge in bankruptcy was not entitled to a discharge of tax liabilities where the debtor filed a late return. The Tenth Circuit, noting contrary decisions by some other courts, applied Bankruptcy Code (BC) §523(a)(1)(B), which provides an exception to discharge for a debtor's tax liabilities where a tax return was not filed.

■ ***Take Away.*** BC §523 provides that a "return" is a return that satisfies "the requirements of applicable nonbankruptcy law (including applicable filing requirements"). The appeals court held that under this definition, a return technically was not a "return" if it was filed late.

Background

A married couple did not file timely federal income tax returns for 2000 and 2001. The IRS issued deficiency notices. The taxpayers did not challenge the determinations, and the IRS assessed taxes for each year. In 2007, the taxpayers filed joint returns for each of the two years. Based on the returns the IRS adjusted the tax liabilities and assessments.

In 2010, the taxpayers filed for bankruptcy. The bankruptcy court issued a general order discharging their debts. The taxpayers then sought a determination that their tax debt was discharged, which the bankruptcy court denied. A federal district court affirmed the bankruptcy court decision.

Court's analysis

The Tenth Circuit first found that some courts have interpreted applicable nonbankruptcy law as treating a submission as a return where the return satisfies the four elements of the test in *Beard (CA-6, 1986)* (the return provides sufficient data to calculate tax liability; purports to be a return; is an honest and reasonable attempt to satisfy the tax law; and includes a penalties of perjury statement).

However, courts disagree whether a late return satisfies the third element requiring an "honest and reasonable" return. Some concluded that a late return that provides accurate information is helpful to the IRS. However, the Bankruptcy Code as amended requires that the return also satisfy "applicable filing requirements."

Based on the plain language of this phrase and on the requirements of the Tax Code, the Tenth Circuit concluded that the deadline for filing a return was part of the applicable filing requirements for a tax return. The court cited *In re McCoy (CA-5, 2012)* as agreeing with this conclusion.

■ ***Comment.*** The court rejected the taxpayers' argument that the Bankruptcy Code language was ambiguous and that filing late is not a requirement for a valid return. The court also rejected the IRS's analysis that once the IRS assesses the liability, the subsequent filing of a return is irrelevant, even though it agreed with the IRS's conclusion. The debt arose by operation of law; assessment was not relevant. If Congress had wanted a different result, it would have used different language, the court concluded.

References: 2015-1 USTC ¶(to be reported); TRC IRS: 57,150.

Rulings

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Rev. Proc. 2015-4. The IRS realigned the Tax Exempt and Government Entities Division (TE/GE) and the technical responsibility for issuing technical advice and letter rulings has shifted from EO Technical to the Office of Associate Chief Counsel (Tax Exempt and Government Entities). The IRS explained that EP Rulings and Agreements will continue to issue letter rulings only on certain matters specified in this Rev. Proc. 2015-4.

Rev. Proc. 2015-5. Rev. Proc. 2015-5 sets forth procedures for applying for and for issuing determination letters on the exempt status under Code Sec. 501(c)(3) of the Internal Revenue Code (Code) using Form 1023–EZ, Streamlined Application for Recognition of Exemption Under Section 501(c)(3) of the Internal Revenue Code. The IRS explained that it may merge the procedures under Code Sec. 2015-5 with the procedures for issuing determination letters on exempt status for organizations applying on Form 1023 in the 2016 annual update. Additionally, the IRS explained that general procedures for technical advice for matters within the jurisdiction of the Commissioner, Tax Exempt and Government Entities, are now handled by the Associate Chief Counsel (Tax Exempt and Government Entities).

Rev. Proc. 2015-6. The IRS made minor reference updates and clarifications, include reflecting changes related to the transfer of technical work from the Tax Exempt and Government Entities Division (TE/GE) to the Office of Associate Chief Counsel (Tax Exempt and Government Entities), adding a summary of the new procedures for processing incomplete applications, and clarifying the submission requirements for applications involving merged plans.

Rev. Proc. 2015-7. The IRS updated the areas in which ruling or determination letters will not ordinarily be issued include whether a taxpayer, withholding agent, or intermediary has properly applied the requirements of the *Foreign Account Tax Compliance Act* (FATCA) or of an applicable intergovernmental agreement to implement FATCA.

Rev. Proc. 2015-8. Rev. Proc. 2015-8 reflects changes related to the realignment of technical work from the Tax Exempt and Government Entities division to the Office of Associate Chief Counsel.

References: FED ¶¶46,209, 46,210, 46,211, 46,212, 46,213, 46,214, 46,215, 46,216; TRC IRS: 12,200.

Chief Counsel Applies Substance Over Form Doctrine To Forward Contract

◆ *CCA 201501012*

IRS Chief Counsel has determined that the agency may disregard the form of a purported forward contract. Chief Counsel explained that the loan could be disregarded as lacking genuine indebtedness. The IRS also could disregard the form of the forward contract.

■ ***Take Away.*** In applying the substance-over-form doctrine, the U.S. Supreme Court has looked to the objective economic realities of a transaction rather than to the particular form the parties employed, *Frank Lyon Co., 78-1* USTC *¶9370*. Where a transaction involves a purported loan that is offset by another element within the transaction, courts have addressed whether the loan is genuine indebtedness, or whether the form of the purported loan should be either disregarded or recast to reflect the objective economic realities of the transaction, Chief Counsel noted.

Background

Chief Counsel explained that the transaction consisted of two legs: a loan obligation and prepaid derivative contracts. The contracts would require the quarterly delivery of a specified bond, or its cash equivalent, in exchange for a predetermined price. The bonds, specified as LIBOR-based variable-rate certificates of deposit, would be subject to a protected minimum floor rate.

The promoter purchased both the loan and contract elements in Year 5 and Year 6, and marketed the transaction to individuals. An investor could sign a subscription agreement and become a limited partner. Alternatively, investors could invest in the transaction by owning a ratable share of the contract and assuming a ratable portion of the loan's liability.

Chief Counsel's analysis

Chief Counsel determined that the IRS could use the substance-over-form doctrine to recast the form of the transaction to disregard the loan and the portion of the contract that offset the loan. Here, Chief Counsel determined that the taxpayers never incurred genuine indebtedness for tax purposes. The loan and contracts were netted as bookkeeping entries with no cash actually being exchanged and no proceeds actually borrowed. The loan and the contracts were circular. There was no risk of default on the loan. Additionally, Chief Counsel determined that the loan and the contracts added needless complexity to a transaction that could have provided the parties with identical results in a cheaper and more straightforward fashion. Consequently, the taxpayers could not claim interest deductions on the loan.

Further, Chief Counsel determined that the form of the contracts, styled as forward contracts, should not be respected. A forward contract, Chief Counsel explained, is an executory contract calling for the delivery of property at a future date in exchange for a payment at that time. A forward contract does not result in a taxable event until the future sale referenced in the contract is actually executed. The contracts here failed to function as forward contracts.

Reference: TRC SALES: 48,056.

Proposed Amendment To Floor-Offset Arrangement Does Not Violate Rule Against Reducing Accrued Benefits

◆ *LTR 201501025*

The IRS has determined that a company was not hindered by the requirements of Rev. Rul. 76-259, which sets forth guidance for pension plan benefits that are offset by profit-sharing plan benefits ("floor-offset arrangements"), from amending its floor-offset arrangement to freeze accruals to affected plan participants. Neither did this proposed freeze amendment violate the requirements under Code Sec. 411(d)(6): The amendment did not retroactively reduce benefits that had been accrued as of the date of the plan amendment.

■ ***Take Away.*** Code Sec. 411(d)(6)(A) prohibits a qualified plan from decreasing the accrued benefit of a plan participant by an amendment of the plan (other than an amendment described in Code Sec. 412(d)(2) or section 4281 of the Employee Retirement Income Security Act of 1974).

Background

A company provided retirement benefits to certain employees under a "floor-offset arrangement" under which participants may receive a normal retirement benefit equal to (i) the participant's "gross" benefit under a pension plan payable at normal retirement age, less (ii) the annuity value of the participant's vested profit sharing plan balance, determined as of the participant's termination of employment converted to an actuarially equivalent annual annuity payable for the life of the participant commencing at the participant's normal retirement date.

The company sought a private letter ruling on whether its proposed amendment to freeze benefit accruals for certain participants under the pension plan and cease discretionary contributions for those participants under the profit sharing plan would violate Rev. Rul. 76-259 or Code Sec. 411(d)(6). The freeze transaction, the IRS determined, would not change the manner or time in which a participant's benefits would be calculated. It would only affect the amounts of the pension floor and profit sharing offset benefits beyond the freeze date.

■ ***Comment.*** Rev. Rul. 76-259 provides that a floor-offset arrangement

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Tax Briefs

Internal Revenue Service

An individual was not permitted to recover administrative costs. The United States' position was substantially justified because the IRS Appeals office conceded the case. When the IRS finally took a position with respect to the taxpayer's claim, it allowed the claim.

Milligan, TC, CCH Dec. 60,104(M), FED ¶47,910(M); TRC LITIG: 3,154.05

Income

The Tax Court properly held that a bonus payment made as part of an oil and gas lease was ordinary income, not capital gain. The couple was properly liable for substantial understatement component of the accuracy-related penalty in the absence of evidence that the taxpayers acted with good cause and in good faith.

Dudek, CA-3, 2015-1USTC ¶50,124; TRC FARM: 15,204

Deductions

A married couple did not have an"economic interest" in oil and gas deposits and, therefore, were not entitled to depletion deductions. The husband's employment agreement did not convey an interest in the minerals but specifically provided that the husband would receive only bonuses, not any ownership interest in the properties. Therefore, the agreement did not convey a depletable economic interest or capital gain income.

Gaudreau, DC Kan., 2015-1USTC ¶50,126; TRC FARM: 15,052

Anti-Injunction Act

The Anti-Injunction Act barred an individual's suit seeking to enjoin the IRS from issuing levy notices and for refund of the monies seized pursuant to the levy because he sought to restrain the collection of tax, and none of the exceptions to the Act applied. The individual failed to establish that the government would not ultimately prevail on the merits or that he lacked an adequate remedy at law. Rather, he had an adequate remedy at law because he could pay his tax liabilities and then sue for a refund under Code Sec. 7422.

Taliaferro v. Freeman, CA-11, 2015-1USTC ¶50,125; TRC IRS: 45,152

Benefits

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must satisfy certain requirements in order to be qualified under Code Sec. 401(a). For example, a defined benefit plan in this type of arrangement must provide "definitely determinable" benefits. Benefits will not be considered definitely determinable unless the benefit offset by the profit sharing plan is determined in a manner that precludes discretion on the part of the employer with respect to the calculation and the timing of the offset. In addition, the accrued benefit under the defined benefit plan determined without regard to the offset derived from the profit sharing plan must satisfy the requirements of Code Sec. 411(b)(1).

IRS analysis

The IRS determined that the floor-offset arrangement satisfied the criteria outlined in Rev. Rul. 76-259. Both the pension and profit sharing plans had received favorable determination letters in the past, there was no employer discretion with respect to the offset calculation or the timing with which it is applied, and the pension plan benefit accruals satisfied Code Sec. 411(b)(1) without regard to the offset from the profit-sharing plan.

Further, the IRS determined that the proposed freeze amendment to the floor-offset arrangement would not retroactively reduce benefits that had accrued as of the amendment date and therefore would not violate Code Sec. 411(d)(6). Neither would the amendment eliminate or reduce an early retirement benefit or a retirement-type subsidiary or eliminate an optional form of benefit, the IRS noted.

Reference: TRC RETIRE: 6,054.05.

IRS Permitted To Reconstruct Couple's Unreported Income From Annual Spending Statistics

The Tax Court has found that the IRS used a permissible method to reconstruct the unreported income of a married couple who did not file federal income tax returns for six tax years. Because the IRS showed sufficient evidence that the taxpayers had unreported income and because the IRS had no accurate records with which to reconstruct the taxpayers' income, it was permissible and reasonable for the agency to reconstruct the unreported income by using statistics published by the Bureau of Labor Statistics (BLS).

■ ***Comment.*** The couple was also liable for additions to tax under Code Secs. 6651 and 6654 for failure to file returns, for failure to pay the tax shown on the returns, and for failure to pay estimated tax penalties. They had operated a business organizing conferences on how to avoid paying federal income taxes that advocated using cash and minimizing financial records.

Mottahedeh, TC Memo. 2014-258, CCH Dec. 60,103(M); TRC ACCTNG: 3,150.

Practitioners' Corner

Sample Client Letter On 2014 Fourth Quarter Federal Tax Developments

The fourth quarter of 2014 brought many tax developments from Washington, the IRS and the courts. Wolters Kluwer has prepared a Second Quarter 2014 Federal Tax Developments client letter. Practitioners can email this letter to clients to alert them to some of these important recent developments.

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

Re: Important 2014 Fourth Quarter Federal Tax Developments

Dear Client:

During the fourth quarter of 2014, there were many important federal tax developments. This letter highlights some of the more significant developments for you. As always, contact our office if you have any questions.

Tax legislation

In December, Congress passed and President Obama signed the Tax Increase Prevention Act of 2014 and the Consolidated and Further Appropriations Act, 2015. The Tax Increase Prevention Act extended more than 50 popular but temporary tax incentives for individuals and businesses through 2014. This means that these tax breaks, including the state and local sales tax deduction, higher education tuition deduction, Code Sec 25C residential energy property credit, research tax credit, and more are available for 2014. Otherwise, taxpayers would not be able to claim them on their 2014 returns. Congress did not, however, make permanent any of the temporary extenders, despite an eleventh-hour push to do so, especially with some of the business tax breaks. *Federal Tax Weekly No. 51, December 18, 2014; Federal Tax Weekly No. 49, December 4, 2014.*

The Consolidated Appropriations Act funds the federal government—including the IRS – for fiscal year (FY) 2015. The Act cuts funding for the IRS by $346 million compared to FY 2014. IRS Commissioner John Koskinen has warned that the budget cut will impair tax enforcement and customer service; and even went so far as to contemplate the possibility of temporary furloughs for agency employees to save money. Some lawmakers, in contrast, have said that the agency's $10.9 billion budget for FY 2015 is adequate for the agency to focus on its core functions. *Federal Tax Weekly No. 1, January 2, 2015.*

Filing season

The IRS announced in December that the 2015 filing season will open on January 20, 2015. Previously, there had been some concern that the start of the 2015 filing season would be delayed because of the passage of late tax legislation in 2014. The IRS needed time to reprogram its return processing systems for the late legislation. *Federal Tax Weekly No. 1, January 2, 2015.*

Affordable Care Act

The IRS released more guidance on the Code Sec. 5000A individual shared responsibility requirement under the Patient Protection and Affordable Care Act (PPACA) in November. The IRS clarified certain government coverage, cafeteria plans, health reimbursement arrangements (HRAs), wellness programs, and affordability for purposes of the individual mandate. At the same time, the IRS identified the hardship exemptions from the shared responsibility requirement that may be claimed on an individual tax return without Marketplace certification. The IRS also announced inflation adjustments for Code Sec. 5000A and the Code Sec. 36B premium assistance tax credit. *Federal Tax Weekly No. 48, December 2, 2014.*

In related news, the Supreme Court announced that it will review *King v. Burwell, 2014-2* USTC *¶50,367,* a much-watched case challenging the IRS's regulations on the Code Sec. 36B premium assistance tax credit. The plaintiffs argue that the Code Sec. 36B regulations are inconsistent with the language of the PPACA. In 2014, the Fourth Circuit Court of Appeals upheld the IRS regulations. The Supreme Court will hear oral arguments in March 2015 and is expected to announce its decision in June 2015. *Federal Tax Weekly No. 1, January 2, 2015.*

The IRS has developed a number of forms to reflect new requirements under the PPACA. These include information statements from employers, insurers and the PPACA Marketplaces along with new forms to claim the Code Sec. 36B premium assistance tax credit or an exemption to the individual shared responsibility requirement. *Federal Tax Weekly No. 44, October 30, 2014.*

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"During the fourth quarter of 2014, there were many important federal tax developments."

Washington Report

by the CCH Washington News Bureau

114th Congress Convenes, GOP leaders plan first votes

The 114th Congress convened on January 6. In one of the first votes, the House is expected to approve a GOP-proposal to direct the Congressional Budget Office (CBO) and the Joint Committee on Taxation (JCT) to apply dynamic scoring to major bills. Generally, CBO and JCT would take into account macroeconomic effects of legislation into their scoring of bills if a bill is expected to have a significant impact on the U.S. economy.

"We are striving for accuracy in score keeping," House Ways and Means Chair Paul Ryan, R-Wisc., told reporters. "We know for a fact that it is not accurate or prudent to ignore the effects of economic growth on policies we make in Congress." House Democrats have criticized the dynamic scoring. "The change would undermine fiscal responsibility," Rep. Sander Levin, D-Mich., said in a statement.

On January 5, House Speaker John Boehner, R-Ohio, indicated on social media that the House is also expected to take up legislation to replace the 30-hour full-time employee threshold under the PPACA employer mandate with a 40-hour threshold. Similar legislation was proposed in the 113th Congress.

Obama to highlight new proposals

In a run-up to his January 20 State of the Union Address, President Obama is expected to preview some proposals during visits to Michigan, Arizona and Tennessee this week. "With a new Congress returning to DC, the President will lay out specific new actions and preview new policy proposals that will be included in his State of the Union address to make sure that all Americans benefit from the economic recovery. The President will begin a three week run up to the State of the Union address starting with travel next week that will highlight the progress we have made in the economy and he will announce policies that he will highlight in the State of the Union address to push us forward," a White House spokesperson said. "The proposals announced will be a mix of executive actions and legislative proposals," the spokesperson added.

President Obama has signaled to Democrats and Republicans that he wants a serious attempt at tax reform in 2015. Republican leaders, for their part, say taxes are one area where they believe compromise is available.

Tax extenders will also have to be addressed in 2015 as the *Tax Increase Prevention Act,* which passed in December, only extended the incentives through 2014. Both sides agree that the research tax credit should be made permanent, but they split on incentives such as the earned income credit and other credits aimed at lower income families.

House plans vote on Hire More Heroes Act

House GOP leaders have announced they intend to re-introduce the Hire More Heroes Act. The bill would permit an employer, for purposes of determining if an employer is an applicable large employer under the Patient Protection and Affordable Care Act (PPACA), to exclude employees who have coverage under a health care program administered by the Department of Defense (DOD), including TRICARE, or the Department of Veterans Affairs (VA). The Hire More Heroes Act is an example of the kind of bipartisan jobs bills the House will be bringing up, Rep. David Rodney, R-Ill., said in a statement. The House approved the bill in the 113th Congress but the Senate did not take up the bill.

Many Marketplace enrollees deemed eligible for Code Sec. 36B credit

The U.S. Department of Health and Human Services (HHS) recently reported that 87 percent of people who obtained health insurance coverage through the PPACA Marketplace in the first month of open enrollment were determined to be eligible for the Code Sec. 36B premium assistance tax credit. That number compared to 80 percent of enrollees who selected plans over a similar period last year, HHS noted.

"We're pleased that nationwide, millions of people signed up for Marketplace coverage starting January 1. The vast majority were able to lower their costs even further by getting tax credits, making a difference in the bottom lines of so many families," HHS Secretary Sylvia Burwell said in a statement. Open Enrollment in the Marketplace runs from November 15, 2014 through February 15, 2015.

HHS also reported that 33 percent of enrollees were under 35 years of age compared to 29 percent in the early months of the first open enrollment period. Of the 3.4 million plan selections, 48 percent (1.6 million) reenrolled in a Marketplace plan and 52 percent (1.8 million) signed up for the first time.

In related news, HHS announced that enrollees in Marketplace coverage for 2014 should receive new Form 1095-A, Health Insurance Marketplace Statement, in the mail by early February. HHS encouraged individuals to verify the accuracy of Form 1095-A to make sure the information matches their records. Individuals with questions about their Form 1095-A should contact the Marketplace Call Center, HHS instructed.

Practitioners' Corner

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Individual taxation

In October, the IRS issued a long list of cost of living adjustments (COLAs) for various Tax Code provisions in 2015 dependent upon the CPI-U index average from September 2013 through August 2014. The Tax Code requires that federal income tax brackets and certain other figures be adjusted annually for inflation. Despite a low rate of inflation during 2014, many provisions will increase for 2015. Some, however, remain the same due to rounding conventions. *Federal Tax Weekly No. 45, November 6, 2014.*

Personal exemptions. Personal and dependency exemptions will increase from $3,950 in 2014 to $4,000 for 2015.

Standard deductions. Standard deductions will increase for 2015 to $12,600 for married joint filers (up from $12,400 for 2014) and $6,300 for single filers and married separate filers (up from $6,200 for 2014). For heads of household, the standard deduction will be $9,250 (up from $9,100 for 2014).

Limitation on itemized deductions. For 2015, the amount of itemized deductions that can be claimed will begin to phase out for certain taxpayers whose income exceeds $309,900 (married joint filers); $284,050 (heads of household); $258,250 (single filers); or $154,950 (married separate filers).

Retirement plans

The IRS issued guidance in October to enable participants in 401(k) plans to invest their accounts in deferred annuities intended to guaranteed income for life to the participants post-retirement. The deferred annuities will be offered through target date funds (TDFs) that are often used by plans as default investments. *Federal Tax Weekly No. 43, October 23, 2014.*

Also in October, the IRS provided relief to U.S. citizens and residents who are participants in Canadian retirement plans. Participants can defer income accruing under the plans until it is distributed, without having to file or make a deferral election on Form 8891. *Federal Tax Weekly, No. 42, October 16, 2014.*

The IRS also announced that many retirement plan contribution and benefit limits will increase slightly in 2015. The cost of living adjustments (COLAs) affect a wide range of retirement savings vehicles, including defined contribution plans, defined benefit plans, employee stock ownership plans (ESOPs), and individual retirement arrangements (IRAs). *Federal Tax Weekly No. 44, October 30, 2014.*

Elective deferrals. The limits on elective deferrals for employees who participate in 401(k)s, 403(b)s, certain 457s, and Thrift Savings Plans will increase from $17,500 for 2014 to $18,000 for 2015.

Catch-up contributions. Eligible individuals age 50 and above may make catch-up contributions to IRAs, 401(k)s and other savings arrangements. The catch-up amounts for 401(k)s, 457s, 403(b)s, and SEPs, increase to $6,000 for 2015. IRA catch-up remain at the flat $1,000 level specified under Code Sec. 219(b)(5)(B).

Defined contribution plans. The limitation for Code Sec. 415(c)(1)(A) defined contribution plans will increase from $52,000 for 2014 to $53,000 for 2014.

IRAs

In November, the IRS clarified transition relief for the one-rollover-per-year limit on rollovers from individual retirement accounts (IRAs). The IRS previously indicated that it would not apply the limit before January 1, 2015. The latest guidance provided that a distribution occurring in 2014 that was rolled over can be disregarded when applying the one-rollover-per-year limit in 2015. Previously, the IRS and many taxpayers took the position that the one-rollover limit applied separately to each IRA maintained by a taxpayer. In *Bobrow, TC Memo. 2014-21,* the Tax Court held that a taxpayer could make only one nontaxable rollover contribution within each one-year period, regardless of how many IRAs the taxpayer maintained. *Federal Tax Weekly No. 46, November 13, 2014.*

Also in November, the IRS updated the two safe harbor explanations in Notice 2009-68 that provide information to retirement plan participants who receive eligible rollover distributions. The changes reflect guidance on the allocation of pretax and after-tax amounts among multiple distributions and on the use of in-plan Roth rollovers. *Federal Tax Weekly No. 49, December 4, 2014.*

Partnerships

Reversing the Tax Court, the Court of Appeals for the Ninth Circuit held in November that a married couple may not opt out of a partnership administrative proceeding under the *Tax Equity and Fiscal Responsibility Act (TEFRA), JT USA, LP, CA-9, November 14, 2014.* The court found that unless a partner elects to have all of his or her partnership items treated as nonpartnership items, the partner cannot elect out of proceedings under TEFRA. *Federal Tax Weekly No. 47, November 20, 2014.*

Also in November, the IRS issued proposed regulations, with partial reliance, on the treatment of "hot assets" (unrealized receivables and inventory items) under Code Sec. 751(b). The proposed regulations prescribe how a partner should measure its interest in a partnership's hot assets, and how to determine the tax consequences of a partnership distribution that reduces the partner's interest in the hot assets. *Federal Tax Weekly No. 45, November 6, 2014.*

Offshore accounts

In October, the IRS clarified its Offshore Voluntary Disclosure Program (OVDP) for U.S. taxpayers (whether residing in the U.S. or abroad) who failed to disclose foreign financial assets and pay taxes due, and who apply for relief under the streamlined filing compliance procedures. The streamlined program provides reduced penalties. The streamlined program is only available to taxpayers who can demonstrate that their actions (or failures to act) did not result from willful conduct on their part. *Federal Tax Weekly No. 42, October 16, 2014.*

Mediation

The IRS announced in December that it expanded its post-Appeals Mediation program for certain offer-in-compromise (OIC) and Trust Fund Recovery Penalty (TFRP) cases nationwide. Mediators, the IRS explained, serve as facilitators, assist in defining the issues, and promote settlement negotiations between the parties. *Federal Tax Weekly No. 51, December 18, 2014.*

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

Sincerely yours,

Compliance Calendar

■ January 9
Employers deposit Social Security, Medicare, and withheld income tax for January 3, 4. 5, and 6.

■ January 12
Employees who received $20 or more in tips during December report them to their employers.

■ January 14
Employers deposit Social Security, Medicare, and withheld income tax for January 7, 8, and 9.

■ January 15
Deadline to make a final payment of estimated tax for 2014, using Form 1040-ES, Estimated Tax for Individuals.

■ January 16
Employers deposit Social Security, Medicare, and withheld income tax for January 10, 11, 12, and 13.

TRC Text Reference Table

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

ACCTNG 21,110	602	FILEBUS 9,206	575	IRS 42,106	600
ACCTNG 24,300	577	FILEIND 15,200	1	IRS 51,056.25	576
ACCTNG 33,204.15	589	HEALTH 3,000	13	IRS 57,150	18
ACCTNG 36,154.65	578	HEALTH 3,250	561	IRS 60,052	14
ACCTNG 36,162.05	566	HEALTH 9,118	4	IRS 63,060.05	565
ACCTNG 36,162.05	6	INDIV 18,058.15	579	LITIG 6,508	577
BUSEXP 6,106.15	553	INDIV 24,050	20	LITIG 7,064.20	577
BUSEXP 6,160.15	588	INDIV 51,152.10	579	PAYROLL 9,202	556
BUSEXP 15,150	555	INDIV 54,106	554	PAYROLL 18,100	567
BUSEXP 18,950	5	INDIV 69,100	551	REAL 6,050	5
BUSEXP 24,506.05	598	INTL 3,754.25	6	RETIRE 6,064.05	19
COMPEN 6,554	554	INTL 30,086	564	RETIRE 30,404.10	591
COMPEN 36,354	563	INTL 33,054.25	15	RETIRE 42,454	590
COMPEN 45,228	7	INTL 36,000	586	RETIRE 42,466	574
COMPEN 45,232	588	INTL 36,052	17	RETIRE 51,052.20	587
DEPR 3,504.05	562	INTLOUT 36,050	575	RETIRE 51,052.20	599
EXEMPT 3,102	590	IRS 3,060	603	RETIRE 51,102.05	587
EXEMPT 3,154	15	IRS 3,204.30	601	RETIRE 66,456	592
EXEMPT 12,204	566	IRS 12,200	17	RETIRE 66,458.10	578
EXEMPT 12,252.15	16	IRS 12,300	4	RETIRE 66,750	2
FILEBUS 9,104.20	601	IRS 24,106	600	SALES 36,350	3
FILEBUS 9,108	599	IRS 33,156	589	SALES 48,056	19

From the Helpline

The following questions have been answered recently by our "CCH Tax Research Consultant" Helpline (1-800-344-3734).

Q A taxpayer's husband died during the year, and she is having problems with the step-children. If the taxpayer wants to file her own return, may she file as a single taxpayer?

A IRS Publication 17 provides that if a spouse dies during the year, the surviving spouse is considered married for the whole tax year for filing status purposes. This means that generally the surviving spouse cannot file returns as a single taxpayer, head of household, or surviving spouse. (A taxpayer does not qualify as a surviving spouse for the same tax year in which the taxpayer's spouse dies. Rather, the taxpayer may file returns as a surviving spouse for two tax years following the year in which the taxpayer's spouse died.) The taxpayer may file a joint return or use married filing separate status. *See TRC FILEIND: 3,212.*

Q In mid-December 2014, Congress extended the exclusion for amounts contributed to charity from a qualified distribution from an IRA belonging to a taxpayer age 70 1/2 or older. What does that mean for IRA owners who took required minimum distributions shortly before the extension passed?

A As long as the taxpayer accomplished the IRA distribution within the 2014 year and met the other requirements, the amount of the donation is nontaxable. *See TRC RETIRE: 66,514.*