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Obama Unveils FY 2016 Budget With Tax Reform Proposals

◆ *FY 2016 Budget Proposals, Treasury Explanations*

President Obama has called for a $3.99 trillion fiscal year (FY) 2016 federal budget, renewing some previous tax proposals along with proposing new ones targeted to businesses and individuals. The President also urged Congress to increase funding for the IRS by nearly $2 billion. At the same time, the Treasury Department released its *General Explanations of the Administration's FY 2016 Revenue Proposals* (known as the "Greenbook").

■ ***Take Away.*** "The administration has said they are hoping the budget proposals will begin a dialogue with Congressional Republicans about tax reform," David Kautter, CPA, partner in charge, Washington National Tax, McGladrey, LLP, told Wolters Kluwer. Since the focus appears to be on business reforms, initial discussions could begin in some areas where there is common ground, such as small business tax relief, Kautter noted.

Some new proposals

Foreign earnings. The President's budget would impose a one-time tax of 14 percent on untaxed foreign earnings that U.S. companies have accumulated overseas. The earnings subject to the one-time tax could then be repatriated without any further U.S. tax, Treasury explained. The President also proposed to impose a minimum tax on foreign income of U.S. multinationals at a rate of 19 percent reduced (but not below zero) by 85 percent of the effective foreign tax rate imposed on that income.

■ ***Comment.*** "The 14 percent tax on accumulated foreign income coupled with a 19 percent minimum tax on CFCs would represent a major cost to US businesses, and indeed, could be seen as anti-competitive. However, if the rates were reduced significantly, this structure would probably be considered a 'territorial' tax structure," Daniel Gottfried, partner, Hinckley Allen LLP, Hartford, told Wolters Kluwer. "This may be the opening posture in a negotiation that leads to a territorial business tax regime."

Capital gains/dividends. The President proposed increasing the top long-term capital gains and qualified dividends tax rate from 20 percent to 24.2 percent for tax years beginning after December 31, 2015. Including the 3.8 percent tax on net investment income (NII), this would increase the top effective long-term capital gains and qualified dividends tax rate to 28 percent, Treasury explained.

Child and dependent care credit. The President's budget calls for tripling the maximum child and dependent care credit for families with children under age five and would make the full credit available to qualified taxpayers with incomes of up to $120,000. In return, the President also proposed to eliminate tax preferences for flexible spending accounts for child care expenses.

Second earner credit. President Obama proposed a new "second earner" tax credit of up to $500 for qualified couples where both spouses work.

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Store Not Open To Public Was Placed In Service And Eligible For Bonus Depreciation

◆ *Stine LLC, D.La., January 27, 2015*

In a grant of summary judgment, a federal district court has concluded that two buildings designed to be retail stores were placed in service when the buildings were substantially complete. The court rejected the government's argument that the buildings were not placed in service until they were open to the public for business.

■ ***Take Away.*** "Buildings are more elusive than equipment," Thomas Yeates III, Cost Segregation Practice Leader, Ernst & Young LLP National Tax, told Wolters Kluwer. "Normally, everybody, including the IRS, looks to the certificate of occupancy (CEO) to determine if the building is ready and available for its intended purpose. Here, the jurisdiction issued a CEO, but it limited occupancy and did not allow customers. That piece of the case was unclear," Yeates said.

Background

The buildings were located in the Gulf Opportunity (GO) Zone in Louisiana. To help the economy recover after two devastating hurricanes in 2005, Congress provided 50 percent bonus depreciation for nonresidential real property, provided the property was placed in service before January 1, 2009. Income taxes of $2.1 million were in dispute.

The taxpayer was a retail seller of home building materials and supplies. The taxpayer built two buildings (stores) that were substantially complete. The stores received certificates of occupancy that authorized them to receive equipment, shelving and merchandise, as well as appropriate personnel to install the equipment and stock the shelves. As of December 31, 2008, the buildings were not open for business, and the certificates of occupancy did not allow customers to enter the buildings.

Code and regs

Code Sec. 1400N authorized bonus depreciation for property located in the GO Zone. The property had to be placed in service by December 31, 2007 (December 31, 2008 for nonresidential real property). The statute provided that depreciation in the GO Zone was governed by Code Sec. 167.

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Tax Proposals

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IRS budget

President Obama proposed to fund the IRS at $12.9 billion for FY 2016, effectively restoring cuts to the agency's budget in recent years. As in past years, the President proposed to give the IRS express authority to regulate unenrolled preparers, improve the whistleblower program, and take additional measures to combat identity theft. Additionally, the President's budget would accelerate the due date for filing for most information returns from late February to January 31, Treasury explained.

■ ***Comment.*** "The AICPA is sympathetic to the impact of service cuts at the IRS and the challenges taxpayers and practitioners have encountered," Edward Karl, CPA, vice president – taxation, AICPA, told Wolters Kluwer. However, proposals to increase funding for the agency are likely to meet resistance in Congress, he noted. Karl also lauded the President for including staggered return due dates in his budget, a proposal the AICPA has promoted for a number of years.

More proposals

Corporate tax rate. Consistent with earlier proposals, the President's budget would reduce the corporate tax rate to 28 percent, with a 25 percent effective rate for domestic manufacturing. The rate reduction would be offset, in part, by eliminating fossil fuel tax breaks and other unspecified business tax incentives.

Education. The American Opportunity Tax Credit (AOTC) would be made permanent and expanded. For simplification and revenue-offset purposes, the President's budget would repeal or let expire the Lifetime Learning Credit, the higher education tuition deduction, the student loan interest deduction (for new borrowers), and Coverdell Education Savings Accounts (for new contributions), Treasury explained.

Higher income taxpayers. As in past years, President Obama proposed to curb tax benefits for higher income individuals. The budget would limit the value of itemized deductions and other tax preferences to 28 percent. The President also renewed his "Buffett Rule" proposal.

Small business stock. The President renewed his proposal to permanently extend the 100 percent exclusion from tax by a non-corporate taxpayer for capital gains realized on the sale of qualified small business stock.

EIC/Child tax credit. Temporary enhancements to the earned income credit (EIC) and child tax credit would be made permanent.

Business incentives. The President's budget would make permanent and enhance the research tax credit, the Work Opportunity Tax Credit, Indian Employment Credit, and the Production Tax Credit. President Obama also called for enhanced Code Sec. 179 expensing to be made permanent and for enhancements to the Code Sec. 45R small employer health insurance credit.

For more details and analysis of the President's FY 2016 budget, see a special Briefing on IntelliConnect.

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*

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Final Regs Authorize Applications By Nonprofit Health Insurance Issuers For Code Sec. 501(c)(29) Status

◆ *TD 9709*

The IRS has issued final regs that authorize it to prescribe procedures for qualified nonprofit health insurance issuers (QNHIIs) to obtain tax-exempt status under Code Sec. 501(c)(29). The final regs authorize the IRS to recognize a QNHII as exempt, effective as of the date of its formation or March 23, 2010, if later.

■ ***Take Away.*** The *Patient Protection and Affordable Care Act* (PPACA) directed the Department of Health and Human Services' (HHS) Center for Medicare and Medicaid Services (CMS) to establish the Consumer Operated and Oriented Plan (CO-OP) program. The program is designed to foster member-governed QNHIIs that will offer qualified health insurance plans, with a strong consumer focus, in the individual and small group markets. Under PPACA Sec. 1322, CMS provides loans and repayable grants to organizations seeking to become QNHIIs, to help with start-up costs and to meet state solvency requirements for health plan issuers.

■ ***Comment.*** The final regs adopt, without revision, temporary and proposed regs issued in February 2012. The IRS rejected revisions proposed by two commenters.

QNHIIs

PPACA authorized tax-exempt QNHIIs to offer health plans, beginning January 1, 2014, through PPACA's Affordable Insurance Exchanges (Marketplaces). PPACA requires that a QNHII be organized as a nonprofit member corporation under state law and that substantially all of its activities be the issuance of qualified health plans in each state in which it is licensed.

CMS states that CO-OPs are directed by their customers and designed to offer additional affordable, consumer-friendly and high-quality health insurance options. All individuals (and their adult dependents) who are issued a CO-OP health plan are members of the CO-OP. An entity cannot be a QNHII unless it offers health plans only in a state that has adopted PPACA's market reforms. CMS requires that at least 2/3 of the policies and contracts issued by a CO-OP in each state be qualified health plans in the individual or small group market. However, CO-OPs may offer some health plans outside of an exchange.

Tax Code

Code Sec. 501(c)(29) recognizes a QNHII as tax-exempt if it has received a loan or grant under the CO-OP program and:

- It has given notice that it is applying for tax-exempt status;
- No part of its net earnings inure to the benefit of a private shareholder or individual;
- No substantial part of its activities may be propaganda or influencing legislation; and
- It does not participate in any political campaign for or against any candidate for public office.

■ ***Comment.*** An exception to the inurement provisions allows profits to be used to lower premiums, improve benefits, or otherwise improve health care for members.

Rev. Proc. 2015-17

Rev. Proc. 2015-17 provides instructions on how an organization should apply for tax-exempt status under Code Sec. 501(c)(29). Under Rev. Proc. 2015-17, a QNHII must submit a letter application with Form 8718 (User Fee), must provide a balance sheet for the current year and the previous three years, and must give both a detailed narrative statement of the QNHII's past and proposed activities and a narrative of its actual and anticipated receipts and expenditures.

The IRS determination of exempt status is effective as of the date of the organization's formation or March 23, 2010 if later, provided the QNHII's purposes and activities prior to issuance of the letter were consistent with the requirements of Code Sec. 501(c)(29), and provided the QNHII submits its application within 15 months after it executes its loan agreement with CMS.

References: FED ¶47,007; TRC EXEMPT: 12,054.

Bonus Depreciation

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Under Reg. §1.167(a)-10, an asset's depreciation period begins when it is placed in service. Reg. §1.167(a)-11 defines "placed in service" as being in a condition of readiness and availability for a specifically designed function. A building that is intended to house machinery and equipment is placed in service when its construction is substantially complete. In the case of a factory, a building's readiness and availability is determined without regard to whether the machinery or equipment (that the building will house) has been placed in service, unless the building itself is essentially an item of machinery or equipment that will house machinery or equipment.

Court's analysis

The court found that the buildings were placed in service under Code Sec. 167 when they were substantially complete and in a condition of readiness to perform the function for which they were built - to house and secure racks, shelving and merchandise. Accordingly, the buildings qualified for 50 percent bonus depreciation in 2008.

The court found no authority for the government's claim that "placed in service" equated to "open for business." In fact, the government conceded that no such authority exists. The taxpayer cited proposed regs under Code Sec. 168 and an IRS Audit Technique Guide, both of which concluded that the issuance of a certificate of occupancy was an indication that a building had been placed in service.

The court found that there is a marked difference in the treatment of a building as opposed to equipment. None of the cases cited by the government involved buildings that functioned independently of the equipment they housed.

References: 2015-1 USTC ¶50,172; TRC DEPR: 3,602.

OVDP Will Remain Open Indefinitely, IRS Indicates

◆ *IR-2015-9*

The IRS will continue its offshore voluntary disclosure program (OVDP) "for an indefinite period until otherwise announced." The IRS first opened the program in 2009 and has maintained it continuously since reopening it in 2012.

■ ***Take Away.*** There have been over 50,000 disclosures, and the IRS has collected more than $7 billion since the OVDP opened in 2009. The IRS reported in June 2014 that more than 45,000 taxpayers had made disclosures and had paid $6.5 billion in back taxes, interest and penalties.

■ ***Comment.*** The announcement came in an IRS information release on the annual "Dirty Dozen" tax scams and schemes. Other Dirty Dozen schemes identified by the IRS in 2015 include "phishing," return preparer fraud, and phone scams.

Offshore reporting

U.S. taxpayers are required to report their worldwide income. Taxpayers are also required to disclose the existence of foreign accounts on Form 1040, Schedule B (Part III) and, if they exceed a $10,000 threshold, on Treasury's Report of Foreign Bank and Financial Accounts. More recently, taxpayers with foreign assets exceeding higher thresholds must start reporting their interests on IRS Form 8938, Statement of Foreign Financial Accounts.

The IRS noted that individuals have been identified as evading U.S. taxes by hiding income in offshore banks, brokerage accounts and nominee entities (often shell corporations and trusts) and then accessing the funds with debit cards, credit cards, and wire transfers. The IRS has conducted thousands of offshore-related civil audits, and the Department of Justice (DOJ) has entered into nonprosecution agreements with foreign banks to obtain the identities of account holders. DOJ has also aggressively prosecuted tax evasion cases involving foreign income.

■ ***Comment.*** With new foreign account reporting requirements phasing in over the next few years, the IRS indicated that hiding offshore income is becomingly increasingly difficult.

Under the OVDP, taxpayers enter into a closing agreement with the IRS to disclose their accounts and pay back taxes and interest, plus a penalty of 27.5 percent. In return, taxpayers avoid criminal prosecution. Significantly, in 2014 the IRS increased the penalties to 50 percent in some cases.

■ ***Comment.*** "The recent string of successful actions against offshore tax cheats and the financial organizations that help them shows that it's a bad bet to hide money and income offshore," IRS Commissioner John Koskinen said. "Taxpayers are best served by coming in voluntarily and getting their taxes and filing requirements in order."

Reference: TRC FILEBUS: 9,104.

Transfer Of Some Corporate Assets To Third Party Will Not Affect Treatment Of Complete Liquidation; Cash In Reorganization Is Tax-Free To Corporation

◆ *LTR 201504007*

The IRS has ruled favorably, in a private letter ruling, on a series of transactions designed to be treated as corporate liquidations under Code Sec. 332 and corporate reorganizations under Code Sec. 368. The transactions also involved a spinoff of corporate assets to shareholders, designed to be tax-free under Code Sec. 355.

■ ***Take Away.*** The IRS stated that it was only ruling on certain discrete legal issues involved in the proposed transaction, and that it was not ruling on whether the transactions satisfied Code Secs. 332, 355 or 368.

Background

P is a U.S. corporation and the parent of an affiliated group of corporations. Through its subsidiaries, P engages in the "Controlled Business" (through the Controlled Subsidiaries) and the "Retained Business" (through the Distributing Subsidiaries).

P owns Sub 1 (S1), Foreign Sub 1 (FS1) and Controlled Corporation (CC), which initially was a disregarded entity. S1 wholly owns S2 and S3. S2, which wholly owns S4, conducts the Retained Business and the Controlled Business. FS1 conducts P's worldwide businesses. P and S3 share ownership of FS1. FS1 wholly owns FS3.

Domestic and foreign transfers

S1, S2 and S3 each converted to a limited liability corporation (LLC) and to a disregarded entity (the "Liquidations"). S2 will distribute the stock of its Controlled Subsidiaries to S1, which will distribute the stock to P, in transactions intended to be disregarded for tax purposes. P will transfer the stock of the Controlled Subsidiaries to CC, also in a transaction to be disregarded.

P will separate the worldwide Retained and Controlled Businesses. FS3 will Form FS4 and contribute the Controlled Business to FS4 for its stock. FS3 will distribute FS4 stock to FS1. S3 will distribute its interest in FS1 to P (through S1), giving P complete ownership of FS1. FS1 will distribute FS4 stock to P, which will contribute the stock to CC.

Proposed transactions

CC will convert from an LLC to a corporation in a transaction treated as a contribu-

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Taxpayer Was Bona Fide Resident Of U.S. Virgin Islands, Tax Court Finds

◆ *Sanders Est., 144 TC No. 5*

The Tax Court has found that a taxpayer was a bona fide resident of the U.S. Virgin Islands (USVI) and correctly filed his income tax returns with the local tax authority, not the IRS. The limitations period had commenced when the taxpayer filed his tax returns with the Virgin Islands Bureau of Internal Revenue (VIBIR) and expired before the IRS had mailed a deficiency notice to the taxpayer.

■ ***Take Away.*** Code Sec. 932 provides that bona fide USVI residents file their tax returns with the Virgin Islands Bureau of Internal Revenue (VIBIR). Those who are not bona fide residents must each file two income tax returns: one with the IRS, and one with the VIBIR. A bona fide resident's single return filed with the VIBIR satisfies the taxpayer's USVI and federal tax obligations.

Background

The taxpayer was a U.S. citizen who moved to the USVI in 2002. Initially, the taxpayer lived in a condominium in the USVI. Later, he purchased a yacht, which he moored in St. Thomas, USVI, where he resided during 2003 and 2004. The taxpayer married in the USVI in 2003 and also maintained bank accounts listing his USVI residence.

For the three years at issue, the taxpayer filed tax returns with the VIBIR but not with the IRS. On his returns he reported a home address in the USVI. The IRS determined that the taxpayer was not a bona fide resident of the USVI and issued notices of deficiency in 2010. The taxpayer died in 2012

Court's analysis

The court looked to *Vento v. Dir. of V.I. Bureau of Internal Revenue, 715 F.3d 455, CA-3, 2013*, for guidance. In Vento, the Third Circuit had grouped 11 factors from *Sochurek, 300 F.2d 34, CA-7, 1962,* into four categories: (1) intent; (2) physical presence, (3) social, family and professional relationships; and (4) the taxpayer's own representations. Here, the court found that the taxpayer had the intent to be a bona fide resident as he intended to remain indefinitely or at least for a substantial period in the USVI. The taxpayer identified himself as a resident of the USVI. For the years in dispute, the taxpayer had timely filed returns with the VIBIR. Additionally, the taxpayer was a partner in a USVI business.

The court further found that the taxpayer had made an honest and reasonable attempt to file returns. As a resident of the USVI, the taxpayer had filed returns with the VIBIR. The returns filed with the VIBIR satisfied the taxpayer's federal tax filing obligations and the Code Sec. 6501(a) limitations period commenced. Therefore, the notice of deficiency by the IRS was made after the three-year limitations period for assessment had expired.

References: Dec. 60,222, TRC INTL: 24,102.05.

Corporate Reorganizations

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tion of the Controlled Subsidiaries, plus certain assets, in exchange for CC's stock. CC also will borrow cash and distribute it to P. P will distribute CC's stock pro rata to its shareholders (the "spin-off"). P will distribute all of the cash to its shareholders, either by purchasing shares or by paying pro rata dividends.

Representations

The Controlled Business's assets owned by S1 and S2 are less than a specified percentage (X percent) of their total assets. The liquidations of S1 and S2 will not involve any sale, transfer or reincorporation of their assets.

The fair market value (FMV) of assets transferred to CC will exceed the liabilities assumed and the cash received. After the exchange, CC's assets will exceed its liabilities. The aggregate basis and FMV of assets transferred to CC will equal or exceed the liabilities assumed, cash, and value of other property received.

Law

Under Code Sec. 332, a corporation has no gain or loss on the receipt of property distributed in a complete liquidation of another corporation. The recipient must own at least 80 percent of the distributing corporation by vote and value.

Code Sec. 368(a)(1) defines corporate reorganizations. Under Code Sec. 361(a), a corporation does not recognize gain or loss on a reorganization involving an exchange of property solely for stock in another corporation. Under Code Sec. 361(b)(1), if the exchange involves the receipt of money or other property, as well as stock, the corporation will not have gain if the corporation receiving the money distributes it under the plan of reorganization.

Under Code Sec. 355, a distribution by a corporation to its shareholders that consists solely of stock in a controlled corporation will generally be tax-free to the shareholders.

Under Code Sec. 1504(a)(3), a corporation that ceases to be a member of a consolidated group (and any successor) cannot be included in any consolidated return for five years.

Rulings

The IRS issued the following rulings:

- The transfer of less than X percent of the assets of S1 and S2 to CC does not prevent the liquidations from being complete liquidations under Code Sec. 332.
- Provided the transactions satisfy Code Secs. 355 and 368(a)(1)(D), P's distribution of the cash to its shareholders will be treated as a distribution under a plan of reorganization.
- CC is not a successor to P under Code Sec. 1504(a)(3).

Reference: TRC CCORP: 12,212.10.

Building Lessee Claiming Rehabilitation Credit Must Include 100 Percent Of Credit Ratably In Gross Income

◆ *CCA 201505038*

IRS Chief Counsel has determined that a property lessee who claims the rehabilitation credit under Code Sec. 47 must include in income the entire amount of the credit. The property lessee has to include the credit in income ratably over the shortest recovery period that could apply to the property.

■ ***Take Away.*** The rehabilitation credit is part of the investment tax credit (ITC) under Code Sec. 46. Code Sec. 50 and former Code Sec. 48 require a taxpayer to reduce the basis of the ITC property by 50 percent of the ITC. However, if the credit being claimed is the rehabilitation credit, the taxpayer must reduce basis by 100 percent. Since property lessees who claim the ITC don't own the property, they must include the credit amount in income, rather than reduce the basis of the property. Chief Counsel addressed the issue because the statute was unclear whether a lessee had to recapture 50 percent of the credit or the full credit.

Background

Under Code Sec. 47, the rehabilitation credit is the sum of 10 percent of the qualified rehabilitation expenditures for a building that is not a certified historic structure, and 20 percent of the qualified expenditures if the building is a certified historic structure. Code Sec. 50(d) requires adjustments to basis for the ITC, based on rules similar to the rules in Code Sec. 48(d) that were previously in effect. Former Code Sec. 48(q) required a 50 percent reduction for a taxpayer claiming the general ITC, and a 100 percent basis reductions for taxpayers claiming the rehabilitation credit ITC.

Former Code Sec. 48(d) allowed the lessor of property to elect to treat the lessee of the property as the taxpayer who owns the property and is entitled to claim the general ITC. The basis adjustment rules in Code Sec. 48(q) did not apply in this situation, because the lessee was not the property owner. Code Sec. 48(d) required the lessee to include 50 percent of the credit amount in income. There was no provision requiring a lessee who claimed the rehabilitation credit to include 100 percent of the credit in income.

100 percent

However, the Joint Committee Explanation of the *Tax Equity and Fiscal Responsibility Act of 1982* (TEFRA) stated that Congress intended the lessee to include 100 percent of the rehabilitation credit in income. Congress adopted technical corrections that amended Code Sec. 48(q) to provide for 100 percent recognition of income if the lessor made the Code Sec. 48(d) election. Congress, however, did not make a corresponding correction to Code Sec 48(d) regarding the 100 percent inclusion.

As a result, a purely technical reading of these statutes could suggest that 100 percent inclusion of the rehabilitation credit did not apply to a lessee. The IRS determined, for several reasons, that this would be an inappropriate conclusion. Therefore, a taxpayer lessee claiming the rehabilitation credit must include 100 percent of the allowable credit in income.

Reference: TRC BUSEXP: 51,150.

IRS Preliminary Data For 2013 Tax Year Reflects Increased Capital Gain Distributions As Economy Improved

The IRS Statistics of Income Division has issued its preliminary data on 2013 tax year returns, which indicates the number of returns filed for 2013 increased by less than two percent from the number filed in 2012 (144.9 million in 2012 to 147.7 million in 2013). The statistics also reflect an overall 0.8-percent increase in the amount of taxable income reported for 2013, which included a marked increase in the reported amount of taxable distributions of net capital gain.

Capital gain distributions. Although the amount of net capital gain reported decreased by $62.4 billion from 2012 to 2013, the amount of capital gain distributions reported in 2013 increased more than one and a half times the amount reported for 2012, showing a percent change of 156.8 percent. Taxpayers in all income categories received increased distributions of net capital gains, owing to the improved economy in 2013. Taxpayers with adjusted gross income (AGI) between $100,000 and $200,000 and between $200,000 and $250,000 brackets experienced the highest percent increases in net capital gain distributions, reporting respective increases of $7.24 billion (a 194-percent change from 2012) and $2.06 billion (a 198-percent change from 2012), the IRS reported. However, taxpayers in lower-income categories also received large increases in capital gain distributions. Taxpayers with AGI between $30,000 and $50,000, for example, experienced a 184-percent change from 2012, the IRS reported.

■ ***Comment.*** During 2013, the U.S. stock market posted record gains by both large-cap and small-cap stocks. The S&P 500 composite index gained nearly 30 percent during the year, with one result in particular being that mutual funds realized large profits that they passed on to individual investors in the form of capital gain distributions.

www.irs.gov, Statistics of Income Tax Stats—Individual Income Tax Returns, 2013 Preliminary Data.

Tax Briefs

Internal Revenue Service

The IRS has released a fact sheet providing information on a taxpayer's right to be informed, one of several taxpayer rights that are grouped into ten categories and are discussed in IRS Publication 1, Your Rights as a Taxpayer. Taxpayers have the right to know what they need to do to comply with the tax laws. This includes entitlement to clear explanations of the laws and IRS procedures in all tax forms, instructions, publications, notices and correspondence. Also, taxpayers have the right to be informed of IRS decisions about their tax accounts and to receive clear explanations of the outcomes.

FS-2015-3, FED ¶46,236; TRC IRS: 12,350

International

The governments of the United States and Kazakhstan have released a Competent Authority Agreement (agreement) regarding the eligibility of entities that are treated as fiscally transparent under the laws of either nation to benefits under the Convention Between the Government of the United States and the Government of the Republic of Kazakhstan for the Avoidance of Double Taxation and the Prevention of Fiscal Evasion with Respect to Taxes on Income and Capital (treaty), which was entered into in 1993. The agreement sets out the cases where fiscally transparent entities are entitled to treaty benefits and clarifies the procedure for claiming such benefits from either country.

Announcement 2015-4, FED ¶46,237; TRC INTL: 18,138

The IRS Criminal Investigation Division (CI) and Her Majesty's Revenue & Customs (HMRC) from the United Kingdom recently co-hosted a three-day international criminal tax symposium.

IR-2015-14; TRC INTL: 18,150

Jurisdiction

A couple was barred by collateral estoppel from disputing the character of payments the husband received from his law firm when he retired. The only difference between the two cases filed by the couple was the amount and years at issue, which did not preclude the application of collateral estoppel.

Wallis, CA-11, 2015-1USTC ¶50,171; TRC LITIG: 3,054.05

An individual's complaint seeking a refund or damages for the IRS's wrongful levy of his pension and Social Security benefits was properly dismissed for lack of subject matter jurisdiction. He failed to show that the government waived its sovereign immunity or consented to be sued.

Lawrence, CA-11, 2015-1USTC ¶50,164; TRC LITIG: 9,054.05

Summons

A corporation's petition to quash IRS third-party collection summonses issued to a bank was dismissed for lack of subject matter jurisdiction. The corporation was not entitled to notice under Code Sec. 7609 because the summons was issued to collect the unpaid tax liabilities of the corporation's alter-ego.

Alpha Tech USA, LLC, DC Tex., 2015-1USTC ¶50,167; TRC IRS: 21,106

A corporation's petition to quash IRS third-party summonses seeking records from banking institutions in connection with an investigation into its tax liabilities was dismissed. The government established its *prima facie* case for summons enforcement, which the corporation failed to rebut.

Advanced Health Strategies, Inc., DC Minn., 2015-1USTC ¶50,166; TRC IRS: 21,108

An individual was not entitled to an order staying his compliance with an IRS summons pending appeal. The individual was not irreparably harmed absent a stay because any injury resulting from compliance would be remedied if his arguments ultimately prevailed on appeal.

Anderson, DC Calif., 2015-1USTC ¶50,161; TRC IRS: 21,300

Credits

The IRS has released a fact sheet for the Earned Income Tax Credit (EITC). The fact sheet provides information on who qualifies for the credit, how much the credit is worth and how to determine eligibility. The IRS urges employees, business owners and farmers who earned $52,427 or less in 2014 to see if they qualify by using the EITC Assistant on IRS.gov. To get the EITC, workers need to file a return and specifically claim the credit even if they aren't required to file.

IR-2015-15, FS-2015-4, FED ¶46,239; TRC INDIV: 57,252

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Treasury/IRS Issue Second Quarter Update To 2014–2015 Guidance Plan; New Projects Added

Treasury and the IRS issued their second quarter update to the 2014–2015 Priority Guidance Plan (PGP). The guidance plan identifies projects that are priorities during the 12-month period from July 2014 through June 2015.

New projects. New projects can be found in the listings for Employee Benefits—Retirement; Employee Benefits—Executive Compensation, Health Care and Other Benefits; and General Tax Issues. New issues included guidance under Code Sec. 36B on the health insurance premium tax credit; Ebola-related guidance; pension funding, IRA rollovers, and cumulative changes to retirement plans; changes in measurement periods for determining full-time employees under Code Sec. 4980H, and additional elections for health coverage under cafeteria plans.

2014-2015 Priority Guidance Plan, Second Quarter Update, FED ¶46,238; TRC IRS: 12,350.

Tax Briefs

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A consulting and engineering company was not entitled to the research credit under Code Sec. 41 because the research expenses under its cost-plus capped contracts were funded and, therefore, were not eligible. The company was paid for predefined tasks at predetermined rates pursuant to a detailed project budget and payment was not contingent upon client satisfaction or approval.

Geosyntec Consultants, Inc., CA-11, 2015-1 USTC ¶50,170; TRC BUSEXP: 54,158.25

Frivolous Arguments

An individual's action for damages against the IRS for alleged fraudulent filing of information returns, unauthorized disclosures, and seeking injunctive relief and also refund of penalties imposed for frivolous filing was dismissed for lack of subject matter jurisdiction and for failure to state a claim. The individual failed to show that the government waived its sovereign immunity to be sued for damages under Code Sec. 7434.

Diamond, DC Calif., 2015-1USTC ¶50,162; TRC IRS: 9,206.10

Liens and Levies

A married couple's tax liabilities were reduced to judgment and the federal tax liens on the couple's shares in a cooperative apartment building were foreclosed to satisfy the outstanding debt. The couple's claim that IRS failed to exhaust reasonable collection alternatives before foreclosing on their primary residence was without merit. The principal residence exemption applies only to administrative levies not to judicial foreclosure actions under Code Sec. 7403.

Martynuk, DC N.Y., 2015-1USTC ¶50,168; TRC IRS: 45,158

An IRS Appeals officer's determination to reject a proposed IRS lien and levy and to place the individual's account in currently not collectible (CNC) status was not an abuse of discretion. The Appeals officer properly considered the issues raised by the taxpayer during both Collection Due Process hearings when issuing the supplemental notice of determination.

Savoy, CA-4, 2015-1USTC ¶50,165; TRC IRS: 51,056.15

Tax Assessments

The government was entitled to reduce to judgment tax liabilities assessed against a couple and foreclose federal tax liens on their real property. The couple's argument that three of the tax years at issue were time-barred under the 10-year collection limitation period was rejected because the couple's installment agreement for those years waived the limitations period.

Payne, DC Ohio, 2015-1USTC ¶50,163; TRC IRS: 45,160

A married couple was properly denied a new trial based on newly discovered evidence in the government's action to reduce their tax assessments to judgment. The district court properly calculated the limitations period and the couple's "new evidence" did not change that calculation.

Meehan, CA-3, 2015-1USTC ¶50,160; TRC LITIG: 9,256

Offer-in-Compromise

The government's collection action against an individual was not barred by the 10-year collections limitation statute. The limitation period was stayed for a period of 280 days because the individual sought an offer-in-compromise.

Rulison, DC N.Y., 2015-1USTC ¶50,169; TRC IRS: 45,202

Bankruptcy

A Chapter 7 debtor corporation held tax refunds pursuant to a tax-sharing agreement (TSA) that created a debtor/creditor relationship between the debtor and its subsidiaries. Therefore, the refunds belonged to the debtor's bankruptcy estate not to the subsidiary bank or its receiver.

In re Downey Financial Corporation, CA-3, 2015-1USTC ¶50,146; TRC IRS: 57,056.10

IRS Amends Rules For Accounting Method Changes To Provide Greater Flexibility For 2014

The IRS has amended Rev. Proc. 2015-13 to provide greater flexibility for taxpayers seeking to obtain automatic consent to make an accounting method change for 2014. Rev. Proc. 2015-13 provides the general procedures for taxpayers to obtain IRS consent to change a method of accounting under either the advance consent rules or the automatic consent rules.

The amended version modifies a transition rule in Sec. 15.02(a) of the revenue procedure to permit taxpayers seeking automatic consent to choose whether to follow Rev. Proc. 2015-13 or Rev. Proc. 2011-14, the predecessor to Rev. Proc. 2015-13. The IRS made the revision to accommodate taxpayers who had already prepared a Form 3115, Application for Change in Accounting Method, for their 2014 tax year under Rev. Proc. 2011-14.

Rev. Proc. 2015-13, FED ¶46,228; TRC ACCTNG: 21,104.

Oklahoma Loses Bid To Have Supreme Court Hear Code Sec. 36B Challenge

The U.S. Supreme Court will not take up Oklahoma's challenge to the IRS's regs on the Code Sec. 36B premium assistance tax credit (*State of Oklahoma v. Burwell, 2014-2* USTC *¶50,459*). The Supreme Court has scheduled oral argument in a similar case, *King v Burwell, 2014-2* USTC *¶50,367,* for March 4.

In 2014, a federal district court found that the *Patient Protection and Affordable Care Act* (PPACA) makes the Code Sec. 36B credit available only to enrollees in state-run Health Insurance Marketplaces and not to enrollees in federally-facilitated Marketplaces. The court struck down the IRS's regs.

Oklahoma asked the Supreme Court to review the district court's decision and bypass the court of appeals review requested by the federal government. On January 26, the Supreme Court announced that Oklahoma's petition was denied.

Supreme Court Order List, January 26, 2015; TRC HEALTH: 3,110.

What's New On 2014 Form 1040, Related Schedules And Other Forms

As the 2015 filing season gets underway, practitioners and taxpayers should note new requirements for individuals under the Patient Protection and Affordable Care Act (PPACA), which have resulted in several significant changes to the 2014 Form 1040, its schedules, and related forms. Many other changes are reflected on the 2014 Form 1040—for example, the increased standard deduction and personal exemption amounts, as well as incentives extended by year-end 2014 tax legislation. This Practitioners' Corner highlights some of the notable changes to 2014 Form 1040, its schedules and other forms.

> *"This Practitioners' Corner highlights some of the notable changes to 2014 Form 1040, its Schedules and other Forms."*

Form 1040

Standard deduction and personal exemption

Line 40, Standard deduction. The standard deduction may be claimed on Form 1040, Line 40. For 2014, the standard deduction for single individuals and married couples filing separately is $6,200. The standard deduction for married couples filing joint returns and qualifying widow(er)s is $12,400. The standard deduction for heads of households is $9,100.

Line 42, Personal exemption. Taxpayers multiply the personal exemption amount for the tax year by the number of exemptions claimed on Form 1040, Line 6d, and enter that amount on Line 42. For 2014, the amount of the personal exemption has slightly increased to $3,950 per exemption.

Health insurance coverage reporting

Line 46, Advance premium tax credit. All taxpayers who received advance payments of the Code Sec. 36B premium assistance tax credit to offset the cost of health insurance coverage obtained through the PPACA Health Insurance Marketplace must reconcile the amounts advanced to their insurers during the year with the actual amount of credit to which they are entitled. If a taxpayer received a greater amount in advance premium tax credit payments than the actual amount to which he or she is entitled, based on his or her actual household income for 2014, the taxpayer reports the excess on Form 1040, Line 46, Excess advance premium tax credit repayment.

Line 69, Premium tax credit. Taxpayers who did not receive advance payments of the Code Sec. 36B premium assistance tax credit payments during 2014, but who are claiming a credit use Form 8962, Premium Tax Credit, to calculate the amount of their credit. Taxpayers report the net credit in the Payments Section of Form 1040, on Line 69, Net premium tax credit. Form 8962 is attached to the taxpayer's return.

■ ***Reminder.*** The Code Sec. 36B credit is only available to individuals who obtain health insurance coverage through the PPACA Marketplace.

■ ***Comment.*** If a taxpayer or a member of the taxpayer's household (for example, a spouse or dependent) obtained minimum essential coverage through the PPACA Health Insurance Marketplace, the Marketplace will provide a Form 1095-A, Health Insurance Marketplace Statement. Form 1095-A is an information return that contains the health coverage information (the name(s) of those covered, the cost of coverage, and the dates covered) necessary for individuals to calculate their Code Sec. 36B credit.

■ ***Comment.*** A taxpayer who claims a premium assistance tax credit for 2014 must file Form 1040, Form 1040A, or Form 1040NR. Form 8962 filers cannot file Form 1040EZ, 1040NR-EZ, Form 1040-SS, or Form 1040-PR.

Line 61, Individual shared responsibility payment. Beginning in 2014, all individuals must carry minimum essential health coverage—unless exempt—or make a shared responsibility payment. The individual responsibility payment is made with his or her tax return.

■ ***Reminder.*** Minimum essential coverage includes employer-sponsored coverage, COBRA coverage, coverage obtained through the PPACA Marketplace, health insurance provided through a student health plan, Medicare Part A coverage, Medicaid, Children's Health Insurance Program (CHIP), and most types of TRICARE coverage.

Individuals report their coverage on Form 1040, Line 61, Health care: individual responsibility. Individuals who had minimum essential coverage for the entire 2014 tax year check the box on Line 61 next to the words, "Full-year coverage."

If an individual did not obtain minimum essential coverage for the full-year, but qualified for an exemption, that individual

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Washington Report

by the CCH Washington News Bureau

Obama releases FY 2016 budget

President Obama proposed a $3.99 trillion budget for fiscal year (FY) 2016. The proposal includes tax reforms, tax simplification and revenue raisers. According to the White House, significant new revenue would be generated by a tax on foreign earnings, with the funds being used for infrastructure spending. The President also called for an increase in funding for the IRS. *For more details and analysis of the President's FY 2016 budget see the lead article in this week's newsletter and a special Briefing on IntelliConnect.*

Hire More Heroes bill moves forward

The Senate Finance Committee (SFC) on January 28 approved the Hire More Heroes Bill (HR 22). The bill generally exempts employees who have U.S. Department of Defense (DOD) health coverage from classification as eligible employees for purposes of the employer mandate under the Patient Protection and Affordable Care Act. Committee members proposed 27 amendments, with most of them relating to veterans' healthcare and employment issues, but none were offered up for a vote. The House approved the bill on January 6 by a vote of 412 to 0.

SFC ranking member Ron Wyden, D-Ore., emphasized that there are "a collection of proven, bipartisan proposals that would spur hiring of veterans and provide a boost for the nation's economy." He cited the Work Opportunity Tax Credit (WOTC) as an example of bipartisan cooperation for veterans.

Hatch, SFC Republicans question IRS service cuts

Senate Finance Committee Chair Orrin Hatch, R-Utah, along with all SFC Republicans, sent a letter on January 29 to IRS Commissioner John Koskinen questioning his warnings about service cuts due to budgetary constraints. In recent weeks, Koskinen has said that the IRS may have to delay taxpayer protections against identity theft; not replace the agency's aging information technology systems; delay refunds, and reduce telephone assistance to taxpayers. Koskinen also said he is exploring employee furlough days to save money.

"These actions, exacerbated by increasingly complicated tax compliance requirements under the Affordable Care Act, threaten to leave taxpayers with the worst tax filing season in recent memory," wrote the senators. The lawmakers listed several ways in which they felt the IRS had engaged in wasteful and low-priority spending, such as the payment of millions of dollars in bonuses and given tens of thousands of paid vacation hours to employees with recently substantiated conduct issues and disciplinary actions, including bonuses to 1,100 employees owing back taxes.

Wyden outlines tax reform principles

Senate Finance Committee (SFC) ranking member Ron Wyden, D-Ore., on January 29 outlined principles for tax reform. "As we move forward with pursuit of comprehensive tax reform, it is critical that we establish clear goals, outline transparent principles, create a process framework and come to the table willing to find common ground," Wyden wrote in a letter to SFC Chair Orrin Hatch, R-Utah.

The first priority that he listed was that the tax reform process would move through regular order and not reconciliation, which some Republicans have mentioned as a way to move tax legislation through Congress. The second principle was that any reforms to the Tax Code are more progressive than what is currently in place to help middle-income taxpayers. Any successful tax reform proposal must have a firm focus on supporting domestic jobs, and tax reform should be focused on providing a revenue base that is adequate in meeting the country's needs for investing in infrastructure, protecting Social Security and providing quality education, he added. Wyden also called for fiscal prudence and international competitiveness.

Senate bill would repeal employer mandate

The leaders of the Senate Finance Committee (SFC), Orrin Hatch, R-Utah, and the Senate Health, Education, Labor and Pensions (HELP) Committee, Lamar Alexander, R-Tenn., on January 29 introduced the American Job Protection Bill, which would repeal the employer mandate under the Patient Protection and Affordable Care Act (PPACA). The lawmakers were joined by 26 senators in cosponsoring the bill.

"The employer mandate continues to hinder job-creation and growth, and the best action Washington can take is to repeal it entirely," Hatch said in a statement. President Obama has said he will veto any legislation that weakens the PPACA.

IRS observes EITC awareness day

The IRS observed earned income tax credit (EITC) awareness day on January 30. "About four out of five eligible workers and families get the credit they earned. That leaves millions missing the credit every year," IRS Commissioner John Koskinen said in Washington, D.C. "It's an important credit and one of the government's best tools to fight poverty."

The amount of EITC varies depending on income, family size and filing status. Last year, almost 28 million eligible workers and families received a total of $66 billion, with an average credit amount of $2,400, the IRS reported. The credit is refundable, so eligible individuals may get a refund from the IRS even if they owe no tax or had no taxes withheld.

Practitioners' Corner

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must report and/or claim the exemption by filing Form 8965, Health Coverage Exemptions, along with his or her return.

- ***Comment.*** Different types of exemptions must be obtained in different ways. Some exemptions are available through the PPACA Marketplace, others by filing a return, and some both ways. Exemptions obtained through the PPACA Marketplace are reported on Part I of Form 8965. Other exemptions may be claimed directly on Form 8965.
- ***Comment.*** Page two of the Instructions for Form 8965 contains a detailed list of exemptions with directions for how to claim them.

If an individual owes an individual shared responsibility payment because she did not obtain minimum essential coverage for the full year and does not qualify for an exemption, that individual must calculate the payment amount and enter it onto Line 61.

- ***Comment.*** For 2014, the individual shared responsibility payment is 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 PPACA Marketplace in 2014. For 2014, the annual national average premium for a bronze level health plan available through the PPACA 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).

Other items to note on the 2014 Form 1040 include:

Line 21, Other income. In January 2014, the IRS issued Notice 2014-7, which provides that certain "qualified Medicaid waiver payments" received by a taxpayer for caring for someone living in her home may be excluded from gross income.

Line 23, Educator expenses (Teachers' classroom expense deduction). The Tax Increase Prevention Act of 2014 (TIPA) extended the above-the-line deduction for qualified eligible educator expenses through 2014.

Line 26, Moving expenses. The standard mileage rate for moving expenses for 2014 is 23.5 cents-per-mile.

Line 34, Tuition and fees deduction. TIPA extended the above-the-line deduction for higher education qualified tuition and related expenses through 2014. Taxpayers claiming the higher education tuition and fees deduction must attach Form 8917, Tuition and Fees Deduction.

Line 45, Alternative minimum tax. The Instructions for 2014 Form 1040 include a new worksheet that taxpayers may use to see whether they must complete Form 6251, Alternative Minimum Tax—Individuals. The AMT exemption amounts for 2014 are $52,800 for single individuals, $82,100 for married couples filing a joint return and widow(er)s, and $41,050 for married couples filing separate returns.

Line 76, Direct Deposit. A maximum of three tax refunds may be directly deposited to a single financial account or prepaid debit card. After this limit is exceeded, the IRS will send paper checks.

Schedule A, Itemized Deductions

Medical and dental expenses, Line 1. For 2014, the standard mileage rate for medical purposes is 23.5 cents per mile.

- ***State and local sales taxes, Line 5b.*** TIPA extended the state and local sales tax deduction through 2014. Despite the late passage of TIPA, the IRS wasted no time in placing the 2014 Optional State Sales Tax Tables in the current 2014 Instructions for Schedule A (Form 1040).

Limit on itemized deductions, Line 21. Deductions for taxpayers with adjusted gross incomes above certain amounts may be reduced: $254,200 for single individuals, $305,050 for married couples filing a joint return or a surviving spouse, $152,525 for married couples filing separate returns, and $279,650 for a head of household.

Schedule B, Interest And Ordinary Dividends

Excludable interest on series EE and I U.S. savings bonds, Line 3. For 2014, the phase-out of the exclusion for education related savings bond interest begins at modified adjusted gross income (MAGI) above $76,000 for single individuals and $113,950 for married couples filing a joint return.

Schedule C, Profit Or Loss From Business

Car and truck expenses, Part II, Line 9. For 2014, the standard mileage rate for use of a vehicle is 56 cents-per-mile for business miles driven.

- ***Comment.*** The standard mileage rate is also used by some taxpayers to complete Form 1040, Schedule E, Supplemental Income And Loss.

Depreciation and section 179 expense deduction, Part II, Line 13. TIPA extended the enhanced Code Sec. 179 dollar limit and investment limit through 2014. The dollar limit and investment limit are at $500,000 and $2 million, respectively.

- ***Comment.*** TIPA also extended 50 percent bonus depreciation through 2014 (through 2015 for certain longer-lived and transportation property).
- ***Comment.*** Taxpayers must complete and attach Form 4562, Depreciation and Amortization, to their Schedule C and tax return if they claim: Depreciation on property placed in service during 2014, depreciation on listed property, regardless of the date it was placed in service; or a Code Sec. 179 expense deduction.

Schedule D, Capital Gains And Losses

Form 1099-B. For 2014, the IRS redesigned Form 1099-B, Proceeds From Broker and Barter Exchange Transactions, so that the information reported in its boxes is numbered to match the corresponding line and column on Form 8949, Sales and Other Dispositions of Capital Assets. In addition, the IRS added a new box at the top of Form 1099-B (labeled "Applicable check box on Form 8949") that tells taxpayers which box they must check when completing Form 8949.

Compliance Calendar

■ February 6
Employers deposit Social Security, Medicare, and withheld income tax for January 31, February 1, 2, and 3.

■ February 10
Employees who received $20 or more in tips during January report them to their employers using Form 4070.

■ February 11
Employers deposit Social Security, Medicare, and withheld income tax for February 4, 5, and 6.

■ February 13
Employers deposit Social Security, Medicare, and withheld income tax for February 7, 8, 9, and 10.

■ February 17
Employees wishing to continue or update payroll withholding exemptions provide employers with a new Form W-4, Employee's Withholding Allowance Certificate.

■ February 19
Employers deposit Social Security, Medicare, and withheld income tax for February 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.

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Conferences

February 10: The Pennsylvania Institute of CPAs is holding a conference in Philadelphia on "Understanding and Implementing the New Repair/Capitalization Regulations in 2014." For more information, visit *www.picpa.org*.

February 10–11: The American Institute of Certified Public Accountants (AICPA) holds a conference in Atlanta. The theme of the conference is a "Roadmap for Profitably Moving Your Client Accounting Services Practice to the Cloud." Visit *www.cpa2biz.com* for more information. The same conference will be held in New York City March 10-11.

February 12: Wolters Kluwer, CCH presents a full-day webinar, "New IRS Tax Accounting Method Change Procedures: Inside Rev. Procs. 2015-13 and 2015-14" that covers the 'why, what, when, and how' on new Rev. Procs. 2015-13 and 2015-14 with a focus on the tangible property regulation (TPR) changes. To register, visit *www.krm.com/cch* or call (800) 775-7654.

February 12–13: The Tax Council Policy Institute holds its 16th Annual Tax Policy and Practice Symposium in Washington, D.C. The theme of the conference is "How Taxes Matter: The Globalization of Tax Policy and Implications for U.S. Economic Growth and Investment." Topics include U.S. corporate tax reform, BEPS, value-added taxes, and globalization of tax policy. For more information, visit *www.tcpi.org*.

February 16: Wolters Kluwer, CCH presents a full-day webinar, "Tangible Property Regulations - Understanding Capitalization vs. Repair and Maintenance" that covers what is a restoration, adaptation, betterment, or improvement, as well as related other important issues for businesses to known now that the new regs are finalized. To register, visit *www.krm.com/cch* or call (800) 775-7654.