Current Federal Tax Developments

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SECTION: SCAMS
IRS RESTARTS GET TRANSCRIPT ONLINE PROGRAM WITH MORE RIGOROUS SCREENING OF USERS

Citation: News Release IR-2016-85, 6/7/16, Website Announcement, 8/15/16

The IRS has relaunched the "Get Transcript" online service with what the agency claims is a more rigorous process than the one that previously existed (News Release IR-2016-85). In May of 2015 the IRS announced that it had discovered there had been unauthorized access to taxpayer's transcript via the "Get Transcript" online service. While the IRS initially estimated the unauthorized access to involve 100,000 taxpayers, by February of 2016 that estimate has ballooned to over 720,000 taxpayers.

While the unauthorized parties were able to access about ½ of the accounts they tried to break into, even under the old system many legitimate taxpayers were unable to complete the process. As would be expected, with the IRS tightening controls on who can get it, even more taxpayers will likely find themselves unable to answer the questions—and some will simply be barred from accessing the transcript online due to the new requirements.

The News Release Notes:

> While some taxpayers may now find it more difficult to authenticate their identities with this strengthened process, the IRS is committed to making sure everyone accessing the site will be able to do so in a safe and secure way. The IRS continues to support multiple options for those taxpayers who may be unable to access online features or who prefer to obtain information in more traditional ways. These options currently include ordering transcripts online or by phone for receipt by mail, which typically are delivered to the address of record within five to 10 days. The IRS continues to look for ways to expand options for all taxpayers.

"More difficult" is, in reality, an understatement of the problem. As the IRS describes the process:

> To access the new Get Transcript Online feature, taxpayers must have an email address, a text-enabled mobile phone and specific financial account information, such as a credit card number or certain loan numbers. Taxpayers who registered using the older process will need to re-register and strengthen their authentication in order to access the tool. As part of the new multi-factor process, the IRS will send verification, activation or security codes via email and text. The IRS warns taxpayers that it will not initiate contact via text or email asking for log-in information or personal data. The IRS texts and emails will only contain one-time codes.

The fact sheet issued with the News Release indicated that the "text enabled" smartphone must be one registered on a post-paid plan, so that taxpayers that have a phone under a pre-paid plan would not eligible. The reason for that restriction is because carriers do verifications and credit checks on individuals obtaining post-paid plans, but do not do that level of investigation on prepaid plans. Thus it would be possible to obtain a prepaid (also referred to in slang as "burner") phone plan in a mark's name to receive the text message if the IRS allowed the prepaid plans phones to work.

Unfortunately, the changing nature of the mobile phone market has made it more likely that even those with stellar credit may turn to prepaid plans. As carriers generally no longer subsidize the purchase of a phone, but rather demand that customers pay the full price for the phone, there's no longer the same incentive to sign up for a post-paid contract to obtain a high end phone at a low (apparent) cost.

And, as the IRS notes, the questions need to be made more difficult in order to (hopefully) remove the ability of the criminals to be able to uncover the answers through either legitimate or less savory sources.

After the Social Security Administration received complaints that many seniors did not have cell phones to be used for a similar program, the administration backed off the cell phone requirement. In August the IRS also modified the phone requirement.

In a statement issued August 19 the IRS indicated taxpayers will now have the option to receive the activation code by mail, being sent to the taxpayer's address of record instead of to the cellular phone. The IRS now indicates on its website "Secure Access: How to Register for Certain Online Self-Help Tool:"

> If you have a pay-as-you-go mobile phone or a business/family plan mobile phone not associated with your name, you may request that we mail an activation code to the address we have on file for you. You still must have a text-enabled, U.S.-based phone to receive a security code text that completes the validation process and allows returning users to access their accounts.

While the notice does not say that the returning security code can go to a prepaid phone, it would appear that such phones will now be sufficient for this purpose. The use of the post-paid phones initially was to verify the person creating the account was the taxpayer. Presumably if the taxpayer is now properly verified via a letter with the code, the IRS believes using a prepaid phone for two factor authentication no longer poses a risk to losing control of the account.

Whether this will be sufficient to "lock down" the Get Transcript program remains to be seen. As the IRS admits in this news release:

> "The incident with Get Transcript Online illustrates a wider truth about identity theft in general, which is that there are no perfect systems," Koskinen said. "No one, either in the public or private sector, can give an absolute guarantee that a system will never be compromised. For that reason, we continue our comprehensive efforts to update the security of our systems, protect taxpayers and their data and investigate crimes related to stolen identity refund fraud."

The Fact Sheet (FS-2016-20) issued with the News Release contains the following details on accessing and using the system:

> **Here's what new users need to get started:**
>
> - A readily available email address;
> - Your Social Security number or Individual Tax Identification Number;
> - Your filing status and address from your last-filed tax return;
> - Access to certain account numbers for either:
> - credit card, or
> - home mortgage loan, or
> - home equity (second mortgage) loan, or
> - home equity line of credit (HELOC), or
> - car loan
> - A readily available mobile phone. Only U.S-based mobile phones may be used. Your name must be associated with the mobile phone account. Landlines, Skype, Google Voice or similar virtual phones as well as phones associated with pay-as-you-go plans cannot be used;
>
> If you have a "credit freeze" on your credit records through Equifax, it must be temporarily lifted before you can successfully complete this process.

Because this process involves verification using financial records, there may be a "soft notice" placed on your credit report. This notice does not affect your credit score.

To securely access Get Transcript Online, first-time users must:

- Submit their name and email address to receive a confirmation code;
- Enter the emailed confirmation code;
- Provide their SSN, date of birth, filing status and address on the last filed tax return;
- Provide some financial account information for verification such as the last eight digits of their credit card number, car loan number, home mortgage account number, or home equity (second mortgage) loan number;
- Enter a mobile phone number to receive a six-digit activation code via text message;
- Enter the activation code;
- Create username and password, create a site phrase and select a site image.

Returning taxpayers who have not completed the new secure access process:

- Log in with an existing username and password;
- Submit financial account information for verification, for example, the last eight digits of a credit card number or car loan number or home mortgage account number or home equity (second mortgage) loan account number;
- Submit a mobile phone number to receive an activation code via text;
- Enter the activation code.

Returning taxpayers who have completed the new secure access process:

- Log in with an existing username and password;
- Receive a security code text via mobile phone provided with account set up;
- Enter the security code into secure access.

SECTION: 31 U.S.C. 9701
IRS PROPOSES TO RAISE FEES FOR INSTALLMENT AGREEMENTS AND REVISE LIST OF CHARGES

Citation: REG-108792-16, 8/19/16

The IRS is proposing to increase fees for entering into installment agreements and add new levels for determining a fee in proposed regulations (REG-108792-16). The proposed changes would take effect on January 1, 2017.

The IRS explained that the fees in place today were set below what it costs the IRS to process the installment agreements. The IRS explains:

> Historically, the IRS charged a user fee that recovered less than the full cost of an installment agreement to make the service more accessible to a broader range of taxpayers. However, in light of constraints on IRS resources for tax administration, the Treasury Department and the IRS have determined that it is necessary to recoup the full costs of the installment agreement program.

The current fees are outlined by the IRS:

> Under § 300.1, the IRS currently charges three rates for installment agreements. The user fee, in general, is $120 for an installment agreement. The user fee is reduced to $52 for a direct debit installment agreement, which is an agreement whereby the taxpayer authorizes the IRS to request the monthly electronic transfer of funds from the taxpayer's bank account to the IRS. The user fee is $43 notwithstanding the method of payment if the taxpayer is a low-income taxpayer, as defined below.

The IRS outlines the following proposed fees:

- **Regular Installment Agreements** -- A taxpayer contacts the IRS in person, by phone, or by mail and sets up an agreement to make manual payments over a period of time either by mailing a check or electronically through the Electronic Federal Tax Payment System (EFTPS). The proposed fee for entering into a regular installment agreement is $225.
- **Direct Debit Installment Agreements** -- A taxpayer contacts the IRS by phone or mail and sets up an agreement to make automatic payments over a period of time through a direct debit from a bank account. The proposed fee for entering into a direct debit installment agreement is $107.
- **Online Payment Agreements** -- A taxpayer sets up an installment agreement through http://www.irs.gov and agrees to make manual payments over a period of time either by mailing a check or electronically through the EFTPS. The proposed fee for entering into an online payment agreement is $149.
- **Direct Debit Online Payment Agreements** -- A taxpayer sets up an installment agreement through http://www.irs.gov and agrees to make automatic payments over a period of time through a direct debit from a bank account. The proposed fee for entering into a direct debit online payment agreement is $31.
- **Restructured/Reinstated Installment Agreements** -- A taxpayer modifies a previously established installment agreement or reinstates an installment agreement on which the taxpayer has defaulted. The proposed fee for restructuring or reinstating an installment agreement is $89.
- **Low-Income Rate** -- A rate that applies when a low-income taxpayer enters into any type of installment agreement, other than a direct debit online payment agreement, and when a low-income taxpayer restructures or reinstates any installment agreement. A low-income taxpayer is a taxpayer that has income at or below 250 percent of the dollar criteria established by the poverty guidelines updated annually in the Federal Register by the U.S. Department of Health and Human Services. Section 300.1(b)(2). The proposed low-income rate is $43.

SECTION: 162
SHARING ECONOMY TAX CENTER WEBSITE CREATED BY IRS

Citation: Sharing Economy Tax Center, IRS Website, 8/22/16

With the growth of the "sharing economy" involving organizations like Uber, Lyft and Airbnb, the IRS has determined there is a need for guidance for individuals who are involved in providing such services.

Many of these individuals have not previously operated a business, nor may they even realize that they truly are operating a business that will trigger special tax issues and obligations.

As the IRS describes the issue on their site:

> An emerging area of activity in the past few years, the sharing economy has changed how people commute, travel, rent vacation places and perform many other activities. Also referred to as the on-demand, gig or access economy, sharing economies allow individuals and groups to utilize technology advancements to arrange transactions to generate revenue from assets they possess - (such as cars and homes) - or services they provide - (such as household chores or technology services). Although this is a developing area of the economy, there are tax implications for the companies that provide the services and the individuals who perform the services

To assist these individuals the IRS has created a Sharing Economy Tax Center on their website.

The site contains information and links related to the following items:

Issues for Individuals Performing Services

- Filing Requirements
- Employee or Independent Contractor
- Tax Payments, Including Estimated Tax Payments
- Self-Employment Taxes
- Depreciation
- Rules for Home Rentals
- Business Expenses

Employment Tax Issues for the Companies Providing Services

- Determining Whether the Individuals Providing Services are Employees or Independent Contractors
- Employer/Payer Employment Tax Obligations

This site can provide a useful resource both to refer clients to who have begun offering services via providers such as Uber and for advisers to understand issues that arise and the IRS's view on the handling of such issues.

SECTION: 408
IRS PROVIDES FOR AUTOMATIC QUALIFIED PLAN/IRA LATE ROLLOVER RELIEF

Citation: Revenue Procedure 2016-47, 8/24/16

The IRS, likely hoping to reduce the number of letter ruling requests related to late IRA rollovers, has released Revenue Procedure 2016-47 that provides automatic relief for certain late rollovers of IRAs and qualified plan distributions. The procedure generally allows a plan administrator, IRA custodian or trustee to rely upon a certification from a taxpayer in accepting a rollover from a taxpayer that he/she meets certain requirements

qualifying for automatic relief from late rollovers. However, if the administrator, custodian or trustee is aware the certification is not correct, he/she will not be allowed to rely on the certification.

Previously Revenue Procedure 2013-16 provided for automatic relief only in limited situations related to errors committed by financial institutions. Otherwise a taxpayer generally had to apply and pay for a private letter ruling granting relief.

Under the new procedure a taxpayer makes a certification meeting certain requirements outlining the taxpayer's qualification for automatic relief under this procedure. The IRS is providing a model certification, found at the end of this article, the taxpayer may use word for word. Otherwise the taxpayer must provide a letter that is materially similar in all respects.

The taxpayer issuing the certification may not have been previously denied relief by the IRS in a waiver request for the distribution in question.

The taxpayer must have missed the rollover deadline due to one of the following reasons:

> (a) an error was committed by the financial institution receiving the contribution or making the distribution to which the contribution relates;
>
> (b) the distribution, having been made in the form of a check, was misplaced and never cashed;
>
> (c) the distribution was deposited into and remained in an account that the taxpayer mistakenly thought was an eligible retirement plan;
>
> (d) the taxpayer's principal residence was severely damaged;
>
> (e) a member of the taxpayer's family died;
>
> (f) the taxpayer or a member of the taxpayer's family was seriously ill;
>
> (g) the taxpayer was incarcerated;
>
> (h) restrictions were imposed by a foreign country;
>
> (i) a postal error occurred;
>
> (j) the distribution was made on account of a levy under § 6331 and the proceeds of the levy have been returned to the taxpayer; or
>
> (k) the party making the distribution to which the rollover relates delayed providing information that the receiving plan or IRA required to complete the rollover despite the taxpayer's reasonable efforts to obtain the information.

The taxpayer must make the contribution to the IRA as soon as practicable after the reasons stated no longer prevent the taxpayer from the completing the rollover. If the taxpayer completes the rollover within 30 days after the reasons no longer prevent the rollover.

The Form 5498 will be modified to indicate that the custodian has accepted a rollover after the 60 day deadline.

The IRS explains the affect on the taxpayer as follows:

> A self-certification is not a waiver by the IRS of the 60-day rollover requirement. However, a taxpayer may report the contribution as a valid rollover unless later informed otherwise by the IRS. The IRS, in the course of an examination, may consider whether a taxpayer's contribution meets the requirements for a waiver. For example, the IRS may determine that the requirements for a waiver were not met because of a material misstatement in the self-certification, the reason or reasons claimed by the taxpayer for missing the 60-day deadline did not prevent the taxpayer from completing the rollover within 60 days following receipt, or the taxpayer failed to make the contribution as soon as practicable after the reason or reasons no longer prevented the taxpayer from making the contribution. In such a case,

the taxpayer may be subject to additions to income and penalties, such as the penalty for failure to pay the proper amount of tax under § 6651.

The IRS may also grant a late rollover waiver during the course of an exam after determining the taxpayer meets the requirements for relief.

The IRS example certification for relief is provided below:

Certification for Late Rollover Contribution

Name
Address
City, State, ZIP Code

Date: _____

Plan Administrator/Financial Institution
Address
City, State, ZIP Code

Dear Sir or Madam:

Pursuant to Internal Revenue Service Revenue Procedure 2016-47, I certify that my contribution of $ [ENTER AMOUNT] missed the 60-day rollover deadline for the reason(s) listed below under Reasons for Late Contribution. I am making this contribution as soon as practicable after the reason or reasons listed below no longer prevent me from making the contribution. I understand that this certification concerns only the 60-day requirement for a rollover and that, to complete the rollover, I must comply with all other tax law requirements for a valid rollover and with your rollover procedures.

Pursuant to Revenue Procedure 2016-47, unless you have actual knowledge to the contrary, you may rely on this certification to show that I have satisfied the conditions for a waiver of the 60-day rollover requirement for the amount identified above. You may not rely on this certification in determining whether the contribution satisfies other requirements for a valid rollover.

Reasons for Late Contribution

I intended to make the rollover within 60 days after receiving the distribution but was unable to do so for the following reason(s) (check all that apply):

___ An error was committed by the financial institution making the distribution or receiving the contribution.

___ The distribution was in the form of a check and the check was misplaced and never cashed.

___ The distribution was deposited into and remained in an account that I mistakenly thought was a retirement plan or IRA.

___ My principal residence was severely damaged.

___ One of my family members died.

___ I or one of my family members was seriously ill.

___ I was incarcerated.

___ Restrictions were imposed by a foreign country.

___ A postal error occurred.

___ The distribution was made on account of an IRS levy and the proceeds of the levy have been returned to me.

___ The party making the distribution delayed providing information that the receiving plan or IRA required to complete the rollover despite my reasonable efforts to obtain the information.

Signature

I declare that the representations made in this document are true and that the IRS has not previously denied a request for a waiver of the 60-day rollover requirement with respect to a rollover of all or part of the distribution to which this contribution relates. I understand that in the event I am audited and the IRS does not grant a waiver for this contribution, I may be subject to income and excise taxes, interest, and penalties. If the contribution is made to an IRA, I understand you will be required to report the contribution to the IRS. I also understand that I should retain a copy of this signed certification with my tax records.

Signature: _____

SECTION: 1366
TAXPAYER UNABLE TO PROVE BASIS IN STOCK, HAS TAXABLE GAIN ON DISTRIBUTIONS

Citation: Power et ux. v. Commissioner, T.C. Memo. 2016-157, 8/21/16

A taxpayer who was unable to establish the basis of his stock in an S corporation found himself stuck with paying tax on distributions from the corporation in the case of *Power et ux. v. Commissioner*, T.C. Memo. 2016-157.

The taxpayer was the sole shareholder of an S corporation which operated a real estate brokerage firm. The Court described his accounting systems and methods as follows:

> In 2007 Power Realty had two employees and used Paychex as its third-party payroll provider. Debbie Berger, a secretary who is not a certified public accountant (C.P.A.), kept and maintained the books and records for Power Realty. In 2011 Power Realty let Ms. Berger go and downsized to a smaller office suite on Hosbrook Road in Cincinnati, Ohio. For the taxable years 2007-11 Mr. Power maintained "Itemized Profit and Loss" and "Transactions by Account" documents for Power Realty. Mr. Power has no formal training in tax or accounting.

While the court does not say so explicitly, the titles of the documents Mr. Power maintained suggests he was using the personal finance software *Quicken* to handle the record-keeping for his business.

Mr. Power did employ tax professionals to prepare his tax returns as described below:

> Power Realty filed Forms 1120S, U.S. Income Tax Return for an S-Corporation, for the taxable years 1993-2011, which were prepared by either Attorney C. Christopher Muth or C.P.A. Andrew J. Bucher. When Mr. Muth prepared returns, Mr. Power would typically provide him with one or two sheets of paper with handwritten income and expense categories and corresponding amounts. Mr. Power would provide underlying documentation to Mr. Muth "[o]ccasionally, but not very frequently." The record does not establish whether Mr. Power followed a similar protocol for tax returns that Mr. Bucher prepared.

As well, the Court noted that Mr. Power was not drawing a salary from the corporation for his services, noting:

> Power Realty compensated Mr. Power through distributions rather than wages or salary. However, Power Realty did not report any distributions to Mr. Power on its Forms 1120S for the taxable years 2007-11. Mr. Power used funds from Power Realty to pay personal living expenses of petitioners for each of the taxable years 2007-11. Furthermore, during the taxable years 2007-11 Power Realty claimed deductions on its Forms 1120S for certain personal living expenses of Mr. Power.

The corporation made distributions to the taxpayer "of $359,860 for 2007; $60,173 for 2008; $221,829 for 2010; and $189,447 for 2011." The IRS determined that the taxpayer had zero basis in his S corporation as of

January 1, 2007. Mr. Power claimed he had a basis of $510,216 as of January `1, 2007 and no distributions in excess of basis were made.

The problem the taxpayer faced was that he bore the burden of proving his basis—and the records he had did not provide reasonable evidence of the existence of the claimed basis.

First, the calculation that was provided was not one that had been maintained over the years but rather an attempt at reconstruction of basis undertaken due to the Court case:

> Mr. Power did not maintain a basis schedule for his Power Realty stock. To establish Mr. Power's basis in his Power Realty stock, petitioners offered Power Realty's Forms 1120S for the taxable years 1993-2011 and a reconstructed stock basis chart attached as an appendix to their posttrial brief.

Generally a taxpayer should maintain a record of his/her basis in the corporation on an ongoing basis in order to determine each year if distributions are in excess of basis from the S corporation. So, at this point, the taxpayer would seem to have, at best, "lucked" into not having a taxable distribution since the reconstructed basis seems to have been just enough to allow him to escape tax.

However, the Court did not find the information the taxpayer provided in support of this reconstruction to be adequate to support the calculation of basis:

> To begin with, the Forms 1120S do not include sufficient information for us to establish Mr. Power's basis in Power Realty. See *Fehlhaber v. Commissioner*, 94 T.C. 863, 869 (1990), *aff'd*, 954 F.2d 653 (11th Cir. 1992). It is also unclear how petitioners calculated Mr. Power's stock basis in Power Realty using Forms 1120S given that Power Realty's income and expenses were improperly divided between Mr. Power's Schedules C and Power Realty's Forms 1120S. Further, petitioners stipulate that Mr. Power was compensated by Power Realty through distributions (not wages or salary) and that petitioners used Power Realty's checking account to pay substantial personal expenses during the taxable years 2007-11. On the basis of the record before us, petitioners have not established that Mr. Power had basis in Power Realty stock or that he did not receive distributions from Power Realty as respondent determined in the notices of deficiency. Accordingly, we conclude that Mr. Power's adjusted stock basis in Power Realty was zero and that he received distributions from Power Realty as respondent determined in the notices of deficiency.

While this is clearly a "bad facts" case that most likely made the Court even more skeptical than it normally would be, fundamentally taxpayers must be aware that proving basis in S stock (or a partnership interest) does involve being able, if necessary, to reach back into the past to provide information to support the calculation—and that may need to be more than just copies of the original returns or K-1s, especially if the years under exam uncovers problems that may be reasonably be suspected to have also taken place in those earlier years.

SECTION: 5000A
AVERAGE MONTHLY BRONZE PREMIUM AMOUNTS FOR 2016 PUBLISHED TO BE USED IN COMPUTING CAP ON SHARED RESPONSIBILITY PAYMENTS

Citation: Revenue Procedure 2016-43, 8/19/16

In Revenue Procedure 2016-43 the IRS provided the 2016 monthly bronze premium amounts for use in computing the premium based limitations on the shared responsibility payments under IRC §5000A.

A shared responsibility payment is generally due for each month that a person fails to have minimum essential coverage for himself or herself or an individual they are eligible to claim as a dependent for tax purposes.

The initial monthly shared responsibility payment is 1/12 of the greater of:

- The flat dollar amount which is the lesser of
    - The applicable dollar amount for each member of the family ($695 for 2016, indexed for inflation for future years). For individuals under 18, the applicable dollar amount is ½ of these amounts
    - 300% of the applicable dollar amount for the year
- A percentage of the taxpayer's household income, set at 2.5%

However, that payment is also capped to be no greater than the average monthly cost of bronze level coverage offered through exchanges that would provide coverage for the taxpayer and the "family" (those whom the taxpayer could claim as a dependent) for the period in question. The cost is taken by multiplying the average monthly premium cost (as published annually by the IRS) by the number of family members (but limited to no more than 5).

The average monthly bronze premium amounts computed by the IRS are:

	2016
Individual amount	$ 223
Maximum family amount	1,115