Current Federal Tax Developments

Week of January 18, 2021

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ACCOUNTING
CONTINUING EDUCATION

KAPLAN

CURRENT FEDERAL TAX DEVELOPMENTS
WEEK OF JANUARY 18, 2021

Published in 2021 by Kaplan Financial Education.

Printed in the United States of America.

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Kaplan Financial Education

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SECTION: 61
AMOUNTS ADVANCED FROM ONE PARTNER WERE DEBTS OF THE PARTNERSHIP, OTHER PARTNERS HAD CANCELLATION OF INDEBTEDNESS INCOME

Citation: Michael Hohlet ux. et al. v. Commissioner, TC Memo 2021-5, 1/13/21

The partnership in the case of *Michael Hohlet ux. et al. v. Commissioner*, TC Memo 2021-5[1] attempted to claim that amounts it received from a partner it had treated in prior years as loans were actually capital contributions in the final year of the partnership. However, both the IRS and the Tax Court did not agree, finding that amount represented cancellation of indebtedness income in the final year of the partnership.

Three of the partners had contributed no funds to start the partnership, but were paid guaranteed payments each year. They each were treated as having a 30% interest. Eduardo Rodriguez put up $265,000 of cash for a 10% interest. In later years, Mr. Rodriguez advanced the partnership money that was treated as loans to the partnership, money used for partnership operations.

The partnership lost money each year, with each of the partners who had contributed no cash or property to the partnership being allocated a portion of the debt from Mr. Rodriguez as recourse debt on their K-1, using that basis to claim their share of the losses.

The partnership ceased operations in 2012. As the opinion describes the facts:

> Echo's 2012 Form 1065 was marked as its final return. Echo reported no income, deductions, losses, or guaranteed payments. Echo's liability increased by $14,184, to $653,506, but unlike past years' liabilities the amount was recorded as "Loans from partners", not as "Other liabilities."
>
> The Schedules K-1 for 2012 reflected Echo's limited operations that year. Echo did not allocate any income, losses, deductions, or guaranteed payments to Mr. Hohl, Mr. Blake, or Mr. Bowles. Their Schedules K-1 each reported negative capital account balances, unchanged from 2011, of $178,210. Mr. Rodriguez' Schedule K-1 reported a negative capital account balance of $59,404, but no longer reported any share of partnership liabilities.
>
> …

[1] *Michael Hohlet ux. et al. v. Commissioner*, TC Memo 2021-5, January 13, 2021, https://www.taxnotes.com/research/federal/court-documents/court-opinions-and-orders/partners-received-income-from-discharge-of-partnership-debt/2drcj (retrieved January 15, 2021)

> In summary, Echo's 2012 return showed a liability remaining on its balance sheet of $653,506, but no partner reported an allocation of any share of that liability. The partnership did not report any income, such as income from the discharge of indebtedness, nor did Echo allocate to any partner any share of any such income. Mr. Hohl and Mr. Blake reported no partnership income for 2012.[2]

The IRS had issues with this final return that simply left the unpaid liability by itself on the final balance sheet. For the two taxpayers in this case, the opinion notes:

> In each notice the Commissioner adjusted the taxpayer's Schedule E income upward by $178,210, the amount of the partner's negative capital account balances, representing the partner's share of cancellation of indebtedness income. The explanation of the adjustment stated: "It is determined that your share of income from the partnership known as Echo Mobile Marketing for taxable year 2012 is $178,210.00 instead of $0.00 as reported on your return. Therefore, taxable income is increased $178,210.00 for tax year ended December 31, 2012." Each couple timely filed a petition with our Court.[3]

Since the IRS position was that there was cancellation of indebtedness income, the Tax Court first looked at whether the amounts advanced by Mr. Rodriguez were debts of the partnership or not. The taxpayers argued that Mr. Rodriguez had actually provided capital contributions.

The Court found that the amounts advanced were debts:

> We do not find credible petitioners' argument that Mr. Rodriguez made capital contributions. While the absence of a written loan document might support petitioners as to the first factor, the partners clearly intended to treat, and did treat, the amounts received from Mr. Rodriguez as loans.
>
> Echo's partners' actions suggest that they considered Mr. Rodriguez' cash infusions to be loans. Echo reported the amounts as liabilities each year it operated. The Schedules K-1 Echo sent to its partners reported the amounts as liabilities every year and allocated a share of those liabilities to each partner in 2009. Mr. Hohl and Mr. Blake each filed individual returns accepting and benefiting from their characterization of these amounts as debt. If Mr. Rodriguez had made a capital contribution of $265,000 in 2009, paragraph 4.4 of the operating agreement would have required Mr. Rodriguez to include that contribution in his initial capital account balance. He did not do so. And according to the agreement, if the partnership needed additional capital contributions, Echo had to notify all partners in writing and give them an equal opportunity to contribute. We have no evidence of any such notices. The record also does not include any

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[2] *Michael Hohlet ux. et al. v. Commissioner*, TC Memo 2021-5, pp. 7-8

[3] *Michael Hohlet ux. et al. v. Commissioner*, TC Memo 2021-5, p. 8

> explanation as to why Mr. Rodriguez' ownership percentage did not change as a result of his supposed additional capital contributions. Mr. Rodriguez did not testify.
>
> As for the third factor, the record includes no evidence that Echo could not have obtained loans from third parties.
>
> The amounts Echo received from Mr. Rodriguez were loans.[4]

So now the question becomes if there was cancellation of debt income in 2012 or another year. The Court notes that the test for when such cancellation occurs is as follows:

> When a taxpayer realizes income from cancellation of indebtedness is a question of fact. Discharge of a debt occurs when it becomes clear that the debt will never be repaid. We look for "[a]ny 'identifiable event' which fixes the loss with certainty."[5]

The Tax Court determined that, in fact, 2012 was the year the cancellation of indebtedness took place:

> It became certain in 2012 that Echo would not repay its debt to Mr. Rodriguez, and thus Echo had income from the discharge of debt for that year. The partners testified that Echo would pay Mr. Rodriguez when the venture became profitable. When Echo ceased operations, it became clear it would never be profitable. Echo ceased operations when it filed its final return in 2012. Echo's termination in 2012 is when the debt became uncollectible.
>
> The Hohls and the Blakes argue that Echo ceased operations in 2011. But the partnership had ongoing activity in 2012, evidenced by Mr. Rodriguez' lending the partnership an additional $14,184 in that year. Echo therefore did not terminate in 2011.[6]

Being a partnership, the next question is how such income will be allocated among the partners. While the partnership had an operating agreement that purported to provide for how the income and losses would be allocated, the Tax Court found that operating agreement in fact had never been followed—and thus the allocations found in it did not have substantial economic effect:

> To have substantial economic effect, allocations must be consistent with the underlying economic arrangement of the partners. The allocations made by Echo's operating agreement (based on capital accounts) do not have substantial economic effect. In all other respects, the partnership and its partners shared items 30-30-30-10, instead of following the formula provided by the operating agreement. This course of conduct makes clear that Echo did not adhere to the

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[4] *Michael Hohlet ux. et al. v. Commissioner,* TC Memo 2021-5, pp. 11-12

[5] *Michael Hohlet ux. et al. v. Commissioner,* TC Memo 2021-5, p. 13

[6] *Michael Hohlet ux. et al. v. Commissioner*, TC Memo 2021-5, p. 14

> allocations in the operating agreement and instead allocated losses on the basis of the partners' 30%, 30%, 30%, and 10% ownership interests. The partners also did not follow the operating agreement's provisions for contributing capital or maintaining capital accounts.[7]

The Tax Court then determined the proper allocation, based on the partners' interests in the partnership:

> Because the allocations provided by the operating agreement do not have substantial economic effect, the partners' distributive shares of income are determined according to their interests in the partnership. A partner's interest in the partnership depends on the facts and circumstances.23 In these cases, during all four years Echo operated, it allocated losses according to the stated 30%, 30%, 30%, and 10% ownership interests. Allocation of the income in 2012 should follow the allocation of losses for each other year of the partnership's existence. Mr. Hohl and Mr. Blake should each have included a 30% share of the income from the discharge of indebtedness in their income for 2012.[8]

This case is an excellent example of what tends to happen to taxpayers whose view of the true nature of a transaction changes from year to year and ends up aligning with what happens to be the most favorable outcome in each year. Courts are skeptical of claims like the one we had in this case where, after relying on the treatment of the transaction as a loan for years to allow the partners to deduct the losses, the taxpayers attempt to argue for a different treatment in the one year that a loan treatment proves disadvantageous. And, most often, the Court rejects this change of treatment, forcing the taxpayers to live with the consequences of the view they had taken for years when that view was advantageous.

SECTION: 61
RELIEF GRANTED IN CERTAIN CASES ON VALUING PERSONAL USE OF EMPLOYER-PROVIDED AUTO FOR 2020 DUE TO PANDEMIC

Citation: Notice 2021-7, 1/4/21

In Notice 2021-7,[9] the IRS has granted relief to certain employers and employees using the automobile lease valuation rule to determine the value of an employee's personal use of an employer-provided automobile. The relief has been granted due to the impact of the COVID-19 pandemic.

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[7] *Michael Hohlet ux. et al. v. Commissioner*, TC Memo 2021-5, p. 15

[8] *Michael Hohlet ux. et al. v. Commissioner*, TC Memo 2021-5,

[9] Notice 2021-7, January 4, 2021, https://www.irs.gov/pub/irs-drop/n-21-07.pdf (retrieved January 4, 2021)

The relief is summarized in the Notice as follows:

> Due solely to the COVID-19 pandemic, if certain requirements are satisfied, employers and employees that are using the automobile lease valuation rule may instead use the vehicle cents-per-mile valuation rule to determine the value of an employee's personal use of an employer-provided automobile beginning as of March 13, 2020. For 2021, employers and employees may revert to the automobile lease valuation rule or continue using the vehicle cents-per-mile valuation rule provided certain requirements are met.[10]

The Problem

The Notice notes the problem that has occurred as many employers have shut down offices and had employees telework due to the COVID-19 pandemic:

> As a result of the pandemic, many employers suspended business operations or implemented telework arrangements for employees. Consequently, employers have indicated that business and personal use of employer-provided automobiles has been reduced for employees. However, due to the way in which the value of an employee's personal use of an employer-provided automobile is computed using the automobile lease valuation rule under section 1.61- 21(d), employers have noted a resulting increase in the lease value required to be included in an employee's income for 2020 compared to prior years.[11]

The key problem is that the overall value of the use of the vehicle is a fixed amount (ignoring any fuel paid for by the employer) under the lease valuation rule. So the amount the employee pays tax on is based on the *ratio* of personal use to overall use of the vehicle, as opposed to the amount of personal use. Thus, if the business use declines substantially, as it generally will during an extended period of having to isolate and conduct business remotely, the percentage of personal use may balloon even though the actual amount of personal use has not gone up—and, frankly, in 2020 due to lockdowns and social distancing, may very well have decreased.

Thus, the Notice points out:

> In contrast, determining the value of an employee's personal use of an employer-provided automobile using the vehicle cents-per-mile valuation rule results in income inclusion of only the value that relates to actual personal use, thereby providing a more accurate reflection of the employee's income in these circumstances.[12]

There are various restrictions on the ability to use the cents per mile rule in the regulations, and the regulations generally apply a consistency requirement on the

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[10] Notice 2021-7, I. PURPOSE

[11] Notice 2021-7, II. BACKGROUND

[12] Notice 2021-7, II. BACKGROUND

method used—taxpayers can't switch from the lease valuation method to the cents-per-mile method and back from year to year.

Relief

Section III of the Notice contains the relief provision, granting relief from the consistency rules found at Reg. §§1.61-27(d)(7) and 1.61-21(e)(5). The relief provides:

> Accordingly, an employer using the automobile lease valuation rule for the 2020 calendar year may instead use the vehicle cents-per-mile valuation rule beginning on March 13, 2020, notwithstanding the consistency rules in section 1.61-21(d)(7), if, at the beginning of the 2020 calendar year, the employer reasonably expected that an automobile with a fair market value not exceeding $50,400 would be regularly used in the employer's trade or business throughout the year, but due to the COVID-19 pandemic the automobile was not regularly used in the employer's trade or business throughout the year.[13]

Note that while the IRS has waived the consistency requirement, the fair market value of the vehicle limit still remains in place—so employees provided with a vehicle with fair market value in excess of $50,400 will still need to have their personal use valued under the standard lease valuation method.

The relief is also not for the entirety of 2020—rather the cents-per-mile rule can only be used beginning on March 13, 2020, the date that the National Emergency began. The Notice provides:

> For this purpose, the COVID-19 pandemic is considered to have commenced on March 13, 2020, the date of the President's emergency declaration. Therefore, employers that choose to switch from the automobile lease valuation rule to the vehicle cents-per-mile valuation rule in the 2020 calendar year must prorate the value of the vehicle using the automobile lease valuation rule for January 1, 2020, through March 12, 2020. Employers should multiply the applicable Annual Lease Value by a fraction, the numerator of which is the number of days during the period beginning on January 1, 2020, and ending on March 12, 2020 (72 days), and the denominator of which is 365.[14]

The choice by the employer to switch to the cents-per-mile rule is also binding on the employee (that is, the employee can't argue for an alternative value using the standard lease valuation rule).[15]

The IRS continues noting the options the employer will have for 2021:

> Further, notwithstanding the consistency rules in section 1.61-21(e)(5), employers that choose to switch from the automobile lease valuation rule to the vehicle cents-per-mile valuation rule during 2020 may revert

[13] Notice 2021-7, SECTION III. GRANT OF RELIEF

[14] Notice 2021-7, SECTION III. GRANT OF RELIEF

[15] Notice 2021-7, SECTION III. GRANT OF RELIEF

> to the automobile lease valuation rule for 2021, provided they meet the requirements of section 1.61-21(d), other than the consistency rules in section 1.61-21(d)(7). Alternatively, employers that choose to switch to the vehicle cents-per-mile valuation rule during 2020 may continue using that rule for 2021, provided they meet the requirements of section 1.61-21(e), other than the consistency rules in section 1.61-21(e)(5). Employees that use one of the special valuation rules for vehicles must use the same special valuation rule for vehicles that is used by their employer.[16]

Note, though, that if an employer wishes to return to the lease valuation rule, the employer must do so for 2021—otherwise the continued use of the cents-per-mile rule will be mandated.

> The consistency rules in section 1.61-21(e)(5) will apply as of January 1, 2021, as if January 1, 2021, were the first day the vehicle was used by the employee for personal use, and the consistency rules in section 1.61-21(d)(7) will apply as of January 1, 2021, as if January 1, 2021, were the first day the vehicle was made available to the employee for personal use. Accordingly, the special valuation rule used for 2021 must continue to be used by the employer and the employee for all subsequent years, except to the extent the employer uses the commuting valuation rule.[17]

Employers are directed to the following methods they can use to implement this change in method for 2020:

> Employers that originally used the automobile lease valuation rule to calculate the value of the personal use of an employer-provided automobile during 2020 and that want to instead begin using the vehicle cents-per-mile valuation rule during 2020 based on the relief provided in this notice may use the rules in Announcement 85-113 for reporting and withholding on taxable noncash fringe benefits, or the adjustment process under section 6413 or the refund claim process under section 6402 to correct any overpayment of federal employment taxes on these benefits (for information on these adjustment and refund claim processes, see the regulations under these sections, Rev. Rul. 2009-39, 2009-52 I.R.B. 951, section 13 of Publication 15 (Circular E), Employer's Tax Guide, and the Instructions for Form 941-X, Adjusted Employer's QUARTERLY Federal Tax Return or Claim for Refund).[18]

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[16] Notice 2021-7, SECTION III. GRANT OF RELIEF

[17] Notice 2021-7, SECTION III. GRANT OF RELIEF

[18] Notice 2021-7, SECTION III. GRANT OF RELIEF

SECTION: 402
QUALIFIED PLAN OFFSET LOAN AMOUNT FINAL REGULATIONS ISSUED BY IRS

Citation: TD 9937, 1/5/21

The IRS has issued final regulations[19] that provide information on the extended time period for those plan participants receiving a noncash distribution from a retirement plan that is a *qualified plan loan offset* (QPLO) to rollover the amount to another retirement plan. This provision was added to the law by the Tax Cuts and Jobs Act (TCJA).

The regulations are finalized versions of the proposed regulations issued in August 2020.[20]

The proposed regulations provided that taxpayers may rely on these regulations beginning with respect to plan loan offset amounts, including qualified plan loan offset amounts, treated as distributed on or after the date the proposed regulations are published in the *Federal Register*[21] and before the date the regulations are published in the *Federal Register* in final form.[22]

For the most part the final regulations are identical to the proposed regulations, as only a single comment was received by the IRS.

However, the IRS made some modifications to the effective date when the final regulations were published, noting in the preamble to the final regulations:

> ..[T]he applicability date in these final regulations is revised from the QPLO proposed regulations, which had proposed to apply the regulations to plan loan offset amounts treated as distributed on or after the date of publication of final regulations. Under the revised applicability date, the final regulations will apply to plan loan offset amounts, including qualified plan loan offset amounts, treated as distributed on or after January 1, 2021. Thus, for example, the rules in §1.402(c)-3 will first apply to 2021 Form 1099-Rs required to be filed and furnished in 2022 (more than one year after the date of publication of the final regulations). This delayed applicability date will give plan administrators and recordkeepers additional time to program systems and otherwise establish procedures for obtaining the exact

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[19] TD 9937, January 5, 2021 (to be published January 6, 2020), https://public-inspection.federalregister.gov/2020-27151.pdf?utm_medium=email&utm_campaign=pi+subscription+mailing+list&utm_source=federalregister.gov (retrieved January 5, 2021)

[20] REG-116475-19, August 17, 2020 (to be published on August 20, 2020), https://s3.amazonaws.com/public-inspection.federalregister.gov/2020-16564.pdf (retrieved August 17, 2020)

[21] Scheduled per the original draft release to be published on August 20, 2020

[22] REG-116475-19, August 17, 2020, Proposed Applicability Date and page one header on the original draft released in PDF form on August 17

> date of severance from employment of a plan participant and tracking the one-year anniversary of that date.
>
> The applicability date in these final regulations is also revised to provide that taxpayers (including a filer of a Form 1099-R) may apply these regulations with respect to plan loan offset amounts, including qualified plan loan offset amounts, treated as distributed on or after August 20, 2020, which is the date of the publication of the QPLO proposed regulations.[23]

The specific language for the applicability date in the final regulations reads as follows:

> These regulations apply to plan loan offset amounts, including qualified plan loan offset amounts, treated as distributed on or after January 1, 2021. Thus, for example, the rules in §1.402(c)-3 will first apply to 2021 Form 1099-Rs required to be filed and furnished in 2022. However, taxpayers (including a filer of a Form 1099-R) may apply these regulations with respect to plan loan offset amounts, including qualified plan loan offset amounts, treated as distributed on or after August 20, 2020.[24]

TCJA Law Change

The Tax Cuts and Jobs Act revised IRC §402(c)(3) in the following manner, as described in the preamble to the proposed regulations:

> Section 13613 of TCJA amended section 402(c)(3) of the Code to provide an extended rollover deadline for qualified plan loan offset (QPLO) amounts (as defined in section 402(c)(3)(C)(ii)). Any portion of a QPLO amount (up to the entire QPLO amount) may be rolled over into an eligible retirement plan by the individual's tax filing due date (including extensions) for the taxable year in which the offset occurs.[25]

Qualified Plan Loan Offset Amount

The preamble to the proposed regulations noted that a QPLO amount is defined under the statute as a plan loan offset amount treated as distributed from a qualified employer plan to an employee or beneficiary *solely* by reason of:

- The termination of the qualified employer plan, *or*
- The failure to meet the repayment terms of the loan from such plan because of the severance from employment of the employee.[26]

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[23] TD 9937, January 5, 2021, Supplementary Information, Summary of Comments and Explanation of Provisions

[24] TD 9937, January 5, 2021, Supplementary Information, Applicability Date

[25] REG-116475-19, August 17, 2020, Background, Section 2

[26] REG-116475-19, August 17, 2020, Background, Section 2, Proposed Reg. §1.402(c)-3(a)(2)(iii)(B)(1)

The loan must be one that met the requirements to be treated as a plan loan under §72(p)(2) not treated as a distribution right up until such time as the QPLO amount is treated as distributed.[27]

Note that not all plan loan offsets are qualified plan loan offsets—the proposed regulations defined the broad term plan loan offsets as follows:

> For purposes of section 402(c), a plan loan offset amount is the amount by which, under the plan terms governing a plan loan, an employee's accrued benefit is reduced (offset) in order to repay the loan (including the enforcement of the plan's security interest in an employee's accrued benefit). A distribution of a plan loan offset amount can occur in a variety of circumstances, for example, when the terms governing a plan loan require that, in the event of the employee's termination of employment or request for a distribution, the loan be repaid immediately or treated as in default. A distribution of a plan loan offset amount also occurs when, under the terms governing the plan loan, the loan is cancelled, accelerated, or treated as if it were in default (for example, when the plan treats a loan as in default upon an employee's termination of employment or within a specified period thereafter). A distribution of a plan loan offset amount is an actual distribution, not a deemed distribution under section 72(p).[28]

A severance from employment is determined by reference to Reg. §1.401(k)-1(d)(2).[29] That regulation provides the following is treated as a severance from employment.[30]

> An employee has a severance from employment when the employee ceases to be an employee of the employer maintaining the plan. An employee does not have a severance from employment if, in connection with a change of employment, the employee's new employer maintains such plan with respect to the employee. For example, a new employer maintains a plan with respect to an employee by continuing or assuming sponsorship of the plan or by accepting a transfer of plan assets and liabilities (within the meaning of section 414(l)) with respect to the employee.[31]

The distribution is deemed to be offset due to the termination of employment when the following conditions are met:

> A plan loan offset amount is treated as distributed from a qualified employer plan to an employee or beneficiary solely by reason of the

[27] REG-116475-19, August 17, 2020, Background, Section 2, Proposed Reg. §1.402(c)-3(a)(2)(iii)(B)(2)

[28] Proposed Reg. §1.402(c)-3(a)(2)(iii)(A)

[29] Reg. §1.402(c)-3(a)(2)(iv)(A)

[30] Reg. §1.402(c)-3(a)(2)(ii)(A)

[31] Reg. §1.401(k)-1(d)(2)

> failure to meet the repayment terms of a plan loan because of severance from employment of the employee if the plan loan offset:
>
> > (1) Relates to a failure to meet the repayment terms of the plan loan, and
> >
> > (2) Occurs within the period beginning on the date of the employee's severance from employment and ending on the first anniversary of that date.[32]

Note that this provides a 12-month period during which the QPLO must be recognized by the plan to be covered under these rules.

Time Period to Rollover the QPLO Amount

QPLO amounts receive an extended time period during which they can be rolled over by the former participant to another retirement plan. That period runs from the date of the QPLO amount distribution up through the individual's tax filing due date (including extensions) for the taxable year in which the QPLO amount is treated as distributed from the plan.[33]

The preamble to the proposed regulations provided that this rollover will be covered by the automatic extended time period to complete certain actions provided by Reg. §301.9100-2(b), so that a taxpayer that files his/her return timely will have until the extended due date of that return to complete the rollover even if no extension of time to file the return is requested. This discussion is referenced in the final regulation preamble. The preamble notes:

> If a taxpayer to whom a QPLO amount is distributed satisfies the conditions in §301.9100-2(b), the taxpayer will have an extended period past his or her tax filing due date in which to complete a rollover of the QPLO amount, even if the taxpayer does not request an extension to file his or her income tax return but instead files the return by the unextended tax filing due date.[34]

The provisions of Reg. §301.9100-2(b) apply to taxpayers that meet the following two conditions:

- The taxpayer's return was timely filed for the year the QPLO amount is treated as distributed; *and*
- The taxpayer takes appropriate corrective action within the six-month period following the original unextended due date (in this case that means completes the rollover).[35]

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[32] Reg. §1.402(c)-3(a)(2)(iv)(B)

[33] Reg. §1.402(c)-3(a)(2)(ii)(B)

[34] REG-116475-19, August 17, 2020, Explanation of Provisions, Section 2, referenced in the Preamble to the Final Regulations in Footnote 4

[35] REG-116475-19, August 17, 2020, Background, Section 2

The extended period to rollover the QPLO amount does *not* extend the time to rollover any part of the rollover distribution that is not a QPLO amount (that is, normally the portion received in cash or employer securities by the employee or amounts withheld and transmitted to the IRS by the plan as federal withholding taxes for the participant).

Examples

The regulations provide the following examples of applying its provisions:

EXAMPLE 1, REG. §1.402(C)-3(A)(2)(V)

Direct rollover of balance after QPLO

(1) In 2020, Employee A has an account balance of $10,000 in Plan Y, of which $3,000 is invested in a plan loan to Employee A that is secured by Employee A's account balance in Plan Y. Employee A has made no after-tax employee contributions to Plan Y. The plan loan meets the requirements of section 72(p)(2). Plan Y does not provide any direct rollover option with respect to plan loans. Employee A severs from employment on June 15, 2020. After severance from employment, Plan Y accelerates the plan loan and provides Employee A 90 days to repay the remaining balance of the plan loan. Employee A, who is under the age set forth in section 401(a)(9)(C)(i)(II), does not repay the loan within the 90 days and instead elects a direct rollover of Employee A's entire account balance in Plan Y. On September 18, 2020 (within the 12-month period beginning on the date that Employee A severed from employment), Employee A's outstanding loan is offset against the account balance.

(2) In order to satisfy section 401(a)(31), Plan Y must make a direct rollover by paying $7,000 directly to the eligible retirement plan chosen by Employee A. When Employee A's account balance was offset by the amount of the $3,000 unpaid loan balance, Employee A received a plan loan offset amount (equivalent to $3,000) that is an eligible rollover distribution. However, under §1.401(a)(31)-1, Q&A-16, Plan Y satisfies section 401(a)(31), even though a direct rollover option was not provided with respect to the $3,000 plan loan offset amount.

(3) No withholding is required under section 3405(c) on account of the distribution of the $3,000 plan loan offset amount because no cash or other property (other than the plan loan offset amount) is received by Employee A from which to satisfy the withholding.

(4) The $3,000 plan loan offset amount is a qualified plan loan offset amount within the meaning of paragraph (a)(2)(iii)(B) of this section. Accordingly, Employee A may roll over up to the $3,000 qualified plan loan offset amount to an eligible retirement plan within the period that ends on the employee's tax filing due date (including extensions) for the taxable year in which the offset occurs.

EXAMPLE 2, REG. §1.402(C)-3(A)(2)(V)

No QPLO at time of severance of employment, later loan default

(1) The facts are the same as in Example 1, except that, rather than accelerating the plan loan, Plan Y permits Employee A to continue making loan installment payments after severance from employment. Employee A continues making loan installment payments until January 1, 2021, at which time Employee A does not make the loan installment payment due on January 1, 2021. In accordance with §1.72(p)-1, Q&A-10, Plan Y allows a cure period that continues until the last day of the calendar quarter following the quarter in which the required installment payment was due. Employee A does not make a plan loan installment payment during the cure period. Plan Y offsets the unpaid $3,000 loan balance against

Employee A's account balance on July 1, 2021 (which is after the 12-month period beginning on the date that Employee A severed from employment).

(2) The conclusion is the same as in Example 1, except that the $3,000 plan loan offset amount is not a qualified plan loan offset amount (because the offset did not occur within the 12-month period beginning on the date that Employee A severed from employment). Accordingly, Employee A may roll over up to the $3,000 plan loan offset amount to an eligible retirement plan within the 60-day period provided in section 402(c)(3)(A) (rather than within the period that ends on Employee A's tax filing due date (including extensions) for the taxable year in which the offset occurs).

EXAMPLE 3, REG. §1.402(C)-3(A)(2)(V)

Offset due to terms of plan, employee does not request an offset

(1) The facts are the same as in Example 1, except that the terms governing the plan loan to Employee A provide that, upon severance from employment, Employee A's account balance is automatically offset by the amount of any unpaid loan balance to repay the loan. Employee A severs from employment but does not request a distribution from Plan Y. Nevertheless, pursuant to the terms governing the plan loan, Employee A's account balance is automatically offset on June 15, 2020, by the amount of the $3,000 unpaid loan balance.

(2) The $3,000 plan loan offset amount is a qualified plan loan offset amount within the meaning of paragraph (a)(2)(iii)(B) of this section. Accordingly, Employee A may roll over up to the $3,000 qualified plan loan offset amount to an eligible retirement plan within the period that ends on Employee A's tax filing due date (including extensions) for the taxable year in which the offset occurs.

EXAMPLE 4, REG. §1.402(C)-3(A)(2)(V)

Employee takes a cash distribution after QPLO rather than a direct rollover

(1) The facts are the same as in Example 1, except that Employee A elects to receive a cash distribution of the account balance that remains after the $3,000 plan loan offset amount, instead of electing a direct rollover of the remaining account balance.

(2) The amount of the distribution received by Employee A is $10,000 (not $3,000). Because the amount of the $3,000 plan loan offset amount attributable to the loan is included in determining the amount of the eligible rollover distribution to which withholding applies, withholding in the amount of $2,000 (20 percent of $10,000) is required under section 3405(c). The $2,000 is required to be withheld from the $7,000 to be distributed to Employee A in cash, so that Employee A actually receives a cash amount of $5,000.

(3) The $3,000 plan loan offset amount is a qualified plan loan offset amount within the meaning of paragraph (a)(2)(iii)(B) of this section. Accordingly, Employee A may roll over up to the $3,000 qualified plan loan offset to an eligible retirement plan within the period that ends on the Employee A's tax filing due date (including extensions) for the taxable year in which the offset occurs. In addition, Employee A may roll over up to $7,000 (the portion of the

distribution that is not related to the offset) within the 60-day period provided in section 402(c)(3).

Note that in this example, the employee will need to come up with the $2,000 of taxes withheld within 60 days to complete a rollover. Only the $3,000 QPLO amount receives the extended period during which a rollover may be completed.

EXAMPLE 5, REG. §1.402(C)-3(A)(2)(V)

Employer securities rather than cash distributed

(1) The facts are the same as in Example 4, except that the $7,000 distribution to Employee A after the offset consists solely of employer securities within the meaning of section 402(e)(4)(E).

(2) No withholding is required under section 3405(c) because the distribution consists solely of the $3,000 plan loan offset amount and the $7,000 distribution of employer securities. This is the result because the total amount required to be withheld does not exceed the sum of the cash and the fair market value of other property distributed, excluding plan loan offset amounts and employer securities.

(3) Employee A may roll over up to the $7,000 of employer securities to an eligible retirement plan within the 60-day period provided in section 402(c)(3). The $3,000 plan loan offset amount is a qualified plan loan offset amount within the meaning of paragraph (a)(2)(iii)(B) of this section. Accordingly, Employee A may roll over up to the $3,000 qualified plan loan offset amount to an eligible retirement plan within the period that ends on Employee A's tax filing due date (including extensions) for the taxable year in which the offset occurs.

EXAMPLE 6, REG. §1.402(C)-3(A)(2)(V)

Employee fails to make payments on plan loan

(1) Employee B, who is age 40, has an account balance in Plan Z. Plan Z provides for no after-tax employee contributions. In 2022, Employee B receives a loan from Plan Z, the terms of which satisfy section 72(p)(2), and which is secured by elective contributions subject to the distribution restrictions in section 401(k)(2)(B).

(2) Employee B fails to make an installment payment due on April 1, 2023, or any other monthly payments thereafter. In accordance with §1.72(p)-1, Q&A-10, Plan Z allows a cure period that continues until the last day of the calendar quarter following the quarter in which the required installment payment was due (September 30, 2023). Employee B does not make a plan loan installment payment during the cure period. On September 30, 2023, pursuant to section 72(p)(1), Employee B is taxed on a deemed distribution equal to the amount of the unpaid loan balance. Pursuant to §1.402(c)-2, Q&A4(d), the deemed distribution is not an eligible rollover distribution.

(3) Because Employee B has not severed from employment or experienced any other event that permits the distribution under section 401(k)(2)(B) of the elective contributions that secure the loan, Plan Z is prohibited from executing on the loan. Accordingly, Employee B's account balance is not offset by the amount of the unpaid loan balance at the time of the

deemed distribution. Thus, there is no distribution of an offset amount that is an eligible rollover distribution on September 30, 2023.

EXAMPLE 7, REG. §1.402(C)-3(A)(2)(V)

Employee defaults on plan loan, separates from service afterward

(1) The facts are the same as in Example 6, except that Employee B has a severance from employment on November 1, 2023. On that date, Employee B's unpaid loan balance is offset against the account balance on distribution.

(2) The plan loan offset amount is not a qualified plan loan offset amount. Although the offset occurred within 12 months after Employee B severed from employment, the plan loan does not meet the requirement in paragraph (a)(2)(iii)(B) of this section (that the plan loan meet the requirements of section 72(p)(2) immediately prior to Employee B's severance from employment). Instead, the loan was taxable on September 30, 2023 (prior to Employee B's severance from employment on November 1, 2023), because of the failure to meet the level amortization requirement in section 72(p)(2)(C). Accordingly, Employee B may roll over the plan loan offset amount to an eligible retirement plan within the 60-day period provided in section 402(c)(3)(A) (rather than within the period that ends on Employee B's tax filing due date (including extensions) for the taxable year in which the offset occurs).

SECTION: 6011
IRS WILL BEGIN ACCEPTING ELECTRONICALLY FILED RETURNS ON FEBRUARY 12

Citation: "2021 tax filing season begins Feb. 12; IRS outlines steps to speed refunds during pandemic," IRS News Release IR-2021-16, 1/15/21

The 2020 filing season will begin on February 12 the IRS has announced.[36] The start is being delayed due to the December 27, 2020 passage of major tax provisions in the Consolidated Appropriations Act, 2021.

The news release explains the situation as follows:

> The Feb. 12 start date for individual tax return filers allows the IRS time to do additional programming and testing of IRS systems following the Dec. 27 tax law changes that provided a second round of Economic Impact Payments and other benefits.
>
> This programming work is critical to ensuring IRS systems run smoothly. If filing season were opened without the correct programming in place, then there could be a delay in issuing refunds to taxpayers. These changes ensure that eligible people will receive any

[36] "2021 tax filing season begins Feb. 12; IRS outlines steps to speed refunds during pandemic," IRS News Release IR-2021-16, January 15, 2021, https://www.irs.gov/newsroom/2021-tax-filing-season-begins-feb-12-irs-outlines-steps-to-speed-refunds-during-pandemic (retrieved January 15, 2021)

> remaining stimulus money as a Recovery Rebate Credit when they file their 2020 tax return.[37]

The release notes that preparers still will be able to prepare returns for taxpayers—they will just be need to be held until the IRS opens up processing on February 12.

> To speed refunds during the pandemic, the IRS urges taxpayers to file electronically with direct deposit as soon as they have the information they need. People can begin filing their tax returns immediately with tax software companies, including IRS Free File partners. These groups are starting to accept tax returns now, and the returns will be transmitted to the IRS starting Feb. 12.[38]

The IRS also provides an expected date for refunds to be received by taxpayers who will be receiving a refund that involves the Earned Income Tax Credit or the Additional Child Tax Credit:

> Under the PATH Act, the IRS cannot issue a refund involving the Earned Income Tax Credit (EITC) or Additional Child Tax Credit (ACTC) before mid-February. The law provides this additional time to help the IRS stop fraudulent refunds and claims from being issued, including to identity thieves.
>
> The IRS anticipates a first week of March refund for many EITC and ACTC taxpayers if they file electronically with direct deposit and there are no issues with their tax returns. This would be the same experience for taxpayers if the filing season opened in late January. Taxpayers will need to check Where's My Refund for their personalized refund date.[39]

The IRS also provides more general information for taxpayers to receive refunds once they electronically file their returns:

> Overall, the IRS anticipates nine out of 10 taxpayers will receive their refund within 21 days of when they file electronically with direct deposit if there are no issues with their tax return. The IRS urges taxpayers and tax professionals to file electronically. To avoid delays in processing, people should avoid filing paper returns wherever possible.[40]

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[37] "2021 tax filing season begins Feb. 12; IRS outlines steps to speed refunds during pandemic," IRS News Release IR-2021-16

[38] "2021 tax filing season begins Feb. 12; IRS outlines steps to speed refunds during pandemic," IRS News Release IR-2021-16

[39] "2021 tax filing season begins Feb. 12; IRS outlines steps to speed refunds during pandemic," IRS News Release IR-2021-16

[40] "2021 tax filing season begins Feb. 12; IRS outlines steps to speed refunds during pandemic," IRS News Release IR-2021-16

SECTION: 6011
IP-PIN PROGRAM AVAILABLE TO ALL TAXPAYERS

Citation: "All taxpayers now eligible for Identity Protection PINs," IRS Website, 1/12/21

The IRS has outlined the details of its voluntary Identity Protection Personal Identification Number (IP-PIN) program where taxpayers will receive an IP-PIN, as well as opening up the process nationwide.[41] In the news release announcing the program, the IRS provides:

> The Identity Protection PIN (IP PIN) is a six-digit code known only to the taxpayer and to the IRS. It helps prevent identity thieves from filing fraudulent tax returns using a taxpayers' personally identifiable information.
>
> "This is a way to, in essence, lock your tax account, and the IP PIN serves as the key to opening that account," said IRS Commissioner Chuck Rettig. "Electronic returns that do not contain the correct IP PIN will be rejected, and paper returns will go through additional scrutiny for fraud."[42]

The news release notes a number of key facts taxpayers need to know before deciding if this program is right for them:

- This is a voluntary program.
- You must pass a rigorous identity verification process.
- Spouses and dependents are eligible for an IP PIN if they can verify their identities.
- An IP PIN is valid for a calendar year.
- You must obtain a new IP PIN each filing season.
- The online IP PIN tool is offline between November and mid-January each year.
- Correct IP PINs must be entered on electronic and paper tax returns to avoid rejections and delays.
- Never share your IP PIN with anyone but your trusted tax provider. The IRS will never call, text or email requesting your IP PIN. Beware of scams to steal your IP PIN.

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[41] "All taxpayers now eligible for Identity Protection PINs," IRS Website, January 12, 2021, https://www.irs.gov/newsroom/all-taxpayers-now-eligible-for-identity-protection-pins (retrieved January 13, 2021)

[42] "All taxpayers now eligible for Identity Protection PINs," IRS Website, January 12, 2021

- There currently is no opt-out option but the IRS is working on one for 2022.[43]

The lack of an ability to opt-out of the program once a taxpayer has obtained an IP PIN is something that needs to be fully understood by any taxpayer making a decision on participating in this program. If, for whatever reason, the taxpayer no longer is able to provide an IP PIN or obtain a replacement, the only option is to file the return in paper form and expect an extended period of time to pass before the IRS finally pays out any refund that may be due.

For taxpayers that do want to use the program, the IRS offers the following instructions:

> Taxpayers who want an IP PIN for 2021 should go to IRS.gov/IPPIN and use the Get an IP PIN tool. This online process will require taxpayers to verify their identities using the Secure Access authentication process if they do not already have an IRS account. See IRS.gov/SecureAccess for what information you need to be successful. There is no need to file a Form 14039, an Identity Theft Affidavit, to opt into the program
>
> Once taxpayers have authenticated their identities, their 2021 IP PIN immediately will be revealed to them. Once in the program, this PIN must be used when prompted by electronic tax returns or entered by hand near the signature line on paper tax returns.[44]

The IRS site describing the Secure Access program notes that taxpayers will need the following information to successfully complete the process:

- Email address
- Social Security Number (SSN) or Individual Tax Identification Number (ITIN)
- Tax filing status and mailing address
- One financial account number linked to your name:
  - Credit card – last 8 digits (no American Express, debit or corporate cards) or
  - Student loan – (Enter the student loan account number provided on your statement. The account number may contain both numbers and letters. Do not include any symbols.) Additionally, we can't verify student loans issued by Nelnet. or
  - Mortgage or home equity loan or
  - Home equity line of credit (HELOC) or
  - Auto loan

[43] "All taxpayers now eligible for Identity Protection PINs," IRS Website, January 12, 2021

[44] "All taxpayers now eligible for Identity Protection PINs," IRS Website, January 12, 2021

- Mobile phone linked to your name (for faster registration) or ability to receive an activation code by mail.[45]

The IRS does provide options for taxpayers who are unable to obtain a number via the online system. The first is for those with adjusted gross income of $72,000 or less:

> Taxpayers whose adjusted gross income is $72,000 or less may complete Form 15227, Application for an Identity Protection Personal Identification Number, and mail or fax to the IRS. An IRS customer service representative will contact the taxpayer and verify their identities by phone. Taxpayers should have their prior year tax return at hand for the verification process.
>
> Taxpayers who verify their identities through this process will have an IP PIN mailed to them the following tax year. This is for security reasons. Once in the program, the IP PIN will be mailed to these taxpayers each year.[46]

Other taxpayers will be forced to verify their identity in person if they want to use this program:

> Taxpayers who cannot verify their identities online or by phone and who are ineligible for file Form 15227 can contact the IRS and make an appointment at a Taxpayer Assistance Center to verify their identities in person. Taxpayers should bring two forms of identification, including one government-issued picture identification.
>
> Taxpayers who verify their identities through the in-person process will have an IP PIN mailed to them within three weeks. Once in the program, the IP PIN will be mailed to these taxpayers each year.[47]

This new program will not impact the program already in place for taxpayers with confirmed identity theft issues:

> Taxpayers who are confirmed identity theft victims or who have filed an identity theft affidavit because of suspected stolen identity refund fraud will automatically receive an IP PIN via mail once their cases are resolved. Current tax-related identity theft victims who have been receiving IP PINs via mail will experience no change.[48]

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[45] "Secure Access: How to Register for Certain Online Self-Help Tools," IRS Website, November 25, 2020, https://www.irs.gov/individuals/secure-access-how-to-register-for-certain-online-self-help-tools (retrieved January 13, 2021)

[46] "All taxpayers now eligible for Identity Protection PINs," IRS Website, January 12, 2021

[47] "All taxpayers now eligible for Identity Protection PINs," IRS Website, January 12, 2021

[48] "All taxpayers now eligible for Identity Protection PINs," IRS Website, January 12, 2021