Current Federal Tax Developments

Week of February 1, 2021

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CURRENT FEDERAL TAX DEVELOPMENTS
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Contents

SECTION: 6050B
IRS PROVIDES RECOMMENDED STEPS TO BE TAKEN BY VICTIMS OF UNEMPLOYMENT COMPENSATION IDENTITY THEFT

Citation: IR-2021-24, 1/28/21

During 2020 a number of states found themselves being faced with claims for unemployment that were fraudulent in nature. Perpetrators would use information they had obtained to claim to be another person, filing for unemployment in that person's name and having the payment redirected to come to them. Some victims are just discovering this issue in January as they receive a Form 1099G from the state government showing that they had been paid unemployment compensation.

In News Release IR-2021-14[1] the IRS outlined steps for such individuals who have received information returns showing payment of unemployment compensation they never applied for to take.

The IRS describes the problem as follows:

> During 2020, millions of taxpayers were impacted by the COVID-19 pandemic through job loss or reduced work hours. Some taxpayers who faced unemployment or reduced work hours applied for and received unemployment compensation from their state. Under federal law, unemployment benefits are taxable income.
>
> However, scammers also took advantage of the pandemic by filing fraudulent claims for unemployment compensation using stolen personal information of individuals who had not filed claims. Payments made as a result of these fraudulent claims went to the identity thieves, and the individuals whose names and personal information were taken did not receive any of the payments.[2]

The IRS advises taxpayers who receive the erroneous Forms 1099G to take the following steps:

> Taxpayers who receive an incorrect Form 1099-G for unemployment benefits they did not receive should contact the issuing state agency to request a revised Form 1099-G showing they did not receive these benefits. Taxpayers who are unable to obtain a timely, corrected form from states should still file an accurate tax return, reporting only the income they received. A corrected Form 1099-G showing zero unemployment benefits in cases of identity theft will help taxpayers

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[1] IR-2021-24, January 28, 2021, https://www.irs.gov/newsroom/irs-offers-guidance-to-taxpayers-on-identity-theft-involving-unemployment-benefits (retrieved January 29, 2021)

[2] IR-2021-24, January 28, 2021

> avoid being hit with an unexpected federal tax bill for unreported income.[3]

The release also notes that the IRS has previously issued guidance to the states indicating that in these circumstances no Form 1099G should be issued,[4] which will hopefully (but not necessarily) make it easier for victims to persuade state agencies to correct these erroneous Forms 1099-G:

> The IRS previously issued guidance requested by states on identity theft guidance regarding unemployment compensation reporting. No Forms 1099-G should be issued to those individuals the states have identified as ID theft victims.[5]

If taxpayers are unable to get the state to issue a corrected Form 1099-G the victim has the right to dispute the Form 1099-G if the IRS attempts to collect related to the erroneous form. IRC §6201(d) provides:

> (d) Required reasonable verification of information returns
>
> In any court proceeding, if a taxpayer asserts a reasonable dispute with respect to any item of income reported on an information return filed with the Secretary under subpart B or C of part III of subchapter A of chapter 61 by a third party and the taxpayer has fully cooperated with the Secretary (including providing, within a reasonable period of time, access to and inspection of all witnesses, information, and documents within the control of the taxpayer as reasonably requested by the Secretary), the Secretary shall have the burden of producing reasonable and probative information concerning such deficiency in addition to such information return.

SECTION: CARES
REVISED DRAFT OF FORM 7200 INDICATES ADVANCE EMPLOYEE RETENTION CREDIT WILL BE CLAIMED VIA THIS FORM

Citation: Draft Form 7200 (Rev. January 2021), 1/28/21

The IRS has released a revised draft version of Form 7200[6] to be used to obtain a refundable payment of the employee retention credit and the qualified sick pay and

[3] IR-2021-24, January 28, 2021

[4] "Identity theft guidance regarding unemployment compensation reporting," IRS website, https://www.irs.gov/forms-pubs/identity-theft-guidance-regarding-unemployment-compensation-reporting (retrieved January 29, 2021)

[5] IR-2021-24, January 28, 2021

[6] Draft Form 7200 (Rev. January 2021), January 28, 2021, https://www.irs.gov/pub/irs-dft/f7200--dft.pdf (retrived January 29, 2021)

family leave credit. The revisions include the first guidance on how employers will claim the advance employee retention credit for 2021.

The Taxpayer Certainty and Disaster Relief Act of 2020 §207(g)(1) revised CARES Act §2301(j)(2)(A) to provide for an advance payment of the employee retention credit to employers who did not employ more than 500 employees in 2019. The maximum credit is set at 70% of the employer's average wages in 2019. A special rule allows for a modified computation for seasonal employers.[7]

The revised Form 7200 has added the following question E to Part I of Form 7200:

> If you're requesting an advance payment of the employee retention credit (Part II, line 1), enter the average number of full-time employees you had in 2019 (or 2020 if your business wasn't in existence in 2019). Aggregation rules apply.[8]

Similarly, line 1 of Part II, where the amount to be paid to the employer is computed, now contains the following line providing for the amount of employee retention credit an employer will claim:

> Total employee retention credit for the quarter. Don't enter more than the amount eligible to be advanced for the quarter. See instructions.[9]

Unfortunately, the IRS did not release the draft instructions at the same time as they released the form. But the draft form does now clarify how the advance employee retention credit will be claimed by employers looking to take advantage of the provision.

SECTION: CIRCULAR 230
IRS ANNOUNCES OPTION FOR TAX PROFESSIONALS TO UPLOAD FORMS 2848 AND 8821 TO THE AGENCY

Citation: News Release IR-2021-20, 1/25/21

The IRS announced a new electronic option for submitting Forms 2848 and 8821 online in News Release IR-2021-20.[10] The release describes the option as follows:

> The Internal Revenue Service today rolled out a new online option that will help tax professionals remotely obtain signatures from individual and business clients and submit authorization forms electronically.

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[7] CARES Act §2301(j)(2)(B) as amended by Taxpayer Certainty and Disaster Relief Act of 2020 §207(g)(1)

[8] Draft Form 7200 (Rev. January 2021), January 28, 2021

[9] Draft Form 7200 (Rev. January 2021), January 28, 2021

[10] News Release IR-2021-20, January 25, 2021, https://www.irs.gov/newsroom/new-irs-submit-forms-2848-and-8821-online-offers-contact-free-signature-options-for-tax-pros-and-clients-sending-authorization-forms (retrieved January 28, 2021)

> Tax professionals can find the new "Submit Forms 2848 and 8821 Online" on the IRS.gov/taxpros page. Tax professionals must have a Secure Access account, including a current username and password, or create an account in advance of submitting an online authorization form.
>
> "This online tool will allow tax professionals to safely obtain signatures from individual and business clients and upload authorization forms," said Chuck Rettig, IRS commissioner. "This is a first step in our ongoing efforts to expand digital options for tax professionals using electronic signatures and online uploads."
>
> The project is a result of the Taxpayer First Act that requires the IRS to expand use of taxpayers' electronic signatures on authorization forms. This online option also will help protect taxpayers and tax professionals by more easily allowing remote transactions.[11]

The new system will accept Forms 2848 and 8821 using either handwritten or electronic signatures:

> The taxpayer and the tax professional must sign Form 2848. If the tax professional uses the new online option, the signatures on the forms can be handwritten or electronic. Form 8821 needs only the taxpayer's signature. If using the new online option, the taxpayer's signature can be handwritten or electronic.[12]

The new system can be used to withdraw previous authorizations but cannot be used to ask questions or address other issues.[13]

While the IRS will continue to accept mailed or faxed authorization forms, signatures on such forms must be handwritten—electronic signatures cannot be used on these forms.[14]

Electronic Signatures

The IRS, in a separate FAQ, notes that an electronic signature is not the same as a digital signature:

> An electronic signature is an electronic symbol attached to an electronic record that a person will sign. A digital signature is a type of electronic signature.[15]

[11] News Release IR-2021-20, January 25, 2021

[12] News Release IR-2021-20, January 25, 2021

[13] News Release IR-2021-20, January 25, 2021

[14] News Release IR-2021-20, January 25, 2021

[15] Submit Forms 2848 and 8821 Online, IRS website, January 28, 2021, https://www.irs.gov/tax-professionals/submit-forms-2848-and-8821-online#2848-8821-faqs (retrieved January 28, 2021)

So, while digital signatures (such as those provided by services such as DocuSign, RightSignature, etc.) would qualify as an electronic signature, simpler versions will also work. The FAQ provides the following description of such electronic signatures:

> An electronic signature is a way to get approval on electronic documents. It can be in many forms and created by many technologies. You do not need specific technology to create electronic signatures. Electronic signatures can be:
>
> 1. A typed name that is typed on a signature block
> 2. A scanned or digitized image of a handwritten signature that is attached to an electronic record
> 3. A handwritten signature input onto an electronic signature pad
> 4. A handwritten signature, mark, or command input on a display screen with a stylus device
> 5. A signature from third-party software.[16]

While such signatures can be used in the new submission system, they cannot be used with faxed powers of attorney:

> For security reasons, all forms mailed or faxed to the IRS must have a "wet" ink signature.[17]

It seems reasonable to assume the same security concerns would prevent an IRS employee whom the professional contacts on the phone from accepting the copy of the form with an electronic signature faxed directly to them when it is discovered the power of attorney has not yet been processed.

That may be a real problem for the use of such signatures, since the FAQ also notes that the new submission process will *not* result in the faster processing of such forms:

> We process forms in the order we receive them, no matter how they are submitted (mail, fax, online). Forms submitted online are reviewed and processed by IRS employees in the same way as those submitted by fax or mail.[18]

[16] Submit Forms 2848 and 8821 Online, IRS website, January 28, 2021, https://www.irs.gov/tax-professionals/submit-forms-2848-and-8821-online#2848-8821-faqs (retrieved January 28, 2021)

[17] Submit Forms 2848 and 8821 Online, IRS website, January 28, 2021, https://www.irs.gov/tax-professionals/submit-forms-2848-and-8821-online#2848-8821-faqs (retrieved January 28, 2021)

[18] Submit Forms 2848 and 8821 Online, IRS website, January 28, 2021, https://www.irs.gov/tax-professionals/submit-forms-2848-and-8821-online#2848-8821-faqs (retrieved January 28, 2021)

Authentication Requirements for New Clients

The electronic signature option does come with additional steps that must be completed for new clients:

> If the tax professional uses the electronic signature option for a new client, the tax professional must first authenticate the client's identity. For details on this process, see the "Authentication" section in the online option's Frequently Asked Questions.[19]

Specifically, the professional must authenticate the following clients per the referenced FAQ:

> You must authenticate a taxpayer's identity when they electronically sign the form in a remote transaction (e.g., not in person) and you do not have a personal or business relationship with them.[20]

The IRS provides the following guidance on how to authenticate an individual taxpayer's identity:

> If you do not have personal knowledge of the taxpayer's identity, you must authenticate their identity if they're signing the authorization form in a remote transaction.
>
> To authenticate the taxpayer's identity for remote transactions, take these steps:
>
> 1. **Inspect** a valid government-issued photo identification (ID) of the taxpayer and compare the photo to the taxpayer via a self-taken picture of the taxpayer or video conferencing to compare. Examples of government-issued photo ID include a driver's license, employer ID, school ID, state ID, military ID, national ID, voter ID, visa or passport;
>
> 2. **Record** the name, Social Security number (SSN) or Individual Taxpayer Identification Number (ITIN), address, and date of birth of the taxpayer; and
>
> 3. **Verify** the taxpayer's name, address and SSN or ITIN through secondary documentation, such as a federal or state tax return, IRS notice or letter, Social Security card or credit card or utility statement. For example, suppose a taxpayer changed their address in 2020. In that case, a 2019 tax return can be used to verify the taxpayer's name and SSN or ITIN, and a

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[19] News Release IR-2021-20, January 25, 2021

[20] Submit Forms 2848 and 8821 Online, IRS website, January 28, 2021, https://www.irs.gov/tax-professionals/submit-forms-2848-and-8821-online#2848-8821-faqs (retrieved January 28, 2021)

recent utility statement can be used to verify the taxpayer's new address.[21]

The IRS provides the following steps to authenticate a business taxpayer's identity:

> To authenticate a business entity taxpayer's identity for remote transactions, take these steps:
>
> 1. Confirm the individual has an authorized covered relationship with the business entity.
>   - **Corporation:**
>   - An officer having authority under applicable state law to bind the corporation,
>   - Any person designated by the board of directors or other governing body,
>   - Any officer or employee on a written request signed by any principal officer and attested to by the secretary or other officer,
>   - Any bona fide shareholder of record owning 1% or more of the outstanding stock of the corporation.
>   - **S Corporation:**
>   - Any person who was a shareholder during any part of the period covered by the return during which an election under section 1362(a) was in effect;
>   - Any person authorized by applicable state law to act for a dissolved corporation; or
>   - Any person who has a material interest that will be affected by information contained therein.
>   - **Partnership:**
>   - Any person who was a member of the partnership during any part of the period covered by the return.
> 2. **Inspect** a valid government-issued photo identification (ID) of the individual authorized to represent the business entity

[21] Submit Forms 2848 and 8821 Online, IRS website, January 28, 2021, https://www.irs.gov/tax-professionals/submit-forms-2848-and-8821-online#2848-8821-faqs (retrieved January 28, 2021)

taxpayer and compare it to a self-taken picture or video conferencing image of the authorized individual. Examples of government-issued photo ID include a driver's license, employer ID, school ID, state ID, military ID, national ID, voter ID, visa or passport;

3. **Record** the name, Employer Identification Number (EIN), and address of the business entity taxpayer; and

4. **Verify** the business entity taxpayer's name, EIN, and address through secondary documentation, such as a tax information reporting form (e.g., W-2, 1099, etc.), IRS notice or letter, or utility statement.[22]

The IRS provides that professionals should use the steps for business entities to authenticate a tax-exempt organization as well.[23]

The IRS also notes that the professional must retain proof of the authentication, stating that "[b]ooks or records relating to a form or its instructions must be retained as long as their contents may become material in the administration of any Internal Revenue law."[24]

Advantages of the New Option and IRS's Future Plans

The IRS touts the new system as providing the following advantages to tax professionals:

> The new online option negates the need for specific equipment (e.g., fax machines, scanners), saves tax professionals' time in obtaining signatures, reduces person-to-person contact, and allows complete flexibility in completing the form anywhere, anytime, for both the tax professional and client.[25]

This program represents an intermediate step in the IRS's goal of moving toward a fully online option for signing and submitting such forms. The News Release notes:

> The "Submit Forms 2848 and 8821 Online" option is a step towards to a broader IRS effort to expand options for electronic signatures on authorization forms as required by TFA.
>
> This summer, the IRS plans to launch the Tax Pro Account. Its initial functionality will allow tax professionals to initiate a third-party authorization on IRS.gov and send it to a client's IRS online account.

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[22] Submit Forms 2848 and 8821 Online, IRS website, January 28, 2021, https://www.irs.gov/tax-professionals/submit-forms-2848-and-8821-online#2848-8821-faqs (retrieved January 28, 2021)

[23] Submit Forms 2848 and 8821 Online, IRS website, January 28, 2021, https://www.irs.gov/tax-professionals/submit-forms-2848-and-8821-online#2848-8821-faqs (retrieved January 28, 2021)

[24] Submit Forms 2848 and 8821 Online, IRS website, January 28, 2021, https://www.irs.gov/tax-professionals/submit-forms-2848-and-8821-online#2848-8821-faqs (retrieved January 28, 2021)

[25] News Release IR-2021-20, January 25, 2021

> Individual clients will access their online account and digitally sign the authorization, sending it to be recorded on the CAF. The IRS expects this new method will dramatically speed processing and allow for almost immediate authorization. More information about the Tax Pro Account and the extent of its initial functionality will be announced in the future.[26]

SECTION: PPP LOAN

AICPA RECOMMENDS IRS ALLOW TAXPAYERS TO COUNT WAGES UNNECESSARILY REPORTED ON PPP FORGIVENESS APPLICATION IN COMPUTING EMPLOYEE RETENTION CREDIT

Citation: AICPA Letter to David J. Kautter, Michael W. Faulkender and Charles P. Rettig, "Re: Employee Retention Credit – Sections 206 of the Taxpayer Certainty and Disaster Relief Act of 2020 (Division EE of the Consolidated Appropriations Act, 2021)," 1/15/21

The AICPA has sent a comment letter to the IRS regarding how to deal with the issue of claiming the 2020 version of the employee retention credit when payroll costs have been reported on a Paycheck Protection Program loan forgiveness application.[27]

Prior to the passage of the Taxpayer Certainty and Disaster Relief Act (TCDRA) of 2020, part of the Consolidated Appropriations Act, 2021, taxpayers who had received a Paycheck Protection Program loan were not eligible to claim the Employee Retention Credit enacted as part of the Coronavirus Aid, Relief, and Economic Security (CARES) Act. However, the December 27, 2020 law removed that restriction, providing instead that such a credit would not be available to be claimed for wages that were used to obtain forgiveness for a Paycheck Protection Program (PPP) loan.

As the AICPA letter describes the situation:

> The CARES Act provided employers with the option to benefit from one of two mutually exclusive incentives, a Paycheck Protection Program (PPP) loan or an employee retention credit (ERC), designed to allow employers to retain employees during the pandemic. Section 206 of the TCDRA allows employers who received a PPP loan to

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[26] News Release IR-2021-20, January 25, 2021

[27] AICPA Letter to David J. Kautter, Michael W. Faulkender and Charles P. Rettig, "Re: Employee Retention Credit – Sections 206 of the Taxpayer Certainty and Disaster Relief Act of 2020 (Division EE of the Consolidated Appropriations Act, 2021)," January 15, 2021, https://www.aicpa.org/content/dam/aicpa/advocacy/tax/downloadabledocuments/56175896-aicpa-comments-erc-ppp-loans.pdf (retrieved January 29, 2021)

> retroactively claim the ERC for wages paid after March 12, 2020, but not for the wages used to obtain PPP loan forgiveness.[28]

Borrowers who applied for forgiveness prior to the enactment of the TCDRA were not aware that there would be an option to claim the Employee Retention Credit or that such a claim would be conditioned on not having used such wages to obtain forgiveness of a PPP loan. As the AICPA letter notes:

> It is unclear how the reporting of wages as payroll costs on a previously filed PPP loan forgiveness application affects an employer's ability to claim the ERC for wages that were included on a loan forgiveness application but did not affect the amount of loan forgiveness.[29]

An applicant could reasonably have concluded that, with a 24-week covered period over which to spend funds that were based on 2.5 months of average 2019 payroll, that they could simply report wages on the application form. Similarly, a borrower might have reported all wages and related expenses on the forgiveness application form, assuming that this would allow full forgiveness even if the bank or SBA decided a portion of their expenses did not qualify for forgiveness.

Now that the rules are changed, are those borrowers simply out of luck? The AICPA letter recommends that the IRS adopt guidance to avoid that result:

> The AICPA recommends that the IRS and Treasury provide guidance stating that the filing of a PPP loan forgiveness application does not constitute an election to forgo the ERC with respect to the amount of wages reported on the application exceeding the amount of wages necessary for loan forgiveness.[30]

The AICPA analysis notes that borrowers had no idea listing excess wages on the application would end up having a potentially negative impact on qualification for this tax credit, since they were not at all eligible for this credit under the law in place when they applied for forgiveness:

> To be eligible for PPP loan forgiveness, an employer must incur or pay payroll, rent, utilities and interest amounts during the covered period or alternative covered period. On loan forgiveness applications, many employers reported only payroll costs (and not rent, utilities, and interest), because the payroll costs generally exceeded the loan amounts. Because employers did not have the option to claim the ERC at the time many loan forgiveness applications were filed, they

[28] AICPA Letter to David J. Kautter, Michael W. Faulkender and Charles P. Rettig, "Re: Employee Retention Credit – Sections 206 of the Taxpayer Certainty and Disaster Relief Act of 2020 (Division EE of the Consolidated Appropriations Act, 2021)," January 15, 2021, p. 1

[29] AICPA Letter to David J. Kautter, Michael W. Faulkender and Charles P. Rettig, "Re: Employee Retention Credit – Sections 206 of the Taxpayer Certainty and Disaster Relief Act of 2020 (Division EE of the Consolidated Appropriations Act, 2021)," January 15, 2021, p. 2

[30] AICPA Letter to David J. Kautter, Michael W. Faulkender and Charles P. Rettig, "Re: Employee Retention Credit – Sections 206 of the Taxpayer Certainty and Disaster Relief Act of 2020 (Division EE of the Consolidated Appropriations Act, 2021)," January 15, 2021, p.2

> were not concerned about reporting wages in excess of those needed for loan forgiveness.[31]

The AICPA letter also points out that the IRS had allowed those who were qualified to claim the ERC to opt out and then later change their mind, but that this guidance doesn't address the PPP issue:

> Qualified wages for ERC purposes are amounts paid by an eligible employer up to $10,000 per employee, unless the employer elects out of the provision. IRS frequently asked question (FAQ) #93 states that an eligible employer can elect not to apply the ERC for any calendar quarter by not claiming the credit on the employer's employment tax return. IRS FAQ # 94 states that the election can be changed by amending a quarterly payroll tax filing and that the employer can claim a credit for a subsequent quarter even though no credit was claimed in the previous quarter. The FAQs do not address the election process when payroll costs have been reported on a PPP loan forgiveness application.[32]

The AICPA letter includes two examples of applying their recommendation to specific facts. The first example deals with a simple case where the borrower simply reported more wages on the forgiveness application than were required to obtain forgiveness, likely because there appeared to be no reason not to.

EXAMPLE 1

Employer X received a $1,000,000 PPP loan. On its PPP loan forgiveness application Employer X reported $1,500,000 of payroll costs for the covered period April 15, 2020 to September 29, 2020. The entire loan was forgiven.

Employer X should be permitted to claim the ERC for qualified wages paid from March 13, 2020 through December 31, 2020, including qualified wages related to the $500,000 of wages reported on the loan forgiveness application in excess of the $1,000,000 of wages necessary for forgiveness, without jeopardizing the validity of the PPP loan forgiveness application.[33]

The second example looks at the case where the borrower, in addition to reporting more payroll costs than would have been necessary to obtain forgiveness, also failed to

[31] AICPA Letter to David J. Kautter, Michael W. Faulkender and Charles P. Rettig, "Re: Employee Retention Credit – Sections 206 of the Taxpayer Certainty and Disaster Relief Act of 2020 (Division EE of the Consolidated Appropriations Act, 2021)," January 15, 2021, p. 2

[32] AICPA Letter to David J. Kautter, Michael W. Faulkender and Charles P. Rettig, "Re: Employee Retention Credit – Sections 206 of the Taxpayer Certainty and Disaster Relief Act of 2020 (Division EE of the Consolidated Appropriations Act, 2021)," January 15, 2021, p. 2

[33] AICPA Letter to David J. Kautter, Michael W. Faulkender and Charles P. Rettig, "Re: Employee Retention Credit – Sections 206 of the Taxpayer Certainty and Disaster Relief Act of 2020 (Division EE of the Consolidated Appropriations Act, 2021)," January 15, 2021, pp. 2-3

include other, non-payroll costs that would have reduced the amount of payroll costs necessary for forgiveness.

EXAMPLE 2

Employer X received a $1,000,000 PPP loan. On its PPP loan forgiveness application, Employer X reported $1,500,000 of payroll costs for the covered period April 15, 2020 to September 29, 2020. In addition, Employer X incurred $100,000 of rent expenses during the covered period that were not reported on the loan forgiveness application as they were not necessary for loan forgiveness. The entire loan was forgiven.

Employer X should be permitted to claim the ERC for qualified wages paid March 13, 2020 through December 31, 2020, including up to $600,000 ($1,500,000 of wages included on the loan forgiveness application + $100,000 of rent expenses not reported on the application - $1,000,000 loan) of payroll costs reported on the loan forgiveness application, without jeopardizing the validity of the PPP loan forgiveness application.[34]

[34] AICPA Letter to David J. Kautter, Michael W. Faulkender and Charles P. Rettig, "Re: Employee Retention Credit – Sections 206 of the Taxpayer Certainty and Disaster Relief Act of 2020 (Division EE of the Consolidated Appropriations Act, 2021)," January 15, 2021, p. 3