

Current Federal Tax Developments

Week of March 1, 2021

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ACCOUNTING
CONTINUING EDUCATION

CURRENT FEDERAL TAX DEVELOPMENTS
WEEK OF MARCH 1, 2021
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SECTION: 61

TAXPAYER ESCAPES PAYING TAX ON NEARLY \$300,000 OF CREDIT CARD REWARDS ACHIEVED BY BUYING GIFT CARDS

Citation: *Anikeev v. Commissioner*, TC Memo 2021-23, 2/23/21

A taxpayer found a way to maximize benefits in an extreme way in an American Express credit card rewards program, so much so that the IRS looked to impose a tax on the gains in the case of *Anikeev v. Commissioner*, TC Memo 2021-23.¹ But the Tax Court found that the IRS's years of informal guidance created a situation where most of the benefits were not taxable—at least not in the way the IRS was attempting to tax the benefits in the case.

Facts of the Case

Konstantin Anikeev had a Blue Cash American Express credit card. American Express established a rewards program that had the following provisions:

During 2013 and 2014 American Express offered a rewards program known as Blue Cash from American Express Card (Blue Cash Rewards Program or Rewards Program). The Blue Cash Rewards Program paid Blue Cash Reward Dollars (Reward Dollars) to credit card users who made eligible purchases on their American Express cards. The number of Reward Dollars that a card user could be awarded pursuant to the Blue Cash Rewards Program was based on a percentage of the dollar amount of the card user's eligible purchases. Eligible purchases were purchases made on the card for goods and services minus returns and other credits.

Pursuant to the terms of the Blue Cash Rewards Program, eligible purchases did not include: (1) fees or interest charges, (2) balance transfers, (3) cash advances, (4) purchases of traveler's checks, (5) purchases or reloading of prepaid cards, or (6) purchases of any cash equivalents. For purposes of the Blue Cash Rewards Program, a Reward Year comprised 12 billing periods in a row beginning with the first anniversary of the opening of the account.

For the first \$6,500 of purchases in each Reward Year petitioners received Reward Dollars equal to 1% of everyday purchases and 0.5% of all other eligible purchases. For purchases in excess of \$6,500 petitioners received Reward Dollars equal to 5% of everyday purchases and 1% of all other eligible purchases. The Blue Cash Rewards

¹ *Anikeev v. Commissioner*, TC Memo 2021-23, February 23, 2021, <https://www.taxnotes.com/tax-notes-today-federal/individual-income-taxation/tax-court-determines-tax-treatment-credit-card-cash-rewards/2021/02/24/2zfqp> (retrieved February 26, 2021)

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Program defined everyday purchases as eligible purchases made in the United States at: (1) supermarkets (superstores and warehouse clubs are not considered supermarkets), (2) gas stations for purchases of \$400 or less of gasoline (superstores, supermarkets, and warehouse clubs that sell gasoline are not considered gas stations), and (3) select major drugstores.

Reward Dollars earned during a billing period became available for redemption after the subsequent billing period if the card was in good standing. American Express treated all of petitioners' purchases in 2013 and 2014 as qualifying for Reward Dollars. The first page of each billing statement included a statement of Reward Dollars earned during the billing period, and the last page included a Reward Dollars summary that described Reward Dollars earned and redeemed during the billing period. Card users could redeem Reward Dollars for Amazon gift cards or as credits on their American Express card balances (statement credits). There was no limit on the amount of Reward Dollars a card user could earn in a Reward Year.²

Mr. Anikeev undertook a program to maximize (and I mean *really* maximize) rewards in this program by purchasing gift cards, something American Express did not object to:

To generate as many Reward Dollars as possible, petitioners used the 1005 Card and the 1001 Card (American Express cards) to buy as many Visa gift cards as they could from local grocery stores and pharmacies. In addition to the values of the gift cards, petitioners were charged service fees for the gift cards of between 0.8% and 1.2% of the gift cards' face values. They used the gift cards to purchase money orders and were charged service fees for the money orders between 0.07% and 0.33% of the dollar amounts of the money orders. They deposited the money orders into their bank accounts. The fees associated with a \$500 gift card and a related money order purchase were between \$6 and \$7.

Upon a payment of their monthly American Express bills, they received the applicable percentage, either 1% or 5%, of the total purchases in Reward Dollars that they could use for a statement credit or redeem for Amazon gift cards. Most of petitioners' total dollars spent with the American Express cards were for purchases of Visa gift cards.

On occasion petitioners paid their American Express bills through MoneyGram, a money transfer company offering its services in participating Walmart stores. When using MoneyGram, petitioners paid the American Express bill as well as the applicable service fee with a reloadable debit card, and MoneyGram would transmit the payment to American Express electronically. Petitioners used their American Express cards to purchase the reloadable debit cards that

² *Anikeev v. Commissioner*, TC Memo 2021-23, February 23, 2021, pp. 3-5

they used to pay their American Express bills, and the purchase of debit cards and reloads also generated Reward Dollars.³

The taxpayer, working with an account with a credit limit of \$35,000, managed to create a very large amount of rewards:

Petitioners redeemed \$36,200 in Reward Dollars as statement credits in 2013 and \$277,275 in 2014.⁴

Tax Issues

The taxpayers did not report these amounts as income on their tax returns for the years in question. As the opinion notes, the IRS concedes that its position is that generally such rewards are not income:

At the outset of the trial of this case, respondent's counsel said: "And it's a long-standing IRS policy, Mr. Sklarz is right, long-standing IRS policy is that card rewards are not taxable. And the rationale for that is that the reward itself acts as a discount on whatever property or services are being purchased by the consumer."

This policy reflects the recognition that a taxpayer who avails himself or herself of a discount in acquiring goods and services has no accession to wealth. That taxpayer has retained more of his or her wealth than a taxpayer who pays full price for the same good or service, but that taxpayer has no additional income; he or she simply has reduced consumption. Although as Benjamin Franklin wisely observed, "[a] penny saved is two pence clear" (which became known more colloquially as "a penny saved is a penny earned"), the income tax law imposes a tax only on the future penny earned, not on the current penny saved.⁵

However, the IRS attempted to argue that this case was different. The opinion quotes the IRS summary of its position:

Generally, when a payment is made by a seller to a customer as an inducement to purchase property, the payment does not constitute income but instead is treated as a purchase price adjustment to the basis of the property. *Pittsburgh Milk Co. v. Commissioner*, 26 T.C. 707 (1956); Rev. Rul. 76-96, 1976-1 C.B. 23. In this case, however, petitioners did not purchase goods or property to which a basis adjustment may apply. Rather, they purchased cash equivalents, in the form of Visa gift cards, Reloads for the Green Dot card, and money orders, to which no such adjustment can apply. See *Cowden v. Commissioner*, 289 F.2d 20, 24 (5th Cir. 1961) (setting forth the cash equivalence doctrine); *Bixby v. Commissioner*, 58 T.C. 757 (1972) (cash equivalents have basis equal to face value). As a result, the Reward

³ *Anikeev v. Commissioner*, TC Memo 2021-23, February 23, 2021, pp. 7-8

⁴ *Anikeev v. Commissioner*, TC Memo 2021-23, February 23, 2021, p. 10.

⁵ *Anikeev v. Commissioner*, TC Memo 2021-23, February 23, 2021, p. 13

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Dollars paid to petitioners as statement credits for the charges relating to cash equivalents are an accession to wealth and income to petitioners under I.R.C. § 61.⁶

However, the taxpayer cited an IRS interrogatory response to note that the IRS position fundamentally comes down to not taxing the reward that is generated by the purchase of a product—in this case the gift cards. As the taxpayer’s statement points out:

The IRS [Internal Revenue Service] proposes to tax Mr. Anikeev’s rewards points because he did not earn them by acquiring goods or services. The IRS’ position is: “rewards generated where no goods or services are purchased are taxable. Thus rewards generated by the purchases of gift cards and then the purchases of money orders, without the purchase of any goods or services are taxable.” The manner of purchase of something, however, does not constitute an accession of wealth. Applying I.R.C. § 61, the rewards points would be taxable when received, not based on how the gift cards were later used. What Mr. Anikeev later used the gift cards (which are a product, given that they have a Universal Product Code) to purchase should not matter.⁷

The Tax Court mainly sides with the taxpayer, finding the IRS created the issue with a vague policy on how to tax such rewards:

This case rests squarely in the legal chasm between the basic principle to broadly define income and respondent’s own policy. Petitioners’ aggressive efforts to generate Reward Dollars have created a dilemma for respondent which is largely the result of the vagueness of IRS credit card reward policy. Petitioners clearly acquired economic benefits by cleverly and relentlessly manipulating the Rewards Program. Their actions never offended American Express and had Mr. Anikeev not been so successful in his efforts he likely would have been ignored by the IRS. However, the scale of his success in acquiring rewards makes this case an extreme test of the longstanding nontaxability of credit card reward programs. To avoid offending his own longstanding policy respondent seeks to apply the cash equivalence concept. As we will explain herein we do not find it is a good fit.⁸

The Court notes this policy has grown out of a single Revenue Ruling issued to deal with rebates offered on the purchase of cars by automobile manufacturers:

Rev. Rul. 76-96, *supra*, is a key link in the chain of IRS reasoning on credit card rewards. It concerned the tax treatment of rebates paid by an automobile manufacturer to qualifying retail customers who purchased its automobiles. Rev. Rul. 76-96, *supra*, held that the receipt

⁶ *Anikeev v. Commissioner*, TC Memo 2021-23, February 23, 2021, p. 11

⁷ *Anikeev v. Commissioner*, TC Memo 2021-23, February 23, 2021, p. 11

⁸ *Anikeev v. Commissioner*, TC Memo 2021-23, February 23, 2021, pp. 13-14

of the rebate by the retail customer did not result in the receipt of gross income. Rather, the rebate was a reduction in the purchase price, requiring a downward adjustment to the basis of the automobile pursuant to section 1012.⁹

The Court noted early in the opinion that the IRS was not asserting that there was a taxable exchange when the taxpayer converted the gift cards to cash equivalents through the purchase of money orders (which is how they got the cash to pay off the purchases charged to their AMEX card that eventually created the rewards), but rather arguing that buying gift cards with the intent not to buy goods or services rendered the rewards points taxable—but the Tax Court wasn't buying the concept:

Respondent's assertion of the inclusion in income of Reward Dollars turns on the ultimate use of the Visa gift cards. Because petitioners used the Visa cards to buy money orders to generate deposits to their bank accounts, respondent contends that petitioners have purchased cash equivalents. Visa gift cards are not redeemable for cash or eligible for deposit into a bank account, which is why petitioners used them to purchase money orders. The benefit provided by allowing a gift card as a substitute for a credit card is conveniently overlooked in respondent's denial of "product" treatment to the gift cards, which depends completely on petitioners' failure to purchase goods or services. Providing a substitute for a credit card is a service via a product which is commonly sold via displays at drug stores and grocery stores. American Express treated such purchases as eligible for Reward Dollars throughout the years at issue. Respondent ignores this, implying that the purchases should not have qualified for Reward Dollars. He points to petitioners' intended use of the cards, but whatever petitioners' intent they paid fees to acquire the gift cards and the convenience embodied in them. The fees were not a function of petitioners' or any customers' intended use of the gift cards.¹⁰

The opinion rejected the IRS's view that these cards were cash equivalents in the manner the Court had found in the case of *Felt v. Commissioner*:

The most recent case respondent cites regarding cash equivalents is *Felt v. Commissioner*, T.C. Memo. 2009-245. In *Felt*, we described the application of the cash equivalent concept to a note that was a promise to pay by a solvent obligor. *Id.*, slip op. at 14-15. Reward Dollars petitioners received were not notes, but they were commitments by American Express to allow petitioners credits against their card balances. Respondent's analysis leaps to the cash equivalence position without an analysis of the origin of the Reward Dollars. Respondent's position holds weight only if the Reward Dollars were not an effect of the purchase price of goods and services. Otherwise, all Reward Dollars would be taxable as cash equivalent income. American Express offered the Rewards Program as an inducement for card holders to use their American Express cards. For his own reasons respondent has

⁹ *Anikeev v. Commissioner*, TC Memo 2021-23, February 23, 2021, p. 12

¹⁰ *Anikeev v. Commissioner*, TC Memo 2021-23, February 23, 2021, pp. 17-18

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made a conscious choice to avoid the application of a rebate analysis to the taxability of the cash rewards as a reduction of basis. In conclusion, we hold that the Reward Dollars associated with the Visa gift card purchases were not properly included in income.¹¹

The Court, however, found that when the taxpayer purchased money orders directly or reloaded debit cards with the American Express card, those rewards were taxable.

However, petitioners' direct purchases of money orders and reloads of cash into the debit cards using the American Express cards presents a different question from the purchase of Visa gift cards. The Visa gift cards have product characteristics. They provide a consumer service embodied in a simple plastic card for convenience. The Visa gift cards are not redeemable for cash, but the money orders purchased with the American Express cards and the infusion of cash into the reloadable debit cards are difficult to reconcile with the IRS credit card reward policy. No product or service is obtained in these uses of the American Express cards other than cash transfers. The money orders are not properly treated as a product subject to a price adjustment because they were eligible for deposit into petitioners' bank account from acquisition. Similarly, the cash infusions to the reloadable debit cards were not product purchases. The reloadable debit cards were used for Moneygram transfers, which are arguably a service. However, the Reward Dollars in dispute were issued for the cash infusions, not the transfer fees. Therefore, we uphold respondent's inclusion in income of the related Reward Dollars for the direct purchases of money orders and the cash infusions to the reloadable debit cards.¹²

A Mess of the IRS's Making

As we've commented recently, the IRS has shown a strong preference for issuing guidance in forms other than regulations or even Revenue Rulings. In this case, we had decades of a rather vague IRS policy on the issue that was derived from a single IRS Revenue Ruling looking at a very specific transaction (purchase of a car).

The Tax Court lectures the IRS on the folly of pursuing issues in this rather haphazard fashion, noting:

We note that the above holdings are not based upon the application of the cash equivalence doctrine but rather the incompatibility of the direct money order purchases and the debit card reloads with the IRS policy excluding credit card rewards for product and service purchases from income. These holdings are based on the unique circumstances of this case. We hope that respondent polices the IRS policy in the future in regulations or public pronouncements rather than relying on piecemeal litigation.¹³

¹¹ *Anikeev v. Commissioner*, TC Memo 2021-23, February 23, 2021, pp. 20-21

¹² *Anikeev v. Commissioner*, TC Memo 2021-23, February 23, 2021, pp. 21-22

¹³ *Anikeev v. Commissioner*, TC Memo 2021-23, February 23, 2021, p. 22

As well, the Court pointed out more than once that the IRS likely would have succeeded if they had gone after the exchange of the gift cards for what clearly were cash equivalents as the taxable event.

But in the final analysis the taxpayer effectively was able to generate nearly \$300,000 of cash on which no tax was paid.

SECTION: 7508A

FOLLOWING WINTER STORM, IRS PROVIDES EXTENSION OF DUE DATE FOR RESIDENTS OF TEXAS

Citation: IR-2021-43, 2/22/21

The IRS has provided relief to taxpayers impacted by winter storms in Texas, pushing back the general return due date from April 15, 2021 to June 15, 2021.¹⁴ As well, the relief will be extended to other states that receive similar disaster declarations by the Federal Emergency Management Agency (FEMA).

The release explains:

Following the recent disaster declaration issued by the Federal Emergency Management Agency (FEMA), the IRS is providing this relief to the entire state of Texas. But taxpayers in other states impacted by these winter storms that receive similar FEMA disaster declarations will automatically receive the same filing and payment relief. The current list of eligible localities is always available on the disaster relief page on IRS.gov.

The release details exactly what items are postponed by this relief:

The tax relief postpones various tax filing and payment deadlines that occurred starting on February 11. As a result, affected individuals and businesses will have until June 15, 2021, to file returns and pay any taxes that were originally due during this period. This includes 2020 individual and business returns normally due on April 15, as well as various 2020 business returns due on March 15. Among other things, this also means that affected taxpayers will have until June 15 to make 2020 IRA contributions.

The June 15 deadline also applies to quarterly estimated income tax payments due on April 15 and the quarterly payroll and excise tax returns normally due on April 30. It also applies to tax-exempt organizations, operating on a calendar-year basis, that have a 2020 return due on May 17.

¹⁴ IR-2021-43, February 22, 2021, <https://www.irs.gov/newsroom/victims-of-texas-winter-storms-get-deadline-extensions-and-other-tax-relief> (retrieved February 23, 2021)

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In addition, penalties on payroll and excise tax deposits due on or after February 11 and before February 26 will be abated as long as the deposits are made by February 26.

The IRS disaster relief page has details on other returns, payments and tax-related actions qualifying for the additional time.¹⁵

The release notes that the IRS will attempt to identify impacted taxpayers:

The IRS automatically provides filing and penalty relief to any taxpayer with an IRS address of record located in the disaster area. Therefore, taxpayers do not need to contact the agency to get this relief.

However, if an affected taxpayer receives a late filing or late payment penalty notice from the IRS that has an original or extended filing, payment or deposit due date falling within the postponement period, the taxpayer should call the number on the notice to have the penalty abated.

In addition, the IRS will work with any taxpayer who lives outside the disaster area but whose records necessary to meet a deadline occurring during the postponement period are located in the affected area. Taxpayers qualifying for relief who live outside the disaster area need to contact the IRS at 866-562-5227. This also includes workers assisting the relief activities who are affiliated with a recognized government or philanthropic organization.¹⁶

Finally the release provides information about tax relief offered in the IRC for those impacted by a disaster:

Individuals and businesses in a federally declared disaster area who suffered uninsured or unreimbursed disaster-related losses can choose to claim them on either the return for the year the loss occurred (in this instance, the 2021 return normally filed next year), or the return for the prior year. This means that taxpayers can, if they choose, claim these losses on the 2020 return they are filling out this tax season. Be sure to write the FEMA declaration number – 4586 – on any return claiming a loss. See Publication 547 for details.¹⁷

¹⁵ IR-2021-43, February 22, 2021

¹⁶ IR-2021-43, February 22, 2021

¹⁷ IR-2021-43, February 22, 2021

SECTION: LEGISLATION

HOUSE PASSES COVID-19 RELIEF PACKAGE WITH TAX AND OTHER PROVISIONS

Citation: American Rescue Plan of 2021, 2/27/21

The bill must still clear the Senate and be signed into law, but the House has now passed the American Rescue Plan of 2021.¹⁸ The bill has 592 pages of material which, while far shorter than the year end Comprehensive Appropriations Act, 2021, is still a very substantial bill with a number of tax and non-tax provisions.

The *Journal of Accountancy* published two articles on the bill as passed by the House, one discussing tax-related provisions in the bill¹⁹ and the other discussing other business related provisions.²⁰

One provision in the House bill that almost certainly will not be in the Senate bill is the provision to increase the minimum wage to \$15 per hour. The Senate parliamentarian has ruled that the provision would not be allowed under the reconciliation rules of the Senate, a necessity for all items in the bill since it is not expected to garner any Republican support. While the Vice President could override the ruling, that move is not expected. This would mean that there would be at least this difference between the bills passed by the chambers, leading to a need to reconcile the bills.

There have been discussions about replacing that provision with a penalty tax on large businesses that don't provide a higher base wage, and a tax credit for smaller businesses that raise such wages. As these would clearly be tax-related items, they could be cleared to be part of a reconciliation package. Whether that provision will be added, clear the Senate and be accepted by the House remains to be seen.

Tax Provisions

Alistair M. Nevius's article notes the following key tax-related provisions found in this bill.²¹

- *Recovery Rebates:* The bill would provide a third advance payment of a recovery rebate, this time providing \$1,400 per taxpayer (\$2,800 for a married couple) and an additional \$1,400 per dependent. Despite discussions that the payment would phase out earlier than prior versions, this version again begins phasing out at \$75,000 of

¹⁸ American Rescue Plan of 2021, February 27, 2021, <https://docs.house.gov/billsthisweek/20210222/BILLS-117hrPIH-american-rescue-planRH.pdf> (retrieved February 27, 2021)

¹⁹ Alistair M. Nevius, J.D., "Tax provisions in the American Rescue Plan Act," *Journal of Accountancy* website, February 27, 2021, <https://www.journalofaccountancy.com/news/2021/feb/tax-provisions-american-rescue-plan-act.html> (retrieved February 27, 2021)

²⁰ Jeff Drew, "House passes \$1.9 trillion stimulus bill with a variety of small business relief," *Journal of Accountancy* website, February 27, 2021, <https://www.journalofaccountancy.com/news/2021/feb/house-passes-stimulus-bill-small-business-relief.html> (retrieved February 27, 2021)

²¹ Alistair M. Nevius, J.D., "Tax provisions in the American Rescue Plan Act," *Journal of Accountancy* website, February 27, 2021

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adjusted gross income (\$150,000 if filing married filing joint). The advance payment will be made using 2019 return numbers unless the taxpayer has already filed his/her 2020 income tax return that the IRS has processed.

- *COBRA Continuation Coverage Credit*
- *Refundable and Advance Child Tax Credit*
- *More Generous Earned Income Tax Credit*
- *Refundable Child and Dependent Care Credit for 2021*
- *Extension Through September 30 and Expansion of Family and Sick Leave Credits*
- *Extend the Employee Retention Credit through the end of 2021*
- *Expansion of the Premium Tax Credit*
- *Repeal of §864(f) that Allowed Affiliated Groups to Allocate Interest on a Worldwide Basis*

Nontax Provisions

Jeff Drew's article²² outlines a number of other changes in the Bill:

- *Funding for state, local and Tribal governments of \$350 billion, \$130 billion for elementary and high schools, \$40 billion for colleges and universities, and \$75 billion for COVID-19 testing and support of vaccine rollout*
- *Small business support including \$15 billion for targeted Economic Injury Disaster Loan advance payments, \$25 billion for restaurants, bars and other providers of food and drink, \$1.25 billion for shuttered venue operators and \$175 million to create a "community navigator" pilot program*
- *Although the end of the program would remain March 31, 2021, the PPP program receives an additional \$7.25 billion of funds and expands to cover additional nonprofit entities*

²² Jeff Drew, "House passes \$1.9 trillion stimulus bill with a variety of small business relief," *Journal of Accountancy* website, February 27, 2021