Current Federal Tax Developments

Week of January 23, 2023

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IRS REPORTS AGENCY NOW ANSWERING PRACTITIONER LINE WITHIN 10 MINUTES

Kristen A. Parillo, "Wait Times Falling for Practitioner Helpline," Tax Notes Today Federal, 1/19/23

An article in *Tax Notes Today Federal* reported that Ken Corbin, the IRS's taxpayer experience officer and Wage and Investment Division Commissioner, stated that the IRS was now answering phone calls to the practitioner helpline in under 10 minutes. Mr. Corbin made this statement in a virtual event hosted by the California Society of Enrolled Agents on January 18, 2023.[1]

Mr. Corbin is cited as stating that the agency is transitioning a workforce of over 12,000 employees back to answering phones.[2]

The article also notes that Mr. Corbin gave some credit for the improvement to the IRS program looking to reduce the effectiveness of robocalling systems:

> Asked by an audience member whether wait times have also been reduced by an IRS initiative to curb robocalls, Corbin said those efforts have played a role. The agency in October 2022 announced plans to use an artificial-intelligence-based tool to weed out calls from phone-queue-jumping services like those offered by enQ Inc.
>
> "We did fix the voice bots," Corbin said. "There were a couple of challenges . . . but we made some improvements to the system. We updated that at the end of the year."[3]

Finally, the article notes that the IRS has eliminated a previous policy that restricted practitioners to discussing five taxpayer accounts per call, though the article did not indicate how many accounts now could be discussed by tax practitioners in a single call.[4]

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[1] Kristen A. Parillo, "Wait Times Falling for Practitioner Helpline," *Tax Notes Today Federal*, January 19, 2023, https://www.taxnotes.com/tax-notes-today-federal/tax-system-administration/wait-times-falling-practitioner-helpline/2023/01/19/7fw7m (retrieved January 20, 2023)

[2] Kristen A. Parillo, "Wait Times Falling for Practitioner Helpline," *Tax Notes Today Federal*, January 19, 2023

[3] Kristen A. Parillo, "Wait Times Falling for Practitioner Helpline," *Tax Notes Today Federal*, January 19, 2023

[4] Kristen A. Parillo, "Wait Times Falling for Practitioner Helpline," *Tax Notes Today Federal*, January 19, 2023

TAXPAYER'S DIABETES DID NOT QUALIFY HIM TO ESCAPE EITHER TAXATION ON RETIREMENT PLAN DISTRIBUTION OR 10% TAX ON A PREMATURE DISTRIBUTION

Lucas v. Commissioner, T.C. Memo. 2023-9, 1/17/23

In the case of *Lucas v. Commissioner*, T.C. Memo. 2023-9, a taxpayer found that his diabetes diagnosis did not either cause his distribution from a §401(k) plan to be exempt from the regular income tax nor exempt it from the 10% tax on a premature distribution under IRC §72(t).

Facts

The opinion begins by describing the situation that led to Mr. Lucas taking the distribution from the §401(k) plan:

> Mr. Lucas began to experience financial problems when he lost his job in 2017. To make ends meet, he obtained a distribution of $19,365 during that year from a section 401(k) plan account administered by Matrix Trust Co. (Matrix). He had not reached 59 ½ years old at the time, and Matrix accordingly reported this amount as an early distribution with no known exception on Form 1099-R, *Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.*[5]

The opinion continues, noting how Mr. Lucas reported the distribution on his tax return:

> For his part, Mr. Lucas reported the distribution on his 2017 federal income tax return but did not include it in his taxable income. Mr. Lucas had been diagnosed with diabetes in 2015, which he had (effectively) treated with insulin shots and other medications. His return reflected his understanding that the distribution did not constitute income because of his medical condition.[6]

The IRS, based upon the Form 1099R issued to Mr. Lucas, determined that the amount he received was both taxable to Mr. Lucas and was subject to the 10% tax under IRC §72(t) as a premature distribution.[7]

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[5] *Lucas v. Commissioner*, T.C. Memo. 2023-9, January 17, 2023, https://www.taxnotes.com/research/federal/court-documents/court-opinions-and-orders/diabetes-didn%e2%80%99t-provide-exception-from-tax-on-early-distribution/7fw2b (retrieved January 21, 2023)
[6] *Lucas v. Commissioner*, T.C. Memo. 2023-9, January 17, 2023
[7] *Lucas v. Commissioner*, T.C. Memo. 2023-9, January 17, 2023

Taxpayer's Attempt to Determine the Tax Treatment via a Web Article

So how had Mr. Lucas come to the determination that this distribution was not subject to tax? He cited an article he found on the internet:

> Mr. Lucas admittedly received a distribution from his 401(k) plan account in 2017. He nonetheless asserts in this Court that this distribution should be excluded from his gross income because of his diabetes. In support of this contention Mr. Lucas relies on a website that (in his view) speaks to these matters.[8]

However, it turns out there were two problems with Mr. Lucas' do-it-yourself tax research. First, he failed to understand the article was talking solely about the 10% addition to tax under IRC §72(t) and not whether the distribution itself was taxable:

> As an initial matter, the website Mr. Lucas relies on addresses the applicability of the early withdrawal penalty in cases of disability, which is a distinct subject from whether the distribution counts as income for those suffering from disability.[9]

But even had the article been dealing with the issue Mr. Lucas thought it did and clearly stated the distribution was not taxable, the Court points out that the article itself is not legal authority:

> More significantly, the website does not constitute legal authority, and nothing in the Internal Revenue Code, Treasury Regulations, or relevant caselaw supports Mr. Lucas's interpretation.[10]

Rather, the law itself treats this distribution includable in Mr. Lucas' income:

> Gross income includes all income from whatever source derived except as otherwise provided. I.R.C. §61(a). This definition includes distributions from employees' trusts. See I.R.C. §§61(b), 72(a)(1), 402(a), (b)(2); see also *Darby v. Commissioner*, 97 T.C. 51, 58 (1991). One type of employees' trust is commonly referred to as a "401(k) plan," a qualified cash or deferred arrangement established for the

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[8] *Lucas v. Commissioner*, T.C. Memo. 2023-9, January 17, 2023
[9] *Lucas v. Commissioner*, T.C. Memo. 2023-9, January 17, 2023
[10] *Lucas v. Commissioner*, T.C. Memo. 2023-9, January 17, 2023

> benefit of employees who meet certain criteria. See I.R.C. §401(k); *Weaver-Adams v. Commissioner*, T.C. Memo. 2014-73, at *4–5.
>
> …
>
> The retirement distribution income accordingly must be included in his 2017 gross income. See I.R.C. §§61(a), 402(a).[11]

The key takeaway from this situation is not that items not constituting legal authority should never be consulted, but rather when doing so the reader must take care on two levels:

- The reader must take care to insure he/she understands *exactly* what the article is discussing. And, on a related point, the reader must never attempt to interpret any ambiguity in the document and determine, based on that interpretation, that the article applies to his/her situation. This is often easier said than done, as we all fall victim to confirmation bias, especially when we know the answer we want.

  In such a situation, it's all too easy to decide the article "clearly" supports the desired result. The question that you must ask in such a case is not "can this be read to support the answer I want" but rather "is it at all possible the author is not speaking to my situation and that the proper answer may be the one I don't want."

- To combat these issues, we need to verify that binding authorities agree with what the article states. For this reason, articles that provide a clear reference to the underlying authorities are far more useful than those that leave off such details. But even when an article does provide such citations, it's important to verify that the authorities actually lead to the conclusion the author arrived at. And, when making that analysis, be conscious of the risk of falling victim to confirmation bias yet again to avoid making what may prove to be an expensive mistake.

  You need to insure that you have developed the skills to be able to read and interpret such authorities, and give them the proper weight that each deserves. As well, you need to be sure that there have not been law changes or other developments since the article was written that would change the analysis.

Ultimately, nonauthoritative articles can be a helpful starting point in arriving at a supportable position in a tax matter, but the tax adviser must be able to defend his/her position by referencing binding legal authorities if the IRS disputes the treatment.

Early Distribution Tax Under §72(t)

So, what about the issue the article was talking about? After all, the IRS did assert that the distribution was subject to the premature distribution tax under IRC §72(t).

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[11] *Lucas v. Commissioner*, T.C. Memo. 2023-9, January 17, 2023

While the case does not discuss what the online article said about the topic, the Court did provide details on how the exemption from the tax under §72(t) based on disability works:

> "Distributions from a qualified retirement account (which includes a 401(k) account) to a taxpayer under 59½ years of age at the time of the distribution are subject to a 10% additional tax unless an exception applies." *Robertson v. Commissioner*, T.C. Memo. 2014-143, at *5; see also I.R.C. §§72(t), 401(k), 4974(c). Section 72(t)(2)(A)(iii) provides one such exception for a distribution "attributable to the employee's being disabled within the meaning of subsection (m)(7)." A taxpayer is considered disabled if, at the time of the disbursement, he is "unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or to be of long-continued and indefinite duration." I.R.C. §72(m)(7); see also *Kopty v. Commissioner*, T.C. Memo. 2007-343, 2007 WL 4142754, at *12–13, *aff'd*, 313 F. App'x 333 (D.C. Cir. 2009); Treas. Reg. § 1.72-17A(f)(1).[12]

The opinion then outlines what a taxpayer must show to provide that he/she is unable to engage in any substantial gainful activity based on a medical condition:

> For these purposes, substantial gainful activity refers to "the activity, or a comparable activity, in which the individual customarily engaged prior to the arising of the disability." Treas. Reg. § 1.72-17A(f)(1). The determination whether an impairment makes one unable to engage in substantial gainful activity depends on all the facts of the case, focusing primarily on the nature and severity of his impairment, as well as factors such as the individual's education, training, and work experience. See id. subparas. (1) and (2). "An individual will not be deemed disabled if, with reasonable effort and safety to himself, the impairment can be diminished to the extent that the individual will not be prevented by the impairment from engaging in his customary or any comparable substantial gainful activity." Id. subpara. (4).[13]

The opinion notes that while diabetes could be such a condition, in Mr. Lucas' case he had been able to continue to perform his work following his diabetes diagnosis:

> Mr. Lucas' diabetes did not render him "unable to engage in any substantial gainful activity" within the meaning of section 72(m)(7) and its accompanying regulations. Although Treasury Regulation § 1.72-17A(f)(2) identifies diabetes as an impairment that "would ordinarily be considered as preventing substantial gainful activity," it

[12] *Lucas v. Commissioner*, T.C. Memo. 2023-9, January 17, 2023
[13] *Lucas v. Commissioner*, T.C. Memo. 2023-9, January 17, 2023

> clarifies that "[a]ny impairment, whether of lesser or greater severity, must be evaluated in terms of whether it does in fact prevent the individual from engaging in his customary or any comparable substantial gainful activity." Treas. Reg. § 1.72-17A(f)(2) (flush language). Mr. Lucas was diagnosed with diabetes in 2015 but was able to work as a software engineer for two years, including the year that he received the distribution from his 401(k) plan account, effectively treating his diabetes with a mix of insulin shots and other medications.[14]

The opinion notes that nothing in the facts given to the court for this case indicated that Mr. Lucas' diabetes had now rendered him unable to engage in any substantial gainful activity:

> The record before us contains no indication that Mr. Lucas's diabetes prevented him "from engaging in his customary or any comparable substantial gainful activity" at the time of the distribution, and we conclude that his condition did "not constitute a disability within the meaning of section 72(m)(7)." See Treas. Reg. § 1.72-17A(f)(4). The distribution in this case accordingly does not qualify for the exception to the early withdrawal penalty set forth in section 72(t)(2)(A)(iii).[15]

IRS ANNOUNCES DEPRECIATION AND LEASE INCLUSION AMOUNTS ON VEHICLES FOR 2023

Revenue Procedure 2023-14, 1/18/23

In Revenue Procedure 2023-14[16] the IRS has released the depreciation limits on automobiles under IRC §280F for 2023.

Table 1[17] applies to passenger automobiles acquired by the taxpayer after September 27, 2017, and placed in service by the taxpayer during calendar year 2023, for which the

[14] *Lucas v. Commissioner*, T.C. Memo. 2023-9, January 17, 2023
[15] *Lucas v. Commissioner*, T.C. Memo. 2023-9, January 17, 2023
[16] Revenue Procedure 2013-14, January 18, 2023, https://www.irs.gov/pub/irs-drop/rp-23-14.pdf (retrieved January 20, 2023)
[17] Revenue Procedure 2013-14, January 18, 2023

§168(k) additional first year depreciation deduction applies. The maximum depreciation deduction allowed for each year is as follows:

Tax Year	Amount
1st Tax Year	$20,200
2nd Tax Year	$19,500
3rd Tax Year	$11,700
Each Succeeding Year	$6,960

Table 2[18] applies to passenger automobiles placed in service by the taxpayer during calendar year 2023 for which no §168(k) additional first year depreciation deduction applies. The maximum depreciation deduction allowed for each year is as follows:

Tax Year	Amount
1st Tax Year	$12,200
2nd Tax Year	$19,500
3rd Tax Year	$11,700
Each Succeeding Year	$6,960

The Revenue Procedure also provides Table 3, which provides the dollar amount used by lessees of passenger automobiles with a lease term beginning in 2023 to determine the income inclusion amount for those passenger automobiles.[19]

[18] Revenue Procedure 2013-14, January 18, 2023
[19] Revenue Procedure 2013-14, January 18, 2023