

Federal Tax Update 2011

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I. Individuals



Public Law 112-9, the Comprehensive 1099 Taxpayer Protection and Repayment of Exchange Subsidy Overpayments Act of 2011, expands the required repayment of excess advance payments of the health insurance premium assistance credit for those with rising incomes effective 2014.

Public Law 112-_____, created a two month extension through February 2012 of the two percent social security tax reduction; unless extended, the reduction expires on February 29, 2012 and self-employeds will apply the two percent reduction to \$18,350 of income.

In National Federation of Independent Business v. Sebelius, and Florida v. Health and Human Services, the US Supreme Court agreed to resolve a split among the Circuits and determine the constitutionality of the healthcare legislation including the individual mandate; 5½ hours of oral argument are scheduled.

In Bakken v. Commissioner, TC Summary Opinion 2011-55, the Tax Court determined that a police officer's disability pension continued to be tax free after he reached age 50 when he would have been eligible to retire had he been able to stay on the job and that it did not convert to taxable retirement as he had completed less than the required 20 years of service and remained ineligible for retirement; the Court distinguished the facts from an earlier Tax Court case in which disability benefits effectively terminated under state law at age 50.

In Harper v. Commissioner, TC Summary Opinion 2011-56, the Tax Court characterized payments by a municipality to the mother of a disabled child as taxable even though she was not a professional caregiver inasmuch as the payments were for her services.

In Karlen v. Commissioner, TC Summary Opinion 2011-129, the Tax Court determined that an individual who withdrew from his children's Section 529 Plan but changed his mind and endorsed the unused check back to the Plan had to include the earnings in income; however, the Court did not impose the 10 percent penalty as the distribution was not used for non-educational expenses.

In Goosen v. Commissioner, 136 TC No. 27, the Tax Court reached a result between that advocated by the taxpayer and the IRS, breaking out the golfer's endorsement fees between personal service income and royalty income and then determining the portion subject to tax in the United States.

In Rose v. Commissioner, TC Summary Opinion 2011-117, the Tax Court determined that interest paid following demolition of an old property to build a vacation home which was never constructed due to financing issues constituted qualified residence interest for up to 24 months.

In Van Dusen v. Commissioner, 136 TC No. 25, the Tax Court determined that out of pocket expenses including a portion of utilities expended in caring for “foster cats” in the home qualified for a charitable deduction.

In Schramm v. Commissioner, TC Memo 2011-212, the Tax Court found that an adjunct professor who taught online courses was an employee and not an independent contractor and could only deduct expenses as miscellaneous itemized deductions.

In Hamper v. Commissioner, TC Summary Opinion 2011-17, a television news anchor was denied a deduction for such expenses as on-air clothing and news magazine subscriptions, the court determined that the clothing expenses were inherently personal despite her testimony that she did not wear such conservative clothing except on the job (she lost credibility by also deducting underwear worn to work).

In McLauchlan v. Commissioner, TC Memo 2011-289, the Tax Court denied all \$100,000 of alleged unreimbursed expenses by a law partner claimed on a Schedule C rather than as an adjustment on a Schedule E; the law partnership reimbursed the partner for over \$60,000 of expenses in each year and had a policy of reimbursing all expenses except for in-town transportation.

In Pang v. Commissioner, TC Memo 2011-55, the Tax Court determined that an individual who went out of pocket by \$250,000 in settling a lawsuit for wrongful death of a pedestrian in an automobile accident could not deduct the payment as a casualty loss (limited to physical damage of a taxpayer's own property).

In Mayo v. Commissioner, 136 TC No. 4, the Tax Court determined that the limitation allowing gambling losses only to the extent of winnings did not apply to other expenses of gambling in the case of a gambling professional.

In Crandall v. Commissioner, TC Summary Opinion 2011-14, the Tax Court disallowed a like-kind exchange where the escrow arrangement did not restrict withdrawals and made no mention of Code Section 1031.

In Bailey v. Commissioner, TC Summary Opinion 2011-22, the Tax Court determined that an individual attempting to qualify as a real estate professional, which would allow all rental property losses to be deducted irrespective of income, could not aggregate the 324 hours spent running an inn which had short term rentals with other rentals inasmuch as the inn activity is reportable on a Schedule C.

In Kay v. Commissioner, TC Memo 2011-159, the Tax Court held that a wage earner averaging \$45,000 per year in income with losses averaging \$850,000 per year from stock trading could not get an ordinary deduction for these losses despite a “mark to market” election inasmuch as he traded only on a small portion of the trading days, had outside income and held most securities in excess of 30 days.

In Schroerlucke v. Commissioner, 108 AFTR2d 2011-5305, the Court of Federal Claims denied a theft loss related to the decline in the stock value of WorldCom of \$6.7 million although the CEO was subsequently convicted of conspiracy to defraud and other crimes; the Court determined that no theft was committed by the Corporation which would have required authorization, request or tolerance by the board of directors or by a manager acting within the scope of his employment.

In Estate of Morhene v. Commissioner, TC Memo 2011-299, the Tax Court denied a theft loss deduction to a former husband for amounts spent by a wife authorized to control the checkbook during their 7-year marriage.

In Tempel v. Commissioner, 136 TC No. 15, the Tax Court determined that the sale of state tax credits constitutes a sale of a capital asset (not a statutory ordinary income item) in which the taxpayer was found under the facts to have no basis; in McNeil v. Commissioner, TC Memo 2011-109, the Tax Court reiterated its decision but found that the gain was short term in this case as there could be no tacking of the period under which the land was held and the subsequent period in which the easement was held.

In Dagres v. Commissioner, 136 TC No. 12, a venture capitalist was allowed a business bad debt deduction as an ordinary loss when he lent money to a person who had given him multiple leads; the dominant motivation was found to be business related.

In Mayo Foundation v. United States, 107 AFTR2d 2011-341, a unanimous US Supreme Court determined that medical students training as residents do not qualify for the student exemption from social security.

In Announcement 2011-14, IRS reversed two prior Information Letters and determined that breast pumps and similar supplies qualify as a medical expense deduction.

In News Release 2011-117, IRS issued the final version of Form 8938 for individuals to report foreign financial assets not reported on another IRS form; thresholds for single individuals living in the United States are \$50,000 on the last day of the tax year or \$75,000 at any time during the tax year (doubled on a joint return) and for singles living abroad \$200,000/\$300,000 (doubled on a joint return).

In Chief Counsel Advice 201125015, IRS confirmed that the federal government is a single employer for purpose of determining whether an employee has received wages equal to the OASDI base.

In Letter Ruling 201135022, IRS revoked Letter Ruling 201005014 which generously allowed employees to receive work related articles of clothing bearing the taxpayer's logo as a *de minimis* fringe benefit.

In Chief Counsel Advice 201138048, IRS determined that an employee is subject to tax on personal use of an employer-provided aircraft to a friend of the employee even if the employee is not on the plane.

In Legal Advice 20115101F, IRS determined that compensation for the temporary taking of property by the Government is ordinary income rather than capital gain because the taxpayer's entire interest in the property was not the subject of an involuntary conversion.

In Action on Decision 2011-03, IRS reversed a 2006 position and accepted a 2010 Tax Court decision which allowed the taxpayer to deduct most costs of sex reassignment surgery as a medical treatment for gender identity disorder.

II. Retirement Plans



In Christy & Swan Profit Sharing Plan v. Commissioner, TC Memo 2011-62, the Tax Court determined that a single participant profit sharing plan which did not make required statutory changes to its documents could lose its exempt status retroactively even though the plan accepted no new contributions.

In Hellweg v. Commissioner, TC Memo 2011-58, the Tax Court determined that an IRA may own a business and that the contribution limits are not subverted despite the annual flow of large dividend payouts to the IRAs (the prohibited transaction rule did not apply as the IRAs obtained the stock at the inception of the corporation); in Ohsman v. Commissioner, TC Memo 2011-98, the Tax Court reiterated its interpretation.

In Chilton v. United States, 107 AFTR2d 2011-1391, a Texas Federal District Court overruled the Bankruptcy Court and that district fell in line with all other Courts which have decided the issue that inherited IRAs qualify for an exemption in bankruptcy; in In Re Thiem, 107 AFTR2d 2011-529, an Arizona Bankruptcy Court reached the same result.

In Willis v. Menotte, 107 AFTR2d 2011-752, the Eleventh Circuit Court of Appeals agreed with a Florida Federal Court that an IRA loses its protection in bankruptcy when the account holder has engaged in a series of prohibited transactions.

In Letter Ruling 201118025, IRS refused to waive the 60-day rollover period for a taxpayer who withdrew funds to assist his elderly mother but failed to redeposit them, indicating that a taxpayer assumes the risk in such a case.

In Letter Ruling 201150037, IRS determined that protections placed on an IRA by a person suffering from bipolar disease requiring, among other steps, notification of the taxpayer's attorney in the case of distributions beyond the required minimum do not disqualify the IRA.

III. Estates and Trusts



Proposed Regulations under Code Section 67
would allow “unusual investment objectives”
of a trust or estate exceeding what would
normally be charged individual investors to be
deducted irrespective of the 2 percent of
adjusted gross income floor.

Proposed Regulations under Code Section 2032 repeal prior Proposed Regulations and provide broad guidance as to how the alternate valuation date works in case of dispositions and exchanges during the six-month period, permitting estates to use alternate valuation not only in the case of a decline due to market conditions but also due to other post-death events including reorganizations and certain distributions.

In In re: Does, 108 AFTR2d 2011-5589, a California Federal District Court allowed IRS to issue a summons to the State of California to detect transfers of real property between non-spouse relatives that were not reported on a gift tax return; California marks the 16th state which will be providing real property transfer records to IRS.

In Estate of Adler v. Commissioner, TC Memo 2011-28, the full value of a large parcel of land divided into fifths during the decedent's lifetime and given to his children was fully included in the estate without discounting as the decedent continued to use and treat the property as his own during his life (which not only brought the gifts back into the estate but also cost the discontinuing of fractional shares).

In Estate of Jorgensen v. Commissioner, 107 AFTR2d 2011-2069, the Ninth Circuit Court of Appeals agreed with the Tax Court that assets transferred to two family limited partnerships remained in a decedent's gross estate where he continued to write checks on partnership accounts to pay personal expenses and to make gifts.

In Estate of Turner v. Commissioner, TC Memo 2011-209, the Tax Court required full inclusion without discounting the full value of assets transferred five years prior into a family limited partnership where the decedent received a management fee for *de minimis* services and the entity made payments for personal purposes of the transferor.

In Estate of Liljestrand v. Commissioner, TC Memo 2011-259, the Tax Court included the full value of family limited partnership assets in a decedent's estate where the partnership agreement guaranteed the decedent all of the income of the partnership.

In Estate of Riese v. Commissioner, TC Memo 2011-60, a residence occupied by a decedent was not included in the gross estate where no rent was paid for the six-month period between termination of a Qualified Personal Residence Trust (QPRT) and the death but an intent to pay could be shown.

In Linton v. United States, 107 AFTR2d 2011-375, the Ninth Circuit Court of Appeals reversed a Washington Federal District Court and remanded the case for further fact finding in order to determine whether gifts of interests occurred prior to creation of a limited liability company (in which case they would not be eligible for discounts) or whether they occurred subsequently (in which case they would be eligible for discounts).

In Estate of Duncan v. Commissioner, TC Memo 2011-256, the Tax Court allowed an illiquid estate to deduct interest expense from a preexisting trust with substantially the same beneficiaries in order to pay estate taxes.

In Estate of Shapiro v. United States, 107 AFTR2d 2011-942, the Ninth Circuit Court of Appeals reversed a Nevada Federal District Court, sending the case back for determining the proper amount of the deduction, and allowed an estate a deduction for the value of a claim by the decedent's live-in paramour who had sued months before death alleging that the couple had agreed to pool resources and to share assets (the claim valued at \$5 million on the return settled at \$1 million following a defense verdict).

In Estate of Saunders v. Commissioner, 136 TC No. 18, the Tax Court denied a \$30 million deduction claimed by the estate of a deceased attorney as an estimate related to a large malpractice claim in that the amount was not reasonably ascertainable at the date of death; the deduction allowed was based on the ultimate payment of \$250,000.

In Bacoei v. United States, 107 AFTR2d 2011-468, the Ninth Circuit Court of Appeals agreed with a California Federal District Court that an incomplete request on Form 4768 for an extension of time to pay estate taxes is not reasonable cause for abatement of the late payment penalty even when accompanied by a letter requesting an extension.

In Revenue Ruling 2011-28, IRS determined that an irrevocable life insurance trust is not included in a decedent's estate by virtue of a power retained by the decedent, as creator of the trust, to substitute assets of equivalent value.

In Revenue Procedure 2011-41 and Notice 2011-66, IRS indicated that estates of 2010 decedents otherwise subject to estate tax avoid the tax by filing Form 8939 and by providing a statement to beneficiaries within 30 days of that filing in order to allocate the limited step-up in basis; the guidance confirms that the Personal Representative may not allocate to an asset beyond its fair market value.

In Notice 2011-37, IRS indicated that investment expenses bundled with fiduciary fees will not need to be segregated until after issuance of final regulations.

Notice 2011-76 gives an extension for filing an estate tax return in the case of 2010 decedents to the later of March 19, 2012 or 15 months after the date of death with no late filing or other penalties due but interest still applying; the due date to file Form 8939 allocating the increase in basis for property acquired from a 2010 decedent was extended two months until January 17, 2012.

In Notice 2011-101, IRS indicated that it is studying the tax treatment on transfers between one irrevocable trust and another, the concept known as “decanting.”

In Letter Ruling 201125009, IRS allowed a surviving spouse to disclaim the balance of her husband's retirement benefits although a distribution was received by automatic quarterly deposit in an account which had been joint with rights of survivorship; the disclaimer related only to the balance in the IRA excluding the post-death deposit.

In Technical Advice Memorandum
201126030, IRS determined that use of the
language “it is my desire” in a Will in the
usual context constitutes a specific bequest.

IV. Business



Public Law 112-10, the Department of Defense and Full-Year Continuing Appropriations Act, repealed the provisions of the Healthcare Legislation dealing with “free choice vouchers” as an alternative to employer sponsored health insurance.

Public Law 112-29, the America Invests Act of 2011, bans tax strategy patents excepting those related to preparation and financial management software.

Public Law 112-56, the 3% Withholding Repeal and Job Creation Act, repeals the 3 percent withholding requirement on payments due to governmental vendors but permits a continuous tax levy on federal payment obligations for property, goods or services received, tightens eligibility for the refundable health-related tax credit and expands the work opportunity tax credit through 2012 to give employers a tax credit of up to \$5,600 for hiring veterans who have been out of work for six months or more and up to \$9,600 for hiring disabled veterans.

Temporary Regulations under Code Sections 162 and 263 establish the distinction between a capital expenditure and a repair, requiring capitalization of improvements to building structures or to component parts such as HVAC, plumbing, electrical, all escalators, all elevators, fire and alarm systems, security systems, gas distribution systems and any other systems separately classified by IRS; (an improvement includes a replacement of a major component of the overall structure or component or a rebuilding to a new like condition after the class life has been exceeded); a retirement of a structural component is treated as a disposition allowing a loss on the undepreciated portion of the component.

Proposed Regulations under Code Section 168,
permit a dropdown from 100 percent to 50
percent bonus depreciation despite
contradictory instructions in the 2010 Form
4562.

Proposed Regulations under Code Section 469

provide that an interest in a limited liability company or limited liability partnership will be treated as an interest of a limited partner in a limited partnership where the entity is classified as a partnership for federal income tax purposes and the holder of the interest does not have rights to manage the entity at all times during the applicable year under law or under the governing documents including the power to bind the entity; the effect is to make the right to participate in management rather than limited liability as the determinant in whether a partner or member can seek to show material participation based on the number of hours of involvement in the activity.

In Gudmundsson v. United States, 107 AFTR2d 2011-852, the Second Circuit Court of Appeals agreed with a New York Federal District Court that income must be recognized by an employee on receipt of an employer's stock despite a one-year inability to transfer the securities in the public market because certain private transfers were permitted; the Court indicated that the trading price set the value despite the fact that it was inflated due to corporate fraud.

In Freda v. Commissioner, 108 AFTR2d 2011-5985, a divided Seventh Circuit Court of Appeals agreed with the Tax Court that a payment to settle trade secret litigation is ordinary income determined by the nature and basis of the action settled rather than the origin of the claim.

In Healthpoint, Ltd. v. Commissioner, TC Memo 2011-241, the Tax Court determined that the allocation in a post-trial settlement must parallel that of the Court decision; punitive damages awarded at trial were recast here.

In Davis v. Commissioner, TC Memo 2011-286, the Tax Court determined that options awarded to a company president and chief executive officer for putting cash in the business for expansion were compensatory in nature, allowing a deduction to the business timed to the reporting of income by the recipient; the Court rejected an additional argument that the value of the options which was in excess of \$36 million constituted unreasonable compensation inasmuch as it was the result of arm's length bargaining although in a family held business.

In Herrington v. Commissioner, TC Memo 2011-73, a business owner was permitted to deduct a theft loss representing funds taken by her boyfriend where she remained silent because he physically abused her and intimidated her verbally with threats to kill her and her children.

In Douglas v. Commissioner, TC Memo 2011-214, a business which acquired an airplane at year end but had no qualified pilot on staff or through outside contract was treated as not having the plane in a state of readiness for use on December 31 and was not allowed to expense or depreciate the cost (the Court did rule in favor of the taxpayer on the accuracy penalty).

In United States v. Howard, 108 AFTR2d 2011-5993, the Ninth Circuit Court of Appeals agreed with a Washington Federal District Court that goodwill on the sale of a dental practice by a C corporation was not personal where the individual had entered into restrictive covenants with the corporation; the Court noted that “the incidence of taxation depends upon the substance, not the form of a transaction” and further stated “so having then made himself available to the advantages of using the corporation, and having entered into the agreements that he did with the corporation, then why should we try to allow him ... out of what he got himself into.”

In Watson v. United States, 107 AFTR2d 2011-311, an Iowa Federal District Court found \$67,000 of purported dividends from the wholly owned S corporation of a certified public accountant with a masters degree in taxation to constitute additional compensation where the CPA took salary of only \$24,000 per year; the Court left alone an average of \$122,000 in other distributions for each of the two years in issue.

In Shellito v. Commissioner, 108 AFTR2d 2011-5218, the Ninth Circuit Court of Appeals, accepting that a spouse may be on a payroll to create a valid family medical reimbursement plan despite being the only employee, remanded the case to the Tax Court to determine whether the spouse was a bona fide employee when she received \$100 per month plus medical reimbursements and the checks were cut on a joint checking account into her individual account (she did work significant hours on the farm).

In Robinson v. Commissioner, TC Memo 2011-99, a vocational instructor teaching police officers and other criminal justice personnel but receiving a paycheck from Temple University under a contract billed to the Commonwealth of Pennsylvania was found to be an independent contractor rather than an employee notwithstanding that he received a W-2 from Temple; the Court looked to the lack of control by the University and the absence of being allowed to participate in benefits given to faculty.

In Colosimo v. United States, 107 AFTR2d 2011-622, the Eighth Circuit Court of Appeals agreed with an Iowa Federal District Court that a 50 percent shareholder and president of a corporation with knowledge of unpaid taxes at some point during the nonpayment could not blame a bookkeeper for failure to pay.

In Concert Staging Services v. Commissioner, TC Memo 2011-231, the Tax Court determined that personal payments labeled “trust fund only” but intended to satisfy a corporation’s installment agreement to IRS could be applied by IRS to non-trust liability in accordance with its Manual.

In Oppliger v. United States, 107 AFTR2d 2011-1518, the Eighth Circuit Court of Appeals followed the weight of authority and agreed with a Nebraska Federal District Court that business owners were responsible for over \$2 million in a trust fund recovery penalty notwithstanding the embezzlement by a bookkeeper who failed to file employment tax returns for more than three years and subsequently committed suicide in that they were responsible parties throughout and used funds for other purposes after they became aware of the liability; the Court indicated that the liability of a newly responsible person is limited to funds on hand upon taking control but this principle does not apply to a responsible person throughout.

In Blackwell v. Commissioner, TC Memo 2011-188, the Tax Court determined that a couple was engaging in horse breeding activities for profit where they had an elaborate business plan and worked diligently in the activity despite full time jobs despite only \$167,000 gross income and \$806,000 in expenses over a 7-year period; the couple had discontinued the activity prior to trial.

In DKD Enterprises v. Commissioner, TC Memo 2011-29, the Tax Court determined that two cat lovers who spent 2,000 and 800 hours per year respectively in the activity including breeding, raising, showing and offering for sale cats were not engaging in a trade or business but were carrying on a hobby, thus disallowing vet bills, litter and food, mileage to cat shows and other expenses (the taxpayers' corporation was however found not to be a personal service corporation as alleged by IRS).

In Campbell v. Commissioner, TC Memo 2011-42, the Tax Court determined that an Amway distributorship was not run for profit but was for the purpose of acquiring products at a discount for use in other businesses and for personal consumption under facts indicating that the activity was not conducted in a business-like manner.

In Rundlett v. Commissioner, TC Memo 2011-229, the Tax Court found that a taxpayer owning 11 weekly timeshares was not engaged in an activity for profit but a “fly by the seat of the pants experiment” involving pleasure travel to lavish beach resorts.

In Revenue Ruling 2011-29, IRS reversed itself and indicated that an accrual basis employer can accrue a dollar amount for bonuses even if individual bonuses are not set provided that the amount cannot revert to the employer and must be divided among employees.

In Revenue Procedure 2011-29, IRS created a “safe harbor” for “success fees” in transactions, permitting payors to immediately deduct 70 percent of the fees while capitalizing the remaining 30 percent.

In Notice 2011-1, IRS delayed the effective date of the nondiscrimination rules for new group health insurance plans which were scheduled to take effect September 23, 2010 for plans not in existence on enactment of the healthcare legislation until an undetermined date subsequent to the issuance of regulations.

In Notice 2011-28, IRS announced that small employers with under 250 Forms W-2 will not be required to report health coverage cost information on the W-2 at least through 2012.

In Announcement 2011-64, IRS announced an effective “amnesty” for businesses treating workers improperly as independent contractors under which the business may file Form 8952 at any time and pay 10 percent of the amount which would have been payable in the preceding tax year in the event of an IRS audit on the groups of workers being converted to employee status; eligibility requires that the workers must have been treated consistently as independent contractors, Forms 1099 must have been issued in the three preceding years when required, the taxpayer must not be under examination by IRS for any reason and the taxpayer must not be under examination by the Department of Labor or any state agency regarding classification (if examined previously, the taxpayer must have complied with the results).

In Field Attorney Advice 2011101, IRS indicated that an automobile dealer could not write off a portion of goodwill acquired when he purchased a franchise containing four lines of automobiles notwithstanding that the manufacturer terminated one line; a 15-year write off continues to apply to all goodwill acquired in the same transaction.

In Action on Decision 2011-06, IRS announced its acquiescence in the 2011 decision of the Tax Court in Mayo that the indirect expenses of a gambler engaged in such a business are not subject to an income limitation as are the direct losses.

In Letter Ruling 201114015, IRS allowed 12 subsidiaries engaging in the practice of medicine in separate states to deduct insurance payments to a “captive company” also owned by the parent finding that there was a sufficient shifting of the risk.

In Internal Legal Memorandum 20115002F, IRS determined that costs associated with retrieving company artifacts for exhibiting at company headquarters are not an “ordinary and necessary” business expense.

In Chief Counsel Advice 201151020, IRS determined that meals provided to airline crew members do not qualify as a “de minimis” fringe benefit; IRS found that the meals are excludable as they are furnished on the employer’s business presence for the convenience of the employer but that only 50 percent of the cost may be deducted by the employer rather than 100 percent if it had qualified as de minimis.

In Chief Counsel Advice 201151021, IRS determined that increased interest deductions in closed years, although not usable in those years or in carryback years, may be carried forward to open years to the extent that they would not have been absorbed in the tax years or carryback years.

V. Procedure



Public Law 112-9, the Comprehensive 1099 Taxpayer Protection and Repayment of Exchange Subsidy Overpayments Act of 2011, repealed the previously enacted expansion of the use of Forms 1099 including its applicability to products, payments made generally to corporations and payments by owners of rental properties.

Proposed Regulations under Code Section 6402 set forth guidance on various types of refunds, stating that, in the absence of specific directive on a form, a refund must be filed with the Service Center at which a taxpayer would be required to file a current tax return for the type of tax related to the claim.

Final Regulations under Circular 230 set the rules for Registered Tax Return Preparers (RTRPs) who are not attorneys, CPAs or Enrolled Agents, permitting them to represent taxpayers before Revenue Agents, customer service representatives and the Taxpayer Advocate but not before Revenue Officers or Appeals Officers.

Proposed Regulations under Circular 230

would require uncredentialed tax return preparers to be fingerprinted; attorneys, CPAs, enrolled agents and enrolled actuaries would be exempt.

In United States v. Richey, 107 AFTR2d 2011-573, the Ninth Circuit Court of Appeals reversed an Idaho Federal District Court and determined that the work papers of an appraiser retained by a law firm who valued a charitable easement were reachable in discovery and were not attorney work product or otherwise protected by attorney-client privilege.

In Custom Stairs and Trim Ltd., Inc. v. Commissioner, TC Memo 2011-155, the Tax Court abated a company's failure to deposit penalty, determining reasonable cause from significant business downturns and from "cascading" penalties because of allocations to the earliest tax liability; the Court noted that certain circuits have taken a contradictory position that financial difficulties can never constitute reasonable cause for failure to deposit.

In Wickersham v. Commissioner, TC Memo 2011-178, taxpayers were found not liable for the accuracy penalty when they hired an enrolled agent to prepare their return who made several errors; the Court determined that the preparer's experience and expertise was sufficient to justify reliance where they provided her with all needed and accurate information.

In Seven W Enterprises, Inc., et al., v. Commissioner, 136 TC No. 26, the Tax Court determined that a business could not avoid the accuracy related penalty based on professional advice when the CPA was an in-house employee (abating the penalty for the earliest year in which he was an outside accountant and separately paid preparer).

In Olsen v. Commissioner, TC Summary Opinion 2011-131, the Tax Court determined that a taxpayer was not liable for the accuracy penalty when he made an “isolated error” in entering K-1 information on the input sheet of his tax preparation software.

In United States v. Quinn, 107 AFTR2d 2011-712, a Kansas Federal District Court ruled that an individual could be prosecuted for willful failure to pay over payroll taxes notwithstanding that she paid the full liability before her trial.

In Shockley v. Commissioner, TC Memo 2011-96, IRS was not allowed to proceed against three former shareholders for amounts in excess of \$26 million as transferees inasmuch as IRS did not send the notice of deficiency against the corporation to its last known address and, accordingly, was returned as undeliverable.

In Thompson v. Commissioner, 137 TC No. 17, a divided Tax Court determined that the applicability of an accuracy penalty relating to a partnership investment in a tax shelter is determined at the partnership level in a TEFRA proceeding.

In Jade Trading, LLC v. United States, 107 AFTR2d 2011-1832, the Court of Federal Claims determined that accuracy related penalties must be determined at the individual level in a TEFRA proceeding where “outside basis” affects the applicability of the penalty.

In Bloomfield State Bank v. United States, 107 AFTR2d 2011-2153, the Seventh Circuit Court of Appeals reversed an Indiana Federal District Court and determined that a bank mortgage loan including a provision giving the bank a security interest in future rental income takes priority over a subsequently filed federal tax lien even though the rentals were received after the tax lien was filed.

In United States v. Heli USA Airways, Inc., 108 AFTR2d 2011-7216, a Nevada Federal District Court indicated that an employer was liable for an employee's unpaid taxes and additions as well as a 50 percent penalty directly against the Company for failure to honor a levy upon the employee's pay; the fact that the CFO had a mental breakdown was determined as insufficient to even avoid the statutory 50 percent penalty.

In United States v. Ryan, 107 AFTR2d 2011-1785, a California Federal District Court allowed IRS to seize the principal residence of a couple with a \$6.2 million outstanding tax liability where no voluntary payment had been made in five years and a transfer of assets to avoid levy had previously been made.

In Law Offices of Scott E. Combs v. United States, 107 AFTR2d 2011-784, a law firm was unable to challenge a levy on its trust account due to “lack of standing”, forcing individual clients to sue for funds; IRS believed that the taxpayer was commingling personal and trust funds.

In Azzari v. Commissioner, 136 TC No. 9, the Tax Court determined that IRS abused its discretion in not subordinating its lien and in not granting an installment arrangement where the taxpayer showed that it would have been able to remain current in payroll taxes and make installment payments upon the subordination.

In Tucker v. Commissioner, TC Memo 2011-67, the Tax Court determined that losses from day trading activities constitute “dissipated assets” that IRS could consider in determining the reasonable collection potential for purpose of considering a taxpayer’s offer in compromise.

In Milhouse v. Commissioner, TC Summary Opinion 2011-12, the Tax Court gave innocent spouse relief to a wife who maintained separate finances from her husband for the one year that they were married and could file a joint return, determining that the wife did not have actual knowledge of the husband's withdrawals from a retirement plan; IRS attempted to improperly use the "reason to know" standard as opposed to the required actual knowledge of the withdrawals.

In Richard v. Commissioner, TC Memo 2011-144, a husband was granted innocent spouse relief to a taxpayer related to his former wife's non-reporting of a \$50,000 distribution from a retirement plan; the Court indicated that the husband may have had reason to know of the distribution but lacked actual knowledge which would have denied him the requested relief.

In Thomassen v. Commissioner, TC Memo 2011-88, the Tax Court gave equitable innocent spouse relief to a wife of 50 years from liabilities on joint returns dating back to 1964 which caused IRS to seek foreclosure of the marital home after the husband's death; the husband, an orthopedic surgeon, was found to have abused her psychologically during more than 50 years of marriage with fits of rage and controlling behavior.

In Torrise v. Commissioner, TC Memo 2011-235, a widow who separated from her husband a decade prior to his death but continued to file joint returns for a number of years following the separation was granted equitable innocent spouse relief for all but the last year with the distinction being that at that point she should have known that the liability would not be paid.

In Waldron v. Commissioner, TC Memo 2011-288, a psychologist was given equitable innocent spouse relief for 30 percent of the unpaid liabilities, tied to the percentage of the pre-divorce installment payments paid by her husband rather than the 50-50 split under the divorce decree where the circumstances strongly suggested that the taxpayer reasonably believed that her former husband would pay only 30 percent.

In Harbin v. Commissioner, 137 TC No. 7, the Tax Court determined that a prior trial in that Court did not bar the husband of a gambler from claiming innocent spouse relief in a subsequent proceeding as he was held to not have participated meaningfully in the prior case where the attorney represented both parties and did not advise as to or assert innocent spouse relief for the husband.

In United States v. Home Concrete & Supply, LLC, the US Supreme Court agreed to hear an appeal from IRS from a decision of the Fourth Circuit that an overstatement of basis does not give rise to a six-year statute of limitations based on understatement of gross income; the Courts of Appeal are deeply divided.

In Brady v. Commissioner, 136 TC No. 19, the Tax Court determined that overpayments in earlier tax years for which refund claims were filed late may not only result in a denied refund but also in a denial as an offset to liability in succeeding years.

In Boensel v. United States, 108 AFTR2d 2011-5626, the US Court of Claims determined that an overpayment of approximately \$112,000 of a \$435,000 payment against federal estate tax was an estimated tax payment and not a “tax deposit”; the latter would have permitted return of an overpayment seven years late but the deposit mechanism was not added to the law until five years after the payment was made.

In Nicholas Acoustics & Specialty Company v. United States, 107 AFTR2d 2011-950, the Fifth Circuit Court of Appeals agreed with a Mississippi Federal District Court that payroll tax remittances were payments rather than “tax deposits” and thus were subject to a 3-year statute of limitations on refunds.

In United States v. Storey, 107 AFTR2d 2011-844, the Sixth Circuit Court of Appeals reversed an Ohio Federal District Court and determined that an individual who met the statutory criteria for discharging income taxes in bankruptcy could not be denied a discharge on a theory of evasion where IRS was unable to show a lavish lifestyle.

In In Re Cannon, 107 AFTR2d 2011-2070, a Georgia Bankruptcy Court concurred with the prevailing view and determined that liability shown on IRS-prepared Substitute for Returns (SFR) can never be discharged in bankruptcy.

In Revenue Procedure 2011-25, IRS indicated that a preparer required to file electronically must obtain a hand-signed and dated statement documenting a taxpayer's choice to file a paper return in which case the return must actually be sent by the taxpayer; an email statement from the taxpayer is insufficient according to the IRS.

In Notice 2011-80, IRS indicated that preparer tax identification numbers (PTINs) must be renewed on an annual basis commencing October 16 of the preceding year.

In News Release 2011-14, IRS revealed a new voluntary disclosure program for taxpayers with undeclared offshore assets under which individuals coming forward would not be criminally prosecuted but must pay back taxes, interest and penalties for eight years (instead of six under the prior program) and creating an additional 25 percent penalty applied to the highest account balance (up from 20 percent under the prior program); a 12½ percent rate will apply for accounts of \$75,000 or less and a 5 percent rate will apply to taxpayers with little connection to their accounts).

In News Release 2011-20, IRS announced that it would not impose a federal tax lien in the case of direct debit installment agreements where the debt is less than \$25,000 and indicated that it would streamline the Offer in Compromise procedure for taxpayers with liabilities of less than \$50,000 and annual incomes of up to \$100,000.

In News Release 2011-80, IRS announced that it will not apply a two-year limitation on seeking equitable innocent spouse relief after the first targeted collection activity.

In Chief Counsel Memorandum 2011-5, IRS indicated its acquiescence in a 2009 Tax Court case of Vinatieri v. Commissioner, 133 TC No. 16, requiring IRS to release a levy creating economic hardship even if the taxpayer has not filed required returns.

In Program Manager Technical Assistance 2010-67, IRS attempted to distinguish a deposit from an overpayment which has a three year statute of limitations, indicating that a deposit must be labeled as such, applied to unassessed taxes and the tax years and basis for the disputable tax must be set forth.

In IRS Memorandum SBSE-05-0711-064, IRS created a policy in which a revenue officer must contact an employer within 15 days following notification through an “alert program” when a semi-weekly payroll tax depositor becomes delinquent (the intent is to catch large delinquencies prior to filing of the quarterly returns).

In Chief Counsel Advice 201106009 and 201106010, IRS said that “adult entertainment clubs” and other businesses that pay cab drivers to deliver customers must file Form 1099 for each driver paid \$600 or more in a calendar year.

In Chief Counsel Advice 201118020, IRS determined that a taxpayer who omits over 25 percent of gross income on the original tax return cannot avoid a six-year statute of limitations on assessment by filing an amended return.

In Chief Counsel Advice 201134018, IRS determined that IRS is precluded from cancelling acceptance of an amended return and reinstating the original liability once the statute of limitations has expired on the original return.

A TIGTA Report dated December 20, 2011 indicated that more than 300 prisoners have received PTIN numbers including 43 who are serving life sentences.

The End



About the Speaker

David S. De Jong is an attorney and certified public accountant accredited in estate planning by the National Association of Estate Planners & Councils (AEP) and credentialed in valuation by both the American Institute of Certified Public Accountants (ABV) and the National Association of Certified Valuation Analysts (CVA). A principal of the Rockville, Maryland law firm of Stein, Sperling, Bennett, De Jong, Driscoll & Greenfeig P.C., Mr. De Jong was named in the December 2006 issue of *Worth* as one of the country's top 100 attorneys and has been twice honored by *CPA Magazine* – in the April-May 2008 issue as one of the country's top 50 IRS Representation Practitioners and in the April-May 2009 issue as one of the country's top 40 Tax Advisors. Mr. De Jong has been listed twice in *Maryland Super Lawyers* as among the top 50 attorneys in the State as chosen by his peers and in *Washington DC Super Lawyers* as among the top 100 “votegetters.” He has also been listed multiple times in *Washingtonian* magazine and *Washington Smart CEO* as one of the D.C./Maryland area's top professionals; among 41 top tax attorneys listed in the December 2011 *Washingtonian*, he was the only one with a suburban office. Mr. De Jong was one of 36 attorneys in the State of Maryland to have received initially the highest possible rating of 10.0 by Avvo.

Mr. De Jong has litigated cases in each of the four judicial forums for federal tax controversies as well as in Maryland Tax Court. He is a frequent writer, lecturer and expert witness on various tax, estate, valuation and business topics. Trained in collaborative law, he has arbitrated and mediated family law disputes. Mr. De Jong has testified before the IRS Oversight Board, been quoted in various publications including the *Wall Street Journal*, *New York Times*, *Fortune Small Business*, *Redbook* and *The Value Examiner* and been profiled in *CPA Magazine* and *Warfields*. His 25 plus speeches annually in the Washington area and nationally focus on federal and state tax developments and on tax and business planning. Mr. De Jong has taught 14 different tax and business management courses at five universities, including 20 years as an Adjunct Professor of Taxation in the Kogod School of Business at American University in Washington, D.C. and, most recently, as a Visiting Professor at the Washington & Lee University School of Law. For 16 years he co-authored the J.K. Lasser annual tax planning book entitled *Year-Round Tax Strategies*. Mr. De Jong received a B.A. degree from the University of Maryland, a J.D. degree from Washington and Lee University where he served as a Law Review editor and an LL.M. degree in Taxation from the Georgetown University Law Center.

Mr. De Jong currently serves on the Character Committee of the Maryland Court of Appeals for the Seventh Appellate Circuit, on the Board of Directors of the Montgomery County (Maryland) Bar Foundation and on the Ethics Board of the National Association of Certified Valuation Analysts (NACVA). He also continues as a Director of the American Association of Attorney-Certified Public Accountants (AAA-CPA), having served as its President for 2003-04 after previously holding every other office in the organization. In 2009 he became the 8th person to receive the Louis S. Goldberg Memorial Award for lifetime services to the AAA-CPA. Mr. De Jong has served as Vice President and President of the Maryland-DC Chapter of NACVA (winning a State Chapter Presidents' Leadership Award), as President, Vice President and Secretary of the Estate Planning Council of Suburban Maryland, as a Trustee of the Attorney-CPA Foundation, as a member of the Maryland State Bar Association Tax Section Council, as Treasurer and Board member of the Metropolitan Center for the Visual Arts, and as Treasurer and Tax Section Chair of the Montgomery County Bar Association as well as Treasurer of its Foundation. In 2008 the Association bestowed on him the President's Citation for Distinguished Service and its Foundation awarded him the Bar Leaders Award for lifetime service to the organization.