RECENT DEVELOPMENTS IN FEDERAL INCOME TAXATION

"Recent developments are just like ancient history, except they happened less long ago."

By

Bruce A. McGovern
Professor of Law and Director, Tax Clinic
South Texas College of Law Houston
Houston, Texas 77002
Tele: 713-646-2920
e-mail: bmcgovern@stcl.edu

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Note: This outline was prepared jointly with Cassady V. ("Cass") Brewer, Associate Professor of Law, Georgia State University College of Law, Atlanta, GA.

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I. ACCOUNTING

A. Accounting Methods

B. Inventories

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II. BUSINESS INCOME AND DEDUCTIONS

III. INVESTMENT GAIN AND INCOME

A. Gains and Losses

1. Pyrrhotite cracking the foundation of your house? IRS to the rescue! Rev. Proc. 2017-60, 2017-50 I.R.B. 559 (11/23/17). Pyrrhotite is a naturally occurring mineral in stone aggregate used to produce concrete. Pyrrhotite oxidizes in the presence of water and oxygen, leading to expansion that cracks and deteriorates concrete foundations prematurely. As discovered and reported by the Connecticut Department of Consumer Protection, some homeowners in New England have suffered premature deterioration in their concrete foundations due to pyrrhotite. This had led taxpayers to inquire of the IRS whether the damage to their concrete foundations caused by pyrrhotite may be claimed as a personal casualty loss under § 165. Normally, a § 165 casualty loss is limited to an identifiable event that is sudden, unexpected, or unusual and that causes damage to property. The amount of a taxpayer's casualty loss ordinarily is the decrease in the fair market value of the property (less any insurance reimbursement) as a result of the casualty, not to exceed the taxpayer's adjusted basis in the damaged property. On the other hand, damage or loss resulting from progressive deterioration of property through a steadily operating cause generally is not considered a casualty loss within the meaning of § 165. *Matheson v. Commissioner*, 54 F.2d 537 (2d Cir. 1931). If a § 165 casualty loss is sustained for personal use property, a deduction is allowable only for (i) the amount of the loss that exceeds $100 per casualty and (ii) the net amount of all of the taxpayer's personal casualty losses (in excess of personal casualty gains, if any) that exceeds 10 percent of the taxpayer's adjusted gross income for the year. In Rev. Proc. 2017-60, the IRS concludes that damage to concrete foundations caused by pyrrhotite may qualify as a § 165 casualty loss if the loss is determined and reported in compliance with the guidance provided by the revenue procedure. Specifically, the revenue procedure creates a safe harbor under which a taxpayer who pays to repair damage to the taxpayer's personal residence caused by pyrrhotite may treat the amount paid as a casualty loss in the year of payment. To qualify for the safe harbor, an affected taxpayer must obtain either (1) a written evaluation from a licensed engineer indicating that the foundation was made with defective concrete and obtain a reassessment report that shows the reduced value of the property based on the written evaluation from the engineer and an inspection pursuant to Connecticut Public Act No. 16-45, or (2) a written evaluation from a licensed engineer indicating that the foundation was made with defective concrete containing the mineral pyrrhotite. The amount of the casualty loss is the amount paid by the taxpayer to repair the damage (limited by the taxpayer's basis in the property and reduced by any insurance proceeds received for the damage). The revenue procedure also specifies other guidelines for claiming a pyrrhotite casualty loss, including reporting the loss on IRS Form 4684 with "Revenue Procedure 2017-60" typed at the top of the form. The revenue procedure is effective for federal income tax returns (including amended returns) filed after November 21, 2017.

a. Thanks again to the IRS, you have until October 15, 2018, to address those pesky pyrrhotite problems. Rev. Proc. 2018-14, 2018-9 I.R.B. 378 (2/7/18). As noted above, Rev. Proc. 2017-60 allowed qualifying taxpayers to claim a casualty loss attributable to pyrrhotite damage in the year the taxpayer paid to repair the damage. For taxable years beginning after 2017 and before 2026, however, new Code § 165(h)(5) (added by § 11044 of the 2017 Tax Cuts and Jobs Act) eliminates the deduction for personal casualty losses (other than those attributable to a federally declared disaster). As a result, the victims of pyrrhotite damage, who otherwise were granted relief under Rev. Proc. 2017-60 above, are denied relief unless they made repair payments before January 1, 2018. This revenue procedure mercifully amends Rev. Proc. 2017-60 to extend the time for taxpayers to pay for pyrrhotite damage and claim a casualty loss deduction on their 2017 or earlier tax returns. Essentially, taxpayers may pay for pyrrhotite damage (as long as the offending concrete was poured before January 1, 2018) up until October 15, 2018, and if they otherwise qualify for relief under pre-TCJA § 165 and Rev. Proc. 2017-60, they may claim a casualty loss deduction for the payment on their original or amended tax return for 2017. Specifically, the revenue procedure provides:

> If a taxpayer pays to repair damage to that taxpayer's personal residence caused by a deteriorating concrete foundation during the taxpayer's 2016 taxable year or earlier, the taxpayer may treat the amount paid as a casualty loss on a timely Amended U.S. Individual Income Tax Return (Form 1040X) for the taxable year of payment. If a taxpayer pays to repair the damage during the taxpayer's 2017 taxable year or prior to a timely filed (including extensions) original U.S. Individual Income Tax Return (Form 1040, 1040A or 1040EZ) for the 2017 taxable year, the taxpayer may treat the amount paid as a casualty loss on the taxpayer's original 2017 income tax return (or a timely filed Form 1040X for the 2017 taxable year). If a taxpayer pays to repair the damage after filing an original 2017 income tax return and prior to the last day for filing a timely Form 1040X for the 2017 taxable year, the taxpayer may treat the amount paid as a casualty loss on a timely filed Form 1040X for the 2017 taxable year. For purposes of this revenue procedure, the term "deteriorating concrete foundation" means a concrete foundation that is damaged as a result of the presence of the mineral pyrrhotite in the concrete mixture used before January 1, 2018, in pouring the foundation.

B. **Interest, Dividends, and Other Current Income**

C. **Profit-Seeking Individual Deductions**

D. **Section 121**

E. **Section 1031**

F. **Section 1033**

G. **Section 1035**

H. **Miscellaneous**

IV. COMPENSATION ISSUES

V. PERSONAL INCOME AND DEDUCTIONS

A. **Rates**

B. **Miscellaneous Income**

1. What's $19 million among friends? A taxpayer who received funds to invest but who used them for personal purposes had gross income. Sun v. Commissioner, 880 F.3d 173 (5th Cir. 1/18/18), *aff'g* T.C. Memo. 2015-56 (3/24/15). The taxpayer controlled and served as Chief Executive Officer of a corporation whose primary business was importing and distributing minerals. He also devoted a significant amount of time to investment activities, both through an LLC that he controlled and through his personal online brokerage account. The taxpayer and his business acquaintance and friend, a Chinese citizen and resident of Hong Kong, orally agreed that the taxpayer would invest his friend's funds. Over a period of two years, the friend sent $19 million to be invested. Of this amount, approximately $15 million was sent to the corporation the taxpayer controlled, where it was held in an officer loan account solely for the taxpayer's benefit. The corporation treated the balance in the account as funds the taxpayer had loaned to the corporation that eventually would be repaid to him. The remaining $4 million was sent either to the taxpayer's personal brokerage account or to the LLC through which he conducted investment activities. Although the taxpayer did invest these latter funds, they were commingled with the taxpayer's own funds and the taxpayer did not maintain a separate accounting of their performance. The taxpayer used several million of the funds in the officer loan account for personal purposes, including the purchase of a Mercedes Benz automobile and for gambling. The taxpayer informed his friend that he had lost approximately $2 million of the friend's funds through gambling. In notices of deficiency issued both to the corporation and to the taxpayer, the IRS asserted the following alternative theories: (1) the corporation must include in gross income the amounts received from the taxpayer's friend and must be treated as making dividend distributions to the taxpayer that resulted in gross income for the taxpayer, and the taxpayer also must include in gross income all fund he received directly from his friend, or (2) the corporation acted merely as a conduit and the taxpayer must include in gross income all amounts received by him and by the corporation. The taxpayer argued that none of the amounts received from his friend were included in the corporation's or his gross income because they were either loans or funds entrusted to the taxpayer for investment. The Tax Court (Judge Paris) held that the funds in question were neither gifts nor loans but were amounts entrusted to the taxpayer for investment; nevertheless, the Tax Court held that the taxpayer had to include in gross income all of the amounts sent by the taxpayer's friend because the taxpayer had misappropriated them. In an opinion by Judge Costa, the U.S. Court of Appeals for the Fifth Circuit affirmed the Tax Court's decision. The court acknowledged that, although the nature of the oral agreement between the taxpayer and his friend was not entirely clear, his friend expected to receive back some funds at some point. Nevertheless, the court relied on *James v. United States*, 366 U.S. 213 (1961), for the proposition that misappropriated funds are included in gross income:

> An obligation to "return some money at some point" is not, however, inconsistent with misappropriation. … For all but the riskiest of investments, an investor with a diversified portfolio expects to get some money back even if the investments do not turn out well. But that does not mean the recipient of the funds is allowed to make personal use of the money. And when the holder of the funds uses the money to enrich

> himself, he has received "economic value," which is the defining characteristic of income. …
>
> A vague understanding that some money will be returned at some undefined time is not the mutual recognition of an agreement to repay in full that *James* contemplates.

The court also affirmed the Tax Court's imposition of the 20 percent accuracy-related penalty of § 6662(a) and (b)(1) for negligence or disregard of rules or regulations in omitting the income in question.

C. Hobby Losses and § 280A Home Office and Vacation Homes

D. Deductions and Credits for Personal Expenses

E. Divorce Tax Issues

F. Education

G. Alternative Minimum Tax

VI. CORPORATIONS

A. Rates

B. Entity and Formation

C. Distributions and Redemptions

D. Liquidations

E. S Corporations

F. Mergers, Acquisitions and Reorganizations

1. Maybe Chubby Checker said it best: ♫♪Jack be nimble; Jack be quick. Jack go under [COI] limbo stick.♪♫ Rev. Proc. 2018-12, 2018-6 I.R.B. 349 (1/24/18). Among other requirements, shareholders of a target corporation must maintain a "substantial" proprietary interest (i.e., stock) in an acquiring corporation to qualify a transaction for tax-deferred reorganization treatment under § 368. The regulations under § 368 set forth this shareholder continuity of interest ("COI") test. *See* Reg. § 1.368-1(e). The COI requirement is designed to prevent transactions that resemble sales from qualifying for tax-deferred reorganization treatment. Determining whether adequate COI exists for any particular transaction requires a comparison of the aggregate value of the target shareholders' stock before the reorganization with the aggregate value of their stock held in the acquiring corporation after the reorganization. The required level of COI—jokingly, the "limbo stick"—varies in height depending upon the type of reorganization attempted (e.g., 50% safe harbor for straight and forward triangular mergers; 80% statutory requirement for reverse triangular mergers). Put differently, if boot in a reorganization is too high, the COI limbo stick is tripped, and the shareholders of the target corporation will not qualify for nonrecognition treatment. Thus, regardless of the type of reorganization attempted, valuation of the target shareholders' pre- and post-reorganization stockholdings is critical for obtaining nonrecognition treatment.

- *Average trading price valuations allowed*. Subject to other requirements and limitations, since 2011 Treasury and the IRS have permitted applicable COI tests to be met based upon <u>actual trading values</u> of publicly-traded acquiror stock on either the closing date (as defined) or the signing date (as defined). *See* Reg. § 1.368-(e)(2). Proposed regulations promulgated in 2011 for publicly-traded acquirors provide that, under specified circumstances, certain *average* trading price determinations of value are allowed for COI purposes. *See* Prop. Reg. § 1.368(e)(2)(vi)(A). Commentators noted that average trading price methods often are used to determine the actual consideration paid by an acquiring corporation to target shareholders under acquisition agreements, so those same commentators argued that such average trading price methods should be acceptable for COI purposes in lieu of actual trading prices on either the closing date or signing date. Rev. Proc. 2018-12 reflects Treasury's and the IRS's general agreement with the commentators that average trading price valuation methods are acceptable for COI purposes. The revenue procedure describes in detail the average trading price valuation methods that may be used for certain reorganization transactions. In particular, Rev. Proc. 2018-12 specifies that it applies to § 368(a)(1)(A) [mergers], (B) [stock for stock], (C) [stock for assets], and (G) [bankruptcy] reorganizations where the acquiring corporation is publicly traded. The safe harbor valuation methods outlined in the revenue procedure are (i) the average of the daily volume weighted average prices; (ii) the average of the average high-low daily prices; and (iii) the average of the daily closing prices. Of course, the specific requirements and limitations of Rev. Proc. 2018-12 are quite technical and must be carefully considered in connection with any potential reorganization transaction relying upon the revenue procedure for COI purposes. Nonetheless, the takeaway is that if one of the foregoing valuation methods is used to determine the stock consideration paid to target shareholders by a publicly-traded acquiring corporation in one of the specified reorganizations, then such method generally may be used for COI purposes as well. Rev. Proc. 2018-12 states that it only applies for COI purposes (not other valuation purposes) and that if the safe harbors of the revenue procedure are not met, the reorganization nevertheless may qualify for nonrecognition treatment under general federal tax principles. Finally, Rev. Proc. 2018-12 provides that the IRS will entertain requests for rulings and determination letters that fall outside the scope of the revenue procedure.

G. Corporate Divisions

H. Affiliated Corporations and Consolidated Returns

I. Miscellaneous Corporate Issues

1. "Lucy, you got some 'splainin' to do" about taxable versus nontaxable contributions to capital. The 2017 Tax Cuts and Jobs Act, § 13312, amended Code § 118 to limit the exclusion for nonshareholder contributions to capital. Pursuant to new § 118(b)(2), nonshareholder contributions to capital made by "any governmental entity or civic group (other than a contribution made by a shareholder as such)" after December 22, 2017, no longer are excludable from the recipient corporation's gross income. Such nontaxable contributions have been made in the past by governmental entities and civic groups to incentivize acquisition and redevelopment projects considered important to those entities and groups. As a nod to these past arrangements, a transition rule grandfathers certain capital contributions made under master development plans approved by governmental entities on or before December 22, 2017. *See* TCJA § 13312(b)(2). Amended § 118 also provides Treasury with regulatory authority to interpret and implement the new rules. *See* § 118(c). The foregoing seems plain enough, but there's more to the story.

Convoluted legislative history. Notably, the House's version of the 2017 TCJA simply repealed § 118, but as mentioned above the conferees decided instead to amend § 118 merely to eliminate any exclusion from gross income for nonshareholder contributions to capital by governmental entities or civic groups. The Conference Report accompanying the amendment to § 118 clarifies that a municipal tax abatement for locating a business in a particular municipality is not considered a taxable contribution to capital. Moreover, the Conference Report states that the amendments to § 118 do not change the application of the meaningless gesture doctrine, described in *Lessinger v. Commissioner*, 872 F.2d 519 (2d. Cir. 1989) and related cases, as well as in prior administrative guidance. Thus, incremental shares of stock are not required to be issued by a corporation under § 351 to avoid gross income when existing shareholders of a corporation (including governmental entity or civic group shareholders) make pro-rata contributions to capital. Finally, in a curious reference to which we refer later in this outline in connection with recent partnership capital contribution cases, the Conference Report states "[t]he conferees intend that section 118, as modified, continue to apply only to corporations;" however, the Conference Report also states in part that "[t]he conference agreement follows the policy of the House bill" which, as noted above, repealed § 118. This nuance is important because the legislative history of the House bill stated in connection with the proposed repeal of § 118 that "a contribution of municipal land by a municipality that is not in exchange for stock (*or for a partnership interest or other interest*) of equivalent value is considered a contribution to capital that is includable in gross income." (Emphasis added.)

Some deeper background. Prior to the 2017 TCJA, the gross income of a corporation generally did not include contributions to capital made by nonshareholders. Section 118(a) continues to provide a general rule of excludability for nonshareholder contributions to capital, and thus the pre-TCJA version of § 118(a) remains intact. As summarized above, however, TCJA added a new limitation to the general rule of § 118(a). Specifically, §118(b)(2) carves out from the general rule of exclusion any nonshareholder contributions to capital made by governmental entities or civic groups. Other limitations on the exclusion existed and continue to exist under § 118 for certain capital contributions "in aid of construction" (as defined, but carving out contributions made by regulated water or sewage utilities) or "as a customer or potential customer." *See* § 118(b)(1). Notwithstanding the foregoing, the pre-TCJA version of § 118 ordinarily allowed a corporation to exclude from gross income nonshareholder contributions to capital made by governmental entities or civic groups for the purpose of inducing the corporation to acquire or construct property within a desired locale. *See, e.g.*, *Brown Shoe Co. v. Commissioner*, 339 U.S. 583 (1950). If property other than money was acquired by a corporation as a nontaxable contribution to capital, then the adjusted basis of the property was zero. If the contribution consisted of money, then the corporation had to reduce the basis of any property acquired with the contributed money within the following 12-month period, and then reduce the basis of other property held by the corporation. *See* § 362(c)(1) & (2); Reg. § 1.362–2. These rules regarding basis reductions remain unaffected for any nonshareholder contributions to capital that somehow remain excludable from gross income under amended § 118.

What about noncorporate entities? Section 118 expressly did not and still does not apply to noncorporate entities such as partnerships and LLCs taxed as partnerships. The IRS previously has taken the position that there is no exclusion from gross income for contributions to the capital of noncorporate entities made by a nonowner. Nevertheless, the IRS acknowledges that taxpayers have taken contrary positions under a "common law contribution to capital doctrine." *See generally* LMSB Coordinated Issue Paper LMSB4-1008-051, Exclusion of Income: Non-Corporate Entities and Contributions to Capital (Nov. 18, 2008). For those taxpayers, the convoluted language in the Conference Report perhaps should lead to the conclusion that those common law "groundrules" (*pun intended*) have changed, at least with respect to governmental entity and civic group capital contributions. In fact, considering two recent cases discussed later in this outline regarding LLCs taxed as partnerships, current trends suggest that contributions to the capital of noncorporate entities are not excludable from gross income notwithstanding any "common law contribution to capital doctrine."

VII. PARTNERSHIPS

A. Formation and Taxable Years

B. Allocations of Distributive Share, Partnership Debt, and Outside Basis

C. Distributions and Transactions Between the Partnership and Partners

D. Sales of Partnership Interests, Liquidations and Mergers

E. Inside Basis Adjustments

F. Partnership Audit Rules

G. Miscellaneous

1. Nonowner contributions to the capital of partnerships and LLCs taxed as partnerships are not excludable, and the common law contribution to capital doctrine is on life support if not dead. The 2017 TCJA amended Code § 118 effective after December 22, 2017, such that nonshareholder contributions to the capital of corporations made by governmental entities or civic groups no longer are excludable from the recipient corporation's gross income. Previously, such capital contributions were nontaxable, and they occasionally were made to incentivize corporations either to locate in particular communities or to acquire or redevelop distressed property in a community (or do both). In addition, the Conference Report accompanying the changes to § 118, along with the cases summarized below, probably leads to the conclusion that similarly-motivated capital contributions to noncorporate entities (i.e., partnerships and LLCs taxed as partnerships) no longer are excludable from gross income (if they ever were), even though such contributions are outside the purview of either old or amended § 118.

a. No good deed goes unpunished. Ginsburg v. United States, 136 Fed. Cl. 1 (1/31/18). In this decision, the Court of Federal Claims held that the State of New York's payment of approximately $1.8 million to an LLC (taxed as a partnership) to incentivize and reward redevelopment of brownfield property is includable in the taxpayer-member's gross income. The taxpayer owned 90%

of an LLC taxed as a partnership for federal income tax purposes. The taxpayer's LLC participated in New York's Brownfield Development Tax Credit program in connection with acquiring an abandoned shoe factory in 2004 and eventually restoring it as a 134-unit residential building by 2011. New York's Brownfield Tax Credit program allows certain credits against state income taxes based upon investment in qualifying brownfield propery. Further, if the credit is fully used by a taxpayer to offset applicable New York state income taxes, the excess of the credit over the amount used against state income taxes is paid to the taxpayer. Accordingly, after certifying that the taxpayer's LLC had complied with the terms of the Brownfield Development Tax Credit program, in 2013 New York paid the taxpayer's LLC approximately $1.8 million in satisfaction of the taxpayer's excess credit amount. The taxpayer took the position on his 2013 federal income tax return that his 90% allocable share of the $1.8 million payment was excludable from gross income as a nontaxable capital contribution to the LLC. (New York law allowed exclusion of the payment for New York income tax purposes.) Upon audit, the IRS determined that the payment constituted gross income to the LLC and thus to the taxpayer as part of his allocable share of partnership income. This adjustment resulted in additional gross income to the taxpayer for 2013 and a corresonding underpayment of approximately $602,000. The taxpayer paid the underpayment, filed a refund claim, and then brought this action in the Court of Federal Claims.

Analysis: Upon cross motions for summary judgment, Court of Federal Claims (Judge Hodges) agreed with the government that the $1.8 million constituted gross income to the taxpayer's LLC and thereby to the taxpayer. The government had argued, and the court agreed, that the payment was includable by the broad terms of § 61(a) (gross income from whatever source derived) and that no statutory exclusions or exceptions applied. The taxpayer argued unsuccessfully that the $1.8 million payment was (i) a nontaxable contribution to the LLC's capital, (ii) a nontaxable recovery of the LLC's investment in the Brownfield project owned by the LLC, or (iii) a nontaxable state "general-welfare" grant to the LLC. The taxpayer acknowledged that under any of the above theories the taxpayer's basis in the brownfield project would be adjusted downward by the amount excludable. Judge Hodges reasoned that, because the taxpayer could not point to an express provision of the Code to support his nontaxable contribution to capital theory, no such exclusion applied. Furthermore, Judge Hodges reasoned that the payment to the partnership could not be a recovery of the LLC's investment in the project because the payment came from a third party (the State of New York), not from the seller of the property. Judge Hodges expressed the view that the recovery of capital doctrine applies only in the context of buyers and sellers of "goods," and in that context, a payment can be nontaxable as a purchase price adjustment. (We believe the court was wrong about basis recovery being limited to sales of "goods." Regardless, the taxpayer's "recovery of investment" argument probably was not a winner anyway. For instance, see the court's analysis in *Uniquest Delaware*, discussed immediately below.) Finally, Judge Hodges determined that New York's payment to the taxpayer's LLC did not qualify for the "general-welfare" exclusion recognized in Rev. Rul. 2005-46, 2005-2 C.B. 120 (state disaster relief grants) because the tax credit in question was not conditioned on a showing of need.

- The holding of the Court of Federal Claims regarding the unavailability of the general welfare exclusion is consistent with the Tax Court's holding in *Maines v. Commissioner*, 144 T.C. 123 (2015). In *Maines*, the Tax Court held that the refundable portions of certain New York targeted economic development credits that remained after first reducing state tax liability were accessions to the taxpayers' wealth and were includable in gross income under § 61 for the year in which the taxpayers received payment or, under the constructive receipt doctrine, were entitled to receive payment, even if they elected to carry forward the credit. The Tax Court concluded that the taxpayers could not exclude the payments under the general welfare exclusion because the payments were not conditioned on a showing of need.

b. Yet again, no good deed goes unpunished. But perhaps there could have been a workaround? Uniquest Delaware, LLC v. United States, 294 F.Supp.3d 107 (W.D.N.Y. 3/27/18). In this decision, the U.S. District Court for the Western District of New York held that a grant paid by the New York State Empire State Development Corporation (which appears to have been a government-funded corporation) to an LLC taxed as a partnership was not excludable from the LLC's gross income as a contribution to capital. The taxpayer in this case was the LLC (unlike *Ginsburg v. United States*, 136 Fed. Cl. 1 (1/31/18), in which the taxpayer was a partner-member of the LLC). The

LLC, a TEFRA partnership, had two equal members, each of which was a disregarded single-member LLC, that in turn were each wholly-owned by separate subchapter S corporations. The case arose in connection with a TEFRA partnership audit of the LLC, a fact which was important to the court's ultimate decision (as explained further below). In 2009, the LLC received an $11 million grant from the New York State Empire State Development Corporation for the restoration of a building in Buffalo. The original grant proposal expressly stated that "[t]here is no element of compensation of specific, quantifiable or other services to the government agencies involved; the grants contemplated by this offer are being offered solely for the purpose of obtaining an advantage for the general community." The LLC did not include the $11 million grant in its income on its partnership tax return for 2009. During the audit and at IRS Appeals, the IRS asserted that the $11 million grant was included in the LLC's gross income in 2009 and ultimately issued an FPAA accordingly. The taxpayer-LLC then sought judicial review of the FPAA in the U.S. District Court for the Western District of New York.

Analysis: As in *Ginsburg*, the IRS's argument in this case was simple: § 61(a) requires inclusion of the $11 million grant in gross income, and no exception or exclusion in the Code provides otherwise. The taxpayer-LLC, similar to the taxpayer in *Ginsburg*, argued alternatively that the $11 million grant was either (i) excludable under the "common law contribution to capital doctrine" or (ii) akin to a "rebate" that resulted in an adjustment to the taxpayer-LLC's basis in the building, but which was not includable in gross income. [As to this latter "rebate" argument, see Rev. Rul. 76-96, 1976-1 C.B. 23 (rebates paid by car manufacturers, but not the dealer who sold the car, are not income but instead reduce the purchaser's basis in the car). Rev. Rul. 76-96 has been suspended in part on other grounds by Rev. Rul. 2005-28, 2005-1 C.B. 997.] Judge Wolford ruled against the taxpayer-LLC with respect to both arguments. Regarding the taxpayer-LLC's "common law contribution to capital doctrine" argument, the court reasoned that the cases supporting the doctrine involved corporate taxpayers only, and the holdings in these cases were codified by § 118 (the pre-TCJA version), which expressly does not apply to noncorporate entities. Regarding the taxpayer-LLC's "rebate" argument, Judge Wolford ruled that the $11 million grant is distinguishable, stating "unlike a retail customer who purchases a car with the knowledge that a rebate is forthcoming, [the taxpayer] purchased the [Buffalo Building] and then subsequently sought and received the [$11 million grant]. Therefore, the [$11 million grant] cannot be considered a discount or reduction in the purchase price of the building."

Indirect §§ 118/702 Argument: The taxpayer-LLC argued that, even if § 118 applies only to corporations, the court should indirectly rule it applicable to resolve the dispute with the IRS because the ultimate owners of the taxpayer-LLC were subchapter S corporations. The taxpayer further argued in this regard that § 118 (pre-TCJA) would have allowed the S corporation members of the taxpayer-LLC to exclude the grant from gross income. Therefore, the taxpayer-LLC argued, if the S corporation members could have excluded the grant under § 118, then the grant ultimately should be held nontaxable by virtue of § 702's distributive share approach to partner-level income. With respect to this final argument, Judge Wolford ruled that because TEFRA audit procedures treat the taxpayer-LLC as an entity separate from its owners, the partner-level treatment by the ultimate owners of the LLC was not within the court's subject-matter jurisdiction. *See* § 6226(f) and *American Boat Co., LLC v United States*, 583 F.3d 471, 478 (7th Cir. 2009) ("A court does not have jurisdiction to consider a partner-level defense in a partnership-level proceeding.")

Planning pointer: Had the subchapter S corporations first received the $11 million grant from New York and then contributed the funds to the taxpayer-LLC as additional capital contributions, we believe the grant would not have been taxable pursuant to the pre-TCJA version of § 118 and § 721, respectively. On the other hand, perhaps the terms of the grant would not allow the funds to be paid to the S corporation members because the acquisition and development was performed by the taxpayer-LLC, not the S corporation members.

VIII. <u>TAX SHELTERS</u>

IX. EXEMPT ORGANIZATIONS AND CHARITABLE GIVING

X. TAX PROCEDURE

A. Interest, Penalties, and Prosecutions

1. Better be careful who you hire as CFO, and raise all your arguments against liability as a responsible person at the summary judgment stage, not afterwards. McClendon v. United States, 119 A.F.T.R.2d 2017-1037 (S.D. Tex. 3/6/17). The government successfully established through a motion for summary judgment that the taxpayer, a physician, was liable under § 6672 for a $4.3 million penalty equal to the amount of unpaid federal employment taxes owed by his medical practice. The CFO he had hired had embezzled funds and ultimately pleaded guilty to felony counts of theft. When the taxpayer learned of the unpaid taxes, he made a loan to the practice to allow it to make payroll, and these funds went to the employees rather than the government. The government used this preferential payment as the basis for establishing that the taxpayer had willfully violated his duty to pay the taxes due. The taxpayer moved for reconsideration and argued that his liability should be limited to the $100,000 preferential payment that was the basis for his liability. The court rejected this argument for two reasons. First, the taxpayer had failed to raise it in response to the government's motion for summary judgment. Second, even if he had raised it in a timely manner, the taxpayer had failed to meet his burden to prove the absence of funds available to pay the taxes due:

> At the summary judgment stage, as now, Dr. McClendon did not try to prove up the funds available to [the practice] or show that whatever funds existed were encumbered so that he had no obligation to pay them to the IRS. Instead, he effectively argues that, at summary judgment, it was the government's burden to demonstrate his liability for each dollar of the penalty. Not so. Dr. McClendon was presumptively liable for the balance of the IRS penalty assessed against him. The government moved for summary judgment and argued that the evidence did not create a genuine factual dispute material to deciding whether the IRS penalty was properly assessed. That discharged the government's summary judgment burden. Dr. McClendon, who would bear the burden at trial, then had the burden to submit or identify record evidence showing that he was not liable.

a. In this § 6672 trust fund recovery case, the Fifth Circuit has reversed and remanded for trial on the issue of the amount of available, unencumbered funds in the business's bank accounts after the responsible person became aware of the unpaid withholding taxes. McClendon v. United States, 892 F.3d 775 (5th Cir. 6/14/18). In the District Court, Dr. McClendon (now deceased) argued that his liability under § 6672 should be limited to $100,000, the amount of the loan he made to the business to allow it to make payroll after he had learned of the unpaid employment taxes. The District Court rejected this argument as untimely because Dr. McClendon had not raised it in his response to the government's motion for summary judgment and instead had raised it for the first time in his motion for reconsideration after the District Court had granted summary judgment in the government's favor. Nevertheless, the District Court considered the merits of the argument and concluded that Dr. McClendon had failed to meet his burden of submitting or identifying evidence in the record to show the amount of the business's funds that were unencumbered and available to pay the unpaid taxes. In an opinion by Judge Davis, the U.S. Court of Appeals for the Fifth Circuit has vacated the District Court's grant of summary judgment and remanded for trial on the issue of the amount of available, unencumbered funds in the business's bank accounts after discovery of the unpaid withholding taxes. The court first noted that its review of the District Court's denial of Dr. McClendon's motion to reconsider its grant of summary judgment is *de novo* because the District Court reached the merits of the motion and considered materials submitted in connection with it. The court cited *Barnett v. I.R.S.*, 988 F.2d 1449 (5th Cir. 1993), for the proposition that, when the government asserts that a responsible person willfully failed to pay employment taxes by using the business's unencumbered funds to pay the business's non-IRS creditors, the responsible person's liability under § 6672 is limited to the amount of "available, unencumbered funds deposited into [the business's] bank accounts after [the responsible person] became aware that the accrued withholding taxes were due." Dr. McClendon, the court explained, had testified in his deposition and in his affidavit regarding the actions taken and the funds available once the unpaid withholding taxes came to light, including his

$100,000 loan and the amount of receivables and insurance proceeds paid to the IRS, and had submitted copies of checks payable to the IRS that he asserted represented the closing balance in the business's accounts shortly after the unpaid taxes were discovered. To oppose the government's motion for summary judgment, the court stated, Dr. McClendon was not required to provide an accounting of the business's funds. The court cited the Eleventh Circuit's recent decision in *United States v. Stein*, 881 F.3d 853 (11th Cir. 2018), in which the court held that an affidavit can create an issue of material fact that precludes summary judgment even if the affidavit is self-serving and uncorroborated. Similarly, the Fifth Circuit reasoned, "[w]e can find no such corroboration requirement under § 6672." In the court's view, Dr. McClendon had come forward with sufficient evidence to establish an issue of material fact warranting trial regarding the amount of available, unencumbered funds.

Concurring Opinion. Judge Jones concurred in the court's opinion. She wrote separately to emphasize that, given Dr. McClendon and his partners had relied on their CFO for a decade before the CFO began embezzling, their reliance on his representations regarding the payment of employment taxes seemed plausible, and therefore she did not see how the District Court could rule as a matter of law on the government's argument that Dr. McClendon had willfully failed to pay employment taxes by acting with reckless disregard of a known or obvious risk that trust funds would not be remitted. She also stated that, in her view, the government had acted irresponsibly by introducing 285 pages of exhibits in support of its motion, including the business's records, and then arguing that Dr. McClendon had not met his burden at the summary judgment stage:

> To challenge the legal consequences of McClendon's $100,000 cash infusion is one thing; to claim, in the face of his sworn affidavit and documents, and their own access to corroborative financial records, that this isn't enough to raise a fact issue is irresponsible at best.

Dissenting Opinion. Judge Higginson dissented and argued that the court should affirm the District Court's grant of summary judgment in favor of the government.

2. Updated instructions on how to rat yourself out. Rev. Proc. 2018-11, 2018-5 I.R.B. 335 (1/26/18). This revenue procedure updates Rev. Proc. 2016-13, 2016-4 I.R.B. 290 (1/25/16), and identifies circumstances under which the disclosure on a taxpayer's income tax return with respect to an item or a position is adequate for the purpose of reducing the understatement of income tax under § 6662(d), relating to the substantial understatement aspect of the accuracy-related penalty, and for the purpose of avoiding the tax return preparer penalty under § 6694(a), relating to understatements due to unreasonable positions. There have been no substantive changes. The revenue procedure does not apply with respect to any other penalty provisions, including § 6662(b)(1) accuracy-related penalties. If this revenue procedure does not include an item, disclosure is adequate with respect to that item only if made on a properly completed Form 8275 or 8275–R, as appropriate, attached to the return for the year or to a qualified amended return. A corporation's complete and accurate disclosure of a tax position on the appropriate year's Schedule UTP, Uncertain Tax Position Statement, is treated as if the corporation had filed a Form 8275 or Form 8275-R regarding the tax position. The revenue procedure does not take into account the effect of tax law changes effective for tax years beginning after December 31, 2017. Accordingly, a taxpayer may have to file Form 8275 or Form 8275-R if a line referenced in the revenue procedure is affected by such a legislative change and requires additional reporting, at least until the IRS prescribes criteria for complying with the requirement.

B. Discovery: Summonses and FOIA

C. Litigation Costs

D. Statutory Notice of Deficiency

E. Statute of Limitations

F. Liens and Collections

1. The 30-day period for requesting review in the Tax Court of a notice of determination following a CDP hearing is jurisdictional and not subject to equitable tolling. Duggan v. Commissioner, 879 F.3d 1029 (9th Cir. 1/12/18), *aff'g* Duggan v. Commissioner, No. 4100-15L (U.S. Tax Court (6/26/15)). Following a collection due process hearing, the IRS issued two notices of determination upholding proposed collection action. The notices informed the taxpayer that, if he wished to contest the determinations, he could do so "by 'fil[ing] a petition with the United States Tax Court within a 30-day period beginning the day after the date of this letter.'" The notices were dated January 7, 2015. The taxpayer mailed his petition to the Tax Court on February 7, 2015, which was 31 days after the date of the notices of determination. The Tax Court (Judge Thornton) granted the IRS's motion to dismiss for lack of subject matter jurisdiction. On appeal, the taxpayer argued that he had been misled by the notices of determination, which caused him to believe that the day after the letter's date was day zero, the following day was day one etc., and that his attempts to comply had been reasonable. In an opinion by Judge Christen, the U.S. Court of Appeals for the Ninth Circuit affirmed the Tax Court's decision. The court held that the 30-day period specified in § 6330(d)(1) is jurisdictional and therefore is not subject to equitable tolling. In reaching this conclusion, the court relied on the plain language of § 6330(d)(1), which provides:

> A person may, within 30 days of a determination under this section, petition the Tax Court for review of such determination (and the Tax Court shall have jurisdiction with respect to such matter).

This provision, the court reasoned, "expressly contemplates the Tax Court's jurisdiction." The court also reasoned that § 6330(d)(1) was similar to statutory provisions establishing similar filing deadlines, such as the 90-day period specified by § 6015(e)(1)(A) for seeking review in the Tax Court of an IRS determination denying innocent spouse relief, which the Second Circuit concluded is jurisdictional. *See Matuszak v. Commissioner*, 862 F.3d 192 (2d Cir. 7/5/17). Because the 30-day period specified in § 6330(d)(1) is jurisdictional, the court concluded, the taxpayer's "failure to meet this deadline divested the Tax Court of the power to hear his case and foreclosed any argument for equitable tolling."

- In *Guralnik v. Commissioner*, 146 T.C. 230 (6/2/16), the Tax Court previously had held that the 30-day period specified in § 6330(d)(1) for seeking review in the Tax Court of an IRS notice of determination following a CDP hearing is jurisdictional and not subject to equitable tolling.

a. Assuming without deciding that the 30-day period for seeking review in the Tax Court of an IRS deternination following a CDP hearing is subject to equitable tolling, this taxpayer failed to establish circumstances that would justify doing so, says the Fourth Circuit. Cunningham v. Commissioner, 716 Fed. Appx. 182 (4th Cir. 1/18/18), *aff'g* Cunningham v. Commissioner, No. 14090-16 L (U.S. Tax Court (12/7/16)). The IRS issued a final notice of intent to levy, in response to which the taxpayer requested a collection due process hearing. Following the CDP hearing, the IRS issued a notice of determination upholding the proposed collection action. The notice of determination advised the taxpayer that, if she wished to contest the determination in the Tax Court, she must do so within the 30-day period prescribed by § 6330(d)(1), and that the 30-day period began to run on the day after the date of the letter. The letter was dated May 16, 2016. The taxpayer mailed her petition to the Tax Court on June 16, 2016, which was 31 days after the date of the letter. The Tax Court granted the IRS's motion to dismiss for lack of subject matter jurisdiction. On appeal, the taxpayer argued that the 30-day period for seeking review in the Tax Court was subject to equitable tolling. In an unpublished opinion by Judge Diaz, the U.S. Court of Appeals for the Fourth Circuit affirmed the Tax Court's decision. According to the Fourth Circuit, the taxpayer had to clear three hurdles in order for equitable tolling to apply: (1) the 30-day period specified by § 6330(d)(1) must be a mandatory claim-processing rule rather than a jurisdictional rule, (2) equitable tolling must be available for untimely actions under the statute, and (3) the circumstances must warrant equitable tolling. In connection with the second "hurdle," the court noted that "it is uncertain whether the presumption [established by *Irwin v. Department of Veterans Affairs*, 498 U.S. 89 (1990), that equitable tolling is available to litigants] applies at all outside the context of Article III courts." But the court rested its decision on the third condition. In the court's view, circumstances warranting equitable tolling were "wholly absent here." The taxpayer argued that she had been misled by the notice of determination, which caused her to believe that the day after the letter's date was day zero, the following day was day one etc. The court rejected this interpretation as contrary not only to Tax Court Rule 25(a), but also to the plain language of the letter and common sense. Equitable tolling, the court emphasized, is available only in rare instances in which it would be unconscionable to enforce a limitations period due to circumstances other than the party's own conduct. In this case, the court stated, the error resulted from the taxpayer's own mistake.

G. Innocent Spouse

1. Never, ever, never rely upon IRS correspondence concerning the law, and school your students and junior colleagues about the harsh reality that there is no equitable relief in tax from jurisdictional requirements. Rubel v. Commissioner, 856 F.3d 301 (3d Cir. 5/9/17), *aff'g* Rubel v. Commissioner, No. 9183-16 (U.S. Tax Court 7/11/16). In a case that went all the way to the U.S. Court of Appeals for the Third Circuit, the taxpayer, admirably represented by the Federal Tax Clinic at the Harvard Legal Services Center, claimed innocent spouse relief under § 6015 for the years 2005 through 2008. The IRS had denied the taxpayer's requests for each year via four separate notices of determination issued in January 2016. Section 6015(e)(1)(A) provides that a taxpayer who seeks innocent spouse relief may petition the Tax Court and that the Tax Court "shall have jurisdiction" if the petition is filed within specified time limits and no later than 90 days after the date the IRS mails the notice of determination. For the years 2006 through 2008, the taxpayer's petition in Tax Court was due by April 4, 2016. For 2005, the taxpayer's petition was due by April 12, 2016. Meanwhile, after receiving the notices, the taxpayer submitted additional information to the IRS concerning her claim for innocent spouse relief. The IRS again denied the taxpayer's claim via letter dated March 3, 2016; however, the letter misrepresented the due date for filing a petition in the Tax Court stating: "Please be advised this correspondence doesn't extend the time to file a petition with the U.S. Tax Court. Your time to petition the U.S. Tax Court began to run when we issued you our final determination [in January] and will end on Apr. 19, 2016. However, you may continue to work with us to resolve your tax matter." The taxpayer subsequently filed a petition in the Tax Court on April 19, 2016, and the IRS moved the Tax Court to dismiss the taxpayer's claim for lack of jurisdiction (because the petition was outside the 90-day period). The Tax Court agreed with the IRS and dismissed the petition. The taxpayer appealed to the Third Circuit arguing for equitable relief and estoppel against the IRS due to the misrepresentation in the March 3, 2016, IRS letter. The Third Circuit affirmed the Tax Court's dismissal of the case stating: "[T]he ninety-day deadline is jurisdictional and cannot be altered 'regardless of the equities' of the case."

a. Another case confirming that you cannot rely on what the IRS tells you about the filing deadline! The 90-day period for filing a Tax Court petition seeking review of an IRS determination denying innocent spouse relief is jurisdictional and not subject to equitable tolling. Matuszak v. Commissioner, 862 F.3d 192 (2d Cir. 7/5/17), *aff'g Matuzak v. Commissioner*, No. 471-15 (U.S. Tax Court 12/29/15). The IRS issued a notice of determination denying the taxpayer's request for innocent spouse relief. Under § 6015(e)(1)(A), the taxpayer then had 90 days from the date of mailing of the notice of determination to file a petition in the Tax Court. The taxpayer filed her petition in the Tax Court one day late. The Tax Court (Judge Marvel) granted the government's motion to dismiss the petition. The Tax Court subsequently denied the taxpayer's motion to vacate. See *Matuszak v. Commissioner*, No. 471-15 (7/29/16). In doing so, the Tax Court rejected the taxpayer's argument that the 90-day period for filing the petition could and should be equitably tolled because she had relied on erroneous verbal advice from IRS agents concerning the deadline for filing the petition. The taxpayer argued that recent developments in jurisdictional jurisprudence warranted overruling *Pollock v. Commissioner*, 132 T.C. 21 (2009), in which the court had concluded that the 90-day period of § 6015(e)(1)(A) is jurisdictional and not subject to equitable tolling. The Tax Court, however, declined to do so. The Tax Court noted that, in *Guralnik v. Commissioner*, 146 T.C. 230 (6/2/16), it had recently rejected a similar argument for changing its view on the jurisdictional nature of the 30-day period in § 6330(d)(1) for seeking review in the Tax Court of an IRS notice of determination following a CDP hearing. In a per curiam opinion, the U.S. Court of Appeals for the Second Circuit affirmed the Tax Court's decision. The Second Circuit acknowledged that recent decisions from the U.S. Supreme Court have distinguished between jurisdictional rules, which are not subject to equitable tolling, and non-jurisdictional claim-processing rules, which are. Nevertheless, the Second Circuit concluded that the 90-day period specified in § 6015(e)(1)(A) is jurisdictional. The court emphasized that the language of the statute provides that "the Tax Court shall have jurisdiction" if the petition is filed within the 90-day period. The court also noted that, in *Maier v. Commissioner*, 360 F.3d 61 (2d Cir. 2004), it had previously recognized the jurisdictional nature of § 6015 by concluding that the statute did not confer jurisdiction on the Tax Court over petitions seeking review of innocent spouse determinations filed by the non-electing spouse.

- The taxpayer was represented on the appeal by the Federal Tax Clinic at the Harvard Legal Services Center.

b. Things really are not looking good for those seeking to toll the 90-day period for filing a Tax Court petition to seek review of an IRS determination denying innocent spouse relief. The Fourth Circuit has agreed with the Second and Third Circuits. Nauflett v. Commissioner, 892 F.3d 649 (4th Cir. 6/14/18), *aff'g Nauflett v. Commissioner*, No. 24427-15 (U.S. Tax Court 8/9/16). The taxpayer in this case sought innocent spouse protection with respect to four years for which she had filed joint returns with her husband. The IRS denied the taxpayer's requested relief in multiple notices of determination dated July 17, 2015. The notices of determination informed the taxpayer of the rule set forth in § 6015(e)(1)(A), which provides that a taxpayer has 90 days from the date of mailing of the notice of determination to file a petition in the Tax Court. The taxpayer asserted that she had contacted both the IRS contact person listed on the notices and an employee at the IRS Taxpayer Advocate Service for assistance, and that they both incorrectly had informed her that she had until September 22, 2015, to file her petition. The taxpayer's petition to the Tax Court was postmarked September 22. However, the last day of the 90-day period specified by § 6015(e)(1)(A) was September 15, 2015. The Tax Court (Judge Marvel) granted the IRS's motion to dismiss the petition. The Tax Court subsequently denied the taxpayer's motion to vacate or revise. *See Nauflett v. Commissioner*, No. 24427-15 (U.S. Tax Court 5/25/17). In an opinion by Judge Agee, the U.S. Court of Appeals for the Fourth Circuit affirmed the Tax Court's decision. The court emphasized that the language of § 6015(e)(1)(A) provides that "the Tax Court shall have jurisdiction" if the petition is filed within the 90-day period. "We need not look beyond that mandate because Congress has, in fact, uttered 'magic words,' expressly conditioning the Tax Court's power on the timely filing of a petition." The court also relied on the "broader context of subsection (e)(1)(A) within § 6015." Because § 6015(e)(1)(A) is jurisidctional, the court concluded, courts do not have discretion to waive compliance based on equitable considerations.

H. <u>Miscellaneous</u>

1. The D.C. Circuit found that registered (?) tax return preparers were entitled to be unqualified. The IRS had de gall to require character, competence, and continuing education for "independent" tax return preparers who only needed PTINs to continue preparing error-laden tax returns for their unsophisticated clientele. Loving v. IRS, 742 F.3d 1013 (D.C. Cir. 2/11/14), *aff'g* 920 F. Supp. 2d 108 (D. D.C. 2/1/13). The D.C. Circuit (Judge Kavanaugh) held that regulations issued in 2011 under 31 U.S.C. § 330 that imposed new character, competence, and continuing education requirements on tax return preparers were "foreclose[d] and render[ed] unreasonable" by the statute, and thus failed at the *Chevron* step 1 standard. They would have also failed at the *Chevron* step 2 standard because they were "unreasonable in light of the statute's text, history, structure, and context."

- Judge Kavanaugh's opinion found six problems with the 2011 regulations: (1) tax return preparers were not "representatives" because they are not "agents" and, thus, lack "legal authority to act on the taxpayer's behalf"; (2) the preparation and filing of a tax return did not constitute "practice … before the Department of the Treasury" because that term implies "an investigation, adversarial hearing, or other adjudicative proceeding"; (3) the history of the statutory language originally enacted in 1884 "indicated that the statute contemplated representation in a contested proceeding"; (4) the regulation was inconsistent with the "broader statutory framework," (?!) in which Congress had enacted a number of statutes specifically directed at tax-return preparers and imposing civil penalties, which would not have been necessary if the IRS had authority to regulate tax-return preparers; (5) the statute would have been clearer had it granted power "for the first time to regulate hundreds of thousands of individuals in the multi-billion dollar tax-preparation industry" ["the enacting Congress did not intend to grow such a large elephant in such a small mousehole"]; and (6) the IRS's past approach showed that until 2011 it never maintained that it had authority to regulate tax return preparers.

- Judge Kavanaugh concluded: "The IRS may not unilaterally expand its authority through such an expansive, atextual, and ahistorical reading of Section 330."

a. In light of the IRS loss in *Loving v. IRS*, a new, voluntary Annual Filing Season Program to give tax return preparers the ability to claim they hold "a valid Annual Filing Season Program Record of Completion" and that they have "complied with the IRS requirements for receiving the Record of Completion." Rev. Proc. 2014-42, 2014-29 I.R.B. 192 (6/30/14). In order to encourage unenrolled tax return preparers, i.e., those who are not attorneys, CPAs or EAs, to complete continuing education courses in order to get a better understanding of federal tax law, the carrot of being able to claim superiority to the ordinary run-of-the-mill slob tax return preparers is offered. The requirements for this voluntary program include a six-hour refresher course, with a 100-question test at the end, plus other continuing education of two hours of ethics and ten hours of federal tax law topics. Holders of the Record of Completion may not use the terms "certified," "enrolled," or "licensed" to describe the designation.

b. The AICPA's challenge to the Annual Filing Season Program fails, but the court signals that others might successfully challenge it. American Institute of Certified Public Accountants vs. Internal Revenue Service, 199 F. Supp. 3d 55 (D.D.C. 8/3/16). The AICPA challenged as unlawful the voluntary Annual Filing Season Program established by the IRS in Rev. Proc. 2014-42, 2014-29 I.R.B. 192 (6/30/14), and the U.S. Court of Appeals for the District of Columbia ruled that the AICPA had standing to bring the challenge. *American Institute of Certified Public Accountants vs. Internal Revenue Service*, 804 F.3d 1193 (D.C. Cir. 10/30/15). In that opinion, the D.C. Circuit declined to address an issue raised by the IRS for the first time on appeal: that the AICPA's grievance does not "fall within the zone of interests protected or regulated by the statutory provision it invokes." On remand, the District Court (Judge Boasberg) held that the AICPA failed the zone of interests test because its grievance (which the court characterized as the grievance of the AICPA's members) is neither regulated nor protected by the relevant statute. Accordingly, the court granted the IRS's motion to dismiss. The court characterized the grievance of the AICPA and its members as competitive injury from brand dilution, i.e., that the AFS Program would dilute the credentials of the AICPA's members by introducing a government-backed credential and government-sponsored public listing. The relevant statute, the court concluded, is 31 U.S.C. § 330(a), which authorizes the Secretary of the Treasury to regulate the practice of representatives of persons before the Treasury Department and to require that certain conditions be satisfied, such as good character, before admitting a person to practice. The AICPA is not a representative of persons within the zone of interests *regulated* by the statute, the court concluded, because to satisfy this requirement the party must be regulated by the particular regulatory action being challenged. To demonstrate that it is in the zone of interests *protected* by the statute, the AICPA would have to demonstrate either that it is an intended beneficiary of the statute or that it is a "suitable challenger" to enforce the statute. The AICPA did not contend that it was an intended beneficiary of the statute, and the court concluded that the AICPA was not a suitable challenger. The court reasoned that the purpose of 31 U.S.C. § 330(a) is consumer protection, and that the AICPA's interest in avoiding intensified competition as a result of the AFS Program was not congruent with that purpose. "On the contrary, AICPA members' competitive interests are on a collision course with Congress's interest in safeguarding consumers."

- Although it dismissed the AICPA's challenge, the court added:

> A final word. While AICPA does not have a cause of action under the APA to bring this suit, the Court has little reason to doubt that there may be other challengers who could satisfy the rather undemanding strictures of the zone-of-interests test.

c. The D.C. Circuit had good news and bad news for the AICPA. The good news: the AICPA had standing to challenge the IRS's Annual Filing Season Program. The bad news: on the merits, the IRS had authority to adopt the program and the program does not violate the Administrative Procedure Act. American Institute of Certified Public Accountants v. Internal Revenue Service, 122 A.F.T.R.2d ¶2018-5507 (D.C. Cir. 8/14/18). The AICPA appealed the decision of the U.S. District Court for the District of Columbia that the AICPA lacked standing to challenge the IRS's Annual Filing Season (AFS) Program and the court's dismissal of the AICPA's challenge. In an opinion by Judge Ginsburg (with Judge Griffith concurring in part and dissenting in part), the U.S. Court of Appeals for the District of Columbia Circuit reversed the District Court on the issue of standing and, reaching the merits of the AICPA's challenge, held that the IRS had statutory authority to create the AFS Program and had not violated the Administrative Procedure Act in doing so. The court addressed three issues: (1) whether the AICPA had standing to challenge the AFS Program, (2) whether the IRS had statutory authority to adopt the AFS Program, and (3) whether the IRS followed the requisite procedures in creating the AFS Program.

Standing. With respect to standing, the court concluded that the AICPA had both constitutional and statutory standing to bring the challenge. The AICPA had constitutional standing, the court held, because its members who employ unenrolled return preparers are injured by the AFS Program, which applies Circular 230 to a new class of employees (the unenrolled preparers) and therefore imposes new supervisory responsibility requirements on those who employ them. On the issue of statutory standing, the court agreed with the District Court that the relevant statute is 31 U.S.C. § 330(a), which authorizes the Secretary of the Treasury to regulate the practice of representatives of persons before the Treasury Department and to require that certain conditions—such as good character—be satisfied before admitting a person to practice. In contrast to the District Court, however, the court held that the AICPA is a representative of persons within the zone of interests *regulated* by the statute. The relevant zone of interests regulated or protected by the statute, the court reasoned, is consumer protection and regulation of those who practice before the IRS. According to the court, the AICPA's injury fell within this zone of interests because its members who employ unenrolled agents are injured by the AFS Program, which imposes new supervisory responsibility requirements on them. In other words, the additional supervisory responsibilities of which the AICPA complained established both constitutional and statutory standing.

Statutory Authority for the AFS Program. The court recognized that, when it reverses a District Court's dismissal of a case for lack of standing, its normal practice is to remand to allow the District Court to address the merits. Nevertheless, the court chose to reach the merits of the AICPA's challenge because it presented purely legal issues that the parties had fully briefed. The court considered whether two statutes provided the IRS with authority to implement the AFS Program. First, the court considered 31 U.S.C. § 330(a), which authorizes the Secretary of the Treasury to regulate the practice of representatives of persons before the Treasury Department. The court rejected the AICPA's argument that the AFS Program relies on this statute to regulate the business of tax return preparation, contrary to the court's decision in *Loving v. IRS*, 742 F.3d 1013 (D.C. Cir. 2014). To the contrary, the court reasoned, unenrolled preparers who participate in the AFS Program do not consent to be subject to Circular 230 in connection with their preparation of tax returns, but rather in connection with their limited right to represent clients before the IRS. The court held that the AFS Program is thus within the IRS's statutory authority to regulate those who practice before the IRS. Second, the court analyzed Code § 7803(a)(2)(A), which authorizes the IRS to "administer … the execution and application of the internal revenue laws or related statutes." This provision, the court concluded, does not provide any additional substantive authority for the AFS Program, but does authorize the IRS to publish the public directory of those who hold a "Record of Completion" of the AFS Program. "In sum, § 330(a) authorizes the IRS to establish and operate the Program, and § 7803(a)(2)(A) authorizes the agency to publish the results of the Program."

Procedural Requirements. The court also considered the AICPA's argument that the IRS had violated the Administrative Procedure Act by issuing Rev. Proc. 2014-42, 2014-29 I.R.B. 192 (6/30/14), to create the AFS Program. The revenue procedure, the AICPA argued, was a legislative rule that could be adopted only by following a notice-and-comment process, which the IRS had failed to do. The court rejected this argument for two reasons. First, the court explained, agency action constitutes a legislative rule only if it binds private parties or the agency with the force of law, which the AFS Program does not do because it "merely provides an opportunity for those unenrolled preparers who choose to participate and satisfy its requirements." Second, the court reasoned, Revenue Procedure 2014-42 did not withdraw a benefit that had been created through a notice-and-comment process and therefore could not be regarded as a legislative rule on that basis. Prior to 2011, when the IRS issued the regulations that ultimately were held invalid in *Loving*, all unenrolled tax return preparers had the ability to represent a taxpayer during an examination if the preparer had prepared and signed the return under examination. Revenue Procedure 2014-42 limits this right to unenrolled preparers who have a Record of Completion under the AFS Program. Nevertheless, the court held, the pre-2011 right of unenrolled preparers to represent taxpayers "was the product of Revenue Procedure 81-38, which—like Revenue Procedure 2014-42—was issued without notice and comment."

Dissenting Opinion. Judge Griffith concurred with the majority on the first two issues (standing of the AICPA and statutory authority for the AFS Program). In a lengthy dissenting opinion, however, he dissented on the issue whether Revenue Procedure 2014-42 was a legislative rule that could be issued only following a notice-and-comment process. In Judge Griffith's view, the revenue procedure is a legislative rule because it binds private parties with the force of law. Specifically, he emphasized, although it is voluntary for those unenrolled preparers who participate, it (1) imposes new supervisory responsibility requirements on enrolled practitioners who employ unenrolled preparers with a Record of Completion, and (2) precludes unenrolled preparers who do not hold a Record of Completion from representing taxpayers before the IRS as they formerly could. In addition, Judge Griffith reasoned, the revenue procedure is a legislative rule because it modifies a rule that had been created following a notice-and-comment process. Contrary to the majority, Judge Griffith expressed the view that the limited practice right of unenrolled preparers had been created not by Rev. Proc. 81-38, but rather by a 1959 regulation, which was subject to notice and comment. *See* Appearance of Unenrolled Preparers of Returns, 24 Fed. Reg. 1157 (2/14/59). Because Judge Griffith viewed Revenue Procedure 2014-42 as a legislative rule that had not been issued following a notice-and-comment process, the AFS Program, he concluded, is unlawful and should be vacated.

2. "All explanations tend to be self-serving." And that's okay, says the Eleventh Circuit. An affidavit that satisfies FRCP 56 can create an issue of material fact and preclude summary judgment even if it is self-serving and uncorroborated. United States v. Stein, 881 F.3d 853 (11th Cir. 1/31/18) (en banc). The government brought this action against the taxpayer to collect assessed but unpaid taxes, penalties, and interest with respect to several years. In the District Court, the government moved for summary judgment and submitted copies of the taxpayer's returns, transcripts of her accounts, and an affidavit from an IRS officer. The taxpayer responded by submitting an affidavit in which she stated that, after her husband's death, she had retained an accounting firm to prepare and file joint returns for the relevant years and that, "to the best of [her] recollection," she had paid the amounts in question. Her affidavit specified, for each year, when she had filed the return, the amount she had paid, and whether the IRS had a record of that payment. Her affidavit also stated that she no longer had bank records for the years in question and could not obtain them. The District Court granted the government's motion for summary judgment on the ground that the taxpayer had the burden to overcome the presumption of correctness that is attributed to the government's documentation, that the taxpayer had failed to meet that burden, and therefore there was no genuine issue of material fact and the government was entitled to judgment as a matter of law. On appeal, a panel of the United States Court of Appeals for the Eleventh Circuit affirmed and cited its previous opinion in *May v. United States*, 763 F.2d 1295 (11th Cir. 1985), for the proposition that "general and self-serving assertions that [the taxpayer] paid the taxes owed and related late penalties for [the relevant] tax years failed to rebut the presumption established by the [IRS's] assessments. The Eleventh Circuit subsequently vacated the panel's opinion and granted rehearing en banc. In a unanimous opinion by Judge Jordan, the Eleventh Circuit held that, if an affidavit satisfies Rule 56 of the Federal Rules of Civil Procedure, it can create an issue of material fact and preclude summary judgment even if the affidavit is self-serving and uncorroborated. The court overruled *May v. United States*, 763 F.2d 1295 (11th Cir. 1985), "to the extent it holds or suggests that self-serving and uncorroborated statements in a taxpayer's affidavit cannot create an issue of material fact with respect to the correctness of the government's assessments." The court reasoned that, if an affidavit is otherwise admissible, nothing in Rule 56 prohibits it from being self-serving or imposes a corroboration requirement. An affidavit cannot be conclusory, the court emphasized, but most of its prior decisions had concluded that a litigant's self-serving statements based on personal knowledge or observation can defeat summary judgment. Tax cases, the court explained, are no different. The court also explained that it was not holding that a self-serving or uncorroborated affidavit always is sufficient to defeat a motion for summary judgment; rather, the court held only that the self-serving and/or uncorroborated nature of an affidavit cannot prevent it from creating an issue of material fact. The court remanded to the panel to determine the impact of the taxpayer's affidavit.

a. The Eleventh Circuit panel remanded to the District Court. United States v. Stein, 889 F.3d 1200 (11th Cir. 5/9/18). After remand to the original Eleventh Circuit panel, the court, in a per curiam opinion, vacated the summary judgment entered by the District Court and remanded for further consideration. In doing so, the Eleventh Circuit panel declined to address arguments that the parties had not presented to the District Court, such as the government's argument that, to defeat summary judgment, the taxpayer had to "show that funds were actually delivered to the [Internal Revenue Service]."

3. Successive motions to vacate or revise a Tax Court decision that raise substantially the same grounds as prior motions do not affect the 90-day period for filing a notice of appeal. Annamalai v. Commissioner, 884 F.3d 530 (5th Cir. 3/8/18). Addressing an issue of first impression, the U.S. Court of Appeals for the Fifth Circuit has held that successive motions to vacate or revise a Tax Court decision that raise substantially the same grounds as a prior motion do not affect the time period in which a party may appeal the Tax Court's decision. Under Federal Rule of Appellate Procedure 13(a), a party who wishes to appeal a decision of the Tax Court must file a notice of appeal within ninety days. The 90-day period runs from either (1) the entry of the Tax Court's decision, or (2) if a party moves to vacate or revise the Tax Court's decision, from the entry of the Tax Court's ruling on that motion. In this case, the Tax Court entered its decision on June 23, 2016. On July 13, 2016, the taxpayers filed motions to vacate the Tax Court's decision. The Tax Court denied those motions on November 18, 2016. On December 12, 2016, the taxpayers jointly filed a motion to vacate that did not raise any substantially new grounds or arguments. The Tax Court denied this second motion on December 22, 2016. On March 15, 2017, the taxpayers filed a notice of appeal with the clerk of the Tax Court. In a per curiam opinion, the Fifth Circuit held that the taxpayers' second motion to vacate, which raised substantially the same grounds as their first, had no effect on the period within which they could appeal the Tax Court's decision. The court found support for its conclusion in its prior decisions concluding that a successive motion for reconsideration based on substantially the same grounds as a prior motion does not toll the running of the thirty-day period provided by Federal Rule of Appellate Procedure 4(a) for appealing decisions in civil cases. The court also noted that its conclusion was consistent with that of the Tenth Circuit, which similarly had held that a taxpayer's "renewed" motion to vacate a decision of the Tax Court did not affect the running of the 90-day period for appeal. *See Okon v. Commissioner*, 26 F.3d 1025 (10th Cir. 1994); *see also Dean v. Commissioner*, 2017 WL 4232520 (D.C. Cir. 9/13/17) (unpublished opinion); *Robertson v. Commissioner*, 22 Fed. Appx. 215 (4th Cir. 2001). Because the taxpayers had filed their notice of appeal more than ninety days after November 18, 2016, the date on which the Tax Court denied their initial motions to vacate, the Fifth Circuit dismissed their appeal as untimely.

XI. WITHHOLDING AND EXCISE TAXES

A. Employment Taxes

B. Self-employment Taxes

C. Excise Taxes

XII. TAX LEGISLATION

A. Enacted

XIII. TRUSTS, ESTATES & GIFTS