

Recent Developments in Federal Income Taxation

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To obtain today's outline and slides:

<https://tinyurl.com/outline0520>

<https://tinyurl.com/slides0520>

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Notice 2020-32, 2020-21 I.R.B. ____ (5/1/20)

Outline: item D.1, page 2

- Federally-backed loans made to businesses under the Paycheck Protection Program (PPP) must be used to fund payroll and certain other expenses.
- Businesses that use the loans in this manner can apply to have the loans forgiven.
- CARES Act § 1106(i) provides that any income arising from having PPP loans forgiven is excluded from gross income.
- Issue: can a business that has a PPP loan forgiven deduct expenses funded with the loan proceeds?
- Notice 2020-32: No. Section 265 precludes a deduction.
 - Section 265(a)(1): disallows a deduction for “any amount otherwise allowable as a deduction which is allocable to one or more classes of income other than interest wholly exempt from the taxes imposed by this subtitle.”

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S Corporations and the Restriction on Distributions For Businesses Obtaining PPP Loans

- CARES Act Section 4003(c)(1)(F) provides for PPP loans that:
 - “the agreement [must] provide[] that, until the date 12 months after the date the loan or loan guarantee is no longer outstanding, the eligible business shall not pay dividends or make other capital distributions with respect to the common stock of the eligible business;”
- Application to S corporations:
 - Is this actually reflected in the PPP loan agreements?
 - S corporations often are required to distribute sufficient funds to shareholders to allow shareholders to pay tax on their share of income.
 - It seems S corporations cannot make such distributions during the 12-month period if they obtain a loan
 - Is it possible to withdraw funds in other forms without violating this condition?

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**Final Regulations-Bonus Deprec'n Under § 168(k)
T.D. 9874, 84 F.R. 50108 (9/24/19)**

Outline: item E.1.b, page 5

- 100% for property *acquired and placed in service* after September 27, 2017
 - Percentage declines beginning in 2023
 - Property acquired *on or before* September 27, 2017, is eligible for only 50% if placed in service in 2017, 40% in 2018, 30% in 2019, 0% after 2019.
- Used property is now eligible for bonus depreciation if *acquired and placed in service* after September 27, 2017
- Technical glitch fixed: pursuant to CARES Act, “qualified improvement property” now has a 15-year recovery period retroactively to 2018.
 - Result: eligible for bonus depreciation.

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Rev. Proc. 2020-25, 2020-19 I.R.B. 785 (04/17/20)

Outline: item E.1.c, page 5

- Technical glitch fixed: pursuant to CARES Act, “qualified improvement property” now has a 15-year recovery period retroactively to 2018.
 - Result: eligible for bonus depreciation.
- Notice 2020-25:
 - Provides guidance allowing a taxpayer to change its depreciation under Code § 168 for qualified improvement property placed in service by the taxpayer after December 31, 2017, in its taxable year ending in 2018 (2018 taxable year), 2019 (2019 taxable year), or 2020 (2020 taxable year).
 - Allows a taxpayer to make a late election, or to revoke or withdraw an election, under § 168(g)(7), (k)(5), (k)(7), or (k)(10) of the Code for the taxpayer's 2018 taxable year, 2019 taxable year, or 2020 taxable year.

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Carryback of 2018 NOLs
Notice 2020-26, 2020-18 I.R.B. 744 (4/10/2020)
Outline: item H.1.d, page 6

- The CARES Act:
 - Suspends the disallowance of “excess business losses” for TY beginning before 2021
 - NOLs arising in 2018, 2019, and 2020:
 - May be carried back to each of the five preceding taxable years, then forward indefinitely.
 - For TY beginning before January 1, 2021 (generally, 2018, 2019 and 2020), the 80 percent taxable income limitation on NOL carryforwards does not apply.

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Notice 2020-26, 2020-18 I.R.B. 744 (4/10/2020)
Outline: item H.1.e, page 6

- To carry back NOLs, a taxpayer can:
 - File an amended return
 - File for a quick carryback using Form 1139 (Corporations) or Form 1045 (taxpayers other than corporations)
- Limitation period:
 - The CARES Act did not change the due date of Forms 1139 or 1045
 - Normally, under § 6411, an application on Form 1139 or 1045 must be filed within 12 months of the close of the taxable year in which the NOL arose.
 - For 2018 NOLs, these forms would have been due December 31, 2019
 - Under § 6081, the Treasury Secretary can grant a reasonable extension of up to 6 months for filing any return declaration, or statement
- Notice 2020-26:
 - Extends to June 30, 2020, the time to file Forms 1139 or 1045 for taxpayers with NOLs that arose in a taxable year that began during calendar year 2018 and that ended on or before June 30, 2019.
 - Include at top of form: Notice 2020-26, Extension of Time to File Application for Tentative Carryback Adjustment.”

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Notice 2020-26, 2020-18 I.R.B. 744 (4/10/2020)

Outline: item H.1.f, page 6

- The IRS has posted FAQs on its website regarding filing forms 1139 and 1045
 - Forms 1139 and 1045 can be faxed to numbers specified in the FAQs
 - Amended returns on Form 1040-X or 1120-X cannot be faxed.
- If taxpayers need to amend a return prior to carrying back an NOL using Form 1139 or 1045, the FAQs provide:
 - If you need to amend a previously filed return prior to filing Form 1139 or Form 1045, follow normal filing procedures by timely filing hard copy Forms 1120-X/1139 and hard copy Forms 1040-X/1045 as applicable, in order to adhere to any filing deadlines particular to your situation.

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CARES Act Suspension of RMDs

Outline: item B.1, page 7

- If a taxpayer turned 70½ in 2019, he or she was required take their 2019 minimum distribution by April 1, 2020.
- Such taxpayers, and others who previously had turned 70½, also must take their 2020 RMD by December 31, 2020.
- The CARES Act:
 - Suspends all RMDs for 2020.
 - These include both RMDs that should have been taken by April 1, 2020, and those that normally would be taken by December 31, 2020.
- Issues:
 - Application to inherited retirement accounts (CARES Act says RMDs suspended for some inherited accounts)
 - How to treat RMDs already taken in 2020? Rollover to IRA? Treat as coronavirus-related distribution and repay over three years?

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Frost v. Commissioner
154 T.C. No. 2 (1/7/20)
Outline: item A.1, page 7

- The IRS has the initial burden of production with respect to a taxpayer's liability for any penalty to come forward with sufficient evidence indicating the imposition of penalties is appropriate.
- As part of that burden, the Service must produce evidence that it complied with § 6751(b)(1), which requires that the initial determination of the assessment of a penalty be personally approved in writing by the immediate supervisor of the person making the determination.
- Held: once the IRS meets its initial burden of production regarding supervisory approval of a penalty, the burden shifts to the taxpayer to show otherwise, e.g., that the penalty was formally communicated to the taxpayer before the supervisory approval.
 - Here, the IRS failed to meet its burden of production with respect to two of the years involved and was precluded from imposing penalties for those years.
 - IRS met its burden with respect to one year and taxpayer failed to offer contrary evidence.

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Melasky v. Commissioner,
151 T.C. No. 8 (10/10/18) and 151 T.C. No. 9 (10/10/18)
Outline: item F.1, page 9

- The taxpayers hand-delivered to the Service at the Service's office in Houston a check for \$18,000 and requested that the check be applied against their 2009 federal income tax liability.
- A few days later, the Service levied against the bank account on which the check had been drawn and applied the proceeds of the levy to an earlier tax year. Therefore, the check bounced.
- The taxpayers had a CDP hearing. The IRS settlement officer determined that the levy proceeds were an involuntary payment that the IRS was free to apply as it wished.
- Held:
 1. The standard of review in Tax Court is for abuse of discretion, not (as the parties had agreed) *de novo*. The underlying tax liability was not at issue.
 2. The levy proceeds were an involuntary payment that the IRS could apply to earlier years.
 3. The IRS did not abuse its discretion in rejecting the taxpayers' proposed partial-pay installment agreement.

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**Melasky v. Commissioner,
125 A.F.T.R.2d 2020-746 (5th Cir. 2/3/20)
*Outline: item F.1.b, page 10***

- The Fifth Circuit has affirmed the Tax Court:
 - Declined to adopt an “equitable exception to the normal rules” regarding voluntary and involuntary tax payments.
 - The Melaskys had notice of the IRS’s intent to levy issued to them in 2001, long before the IRS’s actual levy in 2009.
 - “[b]y choosing . . . a personal check rather than a certified check or money order, the Melaskys ran [the] risk” that the IRS would levy on their bank accounts before the check representing their voluntary payment was presented to the bank by the IRS.

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**Seely v. Commissioner
T.C. Memo. 2020-6 (1/13/20)
*Outline: item H.1, page 10***

- Held: a Tax Court petition that was timely mailed, but that had no postmark in the envelope, was timely mailed within the required 90-day period based on a declaration of mailing from the taxpayer’s attorney.

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Notice 2020-23, 2020-18 I.R.B. 742 (4/9/20)

Outline: item H.2, page 11

- Code § 7508A authorizes the Treasury Secretary to postpone the time for performing certain acts in federally declared disaster areas.
- Notice 2020-17: income tax payments due on 4/16/20 now due on 7/15/20
- Notice 2020-18: income tax returns due on 4/15/20 now due on 7/15/20
- Notice 2020-20: Form 709 and payments of federal gift and GST tax due on 4/15/20 now due on 7/15/20

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Notice 2020-23, 2020-18 I.R.B. 742 (4/9/20)

Outline: item H.2, page 11

- All persons with a federal tax payment obligation or form filing obligation due to be performed on or after 04/01/20 and before 7/15/20 are considered affected by COVID-19
- Extends specified filing and payment obligations to 7/15/20, including
 - Filing Form 1040 series, 1120 series, 1065, 1041, 709, 990-T
 - Payments of income tax, estate tax, gift tax, GST tax, UBIT, quarterly estimated tax payments
- Extends specified time-sensitive actions to 7/15/2020, including
 - Filing a claim for refund (e.g., 2016 refund claims), bringing suit for a refund, and filing a Tax Court petition
- Extends time for IRS to perform time-sensitive acts by 30 days if the act must be performed on or after 04/06/20 and before 07/15/20, such as assessment of tax.

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Limits of Section 165(i)

- Section 165(i)(1):
 - “any loss occurring in a disaster area and attributable to a federally declared disaster may, at the election of the taxpayer, be taken into account for the taxable year immediately preceding the taxable year in which the disaster occurred.”
- Issues:
 - Whether the President’s declaration of a national “emergency” under the Stafford Act due to COVID-19 will be interpreted as being the same as a federally declared disaster.
 - Conclusion: yes. The IRS issued Notice 2020-23 (extending deadlines to July 15) pursuant to Code § 7508A, which authorizes the Treasury Secretary to postpone the time for performing certain acts for taxpayers affected by a “federally declared disaster”
 - What losses in 2020 can be treated as attributable to a federally declared disaster?
 - All realized market losses on theory that all are attributable to the COVID-19 pandemic?

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