RECENT DEVELOPMENTS IN FEDERAL INCOME TAXATION

We apologize to our readers. If we had more time, this outline would be much shorter.

By

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State Bar of Texas Tax Section
First Wednesday Tax Update
August 7, 2024

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I. ACCOUNTING

II. BUSINESS INCOME AND DEDUCTIONS

III. INVESTMENT GAIN AND INCOME

IV. COMPENSATION ISSUES

A. Fringe Benefits

B. Qualified Deferred Compensation Plans

1. Congress has increased the age at which RMDs must begin to 73 and eventually to age 75. A provision of the SECURE 2.0 Act, Division T, Title I, § 107 of the Consolidated Appropriations Act, 2023, amended Code § 401(a)(9)(C)(i)(I) to increase the age at which required minimum distributions (RMDs) from a qualified plan (including IRAs) must begin from 72 to 73. Pursuant to this amendment, RMDs must begin by April 1 of the calendar year following the later of the calendar year in which the employee attains age 73 or, in the case of an employer plan, the calendar year in which the employee retires. This latter portion of the rule allowing deferral of RMDs from employer plans until retirement does not apply to a 5-percent owner (as defined in § 416). The increase in the age at which RMDs must begin to age 73 applies to distributions required to be made after December 31, 2022, with respect to individuals who attain age 73 after such date. Thus, an individual who attained age 72 in 2022 must take his or her first RMD by April 1, 2023, but an individual who attains age 72 in 2023 need not take the first RMD until April 1, 2025. The legislation further increases the age at which RMDs must begin to age 75 for individuals who attain age 75 after 2032.

a. Those born in 1951 (and who therefore attain age 72 in 2023) and who received distributions from January 1 through July 31, 2023, that are mischaracterized as RMDs have until September 30, 2023, to deposit such amounts in an eligible retirement plan and treat the deposit as a tax-free rollover. Notice 2023-54, 2023-31 I.R.B. 382 (7/14/23). Plan administrators and other payors made the Service aware that automated payment systems would need to be updated to reflect the legislative change in the age at which RMDs must begin. Because such changes could take time, it is possible that those born in 1951 and who therefore attain age 72 in 2023 would receive distributions in 2023 that are mischaracterized as RMDs (and therefore normally ineligible for rollover). This notice grants relief targeted at this situation. For employer-sponsored plans, the notice provides that (1) payors or plan administrators will not be treated as having failed to satisfy applicable requirements based on failure to treat a distribution as an eligible rollover distribution merely because the plan made a distribution from January 1, 2023, through July 31, 2023, to a participant born in 1951 (or the participant's surviving spouse) that would have been an RMD if Congress had not increased the age at which RMDs must begin from 72 to 73, and (2) participants born in 1951 who received such a distribution have until September 30, 2023, to roll over the mischaracterized distribution. For IRAs, the notice provides similar relief and specifies that IRA owners born in 1951 (or the owner's surviving spouse) who received a distribution from the IRA from January 1, 2023, through July 31, 2023, that would have been an RMD if Congress had not increased the age at which RMDs must begin from 72 to 73 can roll over the mischaracterized distribution to an eligible retirement plan if they do so by September 30, 2023. Although IRA owners normally can make only one tax-free rollover in a 12-month period, the notice provides that IRA owners entitled to the relief provided by the notice can roll over the mischaracterized distribution even if they have already rolled over a distribution in the previous 12 months. A rollover of the mischaracterized distribution, however, will preclude the IRA owner from rolling over another distribution in the succeeding 12 months (but could still make a direct trustee-to-trustee transfer as described in Rev. Rul. 78-406, 1978-2 CB 157).

b. Those born in 1959 must begin taking RMDs at age 73 (and not age 75). REG-103529-23, Required Minimum Distributions, 89 F.R. 58644 (7/19/24). Treasury and the IRS have issued proposed regulations that address various issues reserved in the final regulations on RMDs issued on the same date and discussed elsewhere in this outline. Generally, the proposed regulations address issues raised by provisions Congress enacted or amended in the SECURE 2.0 Act in late 2022. One of those provisions is § 401(a)(9)(C)(i)(I), which Congress amended to provide that the required beginning date on which RMDs must begin is generally April 1 of the calendar year following the year in which the account owner attains the "applicable age." The proposed regulations clarify an issue raised by the statutory language Congress used. As amended by the 2022 legislation, Code § 401(a)(9)(C)(v) defines the term "applicable age" for purposes of determining whe RMDs must begin in a way that appears to provide that those born in 1959 must begin taking RMDs both at age 73 and at age 75. Section § 1.401(a)(9)-2(b)(2)(v) of the proposed regulations clarifies that those born in 1959 must begin taking RMDs at age 73, and that those born in 1960 and later years must begin taking RMDs at age 75. The following table summarizes the age at which individuals born in specific years must begin taking RMDs:

Year of birth	Age at which RMDs must begin
Before July 1, 1949	70-½
July 1, 1949, through Dec. 31, 1950	72
1951-1959	73
1960 and later	75

2. Final regulations on required minimum distributions. T.D. 10001, Required Minimum Distributions, 89 F.R. 58,886 (7/19/24). Treasury and the IRS have finalized proposed regulations (REG-105954-20, Required Minimum Distributions, 87 F.R. 10504 (2/24/22)) that address required minimum distributions (RMDs) from qualified retirement plans and annuity contracts and related matters. The final regulations update existing regulations to reflect a number of statutory changes. The most significant of these statutory changes were made by the SECURE Act, enacted on December 20, 2019, as Division O of the 2020 Further Consolidated Appropriations Act. Among other changes, the SECURE Act amended Code § 401(a)(9)(E) to modify the RMD rules for inherited retirement accounts (defined contribution plans and IRAs). The final regulations are lengthy and address these and a number of other issues. This discussion will focus on only the guidance provided by the final regulations on the change made by the SECURE Act to RMDs for inherited retirement accounts. Readers should consult the final regulations for additional guidance.

The SECURE Act changes to RMDs from inherited retirement accounts. A provision of the SECURE Act, Division O, Title IV, § 401 of the 2020 Further Consolidated Appropriations Act, amended Code § 401(a)(9)(E) to modify the required minimum distribution (RMD) rules for inherited retirement accounts (defined contribution plans and IRAs). The amendments require all funds to be distributed by the end of the 10th calendar year following the year of death (the "10-year rule"). The current rules, which permit taking RMDs over life expectancy, continue to apply to a designated beneficiary who is an "eligible designated beneficiary," which is any designated beneficiary who is: (1) a surviving spouse, (2) a child of the participant who has not reached the age of majority, (3) disabled within the meaning of § 72(m)(7), (4) a chronically ill individual within the meaning of § 7702B(c)(2) with some modifications, or (5) an individual not in any of the preceding categories who is not more than 10 years younger than the deceased individual. These changes generally apply to distributions with respect to those who die after December 31, 2019.

The final regulations' interpretation of the 10-year rule in the SECURE Act. The final regulations, like the proposed regulations, adopt an interpretation of the 10-year rule that appears to differ from the plain language of the statute and from the interpretation of the legislation of most advisors. The statute provides that, when the designated beneficiary is *not* an eligible designated beneficiary, all funds must be distributed by the end of the 10th calendar year following the year of death and that this rule applies whether or not RMDs to the employee or IRA owner have begun. There appears to be no requirement in the statutory provisions to withdraw any minimum amount before that date. The final regulations, however, like the proposed regulations, distinguish between situations in which the employee or IRA owner dies before the required beginning date for distributions, and situations in which death occurs after such date. When the employee or IRA owner dies *before* the required beginning date for distributions, the final regulations provide that no distribution is required before the 10th calendar year following the year of death. However, in situations in which the employee or IRA owner dies *after* the required beginning date for distributions, the final regulations provide that a designated beneficiary who is *not* an eligible designated beneficiary must begin taking RMDs over the beneficiary's life expectancy in the year following the year of death and must withdraw all funds in the account by the end of the 10th calendar year following the year of death. The preamble to the proposed regulations described this rule as follows:

> For example, if an employee died after the required beginning date with a designated beneficiary who is not an eligible designated beneficiary, then the designated beneficiary would continue to have required minimum distributions calculated using the beneficiary's life expectancy as under the existing regulations for up to nine calendar years after the employee's death. In the tenth year following the calendar year of the employee's death, a full distribution of the employee's remaining interest would be required.

87 F.R. 10514. This interpretation arguably differs from the plain language of the statute and, ironically, even from the interpretation in IRS Publication 590-B (page 11), which was issued for 2021. Treasury and the IRS have adhered to this interpretation in the final regulations despite a significant number of comments on the proposed regulations arguing that, for all beneficiaries who are not eligible designated beneficiaries, the relevant statutory provisions do not require RMDs prior to the tenth year after the year of death.

Prior guidance on missed RMDs. In a series of notices, the IRS provided relief to those who inherited IRAs and who, in the IRS's view, had failed to take RMDs under the interpretation of the 10-year rule set forth in the proposed regulations. The most recent of these notices was Notice

2024-35, 2024-19 I.R.B. 1051 (4/16/24).[1] These notices provide that the IRS will not assert that an excise tax is due under § 4974 from an individual who did not take a "specified RMD." A "specified RMD" is defined as any distribution required to be made in 2021, 2022, 2023, or 2024 under a defined contribution plan or IRA if the payment would be required to be made to (1) a designated beneficiary of an employee or IRA owner who died in 2020, 2021, 2022, or 2023 and on or after the employee or IRA owner's required beginning date, and (2) the designated beneficiary is not taking lifetime or life expectancy payments as required by § 401(a)(9)(B)(iii). In other words, the IRS will not assert that the excise tax of § 4974 is due from a beneficiary who (1) is not an eligible designated beneficiary (and who therefore is subject to the 10-year rule), (2) inherited the retirement account from an employee or IRA owner who died in 2020, 2021, 2022, or 2023 and on or after the required beginning date of distributions, and (3) were required to take RMDs in 2021, 2022, 2023, or 2024 under the interpretation of the 10-year rule in the proposed regulations but failed to do so. These notices provide the same relief to beneficiaries of eligible designated beneficiaries if the eligible designated beneficiary died in 2020, 2021, 2022, or 2023 and was taking lifetime or life expectancy distributions.

Clarification that beneficiaries subject to the 10-year rule need not make up missed RMDs. One significant issue that arose under the notices discussed above was what corrective action, if any, was required after the relief period provided by the notices. For example, assume the designated beneficiary of an IRA is *not* an eligible designated beneficiary (and therefore subject to the 10-year rule) and inherited the account in 2020 from the account owner who died that year when he was already taking RMDs. Under the interpretation of the proposed (and now final) regulations, this designated beneficiary should have begun taking RMDs in 2021. If this designated beneficiary failed to take any RMDs through 2024, the question is how much the beneficiary must withdraw in 2025, the first year for which the IRS did not effectively waive RMDs in this situation. Can the beneficiary simply begin taking RMDs for 2025 and future years and not worry about those for 2021 through 2024, or must the beneficiary withdraw in 2025 those missed in 2021 through 2024 *and* the one for 2025? The final regulations clarify that beneficiaries in this situation need not make up missed RMDs. Therefore, in the example just given, the beneficiary can simply begin taking RMDs for 2025 and future years and need not withdraw the amounts the beneficiary failed to take for 2021 through 2024. The years of the missed RMDs, however, still count as years within the 10-year period. Therefore, this beneficiary must take RMDs for 2025 through 2029 (the five years remaining in the first nine years after the year of death) and must withdraw any remaining funds from the account in 2030.

Effective date. The regulations are generally effective on September 17, 2024, but the rules apply for purposes of determining RMDs for calendar years beginning after 2024.

3. Go ahead and steal your spouse's identity, at least for purposes of receiving RMDs. A provision of the SECURE 2.0 Act, Division T, Title III, § 327 of the Consolidated Appropriations Act, 2023, amended Code § 401(a)(9)(B)(iv) to provide that, if a retirement account participant dies before reaching the age at which RMDs must begin and has designated a spouse as the sole beneficiary, then the spouse can make an irrevocable election to be treated as the participant for purposes of receiving RMDs. Making this election allows the surviving spouse to defer RMDs until the deceased spouse would have reached the age at which RMDs must begin. For example, if a husband passes away at age 63 and is survived by his wife who is age 68 and is his sole designated beneficiary, then she can elect to be treated as her husband for purposes of receiving RMDs. This means that she can defer taking RMDs from the account until her husband would have reached age 73 (a period of 10 years in this example) rather than when she attains age 73. This change is effective for calendar years beginning after December 31, 2023.

[1] The others were Notice 2022-53, 2022-45 I.R.B. 437 (10/7/22) and Notice 2023-54, 2023-31 I.R.B. 382 (7/14/23).

a. Guidance on the surviving spouse's election to be treated as the deceased spouse for purposes of determining when RMDs must begin. REG-103529-23, Required Minimum Distributions, 89 F.R. 58644 (7/19/24). Treasury and the IRS have issued proposed regulations that address various issues reserved in the final regulations on RMDs issued on the same date and discussed elsewhere in this outline. Generally, the proposed regulations address issues raised by provisions Congress enacted or amended in the SECURE 2.0 Act in late 2022. One of those provisions is § 401(a)(9)(B)(iv), which Congress amended to provide that, if a retirement account participant dies before reaching the age at which RMDs must begin and has designated a spouse as the sole beneficiary, then the spouse can make an irrevocable election to be treated as the participant for purposes of receiving RMDs. The proposed regulations provide a series of rules that would apply with respect to this spousal election. *First*, § 1.401(a)(9)–5(g)(3)(ii)(A) of the proposed regulations provides that, if the account owner dies before the owner's required beginning date for RMDs, then the surviving spouse is automatically treated as having made the election, i.e., the surviving spouse need not affirmatively make the election. In contrast, § 1.401(a)(9)–5(g)(3)(ii)(B) of the proposed regulations provides that, if the account owner dies *on or after* the owner's required beginning date for RMDs, then the spouse is not automatically treated as having made the election and must affirmatively make the election. The terms of the plan, however, can make this election a default election for the surviving spouse. *Second*, § 1.401(a)(9)–5(g)(3)(ii)(C) of the proposed regulations provides that, if this election is in effect for a surviving spouse, then the surviving spouse's RMDs are calculated using the Uniform Life Table in Reg. § 1.401(a)(9)-9(c) for the *surviving spouse's* age. Thus, although this election permits a surviving spouse who is older than the deceased spouse to benefit by delaying taking RMDs until the deceased spouse would have reached the age at which RMDs must begin, this benefit is somewhat reduced by the requirement that, when RMDs begin, they are calculated using the suriving spouse's age rather than the deceased spouse's age. The exception to this rule is that, if the deceased spouse died on or after the required beginning date for distributions, then the surviving spouse's RMDs are calculated using the greater of the surviving spouse's life expectancy or the deceased spouse's remaining life expectancy. *Third*, § 1.401(a)(9)–5(g)(3)(ii)(D) of the proposed regulations provides that, if this election is in effect and the surviving spouse has begun receiving RMDs (or is treated as receiving RMDs under specified rules), then the surviving spouse's beneficiary must continue taking RMDs over the surviving spouse's remaining life expectancy and must withdraw any remaining funds in the account by the end of the tenth calendar year following the year of the surving spouse's death. In other words, the surviving spouse's beneficiary is *not* treated as an eligible designated beneficiary and therefore must withdraw all funds in the account by the end of the tenth calendar year following the year of the surviving spouse's death. *Fourth*, § 1.401(a)(9)–5(g)(3)(ii)(E) of the proposed regulations specifies the effective date of the spousal election. The spousal election is available only if the first year for which annual RMDs to the surviving spouse must be made is 2024 or later. The preamble to the proposed regulations provides the following example:

> For example, if an employee who died in 2017 and before the employee's required beginning date would have reached the applicable age in 2024 or later, then the first year for which an annual required minimum distribution is due would be 2024 or later, and the spousal election could apply. However, if the employee would have reached the applicable age in 2022, then the first year for which an annual required minimum distribution is due to the spouse was 2022, and the spousal election would not be available.
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> Similarly, if the employee died in 2021 and after the employee's required beginning date, then the spouse must begin receiving annual required minimum distributions (based on the spouse's remaining life expectancy) in 2022, and the spousal election would not be available.

4. Could you PLESA give me some of my money back for an emergency (or, for that matter, a non-emergency)? Notice 2024-22, 2024-6 I.R.B. 662 (1/12/24). A provision of the SECURE 2.0 Act, specifically Division T, Title VI, § 127 of the Consolidated

Appropriations Act, 2023, amended Code § 402A (and ERISA §§ 801-804) to authorize Pension-Linked Emergency Savings Accounts ("PLESAs") effective for plan years beginning after December 31, 2023. In general, PLESAs are *optional* short-term savings accounts established and maintained within a §§ 401(k), 403(b), or 457(b) defined contribution plan. If an employer's defined contribution plan authorizes a PLESA, eligible employees (generally, non-highly compensated employees) may make Roth-like contributions up to a maximum account balance of $2,500 (indexed annually for inflation) to a PLESA established for the employee's benefit. According to separate guidance issued by the Department of Labor Plans (see DOL's F.A.Q.s), plans have flexibility to apply the $2,500 limitation either to employee contributions or account size. For example, a plan could provide that an employee cannot contribute if the employee already has contributed $2,500, which effectively excludes earnings from the calculation, or the plan could provide that an employee cannot contribute if the total account balance would exceed $2,500, which effectively includes earnings in the calculation. Employers cannot contribute to a PLESA but must take employee contributions to the PLESA into account when determining employer matching contributions to the plan. In other words, if an employer's §§ 401(k), 403(b), or § 457(b) defined contribution plan provides for matching contributions, then employers must match an employee's PLESA contributions; however, such matching contributions are allocated to the non-PLESA portion of the plan. Withdrawals from a PLESA are tax-free regardless of the reason for the withdrawal, i.e., no real "emergency" is required for a PLESA withdrawal. *See* § 402(e)(7) (allowing withdrawals "in whole or in part at the discretion of the participant"). Employees who contribute to a PLESA may withdraw from the PLESA as frequently as monthly without reducing their linked defined contribution plan account and without incurring the normal § 72(t) early withdrawal penalty. In addition, subject to mandatory notice requirements and compensation percentage limits, an employer may automatically enroll its eligible employees into its PLESA program.

- Recall that the authors previously have discussed other SECURE 2.0 exceptions to the early withdrawal penalty of § 72(t): up to $1,000 for "personal and family emergencies" [§ 72(t)(2)(l)]; up to $10,000 for victims of domestic abuse [§ 72(t)(2)(K)]; early distributions to a "terminally ill individual" [§ 72(t)(2)(L)]. For further background regarding PLESAs, see the F.A.Q.s recently issued by the Department of Labor.

Notice 2024-22: The notice does not provide comprehensive guidance regarding PLESA programs but instead provides initial guidance concerning specific anti-abuse rules in Code § 402A(e)(12). Although we leave the details to our readers, the anti-abuse rules under § 402A(e)(12) generally prohibit a participating employee from switching back and forth between contributing to and withdrawing from a PLESA to take advantage of an employer's matching contributions. In other words, left unchecked, an employee could contribute to a PLESA, thereby triggering an employer matching contribution, withdraw the contributed funds, and then contribute them again, triggering another employer matching contribution. The notice permits employers to combat this strategy by adopting reasonable procedures to limit the frequency or amount of an employer match. The notice provides examples of procedures that would *not* be considered reasonable, such as a plan provision that requires employees to forfeit matching contributions due to an employee's withdrawal from the PLESA. Notice 2024-22 also alleviates the concerns of some advisors that Rev. Rul. 74-55, 1974-1 C.B. 89, and Rev. Rul. 74-56, 1974-1 C.B. 89, apply to PLESAs. Oversimplifying for the sake of convenience, Rev. Rul. 74-55 and Rev. Rul. 74-56 prohibit employers from adopting certain unsanctioned withdrawal provisions within retirement plans. Notice 2024-22 states that the "Treasury Department and the I.R.S. do not view these revenue rulings as applicable in the context of PLESAs." Notice 2024-22 also invites practitioner comments and suggestions regarding the matters discussed in the notice as well as any other aspect of PLESA-enabled retirement plans.

C. Nonqualified Deferred Compensation, Section 83, and Stock Options

D. Individual Retirement Accounts

V. PERSONAL INCOME AND DEDUCTIONS

VI. CORPORATIONS

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

1. Judge Gustafson revisits *Grecian Magnesite*, but this time rules against this non-U.S. taxpayer selling her partnership interest due to § 751. Rawat v. Commissioner, T.C. Memo 2023-14 (2/7/23). We previously have written about the entity-theory versus aggregate-theory dust-up between the IRS and non-U.S. persons selling interests in partnerships conducting business in the U.S. For example, in *Grecian Magnesite Mining, Industrial & Shipping Co., S.A. v. Commissioner*, 149 T.C. 63 (2017), the Tax Court (Judge Gustafson) ruled against the IRS (and against the IRS's position in Rev. Rul. 91-32, 1991-1 C.B. 107) to hold that a non-U.S. person's gain from the sale of an interest in a partnership conducting a U.S. trade or business is not U.S.-source income (because the partnership interest is personal property) and therefore is not subject to U.S. taxation unless such gain (i) is captured by § 897(g) (gain attributable to U.S. real property) or (ii) is captured by § 865(e)(2) (gain attributable to a U.S. office or fixed place of business). The IRS in *Grecian Magnesite* had argued that a non-U.S. person's gain from the sale of an interest in a partnership conducting business in the U.S. should be analyzed under the aggregate-theory of partnership taxation, meaning that the gain would be considered U.S. source income because it is attributable to the underlying U.S. assets held by the partnership. *See* Rev. Rul. 91-32, 1991-1 C.B. 107. Nevertheless, Judge Gustafson declined to adopt the IRS's reasoning (labeling the IRS's analysis in Rev. Rul. 91-32 as "cursory") and ruled for the taxpayer. Importantly, *Grecian Magnesite* did not address whether the result might be different if the partnership conducting business in the U.S. held inventory items subject to § 751.

Rawat Decision by Judge Gustafson. In *Rawat v. Commissioner*, T.C. Memo 2023-14 (2/7/23), Judge Gustafson got the chance to address the issue left open in *Grecian Magnesite*: whether gain from a non-U.S. person's sale of an interest in a partnership holding inventory items and conducting business in the U.S. is considered U.S. source income by virtue of § 751 and the U.S. income-sourcing rules of §§ 861-865. This time, the Tax Court (again, Judge Gustafson) adopted the IRS's aggregate-theory argument and held against the taxpayer. The taxpayer in *Rawat* was a Canadian citizen and nonresident of the U.S. during 2007 and 2008. In 2008, the taxpayer sold her interest in a partnership doing business in the U.S. in exchange for a promissory note with a face amount of $438 million. The principal of the promissory note was not payable until 2028. The IRS sought to tax $6.5 million of the taxpayer's gain ("inventory gain") in 2008 because that amount was attributable to § 751 inventory items held by the partnership and allocable to the taxpayer's partnership interest. The taxpayer argued that, because the inventory gain was realized and recognized prior to the enactment of § 864(c)(8) (see below), the Tax Court's decision in *Grecian Magnesite* controlled. The IRS disagreed, arguing that the inventory gain, unlike the gain in *Grecian Magnesite*, was subject to § 751, thereby rendering the gain as U.S. source income under §§ 861-865 and the IRS's aggregate theory asserted in *Grecian Magnesite*. This time around, Judge Gustafson ruled for the IRS and against the taxpayer. Judge Gustafson reasoned that, although § 751 is not a sourcing rule, the rule in § 741 generally treating the sale of a partnership interest as the disposition of a capital asset is expressly subject to the § 751 carve-out for inventory items. Then, examining the special sourcing rules under §§ 861(a)(6) (sale or exchange of inventory property) and 865(b) (exception for inventory property), Judge Gustafson concluded that the taxpayer's inventory gain from the sale of her partnership interest should be considered U.S.-source income subject to U.S. tax notwithstanding the Tax Court's holding in *Grecian Magnesite* regarding more general § 741 gain.

a. D.C. Circuit reverses Tax Court, but almost seven years ago (see below), Congress had the last word. Rawat v. Commissioner, ___ F.4th ___ (D.C. Cir. 7/23/24), *rev'g* T.C. Memo 2023-14 (2/7/23). After losing in the Tax Court, the taxpayer appealed to the U.S. Court of Appeals for the D.C. Circuit. In an opinion by Chief Judge Srinivasan, the court aptly summarized the dispute between the taxpayer and the IRS as follows:

> While the parties agreed that § 751(a) requires inventory gain to be taxed as ordinary income, the Commissioner argued that it does more than that: in his view, § 751(a) also deems gain on the sale of a partnership interest attributable to inventory to be gain on the sale *of* inventory, such that it can be taxable as U.S.-source income. Rawat, however, contended that § 751(a) has a more limited scope. She insisted that it does not give rise to a deemed sale of inventory and thus does not render taxable what would otherwise be nontaxable income. Rather, according to Rawat, § 751(a) merely subjects inventory gain to ordinary-income taxation *if* the gain is otherwise taxable. And Rawat considered the inventory gain she realized to be nontaxable, as it arose from the sale of a partnership interest, not from the actual sale of inventory. Accordingly, she maintained, the gain constitutes proceeds from the sale of general personal property (as opposed to inventory) and is foreign-source income because she is a nonresident alien.

___F.4th at ___. After framing the issue in the above-quoted manner, the court's analysis turned to the essential question: did the non-U.S. taxpayer sell inventory (by virtue of § 751(a)), or did the non-U.S. taxpayer sell a partnership interest? In his opinion, Chief Judge Srinivasan repeatedly emphasized that, as a matter of fact, the taxpayer sold a partnership interest, not the underlying inventory itself. Further, Chief Judge Srinivasan disagreed with the IRS's and Judge Gustafson's position that § 751(a) and the regulations thereunder should be read to treat the taxpayer as if she had sold inventory. Instead, Judge Srinivasan agreed with the taxpayer's argument that § 751(a) is merely a recharacterization provision by taking into account the amount of inventory held by a partnership. Section 751(a) does not convert or treat a partnership interest sale as a disposition of the underlying inventory. Thus, § 751(a) does not modify the then-existing sourcing provisions of §§ 861-865, which *Grecian Magnesite* previously had established did not reach a non-U.S. person's gain from the sale of an interest in a partnership conducting business in the U.S. Chief Judge Srinivasan's opinion concluded: "The short of it is that § 751(a) does not of its own force render Rawat's inventory gain taxable because it does not change the fact that she sold a partnership interest, not inventory." ___ F.4th at ___. Accordingly, the court reversed Judge Gustafson's decision and held for the non-U.S. taxpayer.

- *The final word: 2017 Tax Cuts and Jobs Act.* Regardless of the Tax Court's earlier holding in *Grecian Magnesite* and the D.C. Circuit's holding in *Rawat*, readers may recall that the 2017 Tax Cuts and Jobs Act, § 13501, amended § 864(c) by adding § 864(c)(8) effective for dispositions after November 27, 2017. Section § 864(c)(8) provides that gain or loss (after 11/27/17) on the sale or exchange of all (or any portion of) a partnership interest owned by a nonresident alien individual or a foreign corporation in a partnership engaged in any trade or business within the U.S. is treated as effectively connected with a U.S. trade or business (and therefore taxable by the U.S. unless provided otherwise by treaty) to the extent that the transferor would have had effectively connected gain or loss had the partnership sold all of its assets at fair market value as of the date of the sale or exchange. The amount of gain or loss treated as effectively connected under this rule is reduced by the amount of such gain or loss that is already taxable under § 897 (relating to U.S. real property interests). Put differently, § 864(c)(8) adopts the aggregate theory of partnership taxation with regard to dispositions of partnership interests. Section 864(c)(8) legislatively overrules the Tax

Court's holding in *Grecian Magnesite* and the D.C. Circuit's holding in *Rawat* but only for partnership interest gain realized and recognized after November 27, 2017.

- *Comment*: If *Grecian Magnesite* and *Rawat* are any indication, the courts seem inclined to adopt the entity theory and reject the IRS's aggregate theory of partnership taxation, at least as it relates to a taxpayer's sale or other disposition of a partnership interest. Generally, this is good news for taxpayers because § 741 characterizes a partnership interest as a capital asset, subject to any express exceptions in the Code. Of course, § 751(a) remains an express exception for U.S. taxpayers selling an interest in a partnership holding "hot assets," while relatively new § 864(c)(8) is an express exception for non-U.S. taxpayers selling an interest in a partnership conducting business in the U.S.

E. Inside Basis Adjustments

F. Partnership Audit Rules

G. Miscellaneous

VIII. TAX SHELTERS

IX. EXEMPT ORGANIZATIONS AND CHARITABLE GIVING

A. Exempt Organizations

1. It will cost you $600, but exempt § 501(c)(3) organizations now may obtain a determination letter to switch to another type of § 501(c) organization. Rev. Proc. 2024-5, 2024-5 I.R.B. 1 (1/2/24), *as corrected by* Ann. 2024-7, 2024-7 I.R.B. 673 (2/9/24). As readers know, the IRS publishes guidance each year in January for taxpayers seeking various types of private rulings and determination letters. Typically, we do not discuss such routine, periodic guidance from the IRS. This year, however, the IRS significantly altered its longstanding policy regarding determination letters issued to tax-exempt organizations. Previously, a tax-exempt entity qualifying under § 501(c)(3) ("charitable" organizations) could not obtain a determination letter regarding the termination of its (c)(3) status and transition to another type of § 501(c) organization. For instance, an existing (c)(3) "charitable" organization could not unilaterally apply for IRS approval to operate instead as a § 501(c)(c)(4) "social welfare organization." The primary difference between (c)(3) organizations and other types of § 501(c) tax-exempt entities is the charitable deduction. Under § 170, taxpayers generally may take a charitable deduction (subject, of course, to numerous limitations and qualifications) for contributions to (c)(3) organizations. Taxpayers generally cannot take a § 170 deduction for contributions to other tax-exempts such as (c)(4) "social welfare organizations," (c)(6) "trade associations," or (c)(7) "social clubs." *Note*: A deduction under § 162 (trade or business expense) may be available to taxpayers paying such non-(c)(3) organizations but not a § 170 deduction. Starting in 2024, though, section 3.01(1) of Rev. Proc. 2024-5 provides that the IRS will issue a determination letter to an existing (c)(3) seeking recognition under a different subparagraph of § 501(c) if the organization establishes the following as of the date of its application: (i) it has distributed its assets to another § 501(c)(3) organization or government entity and (ii) it otherwise meets the requirements for the § 501(c) status requested. Rev. Proc. 2024-5 further clarifies that any favorable determination letter so issued is effective only from and after the submission date of the application. Nonetheless, for (c)(3) organizations whose exempt status was revoked automatically under § 6033(j) (failure to file a return), Rev. Proc. 2024-5 allows the organization to apply for retroactive reinstatement under a different paragraph of § 501(c). Organizations use either IRS Form 1024 or Form 1024-A to apply for the change in status and must pay a user fee of $600.

B. Charitable Giving

X. TAX PROCEDURE

A. Interest, Penalties, and Prosecutions

B. Discovery: Summonses and FOIA

C. Litigation Costs

D. Statutory Notice of Deficiency

E. Statute of Limitations

1. Tax Court retains jurisdiction holding that the 90-day period to file a petition for redetermination of a notice of employment tax determination is a nonjurisdictional claim processing rule. [Belagio Fine Jewelry, Inc. v. Commissioner](), 162 T.C. No. 11 (6/25/24). The IRS audited the taxpayer, a corporation, to determine the employment status of individuals performing services for the taxpayer. After determining that the taxpayer had an employee, the IRS issued and mailed a notice of employment tax determination (the Notice) dated August 24, 2021. Pursuant to the 90-day rule provided in § 7436(b)(2), the Notice stated that the last day for the taxpayer to file a petition for redetermination of employment status was November 22, 2021. Taxpayer mailed its petition via FedEx Express Saver on November 18, 2021, which arrived at the Tax Court on November 23, 2021, one day after the 90-day deadline. When the petition arrives after the deadline, however, § 7502(a) provides that a petition is considered to be timely if the taxpayer delivered the petition to the U.S. Postal Service (USPS) before the end of the 90-day period. Under this rule, the petition is considered timely filed if it is timely deposited in the USPS mail before the deadline. Under § 7502(f) this "timely mailed is timely filed" rule continues to apply if certain specifically designated delivery services are used by the taxpayers. The FedEx Express Saver service used by the taxpayer, however, was not, during the year in question, a specifically designated private delivery service. *See* IRS Notice 2016-30, 2016-18 I.R.B. 676. The IRS argued that, because the petition was received a day late, the Tax Court lacked jurisdiction to hear the case. In order to determine whether the petition was a day late, the court first needed to determine the date that the IRS had mailed the notice of employment tax determination to the taxpayer to begin the 90-day period.

Burden of Proof. An IRS agent issuing a notice is required to complete USPS Form 3877, Firm Mailing Book for Accountable Mail, to establish the date of mailing of the notice. See I.R.M. 4.8.10.8.2 (Apr. 20, 2018). Having never previously addressed the issue of which party (the IRS or the taxpayer) has the burden of proving when a notice of employment tax determination was mailed, the Tax Court (Judge Greaves) relied on its prior decisions relating to the mailing of notices of deficiency. In relation to notices of deficiency, the Commissioner has the burden of proving the date of mailing because (1) it was the Commissioner's motion, and (2) the relevant information is within the Commissioner's knowledge. *Casqueira v. Comm'r*, T.C. Memo. T.C. Memo 1981-428. *See also S. Cal. Loan Assoc. v. Comm'r*, 4 B.T.A. 223, 224-25 (1926). Placing the burden on the IRS, the Tax Court concluded that the Form 3877 in this case was incomplete because it did not bear a USPS date stamp. However, even though the Form 3877 did not bear a proper USPS stamp, the court concluded that the form was valid because the IRS agent filled out and initialed the form on August 24, 2021. The IRS also provided evidence that the mailing number listed on the USPS Form 3877 matched the stamp on the Notice. Further, the IRS submitted a sworn declaration by the IRS employee that she completed the forms on the same day. This evidence supported the Court's finding that the IRS carried its burden of proof that the Notice was mailed on August 24, 2021. The issue then became whether the Tax Court had jurisdiction to determine whether the taxpayer's petition had been filed within the 90-day period of § 7436(a).

Clear Statement Standard. The Tax Court began with the Supreme Court's rule that, where a federal court's subject matter jurisdiction depends on a filing deadline, failure by a litigant to comply with the deadline deprives the court of jurisdiction to hear the case. *Kontrick v. Ryan*, 540 U.S. 443, 455 (2004). However, where a party is required under a rule to complete specific procedural steps at certain specified times but the rule does not condition a court's authority to hear the case on compliance with such steps, the rule is treated as a nonjurisdictional "claims processing" rule. *See Boechler, P.C. v. Comm'r*, 142S.Ct. 1493, 1497 (2022). Such claims processing rules do not deprive a court of its jurisdiction to hear a case. *U.S. v. Wong*, 575 U.S. 402, 410 (2015). A procedural requirement is treated as jurisdictional if Congress "clearly states" that a deadline is jurisdictional. In order to determine whether Congress has clearly stated that a requirement is jurisdictional, the Court must examine the (1) text, (2) context, and (3) historical treatment of the requirement. *See Reed Elsevier, Inc. v. Muchnick*, 559 U.S. 154, 166 (2010). The Tax Court first addressed the "text" of § 7436(b)(2) finding that, while the statute provides the 90-day deadline, it does not use the word "jurisdiction". Rather, the statute provides only that a proceeding may not be initiated in the Tax Court if the 90-day rule is not complied with. Thus, nothing in the statute textually restricts the Court's ability to hear the case. Second, the court reasoned that the statutory "context" of the statute supports the conclusion that Congress did not "clearly state" that the 90-day deadline in the statute. The court noted that mere proximity of the jurisdictional grant and the procedural requirement does not indicate that the requirement is jurisdictional. Here, the jurisdictional grant is found in § 7436(a) whereas the 90-day deadline is found in subsection (b)(2). Such a separation without a clear tie of the jurisdictional grant to the 90-day rule supported the court's conclusion that the 90-day deadline is not jurisdictional. In addition to the separation of the jurisdictional grant from the deadline, the court concluded that § 7436(b)(2) has limited applicability because the 90 day deadline applies only to a subset of cases covered by § 7436. Further, the 90-day deadline applies only to cases in which the Commissioner sends a notice of employment tax determination to the taxpayer by certified mail. In cases in which the Commissioner fails to properly send its determination via the mail, the 90-day rule is inapplicable. The Court reasoned that its jurisdiction is based on the IRS determination and not on whether the notice of determination was actually mailed, or not. Third, from a historical context, the Court reasoned that § 7436, as well as similarly worded statutes, lack any historical precedent interpreting deadlines as jurisdictional. As such, the court held, the relevant historical treatment of § 7436 does not reflect an intent on the part of Congress that the 90-day rule be jurisdictional.

Conclusion. After considering the text, statutory context, and history of the statute, the court reasoned that it was not deprived of jurisdiction because of the taxpayer's late filing. The court therefore denied the IRS's motion to dismiss based on a lack of jurisdiction.

F. Liens and Collections

G. Innocent Spouse

H. Miscellaneous

XI. WITHHOLDING AND EXCISE TAXES

XII. TAX LEGISLATION

XIII. TRUSTS, ESTATES & GIFTS