# Recent Developments in Federal Income Taxation

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## Age at Which RMDs Must Begin
## *Outline: item B.1, page 2*

- SECURE 2.0 Act of 2022:
  - Increases the age at which RMDs must begin. In 2022, individuals who attained age 72 were required to begin taking RMDs. SECURE 2.0 increases the RMD age to age 73 in 2023 and to age 75 in 2033.
- Notice 2023-54 (7/14/23):
  - Automated payment systems must be updated to reflect the change in the age at which RMDs must begin and this may take time.
  - Therefore, those born in 1951 (who attain age 72 in 2023) might receive distributions in 2023 that are mischaracterized as RMDs (and therefore normally ineligible for rollover).
  - Individuals who receive such distributions from January 1 through July 31, 2023, had until September 30, 2023, to roll such mischaracterized distributions into an eligible retirement plan.
    - Applies to both employer-sponsored plans and IRAs.
    - The "one rollover every 12 months" rule for IRAs is not a bar.

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## Age at Which RMDs Must Begin
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  - Increases the age at which RMDs must begin. In 2022, individuals who attained age 72 were required to begin taking RMDs. SECURE 2.0 increases the RMD age to age 73 in 2023 and to age 75 in 2033.
- Proposed Regulations (7/19/24):
  - Issue: at what age must those born in 1959 begin taking RMDs?
  - Because of an error in the statutory language Congress enacted in SECURE 2.0, the statute appears to provide that those born in 1959 must begin taking RMDs both at age 73 and at age 75.
  - The final regulations clarify that those born in 1959 must begin taking RMDs at age 73. Prop. Reg. § 1.401(a)(9)-2(b)(2)(v).

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## Age at Which RMDs Must Begin
### *Outline: item B.1, page 2*

- 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 | 70-1/2 |
| July 1, 1949, through Dec. 31, 1950 | 72 |
| 1951-1959 | 73 |
| 1960 and later | 75 |

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## Final Regulations on RMDS (7/19/24) No More Stretch RMDs from Non-Spousal Inherited Retirement Accounts
### *Outline: item B.2, page 3*

- A provision of the SECURE Act, Division O, Title IV, § 401 of the 2020 Further Consolidated Appropriations Act, amended Code § 401(a)(9)(E)
- Modifies the required minimum distribution (RMD) rules for inherited retirement accounts (defined contribution plans and IRAs).
- Requires all funds to be distributed by the end of the 10th calendar year following the year of death.
  - Amended statute does not appear to require the beneficiary to withdraw any minimum amount before that date.
- Current rules, which permit taking RMDs over many years, continue to apply to certain designated beneficiaries, including surviving spouses, children of the participant who have not reached the age of majority, and those not more than 10 years younger than the deceased individual.
- Applies to distributions with respect to those who die after 12/31/19.

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## Final Regulations on RMDs (7/19/24)
## 89 F.R. 58,886
## *Outline: item B.2, page 3*

- These final regulations update existing regulations to address the changes made by the SECURE Act as well as several other statutory changes.
- The final regulations (like the proposed) 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 by most advisors.
- They require RMDs to begin in the year after death when:
  - The account owner died after the required beginning date for RMDs,
  - The designated beneficiary is not an eligible designated beneficiary
- In this situation, the beneficiary must take RMDs over the beneficiary's life expectancy for years 1 through 9 after death and must take any remaining funds in year 10.

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## Final Regulations on RMDs (7/19/24)
## 89 F.R. 58,886
## *Outline: item B.2, page 3*

- Example:
  - Owner passed away in 2020
  - At the time of his death, Owner was the owner of a traditional IRA
  - Owner's death occurred <u>after</u> the required beginning date for distributions from the IRA.
  - Beneficiary is the sole beneficiary of the IRA and is <u>not</u> an eligible designated beneficiary (therefore is subject to the 10-year rule)
  - Under the final regulations, Beneficiary must take RMDs for 2021 through 2029, and any remaining funds in the account must be distributed by the end of 2030.

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## Final Regulations on RMDs (7/19/24)
## 89 F.R. 58,886
## *Outline: item B.2, page 3*

- Missed RMDS:
  - Those who inherited retirement accounts subject to the 10-year rule from a decedent who died in 2020 or later might have missed RMDs they were supposed to take for years 1 through 9 after death.
  - In a series of notices, the IRS provided relief.
    - Notice 2024-35, 2024-19 I.R.B. 1051 (4/16/24).
    - Notice 2023-54, 2023-31 I.R.B. 382 (7/14/23).
    - Notice 2022-53, 2022-45 I.R.B. 437 (10/7/22).
  - Relief:
    - The 50% (or 25%) excise tax of § 4974 for failure to take RMDs will not apply.
    - Applies to those required to take RMDs in 2021, 2022, 2023 or 2024 under the interpretation of the 10-year rule in the proposed (and now final) regulations.

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## Final Regulations on RMDs (7/19/24)
## 89 F.R. 58,886
## *Outline: item B.2, page 3*


- Missed RMDS:
  - Issue: if the IRS effectively waived penalties on missed RMDs for 2021 through 2024 for beneficiaries subject to the 10-year rule, how much must the beneficiary withdraw in 2025?
- Example:
  - Owner passed away in 2020
  - At the time of his death, Owner was the owner of a traditional IRA
  - Owner's death occurred after the required beginning date for distributions from the IRA.
  - Beneficiary is the sole beneficiary of the IRA and is not an eligible designated beneficiary (therefore is subject to the 10-year rule)
  - Under the final regulations Beneficiary must take RMDs for 2021-2029.
  - What if Beneficiary fails to take RMDs for 2021-2024?
  - In 2025, must Beneficiary take the missed RMDs for 2021-2024?

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## Final Regulations on RMDs (7/19/24)
## 89 F.R. 58,886
## *Outline: item B.2, page 3*

- Missed RMDS (cont'd):
  - Final regulations clarify that beneficiaries subject to the 10-year rule need not make up missed RMDs in 2025.
  - Thus, a beneficiary subject to the 10-year rule required to take RMDs for 2021-2024 need not worry about making those up in 2025.
    - This beneficiary would take RMDs for 2025-2029 and withdraw any remaining funds 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.

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## Surviving Spouses Can Defer RMDs
## *Outline: item B.3, page 5*

- SECURE 2.0 Act § 327:
  - Deferral of RMDs for surviving spouses. If a participant dies before reaching the age at which RMDs must begin and has designated a spouse as the sole beneficiary, then the spouse may make an irrevocable election to be treated as the participant for purposes of receiving RMDs.
  - This will allow the surviving spouse to defer RMDs until the deceased spouse would have reached the RMD age.
  - This change is effective in 2024.
  - Example: H is age 62 and W is age 68. H passes away and W is sole beneficiary of his retirement account. W can elect to be treated as H to determine when RMDs must begin. W need not take RMDs until H would have turned 73.

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## Surviving Spouses Can Defer RMDs
## *Outline: item B.3.a, page 7*

- Proposed regulations (7/19/24):
  - Surviving spouse is automatically treated as having made the election If the account owner dies *before* the owner's required beginning date for RMDs. Prop. Reg. § 1.401(a)(9)–5(g)(3)(ii)(A).
    - Surviving spouse is *not* automatically treated as having made the election if the account owner dies *on or after* the owner's required beginning date for RMDs (but plan terms can make this the default election). Prop. Reg. § 1.401(a)(9)–5(g)(3)(ii)(B).
  - Surviving spouse's RMDs are calculated using the Uniform Life Table for the *surviving spouse's* age (reduces deferral benefit of the election). Prop. Reg. § 1.401(a)(9)–5(g)(3)(ii)(C).
  - If election is in effect and the surviving spouse has begun receiving RMDs, surviving spouse's beneficiary must continue taking RMDs over surviving spouse's remaining life expectancy and withdraw any remaining funds by the end of the 10th calendar year following year of surviving spouse's death. Prop. Reg. § 1.401(a)(9)–5(g)(3)(ii)(D) 13

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## Surviving Spouses Can Defer RMDs
## *Outline: item B.3.a, page 7*

- Proposed regulations (7/19/24):
  - <u>Effective date</u>. 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. Prop. Reg. § 1.401(a)(9)–5(g)(3)(ii)(E).
  - <u>Example 1</u>: account owner died in 2017 and before the owner's required beginning date for RMDs. Assume owner would have reached the age at which RMDs must begin in 2024 or later.
    - The first year for which an annual RMD is due would be 2024 or later, and the spousal election could apply.
  - <u>Example 2</u>: account owner died in 2023 after the owner's required beginning date for RMDs. The first year for which an annual RMD is due to the surviving spouse would be 2024, and the spousal election could apply.

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## Notice 2024-22
## 2024-6 I.R.B. 662 (1/12/24)
## ***Outline: item B.4, page 6***

- A provision of the SECURE 2.0 Act, Division T, Title IV, § 127 of the Consolidated Appropriations Act, 2023, amended Code § 402A.
- Amended § 402A authorizes Pension-Linked Emergency Savings Accounts (PLESAs).
- A PLESA is an optional short-term savings account established and maintained within a defined contribution plan.
- Eligible employees can make after-tax contributions to a PLESA subject to a maximum account balance of $2,500.
- Withdrawals from a PLESA are tax-free regardless of the reason for the withdrawal, i.e., no real “emergency” is required.
- Employers cannot contribute to a PLESA but must take employee contributions to the PLESA into account when determining employer matching contributions to the plan.

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## Notice 2024-22
## 2024-6 I.R.B. 662 (1/12/24)
## ***Outline: item B.4, page 6***

- 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).
- 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 (e.g., a plan provision requiring employees to forfeit matching contributions due to employee’s PLESA withdrawal).
- Clarifies that Rev. Rul. 74-55, 1974-1 C.B. 89, and Rev. Rul. 74-56, 1974-1 C.B. 89 do not apply.

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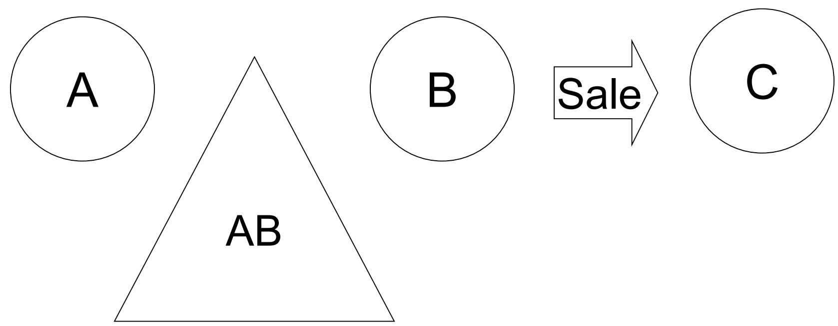
# Sale of a Partnership Interest




Assets of Partnership
- Inventory
- Land

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# Sale of a Partnership Interest

- Section 741: "In the case of a sale or exchange of an interest in a partnership, gain or loss shall be recognized to the transferor partner. Such gain or loss shall be considered as gain or loss from the sale or exchange of a capital asset, except as otherwise provided in section 751 (relating to unrealized receivables and inventory items)."
- Section 751(a): "The amount of any money, or the fair market value of any property, received by a transferor partner in exchange for all or a part of his interest in the partnership attributable to—
  1. unrealized receivables of the partnership, or
  2. inventory items of the partnership,

  shall be considered as an amount realized from the sale or exchange of property other than a capital asset."

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## Grecian Magnesite Mining Co., S.A. v. Comm'r, 149 T.C. No. 3 (7/13/17)
## *[Not in outline]*

- The taxpayer, a corporation organized under the laws of Greece, held an interest in a U.S. LLC taxed as a partnership.
- The partnership redeemed the taxpayer's partnership interest and the taxpayer realized $4 million of gain <u>not</u> associated with U.S. real property.
- <u>Issue</u>: was the taxpayer's gain effectively connected with the conduct of a U.S. trade or business and therefore subject to U.S. tax?
- <u>Held</u>: No. The court:
  1. Held that the taxpayer was treated as selling its partnership interest, rather than an interest in each partnership asset.
  2. Held that the gain was not effectively connected income.
  3. Rejected the contrary conclusion in Rev. Rul. 91-32.

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## Grecian Magnesite Mining Co., S.A. v. Comm'r, 149 T.C. No. 3 (7/13/17)
## *[Not in outline]*

- Section 864(c)(8), added by the 2017 Tax Cuts and Jobs Act, provides that, effective for dispositions after November 27, 2017:
  - gain or loss 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).
- These changes to § 864(c) statutorily reverse the Tax Court's decision in *Grecian Magnesite Mining, Industrial & Shipping Co., S.A. v. Commissioner*, 149 T.C. No. 3 (7/13/17).

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## Rawat v. Commissioner, ___ F.4th ___ (D.C. Cir. 7/23/24)

***Outline: item D.1.a, page 9***

- The taxpayer, a Canadian citizen and nonresident of the U.S., held an interest in a U.S. LLC taxed as a partnership.
- Taxpayer sold her interest in the partnership in 2008 and realized a gain of $22.4 million, of which $6.5 million was attributable to inventory of the partnership held in the U.S.
- Issue: was the taxpayer's gain effectively connected with the conduct of a U.S. trade or business and therefore subject to U.S. tax?
- Held: No. Tax Court's decision reversed.
  - Section 751(a) is a characterization provision. It does not treat the taxpayer as if she sold inventory.
  - Because the taxpayer sold a partnership interest, not inventory, the sourcing rules for sales of inventory do not apply.
  - Therefore, the taxpayer's gain is foreign-source income and therefore not subject to U.S. tax.

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## Rev. Proc. 2024-5 2024-5 I.R.B. 1 (1/2/24)

***Outline: item A.1, page 10***

- 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 for contributions.
- 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:
  1. It has distributed its assets to another § 501(c)(3) organization or government entity, and
  2. It otherwise meets the requirements for the § 501(c) status requested. 22

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## Rev. Proc. 2024-5
## 2024-5 I.R.B. 1 (1/2/24)
## *Outline: item A.1, page 10*

- To apply for a change in status, the tax-exempt organization must submit either Form 1024 or Form 1024-A.
- Requires a $600 user fee.
- One possible use: a § 501(c)(3) organization whose exempt status was revoked for failure to file a return (Form 990) can apply for retroactive reinstatement of exempt status under another paragraph of § 501(c).

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## Belagio Fine Jewelry, Inc. v. Commissioner,
## 162 T.C. No. 11 (6/25/24)
## *Outline: item E.1, page 11*

- Following an audit, the IRS determined that the taxpayer had an employee and mailed a notice of employment tax determination.
- Under § 7436(b)(2), the taxpayer had 90 days to challenge the determination by filing a petition in the U.S. Tax Court.
- The taxpayer filed its petition one day late
- Issue: is the 90-day period of § 7436(b)(2) jurisdictional?
- Held: No. The text, context, and history of the statute indicate that the 90-day period is a nonjurisdictional claim-processing rule.
  - Court denied IRS's motion to dismiss for lack of jurisdiction.

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