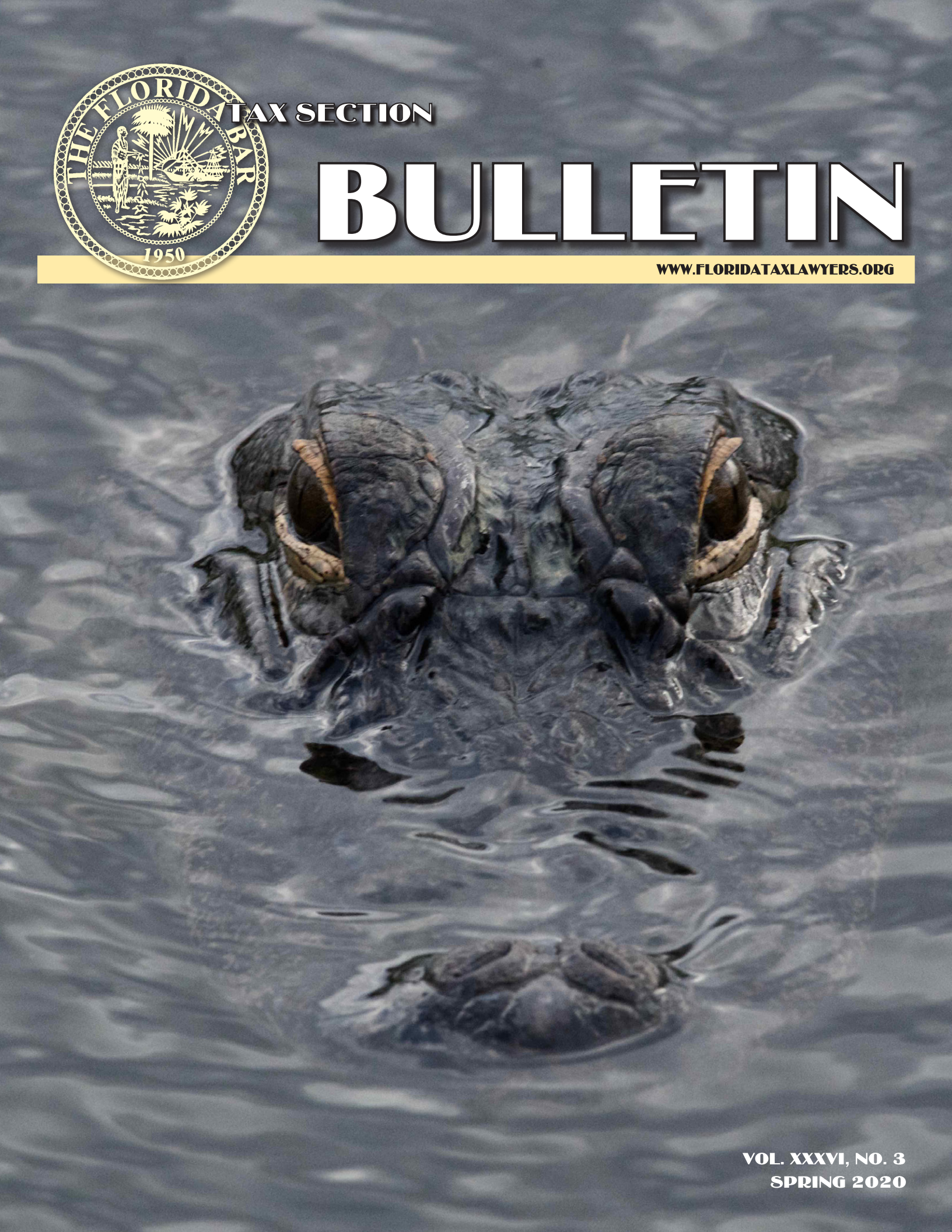
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Tax Section Bulletin

THE FLORIDA BAR

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Cover Photo: Myakka River State Park (Mark Cohen). Mark is a Strategic Consultant with Capstan Financial Consulting Group in Sarasota, Florida. Prior to relocating to Florida in 1999, Mark was a practicing attorney in New Hampshire, concentrating his practice in trusts and estates. He obtained his Juris Doctor from Boston University and he and his wife Ellen have two children. Mark loves being outdoors and creating lasting memories of his travels through his passion for photography. Mark has had one-person exhibitions at The Bishop Museum of Science and Nature, Florida Maritime Museum, Conservation Foundation of the Gulf Coast, and the Arts and Cultural Alliance of Sarasota County. His photographic images have been published in books, as well as local and national magazines, and are owned by museums, corporations, and private collectors.

Message to Our Members

The Florida Bar Tax Section greatly values its members. We are here to support you and to be a resource, particularly during this most difficult time. Florida Bar annual fee renewal will begin this month and you'll have the option to renew your Tax Section membership. If you have been financially impacted by COVID-19 and believe that you will be unable to pay your section dues, please notify Program Administrator Leslie Reithmiller at lreithmiller@floridabar.org regarding the circumstances. The section's Directors' Committee and Executive Council are discussing options to provide accommodation to members in need of assistance with section annual dues and will finalize the decision at the Directors' meeting in May. Please keep in mind that the section values your involvement and we pledge to continue to offer as many benefits as possible, including discounted registration on audio webcasts, excellent publications, the opportunity to be published, exclusive access to the section's online member directory, our monthly free telephonic CLE series, and more. We hope that each of you and your families remain well.

Chair's Message

By Janette M. McCurley
Chair, Florida Bar Tax Section 2019-2020



Dear Tax Section Members:

I am pleased to present our Spring 2020 Tax Section Bulletin. I hope you enjoyed the last Bulletin in the Fall 2019. Our new editor, Lisa Gallagher, is working hard to put together informative, educational, and interesting sets of articles. If you want to see your article in the next Tax Bulletin please contact Lisa and she can guide you on the submission process.

I am more than half-way through my year as your Chair. Time has truly flown by. My service continues to be rewarding as well as a challenge and I thank you all for entrusting our Tax Section to me for this year.

Three weeks ago we held our Directors' meeting at the Waldorf Astoria in Orlando. This meeting included a separate Long Range Planning mini-retreat follow-up. The follow-up was to a January 2018 extensive 2-day Long Range Planning Retreat in Savannah, Georgia. During these retreats, we attempt to identify various topic areas and really do a deep dive into each of them in an effort to improve our Tax Section and better serve our members. Last year, when Michael Minton at his Director's meeting held a mini-retreat to follow-up on the Long Range Planning agenda items, it was such a huge success I decided to follow his lead and scheduled the same at my Directors' meeting. Mark Brown and Shawn Wolf, as chairs of the Long Range Planning Committee, were charged with organizing the mini-retreat. They provided an overview of significant items we have accomplished since that first Long Range Planning meeting and they identified a few areas where we still can improve. As a result of the discussions during this latest mini-retreat, the Directors voted to increase the number of Fellows to 4 and to stagger their terms so there are 2 new openings every year. In addition, the Directors also voted to co-sponsor a CLE event with the Stetson Law School Tax Society. Please be sure to check out the article included in this Bulletin on this unique and exciting student-led Tax Law Society

The Tax Section has been very busy over the last several months. In January, the International Tax Conference and Boot Camp was held. Thank you to Steve Hadjilogiou and his committee for once again putting on a great CLE. Jennifer Wioncek and Alfredo Tamayo, co-Directors of the International Tax Division, gave a brief presentation during one of the receptions to introduce attendees to the new International Tax Division of the Tax Section and what is has to offer.

The Moot Court competition was held March 5-7 at the University of Florida. A HUGE thank you to Daniel Hudson and Keith Hagan for drafting the problem and the bench brief. This is a big task that takes a lot of time and thought. The Tax Section could not continue to have the Moot Court without the continued work of Justin Wallace and Brian Howsare. This year we had 14 teams competing from all over the country. Saturday's final round was judged by three United States Tax Court judges; the early rounds are judged by local practitioners. If you have never volunteered to participate in this incredible event and would like to experience something really inspiring, please consider signing up for next year's event. It is a rewarding experience and CLE hours are earned as well.

My original Chair's Message included details regarding my final meeting as Chair, our Annual Meeting. That meeting was to be held in the Bahamas at the Atlantis Resort. There was going to be a CLE on Friday, May 8th chaired by Shawn Wolf entitled the Amazing, Technical, Learning, Analytical, Nuanced & Training International Seminar (A.T.L.A.N.T.I.S.). Saturday evening there was to be a cocktail reception and dinner honoring Cristin Keane as the Gerald T. Hart Outstanding Tax Attorney of the Year. Unfortunately, due to the coronavirus I had to cancel this meeting. Fortunately, the Atlantis Resort was very accommodating and allowed the Section to cancel the meeting with no cancellation fees and offered to return our deposits. So, although the Section missed out on a fantastic meeting we were not hurt financially. I am, of course, disappointed that I will not get the opportunity to hold my final meeting, and more importantly, publicly thank all of the Section members that have helped make my year so incredibly special. We will reschedule the Tax Attorney of the Year reception and dinner so we will all get the chance to recognize Cristin.

I want to thank our sponsors who are always providing assistance that allows us to continue our work, which is so directly impactful on so many individuals and businesses. This year's sponsors include Platinum sponsor MPI and Silver sponsors, Business Valuation Analysts LLC, Coral Gables Trust, Jones Lowry, Kaufman Rossin, MRW Consulting Group, Alliance Bernstein and

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Vision Point Capital. We feature our sponsors in our monthly e-newsletters as well to give our members the opportunity to get to know them better and find out how they can help you and your clients.

And, let me offer this final thought. All of the Tax Section meetings, including the retreats, are not just technically productive in terms of solidifying plans and establishing goals for the future, but each time we get together, the meetings continue to build upon our expansive and welcoming camaraderie. During our last meeting it was suggested that the real value of getting involved in the Tax Section is beyond quantification. The reason being – what value can be placed on being able to just pick up the phone, or email, or text, to ask a question of some of the leading and brightest minds in Florida practicing across all areas of tax law. I whole-heartedly agree with the sentiment that this is beyond measure and I have first-hand experienced the generosity of time, experience, and wisdom shared with me by my fellow Tax Section members. Thank you to all of you who have been my teachers, my mentors, and have become true friends. I encourage all Tax Section members, particularly new attorneys, who have not attended a Tax Section meeting recently, or ever, to join us and discover for yourself the opportunities that are available to you to become involved and build your own lifetime friendships.

Janette M. McCurley

Chair, Florida Bar Tax Section, 2019-2020



Chair-Elect's Message

By D. Michael O'Leary, Chair-Elect
Florida Bar Tax Section 2020-2021



The 2019-2020 fiscal year is moving rapidly along, and plans for the 2020-21 fiscal year are taking shape. I am grateful for the assistance of our Florida Bar Program Administrator, Leslie Reithmiller, who does an awesome job helping the Tax Section.

The Tax Section will continue to provide numerous opportunities to tax lawyers, including, speaking opportunities (in person and phone CLE programs), writing opportunities (including comments to proposed regulations and writing articles for the Tax Section Bulletin and the Florida Bar Journal), programs that help practitioners keep up with new tax developments, networking, fellowship and more.

Our current Chair, Janette McCurley, spent untold hours organizing the 2019-20 meetings, including what would have been an awesome Annual Meeting at the Atlantis Resort, but like many events it had to be cancelled due to the coronavirus.

Janette has done an amazing job as the Chair. With Janette's experience helping several other Chairs as their "Chief of Staff," I don't believe that there has ever been a person as prepared to be Chair as Janette and it has showed in so many ways, including her leadership of and planning for the Tax Section. It is sad that her year will not end as she had intended but it takes nothing away

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from her year as Chair. She will be a hard act to follow!

For the 2020-21 year, we are still planning to start with the Organizational Meeting at the Omni Amelia Island Plantation from July 2-5, 2020. The Ullman Tax Year in review is scheduled for July 3 in the afternoon and will be followed by a family dinner at which there will be a "jeopardy" style trivia contest which should be great fun. The Tax Section Division meetings will take place on the morning of July 4, and the Tax Section Executive Council meeting will be held in the early afternoon of July 4. Finally, the usual spectacular fireworks will be held on the beach in the evening of July 4.

The Fall meeting is scheduled to be held in Tampa at the Westin Tampa Waterside from Thursday, September 24 to Saturday, September 26, 2020. There will be a CLE program on September 25, which is being organized by Cristin Keane and Mark Brown. The CLE program will be focused on practical estate planning techniques that you can utilize to help your estate planning clients.

Our Annual Meeting is scheduled to be held at the Conrad in downtown Miami from Thursday, April 29- Sunday, May 2, 2021. The inaugural Domestic Tax Conference ("DTC") is scheduled to be held on Friday, April 30 and we will honor the Gerald T. Hart Outstanding Tax Attorney of the Year on the evening of Saturday, May 1. It has been a while since the last meeting in Miami so we are glad to be able to get back to Miami for a meeting. We are optimistic that this meeting and the DTC will be well attended by the many Tax Section members residing in and around Miami.

Finally, we hope to send a delegation to Washington DC to meet with agency heads at the Department of Treasury and other individuals responsible for passing and implementing U.S. tax laws. We plan to send a delegation to Washington DC on a regular basis even though we may not do so every year.

As you can see, we plan to continue the substantive and important work of the Tax Section while having some fun! If you have any ideas that would benefit our members or would like to become more involved the Tax Section, please let me know. I look forward to seeing you at a meeting or otherwise speaking with you.

Stetson Tax Law Society

Hard-working students at Stetson University College of Law are building bridges with top tax practitioners throughout the nation.

Driven students have come together to form an ambitious and active Tax Law Society with over 135 student members. "The Society" (as it has come to be known) is committed to forging a strong partnership between Florida's top tax professionals and Stetson Law. The mission is to cultivate a community of students, professors, and practitioners that work together to innovate the practice of tax law. The Society's efforts have produced results:

S.T.I.X. STETSON TAX INNOVATORS EXCHANGE

The Stetson Tax Innovators Exchange (S.T.I.X.) is the nation's newest and most forward-thinking tax law collaboration event. With help from The Tax Section of the Florida Bar, and numerous members of the Florida tax law community, The Society has put together a ground-breaking event series. The S.T.I.X. event series brings in the nation's top tax minds for a collaborative dive into bleeding-edge approaches to tax law. The first event in the series is taking place on March 31, 2020 at the Stetson Law Gulfport campus at 2:20 p.m. Presenters include IRS Deputy Commissioner of Enforcement and Services, Sunita Lough, and Marc A. Simonetti – Partner, Pillsbury Winthrop Shaw Pittman LLP (New York).



(IRS Deputy Commissioner of Enforcement and Services, Sunita Lough)

S.T.I.X. is not to be mistaken for an "ivory tower" academic lecture. Instead, every speaker slated to present at S.T.I.X. is excited to lead an audience-engaged group discussion on a novel or new approach to tax practice. The audience is encouraged to ask questions and contribute personal experience as the room rolls up their collective sleeves to dive deep into useful new techniques that practitioners can take away and use to advance their practice. Upcoming topics in the series include: Improving the Taxpayer Experience, Opportunity Zone Practice, Advanced TCJA, Transfer Pricing, Sales Tax, IRC 199A, Environmental Tax, and Tax Controversy/ Litigation. This series is must-attend for any practitioner wanting to innovate their practice.

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The Stetson Practical Tax Workshop Series provides Florida tax practitioners with an opportunity to present practical concepts of their choosing, while helping Stetson Law students learn what a career in tax law looks like. Generally, these are 1-hour presentations on Stetson's Gulfport or Tampa campuses, and are attended by dozens of students that are thirsty for exposure to practical tax knowledge. Practitioners share their stories, experiences, and advice with the next generation of Florida tax attorneys. Students gain meaningful insight and get a taste of the life of a tax attorney in Florida. Everyone walks away better for having met.

The Stetson Tax Internship & Externship Programs provide Florida tax law and accounting firms—and corporate tax departments—an opportunity to access Stetson Law's talented and motivated student base, which includes over 100 students who are passionate about tax law. The Tax Internship program allows employers to connect with, interview, and employ Stetson Law students any time throughout the year. The Tax Externship program provides students the opportunity to gain practical educational experience in the area of tax law and is available in either the fall or spring semester.



Professor Andrew Appleby



John Bartel
Tax Law Society President

Led by Professor Andrew Appleby (a former tax law firm partner) and Tax Law Society President John Bartel, The Stetson Tax Law Society is committed to becoming an active and meaningful contributor to the Florida tax community. With NYU, Georgetown, the University of Florida, the University of Miami, and Boston University all making presentations to Stetson students on campus, The Society has helped to bring the exceptional students of Stetson to the attention of these legendary programs.

The Stetson Tax Law Society is helping to build bridges between some of the greatest tax minds, tax firms, and tax programs in the country. To get involved, you can email Tax Law Society President John Bartel at jbartel@law.stetson.edu or Professor Appleby at aappleby@law.stetson.edu.



Summary and Selected Issues in Internal Revenue Code §199A

By: Keith C. Durkin

I. Overview and Summary

The 2017 Tax Cuts and Job Act (2017 Tax Act) created new Internal Revenue Code §199A. Section 199A applies to entities taxed as pass-through entities, such as S corporations, partnerships, sole proprietorships, LLCs taxed as S corporations or partnerships, or those reported as a disregarded entity on taxpayer's Schedule C. The 2017 Tax Act reduced the tax rates on C corporations to 21%, giving them an effective tax rate of 39.8% when factoring in an 18.8% tax on dividends. 199A was created to give owners of pass-through entities a tax break commensurate with the C corporation rate decrease. The general idea with 199A was to provide a 20% deduction so that if an entity qualifies for the deduction, it is only taxed at 80% of its "Qualified Business Income." The deduction is a below-the-line deduction. This means it's less valuable on the return than an above-the-line deduction, which directly offsets income. Typical above-the-line deductions include contributions to retirement plans, self-employment taxes owed, health insurance premiums and domestic production activities.

Qualified Business Income (QBI) is the net amount of qualified items of income, gain, deduction and loss with respect to a trade or business. A qualified item is any income effectively connected with the conduct of a business within the U.S. or Puerto Rico. Dividends, capital gains and capital losses are excluded from QBI. Interest income qualifies if it is related to a qualified trade or business. Compensation paid to a shareholder or a guaranteed payment to a partner for services is excluded from QBI.

Congress and the media consistently referred to 199A as the 20% deduction. The deduction, however, will rarely equal 20% of a pass-through entity's income. Instead, the deduction will equal one of the four following possible amounts: (a) 20% of the taxpayer's adjusted taxable income less capital gain, (b) 20% of QBI, (c) 50% of the W-2 wages paid from the business (Wage Limitation) or (d) 25% of the W-2 wages paid from the business plus 2.5% of the unadjusted basis of qualifying depreciable property (Capital Limitation). The amount of the deduction is determined by the taxpayer's income.

For individual taxpayers with income below $157,500 and married taxpayers with income below $315,000, the deduction will be the lesser of (a) and (b) above. For individual taxpayers with income above $207,500 and married taxpayers with income above $415,000, the deduction will be the greater of (c) and (d) above, which is then compared with 20% of QBI. You take the greater of (c) and (d), then compare it to (b) and take the lesser of this comparison. For individuals with income between $157,500 and $207,500 and married taxpayers with income between $315,000 and $415,000, the deduction amount is subject to a phase-in calculation. The following is a simplified 199A chart.

Taxpayer's Income:	199A Deduction:
Individual less than $157,500	Lesser of 20% QBI or 20% of taxable income less capital gain
Married couple less than $315,000	Lesser of 20% QBI or 20% of taxable income less capital gain
Individual between $157,500 and $207,500	Subject to phase-in calculation
Married couples between $315,000 and $415,000	Subject to phase-in calculation
Individual more than $207,500	(a) Determine greater of 50% W-2 Wage Limitation or 25% of W-2 wages plus 2.5% of depreciable property. (b) Compare (a) to 20% of QBI/taxable income and take lesser value.
Married couple more than $415,000	(a) Determine greater of 50% W-2 Wage Limitation or 25% of W-2 wages plus 2.5% of depreciable property. (b) Compare (a) to 20% of QBI/taxable income and take lesser value.

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Example 1: A is unmarried and operates a computer repair shop as sole proprietorship. The shop generates $100,000 of QBI. A had no capital gains or losses. After deductions unrelated to the business, A has taxable income of $81,000. What is A's deduction? A is below the income threshold so it's the lesser of QBI or taxable income limitation. In this example, A's QBI deduction is $20,000 ($100,000 x .2 = $20,000), and A's taxable income limitation is $16,200 ($81,000 x .2). In this example, A's 20% deduction is limited to $16,200.

Example 2: Same facts as 1, except A has $7,000 in net capital gain. In this example, A's deduction is $14,800. The net capital gains must be subtracted from the taxable income limitation. Accordingly, A's QBI deduction remains $20,000, but A's taxable income limitation becomes $14,800 (($81,000 - $7,000) x .2 = $14,800).

Example 3: A and B are married. B earns $50,000 in wages from a separate employer. A owns 100% of an S corporation that qualifies pursuant to 199A. The entity pays A $150,000 in wages and earns $100,000 in net income from operations. The taxpayers have no capital gain. After deductions, their combined income is $270,000. What is the deduction? The taxpayer's combined income is below $315,000, so it's the lesser of 20% of the QBI or 20% of the income. Here the deduction is $20,000 because 20% of the taxpayer's income is less than 20% of the QBI - ($100,000 x .2 = $20,000); ($270,000 x .2 = $54,000).

Example 4: A, B and C are partners in a law firm that earns $375,000 in annual income. Each partner receives compensation of $125,000 as a guaranteed payment. What is their 199A deduction? Zero, because guaranteed payments are excluded from the 20% deduction.

Example 5: A is unmarried and owns a disregarded entity. The disregarded entity generates $1,000,000 of QBI. A pays no W-2 wages and owns no depreciable property. After deductions, A's taxable income is $980,000. What is A's deduction? Zero, because A is over the threshold and paid no W-2 wages and had no depreciable property.

20% of QBI:	20% of Taxable Income:	W-2 Limitation:	Capital Limitation:
$200,000	$196,000	$0	$0

Example 6: Same facts as above, but D holds depreciable qualifying property of $10,000,000, reports $4,000,000 of QBI, has table income of $3,980,000 and pays no W-2 wages. What is D's deduction? D's deduction is $250,000.

20% of QBI:	20% of Taxable Income:	W-2 Limitation:	Capital Limitation:
$800,000 (.2 x $4,000,000)	$196,000 (.2 x $3,980,000)	$0	$0 (.025 x $10,000,000)

Example 7: A and B are married taxpayers. A owns 30% of an LLC taxed as a partnership. The LLC has W-2 wages of $1,000,000 and depreciable property of $100,000. A has QBI of $900,000 from the LLC and taxable income of $880,000. What is A's deduction? A's deduction equals $150,000.

It is important to remember that the calculations are performed at the individual level and must incorporate

20% of QBI:	20% of Taxable Income:	W-2 Limitation:	Capital Limitation:
$180,000	$176,000	$150,000 ($1,000,000 x .3) x .5 = $150,000)	$75,750 ($1,000,000 x .3) x .25 + ($100,000 x .3) x 2.5%)

A's percentage interest in the entity. Accordingly, you first multiply the wage limitations and depreciable property limitation by A's 30% interest.

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II. Specified Service Trade or Business Exclusion

199A contains complex exclusion rules applicable to a "Specified Service Trade or Business" (SSTB). The SSTB exclusion applies to taxpayers above the initial income threshold; they are completely barred once they exceed the second income limitation (i.e., the $207,500/$415,000 threshold). Put another way, the SSTB exclusion doesn't apply to any business below the initial threshold ($157,500/$315,000). 199A cross-references Internal Revenue Code §1202 to identify specific SSTBs that the exclusion automatically applies to. These specific SSTBs are health, law, accounting, actuarial science, performing arts, consulting, athletics, financial services, brokerage services, investing and investment management, and trading and dealing in securities. Engineers and architects are excluded as SSTBs, and therefore taxpayers engaged in these fields qualify for the 199A deduction regardless of their income. The text of Internal Revenue Code §1202 cross-referenced by 199A contained a problematic catch-all that stated an SSTB would be any trade or business based on the "reputation or skill of one or more of its employees." This catch-all provision had the potential to apply to a great many professions that would otherwise qualify for the 199A deduction. The recently issued Treasury Regulations limit the applicability of this catch-all to (a) a business where someone receives compensation for endorsements; (b) a business where someone licenses or receives fees for his image, likeness, name, signature or trademark; and (c) a business where someone receives appearance fees from radio, television, YouTube or other mediums.

The Treasury Regulations state that SSTBs in health include physicians, pharmacists, nurses, dentist, veterinarians, physical therapists, psychologists and other healthcare professionals, but do not include health clubs, spas, payment processing, research/testing/manufacture/sale of medical devices or pharmaceuticals, nursing homes, surgery centers that rent out their space to doctors, or laboratories performing tests for doctors. SSTBs in law include attorneys, mediators, arbitrators and paralegals, but do not include printers, delivery services or stenographers. In performing arts, SSTBs include actors, singers, musicians, directors and entertainers, but do not include broadcasters or entities creating equipment for use in the performing arts. The Treasury Regulations define consulting to include the provision of professional advice to help someone achieve goals, lobbying and regulator advice, but not to include the sale of general educational products or training. The Treasury Regulations specifically include owners of athletic teams as SSTBs but exclude restaurants as SSTBs. The franchising of financial advice (e.g., Suze Orman and Rich Dad, Poor Dad) would not be an SSTB so long as it is not individually providing services to consumers.

A business could be composed of separate divisions, one of which is an SSTB and the other which is not. The Treasury Regulations incorporate a gross receipts test related to the SSTB to determine whether the business's SSTB services disqualify the entire enterprise as an SSTB. If less than 10% of a business's gross receipts is from an SSTB and its receipts total $25,000,000 or less, then the performance of the SSTB won't disqualify the business. If the business's gross receipts are more than $25,000,000, then only 5% of a business's receipts can originate from an SSTB.

Example 8: An LLC performs health care services, but also sells health care equipment. The LLC has gross receipts of $2,000,000, of which $250,000 is from health care services. In this example, the LLC is an SSTB because more than 10% of its receipts are from an SSTB.

III. 199A Selected Issues

a. Section 754 Elections

Section 754 elections are a popular tool for reducing income taxes in partnerships, but how will they affect the 199A calculation, especially when subject to the Capital Limitation? Individuals buying into a partnership will be able to increase their Capital Limitations by an amount equal to the increase in fair market value. This means partners within the same partnership could have a different Capital Limitation threshold.

Example 9: A, B and C are equal partners in Z, an LLC. Z generates QBI and owns qualifying property with a basis equal to $900,000. A sells her one-third interest to X for $350,000. At sale, the qualifying property has a tax basis equal to $750,000, and Z has a 754 election in place. The amount of X's Section 743(b) basis adjustment in Z's qualifying property is $100,000 ($350,000 - $250,000, which is the cost basis). Remember that the QBI calculation does not utilize depreciation in its calculation, as the taxpayers utilize the unadjusted basis, i.e., acquisition value. In this example, the 754 election allows a $100,000 basis adjustment, but this is not the amount given to X for purposes of determining X's Capital Limitation. Instead, X is permitted to increase its Capital Limitation amount in the qualifying property by an amount called the "excess basis adjustment." The excess basis adjustment is determined by subtracting the original Capital Limitation amount from X's cost basis. In this example, it is calculated as follows: $350,000 (X's cost basis) MINUS $300,000 (the unadjusted basis of the property). Therefore, X's Capital Limitation on the

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qualifying property is 2.5% of $350,000, while B's and C's Capital Limitations on the qualifying property remain 2.5% of $300,000.

b. Trusts and Estates

Trusts and estates qualify for the Section 199A deduction. Trusts and estates receive the lowest threshold, i.e., the individual's income threshold ($157,500). Not surprisingly, grantor trusts are treated as if the individual owned the entity. Electing Small Business Trusts (ESBTs) are entitled to the deduction, so that the S portion of the ESBT takes into account its share of the QBI and other items from any S corporation owned by the ESBT, the grantor trust portion (if any) passes to the grantor/owner, and the non-S grantor portion takes into account any QBI from other items. For purposes of determining the threshold, the S portion and non-S portion are treated as a single trust, which goes against the traditional handling of ESBTs in the Treasury Regulations, which treat an ESBT as two separate trusts – the S portion and the non-S portion. The Treasury Regulations create an anti-abuse rule preventing the creation of separate trusts to achieve multiple 199A deductions. This anti-abuse rule is found in Section 1.643(f) and generally provides that two or more trusts will be aggregated and treated as a single trust if (a) they have the same grantor/grantors, (b) they have substantially the same beneficiaries and (c) the principal purpose for establishing one of the trusts is to avoid income tax. Spouses are treated as one person in these anti-abuse rules. Final regulations clarify that non-grantor trusts can reduce a trust's exposure to the W-2 Wage Limitation and Capital Limitation by distributing income to the beneficiary.

c. 1031 Transactions

Many pass-through entities engage in Section 1031 transactions to defer income tax recognition on the sale of real property. 1031 transactions can affect the Capital Limitation if the pass-through entity receives boot or contributes additional cash to the exchange closing. For the Capital Limitation, the original acquisition value of the property will continue to be the baseline for determining the Capital Limitation unless boot is involved. When contributions are made to close the exchange, the regulations require establishing separate Capital Limitations within the same property. Receipt of boot reduces the Capital Limitation on the property.

Example 10: X purchases Z property for $1,000,000 in 2018. Two years later, the Z property's basis is $820,482 because of Section 168 deductions, and Z is worth $1,300,000. X exchanges Z property for Y property with a value of $1,300,000. X's Capital Limitation threshold for determining QBI remains $1,000,000 and the property is treated as being placed in service in 2018 (remember the 10-year limitation).

Example 11: Same facts as 10 but at the time of the exchange, X must contribute $300,000 to exchange Z property for Y property. In this example, X is deemed to have separate Capital Limitations in the same property, so Z property will have a $1,000,000 Capital Limitation threshold with a service date of 2018 and another Capital Limitation of $300,000 with a service date of 2020. This is a fair result, as the taxpayer is putting additional funds to the purchase of qualifying property.

Example 12: Same facts as 10 except Z property is worth $1,300,000 and Y property is only worth $1,000,000, and X receives $300,000 in cash to compensate her for the variance in value. A's Capital Limitation basis continues to be $1,000,000 because the boot received does not exceed the fair market value of Z property. The Capital Limitations service date is 2018.

Example 13: Same facts as 12 except Y property is only worth $900,000 and Z receives $400,000 in boot. In this example, the Capital Limitation becomes $900,000, as the Capital Limitation is decreased by the excess boot received, which is calculated by subtracting the appreciation of the property's fair market value ($300,000) by the amount of boot received ($400,000) and subtracting this amount from the original property basis.

d. Aggregation Rules

Taxpayers subject to the Wage Limitation and Capital Limitation will want to aggregate trades or businesses to increase their Section 199A deduction by increasing their W-2 Limitation or Capital Limitation. To aggregate separate businesses, the following requirements must be met:

1. The same person or group of persons owns 50% or more of each trade or business (directly or indirectly, subject to attribution rules of Sections 267(b) or 707(b)).

2. Fifty percent of common ownership must exist for a majority of the year.

3. The aggregated trades must report items within the same taxable year (can't have one on fiscal year and one on calendar year).

4. No trade can be an SSTB.

5. Two of the following three thresholds must be met:

(a) The trades or businesses must provide products, property or services similar or customarily offered to-

gether.

(b) The trades or businesses share centralized business elements (accounting, personnel, etc.).

(c) The trades or businesses are operated in coordination or reliance upon one or more businesses.

Example 14: X owns 75% of S1, an S corporation manufacturing clothing, and 75% of PS1, which is a retail pet store. Both are calendar year taxpayers. X manages both S1 and PS1. Will this qualify for aggregation? No. Although X manages both operations, they have common ownership and they're on the same taxable year, they do not have complementary services or shared facilities, and they are not operated in coordination with one another.

Example 15: X owns 60% of PS1 and PS2. PS1 sells nonfood items to grocery stores. PS2 operates a distribution trucking business predominantly shipping PS1's products. PS1 and PS2 are on the calendar year. PS1 and PS2 cannot aggregate because they do not share facilities/centralized business elements and do not have complementary products or services.

Example 16: X owns 100% of S1, a residential condo building, and 100% of S2, commercial rental office space. Both operations share centralized accounting, legal and HR. X cannot aggregate. Although they have centralized operations, the two buildings are not of the same type of property and cannot aggregate.

Example 17: LLC1 performs vet services and sells its own line of dog food at its clinic and through distribution channels. LLC1 has $1,000,000 of vet service fees, and $3,000,000 of dog food sales. LLC1 would be a disqualified SSTB because more than 10% of its gross receipts are from vet services. However, LLC1 can treat the two as separate businesses and therefore qualify for a 199A deduction.

e. Wage Agents

W-2 wages paid by certified professional employer organizations (PEOs), statutory employers and Section 3504 common pay agents will qualify for the 199A deduction. The final regulations clarified this, but there is some uncertainty regarding noncertified PEOs, which don't have to qualify for the bond requirement or audited financials. For more about W-2 issues, see Notice 2018-64.

f. Crack and Pack Strategy

The final regulations prevent the crack and pack strategy that many commentators thought could generate deductions by carving out businesses that could qualify for the 199A deduction from SSTBs and operating them as separate businesses. The final regulations prohibit any 199A deduction from a business that provides services to an SSTB if there is 50% or more common ownership with the business providing services to an SSTB.

Example 18: A law firm is a partnership, owns its office building and employs its own administrative staff. The law firm divides into three partnerships. PS1 performs legal services, PS2 owns the building and rents to PS1, and PS3 employs admin staff for PS1 under contract. Because of common ownership, these are all deemed SSTBs.

Example 19: Same facts as 18, but PS2 rents 50% of the building to PS1 and 50% to unrelated tenants. Fifty percent of PS2's rental will be an SSTB, but the remaining 50% will not, and therefore this 50% could qualify for the 199A deduction.

New Internal Revenue Code §199A is a complicated provision whose application further complicates typical transactions that pass-through entities typically undertake. The 199A Treasury Regulations are largely sensible, taxpayer-friendly interpretations.

About the author:

Keith C. Durkin is a Partner with the law firm of BakerHostetler in Orlando, Florida.

1. For purposes of calculating the Capital Limitation, qualified property is generally any tangible property that is depreciable. The property can be used in the calculation for the later of 10 years or the last day of the full year of the asset's depreciable period.

Submit an Article



The Tax Bulletin is published three times a year, Fall, Spring, and Summer. Each publication accepts up to six articles of approximately 500 to 1,000 words each. The Tax Section would like to thank Mitchell Goldberg of Berger Singerman (Fort Lauderdale) and Guy Whitesman of Henderson Franklin (Fort Myers) for serving as the Tax Bulletin's Content Editors. Lisa Gallagher of Fergeson Skipper, P.A. (Sarasota) currently serves as the Publishing Editor. If you have an article you would like to be considered for publication, or questions regarding deadlines, please reach out to Lisa via email: LGallagher@FergesonSkipper.com

Federal Tax Liens and Defeasible Interests

By: Scott St. Amand

Attachment of Federal Liens to Property and State Law Property Rights

Property rights are determined by state law, and the Internal Revenue Code "merely attaches consequences, federally defined, to rights created under state law." One such consequence is attachment of a Federal tax lien, which is "wholly a creature of federal law" and is one of the "formidable arsenal of collection tools" necessary "to ensure the prompt and certain enforcement of the tax laws in a system relying primarily on self-reporting." Stated another way, the attachment of Federal tax lien depends on whether "property" or "rights to property" exist under state law, but the attachment and priority of a Federal tax lien depends entirely upon federal law.

Transfer of Property Generally does not Affect Lien

"The transfer of property subsequent to the attachment of the lien does not affect the lien." That is to say, "once a lien has attached to an interest in property, the lien cannot be extinguished simply by a transfer or conveyance of the interest." Nevertheless, "the Government's lien under IRC § 6321 cannot extend beyond the property interests held by the delinquent taxpayer."

Federal Tax Lien May Attach to Defeasible Interests

"Where…on the occurrence of an event…an interest will terminate," such an interest is referred to in the Internal Revenue Code as a "terminable interest." Under state law, "where an estate has been devised in fee, subject to being defeated by the happening of some future event," such conveyance may also be known as a "defeasible fee."

It is well settled that a federal tax lien may attach to a terminable interest in real property pursuant to IRC § 6321, because a Federal tax lien attaches to "all property and rights to property, whether real or personal," possessed by a delinquent federal taxpayer. As with any other interest in property, attachment to a terminable interest, ends when the interest terminates.

It follows then, where a taxpayer's property rights are terminable, "the Government's rights, by virtue of its lien upon the taxpayer's interest, are likewise terminable, being no greater than those of the taxpayer." Therefore, when the taxpayer's interest subject to the lien is a terminable interest, the government's lien on that particular property is extinguished at the same time as the taxpayer's interest, "since there is no longer any property…to which a lien can attach."

Hypothetical

Take, for instance, a situation where a father conveys a remainder interest to his son in a piece of property using a Ladybird deed. By doing so the father reserved an "enhanced life estate" to himself. The son owes a federal tax debt, and the IRS places a lien on all of his real property interests—including his remainder interest in his father's property. Therefore, to terminate the tax lien, all the father needs to do is terminate the son's interest.

Because the father reserved the absolute right to convey the property in fee simple, such a conveyance would wholly terminate the son's interest in the property. The father would simply convey the property to himself (in fee simple) by special warranty deed. Once the deed is executed, the son's interest in the property terminates, and the father becomes 100% owner of the property once again—free of any IRS lien.

Conclusion

Although the "transfer of property subsequent to the attachment of the lien does not affect the lien," the attachment of the lien terminates when the underlying interest to which it attaches terminates. As noted in, Rev. Rul. 54-154 and its progeny, when a taxpayer's rights "are terminable, the Government's rights, by virtue of its lien upon the taxpayer's interest, are likewise terminable, being no greater than those of the taxpayer." Accordingly, "when the taxpayer's [property] rights…terminate after the Federal tax lien has arisen, the rights of the United States in the [property] also terminate, since there are no longer any property [rights] to which a lien can attach."

About the Author:
Scott St. Amand is an attorney with the law firm of Fisher, Tousey, Leas & Ball in Jacksonville, Florida.

Endnotes:

1. Drye v. United States, 528 U.S. 49, 58 (1999); United States v. Bess, 357 U.S. 51, 55 (1958); United States v. Librizzi, 108 F.3d 136, 137 (7th Cir. 1997).

2. United States v. Swan, 467 F.3d 655, 656 (7th Cir. 2006) (citing United States v. National Bank of Commerce, 472 U.S. 713, 722 (1985)).

3. Id.; United States v. Craft, 535 U.S. 274, 278-79 (2002).

4. Rodriguez v. Escambron Dev. Corp., 740 F.2d 92, 96 (1st Cir. 1984) (citing United States v. Rodgers, 461 U.S. 677, 683 (1983)).

5. Aquilino v. United States, 363 U.S. 509, 513–515 (1960).

6. Bess, 357 U.S. at 57.

7. Rodriguez, 740 F.2d at 99.

8. Rodgers, 461 U.S. at 690-91; United States v. Jepsen, 131 F. Supp. 2d 1076, 1085 (W.D. Ark. 2000); Rodriguez, 740 F.2d at 99 (holding "[t]

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he government's rights can rise no higher than those of the taxpayer to whom the property [interest] belongs"); Rev. Rul. 54-154 (1954) (holding Federal tax liens attach to property only to the extent of the delinquent taxpayer's interest therein).

9. See, e.g., I.R.C. § 2056(b)(1).

10. Dickson v. Alexandria Hosp., 177 F.2d 876, 880 (4th Cir. 1949); Armenian Assembly of Am., Inc. v. Cafesjian, 811 F. Supp. 2d 120, 127 (D. D.C. 2011), aff'd, 758 F.3d 265 (D.C. Cir. 2014) (holding that a "defeasible fee" is an "estate in fee, subject to be defeated on the happening of some future event").

11. United States v. Baran, 996 F.2d 25, 27 (2d Cir. 1993) (tax lien attached to life estate); I.R.M. 5.17.2.5.5 (tax lien attaches to terminable interests); Segal v. Rochelle, 382 U.S. 375, 379 (1966) (holding that an "interest is not outside reach of tax lien because it is novel or contingent").

12. IRC § 6321.

13. See Swan, 467 F.3d at 656; Rev. Rul. 54-154.

14. Rodgers, 461 U.S. at 690-91.

15. Id.; see also Jepsen, 131 F. Supp. 2d at 1085.

16 Bess, 357 U.S. at 57.

17. See I.R.M. 5.17.2.5.5 (stating "once the [taxpayer's] interest terminates, the Federal tax lien on that interest also terminates").

18. See also, Stuart v. Willis, 244 F.2d 925, 929 (9th Cir. 1957); Lloyd, Kane & Wieder, P.A. v. United States, 757 F. Supp. 683, 684 (D. Md. 1991); Rodgers, 461 U.S. at 696.

19. Id.; see also I.R.M. 5.17.2.5.5.

Ceci n'est Pas Une Penalty: Valuation Problems with Works of Art

By: Samantha Gozlan



I. Intro.

The practice of strategically gifting and devising interests in art is advantageous for collectors with respect to the charitable donation it affords them in both the gift and estate tax realms. However, this practice has also resulted in an exploitation of valuation; the value of gifted art is often inflated in order to maximize a charitable deduction and undervalued in order to escape gift tax consequences. Further, valuation may be tampered in the estate tax realm to reduce estate tax consequences. This paper explores potential penalties that occur when pieces of art are incorrectly valued.

a) Charitable Deductions

Individuals and corporations have the opportunity to make gifts to certain charitable entities in order to receive a deduction to their gross tax liability. The deduction is limited to either thirty or fifty perfect of the taxpayer's contribution base for the taxable year over the amount of charitable contributions allowed. However, a taxpayer may carry over the remainder of his or her donation for each or the succeeding five years when the charitable deduction exceeds the taxpayer's adjusted gross income.

For gifts of art valued at more than $5,000, an appraisal is required. Failure to provide an appraisal will result in the service disallowing the deduction in its entirety. Failure to provide an accurate valuation, permits the Service to impose accuracy and civil fraud penalties against the taxpayer and may also limit or disallow the taxpayer's charitable deduction. However, a more taxpayer-friendly rule states that if the Service completely disallows a deduction, it is not permitted to impose a penalty for the valuation overstatement included in the deduction.

b) Estate Tax

The estate tax is a tax on a decedent's assets at death. The taxable portion of a decedent's estate is referred to as the gross estate, which is the fair market value of the decedent's assets at the time of death. Once the gross estate is calculated, the taxable estate is simply the gross estate less any applicable credits and deductions. After the taxable estate is calculated, the values of the decedent's lifetime gifts are added and adjusted for inflation. If the taxable estate's balance exceeds the statutorily defined threshold (referred to as the unified credit amount), then the decedent's estate is required to pay the top rate of 40 percent estate tax on the excess amount over the unified credit. An estate tax return (IRS Form 706) is required to report estate tax within 9 months after the death of the taxpayer.

Some taxpayers reduce their gross estate by undervaluing the works of art in their possession at death. By undervaluing artwork, the gross estate shrinks along with the tax due. When a work of art is undervalued on an estate tax return, the taxpayer is subject to IRS audits to ensure the estate tax was properly calculated. However, this practice can lead to litigation if the IRS

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values the works of art differently than the appraiser did with respect to the estate tax return.

c) Gift Tax

A gift tax return (Form 709) requires filing for any tax year where the taxpayer makes a gift made directly or indirectly, in trust, or by any other means, to a single individual or non-qualified charity in excess of the annual exclusion ($15,000 in 2019). The taxpayer's lifetime gifts are not taxed if the value of the gifts does not exceed the lifetime gift tax exclusion. Gift tax returns are the method that the IRS uses to track the amount of gifts that an individual has made throughout their lifetime. A gift tax return need not be filed if the gift was made to an eligible charitable entity in pursuit of a charitable deduction. Taxpayers make gifts for a variety of reasons. However, donative intent is irrelevant when determining if a gift is subject to the federal gift tax.

d) Valuation of Works of Art

Procedural issues arise when taxpayers under or overvalue works of art. Since art is an arguably subjective form of currency, its valuation regulation is not a one-size-fits-all analysis. Valuation can differ drastically when compared to fungible assets like stock and real estate. For this reason, the Service requires special rules regarding valuing works of art and collectibles. If an artwork in question has a value of $5,000 of more then the art requires a qualified appraisal. The Service requires that individual works of art with a value of $50,000 or more sophisticated valuation provided by the Service's Art Appraisal Services Assistance (AAS). At the discretion of the AAS, the work of art may further be submitted for appraisal by the Arts Advisory Panel. The panelists review the works of art without knowledge of the owners' identities to provide more accurate valuations. These valuations are then reviewed by the AAS and become the Service's position if accepted. If the taxpayer does not agree with the Service's assessment, then an action may be filed contesting the AAS's valuation.

II. Procedural Issues

When a taxpayer asserts an artwork's valuation and the valuation is contested by the IRS, the taxpayer is subject to different penalties based on where the valuation error occurred and the amount of the under or overstatement. Further, there may be repercussions for the appraiser who completed the valuation of the artwork in question.

a) Penalties to the Taxpayer

Taxpayers face several accuracy potential penalties if they misstate the value of an artwork. These penalties may fall under different sections of the Internal Revenue Code depending on the offense by the taxpayer. For example, IRC 6663 addresses penalties for fraudulent activity, while IRC 6662 can nab a taxpayer who has an accuracy related issues on underpayments. If the taxpayer engages in discussions with an appraiser, to dupe the IRS into thinking an artwork is worth substantially less than it is to reduce the gift tax consequences of making an *inter vivos* transfer of the artwork, then the taxpayer will likely be slapped with an accuracy related penalty and a civil fraud penalty. Under previous law, these penalties could be asserted simultaneously by the Service, however, at this time the accuracy-related penalties apply only to the extent of the underpayment not attributable to the fraudulent activity.

b) Accuracy Related Penalty

I.R.C. § 6662(b)(2) imposes a 20 percent addition to tax on any portion of an underpayment of tax attributable to a "substantial understatement of income." The statute defines a substantial understatement as occurring when the tax return states has an understatement exceeding the greater of: (i)10 percent of the tax required to be shown on the return for the taxable year, or (ii)$5,000. Further, the penalty doubles from 20 percent to 40 percent when appraisals are 40 percent or less of the Service's determination. Taxpayers must be weary of accuracy related penalties, because the Service is able to assess a deficiency based on a valuation, pursuant to subsequent sales of works of art after the Taxpayer's death and the Estate's filing of gift and estate returns. The Service is permitted to use post mortem sales as a factor in valuation. This is a particularly precarious position for taxpayers, given the uncertainty and flux in the art market. Unlike real property or tangible items that have a set value, works of art are single pieces whose valuation can differ based on a myriad of factors including: preference of the appraiser, other sales of works by the same artist, art market conditions, and popularity of the artist. Even when taxpayers are not intentionally trying to evade paying tax, they may be subject to a deficiency action based solely on a particularly active sale at auction. Given the heightened penalty when works of art mis-valued 40 percent or less of the IRS's determination, taxpayers should be weary and make conservative valuations on their prized artworks.

c) Civil Fraud Penalty

I.R.C. § 6663 refers to the civil fraud penalties applied to taxpayers whose behavior exceeds substantially beyond reasonable case and evidences an international effort to underpay taxes. The fraud penalty has a heightened penalty rate of 75 penalty of the portion of the underpayment attributable to fraud. Fraud penalties have been assessed when taxpayers knowingly underreport a Decedent's taxable estate (for estate tax purposes) as well

as for undervaluing assets held in the estate. The Service carries the burden of proving the fraud initially by clear and convincing evidence. This finding will subject the entire underpayment to the 75 percent penalty. Specific intent to avoid a tax as well as intentional wrongdoing are required to prove fraud. The Service is able to use conduct known as *badges of fraud* to illustrate the intent. Once established, the burden of proof shifts to the taxpayer, who only must disprove the fraud by a preponderance of the evidence that the payment is not attributable to fraud.

d) Penalties to the Appraiser

The appraiser who mis-values a work of art may be subject to penalties from the Service. A penalty may be appropriate if, a person who appraises an artwork *knew* or *reasonably should have known* the value of the property and that appraisal is being used in connection with a tax return or a claim for refund, resulting in a substantial valuation misstatement. The definition of a substantial valuation misstatement is provided in I.R.C. § 6662(e) for income tax purposes. For income tax purposes a substantial valuation misstatement occurs when the claimed value of the property at issue is 150% or more of the correct amount of the valuation. It is defined for gift and estate tax purposes under I.R.C. § 6662(g), and gross valuation misstatements are defined under I.R.C. § 6662(h).

Gift/Estate tax substantial valuation understatements are when the value of the property claimed is 65% or less of corrected amount. A gross valuation misstatement is occurs when the claimed value the property is 200% or more of the correct amount of the valuation. A gross estate/gift tax valuation understatement occurs if the value of the property claimed is 40% or less of the amount determined to be the correct amount. The penalty imposed under I.R.C. § 6695A is the lesser of: (a) the greater of 10 percent of the amount of the underpayment attributable to the misstatement or $1000 or 125% of the gross income received from the preparation of the proposal. The appraiser does however have a defense. If the appraiser can establish that the appraisal value, was more likely than not, correct. The statute of limitation on assessment for a I.R.C. § 6695A penalty expires 3 years from the date where the return was filed or the claim for refund was filed. The statue can be extended with the taxpayer's consent.

e) Conclusion

Taxpayers should be weary of appraisals completed in accordance with determining their tax liability because the penalties (and interest) incurred on a mis-valued work of art can catapult a taxpayer's bill above and beyond the expected tax due. A prudent strategy would have taxpayers' complete multiple valuations of artwork to submit along with their required filings and would have those appraisals completed by individuals who do not have a conflict of interest with the taxpayer or the work of art itself. Further, Taxpayers should err on the conservative side of the appraisal due to the required review by the AAS of works of art worth an excess of $50,000. By proceeding with caution and having multiple accurate valuations completed, taxpayers will be able to protect themselves from incurring penalties.

About the author:

Samantha Gozlan is a Candidate for LL.M. in Taxation from the University of Florida Levin College of Law.

Endnotes:

1. By making charitable donations, individuals support the public good by indirectly funding services that would generally be furthered by the public. I.R.C. § 170 was enacted in pursuit of this goal by permitting an individual or corporate taxpayer to deduct charitable contributions from their gross adjusted income. V. Sliskovich, *Charitable Contributions or Gifts: A Contemporaneous Look Back to the Future*, 57 UMKC L. REV. 437, 439 (1989).

2. I.R.C. § 170 permits donation to the following charitable entities to make a taxpayer eligible for a deduction: churches or associations of churches, educations al organizations that have regular pupils, faculty, and curriculum, hospital or medical research organizations, non-profit organizations characterized by tax exemptions under I.R.C. § 501(a), governmental units, private foundations, and agricultural research organizations. I.R.C. § 170 (2019).

3. Treas. Reg. § 1.170A-10 (1975).

4. I.R.C. § 170(f)11)(A)(i)(2019).

5. *See, Manning v. Comm'r*, T.C. Memo 1993-377 (fraud penalty). *See also, Williams v. Comm'r*, 101 T.C.M. (CCH) 1408 (T.C. 2011), aff'd, 498 F. App'x 284 (4th Cir. 2012).(The issue in Williams v. Comm'r was whether the taxpayer was liable for accuracy-related penalties on the underpayments resulting from his deducting of the appraised value donated art rather than his basis in the art. The Court held taxpayer was liable for accuracy related penalties for underpayments resulting from disallowed portions of his charitable contribution deductions.)

6. *United States v. Woods*, 134 S. Ct. 557 (2013).

7. The value of the gross estate of the decedent shall be determined by including the value of all property, real or personal, tangible or intangible, wherever situated at the decedents date of death. I.R.C. §2031. The gross estate includes all property in which the decedent had a present interest at death. It also includes: certain lifetime transfers made without adequate consideration, annuities, portions of jointly owned estates, life insurance proceeds (even if they are payable to beneficiaries that are not the decedents estate, the decedent's general power of appointment property, community property, and some property that was transferred out of the estate within 3 years of the decedents death. I.R.C. §§ 2033-2042 (2019).

8. I.R.C. §§ 2001(c), 2010, 2012–2014 (2019).

9. This tax credit reduces a taxpayer's taxable estate on a dollar-for-dollar amount. For example, taxpayer dies and her estate is valued at 20 million dollars, the basic exclusion amount ($11.4 million) will be applied to taxpayer's estate leaving a residue of eight million six hundred thousand dollars. Thus, a flat tax of 40% would be due on the amount over the basic exclusion amount, i.e. the $8,800,000.00. However, with married taxpayers, the unified credit amount is doubled (22.8 million), only subjecting a limited number of estates to the estate tax. I.R.C. § 2010 (2019).

10. IRS, *Instructions for Form 706*, https://www.irs.gov/pub/irs-pdf/i706.pdf (Rev. Aug. 2019).

11. In *Estate of Kollsman v. Comm'r of Internal Revenue*, the Service assessed a deficiency of $781,488 in reference to an under-valuation of two old masters' paintings in the decedent's estate. After get-

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ting slapped with the bill, the estate petitioned the Tax Court for a redetermination of the paintings' fair market values. After hearing from both the Service and the estate's experts, the Tax Court ruled in favor of the Service's expert, citing to a conflict of interest and exaggeration of degradation of quality by the estate's expert. *Estate of Kollsman v. Comm'r of Internal Revenue*, 113 T.C.M. (CCH) 1172 (T.C. 2017).

12. Gifts in trust treat each beneficiary as an individual-separate-donee for purposes of the annual exclusion. IRS, *Instructions for Form 709*, https://www.irs.gov/instructions/i709#idm140297522564656 (Oct. 30, 2019).

13. The basic exclusion amount for 2019 is $11,400,000. Rev. Proc. 2019-44. This amount is determined based on a gross taxable amount, unlike the annual exclusion amount. The annual exclusion amount is determined on an individual by individual gift basis. So, while the basic exclusion applies to all taxable gifts made in life, the annual exclusion amount is applied to individual gifts to different people made each year. For example, decedent gave each of his three children gifts of 15,000 in 2018, within the annual exclusion limit, therefore none of these gifts will contribute to his lifetime gift exclusion. Further, in 2019 decedent made gift of a 50,000 painting to his favorite nephew. Therefore, 35,000 of the 50,000 gift will be subject to tax and will contribute to decedent's lifetime gift exclusion amount. When decedent died, his total taxable gifts must exceed 11.4 million dollars to be taxable IRS, *What's New in Estate and Gift Tax*, https://www.irs.gov/businesses/small-businesses-self-employed/whats-new-estate-and-gift-tax (Sept. 23, 2019).

14. However, a gift tax return must be filed if only a partial interest was transferred to a qualifying charity. IRS, *Instructions for Form 709*, https://www.irs.gov/instructions/i709#idm140297522564656 (Oct. 30, 2019).

15. Transferor's donative intent is not an essential element in the application of the gift tax to the transfer. Treas. Reg. § 25.2511-1 (1997).

16. I.R.C. § 170(f)(11). A qualified appraisal is an appraisal meets Secretary guidance and must be conducted by a qualified appraiser in accordance with the standards laid out in the Pension Protection Act of 2009, which redefined the standards required. I.R.C. § 170(f)(11)(E). The new Treasury standards state that the appraisal should be consistent with the principals outlined by the Uniform Standards of Appraisal as developed by the Appraisal Standards Board of the Appraisal Foundation. *Id at* § 170(f)(11)(E)(i). For more information on what constitutes a qualified appraisal, qualified appraiser, and who will not qualify as a qualified appraiser, *see Id at* § 170(f)(11)(E)(ii,iii)

17. I.R.M. 4.48.2.2 (10-01-2012).

18. The Arts Advisory Panel is made up of a group of prominent art-world-favorites including curators, scholars, auction representative, and art dealers. Art Advisory Panel of the Comm. Of Internal Revenue, *Annual Summary Report for Fiscal Year 2015* (Closed meeting activity), IRS, https://www.irs.gov/pub/irs-utl/art_adv_panel_annual_summary_report_fy15.pdf (last visited Nov. 15, 2019).

19. I.R.M. 4.48.2.2 (10-01-2012).

20. During the fiscal year of 2015, the panel reviewed and 446 works of art. Average claims by taxpayers valued works of art at $1,455,821. However, the panel only recommended accepting about 35% of the appraisals it received, adjusting the valuation of 65% of the art works. The net adjustments to those items increased their value of about 18%. Annual Summary Report for Fiscal Year 2015 *supra* note 18.

21. One of the most famous works of art to have its valuation disputed was Robert Rauschenberg's 1959 combine painting, *Canyon*. The piece passed through Ileana Sonnabend's estate upon her death in 2007. The work features a taxidermized bald eagle carcass. Under the Bald and Golden Eagle Protection Act (BGEPA) and the Migratory Bird Treaty Act (MBTA), the possession without permit, sale, purchase or export of an eagle (dead or alive) is prohibited. Based on the aforementioned treaties, the estate valued the artwork at $0, since it could not be sold. The Arts Advisory Panel took an aggressive stance valuing the work at $15 million dollars, the estate also was slapped with an $11.7 million dollar penalty for misrepresenting the value of the artwork. The Panel based their valuation on the illegal market activity value of the artwork as they had done in previous cases, however, in those cases there was an actual marker for the case. However, with *Canyon*, the sale of the work would be completely domestically and internationally prohibited. In the end, the Service settled, by waiving the penalty and tax liability and the estate donated *Canyon* to the Museum of Modern Art in New York without taking a charitable deduction. Charlotte Melbinger, Case Note, *The Sonnabend Estate and Fair Market Valuation of Canyon*, 163 U. PA. L. REV. 239 (2015).

22. I.R.C. §§ 6662, 6663 (2019).

23. I.R.C. § 6662(b) (2019).

24. I.R.C. § 6662(d)(1) (2019).

25. IRM 20.1.12.3(5)(d)(12-18-2017).

26. *In Estate of Newberger v. Comm'r*, the taxpayer's executor had a painting by Picasso appraised before it was sold at auction for $5 million. The Service assessed a deficiency after the work was sold for a surprisingly high sum, $12.9 million, way above the valuations previously provided by appraisers. The Tax Court ruled that an artwork's valuation. The difference between the valuation amount and sale amount was subject to 20% accuracy related penalties as well as the 40% estate tax. *Estate of Newberger v. Comm'r*, 110 T.C.M. (CCH) 615 (T.C. 2015).

27. *Id.*

28. *In Estate of Trompeter v. Comm'r*, the service determined that the Estate had knowingly underreported the taxable estate by $22,833,693, including $14 million in omitted assets, an undervaluation of shares and some of the Decedent's gold coins. The fore mentioned items were seized from a safety deposit box (which the service discovered with help from whistle blowers) and the Service claimed that the Estate's executor had further taken an improper deduction. In addition to various deficiency penalties, the Commissioner also assessed a $14,875,909 fraud penalty pursuant to Section 6663(a) of the Internal Revenue Code. *Estate of Trompeter v. Comm'r*, 279 F.3d 767, 769 (9th Cir. 2002).

29. *Id.*

30. I.R.C. 7454(a)

31. *Stoltzfus v. US*, 398 F.2d 1002 (3d Cir. 1968).

32. Some conduct that may indicate fraudulent intent, may include: (1) understatement of income; (2) maintaining inadequate records, (3) giving implausible or inconsistent explanations of behavior; (4) failing to cooperate with tax authorities; (5) providing incomplete or inaccurate information to a tax preparer; and (6) dealing in cash. One specific factor is not enough to prove fraud, but an intent to mislead may be inferred form a pattern of conduct. *Morse v. Comm'r*, T.C. Memo. 2003-332., Aff'd, 419 F.3d 829 (8th Cir. 2005).

33. I.R.C. 6663(b) (2019).

34. IRM 20.1.12.1.1(1) (12-18-2017).

35. *Id.* at 20.1.12.1.1(2) (12-18-2017).

36. I.R.C. § 6662(e) (2019)..

37. *Id.* § 6662(g) (2019).

38. *Id.* § 6662(h) (2019).

39. *Id.* § 6662(h) (2019), IRM 20.1.12.4 (2-4) (12-18-2017).

40. I.R.C. § 6695A (2019).

41. I.R.C. § 6695A, IRM 20.1.12.1.1(3) (12-18-2017).

42. IRM 20.1.12.4 (1)(a,b) (12-18-2017).

43. Taxpayer has the opportunity to file a Form 872-AP, *Consent to Extend the Time on Assessment of IRC Section 6695A Penalty*. IRM 20.1.12.4 (2) (12-18-2017). Taxpayers are unlikely to consent to an extension for the IRS to assess the penalty. Further, dealing with valuations of works of art, are generally not a situation where the taxpayer is taking a risky position that will continue for several years. The Service instructs its agents to obtain signed consents to extend the statute of limitations when the penalty statute of limitations is set to expire within 180 days. IRM 20.1.12.4 (4) (12-18-2017).

Secure Act Explained

By. Keith C. Durkin

On December 20, 2019, President signed into law the Setting Every Community Up for Retirement Enhancement Act, commonly referred to as the SECURE Act. Beginning Jan. 1, the SECURE Act substantially revises the income tax deferral opportunities of qualified retirement plans, such as 401(k)s, IRAs, 403(b)s and other qualified retirement plans. This article summarizes salient points of the SECURE Act and how it may affect a client's income tax and estate planning objectives. Nearly all estate plans should be reviewed to preserve maximum income tax deferral and avoid unanticipated consequences resulting from estate plans drafted prior to passage of the SECURE Act.

I. Mandatory Distribution of Qualified Retirement Accounts to Beneficiaries Other Than Eligible Designated Beneficiaries.

Prior to passage of the SECURE Act, heirs and qualifying trusts designated as a beneficiary of a qualified retirement account could stretch out the distribution of the qualified retirement account over the applicable beneficiary's life expectancy. The undistributed portion of an heir's qualified retirement account would continue to grow income tax free, resulting in substantial income tax savings and untaxed appreciation. The SECURE Act eliminates the ability of most heirs to stretch the qualified retirement account over their life expectancy, and instead requires all beneficiaries, other than "Eligible Designated Beneficiaries," to receive the full balance of the inherited qualified retirement account within 10 years following the year of inheritance. The SECURE Act eliminates annual required minimum distributions to beneficiaries other than Eligible Designated Beneficiaries, and only requires the full balance of the account to be distributed within the 10-year period. This means a beneficiary could defer the full distribution of the account until year 10 and not receive any required minimum distributions in the interim. This 10-year requirement applies to trusts, including trusts qualifying as see-through trusts with conduit trust provisions.

Example: A dies with an IRA balance of $5 million in 2020 and designates the beneficiary of the account as A's adult daughter, B. B does not have to receive any required minimum distributions after A's death and could defer receiving the full IRA balance until 2030. Alternatively, B could receive the IRA balance gradually over the 10-year period to mitigate a large income tax obligation in 2030.

Example: A dies with an IRA balance of $5 million in 2020 and designates the beneficiary of the IRA as A's revocable trust, whose primary beneficiary is a separate subtrust for the primary benefit of A's adult daughter, B. Like the example above, the trustee must receive the full distribution of the account by 2030.

Planning Opportunity – Clients could designate a charitable remainder unitrust (commonly referred to as a CRUT) as the beneficiary of their IRA with their children as the income beneficiaries of the trust, which would allow the children to receive the IRA proceeds over a period longer than 10 years. Clients anticipating net operating losses will want to defer the recognition of an inherited IRA until their net operating losses are incurred. Additionally, clients inheriting IRAs close to retirement will want to defer receipt of the IRA account until retirement, when presumably they will be in a lower income tax bracket.

II. Distribution Provisions of Qualified Retirement Accounts to Eligible Designated Beneficiaries.

The 10-year rule explained above will not apply to Eligible Designated Beneficiaries. The SECURE Act excludes five types of Eligible Designated Beneficiaries from the 10-year rule: (A) spousal beneficiaries; (B) minor children of account owner; (C) individuals who are not more than 10 years younger than the account owner; (D) disabled beneficiaries; and (E) chronically ill beneficiaries.

A. Spousal Beneficiaries. Surviving spouses qualify as Eligible Designated Beneficiaries. They are still entitled to spousal rollover of IRAs and receive required minimum distributions over their life expectancy.

B. Minor Children of Account Owner. Minor children of the account owner qualify as Eligible Designated Beneficiaries and can stretch receipt of the inherited qualified retirement account until they reach the age of 18 years, at which point they are forced to receive the entire qualified retirement account within 10 years after attaining age 18. Put another way, upon attaining age 18, the child is subject to the 10-year rule explained in Section I above. This rule, however, applies only to the account owner's children. Accordingly, minor grandchildren designated by a grandparent as beneficiaries of his or her qualified retirement account would not qualify as Eligible Designated Beneficiaries, and such minor children will be forced to receive the entire qualified retirement account within 10 years following the year of the grandparent's death.

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Example: A dies with a 10-year-old son, B, in a state where the age of majority is 18 years. A designates B as the primary beneficiary of his IRA. B must begin receiving required minimum distributions the year after A's death. Upon attaining age 18, B will be required to receive the entire IRA account by age 28.

Example: A dies with a 10-year-old grandson, B. A designates B as the primary beneficiary of his IRA. Because B is not A's child, B is not an Eligible Designated Beneficiary under the SECURE Act and is forced to receive the entire IRA account within 10 years following the year of A's death.

C. Individuals Not More Than 10 Years Younger Than Account Owner. An individual who is not more than 10 years younger than the account owner qualifies as an Eligible Designated Beneficiary and can stretch receipt of the inherited qualified retirement account by receiving required minimum distributions over his or her lifetime.

Example: A dies without children and designates A's sibling, B, as the beneficiary of A's IRA account. B is 4 years younger than A, and therefore qualifies as an Eligible Designated Beneficiary and can receive required minimum distributions over B's life expectancy.

Example: A dies without children and designates A's sibling, B, as the beneficiary of A's IRA account. B is 12 years younger than A, and therefore is not an Eligible Designated Beneficiary and is forced to receive the entire IRA account balance within 10 years following the year of A's death.

D. Disabled Beneficiaries. Disabled beneficiaries qualify as Eligible Designated Beneficiaries and can stretch receipt of the inherited qualified retirement account by receiving required minimum distributions over their lifetime. A disabled beneficiary is defined pursuant to Internal Revenue Code §72(m)(7), and is an individual "unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment which can be expected to result in death or to be of long-continued and indefinite duration." Individuals receiving Social Security Disability Insurance should qualify as a disabled beneficiary. Other disabled beneficiaries filing IRS Schedule R titled "Credit for the Elderly or Disabled" with their 1040s are qualified as the schedule requires a physician's certification that the individual meets this definition of disability.

E. Chronically Ill Beneficiaries. Chronically ill beneficiaries qualify as Eligible Designated Beneficiaries and can stretch receipt of the inherited qualified retirement account by receiving required minimum distributions over their lifetimes. A chronically ill beneficiary is defined pursuant to Internal Revenue Code §7702B(c)(2), and is an individual that (i) is unable to perform (without substantial assistance from another individual) at least two activities of daily living for a period of at least 90 days due to a loss of functional capacity; or (ii) requires substantial supervision to protect such individual from threats to health and safety due to severe cognitive impairment.

III. Increase in Age for Required Beginning Date for Mandatory Distributions.

Prior to the SECURE Act, account owners were required to begin receiving required minimum distributions from their qualified retirement accounts beginning at age 70½. The SECURE Act increases this age to 72 years, which allows greater income tax deferral to account owners.

IV. Repeal of Maximum Age for Traditional IRA Contributions.

Prior to the SECURE Act, individuals who attained age 70½ could no longer make any contributions to IRAs. The SECURE Act repeals this age prohibition. Individuals over age 70½ can now make contributions to IRAs; however, the requirement that such individual be working and receive compensation remains.

V. Expansion of 529 Benefits.

The SECURE Act expands permissible expenditures from 529 accounts to include apprenticeships, homeschooling, up to $10,000 of qualified student loan repayments (including those of siblings), private elementary school, private secondary schools and religious schools.

Conclusion:

The SECURE Act substantially changes the income tax deferral most clients expected in their estate plans. All estate plans should be reviewed and updated to ensure maximum tax deferral and avoid unanticipated consequences.

About the author:

Keith C. Durkin is a Partner with the law firm of BakerHostetler in Orlando, Florida.

Endnotes:

1. State law determines the age of majority. Most states' age of majority is 18.

Expansion of the IRS' Math Error Authority: An Analysis of Its Legality

By: Anthony Mark Cognasi

As a government taking of property, the Internal Revenue Service (IRS) must respect a taxpayer's Due Process rights when collecting tax revenue. However, the IRS must balance taxpayers' Due Process rights with the need to collect tax revenue efficiently and effectively. In order to promote collection efficiency, the IRS has expanded its math error authority to include post-processed returns so that it may retroactively deny refundable credits paid to low-income[1] taxpayers and collect the paid amounts without going through normal deficiency procedures. This article will outline the IRS' math error authority and examine the arguments for and against its expansion.

Generally, the IRS has three years from the later of the original due date or the filing date of a tax return to propose a deficiency in the taxpayer's tax liability and notify the taxpayer of such proposed deficiency with a Notice of Deficiency.[2] Upon the receipt of the Notice of Deficiency, the taxpayer generally has ninety days from the notice date to petition the Tax Court to challenge the IRS' proposed deficiency.[3] Only after the Tax Court has upheld the IRS' proposed deficiency may the IRS formally assess the deficiency and begin collection of the owed tax. Section 6213(b)(1) allows the IRS to bypass normal deficiency procedures and assess an additional tax. This ability is commonly known as the IRS' math error authority. Under the IRS' math error authority, the IRS may assess a deficiency based on a math or clerical error found on the taxpayer's return and send a notice of the assessment to the taxpayer.[4] However, the taxpayer may request an abatement of the assessment within sixty days of the notice date.[5] Upon the receipt of the request for abatement, the IRS must abate the assessment and proceed with normal deficiency procedures to assess and collect the tax.[6]

The first enactment of the math error authority lacked a definition of what constituted a math or clerical error. In 1977, Congress added a provision that defined a math or clerical error as one of five types of errors.[7] Later, in 1996 and 1998, Congress again expanded the definition of a math or clerical error to included incorrect Taxpayer Identification Numbers (TINs) listed for the purpose of claiming the Earned Income Tax Credit (EITC), Child Tax Credit and Additional Child Tax Credit (CTC/ACTC), or American Opportunity Tax Credit (AOTC).[8] TINs are typically a taxpayer's Social Security Number or a number assigned to the taxpayer by the IRS. An incorrect TIN is one that differs from the TIN that the IRS receives from the agency that issued it.[9] Therefore, if the Social Security Number that the taxpayer provides on the return is different from the Social Security Number that the IRS received from the Social Security Administration, it is incorrect.

On December 18, 2015, the Protection Against Tax Hikes (PATH) Act was enacted into law.[10] Prior to the PATH Act's enactment, taxpayers could claim the EITC, CTC/ACTC, and AOTC on an amended or late return with a TIN that was issued after the tax year in question. However, the PATH Act amended the rules to require that the taxpayer have a valid TIN issued on or before the due date of the original return in order to be eligible to claim the credits.[11]

In its report issued on July 17, 2017, U.S. Treasury Inspector General for Tax Administration (TIGTA) found that the IRS issued $34.8 million in refundable tax credits (such as the EITC, CTC/ACTC, and AOTC) to 15,744 taxpayers whose TINs were not issued on or before the due dates of the returns.[12] In response to the TIGTA report, the IRS released a Program Manager Technical Advice (PMTA) concluding that it is has the authority to use its math error authority to identify TINs incorrectly used to claim the credits listed in the TIGTA report and assess deficiencies by retroactively denying the refunded credits in contravention of normal deficiency procedures. This PMTA is the first time that the IRS has stated that its math error authority applies to post-processed returns with refunds already distributed. The release of the PMTA raised concerns about the expansion's legality, specifically its impact on taxpayers' Due Process rights, with the National Taxpayer Advocate, Nina Olsen, who asked the IRS to reconsider this expansion.

The IRS responded with a new PMTA issued on April 10, 2018. In it, the IRS concluded that nothing in Section 6213 precludes the IRS from using its math error authority to assess deficiencies on post-processed returns. The PMTA notes that Congress imposed no time limits on the IRS' math error authority upon its enactment in 1926, nor in any of the amendments made to the statute expanding the definition of a math or clerical error over the years.[13] Therefore, the PMTA argues that its math error authority is bound by the general statute of limitations found in Section 6213(a), which is three years from the later of the due date or filing date of the return.[14] Once it concludes that the statute does not prevent the IRS from assessing deficiencies on post-processed returns

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using its math error authority, the PMTA addresses the Due Process concerns of the Taxpayer Advocate in three ways. First, it states that the IRS will only use the expanded power sparingly and only in circumstances necessitated by the PATH act.[15] Second, the Due Process rights of taxpayers will not be abridged because the taxpayer may request an abatement upon receiving a notice of assessment. After which, the IRS must abate the assessment if the request is timely and proceed with normal deficiency procedures, which allow the taxpayer to challenge the proposed deficiency in Tax Court.[16] Finally, the hardships of taxpayers with TINs canceled or deactivated at the due date of the original return (which disqualifies them for the credits) only to have the TINs renewed afterwards are mitigated because the issue date relates back to the date the TIN were originally issued. As a result, the TINs would be considered issued on or before the due date of original return, and the taxpayer would be entitled to the credits.[17] Additionally, the PMTA notes that the IRS has gone to extensive efforts to notify potential taxpayers that their TINs would be expiring soon.[18]

The Taxpayer Advocate was unsatisfied with IRS' analysis and attacked it on Due Process grounds. The Taxpayer Advocate argues that EITC and other refundable credits are analogous to welfare benefits which generally require a deprivation hearing before being terminated.[19] However, as the Taxpayer Advocate notes, the Supreme Court has held that Due Process is flexible, and its requirements may change based on the situation.[20] In *Matthews v. Elridge*, the Supreme Court laid the groundwork for the adequacy of Due Process deprivation hearings by listing three factors to be used when determining the sufficiency of the hearing. The factors are the:

> "private interest that will be affected by the official action…the risk of an erroneous deprivation of such interest through the procedures used, and the probable value, if any, of additional or substitute procedural safeguards, and… the Government's interest, including the function involved and the fiscal and administrative burdens that the additional or substitute procedural requirement would entail.[21] "

The PMTA agrees that taxpayers are generally entitled to hearings before the IRS may assess a deficiency but feels that the opportunity to request an abatement sufficiently protects that right.

The Taxpayer Advocate states that under the *Matthews* factors the only way to protect low-income taxpayers' Due Process rights is through the normal deficiency procedure and the Tax Court. First, as mentioned above, the Taxpayer Advocate states that the refundable credits, especially the EITC, are more like welfare benefits than a tax credit. Second, the Taxpayer Advocate cited a 2011 Taxpayer Advocate Service report to show that the risk of erroneous deprivation is substantial.[22] The report found that the IRS reversed itself on 55% of returns that it initially determined had incorrect TINs through its math error authority.[23] Of that 55%, 56% could have been corrected by the IRS on its own due to the correct TINs being listed on a prior year's return.[24] Furthermore, of that 56%, 52% of those taxpayers never responded to the IRS notice and were denied a tax benefit that they were entitled to (averaging $1,274).[25] Finally, the Taxpayer Advocate illustrates that requiring that the IRS go through normal deficiency procedures will not endanger tax revenue due to the larger tax base from which the IRS may collect tax revenue.[26]

The IRS interpretation of Section 6213(b)(1) which allows it to use its math error authority within three years of the later of the due date or filing date is more than likely to be upheld by a court. By imposing a time limit on general deficiency assessment procedures but remaining silent in the same statute in regard to math error assessments, Congress more than likely did not wish to impose a time limit on math error assessments. For example, a prior Treasury Regulation imposed a two-year statute of limitations on equitable innocent spouse relief under Section 6015(f) where none existed in the statute. However, limitations existed for other forms of innocent spouse relief found in Section 6015(b) and (c). In *Lantz v. Commissioner*, initially the Tax Court determined that by not imposing a statute of limitations on relief under Section 6015(f) while imposing statute of limitations for relief under Section 6015(b) and (c), Congress had in fact spoken on the issue and decided that equitable relief would not be barred by a statute of limitations. On appeal, the Seventh Circuit held that "the fact that Congress designated a deadline in two provisions of the same statute and not in a third is not a compelling argument that Congress meant to preclude the Treasury Department from imposing a deadline applicable to cases governed by that third provision," and held that Treasury is allowed to impose a statute of limitation where one did not exist[27] In both the Tax Court's analysis and the Seventh Circuit's analysis, it was determined that imposing a time restriction in one area of a Code section but not another in meant that the other areas of the Code section were not bound by the time restriction. Thus, under a similar analysis, the time restriction in Section 6213(a) would not be applicable to Section 6213(b), and the IRS may assess a deficiency using its math error authority whenever it may choose.

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However, it should be noted that *Lantz* involved a Treasury Regulation. The level of standard of review that Treasury Regulations are examined under is called *Chevron* deference.[28] Under *Chevron* deference, courts will uphold a regulation issued by an agency upon finding that Congress has not directly addressed the issue and that the regulation is a permissible construction of the statute, i.e. not arbitrary or capricious.[29] Here, the IRS is issuing its interpretation of Section 6213(b) in a PMTA without going through the notice-and-comment procedure that most regulations are subjected to. Therefore, a court may conclude the PMTA is more like a Revenue Ruling or Revenue Procedure. As such, the PMTA is entitled to a lesser standard of review called *Skidmore* deference, also known as the "Power to Persuade" deference.[30] The level of deference under *Skidmore* given to an agency's interpretation is determined by "the thoroughness evident in its consideration, the validity of its reasoning, its consistency with earlier and later pronouncements, and all those factors which give it power to persuade."[31] If a court determines that the IRS interpretation of Section 6213(b) is entitled to *Skidmore* deference, it is possible that the court will find that Congress did not intend to extend math error authority to post-processed returns or that the PMTA's analysis is otherwise incorrect. In addition, *Lantz* involved time restrictions on taxpayers requesting relief from joint and several liability of a tax while the PMTA involves a restriction on the IRS' ability to assess a tax.

However, if the refundable credits are found to be analogous to welfare benefits, the Taxpayer Advocate's argument that only a pre-deprivation hearing satisfies Due Process bears significant weight. Under normal circumstances, the IRS would be correct that the sending of the notice and the taxpayer's ability to request a mandatory abatement would constitute sufficient Due Process. However, the refundable credits, especially the EITC, are primarily used by low-income taxpayers who will have issues navigating the byzantine math error notice, also known as a Notice CP11. As noted above, the Taxpayer Advocate has presented evidence that the majority of reversible math error determinations are ignored by taxpayers.

For example, the notice contains "Amount due" in large, bold letters on the front page. In the section on the front page entitled "What you need to do immediately," the notice states that if the taxpayer agrees with the changes then the taxpayer needs to pay the full amount by the due date and includes a payment stub. It is not until the second page that the taxpayer is informed of his or her right to request an abatement in writing; additionally, it is not until page four that the notice lays out the changes to the taxpayer's return. Finally, the remaining three pages of the notice contain boilerplate about penalties, interest, and payment options. In short,

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the notice is not immediately decipherable, and it is likely to be ignored or misunderstood by low-income taxpayers.

In its 2018 Annual Report to Congress, the Taxpayer Advocate reported that the IRS has used its post-processing math error authority to reverse refundable credits on 17,691 returns, with the IRS improperly reversing 289 of the refunded credits.[32] Given the IRS' failure of self-restraint in its use of its newfound math error authority, it is likely that the legality of post-processed math error authority will be the subject of Tax Court litigation. Also, given the potentially low standard of review and Due Process concerns raised by the Taxpayer Advocate, the outcome is anything but certain. Regardless of the Tax Court's holding, hopefully the IRS will rethink its position and implement procedures that prevent incorrectly issued refundable credits while protecting the rights of vulnerable taxpayers.

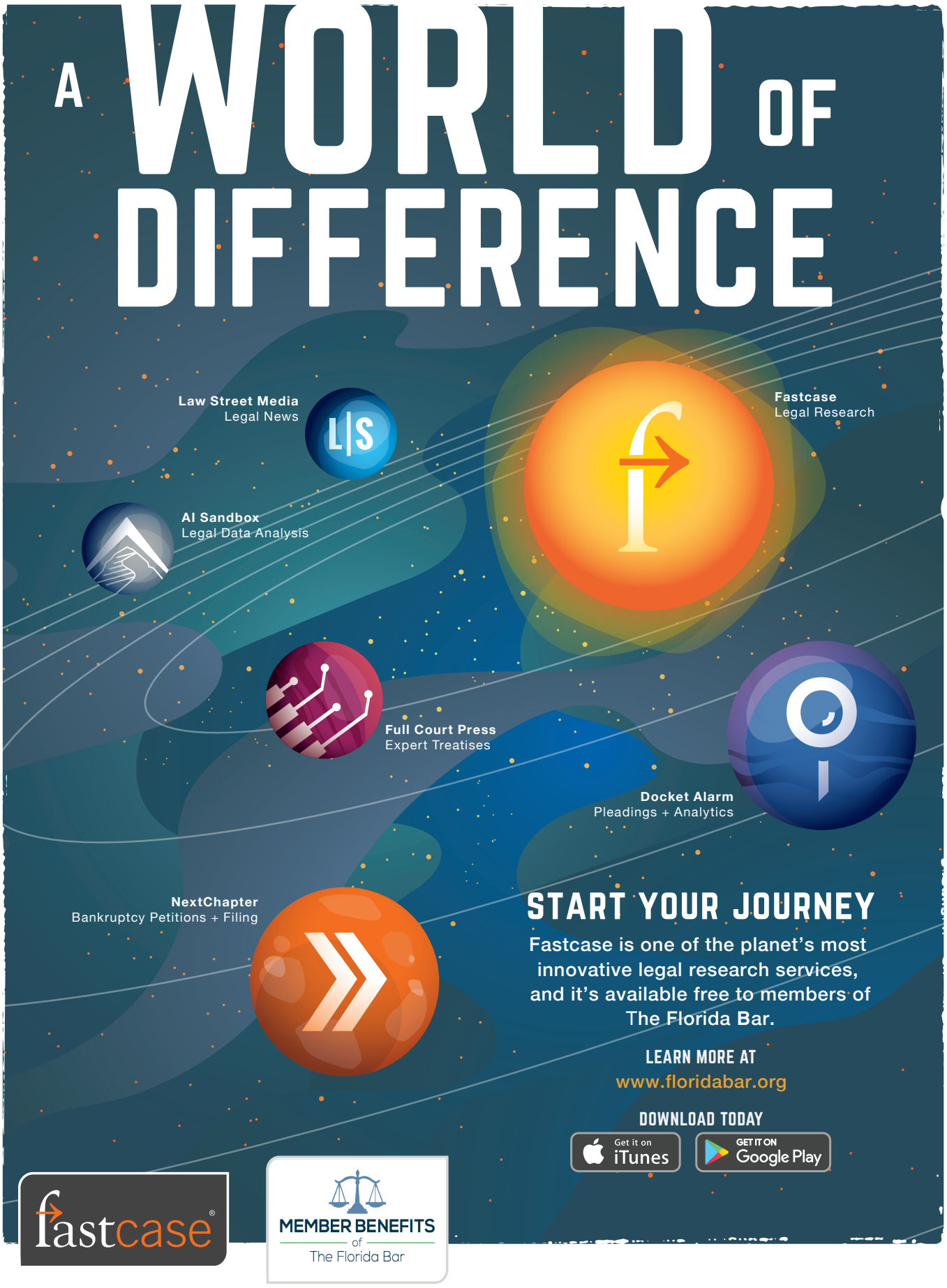
About the author:

Anthony M. Cognasi is a Candidate for LL.M. in Taxation 2020 from the University of Florida Levin College of Law.

Endnotes:

1. A low-income taxpayer has an income below 250% of the Federal Poverty Level. Therefore, a taxpayer with a household of four and an income below $64,375 would qualify as a low-income.
2. §§ 6501, 6213. Unless otherwise indicated, all section references are to the Internal Revenue Code.
3. § 6213(a).
4. § 6213(b)(1).
5. § 6213(b)(2).
6. *Id.*
7. Pub.L. 94–455.
8. Program Manager Technical Advice (PMTA), POSTS 129453-17, 2 (April 10, 2018).
9. § 6213(g)(2).
10. Pub. L. 115-113.
11. §§ 32(m), 24(e), 25(i)(6).
12. TIGTA Report 2017-40-042, 5 (July 27, 2017).
13. PMTA, POSTS 129453-17, 3.
14. *Id.*, at 4.
15. *Id.*, at 4,6.
16. *Id.*, at 5.
17. *Id.*
18. *Id.*, at 5,6.
19. This was the holding of the Supreme Court in *Goldberg v. Kelly*, 397 U.S. 254 (1970). However, it should be noted that this is the only Supreme Court case holding that a judicial style hearing is required pre-deprivation. *Mathews v. Eldridge*, 424 U.S. 319, 333 (1976).
20. *Mathews*, 424 U.S. 319 (1976).
21. *Id.* at 335.
22. Nina Olsen, *The IRS Might Recover EITC Using Its Newly Discovered Post-Processing Math Error Authority, but Is It Constitutional?*, NTA BLOG, Sept. 13, 2018 (https://taxpayeradvocate.irs.gov/news/nta-blog-the-irs-might-recover-eitc-using-its-newly-discovered-post-processing-math-error-authority-but-is-it-constitutional).
23. National Taxpayer Advocate 2011 Annual Report to Congress, Volume 2, 117 (Dec. 31, 2011).
24. *Id.*, at 139 n. 75.
25. *Id.*, at 139.
26 Nina Olsen, *The IRS Might Recover EITC Using Its Newly Discovered Post-Processing Math Error Authority*, NTA BLOG.
27. 607 F.3d 479, 482 (7th Cir. 2010).
28. Chevron, U.S.A., Inc. v. NRDC, Inc., 467 U.S. 837 (1984).
29. Chevron, 467 U.S. at 843.
30. Skidmore v. Swift & Co., 323 U.S. 134 (1944).
31. *Id.* at 140.
32. National Taxpayer Advocate, 2018 ANNUAL REPORT TO CONGRESS, 165 (February 2019).




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