

**AICPA
National Tax Conference**

**Year In Review
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62 – Accountable Plans

Chief Counsel Advice 200745018

Facts

- Auto dealer “rents” tools owned by mechanics
- Maintains records of specific tools and rental value
- Saving payroll taxes

Issue

- Does this avoid payroll taxes for the auto dealer and the mechanic?
-

Conclusion

- No – does not qualify as an accountable plan
 - Fails substantiation
 - Plan does not require the return of excess payments
 - Therefore does not qualify as an “accountable plan” under 1.62-2(e) and (f)

67(e) – Trust Advisory Fees

Sauce for the Goose is Sauce for the Gander
Knight Sup Ct. 2008 (aka Rudkin Trust) afmg
Tax Court and 2nd Cir.

Facts

- 67(a) generally provides that investment advisory fees are subject to 2% AGI limitation
- 67(e) generally provides that, for trusts and estates, administrative costs are a deduction in computing gross income

Issue

- Does (a) or (e) apply for investment advisory fees incurred by a trust?

Arguments

- Knight - professional advice necessary given the fiduciary responsibilities of trustees.
 - That was purpose of 67(e) that provides exception for trusts
- IRS
 - Investment advisory fees common among individual taxpayers and there should not be a different treatment for trusts

Decision (unanimous)

- Same type of fees incurred by an individual and therefore should be treated the same
- Left door open if adviser imposed special charge on fiduciary accounts

Note

- IRS Proposed Regulations 128224-06 provides guidance
 - Costs incurred by a trust avoid the 2% AGI limitation only if the costs could not be incurred by an individual
 - AICPA has protested this as overly restrictive
- AM 20070010 states that 67(e) applies to a bankruptcy estate
 - But presumably still has to pass the "but for" test discussed above in connection with the Rudkin Trust

67(a) – 2% AGI Limitation as Applied to Trusts

Notice 2008-32

- For years beginning before Jan 1, 2008 trusts and estates will not have to "unbundle" a fiduciary fee into portions that are subject to the 2% AGI limitation and those that are not
- Stay tuned for regs that will apply to years beginning in 2008

67 – Miscellaneous Itemized Deductions for Trusts

Notice 2008-32

Interim guidance "bundled expenses"

- Not necessary to break out amounts that are subject to the 2 percent floor from those that are not.
- Full amount can be deducted without regard to the section 67 floor
- Effective date – TYBB January 1, 2008

83 – Compensation in Form of Property

Home Run for the IRS?

- Matt Murphy, the college student who caught Barry Bonds' 756th home run ball told AP that part of his decision to sell the ball, estimated to be worth at least \$500,000, was that he couldn't afford to pay the taxes
- Questions only a CPA would ask
 - Did Matt get good tax advice?
 - When is it taxable – when he catches it or when he sells it?
 - At what rate is it taxable
 - Ordinary income 35%
 - Capital gains – 15% or 28%?

121 – Primary Residence Exclusion

PLR 200820016

Facts

- Daughter subject to teasing on school bus

Issue

- Did this constitute an “unforeseen circumstance” permitting a proportionate exclusion under IRC 121?

Conclusion

- Yes

162(l) – Health Insurance for Self-Employed

Here's to Your Health Shareholders

Notice 2008-1

- Applies to
 - 2% shareholder-employee of an S corporation
 - Where policy held in individual's name
- Permits 100% deduction above the line if:
 - Premiums are paid by S corp or
 - S corp reimburses shareholder-employee for premiums
 - In either case the premium amount must be included in shareholder-employee W-2
- Potential Refund opportunity
 - Notice retroactively effective

163(d) – Investment Interest Deduction

Rev Rul 2008-12

Facts

- Partnership trade or business of investments therefore interest it paid was trade or business interest
- Individual was limited partner

Issue

- Does the interest passed thorough to the partner retain its character as trade or business interest?

Conclusion

- No – The limited partner was not materially active and therefore the activity of the partnership does not carryover to him
- Note – test of material activity under 469 – see 163(d)(5)(A)(ii)

168(k) – Depreciation

Stimulus Act

- Additional write off of 50% of new property (generally) other than buildings
- Then get MACRS computed on remaining basis
- No ATM adjustment
- Automatic unless elect out

- Effective date
 - Property placed in service after 12/31/07
 - 12/31/09 for certain longer life assets (MACRS life >10 yrs etc)

179 – Expensing

Stimulus Act

- Most taxpayers (but not trust, estate and noncorp lessors)
- Can write off up to \$250,000
 - Tangible personal property
 - Phased out between \$800,000 and \$1,050,000
 - No ATM adjustment
- Limited to taxable income from trade or business – excess carried over
- Effective
 - Assets acquired in the tax year beginning after 12.31.07

195 – Start-Up Costs

Regs. 1.195-1 and -11, 1.248-1 and -11

Eliminates need for formal election
Effective for expenses paid or incurred after 9/6/08

Generally

- First \$5,000 deducted in first year
 - Reduced by any excess over \$50,000
- Remainder amortized over 15 years (180 months)

213 – Medical Expenses

Rev Rul 2007-72

- Allowable medical expenses include self-initiated diagnostic test such as an annual physical or self-administered pregnancy test kit
- Not necessary to have symptoms or to be done by direction of a doctor

223 – Health Savings Accounts

Notice 2008-59

40 Q and A's

- Who is eligible
- How to establish
- Taking tax-free distribution
- Prohibited transactions
- Etc.

274(n) – 50% Meal Deduction

Rev Rul 2008-23

Facts

- Leasing company
 - leases trucks and drivers to trucking company
 - Reimburses drivers for meals and incidental expenses

Issue

- Which company is subject to the 50% limitation on meals, the leasing company or the trucking company?

Rev Rul 2008-23

Conclusion

- The trucking company
 - Leasing company substantiated these expenses to the trucking company
 - Trucking company ultimately bore the expense
- Note – in effect the IRS is acquiescing to Transport Labor Contract/Leasing 8th Cir. 2006 rev'g 123 TC 154

280F – Listed Property

Hold the Phone!

INFO 2007-0030

- Where employers provide employees with cell phones, the employers should require employees to keep records of personal calls and include the value of the calls in the employee's W-2.

Note

- Senators Kerry and Ensign have introduced S. 2668 that would remove cell phones from "listed property" under 280F

401 – Minimum Distributions IRA

PLR 200811028

Facts

- Nonspouse inherited IRA
- Nonspouse wanted distributions over her lifetime
- But missed requirement that first distribution be done within 1 yr of death

Issue

- Can nonspouse beneficiary still elect payments over lifetime?

PLR 200811028

Conclusion

- Yes if
 - She makes up the required minimum distributions (5 yrs in ruling) and
 - Pays a penalty excise tax
- Note – without the relief she would have had to accept a 5-yr payout

408 – Economic Stimulus Payments

IRS Ann 2008-44

- Stimulus payments were made as directed on 2007 form 1040
- As a result some were direct deposited to IRA accounts, HSAs, etc.
- If that resulted in an excess contribution, IRS has provided process to correct with a tax-free and penalty-free withdrawal.

Housing and Economic Recovery Tax Act of 2008

Housing provisions

- Refundable credit of lesser of \$7,500 or 10% cost for
 - First home
 - If purchased after 4/9/08 and before 7/1/09
 - Phases out as AGI exceeds \$150,000
 - Must be repaid over 15 years but no interest

Housing provisions

- Standard deduction for property taxes
 - Limited to \$1,000 jt filers
- Apportionment of IRC 121 exclusion if residence sold was not always principal residence
- Permits for AMT
 - Interest on tax exempt housing bonds
 - Low income housing credit
 - Rehab credit
- Increases scope of low-income housing credit
- Election to accelerate AMT and R&D credits in lieu of 50% bonus depreciation

Housing provisions

- Revenue raisers
 - Delay until 2011 worldwide interest allocation
 - Beginning in 2011 credit card companies will report aggregate of transactions processed for each business

409A Deferred Comp

Notice 2007-100
Provides transition relief and guidance on how to correct deficiencies in deferred compensation plans

451(d) – Taxable Year for Inclusion of Crop Insurance Proceeds in Income

Nelson, 130 TC No. 5

Facts

- Sugar beet farmer had historically reported 65% of sale of crop in year of harvest and 35% in year following
- 2001
 - Crops totally destroyed
 - Received \$200,000 in crop insurance in 2001

Issue

- Can farmer report insurance proceeds 65% in 2001 and 35% in 2002?

Nelson, 130 TC No. 5

Decision

- No – all \$200,000 must be reported in year received, 2001
- Note – result apparently would have been different if farmer had historically deferred at least 50% of crop proceeds to year following year of harvest Rev Rul 74-145

461 – Recurring Item Exception Applied to Payroll Taxes

Rev Proc 2008-25

Facts

- Accrual method taxpayer has policy that employees can “carryover” up to two weeks of vacation pay
- At end of year employees have “vested” in \$1mil of vacation pay

Issue

- Can taxpayer accrue a deduction for the payroll taxes related to the \$1 mil

Rev Proc 2008-25

Conclusion

- Yes
- Automatic change
- Effective tax years ending on or after 12/31/07

469 – Passive Activity Losses

Candelaria, DC Texas, 10/5/07

Facts

- Group of doctors formed two partnerships
 1. Radiological medical practice
 2. Ownership of imaging equipment rented to partnership #1
- Imaging equipment partnership reported losses

Issue

- Were the losses of the imaging equipment partnership suspended as passive losses?

Candelaria, DC Texas, 10/5/07

Decision

- Losses not suspended
 - Reg. 1.469-4(d) provides that taxpayers can combine rental losses with trade or business income if:
 1. the two are an appropriate economic unit and
 2. The rental activity is insubstantial relative to the trade or business activity

664 – Charitable Remainder Trusts

Rev Rul 2008-41

Facts

- H & W each beneficiaries of CRT
- H & W divorce
- Trust is split between them

Issue

- Does the split of the trust cause:
 - Trust to fail CRT requirements?
 - Treatment as sale or exchange
 - The trust to be subject to excise tax under 507(c)
 - Constitute an act of self dealing

664 – Charitable Remainder Trusts

Rev Rul 2008-41

IRS position

- No to all the questions above

691 – Income in Respect of a Decedent

PLR 200744001

Facts

- Decedent negotiated for sale of property
- Sale held up until after death when gas pipe line discovered under ground
- Negotiations with gas pipeline for easement continued after death

Issue

- Was gain from sale of property income in respect of a decedent?

Conclusion

- No – the contingency regarding the easement was sufficient to have prevented the sale from closing

911 – Excludable Wages

Get Out the Globe

Gary C. Winslow v. Cir; TCM 2008-43

- Antarctica is not a foreign country
- wages earned while working there not excludable under section 911

1031 – Like-Kind-Exchange

Rev Proc 2008-10

Question

- When does a secondary home qualifies for a 1031 exchange?

Answer

- Must be owned for 24 months prior to exchange
- For each of the two 12 month periods prior to the sale
 - Must be rented at fair value at least 14 days
 - Personal used must be less than 14 days or 10% of the number of days rented

1031 – Like-Kind-Exchange

PLR 200730002

Facts

- Taxpayer, his brother and a trust for his niece owned equal shares of two parcels of land, A and B
- The value of B was approximately twice that of A
- Taxpayer wanted to continue to own A
- Brother and Trust wanted to cash out
- They received an offer to buy property B

Issue

- Will the transaction qualify under 1031 if Taxpayer exchanges his 1/3 interest in B in exchange for the 1/3 interest of his Brother and the Trust in A and A is sold within 2 years of the exchange

Conclusion

- Neither the exchange nor the subsequent sale had the principal purpose of avoidance of tax

1031 – Tax Free Exchanges

Regs 1.1031(k)-1, 1.7872-5 and 1.4688-6

Issue

- How to treat income earned on funds deposited with exchange facilitator while awaiting completion of exchange

Regs 1.1031(k)-1, 1.7872-5 and 1.4688-6

Generally

- Treat funds as demand loan from taxpayer to facilitator
- 7872 regs provide an exemption if funds are less than \$2 mil and held for less than 6 months

Alternative

- Income of taxpayer if terms of agreement with facilitator provide that all earnings are paid to taxpayer

Effective date

- Generally transfers after Oct 8, 2008

1091 – Wash Sale Rule

Rev Rul 2008-5

Facts

- Taxpayer sells stock at a loss
- Less than 30 days later, taxpayer acquires same stock in taxpayer's IRA

Issue

- Does the loss sale rule apply to disallow the loss on the taxpayer's individual return?

Conclusion

- Yes. Although taxpayer did not personally reacquire the stock, he did cause the IRA trust over which he had complete control to acquire the stock.
- Ruling cites Security First National Banks of Los Angeles 28 BT 289 – 1933

1368 – Accumulated Adjustments Account

Rev Rul 2008-42

- Premiums paid on life insurance on an employee owned by S corp do not reduce AAA
- Proceeds received by S corp upon death of the employee do not increase AAA

3121 – Employment Taxes

ILM 200823001

- Retired employees fully vested in deferred compensation
 - Therefore FICA taxes paid on present value of amount to be received
- Employer went bankrupt and deferred comp not paid

Issue

- Is employee entitled to a refund of FICA paid on amounts never received?

6111 – Reportable Transactions

Prop Reg 1.6011-4, Prop Reg 301.6111-3

- Proposals would add tax patents as a new category of reportable transactions
- Note AICPA opposed to tax patents
 - Major legislative initiative underway
 - HR 1908 would outlaw tax patents
 - HR 2365 would make them unenforceable
 - S 2369 would outlaw patents
- Note – recent court decisions have questioned whether “business methods” are patentable
 - Comiskey Fed Cir 2007
 - Bilski

Concerns of AICPA

- Limit ability of taxpayers to comply with the law
- Misdlead taxpayers into thinking the idea is valid under tax law has approved the idea behind the patent
- Will increase costs to taxpayers

6031(b) – Partnership Extensions

IR 2008-84

- Limits to 5 months the extensions for partnership and trust returns.

6694 – Preparer Penalties

Notice 2008-13

- To avoid imposition of the penalty, generally 6694 requires that the preparer disclose any position that does not meet the more-likely-than-not standard
- The notice generally provides that disclosure is adequate if the preparer discusses the issue with the taxpayer and documents the discussion in the files.

GAO Report on Medicare Providers

6/13/08 report states over 27,000 Medicare providers had federal debts, primarily payroll taxes, exceeding \$2 bill for 2006.

Economic Stimulus Act of 2008

Rebates to Individuals

- Must file a 2007 return but
- Single: \$300 (with minimum income of \$3,000) to \$600 or tax liability, whichever is lower
- MFJ: \$600 to \$1,200
- Plus: Children under age 17: \$300 each
- 5% phase-out starts at AGI = \$75,000 SINGLE / \$150,000 MFJ
- 2008 return will be compared to 2007 and additional rebates paid where applicable

Economic Stimulus Act of 2008

- \$250,000 §179 expensing allowance
 - Phaseout starts at \$800,000
- 50% 1st year bonus depreciation – Applies to Section 1245 Property (Business Personal Property)
- Regular MACRS depreciation allowed after 179 and 50% first year

Mortgage Forgiveness

- Effective retroactive to 1/1/07
- Not applicable to Home Equity loans or refinanced proceeds not used to improve property and / or payoff prior housing debt
- Applies only to Cancelled Debt – IRC 108 can be used alternatively

AMT Patch

- 2008 adjustment already introduced in Congress:
 - Expected Exemptions:
 - SINGLE – around \$46,000 up from \$44,350 for 2007
 - MFJ – around \$70,000 up from \$66,250 for 2007

Tax Changes Beginning in 2008

- Kiddie tax expanded to children under 19 (24 for students)
- 0% capital gain for Taxable Income under \$32,050 (Single) and \$65,100 (MFJ)
- 2 year use of \$500,000 home exclusion for surviving spouse – Can be used IN ADDITION to step in basis for surviving spouse

Tax Changes Beginning in 2008

- Phase-out of itemized deduction starts @ AGI of \$159,950
Only 1% for 2008 & 2009
- Minimum personal exemption of \$2,333 (two thirds of \$3,500)
All taxpayers (even Bill Gates) get \$2,333 for 2008

Tax Changes Beginning in 2008

- Money from any retirement plan can be rolled into ROTH IRA – no longer necessary to move money twice
- Special planning device to consider – put money into non-deductible IRA for 2008 and 2009 and rollover in 2010 when \$100,000 AGI maximum is removed – added advantage of reporting half of any taxable rollover in 2010 and half in 2011

Provisions Expiring in 2008

- \$500 personal residence energy credit
- AMT exemption
- AMT reduction for nonrefundable credits
- Research and experiment credit
- \$250 school teacher deduction
- Sales tax deduction
- 15-yr life leasehold/restaurant improvements
- Tuition deduction
- IRA transfer to charity – Be careful with advice on this one

Health Savings Accounts

- Better than ever
- HSA can and will lower medical care costs
 - Requires education, analysis and risk
- Two components of HSA
 - High-deductible health insurance plan (HDHP)
 - Health savings account (HSA)

HSA Tax Advantages

- 1. Deductible contributions for employer and employee
- 2. Withdrawals not taxable if used for medical purposes
- 3. Earnings are tax-exempt
- 4. Rollover of year-end balance – no "use or lose it"
- 5. Can accumulate as a supplemental retirement plan – taxed like an IRA
