

**COMMENTS CONCERNING THE IDENTIFICATION OF POTENTIAL INCREASED
THRESHOLDS AND “SAFE HARBORS”**

The following comments are the individual views of the members of the Section of Taxation who prepared them and do not represent the position of the American Bar Association or of the Section of Taxation.

Principal responsibility was exercised by Samuel L. Braunstein, IRS Small Business/Self Employed Division Coordinator of the Section of Taxation. Substantive contributions were made by Steven R. Schneider and John O. Tannenbaum. The Comments were reviewed by Paul L. Basile, Jr. of the Section’s Committee on Government Submissions.

Although many of the members of the Section of Taxation who participated in preparing these Comments have clients who would be affected by the federal tax principles addressed by these Comments or have advised clients on the application of such principles, no such member (or the firm or organization to which such member belongs) has been engaged by a client to make a government submission with respect to, or otherwise to influence the development or outcome of, the specific subject matter of these Comments.

Contact Person:

Samuel L. Braunstein
Telephone: (203) 254-1118
E-mail: sam@btlawfirm.com

Date: September 2, 2004

EXECUTIVE SUMMARY

1. Summary of the recommendation(s).

The recommendations, if implemented, will simplify tax and information return and extension filing requirements; simplify procedures under which taxpayers make elections, disclosures and notifications; eliminate various duplicative tax reporting forms; provide for additional “safe harbors” in filing, form completion and ancillary matters; and increase the threshold amounts in various areas to reduce required taxpayer form completion and ancillary governmental administrative burden.

2. Summary of the issues which the recommendations address.

The recommendations address two areas which are current major areas of focus of the Office of Taxpayer Burden Reduction: (1) simplifying forms and publications and (2) streamlining internal (IRS) policies and procedures.

3. Please explain how the proposed recommendations will address the issues.

The recommendations provide substantive methods for tax administration simplification and reduction in both taxpayer and government compliance burden. The recommendations contemplate the reduction of taxpayer and government burden, the simplification of the administration of the federal tax laws and address various issues which fall within the purview of the Office of Taxpayer Burden Reduction (OTBR), within the Taxpayer Education and Communications Operating Unit (TEC) of the Small Business/Self Employed Division (SB/SE) of the IRS, which has been charged with the responsibility of: (1) simplifying forms and publications; (2) streamlining internal (IRS) policies and procedures; (3) promoting less burdensome legislation; and (4) developing a more accurate burden measurement methodology.

4. Summary of any minority views or opposition which have been identified.

No known minority views or opposition.

Background

The IRS established the Office of Taxpayer Burden Reduction (OTBR), within the Taxpayer Education and Communications Operating Unit (TEC) of SB/SE, in January 2002. The OTBR works through the Taxpayer Burden Reduction Council (TBRC), a body composed of executives from Treasury, the Office of Chief Counsel, the Taxpayer Advocacy Service, and all IRS Operating Divisions, to identify, develop and implement service-wide, cross-functional initiatives, offering the greatest potential to reduce taxpayer burden.

OTBR's current major areas of focus include: (1) simplifying forms and publications; (2) streamlining internal (IRS) policies and procedures; (3) promoting less burdensome legislation; and (4) developing a more accurate burden measurement methodology.

Over the past year, OTBR has reviewed the Code and Regulations in an attempt to identify thresholds which are within the Commissioner's discretion to increase, where an increase would not involve significant revenue loss and would not promote noncompliance. According to OTBR, very few thresholds were identified which met those criteria. Of those that did, further stratification was made among those thresholds to differentiate those that require regulatory change and those that do not; those that would affect large segments of the taxpaying public and those that would not; and those where an increase could significantly reduce burden and those that would not.

During OTBR's review, it became obvious that the approach of using the Code and Regulations to identify thresholds would not capture all of the thresholds which currently exist in Revenue Rulings, Revenue Procedures, Forms, and other administrative pronouncements. Nor would it, more importantly, provide the opportunity to create thresholds where none previously existed. Accordingly, OTBR determined that focusing its attention on the latter offered the best prospects for meaningful burden reduction.

On June 23, 2004, the ABA Section of Taxation was requested to submit recommendations to the Small Business/Self Employed Division for identifying potential specific areas where establishment of additional "safe harbors", revising threshold amounts and simplification in other areas might further assist in reduction of taxpayer and governmental burden. Accordingly, the following recommendations of the individual members of the ABA Section of Taxation who prepared them are presented for consideration:

Simplify tax and information return and extension filing requirements.

1. Problem identified: extensions to file partnership returns are required to be "paper", which requires additional taxpayer and governmental burden for preparation, transmittal, review and input into the system.

Recommendation: allow paperless (e-file) partnership extensions.

Rationale: with partnerships allowed to e-file, and required to do so when there are 100 or more partners in the affected partnership, it takes less effort to file extensions electronically than to file on paper.

2. Problem identified: initial extensions for partnership returns should be for a longer duration.

Recommendation: the initial extension for partnership returns should be a single 6-month extension.

Rationale: as partnerships are allowed only a 3-month automatic extension with the first extension request; many frequently have to request a second extension for another 3 months; although that second extension is not automatic but is rarely ever denied, it requires additional monitoring, preparation, transmittal, review and input into the system; all other business entities are allowed 6 months automatically with first extension request.

3. Problem identified: extensions for filing of forms ancillary to primary forms do not correspond to those for the primary forms.

Recommendation: extensions for qualifying forms (such as Forms 8804 and 8805) should be the same as those for the primary forms (such as partnership returns).

Rationale: making extensions consistent for related forms would make tracking extensions simpler as well as require less monitoring, preparation, transmittal, review and input into the system.

Simplify procedures whereunder taxpayers make elections, disclosures and notifications.

1. Problem identified: a common error, checking the wrong box, occurs when completing Form 8832, Entity Classification Election, which relates to the default classifications of certain check-the-box elections.

Recommendation: Form 8832 should be modified to clarify election status; for example, if disregarded status is checked, partnership status would apply only if there were two or more members.

Rationale: Form 8832, for check-the-box elections, requires one to “check” for either disregarded entity status or partnership status if flow-thru treatment is desired. The wrong box is often checked.

2. Problem identified: there are many elections required to be made by taxpayers which require the preparation and submission of multiple forms.

Recommendation: for elections, such as accounting methods and other common elections, use a “check-the-box” type of form.

Rationale: by adopting a common election form, the taxpayer is relieved of the burden of creating and the IRS of the burden of tracking multiple election forms, similar to IRS adding a checkbox on Form 1120 to elect out of the NOL carryback provisions.

3. Problem identified: separate signatures are required on supplementary forms filed with the primary return/form.

Recommendation: eliminate the multiple signature requirements on supplementary forms filed with primary returns/forms.

Rationale: signature requirements on other forms (such as statements and elections) should be satisfied by the signature on the primary return/form, which should require that the signature be “under penalties of perjury”. Such would relieve the taxpayer of the burden of multiple execution compliance requirements as well as require less monitoring, preparation, transmittal, review and input into the system.

Eliminate various duplicative tax reporting forms.

Problem identified: the information required on Form 1122, Authorization and Consent of Subsidiary Corporation To Be Included in a Consolidated Income Tax Return, is included on Form 851, Affiliations Schedule, both of which are filed with the same consolidated return.

Recommendation: eliminate the requirement to file Form 1122 in a consolidated return and incorporate the Form 1122 consent in Form 851.

Rationale: inasmuch as the same essential information is found on Form 851 as is contained on Form 1122, both required to be filed as part of a consolidated return, the Form 1122 can be eliminated as a requirement. Additionally, the need to have a qualified officer of the company sign multiple pages of Form 851 and also multiple copies of form 1122 for subsidiaries to elect to file a consolidated return with their parent when the subsidiaries have been included in the Form 851 is duplicative. Such would relieve the taxpayer of the burden of multiple preparation requirements of the same essential information as well as require less monitoring, preparation, transmittal, review and input into the system.

Provide for additional “safe harbors” in filing, form completion and ancillary matters.

1. Problem identified: various foreign jurisdictions mandate a second non-economic owner to comply with local legal requirements.

Recommendation: establish a safe-harbor de minimis rule to eliminate nominal partners from being classified as partners for federal tax purposes.

Rationale: In many foreign jurisdictions, a second non-economic owner is needed for local law requirements; however, this local “legal owner” may have no share of profits and/or losses and may only have a nominal capital contribution. Clarifying that such nominal partners could be ignored would reduce the burden of filing partnership returns for entities where a nominal partner is the only other member in the entity.

Increase the threshold amounts in various areas to reduce required taxpayer form completion and ancillary governmental administrative burden.

1. Problem identified: Offers in Compromise involving compromised amounts of \$50,000 or more require approval of the Office of the Chief Counsel.

Recommendation: The threshold amount should be increased in an Offer in Compromise before approval of the Office of the Chief Counsel is required to at least \$100,000 and possibly as high as \$250,000.

Rationale: Offers in Compromise require Chief Counsel approval (i.e., a determination that the offer is legally sufficient) if the amount being compromised is \$50,000 or more. In view of the fact that the Commissioner's office has jurisdiction to settle and dispose of cases for amounts far in excess of \$50,000, it would seem appropriate to increase this threshold. Such would substantially reduce the burden on the Office of the Chief Counsel in appropriate cases.

2. Problem identified: several partnership items are required to be tracked and separately treated without regard to size.

Recommendation: establish safe-harbor de minimis rules to reduce taxpayer burden compliance requirements.

Rationale: there are various situations relating to the recognition of the gain or loss limitation rules which require affected entities to maintain records regardless of the size of the entity or the item in question. For example, a threshold could be established as being the lesser of some amount (e.g., \$25,000 or 2% of the value of the partnership) with respect to the following items: (1) an exception to tracking IRC Section 704(c)(1)(A) built-in gains or losses under the threshold; (2) an exception to computing a Section 751(b) “hot asset” deemed exchange where the total hot assets in the entity are below the threshold; (3) an allowance to immediately expense Section 195 or Section 709 organizational and start up expenses under the threshold; or (4) a de minimis threshold for reporting Section 465 at risk limitations. Such would address a compliance burden for smaller taxpayers who are currently required to track and separately treat these items, regardless of size.

3. Problem identified: the requirements for the inclusion of supporting documentation when filing Form 706 apply without regard to the size of the estate.

Recommendation: The amount of information and supporting documentation required to be filed with Form 706 in nominal taxable estate situations should be reduced.

Rationale: Treas. Reg. Sections 20.6018-3 and -4 require that certain information be submitted with the estate tax return. Submission of supporting documentation is optional under Reg. 20.6018-4(a). Many estates barely exceed the filing threshold. Furthermore, a significant number of estates are not taxable because of the unlimited marital deduction. Accordingly, for example, there is little reason to provide a complete property description (other than the street address) for a primary or seasonal personal residence which is passing to the surviving spouse; there is no reason for the inclusion of a Form 712 with the return where the recipient of those proceeds is the surviving spouse; a gross estate may exceed the filing threshold, but the taxable estate may be less than the unified credit equivalency amount due to expenses of administration or debts and claims. Completing such returns is time-consuming and costly for the estate and beneficiaries. A higher threshold should be established which, only when it is exceeded, is the full panoply of data required to be submitted. Also, with such smaller estates, the submission of supporting data with the return should be discouraged.