Hot Topics for Closely Held Businesses

Friday, January 31, 2020
ABA Tax Section Meeting: Boca Raton, FL


1. BBA Opt-Out

- Section 6221 provides a mechanism for partnerships with fewer than 100 partners to opt out of BBA.
  - The partnership must be required to furnish fewer than 100 K-1s.
  - The partnership may not be a second-tier or below partnership. Only partnerships with partners who individuals, a C corporation, any foreign entity that would be treated as a C corporation were it domestic, an S corporation, or an estate of a deceased partner are eligible.
- Regulations promulgated in late 2017 make clear that partnerships with partners who are themselves partnerships, trusts, disregarded entities, foreign corporations that would not be treated as C corps, estates other than those of deceased partners, and “[a]ny person that holds an interest in the partnership on behalf of another person” are not eligible. Treas. Reg. 301.6221(b)-1.
- The regulations further clarify that opt-out elections bind the partnership and all partners unless the IRS finds that the election is invalid.
- Under TEFRA, partners were entitled to notice regarding various IRS proceedings and notice partners could reject a settlement agreement with the IRS.
- Under BBA, the partnership representative (PR) has the authority to bind the partnership and all partners, including with respect to statute of limitations extensions and settlements, with other partners having no notice rights.
- The broad authority of the PR under the BBA regime means that the partnership agreement is now the avenue for partners to agree on audit
matters, including opting out of BBA, the requirement to provide notice, and who is responsible for deficiencies.

2. **Boyle in the Electronic Age (abatement of a late filing penalty under 26 U.S.C. § 6651: "reasonable cause" and lack of "willful neglect,")**
   
   - The issue of *Boyle*’s applicability to electronic returns is a novel legal question that has not been addressed squarely by the federal courts.
   
   - In *Haynes v. United States*, 760 F. App’x 324, 326 (5th Cir. 2019), the Fifth Circuit noted the possibility of an exception to *Boyle* for e-filed returns but did not address the issue, remanding the case on other grounds.
   
   - In *Intress v. United States*, 3:18-cv-00851 (D. Tenn. 2019), the district court rejected a married couple’s claim that they were entitled to a refund and abatement of interest and penalties for late filing of their return because their tax preparer mistakenly failed to transmit their request for a filing extension.
   
   - The National Taxpayer Advocate’s 2018 annual report to Congress.

3. **IRC Section 451(b)**
   
   - TCJA added a new income recognition provision in section 451(b), requiring taxpayers to recognize revenue for tax purposes no later than when the taxpayer recognizes the revenue for book/financial statement purposes.
   
   - The new rule applies only to taxpayers with an “applicable financial statement”.
   
   - When combined with new financial reporting standards (and the repeal of the 451-5 regulations), taxpayers may now recognize income much earlier.
   
   - Proposed regulations were released in September 2019.
   
   - They make clear that the new rule under section 451(b) applies only to accrual taxpayers, not taxpayers using a “special method of accounting”—when the Code requires income recognition in a year other than when the all-events test is satisfied.
     
     - Examples include installment sales, long-term contracts, qualified returns, prepaid subscription income, etc.
   
   - The proposed regulations also expand the list of applicable financial statements and provides rules for when a taxpayer’s financial statement year is different than its tax year.
• The Preamble also generally denies an accelerated cost offset/COGS for accelerated income (i.e., economic performance must still be satisfied before a deduction corresponding to the income inclusion is allowed), creating the potential for larger mismatches.

4. Passport Revocation Update

• The report highlights whose tax debts the IRS has targeted for passport revocation, how many have been revoked, and what has happened after the sending of the revocation.

• The new IRM guidance also provides some updates to the reversal of certification of seriously delinquent tax debt as well as expedited decertification. The expedited decertification can shorten the processing time by 2-3 weeks, but the taxpayer must meet all three of the following conditions:

  1. The taxpayer meets a condition in 5.1.12.27.8 Reversal of Certification;

  2. The taxpayer states that they have foreign travel scheduled within 45 days and can provide proof of travel OR the taxpayer lives outside of the US; and

  3. The taxpayer has a pending application for a passport or renewal, has received notification their passport was denied or revoked, and provides a denial letter from the State Department (read: not the CP508-C).

• The updates to the IRM made proof of travel necessary in 2. and a copy of the State Department denial letter necessary in 3.

• There is an exception for taxpayers residing out of the United States who do not have imminent travel plans. If the taxpayer meets the conditions outlined in IRM 5.1.12.27.3 or IRM 5.1.12.27.4 and expresses an urgent need for decertification the IRS is supposed to request expedited decertification.

• According to a recent memo from Acting Taxpayer Advocate Bridget Roberts (TAS-13-0819-0014), effective July 25, 2019, all open TAS cases with a certified taxpayer will be decertified and new TAS taxpayer cases will also be systemically decertified until further notice. This is something for which former NTA Nina Olson advocated prior to leaving office this year.

5. Final regs. loosen 401(k) hardship distribution requirements

• Under the new regulations, a distribution is treated as necessary to satisfy an immediate and heavy financial need of an employee only to the extent that:
1. The amount of the distribution is not in excess of the amount required to satisfy the financial need (including any amounts necessary to pay any federal, state, or local income taxes or penalties reasonably anticipated to result from the distribution);

2. The employee has obtained all other currently available distributions (including distributions of ESOP dividends under Sec. 404(k), but not hardship distributions) under the plan and all other deferred compensation plans, whether qualified or nonqualified, maintained by the employer;

3. The employee has provided the plan administrator with a written representation that he or she has insufficient cash or other liquid assets reasonably available to satisfy the need; and

4. The plan administrator does not have actual knowledge that is contrary to the representation.

- The employer may rely on the employee’s representation (unless the employer has actual knowledge to the contrary) that the need cannot reasonably be relieved from other specified resources.

- The final regulations also modify the safe-harbor list of expenses in existing Regs. Sec. 1.401(k)-1(d)(3)(iii)(B) for which distributions are deemed to be made on account of an immediate and heavy financial need.

  - Due to the fact the casualty loss rules were amended by the law known as the Tax Cuts and Jobs Act, P.L.115-97, so that taxpayers only qualify for a casualty loss deduction if they are in a federally declared disaster area, the new regulations provide that only disaster-related expenses and losses of an employee who lived or worked in the disaster area will qualify for the new safe harbor, and the expenses and losses of the employee’s relatives and dependents will not, unlike under the IRS’s disaster relief provisions.