



Five-Minute Tax Briefing[®]

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Highlights

Business Travel Per Diem Rates: The IRS has released the 2019–2020 per diem rates for substantiating employee business expenses under IRC Sec. 274(d) for lodging, meals, and incidental expenses incurred while traveling away from home. The Meal and Incidental Expense (M&IE) rates for the transportation industry remain at \$66 for travel in the continental U.S. and \$71 for travel outside the continental U.S. The per diem for travel to high-cost localities has increased from \$287 to \$297 (\$71 for M&IE), while the rate for travel to other localities has increased from \$195 to \$200 (\$60 for M&IE). The incidental-expenses-only rate remains at \$5 per day. The updated rates and list of high-cost locations apply to per diem allowances paid to employees after 9/30/19. Notice 2019-55.

Court Dismisses Case on State and Local Tax Deduction Cap: Last year, New York, Connecticut, Maryland, and New Jersey filed a complaint with the U.S. District Court for the Southern District of New York seeking declaratory and injunctive relief to invalidate the State and Local Tax (SALT) deduction cap. According to the complaint, the cap violates the U.S. Constitution by interfering with the states' sovereign authority to decide whether and how much to invest in their residents, businesses, and infrastructure. Recently, the Court dismissed the case, finding that the states failed to present any constitutional principle that would bar Congress from exercising its otherwise plenary power to impose an income tax without a limitless SALT deduction. In addition, the Court held that the cap is not unconstitutionally coercive because it does not meaningfully

constrain the states' exercise of their own sovereign tax powers. *State of New York, et al.*, 124 AFTR 2d 2019-XXXX (DC NY).

IRS Discontinues Form W-2 Verification Code Pilot:The IRS has announced that it will discontinue the Form W-2 verification code pilot for the 2019 tax year. Under this voluntary program, a new verification code box and 16-digit code were added to electronic Form W-2 to help combat fraud and identity theft. Thanks to the Protecting Americans from Tax Hikes (PATH) Act of 2015, employers must submit Form W-2 by January 31 each year. This has allowed the IRS to more quickly verify Form W-2 data with information on Form 1040. Therefore, the pilot program is no longer needed. The IRS's announcement is available at www.irs.gov/individuals/w-2-verification-code .

IRS Finalizes QBI Safe Harbor for Rental Real Estate:The IRS has finalized a safe harbor under which a rental real estate enterprise will be treated as a trade or business for purposes of the Qualified Business Income (QBI) deduction under IRC Sec. 199A. The safe harbor largely follows the proposed version found in Notice 2019-7 , with minor modifications. For example, under the final version, an interest in mixed-use property may be treated as a single rental real estate enterprise or may be bifurcated into separate residential and commercial interests. In addition, recordkeeping requirements are somewhat relaxed if rental services are performed by employees or independent contractors. The safe harbor applies to tax years ending after 2017; however, taxpayers may rely on Notice 2019-7 for 2018. The contemporaneous records requirement doesn't apply to tax years beginning prior to 1/1/20. Rev. Proc. 2019-38.

Other Current Releases

Health Care—Proposed HRA Regulations Clarify Employer Shared Responsibility and Nondiscrimination Rules:The IRS has issued proposed regulations (REG-136401-18) that would clarify the application of the employer shared responsibility provisions and certain nondiscrimination rules to Health Reimbursement Arrangements (HRAs) and other account-based group health plans integrated with individual health insurance coverage or Medicare (*individual coverage HRAs*). The proposed regulations also would provide (1) affordability and minimum value safe harbors for individual coverage HRAs and (2) look-back month and location safe harbors for determining an employee's required HRA contribution for a calendar month. In addition, the proposed rules would provide that an individual coverage HRA that satisfies the age-variation exception under the same terms requirement would not be treated as failing to satisfy the requirements to provide nondiscriminatory benefits solely due to the variation based on age. The regulations are proposed to apply to periods beginning after 12/31/19. Prop. Regs. 1.105-11 and 54.4980H-5 .

IRS Releases Draft Forms 1065, 1120-S, and Schedules K-1 for 2019:The IRS has released draft versions of Form 1065 and Form 1120-S (including their Schedules K-1) for 2019. Both forms include a new checkbox that indicates whether the entity (1) aggregated activities for Section 465

at-risk purposes or (2) grouped activities for Section 469 passive activity purposes. In addition, the draft Schedule K-1 of Form 1065 requires partners to report their share of net unrecognized Section 704(c) gain or loss. Other revisions have been made to reflect changes resulting from the Tax Cuts and Jobs Act. According to the IRS, the draft forms are near-final. The drafts are intended to give software providers the information they need to update systems before final versions are released in December. The draft forms can be accessed at <https://apps.irs.gov/app/picklist/list/draftTaxForms.html> . News Release IR 2019-160 .

IRS Releases List of Extreme Drought Areas:The IRS has released its annual list of counties or parishes in which exceptional, extreme, or severe drought has been reported during the last 12 months. Farmers and ranchers who were forced to sell livestock due to drought conditions in 32 states, plus Guam, the U.S. Virgin Islands, and the Commonwealths of Puerto Rico and the Northern Mariana Islands, have an extended period in which to replace the livestock and defer tax on any gains from the forced sales. For a taxpayer who qualified under IRC Sec. 1033(e)(2)(A) for a four-year replacement period that is scheduled to expire at the end of 2019, the replacement period will be extended another year. The list may be used instead of U.S. Drought Monitor maps to determine whether an extended replacement period applies. News Release IR 2019-161 and Notice 2019-54 .

Penalties—Incarceration Isn't Reasonable Cause for Failure to File Return:The taxpayer, a former professional basketball player, was convicted of wire fraud for running a real estate Ponzi scheme. While incarcerated, he received a pension distribution of approximately \$208,000. Because the taxpayer didn't file a return for the distribution year, the IRS prepared a substitute return that claimed the standard deduction and applied interest and penalties, including the 10% penalty tax under IRC Sec. 72(t). The taxpayer questioned the substitute filing, arguing that (1) his incarceration prevented him from preparing a tax return, (2) all taxes on the pension distribution were properly withheld, and (3) paying the owed amounts would pose a hardship on him and his family. The Tax Court sided with the IRS, holding that incarceration doesn't constitute reasonable cause for failing to timely file a return. In addition, because he didn't file a return, the taxpayer wasn't entitled to any itemized deductions. *Claude T. George*, TC Memo 2019-128 (Tax Ct.).

Procedure—Faxed Copy of Return Not a Proper Filing:The IRS issued a Notice of Final Partnership Administrative Adjustment (FPAA) to the tax matters partner of an LLC taxed as a partnership. The FPAA disallowed substantial losses from a listed transaction. The LLC argued that the determinations in the FPAA were barred by the statute of limitations. The IRS disagreed, claiming that it had never received the return in question. The LLC maintained that it filed the return when it faxed a copy to the IRS revenue agent, and again when its attorney sent a copy of the return to IRS counsel. The Tax Court sided with the IRS, holding that the LLC did not submit a return to the proper place for filing (the Ogden, Utah service center). In addition, the LLC did not intend to file a return when it faxed and mailed a copy to the IRS agent and counsel, respectively. *Seaview Trading, LLC*, TC Memo 2019-122 (Tax Ct.).

Retirement Plans—IRS Issues Final Regulations on Hardship Distributions from 401(k)

Plans:The IRS has issued final regulations on hardship distributions from 401(k) plans that take into account changes from the Bipartisan Budget Act of 2018, the Tax Cuts and Jobs Act, and other acts. Among other things, the final regulations eliminate any requirement that an employee be prohibited from making elective contributions after receiving a hardship distribution, or that an employee must first take plan loans before receiving a hardship distribution. The regulations also eliminate the facts and circumstances determination of whether a distribution is necessary to satisfy a financial need. Under the final rules, a hardship distribution may not exceed the amount of an employee's need, and the employee must represent having insufficient cash or other liquid assets to satisfy the need. The final regulations are substantially similar to regulations proposed in November 2018, and plans that complied with the proposed regulations will satisfy the final regulations. TD 9875 .

Tax-exempt Organizations—Nonprofit Status Revoked for Telemarketing Activities:

A for-profit business relied heavily on telemarketing to promote sales of replacement windows and other home improvement services. Noting a decline in sales due to the National Do Not Call Registry, the company decided to form a nonprofit organization. The organization established a corporate sponsorship program that provided telemarketing opportunities for businesses (including the window company) to help generate leads and give back to charity. The IRS revoked the organization's nonprofit status, finding that the entity was not operated exclusively for exempt purposes within the meaning of IRC Sec. 501(c)(3) . The Tax Court agreed, holding that the organization was primarily engaged in generating sales leads to advance a commercial enterprise. The promised charitable donations were merely a function of the window company's success in securing business. Therefore, the entity did not qualify as an exempt organization under IRC Sec. 501(a) . *Giving Hearts, Inc.*, TC Memo 2019-94 (Tax Ct.).

TIGTA Finds Potentially Erroneous Electric Vehicle Credit Claims:

IRC Sec. 30D authorizes a credit of up to \$7,500 per vehicle for qualifying plug-in electric drive motor vehicles. In a recent report, the Treasury Inspector General for Tax Administration (TIGTA) found that the IRS does not have effective processes to identify and prevent erroneous claims for the electric vehicle credit. As a result, taxpayers have received millions of dollars in potentially erroneous credits. TIGTA made four recommendations to improve the detection and prevention of erroneous claims, all of which the IRS agreed to. They include (1) using data analytics to determine noncompliance; (2) initiating appropriate compliance activities; (3) developing a new audit lead sheet to assist IRS examiners; and (4) introducing a recovery program for potentially erroneous credits. TIGTA's full report can be accessed at www.treasury.gov/tigta/auditreports/2019reports/201930072fr.pdf .

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