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Inside this Issue

IRS Finalizes Material Advisor Regs; Eases Rescission Rules

◆ *TD 9686*

The IRS has issued final regs describing penalties where material advisors fail to file or file a false or incomplete return for reportable and/or listed transactions. The final regs generally track proposed regs issued in 2008.

■ ***CCH Take Away.*** "The final regulations provide important clarifications as to the scope and extent of the potential material advisor penalties and the factors considered by the IRS in rescinding those penalties," Mark Allison, member, Caplin & Drysdale, Chartered, New York, told CCH. "The regulations should serve as a reminder of the significant financial risks to material advisors who fail to comply with section 6707 disclosure requirements."

Background

A material advisor who provides aid, assistance or advice with respect to a reportable or listed transaction after October 22, 2004, must file an information return with the IRS. Generally, a material advisor is any person who: (1) provides any material aid, assistance, or advice with respect to organizing, managing, promoting, selling, implementing, insuring, or carrying out any reportable transaction; and (2) directly or indirectly derives gross income for the advice or assistance in excess of a threshold amount. The IRS issued proposed regs in 2008 and developed Form 8918, Material Advisor Disclosure Statement.

Code Sec. 6707(b)(1) imposes a penalty of $50,000 for failing to file an information return regarding a reportable transaction (other than a listed transaction) timely or for filing a false or incomplete return. Code Sec. 6707(b)(2) imposes a penalty for failing to timely file an information return regarding a listed transaction before the date prescribed, or for filing a false or incomplete return. The Code Sec. 6707(b)(2) penalty is the greater of 50 percent (75 percent in the case of an intentional failure) of the gross income derived from any aid, assistance, or advice provided before the date the return is filed regarding the listed transaction or $200,000.

■ ***Comment.*** A reportable transaction is any transaction with respect to which information must be included with the taxpayer's return because the IRS has determined that the transaction is of the type that has the potential for tax avoidance or evasion. A listed transaction is a reportable transaction that is the same as or substantially similar to a transaction that has been specifically identified by the IRS as a tax avoidance transaction.

Final regs

The IRS clarified in the final regs that only one penalty will apply in the case of a transaction that is both a listed transaction and a reportable transaction other than a listed transaction. The penalty that applies is the penalty for listed transactions, the IRS explained. Additionally, if there is a failure with respect to more than one reportable or listed transaction, a material advisor is subject to a separate

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Route to: ________ ________ ________ ________ ________

IRS Amends Effective Date Of Covered Asset Acquisition Regs To Limit Use Of Retroactive Elections

◆ *Notice 2014-45*

The IRS has amended the effective date of impending foreign tax credit regs to prevent taxpayers from making retroactive elections to avoid the new rules. The regs address abuses of the foreign tax credit from covered asset acquisitions (CAAs).

■ ***CCH Take Away.*** "Generally speaking, under Treas. Reg. §301.7701-3(c)(1)(iii), a check-the-box election can be made effective for an eligible entity up to 75 days prior to the date that it is filed," Joseph Calianno, partner and international technical tax practice leader, Grant Thornton LLP, Washington, D.C., told CCH."When there is a change in an entity's classification, the deemed consequences (e.g., a deemed liquidation of a corporation) generally are treated as occurring the day prior to the effective date of the election. Notice 2014-45 appears to be targeting a scenario similar to the fact pattern of example 1 in Notice 2014-44 where a check-the-box election is filed on or after July 29, 2014 (the date Notice 2014-45 was issued) to treat the foreign target as a disregarded entity but the effective date of such check-the-box election is on or before July 21, 2014. Notice 2014-45 is trying to ensure that the section 901(m) rules relating dispositions of assets contained in Notice 2014-44 apply in this scenario."

■ ***Comment.*** A "CAA" by definition involves a foreign entity.

Background

Code Sec. 901(m) reduces the foreign tax credit that can be claimed by a U.S. taxpayer engaging in a CAA. A CAA creates a disparity, under U.S. versus foreign tax law, of the basis of assets involved in the CAA. Under Code Sec. 901(m), this basis disparity is ignored, and a portion of the foreign tax credit is disallowed.

When assets involved in the CAA are disposed of, the statutory disposition rule under Code Sec. 901(m)(3)(B)(ii) allows taxpayers to claim the balance of the basis disparity and the disallowed portion of the credit. In Notice 2014-44, the IRS indicated that taxpayers were abusing the statutory disposition rule by treating certain transactions, such as a deemed liquidation, as dispositions, even though the basis disparity remained after the transaction, and no gain or loss was recognized for foreign tax purposes.

Notice 2014-44

The IRS announced that it will issue regs to prevent these transactions from being treated as dispositions. The notice provides that taxpayers cannot recover the basis disparity unless the disposition transaction is fully taxable under both U.S. and foreign law. If the disposition is not fully taxable for both U.S. and foreign taxes, the notice provides that the basis disparity continues to be subject to Code Sec. 901(m).

Example One in Notice 2014-44 describes a transaction subject to the new rules. A corporation acquires a foreign corporation in a CAA. Following the CAA, but in the same tax year, the foreign corporation elects to be a disregarded entity (DE). Taxpayers have been treating this deemed distribution as a disposition of the assets under Code Sec. 901(m). The example states that the deemed distribution is not a disposition, and that the CAA rules continue to apply.

Effective dates

Under Reg. §1.301-7701-3(c), an entity can choose its classification or elect to change its classification. The election can be retroactive. Thus, a corporation electing to become a DE can backdate the election. The deemed liquidation and the deemed

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Material Advisors

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penalty for each transaction. The final regs also clarify that only fees from a listed transaction for which an advisor is a material advisor are taken into account to compute the penalty.

Rescission

In the case of listed transactions the penalty is a strict liability penalty. The penalty in the case of reportable transactions may be rescinded by the IRS if rescission would promote compliance and effective tax administration.

In the proposed regs and Rev. Proc. 2007-21, the IRS explained that filing Form 8918 after the due date will be a factor weighing strongly in favor of rescission of the penalty unless Form 8918 is filed after the IRS contacts the material advisor or after the material advisor files Form 8886, Reportable Transaction Disclosure Statement.

The final regs provide that if a material advisor unintentionally failed to file Form 8918, but subsequently files a properly completed Form 8918, that filing will be factor weighing in favor of rescission if the facts suggest that the material advisor did not delay filing the form until after the IRS took steps to identify the material advisor. However, late filing will not weigh in favor of rescission if the facts and circumstances suggest that the material advisor delayed filing Form 8918 until after the advisor's client filed Form 8886.

References: FED ¶47,043; TRC PENALTY: 3,254.10.

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Reference Key

FED references are to *Standard Federal Tax Reporter*
USTC references are to *U.S. Tax Cases*
CCH Dec references are to *Tax Court Reports*
TRC references are to *Tax Research Consultant*

Disregarded Entity Can Use Different Accounting Method From Its Corporate Owner, Chief Counsel Rules

◆ *CCA 201430013*

IRS Chief Counsel has concluded that a limited liability company (LLC) that is treated as a disregarded entity (DE) can use a different method of accounting from its corporate owner. Though treated as a branch of its owner, the DE operated a separate trade or business from its owner and could use its own method of accounting under Code Sec. 446, Chief Counsel determined.

■ ***CCH Take Away.*** Under Reg. §1.446-1(d)(1), a taxpayer with two or more separate and distinct trades or businesses can use different methods of accounting for each business. The fact that the LLC was disregarded as an entity separate from its owner did not foreclose treatment of the LLC as a separate trade or business that was entitled to use its own method of accounting.

Background

Entity A formerly was a corporate subsidiary of another corporation, Entity B. Entity A converted to a limited liability company, with Entity B as the sole owner (member) of the LLC. Because the LLC had not elected to be a corporation, it was treated as a disregarded entity for tax purposes and as a division of Entity B.

Entity B engages in sales, marketing, distribution, research and administrative functions. Entity A primarily manufactures products but does some research for the purchaser of its products. Entities A and B have separate books and records, which are prepared at Entity B's location. The two entities do not share employees, although they do share some executives. Current, A and B use the same accounting method.

Chief Counsel's analysis

Code Sec. 446 permits accounting methods to be chosen at the trade or business level. A taxpayer with two trades or businesses can use different accounting for each trade or business, provided each method clearly reflects income for the particular trade or business. For example, a taxpayer's personal service business can use different accounting from the taxpayer's manufacturing business. Each business must maintain its own separate books and records. If the businesses engage in transactions with each other, so that income is not clearly reflected, the IRS will not consider the trades or businesses to be separate and distinct.

■ ***Comment.*** Courts have indicated that the definition of a trade or business must be broadly construed. A trade or business can include business activities of any kind. It is immaterial where the business was organized, how it is owned, or where it operates.

Chief Counsel stated in the CCA that the treatment of Entity A as an entity disregarded from Entity B does not prevent Entity A from being treated as a separate and distinct trade or business.

Chief Counsel explained that determining whether Entities A and B have separate businesses is a factual determination. In this case, the available information does not foreclose treating each business as separate and distinct, Chief Counsel stated. Accordingly, Chief Counsel concluded that Entities A and B are separate and distinct trades or businesses.

Reference: TRC ACCTNG: 30,054.05.

Covered Assets

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distribution of assets on the change of status would occur on this backdated effective date, not the date of the election.

Notice 2014-44 applies to dispositions of assets that occur on or after July 21, 2014 (the date it was issued). "To prevent abuse," Notice 2014-45 provides that the regs described in Notice 2014-44 will apply to an entity classification election filed on or after July 29, 2014 and that is effective on or before July 21, 2014.

References: FED ¶46,393; TRC INTLOUT: 3,110.30.

Congress Passes Highway Bill With Pension Smoothing; Breaks For August Recess

Just before leaving Washington for its August recess, Congress approved a short-term extension of federal highway funding, the Highway and Transportation Funding Act of 2014 (H.R. 5021), with so-called pension smoothing. Other tax bills, however, must wait for Congress' return in September.

■ ***CCH Take Away.*** "While Congress came to a last-minute agreement to extend the highway bill, they have yet to act on the now-expired tax extenders," Shamik Trivedi, manager, Washington National Tax Office, Grant Thornton LLP, told CCH. "Congress' inability to quickly extend the tax extenders is to the detriment of taxpayers, who cannot properly plan their financial estimates as a result of those expired provisions. Some of those provisions, like the R & D credit and bonus depreciation, are meant to incentivize taxpayers to conduct research and make capital expenditures. But if the provisions are expired, and a divided Congress is yet to act, taxpayers will delay such investments," Trivedi said.

Highway bill. H.R. 5021 provides funding for highway and transportation projects. Pension smoothing was retained as a revenue raiser in the final bill. Additionally, some customs user fees were extended.

■ ***Comment.*** "With Congress in full campaign mode, it is unlikely much will be accomplished in terms of tax legislation until after the November elections. Nonetheless, it is possible that some smaller legislation addressing inversions and tax administration could be passed by Congress before the year is over," Trivedi told CCH.

Highway and Transportation Funding Act of 2014 (H.R. 5021).

Regs Remove Application Of NOL Limitation Rules To Treasury Sales Of EESA Stock

◆ *TD 9685, NPRM REG-105067-14*

The IRS has issued a package of regs to ensure that the net operating loss (NOL) limitation rules of Code Sec. 382 will not apply to certain sales of corporate stock by Treasury. The regs modify the effective date provisions of 2013 regs (TD 9638) under Code Sec. 382.

■ ***CCH Take Away.*** Under the *Emergency Economic Stabilization Act of 2008* (EESA), Treasury purchased and later disposed of shares of a number of private corporations suffering economic problems. The IRS issued Notice 2010-2 to limit the effect of Code Sec. 382 on Treasury's stock sales. However, the IRS became concerned that the 2013 regs had inadvertently nullified the notice. Out of an abundance of caution, the IRS is modifying the 2013 regs to reaffirm the Notice.

Code Sec. 382

The government does not want profitable corporations to acquire corporations with accumulated losses (NOLs) (loss corporations) for the sole purpose of offsetting their income against the other corporation's prior losses. Code Sec. 382 limits the amount of NOLs that a corporation can use after its ownership has changed. An ownership change occurs if the corporation is a loss corporation on the testing date, and the percentage of stock of a loss corporation owned by a five-percent shareholder increases by more than 50 percentage points.

Public Groups

Shareholders who own less than five percent of the loss corporation are aggregated and treated as a single five-percent shareholder. This is called a public group. A segregation rule required the creation of an additional public group on certain stock sales by an person that owned five percent or more of the loss corporation. However, under the 2013 regs, no new public group was created on a transfer of stock to the public group shareholders. Instead, the stock was treated as acquired proportionately by the existing public groups.

■ ***Comment.*** Reducing the number of public groups limits the potential for of an ownership change.

Notice 2010-2

EESA established eight programs (the "programs") for troubled corporations. Through the programs, Treasury purchased a corporation's stock to provide it with financial assistance, and later sold the stock when the corporation's condition improved. Under the segregation rule, any sale of stock could create a new public group subject to Code Sec. 382.

Notice 2010-2 provided that the new group's ownership of the corporation's stock was not considered to increase because of Treasury's sale. This reduced the likelihood that Treasury's sale would create an ownership shift that could limit the use of the corporation's losses.

New regs

The IRS noted that Notice 2010-2 relied on the assumption that the stock sale created a new public group. However, under the 2013 regs, these transfers no longer created a new group. Therefore, it was unclear whether the Notice still applied to prevent an ownership change.

The new regs amend the 2013 regs to reaffirm the application of the Notice to Treasury sales of stock it acquired under the programs. The new regs modify the effective date rule of the 2013 regs to except any Treasury sale of stock under the programs from the changes to the segregation rule. As a result, a sale of stock by Treasury to the public group will still create a new public group, and Notice 2010-2 continues to apply.

■ ***Comment.*** The IRS emphasized that these new rules apply to Treasury sales of EESA program stock and do not affect other transactions involving stock of the corporations that participated in the programs.

References: FED ¶¶47,042,49,626; TRC NOL: 33,056.

IRS Adds To Countries With Waiver Of 2013 Residency Requirements For Foreign Housing Credit/Housing Costs

The IRS has updated its list of countries for which the foreign presence or residency requirements of Code Sec. 911(d)(1) are waived for tax year 2013 for purposes of the foreign earned income and housing cost exclusions. South Sudan has been added to the list of countries in Rev. Proc. 2014-25 for which the Code Sec. 911(d)(1) requirements are waived. The waiver of the foreign presence or residency requirements is applicable to an individual whose date of departure from South Sudan was on or after December 17, 2013. An individual who establishes residency in South Sudan on or after December 17, 2013, will not qualify for the waiver.

■ **Comment.** Code Sec. 911 provides that a U.S. taxpayer working abroad may exclude a certain amount of their foreign earned income and housing costs from gross income if he or she was either a bona fide resident of the foreign country for an entire year or was present within the foreign country for 330 full days during a 12-month consecutive period. The IRS can waive these requirements for qualified individuals if the individual can establish that, but for adverse conditions in the foreign country (for example, war or civil unrest), he or she could reasonably have been expected to meet the eligibility requirements.

Ann. 2014-28; Rev. Proc. 2014-25; TRC EXPAT: 12,058.

Taxpayer Must Show Costs Are Mixed Before Applying Allocation Method To Determine Intangible Development Costs

◆ *Amazon.com Inc., TC Memo. 2014-149*

The Tax Court has denied a taxpayer's motion for summary judgment where the taxpayer argued that the IRS abused its discretion by allocating 100 percent of the taxpayer's certain costs to intangible development costs (IDCs). The taxpayer, the court found, had to show that the costs constituted "mixed" costs, which are costs benefiting other business activities as well as intangible development activities, before it could employ an allocation method to determine IDCs.

■ ***CCH Take Away.*** According to the court, the taxpayer appeared to believe that showing the "mixed" nature of costs would be tedious and time-consuming. The court observed that it would not be necessary that the taxpayer examine each cost. Sampling techniques or a review of critical cost centers may help answer this question, the court noted.

Background

The taxpayer and its U.S. affiliates executed a cost-sharing agreement (CSA) with an affiliate in Luxembourg. In entering into the CSA, the taxpayer and the affiliates agreed to share IDCs. The taxpayer's cost accounting system at that time did not specifically segregate IDCs from other operating costs. In response, the taxpayer developed a formula and applied it to allocate to IDCs a portion of the costs accumulated in various "cost centers" under its method of accounting.

The IRS determined that 100 percent of the costs in the technology and content category constituted IDCs. The taxpayer argued that the IRS's determination was an abuse of discretion.

■ ***Comment.*** The taxpayer's cost centers were accounting classifications/categories used to manage and measure operating expenses. Each category, the court found, was a "rollup" of many individual cost centers. One expense category covered technology and content, which consisted of payroll and related expenses for employees involved in research and development, including application development, editorial content, merchandising selection, systems and telecommunications support, and costs associated with the systems and telecommunications infrastructure.

Court's analysis

The court first found that a CSA is an agreement where taxpayers agree to share the costs of development of one or more intangibles in proportion to their shares of reasonably anticipated benefits from their individual exploitation of the interests in the intangibles assigned to them under the arrangement. A taxpayer participating in a CSA must calculate its share of IDCs on the basis of factors that can reasonably be expected to reflect that participant's share of anticipated benefits.

Here, the court found that the taxpayer had not yet shown that the technology and content category contained nontrivial costs properly characterized as something other than IDCs. Therefore, it was a disputed question of material fact whether the technology and content category contained "mixed" costs. The court concluded that it could not find if the IRS abused its discretion in determining that 100 percent of the technology and content category costs were IDCs until the taxpayer showed that the category contained a nontrivial amount of "mixed" costs.

The court further found that the taxpayer would have to first establish that the technology and content category costs were mixed before the taxpayer could apply an allocation formula. The IRS's regs, the court held, permit costs to be allocated only if a particular cost contributes to the intangible development area and other areas or other business activities. The status of costs as "mixed" is a precondition to the application of an allocation formula, the court concluded.

References: CCH Dec. 59,975(M); TRC INTL: 15,152.

Appeals Court Rejects Origination Clause Challenge To PPACA Individual Mandate

The U.S. Court of Appeals for the District of Columbia Circuit has rejected a taxpayer's claim that the individual shared responsibility provision ("individual mandate") of the *Patient Protection and Affordable Care Act* (PPACA) violated the Origination Clause of the U.S. Constitution. The individual mandate's purpose is not to raise revenue, the court held.

Background. Beginning January 1, 2014, the PPACA requires individuals to have minimum essential health coverage or make a shared responsibility payment, unless eligible for an exemption. The taxpayer did not want to have health insurance and did not qualify for an exemption. According to the taxpayer, the individual mandate violated the Origination Clause because the provision originated in the Senate and not the House.

Court's analysis. The court found that the Supreme Court has held that unless a bill is aimed at levying taxes in the strictest sense, the bill does not fall within the limited scope of the Origination Clause. The individual shared responsibility provision is not a bill for raising revenue under the Origination Clause, the court found. The aim of the PPACA is to increase the number of individuals covered by health insurance and decrease the cost of health care, and not raise revenue through the individual shared responsibility payment. Where a provision's revenue-raising function is incidental to its primary purpose, the Origination Clause does not apply, the court concluded.

Sissel v. HHS, CA-D.C., July 29, 2014; TRC HEALTH: 3,050.

Payments In STARS Transaction Were Income, Indicating Transaction Had Economic Substance, District Court Concludes

◆ *Wells Fargo & Co., D.C.-Minn., July 22, 2014*

A federal district court has found, on a motion for partial summary judgment, that payments to the taxpayer (a U.S. bank) were income and not a rebate of foreign taxes. Because the taxpayer earned net income from the STARS ("structured trust advantaged repackaged securities") transaction, the court in effect concluded that the transaction had economic substance and was not a sham.

- ***CCH Take Away.*** "The government clearly could put out some guideposts on [economic substance and] foreign taxes under Code Sec. 7701(o)," Monte Jackel, Jackel Tax Law, Silver Spring, Md., told CCH. "The foreign tax credit is unique; it would send a message and help in determining future [though not existing] cases."
- ***Comment.*** Several courts have examined STARS transactions in recent years. The Tax Court and Federal Claims Court have agreed with the government that the transactions lacked economic substance. At least one district court has sided with the taxpayer. Some of these cases are on appeal, but none has been decided.

Background

In a STARS transaction, the taxpayer transferred income-producing assets to a United Kingdom trust. The trust's was subject to U.K. taxes (of 22 percent) because its trustee (also a bank) was British. Its income was also included in the taxpayer's U.S. income.

The British bank loaned $1.25 billion to the taxpayer, who paid monthly interest on the loan. The British bank made monthly payments of 48 percent of its U.K. tax credits to the taxpayer (the BX amounts). The interest and BX payments were netted. The court concluded that the taxpayer received an economic benefit from the BX payments, either as a reduction in interest expense or as U.S. income.

Court's rulings

The taxpayer requested, and the district court ruled on, several motions for partial summary judgment.

- The court found that the BX payments should be treated as pre-tax income to the taxpayer, not as a rebate of U.K. taxes. The taxpayer was clearly paid for establishing the U.K. trust. This conclusion strengthened the taxpayer's argument that the transaction generated income and therefore had economic substance. (The ruling did not resolve the economic substance issue, which required factual determinations that were not appropriate for summary judgment.).
- The court rejected a motion that the STARS transaction had business purpose. There was no authority concluding that voluntarily submitting to another country's taxes is itself a business purpose. Furthermore, a business purpose does not necessarily exist just because there is economic substance.
- Code Sec. 269 (which denies deductions and credits for certain transactions evading taxes) does not apply. However, this did not affect the application of the sham transaction doctrine.
- The taxpayer's reporting of the transaction was not negligent under Code Sec. 6662. There are judicial decisions, treaty law, and other authorities that provide a reasonable for the taxpayer's reporting, even if the transaction is ultimately determined to be a sham.
    - ***Comment.*** The court discussed, but did not resolve, whether the two-prong test for a sham transaction (economic substance and business purpose) applied.

References: 2014-2 USTC ¶50,372; TRC CCORP: 42,252.

Magazine Advertising/Event Sponsorships Do Not Imperil Social Club's Exempt Status

◆ *TAM 201430019*

IRS Chief Counsel has found that three activities engaged in by an organization exempt under Code Sec. 501(c)(7) constituted activities traditionally carried on by social clubs. Therefore, the organization's activities and the income these activities generated did not jeopardize its exempt status.

- ***CCH Take Away.*** A social club or similar organization (including a college fraternity or sorority) may be tax-exempt under Code Sec. 501(c)(7) if substantially all of its activities are for pleasure, recreation, or other nonprofit purposes. Each activity an organization engages in must be tested.

Background

The organization was incorporated to promote interest in motoring activities and to encourage safe and skillful driving classes, publications, and activities related to motor touring. The organization actively engaged in three activities in question: the solicitation and receipt of advertising income for a club magazine from nonmembers; the solicitation and receipt of car racing event sponsorship payments from nonmembers; and the conduct of an annual raffle limited to members.

Chief Counsel's analysis

The organization's three activities satisfied the activities test because all of its activities were "normal and usual" activities for a social club, Chief Counsel determined. The magazine included various columns, articles, letters to the editor, product reviews, and technical information for the organization's members, Chief Counsel found. The car event was an annual national club gathering that included driving education and other noncompetitive driving events, club

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Jurisdiction

An individual's claim for damages resulting from an alleged unlawful levy was time-barred and properly dismissed for lack of subject matter jurisdiction. The individual filed his complaint more than two years after the cause of action accrued.

Caudill, CA-9, 2014-2 USTC ¶50,380; TRC IRS: 45,114.

An individual's complaint against the Virgin Islands Bureau of Internal Revenue (VIBIR) to have an overpayment applied to outstanding tax liabilities and to have liens and levies against her property removed was dismissed for lack of subject matter jurisdiction. Since the taxpayer received the relief sought, the case was moot.

Macken v. The United States Virgin Islands, DC V.I., 2014-2 USTC ¶50,378; TRC LITIG: 9,052.

The court lacked jurisdiction over four out of five appeals filed by partners challenging post-judgment collection orders. The first two appeals were dismissed because the judgment was not final as it did not address the relief requested by the government, the appointment of a receiver. The fourth and the fifth appeals, filed after the receiver's appointment, were dismissed because they raised frivolous arguments and sought relief from interlocutory orders in the post-judgment collection proceedings.

Zabka, sub nom Antiques Limited Partnership, CA-7, 2014-2 USTC ¶50,373; TRC LITIG: 9,254.

Tax Crimes

A 21-month sentence imposed upon an individual for filing fraudulent federal tax returns was proper. The evidence showed that the individual knowingly presented false, fictitious and fraudulent claims to the IRS.

Ulloa, CA-1, 2014-2 USTC ¶50,377; TRC IRS: 63,202.

A tax preparer was properly convicted and sentenced for tax fraud conspiracy. The 120-month sentence imposed upon the individual was procedurally and substantively reasonable and sentencing court properly calculated the sentence based on intended loss rather than actual loss.

Morris, CA-10, 2014-2 USTC ¶50,374; TRC IRS: 63,306.

Summons

A summons enforcement case was remanded for the federal district court to decide whether a corporation was entitled to examine an IRS agent regarding the IRS's motives for issuing the summonses. The district court was required to review the taxpayer's evidence to determine whether it pointed to specific facts or circumstances showing that the summons was issued for an improper purpose.

Clarke, CA-11, 2014-2 USTC ¶50,370; TRC IRS: 21,354.

Deductions

A married couple was not entitled to deduct losses generated by a horse-breeding activity run through an S corporation because the taxpayers did not operate their horse-breeding activity in a businesslike manner. Late-filing penalties were also assessed.

Stuller Est., DC Ill., 2014-2 USTC ¶50,379; TRC BUSEXP: 15,100.

An individual's cattle breeding program was not a for-profit business; therefore, expenses allegedly paid by the taxpayer in connection with that program were not deductible as business expenses. In addition, the taxpayer was subject to accuracy-related penalties.

Gardner, TC, CCH Dec. 59,974(M), FED ¶48,090(M); TRC BUSEXP: 15,050.

Liens and Levies

The government was entitled to reduce to judgment taxes, penalties and interest assessed against a couple, foreclose federal tax liens on property held by the couple's nominee and apply the proceeds of the sale to the couple's

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Tax Court Will Not Determine Outside Basis At Partner Level

The Tax Court has found that because the parties had stipulated the amount of the tax deficiency, it was not required to determine a partner's outside basis in a TEFRA case on remand from the Eighth Circuit Court of Appeals. The Tax Court also found that it did not have jurisdiction to review an accuracy-related penalty imposed at the partnership level.

- ***Comment.*** After the Eighth Circuit issued its opinion, the Supreme Court decided another TEFRA case, *Woods, 571 U.S. ___ (2013)*. The Tax Court noted that the Supreme Court observed, "it is not readily apparent why additional partner-level determinations would be required before adjusting outside basis in a sham partnership."

Background. In 2006, the Tax Court ruled that a partnership formed by the taxpayer had engaged in a sham transaction lacking in economic substance. Subsequently, the IRS issued a notice of deficiency to the taxpayer at the partner level, and the taxpayer petitioned the Tax Court. The Tax Court found that it lacked jurisdiction because the 2006 partnership-level decision had become final. On appeal, however, the Eighth Circuit found that the taxpayer's outside basis was an affected item that must be determined at the partner level.

Court's analysis. On remand, the Tax Court found that a partner-level determination of the taxpayer's basis was unnecessary because the parties had stipulated the amount of the deficiency. The Tax Court also found that it still lacked jurisdiction to consider the accuracy-related penalty.

Thompson, TC Memo. 2014-154; CCH Dec. 59,980(M); TRC PART: 60,450.

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outstanding liability. The organization holding title to the property was the husband's nominee. The husband exerted exclusive control over the organization, its bank accounts and its assets.

Bogart, DC Tenn., 2014-2 USTC ¶50,376; TRC IRS: 45,158.

The government was entitled to recover a taxpayer's outstanding federal taxes from his one-third interest in his deceased mother's condo. The taxpayer's right to control his one-third interest in the condo constituted property or rights to property under Code Sec. 6321. Thus, the federal tax liens filed against him attached to his one-third interest in the decedent's condo.

In re Deinlein Est., DC Ky., 2014-2 USTC ¶50,371; TRC IRS: 48,102.

Collection Due Process

A notice of federal tax lien was sustained against an individual who persisted in raising irrelevant arguments in opposition to IRS collection action. At a Collection Due Process hearing before the IRS Appeals Office, the taxpayer was precluded from challenging his underlying tax liability, raised no relevant issues, and offered no collection alternatives. The taxpayer was sanctioned for instituting Tax Court proceedings primarily for purposes of delay.

Kanofsky, TC, CCH Dec. 59,979(M), FED ¶48,095(M); TRC IRS: 51,056.25.

There was no abuse of discretion in denying a collection alternative requested by an individual who failed to participate in her hearing or raise any issues other than her underlying liability. The settlement officer conducted a thorough review of transcripts of the individual's account and verified that the requirements of applicable law and administrative procedure were followed.

McCullar, TC, CCH Dec. 59,976(M), FED ¶48,092(M); TRC IRS: 51,056.25.

Offer-in-Compromise

The IRS Appeals Office did not abuse its discretion in refusing to accept an individual taxpayer's offer in compromise (OIC) or in refusing to withdraw a notice of federal tax lien (NFTL). Because the taxpayer did not submit Form 656 as required, the SO did not abuse his discretion in denying the OIC. The IRS was within its discretion in determining not to withdraw the NFTL.

Bergdale, TC, CCH Dec. 59,978(M), FED ¶48,094(M); TRC IRS: 42,118.

Bankruptcy

A debtor could not exempt the Earned Income Tax Credit (EIC) from her bankruptcy estate as a public assistance benefit. Under State (Illinois) law, a debtor's right to receive benefits is exempt but a benefit already received is not. Since the debtor had already received her benefit, it was not exempt from her estate.

In re Austin, BC-DC Ill., 2014-2 USTC ¶50,375; TRC INDIV: 57,252.10.

Alimony

A lump-sum payment made by an individual to his former spouse after their divorce represented a property settlement, not alimony, and so was not deductible by the taxpayer. An accuracy-related penalty was imposed on the taxpayer based on substantial understatement of tax. The taxpayer did not show that he acted reasonably and in good faith.

Peery, TC, CCH Dec. 59,977(M), FED ¶48,093(M); TRC INDIV: 21,106.

District Court Disallows BLIPS Transactions

A U.S. federal district court has found on summary judgment in a TEFRA partnership case that an investment product called a "Bond Linked Issue Premium Structure" (BLIPS) lacked economic substance and should be disregarded for tax purposes. The BLIPS strategy involved several loan transactions that "no rational investor would pursue . . . for any business reason other than tax avoidance," the court found.

Court's analysis. The district court found that the petitioners bore the burden of proving the transactions were not shams designed only to generate tax losses. Petitioners failed to show either objective or subjective intent to engage in the transaction with a purpose other tax avoidance.

Evidence that petitioners respected state laws and record keeping requirements when forming their limited liability companies (LLCs) was insufficient to demonstrate legitimate economic purpose. Furthermore, statements by the principals of the petitioner suggesting they intended to generate profits from the BLIPS investment strategy were insufficient to establish legitimate profit intent.

■ ***Comment.*** The district court declined to apply the Code Sec. 6662(b)(1) negligence penalty on summary judgment. The court found that it must make a factual determination regarding the intent and knowledge of the petitioners' principals, and such determination was not amenable to summary judgment.

Shasta Strategic Inv. Fund, N.D.-Calif., 2014-2 USTC ¶50,383; TRC BUSEXP: 30,168.

Exempt Status

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racing, technical sessions, vendor displays and presentations as well as social events for members who attended.

■ ***Comment.*** Chief Counsel noted that the advertising and sponsorship activities were an insubstantial part of organization's traditional magazine activities.

Chief Counsel further determined that the organization met the nonmember income test. The percentage of outside income that the organization received from magazine advertising and event sponsorship payments was less than 35 percent of its gross receipts from normal and usual activities. Chief Counsel found, however, that the nonmember income was unrelated business income under Code Sec. 512(a)(3)(A). Chief Counsel also found that unlike the nonmember gross receipts from the magazine advertising and event sponsorships, the gross receipts from organization's raffle were solely derived from its membership.

Reference: TRC EXEMPT: 15,206.