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CPE NETWORK TAX REPORT

NOVEMBER 2021 VOLUME 34, ISSUE 10

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Topics for future editions may include:

- Partnership Distributions
- Reasonable Compensation

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EXECUTIVE SUMMARY

PART 1. CURRENT DEVELOPMENTS

Taxation is the most dynamic area of accounting. It changes daily. While not all changes affect every practitioner's practice, it is important to have an awareness of the changes that occur. This segment highlights many of the recent changes and issues, whether involving Congress, the IRS, or the Courts.

Learning Objective: Upon completion of this segment, the user should be able to analyze current issues in taxation, including assessing the impact of buy-sell agreements on corporate valuation for estate tax purposes, applying the recognition extension for farmers and ranchers affected by drought, and assessing the Wyden partnership proposals. [*Running time 29:38*]

PART 2. INDIVIDUAL TAXATION

Many taxpayers find that they are unable to pay their tax liabilities in full. The IRS has the ability to "compromise" or accept less than the full amount of the tax liability in certain circumstances. The process is referred to as an "Offer in Compromise" (OIC) and constitutes an agreement between a taxpayer and the IRS to accept less than full payment with certain conditions. This process is misunderstood by many taxpayers due to radio and television ads claiming that the IRS is settling for "pennies on the dollar." These claims, which may be true in rare circumstances, are misleading because the IRS will generally not accept an offer if the tax debt can be paid in full or through an installment agreement and/or equity in assets.

Learning Objective: Upon completion of this segment, the user should be able to analyze the need and/or circumstances appropriate for offers in compromise, including evaluating the basis of an offer in compromise, analyzing the types of offers that are available, and determining reasonable collection potential. [*Running time 38:56*]

PART 3. BUSINESS TAXATION

The oldest of the baby boomers were 70 in 2016 and are at the point where they need to consider the implications of required minimum distributions (RMDs) from qualified plans. They have potential and far-reaching tax effects. Proper planning is required to avoid potentially large penalties on failing to take an RMD. In 2019, Congress and the IRS made significant changes to RMDs with extension of the required starting date and a revised life expectancy table, respectively. It is important to have an understanding of the rules applicable to RMDs. The CARES Act of 2020 made significant changes for qualified individuals. One planning tool is the use of trusts as beneficiaries under certain plans. There are many pitfalls that practitioners need to be aware of in using trusts for that purpose.

Learning Objective: Upon completion of this segment, the user should be able to analyze current issues related to required minimum distributions, including identifying the beginning date for RMDs, assessing the distribution upon death, and evaluating the use of a trust as the beneficiary. [*Running time 35:19*]

ABOUT THE SPEAKERS

Ian J. Redpath, JD, LLM, is a nationally recognized tax attorney and consultant from Buffalo, New York and is a principal in the Redpath Law Offices. Mr. Redpath has published numerous articles on contemporary tax issues and co-authored several books on tax topics. He has extensive national and international experience in developing, writing, and presenting professional CPE programs. In addition to his active tax practice, he serves as Chairman of the Department of Accounting and Director of Graduate Accounting Programs as well as Professor of Taxation and Forensic Accounting at Canisius College in Buffalo.

Lawrence K. Y. Pon, CPA/PFS, CFP, is a Certified Public Accountant, Personal Financial Specialist, Certified Financial Planner, Enrolled Agent, United States Tax Court Practitioner, and Accredited Estate Planner in Redwood Shores, California. Mr. Pon has been in practice since 1986 and enjoys helping his clients reach their financial goals. He frequently speaks nationally on tax and financial planning topics to tax professionals, financial advisors, and the general public. Mr. Pon received his BS in Business Administration with emphasis in Accounting and Finance from the University of California, Berkeley and an MS in Taxation from Golden Gate University in San Francisco.

Ed Renn, JD, focuses his practice on domestic and international private client matters which includes U.S. and international estate planning, income maximization strategies, FLP and LLC planning, wealth preservation, business succession planning, international tax planning for entities and individuals, trust structures, estate administration, qualified Opportunity Zone Planning, and planning for single and multi-family offices. Ed frequently utilizes sophisticated life insurance strategies in both income and transfer tax planning. Ed is a frequent speaker, has co-authored several books, and has been featured in many articles on estate and tax planning topics.

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PART 1. CURRENT DEVELOPMENTS

Experts' Forum

This month we join Ian Redpath for Experts' Forum, a popular feature in which we review recent developments in taxation. We begin with a discussion about a case the Supreme Court agreed to hear, one that could have broad implications regarding the jurisdiction of the Tax Court.

Let's join Ian.

A. *Boechler, P.C. v. Commissioner*

SCt Docket No. 20-1472

Mr. Redpath

Hi, everybody. Welcome to the program. I'm Ian Redpath. This is the segment where we go over recent changes, some updates, some proposals. We have some very interesting things to go over that have come from the courts, from the IRS, and from Congress as it happens this month. So, let's start right in with a very interesting case, which could have some significant implications. And this is the Boechler case. The Supreme Court has granted certiorari to hear the case. What does that mean? It means the Supreme Court has agreed that they are going to take up this case and they're going to rule on it. So, what happened in Boechler is it's a Collection Due Process. There was a levy. They got the notice on the levy. They asked for a Collection Due Process hearing. They got the hearing. They got the results of the hearing. They were unhappy with them, and they had 30 days in which to file with the tax court.

Now, historically, the tax court has said the date that's there, that's the date. You're stuck with those dates. So, the 90 day, for example, so the 90-day letter, you have 90 days in which to pay the tax, file in the tax court, or we're going to start collection proceedings. That's the actual assessment of tax. So, that 90-day letter, the IRS has always said, 90 days is 90 days. There's no equitable relief. It doesn't matter why you missed the deadline. It's 90 days. I had a situation where someone came in and said—it was a CPA called me—they wanted me to look at a case. Send it to me.

I said, your 90-day statutory period is up. Now, it doesn't mean we can't go to court. We can still pay it, have the taxpayer pay it, go to the district court, go to the claims court. But as far as the tax court, they've ruled consistently that that is a... It's a mandatory, it's a jurisdictional issue. They have no jurisdiction. They can't waive that 90-day period.

Well, you have the same period, only it's 30 days after the Collection Due Process. So, unfortunately, they mailed the petition one day late. So, they missed it by a day. And the tax court said, sorry, no jurisdiction. We have no jurisdiction over the case because you missed the 30 days.

You might say to yourself, "Well, come on, there's no equitable relief here." The answer is no. The court, the tax court, has consistently said no equitable relief. The circuit courts of appeal that have heard these cases have agreed with the tax court and said, "No, these statutory periods are jurisdictional. The court has no jurisdiction if you don't meet that deadline. So, they can't hear the case. They can't grant you any equitable relief." Now the Eighth Circuit, the Ninth Circuit has specific cases. This is one out of the Eighth Circuit. But the D.C. Circuit disagreed with that and said, well, equitable relief, it's not jurisdictional. An equitable relief could be granted.

So, the Supreme Court said, well, we're going to hear this. So, what's the implication? It's not just that 30 days for the Collection Due Process that's to appeal to the tax court. I'm assuming that the Supreme Court is going to say if it's jurisdictional, so is the 90-day period. And so there's a possibility that we could have jurisdictional relief. I'll give you a great example. I had a client, that a CPA called me. I looked at the case and I said, well, wait a second. We've got a problem here. I looked at the date; and on the 90-day letter, it gives you the date that you have to file in the tax court by. That date was wrong. That date was too long. It was more than 90 days. It was wrong.

Fortunately, we caught it. We filed in the tax court on time. And I asked the tax court judge. I said, "What would you have done on that? You know, I mean, if that stamp is there." He said, "Look, the law's clear. It's a 90-day period. It is not what date the IRS happens to stamp on that. There's no equitable relief." Now, you'd think there you'd have obviously had equitable relief. And again, it didn't matter because we filed in time. But if this case, if the Supreme Court comes down, I think what we'll find is that we would be able to get some types of equitable relief. Now, exactly how broad that will be, who knows? Let's see what the Supreme Court says. But it's certainly an interesting case that will have some broad implications on the jurisdiction of the tax court.

B. *Taryn L. Dodd v. Commissioner*

TC Memo 2021-118

The next is the Dodd case. It's a tax court memo case. You know, this seems simple, but it's something to think about. In 2013, a partnership—Dodd's a member of the partnership—they sold a building for a million dollars. They pass through on the K-1, a million dollars of 1231 gain. Now, there also was a loan that, in 2013, they repaid. And the share of Dodd was a million dollars. And so Dodd said, well, I never got anything because they used the million dollars to pay off the loan. The court said, sorry, they may have used a million dollars to pay off the loan, but that's irrelevant. You still received it. Constructively, it doesn't matter. You have to pick up the income whether you got it or not, because that was your share of the income. It doesn't matter that they used the money to pay off the debt. And that million dollars happened to correspond to the million dollars of gain. Doesn't matter, the court said.

C. TIGTA Audit Report No. 2021-40-070

Calls for Refining Complex and Inconsistent EITC and ACTC Rules

We have another interesting thing coming out of the Treasury Department's Inspector General concerning the EITC and the ACTC, the Advanced Child Tax Credit. And this is Audit Report 2021-40-070. And you know, they're somewhat critical about all of the problems with both of these, with the due diligence, with, they said in evaluating the reasons for disallowance of the earned income and the additional child credit. The audit said that there's such a confusion on, for example, child. Who's a child? Who qualifies? And that the rules are just too complex and too inconsistent as to who qualifies. They also—and this is really a big thing—they recommend that the IRS get correctable error authority, treat any change as a correctable error.

Without that, what the IRS has to do is they have to audit every return to determine, does a person qualify, what is going to be the change in tax? Whereas here, if it's clear, they could just use it as a correctable error, which would obviously save lots of people a lot of time, including the taxpayers' time and money. So, that can be a real advantage so they won't have to go in and audit all the time. They can send you a notice on a correctable error. If you agree, send in the additional amount. If you don't agree, say why you don't agree and provide the information. Again, that's the recommendation of the Treasury Inspector General.

D. *U.S. v. Robin S. Richards*

DC IN

We now have a case, Richards, very interesting if you have farmers. What happened is, there was a filing in Chapter 12. The Richards family because of various issues ended up, and it was basically by the weather and decline in market prices that caused them great financial problems. For several years, they had large losses. The lender refused to review their loans. So, they had to liquidate their farm assets. Then, they had to liquidate equipment; and the proceeds were just used to pay the lender. So essentially, it went to the lender. Then, they file bankruptcy, Chapter 12. And in Chapter 12, Section 1232 would really say that these debts are dischargeable. And so, they submitted a plan under Chapter 12. The IRS didn't challenge it because these debts were dischargeable debts. They were considered unsecured debts.

Then, they overpaid the tax liabilities that weren't [dischargeable]. So, the tax liabilities from the sale of these assets due to these weather conditions were considered an unsecured debt which could be discharged. Their other debts, their other tax debts, not related to this, were not dischargeable. Well, they miscalculated. And what the IRS wanted to do then is they wanted to take a tax refund and then apply it to these dischargeable debts. In other words, keep the refund. And the court said, you can't keep the refund. You can't apply it to these 1232 liabilities because there was a plan, and these are essentially going to be discharged. So, you can't keep their refund on the other taxes and apply it to this.

E. Practice Unit: Section 263A Costs for Self-Constructed Assets

We have an interesting one. Again, if you have clients that have self-constructed assets, the practice unit has come up with a guidance for Section 263 costs for self-constructed assets. It's a really good comprehensive guide as to what's to be included, how it's to be handled. It gets into some detail on Section 471 costs, which are the costs other than interest that you capitalize on your financial statement. And then it gets into the 263A costs. The ones that, again, 263A compared to financial accounting is what I would call super-full absorption. It includes indirect labor costs, officer compensation, employee benefits, interest cost capitalization. And it discusses how those have to be capitalized for self-constructed assets. If you have a client with self-constructed assets, please look at that.

F. Distributions of Property by Corporation to Shareholder

TD 9954

We also have TD 9954. If you see this, I wouldn't get too concerned. The IRS has finally finalized the regs, going back to changes that were made in 1988 to the Code. This just simply finalizes the 2019 proposed regs, essentially without change. So essentially that—and you'll say, well, of course that is because that's been the law for a long time—that distribution amounts is the amount of money plus the fair market value of property received, and the basis of the property received in a 301 distribution is its fair market value. Again, it's just finalizing the rules, the corporate rules, under Section 301.

G. *Patrick Combs v. Commissioner*

CA 9

And now, we have the Combs case. It's a Ninth Circuit Court of Appeals. Combs was a motivational speaker. This is rather interesting with some of the conversations about President Biden's use of an S corp for his speaking fees, et cetera. And so, it's kind of a timely case. The Ninth Circuit Court of Appeals. What happened is Combs is a motivational speaker; he puts all of his fees from his motivational speaking into his corporation. He takes out essentially a nominal salary, but he starts—here's where he gets the problem—he starts paying personal expenditures. Well, once you start paying personal expenditures, you know what's going to happen. The IRS says, hey, wait a second here. The payments of your personal expenses are constructive dividends. And so, therefore, you have to pick that up as dividend income. Now, they didn't say it was for services. They did say it was dividend income. He also said, well, I relied on my investment advisor, kind of a broad term. The IRS said, sorry, this is such a clear-cut case of the law that it doesn't matter. We're not going to waive penalties.

H. *Charles H. Leyh v. Commissioner*

157 TC No. 7

We have another tax court case, Leyh, L-E-Y-H. And this is kind of an interesting one. But you know it goes back to 2014; 2014 is the year in question. And you might say, well, okay, but it's a new case. Yes, the court just decided it. But anytime you look at a court case, remember you have to look at what year it was. Is the law still the same as it was in the year that this occurred?

In this particular case, what happened was there's a divorce proceeding. What he does is, as part of their alimony, he in fact agrees to pay his spouse's health and vision insurance through a cafeteria plan that's provided by his employer. Those payments are excluded from his income. So, he files a separate return, married, filing separately. And he deducts the alimony. He says, well, the spouse has to pick it up into income. Now, keep in mind. I know you might say, well, alimony doesn't matter. Yes, it does. Because the rule says that before 2019, a divorce settlement—I'm sorry, you can have alimony. So, the alimony rules apply. It's the newer ones that the alimony rules don't apply, that it's not a deduction, it's not income to the other side. But you're going to have clients that absolutely have this type of situation. So he goes, this is alimony.

The first thing that the court did is the court agreed. Yes, this can constitute alimony; you're providing for her health insurance. But the IRS said, well, but you can't deduct it because it's a double deduction. You're excluding the income and then deducting it. And they said, if you had filed, and the court looked at it and said, if they'd have filed a joint return for the year, they would have excluded the income. There would have been no deduction. Either way, it would have been excludable income. But that since they filed married filing separately, its excludable income. That wasn't questioned. They said, if you didn't take the deduction, then she would still have to pick it up into her income. And so, it would make it taxable. So the only way to make sure that you get the correct result is to allow him a deduction.

So, it sounds like double-dipping—I got an exclusion and a deduction—but it's not because you're taking away the income being picked up by her. This is just to assure that it wouldn't be taxed. So, he excludes it. He takes a deduction. She picks it up into income. And so you have an offsetting because they said this is alimony. The fact that it's coming from a fringe benefit plan is irrelevant. The alimony rules are separate from the fringe benefit rules. So, they separated those. Again, something to look at if you have a client who's still using alimony.

I. Thomas A. Connelly v. U.S.

DC MO

This is an interesting one, Connelly. It's a district court, Missouri. The Federal District Court said that the proceeds of a life insurance policy on the life, upon the death, payable on the death of the majority shareholder, increased the value of the corporation for estate tax purposes and, therefore, increased the amount subject to tax upon death.

The closely held family business, there was a buyback agreement. There were brothers, two brothers, Michael and Thomas. They owned a roofing business. They ended up having a buy-sell agreement. They bought life insurance so they could have enough cash. Michael dies. The company repurchases his shares for $3 million. The estate paid tax on the $3 million. The IRS came back in and said, you owe us an additional $1 million of estate taxes. Because what they said was that they weren't going to recognize that buy-sell agreement. That it wasn't going to fall into any exception because to fall into the exception, the buy-sell agreement had to be a bona fide business arrangement, not a device to transfer to other members of the family at less than full value, have terms similar to that would be arm's length. It has to have a fixed and determinable offering price and legally binding.

And they said in this particular case, what happened is that they didn't even use... In other words, they didn't use all of the proceeds of the life insurance to buy. They didn't include any type of premium for the majority control. And they said that indicates that the redemption price was not full and adequate consideration. So, this was a device to transfer at less than full and adequate. They also failed to provide any evidence to show that this was similar to other arm's length, and they didn't follow any detailed appraisal mechanism. They just kind of picked up this is what the value's going to be. So they said, they didn't even take it for the full price. They took it for even less and had no justification as to where that number came from. So, they said that just increases the value of the company. And, oh, by the way, it's not the $3 million you got paid for the company from the insurance. The value is much higher because you have to include the insurance proceeds in the value of the corporation.

J. IR-2021-193; Notice 2021-55, 2021-41 IRB

Capital Gain Relief for Farmers and Ranchers

IR-2021-193 and [Notice] 2021-55, the IRS has announced that farmers and ranchers who were forced to sell livestock due to drought can have an additional year to replace it and defer tax on any gains from those forced sales. If you look at Notice 2021-55, that lists the areas. There's regions in 36 states and one territory that this will apply to. It does not apply to livestock that's for slaughter, held for sporting, or poultry. Basically, it's draft, dairy, or breeding purposes for the livestock. Now, generally, there's a four-year period. So, we're kind of looking back right now at ones that were affected in 2017. And the replacement is the first tax year after the first drought-free year to replace it. If you're looking for how this works, look at Notice 2006-82. So, if you have anyone who is affected, you may wish to look at that.

K. Senator Wyden Partnership Reform Draft Legislation

Now I want to quickly go over something that's really important. Now, is it passed? No, this is not part of what's going on in Congress right now. This is a separate and distinct bill. The Wyden proposal on partnerships—and Wyden is Senate Finance Committee—and this would change partnership taxation forever. Something to really watch and monitor. So let's just kind of quickly go through some of these, because again, they're just proposals, but you should be aware of them.

So, number one. They want to have something similar, a reporting mechanism, similar to the Schedule UTP for corporations, that if you have an uncertain tax position for ASC 740-10 on your financial statements, then you're going to have to report that to the Service. And presumably, that will be like the 1120 UTP, Uncertain Tax Position. They want to do away with substantial economic effect rules under 704(b). They want to mandate that your interest, your allocations, have to follow your interest in the partnership. But they also have a special rule that says that if there's related parties who own 50% or more, they're going to have to do it in accordance with the net contributed capital. If you have pre-contribution gain under 704(c), you must use the remedial method. They'll do away with the traditional, traditional plus curative. It will be remedial. Now, right now, we know that you can make certain adjustments. Those adjustments are going to be, if you have a 754 election, you can make the adjustments under 743 or 734 on a distribution. Those will become mandatory. You're going to have to do it. 754 election won't exist. But 743 and 734 adjustments to basis? Those are going to happen for sales, for distributions. They would be mandatory.

It'll mandate revaluations of partnership property when there's a change in the economic relationship of the partners. Right now, that's optional under 704. It will be mandatory. With pre-contribution gain under 704(c), they want to eliminate the seven-year period, which says that if that contributed property with pre-contribution gain is distributed to a non-contributing partner within seven years, the contributing partner has to pick up the remaining pre-contribution gain. They want to eliminate that seven-year rule and say if it's distributed anytime and there's any 704(c) gain still left. Now, remember you now have to report that. Items M and N on the K-1 ask you. Did this person, did this partner contribute any property that has 704(c) gain or loss? And then, it says how much gain or loss is remaining at the end of the year? Those are now on the K-1.

This is going to be interesting. It proposes to eliminate guaranteed payments, whether it's guaranteed payments for services or guaranteed payments for use of capital. Everything will be, I don't know. Does that mean they get a W-2? Does that mean it's going to be treated like an S corp? Not quite sure. But eliminate guaranteed payments. Eliminate 736, so distributions will not follow to your extent of the profits. It's ordinary income and capital gain and all the complicated rules of 736(a) and (b). Eliminate that. They'll just be distributions. Make 707 disguised sale rules not a "gotcha," but self-executing. Practitioners, we're going to have to report that. If we suspect, if we think that it's possibly a disguised sale, we're supposed to report that ourselves.

Another provision says, well, under 708, it is not a termination if any person continues to carry on the business. Now that's interesting because what if all the other partners are gone? It's just one person continuing. How does that affect it? Again, they're talking about general concepts here. There's a lot of things in the weeds they have to get to. Get rid of 751. Remember the hot assets? On a sale, all inventory is hot, but on a distribution, only substantially appreciated. Get rid of substantially appreciated. All inventory will be hot on a 751, on a sale or on a distribution. Totally change the allocation of liabilities, not using the constructive liquidation scenario or the three steps for non-recourse debt, but basically allocate it in accordance with their profits. And the only exception would be there're special rules for related parties.

Eliminate any exception for publicly traded partnerships. All publicly traded partnerships will have to be taxed as corporations. And then, we know right now there's kind of a complicated thing with the business interest limitation, and you kind of track it and you suspend it at the partner level, and you wait to get excess income coming through. Totally change that. Everything will be limited. So, the interest limitations on 163J would be at the partnership. And by the way, S level, also same rule is what they're proposing, will be at that level. And so, only to the extent that it's allowed to be taken at the partnership, would you then flow through to the owners and they would take it then obviously at that point.

So, major changes to partnerships. There's probably going to be changes. They're saying partnership tax is too complicated. They admit that even the government doesn't understand the rules, it is so complicated. We know we had a big change in 2020 going to tax basis capital account reporting. This is just another attempt to—I'm going to use the word—simplify. We never know what's going to happen when the IRS gets involved with the regs because we'll have hundreds and hundreds and hundreds of pages of regulations if this goes through. So, is it going to go through as it is? We don't know. It's a proposal. But there seems to be bipartisan support for something like this, some major overhaul that really does add some simplicity to it. So, let's just keep that and track it.

I want to thank you for joining me, and we'll see you again next month. Be safe.

Current Material: Experts' Forum

By Ian J. Redpath, JD, LLM

A. *Boechler, P.C. v. Commissioner*

SCt Docket No. 20-1472

The Supreme Court has agreed to decide whether the time limit in §6330(d)(1) is a jurisdictional requirement or a claim-processing rule subject to equitable tolling. This section establishes a 30-day limit to file a Tax Court petition for review of a Collection Due Process (CDP) determination. While this is a CDP case, it will have an impact on the general filing limits with the Tax Court.

Boechler, P.C., a small law firm, timely requested a CDP hearing challenging the IRS's intent to levy its property to pay a tax penalty. After the hearing, the Appeals Officer sent a Notice of Determination sustaining the levy. Boechler mailed a petition to the Tax Court seeking review of that determination. The petition was mailed one day later than the 30-day period for such petitions. It was rejected by the Tax Court as untimely filed and rejected the argument that the delay should be excused on an equitable tolling basis. The court held the timing is jurisdictional so the court had no jurisdiction. Boechler appealed the Tax Court's decision to the Eighth Circuit, which affirmed the Tax Court's decision.

The Eighth Circuit's decision added to an existing conflict among the appellate courts. The Eighth and Ninth Circuits have held that the time limit is a jurisdictional filing deadline. However, the DC Circuit reached the opposite conclusion with respect to another Tax Court filing deadline with functionally identical language.

B. *Taryn L. Dodd v. Commissioner*

TC Memo 2021-118

The Tax Court held that a partner was liable for taxes on her distributive share of income from the partnership, regardless of whether she actually or constructively received the share. Under §702(a), she is taxable on her distributive share of the §1231 gain whether or not it was distributed.

In 2013, a partnership in which Ms. Dodd was a partner sold a building. The partnership sent Dodd a K-1 showing $1 million as a net section 1231 gain for the year. Also in 2013, the partnership paid back a loan it had taken out in 2011 on which Dodd was a co-borrower. Her share of the debt relief was more than $1 million. She did not pay income tax on the gain, arguing that she did not actually or constructively received the money because it was used to pay back the loan. [Reg §1.451-2] The Tax Court disagreed.

C. TIGTA Audit Report No. 2021-40-070

Calls for Refining Complex and Inconsistent EITC and ACTC Rules

The Treasury Inspector General for Tax Administration (TIGTA) has released an audit evaluating the reasons for disallowance claims for the earned income tax credit (EITC) and additional child tax credit (ACTC). It also provides assistance related to the examination process.

According to the audit, during 2019, IRS's Automated Questionable Credit, Automated Underreported, and Examination programs adjusted more than $1.9 billion in EITC and ACTC claims on slightly more than 617,000 tax returns. The audit found that addressing "complex and inconsistent" eligibility rules could be a way to lessen unintentional errors and increase participation. "Changes that could help include simplifying the qualifying child relationship rules, making Taxpayer Identification Number (TIN) requirements consistent, and making the definition of income consistent," TIGTA said.

The audit noted that the IRS does not have correctible error authority to address claims with income reporting errors. "Without this flexibility, the IRS must audit each tax return to prevent or recover unsupported refundable tax credits," TIGTA said. "As such, the majority of identified claims with income reporting errors are not addressed," it added.

The TIGTA also found that the multiple use of the same qualifying children continues to result in significant improper refundable credit payments. In addition, the audit stressed that "some egregious" multiple TIN uses are not being addressed. "It is crucial that the IRS notifies parents and legal guardians when it knows a child's TIN has been used multiple times on different tax returns so the parent or guardian can take the steps necessary to protect their child's identity," TIGTA said.

D. *U.S. v. Robin S. Richards*

DC IN

The District Court upheld a bankruptcy court decision that found that the IRS was not entitled, under the farmer's Chapter 12 reorganization plan, to retain the debtor's overpayment to apply to the debtor's other tax liabilities.

The Richards family was engaged in a family farming business. They suffered losses due to weather conditions and market price declines. When the primary lender refused to renew their loan, the family was forced to liquidate the farm's assets. In 2016, virtually all the farm's equipment, vehicles, and other personal property assets were liquidated. The proceeds were paid over to the primary lender and to other lenders with purchase money security interests in the property. In 2018, after filing their Chapter 12 bankruptcy petitions, they sold additional farmland to pay debts. These sales generated income tax liabilities which they were unable to pay.

The family sought relief from the tax liabilities generated by the asset liquidations. Under their Chapter 12 reorganization plan (Plan), *which was confirmed without objection*, their federal and state tax obligations were divided into two categories: (1) tax liabilities for income arising from the sale, transfer, exchange, or other disposition of any property used in the farming operation (Section 1232 Income); and (2) tax liabilities arising from other income sources (Traditional Income). The Plan provided that tax liabilities arising from Traditional Income would retain priority status but the Section 1232 tax liabilities, *regardless of when incurred*, would be treated as general unsecured claims and dischargeable upon completion of the Plan if not fully paid.

After the Plan was confirmed, the IRS objected to the Plan because of the way the debtor calculated its Section 1232 liability. The debtor's calculation of its Section 1232 liability revealed that they overpaid the IRS's claim by $5,574. The debtors wanted this amount refunded, but the IRS wanted to apply (or offset) the overpayment to the Section 1232 liability that would otherwise be discharged under the Plan. The Bankruptcy Court held that the IRS was not entitled to offset the refund against Section 1232 liabilities because it would favor an unsecured creditor. The District Court agreed.

E. Practice Unit: Section 263A Costs for Self-Constructed Assets

The IRS has released a Practice Unit that provides guidance on capitalizing the costs of self-constructed assets. Self-constructed assets are assets produced and used by the taxpayer. They are not sold to customers in the regular course of business.

Taxpayers are required to capitalize certain costs incurred to produce self-constructed assets such as material costs, labor costs, and other incidental costs. These costs fall into three categories:

- IRC §471 costs, which include any cost (other than interest) that a taxpayer capitalizes to its self-constructed assets in its financial statement.

- Additional §263A costs, which are indirect costs that are not included in a taxpayers §471 costs but are required to be capitalized under §263A. These costs include indirect labor costs, officer compensation, and employee benefits, to name a few.

- Interest costs capitalized under §263A(f).

This Practice Unit summarizes how to apply the current regulations under §263A to these costs.

F. Distributions of Property by Corporation to Shareholder

TD 9954

The IRS issued final regulations to reflect changes made to §301 by TAMRA ‘88. These provide that THE amount of distribution is THE amount of money received plus FMV of property received, and that basis of property received in §301(a) distribution is FMV of such property. The Proposed Regulations issued in 2019 were adopted with only clerical changes.

G. *Patrick Combs v. Commisioner*

CA 9

The Tax Court found that a corporation’s payments of the owner’s personal expenses were constructive dividends and the taxpayer’s reliance on a tax planner’s advice regarding the payments was not reasonable or in good faith

Patrick Combs was the sole shareholder of Good Thinking, Inc. He was a motivational speaker whose speaking fees were paid to Good Thinking. He was paid a small salary and reimbursed some of his personal expenses which were not included in his income in accordance with advice provided to him by a financial planner

The IRS audited Combs for tax years 2010–2012 and determined deficiencies and penalties for all years, alleging the payments of the taxpayer’s personal expenses were constructive dividends paid to the taxpayer. The Tax Court agreed with the IRS and found that the taxpayer’s reliance on a tax planner’s advice regarding the payments was not reasonable or in good faith to abate penalties.

The Ninth Circuit upheld the Tax Court.

H. *Charles H. Leyh v. Commissioner*

157 TC No. 7

In a case of first impression, the Tax Court held that an individual who paid for his then spouse’s health insurance through a cafeteria plan with pre-tax payroll amounts could also deduct, as alimony, the premiums paid.

In 2014, the taxpayer, his divorce pending, entered into a separation agreement with his spouse according to which he agreed to pay for his spouse’s health and vision insurance through an employer’s cafeteria plan until the final decree of divorce was granted. As a result, the payments were made by pretax reductions to his salary. Thus, he paid no income tax on that portion of the wages used to pay for the insurance.

The taxpayer filed a separate Form 1040 for 2015 and excluded the insurance payments while also claiming an alimony deduction for the portion of the insurance payments covering his spouse. The IRS disallowed the alimony deduction on the grounds that the alimony deduction was an impermissible double deduction as the insurance payments made to the cafeteria plan were excluded from his income.

The Tax Court agreed with the taxpayer. It noted that if they had filed a joint return for 2015, they would have had:

(1) An exclusion from gross income equal to the insurance payments made by the cafeteria plan,

(2) No alimony deduction for that amount, and

(3) No alimony income inclusion for that amount.

Because they filed separately, the spouse was required to include the alimony payments in her income. The result is that the husband is permitted a corresponding deduction for those payments to match the income recognition by the spouse, not against the cafeteria plan amounts excluded from his income.

The Court also rejected the IRS's contention that §265(a) disallowed Charles's alimony deduction because the insurance payments were allocable to wholly tax-exempt income. It noted that it has never applied this section to disallow an alimony deduction where the supposed "exempt" income at issue was actually included in gross income by a different taxpayer.

I. *Thomas A. Connelly v. U.S.*

DC MO

A District Court determined that the proceeds of a life insurance policy a corporation received upon the death of its majority shareholder increased the value of the corporation (and the shareholder's shares) for estate tax purposes.

The Connelly brothers (Michael and Thomas) owned a roofing and siding business. The brothers entered into a stock purchase agreement that required the company to buy back the shares of the first brother to die (buy-sell agreement). The company bought life insurance to ensure it had enough cash to make good on the agreement. When Michael died in October 2013, the company repurchased his shares for $3 million, and Michael's Estate paid estate taxes on the $3 million. But the IRS disputed the estate's valuation of Michael's shares and assessed additional estate taxes of over $1 million. The Estate argued that the buy-sell agreement controlled the shares' valuation.

A decedent's gross estate includes all the decedent's property (real, personal, tangible, and intangible) valued as of the decedent's date of death. [Reg. §20.2031-1(a)] Generally, the fair market value of any property is determined without regard to a buy-sell agreement; however, there are exceptions. [§2703(b)] To qualify for this exception to the general valuation rule, a buy-sell agreement must (1) be a bona fide business arrangement; (2) not be a device to transfer property to members of the decedent's family for less than full and adequate consideration; and (3) have terms similar to agreements negotiated between persons in an arms' length transaction. The regulations require a buy-sell agreement to (1) have a fixed and determinable offering price; and (2) be legally binding on the parties during life and after death. [Reg. §20.2031-2(h)]

The district court held that the company's value included the insurance proceeds. The buy-sell agreement did not qualify for the exception to the general valuation rule because the Estate failed to show that the buy-sell agreement wasn't a device to transfer wealth to Michael's family members for less than full and adequate consideration. The Estate's process for determining the redemption price of Michael's stock excluded a significant asset (the life insurance proceeds), which indicated that the buy-sell agreement was a testamentary device. In addition, the redemption price did not include a control premium for Michael's majority share of the company, which indicated that the redemption price was not full and adequate consideration. Also, the Estate failed to show the buy-sell agreement's terms were similar to those in agreements negotiated at arms' length, and it did not rely on a Certificate of Agreed Value or follow the detailed appraisal mechanism in the buy-sell agreement to determine the redemption price for Michael's shares. Instead, the Estate and the company completely disregarded the buy-sell agreement and negotiated their own value, which was less than the value of the life insurance proceeds.

J. IR-2021-193; Notice 2021-55, 2021-41 IRB

Capital Gain Relief for Farmers and Ranchers

The IRS announced that farmers and ranchers who were forced to sell livestock due to drought may have an additional year to replace the livestock and defer tax on any gains from the forced sales under §1033(e). To qualify, they must have sold livestock on account of drought conditions in an applicable region. This is a county or other jurisdiction designated as eligible for federal assistance plus counties contiguous to it. Notice 2021-55, 2021-41 IRB, lists applicable regions in 36 states and one U.S. territory.

The relief generally applies to capital gains realized by eligible farmers and ranchers on sales of livestock held for draft, dairy, or breeding purposes. Sales of other livestock, such as those raised for slaughter or held for sporting purposes, or poultry, are not eligible. It should be noted that the sales must be solely due to drought, causing an area to be designated as eligible for federal assistance. Livestock generally must be replaced within a four-year period, instead of the usual two-year period. The IRS is authorized to further extend this replacement period if the drought continues.

The one-year extension gives eligible farmers and ranchers until the end of their first tax year after the first drought-free year to replace the sold livestock. Details, including an example of how this provision works, can be found in Notice 2006-82, 2006-2 CB 529. This applies to extreme or severe drought conditions during any week between September 1, 2020 and August 31, 2021 as determined by the National Drought Mitigation Center.

Eligible farmers and ranchers whose drought-sale replacement period was scheduled to expire on December 31, 2021, in most cases now have until the end of their next tax year to replace the sold livestock. Because the normal drought-sale replacement period is four years, this extension impacts drought sales that occurred during 2017. The replacement periods for some drought sales before 2017 are also affected due to previous drought-related extensions affecting some of these localities.

K. Senator Wyden Partnership Reform Draft Legislation

Senator Wyden has introduced a legislation discussion draft that would significantly alter Subchapter K, partnership taxation. There appears to be bipartisan support for changes; and the IRS agrees that the current rules are far too complicated. The complexity has resulted in fewer audits and a more difficult time in identifying potential mistakes. While only a discussion draft, this far-reaching proposal should be reviewed for any clients considering a choice of entity.

Among the proposals:

- Make technical amendments under §701 corresponding to the Bipartisan Budget Amendment (BBA) provisions. The change is intended to "allow the IRS to enhance reporting requirements of partnership tax positions by aligning tax reporting with Financial Accounting Standards Board (FASB) reporting, which may require the reporting of uncertain tax positions that could trigger an entity-level liability."

- Eliminate the substantial economic effect test under §704(b) and mandate partners' interests in the partnership as the general rule for testing partnership allocations. Certain partnerships where related persons own 50% or more would be required to allocate items consistently based on partner net contributed capital.

- Mandate the use of the remedial method for all §704(c) allocations.

- Mandate revaluations of partnership property upon a change in economic arrangement of the partners. These revaluations currently are optional under Reg. §1.704-1(b)(2)(iv)(*f*).

- Eliminate the seven-year limit for 'mixing bowl' transactions under §§704(c)(1)(B) and 737, such that the rules would apply to contributed property regardless of the time since contribution.

- Permit Treasury to prescribe rules under §705 allowing partners to estimate adjusted basis in their partnership interests in scenarios other than partnership terminations.

- Eliminate guaranteed payments under §707(c) and mandate that all payments to partners for services or use of capital that are not in substance distributions be treated as payments to a partner not acting in its capacity as a partner under §707(a).

- Eliminate special provisions for retiring or withdrawing partners under §§736 and 761.

- Clarify that §707(a)(2)(B), governing the 'disguised sale' of partnership interests, is self-executing and remove the capital expenditure exception from the disguised-sale rules.

- Clarify that a partnership is not terminated under §708 if any part of the business is carried on by a person who was a partner in the prior partnership or by a person related to any of those partners.

- Conform §751(b) to §751(a) by eliminating the "substantially appreciated" inventory requirement on distributions.

- Modify §752 to allocate liabilities in accordance with partnership profits unless a partner or related person was the lender.

- Make adjustments under §§734(b) and 743(b) mandatory.

- Eliminate the exceptions from corporate treatment for publicly traded partnerships under §7704.

- Amend §163(j)(4) to make the business interest limitation fully apply at the entity level for partnerships and S corporations.

- Revise §852(b)(6) such that RICs would be required to recognize gain upon distribution by a corporation of built-in gain property.

- Revise §52 to provide that any taxpayer engaged in an activity in connection with a trade or business or for-profit activity, including a foreign entity, is subject to the aggregation rules under Section 52.

It should be noted that the Biden Administration, as set forth in the Treasury Green Book, has other far-reaching changes proposed for partnerships, such as making contributions of property and distributions of appreciated property taxable events.

A. Discussion Problems

Your client, John, recently passed away and was a 51% shareholder in a corporation owned with Sammi, his sister. There was a buy-sell agreement in place with a valuation mechanism. The executor and Sammi have agreed to transfer the shares at a separately agreed value that is less than the insurance proceeds from the insurance funded buy-sell.

Another client, DiPasquale Farms, has been severely affected by drought. This has caused the sale of numerous livestock during 2021.

A large portion of your practice is businesses that operate as LLCs taxed as partnerships.

Required:

1) Assume that John's executor hires you to do an evaluation of the corporation for estate tax purposes. What consideration, if any, should you give to the buy-sell agreement?

2) Advise DiPasquale Farms on available relief related to the sale of livestock as the result of a drought.

3) What should you consider if your practice is heavily into partnerships?

B. Suggested Answers to Discussion Problems

1) The major concern is whether the life insurance proceeds will increase the value of the estate for estate tax purposes. A decedent's gross estate includes all the decedent's property (real, personal, tangible, and intangible) valued as of the decedent's date of death. [Reg §20.2031-1(a)] Generally, the fair market value of any property is determined without regard to a buy-sell agreement; however, there are exceptions. [§2703(b)] To qualify for this exception to the general valuation rule, a buy-sell agreement must (1) be a bona fide business arrangement; (2) not be a device to transfer property to members of the decedent's family for less than full and adequate consideration; and (3) have terms similar to agreements negotiated between persons in an arms' length transaction. The regulations require a buy-sell agreement to (1) have a fixed and determinable offering price; and (2) be legally binding on the parties during life and after death. [Reg §20.2031-2(h)] Care must be taken to assure that all of the provisions of the exception are met. This may be difficult if the parties are ignoring the terms of the agreement.

2) In IR-2021-193, 9/24/2021; Notice 2021-55, 2021-41 IRB, the IRS announced that farmers and ranchers who were forced to sell livestock due to drought may have an additional year to replace the livestock and defer tax on any gains from the forced sales under §1033(e). To qualify, they must have sold livestock on account of drought conditions in an applicable region. This is a county or other jurisdiction designated as eligible for federal assistance plus counties contiguous to it. Notice 2021-55, 2021-41 IRB, lists applicable regions in 36 states and one U.S. territory. The relief generally applies to capital gains realized by eligible farmers and ranchers on sales of livestock held for draft, dairy, or breeding purposes. Sales of other livestock, such as those raised for slaughter or held for sporting purposes, or poultry, are not eligible. It should be noted that the sales must be solely due to drought, causing an area to be designated as eligible for federal assistance. Livestock generally must be replaced within a four-year period, instead of the usual two-year period. This has been further extended.

3) There is a proposal to significantly revise partnership taxation; it has some bipartisan support and is also looked upon favorably by the IRS. The Wyden draft proposal and the Treasury Green Book on the Biden proposals should be carefully monitored.

PART 2. INDIVIDUAL TAXATION

Offers in Compromise

The Internal Revenue Service may accept an offer in compromise on three grounds—doubt as to liability, doubt as to collectibility, and for effective tax administration. However, there are certain conditions that must be met before an offer in compromise can be considered. Ian Redpath and Larry Pon discuss those conditions along with the components of an offer package and the payment options available if an offer is accepted.

Let's join Ian Redpath and Larry Pon as they discuss offers in compromise.

Mr. Redpath

Larry, welcome to the program.

Mr. Pon

Hello, Ian, how are you?

Mr. Redpath

Great. It's great to have you back again, and this is really an interesting topic. Honestly, when I talked to you about it I really didn't know why we had to do this, because I've heard, "Hey, the IRS is settling for pennies on the dollar, send in now," and "We had $80,000 in taxes due and it was settled for $22.32." And then, I read at the bottom of the television ad, "This may not be typical."

I hear these ads all the time. I hear them on the radio. I watch them on television and I have had clients who say, "What do you mean? We could settle for pennies on the dollar. I heard the IRS has the fresh start initiative, jump in now. You know, the IRS just doesn't want to go after you anymore. So, come on in and they'll settle it for everything." I think I've kind of summarized what we hear about this area. What is that really talking about, That whole area?

Mr. Pon

Right. As tax professionals, I assume none of those are us that are doing those commercials, or advertising, whatever. Of course, the advertising you hear on TV, radio, internet are all extreme examples. There might be a grain of truth for them; but many of these people who do this are always in trouble with the regulators, the state, and different entities. You've got to watch out for that.

Mr. Redpath

Let me tell you, just because I want to comment on what you just said. My firm had a $250,000 judgment against one of the firms—I won't say which one—that no longer is advertising. And one of the reasons is that the person who used to be their spokesperson who started the firm, he got indicted. There's a lot of firms, so that's just exactly what happened. We have nothing to collect from, but some of these firms have been in and out; and the IRS has gone after some of these people for everything from promoting abusive tax schemes. Yes, sometimes you hear about a firm for two years, and then you never hear anything again, and then you read something that someone's been indicted. Again, that's not saying everything. There are some very legitimate and there are some really, really good law firms out there and accounting firms that handle these things and are very competent, but we hear all the things in the paper. And I think what our practitioner viewers need to know is the unreasonable expectations that are established by our clients by looking at that.

Mr. Pon

Right, and it's true that going forward, there's going to be increased IRS enforcement. There's going to be a lot more confusion with taxes. People might be owing money, so they're going to need our help more than ever, and they should not call these people who are advertising. They should look to us first. I think what's important today is for us to go over what we can do to help our clients.

Mr. Redpath

Okay. And that's really the collection process, because you just said it, that there's a lot of things that are going on right now. And honestly, there's been so many changes and confusions that it's not going to be unusual for there to be some mistakes on a return. Because, I mean, they've changed things, they've changed things retroactively. There's been all these elections to make, and how did you handle something? There's talk about really increased enforcement. I think you're right, we're going to see more and more of the situations where our clients are going to receive levy notices, or they're into collection because they haven't paid, and now they come to you. And the question is, now what do we do? A whole different thing would be, there's the CDP, collection due process; and there's the CAP program, collection appeals. Those are different programs. We're going to focus today on the offers in compromise. So, what happens? I mean, you're in collection now. What happens?

Mr. Pon

Before we talk about being in collections, what happens before collections? How do you get there? There's multiple ways of getting there. Number one could be you file a tax return, you owe taxes, you just can't pay it, and then you just file the return, which we recommend because it helps minimize some penalties versus not even filing. That's one way. Filing a return, there you could owe some taxes. Or you don't file a return, the IRS files one for you; and then of course, that's not ever prepared correctly. That's another way of getting to a collections problem. And the third way of getting to a collections problem is you had an audit, and the audit could be a various form. It could be a CP-2000, which many people ignore, or we don't know about it. We don't know about it, because they don't tell us about, could be a CP-2000. It could be a correspondence audit. And we've seen a lot of correspondence audits where you give them a stack of backup information, you do your best, and it all gets disallowed for whatever reason.

Mr. Redpath

Larry, 73%, the last statistic, 73% of all audits today are correspondence audits.

Mr. Pon

Yes, and I talked to an IRS manager about that. I'm very close to an IRS manager, and I asked her about these correspondence audits. She goes, "Yes. You know, I assign those to my least liked employees. So, whoever is on our bad list, they get the correspondence audits." It's never the most experienced, competent employee processing the correspondence audit. Of course, the third way is a field audit or an office audit where the IRS does an audit and boom, they just disallowed everything. It could be right, it could be wrong. But that's what can cause people to get first into a collections problem.

Mr. Redpath

Could you just briefly mention, because you brought something up that causes a lot of confusion and it's ignored a lot, but that CP-2000, because that's technically not an audit.

Mr. Pon

It's not an audit.

Mr. Redpath

People get really confused about what this is. Can you briefly tell us what is that CP-2000? Because I think practitioners need to be aware of that if they aren't, and especially if a client comes, but a lot of younger practitioners are certainly not aware of what the CP-2000 is.

Mr. Pon

Right. A CP-2000 is not technically an audit. It's not an audit; except when a client gets it, they say, "Hey, you got me audited," or whatever. Well, it's real simple. You didn't give me a 1099. Mostly they come from not giving a 1099-B from a brokerage account. Sometimes, it happens when a spouse opens an account and doesn't tell the other spouse. It's like, "What's this account?" Or, a 1099 for interest or dividend from an account they didn't tell us about. That's very common. It's a matching thing.

As seasoned professionals, when we do a client's return, we look at prior-year returns and we kind of know which brokerage firms they have. And we'll say, "Hey, I don't see a 1099 from this firm. Do you have one? Yes, or no, or whatever?" If we have prior history, that helps us avoid those problems. The key is avoiding the CP-2000's, but it happens.

In my organizer's checklist, I give a sheet called the IRS no's prevention checklist. And on that I say, "Give us your 1099's, your 1099-Q's. If you're taking money for a 529, 1099-R's," because some clients "self-censored." They go, "Oh, it's not taxable, so I didn't give it to you." I said, "It might not be taxable. We still need to report it." Like the 1099-Q. The 1099-R? Yes, I know you rolled it over. That's the most common CP-2000, right?

Mr. Redpath

Yes, you know what? I just had one with a client; and actually, it was a mistake, because what they did was a trustee-to-trustee rollover. And it was reported as just a distribution.

Of course, the IRS says, "Hey, you didn't report this distribution. We got it." You know, we just sent back and said, "Here's a copy. Here's where it came out. Here's the account it went to, the trustee-to-trustee rollover. End of story." So, it was over, but that's not an unusual type.

Mr. Pon

Before we even get to a collections issue, that's my first question. Client comes in, or a new client comes in and says, "I owe the IRS $100,000. What do I do?" Well, as a first, let's see if that number's right. That's the first thing we do. Before we start dealing with all these things on collections, because the commercials here on TV are all the ones, they just go blasting straight into an offer in compromise and charging a very large non-refundable fee. But first, let's make sure that the number's correct. And we need the taxpayer's help with that.

Mr. Redpath

I have a good example of that, Larry. I had someone come in my office and they said, "We talked with "blank," and they said we can settle this entire matter for 14,000 and some odd dollars. And I said, "Well, that's really interesting, because number one, you haven't filed tax returns for about eight years. So, what are we compromising? We don't even know what your liability is. No one's even filed anything. So, I can't tell you what your liability is. And how can you possibly [compromise]?" But they gave them a number, $14,000—$14,000 was an odd number—and this will settle it. And I went, "Essentially, what they're going to do is file an offer in compromise, come back; it's going to be denied." "Oh, we're sorry. The IRS denied it, but we can appeal that if you want." And then charge them.

Mr. Pon

For a low fee of, whatever, right? Basically, they're just stretching it out.

Mr. Redpath

Well, the first thing we have to do is file your back tax returns, and then we'll decide how to move forward.

Mr. Pon

Exactly. In the collection process, first of all, number one, make sure the amount is correct. If the amount's correct, okay. Two, what is in that number of the amount due? Are there penalties involved? Can we get abatement of any of those penalties? You know, one of our most powerful tools on the federal level is this thing called the first-time abatement. If we can take advantage of that, we look like a real hero. I've done that before. I've had clients where they had a big penalty, but they qualify for first-time abatement. They got it abated, and there's no dollar limit. It could be a very large amount, and you could be a big hero.

So, number one, take a look if we can abate any of the penalties. Or if there are penalties, is there a reasonable cause for abatement of any of those penalties? Number one is, okay, we got the amount that's due. Let's see what we can do to reduce it. Penalties is one thing we can reduce. We can't reduce interest, but we can reduce penalties.

Mr. Redpath

That's a really good point because a lot of people don't realize that, that the IRS, their hands are tied. So, you'll go in and say, "Well, we have reasonable cause. Why can't we get rid of the interest?" Because, that compounds daily. That really runs up, and you have to understand as you go in that their hands are tied. They cannot.

Mr. Pon

There are rules to follow, but interest—we can't abate interest, but we can certainly reduce interest. When you reduce the amount due, it reduces the amount of penalties.

Okay. After we figure out the dollar amount, and we try to squeeze whatever abatement we can, and that's when we can't get the taxes any lower. It is what it is. Then we look at our options for paying. Well, can they pay it off? Can they not pay it off? Can we negotiate an installment agreement? When were these taxes assessed? Because in some cases, we negotiate an installment agreement as low as we can and try to ride the statute of limitations; and the statute of limitations for collections is 10 years. So, it's really important to look at the date of assessment on the transcript; and then, you can count the time from there.

Mr. Redpath

You know, Larry, you just brought up something that I think it's really important when a client comes in, because one of the things that I like to do, right away, is I'm going to check the transcript. I want to see what was assessed, when was it assessed, or what actions have been taken; because we're going to talk about offer in compromise, and that tolls the statute.

I had a case once where they filed an offer in compromise. He didn't follow it. He had an installment agreement and obviously it's to pay. I mean, this was going on, and on, and on. But when I looked at the transcript, they went to federal court to reduce the assessment to a judgment against him. And we were able to throw out over two and a half million dollars in taxes because of the statute. The statute had been reinstated, so it was running again and the IRS had miscalculated a significant amount. But looking at that transcript it's really important in any collection matter, to see what is the IRS showing and what are these dates?

Mr. Pon

Yes. It's important if you're going to take on a collection case, always get a power of attorney, Form 2848. So you can get a copy of the transcripts, so you can get that information, and then you can review that information. And two things that tolls the statute of limitations. One is an offer in compromise. So, when you file the offer in compromise, the statute of limitation stops. The other thing that tolls the statute of limitations is bankruptcy proceedings.

I had a lawyer that owed over a million dollars. He didn't really make that much money; but he owed over a million dollars because he just didn't pay his taxes for 20 years. So, he owed over a million dollars. He kept running all over town hiring these so-called offer in compromise people to keep filing offers in compromise. I saw five offers in compromise filed, and they were either rejected, or they might've been accepted, but he never fulfilled them. He never fulfilled the terms of them. And then, he tried to file bankruptcy, and so he added 12 years to the statute of limitations.

Look, he could have ridden out the statute of limitations if he didn't play any of these games.

Mr. Redpath

You and I were just talking about that. That's one of the things you have to look at is, and I mentioned to you, I had somebody that came in and I said, "You've got eight months left on the statute of limitations." Again, he had heard the ad, "Let's settle for pennies on the dollar." And I said, "You may be settling for or paying nothing on the dollar if you can ride out the next eight months. I couldn't tell him I'm not going to file an offer in compromise for you at this point. I think that would be almost malpractice for me to do so.

Mr. Pon

Right, and here's another thing that's very important too. If your client owes a sufficient enough amount of money, they get assigned their own revenue officer. As seasoned professionals, we get to know our local revenue officers. They're the ones who come knocking on doors and try to talk to the taxpayer or whatever. So, I've established some relationships with revenue officers. And one advantage of having a good professional cordial relationship is I've been able to get them to assign a non-collectible status on many of my clients, because I was able to convince them that, "Look, her job," and this was back in the recession or a bad time. "Dude, my client's a realtor. Real estate's not selling now. It's not going well. Her income's very unpredictable. So, we cannot commit to an installment agreement with her."

So, the revenue officer said, "Okay, I'll check the box that it's uncollectible." And it's like, "Wow!" And she owed over $100,000, but her status, when you go to the transcript, there's a line on the transcript, it says non-collectible and no letter. So, she gets an annual letter from the IRS saying, "Oh, by the way, you still owe us money." And we're tolling the statute of limitations for her, but we're keeping her nose clean in these current years. So, she's paying her taxes; and if she has any refunds, the IRS keeps the refunds to pay off the back taxes.

That's another way of doing that. I have negotiated installment agreements as low as we can, in one case, $100 a month. I got to $100 a month riding the statute of limitations. And calculate the withholding as close as possible so they don't have refunds, so the refund money doesn't go to back taxes.

Mr. Redpath

Yes. And I think one of the things too we should make our viewers aware of it, because I had a client come in, the one I mentioned to you. They just weren't filing taxes, and they were kind of assuming that they had made a lot of money before and they were employees and they had a lot of withholding and they said, “Well, we overwithheld in all those years.” Well, yes, except the IRS will not let you carry it forward beyond three years. So, carried forward, carried forward. Oh, you’re in trouble.

So, that’s one of the things to keep in mind is that the IRS doesn’t apply it going forward beyond that three-year period. I mean, they never had asked to have the refund applied. IRS said, “Hey, we’re not applying it to those additional taxes. Sorry.” So, keep that in mind. And you have these clients come in and the process itself, there’s a lot of different options there.

And one of the things I think we should have our viewers be aware of is the fact that the IRS has started a new program called Tax Pros, and they want you to go on the internet to do your 2848, your power of attorney. And you can’t do it, approve it, but it speeds the process up because once your client goes on and gets an account, and you can do that with them. As soon as you file it, it automatically goes in and is put into the system with your CAF number. Keep that in mind that the preferred way for the Service now is not by paper. It’s by this new Tax Pros that’s on the IRS website.

You also mentioned installment agreements. There’s a streamlined installment agreement on the IRS website. So you can go in and get an idea; but as you said, that doesn’t mean you don’t still negotiate. You can submit an offer and see what they say.

So, offer in compromise. Now we’re at this point where we’ve decided this is the way to go. We’ve reviewed the transcripts, we’ve done everything we need to do.

Well, let me go back, because you mentioned something. Uncollectible, because that’s really part of this process, and the IRS usually wants one of the forms that we’ll talk about—the 433, A or B, the financial. I had a similar case where I had somebody who had huge medical bills. They had a child that had this rare disease; and they were spending like $3,000 or $4,000 a month to get these treatments. And the IRS put them in uncollectible; and they just said, “Well, they’re not collectible. I mean, we understand.” But, you have to file the financial statements, the 433, in order to get that. What is the offer in compromise? And then we’ll get into the process of getting into it. What exactly is it?

Mr. Pon

Offer in compromise is much later in the process here. We’ve got taxes due. Our client’s having a tough time keeping up with their installment payments, and they just want relief. They want relief. An offer in compromise is an agreement you have with the IRS to settle for the debt for less than what the amount is due. It’s basically a process of doing that. There’s different ways of applying for the offer in compromise. Now, the thing is there are some specific conditions you have to meet to keep the offer in compromise. Because that’s another problem where, like this lawyer, he would keep getting these offers in compromise accepted, but they kept failing because he never met the conditions.

The conditions are you’re supposed to keep filing your tax returns, stay current on your current-year taxes; and if there’s any refunds, the IRS will keep them to pay for the back taxes; and most importantly, pay the amount that you agreed upon.

There’s a timing. You can either pay it at the time they agree to it. You can negotiate some payments over a very short amount of time. There’s different ways of doing it… we make sure that we’re all paid up, and that you don’t file bankruptcy, that’s the other agreement that we have here. So, it’s important that you stay on top of your taxes. If you don’t file your taxes, they’re going to invalidate the offer in compromise that you agreed.

Mr. Redpath

And that’s the basic situation with the guy I was mentioning. He had had several offers in compromise, but every one, he violated.

Then you get to the point of them saying, “No! We’re not going to offer anything.”

Mr. Pon

Exactly. The form you file for the offer in compromise is Form 656. There’s a 656 and a 656-L if you’re filing for as doubt to liability. The most common way a lot of people file for offer in compromise is… There’s three ways to file for offer in compromise. One is doubt as to collectibility. That’s the most common way people file for offer in compromise. Doubt as to liability, and I’ve done that numerous times, and I will continue to do it, and I’ll explain a little later here.

Mr. Redpath

Yes. You're going to have to, because, traditionally, the IRS has taken the position that pretty much, "Hey, that liability has been established," but we've been doing it, and more and more people are saying that they're trying to use that. So, I think we're going to talk about it.

Mr. Pon

We're going to talk about the doubt as to liability, and then there's what they call ETA, effective tax administration. The effective tax administration. So, yes, those are the boxes that you check in how you're filing offer in compromise. But the most important way to get these accepted is, you've got to follow the instructions, read the instructions very carefully. And the IRS is very helpful too, because they have a checklist at the back of the form with the check boxes to make sure that you include a cover letter saying, explain why you deserve relief. What's the story? What's going on here? Because, the OIC officer is a fresh set of eyes. They don't know anything about you, and all they're looking at is transcripts and history here, but they don't know anything about you. Like you said, "I had a heart attack. I can't work anymore," or, "I'm on disability," or, "My landlord evicted me. I don't have a place to live," or, "My business got evicted. So, we're no longer in business." Those sorts of thing.

Mr. Redpath

I think, Larry, what you're saying is really important, because it's not just the form. It's the explanation as to why you can't pay. That's really going to be the tipping point on a lot of these is the reason you can't pay, and the reason that you're offering what you're offering. One thing though, and again, this is what people don't understand when they hear all those ads is, the IRS basically will not accept an offer if it is less than your net worth plus what they can collect over the remaining period. I mean, yes, it's possible to settle an $80,000 debt for $100. It's possible.

Mr. Pon

It's possible. That's for someone who has zero. "I have nothing. I literally have nothing. I'm homeless."

If you're homeless, you'll probably get that deal.

Mr. Redpath

Right. Very unique circumstances. Extremely unique, and that's what the client, they don't understand that. You have to explain it to them that this is kind of the minimum we have to offer, unless we have some extreme circumstance that we can explain.

Mr. Pon

We've had people that owes a $100,000 to the IRS, they don't want to pay it. That's the only reason. They just don't want to pay it. "Hey, Larry, can you negotiate a deal? I'll pay $10,000 towards that." I go, "Well, that's kind of hard. Your brokerage account has $10 million in it. Your 401(k) plan has $1,500,000, and you're making 300,000 a year. I don't think the IRS is going to accept your offer, but we can go and file it, and guess what? I'll charge you a non-refundable fee to do that."

But no; ethically, I can't do that, right? I mean, I can't ethically do that. I won't do that. And that person's probably not going to continue as a client if they keep insisting on that.

Mr. Redpath

Well, honestly, I'm not sure you want them as a client.

Mr. Pon

No, exactly! Exactly.

Mr. Redpath

Those aren't the ones that you want to keep as a client, either.

What are those 453-A and 453-B?

Mr. Pon

433, 433.

Mr. Redpath

Oh, 433, I'm sorry. 433-A and 433-B. What are those forms?

Mr. Pon

I tell my clients, that's kind of like a loan application, but it's the opposite of a loan application. On a loan application, you want to show as much wealth as you can, so the bank will give you a loan. On the 433-A, which is for individuals, a 433-B, which is for your business, it's to report all your bank accounts, your assets, your cars, and then your expenses. Now, the IRS uses something called the national standards. They have something called national standards; and it's geographical too, because cost of housing in San Francisco is different than other areas' cost of housing, and same as cost of transportation and all those kind of expenses.

Mr. Redpath

Even within an area. So, for example, San Francisco would be different than Sacramento, different than LA, different than San Jose. For example.

Mr. Pon

Exactly. So, you have national standards. Now, if your actual expenses are higher than those national standards, you better explain why, because, for example, in the medical expense area, you have insurance and medical expenses under national standards. But let's say I have a disease that's not covered by health insurance, or I have a child with this illness that's not covered by insurance, and you give that explanation. Also, I would include doctor's letters and hospital letters, documentation, even newspaper articles explaining what this disease is. I've also included YouTube video links, because sometimes these officers don't want to read. So I say, "Just watch this YouTube, just a very credible doctor. It's some well-known legitimate doctor, some well-known source, or even a news segment from a credible news source that kind of explains what this disease is and what's going on, and they're trying to get funding for it or whatever."

So, if you have unusual expenses. I had a case of a guy who owed money, and I kind of agreed with the revenue officer. He was paying an exorbitant amount of rent for this place he was living in. And the agent said, "Well, he could easily rent a place for a fraction of that amount." I said, "Yes, I know that. I'm trying. I'm trying."

Mr. Redpath

But one of the things, for example, the IRS doesn't care if your kids go to college.

Mr. Pon

No, they don't care.

Mr. Redpath

You pay us and then let them take out loans or something, but they don't care. I mean, those aren't expenses that they look at. And you mentioned extreme circumstances. I had mentioned the one about collectibility, where I had the person that had huge medical bills. That was putting them in a collection issue. We didn't go to an offer in compromise because they wouldn't have gotten one, but they were put into non-collectible.

We have this other process called audit reconsideration.

Mr. Pon

Right.

Mr. Redpath

That is a process, but doubt as to liability is kind of a similar idea that, well, look, we doubt the liability. So can you explain the differences, doubt as to liability versus doubt as to collectibility? I think collectibility is clear, right? You don't have the finances to pay the full amount and you've run it. The IRS, by the way, so our viewers are aware, the IRS has a qualifier. On the IRS website, you can go through and at least kind of get an idea of whether they would even qualify for an offer in compromise. That's a tool that's available to practitioners on the IRS website, the OIC pre-qualifier. So, it's something to look at. Collectibility, I think is clear. But this doubt as to liability? We never used to do that, because the IRS was like, "Well, you know, you've already gone through the audit. It's already decided. Don't bother me." You've been doing a lot of cases, and I'm hearing more and more people doing cases involving doubt as to liability. Can you explain that?

Mr. Pon

Well, first of all, doubt as to collectibility is very formulaic. That's why on the IRS website, there's a qualifier there because it's basically the instructions to the form. It's the IRS's responses to all of these ads that you see on the TV. So, the IRS says, "Run through your qualifier first." And we do that too. We run through it, we go through it, and it's a math calculation. What's your assets, what's your income? And boom, here's what the settlement amount is. A lot of times the client goes, "Wow, that's kind of high." "Well, it's less than the balance, but here it is. Can you pay it?" If not, we'll do the installment agreement.

Doubt as to liability, in many cases, like I said in the beginning is, is that amount correct or not? It's gone through the whole process of collections. It's gone through the 30-day letter and all these various letters that the taxpayer has gone through. You're in the zone where you owe these taxes, the IRS is trying to collect on it, and it's been a few years now.… Doubt as to liability I've been using in lieu of an audit reconsideration, because audit reconsiderations are a bit challenging to get, and uncertain. Sometimes we submit them. We never hear from them, and it's a difficult process, or it goes back to the same unit, the person who said no, right? Or it goes back to supervisor, same person that says, "No." And then the appeals officers are overwhelmed. Appeals officers are not auditors, so they don't want to review documents or all that.

But the doubt as to liability is a good alternative to use. Basically, it suspends the collections process so it gives us a little breathing room; and normally, what happens is we get referred to an appeals officer. And doubt as to liability, it could be… Here's the cases I've had as to doubt as to liability.

It could be a case where we had an IRS audit and examination, but the agent quit in the middle of the exam. He quit, he disappeared. We didn't know that. Someone else picked it up. He couldn't figure out the case. He didn't have the patience, the time, or the competency to figure it out. He just disallowed everything. Just disallowed everything and just boom, put a report, and we couldn't get anywhere with the new agent. So, now it's in collections. That's a classic case. They're mostly coming from audits, or it could even be a CP-2000 where it's a bit late. The taxpayer ignored it. They weren't a client of ours, but they ignored it. It's another tool in our tool belt with dealing with the IRS. Doubt as to liability.

Mr. Redpath

But I think we've got to go back to the fact that the liability was established in this case; it's not appeals. It's not like you're going to appeals. So, your liability was established. You got your 90-day letter, the liability has been assessed. Essentially, it's in collection, but one of the tools is that you're saying, "Well, that liability isn't correct."

That's why I think I should be allowed to compromise it. Versus, as you said, just the numeric. This is my assets, this is what I can pay. It's collectibility. Do I have that right?

Mr. Pon

Yes you do. Here's another example. We had a client that got assessed a penalty, and it was a bounced check penalty from the IRS, because of course it only happens when it's a big number. I know it's a big number. The husband wrote the tax payment out of the wrong account. He wrote it on the wrong account. He made a mistake. So, he wrote this big check, check bounced, and the IRS assessed a bounced check penalty. And we're trying to argue that, look, the moment he figured out he made that mistake, he sent a replacement check in. So, I think we have reasonable cause to have abatement of this penalty. And it would have fallen under the first-time abatement also; but for some strange reason, we couldn't get any progress on that. So, we applied for doubt as to liability.

And so, what happens, you get a call from an offer in compromise officer, and they're the ones who do not deal with questions of liability. They're not agents, and so they refer it to an appeals officer who might refer it to an IRS agent. It's just the way of another tool to use with the IRS.

Mr. Redpath

When you make an offer, you can make a lump sum payment. I believe, it's 20% of the total.

Mr. Pon

Right. The minimum amount's 20%.

Mr. Redpath

And pay the balance in five or fewer payments over five or fewer months if you're accepted. Then there's the periodic, where you essentially are offering to pay it between six and 24 months. If you do that, you have to make your monthly payments for that for what you're offering. Like if we're offering a $100 a month, you've got to continue to make those $100 a month, or they're going to reject it, because you haven't made that payment. Now, you could have an issue if you are disallowed, right? I mean, you've made a 20% down payment on a lump sum offer. What if they reject your offer?

Mr. Pon

That 20% payment is nonrefundable. That's going to be applied against your outstanding balance. You're not getting it back. If they reject your offer, you're not getting it back.

Mr. Redpath

Well, that's something to think about, right?

Mr. Pon

Exactly.

Mr. Redpath

We have to think about that.

Any last words for our viewers here? Because this is an area that, I think, as we mentioned in the beginning, we're going to see more and more of these. I don't mean the "settle for pennies on the dollar." Those would be the rare one, but we're going to see more and more as there's more enforcement. So, what should our viewers be left with?

Mr. Pon

Yes. I think it's something we can use to help our clients, and we can be a resource to them. I mean, we don't have to do hundreds of these all the time, but it's good to know. But I think what's more important to know is to understand the IRS collections process and how to work with it.

The offer in compromise is not the first thing we jump to. There's other avenues, and we can be a hero to our clients by getting abatement of penalties, negotiating a reasonable installment agreement. You'd be amazed how low you can go. I mean, the IRS will say, "If you follow these rules, boom! This will be an automatic approval." That's true, but it could be a relatively high number. However, for some clients, this is the way they operate. They have installment agreements with the IRS. They build that into their family budget, and it works for them. So, if that's what they want to do, that's fine. However, knowing that you're paying extra for that year, you're having it being financed by the government. You're paying interest and penalties, and it's still ticking away; but I guess it's cheaper than borrowing from other sources.

Mr. Redpath

We have to sit down with each individual client. There's no cookie cutter if I understand what you're saying. Look at the situation. Think about other options that might be available, like an installment agreement, especially if you don't believe that it would be accepted because they wouldn't qualify. Then, look to other options. And reducing the penalties would be, obviously, a major one, which would also reduce the interest. A lot of tools. Offer in compromise is one. What we hear on the television is probably a little bit exaggerated. I'm sorry, I had to say that.

Larry, thanks for being here today. Really, this is a really interesting area and one which I think even if practitioners have not been doing it, they really should look at it and understand the process, because we're going to see more and more clients that this could be helpful with. Larry, thanks for your insight today. Enjoyed having you here.

Mr. Pon

All right. Thank you, Ian. Have a great day.

Mr. Redpath

Thank you.

Offers in Compromise (OIC)

By Ian J. Redpath, JD, LLM

A. Introduction

The IRS has the ability to "compromise" a civil or criminal tax liability after assessment and before referral to the Department of Justice. The taxpayer may seek a compromise based on:

(1) doubt as to collectibility,

(2) doubt as to liability, or

(3) to promote effective tax administration because either (a) collection of the full amount would cause economic hardship for the taxpayer, or (b) compelling public policy or equity considerations justify compromise. [Reg. §1.7122-1]

The process is referred to as an offer in compromise (OIC) and constitutes an agreement between a taxpayer and the IRS to accept less than full payment. [§7122] Generally, the IRS will not accept an offer if the tax debt can be paid in full or through an installment agreement and/or taxpayer's equity in assets. The taxpayer can request a conference in the IRS office having jurisdiction over the offer to explore compromise possibilities before submitting a formal offer. [Reg §601.203(d)]

B. Filing for an Offer in Compromise

Before an offer can be considered, the taxpayer must:

- file all tax returns that the taxpayer is legally required to file,
- have received a bill for at least one tax debt included on the offer,
- make all required estimated tax payments for the current year, and
- make all required federal tax deposits for the current quarter if a business owner with employees, and
- not be in bankruptcy

The offer will be immediately returned, with the application fee, if these conditions are not met. Any initial payment will be applied to the tax debt. This decision cannot be appealed. The IRS has a pre-qualifier on its website (www.irs.gov). While using the pre-qualifier is not mandatory, the IRS asks in the heading of the revised Form 656 if the taxpayer has used the pre-qualifier prior to filing. Additionally, there are FAQs on the website that are very helpful in determining when and how to make the offer.

An OIC must be submitted according to the procedures prescribed by the IRS. [Reg §301.7122-1(d)(1)] Generally, an OIC is submitted on Form 656 accompanied by a financial statement. The financial statements are Form 433-A (OIC) for individuals and self-employed and Form 433-B (OIC) for a business. [Reg. §601.203(d)] Form 656-L is used for doubt as to liability, and no financial statement is attached. [Rev. Proc. 2003-71, 2003-2 CB 517] Taxpayers must use the April 2021 version of the forms, or the IRS will return the Offer.

Generally, a taxpayer must submit a separate non-refundable application fee of $205. Payments may be made using the Electronic Federal Tax Payment System (EFTPS) or by other traditional methods such as a check or money order.

There are two situations where a fee is not required:

- the OIC is based on doubt as to liability, or
- an individual (not a corporation, partnership, or other entity) qualifies for the low-income exception.

The low-income exception applies if the taxpayer's total monthly income falls at or below 250 percent of the poverty guidelines. A taxpayer who claims the low-income exception must complete Section 1 of Form 656 and check the certification box.

A "lump sum cash offer" is an offer to pay the liability in 5 or fewer installments within 5 or fewer months after the offer is accepted. The taxpayer must include a nonrefundable payment equal to 20 percent of the offer amount plus the application fee. If the offer is rejected, the 20 percent payment will be applied to the taxpayer's tax liability. Note that the taxpayer has a right to specify the particular tax liability to which the 20 percent payment is to apply. This should be done with the initial offer and payment of the 20%. Once the IRS accepts an OIC, the taxpayer may no longer designate the payments. The designation is made in Section 5, Form 656.

"Periodic payment" offers are to pay in 6 or more monthly installments within 24 months. When submitting a periodic payment offer, the taxpayer must include the first proposed installment payment. Like the 20 percent payment, this is generally nonrefundable. While pending, the taxpayer must make the proposed payments. Likewise, these are nonrefundable.

Until acceptance of the offer, the taxpayer has the right to designate the particular tax liability to which payments are to apply. This is done on Section 5, Form 656. The low-income exception applies to the payments with the OIC. You may pay more than the required payment and designate it as a deposit. Deposits are in Section 5, Form 656, and may be returned if the offer is not accepted.

In some cases, if the taxpayer did not submit necessary information or meet the requirements, an OIC is returned rather than rejected. There is no right to appeal; however, the offer may be refiled when the issues are resolved. While the application fee is returned, any initial payment submitted is applied to outstanding liability.

An offer in compromise becomes pending when it is accepted for processing. Once the offer has been accepted for processing, an Offer Specialist will review the offer. The IRS may return an offer if it determines that it was submitted solely to delay collection or was otherwise non-processable. An offer returned following acceptance for processing is deemed pending only for the period between the date the offer is accepted for processing and the date the IRS returns the offer to the taxpayer. This affects the period of time that the statute of limitations is suspended. There is no right to appeal.

The taxpayer may withdraw an offer at any time before acceptance. The withdrawal must be in writing, and it is effective upon receipt or upon the issuance of a letter by the IRS confirming the taxpayer's withdrawal. An offer is not accepted until the IRS issues a written notification of acceptance. Likewise, there is a requirement of written notice advising of a rejection, the reason(s) for rejection, and the right to an appeal. The taxpayer has 30 days from the date on the rejection letter to request an appeals conference.

IRC §6331(k) provides that no collection action can be initiated during the pendency of the offer in compromise. If an existing levy creates an economic hardship, the IRS could release it. [§6343(a)(1)(D)] This may be included in the OIC.

C. Review of OIC

A taxpayer may submit a DATL if there is a genuine dispute as to the existence or amount of the correct tax liability under the law. [Reg. § 301.7122-1(b)(2)] This may be submitted in lieu of a Request for Audit Reconsideration. It does not exist where the liability has been established by a final court decision or judgment concerning the existence or amount of the liability. The taxpayer must submit a detailed brief or memorandum explaining why the tax is not owed. This should provide citations to appropriate authority. Remember that this is filed with Form 656-L, and no financial statement is required.

Other grounds include doubt as to collectibility (DATC) and doubt as to collectibility with special circumstances (DATC-SC) if the taxpayer believes that he/she cannot ever pay the full amount of the tax owed. [Reg. §301.7122-1(b)(3)]. DATC and/or DATC-SC exist in any case where the taxpayer can pay some of the liability, but less than all. These are on Form 656, and Form 433-A (OIC) or 433-B (OIC) must be attached. In determining ability to pay, taxpayers are generally applying any discretionary income against the tax liability. The taxpayer is allowed a basic living allowance. The determination of the amount of such basic living allowance is based upon an evaluation of the individual facts and circumstances of the taxpayer. The IRS has published national and local living expense standards. These are used to determine the reasonable collection potential (RCP).

The Internal Revenue Manual (IRM) section 5.8.4.3 provides detailed guidance on an offer based on DATC-SC. IRM 5.8.11.2.1 provides other factors that may be taken into account when considering an offer based on DATC-SC:

- the taxpayer's age and employment status;
- number, age, and health of taxpayer's dependents;
- cost of living in area the taxpayer resides; and
- any extraordinary circumstances such as special education expenses, medical catastrophe, or natural disaster.

In IRM 5.8.11.2.1(6), factors to address in the OIC constituting economic hardship are listed:

- the taxpayer is incapable of earning a living because of a long-term illness, medical condition, or disability, and it is reasonable that the financial resources will be exhausted;
- the taxpayer has set monthly income and no other means of support, and the income is exhausted each month in providing for the care of dependents; and
- the taxpayer has assets, but is unable to borrow against the equity in those assets, and liquidation to pay the outstanding tax would render the taxpayer unable to meet basic living expenses.

Even if a taxpayer can pay the full amount, an OIC may be filed requesting relief due to Effective Tax Administration (ETA). The taxpayer must allege that collection of the full liability would cause the taxpayer "economic hardship" or there are compelling public policy or equity considerations for compromising the liability, and a compromise of the liability will not undermine compliance by taxpayers with the tax laws. [Reg. § 301.7122-1(b)(3)(ii)] Economic hardship is defined as the inability to pay reasonable basic living expenses. [Reg. § 301.6343-1] Compromise based on equity and public policy will not be accepted if collection of the full liability would undermine public confidence that the tax laws are being administered in a fair and equitable manner. The circumstances must be such that compromise is justified even though a similarly situated taxpayer may have paid his liability in full. This is a very high bar to meet.

It should be noted that a DATC-SC offer, while similar to an ETA in analysis, differs in that DATC-SC is a claim that special circumstances exist that warrant acceptance for less than the RCP. In an ETA, the RCP is the full tax liability, but collection would cause a hardship.

One important aspect of the OIC is the brief or memorandum that is attached explaining the basis and facts upon which the request is made. The appropriate Form 433 must be consistent with the memorandum. The IRS will look at the taxpayer's assets, income, liabilities, and expenses in determining the RCP. In preparing these sections, net numbers must not be used. When determining income and expense, you must take into account National and Local Standards. The standards are available on the IRS website and were updated in April 2021.

The IRS requires that an offer generally be greater than the net worth of the taxpayer plus disposable net income. [I.R.M. 5.8.5.7] If there is cash on hand of $1,000 or less, the IRS will treat the account as no cash on hand. If the amount exceeds $1,000 and the client can show that the amount is used to pay for taxpayer's monthly allowable living expenses, then, although listed, it is not included as an asset. In some instances, it is helpful to present more than three months of bank statements if the average more clearly reflects the cash on hand. I.R.M.5.8.5.12 provides an exclusion of $3,450 from the net equity valuation of vehicles used for work, for production of income, and/or for the welfare of the taxpayer's family, and up to two cars per household. The reduction is from the value that is determined to be the current value of the automobile.

Under I.R.M.5.8.5.18, if the IRS determines that the taxpayer has disposed of assets within a three-year period prior to the submission of the offer, an explanation must be provided as to why those funds are not available. The Manual has other specific examples of dissipation.

It should be noted that the many sections of the Internal Revenue Manual are regularly updated, as recently as October 2021. Reference should be made to the updated versions. Reviewing the manual is helpful for practitioners in determining how the IRS will be evaluating the offer.

Taxpayers must attach documentation with the Forms 433 (OIC). For example, the most recent pay stub, most recent investment account statements, three months of bank statements, most recent loan statements, and the like. For businesses, attachments such as a current profit and loss statement covering the most recent 6–12 months, six most recent bank statements, three most recent investment statements, and copies of loan statements. There is a checklist of documents to attach with both Forms 433.

If taxpayers are either unemployed or underemployed, the IRS may impute income to them under the assumption that they will be employed. Also, possible future earning potential of the taxpayer will be considered. The Manual gives specific examples such as child support payments ending or a debt being paid. The period of the future income is different depending on whether the offer is paid within a 5-month period or a 24-month period. The IRS will look only to earnings over a 12-month period if the offer is paid in 5 months, which will mean generally that the offer amount may be less than if the client seeks to pay the offer over 24 months. In any event, the future income over the remaining life of the collection statute of limitations is no longer used. These should be addressed in the memorandum. In some situations, in lieu of averaging past income, the IRS accepts the current income, but enters into a Collateral Agreement that the taxpayer agrees to pay a percentage of future income if that future income is over an agreed amount. [I.R.M. section 5.8.5.20]

The IRS National and Local Standards can be used in determining monthly expenses when required. If using the National Standards, the taxpayer need not prove the amount paid. Those covered by Local Standards are allowed only to the extent the taxpayer can prove that the expenditure was made. In general, no amount will be allowed in excess of the local standard.

National Standards have been established for food, housekeeping supplies, apparel and services, personal care products and services, and health care expenses including medical services, prescription drugs, and medical supplies (e.g. eyeglasses, contact lenses, etc.) and miscellaneous. The out-of-pocket health care standard amount is allowed in addition to the amount taxpayers pay for health insurance. Taxpayers may show exceptional expenses when claiming a hardship. Local Standards have been established for housing and utilities. The housing and utilities standards are derived from Census and Bureau of Labor and Statistics (BLS) data, and are broken down by county and state and, if relevant, family size. Housing and utilities standards include mortgage or rent, property taxes, interest, insurance, maintenance, repairs, gas, electric, water, heating oil, garbage collection, telephone, and cell phone. The Standards were last updated in March of 2021.

Where a taxpayer is offering to compromise a liability for which the taxpayer's spouse has no liability, the assets and income of the non-liable spouse will not be considered in determining the amount of an adequate offer. The assets and income of a non-liable spouse may be considered, however, to the extent property has been transferred by the taxpayer to the non-liable spouse under circumstances that would permit the IRS to effect collection of the taxpayer's liability from such property (e.g., property that was conveyed to defraud a creditor or property has been transferred by the taxpayer to the non-liable spouse for the purpose of removing the property from consideration by the IRS in evaluating the compromise).

Generally, the statutory period for collection by the IRS is suspended during the period that the OIC is pending and for 30 days immediately following the IRS's rejection of an OIC, and for the period in which a timely appealed rejection is being considered by the IRS Office of Appeals. If there is an issue on collection and an OIC was made, be sure to look at the transcript to determine any period of suspension.

D. Appeal of Denial

An appeal from an adverse determination is made on Form 13711 and supported by an Appeal Memoranda. This should address the issues raised in the rejection letter. The appeal is sent to the Offer Specialist. If the Offer Specialist is not persuaded to reconsider the rejection, the offer is forwarded to an Appeals Officer. The Appeal Memoranda should state at the end the desire for a face-to-face conference.

If unsuccessful in Appeals, an option is to apply for arbitration and mediation. [Rev. Proc. 2014-63, 2014-53 IRB 1014 and Rev. Proc. 2015-44, 2015-38 IRB 354]. §7123 provides for non-binding mediation in Appeals on any issue unresolved at the conclusion of Appeals procedures, which occurs when Appeals sustains the IRS's offer determination.

E. Default on an OIC

An OIC can reach default status in one of two ways: the taxpayer failed to make timely payments of the amount agreed, or the taxpayer has not adhered to the compliance provisions of the offer contract. The revenue officer has the discretion to grant up to a six-month extension if the taxpayer can pay the defaulted amount in 6 months or less. If the taxpayer is unable to pay the balance of an accepted offer, the IRS has the option to: (1) temporarily adjust the terms of the offer, (2) formally compromise the existing compromise, or (3) exercise the default provisions of the offer. IRC §7122 authorizes the IRS to accept an offer in compromise of an accepted offer. The new offer to compromise the original offer must be based on doubt as to collectibility. The taxpayer must send a current financial statement (Form 433-A or 433-B) and a written proposal of the new offer in letter format to the office where the original offer was submitted. The letter should be addressed to the Commissioner of the Internal Revenue Service and include the following information:

- Name, address and Social Security number or the taxpayer identification number of the taxpayer;
- Amount proposed and the terms of the payment;
- Acceptance date of the original offer;
- Waiver of any and all claims to amounts due from the United States up to the time of acceptance to the extent of the difference between the amount offered and the amount of the claim covered by the offer; and
- Reasons why request is being made to compromise the existing agreement.

The compliance agreement in Item 7, Form 656, will remain in effect from the date the original offer was accepted.

F. Conclusion

An OIC offers the taxpayers who have legitimate issues concerning the payment of taxes to potentially reduce the amount due. Unlike the constant ads, the IRS is not providing wholesale reductions in tax liabilities. However, for those that qualify, offers in compromise provide a tremendous benefit and should be explored.

A. Discussion Problems

Your client, Sydney, a successful businessperson and former CEO of a major company, has had some medical issues over the last few years that have not allowed her to work at her former high-pressure job. When she was CEO, she lived a lavish lifestyle, mostly on borrowed money. Several years ago, she lost a case in Tax Court and has significant unpaid tax liabilities from that case plus large penalties and interest. She said her attorney believes the Court was wrong, but she couldn't afford an appeal. She has few assets that can be liquidated and is in danger of foreclosure on her home. Currently, she is making $15 per hour working in a small shop as a sales person. She heard that the IRS will take pennies on the dollar to settle taxes.

Required:

1) What is the basis of an offer in compromise (OIC) for Sydney? (There can be more than one.)

2) What types of offers are available?

3) What would you do to determine the reasonable collection potential (RCP)?

B. Suggested Answers to Discussion Problems

1) Sydney cannot use the doubt as to liability (DATL) basis since her case has already been determined in Tax Court. She can use doubt as to collectibility (DATC), doubt as to collectibility with special circumstances (DATC-SC), and effective tax administration (ETA). The reasonable collection potential (RCP) will have to be determined in making the offer. If it is believed that Sydney cannot pay the full liability, then doubt as to collectibility can be used. If the RCP is less than the liability but it is believed she cannot pay the RCP because of special circumstances of hardship, then doubt as to collectibility with special circumstances would be appropriate. If she can pay the full amount, but it could create a hardship, then effective tax administration could be appropriate. The IRS pre-qualifier could be used as a starting point.

2) Two options are available: A lump sum payment, up to 5 installments over 5 months; or a periodic payment, 6 or more installments over 24 months.

3) It is important to determine the RCP as that will be the basis of any determination by the IRS. It will also guide the most appropriate basis for the OIC. To do so, you will have to gather information on all of Sydney's assets, liabilities, income, and expenses. You should refer to the National and Local Standards in determining the appropriate expenses. If there are extraordinary expenses the IRS should consider, those should be set forth.

PART 3. BUSINESS TAXATION

Trusts as Beneficiaries

Planning for retirement and for distribution of assets upon death is extremely important, especially for high net worth individuals. The SECURE Act made some changes, and retirement accounts inherited after December 31, 2019 must generally be distributed within ten years. Lifetime payouts are no longer available for accounts inherited after that date unless the beneficiary is an eligible designated beneficiary. Ian Redpath and Ed Renn discuss the general rules and some exceptions to the rules when individuals and trusts are named as beneficiaries, and they recommend revisiting trusts that were set up prior to passage of the SECURE Act.

Let's join Ian Redpath and Ed Renn as they discuss trusts as beneficiaries.

Mr. Redpath

Ed, welcome to the program.

Mr. Renn

Great to be here, Ian. Happy to be here to talk about an interesting topic.

Mr. Redpath

Yes, and it's great to have your insight, because I know this is an area that you and your firm do an awful lot of. You have a lot of clients that, frankly, we can say they're high net worth individuals. And these types of things are really important for people who are high net worth individuals. And so, we're going to be talking about trusts and naming trusts as beneficiaries. Can you kind of give us the basics, because not everybody is up on exactly what this is going to do, what it implies, as well as when they should be thinking of it. So, can you give us kind of a basic primer on starting here?

Mr. Renn

Sure. I mean, for most people, when they think about who should take the retirement benefits when they pass, very often the spouse is the obvious first choice. And then, if he or she are competent and capable, that's probably the best way to go. Increasingly, because of some of the complexities in using trusts, it wasn't unusual to appoint your assets, your IRAs, your qualified plan assets to your children outright if they were capable and if they didn't have asset protection issues and that kind of thing.

But there were always some beneficiaries that sort of needed some extra help. And you were concerned that if you gave them all the money all at once, instead of being a $20,000 a year cushion to their lifestyle, it would turn into one Ferrari or something like that. Just people with addictions, people with gambling habits, or people just lacking the capacity to manage the money.

Mr. Redpath

Ed, I'm going to just jump in here, because let me just give you a real quick example. I talked to a client of mine at one point about a spendthrift. They had a grandchild. The parent was deceased; their child was deceased. Spendthrift provision, because the kid liked to spend money that he didn't have. They didn't want to do it. The kid talked them into it, not doing it. They put his name on their accounts. Guess what happened? He emptied out a couple of their accounts, and bought, he bought a Corvette. He didn't buy a Ferrari. He bought an $80,000+ Corvette, as well as some nice trips, and emptied it. So, planning can be very important sometimes.

Mr. Renn

Yes, I mean, in some cases, we've got family members who, they don't necessarily have vices, but they're having a hard time making their own way in the world. Maybe they have some limited capacity. They have issues that may make staying employed difficult or whatever.

And it used to be really great when I could look at mom and dad's IRA and say, "Well, if we distribute this out over 40 or 50 years for your son or daughter, we'll know that they have enough money to pay the rent and have health insurance and buy groceries. The SECURE Act back in 2019 kind of killed that in a lot of contexts, because the basic rule, the reason we're talking about this now, is the rules changed.

We used to be able to do lifetime payouts. And now, for anybody who's inheriting an account after 12/31/19, if you're just that designated beneficiary—and the designated beneficiary is just usually an individual, some qualifying trusts, but generally an individual—you don't get a lifetime payout anymore from mom and dad's account. You have to take the money in 10 years. You don't have to take the annual payments anymore, either. That's kind of the good news, but the bad news is, for most folks that qualify as designated beneficiaries. We'll talk about the exception, the eligible designated beneficiary. Just what we needed. I mean, we already had beneficiary, designated beneficiary. Now, we have eligible designated beneficiaries.

Mr. Redpath

Yes, I want to jump in here, because I know there's been some controversy with the IRS's publications on this, about that 10-year rule. What's going on there? If anybody's read the publication, they might be saying, "Well, Ed, you don't know what you're talking about. That's not what it says."

Mr. Renn

Yes, that's called trying to use what you have and just editing and missing a few cuts. I mean, the IRS has acknowledged that they didn't mean what they said in Pub. 530. And the SECURE Act, as most of us understand it, is in fact the law of the land. And there isn't some hidden provision there that you can get a designated beneficiary to qualify for a lifetime payout in circumstances. So, they actually failed to take out some examples. And then, even when they corrected it, they kind of screwed it up again. It's still a work in process, but they know they don't have it right and they're in the process of fixing it.

Mr. Redpath

So, if you've read it, understand it's wrong.

Mr. Renn

Yes, just because you can put your finger on it doesn't mean it's right. Yes, exactly.

Mr. Redpath

It's kind of an unusual circumstance. So, let's talk then about trusts. I mean, kind of a lot of people are not aware of trusts, or I think one of the things people first think about when they think about a trust, I'm talking about practitioners is, well, wait a second. Why would we use a trust? Because the rates of tax are so compressed. Those tax rates, you're at the highest rate at a very low amount of income. So, why would we want to consider a trust? And what is a trust?

Mr. Renn

Yes, that's kind of the problem, Ian. I mean, when we could do lifetime payouts, we often used what we call the conduit trust. And what the conduit trust is, just think of it as a tube. At the top sits the IRA or the qualified plan, and at the bottom of the tube sits the beneficiary. They were usually only done for one beneficiary. So, you take the IRA that you want to benefit the son, you'd put this conduit trust in the way. The required minimum distribution would come out. It would drop right down to the son, but all he got was the RMD in most cases. The trustee usually had discretion to give him more if he or she needed it, but generally it was intended to just distribute the RMD.

The RMD comes out. The trust doesn't pay the tax. The individual recipient pays the tax, and he didn't have control of most of the corpus. What you paid to him was subject to his creditors, but the rest of the account was protected, and it worked pretty well. And if you had 30, 40, or 50 years to make those payments, it was a very, very nice system, because really, most of the money stayed there and grew tax-deferred. And you really only started to cut into the principal if you had relatively modest, mid-single digit growth assumptions. You'd only really cut in; with only 10 or 12 years to go, you'd actually start to reduce the account.

But before that, it was still growing, even though you were making distributions. So, in that scenario, you were able to get the money out into the individual's hands. Now, when you had an accumulation trust, which maybe included more than one beneficiary, you did have that problem, and you had all kinds of other problems about who's the measuring life and that kind of thing.

And that went away, because if those folks are just designated beneficiaries, now it doesn't matter, because you're going to take it all in 10 years. And the thing to point out, Ian, is that this is true of qualified plans, §403(b) annuities, §457 plans, IRAs, and Roth IRAs. So, Roths don't have a tax consequence, so it would seem to make sense if you're a designated beneficiary of the Roth, if you don't need the money, you would literally wait until the last day of the 10th year to take the account out, because you've gotten the tax-free growth. But Roth, this applies to Roth too. And for a lot of my clients, it's been a disincentive to doing Roth conversions; though given some of the current income tax proposals, they're starting to rethink that a little bit.

But one of the primary charms for clients in terms of paying tax now was the idea that it could grow tax free for 30, 40, 50, 60 years for the grandchildren, and that used to be the case.

But, well, if you inherited an IRA before 12/31/19, you still may be able to do lifetime distributions. I don't want anybody to get confused and say that the rules changed for the old and cold. My children inherited a small IRA from my uncle back in 2015, and they've got lifetime distributions. But if they would have inherited that account in 2020, they'd be looking at taking it out over 10 years. One of them would be much happier with that answer.

Mr. Redpath

One question I have for you is, so, you have this trust that's holding, this trust instrument. And in a trust instrument, you have a trustee, the person making these decisions, for example, if there's a provision for health, education, and welfare, people who are making this decision on the distributions. Generally, when you set up a trust for this purpose, who would be the trustee?

Mr. Renn

It would often be the same person that would be the trustee for the revocable trust. Typically, a friend, a business partner, a college roommate, could be a sibling if they're going on at the beginning. In some cases, trust companies. Depends on what the client wanted to do. But what you're looking for, I mean, the reason why you put a trustee in charge of the IRA or the qualified plan monies is because of professional management in terms of the investment assets, so the son or the daughter can't decide they're going to go build a floating racetrack in the nearest ocean or lake. Tax management, because you can do what you can to sort of minimize the tax, so the accumulation trust has a lot of tax compression to it. And it would provide control for a minor, for a disabled child, for a spendthrift, for somebody with an addiction.

So, the interesting thing is those are designated beneficiaries. Some of these people can actually qualify as eligible designated beneficiaries. For instance, if you have a spouse who spends too much money on stock cars or high-heeled shoes, you could still in fact leave the IRA or the qualified plan for that person in a trust and get a lifetime payout, because an eligible designated beneficiary, one of the categories are spouses.

The second category is minor children. And this is kind of interesting, because you can get a lifetime payout for minor children until they either reach the age of majority or age 26 if they continue to go to school during that period of time. And then, at that moment, the lifetime payout turns off again, and we're looking at the 10-year rule. So, they can either take nothing, and at the end of 10 years, take it all; or they could take a tenth a year; or they could try to do some tax planning with it as the markets go up and down in terms of how they want to take the money.

The other categories of eligible designated beneficiaries are any individual who's less than 10 years younger than the account owner. So, that includes folks that are older than the account owner. So, we've really seen that really kick in for siblings. And also for some of my clients who are older, they've got a companion. They don't want to get married. They don't want the complications of marriage, but they want to make sure that the companion is taken care of. More often than not, they come within that 10 years younger exception.

The other two categories are disabled, which is what we know in the tax code, and the chronically ill. And those have special categorizations. And we actually have a new type of trust provided in the code for these folks. But what's really happened, just to be really, really clear, if you're inheriting an account after 12/31/19, on or after 1/1/20, if you're inheriting that account, unless you're an eligible designated beneficiary, you've got to empty that account in 10 years. You can do it annually, or you can do it in one lump sum. You can do it at the beginning, or you can do it at the end, but you've got to do it. It's 10 years. There's no longer an RMD requirement, other than to take it all within that 10-year period.

Mr. Redpath

And that's an interesting one. Can you explain that? You used the term RMD, required minimum distribution; and I think that's another area that people are very confused. There were changes made with the SECURE Act. And I think very positive changes, especially for people who want to continue working. What is an RMD?

Mr. Renn

Required minimum distribution is an amount that you have to take every year, the idea that at some point in time, you've stopped working, or you've attained a certain age, and the money has been growing tax-free. It's supposed to be for your retirement. You have to take it.

With Roth, you don't have a required minimum distribution. With regular IRAs, you do. It used to be the magic age was 70½. That triggered the obligation to start taking them by the following April 1st. Kind of odd concept, 70½.

But it is exactly what it appears to be. It's half a year after you've attained age 70. And that got changed in the SECURE Act to 72, for folks that attained 70½ on or after 1/1/20. So, basically, there's been a couple of additional years given to you to postpone taking distributions.

As we sit here today, there's SECURE Act 2.0 in Congress, which could ultimately push the required beginning date back to 75. And the other change that's coming up, Ian, that our viewers should be aware of is there's new life expectancy tables that are going to kick in on 1/1/22. And effectively, they're pretty significant. They add a couple of years to the life of somebody who's age 72, so your distributions are smaller. That's probably a positive if you're not looking to take out more money, if you don't need the money. If you need the money, you're going to take what you need.

Mr. Redpath

Yes, and I think another thing is planning, because you have an RMD, and a lot of my clients have multiple accounts. They have a §401(k). They have an IRA. They have all sorts of different retirement accounts, so the RMD often is well, what does that mean? Because I've got all these different accounts, and do I have to take an RMD from each account? Can I empty this account and keep the other accounts open? How do I do that? What are the rules on taking that RMD?

Mr. Renn

Well, in terms of qualified plans, §403(b) annuity, it's that kind of thing. §401(k) plans, profit sharing plans, DC plans, each account, each plan, you need to take an RMD from that individual plan. So, if I've got a §401(k) plan and a defined contribution plan with my employer, I'm taking two RMDs. I can't take, let's say, in total it's $5,000. I can't say I'm only going to take $5,000 from one account and leave the other one alone. I've got to take my required percentage out of each account.

IRAs are different. IRAs, you can actually aggregate. So, with IRAs, you can decide I've got three IRAs, and my distribution from all of the IRAs is $15,000. I'm taking it all from IRA one, because it's got the most money or the worst investment performance, or they're charging me the most to manage my money, or whatever the holder's philosophy happens to be at the time they're contemplating the distribution.

I mean, remember, an RMD is a minimum you have to take. You can always take more. And so, if you have a need that's greater than the RMD, and you've got the account balance to support it, you can take that money. But it's a minimum. The only time that doesn't apply really is with a Roth IRA. And in the scenario with qualified plans, if you're not a key employee, if you don't own 5% of the company, and you continue to work after age 70½ [or 72], if the plan provides for it. The code says it's optional. So, it's up to the employer. But if the plan provides for it, you can defer those distributions.

Mr. Redpath

And the RMD, the required minimum distribution, if you take out... You can take out as much as you want, but there is a penalty if you don't take out enough, if you don't meet that RMD. So, it's important.

So, we're talking about, going back, a trust named as the beneficiary. So, you have an IRA. You named the trust as the beneficiary. You've named someone as the trustee, and there's also often a requirement of having a health, education, maintenance type of a provision. Health, education, welfare, that type of a provision to give some level of... I hate to use the word standard, but to have that as a "standard" in there for the individual who is the trustee. That can create some problems. What types of problems does that create?

Mr. Renn

There's a couple of issues there, Ian. I think you're right. I think most trusts and certainly most IRA trusts probably use that HEMS—health, education, maintenance, and support—standard. One of the problems you have in post-SECURE Act trusts is the money's got to come out over 10 years. So, if it's a sizeable account, you might actually have trouble justifying the HEMS standard, because they're supposed to say, how much does my beneficiary need? What's their standard of living? That kind of thing.

I've always preferred absolute discretion in these ways, because you get added creditor protection there. And most of the time, my clients that want trusts wrapped around qualified plan or IRA benefits are concerned about the decision making in the money management capabilities of their beneficiaries. So, whether it's because they're minors or because they've got a track record of not doing the right thing in the eyes of mom or dad or whatever, you would want that. But the HEMS standard has become a little bit of a challenge in some of these circumstances; because if Mom and Dad have a few million dollars in the IRA, and Junior's used to living on $50,000 a year, how do I pay that out in 10 years?

Mr. Redpath

I think one of the problems, though, with the standard sometimes, and it's kind of a bizarre provision in the tax code that if you're the trustee, and you have an unlimited discretion, that can be actually included in your estate for estate tax purposes.

Mr. Renn

Done right, that's not an issue; but yes, done wrong, it could be a problem.

Mr. Redpath

Well, you're right. But I'm saying, done right, you don't have a lot of problems except anticipated problems. Done wrong, you can get a lot of unanticipated problems that come in. So, what would you recommend to our viewers if they in fact have pre-SECURE trusts that were established, now that we're past 1/1/20? What should they be looking at doing?

Mr. Renn

If you have clients or if you have set up a trust, pre-SECURE Act, to hold your qualified plan or IRA money, you probably want to go back and revisit it, unless your beneficiary is going to qualify as an eligible designated beneficiary. And most of the time, when I talk to my clients about the folks that they wanted to set up those conduit trusts for, they don't necessarily think they'll qualify as disabled or chronically ill.

And kind of the scary part here is you can think of somebody as being disabled or chronically ill for decades. If they do not have that condition at the moment in time when the account holder dies, we don't qualify. So, it's really a snapshot at the time of death, so it's hard to even plan into this, because you think they're going to qualify, but what if they don't? It's an independent medical evaluation at that point in time.

But if you set these things up, you want to go back and revisit them. If you've got an accumulation trust, if you were happy with it before, you'll probably still be happy with it. If you have an eligible designated beneficiary who has either a disability or is chronically ill, you can qualify for a new type of multi-beneficiary trust, where as long as the disabled or chronically ill individual gets the benefit, it doesn't matter that there were other beneficiaries, where it can be split into shares as soon as the account holder dies. There's two ways to do that.

But particularly the conduit trust, and also any trust, and occasionally lawyers got lazy and they'd say the distribution was the RMD, required minimum distribution. Well, there really isn't an RMD for most designated beneficiaries anymore. It's pay it all out by year 10.

So, it doesn't provide for an annual stream of payments. It doesn't provide for any opportunity to get the money out in small chunks into the hands of a low-bracket taxpayer. It doesn't provide for any of that. And it can be a problem.

So, it's not that people won't be doing trusts for IRAs or qualified plan assets for individuals that need that kind of control, but they've got to be revisited. And we expected by now to have some pretty serious regulation on this. We thought we'd get some guidance. I think given COVID, given CARES Act and all the things the government's been dealing with for the last two years, we haven't seen them yet. And it would be really good to have them. But right now, I've been waiting for some guidance. I don't have it. I can't really wait anymore. Clients that have these provisions in place need to come in and get them fixed.

Mr. Redpath

What is this Section 678? What is that?

Mr. Renn

678 is really interesting. If you have a beneficiary who is a good kid beneficiary, if you're not worried about the child going and buying the Ferrari or blowing the money. If we've given certain powers of appointment to the beneficiaries, and they've attained those

standards, it's quite possible that we've made the IRA trust into a grantor trust, in the beneficiary's tax bracket. So effectively, instead of having those compressed rates, where at about $14,000, we're at the top marginal rate, we get the full run-up, which is going to be probably less if some of the Biden proposals make it through, but it's still half a million dollars for a married couple. So, there's some real progressivity in the system that we can still take advantage of.

Mr. Redpath

So, in essence, it comes similar to a grantor trust? Is that accurate?

Mr. Renn

Yes, the idea is, I say that in the trust document that my kids can appoint it all to themselves at age 35. And they're all over age 35. I mean, effectively, it's their money. They could take it at the snap of a hat. No creditor protection there, but to the extent that it's taxed to them, they can leave it in the account, and ultimately they'll pay the tax on it at their own rates instead of having the trust pay the tax on it as we go. So they could leave it in trust, allocate GST to it. I mean, there's some, for really dynastic families, where this is a lot of money, but it doesn't really amount to very much, we're seeing some of that activity. And in scenarios where the client is just absolutely freaked out by the idea of the compressed trust tax rates, this provides an out. But again, it's only for the good kid.

Mr. Redpath

Right. I have a lot of clients that are philanthropic, and they have accounts, and they would like to provide for a charity; but obviously, they still want to provide for grandchild, child, grandchild, whatever. What about that? How do we use that in this area?

Mr. Renn

A couple of ways to think about that. Charitable remainder trusts are certainly very viable planning opportunities here; and effectively, you could, using a CRT properly, you can probably go from a 10-year payout to a 20-year payout and, potentially, use some of that additional income to provide some life insurance to replace the missing benefits.

The other thing to think about, and it's really a very good point, Ian. I mean, sometimes I'll find people that are leaving a million dollars to their local charity in their will or in the rev trust, and they're leaving their qualified plan or their IRA to their children or their grandchildren. It's kind of backwards, because effectively, they could get that million dollars out of the estate, at least as we sit here today without paying any income tax on it, and you could give the qualified plan assets or the IRA assets that are basically subject to tax to the charity. The charity won't pay the tax, and they'll still get the million bucks. So, to some extent, it's an opportunity to come in and always make the clients look at their beneficiary designations. Do they have the right people? Are they happy with them?

And then, if you're actually taking after-tax assets and leaving it to the charity, maybe it should be the beneficiary designation of the qualified plan or the IRA, because that would be a much more tax-efficient way to fund your charitable giving.

Mr. Redpath

Ed, you said something a little while ago. We were talking about getting more guidance from the Internal Revenue Service, and you mentioned everything that's happened since 2020. So, we got the SECURE Act, basically kicked in 1/1/20. March comes along; and all of a sudden, everything breaks loose. The IRS has been so busy with everything else going on, and the guidance, and the EIP payments, and everything else that they have been tasked to do. The IRS has said there are millions and multi-millions of returns that they still haven't processed. And you can't fault them with everything that's been going on. So, we haven't had a lot of guidance. And as practitioners, boy, there's been so much to take in and so many changes, really, since March of 2020. We can kind of start with the Families First Act, and work our way through CARES and the Consolidated Appropriations and the acts we've had in 2021. So, we haven't had a lot of guidance.

Would you say that it's fair to say that it's really important now to try to sit down with our clients as soon as possible and go over the issues that we've talked about today?

Mr. Renn

Yes, because I think you know kind of what the right answer is here, right? It's really only around the fringes that we really don't know what's going on. So, for 98% of the clients, it's pretty clear. Some small, very small percentages are going to want to use trusts for IRA qualified plan benefits. Some that have been using trusts might just say, "Look, it doesn't work anymore. It's not worth it for me. It was one thing when Johnny could get it for 35 years, but if he's got to get it in 10, well, let's just give it to him. And let's be tighter with other funds, make sure that he can't really blow it. We'll do the best we can with him."

So, yes, I think now's a good time to come in and do it. I mean, as you mentioned, even in CARES, the RMDs for 2020 were waived. And that happened in March, late March, so people had already taken their distributions in January, February and early March. And they were trying to figure out how to put them back. The IRS does the best they can with the Q & A websites. I mean, there's a lot up on the web. It changes. It morphs. There's actually a provision now to actually start to chronicle their changes.

So, as the guidance changes, and you say, "But it used to say something different." You can actually go back and find where it used to say something different. But again, I mean, it's a democratization of information, but that said, we can't rely on it. It's not a private letter ruling. It's not a notice. It's not a rev ruling or a rev proc. So, that has advantages and disadvantages. But in COVID, we had no choice. We'd still be waiting for PPP, the first set of PPP rules, if we needed a formal process.

Mr. Redpath

Well, there's a good example of how the IRS was trying to catch up as quickly as possible with all the questions, and we still don't have the guidance on S corps that have accumulated E&P. We still don't have a guidance on how that's going to work out, but we're hoping we get it.

One of the things I think, Ed, for our viewers is I know there's a tendency among accountants to say, "You know what? Let the lawyers handle all that." And there's a tendency, and the lawyers, unfortunately, a lot of lawyers just rely on form books. I actually saw a form one time for an individual; and throughout the thing, it had the wrong name. They took somebody else's document and just didn't get the name changed everywhere.

So, I think it's really important for our viewers to understand that from the standpoint, you don't always have people like yourself, Ed, that are tax people and understand the tax law. And there's a lot of attorneys that do a lot of work, very competent, but they don't always know the tax implications of what they've done. So, I think it really is important for the accountants in the audience to understand that you should look at this for your clients. Don't just assume the lawyer is doing it. And don't just assume the lawyer did it right from a tax perspective. So, I want you to look at that. I always looked at it from the standpoint that the accountant and the lawyer, absent a high-level tax attorney, I think the accountant and the lawyer need to work together as a team. And I say that to, when we said, "Look at documents," we're not saying that you write the trust, but you should be at least aware of what the trust is and what a trust does and the types of provisions that should be in there and the tax implications, because maybe you're going to advise their legal counsel on these implications.

Mr. Renn

Yes, and the other player you can add to that is, in some cases, if the investment advisors are skilled and knowledgeable in this space, they're worth having. It's worth having them come and have a seat at the table. Not always, but if there's expertise there, and they have people that do this on a regular basis. A lot of times, they have really practical issues that lawyers and accountants don't necessarily think about.

Mr. Redpath

Well, Ed, a lot of interesting material today; but I think one of the takeaways is look at your client's situation and determine is there something that we need to do. Ed, I want to thank you for being here today. This is a really interesting topic, and your insight was great. So again, Ed, we're going to have you on the program again soon. Thanks for being here.

Mr. Renn

Thanks for having me.

RMDs and Use of Trusts in Retirement Plans

By Ian J. Redpath, JD, LLM

A. Beginning Date of RMDs

Generally, retirement accounts and arrangements are excellent tax shelters. They allow tax deductions or exclusions on the contributions, and the income accrues tax free. However, the government will not allow this to continue forever. At some point, the government wants to finally get the opportunity to tax that income. Distributions may be taken out, without an early withdrawal penalty of 10%, at age 59½. [IRC §72(t)(1)] The Code does provide some exceptions to the early withdrawal penalty, such as medical expenses, for distributions taken out before age 59½. [IRC §72(t)(2)]

In December of 2019, Congress passed the "Setting Every Community Up for Retirement Enhancement" Act (SECURE Act or Act), that significantly changed the RMD beginning date (RBD). The Act changes the required beginning date for distributions required to be made after December 31, 2019, with respect to individuals who attain age 70½ after that date. For IRAs, it is April 1 following the calendar year in which the IRA owner attains age 72. For employer-sponsored retirement plans, for non-5% company owners, the RBD is April 1 following the later of the calendar year in which the employee attains age 72 or retires. For an employee who is a 5% owner, the RBD is the same as for IRAs even if the employee continues to work past age 72 [§§401(a)(9)(C)(i)(I), and (I)] Additionally, where an IRA or retirement plan account owner dies before the RBD and the spouse is the account's beneficiary, the spouse will be able to delay distributions from the decedent's account until December 31 of the year in which the decedent would have attained age 72.

The terms of a plan may allow a person to wait until the year he/she actually retires to take the first RMD. Alternatively, a plan may require him/her to begin receiving distributions by April 1 of the year after he/she reaches age 72, even if he/she has not retired. However, those who are considered to be 5% or more owners of the business sponsoring the plan are not allowed to take advantage of this rule. [PLR 200453015 and PLR 200453026] A plan may provide that an employee can receive a pension plan distribution after reaching age 62, even if he/she has not separated from employment at the time of the distribution. [IRC §401(a)(36), & Reg. §1.401(a)-1(b)(1)(i)]

Even though an employee has commenced receiving RMDs, an employer must continue to make contributions and allow the employee the option to continue making salary deferrals if the plan permits them. If the employer does not, they will be out of compliance with the terms of the plan and lose its qualified status unless corrected. This can be corrected through the Employee Plans Compliance Resolution System.

The RMD rules apply to all employer-sponsored retirement plans, including profit-sharing plans, §401(k) plans, §403(b) plans, and §457(b) plans. The RMD rules also apply to traditional IRAs and IRA-based plans such as SEPs, SARSEPs, and SIMPLE IRAs. The RMD rules also apply to Roth §401(k) accounts. However, the RMD rules do not apply to Roth IRAs while the owner is alive.

B. Calculating the RMD

RMDs are the minimum amount that must be withdrawn from an applicable account each year. This is the minimum, so a taxpayer may always take an amount that is greater than the RMD. The amount distributed will be included in the taxpayer's taxable income except to the extent it is a return of capital (investment) or qualified distribution from designated Roth accounts. This, in addition to the social security that is taxable, will increase the taxpayer's AGI and increase the potential negative effects of a greater AGI.

An IRA owner must calculate the RMD separately for each IRA that he/she owns; however the RMD, in aggregate, can be withdrawn from one or more of the IRAs. The owner of a §403(b) account must calculate the RMD separately for each §403(b) contract and, like an IRA, can take the aggregate RMD from one or more of the §403(b) contracts. This is not the same for other retirement accounts. RMDs from §401(k) and §457(b) plans have to be calculated and withdrawn separately from each of those accounts.

If the owner of a plan rolls over amounts to another plan, then the benefit of the employee under the receiving plan is increased by the amount rolled over for purposes of determining the required minimum distribution for the year following the year in which the amount rolled over is distributed.

In calculating an employee's RMD, consideration is given to any contributions made for the employee. For defined contribution plans, calculate the RMD for an employee by dividing his/her prior December 31 account balance by a life expectancy factor in the applicable table. The tables may be found in Appendix B of IRS Publication 590-B. A defined benefit plan generally must make RMDs by distributing the participant's entire interest, as calculated by the plan's formula, in periodic annuity payments for:

- the participant's life,
- the joint lives of the participant and beneficiary, or
- a "period certain" [Reg. §1.401(a)(9)-6, A-3].

If an account owner dies, the RMD for the year of death is the RMD the account owner would have received that year. Thereafter, the amount of the RMD will depend on the identity of the designated beneficiary. Beneficiaries of retirement accounts and IRAs calculate RMDs using the Single Life Table. The table shows a life expectancy based on the beneficiary's age. The account balance is divided by this life expectancy to determine the first RMD. The life expectancy is reduced by one for each subsequent year. Spouses who are the sole designated beneficiary have special rules that apply. They can:

- treat an IRA as their own, or
  - base RMDs on their own current age;
  - base RMDs on the decedent's age at death, reducing the distribution period by one each year; or
  - withdraw the entire account balance by the end of the 5th year following the account owner's death, if the account owner died before the required beginning date.

When an account owner dies before the required beginning date, the surviving spouse can wait until the owner would have turned 72 to begin receiving RMDs. [IRC §401(a)(9)(B) and Reg. §1.401(a)(9)-3]

Individual beneficiaries, other than a spouse, can:

- withdraw the entire account balance by the end of the 5th year following the account owner's death, if the account owner died before the required beginning date, or
- calculate RMDs using the distribution period from the Single Life Table based on:
  1. If the owner died after RMDs began, the longer of the:
     - beneficiary's remaining life expectancy determined in the year following the year of the owner's death reduced by one for each subsequent year or
     - owner's remaining life expectancy at death, reduced by one for each subsequent year.
  2. If the account owner died before RMDs began, the beneficiary's age at year-end following the year of the owner's death, reducing the distribution period by one for each subsequent year. [Reg.§1.401(a)(9)-3]

After the first year, a taxpayer is required to withdraw the RMD by December 31 of each year. This can result in a bunching of two distributions into income for the first year, the first distribution due by April 1 and an additional distribution by December 31. To avoid having both of these amounts included in income for the same year, the first distribution should be taken by December 31 of the year the person turns 72 instead of waiting until April 1 of the following year.

The IRS adopted new regulations that reflect longer life expectancies than the tables in the existing regulations. The effect of these changes would be to reduce annual RMDs due to longer mortality rates. The life expectancy distribution tables would apply for distributions in calendar years beginning on or after January 1, 2021. [Reg. §1.401(a)(9)-9(f)(1)]

Example: For an individual who attains age 70½ during 2019 (the RMD for the distribution calendar year 2019 is due April 1, 2020), the final regulations would not apply to the RMD for the individual's 2019 distribution calendar year (April 1, 2020), or for the 2020 year, but would apply to the RMD for the individual's 2021 distribution calendar year (December 31, 2021).

If the RMD is not met, there may be a significant penalty. There is a 50% excise tax on the amount not distributed as required. An excess distribution from one year cannot be used to reduce the RMD in another. To report the excise tax, you may have to file Form 5329. The penalty may be waived if the shortfall was due to a reasonable error and that reasonable steps are being taken to remedy the shortfall. In order to qualify for this relief, you must attach a letter of explanation to Form 5329. [IRC §4974(a) and Reg. §54.4974-2]

Under pre-SECURE Act, the after-death minimum distribution rules vary depending on (a) whether an employee (or IRA owner) dies before, on, or after the required beginning date, and (b) whether there is a designated beneficiary for the benefit. Under the regulations, a designated beneficiary generally must be an individual. If an employee (or IRA owner) dies on or after the required beginning date, the basic statutory rule is that the remaining interest must be distributed at least as rapidly as under the method of distribution being used before death.

Effective for distributions with respect to employees (or IRA owners) who die after December 31, 2019, the SECURE Act modifies the required minimum distribution rules upon death of the owner or employee. The general rule is that after an employee (or IRA owner) dies, the remaining account balance must be distributed to designated beneficiaries within 10 years after the date of death. This rule applies regardless of whether the employee (or IRA owner) dies before, on, or after the required beginning date, unless the designated beneficiary is an eligible designated beneficiary. [§401(a)(9)(H)(i)] The Committee Report explains that under the 10-year rule, the remaining account balance must be distributed by the end of the tenth calendar year following the year of the employee or IRA owner's death. This was meant to reduce the use of "stretch IRAs."

An exception to the 10-year rule for post-death required minimum distributions applies to an eligible designated beneficiary. This is an individual who, with respect to the employee or IRA owner, on the date of his or her death, is:

(1) the surviving spouse of the employee or IRA owner;

(2) a child of the employee or IRA owner who has not reached majority;

(3) a chronically ill individual as specially defined in §401(a)(9)(E)(ii)(IV), or

(4) any other individual who is not more than ten years younger than the employee or IRA owner.

In this case, the remaining account balance generally may be distributed (similar to pre-Act law) over the life or life expectancy of the eligible designated beneficiary, beginning in the year following the year of death. [§401(a)(9)(E); §401(a)(9)(H)(ii)] The account balance must be distributed within 10 years after the death of the eligible designated beneficiary. [§401(a)(9)(H)(iii)] After a child of the employee or IRA owner reaches the age of majority, the balance in the account must be distributed within 10 years after that date. [§401(a)(9)(E)(iii)]

For a collectively bargained plan, the changes apply to distributions with respect to employees who die in calendar years beginning after the earlier of:

(1) The later of (A) the date on which the last collective bargaining agreement ratified before the date of enactment (December 20, 2019) terminates, or (B) December 31, 2019; or

(2) December 31, 2021. [SECURE Act §401(b)(2)]

For governmental plans [as defined in §414(d)], the changes apply to distributions with respect to employees who die after December 31, 2021. [SECURE Act §401(b)(3)]

C. Trust Beneficiaries

When a trust is named as the beneficiary of a retirement account, the trust inherits the account at the death of the owner. The account is now an asset of the trust and subject to the terms of the trust, not to be confused with the Code rules that must be applied. The rules of both need to be reviewed to assure that the owner can accomplish what they intend. Since these assets go to the beneficiaries, probate costs are reduced.

There are many reason why a trust may be a good option as a beneficiary. Among those are: providing for minor children or supporting an individual with special needs who will lose access to government benefits if he or she owns assets in his or her own name. It can be used effectively in providing for a second spouse or other person during his/her lifetime and then "pour-over" the remaining assets to others such as children not with that person. The use of a trust can provide so-called "spend-thrift" protection against a beneficiary who the owner believes is not capable of handling finances prudently. While the retirement account may be subject to the creditors of the owner at death, it will not be subject to the claims of the beneficiary's creditors. [*Clark v. Rameker* (2014)] Another advantage of a trust is the ability to name successor beneficiaries and thus maintain a level of control, even after death. Many estate plans for wealthy individuals include trusts designed to minimize and postpone the payment of federal and state estate tax. For such estate plans to work as intended, the portion of these trusts that shelters an individual's federal or state estate tax exemption amounts needs to be funded upon the individual's death. Often, the only asset available to do this funding is an IRA.

For purposes of the RMD rules, only an individual may be a designated beneficiary, However, where a trust is named as a beneficiary, the beneficiaries of the trust (and not the trust itself) will be treated as the designated beneficiaries for purposes of determining the distribution period under the RMD rules. To qualify, the following must be met:

(1) the trust is a valid trust under state law, or would be valid if it were funded;

(2) the trust is irrevocable, or by its terms, will become irrevocable upon the death of the employee;

(3) the beneficiaries of the trust can be identified for rules concerning how individuals who are not named are identified); and

(4) the required documentation is timely provided to the plan administrator. [Reg. §1.401(a)(9)-4, Q&A 5]

This is often called a look-through or see-through trust. It affects the period over which RMDs must be paid as they may be determined using the life of the designated beneficiaries.

The designated beneficiary determination must be made under the terms of the trust as it existed at the IRA owner's (or employee's, as applicable) death. The separate account rules are not available to beneficiaries of a trust with respect to the trust's interest in the employee's benefit. [Reg §1.401(a)(9)-4, Q&A 5(c)] Thus, where a trust was designated as the beneficiary of an IRA, the trust could be divided into three separate accounts (or subtrusts) and placed in three IRAs, one for each of the initial IRA owner's three children, after the IRA owner's death. However, the payout period for required distributions from the three separate accounts had to be determined using the life expectancy of the oldest of the three children. [PLR 200317041; PLR 200317043; and PLR 200317044]

The post-death RMDs for a trust named as an IRA beneficiary will be calculated under either the stretch payout rule, the 10-year rule, or the 5-year rule, depending on certain attributes of the trust and the trust beneficiaries. It matters whether the trust qualifies as a see-through trust, whether it is a conduit trust or an accumulation trust, and whether the trust beneficiaries are non-individuals, "regular" beneficiaries, or part of the new class of "eligible designated beneficiaries."

It is important to remember that the RMD payout rules may be different than the payout provisions of the trust. Even if there is a payout to the trust under the 5-year rule, the trust does not necessarily have to distribute it to its beneficiaries. That is governed by the terms of the trust.

Practitioners should work closely with attorneys to ensure the proper language to obtain the benefit sought is in the trust. The rules are generally strictly construed.

D. Qualified Charitable Distributions

A qualified charitable distribution (QCD) allows a distribution from an IRA of up to $100,000 per year which may be counted towards the owner's RMD for the year. The owner must be at least 70½ years old on the date of distribution under IRC §408(d)(8). The limitation is per taxpayer, not per account. However, the distribution up to $100,000 can come from different IRA accounts of the owner. This can apply to the beneficiary of an inherited IRA as long as the beneficiary is at least age 70½ on the date of the distribution. [Notice 2007-7, Q&A-36] The distribution must go to a public charity under IRC §170(b)(1)(A). It cannot go to a private foundation, a supporting organization, or a donor-advised fund. It must go from the account to the charity and not as a distribution to the owner who then makes the contribution.

Under the Act, effective for distributions made for tax years beginning after December 31, 2019, the amount of a taxpayer's QCD that is not included in gross income for a tax year is reduced (but not below zero) by the excess of: (1) the total amount of IRA deductions allowed to the taxpayer for all tax years ending on or after the date he or she attains age 70½, over (2) the aggregate amount of such reductions for all tax years preceding the current tax year. [§408(d)(8)(A)]

E. Conclusion

The baby boom generation has accumulated a substantial amount of wealth. Many have been engaged in some level of planning for retirement. Practitioners will be faced with an escalating number of challenges in planning for RMDs and the overall impact on our client's tax situation. It is important to have an understanding of the rules applicable to RMDs. Trusts can have a major impact on planning for beneficiaries.

A. Discussion Problems

You have been presented with the following information concerning clients of the firm:

Lauren is widowed and turned age 70½ on February 16, 2020. She has several IRAs, including a Roth IRA that she established many years ago.

Lauren has three children that are eight years apart in age. One of them, Bill, has not been able to keep a regular job, and she is concerned about his ability to handle his finances upon her death.

Required:

1) When does Lauren need to begin taking RMDs?

2) Upon Lauren's death, when must the RMD distributions be made to her children beneficiaries?

3) Discuss the advantage of a trust under these facts.

Address all issues fairly presented.

B. Suggested Answers to Discussion Problems

1) Under the SECURE Act, Lauren's first RMD is due no later than April 1 of the year following the year she turns 72, not 70½ (as it was for individuals that turned 70½ prior to January 1, 2020). Therefore, since Lauren will turn 71 in August of 2020 and 72 in August of 2021, her RBD is April 1 of 2022.

2) The amount of the RMD will depend on the identity of the designated beneficiary. Beneficiaries of retirement accounts and IRAs calculate RMDs using the Single Life Table. The table shows a life expectancy based on the beneficiary's age. The account balance is divided by this life expectancy to determine the first RMD. The life expectancy is reduced by one for each subsequent year. When an account owner dies before the required beginning date, the surviving spouse can wait until the owner would have turned 72 to begin receiving RMDs. [IRC §401(a)(9)(B) and Reg. §1.401(a)(9)-3]

   Individual beneficiaries, other than a spouse, can:

   - withdraw the entire account balance by the end of the 5th year following the account owner's death, if the account owner died before the required beginning date, or
   - calculate RMDs using the distribution period from the Single Life Table based on:
     a) If the owner died after RMDs began, the longer of the:
        - beneficiary's remaining life expectancy determined in the year following the year of the owner's death reduced by one for each subsequent year or
        - owner's remaining life expectancy at death, reduced by one for each subsequent year.
     b) If the account owner died before RMDs began, the beneficiary's age at year-end following the year of the owner's death, reducing the distribution period by one for each subsequent year. [Reg.§1.401(a)(9)-3]

   Effective for distributions with respect to employees (or IRA owners) who die after December 31, 2019, the SECURE Act modifies the required minimum distribution rules upon death of the owner or employee. The general rule is that after an employee (or IRA owner) dies, the remaining account balance must be distributed to designated beneficiaries within 10 years after the date of death. This rule applies regardless of whether the employee (or IRA owner) dies before, on, or after the required beginning date, unless the designated beneficiary is an eligible designated beneficiary. [§401(a)(9)(H)(i)] The Committee Report explains that under the 10-year rule, the remaining account balance must be distributed by the end of the tenth calendar year following the year of the employee or IRA owner's death. This was meant to reduce the use of "stretch IRAs."

   An exception to the 10-year rule for post-death required minimum distributions applies to an eligible designated beneficiary. This is an individual who, with respect to the employee or IRA owner, on the date of his or her death, is:

   (1) the surviving spouse of the employee or IRA owner;

   (2) a child of the employee or IRA owner who has not reached majority;

   (3) a chronically ill individual as specially defined in §401(a)(9)(E)(ii)(IV), or

   (4) any other individual who is not more than ten years younger than the employee or IRA owner.

   A determination is made at that time as to the applicable rules.

(3) The facts indicate that a trust as beneficiary may be needed with Bill's situation. While the RMD will control the distributions to the trust, the terms of the trust will control the distributions to the beneficiaries. The RMD will be based on the age of the youngest beneficiary. Generally, the 10-year distribution rule will apply to this situation. A determination should be made if any of the other children beneficiaries would be a qualified designated beneficiary and an exception to the 10-year rule.

GLOSSARY OF KEY TERMS

Coronavirus Aid, Relief, and Economic Security Act (CARES Act)—H.R. 748, also known as the CARES Act, is the third coronavirus relief package and was signed into law on March 27, 2020. This bill had bipartisan support in both the Senate and House and contains both tax and non-tax provisions applicable to individuals and businesses.

Eligible Designated Beneficiary—An eligible designated beneficiary is an individual who, with respect to the employee or IRA owner, on the date of his or her death, is the surviving spouse of the employee or IRA owner; a child of the employee or IRA owner who has not reached majority; or any other individual who is not more than ten years younger than the employee or IRA owner

Offer in Compromise—The IRS has the ability to "compromise" a civil or criminal tax liability after assessment and before referral to the Department of Justice. The taxpayer may seek a compromise based on doubt as to collectibility, doubt as to liability, or to promote effective tax administration. The process is known as offer in compromise (OIC) and constitutes an agreement between a taxpayer and the IRS to accept less than full payment.

Required Beginning Date (RBD)—The date on which minimum distributions from individual retirement accounts and certain employer-provided retirement plans are required to begin. Under pre-SECURE Act law, the RBD is April 1 following the calendar year in which the owner attains age 70½. The SECURE Act revises this to April 1 following the calendar year in which the IRA owner attains age 72.

Setting Every Community Up for Retirement Enhancement (SECURE Act)—Part of the Further Consolidated Appropriations Act, 2020 (H.R. 1865, P.L. 116-94, the SECURE Act was enacted on December 20, 2019. It provides expanded opportunities for individuals for retirement savings and makes a number of administrative simplifications. It also includes a change to the kiddie tax.

Tax Cuts and Jobs Act (TCJA)—Public Law No. 115-97, an act to provide for reconciliation pursuant to titles II and V of the concurrent resolution on the budget for fiscal year 2018, was signed into law by President Trump on December 22, 2017. Although not the official name for the new legislation, it is most commonly referred to as the Tax Cuts and Jobs Act (TCJA).

CUMULATIVE INDEX 2021

BY TOPIC

BY CITATION

BY SPEAKER

Choose the best response and record your answer in the space provided on the answer sheet.

1. According to Ian Redpath, which of the following emphasizes that partners must report their share of the partnership income as reported on their K-1 regardless of whether they received a distribution?

   A. *Boechler, P.C. v. Commissioner*
   B. *Patrick Combs v. Commissioner*
   C. *Taryn L. Dodd v. Commissioner*
   D. *U.S. v. Robin S. Richards*

2. According to Ian Redpath, which of the following recommends that the IRS get correctable error authority?

   A. IR-2021-193
   B. IRS Practice Unit
   C. TIGTA Audit Report No. 2021-40-070
   D. Wyden Partnership Reform Legislation

3. According to Ian Redpath, which of the following finalizes 2019 proposed regs?

   A. IR-2021-193
   B. IRS Practice Unit
   C. TD 9954
   D. TIGTA Audit Report No. 2021-40-070

4. According to Ian Redpath, which of the following emphasizes that an individual must report as dividend income the amount of personal expenses paid through a corporation?

   A. *Patrick Combs v. Commissioner*
   B. *Taryn L. Dodd v. Commissioner*
   C. *Thomas A. Connelly v. U.S.*
   D. *U.S. v. Robin S. Richards*

5. According to Ian Redpath, which of the following provides guidance for farmers and ranchers seeking capital gain relief?

   A. IR-2021-193
   B. IRS Practice Unit
   C. TD 9954
   D. TIGTA Audit Report No. 2021-40-070

Continued on next page

6. According to Ian Redpath and Larry Pon, which of the following is ***not*** one of the first questions to ask when a client has been turned over to collections and owes the IRS $100,000?

   A. Have all required tax returns been filed?
   B. How much do you want to pay with your offer in compromise?
   C. Is $100,000 the correct amount?
   D. What elements are in the $100,000 total?

7. According to Ian Redpath and Larry Pon, which of the following is ***not*** one of the reasons the IRS will accept an offer in compromise?

   A. Effective tax administration
   B. Doubt as to liability
   C. Doubt as to correctness
   D. Doubt as to collectibility

8. According to Ian Redpath and Larry Pon, which of the following would be most likely to file a Form 433-A?

   A. C corporation with less than 10 stockholders
   B. Individual with Schedule C income
   C. Partnership with 25 or fewer partners
   D. S corporation with two shareholders

9. According to Ian Redpath and Larry Pon, which of the following has the highest probability of having an offer in compromise accepted by the IRS?

   A. Individual currently involved in bankruptcy proceedings
   B. Individual current on business tax returns but not individual returns
   C. Individual with high medical bills for dependent child
   D. Individual with previously unfulfilled offer in compromise

10. According to Ian Redpath and Larry Pon, which of the following is the approximate payment due with a $100,000 offer in compromise filed by an individual (unless they qualify for the low-income exception?

   A. $0
   B. $200
   C. $2,000
   D. $20,000

Continued on next page

11. According to Ian Redpath and Ed Renn, the SECURE Act changed the option of lifetime payouts for designated beneficiaries that inherit an IRA after which of the following?

    A. 12/31/2018
    B. 12/31/2019
    C. 12/31/2020
    D. 12/31/2021

12. According to Ian Redpath and Ed Renn, which of the following is correct regarding IRS Publication 530?

    A. It has been discontinued.
    B. It is a new publication scheduled for 2022.
    C. It has been updated but may not be completely accurate and should be read with caution.
    D. The IRS has confirmed that it is 100% accurate.

13. According to Ian Redpath and Ed Renn, which of the following ***cannot*** generally be deemed an eligible designated beneficiary?

    A. Adult child
    B. Chronically ill
    C. Disabled
    D. Spouse

14. According to Ian Redpath and Ed Renn, what is the RBD for an individual that attains age 70 in January 2020?

    A. April 1, 2020
    B. April 1, 2021
    C. April 1, 2022
    D. April 1, 2023

15. According to Ian Redpath and Ed Renn, which of the following is ***not*** an option for a designated beneficiary that inherits an IRA on April 15, 2022?

    A. They can take lifetime payouts based on the new life expectancy table.
    B. They can take an immediate lump sum distribution.
    C. They can take a lump sum distribution on January 1, 2032.
    D. They can take equal distribution amounts as long as they follow the 10-year rule.

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Evaluation Form

Please take a few minutes to complete this survey related to the **CPE Network® Tax Report** and return it by mail to 2395 Midway Road, Carrollton, Texas 75006, Attn: Managing Editor. All responses will be kept confidential. Comments in addition to the answers to these questions are also welcome. Please send comments to **CPLgrading@thomsonreuters.com.**

How would you rate the topics covered in the November 2021 **CPE Network® Tax Report?** Rate each topic on a scale of 1–5 (5=highest):

	Topic Relevance	Topic Content/ Coverage	Topic Timeliness	Video Quality	Audio Quality	Written Material
Experts' Forum	|_______|	|_______|	|_______|	|_______|	|_______|	|_______|
Offers in Compromise	|_______|	|_______|	|_______|	|_______|	|_______|	|_______|
Trusts as Beneficiaries	|_______|	|_______|	|_______|	|_______|	|_______|	|_______|

Which segments of the November 2021 issue of **CPE Network® Tax Report** did you like the most, and why?

____

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____

____

Which segments of the November 2021 issue of **CPE Network® Tax Report** did you like the least, and why?

____

____

____

____

What would you like to see included or changed in future issues of **CPE Network® Tax Report**?

____

____

____

____

Are there any other ways in which we can improve **CPE Network® Tax Report**?

____

____

____

____

How would you rate the effectiveness of the speakers in the November 2021 **CPE Network® Tax Report**? Rate each speaker on a scale of 1–5 (5 highest):

	Overall	**Knowledge of Topic**	**Presentation Skills**
Ian Redpath	|______|	|______|	|______|
Larry Pon	|______|	|______|	|______|
Ed Renn	|______|	|______|	|______|

Which of the following would you use for viewing CPE Network® A&A Report? DVD ☐ Streaming ☐ Both ☐

Are you using **CPE Network® Tax Report** for: CPE Credit ☐ Information ☐ Both ☐ ______________________

Were the stated learning objectives met? Yes ☐ No ☐ ______________________

If applicable, were prerequisite requirements appropriate? Yes ☐ No ☐ ______________________

Were program materials accurate? Yes ☐ No ☐ ______________________

Were program materials relevant and contribute to the achievement of the learning objectives? Yes ☐ No ☐ __________

Were the time allocations for the program appropriate? Yes ☐ No ☐ ______________________

Were the supplemental reading materials satisfactory? Yes ☐ No ☐ ______________________

Were the discussion questions and answers satisfactory? Yes ☐ No ☐ ______________________

Were the audio and visual materials effective? Yes ☐ No ☐ ______________________

Specific Comments: ____

____

Name/Company ____

Address ____

City/State/Zip ____

Email ____

Once Again, Thank You…
Your Input Can Have a Direct Influence on Future Issues!

CPE Network®

CPE Group Attendance Sheet

Firm/Company Name: ____________________

Account #: ____________________

Location: ____________________

Program Title: CPE Network Tax Report, November 2021 Date: __________

Name	Email	Total Hrs	IRS PTIN ID (if applicable Tax only)	Sign In	Sign Out

I certify that the above individuals viewed and were participants in the group discussion with this issue/segment of the CPE Network® newsletter, and earned the number of hours shown.

Instructor Name: ____________________ Date: __________

E-mail address: ____________________

License State and Number: ____________________

CHECKPOINT LEARNING NETWORK

CPE NETWORK®
USER GUIDE

Group Live CPE Credit (Sponsored by "Checkpoint Learning Network")

Promotional Information:
CPE Program Sponsors must provide descriptive materials that enable CPAs to assess the appropriateness of learning activities. If you are delivering this course within your firm, you should complete the following table and circulate it to attendees prior to the classroom course delivery. Refer to the executive summary for certain information noted below. Be sure to include the completed sheet when you request certificates for this event.

Title of Course (Enter full title)	
Date of Class (MM/DD/YYYY)	
Time (Enter time of class)	
Location (Enter location of class)	
Learning Objectives (Refer to executive summary)	
Program Description (Refer to executive summary)	
Instructional delivery method	Group Live
Recommended CPE credit	3.0 Credits
Recommended field of study(ies) (Refer to executive summary)	
Program Level	Update
Prerequisites (Circle One)	• Basic Accounting and Auditing professional experience
	• Basic Tax professional experience
	• Basic Governmental professional experience
Advance preparation	None required
Course registration and, where applicable, attendance requirements (1)	

(1) Insert instructions for your students to register for the class and any other attendance requirements (e.g., bring your laptop, be prepared to work in groups, you will be required to sign in and sign out of the session, etc.

Determining CPE Credit Increments

Group study sessions are measured by program length, with one 50-minute period equal to one CPE credit. One-half CPE credit increments (equal to 25 minutes) are permitted after the first credit has been earned. Discussion leaders must monitor the program length and the participants' attendance in order to request the appropriate numberof CPE credits.

Note: All Network CPE products are developed and intended to be delivered as 3 CPE credits.*

Monitoring Attendance

While it is the participant's responsibility to report the appropriate number of credits earned, CPE program sponsors must maintain a process to monitor individual attendance at group programs to assign the correct number of CPE credits. A participant's self-certification of attendance alone is not sufficient.

The CPE group attendance sign-in sheet should list the names of each instructor and her/his credentials, as well as the name of each participant attending the seminar. The participant is expected to sign the CPE group attendance sheet at the beginning and sign out at the end of the session. If a participant arrives late and/or leaves early, the hours actual hours they attended should be documented on the sign-in sheet and should be reflected on the participant's CPE certificate.

***Effective November 1, 2018:** Checkpoint Learning CPE Network products 'group live' sessions must be delivered as 3 CPE credits and accredited to the field(s) of study as designed by Checkpoint Learning Network. After November 1, 2018, Checkpoint Learning Network will no longer issue certificates for "group live" deliveries of less than 3 CPE credits (unless the course was delivered as 3 credits and there are partial credit exceptions (such as late arrivals and early departures).

Note that Checkpoint Learning CPE Network can still be tailored by firms to smaller courses (e.g., 1 credit or 2 credit deliveries); however, when this is done, "Checkpoint Learning Network" cannot act as the sponsor and will not issue certificates of completions to participants. If a firm wishes to tailor (i.e., shorten. lengthen, and/or adjust field(s) of study), the firm delivering the tailored content must become the sponsor and that firm's name and sponsor identification number must appear on the certificates of completion. In these cases, there is no need to send attendance sheets back to Checkpoint Learning Network. If attendance sheets are submitted to Checkpoint Learning Network for modified deliveries as noted above (not withstanding late arrivals and early departures), the attendance sheets will be returned to you.

Real Time Instructor During Program Presentation

Group live programs must have a qualified, real time instructor while the program is being presented. Program participants must be able to interact with the instructor while the course is in progress (including the opportunity to ask questions and receive answers during the presentation).

Elements of Engagement

A group live program must include at least one element of engagement related to course content during each credit of CPE (for example, group discussion, polling questions, instructor-posed question with time for participant reflection, or use of a case study with different engagement elements throughout the program).

Make-Up Sessions

Individuals who are unable to attend the group study session may use the program materials for self-study either in print or online.

- If print materials are used, the user should read the materials, watch the DVD, and answer the quizzer questions on the CPE Quizzer Answer Sheet. Send the answer sheet and course evaluation to the address listed on the answer sheet and the CPE certificate will be mailed or emailed to the user. Detailed instructions are provided on Network Program Self-Study Options.
- If the online materials are used, the user should log on to her/his individual Checkpoint Learning account to read the materials, watch the interviews, and answer the quizzer questions. The user will be able to print her/his CPE certificate upon completion of the quizzer. (If you need help setting up individual user accounts, please contact your firm administrator or customer service.)

Awarding CPE Certificates

The CPE certificate is the participant's record of attendance and is awarded by Checkpoint Learning Network after the group study documentation is received (and providing the course is delivered as 3 CPE credits). The certificate of completions should reflect the credit hours earned by the individual, with special calculation of credits for those who arrived late or left early.

Subscriber Survey Evaluation Forms

NASBA requires the group study session to include a means for evaluating quality. At the conclusion of the group live session, evaluations should be distributed and collected from participants and sent to Checkpoint Learning Network along with the other course materials. A preprinted evaluation form is included in the transcript each month for your convenience.

Retention of Records

Regardless of whether Checkpoint Learning Network is the sponsor for the group live session, it is required that the firm hosting the group live session retain the following information for a period of five years from the date the program is completed unless state law dictates otherwise:

- Record of participation (Group Study Attendance sheets; indicating any late arrivals and/or early departures)
- Copy of the program materials;
- Timed agenda with topics covered and elements of engagement used
- Date and location of course presentation
- Number of CPE credits and field of study breakdown earned by participants
- Instructor name and credentials
- Results of program evaluations

Copyrighted Materials

The program materials are copyrighted and may not be reproduced in another document or manuscript in any form without the permission of the publisher. As a subscriber of the CPE Network® series you may reproduce the necessary number of participant manuals needed to conduct your group study session.

Finding the Transcript

When the DVD is inserted into a DVD drive, the video will immediately begin to play and the menu screen will pop up taking the entire screen. Hitting the Esc key should minimize it to a smaller window. To locate the pdf file of the transcript either to save or email to others, go to the start button on the computer. In My Computer, open the drive with the DVD. The Adobe

Acrobat files are the transcript files. If you do not currently have Adobe Acrobat Reader (Mac versions of the reader are also available.), a free version of the reader may be downloaded at:

- https://get.adobe.com/reader/

Request Participant CPE Certificates

When delivered as 3 CPE credits, documentation of your group study session should be sent to Checkpoint Learning by one of the following:

Mail: Thomson Reuters
PO Box 115008
Carrollton, TX 75011-5008

Email: CPLgrading@thomsonreuters.com

Fax: 888.286.9070

Before sending your package to Thomson Reuters, please be sure to include the following:

___ Promotional Sheet (completed)

___ Group Attendance Sheets (indicating any late arrivals and/or early departures)

___ Subscriber Survey Evaluation Forms

___ Name, title, and credentials of discussion leader(s) entered at the bottom of Group Attendance Sheet

CPE Network Self-Study Options

If you are unable to attend the live group study session, we offer two options for you to complete your Network Report program.

Self-Study—Print

Follow these simple steps to use the printed transcript and DVD:

- Watch the DVD.
- Review the supplemental materials.
- Read the discussion problems and the suggested answers.
- Complete the quizzer by filling out the bubble sheet enclosed with the transcript package.
- Complete the survey. We welcome your feedback and suggestions for topics of interest to you.
- Mail your completed quizzer and survey to:

  Thomson Reuters
  PO Box 115008
  Carrollton, TX 75011-5008

Best Practices Via Teams/Zoom

With the events surrounding the coronavirus many groups are unable to meet in person. Playing the video via Teams/Zoom or other conferencing software is one means of viewing the video. While the video from the Checkpoint Learning online accounts can be played through Teams/Zoom, the user experience will be better if the video files are shared via the desktop, which can be accomplished by copying the files from the DVD to the desktop and then sharing. Please note to enable viewers to hear the video being played follow the below instructions.

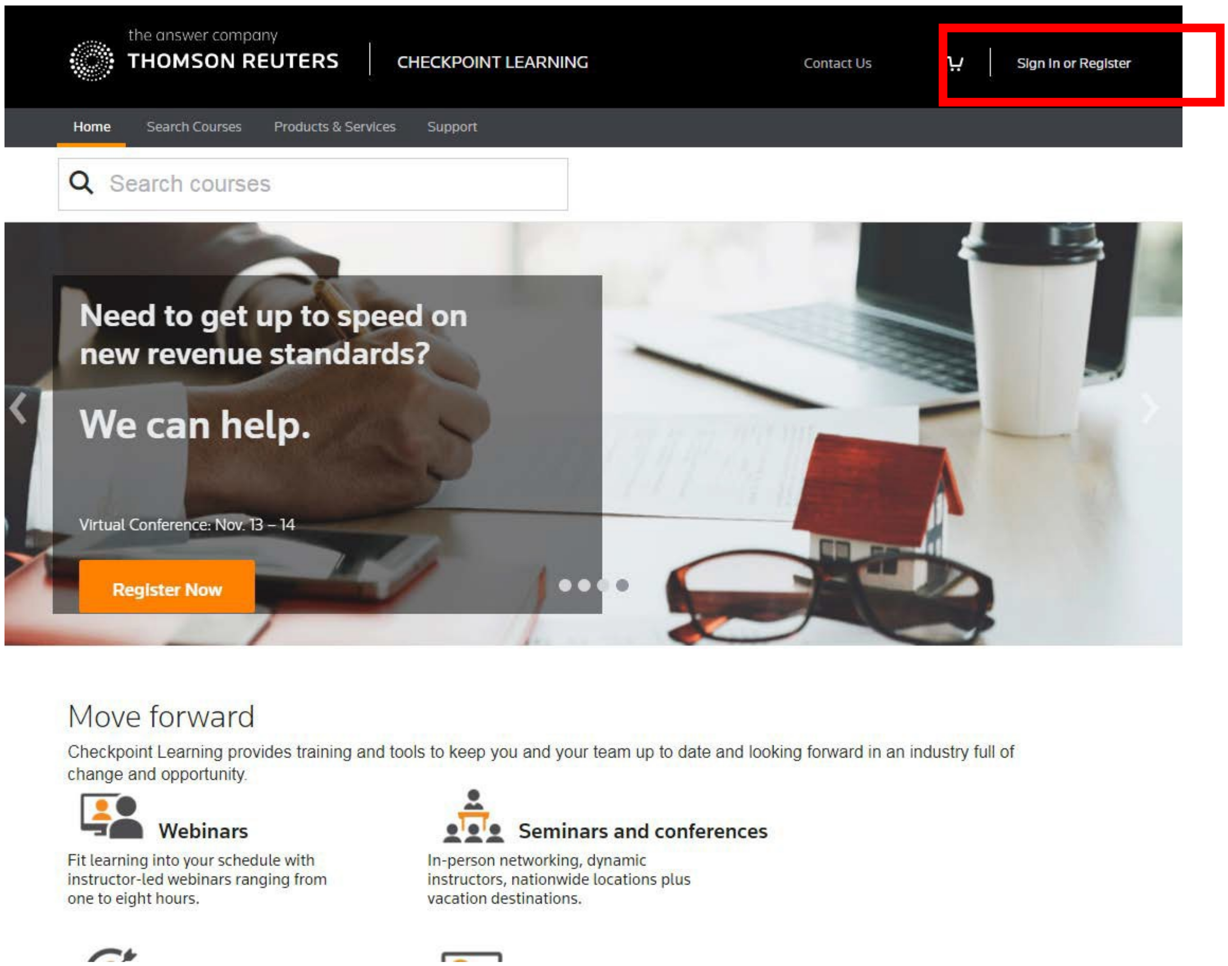
In Teams, when sharing the desktop with others, be sure to check the Share system audio box directly above the desktop to be shared, for the video's audio to be heard by others.

In Zoom, click the Share Screen button in the toolbar. Check the box to Share computer sound at the bottom of the Share Screen popup. Adjust the volume to an appropriate level. Do make sure the video is visible to participants.

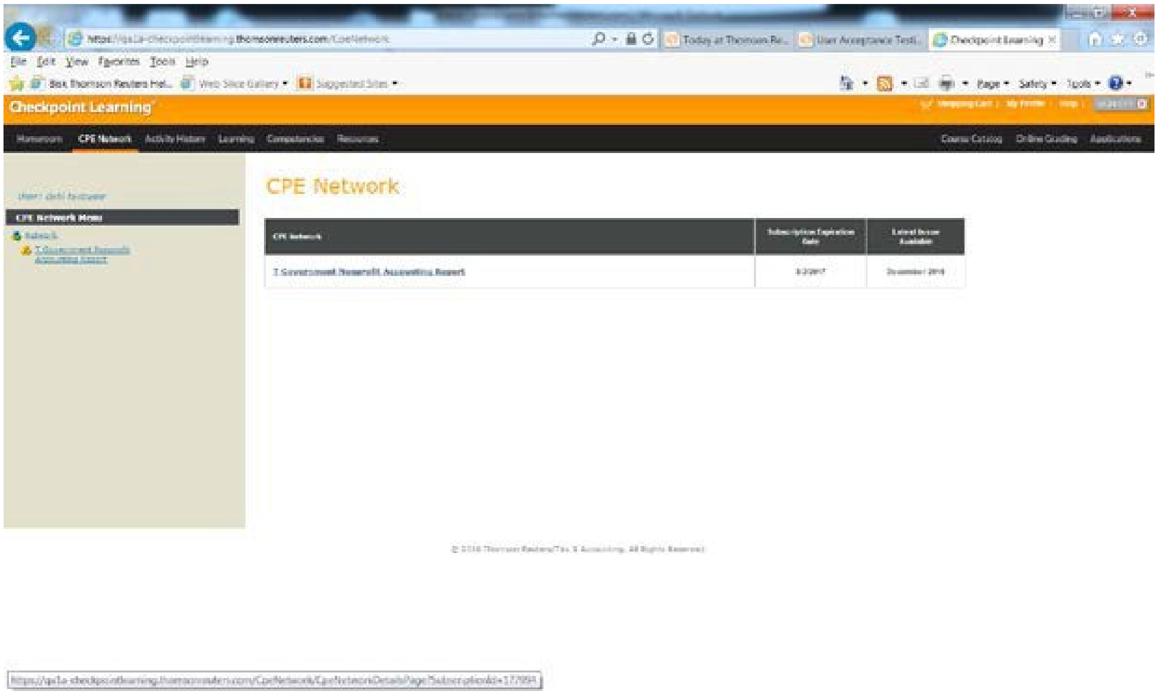
Self-Study—Online

Follow these simple steps to use the online program:

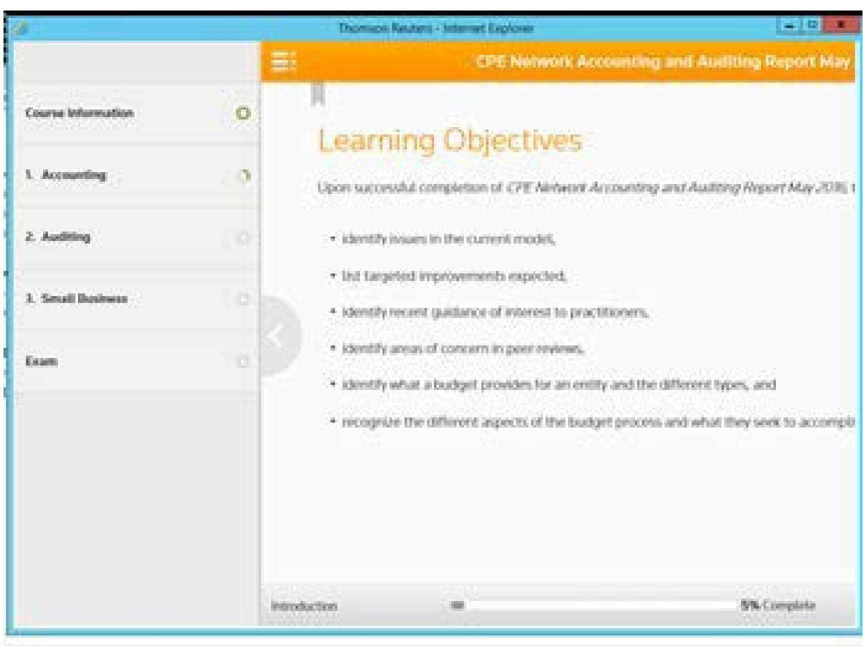
- Go to www.checkpointlearning.thomsonreuters.com .
- Log in using your username and password assigned by your firm's administrator in the upper right-hand margin ("Sign In or Register").



- In the **Network** tab, select the Network Report for the monthdesired.

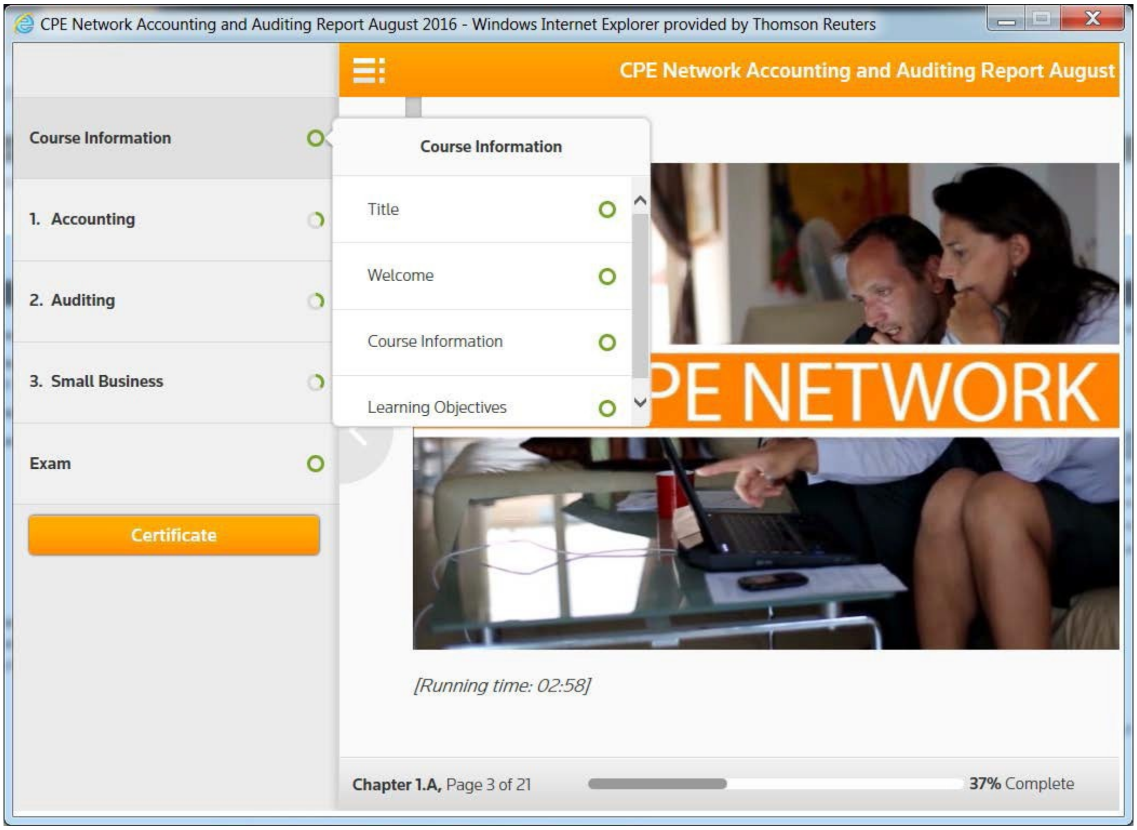


The Chapter Menu is in the gray bar at the left of your screen:

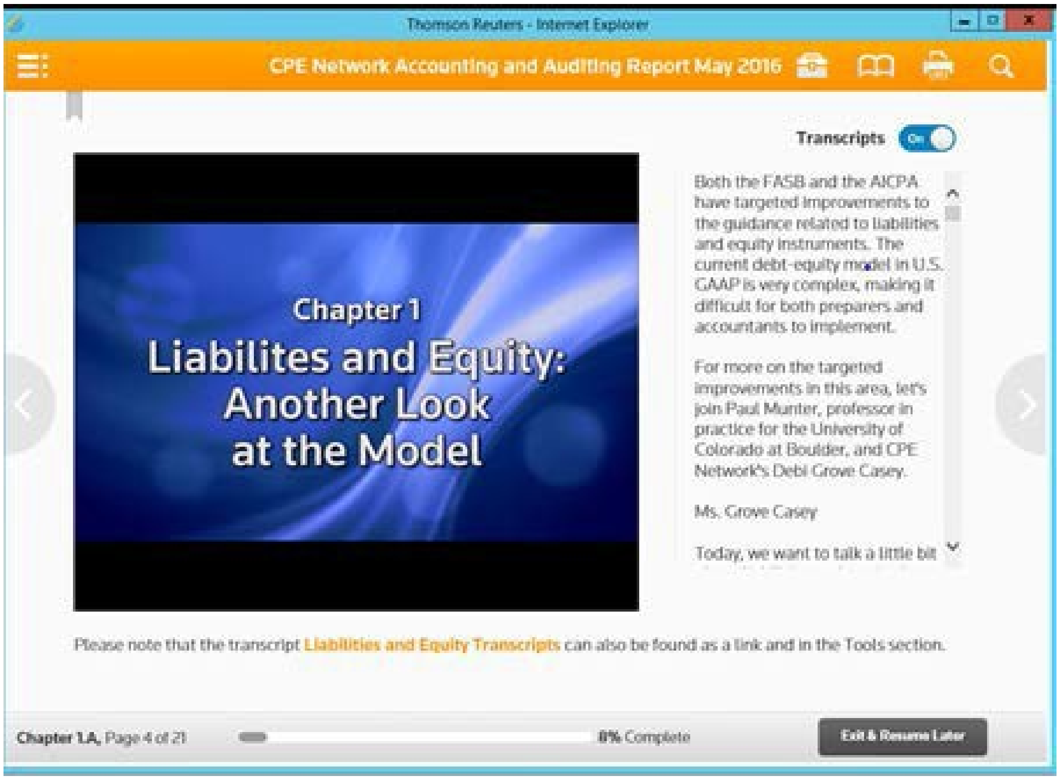


Click down to access the dropdown menu and move between the program Chapters.

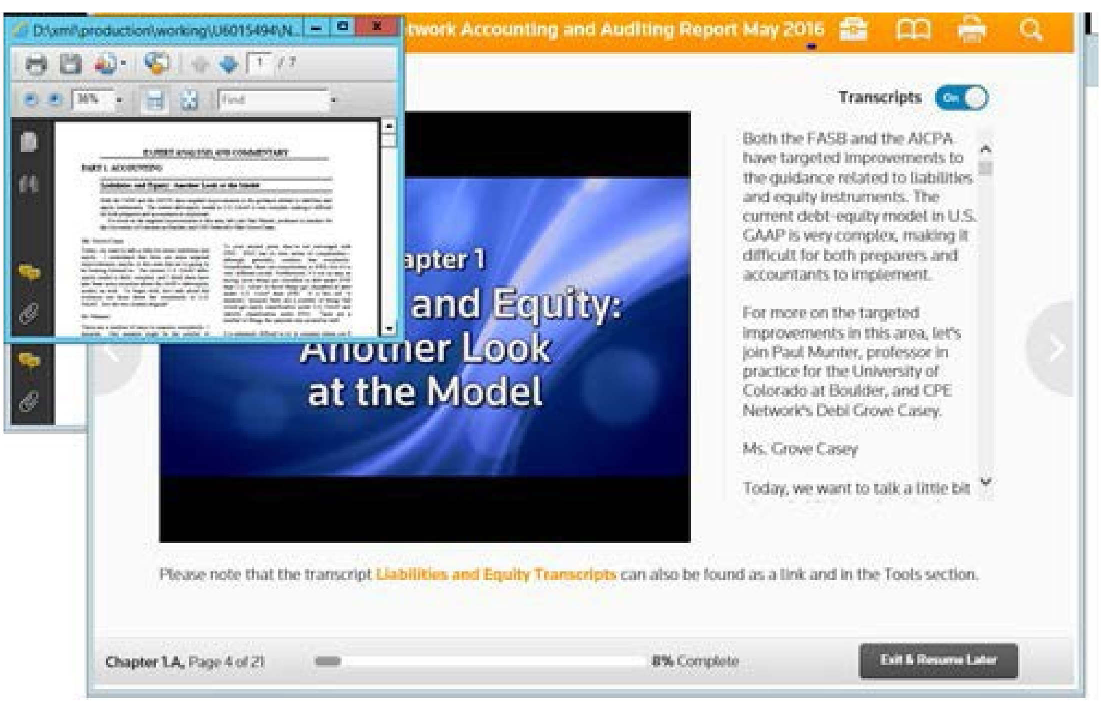
- **Course Information** is the course Overview, including information about the authors and the program learning objectives



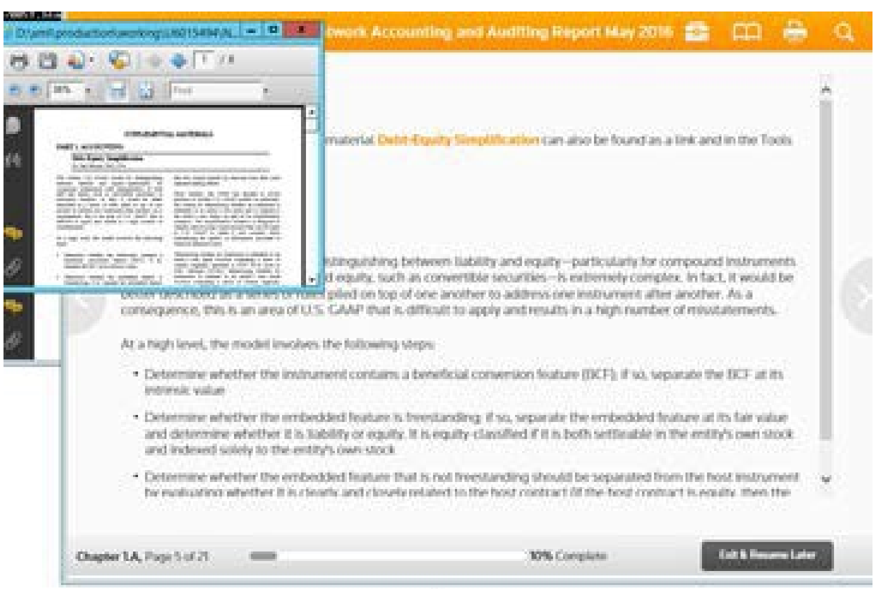
- **Each Chapter is now self-contained.** While on the CPEasy site the interview segments were all together, then all of the supplemental materials, etc., each chapter now contains the executive summary and learning objectives for that segment, followed by the interview, the related supplemental materials and the discussion questions. This more streamlined approach allows administrators and users to more easily access the related materials.



Transcripts for the interview segments can be viewed at the right side of the screen via a toggle button at the top labeled transcripts or via the link to the pdf below the video (also available in the toolbox in the resources section). The pdf will appear in a separate pop-up window.

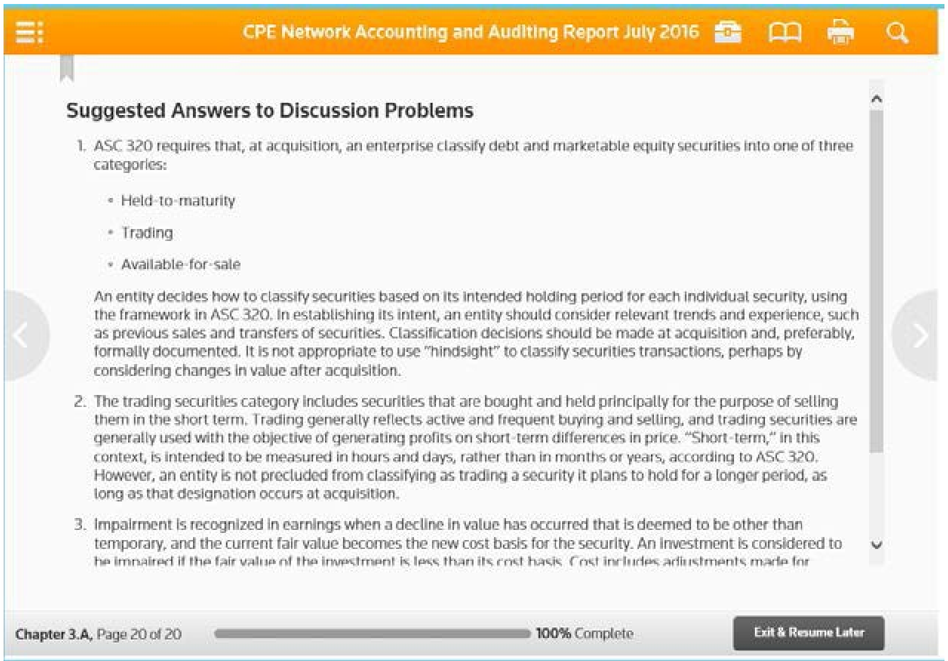


Click the arrow at the bottom of the video to play it, or click the arrow to the right side of the screen to advance to the supplemental material. As with the transcripts, the supplemental materials are also available via the toolbox and the link will pop up the pdf version in a separate window.



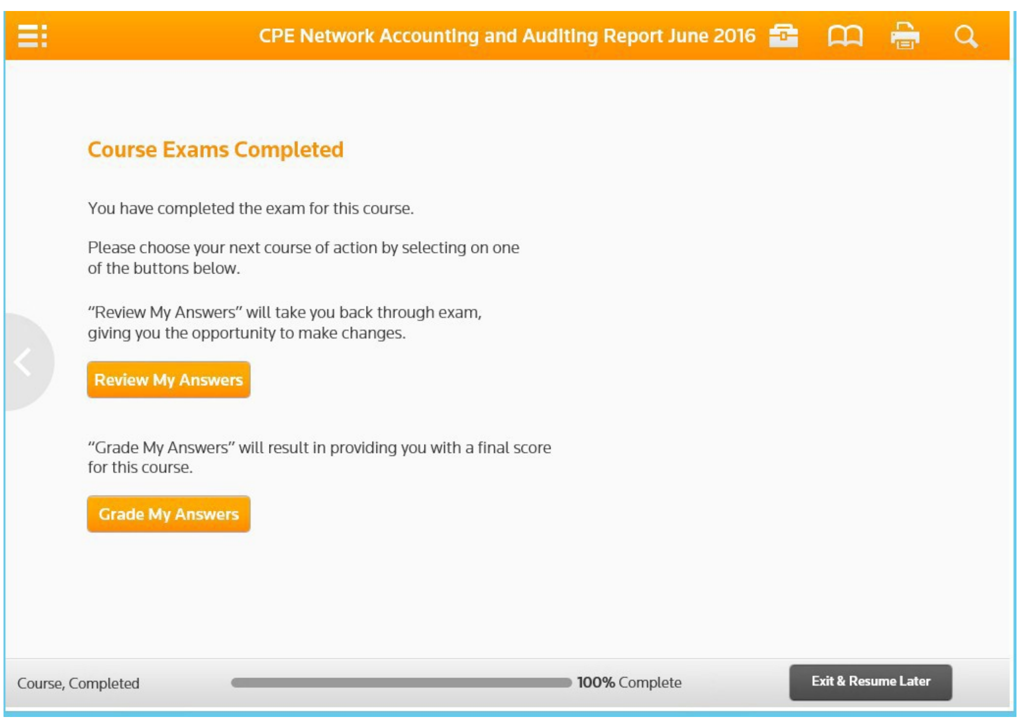
Continuing to click the arrow to the right side of the screen will bring the user to the Discussion p roblems related to the segment.

The Suggested Answers to the Discussion Problems follow the Discussion Problems.



The **Exam** is accessed by clicking the last gray bar on the menu at the left of the screen or clicking through to it. Click the orange button to begin.

When you have completed the quizzer, click the button labeled **Grade or the Review button**.



- Click the button labeled **Certificate** to print your CPEcertificate.
- The final quizzer grade is displayed and you may view the graded answers by clicking the button labeled **view graded answer**.

Additional Features Search

Checkpoint Learning offers powerful search options. Click the **magnifying glass** at the upper right of the screen to begin your search. Enter your choice in the **Search For:** box.

Search Results are displayed with the number of hits.

Print

To display the print menu, click the printer icon in the upper bar of your screen. You can print the entire course, the transcript, the glossary, all resources, or selected portions of the course. Click your choice and click the orange **Print**.

GETTING HELP

Should you need support or assistance with your account, please see below:

Support Group	**Phone Number**	**Email Address**	**Typical Issues/Questions**
Technical Support	800.431.9025 (follow option prompts	checkpointlearning.techsupport@ thomsonreuters.com	• Browser-based • Certificate discrepancies • Accessing courses • Migration questions • Feed issues
Product Support	800.431.9025 (follow option prompts	checkpointlearning.productsupport@ thomsonreuters.com	• Functionality (how to use, where to find) • Content questions • Login Assistance
Customer Support	800.431.9025 (follow option prompts	checkpointlearning.cpecustomerservicet@ thomsonreuters.com	• Billing • Existing orders • Cancellations • Webinars • Certificates

Checkpoint Learning Network: CPE Compliance

Checkpoint Learning Network courses can be group live, group internet based, or self-study. Unless otherwise stated in each course's descriptive information, no other prerequisites or advanced preparation are required.

Checkpoint Learning Network is registered with the National Association of State Boards of Accountancy (NASBA) as a sponsor of continuing education on the National Registry of CPE Sponsors. State boards of accountancy have final authority on the acceptance of individual courses for CPE credit. Complaints regarding registered sponsors may be submitted to the National Registry of CPE Sponsors through its website: www.nasbaregistry.org.

Checkpoint Learning Network is approved for Group Live, Group Internet Based, and QAS Self Study delivery methods.

Checkpoint Learning Network is an approved IRS Continuing Education Provider to deliver CPE to Enrolled Agents and IRS tax preparers. The IRS Tax Preparer Office requires that any course to be used for IRS PTIN holders must be pre-registered with the IRS. If you are a PTIN holder and are interested in obtaining IRS CE credit, be sure to review the course details in Checkpoint Learning to determine if the course you are considering is accredited to IRS.

What Does It Mean To Be a CPE Sponsor?

Your organization is the CPE Sponsor for this monthly series. The sponsor highlights below reflect those of NASBA, the national body that sets guidance for development, presentation, and documentation for CPE programs. **For any specific questions about state sponsor requirements, please contact your state board. They are the final authority regarding CPE Sponsor requirements.** Generally, the following responsibilities are required of the sponsor:

- Arrange for a location for the presentation
- Advertise the course to your anticipated participants and disclose significant features of the program in advance
- Set the start time
- Establish participant sign-in procedures
- Coordinate audio-visual requirements with the facilitator
- Arrange appropriate breaks
- Have a real-time instructor during program presentation
- Ensure that the instructor delivers and documents elements of engagement
- Monitor attendance of the participants (make notations of late arrivals, early departures, and "no shows")
- Solicit course evaluations from participants
- Award CPE credit
- Retain records for five years

The following information includes instructions and generic forms to assist you in fulfilling your responsibilities as program sponsor.

CPE Sponsor Requirements

Determining CPE Credit Increments

Sponsored seminars are measured by program length, with one 50-minute period equal to one CPE credit. One-half CPE credit increments (equal to 25 minutes) are permitted after the first credit has been earned. Sponsors must monitor the program length and the participants' attendance in order to award the appropriate number of CPE credits.

Program Presentation

CPE program sponsors must provide descriptive materials that enable CPAs to assess the appropriateness of learning activities. CPE program sponsors must make the following information available in advance:

- Learning objectives.
- Instructional deliverymethods.
- Recommended CPE credit and recommended field of study.
- Prerequisites.
- Program level.
- Advance preparation.
- Program description.
- Course registration and, where applicable, attendance requirements.
- Refund policy for courses sold for a fee/cancellation policy.
- Complaint resolutionpolicy.
- Official NASBA sponsor statement, if an approved NASBA sponsor (explaining final authority of acceptance of CPEcredits**).**

Disclose Significant Features of Program in Advance

For potential participants to effectively plan their CPE, the program sponsor must disclose the significant features of the program in advance (e.g., through the use of brochures, website, electronic notices, invitations, direct mail, or other announcements). When CPE programs are offered in conjunction with non-educational activities, or when several CPE programs are offered concurrently, participants must receive an appropriate schedule of events indicating those components that are recommended for CPE credit. The CPE program sponsor's registration and attendance policies and procedures must be formalized, published, and made available to participants and include refund/cancellation policies as well as complaint resolution policies.

Monitor Attendance

While it is the participant's responsibility to report the appropriate number of credits earned, CPE program sponsors must maintain a process to monitor individual attendance at group programs to assign the correct number of CPE credits. A participant's self-certification of attendance alone is not sufficient. The sign-in sheet should list the names of each instructor and her/his credentials, as well as the name of each participant attending the seminar. The participant is expected to initial the sheet for their morning attendance and provide their signature for their afternoon attendance. If a participant leaves early, the hours they attended should be documented on the sign-in sheet and on the participant's CPE certificate.

Real Time Instructor During Program Presentation

Group live programs must have a qualified, real time instructor while the program is being presented. Program participants must be able to interact with the real time instructor while the course is in progress (including the opportunity to ask questions and receive answers during the presentation).

Elements of Engagement

A group live program must include at least one element of engagement related to course content during each credit of CPE (for example, group discussion, polling questions, instructor-posed question with time for participant reflection, or use of a case study with different engagement elements throughout the program).

Awarding CPE Certificates

The CPE certificate is the participant's record of attendance and is awarded at the conclusion of the seminar. It should reflect the credit hours earned by the individual, with special calculation of credits for those who arrived late or left early. Attached is a sample *Certificate of Attendance* you may use for your convenience.

CFP credit is available if the firm registers with the CFP board as a sponsor and meets the CFP board requirements. IRS credit is available only if the firm registers with the IRS as a sponsor and satisfies their requirements.

Seminar Quality Evaluations for Firm Sponsor

NASBA requires the seminar to include a means for evaluating quality. At the seminar conclusion, evaluations should be solicited from participants and retained by the sponsor for five years. The following statements are required on the evaluation and are used to determine whether:

1. Stated learning objectives weremet.
2. Prerequisite requirements were appropriate.
3. Program materials wereaccurate.
4. Program materials were relevant and contributed to the achievement of the learning objectives.
5. Time allotted to the learning activity was appropriate.
6. Individual instructors wereeffective.
7. Facilities and/or technological equipment were appropriate.
8. Handout or advance preparation materials were satisfactory.
9. Audio and video materials were effective.

You may use the enclosed preprinted evaluation forms for your convenience.

Retention of Records

The seminar sponsor is required to retain the following information for a period of five years from the date the program is completed unless state law dictates otherwise:

- Record of participation (the original sign-in sheets, now in an editable, electronic signable format)
- Copy of the program materials
- Timed agenda with topics covered and elements of engagement used
- Date and location of course presentation
- Number of CPE credits and field of study breakdown earned by participants
- Instructor name(s) and credentials
- Results of program evaluations

(SAMPLE) Certificate of Attendance (SAMPLE)

This Certifies That:

Participant's Name

Attended:

Course Title

Field(s) of Study and Breakdown

Total CPE Credits

Completion Date

Location (City, State)

Instructor Name(s)

Sponsored By:

Sponsor's Name

Sponsor's Mailing Address

Sponsor's Identification Number

Sponsor's Signature

Sponsor's Signature

In accordance with the standards of the National Registry of CPE Sponsors, CPE credits have been granted based on a 50-minute hour. (Use this Statement if the Sponsor is Registered with NASBA.)