

# **Recent Developments in Federal Income Taxation**

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Bruce A. McGovern

Professor of Law and Director, Tax Clinic  
South Texas College of Law Houston  
Houston, Texas

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State Bar of Texas Tax Section  
First Wednesday Tax Update  
June 3, 2020

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To obtain today's outline and slides:

<https://tinyurl.com/outline0620>

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CLE Number for Today's Webcast:

174086586

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**Costs of Entertainment**  
**2017 TCJA § 13304**  
***Outline: item D.1, page 2***

- TCJA § 13304 amends Code § 274(a) to disallow business deductions for:
  1. Costs “[w]ith respect to an activity which is of a type generally considered to constitute entertainment, amusement, or recreation.”
  2. Membership dues with respect to any club organized for business, pleasure, recreation or other social purposes.
- Applies to taxable years beginning after 2017.
- Notice 2018-76, 2018-42 I.R.B. 599 (10/3/18).
  - Treasury and IRS will issue proposed regulations.
  - Meals are still deductible (subject to 50% limit) if, among other requirements, taxpayer (or employee) is present and meal is provided to current or potential business customer, client, consultant, or similar business contact.

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**Notice 2018-76**  
**2018-42 I.R.B. 599 (10/3/18)**  
***Outline: item D.1.a, page 3***

- Taxpayers may deduct 50 percent of an otherwise allowable business meal expense if:
  1. The expense is an ordinary and necessary expense under § 162(a) paid or incurred during the taxable year in carrying on any trade or business;
  2. The expense is not lavish or extravagant under the circumstances;
  3. The taxpayer, or an employee of the taxpayer, is present at the furnishing of the food or beverages;
  4. The food and beverages are provided to a current or potential business customer, client, consultant, or similar business contact; and
  5. In the case of food and beverages provided during or at an entertainment activity, the food and beverages are purchased separately from the entertainment, or the cost of the food and beverages is stated separately from the cost of the entertainment on one or more bills, invoices, or receipts. The entertainment disallowance rule may not be circumvented through inflating the amount charged for food and beverages.

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**Notice 2018-76**  
**2018-42 I.R.B. 599 (10/3/18)**  
***Outline: item D.1.a, page 32***

■ **Example 1.**

1. Taxpayer A invites B, a business contact, to a baseball game. A purchases tickets for A and B to attend the game. While at the game, A buys hot dogs and drinks for A and B.
2. The baseball game is entertainment as defined in § 1.274-2(b)(1)(i) and, thus, the cost of the game tickets is an entertainment expense and is not deductible by A. The cost of the hot dogs and drinks, which are purchased separately from the game tickets, is not an entertainment expense and is not subject to the § 274(a)(1) disallowance. Therefore, A may deduct 50 percent of the expenses associated with the hot dogs and drinks purchased at the game.

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**Notice 2018-76**  
**2018-42 I.R.B. 599 (10/3/18)**  
***Outline: item D.1.a, page 3***

■ **Example 2.**

1. Taxpayer C invites D, a business contact, to a basketball game. C purchases tickets for C and D to attend the game in a suite, where they have access to food and beverages. The cost of the basketball game tickets, as stated on the invoice, includes the food and beverages.
2. The basketball game is entertainment as defined in § 1.274-2(b)(1)(i) and, thus, the cost of the game tickets is an entertainment expense and is not deductible by C. The cost of the food and beverages, which are not purchased separately from the game tickets, is not stated separately on the invoice. Thus, the cost of the food and beverages also is an entertainment expense that is subject to the § 274(a)(1) disallowance. Therefore, C may not deduct any of the expenses associated with the basketball game.

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**Notice 2018-76**  
**2018-42 I.R.B. 599 (10/3/18)**  
***Outline: item D.1.a, page 3***

■ **Example 3.**

1. Assume the same facts as in Example 2, except that the invoice for the basketball game tickets separately states the cost of the food and beverages.
2. As in Example 2, the basketball game is entertainment as defined in § 1.274-2(b)(1)(i) and, thus, the cost of the game tickets, other than the cost of the food and beverages, is an entertainment expense and is not deductible by C. However, the cost of the food and beverages, which is stated separately on the invoice for the game tickets, is not an entertainment expense and is not subject to the § 274(a)(1) disallowance. Therefore, C may deduct 50 percent of the expenses associated with the food and beverages provided at the game.

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**Proposed Regulations**  
**85 F.R. 11020 (2/26/20)**  
***Outline: item D.1.b, page 4***

■ **Provide guidance on:**

- Entertainment expenses and reiterate that separately-stated, separately-charged food or beverage expenses are not considered entertainment expenses
- Business meal expenses (consistent with Notice 2018-76)
- Other matters, such as travel meal expenses, meals provided at employer-operated eating facilities, and exceptions to the normal 50 percent limitation, such as food or beverages treated as employee comopsnsation.

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## **Families First Coronavirus Response Act Refundable Tax Credits for Paid Sick and Family Leave Wages**

### ***Outline: item F.1, page 5***

- Signed into law on March 18, 2020, the credits offset the cost of paid sick and family leave provided to employees for COVID-19 related leave.
  - Eligible Employer: Less than 500 employees
    - Small businesses with less than 50 employees may qualify for exemption
  - Employee must meet one of 6 specific circumstances to qualify.
  - Paid Sick Leave Credit
  - Paid Family Leave Credit
  - Mechanism:
    - Eligible employers may retain (e.g., not remit) an amount of employment taxes equal to the amount of qualified sick leave wages and qualified family leave wages paid during that quarter (plus certain related health plan expenses and the employer's share of the Medicare taxes on the qualified leave wages)
    - Employers (but not self-employed) can seek advance payment of any credit not recovered through retaining employment taxes by filing Form 7200.

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## **Conard v. Commissioner 154 T.C. No. 6 (3/10/20)**

### ***Outline: item B.1, page 8***

- The taxpayer received nine distributions totaling \$61,777 from her qualified retirement plan in 2008.
  - She was not yet age 59-½ nor eligible for any other exceptions to the § 72(t) 10% penalty on premature distributions.
  - The taxpayer reported the distributions as income but did not report or pay the additional 10% penalty of \$6,177.
  - She attached a statement to her return taking the position that the additional tax was arbitrary and capricious.
- Issue: does the exception to the 10% penalty for distributions made to those at least age 59-½ violate “the [Due Process Clause of the 5th Amendment’s] guarantee of equal treatment under the law.”
- Held: No. The statute affects economic rights and, under the rational basis test, must be sustained if the legislature could have reasonably concluded that the challenged classification would promote a legitimate state purpose.

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**Proposed Regulations on Built-In Gains and Losses**  
**85 F.R. 2061 (1/14/20)**

***Outline: item B.1, page 10***

- Generally, § 382 limits an acquiring corporation's ability to use an acquired corporation's pre-acquisition net operating losses.
  - Section 382 limits the ability of a "loss corporation" to offset its taxable income in periods subsequent to an "ownership change" with losses attributable to periods prior to that ownership change.
  - A loss corporation's built-in gains and built-in losses affect its § 382 limitation.
- Proposed regulations issued in September 2019:
  - Address the items of income and deduction that are included in the calculation of built-in gains and losses under § 382 and reflect changes made by the 2017 Tax Cuts and Jobs Act.
  - Would withdraw Notice 2003-65 and would be effective for ownership changes occurring after the date on which final regulations are published.
- Revised effective date: *subject to two exceptions*, rules would apply to any ownership change occurring after the date that is *30 days after the date* on which on which final regulations are published in the Federal Register. <sup>11</sup>

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**User Fees for Offers in Compromise**

**T.D. 9894, 85 F.R. 14567 (3/13/20)**

***Outline: item F.1.a, page 12***

- Prior to these regulations, the general user fee for processing an offer in compromise was \$186. No fee was charged for:
  - An offer in compromise based solely on doubt as to liability, or
  - A taxpayer who is a low-income taxpayer (defined as a taxpayer who has income at or below 250 percent of the federal poverty guidelines).
- Proposed regulations issued in October 2016:
  - Would have increased the general user fee to \$300 (a 60% increase).
  - Did not change the fee waiver for offers based solely on doubt as to liability or for low-income taxpayers.
- 2019 amendment of § 7122(c)(3):
  - Codified the fee waiver for low-income taxpayers
- Final regulations issued March 2020:
  - Increase the general user fee to \$205 (a 10% increase)
  - Provide a fee waiver for offers based solely on doubt as to liability and for low-income taxpayers.

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**Arlin Geophysical v. United States,**  
**946 F.3d 1234 (10th Cir. 1/14/20)**  
***Outline: item F.2, page 12***

- The Tenth Circuit held that state rights of redemption for foreclosed property do not apply when a federal district court orders foreclosure on property on which the IRS has a valid tax lien.

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**Lander v. Commissioner**  
**154 T.C. No. 11 (3/12/20)**  
***Outline: item F.3, page 13***

- The IRS mailed a notice of deficiency to the taxpayers, a married couple (one copy to their home and one to the federal prison where the husband was incarcerated)
  - The taxpayers never received them.
  - When they received a notice and demand for payment, they requested reconsideration of their liability by the Examination Division and then had a conference with IRS Appeals, which abated their liability to some extent.
- Section 6330(c)(2)(B): a taxpayer can challenge the existence or amount of the taxpayer's underlying tax liability in a CDP hearing only "if the person did not receive any statutory notice of deficiency for such tax liability or did not otherwise have an opportunity to dispute such tax liability."
- Issue: does section 6330(c)(2)(B) bar the taxpayers from challenging their tax liability in the CDP hearing?
- Held: Yes. The conference with IRS Appeals was a prior opportunity to contest their liability.

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**In re Shek,  
947 F.3d 770 (11th Cir. 1/23/20)  
Outline: item H.1.f, page 17**

- Issue: if an individual taxpayer files his or her federal tax return late, can the tax debt ever be discharged in bankruptcy?
- One-day late approach: interprets section 523(a) of the Bankruptcy Code to mean that, if a return is filed even a day late, the tax debt can never be discharged in bankruptcy.
  - *In re McCoy*, 666 F.3d 924 (5th Cir. 2012) (late-filed Mississippi state tax return); *In re Mallo*, 774 F.3d 1313 (10th Cir. 12/29/14) (late-filed federal income tax return); *In re Fahey*, 779 F.3d 1 (1st Cir. 2/18/15) (late-filed Massachusetts state tax return).
- Multi-factor “Beard” test: applied to determine whether taxpayer’s late return qualifies as a “return” w/o addressing merits of one-day late rule:
  - *Justice v. United States*, 817 F.3d 738 (11th Cir. 3/30/16); *In re Smith*, 828 F.3d 1094 (9th Cir. 7/13/16); *Giacchi v. United States*, 856 F.3d 244 (3d Cir. 5/5/17).
- Rejection of the one-day late approach: *In re Shek*, 947 F.3d 770 (11<sup>th</sup> Cir. 1/23/20) (holding tax liability reflected on late-filed Massachusetts state tax return was discharged).

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**E-Filing of Amended Individual Returns  
IR-2020-107 (5/28/20)  
Outline: item H.2, page 17**

- Individuals who wish to amend a federal income tax return by filing Form 1040-X currently must mail the form to the IRS.
- IRS announcement: beginning sometime during the summer of 2020, individuals will be able to e-file Form 1040-X using available software products to amend Forms 1040 or 1040-SR.
  - Taxpayers still will have the option to mail a paper version of Form 1040-X.
  - Only 2019 returns can be amended through e-filing.
  - Whether the ability to e-file amended returns will be expanded to other years is not entirely clear.
    - The announcement states that “[a]dditional enhancements are planned for the future.”

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