Recent Developments in Federal Income Taxation

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Rev. Proc. 2024-25
2024-22 I.R.B. 1333 (5/9/24)
Outline: item A.1, page 2

Health Savings Account Limitations				
Category	**Self-Only Coverage**		**Family Coverage**	
	2024	**2025**	**2024**	**2025**
Limit on Deds. for Contribs. to HSAs	$4,150	$4,300	$8,300	$8,550
High-Deductible Health Plan				
• Min. Deductible	$1,600	$1,650	$3,200	$3,300
• Limit on Out-of-Pocket Exps.	$8,050	$8,300	$16,100	$16,600

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Berman v. Commissioner
163 T.C. No. 1 (7/16/24)
Outline: item B.1, page 3

- The taxpayers in these two consolidated cases each owned one-half of the stock of a C corporation.
- In 2002, they sold some stock to an Employee Stock Ownership Plan (ESOP) established by the corporation and each realized approximately $4 million of gain.
- Taxpayers received installment promissory notes from the ESOP for their stock.
- Using borrowed funds, in 2003 the taxpayers purchased qualified replacement property and elected to defer gain from the stock sale to the ESOP under § 1042(a).
- In 2003, they sold the qualified replacement property (QRP) in a disguised sale.
- Also in 2003, they each received $450,000 from the ESOP under the notes.
- Section 1042(e) provides that, if a taxpayer sells QRP, then
  - "notwithstanding any other provision of this title, gain (if any) shall be recognized to the extent of the gain which was not recognized under [§ 1042(a)] by reason of the acquisition by such taxpayer of such qualified replacement property."
- Issue: did § 1042(e) require the taxpayers to recognize in 2003 the full $8 million of gain deferred under § 1042(a) because they disposed of the QRP?
- Held: No. Taxpayers used the installment method for the 2002 sale of stock to the ESOP and received no payments. They recognized no 2002 gain on the sale

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Corporate Changes in Inflation Reduction Act
August 16, 2022
Outline: item B.1, page 7

- The Inflation Reduction Act, § 138102, adds new Code section 4501
- Imposes excise tax of 1% on the value of any stock that is repurchased by a publicly traded corporation
  - Only repurchases that are treated as redemptions are subject to the tax. Repurchases that are treated as dividends are not.
- Certain exceptions apply, including:
  - Repurchases that are part of a tax-free reorganization, or
  - Repurchases in which total value of stock repurchased does not exceed $1 million
  - Repurchases in which stock repurchased is contributed to employer-sponsored retirement plan, stock ownership plan, or similar plan
- Applies to stock repurchased after December 31, 2022
- New guidance: Notice 2023-2 (12/27/22) – provides interim guidance on the 1% excise tax. See item a, page 7.

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Corporate Changes in Inflation Reduction Act
August 16, 2022
Outline: item B.1.b, page 8

- Proposed and Final Regulations (4/12/24 and 7/3/24):
- Final regulations:
  - Address reporting and payment obligations for the excise tax
    1. The excise tax must be reported on IRS Form 720, Quarterly Federal Excise Tax Return,
    2. Taxpayers must attach an additional form to the Form 720 reflecting the computation of the stock repurchase excise tax
    3. The excise tax must be reported once per taxable year on the Form 720 that is due for the first full quarter after the close of the taxpayer's taxable year
    4. Deadline for payment of the stock repurchase excise tax is the same as the filing deadline
    5. No extensions are permitted for reporting or paying the stock repurchase excise tax.
- Proposed regulations:
  - Address computational matters concerning the excise tax, such as types of transactions subject to the tax and stock issuances that reduce the amount otherwise subject to the § 4501 tax (the "netting rule").

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Maggard v. Commissioner, T.C. Memo. 2024-77 (8/7/24)

Outline: item D.1, page 9

- Taxpayer owned all the stock of an S corporation that operated an engineering business and transferred 60% of the stock to two other individuals.
- The two individuals effectively looted the corporation and made disproportionate distributions to themselves.
- They cut the taxpayer off from the corporation and failed to provide him with Schedules K-1.
  - When the taxpayer requested information to prepare his 2014 to 2016 tax returns, he received a cocktail napkin with a single figure, $300,000 for 2014 and $50,000 for 2015, which allegedly was his share of losses.
- The S corporation later issued Schedules K-1 showing income for each year.
- Issue: did the corporation's S election terminate because it had more than one class of stock by virtue of the disproportionate distributions?
- Held: No. Under relevant regulations, whether shares of stock provide for identical distribution rights is determined under the governing documents.
  - The fact that disproportionate distributions are actually made does not change this result. See Rev. Proc. 2022-19, § 3.02.

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Farhy v. Commissioner, 160 T.C. No. 6 (4/3/23)

Outline: item A.1, page 10

- Section 6038(a) requires every United States person to provide information with respect to any foreign business entity the person controls
  - Form 5471, Information Return of U.S. Persons With Respect to Certain Foreign Corporations.
- Section 6038(b)(1) imposes a penalty of $10,000 for each annual accounting period for which a person fails to provide the required information.
  - In addition, § 6038(b)(2) imposes a continuation penalty of $10,000 for each 30-day period that the failure continues up to a maximum continuation penalty of $50,000 per annual accounting period.
- Issue: can the IRS levy to collect the penalties imposed by § 6038(b)?
- Held: No. There is no statutory authority for the IRS to assess theses penalties. Because they cannot be assessed, the IRS cannot exercise its administrative collection powers to collect them.

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Mukhi v. Commissioner, 162 T.C. No. 8 (4/8/24)

Outline: item A.1.a, page 11

- Section 6038(a) requires every United States person to provide information with respect to any foreign business entity the person controls
  - Form 5471, Information Return of U.S. Persons With Respect to Certain Foreign Corporations.
- Section 6048(a) and (b) require information reporting by a United States person regarding ownership of or transfers to a foreign trust.
  - Form 3520, Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts.
  - Form 3520-A, Annual Information Return of Foreign Trust With a U.S. Owner
- Significant penalties apply for failure to file Forms 5471, 3520, and 3520-A.
- Issues:
  1. Can the IRS levy to collect the penalties imposed by § 6038?
  2. Do fines for failure to file Forms 3520 & 3520-A violate the 8th Amendment?
- Held: (1) No, under prior decision in *Farhy*, and (2) No. The penalties are not "fines" and cannot violate the Excessive Fines Clause of the 8th Amendment; even if they are fines, they are not disproportionate and are constitutional.

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Farhy v. Commissioner, 100 F.4th 223 (D.C. Cir. 5/3/24)

Outline: item A.1.b, page 12

- Section 6038(a) requires every United States person to provide information with respect to any foreign business entity the person controls
  - Form 5471, Information Return of U.S. Persons With Respect to Certain Foreign Corporations.
- Section 6038(b)(1) imposes a penalty of $10,000 for each annual accounting period for which a person fails to provide the required information.
  - In addition, § 6038(b)(2) imposes a continuation penalty of $10,000 for each 30-day period that the failure continues up to a maximum continuation penalty of $50,000 per annual accounting period.
- Issue: can the IRS levy to collect the penalties imposed by § 6038(b)?
- Held: Yes. There is statutory authority for the IRS to assess theses penalties. Because they cant be assessed, the IRS can exercise its administrative collection powers to collect them.
- **Note:** case reverses the U.S. Tax Court on this issue.

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LaRosa v. Commissioner
163 T.C. No. 2 (7/17/24)
Outline: item G.1, page 14

- The IRS issued a refund of allegedly overpaid interest to the taxpayers, a married couple, of about $1.5 million.
  - The IRS later determined that that the refund was erroneous because of a clerical error in computing interest.
- The Department of Justice (DOJ) brought an action in federal district court under § 7405(b) to recover the erroneously refunded interest.
  - DOJ successfully obtained a judgment and lien and sought to foreclose on the taxpayers' real property.
- Mrs. LaRosa filed an administrative claim for innocent spouse relief under §6015(f) (equitable relief) and obtained a stay of proceedings in District Court.
  - The IRS denied her claim for innocent spouse relief. She filed a petition in the U.S. Tax Court.
- Issue: is innocent spouse relief available under § 6015(f) for a liability arising from the IRS's erroneous refund of interest?
- Held: No. Section 6015(f) provides relief from any "unpaid tax or deficiency." The IRS had not asserted a deficiency, and an erroneous refund of interest does not create an "unpaid tax." The refund was a "nonrebate" refund.

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