Recent Developments in Federal Income Taxation

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II. Business Income and Deductions

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Actavis Laboratories, FL, Inc. v. United States, ___ F.4th ___ (Fed. Cir. 8/19/22)

Outline: item B.1.a, page 3

- The taxpayer was a manufacturer of brand-name and generic drugs.
- The taxpayer sought FDA approval of generic drugs by submitting Abbreviated New Drug Applications (ANDAs).
- As required by statute (Hatch-Waxman Act) and the FDA's approval process, the taxpayer:
  - Certified to the FDA that existing patents on the drugs were invalid or would not be infringed by the sale or use of the generic version of the drug, and
  - Sent notice letters to the holders of the patents informing them of the certification.
- Issue: were legal fees incurred to defend patent infringement suits brought in response to the notice letters capital expenditures?
- Held: No. The legal fees were not costs incurred as part of the FDA approval process and therefore were not costs incurred to facilitate the acquisition of an intangible asset (an FDA-approved ANDA).

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Avery v. Commissioner, 134 A.F.T.R.2d 2024-6331 (10th Cir. 12/9/24)

Outline: item D.1, page 5

- Facts
  - The taxpayer, an attorney licensed in Colorado, moved to Indiana and made efforts to establish a practice there.
  - To meet potential clients, he became involved in car-related activities, first by exhibiting collector cars and later by racing cars.
  - He attended a racing school, acquired and rebuilt a 2000 Dodge Viper, and later acquired a 2009 Dodge Viper that he raced in seven states.
  - The taxpayer's name appeared on small areas above the driver's window and the passenger window of his racing vehicle and a decal for his law practice, the Avery Law Firm, appeared on the back tail of the car.
- Issue: could the taxpayer deduct his car-related expenses as advertising expenses that were ordinary and necessary business expenses under § 162?
- Held: No.
  - In determining whether a cost is a deductible business expense, the issue is the taxpayer's primary motive in incurring the expense and whether there is a reasonably proximate relationship to the taxpayer's business. Here, the taxpayer's primary motive was personal.

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Rev. Proc. 2025-16 2025-11 I.R.B. 1100 (2/12/25)

Outline: item E.1, page 6

Section 280F depreciation limits for passenger automobiles	
2025 Passenger Automobiles with § 168(k) first year recovery:	
1st Tax Year	$20,200
2nd Tax Year	$19,600
3rd Tax Year	$11,800
Each Succeeding Year	$7,060
2024 Passenger Automobiles (no § 168(k) first year recovery):	
1st Tax Year	$12,200
2nd Tax Year	$19,600
3rd Tax Year	$11,800
Each Succeeding Year	$7,060

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V. Personal Income and Deductions

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Notice 2024-71
2024-44 I.R.B. 1026 (10/17/24)
Outline: item D.1, page 7

- A taxpayer can use a health flexible spending arrangement (health FSA), Archer medical savings account (Archer MSA), health reimbursement arrangement (HRA), or health savings account (HSA), to pay for expenses that qualify as amounts paid for "medical care" within the meaning of § 213(d).
- Issue: are amounts paid for male condoms amounts paid for "medical care" within the meaning of § 213(d)?
- Conclusion: Yes.
  - Code § 213(d): "medical care" expenses are "amounts paid for the diagnosis, cure, mitigation, treatment, or prevention of disease, or for the purpose of affecting any structure or function of the body."
  - Reg. § 1.213-1(e)(1)(ii): deductions for medical care expenses under § 213 are limited to expenses "incurred primarily for the prevention or alleviation of a physical or mental defect or illness" and do not include deductions for expenses that are merely beneficial to an individual's general health.
  - Although amounts paid for male condoms might or might not be considered paid for "medical care," the Notice creates a "safe harbor" under which such amounts will be treated as paid for medical care.

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X. Tax Procedure

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United States v. Page, 116 F.4th 822 (9th Cir. 9/12/24)

Outline: item E.1, page 8

- Facts
  - The IRS issued to the taxpayer a refund check in the amount of $491,104, but the refund should have been only $3,463.
  - After the government demanded the return of the erroneous refund, the taxpayer returned $210,000 but kept the remaining $277,641.
  - Under § 7405(d) and § 6532(b), a suit to recover an erroneous refund is allowed if it is "begun within 2 years after the making of such refund."
  - May 5, 2017: refund check mailed
  - Unknown date: refund check received by taxpayer
  - April 5, 2018: refund check cashed
  - March 31, 2020: government brought legal action
- Issue: was the government's action to recover the refund timely filed?
- Held: Yes. District Court's grant of summary judgment to taxpayer reversed.
  - The Ninth Circuit joined the First and Seventh Circuits in holding that a refund is "made" for purposes of § 7405(d) and § 6532(b) on the date the check clears the Federal Reserve.

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Ryckman v. Commissioner, 163 T.C. No. 3 (8/1/24)

Outline: item F.1, page 9

- Facts
  - The taxpayer resided in Arizona.
  - In 2017, pursuant to article 26A(2) of the U.S.-Canada tax treaty, the Canada Revenue Agency requested assistance in collecting approximately $200,000 in Canadian tax owed by the taxpayer for 1994 and 1995.
  - The U.S. Competent Authority, an office within the IRS, granted the request.
  - An IRS revenue officer mailed a notice of federal tax lien to Maricopa County.
  - The Revenue Officer also sent the taxpayer a letter stating that a hearing under Code § 6320(b), commonly known as a collection due process (CDP) hearing, was "NOT available to you as a Canadian taxpayer in the United States."
  - Taxpayer requested a CDP hearing on Form 12153, which was denied
- Issue: was taxpayer entitled to a CDP hearing to challenge lien?
- Held: No. Reviewed decision (7-1-6).
  - Under the terms of the treaty, the U.S. must treat the revenue claim as a U.S. tax assessment for which the taxpayer's administrative and judicial rights to restrain collection, including the right to a CDP hearing, have been exhausted.

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United States v. Hughes 113 F.4th 1158 (9th Cir. 8/21/24)

Outline: item H.1.a, page 12

- The taxpayer, a U.S. citizen, owned wine businesses in New Zealand through a wholly-owned LLC.
- She had control over the business's bank accounts in New Zealand.
- Taxpayer failed to file Foreign Bank Account Reports (FBARs) for 2010-2013.
- On her 2010-2011 returns, she did not indicate that she had foreign bank accounts, but she indicated she did have such accounts on 2012-2013 returns.
- The penalties for failure to file an FBAR are:
  - Non-willful violation: $10,000
  - Willful violation: greater of $100,000 or 50% of undisclosed account value.
- Issue: Can recklessness be sufficient to establish a willful violation of FBAR reporting requirements (in this case, for 2012-2013)?
- Held: Yes. Joins all other Circuits that have considered the issue.
  - The government can establish a willful FBAR violation by proving that the defendant (1) clearly ought to have known that (2) there was a grave risk that an accurate FBAR was not being filed and that (3) he was in a position to find out for certain very easily.

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XI. Withholding and Excise Taxes

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Texas Truck Parts & Tire, Inc. v. United States
118 F.4th 687 (5th Cir. 10/8/24)
Outline: item C.1, page 13

- The taxpayer, a wholesaler and retailer of truck parts and tires based in Houston, purchased tires from Chinese manufacturers from 2012 to 2017.
- The Chinese manufacturers arranged for the tires to be transported from China to the United States, clear U.S. Customs, and be delivered to taxpayer.
- Code § 4071(a) imposes an excise tax "on taxable tires sold by the manufacturer, producer, or importer thereof."
- The taxpayer neither filed quarterly excise tax returns on Form 720 nor paid any excise tax on the tires.
- Issue: was taxpayer the importer of the tires within the meaning of § 4071?
- Held: Yes.
  - Under Reg. § 48.0-2(a)(4)(i), an importer is "any person who brings such an article into the United States from a source outside the United States" or the beneficial owner "if the nominal importer of a taxable article is not its beneficial owner."
  - Taxpayer did not bring the tires into the U.S., but it is the beneficial owner.
  - Agrees with *Terry Haggerty Tire Co., Inc. v. United States*, 899 F.2d 1199 (Fed. Cir. 1990).

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