Daily Tax Report™

No. 144

Wednesday, July 27, 2011

Page G-7

ISSN 1522-8800

Federal Tax & Accounting

Tax Regulations

For 2011-12 Plan, Attorneys Seek Guidance On Exempts, Partnerships, LLCs, Real Estate

Guidance on exempt organizations, partnerships and limited liability companies, and real estate topped tax attorneys' wish list for projects from the Internal Revenue Service for the 2011-12 plan year.

Committees of the American Bar Association Section of Taxation asked for 15 projects in the exempt organizations area, 12 in the partnership arena, and 11 in the real estate area.

Other areas of high interest were estate and gift taxes, civil and criminal tax penalties, and U.S. activities of foreigners and tax treaties—all at eight projects.

“A lot of these are carryforwards, because frankly the IRS didn't get much out last year,” Steven Schneider, chairman of the tax section’s Partnerships and LLCs Committee, said July 26. Schneider is an attorney with Goulston & Storrs.

The tax section's exempt organizations list suggests an urgent need for guidance on tax code Section 501(c)(4) tax code Section 501(c)(4) political activity, with four projects related to that topic.

On partnerships and LLCs, guidance allowing securities partnerships that use an aggregation method for financial assets to treat basis adjustment under other sections as separate assets and recover them under a reasonable method—rather than allocating the basis adjustments to particular partnership assets—were among the priorities.

“A lot of folks are having trouble doing the calculations because the rules are too narrow,” Schneider said. “So there's a big push for that in the industry.”

Real estate practitioners are looking for final rules under Section 460 on home construction contract exemptions, and guidance under Section 108(c), with particular focus on the definition of “secured by real property.”

Multiple Section 501(c)(4) Political Activity Projects

Several projects on the exempt organizations committee list reflect the January 2010 *Citizens United v. Federal Election Commission* Supreme Court decision that significantly expanded the right of corporations and labor unions to make political expenditures (20 DTR K-1, 2/2/10 ).

“Citizens United has changed the use of 501(c)(4)s so much,” Suzanne Ross McDowell, exempt organizations committee chairman and partner at Steptoe & Johnson, told BNA July 26. “Money poured into them during the mid-term elections in volumes we haven't seen before,” she said. The 501(c)(4) area is one in which the committee has been seeking guidance for some time, she said.

Two projects on that list would expand previous requests for guidance.

One asks for guidance on the measurement and extent of political campaign activity that is allowable by social welfare organizations, trade associations, and exempts other than charities so that they can state with assurance that their non-political activities are their primary activities and not run afoul of IRS rules.

A related issue is a request for guidance on the applicability of the estate and gift taxes to bequests and inter vivos gifts to Section 501(c)(4) organizations, including a review and updating of Revenue Ruling 82-216. That guidance states that gratuitous transfers to people other than Section 527(e) organizations are subject to gift tax, unless there is a specific law to the contrary, “even though the transfers may be motivated by a desire to advance the donors’ own social, political, or charitable goals.”

“I guess we got our wish on that one, or at least the IRS has said they are studying it,” McDowell said, referring to the IRS's recent announcement that it backed off five ongoing gift tax audits involving Section 501(c)(4) organizations.

IRS has said, however, that it will be reviewing Revenue Ruling 82-216. “It's conceivable they could conclude the gift tax does not apply to 501(c)(4)s, but the way the code is written it would appear to apply because there is no exception for a gift to a 501(c)(4),” she said.

Other exempt projects on the wish list include guidance on what constitutes nondeductible political campaign activity under Sections 162(e) and 6033(e), consistent with interpretations of the legislative lobbying limit and candidate electioneering prohibition under Section 501(c)(3).

McDowell said practitioners also would like to see guidance to update the public support test and simplify the procedures for foreign equivalency determinations, and guidance on the deductibility of gifts made to a disregarded entity under Section 170 when the sole owner is a Section 501(c)(3) charity.

Partnerships

Schneider said several of the projects listed in his area need attention now. They include guidance on the application of Revenue Ruling 99-6 to nonrecognition transactions and situations where the terminating partnership has liabilities, Section 751 property, or Section 704(c) property.

The IRS has been promising for months to repropose regulations on partnership options, he said, but since they have not appeared yet, that was also included on the list.

Guidance is needed on partial interest transfers. Rev. Rul. 84-53 and the income tax regulations under Section 704 need to be clarified to address situations in which transferred interest and the retained interest are not identical, he said.

Finally, Schneider said his area has been waiting since 2005 for IRS to issue guidance on changes to Section 734, 743, and 755 under the American Jobs Creation Act of 2004. Questions involve built-in losses and how to deal with them.

“In 2004, people had built-in gains, but now they have built-in losses,” he said. “It's important to get those out sooner rather than later.”

Eliot Kaplan, chairman of the real estate committee and partner with Squire Sanders, said some of his group's priorities are revisions to Treasury regulations addressing distressed debt acquisitions and modifications, and issues arising under guidance relating to stock dividends by REITs, as well as guidance regarding the determination of a partner's insolvency and the application of Rev. Rul. 92-53 for discharged nonrecourse debt of a partnership.

The Real Estate Committee also is looking for revisions to the “fractions rule.”

Kaplan said the purpose of the rule is to prevent tax avoidance by limiting the permanent or temporary transfer of tax benefits from tax-exempt partners to taxable partners, whether by directing income or gain to tax-exempt partners, by directing losses, deductions, or credits to taxable partners, or by some other similar manner. “Although we fully support the anti-avoidance purpose of the fractions rule, we believe that the rule itself, as implemented under the applicable regulations, adopts an approach that is dramatically overbroad as compared to what is necessary to prevent the stated tax avoidance.”

In 2010, his committee submitted comments detailing a number of problems presented by the fractions rule in the context of common business arrangements undertaken by investment funds generally, and the committee said the fractions rule can be simplified.

U.S. activities of foreigners, along with tax treaties, also commanded significant attention, with guidance requested under Sections 1471 through 1474 on the definition of “primary and substantial” in the definition of foreign financial institution, and possible exceptions to FFI and identification of additional entities that could be deemed compliant.

*By **Diane Freda***

Text of the ABA tax section letter  is in TaxCore.