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Tax News and Industry Updates

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Reliance on CPA Avoids Penalty

Cross References

• *Okonkwo,* T.C. Memo. 2015-181, September 14, 2015

In 1997, the taxpayers constructed a single-family house in an attempt to sell it for a profit. In 2002, they ceased their sales efforts and rented it out for $6,000 per month to an unrelated tenant. From 2007 through March 2010, the taxpayer's daughter resided in the house and paid rent of $2,000 per month. During this time, the taxpayers resumed their efforts to sell the house. They reported rental income and deductions on their Schedule E indicating that the house was rental real estate. They characterized their net loss as passive.

For 2009 and 2010, they hired a CPA who had real estate investment experience to prepare their tax returns. The CPA noticed and asked the taxpayers about the significant decrease in their rental income. The taxpayers informed him that the decrease was attributable to their previous tenant's moving out of, and their daughter's moving into the house.

The CPA prepared the 2009 and 2010 tax return reporting rental income and deductions on Schedule C, *Profit or Loss From Business,* rather than Schedule E, *Supplemental Income and Loss,* listing the activity as a real estate developer. Each year reported a net loss from the activity. The CPA also advised that the 2008 return be amended to report the loss on Schedule C rather than Schedule E. The IRS audited the returns and disallowed the losses.

The Tax Court agreed with the IRS. The taxpayer's daughter's use of the house was personal and was attributed to the taxpayers. Because their daughter did not pay fair rental, they do not qualify for an exception to this rule. Thus, rental deductions are limited to the extent of rental income. The Tax Court rejected the taxpayer's argument that they were real estate developers and that they rented the house to their daughter because their homeowners policy required that the house be occupied. The taxpayers were subject to tax on the excess deductions that they had claimed.

The IRS also tried to impose the accuracy-related penalty for negligence relating to the portions of underpayments attributable to IRC section 280A limitations. The Tax Court said the taxpayers, in good faith, relied on their CPA's judgement that expenses relating to the house were fully deductible. Accordingly, the taxpayers were not liable for the accuracy-related penalty for that portion of the underpayment.

IRS Releases New Proposed Regulations for Same-Sex Marriages

Cross References

• REG-148998-13, October 23, 2015

The IRS has released new proposed regulations providing that a marriage of two individuals, whether of the same sex or the opposite sex, will be recognized for federal tax purposes if that marriage is recognized by any state, possession, or territory of the United States. The proposed regulations also interpret the terms "husband" and "wife" to include same-sex spouses as well as opposite-sex spouses. These regulations implement the decision in *Obergefell v. Hodges,* U.S. Supreme Court, June 26, 2015.

"The proposed regulations confirm that terms in the federal tax code relating to marriage should be interpreted to include same-sex spouses as well as opposite-sex spouses, ensuring that all are treated equally under the law," said Treasury Secretary Lew. "These regulations provide additional clarity on how the federal government will treat same-sex couples for tax purposes in light of the Supreme Court's historic decision on same-sex marriage."

The proposed regulations clarify and strengthen guidance provided in Revenue Ruling 2013-17 implementing the Supreme Court's decision in *Windsor,* U.S. Supreme Court, June 26, 2013. That revenue ruling stated that same-sex couples legally married in jurisdictions that authorize same-sex marriage will be treated as married for federal tax purposes. The proposed regulations update these rules to reflect that same-sex couples can now marry in all states and that all states will recognize these marriages.

The proposed regulations apply to all federal tax provisions where marriage is a factor, including filing status, claiming personal and dependency exemptions, taking the standard deduction, employee benefits, contributing to an IRA, and claiming the Earned Income Credit or Child Tax Credit.

The proposed regulations do not treat registered domestic partnerships, civil unions, or similar relationships not denominated as marriage under state law as marriage for federal tax purposes. This rule protects individuals who have specifically chosen to enter into a state law registered domestic partnership, civil union, or similar relationship rather than a marriage, because they can retain their status as single for federal tax purposes.

Since publication of Revenue Ruling 2013-17, legally married couples generally must file their federal income tax return using either the "married filing jointly" or "married filing separately" filing status.

New W-2 Verification Code

Cross References

• www.irs.gov

For filing season 2016, the Internal Revenue Service will test a capability to verify the authenticity of Form W-2 data. This test is one in a series of steps to combat tax-related identity theft and refund fraud.

The objective is to verify Form W-2 data submitted by taxpayers on e-filed individual tax returns. The IRS has partnered with certain Payroll Service Providers (PSPs) to include a 16-digit code and a new Verification Code field on a limited number of Form W-2 copies provided to employees.

The code will be displayed in four groups of four alphanumeric characters, separated by hyphens. *Example:* XXXX-XXXX-XXXX-XXXX.

The Verification Code will appear on some versions of payroll firms' Form W-2 copies B and C, in a separate, labeled box (Copy B is "To be filed with employee's federal tax return" and Copy C is "For employee's records.")

The form will include these instructions to taxpayer and tax preparers:

> *Verification Code. If this field is populated, enter this code when it is requested by your tax return preparation software. It is possible your software or preparer will not request the code. The code is not entered on paper-filed returns.*

Some W-2s that employees receive will have a "Verification Code" box which is blank. These taxpayers do not need to enter any code data into their tax software product.

For the purposes of the test, omitted and incorrect W-2 Verification Codes will not delay the processing of a tax return. The IRS will analyze this pilot data in a "test-and-learn" review to see if it is useful in evaluating the integrity of W-2 information.

The code will not be included in Forms W-2 or W-2 data submitted by the PSPs to the Social Security Administration or any state or local departments of revenue. Nor will this pilot affect state and local income tax returns or paper federal returns.

Standard Mileage Rate

Cross References

- Rev. Proc. 2010-51
- Notice 2016-1

The IRS has released the 2016 standard mileage rates for taxpayers to use in computing the deductible costs of operating an automobile for business, charitable, medical, or moving expense purposes. The following chart reflects the new 2016 standard mileage rates compared to the 2015 and 2014 tax year standard mileage rates.

	2016	2015	2014
Business rate per mile	54.0¢	57.5¢	56.0¢
Medical and moving rate per mile	19.0¢	23.0¢	23.5¢
Charitable rate per mile	14.0¢	14.0¢	14.0¢
Depreciation rate per mile	24.0¢	24.0¢	22.0¢

Form 1095 Due Dates Extended

Cross References

- Notice 2016-4

Under the Patient Protection and Affordable Care Act (ACA), health insurance issuers, self-insuring employers, government agencies, and other providers of minimum essential coverage are required to furnish Form 1095-B, *Health Coverage,* to individuals receiving the health insurance coverage by February 1, 2016, for the 2015 coverage period. Form 1095-B is then used by the individual to prove which months during 2015 he or she received minimum essential coverage, as well as all other covered individuals under the same policy.

Likewise, applicable large employers (generally those with 50 or more full-time employees) are required to furnish Form 1095-C, *Employer-Provided Health Insurance Offer and Coverage,* to their employees by February 1, 2016, for the 2015 coverage period. Form 1095-C is then used by the employee to prove which months during 2015 he or she received minimum essential coverage from the employer. The form also provides the employee information on which months the employer offered coverage and whether or not that coverage was affordable. The employee in turn does not qualify for the premium tax credit for any month the employer offered affordable coverage, even if the employee refuses employer coverage and purchases health insurance through the Marketplace.

Both Form 1095-B and Form 1095-C provide essential information needed to prepare a correct individual tax return for 2015. For example, Form 1095-B can be used to prove the taxpayer is not subject to the Shared Responsibility Payment. Likewise, Form 1095-C can be used to determine which months an employee does not qualify for the Premium Tax Credit because of being offered affordable coverage from the employer.

The IRS recently determined that some employers, insurers, and other providers of minimum essential coverage need additional time to adapt and implement systems and procedures to gather, analyze, and report information required to be reported on these forms. Therefore, the IRS has extended the due dates for furnishing these forms to recipients from February 1, 2016 to March 31, 2016.

The due date extension does not apply to Form 1095-A, *Health Insurance Marketplace Statement,* which is furnished by the Marketplace to individuals who purchased their health insurance through the Marketplace.

Due date extension does not delay filing Form 1040. The notice specifically tells individuals that they may rely upon other information to file their tax returns before receiving Form 1095-B and/or Form 1095-C, and that they need not amend their returns once they receive their Form 1095-B and/or Form 1095-C (or any corrected Form 1095-B and/or Form 1095-C). The notice makes clear that this provision applies for the 2015 tax year only and not to any future year.