Tax Shorts

April 27, 2023

By: Joseph Dolan, Crystal Edwards, John Elias, Charles Falk, I. Richard Ploss, Philip Siana, Deirdre Wheatley-Liss

Tax shorts is a variety of short unrelated tax topics. In this edition of the *Porzio Tax Letter*, the following is discussed:

I. Spotlight on Tax Returns

II. Developments Affecting S Corporations

III. Athletes, Residency, and Taxes-What Motivates Them

IV. Monetized Installment Sales

V. State Wealth Taxes

VI. The Employee Retention Credit

I. Spotlight on Tax Returns

Tax preparers are currently in the throughs of tax season. Some recent developments:

- **Erroneous 1099 Forms:** Form 1099 informs you and the IRS how much gross income a third-party claims that it paid you. Suppose you receive a form 1099 that you disagree with? You should request a "corrected" form from the issuer. If the issuer will not issue a new form, what do you do? The best strategy is to enclose a statement with you return disclosing that the form 1099 that you received is wrong. Form 8275 can be used for this purpose. It should be noted that erroneous 1099 forms have been common from Crypto exchanges.

- **Does the Filing of a Form 8275 Increase Your Chances of an Audit:** A form 8275, or a form 8275-R, can be used to disclose a position taken on a tax return to avoid the imposition of penalties if the position is subsequently not allowed by the IRS. Form 8275-R is used for positions on a tax return that contradict the law. The IRS provides when a form 8275 should be filed:

Form 8275 is used by taxpayers and tax return preparers to disclose items or positions, except those taken contrary to a regulation, that are not otherwise adequately disclosed on a tax return to avoid certain penalties. The form is filed to avoid the portions of the accuracy-related penalty due to disregard of rules or to a substantial understatement of income tax for non-tax shelter items if the return position has a reasonable basis.

Generally, filing a form 8275 will not increase a Taxpayer's chance of an audit. It is a very good way to avoid the imposition of penalties.

- **Faxed Partnership Return was not "Filed":** The Ninth Circuit Court of Appeals recently held in *Seaview Trading LLC v. CIR* that a tax return faxed to an IRS agent who was auditing a partnership was not "filed" for purposes of the Statute of Limitations. Generally, the IRS specifies where a tax return should be filed. Often, an IRS auditor will request that a delinquent return be filed with the auditor. Based on *Seaview*, a prudent taxpayer should file a delinquent return with the IRS Service Center even if a request is made by an IRS agent for the delinquent return. A return should be sent to the Service Center and the Agent.

II. Developments Affecting S Corporations

There are two recent developments regarding "S" corporations, one at the federal level, and one affecting New Jersey S corporations:

- **Simplified Procedure for Correcting S Errors:** The IRS recently issued Revenue Procedure 2022-19 that permits corrections to invalid S elections without requiring the S corporation obtaining a private letter ruling, which can be time-consuming and expensive. Certain requirements must be met to utilize the Revenue Procedure, but they are not burdensome.

- **New Jersey Follows Federal S Elections:** On December 22, 2022, Governor Murphy signed legislation that allows a New Jersey corporation to be treated as an "S" corporation for New Jersey purposes if the corporation made a valid federal S Election. If a corporation makes a valid S election for federal purposes, and does not want to be an S corporation for New Jersey purposes, it must affirmatively elect-out as a New Jersey S corporation.

III. Athletes, Residency, and Taxes-What Motivates Them

We often read about athletes signing big contracts. Rarely do we consider how taxes impact where an athlete signs. When Tyreek Hill signed a four-year, $120 million contract with the Miami Dolphins, he confirmed that state income taxes played a role in his decision of where to play. Hill considered playing for the New York Jets, which would have made him subject to New Jersey income taxes (the New York Jets have no connection to New York). Florida has no state income tax. Hill stated, "those state taxes, man. I had to make a grown-up decision." It is projected that had Hill signed with the Jets, he would have paid more than $3 million in New Jersey income taxes. He pays no state income tax in Florida. Former New York Islanders head coach, Barry Trotz, moved to Tennessee after being fired. Trotz had one year remaining on his contract that he had signed and would be paid for. By moving to a no-income-tax-state, Tennessee, from a high-income-tax-state, New York, Trotz saved more than $300,000 in state income taxes. Trotz admitted his move from New York to Tennessee was solely due to state income taxes.

IV. Monetized Installment Sales

Monetized installment sales made the IRS equivalent of the FBI's Most Wanted for the second year in a row. The IRS version of the FBI"s most wanted is the "Dirty Dozen" tax scams. The IRS has warned Taxpayers and their advisors about using a Monetized Installment Sale strategy to receive the proceeds from a sale and defer the income taxes:

These transactions involve the inappropriate use of the installment sale rules under section 453 by a seller who, in the year of a sale of property, effectively receives the sales proceeds through purported loans. In a typical transaction, the seller enters into a contract to sell appreciated property to a buyer for cash and then purports to sell the same property to an intermediary in return for an installment note. The intermediary then purports to sell the property to the buyer and receives the cash purchase price. Through a series of related steps, the seller receives an amount equivalent to the sales price, less various transactional fees, in the form of a purported loan that is nonrecourse and unsecured. Taxpayers who have engaged in any of these transactions or who are contemplating engaging in them should carefully review the underlying legal requirements and consult independent, competent advisors before claiming any purported tax benefits. **Taxpayers who have already claimed the purported tax benefits of one of these…transactions on a tax return should consider taking corrective steps, such as filing an amended return…**

The principle of "if its too good to be true it usually is," applies in this case. If a Taxpayer remains committed to using the Monetized Installment Sale strategy, the Taxpayer should file a form 8275 (see discussion above) to try to mitigate any penalties if the IRS challenges the transaction, or make some other disclosure on the return.

V. The Employee Retention Credit

You can hardly go through a day without hearing several radio and television commercials touting the benefits of applying for the Employee Retention Credit ("ERC"). The commercials make it sound like a no-brainer. An Employer puts no money down, applies for the ERC, and the Employer may get a check for up to $26,000 per employee, before paying a usual fee of one-third to the enabler. The IRS Office of Professional Responsibility recently warned employers and their advisors of issues when applying for the ERC. While applying for the ERC is a legitimate claim, Taxpayer/Employers need to heed the IRS advice and make sure that the person submitting the claim will be there if (usually "when") the Employer is audited. The advisor needs to do due diligence when applying for the ERC. The IRS Bulletin stated, "While this is a legitimate credit that has provided a financial lifeline to millions of businesses, there continue to be promoters who aggressively mislead people and businesses into thinking they can claim these credits." Further, the IRS alert also warned that employers who receive the ERC do so by filing employment tax returns. If an employer receives an ERC, it restricts the employer's deduction for the wages on the income tax returns that the employer filed. Thus, an amended income tax return may need to be filed. Lastly, a preparer of the ERC claim may not have prepared the income tax return claiming the deduction, and the preparer needs to verify what was reported on the income tax return. It is more efficient for the preparer of the income tax return to also prepare the ERC claim.