

Tax News and Industry Updates

2016
Volume 4, Issue 4



WWW.NANCYOLASKY.COM

OLASKY & ASSOCIATES

15187 UNIVERSITY

ALLEN PARK MI 48101

PH 313.388.8800 FX 313.388.9785



Inside This Issue

New Law to Affect Refunds in 2017.....	1
Compliance Costs of IRS Regulations.....	1
Money Market Fund Gains and Losses.....	2
ITIN Renewals.....	2
Restricted Property.....	3

New Law to Affect Refunds in 2017

Cross References

- www.irs.gov

The IRS has announced initial plans for processing tax returns involving the Earned Income Tax Credit (EITC) and Additional Child Tax Credit (ACTC) during the opening weeks of the 2017 filing season. The IRS is sharing the information now to help the tax community prepare for the 2017 season, and plans are being made for a wider communication effort later in the summer and fall to alert taxpayers about the changes that will affect some early filers.

This action is driven by the Protecting Americans from Tax Hikes Act of 2015 (PATH Act) that was enacted into law on December 18, 2015. Section 201 of this new law mandates that no credit or refund for an overpayment for a taxable year shall be made to a taxpayer before February 15 if the taxpayer claimed the Earned Income Tax Credit or Additional Child Tax Credit on the return.

This change begins January 1, 2017, and may affect some returns filed early in 2017.

- To comply with the law, the IRS will hold the refunds on EITC and ACTC-related 2016 returns until February 15, 2017.
- This allows additional time to help prevent revenue lost due to identity theft and refund fraud related to fabricated wages and withholdings.
- The IRS will hold the entire refund. Under the new law, the IRS cannot release the part of the refund that is not associated with the EITC and ACTC.
- Taxpayers should file as they normally do, and tax return preparers should also submit returns as they normally do.
- The IRS will begin accepting and processing tax returns once the filing season begins, as they do every year.
- The IRS still expects to issue most refunds in less than 21 days, though IRS will hold refunds for EITC and ACTC-related tax returns filed early in 2017 until February 15 and then begin issuing them.



Compliance Costs of IRS Regulations

Cross References

- www.taxfoundation.org

The Tax Foundation recently issued a fiscal fact report on the growing complexity of the U.S. tax code and IRS regulations. The report is based on data from the Office of Information and Regulatory Affairs and the Bureau of Labor Statistics. The report is designed to encourage

Congress to take up the kind of tax reform that will improve economic growth, boost wages, and encourage new investment throughout the economy.

According to the report, over the last century, the federal tax code has expanded dramatically in size and scope. In 1955, the Internal Revenue Code stood at 409,000 words. Since then, it has grown to a total of 2.4 million words. Today there are also some 7.7 million words of tax regulations, promulgated by the IRS which clarifies how the U.S. tax statutes work in practice. There are also some 60,000 pages of tax-related case law.

Tax complexity creates real costs for American households and businesses. According to the latest estimates from the Office of Information and Regulatory Affairs, Americans will spend more than 8.9 billion hours complying with IRS tax filing requirements in 2016. The time it takes to comply with the tax code imposes a real cost on the economy. Individuals and businesses need to devote resources to complying with the tax code instead of doing other productive activities. According to Tax Foundation estimates, 8.9 billion hours equates to \$409 billion each year in lost productivity, or greater than the gross product of 36 states.



Money Market Fund Gains and Losses

Cross References

- Rec. Proc. 2016-39
- T.D. 9774

A money market fund (MMF) is a type of investment fund that historically seeks to keep stable (typically at \$1.00) the prices at which their shares are issued and redeemed (stable-NAV MMF). Some MMFs may have share prices that change frequently, such as a floating-NAV MMF. A floating-NAV MMF uses market factors to value their securities.

MMFs are not the type of investment with which investors expect to realize gains on capital appreciation. Rather, shareholders often use MMFs to temporarily hold money, such as dividend earnings and sale proceeds from transactions involving other types of investments such as mutual funds, stocks, and securities. Because of this type of usage, the IRS has issued guidance to simplify the tax ramifications of money going in and out of MMFs. For example, in 2014 the IRS issued Revenue Procedure 2014-45 which states money going into and out of MMFs is not subject to the Wash Sale rules under IRC section 1091 if the fund is a floating-NAV MMF.

In July 2016, the IRS issued further guidance for MMF gains and losses. Under the net asset value (NAV) method, the net gain or loss is computed based on aggregate transactions and aggregate fair market values during a computation period, rather than on a transaction-by-transaction basis. This rule applies to both stable-NAV MMFs as well as floating-NAV MMFs.

The net gain or loss for each computation period equals the ending value of the MMF, minus the starting basis, minus the net investment in the MMF for the computation period. Computation periods under the final regulations may be of equal or of varying lengths.

For taxpayers changing from a realization accounting method to the NAV method, a simplified filing of Form 3115, *Application for Change in Accounting Method*, requires only limited information. Form 3115 is not needed for shares in a stable-NAV MMF if certain requirements are satisfied. For details, see Revenue Procedure 2016-39.



ITIN Renewals

Cross References

- Notice 2016-48

The IRS issues Individual Taxpayer Identification Numbers (ITINs) to individuals who are required to have a U.S. taxpayer identification number for U.S. tax purposes, but who do not have and are not eligible to obtain a Social Security Number from the Social Security Administration. Under the Protecting Americans from Tax Hikes Act of 2015 (PATH Act), ITINs are now subject to expiration.

ITINs that need to be renewed beginning in 2017.

Prior to the PATH Act, a taxpayer applied for and received an ITIN only once. The ITIN remained in effect unless the taxpayer applied for and received a Social Security Number. Under the PATH Act, certain ITINs will no longer be in effect unless they are renewed.

Any ITIN that is not used on a federal tax return for three consecutive tax years, either as the ITIN of an individual who files the return or as the ITIN of a dependent included on a return, will expire on December 31 of the third consecutive tax year of non-use. This rule applies to all ITINs regardless of when the ITIN was issued.

ITINs issued before 2013. Under the PATH Act, for ITINs issued before 2013, ITINs will no longer be in effect according to the following schedule, unless the ITIN has already expired due to non-use for three consecutive years:

- ITINs issued before 2008 will remain in effect until January 1, 2017.

- ITINs issued in 2008 will remain in effect until January 1, 2018.
- ITINs issued in 2009 or 2010 will remain in effect until January 1, 2019.
- ITINs issued in 2011 or 2012 will remain in effect until January 1, 2020.

How to Renew an ITIN

ITINs that have expired due to non-use may be renewed anytime starting October 1, 2016, by filing a Form W-7 and required documentation. These individuals may renew their ITIN without having to attach a tax return to the Form W-7. Follow the Form W-7 instructions. Alternatively, individuals may choose to wait to submit their Form W-7 when they file their tax return.

ITINs issued before 2013 and currently in use. ITINs issued before 2013 that have been used on a tax return in the last three consecutive years are set to expire based on the schedule listed above. To simplify the renewal process, the IRS will administer the renewal of ITINs on a schedule that is different than the schedule listed above under the PATH Act. The IRS will administer the renewal of ITINs based upon the fourth and fifth digits (middle digits) in the ITIN. ITINs that contain the middle digits of 78 or 79 will no longer be in effect beginning January 1, 2017. The expiration and renewal schedules of ITINs with middle digits other than 78 or 79 will be announced in future guidance.

The IRS will send a Letter 5821 to individuals holding ITINs with the middle digits of 78 or 79 if the ITIN was used for a taxpayer or a dependent on a U.S. income tax return in any of the last three consecutive tax years informing them that they may submit a Form W-7 with original or certified documents to renew their ITINs. Form W-7 with required documentation may be submitted by the taxpayer starting October 1, 2016. Include a copy of Letter 5821 with Form W-7.

ITINs with middle digits other than 78 or 79 that have been in use within the last three consecutive tax years should not be renewed and require no immediate action from the ITIN holder. The IRS will provide information about the expiration schedule and renewal process for the remaining ITINs issued before 2013 in future guidance.

What if an ITIN is not renewed? Returns filed by individuals who have not renewed their ITIN will be accepted by the IRS. However, there may be a delay in processing these returns, and certain credits, such as the Child Tax Credit and the American Opportunity Tax Credit, may not be allowed unless the ITIN is renewed.

Individuals who have become eligible for an SSN.

Individuals with expired ITINs who have become eligible for a Social Security Number should not renew the ITIN. Instead, write a letter to the IRS explaining that they now have an SSN and that they want all their tax records combined under their SSN.

Use of ITIN solely on an information return. An individual whose expired ITIN is used only on information returns filed and furnished by third parties, such as Forms 1099, is not required to renew the ITIN. ITINs may continue to be used for information return purposes regardless of whether they have expired for individual income tax return filing purposes. If the individual is later required to file a tax return, however, the individual's ITIN will have to be renewed at that time. Additionally, the third parties who file and furnish information returns with an expired payee ITIN will not be subject to information return penalties solely because the ITIN is expired.



Restricted Property

Cross References

- IRS Pub 525, *Taxable and Nontaxable Income*
- IRC §83
- Reg. §1.83-2

If a taxpayer receives property in exchange for rendering services, the fair market value of the property is taxable in the year the property is received. If the taxpayer receives stock or other property that has certain restrictions that affect its value, the fair market value of the property is generally not included in income until it has been substantially vested.

Until the property becomes substantially vested, it is owned by the person who transfers the property to the taxpayer who renders the services. However, any income from the property, or the right to use the property, is included in the taxpayer's income as additional compensation in the year the income is received or the year the taxpayer has the right to use the property.

When the property becomes substantially vested, the taxpayer must include its fair market value in income for that year, minus any amount paid for by the taxpayer. The holding period begins when the property becomes substantially vested.

Example #1: Amy works for ABC Corporation. ABC sells Amy 100 shares of its stock at \$10 per share. At the time of the sale, the fair market value of the stock is \$100 per share. Under the terms of the sale, Amy agrees to give up her stock if she quits her job before the 5-year period ends. The stock is

under a substantial risk of forfeiture during that 5-year period. Since Amy is not substantially vested when she purchased the stock, the excess of the fair market value over the price paid is not included in her income. At the end of the 5-year period, Amy still works for ABC. She is no longer under substantial risk of forfeiture. The fair market value of the stock at the end of the 5-year period is \$200 per share. Amy must include \$19,000 in income at the end of the 5-year period $[(\$200 \text{ FMV} - \$10 \text{ purchase price}) \times 100 \text{ shares}]$.

Substantially vested. Property is substantially vested when:

- It is transferable, or
- It is not subject to a substantial risk of forfeiture.

Property is transferable if the taxpayer can sell, assign, or pledge his or her interest in the property to someone else. A substantial risk of forfeiture exists only if rights in property that are transferred are conditioned on the future performance of substantial services, or on the occurrence of a condition related to a purpose of the transfer if the possibility of forfeiture is substantial.

Election under IRC section 83. A taxpayer can choose to include in income the value of restricted property at the time of the transfer (minus any amount paid for the property). If this election is made, the substantial vesting rules do not apply and generally any later appreciation in value is not included in compensation when the property becomes substantially vested. Basis for figuring gain or loss when the property is sold is the amount paid for plus the amount included in income as compensation.

Example #2: Assume the same facts as Example #1, above, except that Amy elects to include the fair market value of the stock in income as compensation in the year the stock is purchased. Amy includes \$9,000 in income in the year of purchase $[(\$100 \text{ FMV} - \$10 \text{ purchase price}) \times 100 \text{ shares}]$. Her basis in the stock is \$10,000 (\$9,000 compensation plus \$1,000 purchase price). Any appreciation in the value of the stock after the purchase is taxable only when Amy sells or exchanges the stock.

The election is made by filing a written statement with the IRS where the taxpayer files his or her return no later than 30 days after the date the property was transferred. Prior to 2016, the written statement must also be attached to the tax return for the year in which the property is transferred.

Final regulations. The IRS recently released final regulations under Regulation section 1.83-2(c) for property transferred after 2015, which removes the requirement to submit a copy of the IRC section 83(b) election with the taxpayer's tax return for the year in which the property was transferred. The final regulations simplify the procedure for electronic filing by not requiring the written statement to be attached to the tax return. The taxpayer must still file a separate written IRC section 83(b) election with the IRS within 30 days after the date the property was transferred.

