IRS Insights | A closer look

Tax Court reiterates rule that each tax year stands on its own

In *Couturier*, the Tax Court recently reiterated the well-established rule that the IRS's failure to audit a tax position is not a concession that the tax position is correct.[1]

Background

Before 2004, taxpayer Clair Couturier had stock in his employer's employee stock ownership plan (ESOP) and interests in several compensatory plans. In 2004, Mr. Couturier's employer bought out his interests. The employer paid Mr. Couturier $26 million: $12 million was paid directly to his IRA and the remaining $14 million was a promissory note payable to his IRA. On his 2004 Form 1040, Mr. Couturier reported the $26 million as a nontaxable distribution that was a direct rollover to an IRA.

During an audit of the employer's ESOP, the IRS determined that the value of Mr. Couturier's stock in the ESOP was only $830,292 and the remaining $25.2 million payment was in exchange for Mr. Couturier's relinquishment of his interest in the compensation plans. Accordingly, the IRS asserted that Mr. Couturier made an excess contribution to his IRA and that he owed section 4973's excise tax for excessive contributions. If the IRS's position was correct, it also meant that Mr. Couturier should have paid income tax on the $25.2 million. However, the IRS never audited Mr. Couturier's 2004 Form 1040 or asserted any income tax deficiency for 2004.

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Taxpayer's position

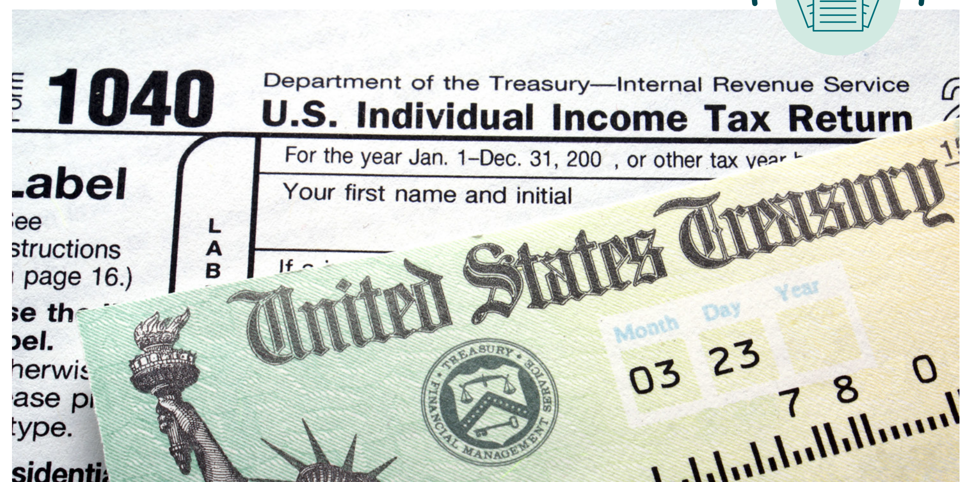
On motion for summary judgment, Mr. Couturier argued that the IRS cannot assert an excise tax liability against him for the $25.2 million IRA contribution because the IRS did not assert the $25.2 million was subject to income tax. The taxpayer argued the IRS could not assert the excise tax position against him because that position was inconsistent with the IRS's position regarding his income tax.

Court's decision

The Tax Court summarily rejected Mr. Couturier's argument. Preliminarily, the court found that nothing in the excise tax statute or regulations "makes the assertion of an income tax deficiency a precondition for determining an excise tax deficiency for the same year."

As for the taxpayer's inconsistency argument, the court concluded the IRS did not take an inconsistent position. The Tax Court stated that the IRS could not have taken an inconsistent position because "the IRS took no position whatever" about Mr. Couturier's 2004 Form 1040. The IRS did not take a position because the IRS did not audit or make any determinations regarding Mr. Couturier's 2004 Form 1040.

The Tax Court rejected Mr. Couturier's argument that the IRS's inaction regarding his 2004 Form 1040 was tantamount to the IRS's approval of the positions taken on the Form 1040. The court said it is "well established" and a "bedrock principle" that the IRS's failure to examine a return (or challenge a position on the return) does not constitute a concession or admission that the position was correct.



The Tax Court contrasted Mr. Couturier's situation with the *Hellweg*[2] case, where the Tax Court barred the IRS from assessing an excise tax because it took an inconsistent position. In Hellweg, the IRS audited the relevant tax returns, made no adjustments, and issued no change letters. The IRS conceded that, for income tax purposes, the transaction should have been given effect. However, the IRS took a contrary position with respect to the excise tax—for excise tax purposes, the IRS argued that the transaction lacked substance. The Tax Court held the IRS was bound by its concession that the transaction was valid for income tax purposes and that the IRS could not take inconsistent positions regarding income and excise tax consequences of the same transaction. Because the IRS did not audit Mr. Couturier's returns, the court ruled that *Hellweg* did not apply.

Conclusion

Based on the above, the Tax Court denied Mr. Couturier's motion for summary judgment, and the IRS is permitted to assert the $25.2 million contribution is subject to the excise tax for excessive contributions, even though the IRS did not assert an income tax deficiency with respect to the $25.2 million.

District court upholds IRS denial of charitable contribution deduction as assignment of income and due to lack of sufficient contemporaneous written acknowledgment

In *Keefer v.* United States,[3] the district court granted partial summary judgment in favor of the government and held the Internal Revenue Service properly denied a charitable deduction stemming from the donation of a 4% limited partnership interest to a private foundation ("Foundation") to establish a donor-advised fund (DAF).

Background

Kevin Keefer indirectly held a limited partnership interest in a limited partnership (LP) that owned and operated a single hotel in Los Angeles, California. In April 2015, LP was approached by a Real Estate Investment Trust (REIT) that expressed interest in acquiring the hotel and exchanged a nonbinding letter of intent (LOI) with LP for the deal. LP did not sign the LOI and continued to search for other interested buyers.

Before finalizing any sale of LP, Mr. Keefer converted a portion of his indirect interest into a direct 4% interest and then donated that interest to the Foundation establishing a DAF. Mr. Keefer executed the documents that had been provided by the Foundation to establish the DAF ("DAF Packet") on June 8, 2015. In connection with the donation, Mr. Keefer commissioned an appraisal of the donated interest in mid-June 2015. While the appraisal described the appraiser's qualifications, it did not include the appraiser's tax identification number. The appraisal concluded that the fair market value of the donated interest was $1.26 million.

On July 2, 2015, REIT and LP signed the sales contract, and the sale of the hotel closed on August 11, 2015.

In early September, the Foundation provided Mr. Keefer with a letter acknowledging the donation (the "Acknowledgment Letter").

Mr. Keefer and his wife timely filed their 2015 federal income tax return claiming a $1.26 million charitable contribution deduction for the donation to the DAF. The Form 8283, *Noncash Charitable Contributions*, filed as part of their 2015 federal income tax return, included the appraiser's tax identification number, a copy of the appraisal, the DAF Packet, and the Acknowledgment Letter.

In the summer of 2019, the IRS denied the charitable deduction and increased the Keefers' 2015 tax liability by $423,304 plus penalties and interest. The IRS asserted that the Keefers did not have a contemporaneous written acknowledgment (CWA) from the donee showing the DAF had "exclusive legal control over the assets contributed" and had failed to include the appraiser's identifying number.

The Keefers paid the additional liability and filed a claim for refund in November 2019, which was denied in March 2020, as untimely. The suit in district court followed.

Court's ruling

Both parties moved for summary judgment, and the court ultimately concluded that (1) the Keefers' refund claim was timely, (2) the Doctrine of Variance did not bar their claims, (3) the donation was an anticipatory assignment of income, (4) the IRS properly denied the charitable deduction because the Keefers' CWA did not meet the requirements of IRC sections 170(f)(8) and (18), and (5) the Keefers were not entitled to a refund of their 2015 taxes. A discussion of only the assignment of income and CWA issues follows below.

Anticipatory assignment of income

The government argued that the donation to the Foundation made just before the sale of the hotel to REIT was to close amounted to an anticipatory assignment of income, which required the Keefers to recognize the income from the sale rather than merely deduct the value of the noncash asset as a charitable contribution.

Recognizing that taxpayers cannot escape tax on earned income by assigning said income to another party, the court noted that "the crucial question is whether the [donated] asset itself, or merely the income

from it, has been transferred." Under the test established in *Humacid Co. v. Commissioner*,[4] "courts will respect the form of a donation of appreciated stock if the donor (1) gives the property away absolutely and parts with title thereto (2) before the property gives rise to income by way of a sale."

The Keefers argued that their donation met both prongs of the Humacid test and claimed that the sale of the hotel to REIT remained uncertain in June when they assigned the 4% partnership interest in LP to the Foundation. The government, however, argued that the hotel sale was "practically certain" at the time of the donation and that "the Keefers carved out and retained a portion of the partnership asset by oral agreement."

The Keefers executed the DAF Packet on June 18, 2015, at which time, the hotel was not yet under contract. The sales contract was signed on July 2, 2015, and even then, REIT has 30 days to review the property and withdraw from the deal. As such, the court found that absent any binding obligation to close, "the deal was not 'practically certain' to go through," and the presence of the pending sale did not render the donation an anticipatory assignment of income.

The court did, however, conclude that the Keefers had carved out a partial interest in the 4% partnership interest when they donated it causing them to fail the first prong of the *Humacid* test. Specifically, there was an oral agreement between Mr. Keefer and the Foundation that the Foundation would receive 4% of the proceeds from the sale of the hotel as opposed to other partnership assets not covered by the sale. The government argued, and the court concurred, that this oral agreement demonstrated that the Keefers "did not donate a true partnership interest." Instead, they effectively donated 4% of the net cash from the sale of one of LP's, which "is the classic assignment of income."

Contemporaneous written acknowledgment

While the court's determination that the transfer to the Foundation was an anticipatory assignment of income and that no deduction would be allowed for the contribution, the court went on to also find that the lack of a CWA that met the requirements of IRC sections 170(f)(8) and (18) would have also been grounds upon which to deny the deduction.

The Keefers argued that, taken together, the Acknowledgement Letter and DAF Packet constituted a statutorily sufficient CWA. On the contrary, the government contended that multiple documents could not be used to piece together a compliant CWA unless the documents included a merger clause. Additionally, neither document offered by the Keefers stated that the Foundation had "exclusive legal control" over the donated assets.

The court agreed with the government and concluded that the CWA was not in compliance with the statutory requirements; moreover, the doctrine of substantial compliance is inapplicable. As such, the IRS properly denied the charitable deduction. The court found that the DAF Packet did not constitute a CWA because it was issued before the donation took place, and with no binding requirement that a donation be made, it didn't serve as an acknowledgment of anything. Moreover, the Acknowledgment Letter could not be used to supplement the DAF Packet as there were no references to the DAF or the DAF Packet. Because IRC section 170(f)(8) requires "strict compliance," and the Acknowledgment Letter, which the court deemed to be the CWA, did not "reference the Keefer DAF or otherwise affirm [the Foundation]'s exclusive legal control, as required by section 170(f)(18)" the CWA did not meet the necessary statutory requirements.

Conclusion

For taxpayers looking to donate to a DAF, attention must be paid to ensure that proper documentation is received from the charitable organization or they risk having the charitable deduction disallowed. While the donee is generally not required to record or report the information provided on the CWA to the IRS, the burden falls on the donor to ensure the CWA they received from the donee meets the strict compliance requirements of sections 170(f)(8) and (18).

Tax Court ruled taxpayer could not challenge NFTL because she already had opportunity to contest liability

In *Hammock v. Commissioner*, the Tax Court issued a bench opinion on a challenge to a notice of federal tax lien finding that a taxpayer could not challenge the underlying penalty because she already had forgone a prior opportunity to contest the liability.

The case arose from a challenge to a notice of federal tax lien and notice of intent to levy issued to the taxpayer, Ms. Hammock. Ms. Hammock inherited the family business after the death of her parents. In addition, at that time, Ms. Hammock also became the treasurer of the company; however, the day-to-day operations were run by a close family friend. In 2015, Ms. Hammock learned that this family friend had been embezzling from the company and the company had not been paying its employment taxes from 2012–2015. Later that same year, the company declared bankruptcy.

In July 2016, a revenue officer sent Ms. Hammock a pair of letters informing her of the IRS's attempt to collect the company's unremitted employment taxes. One of the letters informed Ms. Hammock that the IRS may hold her responsible for some of the company's unpaid employment taxes. The other letter scheduled an in-person meeting with Ms. Hammock to discuss Ms. Hammock's duties and responsibilities as an officer of the company.

Ms. Hammock retained attorneys to represent her; however, her representatives failed to file a valid Form 2848, *Power of Attorney and Declaration of Representative*. On the first Form 2848, essential information about the tax form and period was omitted. Ms. Hammock's attorneys sent in a second

Form 2848 later to correct the issues from the first form. However, the second Form 2848 lacked Ms. Hammock's signature. Due to these mistakes, there was no valid Form 2848 in effect for Ms. Hammock's attorneys. As a result, the IRS did not provide copies of correspondence to Ms. Hammock's attorneys.

After reviewing the available records, the revenue officer determined that Ms. Hammock was among those responsible for the failure to remit the payroll taxes and proposed a trust fund recovery penalty.[5] On February 10, 2017, the revenue officer made the initial determination to assess the trust fund recover penalty, and the group manager approved the determination that same day. On February 15, 2017, the IRS mailed a Letter 1153 directly to Ms. Hammock via certified mail, informing her that the IRS proposed assessing the trust fund recovery penalty under IRC section 6672 against her. The Letter 1153 also notified Ms. Hammock that she had 60 days to appeal the decision before collection action would be initiated.

Ms. Hammock claimed that she did not receive this letter, but the postal tracking information indicated that the letter was delivered to a person at her address. By the time Ms. Hammock's attorneys had filed a valid Form 2848 and submitted a protest on behalf of Ms. Hammock, the 60-day appeal period had expired. As a result, the Revenue Officer rejected as untimely the protest challenging the liability that was filed by the attorneys on behalf of Ms. Hammock. The IRS assessed the tax against Ms. Hammock and then mailed her a notice of federal tax lien and notice of intent to levy. Ms. Hammock requested a collection due process hearing, stating that she disputed both notices as she was not a responsible person for the tax periods at issue. A settlement officer from the IRS Independent Office of Appeals held a CDP proceeding. Ms. Hammock's attorney acknowledged receipt of the Letter 1153 at some point but argued that the Commissioner had violated Ms. Hammock's due process rights by failing to send a copy of the letter to her attorney. The settlement officer verified that the IRS properly mailed a Form 1153 to Ms. Hammock and allowed the allotted time to protest the decision to expire; as a result, the settlement officer determined that Ms. Hammock was precluded from challenging the underlying penalties. Ms. Hammock subsequently filed a petition with the Tax Court.

At trial, Ms. Hammock argued that she did not have a prior opportunity to challenge the underlying liability and that she was not a responsible person for purposes of the trust

fund recovery penalty. The IRS argued that Ms. Hammock is precluded from challenging the underlying liability and that she is liable for the trust fund recovery penalty.

The trust fund recovery penalty is predicated on an employer's duty to withhold its employees share of federal taxes from their wages and remit those taxes to the federal government.[6] These withheld amounts are known as trust fund taxes because the employer holds them in trust for the government.[7] If the employer fails to remit the taxes, the penalty provides a tool to collect the liability from those who may have been responsible to withhold the taxes.[8] The trust fund recovery penalty allows the IRS to impose a trust fund recovery penalty on certain people who willfully fail to withhold, account for, and pay over trust fund taxes. The Internal Revenue Code provides that officers or employees of the corporation who are under a duty to collect, account for, and pay over taxes are considered responsible persons for purposes of the penalty.

In determining the standard of review to apply in this collections case, the Tax Court looked to determine whether the underlying liability was properly at issue. If the underlying liability is not properly at issue, the Tax Court reviews IRS determinations for abuse of discretion.

The question of whether the underlying liability can be contested in a collection proceeding turns on whether the taxpayer received a notice of deficiency or otherwise had a prior opportunity to dispute the liability. In order to determine whether Ms. Hammock had a prior opportunity to contest the penalty, the Tax Court looked to determine whether Ms. Hammock received the Letter 1153. The Tax Court observed that the IRS was able to establish that a Letter 1153 was mailed by certified mail to Ms. Hammock's last known address. If the IRS can prove proper mailing, it is presumed to be delivered to the individual to which it was addressed. The taxpayer bears the burden of rebutting this presumption. The Tax Court found that Ms. Hammock could not rebut this presumption and, as a result, Ms. Hammock could not contest the underlying liability at issue.

Thus, the Tax Court reviewed the notice of determination to determine whether the IRS abused its discretion. The Tax Court thus concluded that the IRS did not abuse its discretion; instead, it found that the IRS followed all of the requirements of applicable law and administrative procedure for collecting a trust fund recovery penalty.

Endnotes

1. *Couturier v. Commissioner*, T.C. Memo 2022-9.
2. *Hellweg v. Commissioner*, T.C. Memo 2011-58.
3. *Keefer v. United States*, No. 3:20-cv-0836, 2022 U.S. Dist. LEXIS 118271 (N.D. Tex. July 6, 2022).
4. 42 T.C. 894 (1964).
5. IRC Section 6672.
6. *Kazmi v. Commissioner*, T.C. Memo 2022-13, at *6.
7. *Id.*
8. IRC Section 6672(a).

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