# Key tax developments during the third quarter of 2016

The following is a summary of important tax developments that have occurred in the past three months that may affect you, your family, your investments, and your livelihood. Please call us for more information about any of these developments and what steps you should implement to take advantage of favorable developments and to minimize the impact of those that are unfavorable.

*Proposed regulations would close family business estate/gift tax loopholes.* In August, the IRS issued new proposed regulations that would close two estate and gift tax loopholes. These complex loopholes treat the lapse of certain rights in a family business as a transfer to family members, and value transfers of an interest in a family business to a family member without considering certain restrictions on that interest. Taxpayers or their estates owning closely held businesses or other entities have used these loopholes to lower the taxable value of their transferred assets and thereby minimize their estate or gift tax burden. There is still time to act, however, as the loopholes will remain open until final regulations are issued.

*Loss deduction OK'd for estate that suffered Ponzi losses through an entity.* The Tax Court has allowed an estate to claim a theft loss deduction for losses incurred by a limited liability company (LLC) in which it held a 99% interest. The LLC's sole asset was an account that, during the settlement of the case, became worthless as a result of Bernie Madoff's Ponzi scheme. The losses were allowed under a tax code provision (Sec. 2054) allowing estates a deduction for casualty losses incurred during the settlement of the estate, including losses arising from fires, storms, shipwrecks or other casualties, or from theft, if the losses are not compensated for by insurance or otherwise.

*Final regulations encourage partial annuity option for pension plan payouts.* Defined benefit (pension) plan participants are often confronted with a "cash or annuity" decision upon retirement. But, many employees may prefer a combination of options, for example, the payment of some benefit as a stream of income for life (to provide protection against the risk of outliving one's savings) and the rest of the benefit as a lump sum (to provide for liquidity). New final regulations allow defined benefit plans to simplify the treatment of certain optional forms of benefit that are paid partly in the form of an annuity and partly in a more accelerated form. The final regulations simplify the calculation of split benefits, making it easier for retirees to choose to receive part of their benefits as a lifetime stream of income.

*New self-certification procedure for those who miss the 60-day rollover deadline.* The IRS has provided a new self-certification procedure designed to help recipients of retirement plan distributions who, due to one or more specified reasons, inadvertently miss the 60-day time limit for properly rolling these amounts into another IRA (or other eligible retirement plan). The new self-certification procedure allows these taxpayers to claim eligibility for a waiver of the 60-day rollover requirement that can be relied upon by a plan administrator or IRA trustee in accepting and reporting receipt of the rollover contribution. The new procedure permits individuals to get rollover relief without having to follow a cumbersome private letter ruling request procedure.

*IRS agrees that residence interest limits are applied separately for unmarried co-owners.* The IRS has announced its acquiescence to a decision of the Court of Appeals for the Ninth Circuit that the limitations on deductions for qualified residence interest ($1 million of acquisition debt and $100,000 of home equity debt) are applied on a per-individual basis, and not a per-residence basis. Thus, the IRS now agrees that unmarried co-owners are collectively limited to a deduction for interest paid on a maximum of $2.2 million, rather than $1.1 million, of acquisition and home equity debt.

*Finalized regulations explain when research credit is available for internal use software.* As a general rule, except as provided by regulations, the research tax credit is not available for computer software that is developed by (or for the benefit of) the taxpayer primarily for its internal use. New final regulations carry an exception by providing that the research tax credit is available for the development of internal use software that meets a "high threshold of innovation test." Under this test, internal use software can qualify for the credit if it is innovative, the software development involves significant economic risk, and the software is not commercially available for use by the taxpayer. Under the final regulations, part of the cost of computer software that is developed for both internal use and non-internal use (dual function computer software) also may be eligible for the credit.

*Temporary regulations explain how to elect new partnership uniform audit rules.* A law enacted in 2015 (The Bipartisan Budget Act of 2015, signed into law on Nov. 2, 2015) eliminated the TEFRA unified partnership audit rules (so-called because they were introduced in the Tax Equity And Fiscal Responsibility Act of '82) and the electing large partnership rules, and replaced them with streamlined partnership audit rules. The new rules are effective for returns filed for partnership tax years beginning after Dec. 31, 2017, but taxpayers can elect to apply them earlier. Now the IRS has issued temporary regulations explaining how a partnership may elect to have the new partnership audit rules apply to any partnership tax year beginning after Nov. 2, 2015 and before Jan. 1, 2018.

*Simplified per-diem increase for post-Sept. 30, 2016 business travel.* An employer may pay a per-diem amount to an employee on business-travel status instead of reimbursing actual substantiated expenses for away-from-home lodging, meal and incidental expenses (M&IE). If the rate paid doesn't exceed IRS-approved maximums, and the employee provides simplified substantiation, the reimbursement isn't subject to income- or payroll-tax withholding and isn't reported on the employee's Form W-2. In general, the IRS-approved per-diem maximum is the GSA per-diem rate paid by the federal government to its workers on travel status. This rate varies from locality to locality. Instead of using actual per-diems, employers may use a simplified "high-low" per-diem, under which there is one uniform per-diem rate for all "high-cost" areas within the continental U.S. (CONUS), and another per-diem rate for all other areas within CONUS. The IRS has released the "high-low" simplified per-diem rates for post-Sept. 30, 2016, travel. The high-cost area per-diem increases $7 to $282 (consisting of $214 for lodging and $68 for M&IE), and the low-cost area per-diem increases $4 to $189 (consisting of $132 for lodging and $57 for M&IE).