Current Federal Tax Developments

Week of November 22, 2021

Edward K. Zollars, CPA
(Licensed in Arizona)

CURRENT FEDERAL TAX DEVELOPMENTS
WEEK OF NOVEMBER 22, 2021

Published in 2021 by Kaplan Financial Education.

Printed in the United States of America.

Current Federal Tax Developments

Table of Contents

SECTION: 274
MEALS & INCIDENTS EXPENSE PORTION OF PER DIEM DEEMED TO BE 100% DEDUCTIBLE RESTAURANT PROVIDED MEALS FOR 2021 AND 2022

Citation: Notice 2021-63, 11/16/21

In Notice 2021-63[1] the IRS provides guidance on the interaction of the per diem rules found in Revenue Procedure 2019-48[2] and the temporary allowance of a 100% deduction for business meals provided by a restaurant found at IRC §274(n)(2)(D) for amounts paid or incurred in 2021 and 2022.

The Notice describes the per diem rules as follows:

> Section 274(d) generally provides that no deduction is allowed for any traveling expense (including meals while away from home) unless the taxpayer substantiates such expense by adequate records or by sufficient corroborating evidence. However, § 274(d) authorizes the Secretary of the Treasury or her delegate to prescribe by regulation that some or all of the substantiation requirements do not apply in the case of an expense which does not exceed a particular amount. Section 1.274-5(j)(1) of the Income Tax Regulations authorizes the Commissioner of Internal Revenue (Commissioner) to establish a method allowing a taxpayer to treat a specific amount as paid or incurred for meals while traveling away from home instead of substantiating the actual cost. See also § 1.274-5(g).
>
> In Rev. Proc. 2019-48, 2019-51 I.R.B. 1392, the Commissioner provides rules for taxpayers that choose to use a per diem rate to substantiate, under § 274(d) and § 1.274-5, the amount of ordinary and necessary business expenses paid or incurred while traveling away from home for: lodging, meal, and incidental expenses; meals and incidental expenses only; or incidental expenses only. Taxpayers that follow the rules in Rev. Proc. 2019-48 are deemed to meet the substantiation requirements in § 274(d) for the applicable travel expenses. See, for example, section 4.01 of Rev. Proc. 2019-48. Except for incidental expenses only deductions, all or part of the amount of an expense deemed substantiated under Rev. Proc. 2019-48 is subject to the appropriate limitation under § 274(n) on the deductibility of food or beverage expenses. See section 6.05 of Rev. Proc. 2019-48.[3]

---

[1] Notice 2021-63, November 16, 2021, https://www.taxnotes.com/research/federal/irs-guidance/notices/irs-clarifies-application-of-temporary-meal-expense-deduction/7clyd?h=2021-63

[2] Revenue Procedure 2019-48, November 26, 2019, https://www.taxnotes.com/research/federal/irs-guidance/revenue-procedures/irs-provides-per-diem-rate-rules-for-substantiating-expenses/2b5g2

[3] Notice 2021-63, November 16, 2021

The Notice provides that the IRS will allow taxpayers to treat the meals and incidental expense portion of the per diem allowance as consisting of food and beverages provided by a restaurant:

> Solely for purposes of § 274(n)(2)(D), a taxpayer that properly applies the rules of Rev. Proc. 2019-48 may treat the meal portion of a per diem rate or allowance paid or incurred after December 31, 2020, and before January 1, 2023, as being attributable to food or beverages provided by a restaurant.[4]

The ruling applies to both reimbursements to employees and amounts properly claimed under the per diem rules by self-employed individuals in accordance with Revenue Procedure 2019-48.[5]

SECTION: 408
TAXPAYER FOUND TO HAVE DISTRIBUTION FROM SELF-DIRECTED IRA FOR COINS OWNED BY LLC HELD BY IRA STORED IN TAXPAYER'S SAFE AT HOME

Citation: McNulty v. Commissioner, 157 TC No. 10, 11/18/21

In a published decision, the IRS ruled that a taxpayer who took physical possession of and stored in a safe in her home coins that she argued were owned by an LLC whose interests were held by her self-directed IRA had a taxable distribution from the IRA.[6]

The coins in question were acquired by an LLC whose sole member, per the taxpayers, was an IRA for the benefit of Donna McNulty. Donna was appointed as the sole manager of this LLC owned by her IRA.

The Self-Directed IRA, the LLC and the Coins

The story begins in 2015 when Ms. McNulty retained the services of Checkbook IRA, LLC to assist her in setting up a self-directed IRA. Per the opinion for the case, she did so based on the following information she found on their website:

> In August 2015 Mrs. McNulty purchased services from Check Book IRA, LLC (Check Book), through its website, that included assistance in establishing a self-directed IRA and forming an LLC to which she would transfer IRA funds through purchases of membership interests and then purchase AE coins using IRA funds. During 2015 Check Book's website advertised that an LLC owned by an IRA could invest in AE coins and IRA owners could hold the coins at their homes

---

[4] Notice 2021-63, November 16, 2021

[5] Notice 2021-63, November 16, 2021, Section 4

[6] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021, https://www.taxnotes.com/research/federal/court-documents/court-opinions-and-orders/coins-in-ira-owner%e2%80%99s-possession-were-taxable-distributions/7cmb0

> without tax consequences or penalties so long as the coins were "titled" to an LLC.[7]

Based on that information, she took the following actions to obtain a trustee for the IRA and establish the LLC that the IRA would own:

> On August 19, 2015, Mrs. McNulty established a self-directed IRA using Check Book's services and named Kingdom Trust Co. (Kingdom Trust) the IRA custodian. Kingdom Trust is an independent qualified custodian under the Investment Advisers Act of 1940. On August 24, 2015, Check Book formed Green Hill Holdings, LLC (Green Hill). Green Hill's articles of organization, which were filed with the secretary of state of Rhode Island on August 25, 2015, state that Green Hill is a single-member LLC that is a disregarded entity for Federal tax purposes and its sole initial member was Mrs. McNulty's IRA.
>
> Petitioners were appointed Green Hill's initial managers and were the managers during 2015 and 2016. Petitioners' personal residence is Green Hill's principal place of business. Green Hill opened a bank account over which petitioners had signatory authority. With Check Book's assistance, Green Hill obtained a Federal taxpayer identification number.[8]

Now that there is an LLC and the IRA in place, Ms. McNulty went about funding the IRA and acquiring the coins in question. The IRA obtained its funds as follows:

> Mrs. McNulty exercised sole control over her IRA's investment decisions. She funded the IRA through direct transfers from two qualified retirement accounts: an individual retirement annuity with MetLife (MetLife annuity) and an employer-sponsored section 401(k) profit-sharing retirement plan (401(k)). Upon Mrs. McNulty's instruction $378,487 was transferred from the MetLife annuity to her IRA during 2015 and $48,375 from the 401(k) during 2016. Petitioners did not report any part of these transfers as gross income.[9]

Now she has those funds used by the trustee to purchase LLC interests and then have the LLC, with her as the manager, purchase the coins:

> Mrs. McNulty instructed Kingdom Trust to use her IRA funds to purchase membership interests in Green Hill. The IRA purchased membership interests on three occasions during 2015 and 2016 (Green Hill investments). For each investment Mrs. McNulty instructed Kingdom Trust to transfer the purchase price of the membership interests from the IRA to Green Hill's bank account. In turn, Mrs. McNulty, as the LLC's manager, had Green Hill use almost all of the funds to purchase AE coins from Miles Franklin, Ltd. (Miles Franklin),

---

[7] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[8] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[9] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

> an authorized coin dealer. The funds to purchase the coins were transferred from Green Hill's bank account to Miles Franklin.[10]

But now the situation gets unclear with regard to whose coins they are, at the very least showing failure to always respect the LLC as the owner of the coins and having the coins stored in Ms. McNulty's residence along with coins owned personally:

> The invoices from Miles Franklin list Green Hill as the purchaser. However, the shipping labels identified Mrs. McNulty individually or along with her IRA as the recipient of the shipments. The coins were shipped to petitioners' personal residence and were stored in a safe there (safe) along with coins purchased with funds from Mr. McNulty's IRA and coins purchased by petitioners directly (collectively, non-IRA assets). The AE coins purchased with funds from Mrs. McNulty's IRA, through Green Hill, were labeled as such.[11]

The opinion continues, outlining all of the various transactions for this self-directed IRA and the LLC it is purported to own:

> The first Green Hill investment and coin purchase occurred in August through September 2015 with the funds transferred from the MetLife annuity. Mrs. McNulty instructed Kingdom Trust to purchase 375,000 membership units of Green Hill at $1 per unit for an investment of $375,000. The funds for the purchase were wired from the IRA to Green Hill's bank account. Mrs. McNulty then had Green Hill purchase 320 one-ounce AE gold coins for $374,000 from Miles Franklin (2015 AE gold coins), and $374,000 was wired from Green Hill's bank account to Miles Franklin. Miles Franklin shipped the coins to petitioners' residence, addressed to "Donna McNulty Green Hill", where they were stored in the safe.
>
> The second Green Hill investment and AE coin purchase occurred in late January through February 2016 with IRA funds that had been transferred from the 401(k). Mrs. McNulty instructed Kingdom Trust to purchase 43,274.70 membership units of Green Hill at $1 per unit for an investment of $43,274.70. Kingdom Trust wired $43,274.70 from the IRA to Green Hill's bank account. Mrs. McNulty had Green Hill use part of the funds to purchase 2,000 one-ounce AE silver coins for $37,380 (2016 AE silver coins), and $37,380 was wired from Green Hill's bank account to Miles Franklin. Miles Franklin shipped the coins to petitioners' residence, to "Green Hill * * * FBO Donna McNulty", where they were stored in the safe.
>
> In August 2016 Green Hill used $6,731 of the funds remaining in its bank account from the MetLife annuity and 401(k) transfers to purchase four one-ounce AE gold coins, two one-quarter-ounce AE gold coins, and one one-tenth-ounce AE gold coin (2016 AE gold coins). A payment of $6,746 for the AE coins plus insured shipping

[10] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[11] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

> was wired from Green Hill's bank account to Miles Franklin. Miles Franklin shipped the coins to "Donna McNulty" at petitioners' residence, where they were stored in the safe.
>
> The third Green Hill investment occurred in November to December 2016. Around November 20, 2016, Mrs. McNulty instructed Kingdom Trust to purchase 6,898.92 membership units of Green Hill at $1 per unit for an investment of $6,898.92. Approximately one week later, she instructed the custodian of her 401(k) to transfer $5,101 from her 401(k) to her IRA. Thereafter, $6,989.92 was wired from Mrs. McNulty's IRA to Green Hill's bank account. There was no purchase of AE coins after this investment.

There were also issues with the annual valuations of the IRA that were submitted by the trustee to the IRS. While the coin dealer provided annual valuations for the gold coins, it did not provide any values for the silver coins and no other valuations were obtained.

The trustee obtained the valuation it used by asking Ms. McNulty to provide a yearend value of the assets held in her IRA. And Ms. McNulty had various issues that caused her to omit certain assets from the valuation:

> Kingdom Trust required Mrs. McNulty to provide a yearend valuation of her IRA's assets. She completed a valuation form that she submitted to Kingdom Trust on which she identified herself as Green Hill's sole owner and represented Green Hill's value as $347,680 and $388,047 for 2015 and 2016, respectively. As of yearend 2015 and 2016, Green Hill's bank account had balances of $993 and $6,899, respectively. Mrs. McNulty omitted the bank account balance on the 2015 valuation form and omitted the value of the 2016 AE silver coins on the 2016 valuation form.
>
> Kingdom Trust filed Form 5498, IRA Contribution Information, with the Internal Revenue Service (IRS) for 2015 and 2016, reporting the IRA's fair market values of $349,856 and $388,247, respectively. The 2015 Form 5498 omitted Green Hill's yearend bank account balance, and the 2016 Form omitted the value of the 2016 AE silver coins. Kingdom Trust did not have any role in the management of Green Hill, the purchase of the AE coins, or the administration of Green Hill's assets or the IRA assets.[12]

While the taxpayer had a CPA prepare their return, the CPA was not consulted on the self-directed IRA and also was not informed about how the coins were being held:

> Petitioners' 2015 and 2016 tax returns were prepared by a certified public accountant (C.P.A.). Petitioners did not seek or receive advice from the C.P.A. about the tax reporting with respect to their self-directed IRAs or their physical possession of AE coins purchased using funds from their IRAs or the LLC through which Mr. McNulty's

---

[12] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

> IRA held the condo. Nor did they disclose to their C.P.A. that they had physical possession of the AE coins at their residence.[13]

IRS Exam

The IRS examined the taxpayers' returns and found issues with both taxpayers' IRAs:

> On October 30, 2018, respondent issued to petitioners a notice of deficiency for 2015 and 2016 in which he determined that they each received taxable distributions from their IRAs that they failed to report. He also determined that they were liable for section 6662(a) and (b)(1) and (2) accuracy-related penalties for both years for underpayments due to substantial understatements of income tax and, alternatively, negligence or disregard of rules or regulations, attributed to their failure to report the distributions. He determined that petitioners each received taxable distributions upon their receipt of the AE coins equal to the costs of the coins, including, with respect to Mrs. McNulty, taxable distributions of $374,000 and $37,380 for 2015 and 2016, respectively.[14]

The taxpayers and the IRS had settled on the issue of the distribution to Mr. McNulty before the case went to trial, so the remaining issues were whether there was a taxable distribution to Ms. McNulty and whether there were penalties due for any amounts of underpayments.

Did Ms. McNulty Have a Taxable Distribution from Her IRA?

The Court begins by describing the rules that require IRA assets to be held bin a trust (including a custodial account treated as a trust under IRC §408(a)). The requirements for that trust are outlined by the Court as follows:

> The trustee must be a bank (as defined in section 408(n)) or such other person who demonstrates to the satisfaction of the Secretary that the manner in which it will administer the trust will be consistent with the requirements of section 408. *Id.* subsec. (a)(2). For a person to qualify as a trustee, the person must demonstrate by written application to the Commissioner that it meets the requirements set forth in the regulations for a trustee. Sec. 1.408-2(e)(1), Income Tax Regs. The applicant "must demonstrate in detail its ability to act within the accepted rules of fiduciary conduct." *Id.* subparas. (2) (defining a trustee), (5) (setting forth the requirements for a nonbank trustee).[15]

A key issue in this case will be the rules regarding the holding and safekeeping of the asset by the trustee:

> The trustee must keep separate and distinct records with full information on each IRA. *Id.* subpara. (5)(vii)(A). If assets require

[13] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[14] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[15] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

> safekeeping, the trustee must deposit them into an "adequate vault" and keep a permanent record of deposits and withdrawals from the vault. *Id.* subdiv. (v)(B). The IRA asset cannot be commingled with other property except in a common trust fund or common investment fund. Sec. 408(a)(5); sec. 1.408-2(b)(5), Income Tax Regs.[16]

The IRS argued that how the coins were held in this case meant that Ms. McNulty had access to the assets in the IRA supposedly under the control of the IRA's trustee. Per the IRS, it was not relevant that the coins were claimed to be the property of the LLC and that Ms. McNulty was acting solely as the manager of the LLC, with the LLC interests held by the trustee. The taxpayers, as expected, argued that these particular facts of the form of the transaction are crucial and thus Ms. McNulty had not received a distribution of the coins.

The Court noted the various items of disagreement as follows:

> The parties' arguments reveal numerous disagreements including whether Mrs. McNulty or her IRA was Green Hill's sole member, who owned the AE coins, who held legal title to the AE coins, whether AE coins are bullion, whether the AE coins were commingled with non-IRA assets, and who can have physical possession of the AE coins purchased with IRA funds.[17]

Unfortunately for the taxpayers, the Court focused on the last issue—who had physical possession of the coins that had been purchased with the IRA's funds. Note that in stating that last issue, the Court did not mention the LLC—but rather the coins.

The opinion notes that a self-directed IRA owner can direct investments and the IRA can acquire a single member LLC:

> An owner of a self-directed IRA is entitled to direct how her IRA assets are invested without forfeiting the tax benefits of an IRA. *McGaugh v. Commissioner*, T.C. Memo. 2016-28, at *9, *aff'd*, 860 F.3d 1014 (7th Cir. 2017). A self-directed IRA is permitted to invest in a single-member LLC. *Swanson v. Commissioner*, 106 T.C. 76 (1996); *Ellis v. Commissioner*, T.C. Memo. 2013-245 (holding that an IRA's investment in a newly formed LLC was not a prohibited transaction because the LLC did not have any members when the investment was made and thus was not a disqualified person at that time), aff'd, 787 F.3d 1213 (8th Cir. 2015).[18]

But as was true in other self-directed IRA cases that haven't gone well for the taxpayers in the end (including the *Ellis* case the Court cited), the problems begin once assets make their way into that LLC.

[16] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[17] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[18] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

In Ms. McNulty's case, the problem is that eventually she had direct personal control of the coins purchased with the IRA funds. The Court outlines why this is an issue:

> A qualified custodian or trustee is required to be responsible for the management and disposition of property held in a self-directed IRA. Sec. 1.408-2(e), Income Tax Regs. A custodian is required to maintain custody of the IRA assets, maintain the required records, and process transactions that involve IRA assets. See sec. 408(h) and (i); sec. 1.408-2(e)(4), (5)(i)(2), (iii), (vii), Income Tax Regs. The presence of such a fiduciary is fundamentally important to the statutory scheme of IRAs, which is intended to encourage retirement savings and to protect those savings for retirement. Independent oversight by a third-party fiduciary to track and monitor investment activities is one of the key aspects of the statutory scheme. When coins or bullion are in the physical possession of the IRA owner (in whatever capacity the owner may be acting), there is no independent oversight that could prevent the owner from invading her retirement funds. This lack of oversight is clearly inconsistent with the statutory scheme. Personal control over the IRA assets by the IRA owner is against the very nature of an IRA.[19]

The Court found that "Mrs. McNulty had complete, unfettered control over the AE coins and was free to use them in any way she chose."[20] The opinion continues:

> This is true irrespective of Green Hill's purported ownership of the AE coins and her status as Green Hill's manager. Once she received the AE coins there were no limitations or restrictions on her use of the coins even though she asserts on brief that she did not use them. While an IRA owner may act as a conduit or agent of the IRA custodian, she may do so only as long as she is not in constructive or actual receipt of the IRA assets. See *Ancira v. Commissioner*, 119 T.C. 135, 137-140 (2002) (holding no taxable distribution occurred when the IRA owner personally received a check that he could not negotiate, the funds were then used to acquire stock, and the stock certificate was issued in the IRA's name); *McGaugh v. Commissioner*, at *13-*14 (holding no taxable distribution occurred even if a stock certificate was in the IRA owner's possession but it issued in the IRA's name and thus the owner could not realize any benefits from it and did not have constructive receipt of IRA assets); *Dabney v. Commissioner*, T.C. Memo. 2014-108 (holding a taxable distribution occurred when real estate was titled in the IRA owner's name).[21]

Why didn't the existence of the LLC matter? The opinion comments on this issue in a footnote to the first sentence in the above quotation from the case. That discussion

---

[19] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[20] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[21] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

begins by citing what appears at first to be odd cases relating to holding FSCs and DISCs in Roth IRAs:

> The Court of Appeals for the First Circuit, to which this case is appealable absent a stipulation to the contrary, has rejected use of the substance-over-form doctrine to recharacterize the form of a Roth IRA's investment in a domestic international sales corporation (DISC). *Benenson v. Commissioner*, 887 F.3d 511, 523 (1st Cir. 2018), *rev'g Summa Holdings, Inc. v. Commissioner,* T.C. Memo. 2015-119; see also *Summa Holdings, Inc. v. Commissioner,* 848 F.3d 779, 785 (6th Cir. 2017), *rev'g* T.C. Memo. 2015-119. *Benenson* involved whether the Roth IRA's receipt of DISC dividends was an excessive contribution in violation of the limits of sec. 219. It did not address the fiduciary or custodial requirements of IRAs.[22]

The reader may be a bit confused at this point—isn't the Court in this looking at the substance of the transactions and bypassing the form of the LLC? But the Court now points out an interesting fact—the LLC was being treated as a disregarded entity in this case:

> Moreover, respondent does not disregard Green Hill. Mrs. McNulty chose for Green Hill to be a disregarded entity for Federal tax purposes. Petitioners have not established that Mrs. McNulty should be entitled to disavow her chosen form. See *Complex Media, Inc. v. Commissioner*, T.C. Memo. 2021-14, at *64 (setting forth standards under which taxpayers may try to disavow the form of a transaction) [23]

But the footnote eventually argues that none of that matters in this case.

> Finally, resolution of the issues here does not depend on Green Hill's status as a disregarded entity or its separate legal existence.[24]

The Court found that this situation amounted to complete and unfettered control over the coins for Ms. McNulty, a situation that resulted in distributions to her of those coins from the IRA:

> An owner of a self-directed IRA may not take actual and unfettered possession of the IRA assets. It is a basic axiom of tax law that taxpayers have income when they exercise complete dominion over it. See *Commissioner v. Banks*, 543 U.S. 426, 434 (2005); *Commissioner v. Glenshaw Glass Co.*, 348 U.S. 426, 431 (1955). Constructive receipt occurs where funds are subject to the taxpayer's unfettered command and she is free to enjoy them as she sees fit. *Ancira v. Commissioner*, 119 T.C. at 138-139. Mrs. McNulty's possession of the AE coins is a taxable distribution. Accordingly, the value of the coins is includible in her gross income. Petitioners' arguments to the contrary would make permissible a situation that is ripe for abuse and that would undermine

---

[22] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021, Footnote 5

[23] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021, Footnote 5

[24] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021, Footnote 5

the fiduciary requirements of section 408. Mrs. McNulty took possession of the AE coins and had complete control over them. Accordingly, she had taxable distributions from her IRA.[25]

Does IRC §408(m) Specifically Exempt the Coins from the Custodial Requirement?

The taxpayers did have an additional line of defense, arguing that even if she did have actual custody of the coins, the coins were specifically exempted from the custodial requirements generally imposed by IRC §408(a) and the related Treasury regulations by the language of IRC §408(m)(3).

IRC §408(m) generally prohibits an IRA from investing in collectibles, and IRC §408(m)(2)(D) includes coins as such a collectible that the IRA cannot invest in. However, IRC §408(m)(3) provides an exception from this rule for certain coins and bullion.

IRC §408(m)(3) reads:

> (3) Exception for certain coins and bullion
>
> For purposes of this subsection, the term "collectible" shall not include--
>
> (A) any coin which is--
>
> (i) a gold coin described in paragraph (7), (8), (9), or (10) of section 5112(a) of title 31, United States Code,
>
> (ii) a silver coin described in section 5112(e) of title 31, United States Code,
>
> (iii) a platinum coin described in section 5112(k) of title 31, United States Code, or
>
> (iv) a coin issued under the laws of any State, or
>
> (B) any gold, silver, platinum, or palladium bullion of a fineness equal to or exceeding the minimum fineness that a contract market (as described in section 5 of the Commodity

[25] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

> Exchange Act, 7 U.S.C. 7) requires for metals which may be delivered in satisfaction of a regulated futures contract,

> if such bullion is in the physical possession of a trustee described under subsection (a) of this section.

The very last clause of that subsection is what is referred to in a statute as "flush text" since, although it follows the (B) subsection, it's really the last line of the overall §408(m)(3).

The taxpayers argue that this clause only applies to bullion and, as such, creates an exception under which coins would not need to be held by the trustee as, in their view, coins are not bullion. As the opinion explains:

> Petitioners argue that the text at the end of section 408(m)(3) makes physical possession by a trustee a condition of an IRA's ownership of bullion. They further argue that the flush text applies only to bullion described in subparagraph (B), that AE coins are not bullion, and thus that a trustee is not required to have physical possession of AE coins. Respondent disagrees with petitioners on each of these points.[26]

The Tax Court however concludes that what the flush text applies to is irrelevant, holding:

> The flush text does not create an exception to the custodial and fiduciary requirements of section 408(a) irrespective of whether it applies to both subparagraphs (A) and (B) or whether AE coins are bullion.[27]

The Court notes that both parties agree that if the statutory text is unambiguous then that determines the proper treatment, though both argue that the text supports their interpretation. The Tax Court finds that the IRS is correct in this context—the language doesn't provide for any exception from the general rules for coins as some special type of IRA asset, regardless of whether or not they are bullion:

> The flush text does not address the fiduciary or custodial requirements of section 408(a), and we do not interpret it to create an exception to those requirements in the absence of express wording that does so. In matters of statutory interpretation, "[w]e assume that Congress is aware of existing law when it passes legislation." *Miles v. Apex Marine Corp.*, 498 U.S. 19, 32 (1990) (quoting *Robinson v. Shell Oil Co.*, 519 U.S. 337, 341 (1997)). Statutory interpretation must take into account "the broader context of the statute as a whole." *Util. Air Regulatory Grp. v. EPA*, 573 U.S. 302, 321 (2014). There is no evidence of legislative intent to discontinue the fiduciary requirements generally applicable to IRAs for IRA investments in coins or bullion. The flush text did not add the custodial requirements; they already existed. It is section 408(a)

---

[26] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[27] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

> and the regulations thereunder that impose the custodial and fiduciary requirements.[28]

The taxpayers were trying to create a "plain text" exception by omission, but at best that can only be found by implication. A statement that a certain type of asset must be held by a trustee doesn't repeal a general rule that a trustee must secure all assets.

The taxpayer's argument effectively is going to depend on evidence outside of the text of the statute, such as documentation of Congressional intent to do what they claim by passing this provision (remove coins from any requirement to be held by the trustee) and enough ambiguity in the statute to allow that to be read into the statute even though not specifically stated in the statutory text.

But even going down that path, the Court notes that they presented no evidence that Congress intended to create a special backdoor exception for coins as they enacted IRC §408(m)(3) in pieces over time. The Court noted how the language that currently makes up IRC §408(m)(3) was brought into the IRC:

> Congress has amended section 408(m) on three occasions to exclude certain coins and bullion from the definition of "collectible". First, in 1986 Congress allowed IRAs to invest in certain coins minted by the United States Mint. This amendment coincided with the Mint's 1986 launch of the AE coin program. Tax Reform Act of 1986, Pub. L. No. 99-514, sec. 1144, 100 Stat. at 2490. In 1988 it allowed IRAs to invest in certain coins issued by States and in 1997 to invest in bullion and certain platinum coins. Technical and Miscellaneous Revenue Act of 1988, Pub. L. No. 100-647, sec. 6057, 102 Stat. at 3698; Taxpayer Relief Act of 1997, Pub. L. No. 105-34, sec. 304, 111 Stat. at 831. Congress added the flush text in 1997 when it revised section 408(m)(3) to add subparagraph (B) to allow IRAs to invest in bullion.[29]

Note that Congress did not provide any hint that coins were exempt from the general rules of IRC §408(a) when the exception allowing them to be held in an IRA was added to the IRC. Rather, the flush language was only added at the same time the ability for an IRA to hold bullion was added in 1997.

The Court obviously reads this as Congress emphasizing that it saw such holdings as being of a nature where the statute itself would directly require physical possession by the trustee of the asset, rather than looking to the more general rule in the statute to secure such assets found in IRC §408(a) specified in the regulations adopted by Treasury. Having the explicit requirement in the statute eliminates the option for Treasury to remove such a requirement in later revisions to the regulations—even if the Department does make revisions to remove rules related to how these assets are held in the regulations, bullion would have to be held by the trustee.

---

[28] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[29] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

The Court states:

> The plain text of the statute is that an IRA's bullion that is not in the physical possession of a trustee is a collectible. The flush text does not address the fiduciary or custodial requirements of section 408(a), and we do not interpret it to create an exception to those requirements in the absence of express wording that does so. In matters of statutory interpretation, "[w]e assume that Congress is aware of existing law when it passes legislation." *Miles v. Apex Marine Corp*., 498 U.S. 19, 32 (1990) (quoting *Robinson v. Shell Oil Co*., 519 U.S. 337, 341 (1997)). Statutory interpretation must take into account "the broader context of the statute as a whole." *Util. Air Regulatory Grp. v. EPA,* 573 U.S. 302, 321 (2014). There is no evidence of legislative intent to discontinue the fiduciary requirements generally applicable to IRAs for IRA investments in coins or bullion. The flush text did not add the custodial requirements; they already existed. It is section 408(a) and the regulations thereunder that impose the custodial and fiduciary requirements.[30]

Thus, the Court concludes:

> According to petitioners' argument, the flush text negates the basic requirement of section 408(a) that there be a trustee that acts as a fiduciary and administers IRA assets. We will not apply such a negative inference to override the basic fiduciary and custodial requirements of section 408(a) that are fundamental to the retirement savings scheme, particularly in the absence of clear statutory text. The flush text does not create an exception to the well-established rules that IRA assets must be held by a trustee and that an IRA owner who takes possession of IRA assets receives a taxable distribution. Accordingly, Mrs. McNulty's receipt of each purchase of the AE coins paid for with her IRA funds was a taxable distribution pursuant to section 408(d).[31]

Did Ms. McNulty Violate the Commingling Ban of IRC §408(a)(5)?

Regardless of the above issues, the Court found Ms. McNulty had violated a separate provision of the law that caused a distribution from the IRA. The law and regulations bar commingling of IRA assets with other property, as explained in the opinion:

> Section 408(a)(5) provides that "[t]he assets of the trust will not be commingled with other property except in a common trust fund or common investment fund." See also sec. 1.408-2(b)(5), (e)(5)(v), Income Tax Regs. The safe was not a common trust fund or a common investment fund and was not administered as such for purposes of section 408(a)(5). See sec. 1.408-2(b)(5)(ii), (e)(5)(vi), (viii)(C), Income Tax Regs.[32]

---

[30] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[31] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[32] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

The IRS and taxpayers disputed whether there had been impermissible commingling. The Court explains:

> Respondent argues that Mrs. McNulty violated the prohibition against commingling IRA assets when the AE coins were stored in the safe with non-IRA assets. He argues that the commingling results in taxable distributions even if Mrs. McNulty's physical custody of the AE coins did not. Petitioners argue that there was no commingling because the AE coins purchased using the IRA funds were labeled as such before they were placed in the safe.[33]

The Court found the IRS's argument far more persuasive:

> We question whether labeling is sufficient to satisfy the Code's prohibition against commingling or whether storage in a safe satisfies the requirement that assets requiring safekeeping be kept in an adequate vault. However, we do not need to resolve this issue as Mrs. McNulty's physical possession of the AE coins resulted in taxable distributions irrespective of whether commingling occurred.[34]

Penalty Relief Based Research the Taxpayer Conducted

The taxpayers had already conceded tax was due based on actions of Mr. McNulty with his IRA and the Court had concluded that additional tax was due for Ms. McNulty's IRA activities. But the question remained whether the taxpayers could escape penalties under IRC §6662(a).

In favor of the taxpayers was the fact that some of these issues that lead to tax being due had not been decided by the Tax Court before. As the Tax Court notes:

> We have refused to impose a penalty where the issue is one of first impression and the taxpayer's position was reasonably debatable, *Williams v. Commissioner*, 123 T.C. 144, 153-154 (2004), or the statute at issue was not entirely clear, *Hitchins v. Commissioner*, 103 T.C. 711, 719-720 (1994), so long as the taxpayer made a reasonable attempt to comply with tax law.[35]

Similarly, the Court notes that reasonable reliance on professional advice can also constitute reasonable cause if the taxpayers sought such advice and it was based on all pertinent facts. A failure by the taxpayer to disclose relevant facts will bar relying on the advice for reasonable cause relief from penalties.

The use of a CPA to prepare the taxpayers' returns for the years in question does not create reasonable cause since they did not seek advice from the CPA on this matter and

[33] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[34] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[35] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

they never disclosed the key facts regarding where the IRA's assets were being held to the CPA:

> Petitioners did not seek or receive any advice from their C.P.A., who prepared their 2015 and 2016 returns, regarding their self-directed IRAs. They failed to disclose the relevant information to their C.P.A. Such a failure to disclose pertinent facts shows a lack of good faith in tax reporting; and on the basis of this failure we conclude that petitioners have not established that they acted reasonably or in good faith. Petitioners are both professionals. They liquidated nearly $750,000 from their existing qualified retirement accounts to invest in a questionable internet scheme without disclosing the transactions to their C.P.A.[36]

In fact, the last line of the above quotation implies that the use of a CPA to prepare the returns, but then failing to discuss this transaction with the CPA, actually was a factor that argued that the taxpayers had not acted reasonably to discover their proper tax liability. The failure to seek advice from such an obvious source does not appear to be a step someone reasonably trying to determine the proper amount of tax to pay would have taken.

The taxpayers argued that they had researched this structure and concluded they could hold the IRA coins in their home without negative tax consequences based on that research. Per the Court:

> They argue that there was conflicting information, including the IRS' own guidance, about whether the flush text of section 408(m)(3) applies to AE coins and whether taxpayers may take physical possession of AE coins when they are held through the IRA's ownership of an LLC. They also contend that Mr. McNulty did not know that he had engaged in a prohibited transaction when petitioners filed their returns.[37]

But the Court found that they gave few details about this research and how they came to their conclusion. And the information they did mention that might be viewed to represent such research appeared inadequate and/or clearly biased.

The Court looked at the information on the website for the organization they used to set up the IRA and that of the trustee which seemed to constitute the source of the taxpayers' belief this structure was acceptable:

> They stipulated exhibits of three versions of Check Book's website from three dates during 2015, implying that petitioners' research included a review of the website at some point during 2015. Check Book's website advertised that taxpayers could purchase AE coins with their IRA funds and obtain physical possession of the coins without any tax consequences. The parties also stipulated part of Kingdom

[36] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[37] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

> Trust's website, which states that AE coins must be held in a depository.
>
> …
>
> Petitioners have not argued that Check Book's online services are professional advice upon which they were entitled to rely. Rather, they argue in vague terms that they performed research about an IRA investment in AE coins through an LLC structure, without identifying the source or specific results of the research. They did not stipulate their purported research other than stipulating parts of Check Book's and Kingdom Trust's websites as exhibits.
>
> We question whether Check Book's website and/or services could constitute professional advice upon which a reasonable person could rely for purposes of section 6664(c)(1). See sec. 1.6664-4(c)(2), Income Tax Regs. (defining advice). Check Book's website is an advertisement of its products and services, and a reasonable person would recognize it as such and would understand the difference between professional advice and marketing materials for the sale of products or services. Petitioners have not provided any evidence that sets forth Check Book's qualifications to provide professional tax advice. Nor was Check Book disinterested. It benefited financially from petitioners' purchase of its services. See *106 Ltd. v. Commissioner,* 136 T.C. 67, 79 (2011) (stating that reliance on an adviser who participated in structuring the transaction, i.e., a promoter, is not reasonable cause), aff'd, 684 F.3d 84 (D.C. Cir. 2012).[38]

The taxpayers should have recognized that these parties, who had a strong incentive to persuade the taxpayers to enter into this transaction, were not unbiased sources of information that should be relied upon by a reasonable person to decide upon the proper tax treatment without obtaining some sort of outside corroboration of these items.

The taxpayer also included a printout of an IRS website from 2019 to support their flush text argument. But the Court found a number of problems with that document.

First the Court points out that the item was not properly submitted as an exhibit before the Court and thus cannot be considered by the Court:

> Respondent objects to the printout because it was not stipulated as an exhibit. We sustain respondent's objection. The printout is not part of the record.[39]

But the Court pointed out an even more basic problem this printout presented—obviously, they could not have read this as part of their research they undertook before entering into the transactions in question that were reported on their 2015 and 2016

[38] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[39] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

returns, at least unless they had also discovered a method of time travel to enable them to read a 2019 web site to determine actions taken years earlier.

Finally, even if they had developed this form of time travel, the Court found that it would not have supported a reasonable cause defense:

> The printout would offer little support for a reasonable cause defense as it merely states that IRAs can invest in bullion that is in the physical possession of a trustee. It does not state that taxpayers can take physical custody of AE coins held through the IRA's ownership of an LLC.[40]

Thus, the Court found that the understatement would be subject to the accuracy related penalties of IRC §6662(a).

Self-Directed IRAs – Allowable But Easy to Foul Up

The real lesson from this case is not that self-directed IRAs cannot be successfully used by taxpayers. The Court indicated such was possible in its opinion.

But these structures have lots of detailed and intricate rules that must be meticulously followed to avoid a tax disaster. As we've noted in the past,[41] there are numerous ways to violate these rules and the violation usually results in an immediate distribution of all funds from the IRA.

And doing quick internet searches to figure out these rules does not serve as adequate evidence of a reasonable attempt to properly determine a taxpayer's obligations, especially when the taxpayer relies primarily on marketing sites from organizations seeking to have the taxpayer hire them to create such structures.

It is not impossible for someone not trained in income taxation or law to do such research properly—but it is a skill that even those who have been formally trained in the area find quite challenging and requires having the ability to recognize the potential biases of sources, as well as understanding the nature of sources that Courts will turn to in deciding these issues, and how Courts would resolve any conflict between those sources the court will look to.

Good research skills always involve a level of proper skepticism about any information uncovered, be it source material (has this source of the Internal Revenue Code been updated for the most recent laws passed by Congress, has the law changed since this regulation, ruling, etc. was issued, …) or editorial materials (what is the source material the author of this article used to back up his/her statements, is the author skilled in

---

[40] *McNulty v. Commissioner,* 157 TC No. 10, November 18, 2021

[41] See our articles "Payment of Salary by Corporation Formed with IRA Funds to IRA Beneficiary Found to Be Prohibited Transaction by Both Tax Court and Eighth Circuit," *Current Federal Tax Developments* website June 10, 2015, https://www.currentfederaltaxdevelopments.com/blog/2015/6/10/payment-of-salary-by-corporation-formed-with-ira-funds-to-ira-beneficiary-found-to-be-prohibited-transaction-by-both-tax-court-and-eighth-circuit and "Taxpayer Not Allowed to Use Step Transaction Doctrine to Escape Consequences of Prohibited Transaction With His IRA," *Current Federal Tax Developments* website, March, 30, 2015, https://www.currentfederaltaxdevelopments.com/blog/2016/3/30/taxpayer-not-allowed-to-use-step-transaction-doctrine-to-escape-consequences-of-prohibited-transaction-with-his-ira

conducting such source material research, does the author have a vested interest in arriving at a certain answer, etc.).

In this case, the taxpayers' own research was never adequately explained, nor did the taxpayers explain how those research materials supported their position, why these research materials offered sufficient evidence to support their actions, and how they had evaluated the credibility of the various materials they uncovered on the web.

SECTION: 448
IRS GIVES GUIDANCE ON TIMING OF PPP LOAN RELIEF, AS WELL AS OTHER ISSUES RELATED TO TAX EXEMPT COVID RELIEF PROGRAMS

Citation: Revenue Procedures 2021-48, 2021-49 and 2021-50, 11/18/21

The IRS finally addressed the options for the timing of PPP forgiveness for tax purposes in Revenue Procedure 2021-48[42] as well as issuing two related procedures at the same time dealing with related issues. This includes a very limited time period when an affected BBB partnership can file an amended income tax return in lieu of filing the otherwise required Administrative Adjustment Request.

Timing of Income Inclusion

The procedure provides that a taxpayer may treat tax-exempt income as received or accrued from a PPP loan under any of the following three methods:

- The tax-exempt income may be recognized as, and to the extent that, the taxpayer pays or incurs eligible expenses leading to forgiveness. Under this option, a taxpayer that has elected to use the safe harbor provided under Revenue Procedure 2021-20 will be treated as paying or incurring the eligible expenses during the taxpayer's immediately subsequent taxable year following the taxpayer's 2020 taxable year in which the expenses were actually paid or incurred, as described in Revenue Procedure 2021-20;
- When the taxpayer files an application for forgiveness of the PPP Loan; or
- When the PPP Loan forgiveness is granted.[43]

The Procedure describes Revenue Ruling 2021-20, noted above, as follows:

> Revenue Procedure 2021-20, 2021-19 I.R.B. 1150 (May 10, 2021), provides a safe harbor that allows certain taxpayers that, under prior guidance issued by the Treasury Department and the Internal Revenue

[42] Revenue Procedure 2021-48, November 18, 2021, https://www.taxnotes.com/research/federal/irs-guidance/revenue-procedures/irs-clarifies-when-to-claim-tax-exempt-ppp-forgiveness-amounts/7cm9r

[43] Revenue Procedure 2021-48, November 18, 2021

> Service, did not deduct certain otherwise deductible PPP-related expenses on a tax return that was filed prior to the enactment of the COVID Tax Relief Act to deduct such expenses in the next taxable year (that is, the taxable year following the taxable year in which such expenses were paid or incurred).[44]

If PPP Loan is Not Fully Forgiven

The Revenue Procedure provides the following provisions that apply if, after using these methods, the PPP Loan is ultimately not fully forgiven:

> Unless otherwise provided in the 2021 filing year form instructions, if the taxpayer receives forgiveness for an amount of the PPP Loan that is less than the amount that the taxpayer previously treated as tax-exempt income, the taxpayer must make appropriate adjustments on an amended Federal income tax return, information return or AAR, as applicable, for the taxable year(s) in which the taxpayer treated tax-exempt income from the forgiveness of such PPP Loan as received or accrued. Partners and shareholders that receive amended Forms K-1 as provided in this section 3.03 must file amended Federal income tax returns, information returns or AARs, as applicable, consistent with the Forms K-1 received.[45]

The Procedure requires that taxpayers who use these methods must apply them consistently for Federal income tax purposes:

> To the extent tax-exempt income resulting from the partial or complete forgiveness of a PPP Loan is treated as gross receipts under a particular Federal tax provision, including but not limited to §§ 448(c) and 6033 of the Code, section 3 of this revenue procedure applies for purposes of determining the timing and, to the extent relevant, reporting of such gross receipts.[46]

IRS Instructions

The Procedure provides an assurance the IRS will provide instructions on how to report these items on 2021 returns, but taxpayers do not have to wait for the issuance of those 2021 instructions to begin using these procedures:

> The IRS will publish form instructions for the 2021 filing season that will detail how taxpayers can report consistently with sections 3.01 through 3.03 of this revenue procedure. However, taxpayers do not need to wait until the instructions are published to apply this revenue procedure.[47]

---

[44] Revenue Procedure 2021-48, November 18, 2021

[45] Revenue Procedure 2021-48, November 18, 2021

[46] Revenue Procedure 2021-48, November 18, 2021

[47] Revenue Procedure 2021-48, November 18, 2021

Partnerships

Revenue Procedure 2021-49,[48] issued at the same time as Revenue Procedure 2021-48, provides guidance for partnerships regarding allocation of amounts excluded from gross income and deductions relating to PPP loan programs and certain other COVID relief programs. Specifically, the Procedure applies to:

- A partnership that
  - Received a PPP Loan; and
  - Received partial or complete forgiveness of the PPP Loan such that, in accordance with § 7A(i) of the Small Business Act, or §§ 276(b) or 278(a)(1) of the COVID Tax Relief Act, as applicable, the forgiveness amount is not included in the gross income of the eligible recipient, entity, or borrower.
- A partnership for which the SBA made payments with respect to a covered loan under § 1112(c) of the CARES Act.
- A partnership that received an Emergency EIDL Grant, a Targeted EIDL Advance, or a Shuttered Venue Operator Grant.
- A partnership that received a Supplemental Targeted EIDL Advance.
- A partnership that received a Restaurant Revitalization Grant.[49]

The Procedure provides the following protection for partnerships that follow this procedure:

> If a Covered Taxpayer that is a partnership satisfies all of the applicable requirements provided in section 4.02 of this revenue procedure, and complies with all information reporting requirements described in section 6 of this revenue procedure, the Internal Revenue Service (IRS) will treat the Covered Taxpayer's allocation of amounts treated as tax exempt income and allocation of deductions described in section 4.02(1), (2), (3), or (4) of this revenue procedure (as the case may be) as determined in accordance with § 704(b) of the Code. Under § 705(a) of the Code, a partner's basis in its interest is increased by the partner's distributive share of tax exempt income and is decreased by the partner's distributive share of deductions described in section 4.02(1), (2), (3), or (4) of this revenue procedure.[50]

[48] Revenue Procedure 2021-49, November 18, 2021

[49] Revenue Procedure 2021-49, November 18, 2021

[50] Revenue Procedure 2021-49, November 18, 2021

PPP Loans

A qualifying partnership will satisfy the requirements of this Procedure with regard to PPP loans if all of the following conditions are met:

- The allocation of deductions resulting from expenditures giving rise to the forgiveness of a PPP Loan is determined under § 1.704-1(b)(3), according to the partners' overall economic interests in the partnership.

- The allocation of amounts treated as tax exempt income under § 7A(i) of the Small Business Act, § 276(b) of the COVID Tax Relief Act, or § 278(a) of the COVID Tax Relief Act, as applicable, is made in accordance with the allocation of the deductions described in section 4.02(1)(a) of this revenue procedure.

- If any expenditure giving rise to the forgiveness of a PPP Loan is required to be capitalized under the Code (capitalized expenditure), the allocation of amounts treated as tax exempt income under § 7A(i) of the Small Business Act, § 276(b) of the COVID Tax Relief Act, or § 278(a) of the COVID Tax Relief Act, as applicable, is made in accordance with the allocation of the deemed loss, as provided in this section 4.02(1)(c), with respect to the capitalized expenditure's basis. Solely for purposes of this revenue procedure, the deemed loss with respect to the capitalized expenditure's basis is treated as a loss allowable as a deduction and is equal to the amount of loss that would be recognized if the property to which the capitalized expenditure relates were treated as disposed of in a fully taxable transaction for no consideration (hypothetical transaction) and, with respect to each partner, the allocation of the deemed loss associated with the capitalized expenditure's basis is determined under § 1.704-1(b)(3), according to the partners' overall economic interests in the partnership. The hypothetical transaction and resulting deemed loss are solely for purposes of determining the manner in which tax exempt income described in this section 4.02(1)(c) is allocated to the partnership's partners.[51]

Payments Made by the SBA for Covered Loans

A qualifying partnership will satisfy the requirements of this Procedure with regard to payments made by the SBA on applicable loans if all of the following conditions are met:

- The allocation of deductions resulting from payments of interest and fees described in § 1112(c) of the CARES Act is determined under § 1.704-1(b)(3), according to the partners' overall economic interests in the partnership.

- The allocation of amounts treated as tax exempt income under § 278(c) of the COVID Tax Relief Act attributable to interest and fees described in § 1112(c) of the CARES Act is made in accordance with the allocation of the deductions described in section 4.02(2)(a) of this revenue procedure.

- The allocation of amounts treated as tax exempt income under § 278(c) of the COVID Tax Relief Act attributable to payments of principal described in § 1112(c)

[51] Revenue Procedure 2021-49, November 18, 2021

of the CARES Act is made in accordance with each partner's share of the liability under § 752 of the Code and the regulations thereunder.

- If any expenditure related to the payment of interest and fees described in §1112(c) of the CARES Act is required to be treated as a capitalized expenditure, the allocation of amounts treated as tax exempt income under § 278(c) of the COVID Tax Relief Act is made in accordance with the allocation of the deemed loss, as described in section 4.02(1)(c) of this revenue procedure, with respect to the capitalized expenditure's basis. Upon the hypothetical transaction, the allocation of the deemed loss is determined under § 1.704-(1)(b)(3), according to the partners' overall economic interests in the partnership. The hypothetical transaction and resulting deemed loss are solely for purposes of determining the manner in which tax exempt income described in this section 4.02(2)(d) is allocated to the partnership's partners.[52]

Emergency EIDL Grant, Targeted EIDL Advance, or a Shuttered Venue Operator Grant

A qualifying partnership will satisfy the requirements of this Procedure with regard to Emergency EIDL Grants, Targeted EIDL Advances, or Shuttered Venue Operator Grants if all of the following conditions are met:

- The allocation of deductions resulting from the expenditure of proceeds of an Emergency EIDL Grant, a Targeted EIDL Advance, or a Shuttered Venue Operator Grant is determined under § 1.704-1(b)(3), according to the partners' overall economic interests in the partnership.

- The allocation of amounts treated as tax exempt income under § 278(b) and (d) of the COVID Tax Relief Act is made in accordance with the allocation of the deductions described in section 4.02(3)(a) of this revenue procedure.

- If any expenditure paid with the proceeds from an Emergency EIDL Grant, a Targeted EIDL Advance, or a Shuttered Venue Operator Grant is required to be treated as a capitalized expenditure, the allocation of amounts treated as tax exempt income under § 278(b) and (d) of the COVID Tax Relief Act is made in accordance with the allocation of the deemed loss, as described in section 4.02(1)(c) of this revenue procedure, with respect to the capitalized expenditure's basis. Upon the hypothetical transaction, the allocation of the deemed loss is determined under § 1.704-(1)(b)(3), according to the partners' overall economic interests in the partnership. The hypothetical transaction and resulting deemed loss are solely for purposes of determining the manner in which tax exempt income described in this section 4.02(3)(c) is allocated to the partnership's partners.

[52] Revenue Procedure 2021-49, November 18, 2021

Supplemental Targeted EIDL Advance or a Restaurant Revitalization Grant

A qualifying partnership will satisfy the requirements of this Procedure with regard to a Supplemental Targeted EIDL Advance or a Restaurant Revitalization Grant if all of the following conditions are met:

- The allocation of deductions resulting from the expenditure of proceeds of a Supplemental Targeted EIDL Advance or a Restaurant Revitalization Grant is determined under § 1.704-1(b)(3), according to the partners' overall economic interests in the partnership.

- The allocation of amounts treated as tax exempt income under §§ 9672 and 9673 of the ARP is made in accordance with the allocation of the deductions described in section 4.02(4)(a) of this revenue procedure.

- If any expenditure paid with the proceeds from a Supplemental Targeted EIDL Advance or a Restaurant Revitalization Grant is required to be treated as a capitalized expenditure, the allocation of amounts treated as tax exempt income under §§ 9672 and 9673 of the ARP is made in accordance with the allocation of the deemed loss, as described in section 4.02(1)(c) of this revenue procedure, with respect to the capitalized expenditure's basis. Upon the hypothetical transaction, the allocation of the deemed loss is determined under § 1.704-(1)(b)(3), according to the partners' overall economic interests in the partnership. The hypothetical transaction and resulting deemed loss are solely for purposes of determining the manner in which tax exempt income described in this section 4.02(4)(c) is allocated to the partnership's partners.

Reporting Requirements

Revenue Procedure 2021-49 concludes by providing:

> A Covered Taxpayer that is a partnership must report to the IRS all partnership items described in section 4 of this revenue procedure that the Commissioner of Internal Revenue or the Commissioner's delegate may require in forms, instructions, or other guidance.[53]

Consolidated Groups

Revenue Procedure 2021-49 provides the following information for consolidated groups with regard to such COVID-related income exclusions:

> With regard to a Covered Taxpayer that is a member of a consolidated group, the IRS will treat any amount excluded from gross income under § 7A(i) of the Small Business Act, § 276(b) of the COVID Tax Relief Act, or § 278(a)(1) of the COVID Tax Relief Act, as applicable, as tax exempt income for purposes of § 1.1502-32(b)(2)(ii). A Covered Taxpayer that is a member of a consolidated group may rely on the IRS treatment provided by this section 5 only if the consolidated group attaches a signed statement to its consolidated tax return

[53] Revenue Procedure 2021-49, November 18, 2021

> indicating that all Covered Taxpayers in the consolidated group are relying on this section 5 and reporting consistently.[54]

Amended Returns

The Revenue Procedure 2021-48 provides the following information about amended tax returns related to these timing issues for recognizing PPP loan forgiveness:

> Taxpayers may report tax-exempt income pursuant to section 3.01 on a timely filed original or amended Federal income tax return, information return or administrative adjustment request (AAR) under § 6227 of the Code.[55]

However, the Procedure notes that the IRS, at the same time as releasing Revenue Procedure 2021-48, also released Revenue Procedure 2021-50 which provides optional relief from the BBA Partnership Audit rules that would otherwise mandate the use of an AAR for a partnership that had not opted out of the BBA regime on their original returns:

> See also Revenue Procedure 2021-50, 2021-49 I.R.B. ____, released November 18, 2021, allowing an eligible partnership to file an amended Form 1065, *U.S. Return of Partnership Income*, as an alternative to filing an AAR, and furnish a corresponding amended Schedule K-1 (Form 1065), Partner's Share of Income, Deductions, Credits, etc., to each of its partners. Partners and shareholders that receive amended Forms K-1 as provided in this section 3.02 must file amended Federal income tax returns, information returns or AARs, as applicable, consistent with the Forms K-1 received.[56]

Revenue Procedure 2021-50 provides the following option to file an amended return in lieu of an AAR request for a qualifying BBA partnership (note the very short time period to file this amended return):

> BBA partnerships that filed a Form 1065 and furnished all required Schedules K-1 for taxable years ending after March 27, 2020 and did so prior to the issuance of this revenue procedure may file amended partnership returns and furnish corresponding amended Schedules K-1 on or before *December 31, 2021(emphasis added)*. The amended returns must take into account tax changes under Rev. Proc. 2021-48 or Rev. Proc. 2021-49, but eligible BBA partnerships under section 3.03 of this revenue procedure may make any additional changes on their amended returns.[57]

---

[54] Revenue Procedure 2021-49, November 18, 2021

[55] Revenue Procedure 2021-48, November 18, 2021

[56] Revenue Procedure 2021-48, November 18, 2021

[57] Revenue Procedure 2021-50, November 18, 2021, https://www.taxnotes.com/research/federal/irs-guidance/revenue-procedures/partnerships-pursuing-ppp-loan-forgiveness-benefits-may-amend-returns/7cm9q

These special rules are available only to BBA partnerships that filed Forms 1065 and furnished Schedules K-1 for the partnership taxable years ending after March 27, 2020 and prior to the issuance of Rev. Proc. 2021-48 or Rev. Proc. 2021-49 (November 18, 2021).

Additionally, to be eligible for the amended return filing and furnishing option, BBA partnerships must:

- Be within the scope of section 3 of Rev. Proc. 2021-49 and meet the requirements of section 4.02(1), 4.02(2), 4.02(3), or 4.02(4) of Rev. Proc. 2021-49 by filing an amended Form 1065 in accordance with procedures in section 6 of Rev. Proc. 2021-49, or

- Treat tax-exempt income resulting from the forgiveness of a PPP Loan, at a time described in section 3.01(1), (2) or (3) of Rev. Proc. 2021-48 by filing an amended Form 1065 in accordance with procedures in section 3.02 of Rev. Proc. 2021-48, as applicable.[58]

The Procedure provides that for purposes of the partner consistent reporting rules for BBA partnerships found at IRC §6222, "the amended return replaces any prior return (including any AAR filed by the partnership) for the taxable year for purposes of determining the partnership's treatment of partnership-related items."

Eligible tax years for this special amended return procedure are "any partnership taxable year ending after March 27, 2020 and prior to the issuance of Rev. Proc. 2021-48 and Rev. Proc. 2021-49."[59]

Filing an Amended Return in Lieu of an AAR

The Procedure provides the following method for filing amended returns in lieu of AARs for these purposes:

> To take advantage of the option to file an amended return provided by section 3 of this revenue procedure, a BBA partnership must file a Form 1065 (with the "Amended Return" box checked) and furnish corresponding amended Schedules K-1 to its partners. The BBA partnership must clearly indicate the application of this revenue procedure on the amended return and write "FILED PURSUANT TO REV PROC 2021-50" at the top of the amended return and attach a statement with each amended Schedule K-1 furnished to its partners with the same notation. The BBA partnership may file electronically or by mail but filing electronically may allow for faster processing of the amended return. The BBA partnership filing an amended return pursuant to this revenue procedure should not include any forms that are normally only filed with an AAR, such as Form 8985, *Pass-Through Statement-Transmittal/Partnership Adjustment Tracking Report (Required Under Sections 6226 and 6227)* or Form 8986, *Partner's Share of*

[58] Revenue Procedure 2021-50, November 18, 2021

[59] Revenue Procedure 2021-50, November 18, 2021

> *Adjustment(s) to Partnership-Related Item(s) (Required Under Sections 6226 and 6227).*[60]

If the BBA partnership's returns are under examination, the following provision applies:

> If a BBA partnership is currently under examination for a taxable year ending after March 27, 2020, and wishes to take advantage of the option to file an amended return provided by section 3 of this revenue procedure, the partnership may only do so if the partnership sends notice in writing to the revenue agent coordinating the partnership's examination that the partnership seeks to use the amended return option described in this revenue procedure prior to or contemporaneously with filing the amended return as described in section 4.01 of this revenue procedure. The partnership must also provide the revenue agent with a copy of the amended return and amended Schedules K-1 upon filing.[61]

If the BBA partnership has previously filed an AAR for the same taxable year, the following guidance applies:

> If a BBA partnership has previously filed an AAR and wishes to file an amended return pursuant to this revenue procedure for the same taxable year, the partnership should use the items as adjusted in the AAR, where applicable, in lieu of any reporting from the originally filed partnership return.[62]

If a passthrough-partner of the partnership filing an amended return in lieu of an AAR is itself also a BBA partnership, that partner can also file an amended return in lieu of an AAR but only for items included on the revised K-1 it received using the same procedures. The time limit to file an amended return of December 31, 2021 does not apply to this flow-through partner. These same relief rules apply to BBA partnerships that received an amended Schedule K-1 under any other previously issued revenue procedure allowing BBA partnerships to issue amended Schedules K-1.[63]

---

[60] Revenue Procedure 2021-50, November 18, 2021

[61] Revenue Procedure 2021-50, November 18, 2021

[62] Revenue Procedure 2021-50, November 18, 2021

[63] Revenue Procedure 2021-50, November 18, 2021