Current Federal Tax Developments

Week of September 7, 2020

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SECTION: 170
TAX COURT DENIES IRS ATTEMPT TO ARGUE CONTRIBUTION OF STOCK WAS A DISGUISED TAXABLE REDEMPTION FOLLOWED BY A CASH CONTRIBUTION

Citation: Dickinson v. Commissioner, TC Memo 2020-128, 9/3/20

In the case of *Dickinson v. Commissioner*[1] the IRS was attempting to treat a taxpayer's contribution of shares of stock directly to a charity as being rather a redemption of the stock, creating taxable capital gain, followed by a deductible charitable contribution.

In this case, the taxpayers donated shares in a privately held company in which the husband was the CFO to Fidelity Investments Charitable Gift Fund. The case notes:

> The GCI board of directors (Board) authorized shareholders to donate GCI shares to Fidelity Investments Charitable Gift Fund (Fidelity), an organization tax exempt under section 501(c)(3), through written consent actions in 2013 and 2014. In both consent actions the Board stated that Fidelity "has a donor advised fund program which incorporates procedures requiring * * * [Fidelity] to immediately liquidate the donated stock" and "seeks an imminent exit strategy and, therefore promptly tenders the donated stock to the issuer for cash". The Board approved a third round of donations at a Board meeting by unanimous vote in 2015; the Board members signed the written minutes of the meeting. After each Board authorization, petitioner husband donated appreciated GCI shares to Fidelity. Petitioner husband remained a full-time GCI employee following each donation.[2]

A taxpayer is allowed to deduct the fair market value of appreciated property donated to a charity that would have generated long term capital gain income if sold, but without having to recognize the long term capital gain income.[3] This creates a larger net deduction than would be achieved had the taxpayer sold the asset (triggering recognition of the gain) and then donated the cash proceeds to charity.

But the IRS objected that, in this case, the taxpayer knew when the donation was made that Fidelity would immediately sell the shares, so the transaction should be more properly viewed as a taxable redemption of the shares donated, followed by a donation of the cash proceeds.

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[1] *Dickinson v. Commissioner*, TC Memo 2020-128, September 3, 2020, https://www.ustaxcourt.gov/UstcInOp2/OpinionViewer.aspx?ID=12323 (retrieved September 3, 2020)

[2] *Dickinson v. Commissioner*, pp. 2-3

[3] See IRC §§170 and 61(3) and Reg. §1.170A-1(c)(1)

The Tax Court did not agree with the IRS's view of the transaction. The Court, citing *Humacid v. Commissioner*, 42 TC 894, 913 (1964) found that the form of the transaction as a contribution of the shares to Fidelity had to be respected if:

- The taxpayer has given away the property absolutely and parts with the title to the property and
- That gift takes place prior to when the property would give rise to income by way of a sale.[4]

The Court first looks to see if the taxpayer truly donated all of his rights in the stock to the charity. The Court finds that, despite the IRS's arguments, there was no question that the property was truly transferred to the charity:

> GCI's letters to Fidelity confirming ownership transfer, Fidelity's letters to petitioners explaining that Fidelity had "exclusive legal control" over the donated stock, and the LOUs to the same effect all support petitioners' claim that petitioner husband transferred all his rights in the shares. Respondent makes much of the fact that Fidelity regularly redeemed the GCI shares shortly after each donation, according to what the Board understood to be Fidelity's internal procedures. Respondent argues that these facts suggest petitioner husband, GCI, and Fidelity could have arranged the redemptions in advance of the gifts, but a preexisting understanding among the parties that the donee would redeem donated stock does not convert a postdonation redemption into a predonation redemption. *See Behrend*, 1972 WL 2627, at *3. Furthermore, neither a pattern of stock donations followed by donee redemptions, a stock donation closely followed by a donee redemption, nor selection of a donee on the basis of the donee's internal policy of redeeming donated stock suggests that the donor failed to transfer all his rights in the donated stock. *See, e.g., Grove v. Commissioner*, 490 F.2d at 242- 245 (respecting form of transaction where donee needed to fundraise to support its operations, and over a decade consistently redeemed annual donations of stock for which donor remained entitled to dividends); *Carrington v. Commissioner*, 476 F.2d at 705-706 (respecting form of transaction where donee redeemed stock eight days after it was donated); *Palmer v. Commissioner*, 62 T.C. 684, 692-693 (1974), (respecting form of transaction where, pursuant to a single plan, the taxpayer donated stock to a foundation and then caused the corporation to redeem the stock from the foundation the day after the donation), *aff'd*, 523 F.2d 1308 (8th Cir. 1975). Petitioners' contemporaneous documentary evidence of an absolute gift, and respondent's failure to assert facts indicating any genuine controversy on this point, lead us to conclude that petitioner husband's donations satisfy the first *Humacid* requirement.[5]

But even if there was an actual transfer of ownership, the transfer could still fail if the sale was already a *fait accompli*. That would serve as an impermissible assignment of

[4] *Dickinson v. Commissioner*, pp. 5-6

[5] *Dickinson v. Commissioner*, pp. 6-8

income, violating the second requirement under *Humacid*. As the Court notes, "*Humacid* prong two ensures that if stock is about to be acquired by the issuing corporation via redemption, the shareholder cannot avoid tax on the transaction by donating the stock before he receives the proceeds."[6]

For that to be the case, the Court finds the following has to be true:

> Where a donee redeems shares shortly after a donation, the assignment of income doctrine applies only if the redemption was practically certain to occur at the time of the gift, and would have occurred whether the shareholder made the gift or not. *See Palmer v. Commissioner*, 62 T.C. at 694-695; *see also Ferguson v. Commissioner*, 174 F.3d 997, 1003-1004 (9th Cir. 1999) (finding that the shareholder recognizes income from a stock sale where acquisition is "practically certain to occur", rather than the subject of "a mere anticipation or expectation", before the shareholder donates stock), aff'g 108 T.C. 244 (1997). In *Hudspeth v. United States*, 471 F.2d 275, 276 (8th Cir. 1972), for example, the court recast a stock donation as a taxable stock sale and donation of the sale proceeds where the taxpayer donated stock after the issuing corporation's directors and shareholders had adopted a plan of complete liquidation. *See also Jones v. United States*, 531 F.2d 1343, 1343-1344 (6th Cir. 1976); *Allen v. Commissioner*, 66 T.C. 340, 347 (1976).[7]

The Tax Court notes that the Ninth Circuit has gone further in its analysis of similar cases in a footnote to the above analysis:

> The Court of Appeals for the Ninth Circuit has gone a step further, asserting in dicta that stock sale proceeds are taxable to a shareholder who donates stock absent a binding obligation to sell if the facts and circumstances indicate that a tender offer and merger are "practically certain to proceed" in the immediate future. *See Ferguson v. Commissioner*, 174 F.3d 997, 1004 (9th Cir. 1999), *aff'g* 108 T.C. 244 (1997).[8]

But the Tax Court found this case was not of that sort, noting:

> By contrast, there was no assignment of income in *Palmer v. Commissioner*, 62 T.C. at 687-688, 695, even though all parties were related and anticipated the redemption before the donation, because "no vote for the redemption had yet been taken" when the shareholder donated the stock. As in Palmer, the redemption in this case was not a fait accompli at the time of the gift. As noted above, respondent argues that the parties may have prearranged for Fidelity to redeem the stock. Even if that was the case, it would not affect the analysis under the second *Humacid* requirement. Rather, we respect the

[6] *Dickinson v. Commissioner,* p. 8

[7] *Dickinson v. Commissioner,* p. 9

[8] *Dickinson v. Commissioner,* Footnote 2, p. 9

> form of the transaction because petitioner husband did not avoid receipt of redemption proceeds by donating the GCI shares.[9]

Basically, there was no income to assign—absent the contribution, the taxpayer was not going to receive cash in exchange for a portion of his shares. No buyer was sitting in the wings who was going to buy the shares in the near future regardless of the owner.

Of interest is the fact that the Court declined to follow the holding in Revenue Ruling 78-197 to decide the case, even though both parties referred the Court to it. In that ruling, the IRS, in announcing it would follow the *Palmer* decision noted earlier, held:

> The Service will treat the proceeds of a redemption of stock under facts similar to those in Palmer as income to the donor only if the donee is legally bound, or can be compelled by the corporation, to surrender the shares for redemption.[10]

The Court notes:

> This Court has not adopted Rev. Rul. 78-197, supra, as the test for resolving anticipatory assignment of income issues, *see Rauenhorst v. Commissioner*, 119 T.C. at 166, and does not do so today. The ultimate question, as noted in *Palmer*, is whether the redemption and the shareholder's corresponding right to income had already crystallized at the time of the gift. See Palmer v. Commissioner, 62 T.C. at 694-695. Regardless of whether the donee's obligation to redeem the stock may suggest the donor had a fixed right to redemption income at the time of the donation, *see Rauenhorst v. Commissioner*, 119 T.C. at 166-167, respondent does not allege that petitioner husband had any such right in this case. Accordingly, respondent's resort to Rev. Rul. 78-197, supra, is unavailing.

Thus, the Court concludes:

> As required by *Humacid* and its progeny, petitioner husband made an absolute gift of the GCI shares in each taxable year before the stock gave rise to income by way of a sale.[11]

Therefore, the taxpayer was not required to recognize as income a gain that would have resulted from a redemption of the donated shares immediately prior to the donation.

[9] *Dickinson v. Commissioner,* p. 9

[10] Rev. Rul. 78-197; 1978-1 C.B. 83

[11] *Dickinson v. Commissioner,* pp. 10-11

SECTION: 401
QUESTIONS AND ANSWERS ISSUED IN IRS NOTICE REGARDING SECURE ACT AND MINER'S ACT CHANGES TO RETIREMENT PROGRAMS

Citation: Notice 2020-68, 9/2/20

The SECURE Act, enacted in late 2019 by the Congress, provided for a number of changes to retirement plans and IRAs. In Notice 2020-68[12] the IRS has provided initial guidance on some of these changes in question and answer format. The Notice also covered plan related provisions found in the Bipartisan American Miner's Act of 2019 (Miners Act) that was enacted at the same time as the SECURE Act.

Business Credit for Automatic Contribution Arrangement (IRC §45T)

The law provides an income tax credit for an employer establishing an *eligible automatic contribution arrangement* (EACA). The Notice describes this credit as follows:

> Section 105 of the SECURE Act amends the Internal Revenue Code (Code) to add new § 45T, which provides a business credit under § 38 of the Code for an eligible employer that establishes an eligible automatic contribution arrangement under a qualified employer plan. The credit is equal to $500 for any taxable year of an eligible employer that occurs during a credit period. Under § 45T(b)(2), a taxable year is not treated as occurring during a credit period unless the arrangement is included in the plan for the taxable year. Under § 105(d) of the SECURE Act, the new credit applies to taxable years beginning after December 31, 2019.[13]

The Notice clarifies that an employer can only receive a credit for single three-year period.

> Q. A-1: May an eligible employer receive a credit with respect to taxable years in more than one 3-year credit period?
>
> A. A-1: No. An eligible employer may receive a credit for taxable years only during a single 3-year credit period that begins when the employer first includes an EACA in any qualified employer plan. [14]

The Q&A provides two examples of applying this provision:

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[12] Notice 2020-68, September 2, 2020, https://www.irs.gov/pub/irs-drop/n-20-68.pdf (retrieved September 3, 2020)

[13] Notice 2020-68, Section A

[14] Notice 2020-68, Section A

EXAMPLE 1, NOTICE 2020-68, SECTION A, Q&A-1

For example, if an eligible employer, Employer W, first includes an EACA in one of its qualified employer plans, Plan A, during Employer W's 2021 taxable year (so that the 2021, 2022, and 2023 taxable years included in Employer W's 3-year credit period are all taxable years after § 45T is applicable), and also includes an EACA in a second qualified employer plan, Plan B, during the 2022, 2023, and 2024 taxable years, Employer W may receive no more than a $500 credit for each taxable year during the 3-year credit period that begins with the 2021 taxable year and is not permitted to receive the credit for the 2024 taxable year. [15]

EXAMPLE 2, NOTICE 2020-68, SECTION A, Q&A-1

As another example, if a different eligible employer, Employer X, first included an EACA in one of its qualified employer plans, Plan C, during Employer X's 2018 taxable year (so that the only taxable year included in Employer X's 3-year credit period after § 45T is applicable is 2020) and also includes an EACA in a second qualified employer plan, Plan D, during the 2020, 2021, and 2022 taxable years, Employer X may receive only a $500 credit for the 2020 taxable year and no credit for subsequent taxable years.[16]

The employer must continue to use the same EACA for the following two years to get any available credits for those years.

> Q. A-2: To be eligible for the § 45T credit for the second or third taxable years of an eligible employer's 3-year credit period that begins when the eligible employer first includes an EACA in a qualified employer plan, must the eligible employer include the same EACA in the same plan in that second or third taxable year?
>
> A. A-2: Yes. [17]

The IRS provides the following example as part of the Notice, which explains a method for having a second plan spun out to carry on an EACA rather than creating a new plan and terminating the EACA in the first plan which would bar claiming the credit from that point forward.

EXAMPLE 1, NOTICE 2020-68, SECTION A, Q&A-2

For example, if an eligible employer, Employer Y, first includes an EACA in one of its qualified employer plans, Plan E, for its 2021 taxable year, amends Plan E to remove the EACA from Plan E during its 2022 taxable year, and includes an EACA in another qualified employer plan, Plan F, during its 2023 taxable year, Employer Y will not be eligible for the § 45T credit for its 2023 taxable year.

If, however, rather than amending Plan E to remove the EACA during the 2022 taxable year, Employer Y spun-off a portion of Plan E and continued to include the EACA in the spun-off portion of Plan E during its 2022 and 2023 taxable years, Employer Y would be treated as

[15] Notice 2020-68, Section A

[16] Notice 2020-68, Section A

[17] Notice 2020-68, Section A

continuing to maintain the same EACA in the same plan for those taxable years and would be eligible for the credit for those taxable years.[18]

This tax credit applies separately to each employer involved in a multiple employer plan.

> Q. A-3: Does the § 45T credit apply separately to each eligible employer that participates in a multiple employer plan (MEP) under § 413(c)?
>
> A. A-3: Yes. The § 45T credit applies to an eligible employer that participates in a MEP in the same way that the credit would apply if each employer participating in the MEP were the sponsor of a single-employer plan maintained by the eligible employer. Thus, each employer that is an eligible employer (after application of the rules in Notice 98-4 under which certain related employers are treated as a single employer) generally would be eligible for the credit for the 3-year credit period beginning with the first taxable year in which the eligible employer's participating employees are first covered by an EACA under the MEP.[19]

The Notice provides the following example of the application of the credit in an MEP setting.

EXAMPLE 1, NOTICE 2020-68, SECTION A, Q&A-3

For example, if an eligible employer, Employer Z, had not previously maintained a plan that included an EACA, and a MEP, Plan G, first includes an EACA that covers Employer Z's participating employees during the 2020 taxable year, the 3-year credit period consisting of the 2020, 2021, and 2022 taxable years would apply to Employer Z.

In addition, Employer Z would continue to be eligible for the credit for the 2021 and 2022 taxable years if Plan G spun off the assets attributable to Employer Z to Plan H, a single-employer plan maintained by Employer Z, and Employer Z continued to include an EACA in Plan H for the 2021 and 2022 taxable years.[20]

Contributions to a Traditional Individual Retirement Account After Age 70 ½ (Repeal of Prior IRC §219(d)(1))

The SECURE Act eliminated the bar on contributions to traditional IRAs beginning with the tax year the taxpayer attained age 70 ½. The law also added a special provision that applied to any taxpayer who made such a contribution and then later makes a qualified charitable distribution (QCD) from a traditional IRA that barred the treatment of the contribution as a QCD until the distributions exceeded the prior post 70 ½ contributions.

[18] Notice 2020-68, Section A

[19] Notice 2020-68, Section A

[20] Notice 2020-68, Section A

The Q&As provide first that a financial institution is not required to accept post 70 ½ contributions to an IRA the agency is custodian for:

> Q. B-1: Is a financial institution that serves as trustee, issuer, or custodian for an IRA (financial institution) required to accept post-age 70½ contributions in 2020 or subsequent taxable years?
>
> A. B-1: No. A financial institution is not required to accept post-age 70½ contributions. However, a financial institution may choose to accept post-age 70½ contributions beginning on a date after December 31, 2019, as selected by the financial institution.[21]

However, if a financial institution does accept such contributions, the IRA contracts of the institution will need to be amended to allow for such contributions.

> Q. B-2: If a financial institution chooses to accept post-age 70½ contributions, must the financial institution amend its IRA contracts to provide for those contributions, and if so, what is the deadline for the amendment?
>
> A. B-2: Yes. A financial institution that chooses to accept post-age 70½ contributions must amend its IRA contracts to provide for those contributions. See Q&A G-1 of this notice for the deadline for a financial institution to amend its IRA contracts. The IRS expects to issue revised model IRAs and prototype language addressing changes made to the relevant Code provisions under the SECURE Act.[22]

The revised contract will have to be distributed to each benefitted individual.

> Q. B-3: If a financial institution chooses to amend an IRA contract to accept post-age 70½ contributions, must the financial institution distribute a copy of the amendment and a new disclosure statement to each benefited individual?
>
> A. B-3: Yes. If a financial institution chooses to amend an IRA contract to accept post-age 70½ contributions, the financial institution must update the disclosure statement that is required under § 408(i) to reflect the contents of the amended IRA and must distribute copies of the amendment and the amended disclosure statement to each benefited individual. Section 1.408-6(d)(4)(ii)(c) provides that the financial institution must deliver or mail the copies to the last known address of the benefited individual not later than the 30th day after the later of the date on which the amendment is adopted or the date it becomes effective.[23]

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[21] Notice 2020-68, Section B

[22] Notice 2020-68, Section B

[23] Notice 2020-68, Section B

The IRA beneficiary is not allowed to offset the distribution with the IRA contribution when reporting on their tax return for the year in question.

> Q. B-4: May an individual offset the amount of required minimum distributions for a taxable year from the individual's IRA by the amount of post-age 70½ contributions for the same taxable year?
>
> A. B-4: No. An individual may not offset the amount of required minimum distributions from the individual's IRA by the amount of post-age 70½ contributions for the same taxable year. Contributions and distributions are each separate transactions and are independently reported by the financial institution to the IRS.[24]

Section B concludes with Q&A B-5 that provides the following example of the reduction of the excludable amount of qualified charitable distributions caused by a deduction of post-age 70½ contributions

EXAMPLE, NOTICE 2020-68, SECTION B, Q&A-5

An individual who turned age 70½ before 2020 deducts $5,000 for contributions for each of 2020 and 2021 but makes no contribution for 2022. The individual makes no qualified charitable distributions for 2020 and makes qualified charitable distributions of $6,000 for 2021 and $6,500 for 2022.

The excludable amount of qualified charitable distributions for 2021 is the $6,000 of qualified charitable distributions reduced by the $10,000 aggregate amount of post-age 70½ contributions for 2021 and earlier taxable years. For this individual, these amounts are $5,000 for each of 2020 and 2021, resulting in no excludable amount of qualified charitable distributions for 2021 (that is, $6,000 - $10,000 = ($4,000)).

The excludable amount of the qualified charitable distributions for 2022 is the $6,500 of qualified charitable distributions reduced by the portion of the $10,000 aggregate amount of post-age 70½ contributions deducted that did not reduce the excludable portion of the qualified charitable distributions for earlier taxable years. Thus, $6,000 of the aggregate amount of post-age 70½ contributions deducted does not apply for 2022 because that amount has reduced the excludable amount of qualified charitable distributions for 2021. The remaining $4,000 of the aggregate amount of post-age 70½ contributions deducted reduces the excludable amount of any qualified charitable distributions for subsequent taxable years. Accordingly, the excludable amount of the qualified charitable distributions for 2022 is $2,500 ($6,500 - $4,000 = $2,500).

As described above, because the $4,000 amount reduced the excludable amount of qualified charitable distributions for 2022, that $4,000 amount does not apply again in later years, and

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[24] Notice 2020-68, Section B

no amount of post-age 70½ contributions remains to reduce the excludable amount of qualified charitable distributions for subsequent taxable years.[25]

§401(k) Plan Mandatory Coverage of Long-Term Part Time Employees (IRC §401(k)(2)(D))

The SECURE Act requires §401(k) plans to offer limited participation to employees who have more than 500 hours of service in three preceding years. The rule takes effect for years beginning after December 31, 2020, but for purposes of handling the 500-hour test to require participation, 12-month periods beginning before January 1, 2021 are not taken into account.[26]

As a practical matter, this means the provision will first serve to require certain part time employees to be offered limited participation in plan years beginning after January 1, 2024.

The special rules excluding periods beginning before January 1, 2021 for allowing these employees into the plan do not apply to also exclude those periods from the revised vesting calculations of this provision. The IRS provides in the single Q&A for this provision:

> Q. C-1: Does the exception in § 112(b) of the SECURE Act that excludes 12-month periods beginning before January 1, 2021, from being taken into account for purposes of the special eligibility rule in § 401(k)(2)(D)(ii) of the Code also apply for purposes of the special vesting rules in § 401(k)(15)(B)(iii) of the Code?
>
> A. C-1: No. Generally, all years of service with the employer or employers maintaining the plan must be taken into account for purposes of determining a long-term, part-time employee's nonforfeitable right to employer contributions under the special vesting rules in § 401(k)(15)(B)(iii).
>
> Section 401(k)(15)(B)(iii) provides that, for purposes of determining whether a long-term, part-time employee has a nonforfeitable right to employer contributions (other than elective deferrals) under the arrangement, each 12-month period for which the employee has at least 500 hours of service is treated as a year of service.
>
> Section 411(a)(4) generally requires that all years of service with the employer or employers maintaining the plan be taken into account for purposes of determining an employee's nonforfeitable right to employer contributions, subject to certain exceptions. Those exceptions include, for example, years of service before the employee attains age 18 (see § 411(a)(4)(A)).
>
> Section 112(b) of the SECURE Act excludes 12-month periods beginning before January 1, 2021, for purposes of determining a long-

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[25] Notice 2020-68, Section B

[26] Notice 2020-68, Section C

> term, part-time employee's eligibility to participate under § 401(k)(2)(D)(ii) of the Code. However, § 112(b) of the SECURE Act does not exclude 12-month periods beginning before January 1, 2021, for purposes of determining a long-term, part-time employee's nonforfeitable right to employer contributions under § 401(k)(15)(B)(iii) of the Code. Therefore, unless a long-term, part-time employee's years of service may be disregarded under § 411(a)(4), all years of service with the employer or employers maintaining the plan must be taken into account for purposes of determining the long-term, part-time employee's nonforfeitable right to employer contributions under § 401(k)(15)(B)(iii), including 12-month periods beginning before January 1, 2021.

Qualified Birth or Adoption Expense Distributions from IRAs and Qualified Retirement Plans (IRC §72(t))

The SECURE Act added a new provision to §72 dealing with distributions made within one year of the birth of the taxpayers' child or the taxpayers' adoption of a child. The Notice describes this provision as follows:

> Section 113 of the SECURE Act amended § 72(t)(2) of the Code to add a new exception to the 10% additional tax for any qualified birth or adoption distribution. Section 72(t)(2)(H) permits an individual to receive a distribution from an applicable eligible retirement plan of up to $5,000 without application of the 10% additional tax if the distribution meets the requirements to be a qualified birth or adoption distribution. An applicable retirement plan is defined in § 72(t)(2)(H)(vi)(I) as an eligible retirement plan described in § 402(c)(8)(B) other than a defined benefit plan. A qualified birth or adoption distribution is includible in gross income, but is not subject to the 10% additional tax under § 72(t)(1). A qualified birth or adoption distribution is defined as any distribution from an applicable eligible retirement plan to an individual if made during the 1-year period beginning on the date on which the child of the individual is born or the legal adoption by the individual of an eligible adoptee is finalized.
>
> An individual generally may recontribute a qualified birth or adoption distribution (not to exceed the aggregate amount of all qualified birth and adoption distributions made to the individual from the plan) to an applicable eligible retirement plan in which the individual is a beneficiary and to which a rollover can be made. However, a qualified birth or adoption distribution is not treated as an eligible rollover distribution for purposes of the direct rollover rules of § 401(a)(31), the notice requirement under §402(f), or the mandatory withholding rules under § 3405. The Treasury Department and the IRS intend to issue regulations under § 72(t) that will address the recontribution rules, including rules related to the timing of recontributions.[27]

[27] Notice 2020-68, Section D

The IRS divides up this section into two portions, one aimed at individuals receiving a distribution and the other dealing with qualified plans looking to add such a provision.

Individuals Receiving a Qualified Birth or Adoption Distribution

The IRS begins by defining what qualifies for this type of distribution.

> Q. D-1: What is a qualified birth or adoption distribution?
>
> A. D-1: A qualified birth or adoption distribution, as defined in § 72(t)(2)(H)(iii)(I), is any distribution of up to $5,000 from an applicable eligible retirement plan to an individual if made during the 1-year period beginning on the date on which the child of the individual is born or the legal adoption by the individual of an eligible adoptee is finalized.
>
> Q. D-2: Are there any additional requirements for a distribution to be a qualified birth or adoption distribution?
>
> A. D-2: Yes. Section 72(t)(2)(H)(vi)(III) provides that a distribution to an individual will not be treated as a qualified birth or adoption distribution with respect to any child or eligible adoptee unless the individual includes the name, age, and the Taxpayer Identification Number (TIN) of the child or eligible adoptee on the individual's tax return for the taxable year in which the distribution is made.[28]

The types of retirement plans eligible to provide such a distribution are listed in Q&A D-3:

> Q. D-3: Which types of plans are eligible to permit a qualified birth or adoption distribution?
>
> A. D-3: A qualified birth or adoption distribution may be made from an applicable eligible retirement plan, which is defined in § 72(t)(2)(H)(vi)(I) as an eligible retirement plan described in § 402(c)(8)(B), other than a defined benefit plan. Therefore, a § 401(a) qualified defined contribution plan, a § 403(a) annuity plan, a § 403(b) annuity contract, a governmental § 457(b) plan, or an IRA is eligible to permit a qualified birth or adoption distribution.[29]

[28] Notice 2020-68, Section D

[29] Notice 2020-68, Section D

The qualified birth or adoption distribution is exempted from the 10% early distribution tax under IRC §72(t):

> Q. D-4: Is a qualified birth or adoption distribution subject to the 10% additional tax under § 72(t)?
>
> A. D-4: No. While a qualified birth or adoption distribution is includible in gross income, it is not subject to the 10% additional tax under § 72(t)(1).[30]

Note that the distribution is subject to tax unless the balance is recontributed. While the law provides no limit on the time during which a recontribution may be made, unless the amounts are recontributed before the statute of limitations for claiming a refund for the year of distribution expires, the taxpayer would be unable to get a refund of the taxes paid.

The IRS provides information on who is an eligible adoptee in questions 5 and 6:

> Q. D-5: Who is an eligible adoptee?
>
> A. D-5: Section 72(t)(2)(H)(iii)(II) defines the term "eligible adoptee" as any individual who has not attained age 18 or is physically or mentally incapable of self-support. However, an eligible adoptee does not include an individual who is the child of the taxpayer's spouse.
>
> Q. D-6: For purposes of determining who is an eligible adoptee, when is an individual considered "physically or mentally incapable of self-support?"
>
> A. D-6: For purposes of § 72(t)(2)(H)(iii)(II), the determination of whether an individual is physically or mentally incapable of self-support is made in the same manner as the determination of whether an individual is disabled under § 72(m)(7), which defines when an individual is disabled for purposes of the exception to the 10% additional tax under § 72(t)(2)(A)(iii). Section 72(m)(7) provides that an individual is considered to be disabled if that individual is unable to engage in any substantial gainful activity by reason of any medically determinable physical or mental impairment that can be expected to result in death or to be of long-continued and indefinite duration.[31]

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[30] Notice 2020-68, Section D

[31] Notice 2020-68, Section D

The limitation on the amount of the distribution applies on both a per parent and per child basis.

> Q. D-7: May each parent receive a qualified birth or adoption distribution up to $5,000 with respect to the same child or eligible adoptee?
>
> A. D-7: Yes. Each parent may receive a qualified birth or adoption distribution of up to $5,000 with respect to the same child or eligible adoptee.
>
> Q. D-8: May an individual receive qualified birth or adoption distributions with respect to multiple births of children or adoptions of eligible adoptees (for example, twins or triplets)?
>
> A. D-8: Yes. An individual is permitted to receive qualified birth or adoption distributions with respect to the birth of more than one child or the adoption of more than one eligible adoptee if the distributions are made during the 1-year period following the date on which the children are born or the legal adoption for the eligible adoptees is finalized.

EXAMPLE BASED ON NOTICE 2020-68, SECTION D, Q&AS 7 AND 8

Employee A gives birth to twins in October 2020. Employee A takes a $10,000 distribution from her § 401(k) plan in January 2021. The entire $10,000 distribution is a qualified birth or adoption distribution, assuming that Employee A includes the TINs of her twins and other required information on her 2021 tax return.

Employee A's spouse is also allowed to take a $10,000 distribution from a qualified retirement plan, subject to the same requirements as apply to Employee A. So the couple will be able to take total distributions of up to $20,000 for the birth of twins.[32]

Finally, the IRS addresses the recontribution issue in Q&A 9:

> Q. D-9: May an individual recontribute a qualified birth or adoption distribution to an applicable eligible retirement plan?
>
> A. D-9: Yes. An individual may recontribute any portion of a qualified birth or adoption distribution (up to the entire amount of the qualified birth or adoption distribution) to an applicable eligible retirement plan in which the individual is a beneficiary and to which a rollover can be made under § 402(c), 403(a)(4), 403(b)(8), 408(d)(3), or 457(e)(16), as applicable.[33]

[32] Notice 2020-68, Section D

[33] Notice 2020-68, Section D

Eligible Retirement Plans and Qualified Birth or Adoption Distributions

The IRS provides additional guidance to those maintaining plans that are eligible to make such distributions.

First, the IRS notes that a plan is *not required* to offer these qualified birth or adoption distributions:

> Q. D-10: Is an applicable eligible retirement plan required to permit in-service distributions for qualified birth or adoption distributions under § 72(t)(2)(H)?
>
> A. D-10: No. It is optional for an applicable eligible retirement plan to permit in-service distributions for qualified birth or adoption distributions pursuant to § 72(t)(2)(H). Plan amendments adopted to permit qualified birth or adoption distributions are discretionary amendments for purposes of the plan amendment rules discussed in Q&A G-1 of this notice.[34]

As well, a plan wishing to offer such an option will be required to amend the plan to allow for these distributions:

> Q. D-11: If an employer chooses to amend its applicable eligible retirement plan to permit in-service distributions for qualified birth or adoption distributions, what is the deadline for adopting that amendment?
>
> A. D-11: For information relating to the deadline for adopting plan amendments, see Q&A G-1 of this notice.[35]

The IRS provides that a plan is generally allowed to accept the participant's representation that the participant is eligible for such a distribution.

> Q. D-12: May a plan sponsor or plan administrator rely on a reasonable representation from an individual that the individual is eligible for a qualified birth or adoption distribution?
>
> A. D-12: Yes. In making a determination whether an individual is eligible for a qualified birth or adoption distribution, a plan sponsor or plan administrator of an applicable eligible retirement plan is permitted to rely on reasonable representations from the individual, unless the plan sponsor or plan administrator has actual knowledge to the contrary.[36]

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[34] Notice 2020-68, Section D

[35] Notice 2020-68, Section D

[36] Notice 2020-68, Section D

Plans that allow for such distributions are also required to accept recontributions:

> Q. D-13: If an applicable eligible retirement plan permits qualified birth or adoption distributions, is the plan required to accept a recontribution of that distribution to the plan?
>
> A. D-13: Yes. An applicable eligible retirement plan must accept the recontribution of a qualified birth or adoption distribution from an individual if the following apply:
>
>> (a) the plan permits qualified birth or adoption distributions;
>>
>> (b) the individual received a qualified birth or adoption distribution from that plan; and
>>
>> (c) the individual is eligible to make a rollover contribution to that plan at the time the individual wishes to recontribute the qualified birth or adoption distribution to the plan.

As will be noted later, a participant may still be allowed to treat a distribution allowed under another provision of the plan as a qualified birth or adoption distribution. But if the plan does not provide separately for qualified birth or adoption distributions, it would not need to accept the recontribution of the distribution that was treated by the employee as a qualified birth or adoption distribution, though the employee could deposit the funds in an IRA to complete the repayment.

The guidance also provides that such distributions are treated as allowed distributions for purposes of various plan qualification provisions:

> Q. D-14: Do qualified birth or adoption distributions from an applicable eligible retirement plan meet the distribution restriction requirements in §§ 401(k)(2)(B)(i), 403(b)(7)(A)(i), 403(b)(11), and 457(d)(1)(A)?
>
> A. D-14: Qualified birth or adoption distributions are treated as meeting the distribution restrictions for qualified cash or deferred arrangements under §401(k)(2)(B)(i), custodial accounts under § 403(b)(7)(A)(i), annuity contracts under §403(b)(11), and governmental deferred compensation plans under § 457(d)(1)(A). Thus, for example, an employer may expand the distribution options under its plan to allow an amount attributable to an elective, qualified nonelective, qualified matching, or safe harbor contribution under a § 401(k) plan to be distributed as a qualified birth or adoption distribution even though it is distributed before an otherwise permitted distributable event, such as severance from employment, disability, or attainment of age 59½.[37]

The IRS indicates that the distribution is not going to trigger a number of rules that apply to qualified plans when an otherwise qualified rollover distribution is made,

[37] Notice 2020-68, Section D

including having no requirement for the withholding of tax from the distribution by the plan:

> Q. D-15: Is a qualified birth or adoption distribution treated by an applicable eligible retirement plan as an eligible rollover distribution for purposes of the direct rollover rules, § 402(f) notice requirements, and the mandatory withholding rules?
>
> A. D-15: No. A qualified birth or adoption distribution is not treated as an eligible rollover distribution for purposes of the direct rollover rules of § 401(a)(31), the notice requirement under § 402(f), and the mandatory withholding rules under § 3405. Thus, the plan is not required to offer an individual a direct rollover with respect to a qualified birth or adoption distribution. In addition, the plan administrator is not required to provide a § 402(f) notice. Finally, the plan administrator or payor of the qualified birth or adoption distribution is not required to withhold an amount equal to 20% of the distribution, as generally is required in § 3405(c)(1). However, a qualified birth or adoption distribution is subject to the voluntary withholding requirements of § 3405(b) and § 35.3405-1T.[38]

When a participant recontributes the distribution to the plan or IRA, the plan or IRA will treat that as a direct transfer within 60 days of the distribution (even though the recontribution will almost certainly be far past the 60 day time period):

> Q. D-16: Is a recontribution made with respect to a qualified birth or adoption distribution from an applicable eligible retirement plan other than an IRA treated as the direct transfer of an eligible rollover distribution as defined in § 402(c)(4)?
>
> A. D-16: Yes. Section 72(t)(2)(H)(v)(III) provides that, in the case of a recontribution made with respect to a qualified birth or adoption distribution from an applicable eligible retirement plan other than an IRA, an individual is treated as having received the distribution as an eligible rollover distribution (as defined in § 402(c)(4)) and as having transferred the amount to an applicable eligible retirement plan in a direct trustee-to-trustee transfer within 60 days of the distribution.
>
> Q. D-17: Is a recontribution made with respect to a qualified birth or adoption distribution from an IRA treated as the direct transfer of an eligible rollover distribution as defined in § 408(d)(3)?
>
> A. D-17: Yes. Section 72(t)(2)(H)(v)(IV) provides that, in the case of a recontribution made with respect to a qualified birth or adoption distribution from an IRA, an individual is treated as having received the distribution as an eligible rollover distribution (as defined in § 408(d)(3)) and as having transferred the amount to an applicable

[38] Notice 2020-68, Section D

> eligible retirement plan in a direct trustee-to-trustee transfer within 60 days of the distribution.[39]

The Q&A also provides a potential workaround for participants in plans that do not provide for qualified birth and adoption distributions. If the participant has the right to an in-service distribution from the plan and takes that distribution, the participant is allowed to treat that distribution as a qualified birth or adoption distribution. The participant also can later recontribute that balance back to an IRA even if the plan it came from won't accept such recontributions.

> Q. D-18: If an applicable eligible retirement plan does not permit qualified birth or adoption distributions, may an individual treat an otherwise permissible in-service distribution as a qualified birth or adoption distribution?
>
> A. D-18: Yes. If an applicable eligible retirement plan does not permit qualified birth or adoption distributions and an individual receives an otherwise permissible in-service distribution that meets the requirements of a qualified birth or adoption distribution, the individual may treat the distribution as a qualified birth or adoption distribution on the individual's federal income tax return. The distribution, while includible in gross income, is not subject to the 10% additional tax under § 72(t)(1). If the individual decides to recontribute the amount to an eligible retirement plan, the individual may recontribute the amount to an IRA.[40]

Difficulty of Care Payments as the Basis for a Retirement Plan Contribution (IRC §§408(o)(5) and 415(c)(8))

The SECURE Act dealt with the use of difficulty of care payments to fund a retirement plan. As the Notice describes the issue:

> A difficulty of care payment is a type of qualified foster care payment that is excludable from gross income under § 131. Because a difficulty of care payment is excludable from gross income, it was not, prior to the SECURE Act, included in a participant's compensation for purposes of calculating the annual additions limit of § 415(c)(1). Accordingly, an employee who received difficulty of care payments from an employer was not permitted to make contributions to, or receive allocations under, the employer's plan based on the difficulty of care payments.[41]

The applicable SECURE Act changes are detailed in the Notice as follows:

> Section 116(a) of the SECURE Act adds § 408(o)(5) to the Code to allow a taxpayer to elect to increase the nondeductible contribution limit by the amount of excludable difficulty of care payments in a

[39] Notice 2020-68, Section D

[40] Notice 2020-68, Section D

[41] Notice 2020-68, Section E

> situation in which the taxpayer does not have sufficient compensation that is includible in the taxpayer's gross income to equal the deductible amount under § 219(b)(5) of the Code. The addition of § 408(o)(5) applies to contributions made after December 20, 2019.
>
> Section 116(b) of the SECURE Act adds § 415(c)(8) to the Code to increase the annual additions limit for retirement plans to include difficulty of care payments. Section 415(c)(8)(A), as amended, provides that a participant's compensation for purposes of § 415(c)(1) is increased by the amount of excludable difficulty of care payments. Accordingly, a participant may make contributions to, or receive allocations under, the plan that are based on the participant receiving difficulty of care payments, even if the participant has no other compensation. Section 415(c)(8)(B), as amended, provides that if a contribution is made based on difficulty of care payments, the contribution is treated as investment in the contract and will not cause a plan to be treated as failing any requirements of §§ 1 through 1400Z-2 solely by reason of allowing the contribution. The addition of § 415(c)(8) applies to plan years beginning after December 31, 2015.[42]

While the amount may be added to the §415(c)(1) compensation amount of an employer plan to increase the annual additions limit, the amount will not be considered compensation unless the amount is paid by the employer:

> Q. E-1: Are difficulty of care payments received by an employee from a person other than his or her employer includible in the definition of compensation under that employer's plan?
>
> A. E-1: No. Compensation under § 415(c)(3) only includes compensation from an individual's employer. Thus, difficulty of care payments received by an employee from a person other than his or her employer are not includible in the definition of compensation under that employer's plan.[43]

Generally, a plan will not be amended to include such payments in §415(c)(1) compensation unless the employer is paying or begins paying such payments to employees.

> Q. E-2: If an employer does not make difficulty of care payments to its employees that are eligible to participate in the employer's plan, must the plan be amended to include difficulty of care payments in the plan's definition of § 415(c)(1) compensation?
>
> A. E-2: No. If an employer does not make difficulty of care payments to its employees that are eligible to participate in the employer's plan, then the plan does not need to be amended to include difficulty of care payments in the plan's definition of §415(c)(1) compensation. However, if the employer changes its practice and begins to make

[42] Notice 2020-68, Section E

[43] Notice 2020-68, Section E

> difficulty of care payments to its employees, the plan must be amended timely to include difficulty of care payments in that definition.[44]

Interestingly, the IRS declines to provide an answer at this time to the question of whether the excise tax on excess contributions under §4973 is applicable to nondeductible IRA contributions based on difficulty of care payments:

> Q. E-3: Does the excise tax on excess IRA contributions under § 4973 apply to nondeductible IRA contributions that are based on difficulty of care payments?
>
> A. E-3: The applicability of the excise tax on excess IRA contributions under §4973 to nondeductible IRA contributions that are based on difficulty of care payments will be addressed in future guidance.[45]

Reduction of Minimum Age for In-Service Distributions to 59 ½ (IRC §401(a)(36)

The Miner's Act was also part of the package of bills passed as the Further Consolidated Appropriations Act, 2020 along with the SECURE Act. While the SECURE Act was the location for the vast majority of retirement plan provisions, one new provision applicable to qualified retirement plans was found at Section 104 of the Miner's Act.

The Notice describes the change, which reduces the minimum age at which a plan may permit in-service distributions from age 62 (or 70 ½ for §457 plans) to age 59 ½, as follows:

> Under § 401(a)(36), a pension plan does not fail to be qualified solely because the plan provides that a distribution may be made from the plan to an employee who has attained a minimum age and who is not separated from employment at the time of the distribution (generally referred to as an in-service distribution). Prior to the effective date of the Miners Act, the minimum age for allowable in-service distributions under §401(a)(36) was age 62. Section 104(a) of the Miners Act lowers the minimum age from age 62 to age 59½.
>
> In order to be an eligible deferred compensation plan under § 457(b), a plan must satisfy the distribution requirements of § 457(d). Section 457(d)(1)(A) provides that amounts under the plan may not be made available earlier than the occurrence of certain events. Prior to the enactment of the Miners Act, § 457(d)(1)(A)(i) provided, in general, that amounts may not be made available to participants earlier than the calendar year in which a participant attains age 70½ or when a participant has a severance from employment with the employer. Section 104(b) of the Miners Act amended § 457(d)(1)(A)(i) of the Code to provide that, in the case of a governmental plan under § 457(b) of the Code (that is, a plan maintained by an employer that is a

[44] Notice 2020-68, Section E

[45] Notice 2020-68, Section E

> State, a political subdivision of a State, or any agency or instrumentality of a State or political subdivision of a State, as provided in § 457(e)(1)(A) of the Code), amounts may be made available as early as the calendar year in which a participant attains age 59½.[46]

These changes apply to plan years beginning after December 31, 2019.[47]

These changes are not ones that a plan is required to implement. Q&A 1 of Section F provides:

> Q. F-1: Is a plan qualified under § 401(a) of the Code (qualified plan) or a governmental plan under § 457(b) of the Code required to implement the changes made by § 104 of the Miners Act?
>
> A. F-1: No. In general, neither a qualified plan nor a § 457(b) governmental plan is required to provide for in-service distributions. Thus, if a plan does not provide for in-service distributions, or provides for in-service distributions at an age that is later than age 59½ (the minimum age permitted by § 104(a) or (b) of the Miners Act), the plan is not required to be amended to permit in-service distributions to commence at age 59½.

EXAMPLE, NOTICE 2020-68, SECTION F, Q&A 1

A qualified plan that provides for in-service distributions commencing at age 62 is not required to be amended to provide for in-service distributions commencing at age 59½.[48]

The IRS provides the following guidance in response to the question of whether a pension plan that lowers its minimum age for an in-service distribution to age 59 ½ may also change its definition of normal retirement age to the same age or higher, but lower than age 62. Essentially, the answer is that an employer cannot simply assume that an age lower than 62 will not cause an issue with plan qualification.

> Q. F-2: If a pension plan is amended to lower its minimum age for an in-service distribution from age 62 to age 59½ pursuant to § 401(a)(36), may the plan also change its definition of normal retirement age to age 59½ or later without violating other qualification requirements, such as the definitely determinable benefit requirement in § 1.401(a)-1(b)(1)(i)?
>
> A. F-2: The in-service distribution rule in § 401(a)(36) is separate from the definitely determinable benefit requirement in § 1.401(a)-1(b)(1)(i). A plan does not fail to satisfy the requirements in § 1.401(a)-1(b)(1)(i) merely because the plan provides for in-service distributions in accordance with § 401(a)(36). In addition to satisfying other applicable qualification requirements (such as § 411(d)(6)), any change to a pension plan's definition of normal retirement age must satisfy the requirements in § 1.401(a)-1(b)(2), including the requirement that a

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[46] Notice 2020-68, Section F

[47] Notice 2020-68, Section F

[48] Notice 2020-68, Section F

> normal retirement age must be an age that is not earlier than the earliest age that is reasonably representative of the typical retirement age for the industry in which the covered workforce is employed. A normal retirement age of age 62 or later is deemed to satisfy the reasonably representative requirement (see § 1.401(a)-1(b)(2)(ii)). For purposes of the reasonably representative requirement, governmental pension plans may continue to rely on proposed regulations that were published in the Federal Register on January 27, 2016 (81 FR 4599).[49]

Plan Amendments With Regard to These Provisions

The guidance ends with a Q&A regarding the dates that a plan must be amended to comply with the SECURE Act and §104 of the Miner's Act:

> Q. G-1: When must a retirement plan be amended to reflect the provisions of the SECURE Act, the regulations thereunder, or § 104 of the Miners Act?
>
> A. G-1: The deadlines to amend a retirement plan for provisions of the SECURE Act, the regulations thereunder, or § 104 of the Miners Act are set forth in this Q&A G-1. These amendment deadlines apply to both required and discretionary plan amendments.
>
> **(a) Qualified plans**
>
> In general, for a qualified plan that is not a governmental plan within the meaning of § 414(d) of the Code, or an applicable collectively bargained plan, the deadline to amend a plan for provisions of the SECURE Act, the regulations thereunder, or § 104 of the Miners Act is the last day of the first plan year beginning on or after January 1, 2022. The plan amendment deadline for a qualified governmental plan, as defined in § 414(d), or for an applicable collectively bargained plan, is the last day of the first plan year beginning on or after January 1, 2024.
>
> A sponsor of a qualified plan may amend its plan to reflect the SECURE Act, the regulations thereunder, or § 104 of the Miners Act after the dates set forth in the preceding paragraph, in accordance with Rev. Proc. 2016-37, as modified by Rev. Proc. 2017-41 and Rev. Proc. 2020-40. However, under Rev. Proc. 2016-37, amendments made after the dates set forth in the preceding paragraph, are not entitled to the anti-cutback relief provided by § 411(d)(6) of the Code or § 204(g) of ERISA.
>
> **(b) Section 403(b) plans**
>
> In general, the deadline for a § 403(b) plan that is not maintained by a public school, as described in § 403(b)(1)(A)(ii), to amend a plan for provisions of the SECURE Act or the regulations thereunder is the

[49] Notice 2020-68, Section F

last day of the first plan year beginning on or after January 1, 2022. The plan amendment deadline for a § 403(b) plan that is maintained by a public school, as described in § 403(b)(1)(A)(ii), is the last day of the first plan year beginning on or after January 1, 2024.

A sponsor of a § 403(b) plan may be entitled to amend its plan to reflect the SECURE Act or the regulations thereunder after the dates set forth in the preceding paragraph, in accordance with Rev. Proc. 2019-39, as modified by Notice 2020-35 and Rev. Proc. 2020-40. However, under Rev. Proc. 2019-39, amendments to a § 403(b) plan that is subject to ERISA that are made after the dates set forth in the preceding paragraph are not entitled to the anti-cutback relief provided by § 204(g) of ERISA.

(c) Section 457(b) governmental plans

The deadline to amend a governmental plan under § 457(b) of the Code for provisions of the SECURE Act, the regulations thereunder, or § 104 of the Miners Act is the later of (i) the last day of the first plan year beginning on or after January 1, 2024, or (ii) if applicable, the first day of the first plan year beginning more than 180 days after the date of notification by the Secretary that the plan was administered in a manner that is inconsistent with the requirements of § 457(b) of the Code.

(d) Individual retirement plans

The deadline to amend the trust governing an IRA that is an individual retirement account or the contract issued by an insurance company with respect to an IRA that is an individual retirement annuity for provisions of the SECURE Act or the regulations thereunder is December 31, 2022, or such later date as the Secretary prescribes in guidance.

In the case of a deemed IRA described in § 408(q), the deadline to amend the deemed IRA provisions is the deadline applicable to the plan under which the deemed IRA is established.[50]

SECTION: 3101
DRAFT FORM 941 ISSUED TO ADD LINE TO DEAL WITH PAYROLL TAX HOLIDAY EMPLOYEE OASDI TAX DEFERRAL

Citation: Form 941 for 2020: Employer's QUARTERLY Federal Tax Return (DRAFT), 8/28/20

The IRS, following the release of guidance on the payroll tax holiday set to begin on September 1, 2020 in Notice 2020-65, has now released a draft version of a revised

[50] Notice 2020-68, Section F

Form 941 to take into account the employee old age, survivor and disability insurance withholding that is deferred from September 1 to December 31.[51]

The key change is found on page 3 in Part 3, line 24, which asks for the "Deferred amount of the employee share of social security tax included in line 13b." Line 13b on page 1 currently has the deferred *employer* portion of social security taxes under the CARES Act, so the line on page 1 will be used to cover both types of deferred social security taxes, while line 24 will alert the IRS to the portion of the total deferral that must be paid in by May 1, 2021.

Part 3: Tell us about your business. If a question does NOT apply to your business, leave it blank.

DRAFT AS OF August 28, 2020 DO NOT FILE

17	If your business has closed or you stopped paying wages . . . . ☐ Check here, and enter the final date you paid wages / / ; also attach a statement to your return. See instructions.		
18	If you're a seasonal employer and you don't have to file a return for every quarter of the year . . . ☐ Check here.		
19	Qualified health plan expenses allocable to qualified sick leave wages	19	.
20	Qualified health plan expenses allocable to qualified family leave wages	20	.
21	Qualified wages for the employee retention credit	21	.
22	Qualified health plan expenses allocable to wages reported on line 21	22	.
23	Credit from Form 5884-C, line 11, for this quarter	23	.
24	Deferred amount of the employee share of social security tax included on line 13b . . .	24	.
25	Reserved for future use	25	.

As of the time this was written just before 1:00 pm MST on August 29, 2020, the IRS had not yet posted the draft instructions for this version of the Form 941. Those instructions may, like the instructions for second quarter 941 revision that outlined instructions for handling the employer old age, survivor and disability insurance deferral, confirm that employers can "opt-out" from participating in this deferral program.

[51] Form 941 for 2020: Employer's QUARTERLY Federal Tax Return (DRAFT), August 28, 2020 https://www.irs.gov/pub/irs-dft/f941--dft.pdf (retrieved August 29, 2020)

SECTION: 3121
MINISTER FINDS THAT CHURCH WAS NOT REQUIRED TO AND HAD NOT WITHHELD FICA AND HE THUS FAILS TO QUALIFY FOR FICA OR MEDICARE

Citation: Hermann Kuma v. Greater New York Conference of Seventh-Day Adventist Church et al, USDC SD NY, Case No. 1:19-cv-0848, 8/28/20

In the case of *Hermann Kuma v. Greater New York Conference of Seventh-Day Adventist Church et al.*[52] a former pastor was suing a church for failing to classify him as an employee and withhold FICA and Medicare taxes on the wages he was paid over a 21 year period.

Mr. Kuma was told when he attempted to apply for Social Security benefits that he did not have enough quarters of coverage on his account to qualify for benefits or to be eligible for Medicare. Mr. Kuma claimed that the church had treated him improperly as an independent contractor, causing him to face the loss of benefits under Social Security and Medicare and was looking to be awarded damages in compensation.

But Mr. Kuma faced a problem. Even if he was correct that the church had improperly treated him as an independent contractor, something the court did not specifically rule on, that would not have created his problem.

While generally employers are required to withhold and pay FICA taxes on wages paid to employees (see IRC §3111(a)), IRC §3121(b)(8)(A) specifically excludes from FICA withholding or the payment of employer FICA the "service performed by a duly ordained, commissioned, or licensed minister of a church in the exercise of his ministry or by a member of a religious order in the exercise of duties required by such order,…"

Rather, such ministers are subject to self-employment tax under IRC §1402(a)(8), unless they have been granted an exemption from the tax (for instance, pursuant to IRC §1402(e)(1)). Note that an exemption under §1402(e)(1) would have also resulted in Mr. Kuma being ineligible for the benefits as he would also lack sufficient quarters of coverage.

Thus, Mr. Kuma as either an employee minister or an independent contractor should have reported his income as self-employment income under IRC §1402(a), paying the self-employment tax that would have qualified him for the benefits he now finds he is unable to obtain. The church had acted properly in not withholding and paying FICA taxes on Mr. Kuma's earnings for those 21 years.

[52] *Hermann Kuma v. Greater New York Conference of Seventh-Day Adventist Church et al.*, USDC SD NY, Case No. 1:19-cv-0848

SECTION: 6221
WEB PAGE PROVIDING IRS GUIDANCE FOR BBA CENTRALIZED PARTNERSHIP AUDIT REGIME PUBLISHED BY THE AGENCY

Citation: "BBA Centralized Partnership Audit Regime," IRS website, 9/1/20

The IRS has established a web page on the agency's site devoted to the BBA Centralized Partnership Audit Regime.[53]

The page is meant to provide a centralized location for the agency's information and guidance on the new audit regime introduced by the Bipartisan Budget Act of 2015, which replaces the prior TEFRA partnership audit regime.

The sections of guidance found on the page are:

- Filing Requirements;
- BBA Partnership Audit notices;
- Regulations for the BBA audits; and
- Interim Guidance for the BBA audits.

The page concludes with a high level comparison table:

Partnership Procedures	TEFRA	BBA
Partnership point of contact for examination	Tax Matters Partner	Partnership Representative
Partner participation rights during examination	Partners have the ability to participate in the examination and challenge partnership adjustments	Partners have no participation right to challenge partnership adjustment

[53] "BBA Centralized Partnership Audit Regime," IRS website, September 1, 2020 https://www.irs.gov/businesses/partnerships/bba-centralized-partnership-audit-regime (retrieved September 2, 2020)

Partnership Procedures	TEFRA	BBA
Partner consistency of reporting	Partners must report items consistently with the partnership	Partners must report items consistently with the partnership
Notice requirements	Notice requirements (NBAP, FPAA)	Notice requirements (NAP, NOPPA, FPA)
Items adjusted during examination	Partnership item/Affected item	Partnership related item (PRI)
Where adjustments/assessments occur	Adjustments at the partnership level/tax assessment at the partner level	Adjustment and assessment at the partnership level (imputed underpayment)
Distinct phases of examination	Field examination	Field examination phase
	Not applicable	Modification phase (optional)
	FPAA phase	FPA phase
	Not applicable	Push-out phase (optional)