

Current Federal Tax Developments

Week of February 8, 2021

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ACCOUNTING
CONTINUING EDUCATION

CURRENT FEDERAL TAX DEVELOPMENTS
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Kaplan Financial Education

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SECTION: 61

IRS REVISES INSTRUCTIONS TO VIRTUAL CURRENCY QUESTION, BUT NOT ACTUAL QUESTION, CREATING UNCERTAINTY ON WHAT ANSWER IS APPROPRIATE IN SOME CASES

Citation: 1040 and 1040-SR Instructions, 1/6/2021

The final 1040 instructions seem to suggest that an “acquisition of a financial interest in a virtual currency” may not be an “acquisition of an interest in a virtual currency” in some cases for purposes of answering the first question to be answered on Form 1040 after the taxpayer’s identifying information and address. But the instructions don’t provide any information on how such non-acquisition acquisitions are to be identified.

In the final version of the Form 1040 Instructions¹ the IRS modified the list of reportable virtual currency transactions, eliminating certain items found in the December 31, 2020 draft version, but the question on the Form 1040 remained unchanged—and still suggests, at least to some, that the deleted items would still be reportable.

Just below the address block on the 2020 Form 1040 is the following question related to virtual currency:

At any time during 2020, did you receive, sell, send, exchange, or otherwise acquire any financial interest in any virtual currency?²

In a set of draft Form 1040 instructions released on December 31 the IRS noted that a transaction involving virtual currency includes, but is not limited to, certain examples. Two of the listed examples were:

- A *purchase* or sale of virtual currency and
- An *acquisition* or disposition of a financial interest in a virtual currency.³

Thus, the instructions provided, in those cases the question would be answered with a yes.

A week later the final version of the instructions was released and the references to a purchase or acquisition in the example transactions were omitted. However, the question on the front page of the Form 1040 continued to ask if the taxpayer had otherwise acquired “any financial interest in any virtual currency.”

¹ 1040 and 1040-SR Instructions, January 6, 2021, <https://www.irs.gov/pub/irs-pdf/i1040gi.pdf> (retrieved February 6, 2021)

² 2020 Form 1040, p. 1

³ Draft 1040 and 1040-SR Instructions, December 31, 2020, p. 16

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Since purchasing a currency seems to be an acquisition of a financial interest in the currency and, even more clearly, an acquisition of a financial interest in a virtual currency would be an acquisition of a financial interest in a virtual currency, it wasn't clear what, if anything, was changing due to this revision of the instructions.

But the IRS seems to be taking the position that they did remove items from the types of transactions that would require answering "yes" to the question.

In an article published in the February 8, 2021 issue of *Tax Notes Today Federal*, an IRS spokesperson is quoted as saying that "[i]f the only activity someone has is a purchase/acquire and hold, then they don't have to check the box."⁴

However, as Zhanna A. Ziering of Caplin & Drysdale Chtd. was quoted as observing in the article, the answer appears to be at odds with the plain language of the question on the Form 1040.⁵

Likely the IRS is trying to figure out how to ask for transactions that would have a tax impact, ignoring those that don't, but at this point the question remains broad in scope—and nowhere does the IRS explicitly state that only a taxable transaction should lead to a yes answer to that question.

SECTION: 62 SAFE HARBOR PROVIDED FOR EDUCATOR'S COVID-19 PROTECTIVE ITEMS ELIGIBLE FOR AN ABOVE-THE-LINE DEDUCTION

Citation: Revenue Procedure 2021-15, 2/4/21

The COVID-related Tax Relief Act of 2020 Section 275 required the IRS to "clarify" that COVID-19 Protective Items used by an educator for the prevention of the spread of COVID-19 will qualify as an item allowed to be treated as an expense in calculating the above the line deduction (not in excess of \$250) for qualified educators under IRC §62(a)(2)(D). In Revenue Procedure 2021-15⁶ provides a safe harbor educators may use to claim these expenses.

The Procedure describes the deduction in question as follows:

Section 62 of the Code sets forth the deductions an individual may deduct from gross income in arriving at adjusted gross income. Section 62(a)(2)(D) provides, in part, that deductions allowed under § 162 not

⁴ Kristen A. Parillo, "Final Crypto Instructions May Send Mixed Signals," *Tax Notes Today Federal*, February 8, 2021, 2021 TNTF 25-5, <https://www.taxnotes.com/tax-notes-today-federal/cryptocurrency/final-crypto-instructions-may-send-mixed-signals/2021/02/08/2r46r> (retrieved February 6, 2021, subscription required)

⁵ Kristen A. Parillo, "Final Crypto Instructions May Send Mixed Signals," *Tax Notes Today Federal*, February 8, 2021, 2021 TNTF 25-5, <https://www.taxnotes.com/tax-notes-today-federal/cryptocurrency/final-crypto-instructions-may-send-mixed-signals/2021/02/08/2r46r> (retrieved February 6, 2021, subscription required)

⁶ Revenue Procedure 2021-15, February 4, 2021, <https://www.irs.gov/pub/irs-drop/rp-21-15.pdf> (retrieved February 4, 2021)

in excess of \$250 (\$500 if married filing jointly and both spouses are eligible educators, but not more than \$250 each) that consist of unreimbursed expenses described in § 62(a)(2)(D)(ii) that are paid or incurred by an eligible educator may be deducted in arriving at gross income. The unreimbursed expenses described in § 62(a)(2)(D)(ii) are those paid or incurred by an eligible educator in connection with books, supplies (other than nonathletic supplies for courses of instruction in health or physical education), computer equipment (including related software and services), other equipment, and supplementary materials used by the eligible educator in the classroom.⁷

The Revenue Procedure provides the following safe harbor to be used in determining if an item represents a COVID-19 Protective Item eligible to be considered under this provision for a deduction:

In accordance with section 275 of the COVID Tax Relief Act, an eligible educator may treat unreimbursed expenses paid or incurred after March 12, 2020, for COVID-19 Protective Items that are, or will be, used by that eligible educator for the prevention of the spread of COVID-19 in the classroom, as expenses that are described in § 62(a)(2)(D)(ii) and allowable as a deduction under § 62(a)(2)(D), subject to the aggregate dollar limitation provided in such provision. For purposes of this revenue procedure, COVID-19 Protective Items include, but are not limited to: face masks; disinfectant for use against COVID-19; hand soap; hand sanitizer; disposable gloves; tape, paint or chalk used to guide social distancing; physical barriers (for example, clear plexiglass); air purifiers; and other items recommended by the Centers for Disease Control and Prevention (CDC) to be used for the prevention of the spread of COVID-19.⁸

The Procedure applies to unreimbursed expenses paid or incurred by the eligible educator after March 12, 2020.⁹

SECTION: 125 EMPLOYEE MAY NOT RECEIVE REFUND OF UNUSED DEPENDENT CARE FSA FUNDS AS PANDEMIC RELIEF DOES NOT ALLOW GIVING A REFUND

Citation: INFO 2020-0027, 12/31/20

While the IRS published relief that sponsors could give to participants in their cafeteria plans in Notice 2020-29 for 2020 plan years, and the Congress provided additional relief in §214 of the Taxpayer Certainty and Disaster Relief Act of 2020, not all

⁷ Revenue Procedure 2021-15, Section 2.01

⁸ Revenue Procedure 2021-15, Section 3

⁹ Revenue Procedure 2021-15, Section 4

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situations are eligible for relief that will make the participant whole. One such situation was discussed in IRS Information Letter 2020-0027.¹⁰

The letter was written to respond to a constituent of Rep. Madeleine Dean of Pennsylvania who found themselves out funds that had been directed by them into a dependent care flexible spending account in their employer's cafeteria plan.

The memorandum notes that Rep. Dean's constituent:

...explained that he will have unused amounts in his dependent care flexible spending arrangement (FSA) under a Section 125 cafeteria plan because his children did not attend summer camp due to COVID-19 and he does not expect to have additional childcare expenses during 2020.¹¹

Rep. Dean's constituent was asking if the unused funds could be repaid to him, noting that he was aware that relief had been granted during the year to allow the suspension of amounts being deferred into the program.

The IRS had to inform the constituent that the relief he sought wasn't available. The letter noted:

As * * * noted, the IRS provided relief in Notice 2020-29 to allow, but not require, an employer to amend a Section 125 cafeteria plan to give employees increased flexibility to make mid-year election changes to their dependent care FSAs during 2020 on a prospective basis. However, this relief does not modify the rule that an employee's contributions to a dependent care FSA cannot be returned other than as reimbursements for dependent care expenses. This also applies to contributions the employee made before a mid-year election change. See Proposed Treas. Reg. § 1.125-5(i)(3).¹²

The letter also noted that any payments had to be limited to reimbursement of dependent care expenses that are employment related.¹³ Presumably the author was concerned about the nature of the camp payments and if they truly would meet the requirements for employment related dependent care—they might, but then again they might not.

This letter, while released on December 31, 2020 in redacted form, was sent to Rep. Dean in September. Since then Congress did provide relief that might (or might not) help in this situation—but it would not result in a refund.

Section 214 of the Taxpayer Certainty and Disaster Relief Act of 2020, enacted as part of the Consolidated Appropriations Act, 2021, allows cafeteria plans to be modified to allow carryover of unused health care or dependent care flexible spending account

¹⁰ INFO 2020-0027, December 31, 2020, <https://www.irs.gov/pub/irs-wd/20-0027.pdf> (retrieved February 6, 2021)

¹¹ INFO 2020-0027, December 31, 2020

¹² INFO 2020-0027, December 31, 2020

¹³ INFO 2020-0027, December 31, 2020

balances into the following year for plan years ending in 2020 or 2021. As well, the Taxpayer Certainty and Disaster Relief Act of 2020 §214(d)(1) and (2) provides potential relief in cases where the child would “age out” of the dependent care benefit in the following year, giving limited relief from the age restriction for those unused funds.

SECTION: 6041

IRS REMOVES INFORMATION RETURN REPORTING FOR CAA TAX EXEMPT RELIEF AND ADDS THREATENED PENALTIES FOR FAILURE TO REVISE ALREADY ISSUED FORMS ON SBA LOAN PAYMENTS

Citation: Notice 2021-6 and Announcement 2021-2, 2/1/21

The IRS has released guidance providing that certain information forms should not be filed that relate to items made tax exempt by the COVID-related Tax Relief Act of 2020,¹⁴ as well as directing institutions that had already issued Forms 1099MISC related to payments made by the SBA on loans to file amended information returns¹⁵ that contained an implied threat that those that fail to update those forms in a timely manner will face potential penalties.

Information Return Relief

The IRS had provided guidance in Announcement 2020-12 prior to the passage of the COVID-related Tax Relief Act of 2020 that provided that Forms 1099C for relief of indebtedness should not be issued for PPP loan forgiveness as CARES Act §1106(i) had provided such relief would not be subject to tax.¹⁶

The COVID-related Tax Relief Act expanded the tax exempt treatment to cover a number of other relief programs enacted both under the CARES Act and in the various provisions found in the overall Consolidated Appropriations Act, 2021. The Act also provided that the IRS was granted the authority to provide an exemption from certain information return requirements:

Section 279 of the COVID Relief Act authorizes the Secretary of the Treasury or the Secretary's delegate to provide an exception from any requirement to file an information return otherwise required under chapter 61 of the Code with respect to any amount excluded from

¹⁴ Notice 2021-6, January 19, 2021, <https://www.taxnotes.com/research/federal/irs-guidance/notices/reporting-requirement-waived-for-some-excluded-amounts/2l6h5> (retrieved February 2, 2021)

¹⁵ Announcement 2021-2, February 1, 2021, <https://www.taxnotes.com/research/federal/irs-guidance/announcements/some-lenders-will-need-to-file-corrected-forms-1099-misc/2r3p4> (retrieved February 2, 2021)

¹⁶ Announcement 2020-12, September 22, 2020, <https://www.taxnotes.com/research/federal/irs-guidance/announcements/irs-forgives-information-reporting-for-ppp-loans%20%a0/2czjj> (retrieved February 2, 2021)

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gross income by reason of section 7A(i) of the Small Business Act or sections 276(b), 277, or 278 of the COVID Relief Act.¹⁷

The IRS in Notice 2021-6 made use of that authority to provide the following relief:

Under the authority provided by section 279 of the COVID Relief Act, the Treasury Department and the IRS waive the requirement to file information returns or furnish payee statements as described in the following list:

1. Original PPP covered loan forgiveness. A lender is not required to file with the IRS, or furnish to a borrower, a Form 1099-C reporting forgiveness of PPP covered loans under section 7A(i) of the Small Business Act as redesignated, transferred, and amended by the Economic Aid Act.
2. PPP II covered loan forgiveness. A lender is not required to file with the IRS, or furnish to a borrower, a Form 1099-C reporting forgiveness of PPP II covered loans under section 311 of the Economic Aid Act.
3. Student emergency financial aid grants. A grantor is not required to file with the IRS, or furnish to a student, a Form 1099-MISC, Miscellaneous Information, reporting the payment of an emergency grant to the student under section 3504, 18004, or 18008 of the CARES Act or another emergency financial aid grant described in section 277(b)(3) of the COVID Relief Act made to students in response to qualifying emergencies.
4. Treasury Program loan forgiveness. A lender is not required to file with the IRS, or furnish to a borrower, a Form 1099-C reporting forgiveness of loans under section 1109 of the CARES Act.
5. EIDL grants. The Administrator is not required to file with the IRS, or furnish to a recipient, a Form 1099-MISC reporting the payment of an advance under section 1110(e) of the CARES Act or a grant under section 331 of the Economic Aid Act.
6. Loan subsidies. Neither the Administrator nor a lender is required to file with the IRS, or furnish to a borrower, a Form 1099-MISC reporting the payment of principal, interest, and any associated fees through a loan subsidy authorized under section 1112(c) of the CARES Act.
7. Shuttered venue operator grants. The Administrator is not required to file with the IRS, or furnish to a recipient, a Form

¹⁷ Notice 2021-6, Section II

1099-MISC reporting the payment of a grant to a shuttered venue operator under section 324(b) of the Economic Aid Act.¹⁸

The Notice limits its relief to items covered in the COVID-related Tax Relief Act and does not eliminate the need to file other information returns:

The waivers of information reporting requirements described in section III of this notice apply only to requirements to file and furnish Form 1099 series information returns and payee statements for the described grants, payments, subsidies, or loan forgiveness, which are excluded from gross income. The waivers do not affect any requirements to file and furnish other forms, such as forms in the 1098 series. For example, the waiver does not apply to the requirement to file and furnish Form 1098-T, Tuition Statement, with respect to any payments received for qualified tuition and related expenses, including qualified tuition and related expenses paid with grants described in this notice.¹⁹

Interest Paid by the SBA Under CARES Act §1112

The guidance also contains a clarification regarding the reporting of interest paid by the Small Business Administration under CARES Act §1112, noting that such interest *is deductible by the borrower* and such interest should be reported on any Forms 1098 the lender is required to file:

Because borrowers may deduct mortgage interest that the Small Business Administration (SBA) paid to lenders under section 1112 of the CARES Act, lenders may include those mortgage interest payments in Box 1 of Form 1098, Mortgage Interest Statement, notwithstanding § 1.6050H-1(e)(3)(ii) of the Income Tax Regulations. The payments should be included on both the Form 1098 that is filed with the IRS and the copy that is furnished to borrowers. Including this interest on Form 1098 will inform borrowers of the total amount of mortgage interest they may deduct. In addition, this reporting will avoid discrepancies between interest reported to the IRS and interest claimed as a deduction by borrowers on their income tax returns.²⁰

This also contains a “suggestion” to lenders that if they had filed Forms 1098 omitting this interest that a corrected Form 1098 should be filed.

The filing of information returns with the IRS omitting mortgage interest that the SBA paid to lenders under section 1112 of the CARES Act could result in the issuance of underreporter notices (IRS Letter CP2000) to eligible recipients who correctly deduct that interest. Lenders who are unable to furnish by February 1, 2021, a Form 1098 to a borrower that includes mortgage interest that the SBA paid to

¹⁸ Notice 2021-6, Section III

¹⁹ Notice 2021-6, Section IV

²⁰ Notice 2021-6, Section IV

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lenders under section 1112 of the CARES Act may furnish a corrected Form 1098 including this interest in box 1. Lenders are encouraged to do so as promptly as possible.²¹

Requirement to Amend Certain Information Returns

The IRS may have concluded that some payors were treating Notice 2021-6's relief to be a voluntary bit of guidance, and that they could continue to simply issue 1099s the way they previously planned to, avoiding having to reprogram systems that generate such filings for the payor.

In Announcement 2021-2 the IRS made it clear that for at least one set of information returns, the IRS does not see compliance with the relief found in Notice 2021-6 as being optional. While the language for the Forms 1098 suggested lenders "may" furnish corrected Forms 1098 and encouraged them to do so as soon as possible, the IRS when looking at 1099-MISC forms issued for the SBA's payment of certain loans issued more direct language mandating a fix.

The Announcement begins as follows:

This announcement notifies lenders who have filed with the Internal Revenue Service (IRS), or furnished to a borrower, a Form 1099-MISC, *Miscellaneous Information*, reporting certain payments on loans subsidized by the Administrator of the U.S. Small Business Administration (Administrator) as income of the borrower that the lenders must file and furnish corrected Forms 1099-MISC that exclude these subsidized loan payments.²²

The IRS provides the following mandate in the Announcement:

If a lender has already furnished to borrowers Forms 1099-MISC that report these loan payments, whether before, on, or after December 27, 2020, the lender must furnish to the borrowers corrected Forms 1099-MISC that exclude these loan payments. In addition, if a lender has already filed with the IRS Forms 1099-MISC that report these loan payments, whether before, on, or after December 27, 2020, the lender must file with the IRS corrected Forms 1099-MISC that exclude these loan payments. Directions for how to file corrected Forms 1099-MISC are included in the 2020 Instructions for Forms 1099-MISC and 1099-NEC and the 2020 General Instructions for Certain Information Returns.²³

²¹ Notice 2021-6, Section IV

²² Announcement 2021-2

²³ Announcement 2021-2

And just in case a lender is tempted to ask what happens if they don't send out the corrections, the IRS threatens lenders who fail to promptly file corrected forms with penalties.

If a lender described in this announcement furnishes corrected payee statements within 30 days of the furnishing deadline, it will have reasonable cause for any failure-to-furnish penalty imposed under section 6722. A lender described in this announcement must file corrected information returns by the filing deadline in order to avoid section 6721 failure-to-file penalties.²⁴

While the Announcement is limited to the Form 1099-MISC forms for these SBA payments, presumably the same logic that would allow the IRS to penalize a lender for failing to revise those forms could be applied for the other forms that Notice 2021-6 revised the reporting on.

²⁴ Announcement 2021-2