



ACCOUNTING

CONTINUING EDUCATION

2024 Current Federal Tax Developments

(CFTD)

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(CFTD)



2024 CURRENT FEDERAL TAX DEVELOPMENTS(CFTD)

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Published in 2024 by Kaplan Financial Education.

Printed in the United States of America.

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ISBN: 978-1-0788-4441-3

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Unit 1

Tax Cuts and Jobs Act Expiring Provisions

LEARNING OBJECTIVES

After completing this unit, you will be able to:

- List the key provisions of the Tax Cuts and Jobs Act that will leave the law at the end of 2025 or shortly thereafter
- Using the cost of extending or not extending various provisions and various other factors, help clients understand issues that may cause provisions to be extended or not extended by Congress.

Traditionally we start the Current Federal Tax Developments course out with a dive into the key legislation Congress passed in the current or just preceding year. But the 118th Congress has the distinction of not being able to pass any significant legislation during its term that began on January 3, 2023, and is set to end on January 3, 2025. So, the biggest legislative issue that impacts current tax practice is trying to determine what, if anything, the 119th Congress will do about the large number of provisions in the Tax Cuts and Jobs Act that will expire at the end of 2025.

Now that we are at the very end of 2024, it's a good time to review the Tax Cuts and Jobs Act provisions which are scheduled to expire at the end of 2025 if no action is taken by Congress to extend them. A complete outline of the provisions can be found in the November 2023 Congressional Research Service publication *Reference Table: Expiring Provisions in the "Tax Cuts and Jobs Act"* (TCJA, P.L. 115-97).¹ In this unit we'll briefly highlight some of the more significant items scheduled to disappear from the law when we enter 2026.

The projected cost or revenue raising score for each provision calculated by the Congressional Budget Office (CBO) is provided, as these amounts may become a consideration in determining which of these provisions will be successfully extended and which will be allowed to expire as scheduled.

¹ Congressional Research Service, *Reference Table: Expiring Provisions in the "Tax Cuts and Jobs Act"* (TCJA, P.L. 115-97), November 21, 2023, <https://crsreports.congress.gov/product/pdf/R/R47846>

INDIVIDUAL PROVISIONS

Many of the changes made to individual tax provisions in the 2017 Act terminate at the end of 2025, restoring the pre-TCJA law to take effect in 2026. Some of those key items are:

- Individual tax rates will revert to the old law levels of 10%, 15%, 25%, 28%, 33%, 35%, and 39.6% in 2026. The CBO estimates the cost of making the TCJA rates permanent would be \$1.8 trillion over the following ten years.²
- Individual standard deductions will revert to their much lower pre-TCJA levels, though subject to inflation adjustment from the 2017 levels. Even with the inflation adjustments, the standard deductions will be far lower than if the TCJA law continued to apply. The 10-year cost for making this provision permanent is projected to be \$1.0 trillion.³
- Personal exemptions will return to personal income tax returns in 2026, though at the same time the child tax credit will revert to its lower pre-TCJA levels with a much earlier phase-out of the credit and there will be no tax credit for other dependents. Permanently extending the elimination of personal exemptions is projected to raise \$1.6 trillion over 10 years, while permanently extending the TCJA child and dependent tax credit is projected to cost \$592.5 billion.⁴
- Changes to itemized deductions include the following items. If the TCJA changes are made permanent, it is estimated they would raise \$908 billion in revenue (net).⁵
- Charitable deductions to public charities for an individual will go back to being limited to 50% of adjusted gross income, rather than the 60% allowed under TCJA.
- State and local taxes allowed on Schedule A would no longer be capped at \$10,000 beginning in 2026.
- A less restrictive home mortgage interest deduction will be restored beginning in 2026, with the amount of first and second home acquisition debt on which interest can be claimed returning to \$1 million from the TJCA \$750,000 limit. Taxpayers will once again be able to deduct interest on up to \$100,000 of home equity debt as well.
- Personal casualty and theft losses will return to being deductible even if the loss is not related to a federally declared disaster.

² Congressional Research Service, *Reference Table: Expiring Provisions in the “Tax Cuts and Jobs Act”* (TCJA, P.L. 115-97), November 21, 2023, p. 2

³ Congressional Research Service, *Reference Table: Expiring Provisions in the “Tax Cuts and Jobs Act”* (TCJA, P.L. 115-97), November 21, 2023, p. 2

⁴ Congressional Research Service, *Reference Table: Expiring Provisions in the “Tax Cuts and Jobs Act”* (TCJA, P.L. 115-97), November 21, 2023, p. 2-4

⁵ Congressional Research Service, *Reference Table: Expiring Provisions in the “Tax Cuts and Jobs Act”* (TCJA, P.L. 115-97), November 21, 2023, p. 4

- Taxpayers will once again be able to claim a deduction for miscellaneous itemized deductions to the extent such expenses exceed 2% of adjusted gross income beginning in 2026.
- A less welcome change for taxpayers will be the return of the overall limit on itemized deductions under IRC §68, with the deductions reduced by 3% of the amount that a taxpayer's adjusted gross income exceeds the threshold, with the limitation capped at 80% of itemized deductions.
- Alternative minimum tax rates, phase-outs and exemptions return to their pre-TCJA amounts (after updating for an inflation adjustment), all of which are less taxpayer friendly. The CBO estimated the 10-year cost of making this provision permanent to be \$1,088.4 billion.⁶
- Taxpayers will also be once again allowed to exclude from their income qualified employer moving expense reimbursements. The projected 10-year additional revenue to be gained by the TCJA treatment that gives no exclusion permanent is \$6.7 billion.⁷

BUSINESS PROVISIONS

While the 21% corporate rate is not scheduled to go away at the end of 2025, there are certain business provisions that will no longer remain in the law once 2026 arrives. Some key elements are discussed below.

- The most significant business tax benefit found in the TCJA to disappear after 2025 is the deduction for qualified business income under IRC §199A which, unlike the lower corporate tax rate, was not made permanent as part of the Act. CBO estimates the 10-year cost of making this provision permanent to be \$548 billion.⁸
- Bonus depreciation is already being reduced from the original 100% first year rate allowed by TCJA, but it is scheduled to entirely leave the law at the end of 2026 (one year after most other TCJA provisions we are discussing expire). The CBO projects the 10-year cost of making this provision permanent to be \$325 billion.⁹

OTHER TAX PROVISIONS

There are a few other provisions that are set to expire at the end of 2025. Two of the key changes are discussed below:

- The estate and gift tax exclusions will be reduced to their pre-TCJA levels of \$5 million, after adjustment for inflation from their TCJA levels that were set at twice that amount before

⁶ Congressional Research Service, *Reference Table: Expiring Provisions in the "Tax Cuts and Jobs Act"* (TCJA, P.L. 115-97), p. 9

⁷ Congressional Research Service, *Reference Table: Expiring Provisions in the "Tax Cuts and Jobs Act"* (TCJA, P.L. 115-97), November 21, 2023, p. 8

⁸ Congressional Research Service, *Reference Table: Expiring Provisions in the "Tax Cuts and Jobs Act"* (TCJA, P.L. 115-97), November 21, 2023, p. 11

⁹ Congressional Research Service, *Reference Table: Expiring Provisions in the "Tax Cuts and Jobs Act"* (TCJA, P.L. 115-97), November 21, 2023, p. 12

adjustment for inflation. The IRS in Reg. §20.2010-2 held that if a portability election is made for a spouse that dies before the end of 2026, the deceased spouse unused exclusion (DSUE) amount will not decrease for the estate of the surviving even if that spouse lives beyond the end of 2025. The 10-year cost of making the higher exclusion amounts permanent is projected by the CBO to be \$126.5 billion.¹⁰

- The ability to use Qualified Opportunity Zone investments to defer gains already incurred and to exclude future gains on the Qualified Opportunity fund will no longer be eligible to be elected for gains incurred after December 31, 2026 (one year later than most other provisions). The CBO projects the estimated 10-year measuring period cost of making these provisions permanent (thus meaning counting 9 years in the measurement) would be \$67.3 billion.¹¹

CONSIDERATIONS THAT COULD IMPACT WHETHER OR NOT PROVISIONS ARE EXTENDED

Predicting if Congress will or will not extend these provisions is a task fraught with great risk and a high likelihood of getting the final results wrong. But we do need to help clients come to reasonable conclusions about possible results and clearly understand that any such prediction has to be understood to not be assured.

Obviously, the results of November's election (something not known when this unit was written in September) will likely have a very big impact on what provisions of the law are and are not extended. But a tax adviser needs to understand certain rules that Congress, and especially, the United States Senate has operated under in recent years. While the Senate can change its rules that it adopts at the beginning of each session, generally both parties have resisted making such changes when they hold the majority because of concerns about wanting these provisions to still be in place when they inevitably lose the majority.

Congressional Rules

Under the rules of the Senate, for most legislation a final vote can only be held after a successful vote to call for cloture (ending debate). That vote to bring the bill forward for its vote must pass the chamber by a super-majority of at least 60 votes. Unless one party holds 60 of the 100 seats in the Senate (something that last existed nearly 15 years ago), for a bill to advance at least some members of the minority party must vote to allow the bill to go to a floor vote.

In recent years the majority party has had very narrow margins in the Senate, so that has meant needing to obtain 8 to 10 members of the opposite party to agree to allow a vote to move forward. The minority party (or least certain members of that party) tend to impose conditions on allowing such a bill to move forward.

¹⁰ Congressional Research Service, *Reference Table: Expiring Provisions in the "Tax Cuts and Jobs Act"* (TCJA, P.L. 115-97), November 21, 2023, p. 13

¹¹ Congressional Research Service, *Reference Table: Expiring Provisions in the "Tax Cuts and Jobs Act"* (TCJA, P.L. 115-97), November 21, 2023, p. 14

The House does not operate under any similar restriction. If a majority party can keep all of its members in line, legislation can be passed in the House on a party line vote no matter how razor-thin that party's majority might be.

Budget Reconciliation Process – An Exception to the Cloture Rule With Strings Attached

As you might expect, the minority party uses the cloture process quite often to block action on legislation they don't agree with, giving that party an effective veto on bills subject to this provision. Congress recognized that this could be a major problem for the annual budget bills that must be passed for the Government to operate.

To address this issue, special rules apply for bills that are part of the annual budget reconciliation process. Such bills are limited to those that directly affect spending and revenue (so unrelated policy bills can't be attached to the bill) and these bills generally can't result in an increase in deficits for any year more than 10 years beyond the reconciliation year. But note that tax provisions are clearly within topics allowed to be part of this bill, subject to the 10-year provision.

But the key feature of reconciliation are the special debate rules in the Senate. When the bill goes to the Senate floor, the debate on the bill and related amendments is limited to 20 hours, after which it goes directly to a floor vote, bypassing the super-majority cloture vote. Bills covered by the reconciliation process thus only need the support of majority of Senators (or even the same number for and against, with the Vice-President then allowed to make a tie-breaking vote) to pass.

This is the process by which virtually all major tax legislation enacted while a single party controls the Presidency, House and Senate has been enacted since 2001, as the bill can be enacted without a single vote from any member of the other party.

But this is also why, back in 2017, the Republican majority was unable to permanently enact the provisions found in the Tax Cuts and Jobs act that we are discussing in this unit. If, once the dust settles from the November 2024 elections, one party wins the Presidency and controls both chambers of Congress it is very likely there will at least be an attempt to pass a bill resolving the issues in this unit on a strict party-line vote.

If there is a split in control, it's likely that if any of these provisions are to be extended there will need to be concessions granted to the party not holding the majority.

Other Issues Likely Impacting What Will or Won't Be Extended

In recent years, the size of the deficit has impacted these reconciliation bills that have been passed, with some members in each parties seeking to impose a limit on how much deficits are projected to be increased during that 10-year period under the bill. The need to meet such a limit to obtain certain Republican votes for the Tax Cuts and Jobs Act resulted in having to add revenue raising provisions to the bill and impose certain restrictions on tax benefits enacted as part of the bill.

More recently inflation has been considered a major reason to look to limit budget deficits. Reports of higher inflation in the coming months would likely reduce the amount of increased deficits Congress will accept to extend some expiring TCJA provisions, while more positive inflation reports will have the opposite impact.

FULL CONGRESSIONAL RESEARCH SERVICE DOCUMENT

On the following pages we've provided the entire detailed report prepared by the Congressional Research Service.

INSERT 19 PAGE REPORT FOUND AT <https://crsreports.congress.gov/product/pdf/R/R47846>

Unit 2

Recent Tax Legislation: SECURE 2.0 Act of 2022 and Final Regulations

The SECURE 2.0 Act of 2022 was signed into law as part of the Consolidated Appropriations Act, 2023 (CAA 2023), on December 29, 2022. Division T of the CAA 2023 contains the SECURE 2.0 Act of 2022. This is the last significant piece of legislation enacted by Congress. Absent passing a tax bill in a lame duck session, the 118th Congress will be the first in a long time to have passed no significant tax legislation during its time in office.

But this bill is still of significance, as many of its provisions are just now coming into effect now and we also got a significant set of final regulations impacting both the original SECURE Act passed in 2019 and this bill, specifically impacting required minimum distributions.

EXPANDING COVERAGE AND INCREASING RETIREMENT SAVINGS (TITLE I)

Expanding Automatic Enrollment in Retirement Plans (Section 101)

Effective Date: Plan years beginning after December 31, 2024.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 101

One of the main reasons many Americans reach retirement age with little or no savings is that too few workers are offered an opportunity to save for retirement through their employers. However, even for those employees who are offered a retirement plan at work, many do not participate. But automatic enrollment in 401(k) plans – providing for people to participate in the plan unless they take the initiative to opt out – significantly increases participation. Since first defined and approved by the Treasury Department in 1998, automatic enrollment has boosted participation by eligible employees generally, and particularly for Black, Latinx, and lower-wage employees. An early study found that adoption of automatic enrollment increased participation in a 401(k) plan by short-tenure Latinx employees from 19 percent to 75 percent. An Ariel/Aon-

Hewitt study found that, in plans using automatic enrollment, “[t]he most dramatic increases in enrollment rates are among younger, lower-paid employees, and the racial gap in participation rates is nearly eliminated among employees subject to auto-enrollment.”

Section 101 requires 401(k) and 403(b) plans to automatically enroll participants in the respective plans upon becoming eligible (and the employees may opt out of coverage). The initial automatic enrollment amount is at least 3 percent but not more than 10 percent. Each year thereafter that amount is increased by 1 percent until it reaches at least 10 percent, but not more than 15 percent. All current 401(k) and 403(b) plans are grandfathered. There is an exception for small businesses with 10 or fewer employees, new businesses (i.e., those that have been in business for less than 3 years), church plans, and governmental plans. Section 101 is effective for plan years beginning after December 31, 2024.

Analysis

New IRC §414A is added by the Act which details requirements for automatic enrollment for §401(k) and §403(b) salary reduction plans. The requirements apply (with exceptions) to:

- A qualified cash or deferred arrangement described in §401(k) and
- An annuity contract otherwise described in §403(b) which is purchased under a salary reduction agreement.¹²

The plan must meet the automatic enrollment requirements found in IRC §414(w)(3) which requires an arrangement:

- Under which a participant may elect to have the employer make payments as contributions under the plan on behalf of the participant, or to the participant directly in cash,
- Under which the participant is treated as having elected to have the employer make such contributions in an amount equal to a uniform percentage of compensation provided under the plan until the participant specifically elects not to have such contributions made (or specifically elects to have such contributions made at a different percentage), and
- Which meets the notice requirements found in IRC §414(w)(4).¹³

The notice shall be given within a reasonable period before plan year to each employee. Such notice must provide information about the rights and obligations under the arrangement which:

- Is sufficiently accurate and comprehensive to apprise the employee of such rights and obligations, and
- is written in a manner calculated to be understood by the average employee to whom the arrangement applies.¹⁴

¹² IRC §414A(a)

¹³ IRC §414A(b)

¹⁴ IRC §414(w)(4)(A)

The notice will not be treated as meeting these requirements unless:

- The notice includes an explanation of the employee's right under the arrangement to elect not to have elective contributions made on the employee's behalf (or to elect to have such contributions made at a different percentage),
- The employee has a reasonable period of time after receipt of the notice and before the first elective contribution is made to make such election, and
- The notice explains how contributions made under the arrangement will be invested in the absence of any investment election by the employee.¹⁵

The program must allow for permissible withdrawals as defined in IRC §414(w)(2). Such a withdrawal:

- Is made pursuant to an election by an employee, and
- Consists of elective contributions under the program (and earnings attributable thereto).¹⁶

The election must be made no later than 90 days after the date of the first elective contribution with regard to the employee.¹⁷ As well, the amount of any distribution by reason of the election is equal to the amount of elective contributions made with respect to the first payroll period to which the eligible automatic contribution arrangement applies to the employee and any succeeding payroll period beginning before the effective date of the election (and earnings attributable thereto).¹⁸

Minimum Contribution Percentage

The uniform percentage of compensation contributed by the participant under such arrangement during the first year of participation is not less than 3% and not more than 10% unless the participant specifically elects not to have such contributions made or to have such contributions made at a different percentage.¹⁹ This percentage is then increased as of the first day of each subsequent year by 1% point to at least 10% but not more than 15% unless the participant specifically elects not to have such contributions made or to have such contributions made at a different percentage.²⁰

The ceiling is reduced to 10% for plan years ending before January 1, 2025 except for an arrangement meeting the requirements of IRC §401(k)(12) or (13).²¹

¹⁵ IRC §414(w)(4)(B)

¹⁶ IRC §414(w)(2)(A)

¹⁷ IRC §414(w)(2)(B)

¹⁸ IRC §414(w)(2)(C)

¹⁹ IRC §414W(b)(3)(A)(i)

²⁰ IRC §414W(b)(3)(A)(ii)

²¹ IRC §414W(b)(3)(B)

Investment Requirements

The arrangement must provide that the amounts contributed pursuant to such arrangement, and for which no investment is elected by the participant, are invested in accordance with the requirements of section 2550.404c-5 of title 29, Code of Federal Regulations²² (or any successor regulations).²³

Exceptions

There are a number of plans that are exempt from these requirements.

The automatic enrollment requirements do not apply to SIMPLE plans (as defined in IRC §401(k)(11)).²⁴

Generally, the rules do not apply to preexisting plans and arrangements, specifically exempting:

- Any qualified cash or deferred arrangement established before the date of enactment of this section or
- Any annuity contract purchased under a plan established before the date of enactment of this section.²⁵

However, the preexisting plan/arrangement exception does not apply in the case of an employer adopting after the date of enactment a plan maintained by more than one employer. In such a case, the automatic enrollment rules will apply with respect to that employer as if the plan were a single plan.²⁶

The automatic enrollment provisions also do not apply to:

- Any governmental plan (within the meaning of IRC §414(d) or
- Any church plan (within the meaning of IRC §414(e)).²⁷

New businesses get an exemption from the automatic enrollment requirements. The law provides that the automatic enrollment provisions do not apply to any qualified cash or deferred arrangement, or any annuity contract purchased under a plan, while the employer maintaining such a plan (and any predecessor employer) has been in existence for less than 3 years.²⁸

²² <https://www.ecfr.gov/current/title-29/subtitle-B/chapter-XXV/subchapter-F/part-2550/section-2550.404c-5> (Retrieved December 26, 2022)

²³ IRC §414(b)(4)

²⁴ IRC §414W(c)(1)

²⁵ IRC §414W(c)(2)(A)

²⁶ IRC §414W(c)(2)(B)

²⁷ IRC §414W(c)(3)

²⁸ IRC §414W(c)(4)(A)

A small employer exception to these rules is also found in the Act. The automatic enrollment rules shall not apply to any qualified cash or deferred arrangement, or any annuity contract purchased under a plan, earlier than the date that is 1 year after the close of the first taxable year with respect to which the employer maintaining the plan normally employed less than 10 employees.²⁹

A multiple employer plan applies the new business and small business exception separately for each qualifying employers. Such a multiple employer plan shall treat all employer plans that do not qualify for either the new business or small employer exception applies as maintaining a single plan.³⁰

Modification of Credit for Small Employer Pension Plan Startup Costs (Section 102)

Effective Date: Taxable years beginning after December 31, 2022.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 102

The 3-year small business startup credit is currently 50 percent of administrative costs, up to an annual cap of \$5,000. Section 102 makes changes to the credit by increasing the startup credit from 50 percent to 100 percent for employers with up to 50 employees. Except in the case of defined benefit plans, an additional credit is provided. The amount of the additional credit generally will be a percentage of the amount contributed by the employer on behalf of employees, up to a per-employee cap of \$1,000. This full additional credit is limited to employers with 50 or fewer employees and phased out for employers with between 51 and 100 employees. The applicable percentage is 100 percent in the first and second years, 75 percent in the third year, 50 percent in the fourth year, 25 percent in the fifth year – and no credit for tax years thereafter. Section 102 is effective for taxable years beginning after December 31, 2022.

Analysis

Prior to the SECURE 2.0 Act changes, IRC §45E provided for a credit equal to 50% of *qualified startup costs* paid or incurred by an *eligible employer*. The credit, which only applies for three consecutive years, cannot exceed the greater of:

- \$500 or
- The lesser of
 - \$250 for each employee (other than highly compensated employees) of the employer who is eligible to participate in the plan or

²⁹ IRC §414W(c)(4)(B)

³⁰ IRC §414W(c)(4)(C)

— \$5,000.³¹

The plan must be a new plan, meaning the employer does not qualify if, during the 3-taxable year period immediately preceding the 1st taxable year for which the credit under this section is otherwise allowable for a qualified employer plan of the employer, the employer or any member of any controlled group including the employer (or any predecessor of either) established or maintained a qualified employer plan with respect to which contributions were made, or benefits were accrued, for substantially the same employees as are in the qualified employer plan.³²

An *eligible employer* is an employer which had no more than 100 employees who received at least \$5,000 of compensation from the employer for the preceding year.³³

SECURE 2.0 Act Modifications

The SECURE Act 2.0 both doubles the base credit for those who employ 50 or fewer employees and creates an additional credit.

Increased Credit for Employers with 50 or Fewer Employees

The small business pension plan startup costs credit is modified for employers who have 50 or fewer employees who received at least \$5,000 of compensation from the employer for the preceding year.³⁴ Such employers will qualify for a credit equal to 100% (up from 50%) of qualified plan startup costs paid or incurred by the taxpayer during the taxable year.³⁵

Employer Contribution Credit

An additional credit is added to IRC §45E by the SECURE 2.0 Act, a credit based on employer contributions to the plan. The §45E credit is increased by an amount equal to the *applicable percentage* of employer contributions by the employer to an eligible employer plan. The credit does not apply, though, to employer contributions to defined benefit plans.³⁶

This portion of the credit is subject to a \$1,000 per employee limitation.³⁷

³¹ IRC §45E(b)

³² IRC §45E(c)(2)

³³ IRC §45E(c)(2), IRC §408(p)(2)(C)(i)

³⁴ IRC §45E(e)(4), IRC §408(p)(2)(C)(i)

³⁵ IRC §45E(e)(4)

³⁶ IRC §45E(f)(1)

³⁷ IRC §45E(f)(2)(A)

The *applicable percentage*³⁸ is 100% for the taxable year in which the plan is established, with the percentage in following years determined under this table:

Taxable year following the year the plan is established	Applicable percentage
1 st	100%
2 nd	75%
3 rd	50%
4 th	25%
Any subsequent years	0%

Contributions made to employees who receive wages from the employer during the taxable year in excess of \$100,000 are excluded in computing this additional credit.³⁹ For taxable years beginning in a calendar year after 2023, the \$100,000 value will be indexed for inflation in \$5,000 increments.⁴⁰

For employers with more than 50 employees, the credit is phased-out ratably up to 100 employees.⁴¹

For purposes of determining whether an employer is an eligible employer the requirement for a new qualified employer plan found at IRC §45E(c)(2) shall only apply to the taxable year during which the eligible employer plan to which this section applies is established with respect to the eligible employer.⁴²

IRC §45E(e)(2) is amended to provide that deductions for employer contributions for a year are to be reduced by the amount of the additional credit allowed. IRC §45(e)(2) had already reduced the deduction for the applicable administrative costs by the amount of standard §45E(a) credit allowed for those costs.

Saver's Match (Section 103)

Effective Date: Taxable years beginning after December 31, 2026

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 103

Current law provides for a nonrefundable credit for certain individuals who make contributions to individual retirement accounts ("IRAs"), employer retirement plans (such as 401(k) plans), and ABLE accounts. Section

³⁸ IRC §45E(f)(3)

³⁹ IRC §45E(f)(2)(C)(i)

⁴⁰ IRC §45E(f)(2)(C)(iii)

⁴¹ IRC §45E(f)(2)(B)

⁴² IRC §45E(f)(4)

103 repeals and replaces the credit with respect to IRA and retirement plan contributions, changing it from a credit paid in cash as part of a tax refund into a federal matching contribution that must be deposited into a taxpayer's IRA or retirement plan. The match is 50 percent of IRA or retirement plan contributions up to \$2,000 per individual. The match phases out between \$41,000 and \$71,000 in the case of taxpayers filing a joint return (\$20,500 to \$35,500 for single taxpayers and married filing separate; \$30,750 to \$53,250 for head of household filers). Section 103 is effective for taxable years beginning after December 31, 2026.

Promotion of Saver's Match (Section 104)

Effective Date: The Treasury Department must report on its anticipated promotional efforts no later than July 1, 2026

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 104

Section 104 directs the Treasury Department to increase public awareness of the Saver's Match to increase use of the match by low and moderate income taxpayers. The promotion will make clear that the Saver's Match cannot be withdrawn without incurring penalties, including repayment to the Treasury Department in some cases where the Saver's Match is withdrawn from an individual retirement account before retirement. Taxpayers will have an election to designate a retirement account to receive the repaid Saver's Match. The Treasury Secretary must report to Congress on the Treasury Department's anticipated promotion efforts no later than July 1, 2026.

Pooled Employer Plan Modification (Section 105)

Effective Date: Plan years beginning after December 31, 2022

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 105

Section 105 clarifies that a pooled employer plan ("PEP") may designate a named fiduciary (other than an employer in the plan) to collect contributions to the plan. Such fiduciary would be required to implement written contribution collection procedures that are reasonable, diligent, and systematic. Section 105 is effective for plan years beginning after December 31, 2022.

Multiple Employer 403(b) Plans (Section 106)

Effective Date: Plan years beginning after December 31, 2022

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 106

Multiple employer plans (“MEPs”) provide an opportunity for small employers to band together to obtain more favorable retirement plan investment results and more efficient and less expensive management services. The Setting Every Community Up for Retirement Enhancement Act of 2019 (“SECURE Act”) made MEPs more attractive by eliminating outdated barriers to the use of MEPs and improving the quality of MEP service providers. Section 106 allows 403(b) plans, which are generally sponsored by charities, educational institutions, and non-profits, to participate in MEPs and PEPs, including relief from the one bad apple rule so that the violations of one employer do not affect the tax treatment of employees of compliant employers. Section 106 is effective for plan years beginning after December 31, 2022.

Increase in Age for Required Beginning Date for Mandatory Distributions (Section 107)

Effective Date: Distributions required to be made after December 31, 2022, with respect to individuals who attain age 72 after such date. But see the note below about a drafting error in the bill.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 107

Under current law, participants are generally required to begin taking distributions from their retirement plans at age 72. The policy behind this rule is to ensure that individuals spend their retirement savings during their lifetime and not use their retirement plans for estate planning purposes to transfer wealth to beneficiaries. The SECURE Act of 2019 increased the required minimum distribution age to 72. Section 107 further increases the required minimum distribution age further to 73 starting on January 1, 2023 – and increases the age further to 75 starting on January 1, 2033.

Drafting Problem for Those Born in 1959

The legislation contains a drafting glitch that results in the “applicable age” for those born in 1959 being *both* age 73 and age 75. Revised IRC §401(a)(9)(C)(v) reads:

(v) APPLICABLE AGE.—

(I) In the case of an individual who attains age 72 after December 31, 2022, and age 73 before January 1, 2033, the applicable age is 73.

(II) In the case of an individual who attains age 74 after December 31, 2032, the applicable age is 75.

A person born in 1959 will attain age 73 after December 31, 2022 and before January 1, 2033 (that is, during 2032). Per §409(a)(9)(C)(v)(I) that would make the individual's applicable age 73. Therefore, the individual's first required minimum distribution would have to take place no later than April 1, 2033.

However, that person would also have attained age 74 after December 31, 2032 (since they would turn 74 in 2033), making their applicable age 75, which would set the required beginning date at April 1, 2035 (since this person would reach age 75 in 2034).

It would appear that the law should state that age 75 with the required beginning date for those who attained age 73 after December 31, 2032.

Indexing IRA Catch-Up Limit (Section 108)

Effective Date: Taxable years beginning after December 31, 2023

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 108

Under current law, the limit on IRA contributions is increased by \$1,000 (not indexed) for individuals who have attained age 50. Section 108 indexes such limit and is effective for taxable years beginning after December 31, 2023.

Analysis

The indexing described above provided for in IRC §219(b)(5)(C)(iii) will take place in \$100 increments.

Higher Catch-Up Limit to Apply at Age 60, 61, 62 and 63 (Section 109)

Effective Date: Taxable years beginning after December 31, 2024.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 109

Under current law, employees who have attained age 50 are permitted to make catch-up contributions under a retirement plan in excess of the otherwise applicable limits. The limit on catch-up contributions for 2021 is \$6,500, except in the case of SIMPLE plans for which the limit is \$3,000. Section 109 increases these limits to the greater of \$10,000 or 50 percent more than the regular catch-up amount in 2025 for individuals who have attained ages 60, 61, 62 and 63. The increased amounts are indexed for inflation after 2025. Section 109 is effective for taxable years beginning after December 31, 2024.

Treatment of Student Loan Payments as Elective Deferrals for Purposes of Matching Contributions (Section 110)

Effective Date: Contributions for plan years beginning after December 31, 2023

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 110

Section 110 is intended to assist employees who may not be able to save for retirement because they are overwhelmed with student debt, and thus are missing out on available matching contributions for retirement plans. Section 110 allows such employees to receive those matching contributions by reason of repaying their student loans. Section 110 permits an employer to make matching contributions under a 401(k) plan, 403(b) plan, or SIMPLE IRA with respect to “qualified student loan payments.” A qualified student loan payment is broadly defined as any indebtedness incurred by the employee solely to pay qualified higher education expenses of the employee. Governmental employers are also permitted to make matching contributions in a section 457(b) plan or another plan with respect to such repayments. For purposes of the nondiscrimination test applicable to elective contributions, Section 110 permits a plan to test separately the employees who receive matching contributions on student loan repayments. Section 110 is effective for contributions made for plan years beginning after December 31, 2023.

Application of Credit for Small Employer Pension Plan Startup Costs to Employers (Section 111)

Effective Date: Retroactively effective for taxable years beginning after December 31, 2019

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 111

Section 111 ensures the startup tax credit is available for 3 years for employers joining a MEP, regardless of how long the MEP has been in existence. Under both pre- and post-SECURE Act law, the startup tax credit only applies for the first 3 years that a plan is in existence. For example, if a small business joins a MEP that has already been in existence for 3 years, the startup credit is not available. If, for example, the MEP has been in existence for 1 or 2 years when a small business joins, the small business may be able to claim the credit for 1 or 2 years, respectively. Section 111 fixes this issue so that employers joining a MEP (which includes PEPs) are eligible for the credit for all 3 years. Section 111 is effective retroactively for taxable years beginning after December 31, 2019.

Military Spouse Retirement Plan Eligibility Credit for Small Employers (Section 112)

Effective Date: Taxable years beginning after the date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 112

Military spouses often do not remain employed long enough to become eligible for their employer's retirement plan or to vest in employer contributions. Section 112 provides small employers a tax credit with respect to their defined contribution plans if they (1) make military spouses immediately eligible for plan participation within two months of hire, (2) upon plan eligibility, make the military spouse eligible for any matching or nonelective contribution that they would have been eligible for otherwise at 2 years of service, and (3) make the military spouse 100 percent immediately vested in all employer contributions. The tax credit equals the sum of (1) \$200 per military spouse, and (2) 100 percent of all employer contributions (up to \$300) made on behalf of the military spouse, for a maximum tax credit of \$500. This credit applies for 3 years with respect to each military spouse – and does not apply to highly compensated employees. An employer may rely on an employee's certification that such employee's spouse is a member of the uniformed services. Section 112 is effective for taxable years beginning after the date of enactment of this Act.

Small Immediate Incentives for Contributing to a Plan (Section 113)

Effective Date: Plan years beginning after the date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 113

Under current law, employers may provide matching contributions as a long-term incentive for employees to contribute to a 401(k) plan. However, immediate financial incentives (like gift cards in small amounts) are prohibited even though individuals may be especially motivated by them to join their employers' retirement plans. Section 113 enables employers to offer de minimis financial incentives, not paid for with plan assets, such as low-dollar gift cards, to boost employee participation in workplace retirement plans by exempting de minimis financial incentives from section 401(k)(4)(A) and from the corresponding rule under section 403(b). Section 113 is effective for plan years beginning after the date of enactment of this Act.

Potential Unexpected Interaction with De Minimis Fringe Benefit Rules at IRC §132

While the Act allows for these de minimis incentives to be paid out by an employer to an employee without jeopardizing the qualification of the employee retirement plan, that does not mean such incentives might not end up being taxable income to the employee.

While IRC §132(a)(4) does provide for an exclusion from income for *de minimis* fringe benefits, §132 has its own, section specific definition of what is such a *de minimis* fringe benefit. IRC §132(e)(1) contains this definition that must be met for the incentive to avoid inclusion in income:

(e) **De minimis fringe defined.** For purposes of this section--

(1) **In general.** The term “de minimis fringe” means any property or service the value of which is (after taking into account the frequency with which similar fringes are provided by the employer to the employer’s employees) so small as to make accounting for it unreasonable or administratively impracticable.

The key issue is that the benefit must be one for which it is unreasonable or administratively impracticable to account.

The Senate Finance Committee explanation specifically offers up as an example of a *de minimis* incentive that would not put plan qualification at risk the provision of low dollar amount gift cards to an employee for participation in the retirement plan.

However, since such cards have a specific dollar amount stated, Reg. §1.132-6(c) takes the position that such gift certificate items are cash equivalents that must always be included in the employee’s income:

(c) **Administrability.** Unless excluded by a provision of chapter 1 of the Internal Revenue Code of 1986 other than section 132(a)(4), the value of any fringe benefit that would not be unreasonable or administratively impracticable to account for is includible in the employee’s gross income. Thus, except as provided in paragraph (d)(2) of this section, the provision of any cash fringe benefit is never excludable under section 132(a) as a *de minimis* fringe benefit. Similarly except as otherwise provided in paragraph (d) of this section, a cash equivalent fringe benefit (such as a fringe benefit provided to an employee through the use of a gift certificate or charge or credit card) is generally not excludable under section 132(a) even if the same property or service acquired (if provided in kind) would be excludable as a *de minimis* fringe benefit.⁴³

Thus, if the plan sponsor gave each employee participating in the retirement plan for the year a \$10 gift card for Starbucks, that \$10 would have to be included in the employee’s W-2 as income subject to withholding for the year, as well as being subject to payroll taxes unless the IRS adopts changes to the regulations under IRC §132 to exclude items determined to be *de minimis* retirement plan incentives.

⁴³ Treasury Reg. §1.132-6(c)

Deferral of Tax for Certain Sales of Employer Stock to Employee Stock Ownership Plans (Section 114)

Effective Date: Sales after December 31, 2027.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 114

Under section 1042 of the Internal Revenue Code (“Code”), an individual owner of stock in a non-publicly traded C corporation that sponsors an employee stock ownership plan (“ESOP”) may elect to defer the recognition of gain from the sale of such stock to the ESOP if the seller reinvests the sales proceeds into qualified replacement property, such as stock or other securities issued by a U.S. operating corporation. After the sale, the ESOP must own at least 30 percent of the employer corporation’s stock. Section 114 expands the gain deferral provisions of Code section 1042 with a 10 percent limit on the deferral to sales of employer stock to S corporation ESOPs. Section 114 is effective for sales made after December 31, 2027.

Withdrawals for Certain Emergency Expenses (Section 115)

Effective Date: Distributions made after December 31, 2023.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 115

Generally, an additional 10 percent tax applies to early distributions from tax-preferred retirement accounts, such as 401(k) plans and IRAs, unless an exception applies. Section 115 provides an exception for certain distributions used for emergency expenses, which are unforeseeable or immediate financial needs relating to personal or family emergency expenses. Only one distribution is permissible per year of up to \$1,000, and a taxpayer has the option to repay the distribution within 3 years. No further emergency distributions are permissible during the 3-year repayment period unless repayment occurs. Section 115 is effective for distributions made after December 31, 2023.

Allow Additional Nonelective Contributions to SIMPLE Plans (Section 116)

Effective Date: Taxable years beginning after December 31, 2023.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 116

Current law requires employers with SIMPLE plans to make employer contributions to employees of either 2 percent of compensation or 3 percent of employee elective deferral contributions. Section 116 permits an employer to make additional contributions to each employee of the plan in a uniform manner, provided

that the contribution may not exceed the lesser of up to 10 percent of compensation or \$5,000 (indexed). Section 116 is effective for taxable years beginning after December 31, 2023.

Contribution Limit for SIMPLE Plans (Section 117)

Effective Date: Change to contribution limits applies for taxable years beginning after December 31, 2023. Treasury shall report to Congress on data related to SIMPLE-IRAs by December 31, 2024 and annually thereafter.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 117

Under current law, the annual contribution limit for employee elective deferral contributions to a SIMPLE IRA plan is \$14,000 (2022) and the catch-up contribution limit beginning at age 50 is \$3,000. A SIMPLE IRA plan may only be sponsored by a small employer (100 or fewer employees), and the employer is required to either make matching contributions on the first 3 percent of compensation deferred or an employer contribution of 2 percent of compensation (regardless of whether the employee elects to make contributions). Section 117 increases the annual deferral limit and the catch-up contribution at age 50 by 10 percent, as compared to the limit that would otherwise apply in the first year this change is effective, in the case of an employer with no more than 25 employees. An employer with 26 to 100 employees would be permitted to provide higher deferral limits, but only if the employer either provides a 4 percent matching contribution or a 3 percent employer contribution. Section 117 makes similar changes to the contribution limits for SIMPLE 401(k) plans. Section 117 is effective for taxable years beginning after December 31, 2023. The Secretary of Treasury shall report to Congress on data related to SIMPLE IRAs by December 31, 2024, and annually thereafter.

Tax Treatment for Certain Non-Trade or Business SEP Contributions (Section 118)

Effective Date: Taxable years beginning after the date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 118

Section 118 permits employers of domestic employees (e.g., nannies) to provide retirement benefits for such employees under a Simplified Employee Pension (“SEP”). Section 118 is effective for taxable years beginning after date of enactment of this Act.

Application of \$415 Limit for Certain Employees of Rural Electric Cooperatives (Section 119)

Effective Date: Effective for limitation years ending after date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 119

Under current law, section 415 generally limits the amount that may be paid by a pension plan in annual benefits to a participant to the lesser of \$245,000 (2022) or 100 percent of the participant's average compensation. Section 119 eliminates the compensation-based limit for participants who are non-highly compensated employees and participate in a rural electric cooperative retirement plan. Section 119 is effective for limitation years ending after the date of enactment of this Act.

Exemption for Certain Automatic Portability Transactions (Section 120)

Effective Date: Transactions occurring on or after the date that is 12 months after the date of the enactment of the Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 120

Under current law, an employer is permitted to distribute a participant's account balance without participant consent if the balance is under \$5,000 and the balance is immediately distributable (e.g., after a termination of employment). Current law also requires an employer to roll over this distribution into a default IRA if the account balance is at least \$1,000 and the participant does not affirmatively elect otherwise. Section 120 permits a retirement plan service provider to provide employer plans with automatic portability services. Such services involve the automatic transfer of a participant's default IRA (established in connection with a distribution from a former employer's plan) into the participant's new employer's retirement plan, unless the participant affirmatively elects otherwise. Section 120 is effective for transactions occurring on or after the date which is 12 months after the date of enactment of this Act.

Starter \$401(k) Plans for Employers with No Retirement Plan (Section 121)

Effective Date: Plan years beginning on or after December 31, 2023.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 121

Section 121 permits an employer that does not sponsor a retirement plan to offer a starter 401(k) plan (or safe harbor 403(b) plan). A starter 401(k) plan (or safe harbor 403(b) plan) would generally require that all employees be default enrolled in the plan at a 3 to 15 percent of compensation deferral rate. The limit on annual deferrals would be the same as the IRA contribution limit, which for 2022 is \$6,000 with an additional \$1,000 in catch-up contributions beginning at age 50. Section 121 is effective for plan years beginning after December 31, 2023.

Assisting States in Locating Owners of Applicable Savings Bonds (Section 122)

<i>Effective Date: Effective on the date of enactment of this Act.</i>
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SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 122

To facilitate efforts to locate the owners of matured and unredeemed savings bonds, Section 122 requires the Treasury Secretary to share certain relevant information with a state that relates to an applicable savings bond registered to an owner with a last known or registered address in that state. The state is permitted to use that information to locate the registered owner in accordance with the state's standards for recovery of abandoned property. Section 122 further requires the Treasury Secretary to develop guidance as may be necessary to carry out the proper disclosure and protection of such information. The Treasury Secretary also is required to submit to the Senate Appropriations and Finance Committees and House Appropriations and Ways and Means Committees an annual report assessing its efforts to provide states with information on unclaimed savings bonds. Section 122 is effective on the date of enactment of this Act.

Certain Securities Treated as Publicly Traded in Case of Employee Stock Ownership Plans (Section 123)

<i>Effective Date: Plan years beginning after December 31, 2027.</i>
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SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 123

Section 123 updates certain ESOP rules related to whether a security is a “publicly traded employer security” and “readily tradeable on an established securities market.” Section 123 allows certain non-exchange traded securities to qualify as “publicly traded employer securities” so long as the security is subject to priced quotations by at least four dealers on a Securities and Exchange Commission-regulated

interdealer quotation system, is not a penny stock and is not issued by a shell company, and has a public float of at least 10 percent of outstanding shares. For securities issued by domestic corporations, the issuer must publish annual audited financial statements. Securities issued by foreign corporations are subject to additional depository and reporting requirements. The updated definitions in Section 123 will allow highly regulated companies with liquid securities that are quoted on non-exchange markets to treat their stock as “public” for ESOP purposes, thus making it easier for these companies to offer ESOPs to their U.S. employees. Section 123 is effective for plan years beginning after December 31, 2027.

Modification of Age Requirement for Qualified Able Programs (Section 124)

Effective Date: Taxable years beginning after December 31, 2025.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 124

Current law allows states to create qualified ABLE programs, which are tax-advantaged savings programs for certain people with disabilities. Distributions from an ABLE account are tax-free if used for qualified disability expenses of the account’s designated beneficiary. Section 124 increases the age by which blindness or disability must occur for an individual to be an eligible individual by reason of such blindness or disability for an ABLE program. Section 124 is effective for taxable years beginning after December 31, 2025.

Improving Coverage for Part-Time Workers (Section 125)

Effective Date: The reduction of the 3 year rule to 2 years is effective for plan years beginning after December 31, 2024. The provisions providing that pre-2021 service is disregarded for vesting purposes is retroactively effective as if included in the SECURE Act of 2019.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 125

The SECURE Act requires employers to allow long-term, part-time workers to participate in the employers’ 401(k) plans. The SECURE Act provision provides that – except in the case of collectively bargained plans – employers maintaining a 401(k) plan must have a dual eligibility requirement under which an employee must complete either 1 year of service (with the 1,000-hour rule) or 3 consecutive years of service (where the employee completes at least 500 hours of service). Section 125 reduces the 3-year rule to 2 years, effective for plan years beginning after December 31, 2024. Section 125 also provides that pre-2021 service is disregarded for vesting purposes, just as such service is disregarded for eligibility purposes under current law, effective as if included in the SECURE Act to which the amendment relates. This provision also extends the long-term part-time coverage rules to 403(b) plans that are subject to ERISA.

Special Rules for Certain Distributions from Long-Term Qualified Tuition Programs to Roth IRAs (Section 126)

Effective Date: Distributions made after December 31, 2023.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 126

Section 126 amends the Internal Revenue Code to allow for tax and penalty free rollovers from 529 accounts to Roth IRAs, under certain conditions. Beneficiaries of 529 college savings accounts would be permitted to rollover up to \$35,000 over the course of their lifetime from any 529 account in their name to their Roth IRA. These rollovers are also subject to Roth IRA annual contribution limits, and the 529 account must have been open for more than 15 years.

Families and students have concerns about leftover funds being trapped in 529 accounts unless they take a non-qualified withdrawal and assume a penalty. This has led to hesitating, delaying, or declining to fund 529s to levels needed to pay for the rising costs of education. Section 126 eliminates this concern by providing families and students with the option to avoid the penalty, resulting in families putting more into their 529 account. Families who sacrifice and save in 529 accounts should not be punished with tax and penalty years later if the beneficiary has found an alternative way to pay for their education. They should be able to retain their savings and begin their retirement account on a positive note. Section 126 is effective with respect to distributions after December 31, 2023.

Emergency Savings Accounts Link to Individual Account Plans (Section 127)

Effective Date: Plan years beginning after 2023.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 127

Though individuals can save on their own, far too many fail to do so. According to a report by the Federal Reserve, almost half of Americans would struggle to cover an unexpected \$400 expense. Many are forced to tap into their retirement savings. A recent study found that, in the past year, almost 60 percent of retirement account participants who lack emergency savings tapped into their long-term retirement savings, compared to only 9 percent of those who had at least a month of emergency savings on hand. Separating emergency savings from one's retirement savings account will provide participants a better understanding that one account is for short-term emergency needs and the other is for long-term retirement savings, thus empowering employees to handle unexpected financial shocks without jeopardizing their long-term financial security in retirement through emergency hardship withdrawals.

Section 127 provides employers the option to offer to their non-highly compensated employees pension-linked emergency savings accounts. Employers may automatically opt employees into these accounts at no more than 3 percent of their salary, and the portion of an account attributable to the employee's

contribution is capped at \$2,500 (or lower as set by the employer). Once the cap is reached, the additional contributions can be directed to the employee's Roth defined contribution plan (if they have one) or stopped until the balance attributable to contributions falls below the cap. Contributions are made on a Roth-like basis and are treated as elective deferrals for purposes of retirement matching contributions with an annual matching cap set at the maximum account balance – i.e., \$2,500 or lower as set by the plan sponsor. The first four withdrawals from the account each plan year may not be subject to any fees or charges solely on the basis of such withdrawals. At separation from service, employees may take their emergency savings accounts as cash or roll it into their Roth defined contribution plan (if they have one) or IRA.

Enhancement of §403(b) Plans (Section 128)

<i>Effective Date: Amounts invested after the date of enactment of this Act.</i>
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SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 128

Under current law, 403(b) plan investments are generally limited to annuity contracts and publicly traded mutual funds. This limitation cuts off 403(b) plan participants – generally, employees of charities and public schools, colleges, and universities– from access to collective investment trusts, which are often used by 401(a) plans to expand investment options for plan participants at a lower overall cost. Section 128 would permit 403(b) custodial accounts to participate in group trusts with other tax-preferred savings plans and IRAs, and would be effective after date of enactment.

PRESERVATION OF INCOME (TITLE II)

Remove Required Minimum Distribution Barriers for Life Annuities (Section 201)

<i>Effective Date: Calendar years ending after the date of enactment of the Act.</i>
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SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 201

Section 201 eliminates certain barriers to the availability of life annuities in qualified plans and IRAs that arise under current law due to an actuarial test in the required minimum distribution regulations. The test is intended to limit tax deferral by precluding commercial annuities from providing payments that start out small and increase excessively over time. In operation, however, the test commonly prohibits many important guarantees that provide only modest benefit increases under life annuities. For example, guaranteed annual increases of only 1 or 2 percent, return of premium death benefits, and period certain guarantees for participating annuities are commonly prohibited by this test. Without these types of

guarantees, many individuals are unwilling to elect a life annuity under a defined contribution plan or IRA. Section 201 is effective for calendar years ending after the date of enactment of this Act.

Qualifying Longevity Annuity Contracts (Section 202)

Effective Date: Contracts purchased or received in an exchange on or after the date of enactment of this Act. Treasury must update the regulations within 18 months of the date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 202

In 2014, the Treasury Department published final regulations on qualifying longevity annuity contracts (“QLACs”). QLACs are generally deferred annuities that begin payment at the end of an individual’s life expectancy. Because payments start so late, QLACs are an inexpensive way for retirees to hedge the risk of outliving their savings in defined contribution plans and IRAs. The minimum distribution rules were an impediment to the growth of QLACs in defined contribution plans and IRAs because those rules generally require payments to commence at age 72, before QLACs begin payments. The 2014 regulations generally exempted QLACs from the minimum distribution rules until payments commence. However, due to a lack of statutory authority to provide a full exemption, the regulations imposed certain limits on the exemption that have prevented QLACs from achieving their intended purpose in providing longevity protection. Section 202 addresses these limitations by repealing the 25 percent limit w [sic] and allowing up to \$200,000 (indexed) to be used from an account balance to purchase a QLAC. Section 202 also facilitates the sales of QLACs with spousal survival rights – and clarifies that free-look periods are permitted up to 90 days with respect to contracts purchased or received in an exchange on or after July 2, 2014. Section 202 is effective for contracts purchased or received in an exchange on the date of enactment of this Act, and the Treasury Secretary must update the relevant regulations within 18 months of the date of enactment of this Act.

Insurance-Dedicated Exchange-Traded Funds (Section 203)

Effective Date: Applies to segregated asset account investments made on or after the date which is seven years after the date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 203

Exchange-traded funds (“ETFs”) are pooled investment vehicles that are traded on stock exchanges. They are similar to mutual funds, except the shares can be traded throughout the day on the stock market, rather than having to be held until after the market closes. ETFs are widely available through retirement plans, IRAs, and taxable investment accounts. However, outdated Treasury Department regulations have prevented ETFs from being widely available through individual variable annuities. Simply because the regulations were written before ETFs existed, ETFs cannot satisfy the regulatory requirements to be “insurance-dedicated.” Section 203 directs the Treasury Department to update the regulations to reflect the ETF structure to provide that ownership of an ETF’s shares by certain types of institutions that are necessary

to the ETF's structure would not preclude look-through treatment for the ETF, as long as it otherwise satisfies the current-law requirements for look-through treatment. This essentially would facilitate the creation of a new type of ETF that is "insurance-dedicated." Section 203 is effective for segregated asset account investments made on or after 7 years after the date of enactment of this Act, and directs the Treasury Secretary to update the relevant regulations by that time.

Eliminating a Penalty on Partial Annuitization (Section 204)

<i>Effective Date: Date of enactment of this Act.</i>

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 204

If a tax-preferred retirement account also holds an annuity, current law requires that the account be bifurcated between the portion of the account holding the annuity and the rest of the account for purposes of applying the required minimum distribution rules. This treatment may result in higher minimum distributions than would have been required if the account did not hold an annuity. Section 204 permits the account owner to elect to aggregate distributions from both portions of the account for purposes of determining minimum distributions and is effective on the date of enactment of this Act. The Treasury Secretary is to update the relevant regulations accordingly.

SIMPLIFICATION AND CLARIFICATION OF RETIREMENT PLAN RULES (TITLE III)

Recovery of Retirement Plan Overpayments (Section 301)

<i>Effective Date: Date of enactment of this Act.</i>

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 301

Sometimes retirees mistakenly receive more money than they are owed under their retirement plans. These mistakes cause problems when they occur over time, and plan fiduciaries later seek to recover the overpayments from unsuspecting retirees. When an overpayment has lasted for years, plans often compel retirees to repay the amount of the overpayment, plus interest, which can be substantial. Even small overpayment amounts can create a hardship for a retiree living on a fixed income. Section 301 allows retirement plan fiduciaries the latitude to decide not to recoup overpayments that were mistakenly made to retirees. If plan fiduciaries choose to recoup overpayments, limitations and protections apply to safeguard innocent retirees. This protects both the benefits of future retirees and the benefits of current retirees. Rollovers of the overpayments also remain valid. Section 301 is effective on the date of enactment of this Act, and further outlines how plan fiduciaries may proceed with respect to determinations made prior to the date of enactment of this Act to seek or not to seek recovery of overpayments.

Reduction of Excise Tax on Certain Accumulations in Retirement Plans (Section 302)

Effective Date: Taxable years beginning after the date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 302

Section 302 reduces the penalty for failure to take required minimum distributions from 50 to 25 percent. Further, if a failure to take a required minimum distribution from an IRA is corrected in a timely manner, as defined under this Act, the excise tax on the failure is further reduced from 25 percent to 10 percent. Section 302 is effective for taxable years beginning after the date of enactment of this Act.

Retirement Savings Lost and Found (Section 303)

Effective Date: Database to be created no later than 2 years after the date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 303

Every year, thousands of people approach retirement but are unable to find and receive the benefits that they earned often because the company they worked for moved, changed its name, or merged with a different company. Similarly, every year there are employers around the country ready to pay benefits to retirees, but they are unable to find the retirees because the former employees changed their names or addresses. Section 303 creates a national online searchable lost and found database for Americans' retirement plans at the Department of Labor ("DOL"). The database will enable retirement savers, who might have lost track of their pension or 401(k) plan, to search for the contact information of their plan administrator. Section 303 directs the creation of the database no later than 2 years after the date of enactment of this Act.

Updating Dollar Limit for Mandatory Distributions (Section 304)

Effective Date: Distributions made after December 31, 2023.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 304

Under current law, employers may transfer former employees' retirement accounts from a workplace retirement plan into an IRA if their balances are between \$1,000 and \$5,000. Section 307 inc

Expansion of Employee Plans Compliance Resolution System (EPCRS) (Section 305)

Effective Date: Date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 305

Because of the ever growing complexity of retirement plan administration, Section 305 expands the Employee Plans Compliance Resolution System (“EPCRS”) to (1) allow more types of errors to be corrected internally through self-correction, (2) apply to inadvertent IRA errors, and (3) exempt certain failures to make required minimum distributions from the otherwise applicable excise tax. For example, Section 305 allows for correction of many plan loan errors through self-correction, which are a frequent area of error and can be burdensome to correct a single loan error through the Internal Revenue Service. Section 305 is effective on the date of enactment of this Act. Any guidance or revision of guidance required by Section 305 shall be promulgated no later than 2 years after the date of enactment of this Act. Revenue Procedure 2021-30 (or any successor guidance) shall be updated to take into account the provisions of this section no later than 2 years after the date of enactment of this Act.

Eliminate the “First Day of the Month” Requirement for Governmental §457(b) Plans (Section 306)

Effective Date: Taxable years beginning after the date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 306

Under current law, participants in a governmental 457(b) plan must request changes in their deferral rate prior to the beginning of the month in which the deferral will be made. This rule does not exist for other defined contribution plans. Section 306 allows such elections to be made at any time prior to the date that the compensation being deferred is available. Section 306 is effective for taxable years beginning after the date of enactment of this Act.

One-Time Election for Qualified Charitable Distribution to Split-Interest Entity (Section 307)

Effective Date: Taxable years beginning after the date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 307

Section 307 expands the IRA charitable distribution provision to allow for a one-time, \$50,000 distribution to charities through charitable gift annuities, charitable remainder unitrusts, and charitable remainder annuity trusts, effective for distributions made in taxable years beginning after the date of enactment of this Act. Section 307 also indexes for inflation the annual IRA charitable distribution limit of \$100,000, effective for distributions made in taxable years ending after the date of enactment of this Act.

Distributions to Firefighters (Section 308)

<i>Effective Date: Distributions made after the date of enactment of this Act.</i>
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SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 308

Under current law, if an employee terminates employment after age 55 and takes a distribution from a retirement plan, the 10 percent early distribution tax does not apply. However, there is a special rule for “qualified public safety employees” in governmental plans, under which age 50 is substituted for age 55 for purposes of this exception from the 10 percent tax. This exemption applies to public sector firefighters, but not private sector firefighters. Section 308 extends the age 50 rule to private sector firefighters, who merit the same treatment for distributions. Section 308 is effective for distributions made after the date of enactment of this Act.

Exclusion of Certain Disability-Related First Responder Retirement Payments (Section 309)

<i>Effective Date: Amounts received with respect to taxable years beginning after December 31, 2026.</i>
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SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 309

Section 309 permits first responders to exclude service-connected disability pension payments from gross income after reaching retirement age. Section 309 is effective for amounts received in taxable years beginning after December 31, 2026.

Application of Top Heavy Rules to Defined Contribution Plans Covering Excludable Employees (Section 310)

Effective Date: Plan years beginning after December 31, 2023.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 310

Under current law, qualified retirement plans must pass the top-heavy test, in addition to other nondiscrimination tests. Plans that are deemed top-heavy are required to provide employees with a minimum of a 3 percent of pay nonelective contribution, which is a significant cost to small businesses. Other nondiscrimination tests that apply to 401(k) plans allow an employer to test otherwise excludable employees (e.g., those who are under age 21 and have less than 1 year of service) separately. This was intended to encourage plan sponsors to permit employees to defer earlier than the minimum age and service conditions permitted under the law because it reduces the situations where plans would fail the nondiscrimination tests if these employees were included when performing the test. However, this separate testing is not allowed for the top-heavy test. Small business retirement plans often do not cover excludable employees because, if the plan is or becomes top heavy, the employer may be required to contribute a top-heavy employer contribution for all employees who are eligible to participate in the plan, straining the budget for these small businesses. Section 310 allows an employer to perform the top-heavy test separately on the non-excludable and excludable employees. This removes the financial incentive to exclude employees from the 401(k) plan and increase retirement plan coverage to more workers. Section 310 is effective for plan years beginning after December 31, 2023.

Repayment of Qualified Birth or Adoption Distributions Limited to 3 Years (Section 311)

Effective Date: Distributions made after the date of enactment of this Act and retroactively to the 3 year period beginning on the day after the date such distribution was received.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 311

The SECURE Act included a provision that allows individuals to receive distributions from their retirement plan in the case of birth or adoption without paying the 10 percent additional tax under Code section 72(t) (known as a qualified birth or adoption distribution, or “QBAD”). The distributions can be recontributed to a retirement plan at any time and are treated as rollovers. The problem with current law is the allowance of recontributions at any time. Code section 6511 prevents a refund from being provided to a taxpayer after the period of limitations for the return has closed, which is generally a 3 year period. Thus, there would not be a mechanism under the Code allowing someone who took a birth/adoption distribution to recontribute the distribution more than 3 years later and amend their return to receive a refund for the taxes that were paid in the year of the withdrawal. Section 311 amends the QBAD provision to restrict the recontribution period to 3 years. Section 311 is effective to distributions made after the date of the enactment of this Act

and retroactively to the 3 year period beginning on the day after the date on which such distribution was received.

Employer May Rely on Employee Certifying That Deemed Hardship Distribution Conditions Met (Section 312)

Effective Date: Plan years beginning after the date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 312

Section 312 provides that, under certain circumstances, employees are permitted to self-certify that they have had an event that constitutes a hardship for purposes of taking a hardship withdrawal. This is a logical step in light of the success of the coronavirus-related distribution self-certification rules and the current hardship regulations that already permit employees to self-certify that they do not have other funds available to address a hardship. Section 312 is effective for plan years beginning after the date of enactment of this Act.

Individual Retirement Plan Statute of Limitations for Excise Tax on Excess Contributions and Certain Accumulations (Section 313)

Effective Date: Date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 313

Under current law, the statute of limitations for excise taxes imposed on excess contributions, or required minimum distribution failures starts running as of the date that a specific excise tax return (Form 5329) is filed for the violation. Individuals often are not aware of the requirement to file Form 5329, and this can lead to an indefinite period of limitations that can cause hardship for taxpayers due to the accumulation of interest and penalties (see *Paschall v. C.I.R.*, 137 T.C. 8 (2011)). In order to provide finality for taxpayers in the administration of these excise taxes, Section 313 provides that a 3 year period of limitations begins when the taxpayer files an individual tax return (Form 1040) for the year of the violation, except in the case of excess contributions, in which case the period of limitations runs 6 years from the date Form 1040 is filed. There is a further exception from this 6-year rule for taxes that arise out of a bargain sale to the IRA. In general, these changes are intended to ensure that there is a reasonable period of limitations for violations of which taxpayers were not aware and thus did not file an excise tax return, while retaining existing law in fact scenarios that involve a bargain sale. Section 313 is effective on the date of enactment of this Act.

Penalty-Free Withdrawal from Retirement Plans for Individual in Case of Domestic Abuse (Section 314)

Effective Date: Distributions made after December 31, 2023

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 314

A domestic abuse survivor may need to access his or her money in their retirement account for various reasons, such as escaping an unsafe situation. Section 314 allows retirement plans to permit participants who self-certify that they experienced domestic abuse to withdraw a small amount of money (the lesser of \$10,000, indexed for inflation, or 50 percent of the participant's account). A distribution made under Section 314 is not subject to the 10 percent tax on early distributions. Additionally, a participant has the opportunity to repay the withdrawn money from the retirement plan over 3 years and will be refunded for income taxes on money that is repaid. Section 318 is effective for distributions made after December 31, 2023.

Reform of Family Attribution Rule (Section 315)

Effective Date: Plan years beginning after December 31, 2023.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 315

Under the Code, certain related businesses must be aggregated when performing the coverage and nondiscrimination tests. The aggregation rules are generally based on the degree of common ownership of the businesses. In determining the level of ownership in a business, the tax laws have certain attribution rules whereby an individual is deemed to own stock held by other individuals or entities. Section 315 updates two stock attribution rules. The first update addresses inequities where spouses with separate businesses reside in a community property state when compared to spouses who reside in separate property states. The second update modifies the attribution of stock between parents and minor children. Section 315 is effective for plan years beginning after December 31, 2023.

Amendments to Increase Benefit Accruals Under Plan for Previous Plan Year Allowed Until Employer Tax Return Due Date (Section 316)

Effective Date: Plan years beginning after December 31, 2023.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 316

The SECURE Act permits an employer to adopt a new retirement plan by the due date of the employer's tax return for the fiscal year in which the plan is effective. Current law, however, provides that plan

amendments to an existing plan must generally be adopted by the last day of the plan year in which the amendment is effective. This precludes an employer from adding plan provisions that may be beneficial to participants. Section 316 amends these provisions to allow discretionary amendments that increase participants' benefits to be adopted by the due date of the employer's tax return. Section 316 is effective for plan years beginning after December 31, 2023.

Retroactive Elective Deferrals for Sole Proprietors (Section 317)

Effective Date: Plan years beginning after December 31, 2023.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 317

Under the SECURE Act, an employer may establish a new 401(k) plan after the end of the taxable year, but before the employer's tax filing date and treat the plan as having been established on the last day of the taxable year. Such plans may be funded by employer contributions up to the employer's tax filing date. Section 317 allows these plans, when they are sponsored by sole proprietors or single-member LLCs, to receive employee contributions up to the date of the employee's tax return filing date for the initial year. Section 317 is effective for plan years beginning after the date of enactment of this Act.

Performance Benchmarks for Asset Allocation Funds (Section 318)

Effective Date: The Department of Labor is to update its regulations no later than two years after the date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 318

The DOL's participant disclosure regulation requires that each designated investment alternative's historical performance be compared to an appropriate broad-based securities market index. However, the rule does not adequately address increasingly popular investments like target date funds that include a mix of asset classes. Section 318 directs the Labor Secretary to update the DOL's regulations so that an investment that uses a mix of asset classes can be benchmarked against a blend of broad-based securities market indices, provided (a) the index blend reasonably matches the fund's asset allocation over time, (b) the index blend is reset at least once a year, and (c) the underlying indices are appropriate for the investment's component asset classes and otherwise meet the rule's conditions for index benchmarks. This change in the disclosure rule allows better comparisons and aids participant decision-making. The DOL is to update its regulations no later than two years after enactment of this Act. Section 318 also requires DOL to report to Congress on the effectiveness of its benchmarking requirements no later than 3 years after the applicability date of the regulations.

Review and Report to Congress Relating to Reporting and Disclosure Requirements (Section 319)

Effective Date: Agency reports required to be delivered to Congress no later than three years after the date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 319

Section 319 directs the Treasury Department, DOL, and Pension Benefit Guaranty Corporation to review reporting and disclosure requirements for pension plans as soon as practicable after enactment of this Act. Section 319 further directs the agencies to make recommendations to Congress to consolidate, simplify, standardize, and improve such requirements no later than 3 years after the date of enactment of this Act.

Eliminating Unnecessary Plan Requirements Related to Unenrolled Participants (Section 320)

Effective Date: Plan years beginning after December 31, 2022.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 320

Under current law, employees eligible to participate in a retirement plan are required to receive a broad array of notices that are intended to inform them of their various options and rights under the plan. In the case of eligible employees who have not elected to participate in the plan (“unenrolled participants”), these notices – such as notices regarding the different investment options available under the plan – are generally unnecessary, and can even have adverse effects on savings and coverage.

Section 320 no longer requires employers to provide certain intermittent ERISA or Code notices to unenrolled participants who have not elected to participate in a workplace retirement plan. However, to further encourage participation of unenrolled participants, the plan is required to send (1) an annual reminder notice of the participant’s eligibility to participate in the plan and any applicable election deadlines, and (2) any otherwise required document requested at any time by the participant. This rule applies only with respect to an unenrolled participant who received the summary plan description, in connection with initial eligibility under the plan, and any other notices related to eligibility under the plan required to be furnished. Section 320 is effective for plan years beginning after December 31, 2022.

Review of Pension Risk Transfer Interpretive Bulletin (Section 321)

Effective Date: Report due from Department of Labor no later than one year after the date of enactment of the Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 321

Section 321 requires the DOL to review the current interpretive bulletin governing pension risk transfers to determine whether amendments are warranted and to report to Congress its finding, including an assessment of any risk to participant, no later than 1 year after enactment of this Act.

Tax Treatment of IRA Involved in a Prohibited Transaction (Section 322)

<i>Effective Date: Taxable years beginning after the date of enactment of this Act.</i>

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 322

When an individual engages in a prohibited transaction with respect to their IRA, the IRA is disqualified and treated as distributed to the individual, irrespective of the size of the prohibited transaction. Section 322 clarifies that if an individual has multiple IRAs, only the IRA with respect to which the prohibited transaction occurred will be disqualified. Section 322 is effective for taxable years beginning after the date of enactment of this Act.

Clarification of Substantially Equal Periodic Payment Rule (Section 323)

<i>Effective Date: For transfers, rollovers, exchanges after December 31, 2023 and effective for annuity distributions on or after the date of enactment of this Act.</i>

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 323

Current law imposes a 10 percent additional tax on early distributions from tax-preferred retirement accounts, but an exception applies to substantially equal periodic payments that are made over the account owner's life expectancy. Section 323 provides that the exception continues to apply in the case of a rollover of the account, an exchange of an annuity providing the payments, or an annuity that satisfies the required minimum distribution rules. Section 323 is effective for transfers, rollovers, exchanges after December 31, 2023 and effective for annuity distributions on or after the date of enactment of this Act.

Treasury Guidance on Rollovers (Section 324)

Effective Date: Development and release of the sample forms must be completed no later than January 1, 2025.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 324

Section 324 requires the Treasury Secretary to simplify and standardize the rollover process by issuing sample forms for direct rollovers that may be used by both the incoming and outgoing retirement plan or IRA. Development and release of the sample forms must be completed no later than January 1, 2025.

Roth Plan Distribution Rules (Section 325)

Effective Date: Elimination of pre-death Roth plan distribution requirement is effective for taxable years beginning after December 31, 2023. The new law does not apply to distributions with respect to years beginning before January 1, 2024, but are permitted to be paid on or after such date.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 325

Under current law, required minimum distributions are not required to begin prior to the death of the owner of a Roth IRA. However, pre-death distributions are required in the case of the owner of a Roth-designated account in an employer retirement plan (e.g., 401(k) plan). Section 325 eliminates the pre-death distribution requirement for Roth accounts in employer plans, effective for taxable years beginning after December 31, 2023. Section 325 does not apply to distributions that are required with respect to years beginning before January 1, 2024, but are permitted to be paid on or after such date.

Exemption to Penalty on Early Distributions from Qualified Plans for Individuals with a Terminal Illness (Section 326)

Effective Date: Distributions made after the date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 326

Under current law, an additional 10 percent tax applies to early distributions from tax-preferred retirement accounts. Section 326 provides an exception to the tax in the case of a distribution to a terminally ill individual and would be effective for distributions made after the date of enactment of this Act.

Surviving Spouse Election to Be Treated as an Employee (Section 327)

Effective Date: Calendar years beginning after December 31, 2023.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 327

Section 327 allows a surviving spouse to elect to be treated as the deceased employee for purposes of the required minimum distribution rules. Section 327 is effective for calendar years beginning after December 31, 2023.

Repeal of Direct Payment Requirement on Exclusion from Gross Income of Distributions from Governmental Plans for Health and Long-Term Care Insurance (Section 328)

Effective Date: Distributions made after the date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 328

Current law provides an exclusion from gross income (\$3,000) for a distribution from a governmental retirement plan to a public safety officer to pay for their health insurance premiums. The exclusion requires that the plan directly pay the insurance premiums. Section 328 repeals the direct payment requirement and is effective for distributions made after the date of enactment of this Act.

Modification of Eligible Age for Exemption from Early Withdrawal Penalty (Section 329)

Effective Date: Distributions made after the date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 329

The 10 percent additional tax on early distributions from tax preferred retirement savings plans does not apply to a distribution from a governmental plan to a public safety officer who is at least age 50. Section 329 extends the exception to public safety officers with at least 25 years of service with the employer sponsoring the plan and is effective for distributions made after the date of enactment of this Act.

Exemption from Early Withdrawal Penalty for Certain State and Local Government Corrections Employees (Section 330)

Effective Date: Distributions made after the date of enactment of this Act

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 330

Section 330 extends the public safety officer exception to the 10 percent early distribution tax to corrections officers who are employees of state and local governments, effective for distributions made after the date of enactment of this Act.

Special Rules for Use of Retirement Funds in Connection with Qualified Federally Declared Disasters (Section 331)

Effective Date: Disasters occurring after January 26, 2021.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 331

Section 331 provides permanent rules relating to the use of retirement funds in the case of a federally declared disaster. The permanent rules allow up to \$22,000 to be distributed from employer retirement plans or IRAs for affected individuals. Such distributions are not subject to the 10 percent additional tax and are taken into account as gross income over 3 years. Distributions can be repaid to a tax preferred retirement account. Additionally, amounts distributed prior to the disaster to purchase a home can be recontributed, and an employer is permitted to provide for a larger amount to be borrowed from a plan by affected individuals and for additional time for repayment of plan loans owed by affected individuals. Section 331 is effective for disasters occurring on or after January 26, 2021.

Employers Allowed to Replace SIMPLE Retirement Accounts with Safe Harbor §401(k) Plans During a Year (Section 332)

Effective Date: Plan years beginning after December 31, 2023.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 332

Section 332 allows an employer to replace a SIMPLE IRA plan with a SIMPLE 401(k) plan or other 401(k) plan that requires mandatory employer contributions during a plan year, and is effective for plan years beginning after December 31, 2023.

Elimination of Additional Tax on Corrective Distributions of Excess Contributions (Section 333)

Effective Date: Applies to any determination of, or affecting, liability for taxes, interest, or penalties which is made on or after the date of the enactment of this Act, without regard to whether the act (or failure to act) upon which the determination is based occurred before such date of enactment.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 333

Current law requires a distribution if too much is contributed to an IRA. The corrective distribution includes the excessive contribution and any earnings allocable to that contribution. Section 333 exempts the excess contribution and earnings allocable to the excess contribution from the 10 percent additional tax on early distributions, and is effective for any determination of, or affecting, liability for taxes, interest, or penalties that is made on or after the date of enactment of this Act, without regard to whether the act (or failure to act) upon which the determination is based occurred before such date of enactment.

Long-Term Care Contracts Purchased with Retirement Plan Distributions (Section 334)

Effective Date: Distributions made after the date which is three years after the date of enactment of the date of the Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 334

Section 334 permits retirement plans to distribute up to \$2,500 per year for the payment of premiums for certain specified long term care insurance contracts. Distributions from plans to pay such premiums are exempt from the additional 10 percent tax on early distributions. Only a policy that provides for high quality coverage is eligible for early distribution and waiver of the 10 percent tax. Section 334 is effective 3 years after date of enactment of this Act.

Corrections of Mortality Tables (Section 335)

Effective Date: Required amendments will be deemed to be made as of the date of enactment of the Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 335

Section 335 generally requires that for purposes of the minimum funding rules, a pension plan is not required to assume beyond the plan's valuation date future mortality improvements at any age greater

than 0.78 percent. The Treasury Secretary shall amend the relevant regulation on the matter within 18 months, though Section 335 shall be deemed to take effect on the date of enactment of this Act.

Report to Congress on §402(f) Notices (Section 336)

Effective Date: Report due from Comptroller of the Currency no later than 18 months after the date of enactment of the Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 336

Section 402(f) notices are given by employer retirement plans in the case of a distribution to a participant that is eligible for rollover to another tax preferred retirement account and describe distribution options and tax consequences. Section 336 requires the Government Accountability Office to issue a report to Congress on the effectiveness of section 402(f) notices within 18 months after the date of enactment of this Act.

Modification of Required Minimum Distribution Rules for Special Needs Trusts (Section 337)

Effective Date: Calendar years beginning after the date of enactment of the Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 337

The SECURE Act placed limits on the ability of beneficiaries of defined contribution retirement plans and IRAs to receive lifetime distributions after the account owner's death. Special rules apply in the case of certain beneficiaries, such as those with a disability. Section 337 clarifies that, in the case of a special needs trust established for a beneficiary with a disability, the trust may provide for a charitable organization as the remainder beneficiary. Section 337 is effective for calendar years beginning after the date of enactment of this Act.

Requirement to Send Paper Statements in Certain Cases (Section 338)

Effective Date: Plan years beginning after December 31, 2025.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 338

Section 338 amends ERISA to generally provide that, with respect to defined contribution plans, unless a participant elects otherwise, the plan is required to provide a paper benefit statement at least once annually. The other three quarterly statements required under ERISA are not subject to this rule (i.e., they can be provided electronically). For defined benefit plans, unless a participant elects otherwise, the statement that must be provided once every 3 years under ERISA must be a paper statement. The Labor Secretary must update the relevant sections of their regulations and corresponding guidance by December 31, 2024, and the annual paper statement is effective for plan years beginning after December 31, 2025.

Recognition of Tribal Government Domestic Relations Orders (Section 339)

Effective Date: Domestic relations orders received by plan administrators after December 31, 2022, including any such order which is submitted for reconsideration after such date.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 339

Section 339 adds Tribal courts to the list of courts authorized under federal law to issue qualified domestic relations orders. Section 339 is effective for domestic relations orders received by plan administrators after December 31, 2022, including any such order which is submitted for reconsideration after such date.

Defined Contribution Plan Fee Disclosure Improvements (Section 340)

Effective Date: Actions by Department of Labor due three years after of enactment.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 340

Section 340 builds on recommendations recently made to the DOL by the Government Accountability Office, and requires the agency to review its fiduciary disclosure requirements in participant-directed individual account plan regulations. A report must be submitted to Congress within 3 years on such findings, including recommendations for legislative changes.

Consolidation of Defined Contribution Plan Notices (Section 341)

Effective Date: Actions by Departments of Labor and Treasury not later than two years after date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 341

Current law requires certain retirement plan notices to be provided to participants as individual notices. Section 341 directs the Treasury and DOL Secretaries within 2 years to amend regulations to permit a plan to consolidate certain required plan notices.

Information Needed for Financial Options Risk Mitigation (Section 342)

Effective Date: Department of Labor must issue regulations not earlier than one year after date of enactment of this Act and they must be applicable not earlier than the issuance of a final rule and not later than one year after issuance of the final rule.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 342

Section 342 requires pension plan administrators to provide plan participants and retirees with critical information that would allow people considering what is best for their financial futures to compare between benefits offered under the plan and the lump sum, and would explain how the lump sum was calculated, the ramifications of accepting a lump sum, such as the loss of certain federal protections, details about the election period, where to follow up with questions, and other information. The DOL Secretary must issue regulations implementing this provision not earlier than 1 year after enactment. Such regulations must be applicable not earlier than the issuance of a final rule and not later than 1 year after issuance of a final rule.

Defined Benefit Annual Funding Notices (Section 343)

Effective Date: Plan years beginning after December 31, 2023

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 343

Section 343 aims to identify defined benefit pension plan funding issues more clearly on a plan's annual funding notice. Section 343 is effective for plan years beginning after December 31, 2023.

Report on Pooled Employer Plans (Section 344)

Effective Date: The Department of Labor study must be completed within five years.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 344

Section 344 requires the DOL Secretary to conduct a study on the new and growing pooled employer plan industry. A report on the findings of the study must be completed within 5 years, with subsequent reports completed every 5 years thereafter.

Annual Audit for Group of Plans (Section 345)

Effective Date: Date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 345

Under current law, generally, a Form 5500 for a defined contribution plan must contain an opinion from an independent qualified public accountant as to whether the plan's financial statements and schedules are fairly presented. However, no such opinion is required with respect to a plan covering fewer than 100 participants. Section 345 clarifies that plans filing under a Group of Plans need only to submit an audit opinion if they have 100 participants or more. In other words, DOL and Treasury would continue to receive full audit information on at least the number of plans as under current law. Section 345 is effective on the date of enactment of this Act.

Worker Ownership, Readiness and Knowledge (Section 346)

Effective Date: Grants to be made in fiscal years 2025 to 2029

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 346

Section 346 boosts employee ownership programs through the DOL, which may make grants to promote employee ownership through existing and new programs. Funds are authorized to be appropriated for the purpose of making grants for fiscal years 2025 to 2029.

Report by the Secretary of Labor on the Impact of Inflation on Retirement Savings (Section 347)

Effective Date: Report to be submitted by Departments of Labor and Treasury within 90 days.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 347

Section 347 directs the DOL Secretary, in consultation with the Treasury Secretary, to study the impact of inflation on retirement savings and submit a report to Congress within 90 days on the findings of the study.

Cash Balance (Section 348)

Effective Date: Plan years beginning after the date of enactment of this Act

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 348

Section 348 clarifies the application of the Code and ERISA's rules, prohibiting the backloading of benefit accruals, as they relate to hybrid plans that credit variable interest. Specifically, Section 348 clarifies that, for purposes of the applicable Code and ERISA rules, the interest crediting rate that is treated as in effect and as the projected interest crediting rate is a reasonable projection of such variable interest rate, subject to a maximum of 6 percent. This clarification will allow plan sponsors to provide larger pay credits for older longer service workers. Section 346 is effective for plan years beginning after the date of enactment of this Act.

Termination of Variable Rate Premium Indexing (Section 349)

Effective Date: Effective on date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 349

Section 349 removes the "applicable dollar amount" language in the rules for determining the premium fund target for purposes of unfunded vested benefits and replaces it with a flat \$52 for each \$1,000 of unfunded vested benefits. Section 349 is effective on the date of enactment of this Act.

Safe Harbor for Corrections of Employee Elective Deferral Failures (Section 350)

Effective Date: Errors after December 31, 2023.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 350

Under current law, employers that adopt a retirement plan with automatic enrollment and automatic escalation features could be subject to significant penalties if even honest mistakes are made. The Internal Revenue Service has issued guidance on the correction of failures relating to default enrollment of employees into retirement plans. This guidance includes a safe harbor, which expires December 31, 2023, that permits correction if notice is given to the affected employee, correct deferrals commence within certain specified time periods, and the employer provides the employee with any matching contributions that would have been made if the failure had not occurred. Employers are concerned about the lapse of the safe harbor at the end of 2023. Section 350 eases these concerns by allowing for a grace period to correct, without penalty, reasonable errors in administering these automatic enrollment and automatic escalation features. Errors must be corrected prior to 9 ½ months after the end of the plan year in which the mistakes were made. Section 350 is effective for errors after December 31, 2023.

TECHNICAL AMENDMENTS (TITLE IV)

Amendments Related to Setting Every Community Up for Retirement Enhancement (SECURE) Act of 2019 (Section 401)

Effective Date: Effective as if included in the SECURE Act of 2019.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 401

Section 401 includes three technical and five clerical amendments to the SECURE Act. These amendments are effective as if included in the section of the SECURE Act to which the amendment relates.

ADMINISTRATIVE PROVISIONS (TITLE V)

Provisions Related to Plan Amendments (Section 501)

Effective Date: Plan amendments may be made on or before the last day of the first plan year beginning on or after January 1, 2025 (2027 in the case of governmental plans).

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 501

Section 501 allows plan amendments made pursuant to this Act to be made on or before the last day of the first plan year beginning on or after January 1, 2025 (2027 in the case of governmental plans) as long as the plan operates in accordance with such amendments as of the effective date of a bill requirement or amendment. Section 501 also conforms the plan amendment dates under the SECURE Act, the CARES Act, and the Taxpayer Certainty and Disaster Tax Relief Act of 2020 to these new dates (instead of 2022 and 2025).

REVENUE PROVISIONS (TITLE VI)

SIMPLE and SEP Roth IRAs (Section 601)

<i>Effective Date: Taxable years beginning after December 31, 2022.</i>

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 601

Generally, all plans that allow pre-tax employee contributions are permitted to accept Roth contributions with one exception – SIMPLE IRAs. 401(k), 403(b), and governmental 457(b) plans are allowed to accept Roth employee contributions. Section 601 allows SIMPLE IRAs to accept Roth contributions too. In addition, aside from grandfathered salaried reduction simplified employee pension plans, under current law, simplified employee pension plans (“SEPs”) can only accept employer money and not on a Roth basis. Section 601 allows employers to offer employees the ability to treat employee and employer SEP contributions as Roth (in whole or in part). The provisions in Section 601 are effective for taxable years beginning after December 31, 2022.

Hardship Withdrawal Rules for §403(b) Plans (Section 602)

<i>Effective Date: Plan years beginning after December 31, 2023.</i>
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SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 602

Under current law, the distribution rules for 401(k) and 403(b) are different in certain ways that are historical anomalies for varied reasons. For example, for 401(k) plans, all amounts are available for a hardship distribution. For 403(b) plans, in some cases, only employee contributions (without earnings) are available for hardship distributions. Section 602 conforms the 403(b) rules to the 401(k) rules, effective for plan years beginning after December 31, 2023.

Elective Deferrals Generally Limited to Regular Contribution Limit (Section 603)

Effective Date: Taxable years beginning after December 31, 2023.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 603

Under current law, catch-up contributions to a qualified retirement plan can be made on a pre-tax or Roth basis (if permitted by the plan sponsor). Section 603 provides all catch-up contributions to qualified retirement plans are subject to Roth tax treatment, effective for taxable years beginning after December 31, 2023. An exception is provided for employees with compensation of \$145,000 or less (indexed).

Optional Treatment of Employer Matching or Nonelective Contributions as Roth Contributions (Section 604)

Effective Date: Date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 604

Under current law, plan sponsors are not permitted to provide employer matching contributions in their 401(k), 403(b), and governmental 457(b) plans on a Roth basis. Matching contributions must be on a pre-tax basis only. Section 604 allows defined contribution plans to provide participants with the option of receiving matching contributions on a Roth basis, effective on the date of enactment of this Act.

Charitable Conservation Easements (Section 605)

Effective Date: Contributions made after the date of enactment of this Act.

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 605

The tax deduction for charitable contributions of conservation easements has long played a crucial role in incentivizing the preservation of critical habitats, open spaces, and historically important areas and structures. However, since 2016 IRS has identified certain syndicated conservation easement transactions involving pass-through entities as “listed transactions” carrying a high potential for abusive tax avoidance. Section 605 disallows a charitable deduction for a qualified conservation contribution if the deduction claimed exceeds two and one-half times the sum of each partner’s relevant basis in the contributing partnership, unless the contribution meets a 3-year holding period test, substantially all of the contributing partnership is owned by members of a family, or the contribution relates to the preservation of a certified historic structure. In the case of a contribution for the preservation of a certified historic structure, a new

reporting requirement applies. Section 605 also provides taxpayers the opportunity to correct certain defects in an easement deed (excluding easements involved in abusive transactions) and makes certain changes to statute of limitations and penalty provisions. Section 605 is generally effective for contributions made after the date of enactment of this Act.

Enhancing Retiree Health Benefits in Pension Plans (Section 606)

<i>Effective Date: Transfer made on or after the date of enactment of this Act.</i>

SENATE FINANCE COMMITTEE EXPLANATION OF SECTION 606

Under current law, an employer may use assets from an overfunded pension plan to pay retiree health and life insurance benefits. These rules sunset at the end of 2025. Section 606 extends the sunset date to the end of 2032 and would permit transfers to pay retiree health and life insurance benefits provided the transfer is no more than 1.75 percent of plan assets and the plan is at least 110 percent funded. Section 606 is effective for transfers made on or after the date of enactment of this Act.

KEY DEVELOPMENTS IN 2024

During 2024 there two major developments related to required minimum distribution rules, one to provide on final year of relief for required minimum distributions for those inheriting an IRA or defined contribution plan account balance from a decedent who passed away after 2019 and the second a set of proposed regulations related to these provisions.

One Last Year of RMD Relief

Consistent with its stance from 2021 to 2023, the Internal Revenue Service (IRS) has announced, via Notice 2024-35⁴⁴, that penalties will not be imposed on taxpayers who fail to take the required minimum distributions (RMDs) from most individual retirement accounts (IRAs) and defined contribution plans inherited from decedents who passed away post-2019.

The Proposed Regulations released in 2022, addressing the amended RMD regulations for IRAs and defined contribution plans as instituted by the SECURE Act, stipulated that taxpayers inheriting an IRA or defined contribution account from an individual who passed away after 2019, and who had reached their required beginning date for distributions, were mandated to receive distributions based on the life expectancy of the designated beneficiary. This was to occur each year for the nine years following the decedent's death, with the total remaining balance to be distributed by the end of the tenth year.

⁴⁴ Notice 2024-35, April 16, 2024, <https://www.irs.gov/pub/irs-drop/n-24-35.pdf> (retrieved April 17, 2024)

Several advisors interpreted the amendments in the SECURE Act as superseding the necessity for distributions within the initial nine-year period, even if the decedent had reached their required beginning date before death. In acknowledgment of these interpretations, the IRS published Notices 2022-53 and 2023-54, exempting taxpayers from penalties for non-compliance with these distribution requirements for years 2021-2023, irrespective of whether the final regulations would uphold such obligatory distributions within the first nine years.

The IRS has now extended this relief to cover 2024 *specified distributions* as well. Section IV.C of the Notice provides the following definition of a *specified distribution*:

For purposes of this notice, a specified RMD is any distribution that, under the interpretation included in the proposed regulations, would be required to be made pursuant to §401(a)(9) in 2024 under a defined contribution plan or IRA that is subject to the rules of §401(a)(9)(H) for the year in which the employee (or designated beneficiary) died if that payment would be required to be made to:

- a designated beneficiary of an employee under the plan (or IRA owner) if: (1) the employee (or IRA owner) died in 2020, 2021, 2022, or 2023, and on or after the employee's (or IRA owner's) required beginning date, and (2) the designated beneficiary is not using the lifetime or life expectancy payments exception under §401(a)(9)(B)(iii); or
- a beneficiary of an eligible designated beneficiary (including a designated beneficiary who is treated as an eligible designated beneficiary pursuant to §401(b)(5) of the SECURE Act) if: (1) the eligible designated beneficiary died in 2020, 2021, 2022, or 2023, and (2) that eligible designated beneficiary was using the lifetime or life expectancy payments exception under §401(a)(9)(B)(iii) of the Code.⁴⁵

The Notice clarifies that a defined contribution retirement plan shall not be deemed noncompliant with the distribution provisions outlined in Internal Revenue Code (IRC) §401(a)(9) due to a failure to execute a *specified distribution* in 2024. Furthermore, the Internal Revenue Service (IRS) will not enforce the excise tax imposed under IRC §4974 for neglecting to take the required minimum distribution against beneficiaries for any *specified distribution* not taken in 2024.⁴⁶

In contrast to the previous Notices, the current Notice does not state that penalties for distributions will commence no earlier than the subsequent year, which would be 2025 in this instance. Such omissions have historically left the applicability of penalties in the following year ambiguous, with the IRS not specifying its expectations regarding the enforcement of these rules for distributions in that year. And, in fact, such penalties have not been applied in those subsequent years.

Instead, the current Notice indicates that the final regulations are projected to be applicable for determining required minimum distributions (RMDs) for calendar years starting from January 1,

⁴⁵ Notice 2024-35, April 16, 2024

⁴⁶ Notice 2024-35, April 16, 2024

2025.⁴⁷ As is discussed in the next section, those final regulations were released, so 2024 is the last year to have this relief.

Final Required Minimum Distribution Regulations

Proposed regulations were released in 2022 providing guidance for changes to required minimum distribution rules found in 2019's SECURE Act. But before the regulations could be finalized, Congress passed the SECURE 2.0 Act in 2022 which made additional changes to some of these provisions, which resulted in a two year delay in issuing final regulations.

One of the major provisions of the original SECURE Act was the elimination of most "stretch IRA" programs, requiring all funds be out of defined contribution programs (including IRAs) by 10 years after the year of death for those inheriting an account from a decedent who died after 2019.

The general rule under the SECURE Act is that so long as there is a designated beneficiary the entire balance must be distributed out of the plan by the end of the 10th year following the year of death. The 10-year rule applies regardless of whether or not the decedent had lived beyond his/her required beginning date, which is the date by which an employee or IRA owner must begin receiving required minimum distributions in most cases.

But the IRS noted that IRC §401(a)(9)(B) was not repealed or overridden by either Act. That section reads:

IRC §401(a)(9)(B) Required distribution where employee dies before entire interest is distributed.

(i) Where distributions have begun under subparagraph (A)(ii). A trust shall not constitute a qualified trust under this section unless the plan provides that if--

(I) the distribution of the employee's interest has begun in accordance with subparagraph (A)(ii), and

(II) the employee dies before his entire interest has been distributed to him,

the remaining portion of such interest will be distributed *at least as rapidly* as under the method of distributions being used under subparagraph (A)(ii) as of the date of his death.

Under the prior law, the IRS had concluded that "at least as rapidly" meant over the life expectancy of the designated beneficiary with the shortest life expectancy, assuming all beneficiaries were *designated beneficiaries*. Designated beneficiaries are individuals and look-through trusts.

- Entities (estates, charities, etc.) have a life expectancy of 0 years (not a designated beneficiary)

⁴⁷ Notice 2024-35, April 16, 2024

- Beneficiaries determined as of September 30 of the year following the year of death, which allows for dividing the inherited amounts into separate accounts for each beneficiary and/or paying out those that aren't designated beneficiaries

Many commentators had read the SECURE Act provisions to eliminate those annual distributions for accounts in pay status at the date of death and only have the 10-year rule apply

- They believed that meant no distributions would be due in the first 9 years (although distributions could be taken)
- Any remaining balance in the account would come out in year 10

This position was used by many taxpayers for 2021 RMDs for decedents who died in 2020 based on the advice of their broker, financial adviser, or tax adviser.

But the proposed regulations, issued in February 2022, held that position was in error. Rather distributions for those inheriting an IRA from those who died after 2019 and had reached their required beginning date before they died had to satisfy two separate rules:

- The annual distribution rule based on the shortest life expectancy of the designated beneficiaries (assuming all beneficiaries were designated beneficiaries) was to be used in years 1-9 just as under the pre-SECURE Act law and
- Any remaining balance had to be distributed in year 10, which was the change made by the SECURE Act per the IRS.

Those same rules applied to minor children of the deceased when they reached the age of majority (they are a special class of *eligible designated beneficiaries* under the law).

The SECURE Act allowed what was commonly referred to as stretch IRAs only for

- Benefits inherited from a decedent who died prior to 2020 and
- For certain *eligible* designated beneficiaries (surviving spouse, minor child of the deceased, disabled individual, chronically ill individual, and an individual less than 10 years younger than the deceased).

In the case of an eligible designated beneficiary, life expectancy payouts could continue for the life of the beneficiary all except for the minor child of the deceased. For the minor child, once they reached age 21 they would begin to start a 10-year countdown until all benefits had to be removed from the account, with life expectancy distributions still required for each intervening year.

However, if the eligible designated beneficiary that inherited the account dies before the account is exhausted, the next level beneficiaries would be subject to the 10-year rule.

Due to many comments received by the IRS and the fact that many individuals inheriting impacted IRAs and defined contribution plan balances in pay status from decedents dying in 2020 had not

taken distributions in 2021, the IRS released a number of relief Revenue Notices that applied to distributions that would have due in years 1-9 from 2021-2024

- Notices 2022-53, 2023-54 and 2024-35
 - Provided that no penalties would be imposed for failure to take the annual distributions
 - Also, there would be no sanctions on plans that failed to make such distributions

Final regulations⁴⁸ released in July of 2024 adopted the proposed regulations with only minor changes

- Revised required beginning dates (eventually moving the RBD to age 75 for those born in or after 1960)
- Most similar changes found in SECURE 2.0 Act
- However, decided some SECURE 2.0 issues impacting RMD needed to have proposed regulations issued

The required distributions in years 1-9 were retained in the final regulations for those inheriting the account from a deceased who had reached his/her required beginning date.

No requirement was added in the regulations to “catch up” for any distributions skipped under the Notices in 2021-2024 (some commentators had concerns the IRS might require this, but the IRS did not make any mention of picking up those missed contributions). However, the 10-year count still looks back to the date of death, and the single life expectancy determined in the year after the decedent’s death is used to compute the divisors for years 1-9.

The finalization of the rules does mean those distributions will be required in 2025 and subject to penalties and plan sanctions if not made in that year or later years. 2024 is the last year to skip distributions without consequence.

Proposed Regulations Address the Drafting Error in SECURE 2.0 for Those Born in 1959

At the same time as the above final regulations were issued, the IRS released additional proposed regulations that address issues raised by the SECURE 2.0 Act. One of the issues addressed involved a clear drafting error in the SECURE 2.0 Act that will eventually impact those born in 1959.

The problem is that, per the text of the Act, those born in 1959 attain

- Age 73 in 2032 and (*applicable age 73*)
- Age 74 in 2033 (*applicable age 75*)

⁴⁸ TD 10001, July 19, 2024

A taxpayer must take their initial required minimum distribution by April 1 of the year after the taxpayer attains his/her *applicable age*. Having two applicable ages for those in born in 1959 raises the key question of which of the two possible April 1 required beginning dates those taxpayers must use, assuming Congress does not pass a technical correction (which they had not at the time this unit was written).

IRS resolves this issue by using the lower age in the proposed regulations, assuming the law is not fixed by the time this would have an impact on those born in 1959 (April 1, 2033).

Most likely this will be addressed by Congress in a technical corrections bill, but if not the IRS has indicated which interpretation they plan to use. These proposed regulations will hopefully serve to force Congress to act to clarify this issue.

NOTES

Unit 3

Beneficial Ownership Information Reports Update

LEARNING OBJECTIVES

- Analyze client compliance with the reporting requirements based on guidance issued in the past year along with that issued earlier
- Explain to clients the reasons Congress used to justify the requirements to establish the beneficial ownership reporting requirements.
- Identify whether a particular corporation or LLC qualifies as an exempted large operating company
- List the information required to be provided in the initial and update reports on behalf of the entity, beneficial owners, and company applicants.

On January 1st, 2021, a new law was born. Buried in the William M. (Mac) Thornberry National Defense Authorization Act for Fiscal Year 2021, this law - also known as the “Corporate Transparency Act” - requires corporations, LLCs, and other entities to report beneficial owner information to the Financial Crimes Enforcement Network (FinCEN). This data will be collected in a database for future reference.

Fast forward to September 2022, when FinCEN released the final regulations⁴⁹ for the law. Reporting will officially begin on January 1st, 2024. However, it’s worth noting that there will be different rules for entities that existed before 2024 and those created in or after that year.

Though there are some exceptions to these requirements, many advisers will find that most of the small, closely held LLCs and corporations they work with will need to file these reports. And to top it off, any changes to the information provided must be updated within 30 days.

In short, this is a law that will impact many businesses across the country, so it’s important to stay informed and up-to-date on its requirements.

⁴⁹ Federal Register, Vol. 87, No. 189, 87 FR 59498, September 30, 2023, <https://www.federalregister.gov/d/2022-21020> (retrieved April 29, 2023)

WHY DID CONGRESS SEE THE NEED TO ENACT THESE RULES

Section 6402 of the Thornberry Act outlines the “Sense of Congress” regarding the justification for these provisions. That section notes, in part, that:

- More than 2,000,000 corporations and limited liability companies are being formed under the laws of the States each year;⁵⁰
- Most or all States do not require information about the beneficial owners of the corporations, limited liability companies, or other similar entities formed under the laws of the State;⁵¹
- Malign actors seek to conceal their ownership of corporations, limited liability companies, or other similar entities in the United States to facilitate illicit activity, including money laundering, the financing of terrorism, proliferation financing, serious tax fraud, human and drug trafficking, counterfeiting, piracy, securities fraud, financial fraud, and acts of foreign corruption, harming the national security interests of the United States and allies of the United States;⁵² and
- Money launderers and others involved in commercial activity intentionally conduct transactions through corporate structures in order to evade detection, and may layer such structures, much like Russian nesting “Matryoshka” dolls, across various secretive jurisdictions such that each time an investigator obtains ownership records for a domestic or foreign entity, the newly identified entity is yet another corporate entity, necessitating a repeat of the same process.⁵³

The Section goes on to explain why this situation requires Federal intervention:

- Federal legislation providing for the collection of beneficial ownership information for corporations, limited liability companies, or other similar entities formed under the laws of the States is needed to—
 - set a clear, Federal standard for incorporation practices;
 - protect vital United States national security interests;
 - protect interstate and foreign commerce;
 - better enable critical national security, intelligence, and law enforcement efforts to counter money laundering, the financing of terrorism, and other illicit activity; and
 - bring the United States into compliance with international anti-money laundering and countering the financing of terrorism standards.⁵⁴

⁵⁰ Thornberry Act §6402(1)

⁵¹ Thornberry Act §6402(2)

⁵² Thornberry Act §6402(3)

⁵³ Thornberry Act §6402(4)

⁵⁴ Thornberry Act §6402(5)

Congress explains next how this information will be used:

- Beneficial ownership information collected under the amendments made by this title is sensitive information and will be directly available only to authorized government authorities, subject to effective safeguards and controls, to—
 - facilitate important national security, intelligence, and law enforcement activities; and
 - confirm beneficial ownership information provided to financial institutions to facilitate the compliance of the financial institutions with anti-money laundering, countering the financing of terrorism, and customer due diligence requirements under applicable law.⁵⁵

The program is to be handled by the Treasury Department with Congress providing:

- Consistent with applicable law, the Secretary of the Treasury shall—
 - maintain the information obtained in a secure, nonpublic database, using information security methods and techniques that are appropriate to protect nonclassified information systems at the highest security level; and
 - take all steps, including regular auditing, to ensure that government authorities accessing beneficial ownership information do so only for authorized purposes consistent with this title; and
- in prescribing regulations to provide for the reporting of beneficial ownership information, the Secretary shall, to the greatest extent practicable consistent with the purposes of this title—
 - seek to minimize burdens on reporting companies associated with the collection of beneficial ownership information;
 - provide clarity to reporting companies concerning the identification of their beneficial owners; and
 - collect information in a form and manner that is reasonably designed to generate a database that is highly useful to national security, intelligence, and law enforcement agencies and Federal functional regulators.⁵⁶

Note that while Treasury is required to “seek” to minimize the burden, that doesn’t mean the burden will be minimal (the fact the agency seeks something doesn’t mean they will find a way to do it). Contrast this with the final charge which doesn’t have such a modifier, but rather requires the agency to create a “highly useful” database for the intended users of the information.

⁵⁵ Thornberry Act §6402(6)

⁵⁶ Thornberry Act §6402(7) and (8)

In an FAQ issued on March 24, 2023,⁵⁷ FinCEN summarized the reasons why this information must be reported to the Treasury Department:

Very few U.S. states or territories require companies to disclose information about their beneficial owners—the individuals who own or control companies. This lack of transparency allows criminals, corrupt officials, and other bad actors to hide their identities and launder illicit funds through the United States using shell and front companies. This in turn hurts ordinary Americans because the lack of transparency results in an uneven playing field for honest and legitimate U.S. businesses. The inaccessibility of beneficial ownership information also makes it hard for law enforcement to track and prosecute criminal activity.

In 2021, Congress, with bipartisan support, enacted the Corporate Transparency Act to address this problem. The Corporate Transparency Act requires certain types of U.S. and foreign entities to report information about their beneficial owners to the Treasury Department’s Financial Crimes Enforcement Network, commonly known as FinCEN. FinCEN is responsible for safeguarding the U.S. financial system from illicit use. Subject to strict safeguards and controls, FinCEN will disclose the reported beneficial ownership information to certain authorized government authorities, financial institutions, and other authorized users.

By collecting beneficial ownership information and sharing it with law enforcement, financial institutions, and other authorized users, FinCEN is making it harder for bad actors to hide or benefit from their ill-gotten gains. Companies that report beneficial ownership information will contribute to this important goal.⁵⁸

We will look at the rules that were issued as part of the reporting regulations issued in September of 2022, as well as the additional guidance published by the agency in March of 2023 on the FinCEN website.

FILING REQUIREMENTS

The FAQ cited above is FinCEN’s attempt to provide a plain English explanation of the law and how it will impact entities required to file. In addition to the FAQ, at the same time FinCEN published two other single page documents that provide summaries of key issues.

⁵⁷ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, March 24, 2023, https://www.fincen.gov/sites/default/files/shared/BOI_FAQs_FINAL_508.pdf (retrieved April 28, 2023)

⁵⁸ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, March 24, 2023, pp. 1-2

The first item is a one page PDF⁵⁹ showing the key reporting dates under this program:

BENEFICIAL OWNERSHIP INFORMATION REPORT FILING DATES

 FinCEN will begin accepting beneficial ownership information reports from reporting companies¹ that are not exempt² on January 1, 2024, the effective date of the reporting requirement.



Existing reporting companies

Created or registered to do business in the United States before January 1, 2024.

Reports due by **January 1, 2025**.



INITIAL REPORTS

New reporting companies

Created or registered to do business in the United States on or after January 1, 2024.

Reporting companies created or registered **on or after January 1, 2024** and **before January 1, 2025**, have **90 calendar days** after receiving actual or public notice that their company's creation or registration is effective to file their initial BOI reports.

Reporting companies created or registered **on or after January 1, 2025**, will have **30 calendar days** from receipt of actual or public notice that their creation or registration is effective to file their initial BOI reports.



UPDATED REPORTS

Required when there is a change to previously reported information about the reporting company itself or its beneficial owners.

Updated reports due within **30 calendar days** after a change occurs.



CORRECTED REPORTS

Required when previously reported information was inaccurate when filed.

Corrected reports due within **30 calendar days** after the reporting company becomes aware or has reason to know of an inaccuracy.

More information can be found at www.fincen.gov/boi.

¹ There are two types of reporting companies: domestic and foreign. A **domestic reporting company** is any entity that is a corporation, a limited liability company (LLC), or created by the filing of a document with a secretary of state or any similar office under the law of a U.S. state or Indian tribe. A **foreign reporting company** is any entity that is a corporation, LLC, or other entity that is formed under the law of a foreign country and registered to do business in any U.S. state or tribal jurisdiction by the filing of a document with a secretary of state or any similar office under the law of a U.S. state or Indian tribe.

² There are 23 categories of entities that are exempt from the definition of reporting company. Please review FinCEN's final beneficial ownership information reporting rule, as well as FinCEN's reference materials published on www.fincen.gov/boi, for more details.



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⁵⁹ "Beneficial Ownership Interest Report Filing Dates," Financial Crimes Enforcement Network, United States Treasury, December 1, 2023, https://www.fincen.gov/sites/default/files/shared/BOI%20Reporting%20Filing%20Dates_11.23_508C.pdf (retrieved December 2, 2023)

The second one-page document outlines a number of key questions⁶⁰ to be answered.

BENEFICIAL OWNERSHIP REPORTING – KEY QUESTIONS

This document is explanatory only and does not supplement or modify any obligations imposed by statute or regulation. Please refer to the beneficial ownership information reporting final rule, available at www.fincen.gov/boi, for details on specific provisions.



1. Does my company have to report its beneficial owners?

While certain types of entities are exempt, if you are a small corporation or LLC, you will likely be required to report your beneficial ownership information to FinCEN. A key factor in determining whether your company will have to report is whether you had to file a document with your state's secretary of state or a similar office to create your company or, for foreign companies, register it to do business in the United States.



2. Who is a beneficial owner of my company?

A beneficial owner is any individual who exercises *substantial control* over your company, or who *owns or controls at least 25 percent* of your company.



3. Does my company have to report its company applicants?

There can be up to two individuals who qualify as company applicants — (1) the individual who directly files the document that creates, or first registers, the reporting company; and (2) the individual that is primarily responsible for directing or controlling the filing of the relevant document.

Your company is only required to report its company applicants if it is created or registered on or after January 1, 2024.



4. What specific information does my company need to report?

A reporting company will need to provide: (1) its legal name and any trade name or DBA; (2) its address; (3) the jurisdiction in which it was formed or first registered, depending on whether it's a U.S. or foreign company; and (4) its Taxpayer Identification Number (TIN).

For each of your company's beneficial owners and each company applicant (if required), your company will need to provide the individual's: (1) legal name; (2) birthdate; (3) address (in most cases, a home address); and (4) an identifying number from a driver's license, passport, or other approved document for each individual, as well as an image of the document that the number is from.



5. When and how should my company file its initial report?

If your company already exists as of January 1, 2024, it must file its initial BOI report by January 1, 2025. If your company is created or registered to do business in the United States on or after January 1, 2024, and before January 1, 2025, it will have 90 calendar days after receiving actual or public notice that the company's creation or registration is effective to file its initial BOI report. If your company is created or registered on or after January 1, 2025, it will have 30 calendar days from actual or public notice that its creation or registration is effective to file its initial BOI report.



6. What if there are changes to or inaccuracies in reported information?

Your company will have 30 days to report any changes to reported information. For updates, the 30 days start from when the relevant change occurs. For corrections, the 30 days start after you become aware of, or have reason to know of, an inaccuracy in a prior report.



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⁶⁰"Beneficial Ownership Reporting – Key Questions," Financial Crimes Enforcement Network, United States Treasury, March 24, 2023, https://www.fincen.gov/sites/default/files/shared/BOI_Reporting_Key_Questions_Published_508C.pdf (retrieved April 28, 2023)

We will look at the FAQ, which has more detailed information, below, along with citing back to the law and regulations underlying the FAQ's answers.

When Are Initial Reports to Be Filed?

A key issue to note is that no reports will need to be filed until 2024. FAQ Question 3 provides:

3. Should my company report beneficial ownership information now?

No. No one needs to report beneficial ownership information to FinCEN until January 1, 2024. FinCEN is currently not accepting any beneficial ownership information reports.⁶¹

While Reg. 31 CFR 1010.380(a)(1) provides the detail for initial reports, the FAQ provides a more simplified description of the initial filing dates:

B. 2. When do I need to report my company's beneficial ownership information to FinCEN?

A reporting company created or registered to do business **before January 1, 2024**, will have until **January 1, 2025** to file its initial beneficial ownership information report.

A reporting company created or registered **on or after January 1, 2024, and before January 1, 2025**, will have **90 calendar days** after receiving notice of the company's creation or registration to file its initial BOI report. This 90-calendar day deadline runs from the time the company receives actual notice that its creation or registration is effective, or after a secretary of state or similar office first provides public notice of its creation or registration, whichever is earlier.

Reporting companies created or registered **on or after January 1, 2025**, will have **30 calendar days** from actual or public notice that the company's creation or registration is effective to file their initial BOI reports with FinCEN.

[Updated December 1, 2023]⁶²

⁶¹ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, December 1, 2023, Question B.2, <https://www.fincen.gov/boi-faqs> (retrieved December 2, 2023)

⁶² "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, March 24, 2023, p. 2

This explanation omits what happens if an entity that is exempt from filing (classes that will be listed later) no longer meets the criteria for exemption, providing:

Any entity that no longer meets the criteria for any exemption under paragraph (c)(2) of this section shall file a report within 30 calendar days after the date that it no longer meets the criteria for any exemption.⁶³

It is important to note that while entities in existence before 2024 can file initial reports as late as January 1, 2025, entities formed in 2024 will not be able to wait until that date.

EXAMPLE – ENTITY CREATED IN 2024

ABC, LLC received actual notice of its creation from the appropriate state authority on December 31, 2023. ABC, LLC's deadline to file its initial report is **January 1, 2025** as the entity was in existence before January 1, 2024.

XYZ, LLC received actual notice of its creation on January 2, 2024 from the appropriate state authority. While formed just two days later than ABC, LLC, this LLC's deadline is much earlier, needing to file within 90 days after the date of formation, or by **April 1, 2024**.

Later, LLC received actual notice of its creation on January 2, 2025 from the appropriate state authority. Since it was formed after 2024, it has only 30 days to file its initial report, or by **February 1, 2025**.

The process by which a company established or registered after January 1, 2024, determines its date of creation or registration is elaborated upon in question G.5. of the FAQ, which was incorporated on December 12, 2023.

G. 5. How does a company created or registered after January 1, 2024, determine its date of creation or registration?

The date of creation or registration for a reporting company is the earlier of the date on which: (1) the reporting company receives actual notice that its creation (or registration) has become effective; or (2) a secretary of state or similar office first provides public notice, such as through a publicly accessible registry, that the domestic reporting company has been created or the foreign reporting company has been registered.

FinCEN recognizes that there are varying state filing practices. In certain states, automated systems provide notice of creation or registration to newly created or registered companies. In other states, no actual notice of creation or registration is provided, and newly created companies receive notice through the public posting of state records. FinCEN believes that individuals who create or register reporting companies will likely stay apprised of creation or registration notices or publications,

⁶³ 31 CFR 1010.380(a)(1)(iv)

given those individuals' interest in establishing an operating business or engaging in the activity for which the reporting company is created.⁶⁴

Extension of Time to File for Entities Formed in 2024

The Financial Crimes Enforcement Network (FinCEN) has issued a proposed rule⁶⁵ which was made final with no changes on November 30, 2023,⁶⁶ extending the deadline for covered entities formed in 2024 to file their initial beneficial ownership information reports under the Corporate Transparency Act. The new deadline is 90 days after formation, an increase from the previous 30-day requirement.

Concurrently, the agency issued a news release⁶⁷ detailing the new proposed rule.

The news release outlines the proposed revision of the rule as follows:

The Financial Crimes Enforcement Network (FinCEN) is issuing a Notice of Proposed Rulemaking (NPRM) to extend the deadline for certain reporting companies to file their initial beneficial ownership information (BOI) reports. FinCEN is proposing to amend its final BOI Reporting Rule to provide 90 days for reporting companies created or registered in 2024 to file their initial reports, instead of 30 days.⁶⁸

The release further clarifies that this rule solely impacts entities created or registered in 2024. Due dates for initial reports for entities created or registered before or after 2024 would remain unchanged.

The proposed rule would not make any other changes to the final BOI Reporting Rule: reporting companies created or registered before January 1, 2024, would have until January 1, 2025, to file their initial BOI reports with FinCEN, and entities created or registered on or after January 1, 2025, would have 30 days to file their initial BOI reports.⁶⁹

⁶⁴ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

⁶⁵ RIN: 1506-AB62, "Beneficial Ownership Information Reporting Deadline Extension for Reporting Companies Created or Registered in 2024," September 27, 2023 (to be published in the Federal Register on September 28, 2023), <https://public-inspection.federalregister.gov/2023-21226.pdf> (Retrieved September 27, 2023)

⁶⁶ RIN 1506-AB62, 31 CFR Part 1010, November 30, 2023

⁶⁷ "FinCEN issues a Notice of Proposed Rulemaking to extend the deadline for certain companies to file their beneficial ownership information reports," FinCEN website, September 27, 2023, <https://www.fincen.gov/news/news-releases/fincen-issues-notice-proposed-rulemaking-extend-deadline-certain-companies-file> (retrieved September 27, 2023)

⁶⁸ "FinCEN issues a Notice of Proposed Rulemaking to extend the deadline for certain companies to file their beneficial ownership information reports," FinCEN website, September 27, 2023

⁶⁹ "FinCEN issues a Notice of Proposed Rulemaking to extend the deadline for certain companies to file their beneficial ownership information reports," FinCEN website, September 27, 2023

FinCEN's press release provides the following rationale for this proposed change:

FinCEN believes the proposed extension will have significant benefits. An extension will give reporting companies created or registered in 2024 additional time to understand their regulatory obligations under the Reporting Rule and obtain the required information. They will also have additional time to become familiar with FinCEN's guidance and educational materials located at www.fincen.gov/boi and resolve questions that may arise in the process of completing their initial BOI reports. After January 1, 2025, however, reporting companies should be familiar with BOI reporting requirements and be in a better position to file required BOI reports on a timely basis.⁷⁰

In its explanation of the proposed rule, the Agency acknowledges that the delay will result in a less immediate availability of a complete database of entities for law enforcement access compared to the original rule. This statement suggests that the agency may be disinclined to further postpone such reporting due to law enforcement considerations. Moreover, the agency is actively soliciting comments on the perceived low impact of this delay on law enforcement interests, as well as any other potential adverse effects of this postponement.

Although FinCEN believes that providing this additional time and flexibility for reporting companies created or registered in 2024 to file their initial BOI reports will benefit reporting companies and their service providers, FinCEN recognizes that the extension could cause a delay in submissions to the BOI database in the first year of its operation. For example, under the proposed rule, if entities are created or registered on December 31, 2024, they would have until April 1, 2025 (90 days after December 31, 2024) to submit their initial BOI reports. In contrast, under the Reporting Rule, law enforcement could expect all compliant reporting companies created or registered on or before December 31, 2024, to have submitted their initial BOI reports by January 30, 2025 (30 days after December 31, 2024). With all of that taken into account, FinCEN still believes that the potential adverse effects of any such delay in the first year of the program are outweighed by the relief they will provide for small businesses, as explained above. FinCEN solicits comment on this assessment, and on whether there are any other potential consequences of the extension that it has not identified.⁷¹

⁷⁰ "FinCEN issues a Notice of Proposed Rulemaking to extend the deadline for certain companies to file their beneficial ownership information reports," FinCEN website, September 27, 2023

⁷¹ RIN: 1506-AB62, "Beneficial Ownership Information Reporting Deadline Extension for Reporting Companies Created or Registered in 2024," September 27, 2023

As revised, CTA rule §1010.380(a) reads as follows:

(a) Reports required; timing of reports—

(1) Initial report. Each reporting company shall file an initial report in the form and manner specified in paragraph (b) of this section as follows:

(i) (A) Any domestic reporting company created on or after January 1, 2024, and before January 1, 2025, shall file a report within 90 calendar days of the earlier of the date on which it receives actual notice that its creation has become effective or the date on which a secretary of state or similar office first provides public notice, such as through a publicly accessible registry, that the domestic reporting company has been created.

(B) Any domestic reporting company created on or after January 1, 2025, shall file a report within 30 calendar days of the earlier of the date on which it receives actual notice that its creation has become effective or the date on which a secretary of state or similar office first provides public notice, such as through a publicly accessible registry, that the domestic reporting company has been created.

(ii) (A) Any entity that becomes a foreign reporting company on or after January 1, 2024, and before January 1, 2025, shall file a report within 90 calendar days of the earlier of the date on which it receives actual notice that it has been registered to do business or the date on which a secretary of state or similar office first provides public notice, such as through a publicly accessible registry, that the foreign reporting company has been registered to do business.

(B) Any entity that becomes a foreign reporting company on or after January 1, 2025, shall file a report within 30 calendar days of the earlier of the date on which it receives actual notice that it has been registered to do business or the date on which a secretary of state or similar office first provides public notice, such as through a publicly accessible registry, that the foreign reporting company has been registered to do business.⁷²

⁷² Rule §1010.380(a)(1) as revised, November 30, 2023

Reporting Company

The law requires certain entities to file these reports. Roughly reporting companies can be divided into two broad categories:

Type	Definition
Domestic reporting company	Any entity that is: (A) a corporation; (B) a limited liability company; or (C) created by the filing of a document with a secretary of state or any similar office under the law of a State or Indian tribe. ⁷³
Foreign reporting company	Any entity that is: (A) a corporation, limited liability company, or other entity; (B) formed under the law of a foreign country; and (C) registered to do business in any State or tribal jurisdiction by the filing of a document with a secretary of state or any similar office under the law of a State or Indian tribe. ⁷⁴

The FAQ provides the following details on reporting companies:

7. What companies will be required to report beneficial ownership information to FinCEN?

Certain companies — referred to as “reporting companies” — will be required to report their beneficial ownership information to FinCEN. There are two types of reporting companies — domestic reporting companies and foreign reporting companies.

A domestic reporting company is defined as —

- a corporation,
- a limited liability company, or
- any other entity created by the filing of a document with a secretary of state or any similar office under the law of a state or Indian tribe.

A foreign reporting company is any entity that is —

- a corporation, limited liability company, or other entity formed under the law of a foreign country, AND
- registered to do business in any U.S. state or in any Tribal jurisdiction, by the filing of a document with a secretary of state or any similar office under the law of a U.S. state or Indian tribe.

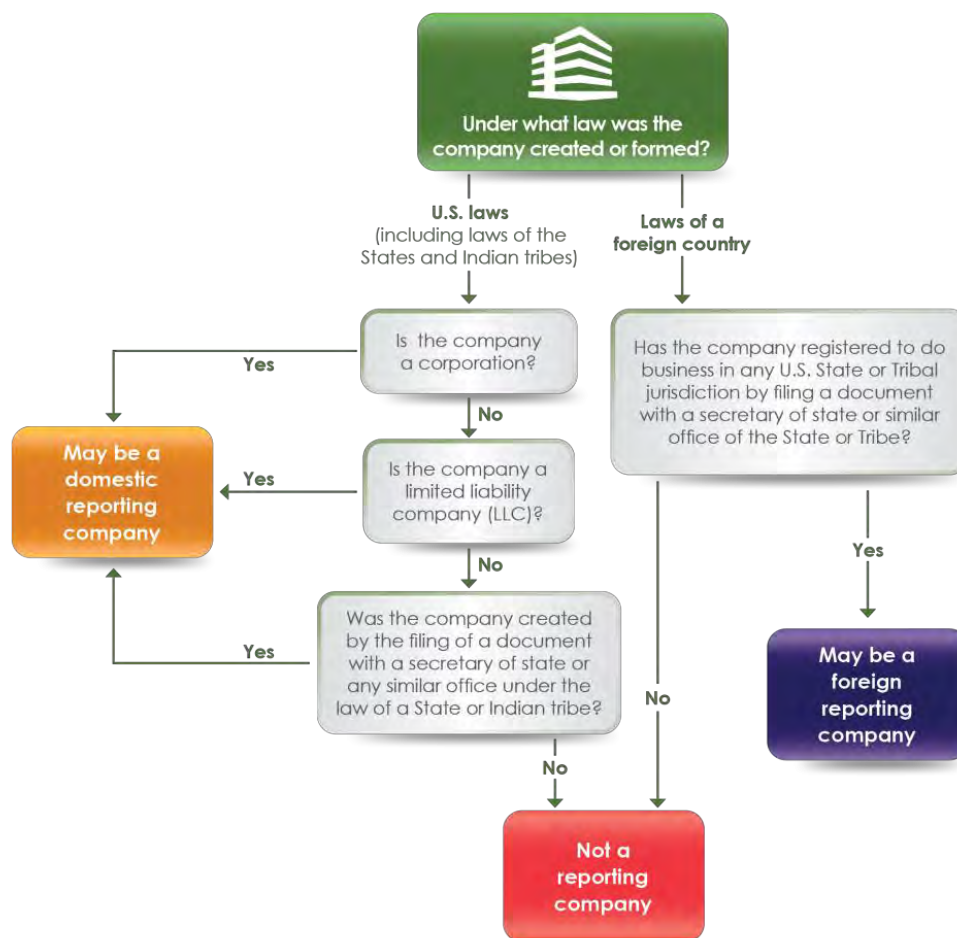
⁷³ 31 CFR 1010.380(c)

⁷⁴ 31 CFR 1010.380(c)

If you had to file a document with a state or Indian Tribal-level office such as a secretary of state to create your company, or to register it to do business if it is a foreign company, then your company is a reporting company, unless an exemption applies.

For the definitions of both domestic and foreign reporting companies, a “state” means any state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, American Samoa, Guam, the U.S. Virgin Islands, and any other commonwealth, territory, or possession of the United States.⁷⁵

In September FinCEN added this chart to a revised version of the FAQ to show reporting company obligations.⁷⁶



⁷⁵ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, March 24, 2023, p. 3

⁷⁶ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p. 4

Entities registered or created in a U.S. territory can be a reporting company in the same manner as ones created or registered in any state or the District of Columbia:

C. 7. Can a company created or registered in a U.S. territory be considered a reporting company?

Yes. In addition to companies in the 50 states and the District of Columbia, a company that is created or registered to do business by the filing of a document with a U.S. territory's secretary of state or similar office, and that does not qualify for any exemptions to the reporting requirements, is required to report beneficial ownership information to FinCEN. U.S. territories are the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, American Samoa, Guam, and the U.S. Virgin Islands.⁷⁷

The Act does not offer broad exemptions from filing the BOI report, regardless of the nature of the entity's activities or its revenue. As indicated in question C.5., which was introduced in the December 12 FAQ update:

C. 5. Does the activity or revenue of a company determine whether it is a reporting company?

Sometimes. A reporting company is (1) any corporation, limited liability company, or other similar entity that was created in the United States by the filing of a document with a secretary of state or similar office (in which case it is a domestic reporting company), or any legal entity that has been registered to do business in the United States by the filing of a document with a secretary of state or similar office (in which case it is a foreign reporting company), that (2) does not qualify for any of the exemptions provided under the Corporate Transparency Act. An entity's activities and revenue, along with other factors in some cases, can qualify it for one of those exemptions. For example, there is an exemption for certain inactive entities, and another for any company that reported more than \$5 million in gross receipts or sales in the previous year and satisfies other exemption criteria. Neither engaging solely in passive activities like holding rental properties, for example, nor being unprofitable necessarily exempts an entity from the BOI reporting requirements.

FinCEN's Small Entity Compliance Guide provides additional information concerning exemptions in Chapter 1.2, "Is my company exempt from the reporting requirements?"⁷⁸

⁷⁷ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised January 12, 2024

⁷⁸ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

Several entities are exempt from filing this report, but only during the period the entity qualifies for the exemption. The FAQ provides the following detail:

8. Are there exemptions from the reporting requirement?

Yes. The Corporate Transparency Act exempts 23 types of entities from the beneficial ownership information reporting requirement. Below is a list of the types of entities that are exempt —

- (i) Certain types of securities reporting issuers.
- (ii) A U.S. governmental authority.
- (iii) Certain types of banks.
- (iv) Federal or state credit unions as defined in section 101 of the Federal Credit Union Act.
- (v) Any bank holding company as defined in section 2 of the Bank Holding Company Act of 1956, or any savings and loan holding company as defined in section 10(a) of the Home Owners' Loan Act.
- (vi) Certain types of money transmitting or money services businesses.
- (vii) Any broker or dealer, as defined in section 3 of the Securities Exchange Act of 1934, that is registered under section 15 of that Act (15 U.S.C. 78o).
- (viii) Securities exchanges or clearing agencies as defined in section 3 of the Securities Exchange Act of 1934, and that is registered under sections 6 or 17A of that Act.
- (ix) Certain other types of entities registered with the Securities and Exchange Commission under the Securities Exchange Act of 1934.
- (x) Certain types of investment companies as defined in section 3 of the Investment Company Act of 1940, or investment advisers as defined in section 202 of the Investment Advisers Act of 1940.
- (xi) Certain types of venture capital fund advisers.
- (xii) Insurance companies defined in section 2 of the Investment Company Act of 1940.
- (xiii) State-licensed insurance producers with an operating presence at a physical office within the United States, and authorized by a State, and subject to supervision by a State's insurance commissioner or a similar official or agency.

- (xiv) Commodity Exchange Act registered entities.
- (xv) Any public accounting firm registered in accordance with section 102 of the Sarbanes-Oxley Act of 2002.
- (xvi) Certain types of regulated public utilities.
- (xvii) Any financial market utility designated by the Financial Stability Oversight Council under section 804 of the Payment, Clearing, and Settlement Supervision Act of 2010.
- (xviii) Certain pooled investment vehicles.
- (xix) Certain types of tax-exempt entities.
- (xx) Entities assisting a tax-exempt entity described in (xix) above.
- (xxi) Large operating companies with at least 20 full-time employees, more than \$5,000,000 in gross receipts or sales, and an operating presence at a physical office within the United States.
- (xxii) The subsidiaries of certain exempt entities.
- (xxiii) Certain types of inactive entities that were in existence on or before January 1, 2020, the date the Corporate Transparency Act was enacted.

Many of these exempt entities are already regulated by federal and/or state government, and many already disclose their beneficial ownership information to a governmental authority.

Additional information about the entities that are exempt can be found in the Beneficial Ownership Information Reporting Regulations at 31 CFR § 1010.380(c)(2).

You should consult the text of the regulations, which include specific criteria for the exemptions, before concluding that an entity qualifies for an exemption.⁷⁹

The last paragraph of the answer to question 8 is one to pay attention to, as there are specific requirements for each of the categories. We will look at some of the exceptions you are more likely to run into below.

⁷⁹ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, March 24, 2023, pp. 3-5

Nonetheless, if there is no reporting company involved, such as a separate entity like a single-member LLC, reporting becomes unnecessary. Question C.6, introduced in the December 12 FAQ update, directly addresses the issue of whether a sole proprietorship qualifies as a reporting company:

C. 6. Is a sole proprietorship a reporting company?

No, unless a sole proprietorship was created (or, if a foreign sole proprietorship, registered to do business) in the United States by filing a document with a secretary of state or similar office. An entity is a reporting company only if it was created (or, if a foreign company, registered to do business) in the United States by filing such a document. Filing a document with a government agency to obtain (1) an IRS employer identification number, (2) a fictitious business name, or (3) a professional or occupational license does not create a new entity, and therefore does not make a sole proprietorship filing such a document a reporting company.⁸⁰

Large Operating Company

The exception that will apply most often is the one that applies to *large operating companies*, found at 31 CFR §1010.380(c)(2)(xxi) and 31 USC §5336(a)(11)(B)(xxi). To qualify for this exemption, all of the following three criteria must be met:

- Employ more than 20 employees on a full-time basis in the United States;⁸¹
- Filed federal income tax returns in the previous year that reported more than \$5,000,000 in gross receipts or sales in the aggregate, including the receipts or sales of
 - other entities owned by the entity; and
 - other entities through which the entity operates;⁸² and
- Has an operating presence at a physical office in the United States.⁸³

The final rules provide more details on meeting the 20 full-time employee test. The test borrows definitions found in the regulations for the applicable large employer (ALE) provisions of the Affordable Care Act (ACA) found at Treasury Reg. §§54.4980H-1(a) (which provides definitions of employees and full-time employees) and 54.4980H-3 (which determines full-time employees under the ACA for the ALE rules). Some key issues to note are:

- The definition of an *employer* under Reg. §54.4980H-1(a)(16) provides for treating all members of certain related party groups as employing all members of the related party group. Specifically, the regulation provides “For purposes of determining whether an employer is an applicable large

⁸⁰ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

⁸¹ 31 USC §5336(a)(11)(B)(xxi)(I)

⁸² 31 USC §5336(a)(11)(B)(xxi)(II)

⁸³ 31 USC §5336(a)(11)(B)(xxi)(I)(III)

employer, all persons treated as a single employer under section 414(b), (c), (m), or (o) are treated as a single employer. Thus, all employees of a controlled group of entities under section 414(b) or (c), an affiliated service group under section 414(m), or an entity in an arrangement described under section 414(o), are taken into account in determining whether the members of the controlled group or affiliated service group together are an applicable large employer.”

- A *full time employee* is defined generally as an employee who is employed an average of at least 30 hours a week in a calendar month,⁸⁴ with 130 hours per month being treated as equivalent of being employed on average at least 30 hours a week in a calendar month.⁸⁵

One modification to the ACA rules is that the definition of United States is changed to use the definition found at 31 USC §1010(hhh). That definition defines the United States as “[t]he States of the United States, the District of Columbia, the Indian lands (as that term is defined in the Indian Gaming Regulatory Act), and the Territories and Insular Possessions of the United States.” Under the ACA the definition of United States is the one found at IRC §7701(a)(9)⁸⁶ which limits the definition to only the States of the United States and the District of Columbia.

However, the FAQ update on November 16 clarified that related companies cannot combine their employees to meet the 20-employee test.⁸⁷

L. 4. If I own a group of related companies, can I consolidate employees across those companies to meet the criteria of a large operating company exemption from the reporting company definition?

No. The large operating company exemption requires that the entity itself employ more than 20 full-time employees in the United States and does not permit consolidation of this employee count across multiple entities.

FinCEN’s Small Entity Compliance Guide includes a checklist for this exemption (see exemption #21).

The final rule also provides more details on the \$5,000,000 test found in the statute. 31 CFR §1010.380(c)(2)(xxi)(C) provides:

(C) Filed a Federal income tax or information return in the United States for the previous year demonstrating more than \$5,000,000 in gross receipts or sales, as reported as gross receipts or sales (net of returns and allowances) on the entity’s IRS Form 1120, consolidated IRS Form 1120, IRS Form 1120–S, IRS Form 1065, or other applicable IRS form, excluding gross receipts or sales from sources outside the United States, as determined under Federal income tax principles. For an entity that is part of an affiliated group of corporations within the meaning of 26 U.S.C. 1504

⁸⁴ Treasury Reg. §54-4980H-1(a)(21)(i)

⁸⁵ Treasury Reg. §54-4980H-1(a)(21)(ii)

⁸⁶ Treasury Reg. §54-4980H-1(a)(48)

⁸⁷ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p. 4

that filed a consolidated return, the applicable amount shall be the amount reported on the consolidated return for such group.

Subsidiary of Certain Exempt Entities

Another exempt category consists of any entity whose ownership interests are controlled or owned, directly or indirectly, by one of the following entities that qualify on their own for exemption under the law and regulations:⁸⁸

- Securities reporting issuer;
- Governmental authority;
- Bank;
- Credit union;
- Depository institution holding company;
- Money services business;
- Broker or dealer in securities;
- Securities exchange or clearing agency;
- Other Exchange Act registered entity;
- Investment company or investment adviser;
- Venture capital fund adviser;
- Insurance company;
- State-licensed insurance producer;
- Commodity Exchange Act registered entity;
- Accounting firm (registered under Section 102 of the Sarbanes-Oxley Act);
- Public utility;
- Financial market utility;
- Tax-exempt entity; or

⁸⁸ 31 USC §5336(a)(11)(B)(xxii)

- Large operating company.⁸⁹

Note that each of those definitions has detailed technical requirements, so be sure to consult the final rule to determine whether the owning entity in fact is itself exempt.

In the January 4, 2024 update to the FAQ, FinCEN clarified that the subsidiary must be *entirely* owned or controlled by the exempt entity.

L. 6. Does a subsidiary whose ownership interests are partially controlled by an exempt entity qualify for the subsidiary exemption?

No. If an exempt entity controls some but not all of the ownership interests of the subsidiary, the subsidiary does not qualify. To qualify, a subsidiary's ownership interests must be fully, 100 percent owned or controlled by an exempt entity.

A subsidiary whose ownership interests are controlled or wholly owned, directly or indirectly, by certain exempt entities is exempt from the BOI reporting requirements. In this context, control of ownership interests means that the exempt entity entirely controls all of the ownership interests in the reporting company in the same way that an exempt entity must wholly own all of a subsidiary's ownership interests for the exemption to apply.⁹⁰

Inactive Entity

A special category which exists solely to create a category of “grandfathered” exempt entities to avoid having long forgotten entities run afoul of these rules is the inactive entity category. Such an entity must meet *all* of the following criteria:

- Was in existence on or before January 1, 2020; (thus, no more entities of this type can be created)
- Is not engaged in active business;
- Is not owned by a foreign person, whether directly or indirectly, wholly or partially;
- Has not experienced any change in ownership in the preceding twelve-month period;
- Has not sent or received any funds in an amount greater than \$1,000, either directly or through any financial account in which the entity or any affiliate of the entity had an interest, in the preceding twelve-month period; and

⁸⁹ 31 USC §5336(a)(11)(B)(xxii)

⁹⁰ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised January 4, 2024

- Does not otherwise hold any kind or type of assets, whether in the United States or abroad, including any ownership interest in any corporation, limited liability company, or other similar entity.⁹¹

If an individual created or creates a new LLC or corporation on or after January 1, 2020, that entity will need to comply with the registration rules until the entity is dissolved unless it is otherwise exempt. The fact that it does nothing and never will do anything will not exempt such entities from facing potential consequences if they fail to comply with this law.

Trusts

The reporting requirements for trusts have been a source of concern for many CPAs. FinCEN's November FAQ update provides some guidance on these matters.

The first question examines the circumstances under which various types of trusts may be considered reporting companies.

C. 3. Are certain corporate entities, such as statutory trusts, business trusts, or foundations, reporting companies?

It depends. A domestic entity such as a statutory trust, business trust, or foundation is a reporting company only if it was created by the filing of a document with a secretary of state or similar office. Likewise, a foreign entity is a reporting company only if it filed a document with a secretary of state or a similar office to register to do business in the United States.

State laws vary on whether certain entity types, such as trusts, require the filing of a document with the secretary of state or similar office to be created or registered.

- If a trust is created in a U.S. jurisdiction that requires such filing, then it is a reporting company, unless an exemption applies.

Similarly, not all states require foreign entities to register by filing a document with a secretary of state or a similar office to do business in the state.

- However, if a foreign entity has to file a document with a secretary of state or a similar office to register to do business in a state, and does so, it is a reporting company, unless an exemption applies.

Entities should also consider if any exemptions to the reporting requirements apply to them. For example, a foundation may not be required to report beneficial

⁹¹ 31 USC §5336(a)(11)(B)(xxiii)

ownership information to FinCEN if the foundation qualifies for the tax-exempt entity exemption.

Chapter 1 of FinCEN's Small Entity Compliance Guide ("Does my company have to report its beneficial owners?") may assist companies in identifying whether they need to report.⁹²

The FAQ also clarifies that simply registering with a court of law to establish the court's authority over the trust does not, in itself, make the trust a reporting company for BOI purposes.

C. 4. Is a trust considered a reporting company if it registers with a court of law for the purpose of establishing the court's jurisdiction over any disputes involving the trust?

No. The registration of a trust with a court of law merely to establish the court's jurisdiction over any disputes involving the trust does not make the trust a reporting company.⁹³

Parent Companies Cannot File a Single Report

The September 29 FAQ clarified that a parent company *cannot* file a single report on behalf of its group of companies—each entity must file its own report.⁹⁴

G. 2. Can a parent company file a single BOI report on behalf of its group of companies?

No. Any company that meets the definition of a reporting company and is not exempt is required to file its own BOI report.⁹⁵

In the December 12 FAQ update, FinCEN also emphasized that a reporting company is typically not obligated to report information concerning its parent or subsidiary companies:

F. 7. Does a reporting company have to report information about its parent or subsidiary companies?

No, though if a special reporting rule applies, the reporting company may report a parent company's name instead of beneficial ownership information. A reporting company usually must report information about itself, its beneficial owners, and, for

⁹² "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, pp. 5-6

⁹³ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p. 6

⁹⁴ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p. 20

⁹⁵ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised September 29, 2023

reporting companies created or registered on or after January 1, 2024, its company applicants. However, under a special reporting rule, a reporting company may report a parent company's name in lieu of information about its beneficial owners if its beneficial owners only hold their ownership interest in the reporting company through the parent company and the parent company is an exempt entity.

Chapter 4 of FinCEN's Small Entity Compliance Guide ("What specific information does my company need to report?") provides additional information on what must be reported to FinCEN. Chapter 4.2 ("What do I report if a special reporting rule applies to my company?") specifically provides details on what information must be reported pursuant to special reporting rules.⁹⁶

Reports Must Be Filed Even if Same Information Was Reported to the IRS, a State, or a Bank

In the December 12, 2023 FAQ update, FinCEN reiterated that this report must be filed, even if identical information has previously been provided to the IRS, a state agency, or the entity's banking institution.

F. 9. Have I met FinCEN's BOI reporting obligation if I filed a form or report that provides beneficial ownership information to a state office, a financial institution, or the IRS?

No. Reporting companies must report beneficial ownership information directly to FinCEN. Congress enacted a law, the Corporate Transparency Act, that requires the reporting of beneficial ownership information directly to FinCEN. State or local governments, financial institutions, and other federal agencies, such as the IRS, may separately require entities to report certain beneficial ownership information. However, by law, those requirements are not a substitute for reporting beneficial ownership information to FinCEN.⁹⁷

⁹⁶ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

⁹⁷ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

Beneficial Owner

Under the law, information about each “beneficial owner” of a non-exempt entity must be reported to FinCEN, with any changes in that information timely reported as well. So a key issue is the definition of a beneficial owner, found at 31 USC §5336(a)(3)(A). That law provides:

(3) Beneficial owner.— The term “ beneficial owner ”—

(A) means, with respect to an entity, an individual who, directly or indirectly, through any contract, arrangement, understanding, relationship, or otherwise—

(i) exercises substantial control over the entity; or

(ii) owns or controls not less than 25 percent of the ownership interests of the entity;

The final rule provides the following definition of what constitutes *substantial control*:

(1) **Substantial control**—(i) Definition of substantial control. An individual exercises substantial control over a reporting company if the individual:

(A) Serves as a senior officer of the reporting company;

(B) Has authority over the appointment or removal of any senior officer or a majority of the board of directors (or similar body);

(C) Directs, determines, or has substantial influence over important decisions made by the reporting company, including decisions regarding:

(1) The nature, scope, and attributes of the business of the reporting company, including the sale, lease, mortgage, or other transfer of any principal assets of the reporting company;

(2) The reorganization, dissolution, or merger of the reporting company;

(3) Major expenditures or investments, issuances of any equity, incurrence of any significant debt, or approval of the operating budget of the reporting company;

(4) The selection or termination of business lines or ventures, or geographic focus, of the reporting company;

(5) Compensation schemes and incentive programs for senior officers;

(6) The entry into or termination, or the fulfillment or non-fulfillment, of significant contracts;

(7) Amendments of any substantial governance documents of the reporting company, including the articles of incorporation or similar formation documents, bylaws, and significant policies or procedures; or

(D) Has any other form of substantial control over the reporting company.⁹⁸

Per the final rule, such substantial control can be exercised in any of the following manners:

(ii) Direct or indirect exercise of substantial control. An individual may directly or indirectly, including as a trustee of a trust or similar arrangement, exercise substantial control over a reporting company through:

(A) Board representation;

(B) Ownership or control of a majority of the voting power or voting rights of the reporting company;

(C) Rights associated with any financing arrangement or interest in a company;

(D) Control over one or more intermediary entities that separately or collectively exercise substantial control over a reporting company;

(E) Arrangements or financial or business relationships, whether formal or informal, with other individuals or entities acting as nominees; or

(F) any other contract, arrangement, understanding, relationship, or otherwise.⁹⁹

The final rule also provides details about what constitutes ownership for purposes of determining if someone is a beneficial owner:

(2) Ownership Interests—(i) Definition of ownership interest. The term “ownership interest” means:

(A) Any equity, stock, or similar instrument; preorganization certificate or subscription; or transferable share of, or voting trust certificate or certificate of deposit for, an equity security, interest in a joint venture, or certificate of interest in a business trust; in each such case, without regard to whether any

⁹⁸ 31 CFR 1010.380(d)(1)(i)

⁹⁹ 31 CFR 1010.380(d)(1)(ii)

such instrument is transferable, is classified as stock or anything similar, or confers voting power or voting rights;

(B) Any capital or profit interest in an entity;

(C) Any instrument convertible, with or without consideration, into any share or instrument described in paragraph (d)(2)(i)(A), or (B) of this section, any future on any such instrument, or any warrant or right to purchase, sell, or subscribe to a share or interest described in paragraph (d)(2)(i)(A), or (B) of this section, regardless of whether characterized as debt;

(D) Any put, call, straddle, or other option or privilege of buying or selling any of the items described in paragraph (d)(2)(i)(A), (B), or (C) of this section without being bound to do so, except to the extent that such option or privilege is created and held by a third party or third parties without the knowledge or involvement of the reporting company; or

(E) Any other instrument, contract, arrangement, understanding, relationship, or mechanism used to establish ownership.¹⁰⁰

A person's ownership or control of an interest can be established by any of the following:

(ii) Ownership or control of ownership interest. An individual may directly or indirectly own or control an ownership interest of a reporting company through any contract, arrangement, understanding, relationship, or otherwise, including:

(A) Joint ownership with one or more other persons of an undivided interest in such ownership interest;

(B) Through another individual acting as a nominee, intermediary, custodian, or agent on behalf of such individual;

(C) With regard to a trust or similar arrangement that holds such ownership interest:

(1) As a trustee of the trust or other individual (if any) with the authority to dispose of trust assets;

(2) As a beneficiary who:

(i) Is the sole permissible recipient of income and principal from the trust; or

(ii) Has the right to demand a distribution of or withdraw substantially all of the assets from the trust; or

¹⁰⁰ 31 CFR 1010.380(d)(2)(i)

(3) As a grantor or settlor who has the right to revoke the trust or otherwise withdraw the assets of the trust; or

(D) Through ownership or control of one or more intermediary entities, or ownership or control of the ownership interests of any such entities, that separately or collectively own or control ownership interests of the reporting company.¹⁰¹

The calculation of the percentage of such ownership interests is also provided for in the final rule:

(iii) Calculation of the total ownership interests of a reporting company. In determining whether an individual owns or controls at least 25 percent of the ownership interests of a reporting company, the total ownership interests that an individual owns or controls, directly or indirectly, shall be calculated as a percentage of the total outstanding ownership interests of the reporting company as follows:

(A) Ownership interests of the individual shall be calculated at the present time, and any options or similar interests of the individual shall be treated as exercised;

(B) For reporting companies that issue capital or profit interests (including entities treated as partnerships for federal income tax purposes), the individual's ownership interests are the individual's capital and profit interests in the entity, calculated as a percentage of the total outstanding capital and profit interests of the entity;

(C) For corporations, entities treated as corporations for federal income tax purposes, and other reporting companies that issue shares of stock, the applicable percentage shall be the greater of:

(1) the total combined voting power of all classes of ownership interests of the individual as a percentage of total outstanding voting power of all classes of ownership interests entitled to vote, or

(2) the total combined value of the ownership interests of the individual as a percentage of the total outstanding value of all classes of ownership interests; and

(D) If the facts and circumstances do not permit the calculations described in either paragraph (d)(2)(iii)(B) or (C) to be performed with reasonable certainty, any individual who owns or controls 25 percent or more of any class or type of ownership interest of a reporting company shall be deemed to own or control 25 percent or more of the ownership interests of the reporting company.¹⁰²

¹⁰¹ 31 CFR 1010.380(d)(2)(ii)

¹⁰² 31 CFR 1010.380(d)(2)(iii)

EXAMPLE – OWNERSHIP INTEREST OF A CORPORATION

An individual currently owns 35% of the voting stock of the corporation. However, he also has an option to obtain another 10% interest that he can exercise at any time over the next five years but hasn't exercised yet.

To calculate the individual's total ownership interest in the reporting company, we need to consider the regulations issued by FinCEN for the Beneficial Owner Reporting rules found in the Corporate Transparency Act.

Since the corporation issues shares of stock, we need to apply 31 CFR §1010.380(d)(2)(iii)(C) to calculate the individual's ownership percentage. We need to determine whether the individual's total combined voting power of all classes of ownership interests or the total combined value of the ownership interests is greater.

As the individual currently owns 35% of the voting stock of the corporation, we can calculate his total combined voting power as:

Total combined voting power = 35%

If the individual exercises his option to obtain another 10% interest, his total combined voting power would be:

Total combined voting power = 35% + 10% = 45%

Thus, under 31 CFR §1010.380(d)(2)(iii)(C), the individual's ownership interest in the reporting company would be the greater of the total combined voting power or the total combined value of the ownership interests.

Therefore, if the corporation has only one class of stock outstanding and each share of stock has the same voting power and value, the individual's ownership interest in the reporting company would be 45%.

The FAQ provides the following information on beneficial interests:

9. Who is a beneficial owner of a reporting company?

In general, a beneficial owner is any individual (1) who directly or indirectly exercises "substantial control" over the reporting company, or (2) who directly or indirectly owns or controls 25 percent or more of the "ownership interests" of the reporting company.

Whether an individual has "substantial control" over a reporting company depends on the power they may exercise over a reporting company. For example, an individual will have substantial control of a reporting company if they direct, determine, or exercise substantial influence over, important decisions the reporting company makes. In addition, any senior officer is deemed to have substantial control over a reporting company. Other rights or responsibilities may also constitute substantial control. Additional information about the definition of substantial control and who qualifies as exercising substantial control can be found in the

Beneficial Ownership Information Reporting Regulations at 31 CFR §1010.380(d)(1).

“Ownership interests” generally refer to arrangements that establish ownership rights in the reporting company, including simple shares of stock as well as more complex instruments. Additional information about ownership interests, including indirect ownership, can be found in the Beneficial Ownership Information Reporting Regulations at 31 CFR §1010.380(d)(2).¹⁰³

The FAQ, in a footnote, clarifies the definition of a “senior officer”:

The term “senior officer” means any individual holding the position or exercising the authority of a president, chief financial officer, general counsel, chief executive officer, chief operating officer, or any other officer, regardless of official title, who performs a similar function. 31 CFR 1010.380(f)(8).¹⁰⁴

FinCEN provides some examples in the FAQ of applying these rules:

EXAMPLE 1 – FAQ QUESTION 9

Example 1: The reporting company is a limited liability company (LLC). You are the sole owner and president of the company and make important decisions for the company. No one else owns or controls ownership interests in your company or exercises substantial control over your company.

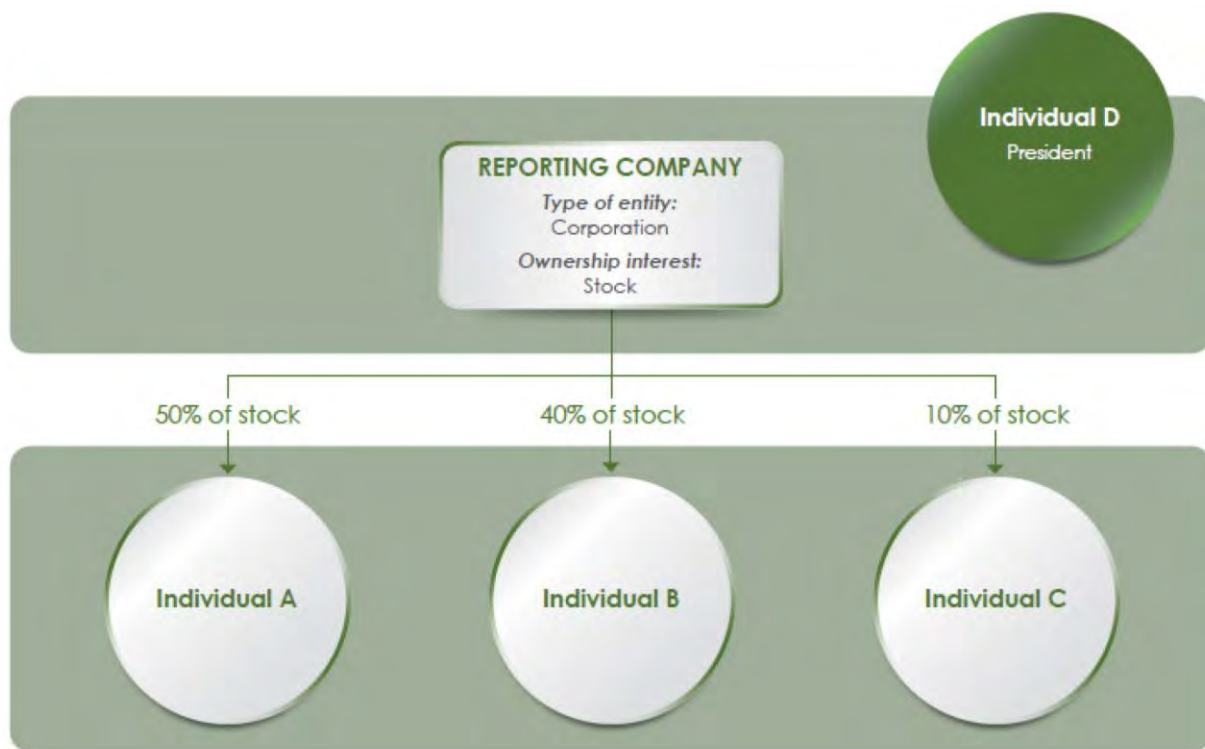
You are a beneficial owner of the reporting company in two different ways, assuming no other facts. First, you exercise substantial control over the company because you are a senior officer of the company (the president) and because you make important decisions for the company. Second, you are also a beneficial owner because you own 25 percent or more of the reporting company’s ownership interests.

Because no one else owns or controls ownership interests in your LLC or exercises substantial control over it, and assuming there are no other facts to consider, you are the only beneficial owner of this reporting company, and your information must be reported to FinCEN.

¹⁰³ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, March 24, 2023, p. 5

¹⁰⁴ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, March 24, 2023, p. 14

The second example uses the following illustration to help show the entity's structure:



EXAMPLE 2 – FAQ QUESTION 9

Example 2: The reporting company is a corporation. The company's total outstanding ownership interests are shares of stock. Three people (Individuals A, B, and C) own 50 percent, 40 percent, and 10 percent of the stock, respectively, and one other person (Individual D) acts as the President for the company, but does not own any stock.

Assuming there are no other facts, Individuals A, B, and D are all beneficial owners of the company and their information must be reported. Individual C is not a beneficial owner.

Individual A owns 50 percent of the company's stock and therefore is a beneficial owner because they own 25 percent or more of the company's ownership interests. Individual B owns 40 percent of the company's stock and therefore is a beneficial owner because they own 25 percent or more of the company's ownership interests.

Individual C is not a company officer and does not directly or indirectly exercise any substantial control over the company. Individual C also owns 10 percent of your company's stock, which is less than the 25 percent or greater interest needed to qualify as a beneficial owner by virtue of ownership interests. Individual C is therefore not a beneficial owner of the company.

Individual D is the president of the company and is therefore a beneficial owner. As a senior officer of the company, Individual D exercises substantial control, regardless of whether the individual owns or controls 25 percent or more of the company's ownership interests.

EXAMPLE 3 – FAQ QUESTION 9

Example 3: The reporting company is a corporation owned by four individuals who each own 25 percent of the company's ownership interests (e.g., shares of stock). Four other individuals serve as the reporting company's CEO, CFO, COO, and general counsel, respectively, none of whom hold any of the company's ownership interests.

In this example, there are eight beneficial owners. All four of the individuals who each own 25 percent of the company's ownership interests are beneficial owners of the company by virtue of their holdings in it, even if they exercise no substantial control over it. The CEO, CFO, COO, and general counsel are all senior officers and therefore exercise substantial control over the reporting company, making them beneficial owners as well.

The November 16 FAQ also adds the following chart that can be used to determine substantial control.¹⁰⁵

SUBSTANTIAL CONTROL



¹⁰⁵ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p.8

The November 16 FAQ in addition provided this graphic on ownership interests.¹⁰⁶



Accountant and Attorney as Beneficial Owners

The November 16 FAQ added the following Q&A regarding whether and under what conditions an entity's attorney and/or accountant should be listed as a beneficial owner.¹⁰⁷

D. 6. Is my accountant or lawyer considered a beneficial owner?

Accountants and lawyers generally do not qualify as beneficial owners, but that may depend on the work being performed.

Accountants and lawyers who provide general accounting or legal services are not considered beneficial owners because ordinary, arms-length advisory or other third-party professional services to a reporting company are not considered to be

¹⁰⁶ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p.11

¹⁰⁷ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p.10

“substantial control” (see Question D.2). In addition, a lawyer or accountant who is designated as an agent of the reporting company may qualify for the “nominee, intermediary, custodian, or agent” exception from the beneficial owner definition.

However, an individual who holds the position of general counsel in a reporting company is a “senior officer” of that company and is therefore a beneficial owner. *FinCEN’s Small Entity Compliance Guide includes a checklist to help determine whether an individual qualifies for an exception to the beneficial owner definition (see Chapter 2.4, “Who qualifies for an exception from the beneficial owner definition?”).*

Board of Director Members

The September 29 FAQ update provided guidance on the treatment of members of an entity’s board of directors as beneficial owners.¹⁰⁸

D. 9. Is a member of a reporting company’s board of directors always a beneficial owner of the reporting company?

No. A beneficial owner of a company is any individual who, directly or indirectly, exercises substantial control over a reporting company, or who owns or controls at least 25 percent of the ownership interests of a reporting company.

Whether a particular director meets any of these criteria is a question that the reporting company must consider on a director-by-director basis.

FinCEN’s Small Entity Compliance Guide includes additional information on how to determine if an individual qualifies as a beneficial owner in Chapter 2, “Who is a beneficial owner of my company?”. This chapter includes separate sections with more information about substantial control and ownership interest: Chapter 2.1 “What is substantial control?” and Chapter 2.2 “What is ownership interest?”

Partnership Representative and Tax Matters Partner

The September 29 FAQ update provides the following guidance for the treatment of partnership representatives under the BBA audit regime.¹⁰⁹

D. 10. Is a reporting company’s designated “partnership representative” or “tax matters partner” a beneficial owner?

It depends. A reporting company’s “partnership representative,” as defined in 26 U.S.C. 6223, or “tax matters partner,” as the term was previously defined in now-repealed 26 U.S.C. 6231(a)(7), is not automatically a beneficial owner of the

¹⁰⁸ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p.12

¹⁰⁹ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p.12

reporting company. However, such an individual may qualify as a beneficial owner of the reporting company if the individual exercises substantial control over the reporting company, or owns or controls at least 25 percent of the company's ownership interests.

Chapter 2 of FinCEN's Small Entity Compliance Guide ("Who is a beneficial owner of my company?") has additional information on how to determine if an individual qualifies as a beneficial owner of a reporting company.

Note that a "partnership representative" or "tax matters partner" serving in the role of a designated agent of the reporting company may qualify for the "nominee, intermediary, custodian, or agent" exception from the beneficial owner definition.

FinCEN's Small Entity Compliance Guide includes additional information on such exemptions in Chapter 2.4, "Who qualifies for an exception from the beneficial owner definition?"

What if Beneficial Owners Don't Provide the Necessary Information

In December 2023, FinCEN introduced two Q&As addressing the challenge of non-cooperative beneficial owners who either furnish incorrect information or decline to provide such information to the entity tasked with filing the report. Unfortunately, the responses provided in both cases do not offer substantial reassurance.

The initial question pertains to the extent to which the company can depend on information received from various parties. It concludes that the entity has a responsibility to ensure the accuracy of the information provided.

K. 4. Is a reporting company responsible for ensuring the accuracy of the information that it reports to FinCEN, even if the reporting company obtains that information from another party?

Yes. It is the responsibility of the reporting company to identify its beneficial owners and company applicants, and to report those individuals to FinCEN. At the time the filing is made, each reporting company is required to certify that its report or application is true, correct, and complete. Accordingly, FinCEN expects that reporting companies will take care to verify the information they receive from their beneficial owners and company applicants before reporting it to FinCEN.¹¹⁰

The second question addresses the scenario in which a beneficial owner or company applicant chooses to withhold information, and FinCEN suggests that the entity must take steps to ensure they

¹¹⁰ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

will have the required information. Such language implies that FinCEN envisions entities putting agreements in place to take action against uncooperative beneficial owners.

K. 5. What should a reporting company do if a beneficial owner or company applicant withholds information?

While FinCEN recognizes that much of the information required to be reported about beneficial owners and company applicants will be provided to reporting companies by those individuals, reporting companies are responsible for ensuring that they submit complete and accurate beneficial ownership information to FinCEN. Starting January 1, 2024, reporting companies will have a legal requirement to report beneficial ownership information to FinCEN.

Existing reporting companies should engage with their beneficial owners to advise them of this requirement, obtain required information, and revise or consider putting in place mechanisms to ensure that beneficial owners will keep reporting companies apprised of changes in reported information, if necessary. Beneficial owners and company applicants should also be aware that they may face penalties if they willfully cause a reporting company to fail to report complete or updated beneficial ownership information.

Persons considering creating or registering legal entities that will be reporting companies should take steps to ensure that they have access to the beneficial ownership information required to be reported to FinCEN, and that they have mechanisms in place to ensure that the reporting company is kept apprised of changes in that information.¹¹¹

Ownership in Dispute

In an update to the FAQ published on January 12, FinCEN gave guidance on how a reporting company is to handle the situation of filing reports if there is a legal dispute regarding the ownership of the company.

D. 11. What should a reporting company report if its ownership is in dispute?

If ownership of a reporting company is the subject of active litigation and an initial BOI report has not been filed, a person authorized by the company to file its beneficial ownership information should comply with the requirements by reporting:

- all individuals who exercise substantial control over the company, and
- all individuals who own or control, or have a claim to ownership or control of, at least 25 percent ownership interests in the company.

¹¹¹ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

If an initial BOI report has been filed, and if the resolution of the litigation leads to the reporting company having different beneficial owners from those reported (for example, because some individuals' claims to ownership or control have been rejected), the reporting company must file an updated BOI report within 30 calendar days of resolution of the litigation.¹¹²

What if a Corporate Entity Owns or Controls More Than 25% of the Reporting Company

FinCEN clarified in an FAQ question how a reporting company where a corporation owns or controls more than 25% of the company.

D. 12. Who does a reporting company report as a beneficial owner if a corporate entity owns or controls 25 percent or more of the ownership interests of the reporting company?

Ordinarily, such a reporting company reports the individuals who indirectly either (1) exercise substantial control over the reporting company or (2) own or control at least 25 percent of the ownership interests in the reporting company through the corporate entity. It should not report the corporate entity that acts as an intermediate for the individuals.

For an example of how to calculate the percentage of ownership interests an individual owns or controls in a reporting company if the individual's ownership interests are held through an intermediate entity, please review example 4 in Chapter 2.3, "What steps can I take to identify my company's beneficial owners?" of FinCEN's Small Entity Compliance Guide.

Two special rules create exceptions to this general rule in very specific circumstances:

1. A reporting company may report the name(s) of an exempt entity or entities in lieu of an individual beneficial owner who owns or controls ownership interests in the reporting company entirely through ownership interests in the exempt entity or entities; or
2. If the beneficial owners of the reporting company and the intermediate company are the same individuals, a reporting company may report the FinCEN identifier and full legal name of an intermediate company through which an individual is a beneficial owner of the reporting company.

¹¹² "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised January 12, 2024

FinCEN’s Small Entity Compliance Guide includes additional information about these special reporting rules (see Chapter 4.2, “What do I report if a special reporting rule applies to my company?”).¹¹³

Individuals Not Treated as Beneficial Owners

Even if an individual would qualify as a beneficial owner under the above rules, they may be in an excluded class found in 31 USC §5336(a)(3)(B). Those excluded are:

- A minor child, as defined in the State in which the entity is formed, if the information of the parent or guardian of the minor child is reported in accordance with this section;
- An individual acting as a nominee, intermediary, custodian, or agent on behalf of another individual;
- An individual acting solely as an employee of a corporation, limited liability company, or other similar entity and whose control over or economic benefits from such entity is derived solely from the employment status of the person;
- An individual whose only interest in a corporation, limited liability company, or other similar entity is through a right of inheritance; or
- A creditor of a corporation, limited liability company, or other similar entity, unless the creditor meets the requirements of ownership discussed earlier (that is, simply being a creditor won’t make someone a beneficial owner).¹¹⁴

The final rules provide clarification on the application of these exclusions. First, the determination of whether an individual is a minor child is made under the law of the State or Indian tribe in which a domestic reporting company is created or a foreign reporting company is first registered.¹¹⁵

The employee exception will not apply if the individual is a senior officer as described in the FAQ footnote cited earlier and 31 CFR 1010.380(f)(8).¹¹⁶

The right of inheritance rule only applies to a *future* interest—it would not serve to exclude the person from being a beneficial owner once the interest has passed to the individual.¹¹⁷

The final rule also clarified that someone is considered a creditor “solely through rights or interests for the payment of a predetermined sum of money, such as a debt incurred by the reporting

¹¹³ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised January 12, 2024

¹¹⁴ 31 USC §5336(a)(3)(B)

¹¹⁵ 31 CFR 1010.380(d)(3)(i)

¹¹⁶ 31 CFR 1010.380(d)(3)(iii)

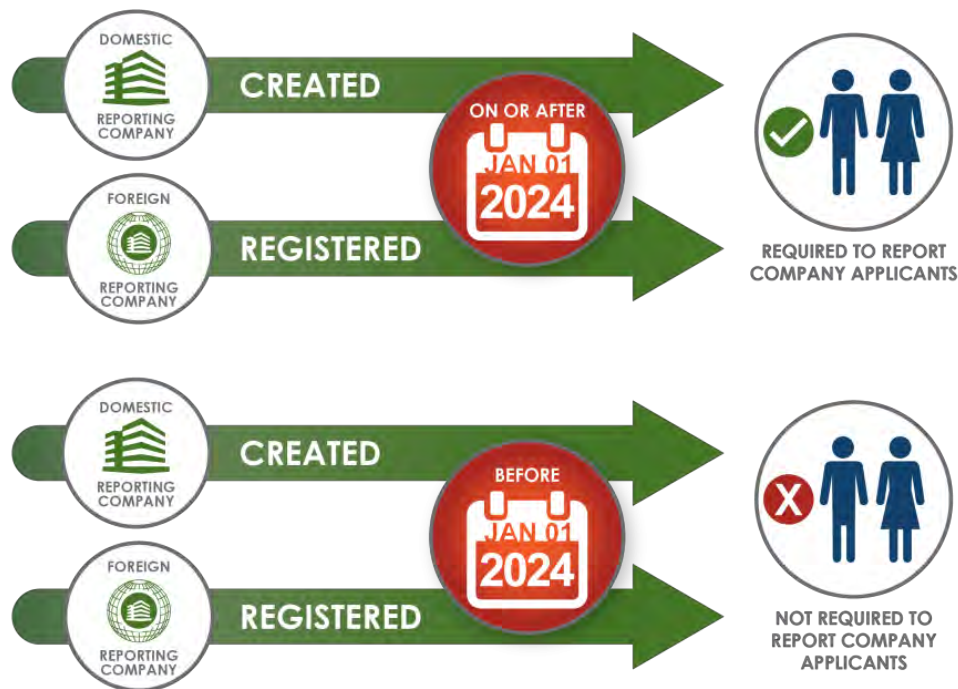
¹¹⁷ 31 CFR 1010.380(d)(3)(iv)

company, or a loan covenant or other similar right associated with such right to receive payment that is intended to secure the right to receive payment or enhance the likelihood of repayment.”¹¹⁸

Company Applicants

Information on “company applicants” will need to be reported about its company applicants if the entity is created or registered on or after January 1, 2024, but such information is not required to be submitted for entities created before that date.¹¹⁹

The FAQ provides the following chart illustrating this point.¹²⁰



A *company applicant* is defined as follows in the final rule:

(e) **Company applicant.** For purposes of this section, the term “company applicant” means:

- (1) For a domestic reporting company, the individual who directly files the document that creates the domestic reporting company as described in paragraph (c)(1)(i) of this section;

¹¹⁸ 31 CFR 1010.380(d)(3)(v)

¹¹⁹ 31 CFR 1010.380(b)(1)(ii) and (b)(2)(iv)

¹²⁰ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p.15

(2) For a foreign reporting company, the individual who directly files the document that first registers the foreign reporting company as described in paragraph (c)(1)(ii) of this section; and

(3) Whether for a domestic or a foreign reporting company, the individual who is primarily responsible for directing or controlling such filing if more than one individual is involved in the filing of the document.¹²¹

The FAQ provides:

10. Will a reporting company need to report any other information in addition to information about its beneficial owners?

Yes. The information that needs to be reported, however, depends on when the company was created or registered.

- If a reporting company is created or registered on or after January 1, 2024, the reporting company will need to report information about itself, its beneficial owners, and its company applicants.
- If a reporting company was created or registered before January 1, 2024, the reporting company only needs to provide information about itself and its beneficial owners. The reporting company does not need to provide information about its company applicants.

11. Who is a company applicant of a reporting company?

There can be up to two individuals who qualify as company applicants —

- the individual who directly files the document that creates, or first registers, the reporting company; and
- the individual that is primarily responsible for directing or controlling the filing of the relevant document.

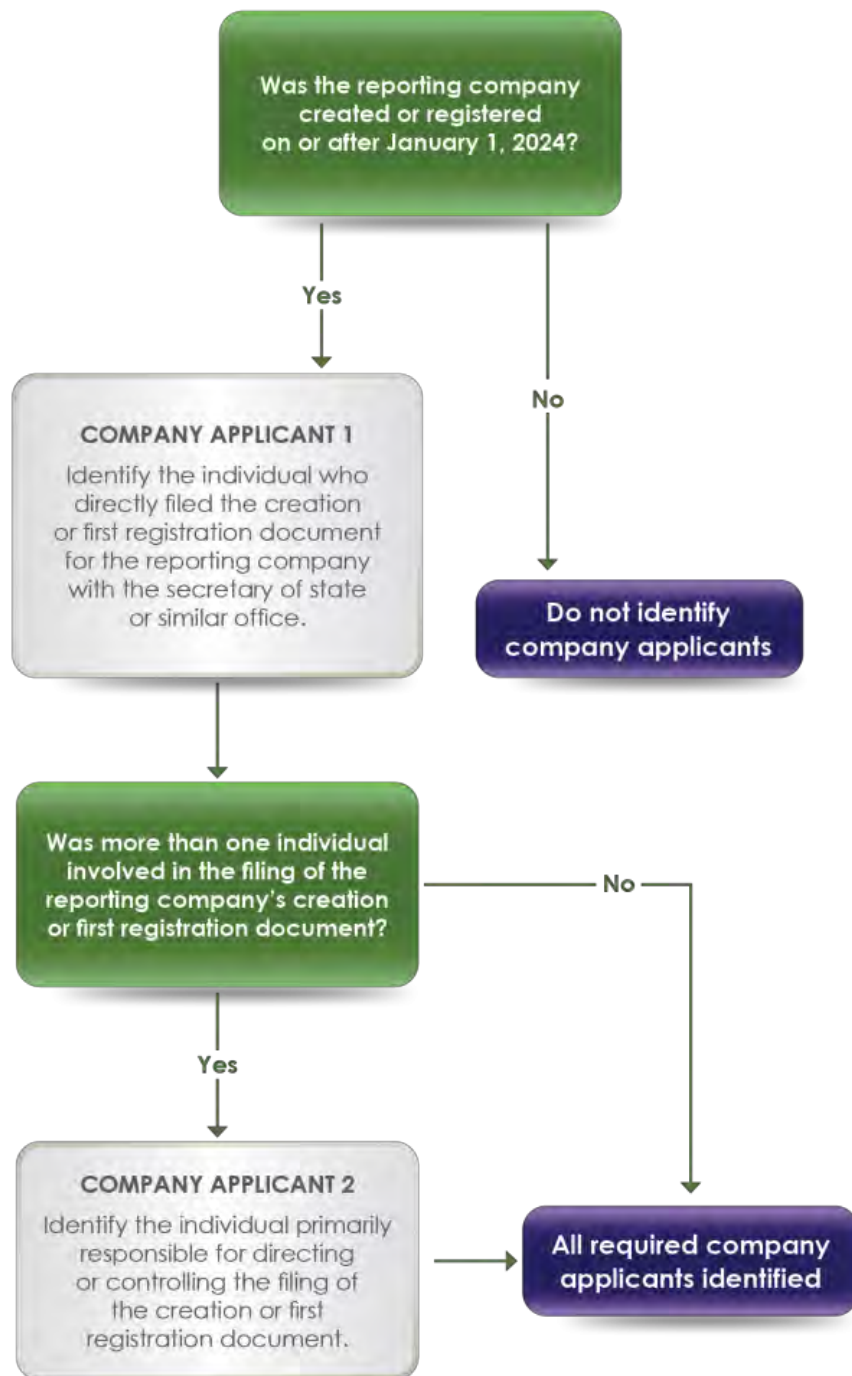
No reporting company will have more than two company applicants. If only one person was involved in filing the relevant document, then only that person should be reported as a company applicant.

Only reporting companies formed or registered on or after January 1, 2024, will have to report their company applicants. Companies created or registered before January 1, 2024, do not have to report their company applicants.¹²²

¹²¹ 31 CFR 1010.380(e)

¹²² “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, March 24, 2023, pp. 7-8

The November 16 FAQ illustrates the application of these rules as follows.¹²³



¹²³ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p.15

The November 16 update to the FAQ clarified that a company applicant's information, in addition to never being updated, or also never removed from the company's report even if the applicant no longer has any ties to the reporting company.¹²⁴

E. 4. Can a company applicant be removed from a BOI report if the company applicant no longer has a relationship with the reporting company?

No. A company applicant may not be removed from a BOI report even if the company applicant no longer has a relationship with the reporting company. A reporting company created on or after January 1, 2024, is required to report company applicant information in its initial BOI report, but is not required to file an updated BOI report if information about a company applicant changes.

In a September 18 update to the FAQ, FinCEN provided the following information on when the company's accountant or attorney would be a company applicant.¹²⁵

E. 3. Is my accountant or lawyer considered a company applicant?

An accountant or lawyer could be a company applicant, depending on their role in filing the document that creates or registers a reporting company. In many cases, company applicants may work for a business formation service or law firm.

An accountant or lawyer may be a company applicant if they directly filed the document that created or registered the reporting company. If more than one person is involved in the filing of the creation or registration document, an accountant or lawyer may be a company applicant if they are primarily responsible for directing or controlling the filing.

For example, an attorney at a law firm that offers business formation services may be primarily responsible for overseeing preparation and filing of a reporting company's incorporation documents. A paralegal at the law firm may directly file the incorporation documents at the attorney's request. Under those circumstances, the attorney and the paralegal are both company applicants for the reporting company.

FinCEN explains how to determine the individual primarily responsible for the filing in the January 4, 2024 revision to the FAQ.

E. 5. The company applicants of a reporting company include the individual "primarily responsible for directing the filing of the creation or registration"

¹²⁴ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p. 16

¹²⁵ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p. 16

document.” What makes an individual “primarily responsible” for directing such a filing?

At most, two individuals need to be reported as company applicants:

1. the person who directly files the document with a secretary of state or similar office, and
2. if more than one person is involved in the filing of the document, the person who is primarily responsible for directing or controlling the filing.

For the purposes of determining who is a company applicant, it is not relevant who signs the creation or registration document, for example, as an incorporator. To determine who is primarily responsible for directing or controlling the filing of the document, consider who is responsible for making the decisions about the filing of the document, such as how the filing is managed, what content the document includes, and when and where the filing occurs. The following three scenarios provide examples.

Scenario 1: Consider an attorney who completes a company creation document using information provided by a client, and then sends the document to a corporate service provider for filing with a secretary of state. In this example:

- The attorney is the company applicant who is primarily responsible for directing or controlling the filing because they prepared the creation document and directed the corporate service provider to file it.
- The individual at the corporate service provider is the company applicant who directly filed the document with the secretary of state.

Scenario 2: If the attorney instructs a paralegal to complete the preparation of the creation document, rather than doing so themselves, before directing the corporate service provider to file the document, the outcome remains the same: the attorney and the individual at the corporate service provider who files the document are company applicants. The paralegal is not a company applicant because the attorney played a greater role than the paralegal in making substantive decisions about the filing of the document.

Scenario 3: If the client who initiated the company creation directly asks the corporate service provider to file the document to create the company, then the client is primarily responsible for directing or controlling the filing, and the client should be reported as a company applicant, along with the individual at the corporate service provider who files the document.¹²⁶

¹²⁶ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised January 4, 2024

FinCEN also gave guidance for a situation where an individual used an automated incorporation service to file creation or registration documents.

E. 7. If an individual used an automated incorporation service, such as through a website or online platform, to file the creation or registration document for a reporting company, who is the company applicant?

If a business formation service only provides software, online tools, or generally applicable written guidance that are used to file a creation or registration document for a reporting company, and employees of the business service are not directly involved in the filing of the document, the employees of such services are not company applicants. For example, an individual may prepare and self-file documents to create the individual's own reporting company through an automated incorporation service. In this case, this reporting company reports only that individual as a company applicant.¹²⁷

A third-party courier who merely delivers the documents that create or register a company is not a company applicant per the FinCEN FAQ update issued on January 4, 2024.

E. 6. Is a third-party courier or delivery service employee who only delivers documents that create or register a reporting company a company applicant?

No. A third-party courier or delivery service employee who only delivers documents to a secretary of state or similar office is not a company applicant provided they meet one condition: the third-party courier, the delivery service employee, and any delivery service that employs them does not play any other role in the creation or registration of the reporting company.

When a third-party courier or delivery service employee is used solely for delivery, the individual (e.g., at a business formation service or law firm) who requested the third-party courier or delivery service to deliver the document will typically be a company applicant.

Under FinCEN's regulations, an individual who "directly files the document" that creates or registers the reporting company is a company applicant. Third-party couriers or delivery service employees who deliver such documents facilitate the documents' filing, but FinCEN does not consider them to be the filers of the documents given their only connection to the creation or registration of the reporting company is couriating the documents.

Rather, when a third-party courier or delivery service is used by a firm, the company applicant who "directly files" the creation or registration document is the individual

¹²⁷ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised January 4, 2024

at the firm who requests that the third-party courier or delivery service deliver the documents.

- For example, an attorney at a law firm may be involved in the preparation of incorporation documents. The attorney directs a paralegal to file the documents. The paralegal may then request a third-party delivery service to deliver the incorporation documents to the secretary of state's office. The paralegal is the company applicant who directly files the documents, even though the third-party delivery service delivered the documents on the paralegal's behalf. The attorney at the law firm who was involved in the preparation of the incorporation documents and who directed the paralegal to file the documents will also be a company applicant because the attorney was primarily responsible for directing or controlling the filing of the documents.

In contrast, if a courier is employed by a business formation service, law firm, or other entity that plays a role in the creation or registration of the reporting company, such as drafting the relevant documents or compiling information to be submitted as part of the documents delivered, the conclusion is different. FinCEN considers such a courier to have directly filed the documents—and thus to be a company applicant—given the courier's greater connection (via the courier's employer) to the creation or registration of the company.

- For example, a mailroom employee at a law firm may physically deliver the document that creates a reporting company at the direction of an attorney at the law firm who is primarily responsible for decisions related to the filing. Both individuals are company applicants.¹²⁸

FinCEN provided examples of applying these provisions in the FAQ.

EXAMPLE – FAQ QUESTION 11

Example 1: Individual A is creating a new company. Individual A prepares the necessary documents to create the company and files them with the relevant state or Tribal office, either in person or using a self-service online portal. No one else is involved in preparing, directing, or making the filing.

Individual A is a company applicant because Individual A directly filed the document that created the company. Because Individual A is the only person involved in the filing, Individual A is the only company applicant. State or Tribal employees who receive and process the company creation or formation documents should not be reported as company applicants.

¹²⁸ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised January 4, 2024

EXAMPLE – FAQ QUESTION 11

Example 2: Individual A is creating a company. Individual A prepares the necessary documents to create the company and directs Individual B to file the documents with the relevant state or Tribal office. Individual B then directly files the documents that create the company.

Individuals A and B are both company applicants—Individual B directly filed the documents, and Individual A was primarily responsible for directing or controlling the filing. Individual B could, for example, be Individual A’s spouse, business partner, attorney, or accountant; in all cases, Individuals A and B are both company applicants in this scenario.

Information to Be Provided

Information will need to be provided and kept up to date about the entity itself, each beneficial owner, and, if formed on or after January 1, 2024, each company applicant.

Information to Be Provided About the Entity

The initial report will contain the following information about the company:

- The full legal name of the reporting company;
- Any trade name or “doing business as” name of the reporting company;
- A complete current address consisting of:
 - In the case of a reporting company with a principal place of business in the United States, the street address of such principal place of business; and
 - In all other cases, the street address of the primary location in the United States where the reporting company conducts business;
- The State, Tribal, or foreign jurisdiction of formation of the reporting company;
- For a foreign reporting company, the State or Tribal jurisdiction where such company first registers; and
- The Internal Revenue Service (IRS) Taxpayer Identification Number (TIN) (including an Employer Identification Number (EIN)) of the reporting company, or where a foreign reporting company has not been issued a TIN, a tax identification number issued by a foreign jurisdiction and the name of such jurisdiction.¹²⁹

¹²⁹ 31 CFR 1010.380(b)(1)(i)

The FAQ provides as well that “[a] reporting company will also have to indicate the type of filing it is making (that is, whether it is filing an initial report, a correction of a prior report, or an update to a prior report).”¹³⁰

In the January 4, 2024, update to the FAQ, FinCEN provided the following advice related to issues certain entities have in timely obtaining the required identification number:

G. 3. How can I obtain a Taxpayer Identification Number (TIN) for a new company quickly so that I can file an initial beneficial ownership information report on time?

The Internal Revenue Service (IRS) offers a free online application for an Employer Identification Number (EIN), a type of TIN, which is provided immediately upon submission of the application. For more information on TINs, see “Taxpayer Identification Numbers (TIN)” at IRS.gov (<https://www.irs.gov/individuals/international-taxpayers/taxpayer-identification-numbers-tin>). For more information on Employer Identification Numbers and to access the EIN online application, see “Apply for an Employer Identification Number (EIN) Online” at IRS.gov (<https://www.irs.gov/businesses/small-businesses-self-employed/apply-for-an-employer-identification-number-ein-online>).

A paper filing is required if a foreign person that does not have an Individual Taxpayer Identification Number (ITIN) applies for an EIN. According to the IRS, receiving an EIN through this process could take six to eight weeks. If you are a foreign person that may need to obtain an EIN for a reporting company, we recommend applying early for an ITIN. Foreign reporting companies that are not subject to U.S. corporate income tax may report a foreign tax identification number and the name of the relevant jurisdiction instead of an EIN or TIN.¹³¹

In the December 12 FAQ update, FinCEN unequivocally stated that the utilization of a P.O. Box instead of a street address will not be permissible on the BOI report.

F. 8. Can a reporting company report a P.O. box as its current address?

No. The reporting company address must be a U.S. street address and cannot be a P.O. box.

FinCEN’s Small Entity Compliance Guide includes additional information on what must be reported in Chapter 4, “What specific information does my company need to report?”¹³²

¹³⁰ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, March 24, 2023, p. 9

¹³¹ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised January 4, 2024

¹³² “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

Information to Be Provided for Beneficial Owners and Company Applicants

Information will need to be provided on initial reports (and kept updated) for beneficial owners and, for entities formed on or after January 1, 2024, company applicants.

The information provided will consist of:

- The full legal name of the individual;
- The date of birth of the individual;
- A complete current address consisting of:
 - In the case of a company applicant who forms or registers an entity in the course of such company applicant’s business, the street address of such business; or
 - In any other case, the individual’s residential street address;
- A unique identifying number and the issuing jurisdiction from one of the following documents:
 - A non-expired passport issued to the individual by the United States government;
 - A non-expired identification document issued to the individual by a State, local government, or Indian tribe for the purpose of identifying the individual;
 - A non-expired driver’s license issued to the individual by a State; or
 - A non-expired passport issued by a foreign government to the individual, if the individual does not possess any of the prior three documents
- An image of the document from which the unique identifying number was obtained.¹³³

Per the *BOI Report Filing Instructions* the image must be in one of the following formats:

- JPEG/JPG
- PNG or
- PDF¹³⁴

The image must contain a “clear, readable image of the page or side of the identifying document ... containing the unique identifying number and other identifying data.”¹³⁵

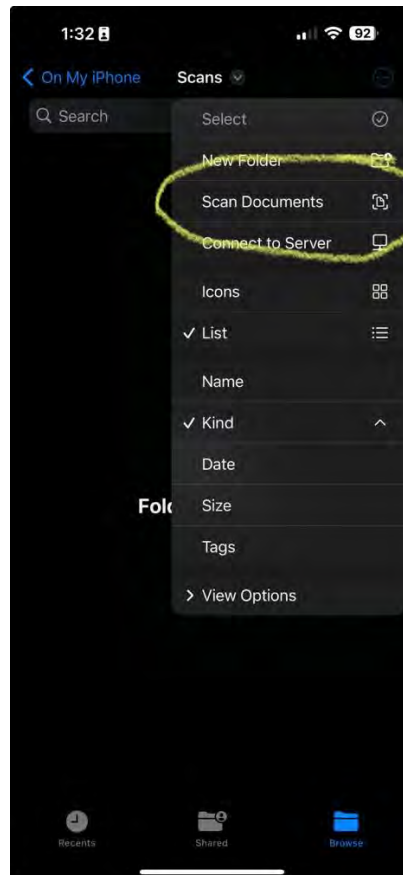
¹³³ 31 CFR 1010.380(b)(1)(ii)

¹³⁴ *Beneficial Ownership Information Reporting Filing Instructions*, FinCEN, January 2024 – Version 1.0, p. 17

¹³⁵ *Beneficial Ownership Information Reporting Filing Instructions*, FinCEN, January 2024 – Version 1.0, p. 17

The file format requirements may create issues for iPhone users. Versions of iOS since iOS 11 by default store pictures taken with the camera in HEIC format which is not a format supported by FinCEN for this application.¹³⁶

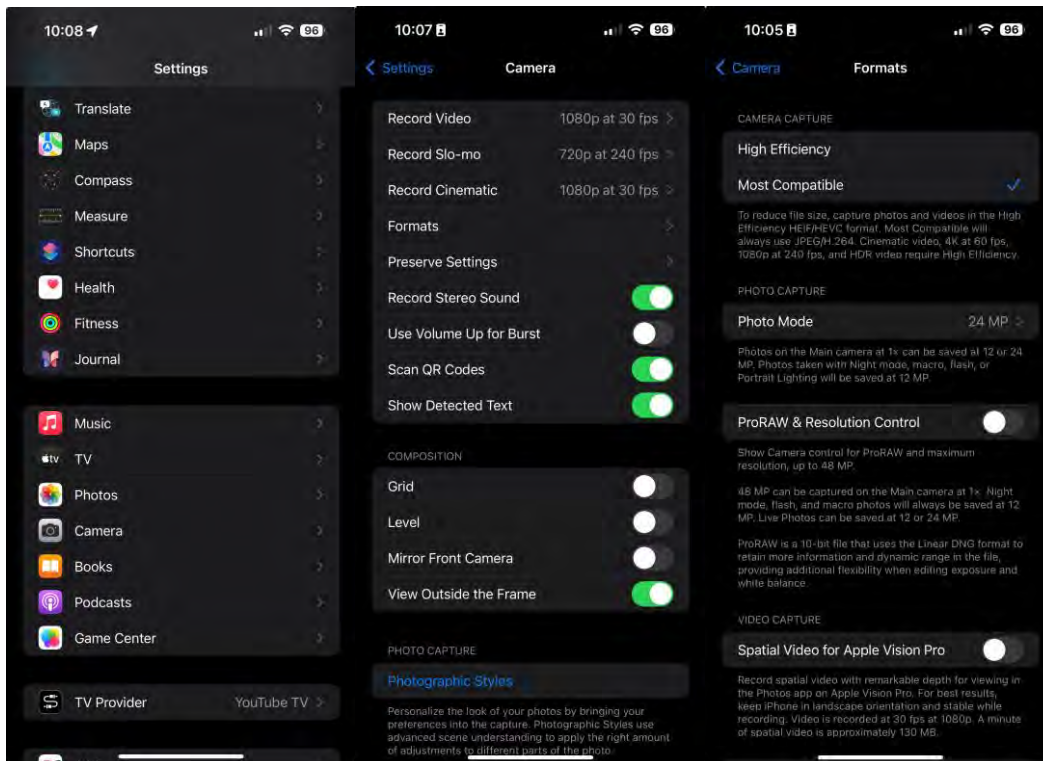
If a party plans to use an iPhone to take an image of the page in question, they either should use the built-in capable to use the iPhone as a scanner found in the Files App on the phone:



PDFs can also be captured via the Notes App.

Alternatively, the users can set the phone to produce JPEG rather HEIC formatted pictures by default. JPEG was the format used by the iPhone prior to iOS 11. To change this setting the iPhone user should go to Camera → Formats → Most Compatible.

¹³⁶ This is not all that unusual as HEIC has far less widespread acceptance than the other formats. In 2020 the College Board had major issues with Advanced Placement tests when test takers attempted to send iPhone HEIC photos to send copies of written answers. Monica Chin, "Students are failing AP tests because the College Board can't handle iPhone photos," *The Verge*, <https://www.theverge.com/2020/5/20/21262302/ap-test-fail-iphone-photos-glitch-email-college-board-jpeg-heic>, May 20, 2020



The user may want to switch the format back to High Efficiency after the picture has been taken and uploaded, especially if the iPhone will be used to record video as the new format uses less storage space on the phone.

The FAQ contains the following specific information on the address supplied:

Address: For a beneficial owner, the reporting company must report the residential street address.

For a company applicant, the reporting company must report the individual's residential street address. However, if an individual engages in the business of corporate formation (e.g., as an attorney or corporate formation agent) and files the formation or registration document in the course of that business, then the reporting company must report the current street address of the company applicant's business. For example, if the company applicant is a paralegal who filed the document while working at a law firm, the reporting company must report the business address of the law firm where the paralegal worked when filing the document.¹³⁷

¹³⁷ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, March 24, 2023, p. 10

The FAQ goes on to provide more details about the identifying documents:

Identification Document: The list below sets out the forms of acceptable identification documents:

- A non-expired driver's license issued by a U.S. state. A "U.S. state" means any state of the United States, the District of Columbia, the Commonwealth of Puerto Rico, the Commonwealth of the Northern Mariana Islands, American Samoa, Guam, the U.S. Virgin Islands, and any other commonwealth, territory, or possession of the United States.
- A non-expired identification document issued by a U.S. state or local government, or Indian Tribe that is issued for the purpose of identifying the individual. For example, a non-driver identification card issued by a state Department of Motor Vehicles would qualify because it is issued for identification purposes.
- A non-expired passport issued by the U.S. government; or
- If the individual does not have any of the three forms of identification document described above, the reporting company may provide the identifying number from a non-expired passport issued by a foreign government.¹³⁸

Beneficial Owner Without a Permanent Residence

FinCEN added information about what is to be done if an individual does not have a permanent residential address:

F. 11. What residential address should be reported if a reporting company is required to report an individual's residential address, but that individual does not have a permanent residential residence?

The residential address that is current at the time of filing should be reported to FinCEN. An updated report should be submitted within 30 calendar days if the address, or any other information previously reported, changes.

FinCEN's Small Entity Compliance Guide includes additional information on what information must be reported in Chapter 4, "What specific information does my company need to report?" and what to do when previously reported information needs to be updated in Chapter 6.1 "What should I do if previously reported information changes?"¹³⁹

¹³⁸ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, March 24, 2023, p. 10

¹³⁹ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised January 4, 2024

Beneficial Owners Holding Their Ownership Interests Via Exempt Entities

The September 29 update to the FAQ added special reporting rules for individuals who held their interests in a reporting company solely via interests they hold in an exempt entity.¹⁴⁰

D. 7. What information should a reporting company report about a beneficial owner who holds their ownership interests in the reporting company through multiple exempt entities?

If a beneficial owner owns or controls their ownership interests in a reporting company exclusively through multiple exempt entities, then the names of all of those exempt entities may be reported to FinCEN instead of the individual beneficial owner's information.

- Note that this special rule does not apply when an individual owns or controls ownership interests in a reporting company through both exempt and non-exempt entities. In that case, the reporting company must report the individual as a beneficial owner (if no exception applies), but the exempt companies do not need to be listed.

FinCEN's Small Entity Compliance Guide includes more information about this special reporting rule in Chapter 4.2, "What do I report if a special reporting rule applies to my company?"

Unaffiliated Company Providing Services to a Reporting Company

The September 29 update to the FAQ also addressed the case where an unaffiliated entity provides services to the reporting company.¹⁴¹

D. 8. Is an unaffiliated company that provides a service to the reporting company by managing its day-to-day operations, but does not make decisions on important matters, a beneficial owner of the reporting company?

The unaffiliated company itself cannot be a beneficial owner of the reporting company because a beneficial owner must be an individual. Any individuals that exercise substantial control over the reporting company through the unaffiliated company must be reported as beneficial owners of the reporting company. However, individuals who do not direct, determine, or have substantial influence over important decisions made by the reporting company, and do not otherwise exercise substantial control, may not be beneficial owners of the reporting company.

¹⁴⁰ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p. 11

¹⁴¹ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p. 12

Please see Chapter 2.1 of FinCEN's Small Entity Compliance Guide, "What is substantial control?" for additional information on how to determine whether an individual has substantial control over a reporting company.

Historical Owners Not to Be Reported

The November 16 FAQ clarified that a report should only contain *current* owners and not have information about historical owners of the company.¹⁴²

4. Should an initial BOI report include historical beneficial owners of a reporting company, or only beneficial owners as of the time of filing?

An initial BOI report should only include the beneficial owners as of the time of the filing. Reporting companies should notify FinCEN of changes to beneficial owners and related BOI through updated reports.

FinCEN's Small Entity Compliance Guide includes more information about when to file updated or corrected BOI reports in Chapter 6, "What if there are changes to or inaccuracies in reported information?"

Beneficial Owner's Identification Document Lacks a Photograph for Religious Reasons

FinCEN provided on January 4, 2024 the following guidance should a reporting company have a beneficial owner or company applicant whose identification document lacks a photograph for religious reasons.

F. 10. If a beneficial owner or company applicant's acceptable identification document does not include a photograph for religious reasons, will FinCEN accept the identification document without the photograph?

Yes. If a beneficial owner or company applicant's identification document does not include a photograph for religious reasons, the reporting company may nonetheless submit an image of that identification document when submitting its report, as long as the identification document is one of the types of identification accepted by FinCEN, such as a non-expired State-issued identification document. Please see Question F.5 for a list of acceptable identification documents.¹⁴³

¹⁴² "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p. 12

¹⁴³ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2024

Updated Reports

An entity's responsibility to file reports goes beyond the initial filings. In various situations, an updated report must be filed with FinCEN. The table below, created with the assistance of ChatGPT 3.5, provides a general summary of situations where an updated report must be filed:

Situation	When the time to file an updated report begins
Change in required information previously submitted to FinCEN concerning a reporting company or its beneficial owners (with more specific examples provided in the following rows)	The date on which such change occurs
Reporting company meets the criteria for any exemption subsequent to the filing of an initial report	When the event occurs that causes the entity to meet the criteria.
Death of a beneficial owner	When the estate of the deceased beneficial owner is settled, either through the operation of the intestacy laws of a jurisdiction within the United States or through a testamentary deposition. The updated report shall, to the extent appropriate, identify any new beneficial owners.
Minor child attains the age of majority	When the minor child attains the age of majority
Change in information on an identifying document	When the name, date of birth, address, or unique identifying number on such document changes

In all of these situations, the reporting company must file an updated report in the form and manner specified in the final rule within 30 calendar days after the date on which such change occurs.

The final rule provides details on updated reporting requirements. FinCEN has required updates to be made 30 days after information that is required to be provided on the report has changed. The rule provides:

- (i) If there is any change with respect to required information previously submitted to FinCEN concerning a reporting company or its beneficial owners, including any change with respect to who is a beneficial owner or information reported for any particular beneficial owner, the reporting company shall file an updated report in the form and manner specified in paragraph (b)(3) of this section within 30 calendar days after the date on which such change occurs.¹⁴⁴

¹⁴⁴ 31 CFR 1010.380(a)(2)

The final rule provides detail as well on the information to be provided in such updated reports:

- (i) Updated reports—in general. An updated report required to be filed pursuant to paragraph (a)(2) of this section shall reflect any change with respect to required information previously submitted to FinCEN concerning a reporting company or its beneficial owners.¹⁴⁵

One requirement found in the regulations that may surprise some professionals is the requirement to file a report to inform FinCEN that an organization now meets the requirements to be exempt from the filing requirements:

- (ii) Updated reports—newly exempt entities. An updated report required to be filed pursuant to paragraph (a)(2)(ii) of this section shall indicate that the filing entity is no longer a reporting company.¹⁴⁶

And the requirement to file that information is found earlier in the final rule:

- (ii) If a reporting company meets the criteria for any exemption under paragraph (c)(2) of this section subsequent to the filing of an initial report, this change will be deemed a change with respect to information previously submitted to FinCEN, and the entity shall file an updated report.¹⁴⁷

The September 18 update to the FAQ contained information on this report to indicate that the entity is now exempt from reporting.¹⁴⁸

J. 1. What should a reporting company do if it becomes exempt after already filing a report?

If a reporting company filed a beneficial ownership information report but then becomes exempt from filing the report, the company should file an updated report indicating that it is no longer a reporting company. An updated BOI report for a newly exempt entity will only require that: (1) the entity identify itself; and (2) check a box noting its newly exempt status. Chapter 6.3, “What should my company do if it becomes exempt after already filing a report?” of FinCEN’s Small Entity Compliance Guide includes more information.

¹⁴⁵ 31 CFR 1010.380(b)(3)(i)

¹⁴⁶ 31 CFR 1010.380(b)(3)(ii)

¹⁴⁷ 31 CFR 1010.380(a)(2)(ii)

¹⁴⁸ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p. 22

Similarly, if an entity that had been exempt now fails to meet the requirements, that entity will also need to file what will be an *initial* report within 30 days:

- (iv) Any entity that no longer meets the criteria for any exemption under paragraph (c)(2) of this section shall file a report within 30 calendar days after the date that it no longer meets the criteria for any exemption.¹⁴⁹

The final rule contains special rules that will take effect if a beneficial owner dies and his/her interest is transferred:

- (iii) If an individual is a beneficial owner of a reporting company by virtue of property interests or other rights subject to transfer upon death, and such individual dies, a change with respect to required information will be deemed to occur when the estate of the deceased beneficial owner is settled, either through the operation of the intestacy laws of a jurisdiction within the United States or through a testamentary deposition. The updated report shall, to the extent appropriate, identify any new beneficial owners.¹⁵⁰

Similarly, when a minor child reaches the age of majority, an updated report must be filed:

- (iv) If a reporting company has reported information with respect to a parent or legal guardian of a minor child pursuant to paragraphs (b)(2)(ii) and (d)(3)(i) of this section, a change with respect to required information will be deemed to occur when the minor child attains the age of majority.¹⁵¹

Finally, the regulation provides that if the identifying documents whose image was provided to FinCEN changes, that also will require an updated report:

- (v) With respect to an image of an identifying document required to be reported pursuant to paragraph (b)(1)(ii)(E) of this section, a change with respect to required information will be deemed to occur when the name, date of birth, address, or unique identifying number on such document changes.¹⁵²

In December 2023, FinCEN provided clarification in Q&A H.6. regarding the filing procedure when an entity has previously submitted a “newly exempt entity” updated report. It was emphasized that if the entity no longer qualifies for an exemption, it should file an updated report rather than an initial report. The final rule specified that if the entity was exempt when its initial report was due, the loss of exemption subsequently necessitates the filing of an initial report. However, if an initial report

¹⁴⁹ 31 CFR 1010.380(a)(1)(iv)

¹⁵⁰ 31 CFR 1010.380(a)(2)(iii)

¹⁵¹ 31 CFR 1010.380(a)(2)(iv)

¹⁵² 31 CFR 1010.380(a)(2)(v)

had already been submitted in the past, it is not appropriate to file another initial report if the entity loses its exempt status.

H. 6. If a reporting company last filed a “newly exempt entity” BOI report but subsequently loses its exempt status, what should it do?

A reporting company should file an updated BOI report with FinCEN with the company’s current beneficial ownership information when it determines it no longer qualifies for an exemption.¹⁵³

A change in the type of ownership interest of a beneficial owner holds does not necessarily require the filing of an updated report, as FinCEN discusses in FAQ question H.3. added on December 12, 2023:

H. 3. Is an updated BOI report required when the type of ownership interest a beneficial owner has in a reporting company changes?

No. A change to the type of ownership interest a beneficial owner has in a reporting company—for example, a conversion of preferred shares to common stock—does not require the reporting company to file an updated BOI report because FinCEN does not require companies to report the type of interest. Updated BOI reports are required when information reported to FinCEN about the reporting company or its beneficial owners changes.

FinCEN’s Small Entity Compliance Guide includes additional information on when and how reporting companies must update information in Chapter 6, “What if there are changes to or inaccuracies in reported information?”¹⁵⁴

In the December update of the FAQ, a question was introduced that addressed the submission of late BOI reports. However, it primarily advises taking precautions to prevent such situations from occurring.

H. 5. Can a filer submit a late updated BOI report?

An updated BOI report can be submitted to FinCEN at any time. However, the reporting company is responsible for ensuring that updates are filed within 30 days of a change occurring. If a reporting company has engaged a third-party service provider to file BOI reports and updates on its behalf, then it should communicate any changes to its beneficial ownership information to the third-party service provider with enough time to meet the 30-day deadline.

¹⁵³ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

¹⁵⁴ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

Corrected Reports

If an error is made in a filing, a corrected report must be filed within 30 days of when the reporting entity becomes aware of the error.

If any report under this section was inaccurate when filed and remains inaccurate, the reporting company shall file a corrected report in the form and manner specified in paragraph (b) of this section within 30 calendar days after the date on which such reporting company becomes aware or has reason to know of the inaccuracy.¹⁵⁵

The regulations also provide that the original filing won't be treated as a problem if the correction is made within 90 days of the original filing. This is a separate deadline from the 30-day requirement. Thus, if an error is discovered after 90 days, the correction must still be filed but FinCEN could take action to impose penalties:

A corrected report filed under this paragraph (a)(3) within this 30-day period shall be deemed to satisfy 31 U.S.C. 5336(h)(3)(C)(i)(I)(bb) if filed within 90 calendar days after the date on which the inaccurate report was filed.¹⁵⁶

No Annual Reporting Requirement

The November 16 update to the FAQ reminds reporting companies that the reporting requirement is not an annual requirement, but rather is driven by the happening of specific events.¹⁵⁷

F. 6. Is there a requirement to annually report beneficial ownership information?

No. There is no annual reporting requirement. Reporting companies must file an initial BOI report and updated or corrected BOI reports as needed.

FinCEN's Small Entity Compliance Guide includes more information about when to file initial BOI reports in Chapter 5.1, "When should my company file its initial BOI report?" and when to file updated and corrected BOI reports in Chapter 6, "What if there are changes to or inaccuracies in reported information?"

Some entities will need to file multiple reports within a single year, while others may go years between having to make any updates to their reports.

FinCEN Identifier

Individuals and companies are offered the option of obtaining a FinCEN identifier which contains the information required for the report. Presumably, this would allow the individual to file a single

¹⁵⁵ 31 CFR 1010.380(a)(3)

¹⁵⁶ 31 CFR 1010.380(a)(3)

¹⁵⁷ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, pp. 18-19

update for any changed information rather than having to make the same change on each company report.

The final rule provides the following information on the application process:

(i) Application.

(A) An individual may obtain a FinCEN identifier by submitting to FinCEN an application containing the information about the individual described in paragraph (b)(1) of this section.

(B) A reporting company may obtain a FinCEN identifier by submitting to FinCEN an application at or after the time that the entity submits an initial report required under paragraph (b)(1) of this section.

(C) Each FinCEN identifier shall be specific to each such individual or reporting company, and each such individual or reporting company (including any successor reporting company) may obtain only one FinCEN identifier.¹⁵⁸

The final rule provides the following information on the use of the FinCEN identifier:

(ii) Use of the FinCEN identifier.

(A) If an individual has obtained a FinCEN identifier and provided such FinCEN identifier to a reporting company, the reporting company may include such FinCEN identifier in its report in lieu of the information required under paragraph (b)(1) of this section with respect to such individual.

(B) [Reserved]¹⁵⁹

The “reserved” section suggests that FinCEN has plans to add more information on the use of this identifier, perhaps to make it more attractive and powerful.

Update and correction rules for FinCEN identifiers are very similar to those for the entity filings:

(iii) Updates and corrections. (A) Any individual that has obtained a FinCEN identifier shall update or correct any information previously submitted to FinCEN in an application for such FinCEN identifier.

(1) If there is any change with respect to required information previously submitted to FinCEN in such application, the individual shall file an

¹⁵⁸ 31 CFR 1010.380(b)(4)(i)

¹⁵⁹ 31 CFR 1010.380(b)(4)(ii)

updated application reflecting such change within 30 calendar days after the date on which such change occurs.

(2) If any such application was inaccurate when filed and remains inaccurate, the individual shall file a corrected application correcting all inaccuracies within 30 calendar days after the date on which the individual becomes aware or has reason to know of the inaccuracy. A corrected application filed under this paragraph within this 30-day period will be deemed to satisfy 31 U.S.C. 5336(h)(3)(C)(i)(I)(bb) if filed within 90 calendar days after the date on which the inaccurate application was submitted.

(B) Any reporting company that has obtained a FinCEN identifier shall file an updated or corrected report to update or correct any information previously submitted to FinCEN. Such updated or corrected report shall be filed at the same time and in the same manner as updated or corrected reports filed under paragraph (a) of this section.¹⁶⁰

The September 29 update to the FAQ added a number of Q&As related to the FinCEN identifier. Q&A M.2 outlines how a FinCEN identifier can be used, later revised in the January 12 update.¹⁶¹

M. 2. How can I use a FinCEN identifier?

When a beneficial owner or company applicant has obtained a FinCEN identifier, reporting companies may report the FinCEN identifier of that individual in the place of that individual's otherwise required personal information on a beneficial ownership information report.

A reporting company may report another entity's FinCEN identifier and full legal name in place of information about its beneficial owners when three conditions are met: (1) the other entity obtains a FinCEN identifier and provides it to the reporting company; (2) the beneficial owners hold interests in the reporting company through ownership interests in the other entity; and (3) the beneficial owners of the reporting company and the other entity are the exact same individuals.

Q&A M.3 outlines the process to obtain a FinCEN identifier.¹⁶²

M. 3. How do I request a FinCEN identifier?

Individuals may request a FinCEN identifier starting January 1, 2024, by completing an electronic web form at <https://fincenid.fincen.gov>. Individuals will

¹⁶⁰ 31 CFR 1010.380(b)(4)(iii)

¹⁶¹ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised January 12, 2024

¹⁶² "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, pp. 26-27

need to provide their full legal name, date of birth, address, unique identifying number and issuing jurisdiction from an acceptable identification document, and an image of the identification document. After an individual submits this information, they will immediately receive a unique FinCEN identifier.

Reporting companies may request a FinCEN identifier by checking a box on the beneficial ownership information report upon submission. After the reporting company submits the report, the company will immediately receive a unique FinCEN identifier. If a reporting company wishes to request a FinCEN identifier after submitting its initial beneficial ownership report, it may submit an updated beneficial ownership information report requesting a FinCEN identifier, even if the company does not otherwise need to update its information.¹⁶³

Q&A M.4 notes that obtaining and using a FinCEN identifier is not required.

Q&A M.7 furnishes information pertaining to the individuals authorized to request a FinCEN identifier on behalf of another individual.

M. 7. Who can request a FinCEN identifier on behalf of an individual?

Anyone authorized to act on behalf of an individual may request a FinCEN identifier on the individual's behalf on or after January 1, 2024.

FinCEN identifiers for individuals are provided upon request after the requesting party has submitted the necessary information. Obtaining a FinCEN identifier for an individual requires the requesting party to create a Login.gov account, which is tied to the individual receiving the FinCEN identifier. Individuals who receive a FinCEN identifier should ensure their login credentials, including email address and related multi-factor information associated with their Login.gov account, are saved for future reference.

FinCEN's Small Entity Compliance Guide includes additional information on the FinCEN identifier in Chapter 4.3 "What is a FinCEN identifier and how can I use it?"¹⁶⁴

¹⁶³ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised January 4, 2024

¹⁶⁴ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

Q&A M.5 outlines the requirements to update a FinCEN if an individual or entity has decided to obtain one.¹⁶⁵

M. 5. Do I need to update or correct the information I submitted to obtain a FinCEN identifier?

Yes. Individuals must update or correct information through the FinCEN identifier application that is also used to request a FinCEN identifier.

- Individuals must report any change to the information they submitted to obtain a FinCEN identifier no later than 30 days after the date on which the change occurred.
- If there is any inaccuracy in this information, an individual must correct the information no later than 30 days after the date the individual became aware of the inaccuracy or had reason to know of it.

Reporting companies with a FinCEN identifier must update or correct the company's information by filing an updated or corrected beneficial ownership information report, as appropriate.

The section closes with Q&A M.6 which indicates that the ability to deactivate a FinCEN identifier is a work process at this point:¹⁶⁶

M. 6. Is there any way to deactivate an individual's FinCEN identifier that is no longer in use so that the individual no longer has to update the information associated with it?

FinCEN is actively assessing options to allow individuals to deactivate a FinCEN identifier so that they do not need to update the underlying personal information on an ongoing basis. FinCEN will provide additional guidance on this functionality upon completion of that process.

Third Party FinCEN Reporting

A question many CPAs have asked is if third parties will be able to file the reports on behalf of reporting companies and/or if third party software will be able to be used to file the report. Q&A N.1 indicates that the answer to both will be yes.¹⁶⁷

¹⁶⁵ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p. 27

¹⁶⁶ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p. 27

¹⁶⁷ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p. 28

N. 1. Can a third-party service provider assist reporting companies by submitting required information to FinCEN on their behalf?

Yes. Reporting companies may use third-party service providers to submit beneficial ownership information reports. Third-party service providers will have the ability to submit the reports via FinCEN's BOI E-Filing website or an Application Programming Interface (API). To request the API technical specifications, use FinCEN's contact form (<https://www.fincen.gov/contact>). Please do the following when submitting your inquiry: (1) select the topic associated with Beneficial Ownership (BO) / Corporate Transparency Act (CTA); (2) select the subject associated with API requests; (3) in the message body, indicate the nature of your API-related inquiry (e.g., "I would like to review the API technical specifications," "I would like to request access to the API," etc.).¹⁶⁸

The API will facilitate the ability for third-party service providers to submit multiple reports simultaneously.

N. 3. Will a third-party service provider be able to submit multiple BOI reports to FinCEN at the same time?

Yes. Third-party service providers will be able to submit multiple BOI reports through an Application Programming Interface (API).¹⁶⁹

In Q&A N.2., FinCEN offers guidance on the type of evidence a company should acquire from a third-party filer to verify the submission of their BOI report.

N. 2. What type of evidence will a reporting company receive as confirmation that its BOI report has been successfully filed by a third-party service provider?

The BOI E-Filing application, available beginning January 1, 2024, provides acknowledgement of submission success or failure, and the submitter will be able to download a transcript of the BOI report. The reporting company will need to obtain this confirmation from the third-party service provider.¹⁷⁰

¹⁶⁸ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised January 4, 2024

¹⁶⁹ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

¹⁷⁰ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

FinCEN also provided in Q&A B.7 that while an entity is not required to use an attorney or accountant to file the reports, they should be able to seek assistance from an attorney or accountant for help in meeting reporting obligations.¹⁷¹

B. 7. Is a reporting company required to use an attorney or a certified public accountant (CPA) to submit beneficial ownership information to FinCEN?

No. FinCEN expects that many, if not most, reporting companies will be able to submit their beneficial ownership information to FinCEN on their own using the guidance FinCEN has issued. Reporting companies that need help meeting their reporting obligations can consult with professional service providers such as lawyers or accountants.

A prominent debate among accountants (including CPAs), professional liability insurers, and other stakeholders concerns whether activities by non-attorneys in these filings might constitute unauthorized legal practice. The Financial Crimes Enforcement Network's (FinCEN) response implies an expectation for accountants to be involved in the reporting process.

However, it is important to acknowledge that the unauthorized practice of law is predominantly governed at the state level, except in instances where federal provisions apply. An example of such a federal provision is found in 5 USC 500(c), which authorizes CPAs to practice before the Internal Revenue Service.

Penalties for Reporting Violations

Reporting violations are found at 31 USC 5336(h)(1) which reads:

(h) Penalties.—

(1) Reporting violations.— It shall be unlawful for any person to—

(A) willfully provide, or attempt to provide, false or fraudulent beneficial ownership information, including a false or fraudulent identifying photograph or document, to FinCEN in accordance with subsection (b); or

(B) willfully fail to report complete or updated beneficial ownership information to FinCEN in accordance with subsection (b).

The final rule provides the following additional details regarding a reporting violation:

(g) Reporting violations. It shall be unlawful for any person to willfully provide, or attempt to provide, false or fraudulent beneficial ownership information, including a false or fraudulent identifying photograph or document, to FinCEN in accordance

¹⁷¹ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised November 16, 2023, p. 3

with this section, or to willfully fail to report complete or updated beneficial ownership information to FinCEN in accordance with this section. For purposes of this paragraph (g):

- (1) The term “person” includes any individual, reporting company, or other entity.
- (2) The term “beneficial ownership information” includes any information provided to FinCEN under this section.
- (3) A person provides or attempts to provide beneficial ownership information to FinCEN if such person does so directly or indirectly, including by providing such information to another person for purposes of a report or application under this section.
- (4) A person fails to report complete or updated beneficial ownership information to FinCEN if, with respect to an entity:
 - (i) such entity is required, pursuant to title 31, United States Code, section 5336, or its implementing regulations, to report information to FinCEN;
 - (ii) the reporting company fails to report such information to FinCEN; and
 - (iii) such person either causes the failure, or is a senior officer of the entity at the time of the failure.¹⁷²

The penalties for a reporting violation are found at 31 USC §5336(h)(3)(A):

(3) Criminal and civil penalties.—

(A) Reporting violations.— Any person that violates subparagraph (A) or (B) of paragraph (1)—

- (i) shall be liable to the United States for a civil penalty of not more than \$500 for each day that the violation continues or has not been remedied; and
- (ii) may be fined not more than \$10,000, imprisoned for not more than 2 years, or both.

The civil penalty is subject to adjustment for inflation. As discussed later, the penalty for 2024 will be **\$591 per day**.

¹⁷² 31 CFR 1010.380

EXAMPLE

Under 31 USC §5336, a person may be subject to a civil penalty of up to \$500 for each day the report is not filed, is filed with improper information or is not timely updated. The taxpayer may also be fined, up to a maximum of \$10,000, and imprisoned for not more than 2 years or both. In this case, Joe willfully failed to file a beneficial ownership report for Joe's Store, LLC, and the report was due on June 30, 2025. Joe finally filed the report on December 12, 2025, which means that the report was overdue for a total of 165 days.

Since FinCEN has decided to impose the maximum per day financial penalty, the penalty imposed on Joe would be \$500 for each day the report was overdue, multiplied by 165 days. Therefore, the total penalty amount would be \$82,500.

The penalty amount was appropriate because Joe willfully failed to file the beneficial ownership report for Joe's Store, LLC, and the report was overdue for a significant period of time. Additionally, imposing the maximum per day financial penalty serves as a strong deterrent to others who may be tempted to willfully fail to file beneficial ownership reports in the future.

The \$10,000 fine limit did not limit the civil penalty because it is only applicable to criminal penalties under the same section of law. In this case, FinCEN imposed a civil penalty, not a criminal penalty, for Joe's failure to file the beneficial ownership report.

The December 2023 update to the FAQs provided supplementary information concerning the penalties that individuals may face for failing to comply with BOI reporting requirements. Q&A K.2. reaffirms FinCEN's interpretation that the \$500 per day civil penalty is not constrained by the separate \$10,000 fine stipulated in the legislation. Consequently, the civil penalty of up to \$500 per day has the potential to escalate without a predetermined limit as long as the report remains in non-compliance.

K. 2. What penalties do individuals face for violating BOI reporting requirements?

As specified in the Corporate Transparency Act, a person who willfully violates the BOI reporting requirements may be subject to civil penalties of up to \$500 for each day that the violation continues. That person may also be subject to criminal penalties of up to two years imprisonment and a fine of up to \$10,000. Potential violations include willfully failing to file a beneficial ownership information report, willfully filing false beneficial ownership information, or willfully failing to correct or update previously reported beneficial ownership information.¹⁷³

¹⁷³ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

The FAQ further highlights the extensive range of individuals and entities that may be subject to penalties under the BOI regime.

K. 3. Who can be held liable for violating BOI reporting requirements?

Both individuals and corporate entities can be held liable for willful violations. This can include not only an individual who actually files (or attempts to file) false information with FinCEN, but also anyone who willfully provides the filer with false information to report. Both individuals and corporate entities may also be liable for willfully failing to report complete or updated beneficial ownership information; in such circumstances, individuals can be held liable if they either cause the failure or are a senior officer at the company at the time of the failure.

i. Can an individual who files a report on behalf of a reporting company be held liable?

Yes. An individual who willfully files a false or fraudulent beneficial ownership information report on a company's behalf may be subject to the same civil and criminal penalties as the reporting company and its senior officers.

ii. Can a beneficial owner or company applicant be held liable for refusing to provide required information to a reporting company?

Yes. As described above, an enforcement action can be brought against an individual who willfully causes a reporting company's failure to submit complete or updated beneficial ownership information to FinCEN. This would include a beneficial owner or company applicant who willfully fails to provide required information to a reporting company.¹⁷⁴

In early 2024, the Treasury Department published the inflation adjustments for various FinCEN penalties, including the civil penalty for beneficial ownership information reporting violation under 31 U.S.C. §5336(h)(3)(A)(i). As the \$500 penalty was set back in 2001 (when the bill was enacted), the 2024 inflation adjustment will bring the per day penalty to \$591.¹⁷⁵

¹⁷⁴ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

¹⁷⁵ 31 CFR §1010.821, January 25, 2024, <https://www.govinfo.gov/content/pkg/FR-2024-01-25/pdf/2024-01420.pdf>

How Reports Will Be Filed

The FAQ has information regarding how the reports will be filed. As is true of other FinCEN reports, such as the Foreign Bank Account Reporting (FBAR) filing, this report will be filed online:

14. How will I report my company's beneficial ownership information?

If you are required to report your company's beneficial ownership information to FinCEN, you will do so electronically through a secure filing system available via FinCEN's website. This system is currently being developed and will be available before your report must be filed.¹⁷⁶

In the December 12, 2023 update to the FAQ, FinCEN provided the following information regarding who can file a BOI report:

B. 8. Who can file a BOI report on behalf of a reporting company, and what information will be collected on filers?

Anyone whom the reporting company authorizes to act on its behalf—such as an employee, owner, or third-party service provider—may file a BOI report on the reporting company's behalf. When submitting the BOI report, individual filers should be prepared to provide basic contact information about themselves, including their name and email address or phone number.¹⁷⁷

A Q&A included in the December update of the FAQ supplied information about certain aspects of the procedures for filing and updating the report.

H. 4. If a reporting company needs to update one piece of information on a BOI report, such as its legal name, does the reporting company have to fill out an entire new BOI report?

Updated BOI reports will require all fields to be submitted, including the updated pieces of information. For example, if a reporting company changes its legal name, the reporting company will need to file an updated BOI report to include the new legal name and the previously reported, unchanged information about the company, its beneficial owners, and, if required, its company applicants.

A reporting company that filed its prior BOI report using the fillable PDF version may update its saved copy and resubmit to FinCEN. If a reporting company used FinCEN's web-based application to submit the previous BOI report, it will need to submit a new report in its entirety by either accessing FinCEN's web-based

¹⁷⁶ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, March 24, 2023, p. 10

¹⁷⁷ "Beneficial Ownership Information Reporting Frequently Asked Questions," Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

application to complete and file the BOI report, or by using the PDF option to complete the BOI report and upload to the BOI e-Filing application.¹⁷⁸

Entities with Access to Beneficial Ownership Information

Clients will likely ask who will have access to this information, much of which they may consider private and sensitive. The FAQ has information on the limited list of those who will be able to request access to the information in this database:9488741008, 9488751008

15. Who will be able to access reported beneficial ownership information and for what purposes?

The Corporate Transparency Act authorizes FinCEN to disclose beneficial ownership information in certain circumstances to six types of requesters:

- o U.S. Federal agencies engaged in national security, intelligence, and law enforcement activities;
- o State, local, and Tribal law enforcement agencies with court authorization;
- o The U.S. Department of the Treasury;
- o Financial institutions using beneficial ownership information to conduct legally required customer due diligence, provided the financial institutions have their customer consent to retrieve the information;
- o Federal and state regulators assessing financial institutions for compliance with legally required customer due diligence obligations; and
- o Foreign law enforcement agencies and certain other foreign authorities who submit qualifying requests for the information through a U.S. Federal agency.

The Corporate Transparency Act imposes stringent access requirements and safeguards on each group of requesters.¹⁷⁹

FinCEN ends the FAQs with a discussion of the steps being taken to protect this data:

16. How will FinCEN protect beneficial ownership information reported to it?

Protecting the security and confidentiality of beneficial ownership information is a top priority for FinCEN. Federal law requires FinCEN to implement protocols to safeguard beneficial ownership information, to build a secure IT system to store the

¹⁷⁸ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, Revised December 12, 2023

¹⁷⁹ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, March 24, 2023, p. 11

information, and to establish processes and procedures to ensure that only authorized users can access beneficial ownership information for authorized purposes.

FinCEN is developing the policies and procedures that will govern access to and handling of beneficial ownership information. FinCEN is also building a secure and confidential IT system to store the information. Consistent with Federal law, the system will be cloud-based, and will meet the highest Federal Information Security Modernization Act (FISMA) level to keep beneficial ownership information secure.

FinCEN will work closely with those authorized to access beneficial ownership information to ensure that they understand their roles and responsibilities to ensure that the reported information is used only for authorized purposes and handled in a way that protects its security and confidentiality.¹⁸⁰

FINCEN BENEFICIAL OWNERSHIP INFORMATION REPORT FILING

On January 1, 2024, as promised, FinCEN opened up its website at <http://www.fincen.gov/boi> for filing reports and obtaining FinCEN identifiers. The main page now provides the following links.



When the option to file using the BOI E-Filing System is selected, two options are presented.

¹⁸⁰ “Beneficial Ownership Information Reporting Frequently Asked Questions,” Financial Crimes Enforcement Network, United States Treasury, March 24, 2023, p. 11



File the Beneficial Ownership Information Report (BOIR)

Select the filing method that works best for you:



File PDF BOIR

- Adobe Reader is required
- Prepare report offline at your own pace, save as you go
- Reuse PDF BOIR when filing updates/corrections
- Download BOIR transcript upon submission

Prepare BOIR

Submit BOIR



File Online BOIR

- Adobe Reader NOT required
- Prepare report online and submit now
- Prepare new Online BOIR when filing updates/corrections
- Download BOIR transcript upon submission

Prepare & Submit BOIR

The PDF form is reproduced on the following pages. That form is to be filled out and the completed copy uploaded to FinCEN.

Beneficial Ownership Information Report

[Home](#)[Reporting Company](#)[Company Applicant\(s\)](#)[Beneficial Owner\(s\)](#)

Beneficial Ownership Information Report

OMB No. 1506-0076

Version Number: 1.0

Release Date: 01-01-2024

Report Preparation & Submission Instructions:

[Instructions](#)1. Complete the report in its entirety with all required information. Click **Instructions** for help.[Validate](#)2. Click **Validate** to ensure all entered data is properly formatted and that all required fields are completed.[Finalize](#)3. Click **Finalize** to lock the entries in the report and prepare it for submission. Click **Edit Report** to unlock and re-edit.[Save](#)4. Click **Save** to retain a local copy of the report (this can be done at any time during report preparation).[Print](#)5. (Optional) Click **Print** to print a hard copy of your completed report.[Ready To File](#)6. Select **Ready to File** (activated after the report is finalized and saved locally) to begin the submission process.

Filing Information

1. *Type of filing:

a. Initial report

☐

b. Correct prior report

☐

c. Update prior report

☐

d. Newly exempt entity

☐

Reporting Company information associated with most recent report, if any:

e. Legal name

f. Tax Identification type

g. Tax Identification number

h. Country/Jurisdiction (if foreign tax ID only)

2. Date prepared (auto-filled when form is finalized)

PRIVACY ACT AND PAPERWORK REDUCTION ACT NOTICE

This notice is given under the Privacy Act of 1974 (Privacy Act) and the Paperwork Reduction Act of 1995 (Paperwork Reduction Act). The Privacy Act and Paperwork Reduction Act require that FinCEN inform persons of the following when requesting and collecting information in connection with this collection of information. This collection of information is authorized under 31 U.S.C. 5336 and 31 C.F.R. 1010.380. The principal purpose of this collection of information is to generate a database of information that is highly useful in facilitating national security, intelligence, and law enforcement activities, as well as compliance with anti-money laundering, countering the financing of terrorism, and customer due diligence requirements under applicable law. Pursuant to 31 U.S.C. 5336 and 31 C.F.R. 1010.380, reporting companies and certain other persons must provide specified information. The provision of that information is mandatory and failure to provide that information may result in criminal and civil penalties. The provision of information for the purpose of requesting a FinCEN Identifier is voluntary; however, failure to provide such information may result in the denial of such a request. Generally, the information within this collection of information may be shared as a "routine use" with other government agencies and financial institutions that meet certain criteria under applicable law. The complete list of routine uses of the information is set forth in the relevant Privacy Act system of record notice available at <https://www.federalregister.gov/documents/2023/09/13/2023-19814/privacy-act-of-1974-system-of-records>. According to the Paperwork Reduction Act of 1995, no persons are required to respond to a collection of information unless it displays a valid OMB control number. The valid OMB control number for this information collection is 1506-0076. It expires on November 30, 2026. The estimated average burden associated with this collection of information from reporting companies is 90 to 650 minutes per respondent for reporting companies with simple or complex beneficial ownership structures, respectively. The estimated average burden associated with reporting companies updating information previously provided is 40 to 170 minutes per respondent for reporting companies with simple or complex beneficial ownership structures, respectively. The estimated average burden associated with this collection of information from individuals applying for FinCEN identifiers is 20 minutes per applicant. The estimated average burden associated with individuals who have obtained FinCEN identifiers updating information previously provided is 10 minutes per individual. Comments regarding the accuracy of this burden estimate, and suggestions for reducing the burden should be directed to the Financial Crimes Enforcement Network, P. O. Box 39, Vienna, VA 22183, Attn: Policy Division.

Beneficial Ownership Information Report

Home

Reporting Company

Company Applicant(s)

Beneficial Owner(s)

Part I. Reporting Company Information

3. Request to receive FinCEN Identifier (FinCEN ID) ☐

4. Foreign pooled investment vehicle ☐

Full legal name and alternate name(s):

5. * Reporting Company legal name

6. Alternate name (e.g. trade name, DBA)

Form of identification:

7. * Tax Identification type

8. * Tax Identification number

9. Country/Jurisdiction (if foreign tax ID only)

Jurisdiction of formation or first registration:

10. * a. Country/Jurisdiction of formation

Domestic Reporting Company:

b. State of formation

c. Tribal jurisdiction of formation

d. Name of the other Tribe

Foreign Reporting Company:

e. State of first registration

f. Tribal jurisdiction of first registration

g. Name of the other Tribe

Current U.S. Address:

11. * Address (number, street, and apt. or suite no.)

12. * City

13. * U.S. or U.S. Territory

14. * State

15. * ZIP Code

Beneficial Ownership Information Report

[Home](#)[Reporting Company](#)[Company Applicant\(s\)](#)[Beneficial Owner\(s\)](#)

16. Existing Reporting Company ☐ (check if Reporting Company was created or registered before January 1, 2024)
17. (This item is reserved for future use)

Part II. Company Applicant Information

1 of 1



Company Applicant FinCEN ID:

18. FinCEN ID

Full legal name and date of birth:

19. * Individual's last name

20. * First name

21. Middle name

22. Suffix

23. * Date of birth

Current address:

24. * Address type ☐ a. Business address ☐ b. Residential address

25. * Address (number, street, and apt. or suite no.)

26. * City

27. * Country/Jurisdiction

28. * State

29. * ZIP/Foreign postal code

Form of identification and issuing jurisdiction:

30. * Identifying document type

31. * Identifying document number

32. * Identifying document issuing jurisdiction:

a. Country/Jurisdiction

b. State

c. Local/Tribal

d. Other local/Tribal description

33. * Identifying document image

Beneficial Ownership Information Report

[Home](#)[Reporting Company](#)[Company Applicant\(s\)](#)[Beneficial Owner\(s\)](#)

34. *(This item is reserved for future use)*

Part III. Beneficial Owner Information

1 of 1



35. Parent/Guardian information instead of minor child ☐ *(check if the Beneficial Owner is a minor child and the parent/guardian information is provided instead)*

Beneficial Owner FinCEN ID:

36. FinCEN ID

Exempt entity:

37. Exempt entity

☐

Full legal name and date of birth:

38. * Individual's last name or entity's legal name.

39. * First name

40. Middle name

41. Suffix

42. * Date of birth

Residential address:

43. * Address (number, street, and apt. or suite no.)

44. * City

45. * Country/Jurisdiction

46. * State

47. * ZIP/Foreign postal code

Form of identification and issuing jurisdiction:

48. * Identifying document type

49. * Identifying document number

50. * Identifying document issuing jurisdiction:

a. Country/Jurisdiction

b. State

c. Local/Tribal

d. Other local/Tribal description

51. * Identifying document image

Add Attachment

Remove Attachment

CHECKLIST OF STEPS TO ASSIST CLIENTS WITH BENEFICIAL OWNER REPORTING

Below is a checklist of items for a CPA to consider when advising their client on the beneficial ownership reporting provisions of the Corporate Transparency Act (CTA). Note that this checklist is not exhaustive and should be tailored to each client's specific situation. It's essential to stay updated on the latest regulatory guidance and requirements.

- Determine applicability:
 - Confirm if the client's entity is a "reporting company" under the CTA.
 - Identify any exemptions (e.g., publicly traded companies, banks, credit unions, investment companies, etc.).
- Identify beneficial owners:
 - Understand the CTA's definition of a beneficial owner (i.e., individuals who own 25% or more of the entity or exercise substantial control).
 - Assist the client in identifying all qualifying beneficial owners.
 - Advise on reporting requirements for indirect ownership interests or multi-layered ownership structures.
- Collect required information:
 - Obtain full legal names, dates of birth, current residential or business addresses, and a unique identifying number and document image for each beneficial owner.
 - Ensure the accuracy and completeness of the collected information.
- Initial reporting:
 - Determine if an initial report is required upon the formation or registration of a new entity.
 - Prepare and submit the initial report to the Financial Crimes Enforcement Network (FinCEN) within the required timeframe.
- Updates and changes:
 - Advise clients on the obligation to report changes in beneficial ownership within 30 days after becoming aware of the change in information.
 - Establish procedures for monitoring and tracking beneficial ownership changes.

- Assist with preparing and submitting reports to FinCEN for any changes.
- Recordkeeping requirements:
 - Help clients establish systems for maintaining accurate records of beneficial ownership information for at least five years after the entity’s dissolution or termination.
- Compliance programs and training:
 - Assist clients in developing a compliance program tailored to their specific risk profile and industry.
 - Provide training on CTA requirements and reporting obligations.
- Penalties and enforcement:
 - Inform clients about the potential civil and criminal penalties for non-compliance, including fines and imprisonment.
 - Advise on the importance of timely reporting and accurate recordkeeping.
- Privacy and data security:
 - Educate clients on the privacy implications of reporting beneficial ownership information.
 - Assist in implementing data security measures to protect sensitive information.
- Monitor regulatory updates:
 - Stay informed about new guidance, regulations, or amendments to the CTA.
 - Update clients on any changes that may affect their reporting obligations.

Remember to consult with legal counsel and other experts as needed, as this checklist is for informational purposes only and does not constitute legal or professional advice.

NOTES

Unit 4

Status of Employee Retention Credit Claims and IRS Programs

LEARNING OBJECTIVES

- ❑ Determine what IRS programs a client with an outstanding ERC credit claim applies to the client and the advisability of the client using such a program
- ❑ Advise a client on options that exist if a taxpayer has grown tired of waiting for the IRS to act on their claim
- ❑ Understand the interaction of appeals rights for a taxpayer with a disallowed claim with the statute of limitations on filing suit to challenge the IRS's denial of the claim

The CARES Act employee retention credit and the later modifications continue to cause issues for tax advisers. The IRS had announced a moratorium on processing claims filed after mid-September of 2023, one that still applies to claims filed after January 31, 2024. But even for claims not covered by the moratorium the IRS has been overwhelmed by the sheer number of claims and many taxpayers are awaiting decisions on claims filed long ago.

As well, the IRS continues to emphasize the amount of obviously erroneous claims they state exist in the claims they have received (at least in their view). In this section, we'll look at the current state of the program and potential options taxpayers have to end the mystery regarding their claim—but note that many of these options are either not cost-effective for many taxpayers, involve giving up on their claim or asking for assistance from parties such as the IRS Taxpayers Advocate Office who may decline to assist absent a showing of serious financial distress.

IRS VOLUNTARY WITHDRAWAL PROGRAM

Taxpayers who have not yet received payment of their refund claim may decide to withdraw their claim. Although this may seem a rather sub-optimal way to resolve uncertainty related to the claim, taxpayers who have had a party show interest in acquiring their business entity may be concerned about moving forward when there is a potential the IRS might pay the claim, but then later come back to the entity to recover the refund paid.

As well, the client may have now decided their claim likely was too aggressive and just wanted to avoid the risk of running into a dispute with the IRS.

The Internal Revenue Service (IRS) has provided details about its program allowing employers to voluntarily withdraw their refund claims for the Employee Retention Tax Credit (ERC). This provision applies to those who have not yet received the refund or, if received, have not cashed the check.¹⁸¹

The news release delineates the reasons the IRS introduced this program for employers:

This new withdrawal option allows certain employers that filed an ERC claim but have not yet received a refund to withdraw their submission and avoid future repayment, interest and penalties. Employers that submitted an ERC claim that's still being processed can withdraw their claim and avoid the possibility of getting a refund for which they're ineligible.

The IRS created the withdrawal option to help small business owners and others who were pressured or misled by ERC marketers or promoters into filing ineligible claims. Claims that are withdrawn will be treated as if they were never filed. The IRS will not impose penalties or interest.

Those who willfully filed a fraudulent claim, or those who assisted or conspired in such conduct, should be aware that withdrawing a fraudulent claim will not exempt them from potential criminal investigation and prosecution.¹⁸²

Taxpayers Eligible for the Program

Simultaneously with the news release, the IRS published Fact Sheet 2023-24¹⁸³, offering further details about the program. The release specifies which parties can request the withdrawal of an ERC claim.

Employers can use the ERC claim withdrawal process if of **all** the following apply:

- They made the claim on an **adjusted employment tax return** (Forms 941-X, 943-X, 944-X, CT-1X).

¹⁸¹ "IRS announces withdrawal process for Employee Retention Credit claims; special initiative aimed at helping businesses concerned about an ineligible claim amid aggressive marketing, scams," IR-2023-193, October 19, 2023, <https://www.irs.gov/newsroom/irs-announces-withdrawal-process-for-employee-retention-credit-claims-special-initiative-aimed-at-helping-businesses-concerned-about-an-ineligible-claim-amid-aggressive-marketing-scams> (retrieved October 19, 2023)

¹⁸² "IRS announces withdrawal process for Employee Retention Credit claims; special initiative aimed at helping businesses concerned about an ineligible claim amid aggressive marketing, scams," IR-2023-193, October 19, 2023

¹⁸³ "Help for businesses: Steps for withdrawing an Employee Retention Credit claim," Fact Sheet FS-2023-24, October 19, 2023, <https://www.irs.gov/newsroom/help-for-businesses-steps-for-withdrawing-an-employee-retention-credit-claim> (retrieved October 19, 2023)

- They filed the adjusted return only to claim the ERC, and they made **no other adjustments**.
- They want to withdraw **the entire amount** of their ERC claim.
- The IRS **has not paid** their claim, or the IRS has paid the claim, but they haven't cashed or deposited the refund check.

Businesses that have willfully filed fraudulent claims, assisted in such conduct or conspired to do so should be aware, however, that withdrawing a fraudulent claim will not exempt them from potential criminal investigation and prosecution.¹⁸⁴

The Fact Sheet indicates that certain employers, even if ineligible for this process, might pursue an alternative approach:

Employers that can't use this process may still be able to file another adjusted return if they need to:

- Reduce the amount of their ERC claim
- Make other changes to their adjusted return

The frequently asked questions¹⁸⁵ about the ERC have more details for these employers.¹⁸⁶

Question 1 in the "Amending a Return" section of the Frequently Asked Questions page provides guidance for employers looking to reduce their claimed credit:

Prepare a new adjusted return (Form 941-X, Form 943-X, Form 944-X, Form CT-1X) with the correct amount of ERC and any other corrections for that tax period. Mail the new adjusted return to the IRS using the address in the instructions for the form that applies to your business or organization. Do not send the new adjusted return to the dedicated ERC claim withdrawal fax line. IRS will not process new adjusted returns sent to this fax line.¹⁸⁷

¹⁸⁴ "Help for businesses: Steps for withdrawing an Employee Retention Credit claim," Fact Sheet FS-2023-24, October 19, 2023

¹⁸⁵ "Frequently asked questions about the Employee Retention Credit," IRS website, October 19, 2023, <https://www.irs.gov/coronavirus/frequently-asked-questions-about-the-employee-retention-credit> (retrieved October 19, 2023)

¹⁸⁶ "Help for businesses: Steps for withdrawing an Employee Retention Credit claim," Fact Sheet FS-2023-24, October 19, 2023

¹⁸⁷ "Frequently asked questions about the Employee Retention Credit," IRS website, October 19, 2023

Question 2 addresses situations where a taxpayer intends to withdraw the ERC claim but also requires additional, non-ERC related amendments to their payroll tax return.

Prepare a new adjusted return (Form 941-X, Form 943-X, Form 944-X, Form CT-1X) with the correct amount of ERC and any other corrections for that tax period. Mail the new adjusted return to the IRS using the address in the instructions for the form that applies to your business or organization. Do not send the new adjusted return to the dedicated ERC claim withdraw fax line. IRS will not process new adjusted returns sent to this fax line.¹⁸⁸

How to Handle a Withdrawal Request – Those Who Used a Payroll Company

The Fact Sheet initiates its section on requesting the withdrawal of an ERC claim by addressing the unique scenario in which an employer has submitted the initial ERC claim via a professional payroll service.

Employers that filed their ERC claim through a professional payroll company and want to request a claim withdrawal will need to contact the entity that filed the claim on their behalf. These companies may include a certified professional organization (CPEO), professional employer organization (PEO) or other Section 3504 agents.¹⁸⁹

The Fact Sheet subsequently addresses different scenarios pertaining to taxpayers who did not utilize a professional payroll service.

How to Handle a Withdraw Request - Employers Who Haven't Received a Refund and Haven't Been Notified Their Claim is Under Audit

For employers who have not received a refund and have not been informed by the IRS that their examination is under audit, the Fact Sheet offers the subsequent guidelines.

If the employer filed an adjusted return (Form 941-X, 943-X, 944-X, CT-1X) to claim the ERC and would like to withdraw the entire claim, they can use the process below. If they filed adjusted returns for more than one tax period, they must follow the steps below **for each tax period** for which they are requesting a withdrawal.

To request a withdrawal, follow these steps:

- Make a **copy** of the adjusted return with the claim they wish to withdraw.
- In the left margin of the first page, write “**Withdrawn.**”

¹⁸⁸ “Frequently asked questions about the Employee Retention Credit,” IRS website, October 19, 2023

¹⁸⁹ “Help for businesses: Steps for withdrawing an Employee Retention Credit claim,” Fact Sheet FS-2023-24, October 19, 2023

- In the right margin of the first page:
 - Have an authorized person **sign** and **date** it.
 - Write their **name** and **title** next to their signature.
- **Fax the signed copy** of the return to the IRS's ERC claim withdrawal fax line at 855-738-7609. This is the withdrawal request. Keep the copy with tax records.

If a taxpayer can't fax their request, they can mail the signed copy to the address in the instructions for the adjusted return that applies to their business or organization. Before doing so they should make a copy of the signed and dated first page to keep with their tax records. It will take longer for the IRS to receive a mailed request. Track the package to confirm delivery.

How to Handle a Withdraw Request - Employers That Haven't Received a Refund and Have Been Notified Their Claim is Under Audit

For taxpayers who are under examination but have not yet received their refund check, the Fact Sheet prescribes the subsequent procedures to be taken if they wish to withdraw their claim:

Employers facing an IRS audit, also referred to as an exam, can still withdraw their ERC claim. If a taxpayer has been notified that the IRS is auditing the adjusted return that includes their ERC claim, they should prepare their withdrawal request using the steps in Section A, above, but they should not fax it to the withdrawal fax line or mail it using the address below. Instead:

- If they've been assigned an examiner, they should communicate with the examiner about how to fax or mail the withdrawal request directly to them.
- If they haven't been assigned an examiner, they should respond to the audit notice with the withdrawal request, using the instructions in the notice for responding.¹⁹⁰

¹⁹⁰ "Help for businesses: Steps for withdrawing an Employee Retention Credit claim," Fact Sheet FS-2023-24, October 19, 2023

How to Handle a Withdraw Request - Employers Who Received a Refund Check but Haven't Cashed or Deposited It

When a taxpayer has received a refund check for their claim, has not cashed or deposited it, and now desires to withdraw their claim, the IRS provides the following guidance for the employer:

Employers that have received a refund check but still haven't cashed or deposited it, can still withdraw their claim. They need to mail the voided check with their withdrawal request using these steps:

- Prepare the **claim withdrawal request** using the steps in Section A,¹⁹¹ above, but don't fax the request.
- Write "**Void**" in the endorsement section on the back of the refund check.
- Include a **note** that says, "ERC Withdrawal" and briefly explain the reason for returning the refund check.
- Make **copies for tax records** of the front and back of the voided check, the explanation notes and the signed and dated withdrawal request page.
- Don't staple, bend or paper clip the voided check; include it with your claim withdrawal request and **mail it** to the IRS at:
Cincinnati Refund Inquiry Unit
PO Box 145500
Mail Stop 536G
Cincinnati, OH 45250
- Track your package to confirm delivery.

What Happens Next?

The employer is not yet assured the withdrawal of their claim will be accepted merely because they followed these steps. Rather the taxpayer must await confirmation from the IRS of the acceptance of the withdrawal as noted in the Fact Sheet.

Taxpayers will get a letter from the IRS about whether their withdrawal request was accepted or rejected. The approved request is not effective until the taxpayer has the acceptance letter from the IRS.

¹⁹¹ The steps used by an employer who had not received a refund yet and is not under exam.

If the IRS accepts the withdrawal, the taxpayer may need to amend their income tax return. See Claiming the ERC for explanation of how ERC affects your income tax return. If a taxpayer needs help, they should consult a trusted tax professional.¹⁹²

If the withdrawal is not accepted, the employer will need to evaluate why the withdrawal was not accepted. If it was merely because the employer had already cashed the refund check, then the employer needs to wait for the IRS guidance to come for those taxpayers. If the taxpayer simply didn't follow the correct procedure (they were under exam but attempted to file the form as if they weren't), then the employer needs to follow the correct procedure.

But if the employer appears to otherwise qualify, that could indicate that the IRS believes the taxpayer had filed a fraudulent claim and the employer may wish to consult with legal counsel if that has not already taken place.

SUIT FOR REFUND

An employer that filed a claim for an ERC refund more than 6 months ago has the ability to force the matter without waiting on the IRS to rule on their claim. That sounds like good news, but there is a bit of downside. The solution is to file a suit for refund against the IRS in federal court which also means incurring substantial legal fees even though there's no assurance that the employer's claim will be upheld. In many cases, even if the claim would be upheld, the potential costs of litigating the claim could easily be more than the claim itself.

Under IRC §6532, a taxpayer must first file an administrative claim for refund with the IRS before filing suit for refund. Once that is done the taxpayer must wait until one of the following two events takes place before filing suit for the fund:

- The IRS disallows part or all of the claim for refund or
- Six months has passed since the date the claim was filed with the IRS.¹⁹³

If the IRS does formally disallow all or part of the claim, the suit must be filed within 2 years of the date the IRS mails the notice of disallowance to the IRS by certified or registered mail.¹⁹⁴

Note that the two-year period to file the suit after the IRS notice of disallowance can be extended in writing by agreement of the taxpayer and the IRS.¹⁹⁵ However, that period to file the refund suit is *not* extended by any reconsideration, consideration or other action by the IRS (aside from the written agreement just noted)—and that includes having the disallowance before the IRS Appeals Division.¹⁹⁶

¹⁹² "Help for businesses: Steps for withdrawing an Employee Retention Credit claim," Fact Sheet FS-2023-24, October 19, 2023

¹⁹³ IRC §6532(a)(1)

¹⁹⁴ IRC §6532(a)(1)

¹⁹⁵ IRC §6532(a)(2)

¹⁹⁶ IRC §6532(a)(4)

IRC §6532(a) reads as follows:

(a) **Suits by taxpayers for refund.**

(1) **General rule.** No suit or proceeding under section 7422(a) for the recovery of any internal revenue tax, penalty, or other sum, shall be begun before the expiration of 6 months from the date of filing the claim required under such section unless the Secretary renders a decision thereon within that time, nor after the expiration of 2 years from the date of mailing by certified mail or registered mail by the Secretary to the taxpayer of a notice of the disallowance of the part of the claim to which the suit or proceeding relates.

(2) **Extension of time.** The 2-year period prescribed in paragraph (1) shall be extended for such period as may be agreed upon in writing between the taxpayer and the Secretary.

(3) **Waiver of notice of disallowance.** If any person files a written waiver of the requirement that he be mailed a notice of disallowance, the 2-year period prescribed in paragraph (1) shall begin on the date such waiver is filed.

(4) **Reconsideration after mailing of notice.** Any consideration, reconsideration, or action by the Secretary with respect to such claim following the mailing of a notice by certified mail or registered mail of disallowance shall not operate to extend the period within which suit may be begun.

(5) **Cross reference.** For substitution of 120-day period for the 6-month period contained in paragraph (1) in a title 11 case, see section 505(a)(2) of title 11 of the United States Code.

This past year saw a taxpayer lose a case on the very issue of the IRS's inability to extend the statute informally in the case of *Moy v. United States*, USDC ND Calif, Docket No. 5:23-CV-03151, May 21, 2024.¹⁹⁷ While not an ERC case, the IRS denied a claim for a refund of foreign tax credit that was filed timely. The denial took place in August 2018 and the taxpayer filed a protest in November 2019, with the matter sent to Appeals.

Twice Appeals wrote to the taxpayer saying they would look into the matter and respond within 60 days (in December 2019 and February 2020). In January 2021 Appeals wrote the taxpayer stating that the Appeal was denied because she had failed to file suit within 2 years of the denial (any suit had to have been filed by August 2020). The trial court upheld the IRS motion to dismiss her suit as

¹⁹⁷ *Moy v. United States*, USDC ND Calif, Docket No. 5:23-CV-03151, May 21, 2024, <https://www.taxnotes.com/research/federal/court-documents/court-opinions-and-orders/irs-letters-didnt-extend-limitations-period-refund-suit-dismissed/7k70w>

untimely because the unambiguous wording of the statute clearly barred the IRS from unilaterally extending the statute.

CPAs who are used to dealing with appeals of agent's findings in exams must note that, in this case, a failure to get the statute extended before it expires if a matter is still waiting to be heard in Appeals, for Appeals to issue its findings or even if Appeals has agreed to the refund even though not yet paid will result in the taxpayer not receiving that refund even if all parties agree the employer was eligible for it.

Some taxpayers, upset with the slowness of the process, may wonder if they should file suit to try and speed up the process. Various counsel have suggested that filing a suit might make sense from a cost-benefit standpoint if the taxpayer's claim is based on a drop in gross receipts. In such a case the items potentially in dispute are limited and the taxpayer may be in possession of clear evidence that their receipts took the requisite dip. If the employer is small enough to be eligible to make a qualified offer in such a case.

If the requirements are met, a taxpayer who makes a qualified offer allows the IRS 90 days to accept that offer to settle the case. If the IRS does not accept that offer within that period of time and the taxpayer is awarded a refund of at least the qualified offer amount, the IRS can be on the hook for paying the taxpayer's legal fees incurred following the rejection of the offer. The offer thus puts the IRS "on the clock" to decide whether to accept the offer or go to court and risk an award of legal fees to the taxpayer.

Most counsel are not advising filing suit to speed up the process for partial suspension cases. At this point, it's not clear what the courts will finally accept as a partial suspension for these purposes. As the attorney put it on the Arizona Society of CPA's Connect tax forum, there is much more for the parties to dispute in such a case, thus the costs of discovery could be quite high. And he also suggested it would not be a bad idea to first see if Appeals would agree to accept some or all of the claim before taking on the burden of litigating the case.

IRS VOLUNTARY DISCLOSURE PROGRAM

The IRS originally announced its first voluntary disclosure program for those taxpayers that have received a refund but now believe they do not qualify for it in December of 2021, with that first program ending on March 22, 2024.¹⁹⁸

The key features of that program were that employers who received a refund related to the employee retention credit could apply only if the following were true:

- The employer is not under criminal investigation and has not been notified that they are under criminal investigation.

¹⁹⁸ "IRS: New Voluntary Disclosure Program lets employers who received questionable Employee Retention Credits pay them back at discounted rate; interested taxpayers must apply by March 22," IR-2023-247, Dec. 21, 2023

- The employer is not under an IRS employment tax examination for the tax period for which they're applying to the Voluntary Disclosure Program.
- The employer has not received an IRS notice and demand for repayment of part or all of the ERC.
- The IRS has not received information from a third party that the taxpayer is not in compliance or has not acquired information directly related to the noncompliance from an enforcement action.¹⁹⁹

The taxpayer cannot use this program to adjust the amount of the claim for any quarter—rather, it only applies if the taxpayer agrees to waive all rights to any ERC credit for that quarter. A participating taxpayer received the following benefits if accepted into the program:

- The taxpayer only needs to pay back 80% of the refund amount they received for the quarter(s) in question. The reduced amount paid back was in recognition of the fact that many employers had paid significant contingent fees to consultants when applying for the credit.
- The taxpayer does not need to repay any interest paid to the taxpayer with the refund fund.
- If the balance due is paid when the taxpayer is accepted into the program, no penalties (including failure to pay) will be assessed against the taxpayer for the quarter(s) involved and no interest will be required to be paid. If the taxpayer is unable to pay the entire balance, the taxpayer can apply for an installment agreement. However, interest and penalties will be incurred for the term of the agreement until the entire balance due is paid.

The taxpayer must file *Form 15434, Application for Employee Retention Credit Voluntary Disclosure Program*. On that form, the taxpayer, among other things, must disclose the names, addresses, and other information about any party that either advised them regarding their claim or prepared the claim.

Taxpayers who participate in this program are *not* provided with any protection from later criminal prosecution by the IRS. Taxpayers who believe they may have exposure to criminal charges would need to enter the Criminal Investigation Division's separate general voluntary disclosure program. Those using that program will not be able to access the favorable terms found in the voluntary program.

In August the IRS announced the opening of a second voluntary disclosure program related to the ERC.²⁰⁰

¹⁹⁹ "IRS: New Voluntary Disclosure Program lets employers who received questionable Employee Retention Credits pay them back at discounted rate; interested taxpayers must apply by March 22," IR-2023-247, Dec. 21, 2023

²⁰⁰ "IRS reopens Voluntary Disclosure Program to help businesses with problematic Employee Retention Credit claims; sending up to 30,000 letters to address more than \$1 billion in errant claims," IR-2024-212, Aug. 15, 2024

The IRS provides the following information related to this new program in IR-2024-213:²⁰¹

Interested employers must apply to the second ERC Voluntary Disclosure Program by Nov. 22, 2024. Applicants that the IRS accepts into the program will need to repay only 85% of the credits they received. This second round of the program is open for tax periods in 2021. Employers can't use the second VDP to disclose and repay ERC money from tax periods in 2020.

If the IRS paid interest on the employer's ERC refund claim, the employer doesn't need to repay that interest. Employers who are unable to repay the required 85% of the credit may be considered for an Installment Agreement on a case-by-case basis, pending submission and review of *Form 433-B, Collection Information Statement for Businesses*, and all required supporting documentation. Form 433-B is available on IRS.gov.

The IRS will not charge program participants interest or penalties on any credits they timely repay. However, if an employer can't repay the required 85% of the credit at the time they sign their closing agreement, they'll be required to pay penalties and interest in connection with an alternative payment arrangement such as an installment agreement.

To qualify for this program, employers must provide the IRS with the names, addresses, telephone numbers and details about the services provided by any advisors or tax preparers who advised or assisted them with their claims.

The IRS has provided a set of Frequently Asked Questions about the second ERC Voluntary Disclosure Program to help employers understand the terms of the program.²⁰²

To summarize, the key differences are:

- ERC refund claims from 2020 calendar quarters are *not* eligible for this program
- The amount of the refund that must be repaid is increased to 85% of the amount paid (that's up from 80% in the first program)

The program is open through November 22, 2024. As with the first program, participants in this program are offered no protection from criminal charges.

²⁰¹ "IRS provides details of second Employee Retention Credit Voluntary Disclosure Program; program for improper claims open through Nov. 22," IR-2024-213, Aug. 15, 2024

²⁰² "IRS provides details of second Employee Retention Credit Voluntary Disclosure Program; program for improper claims open through Nov. 22," IR-2024-213, Aug. 15, 2024

NATIONAL TAXPAYER ADVOCATE ADDRESSES ISSUES IN IRS ERC CLAIMS PROCESS

On August 21, 2024, the National Taxpayer Advocate issued a statement on the Employee Retention Credit in the form of a blog post.²⁰³ This statement aimed to provide taxpayers with comprehensive information regarding the subsequent procedures for those who have recently received a Notice of Disallowance for their Employee Retention Credit (ERC) claim. Additionally, the statement addressed perceived issues within the process currently and prospectively employed by the Internal Revenue Service (IRS) for these claims.

The post commences by highlighting recent advancements in the program, as the Internal Revenue Service (IRS) has concluded its moratorium on processing claims received subsequent to September 14, 2024. Consequently, the IRS will now give consideration to claims filed through January 31, 2024.

For many months I have been advocating for the IRS to lift the moratorium and pay the valid claims for the many businesses still waiting to receive their refunds. I was glad to see on August 8, 2024, the IRS announced that it will start processing claims filed through January 31, 2024, and will be sending over 50,000 refunds to businesses that filed claims prior to the moratorium. I encourage the IRS to continue on this track and move quickly toward either approving claims or, if necessary, requesting taxpayers provide supporting information.²⁰⁴

However, she observes that tax professionals have raised inquiries regarding several of the rejected claims and have also noted that the agency neglected to provide information about the appeal rights of some individuals who received a Notice of Disallowance of their claim along with that notice.

Although the IRS believed these were the low-hanging fruit among both the qualifying and non-qualifying claims, initial responses from some practitioners indicate that some of these disallowed claims are likely to qualify. In addition, some of the disallowance letters failed to inform taxpayers of their appeal rights or the basis for the disallowance, which the IRS acknowledges was a mistake. I discuss this issue in more detail later in the blog and provide recommendations as to how the IRS can right this wrong.²⁰⁵

²⁰³ “Did You Receive a Notice of Claim Disallowance for Your Employee Retention Credit Refund Claim? If So, Now What?,” NTA Blog, August 21, 2024, <https://www.taxpayeradvocate.irs.gov/news/nta-blog/did-you-receive-a-notice-of-claim-disallowance-for-your-employee-retention-credit-refund-claim-if-so-now-what/2024/08/> (retrieved August 22, 2024)

²⁰⁴ “Did You Receive a Notice of Claim Disallowance for Your Employee Retention Credit Refund Claim? If So, Now What?,” NTA Blog, August 21, 2024

²⁰⁵ “Did You Receive a Notice of Claim Disallowance for Your Employee Retention Credit Refund Claim? If So, Now What?,” NTA Blog, August 21, 2024

The article provides a detailed account of the procedures to which these claims were subjected, which deviated significantly from the Internal Revenue Service's standard protocols for handling such claims.

The manner in which the IRS generated this most recent batch of ERC disallowances and the process the IRS will use to review taxpayers' responses to these denials deviates significantly from normal IRS procedures. Typically, the IRS issues a notice of claim disallowance after conducting an examination (audit) of the taxpayer's claim. During this examination, the taxpayer can provide support for their refund claim. If the IRS disallows a taxpayer's claim, the taxpayer can choose to have the examiners' determination reviewed by the IRS's Independent Office of Appeals (Appeals) by submitting a protest requesting an administrative review of the IRS's determination, which under IRS administrative rules should generally be submitted 30 days from the date on the notice of claim disallowance. As the 30 day period is only an administrative deadline, we recommend that the IRS provide additional time for taxpayers to submit a protest. Considering the long delay in processing these claims and the errors in the notices of claim disallowance the IRS should be flexible.

By contrast, the IRS did not subject disallowed ERC claims to an examination; rather, the IRS conducted a risk-scoring analytic process. For these disallowed claims, the IRS's analytics determined the claim showed a high risk of being incorrect without first conducting an examination. Another stark difference from normal IRS processes is the processing pipeline in which a taxpayer's response to a notice of claim disallowance will travel. In fact, it almost turns normal IRS processes on its head. Specifically, when a taxpayer responds to a notice of claim disallowance they believe they are submitting a protest of the denial to Appeals, which is standard practice. However, this response will generally first be reviewed by the IRS and sent to a Revenue Agent for consideration.²⁰⁶

The article proceeds to illustrate the review process that will be incorporated before the return is forwarded to the Appeals.

The IRS is not calling this review an examination, but if it looks like a duck and walks like a duck... Based upon the response the IRS can allow the claim, request additional documentation from the taxpayer, or uphold the denial after considering all available documentation and forward the response to Appeals. It is only after this quasi-exam that the taxpayer's response would be sent to Appeals.

²⁰⁶ "Did You Receive a Notice of Claim Disallowance for Your Employee Retention Credit Refund Claim? If So, Now What?," NTA Blog, August 21, 2024

The IRS is still working to finalize this process, but taxpayers should receive a letter from the IRS informing them a review of their response has been conducted and their case is being forwarded to Appeals.²⁰⁷

In light of the extraordinary circumstances surrounding the claim's progression to this juncture, the Advocate presents the IRS with a series of formal recommendations outlining her proposed approach for the conduct of this process.

I recommend the IRS provide a detailed explanation of the basis for the disallowance and provide taxpayers an opportunity to respond to issues or questions identified during the IRS review process. This letter should include a deadline by which the taxpayer can provide additional information in response to the IRS' determination. This process would more closely mirror the examination process of a Revenue Agent issuing a Revenue Agent Report and allowing the taxpayer an opportunity to respond to issues and conclusions in the report. If taxpayers do not respond to this letter or if the IRS is still not persuaded after receiving even more information from the taxpayer, the IRS should forward the case to Appeals.²⁰⁸

The post proceeds to highlight a potential issue that could emerge due to this insertion of what is essentially a traditional examination step (requesting, obtaining, and analyzing information relevant to the claim) after the issuance of a Notice of Disallowance and before the matter is referred to the Office of Appeals.

Under current procedures, Appeals does not consider new information the IRS did not review first. Thus, if the IRS does not allow the taxpayer the opportunity to respond to the IRS's conclusion after reviewing the taxpayer's response to the notice of claim disallowance, the IRS may ultimately treat the taxpayer's case like a ping-pong ball. Specifically, if the IRS does not afford the taxpayer the opportunity to provide new information as part of the IRS review process, the taxpayer may do so once in Appeals. In this case, Appeals would send the case back to the IRS review function for further consideration of the new facts. This back-and-forth would undoubtedly elongate an already lengthy IRS process.²⁰⁹

The protracted proceedings that numerous taxpayers have already undergone will likely extend considerably should the taxpayer elect to exercise their appellate rights.

It is important for taxpayers and practitioners to understand that any IRS process involving a review of facts and circumstances, along with a referral to Appeals for its consideration, is going to be lengthy. Taxpayers should anticipate it will take many months, or even longer, before the IRS makes a determination prior to forwarding

²⁰⁷ "Did You Receive a Notice of Claim Disallowance for Your Employee Retention Credit Refund Claim? If So, Now What?," NTA Blog, August 21, 2024

²⁰⁸ "Did You Receive a Notice of Claim Disallowance for Your Employee Retention Credit Refund Claim? If So, Now What?," NTA Blog, August 21, 2024

²⁰⁹ "Did You Receive a Notice of Claim Disallowance for Your Employee Retention Credit Refund Claim? If So, Now What?," NTA Blog, August 21, 2024

the protest to Appeals. Additionally, once the case is assigned to Appeals, it can take up to five months or longer to hold an initial Appeals conference.²¹⁰

The post suggests that requesting an Appeals Fast Track may be useful in speeding up the process. However, the Advocate notes that it is not clear if those who respond to these notices will qualify for the fast track process. The post alludes to the potential utility of requesting an Appeals Fast Track in expediting the appeals process. However, the Advocate highlights the ambiguity surrounding the fast track eligibility criteria for those responding to such notices.

Taxpayers who qualify may want to request an Appeals Fast Track (FT). However, there is a question as to whether taxpayers who are responding to this batch of ERC notices of disallowance will qualify. FT is designed to quickly resolve a dispute between IRS Exam and the taxpayer. As mentioned above, taxpayers who respond to these notices of claim disallowance are going to be subject to an “exam-like” review, thereby potentially disqualifying them from seeking FT. Because the IRS is employing what is effectively an exam process, and having most of these taxpayer responses reviewed by a Revenue Agent, it should exercise its administrative authority and allow these taxpayers to request an FT²¹¹

The post points out a key issue a number of professionals may miss regarding when the deadline to file a challenge to the IRS Notice of Disallowance in court and even to receive any refund whatsoever. In a standard IRS exam, the deadline to file suit to challenge the IRS agent’s finding does not begin to run until the taxpayer’s appeal has run its course, either due to the appeals process being completed or the taxpayer letting the 30 day deadline to file an appeal run. The article draws attention to a crucial matter that many professionals may overlook concerning the deadline for contesting the IRS Notice of Disallowance in court and, more importantly, for receiving any refund whatsoever. In a typical IRS audit, the time frame to file a lawsuit challenging the IRS agent’s determination does not commence until the taxpayer’s appeal has reached its conclusion, either due to the completion of the appeals process or the taxpayer letting the 30-day deadline for filing an appeal elapse.

However, in this instance, the two-year time frame within which a lawsuit must be initiated commences promptly upon the issuance of the Notice of Disallowance and is not suspended while the taxpayer pursues an appeal unless a distinct agreement to extend the statute of limitations is entered into by the taxpayer and the Internal Revenue Service.

If a business who received a claim disallowance does not wish to contest the ERC disallowance, they do not have to do anything further. But if the business wants to pursue its claim in the courts, they may file suit in a U.S. district court or the U.S. Court of Federal Claims after receiving the notice of claim disallowance, whether or not they’ve first sought review of their claim in Appeals.

²¹⁰ “Did You Receive a Notice of Claim Disallowance for Your Employee Retention Credit Refund Claim? If So, Now What?,” NTA Blog, August 21, 2024

²¹¹ “Did You Receive a Notice of Claim Disallowance for Your Employee Retention Credit Refund Claim? If So, Now What?,” NTA Blog, August 21, 2024

Taxpayers who wish to file suit must do so within two years of receiving the notice of claim disallowance. The two-year period runs from the date on the top right-hand corner of the first page of the notice of claim disallowance. Not only does the taxpayer only have two years to file suit, but the IRS cannot issue the taxpayer a refund beyond this two-year period. In other words, if the taxpayer goes to Appeals, and Appeals agrees with the taxpayer but the two-year period has expired, the IRS cannot issue a refund because any such refund would be considered erroneous. It is important to note that going to Appeals does not extend this time period to file suit or for the IRS to issue a refund. However, the time period can be extended if the IRS and taxpayer agree and sign a Form 907.²¹²

Therefore, why not simply file a lawsuit? While a taxpayer possesses the ability to do so, disregarding other potential complications, this option frequently proves impractical due to the financial implications associated with pursuing the matter in a court of law. The expenses incurred during the legal process can readily exceed the value of the claim, and there is no assurance that the taxpayer will ultimately prevail.

Filing suit can be an expensive option. Before taxpayers take this journey, they should first ask themselves whether the claim disallowance is appropriate and the IRS is correct, or if they have compelling arguments as to why they are entitled to the ERC that deserve further review. The ERC rules are complex, so determining eligibility may not be a quick and simple answer. Depending on the basis for the disallowance, the taxpayer may need to consult with a tax professional to review the merits of their claim before making a decision to move forward with litigation.²¹³

The Advocate advises taxpayers to ensure they procure capable and impartial counsel pertaining to the validity of their claim in order to determine the actions to undertake and the associated expenses to accrue in the pursuit of their claim.

Recommendation and word of caution: Be diligent in selecting an advisor to help you determine the strength of your case and next steps. If you believe your claim qualifies, don't give up. But as you make that assessment, be realistic and remember the adage, "if it sounds too good to be true, it probably is."²¹⁴

In conclusion, the Advocate describes further problems that have been observed in the recently disseminated IRS notices.

As I mentioned towards the beginning of this blog, the IRS's notices of claim disallowance had problems causing many taxpayers to be confused. Specifically, taxpayers reported these notices omitted language explaining their rights and offered

²¹² "Did You Receive a Notice of Claim Disallowance for Your Employee Retention Credit Refund Claim? If So, Now What?," NTA Blog, August 21, 2024

²¹³ "Did You Receive a Notice of Claim Disallowance for Your Employee Retention Credit Refund Claim? If So, Now What?," NTA Blog, August 21, 2024

²¹⁴ "Did You Receive a Notice of Claim Disallowance for Your Employee Retention Credit Refund Claim? If So, Now What?," NTA Blog, August 21, 2024

unclear explanations of the reason(s) for the disallowance. Although in the IRS's August 8, 2024, announcement, it stated that more than 90 percent of the notices of claim disallowance were "validly issued," this doesn't mean they didn't contain errors – rather, it only means the IRS believes the errors did not invalidate the notices. Thus, I suspect it's possible – if not likely – that many of the notices, even if valid, contained errors. The IRS acknowledged in its August 8, 2024, news release,

"The IRS learned that some of the recent early mailings have inadvertently omitted a paragraph highlighting the process for filing an appeal to the IRS or district court, and the agency is taking steps to ensure this language is mailed to all relevant taxpayers. Regardless of the language in the notice, the IRS emphasizes taxpayers have administrative appeals rights available to them..."

Another complaint TAS has heard from taxpayers and practitioners involves incorrect explanations of the basis on which the IRS denied the claim. This indicates the IRS may have a problem with its risk-scoring filters. These errors have left taxpayers in a precarious situation. For instance, if taxpayers believed the explanation in the notice of claim disallowance is incorrect, do they only provide documentation to respond to what they believe is an incorrect conclusion? Or do they provide enough documentation to support the ERC claim more broadly? This is the tough predicament the IRS has put taxpayers in. This is further complicated by the lack of information the IRS has made available regarding the process for reviewing taxpayer responses to the notices of claim disallowance, and when these responses will reach Appeals. It is my understanding that the IRS intends to send letters to taxpayers recognizing that some notices of claim disallowance contained errors and reiterate a taxpayer's right to seek review of the IRS's determination from Appeals. These letters should also correct any errors related to the explanation of the disallowance, while clearly setting out the IRS's process for reviewing taxpayer responses to the disallowances and forwarding cases to Appeals. In this letter, the IRS should provide these taxpayers additional time for submission of their claim disallowance protest.²¹⁵

²¹⁵ "Did You Receive a Notice of Claim Disallowance for Your Employee Retention Credit Refund Claim? If So, Now What?," NTA Blog, August 21, 2024

NOTES

Unit 5

Estate and Gift Tax Developments

LEARNING OBJECTIVES

- Recognize clients who insured buy/sell arrangements may be impacted by the Supreme Court's decision in *Connelly*
- Advise clients regarding structuring insured buy/sell arrangements to reduce or eliminate the impact of *Connelly*

US SUPREME COURT HOLDS THAT LIABILITY TO REDEEM DECEDENT'S SHARES DOES NOT OFFSET LIFE INSURANCE PROCEEDS WHEN VALUING THE CORPORATION FOR ESTATE TAX PURPOSES

In the case of *Connelly v. United States*, US Supreme Court, Docket 23-146, June 6, 2024,²¹⁶ the U.S. Supreme Court resolved inconsistent holdings in lower courts. In a unanimous opinion, the Court, authored by Justice Thomas, found that although life insurance proceeds received by the corporation that were intended to be used to redeem a deceased majority shareholder had to be included in valuing the corporation as of the date the shareholder died, the estate could not use the obligation to redeem those shares to reduce the value of the corporation when valuing the interest.

The opinion begins by outlining the basic facts and the fundamental issue to be decided in this case:

Michael and Thomas Connelly owned a building supply corporation. The brothers entered into an agreement to ensure that the company would stay in the family if either brother died. Under that agreement, the corporation could be required to redeem (i.e., purchase) the deceased brother's shares. To fund the possible share redemption, the corporation obtained life insurance on each brother. After Michael

²¹⁶ [1] *Connelly v. United States*, US Supreme Court, Docket 23-146, June 6, 2024, <https://www.taxnotes.com/research/federal/court-documents/court-opinions-and-orders/insurance-proceeds-included-estate-tax-value-supreme-court-holds/7k9cn>

died, a narrow dispute arose over how to value his shares for calculating the estate tax. The central question is whether the corporation's obligation to redeem Michael's shares was a liability that decreased the value of those shares.²¹⁷

The opinion notes that a decedent's estate would include interests in any closely held corporation he/she might have owned at his/her death. These interests have various unique features:

A decedent's taxable estate includes his shares in a closely held corporation. 26 U.S.C. §2031(b). Closely held corporations ordinarily have only a few shareholders (often within the same family) and, unlike public corporations, those shareholders typically participate in the corporation's day-to-day management. 3 J. Cox & T. Hazen, *Law of Corporations* §14.1 (3d ed. 2010) (Cox & Hazen). Given this close working relationship, shareholders sometimes enter into an agreement to restrict the transfer of shares to outside investors. 3 *id.*, §14.9. One such arrangement involves "giving the corporation or the other shareholders the right to purchase the shares of a holder on his death." *Ibid.* A related arrangement, called a share redemption agreement, contractually requires a corporation to repurchase a deceased shareholder's shares. Although such an agreement may delineate how to set a price for the shares, it is ordinarily not dispositive for valuing the decedent's shares for the estate tax. See 26 U.S.C. §2703. As a general rule, the fair market value of the corporation determines the value of the shares, and one must therefore consider "the company's net worth, prospective earning power and dividend-paying capacity, and other relevant factors," "including proceeds of life insurance policies payable to . . . the company." 26 CFR §20.2031-2(f)(2).²¹⁸

In this case, two brothers held the corporation's shares and entered into a redemption agreement with the corporation that took effect upon either of their deaths.

Brothers Michael and Thomas Connelly were the sole shareholders in Crown C Supply, a small but successful building supply corporation in St. Louis, Missouri. Michael owned 77.18% of Crown's outstanding shares (385.9 out of 500 shares), and Thomas owned the remaining 22.82% (114.1 shares). The brothers entered into an agreement with Crown to ensure a smooth transition of ownership and keep Crown in the family in the event one of the brothers died. The agreement provided that if either Michael or Thomas died, the surviving brother would have the option to purchase the deceased brother's shares. And, if the surviving brother declined to do so, then Crown itself would be contractually required to redeem the shares. With an exception not relevant here, the agreement specified that the redemption price for each share would be based upon an outside appraisal of Crown's fair market value. App. 12-14. To ensure that Crown would have enough money to redeem the shares if required, Crown obtained \$3.5 million in life insurance on each brother.²¹⁹

²¹⁷ *Connelly v. United States*, US Supreme Court, Docket 23-146, June 6, 2024

²¹⁸ *Connelly v. United States*, US Supreme Court, Docket 23-146, June 6, 2024

²¹⁹ *Connelly v. United States*, US Supreme Court, Docket 23-146, June 6, 2024

But when Micheal died, Thomas and the heir, Michael's son, did not exactly follow this agreement:

When Michael died in 2013, Thomas opted not to purchase Michael's shares. As a result, Crown was obligated under the agreement to redeem Michael's shares. Rather than secure an outside appraisal of the company's fair market value (as the agreement contemplated), Michael's son and Thomas agreed in an "amicable and expeditious manner" that the value of Michael's shares was \$3 million. *Id.*, at 25-26. Crown then used \$3 million of the life-insurance proceeds to redeem Michael's shares, leaving Thomas as Crown's sole shareholder.²²⁰

Thomas was also the executor of Michael's estate, so he had prepared and filed an estate tax return as described below:

As the executor of Michael's estate, Thomas then filed a federal tax return for the estate. The return reported the value of Michael's shares as \$3 million, in accordance with the agreement between Michael's son and Thomas. The Internal Revenue Service (IRS) audited the return. During the audit, Thomas obtained a valuation from an accounting firm. The firm's analyst took as given the holding in *Estate of Blount v. Commissioner*, 428 F. 3d 1338 (CA11 2005), which concluded that insurance proceeds should be "deduct[ed] . . . from the value" of a corporation when they are "offset by an obligation to pay those proceeds to the estate in a stock buyout." *Id.*, at 1345. The analyst thus excluded the \$3 million in insurance proceeds used to redeem Michael's shares, and determined that Crown's fair market value at Michael's death was \$3.86 million. Because Michael held a 77.18% ownership interest, the analyst calculated the value of Michael's shares as approximately \$3 million (\$3.86 million x 0.7718).²²¹

The Eleventh Circuit had, in the *Estate of Blount* cited above, approved considering the obligation to redeem the shares as a liability of the corporation, which was appropriate to consider as largely offsetting the life insurance proceeds the corporation received. But the IRS did not agree with the Eleventh Circuit holding, nor the estate's use of that holding to reduce the value of the shares redeemed:

The IRS took a different view, insisting that Crown's redemption obligation did not offset the life-insurance proceeds. The IRS counted the \$3 million in life-insurance proceeds excluded by the analyst and assessed Crown's total value as \$6.86 million (\$3.86 million + \$3 million). And, the IRS thus calculated the value of Michael's shares as \$5.3 million (\$6.86 million x 0.7718). Based on this higher valuation, the IRS determined that the estate owed an additional \$889,914 in taxes.²²²

The estate paid the tax and then sued for a refund. However, the lower court disagreed with the Eleventh Circuit's analysis and ruled that the estate was not entitled to a refund.

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²²¹ *Connelly v. United States*, US Supreme Court, Docket 23-146, June 6, 2024

²²² *Connelly v. United States*, US Supreme Court, Docket 23-146, June 6, 2024

The estate paid the deficiency and Thomas, acting as executor, sued the United States for a refund. As relevant, Thomas argued that the \$3 million in life-insurance proceeds used to redeem Michael’s shares should not be counted when calculating the value of those shares. The District Court granted summary judgment to the Government, concluding that Michael’s estate was not entitled to a refund. *Connelly v. Department of Treasury, IRS*, 2021 WL 4281288, *17 (ED Mo., Sept. 21, 2021). The court held that the \$3 million in life-insurance proceeds must be counted to accurately value Michael’s shares. It explained that, under customary valuation principles, Crown’s obligation to redeem Michael’s shares was not a liability that reduced the corporation’s fair market value. *Id.*, at *14. The court therefore held that Crown’s redemption obligation did not offset the life-insurance proceeds. *Id.*, at *15-*17. The Court of Appeals affirmed on the same basis. *Connelly v. Department of Treasury, IRS*, 70 F. 4th 412 (CA8 2023).²²³

As there was now a clear split of opinion between the Eleventh Circuit’s holding in *Blount* and the Eighth Circuit’s holding in *Connelly*, the Supreme Court decided to hear the estate’s appeal of the *Connelly* holding.

The opinion notes that both parties agree that the life insurance proceeds increased the corporation’s value, but the question was whether a partially offsetting liability was also in place:

The dispute in this case is narrow. All agree that, when calculating the federal estate tax, the value of a decedent’s shares in a closely held corporation must reflect the corporation’s fair market value. And, all agree that life-insurance proceeds payable to a corporation are an asset that increases the corporation’s fair market value. The only question is whether Crown’s contractual obligation to redeem Michael’s shares at fair market value offsets the value of life-insurance proceeds committed to funding that redemption.²²⁴

The opinion goes on to outline both parties’ position on the issue of whether or not the obligation to redeem the shares should be considered in valuing the shares:

Thomas argues that a contractual obligation to redeem shares is a liability that offsets the value of life-insurance proceeds used to fulfill that obligation. Brief for Petitioner 17. He accordingly contends that anyone purchasing “a subset of the corporation’s shares would treat the two as canceling each other out.” *Ibid.* By contrast, the Government argues that Crown’s obligation to pay for Michael’s shares did not reduce the value of those shares. It contends that “no real-world buyer or seller would have viewed the redemption obligation as an offsetting liability.” Brief for United States 15.²²⁵

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²²⁴ *Connelly v. United States*, US Supreme Court, Docket 23-146, June 6, 2024

²²⁵ *Connelly v. United States*, US Supreme Court, Docket 23-146, June 6, 2024

The Court quickly states that, in its view, the answer is that redemption is irrelevant in determining the fair value of the interest.

An obligation to redeem shares at fair market value does not offset the value of life-insurance proceeds set aside for the redemption because a share redemption at fair market value does not affect any shareholder's economic interest.²²⁶

Justice Thomas offers an example to explain this holding:

A simple example proves the point. Consider a corporation with one asset — \$10 million in cash — and two shareholders, A and B, who own 80 and 20 shares respectively. Each individual share is worth \$100,000 (\$10 million ÷ 100 shares). So, A's shares are worth \$8 million (80 shares x \$100,000) and B's shares are worth \$2 million (20 shares x \$100,000). To redeem B's shares at fair market value, the corporation would thus have to pay B \$2 million. After the redemption, A would be the sole shareholder in a corporation worth \$8 million and with 80 outstanding shares. A's shares would still be worth \$100,000 each (\$8 million ÷ 80 shares). Economically, the redemption would have no impact on either shareholder. The value of the shareholders' interests after the redemption — A's 80 shares and B's \$2 million in cash — would be equal to the value of their respective interests in the corporation before the redemption. Thus, a corporation's contractual obligation to redeem shares at fair market value does not reduce the value of those shares in and of itself.²²⁷

Thus, Justice Thomas goes on to note that the theoretically willing buyer would not consider the redemption when buying the decedent's shares.

Because a fair-market-value redemption has no effect on any shareholder's economic interest, no willing buyer purchasing Michael's shares would have treated Crown's obligation to redeem Michael's shares at fair market value as a factor that reduced the value of those shares. At the time of Michael's death, Crown was worth \$6.86 million — \$3 million in life-insurance proceeds earmarked for the redemption plus \$3.86 million in other assets and income-generating potential. Anyone purchasing Michael's shares would acquire a 77.18% stake in a company worth \$6.86 million, along with Crown's obligation to redeem those shares at fair market value. A buyer would therefore pay up to \$5.3 million for Michael's shares (\$6.86 million x 0.7718) — i.e., the value the buyer could expect to receive in exchange for Michael's shares when Crown redeemed them at fair market value. We thus conclude that Crown's promise to redeem Michael's shares at fair market value did not reduce the value of those shares.[\[13\]](#)

The Court then outlines the estate's argument against this position, which relies upon the holding in *Blount*:

Thomas resists this straightforward conclusion. He suggests that Crown's redemption obligation "would make it impossible" for a hypothetical buyer seeking to purchase 77.18% of Crown "to capture the full value of the insurance proceeds."

²²⁶ *Connelly v. United States*, US Supreme Court, Docket 23-146, June 6, 2024

²²⁷ *Connelly v. United States*, US Supreme Court, Docket 23-146, June 6, 2024

Brief for Petitioner 26. That is so, according to Thomas, because the insurance proceeds would leave the company as soon as they arrived to complete the redemption. He argues that the “buyer would thus not consider proceeds that would be used for redemption as net assets.” *Ibid.* In other words, Thomas views the relevant inquiry as what a buyer would pay for shares that make up the same percentage of the less-valuable corporation that exists after the redemption. See *Estate of Blount v. Commissioner*, 87 TCM 1303 (2004), ¶2004-116 RIA Memo TC, *aff’d in part and rev’d in part*, 428 F. 3d 1338 (CA11 2005); see also A. Chodorow, *Valuing Corporations for Estate Tax Purposes*, 3 *Hastings Bus. L. J.* 1, 25 (2006) (“Any valuation that takes the redemption obligation into account effectively values the corporation on a ‘post-redemption’ basis, i.e., after the decedent’s shares have been redeemed”).²²⁸

But the Justices’ opinion holds that the proper time to value the corporation is before the redemption takes place:

But, for calculating the estate tax, the whole point is to assess how much Michael’s shares were worth at the time that he died — before Crown spent \$3 million on the redemption payment. See 26 U.S.C. §2033 (defining the gross estate to “include the value of all property to the extent of the interest therein of the decedent at the time of his death”); 26 CFR §20.2031-1(b) (the “value of every item of property includible in a decedent’s gross estate . . . is its fair market value at the time of the decedent’s death” (emphasis added)). A hypothetical buyer would thus treat the life-insurance proceeds that would be used to redeem Michael’s shares as a net asset.²²⁹

The opinion goes on to consider an issue that took up quite a bit of time in the oral arguments before the Court. The estates’ position ignores the fact that while Michael’s son received cash equal to what the estate claimed was the value of his father’s shares, at the same time Thomas managed to go from holding a minority interest in the company to now holding 100% of the shares of a company still worth what the estate claimed it was worth at his brother’s passing.

Moreover, Thomas’s argument that the redemption obligation was a liability cannot be reconciled with the basic mechanics of a stock redemption. As the District Court explained, when a shareholder redeems his shares he “is essentially ‘cashing out’ his shares of ownership in the company and its assets.” 2021 WL 4281288, *16. That transaction necessarily reduces a corporation’s total value. And, because there are fewer outstanding shares after the redemption, the remaining shareholders are left with a larger proportional ownership interest in the less-valuable corporation. Thomas’s understanding, however, would turn this ordinary process upside down. In Thomas’s view, Crown’s redemption of Michael’s shares left Thomas with a larger ownership stake in a company with the same value as before the redemption. Thomas argues that Crown was worth only \$3.86 million before the redemption, and thus that Michael’s shares were worth approximately \$3 million (\$3.86 million

²²⁸ *Connelly v. United States*, US Supreme Court, Docket 23-146, June 6, 2024

²²⁹ *Connelly v. United States*, US Supreme Court, Docket 23-146, June 6, 2024

x 0.7718). But, he also argues that Crown was worth \$3.86 million after Michael's shares were redeemed. See Reply Brief 6. That cannot be right: A corporation that pays out \$3 million to redeem shares should be worth less than before the redemption. See Cox & Hazen §21.2. Thomas's argument thus cannot be reconciled with an elementary understanding of a stock redemption.²³⁰

Finally, the Court did not consider the estate's argument that this decision would make estate planning for closely held corporations much more difficult, noting that the entire issue could have been avoided with a cross-purchase structure, although the Court concedes that a cross-purchase agreement adds certain non-estate tax issues to the transaction.

Finally, Thomas asserts that affirming the decision below will make succession planning more difficult for closely held corporations. He reasons that if life-insurance proceeds earmarked for a share redemption are a net asset for estate-tax purposes, then "Crown would have needed an insurance policy worth far more than \$3 million in order to redeem Michael's shares at fair market value." Brief for Petitioner 33. True enough, but that is simply a consequence of how the Connelly brothers chose to structure their agreement. There were other options. For example, the brothers could have used a cross-purchase agreement — an arrangement in which shareholders agree to purchase each other's shares at death and purchase life-insurance policies on each other to fund the agreement. See S. Pratt, *Valuing a Business* 821. (6th ed. 2022). A cross-purchase agreement would have allowed Thomas to purchase Michael's shares and keep Crown in the family, while avoiding the risk that the insurance proceeds would increase the value of Michael's shares. The proceeds would have gone directly to Thomas — not to Crown. But, every arrangement has its own drawbacks. A cross-purchase agreement would have required each brother to pay the premiums for the insurance policy on the other brother, creating a risk that one of them would be unable to do so. And, it would have had its own tax consequences. By opting to have Crown purchase the life-insurance policies and pay the premiums, the Connelly brothers guaranteed that the policies would remain in force and that the insurance proceeds would be available to fund the redemption. As we have explained, however, this arrangement also meant that Crown would receive the proceeds and thereby increase the value of Michael's shares. Thomas' concerns about the implications of how he and Michael structured their agreement are therefore misplaced.²³¹

²³⁰ *Connelly v. United States*, US Supreme Court, Docket 23-146, June 6, 2024

²³¹ *Connelly v. United States*, US Supreme Court, Docket 23-146, June 6, 2024

IRS REVERSES POSITION PREVIOUSLY TAKEN IN 2016 LETTER RULING REGARDING GIFT TAX TREATMENT OF ADDING A TAX REIMBURSEMENT CLAUSE TO AN IDGT

In [Chief Counsel Advice 202352018](#), dated December 29, 2023, the IRS issued guidance explicitly stating that it no longer upholds the stance outlined in [Private Letter Ruling \(PLR\) 201647001](#). The focal issue is the determination of gift (and possible subsequent estate) tax consequences arising from the modification of an intentionally defective grantor trust. This modification entails adding a provision that permits the trust to reimburse the grantor for taxes paid on the trust's income.

Intentionally Defective Grantor Trust

An Intentionally Defective Grantor Trust (IDGT) is a strategic tool frequently employed in estate planning. Its purpose is to transfer assets out of the grantor's estate, while the grantor remains responsible for paying income tax on the trust's earnings. Notably, these tax payments are not considered additional gifts by the grantor. This approach leverages the income tax grantor trust rules (outlined in IRC §§671-679), treating the assets as though they are owned by the grantor for income tax purposes. This is achieved through various powers retained by the grantor, yet structured in a way that does not impede the completion of the gift for estate tax purposes.

However, there are instances where grantors may reconsider this arrangement, particularly when faced with income tax obligations exceeding their comfort level. In response to these concerns, some advisers have recommended modifying the trust. Such modifications could include granting the independent trustee discretion to distribute assets to the grantor for income tax payments. This suggestion was previously underpinned by the IRS's conclusions in Private Letter Ruling 201647001, which indicated that these modifications would not trigger gift or income tax consequences.

The Issue Addressed in the Chief Counsel Advice

The specific issue addressed in Chief Counsel Advice (CCA) 202352018 is as follows:

What are the gift tax consequences to the beneficiaries when the trustee of an irrevocable trust, with respect to which the grantor is treated as the owner under subpart E, part I, subchapter J, chapter 1 (subpart E) of the Internal Revenue Code (Code), modifies the trust, with the beneficiaries' consent, to add a tax reimbursement clause that provides the trustee the discretionary power to make distributions of income or principal from the trust in an amount sufficient to reimburse the grantor for the income tax attributable to the inclusion of the trust's income in the grantor's taxable income? [CCA 202352018]

The illustrative facts forming the basis of the ruling are as follows:

In Year 1, A establishes and funds Trust, an irrevocable inter vivos trust, for the benefit of A's Child and Child's descendants. Trustee is the current trustee of Trust

and satisfies the governing instrument requirement that a trustee of Trust must be a person not related or subordinate to A within the meaning of §672(c) of the Code. Under the governing instrument of Trust, a trustee of Trust may distribute income and principal to or for the benefit of Child in the trustee's absolute discretion. Upon Child's death, Trust's remainder is to be distributed to Child's issue, per stirpes.

Under the governing instrument of Trust, A retains a power that causes A to be the deemed owner of Trust under §671 of the Code, and, accordingly, all items of income, deductions, and credits attributable to Trust are included in A's taxable income.

Neither State law nor the governing instrument of Trust requires or provides authority to a trustee of Trust to distribute to A amounts sufficient to satisfy A's income tax liability attributable to the inclusion of Trust's income in A's taxable income.

In Year 2, when Child has no living grandchildren or more remote descendants, Trustee petitions State Court to modify the terms of Trust. Pursuant to State Statute, Child and Child's issue consent to the modification. Later that year, State Court grants the petition and issues an Order modifying Trust to provide a trustee of Trust the discretionary power to reimburse A for any income taxes A pays as a result of the inclusion of Trust's income in A's taxable income. [CCA 202352018]

Analysis of the Case

[Revenue Ruling 2004-64](#) offers guidance for scenarios where a reimbursement clause is included from the inception of the trust. The Chief Counsel Advice (CCA) summarizes this ruling as follows:

In Rev. Rul. 2004-64, 2004-2 C.B. 7, a grantor created an irrevocable inter vivos trust for the benefit of the grantor's descendants and retained sufficient powers with respect to the trust so that the grantor is treated as the owner of the trust under subpart E of the Code. In relevant part, the ruling considers two situations in which the trustee reimburses the grantor for taxes paid by the grantor that are attributable to the inclusion of all or part of the trust's income in the grantor's income. In Situation 2 of Rev. Rul. 2004-64, the distribution reimbursing the grantor is mandated under the terms of the governing instrument. In Situation 3 of Rev. Rul. 2004-64, the governing instrument provides the trustee with the discretionary authority to make a reimbursing distribution. In both of these situations, when the trustee of the trust reimburses the grantor for the income tax paid by the grantor, the ruling concludes that the payment does not constitute a gift by the trust beneficiaries because the distribution was either mandated by the terms of the governing instrument or made pursuant to the exercise of the trustee's discretionary authority granted under the terms of the governing instrument. [CCA 202352018]

In Private Letter Ruling (PLR) 201647001, the IRS previously determined that adding a reimbursement clause to an intentionally defective grantor trust (IDGT) after its initial formation did

not result in a transfer tax issue. However, the IRS has since revised its stance, no longer considering this interpretation as the correct application of law to the given facts. The IRS's current analysis is outlined as follows:

Under the governing instrument of Trust, Child and Child's issue each have an interest in the trust property. As a result of the Year 2 modification of Trust, A acquires a beneficial interest in the trust property in that A becomes entitled to discretionary distributions of income or principal from Trust in an amount sufficient to reimburse A for any taxes A pays as a result of inclusion of Trust's income in A's gross taxable income. In substance, the modification constitutes a transfer by Child and Child's issue for the benefit of A. This is distinguishable from the situations in Rev. Rul. 2004-64 where the original governing instrument provided for a mandatory or discretionary right to reimbursement for the grantor's payment of the income tax. Thus, as a result of the Year 2 modification, Child and Child's issue each have made a gift of a portion of their respective interest in income and/or principal.¹ See §25.2511-1(e) and §25.2511-2(b). See also *Robinette v. Helvering*, 318 U.S. 184 (1943). The result would be the same if the modification was pursuant to a state statute that provides beneficiaries with a right to notice and a right to object to the modification and a beneficiary fails to exercise their right to object.

The gift from Child and Child's issue of a portion of their interests in trust should be valued in accordance with the general rule for valuing interests in property for gift tax purposes in accordance with the regulations under §2512 and any other relevant valuation principles under subtitle B of the Code. [CCA 202352018]

Within this Chief Counsel Advice, there are two footnotes of significance. The first footnote acknowledges the Office of the Chief Counsel's shift in position, specifically refuting the analysis previously presented in Private Letter Ruling (PLR) 201647001.

PLR 201647001 concludes that the modification of a trust to add a discretionary trustee power to reimburse the grantor for the income tax paid attributable to the trust income is administrative in nature and does not result in a change of beneficial interests in the trust. These conclusions no longer reflect the position of this office. [CCA 202352018, Note 1]

The second footnote concedes that significant practical challenges arise in valuing the gift, as concluded by the Chief Counsel Advice (CCA).

Although the determination of the values of the gifts requires complex calculations, Child and Child's issue cannot escape gift tax on the basis that the value of the gift is difficult to calculate. See *Smith v. Shaughnessy*, 318 U.S. 176, 180 (1943) ("The language of the gift tax statute, 'property . . . real or personal, tangible or intangible,' is broad enough to include property, however conceptual or contingent.") [CCA 202352018, Note 2]

Unit 6

Tax Practice Issues

LEARNING OBJECTIVES

- ❑ Advise clients on the potential impact of the Supreme Court's two end-of-term cases on Court review of regulations and how they may impact various Treasury Regulations
- ❑ Apply these rulings in your analysis regarding whether tax positions contrary to regulations or other IRS guidance have a reasonable basis for purposes of signing a return

SUPREME COURT OVERTURNS CHEVRON DEFERENCE ON AGENCY REGULATIONS

The US Supreme Court overturned its decision in *Chevron U. S. A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U. S. 837, eliminating what has been referred to as *Chevron* deference in cases reviewing the validity of a regulation.²³²

This case does not involve a tax issue but rather deals solely with whether a court is bound by the Supreme Court's *Chevron U. S. A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U. S. 837 decision (referred to as *Chevron* deference). The courts had been chipping away at *Chevron* in recent years, creating a number of special cases that worked around *Chevron* but had not explicitly overturned the decision.

In 2010 the Supreme Court had issued the opinion in *Mayo Foundation for Medical Ed. and Research v. United States*, 562 U.S. 44 (2010) that was related to payroll tax matters. The Court's opinion did cite *Chevron* but also found a specific delegation of authority made by Congress to the IRS at IRC §7805(a) (Justice Roberts wrote both opinions). This becomes just one of many prior opinions that may be subject to being revisited following the decision in *Loper Bright*.

So what was *Chevron* deference? *Chevron* had courts apply a two-pronged test for a court to determine a tax regulation's validity

²³² *Loper Bright Enterprises v. Raimondo*, USSC Case Nos. 22-451 and 22-1219, June 27, 2024, https://www.supremecourt.gov/opinions/23pdf/22-451_7m58.pdf

- First, did the IRC itself unambiguously address and provide an unambiguous answer on the matter in question – if so, that is the answer & a contrary regulation is invalid (*Connecticut National Bank v. Germain*, 503 US 249 (1992))
- If there is ambiguity, is Treasury’s regulation a reasonable interpretation of the law? If so, the regulation is valid even if the Court believes there exists a better reasonable interpretation using standard statutory interpretative techniques

The first test remains intact to mount a regulatory challenge, but those challenging a regulation are now allowed to argue there are interpretations that are superior to that promulgated by Treasury based on standard canons of statutory interpretation.

The issue under dispute involved a case on fishing boat regulations issued by the federal government where the court had decided the case based solely on reliance on *Chevron* deference

- Found the statute was ambiguous on the issue in question (charges to certain boats to pay for observers) and
- The court concluded applying such charges to the boat owners was a reasonable interpretation of the statute (thus valid under *Chevron*).

However, the trial and the appellate court did not consider if that was the “best” interpretation of the law under the rules of statutory interpretation.

The Supreme Court’s majority opinion found that *Chevron* deference was contrary to the Administrative Procedures Act, a law enacted by Congress that outlines the process agencies are to issue regulations.

Rather, the opinion finds that the courts are in charge of the proper interpretation of legal issues and do not have to defer to the agencies when considering strictly matters of legal interpretation. An agency’s position is deserving of respect assuming there is a reasonable amount of evidence behind it, especially in areas that involve the agency’s special expertise (judges aren’t assumed to be subject matter experts in, let’s say, nuclear physics).

However, the Court is not required to simply accept that position, even if it is a reasonable interpretation of the law, to the extent the rules of statutory interpretation arrive at another superior interpretation of the law.

The respect of the agency’s position can extend to legal issues that are impacted by the agency’s special expertise, but the court notes not all legal issues benefit from the agency’s subject matter expertise. Agencies should receive more respect for their position on factual issues related to their specific expertise, while judges, trained in legal matters, are the best parties to deal with legal matters.

The opinion argued that *Chevron* did not provide uniformity or predictability for the application of the law, one of the key arguments of the government and the dissent to keep the doctrine intact. *Stare decisis* is not adequate to save *Chevron* in the majority’s view, as it was, in the view of the

majority, poorly decided and not useful as a practical method to handle these matters. The dissenters, predictably, disagreed on those two points.

The major did not agree the mere fact that a precedential case that was issued before this opinion was decided based on *Chevron* deference does not mean it is automatically invalid. However, to this reader, it seems like such cases would be subject to review using the standards outlined in this case.

So what is the likely impact in tax matters CPAs deal with? While it will be easier to challenge an IRS regulation in court, that only helps if your client truly can afford to take the IRS to court. We can expect the IRS to seek to defend the validity of their existing regulations even under these rules, and a successful challenge could very well require going at least to the applicable Circuit Court of Appeals regardless of how a trial court might rule.

Specifically, don't expect IRS agents to accept such a challenge to final regulation absent existing clear controlling precedent (you need someone else to get it to trial) simply by citing *Loper Bright*. Most likely agents are not likely ever to concede a regulation is invalid, and that is very likely true at Appeal as well in most cases.

However, if a client has the resources and it would make economic sense to take the matter to trial, you may find the IRS decide to settle before the matter could get to court if Counsel believes your case may have merit (want to avoid a problematic decision) - see *Jarrett et al v. United States* from the US District Court in Tennessee where the IRS avoided going to trial on whether amounts received for staking cryptocurrency are taxable income.

What about the impact on future guidance on tax matters? As *Chevron* only *officially* affects regulations, you may see the IRS lean harder on unofficial guidance (website, announcements, etc.). However, we've already seen some courts look to prospectively apply *Loper Bright* to certain IRS positions found in sub-regulatory guidance, and looking to see even if the IRS formalized the guidance in a final regulation if it would survive analysis under standard rules of statutory construction.

Since the "correct" answer seems unclear to judges at times (see the 6-2(or maybe 3...) decision in this case), you can expect to see more Circuit splits (where a taxpayer lives may have an impact on the law unless the taxpayer can litigate at Court of Claims or get SCOTUS to hear the case)

We will also need to see how much difference the "respect" test makes vs. *Chevron* deference. Respect clearly gives the position less impact than the deference standard, but how much less we will only see after a number of cases go through the courts.

STATUTE OF LIMITATIONS TO CHALLENGES TO REGULATIONS UNDER APA STATUTE BEGINS WHEN A PARTICULAR PLAINTIFF FIRST SUFFERED INJURY

The Supreme Court at the end of its session in the summer of 2024 dealt with a second case on review of regulations beyond the *Loper Bright*. In the case of *Corner Post Inc. v. Federal Reserve*, USSC

Case No. 22-1008, July 1, 2024²³³ the Supreme Court looked at when the statute of limitations begins to run on challenges to the process an agency used to set regulations under the Administrative Procedures Act.

The Administrative Procedures Act outlines the procedures an agency must follow when issuing rules and regulations related to statutes enacted by Congress. Under the APA a challenge can be brought up to 6 years after “the right of action first accrues.” The key question is how we determine when the “right of action first accrues” under the statute. Is there a single date that covers that regulation (so effectively six years following final publication) or does each plaintiff have his/her own six-year statute (six years after the regulation in question first damaged that individual, giving rise to their personal right of action)?

Six Circuits had held that for a facial challenge to a regulation, a right of action accrues, and the limitation period begins, upon publication of the regulation, even that regulation had not yet had any impact on the particular litigant at that date. However, the Sixth Circuit held that the limitation period begins only when the party is injured by the final action, creating a split among the Circuits, the sort of thing that often attracts the attention of the Supreme Court.

The Supreme Court opinion notes that under the law, an individual plaintiff cannot sue over the issue of the validity of this regulation’s adoption until they have incurred an injury. For example, a party likely could not file a lawsuit challenging regulations that impact certain aspects of operating a paint manufacturing facility unless the party actually operated a paint manufacturing facility.

The Government had argued that a claim “accrues” under the Act when the final regulation is published, so that would be six years from that date the APA claim would be outside of statute for everyone even if they could show the regulation had no impact on them until a date within six years of the date they filed the suit.

The Supreme Court specifically found a right of action accrues when the plaintiff has a complete and present cause of action – that is, the right to bring suit. That only occurs under the Act when the party suffers an actual injury, not when the causes that may eventually lead to an injury took place

The injury test for a cause of action is the standard rule and there’s no indication Congress intended a different interpretation –Congress has clearly written such earlier start dates into other laws but did not do so in this one.

As well, it doesn’t matter that some other person had the right to sue on the date the final rule was published (in this particular case existing businesses were being charged interchange fees for accepting debit cards at the time the rule was finalized, even though Corner Post, Inc. itself did not yet exist).

The majority opinion also rejected claims that the statute should start when the rule is finalized to give certainty and not disadvantage those who have relied upon the regulation for years – the majority finds that “administrative convenience” does not override the clear wording of the statute and then there are other means by which a long-standing regulation can be challenged.

²³³ *Corner Post Inc. v. Federal Reserve*, USSC Case No. 22-1008, July 1, 2024, https://www.supremecourt.gov/opinions/23pdf/22-1008_1b82.pdf

So what is the impact on tax matters?

- This holding allows impacted taxpayers to challenge the regulation via failure to properly follow the APA along with other existing options to challenge the regulation.
- Even if the taxpayer cannot show his/her preferred view of how the statute should be interpreted is the best interpretation, showing the agency failed to follow the APA should force the agency to restart the process of issuing the regulation in question.
- The holding could be useful combined with the repeal of the *Chevron* rule to bring certain regulations back before the courts or back before the agency itself.

With this holding along with that in *Loper Bright*, it's likely we'll see more challenges to regulations. Even if your client cannot afford to bring a challenge for their own return, they may find options to file protective claims if there is a taxpayer with more dollars involved currently pursuing a suit on the matter.

TAXPAYER ALLOWED TO RELY ON NOTICE OF DEFICIENCY STATEMENT OF LAST DAY TO FILE A TAX COURT PETITION EVEN WHEN THE DATE WAS MORE THAN A YEAR AFTER THE NOTICE WAS ISSUED

What are the implications when the Internal Revenue Service (IRS) erroneously states the filing deadline for a petition in the Tax Court to contest a notice of deficiency? In a situation where this error significantly favored the taxpayer, the Tax Court determined that the taxpayer was entitled to rely on the date specified in the initial notice, despite the IRS issuing a corrected notice the following day. ([*Dodson v. Commissioner*](#), 162 TC No. 1)

The Notices the IRS Mailed

The IRS issued the original notice of deficiency to the taxpayers on October 7, 2021, concerning their 2017 tax return. The Tax Court details this notice as follows:

On October 7, 2021, respondent mailed the first notice to petitioners for their 2017 taxable year. Tracking information for two copies of the first notice reflects the delivery of both copies in Alamogordo, New Mexico, on October 12, 2021, by the U.S. Postal Service (USPS). The first notice bears a stamped date specifying December 5, 2022, as the last day to file a petition. Petitioners filed their Petition on March 3, 2022. The Petition attached a copy of the first notice and no other notice of deficiency.

However, upon recognizing the error, the IRS, a day later, dispatched a corrected notice of deficiency to the taxpayers. The Tax Court opinion further elaborates on the circumstances pertaining to this subsequent notice.

Respondent has also produced the second notice, which he mailed to petitioners on October 8, 2021, and which purports to be a corrected version of the first notice. The second notice bears a stamped date specifying January 6, 2022, as the last day to file a petition. The second notice is accompanied by a cover sheet stating: “PREVIOUS NOTICE SENT WITH INCORRECT DATE. CORRECTED NOTICE WITH CORRECT DATES.” The second notice does not differ from the first notice in any other material respect.

The taxpayers contend that they did not receive this subsequent notice. The Tax Court observes that, in contrast to the original notice, the tracking information provided by the IRS fails to indicate delivery of the document to the taxpayers.

Petitioners state that they did not receive the second notice. Petitioners have produced tracking information for two copies of the second notice reflecting the departure of the notice copies from USPS’s El Paso, Texas, distribution center on October 13, 2021, without any indication that USPS ever delivered them to petitioners.

The opinion states that the taxpayers submitted their petition considerably before the due date indicated on the original notice of deficiency. However, this submission occurred significantly beyond the standard 90-day period following the issuance of either notice.

Petitioners filed their Petition in this case on March 3, 2022, which is 147 days after respondent mailed the first notice and 146 days after respondent mailed the second notice.

So the question facing the Court is whether the taxpayers had timely filed their petition in these circumstances.

The Law

The Tax Court begins by noting that they are a court of limited jurisdiction, and so must make their own determination of whether they have jurisdiction in this case:

Our jurisdiction in a case for the redetermination of a deficiency depends on the issuance of a valid notice of deficiency to the taxpayer and the timely filing of a petition by the taxpayer. See *Monge v. Commissioner*, 93 T.C. 22, 27 (1989); *Normac, Inc. v. Commissioner*, 90 T.C. 142, 147 (1988); see also *Sanders v. Commissioner*, No. 15143-22, 161 T.C. (Nov. 2, 2023); *Hallmark Rsch. Collective v. Commissioner*, 159 T.C. 126 (2022). Generally, the petition must be filed within 90 days after the notice is mailed (not counting Saturday, Sunday, or a legal holiday in the District of Columbia as the last day). See *Sanders v. Commissioner*, No. 25868-22, 160 T.C., slip op. at 5 (June 20, 2023). This filing deadline is jurisdictional, and equitable tolling does not apply. See *Hallmark Rsch. Collective*, 159 T.C. at 166–67.

The concluding sentence reiterates that the Tax Court has not adopted the Third Circuit's stance on equitable tolling being applicable to this deadline, as established in *Culp v. Commissioner of Internal Revenue*, No. 22-1789 (3d Cir. July 19, 2023). The opinion highlights that any appeals in this case would fall under the jurisdiction of the Tenth Circuit Court of Appeals. Consequently, the Tax Court will not apply the precedent set in the *Culp* decision, given that the Tenth Circuit has yet to endorse the Third Circuit's position.

The Tax Court turns to the last sentence of IRC §6213(a) which reads "Any petition filed with the Tax Court on or before the last date specified for filing such petition by the Secretary in the notice of deficiency shall be treated as timely filed."

The Court observes that the date indicated on the initial notice sent to the taxpayer precedes the date on which the taxpayer filed their petition.

The Petition in this case attached the first notice. The first notice unambiguously determines a deficiency against petitioners and is therefore valid. See *Dees v. Commissioner*, 148 T.C. 1, 6 (2017) ("[I]f the notice is sufficient to inform a reasonable taxpayer that the Commissioner has determined a deficiency, our inquiry [as to the notice's validity] ends there; the notice is valid."). Petitioners filed their Petition before December 5, 2022, the last day specified in the first notice for filing a petition in this Court. This is sufficient to comply with the last sentence of section 6213(a), which in the words of the Tenth Circuit means that "if a notice indicates a petition date that is more than 90 days after the date of mailing, that date controls." *Smith v. Commissioner*, 275 F.3d at 916.

However, consideration must also be given to the second notice, which was dispatched a day later. In this context, the Tax Court references Internal Revenue Code (IRC) §6212(d), Revenue Procedure 98-54, and Form 8626, stating:

The record discloses no consent by petitioners to a rescission of the first notice in any manner, let alone in a form complying with Rev. Proc. 98-54. Absent a rescission with petitioners' consent, the first notice continued to "be treated as a notice of deficiency for purposes of . . . section 6213(a)," see §6212(d), including for purposes of the last sentence of section 6213(a). Accordingly, respondent's issuance of the second notice without petitioners' consent did not have the effect of rescinding the first notice, either in whole or in part. See *Hanashiro v. Commissioner*, T.C. Memo. 1999-78, slip op. at 10 ("The rescission of a notice of deficiency requires mutual consent by the Commissioner and the taxpayer, and such mutual consent must be objectively apparent."); *Slattery v. Commissioner*, T.C. Memo. 1995-274, 69 T.C.M. (CCH) 2953, 2956 ("Clearly, the statute requires mutual consent by the Secretary and the taxpayer to effect a rescission of a notice of deficiency. We know of no authority deeming a notice of deficiency rescinded in absence of a formal rescission." (Footnote omitted.)). As soon as respondent mailed the first notice to petitioners on October 7, 2021, respondent could no longer unilaterally rescind the first notice.

The restriction on nonconsensual rescissions found in section 6212(d), unlike the restriction on further deficiency letters found in section 6212(c), is not limited to situations where the Secretary determines an additional deficiency of income tax (or certain other taxes) for the same taxable year. Our straightforward conclusion, derived from the plain text of sections 6213(a) and 6212(d), is that we are required to treat the Petition as timely filed. Accordingly, we will do so. This is not a case where a taxpayer petitions us for redetermination of a deficiency in a notice that purports to correct a prior notice of deficiency, a circumstance for which we express no view on the application of the last sentence of section 6213(a).”

The Tax Court dismissed several arguments presented by the IRS, referencing prior instances where the deadline for filing a petition was not included in notices issued by the IRS. Additionally, the Court rejected the notion that the discrepancy constituted an ‘obvious error’ that the taxpayer should have identified:

Respondent repeatedly characterizes the petition filing date on the first notice as an “obvious mistake,” but this characterization is misleading. As recognized by the Tenth Circuit, a taxpayer may timely file a deficiency petition by meeting the requirements of the first sentence of section 6213(a) or, alternatively, the last sentence of section 6213(a). See *Smith v. Commissioner*, 275 F.3d at 916 (“[I]f a notice indicates a petition date that is more than 90 days after the date of mailing, that date controls.”). Here, the petition filing date on the first notice had independent legal effect, and petitioners were permitted to rely on it regardless of whether they retained counsel and regardless of whether prejudice would result from applying another deadline. Respondent’s position in this case attempts to create uncertainty about the meaning of the last sentence of section 6213(a) where there is none.

USE OF WRONG FEDEX SERVICE MEANT TAXPAYER’S TAX COURT PETITION WAS NOT TIMELY FILED

In the case of [Nguyen v. Commissioner, TC Memo 2023-151](#), the taxpayer’s choice of an incorrect delivery service resulted in the filing of their Tax Court petition beyond the designated final filing date.

Timely Mailing, Timely Filing Rule Under IRC §7502

IRC §7502(a) establishes the principle of “timely mailing is timely filing” for federal tax documents, including petitions to the Tax Court. This section of the law states:

(a) General rule.

(1) **Date of delivery.** If any return, claim, statement, or other document required to be filed, or any payment required to be made, within a prescribed period or on or before a prescribed date under authority of any provision of the internal revenue

laws is, after such period or such date, delivered by United States mail to the agency, officer, or office with which such return, claim, statement, or other document is required to be filed, or to which such payment is required to be made, the date of the United States postmark stamped on the cover in which such return, claim, statement, or other document, or payment, is mailed shall be deemed to be the date of delivery or the date of payment, as the case may be.

IRC §7502(c) offers a method for obtaining proof of postmark through the use of registered mail. Additionally, it authorizes the IRS to accord similar status to certified mail, as outlined in the regulations issued by the agency.

(c) Registered and certain mailing; electronic filing.

(1) Registered mail. For purposes of this section, if any return, claim, statement, or other document, or payment, is sent by United States registered mail--

(A) such registration shall be prima facie evidence that the return, claim, statement, or other document was delivered to the agency, officer, or office to which addressed; and

(B) the date of registration shall be deemed the postmark date.

(2) Certified mail; electronic filing. The Secretary is authorized to provide by regulations the extent to which the provisions of paragraph (1) with respect to prima facie evidence of delivery and the postmark date shall apply to certified mail and electronic filing.

Subsequently, Congress broadened this provision by introducing IRC §7502(f), which extends similar treatment to designated private delivery services.

(f) Treatment of private delivery services.

(1) In general. Any reference in this section to the United States mail shall be treated as including a reference to any designated delivery service, and any reference in this section to a postmark by the United States Postal Service shall be treated as including a reference to any date recorded or marked as described in paragraph (2)(C) by any designated delivery service.

(2) Designated delivery service. For purposes of this subsection, the term “designated delivery service” means any delivery service provided by a trade or business if such service is designated by the Secretary for purposes of this section. The Secretary may designate a delivery service under the preceding sentence only if the Secretary determines that such service--

(A) is available to the general public,

(B) is at least as timely and reliable on a regular basis as the United States mail,

(C) records electronically to its data base, kept in the regular course of its business, or marks on the cover in which any item referred to in this section is to be delivered, the date on which such item was given to such trade or business for delivery, and

(D) meets such other criteria as the Secretary may prescribe.

(3) Equivalents of registered and certified mail. The Secretary may provide a rule similar to the rule of paragraph (1) with respect to any service provided by a designated delivery service which is substantially equivalent to United States registered or certified mail.

The IRS has issued Notice 2016-30, enumerating the private delivery services (PDSs) considered equivalent to registered and certified mail. The designated PDSs were:

■ DHL Express:

- DHL Express 9:00
- DHL Express 10:30
- DHL Express 12:00
- DHL Express Worldwide
- DHL Express Envelope
- DHL Import Express 10:30
- DHL Import Express 12:00
- DHL Import Express Worldwide

■ FedEx:

- FedEx First Overnight
- FedEx Priority Overnight
- FedEx Standard Overnight
- FedEx 2 Day
- FedEx International Next Flight Out
- FedEx International Priority
- FedEx International First

- FedEx International Economy
- UPS:
 - UPS Next Day Air Early AM
 - UPS Next Day Air
 - UPS Next Day Air Saver
 - UPS 2nd Day Air
 - UPS 2nd Day Air A.M.
 - UPS Worldwide Express Plus
 - UPS Worldwide Express

The services listed in Notice 2016-30 were the officially recognized private delivery services (PDSs) as of the date when the taxpayer filed their petition with the U.S. Tax Court.

Facts of the Taxpayer’s Case

The U.S. Tax Court received the taxpayer’s petition one day beyond the final date permitted for filing.

The Petition in this case was filed on January 12, 2023, one day after expiration of the 90-day filing period. In urging that we nonetheless have jurisdiction, petitioners rely on the “timely mailed, timely filed” rule in section 7502. It sets forth the general rule that, for any document “delivered by United States mail . . . the date of the United States postmark stamped on the cover . . . shall be deemed to be the date of delivery.” §7502(a)(1).

Petitioners did not send their Petition to the Court by U.S. mail, but rather used FedEx, a private delivery service. Section 7502(f), captioned “Treatment of Private Delivery Services,” provides that “[a]ny reference in this section to the United States mail shall be treated as including a reference to any designated delivery service.” Section 7502(f)(2) defines a “designated delivery service” to mean a private delivery service “if such service is designated by the Secretary for purposes of this section.”

The Court acknowledged the earlier-mentioned IRS publication listing designated PDSs. It noted that the taxpayers utilized FedEx Ground, a service not included on that list, for delivering their petition to the Tax Court.

The IRS has published a list of all private delivery services that have been designated by the Secretary for purposes of section 7502. See I.R.S. Notice 2016-30, 2016-18 I.R.B. 676. This list includes certain forms of delivery made available by FedEx, but

not FedEx Ground, the delivery service petitioners used. Notice 2016-30, 2016-18 I.R.B. at 676, specifically states that “FedEx . . . [is] not designated with respect to any type of delivery service not enumerated in this list.” Because petitioners did not use a “designated delivery service” as defined by section 7502, they are unable to avail themselves of the “timely mailed, timely filed” rule. Cf. *Guralnik v. Commissioner*, 146 T.C. 230, 240-42 (2016) (holding that the “timely mailed, timely filed” rule does not apply to “FedEx First Overnight” because that service is not a designated private delivery service); *Rackowski v. Commissioner*, T.C. Memo. 2007-72, 93 T.C.M. (CCH) 1045, 1046 (holding that the “timely mailed, timely filed” rule does not apply to “UPS Ground” because that service is not a designated private delivery service).

The taxpayers contended that FedEx Ground, in this instance, was substantially similar to FedEx 2-Day—a service included in the IRS’s list of designated PDSs. They argued that this similarity should permit them to utilize the timely mailing rule. However, the Tax Court did not concur with this perspective.

Petitioners do not dispute that their Petition was filed after the 90-day period specified in section 6213(a), nor do they dispute that FedEx Ground is not on the list of private delivery services that have been “designated by the Secretary.” Rather, they contend that FedEx Ground is “substantially identical” to “FedEx 2-Day,” a delivery service that has been designated by the Secretary for purposes of section 7502. On the basis of this asserted similarity between the two delivery services, petitioners contend that the “timely mailed, timely filed” rule should be available to them.

Unfortunately we must disagree. FedEx Ground may well be substantially similar to the FedEx 2-Day delivery service. But this Court may not rely on general equitable principles to expand the statutorily prescribed time for filing a petition. See *Eichelburg v. Commissioner*, T.C. Memo. 2013-269, 106 T.C.M. (CCH) 606, 607. Congress has chosen to make the “timely mailed, timely filed” rule available for a private delivery service only “if such service [has been] designated by the Secretary.” §7502(f)(2). Because FedEx Ground has not been so designated, our hands are tied. We are not at liberty to make a designation that Congress has explicitly committed to the Secretary’s discretion.

The Court determined that the taxpayers cannot contest the IRS’s assessment in the Tax Court. However, other alternatives, likely less favorable, remain available for the taxpayers to further pursue the issue.

Because the Petition was not filed within the time prescribed by section 6213(a) and the “timely mailed, timely filed” rule is not available, we lack jurisdiction and must grant respondent’s Motion to Dismiss. Although petitioners may not prosecute this case in the Tax Court, we note that they may pursue with the IRS an administrative resolution of their 2017 and 2018 tax liabilities. Another remedy potentially available to them is to pay the tax in dispute and file a claim for refund with the IRS. If that claim is denied (or not acted upon after six months), petitioners may file

a suit for refund in the appropriate U.S. district court or the U.S. Court of Federal Claims. See *McCormick v. Commissioner*, 55 T.C. 138, 142 n.5 (1970).

What About Equitable Relief?

Recall that in *Culp v. Commissioner*, 75 F.4th 196, 205 (3d Cir. 2023), the Third Circuit acknowledged the Tax Court's authority to grant equitable relief. Does this precedent have applicability in the current case, potentially allowing it to progress? Regrettably for the taxpayer, any appeal in this instance would fall under the jurisdiction of the Tenth Circuit Court of Appeals. As indicated in a footnote to the opinion:

Absent stipulation to the contrary this case is appealable to the Tenth Circuit, and we thus follow its precedent, which is squarely on point. See *Golsen v. Commissioner*, 54 T.C. 742, 756-57 (1970), *aff'd*, 445 F.2d 985 (10th Cir. 1971). The Tenth Circuit has long agreed with this Court's holdings that the statutory period prescribed by section 6213(a) is a jurisdictional requirement. See *Armstrong v. Commissioner*, 15 F.3d at 973 n.2; *Foster v. Commissioner*, 445 F.2d 799, 800 (10th Cir. 1971). Thus, we need not address a recent ruling by the U.S. Court of Appeals for the Third Circuit that the statutory filing deadline in deficiency cases is a non-jurisdictional "claims-processing" rule. See *Culp v. Commissioner*, 75 F.4th 196, 205 (3d Cir. 2023).

REFUND CLAIM RECEIVED AFTER STATUTE CLOSED NOT TREATED AS REVISION TO TIMELY INFORMAL BUT FLAWED CLAIM

In the case of *American Guardian Holdings, Inc. v. United States*, USDC ND Ill., Case No. 1:23-cv-01482, February 7, 2024²³⁴ we can look at issues involved with how much can be changed when perfecting an informal claim for a refund once the due date for filing a claim has passed.

In 2019 taxpayer's accountant discovered an error in its 2015 return, believing the tax had been overpaid by \$1,179,563. The accountant prepared an amended return, but it appears from the facts in the case that this return was never actually sent to the IRS.

The corporation hired a new accountant in the fall of 2019. That new accountant prepared a new amended return that now showed no tax at all was due for 2015 (the first accountant's return only showed that less tax was due). The new accountant attached the first amended return to the one he had prepared, had the client sign the return, and sent it to the IRS.

The new accountant's amended return's originally reported income came from the first (apparently never filed) amended return, not the original tax return that was filed by the corporation. The IRS returned the amended return as not processible since the originally reported income did not agree

²³⁴ *American Guardian Holdings, Inc. v. United States*, USDC ND Ill., Case No. 1:23-cv-01482, February 7, 2024, <https://www.taxnotes.com/research/federal/court-documents/court-opinions-and-orders/court-rejects-argument-deeming-refund-claim-timely/7j5dc>

with the original return (the only one filed with the IRS) and asked to correct the numbers (but did not provide a deadline for responding to their request).

The second accountant prepared and submitted another materially different amended return in February 2020 in response to the IRS notice. This time the new accountant wrote that this return was meant to allow the taxpayer to file a Form 1120-PC (property & casualty insurance company) instead of a Form 1120, something not mentioned in the earlier amended return. Now, for the first time, the return showed a large negative income number of more than \$127,000,000. So this was the third return, all of which were materially different.

The IRS argued that this claim was too late as the statute for claiming a refund had closed. One position they argued was that even if the first two claims were informal claims for refund, this last one wasn't a simple update to that claim but rather a totally different one and as such, those informal claims would not have kept the statute open for this radically different claim.

The Court agreed with the IRS that this was a completely new claim - and, as such, was filed late as it had an entirely different basis for the refund. An informal claim must appraise the IRS of *the basis of the claim* which was never provided until February 2020, after the statute to claim a refund on the return in question had closed.

Unit 7

Passthrough Updates

LEARNING OBJECTIVES

- Advise taxpayers on the impact of the IRS's focus on self-employment tax issues in entities taxed as partnerships that are primarily in service industries following the *Soroban Capital Partners* case.

TAX COURT RULES STATE LAW LIMITED PARTNER STATUS IS NOT CONTROLLING FOR EXCLUSION FROM SELF-EMPLOYMENT INCOME FOUND AT IRC §1402(A)(13)

The potentially pivotal role of the phrase “as such” in determining whether state law limited partners are automatically exempt from recognizing self-employment income from the partnership was underscored in *Soroban Capital Partners LP et al. v. Commissioner*, 161 TC No. 12.²³⁵

Facts of the Case

The partnership in question had a structure described by the Court as follows:

Soroban's Limited Partnership Agreement sets forth the terms of the partnership. It states that Soroban has six partners in total, which includes one general partner and five limited partners. Petitioner is the general partner and tax matters partner. The limited partners are Eric Mandelblatt, Gaurav Kapadia, Scott Friedman, EWM1 LLC, and GKK LLC. However, because both EWM1 and GKK are single-member LLCs wholly owned by Mr. Mandelblatt and Mr. Kapadia, respectively, they are disregarded for federal income tax purposes. Therefore, for federal income tax purposes, Soroban has only three limited partners (Mr. Mandelblatt, Mr. Kapadia, and Mr. Friedman).

The Limited Partnership Agreement provides the roles and responsibilities of Soroban's partners. It lists the general partner and its role and authority over the business affairs of the partnership; the limited partners and their roles and interests

²³⁵ *Soroban Capital Partners LP et al. v. Commissioner*, 161 TC No. 12, November 28, 2023, <https://www.taxnotes.com/research/federal/court-documents/court-opinions-and-orders/tax-court-can-make-limited-partner-inquiry-at-partnership-level/7h1k4> (retrieved November 28, 2023)

in the partnership; how the profits and losses are to be allocated; the terms surrounding capital contributions; the voting classes; and the compensation provided to the limited partners in exchange for their services. Mr. Mandelblatt, Mr. Kapadia, and Mr. Friedman received guaranteed payments in exchange for providing services to Soroban.²³⁶

The Court goes on to describe the reporting on the partnership's 2016 and 2017 income tax returns, the years before the Court in this case:

Soroban filed Forms 1065, U.S. Return of Partnership Income, for the years in issue. On those returns Soroban identified petitioner as the general partner and Mr. Mandelblatt, Mr. Kapadia, and Mr. Friedman as limited partners. It reported total net earnings from self-employment of \$2,035,395 and \$1,901,131 for 2016 and 2017, respectively. These totals represented the guaranteed payments received by Mr. Mandelblatt, Mr. Kapadia, and Mr. Friedman for their services to the partnership, and petitioner's share of Soroban's ordinary business income. However, Soroban excluded Mr. Mandelblatt's, Mr. Kapadia's, and Mr. Friedman's shares of Soroban's ordinary business income in its computation of net earnings from self-employment.²³⁷

The IRS objected to the treatment of the limited partners' ordinary income from inclusion as self-employment income.

Self-Employment Income for a Partner

IRC §1402(a) provides the following general rule for the computation of a partner's self-employment income:

(a) **Net earnings from self-employment.** The term "net earnings from self-employment" means the gross income derived by an individual from any trade or business carried on by such individual, less the deductions allowed by this subtitle which are attributable to such trade or business, plus his distributive share (whether or not distributed) of income or loss described in section 702(a)(8) from any trade or business carried on by a partnership of which he is a member;

However, a number of exclusions from self-employment income are found following that language, one of which is found at IRC §1402(a)(13):

(13) there shall be excluded the distributive share of any item of income or loss of a limited partner, as such, (*emphasis added*) other than guaranteed payments described in section 707(c) to that partner for services actually rendered to or on behalf of the partnership to the extent that those payments are established to be in the nature of remuneration for those services;

²³⁶ *Soroban Capital Partners LP et al. v. Commissioner*, 161 TC No. 12, November 28, 2023

²³⁷ *Soroban Capital Partners LP et al. v. Commissioner*, 161 TC No. 12, November 28, 2023

The Importance of “As Such” in the View of Tax Court

The dispute centered on whether the term “limited partner” in IRC §1402(a)(13) inherently encompasses any limited partner as defined by applicable state law, thereby exempting these partners’ shares of the partnership’s income under §1402(a) from being classified as self-employment income. The Tax Court noted that the IRC does not define “limited partner, as such,” as referenced in IRC §1402(a)(13):

Section 1402(a)(13) does not define the phrase “limited partner, as such.” However, legislative history and caselaw provide us with insight on Congress’s intended meaning. The limited partner exception under section 1402(a)(13) was enacted in 1977 to “exclude from social security coverage, the distributive share of income or loss received by a limited partner from the trade or business of a limited partnership.” Social Security Amendments of 1977, §313(b), 91 Stat. at 1536; H.R. Rep. No. 95-702, pt. 1, at 11, as reprinted in 1977 U.S.C.C.A.N. at 4168. Essentially, it was enacted to exclude earnings that are of an investment nature. H.R. Rep. No. 95-702, pt. 1, at 11, as reprinted in 1977 U.S.C.C.A.N. at 4168.²³⁸

In 1997, the IRS sought to define the phrase in question. Recognizing the emergence of new business entities like LLCs and LLPs, which were not prevalent when IRC §1402(a)(13) was enacted, the IRS chose not to solely rely on an individual’s state law limited partner status. Instead, it introduced a series of independent tests, effectively sidelining the state law’s limited partner status.

In 1997 Treasury issued a proposed regulation seeking to define the scope of the limited partner exception. See Prop. Treas. Reg. § 1.1402(a)-2, 62 Fed. Reg. 1702 (Jan. 13, 1997). The proposed regulation provided that an individual would not be treated as a limited partner if the individual had personal liability for partnership debts, had authority to contract on behalf of the partnership, or participated in the partnership’s trade or business for more than 500 hours during the partnership’s taxable year. *Id.* para. (h)(2), 62 Fed. Reg. at 1704.²³⁹

The proposed regulations sparked controversy; they were notably referred to as “stealth tax” regulations by then-Speaker Newt Gingrich.

This proposal received much criticism. That criticism led Congress to issue a moratorium prohibiting Treasury from issuing any temporary or final regulation with respect to the definition of a limited partner under section 1402(a)(13) until July 1, 1998. Taxpayer Relief Act of 1997, Pub. L. No. 105-34, §935, 111 Stat. 788, 882. Congress’s reasoning behind the moratorium was that “the Senate [was] concerned that the proposed change in the treatment of individuals who are limited partners under applicable State law exceeds the regulatory authority of the Treasury Department and would effectively change the law administratively without

²³⁸ *Soroban Capital Partners LP et al. v. Commissioner*, 161 TC No. 12, November 28, 2023

²³⁹ *Soroban Capital Partners LP et al. v. Commissioner*, 161 TC No. 12, November 28, 2023

congressional action.” Revenue Reconciliation Act of 1997, H.R. 2014, 105th Cong., 143 Cong. Rec. S6694, S6774, S6819 (1997).²⁴⁰

However, Congress did not take action before the moratorium’s expiration on July 1, 1998. Since then, Congress has not directly addressed the issue through legislation. Similarly, the IRS has not issued any regulations in this area following the end of the moratorium.

Since the moratorium, Congress has briefly discussed the definition of limited partner but has not defined it. See, e.g., Staff of J. Comm. on Tax’n, 110th Cong., Present Law and Analysis Relating to Tax Treatment of Partnership Carried Interests and Related Issues, Part I, JCX-62-07, at 35 n.64 (J. Comm. Print 2007) (“[L]imited partner status is determined under State law. Issues have arisen under present law as to the proper [self-employment] tax treatment of individuals who may be limited partners under State law but who participate in the management and operation of the partnership.”).⁸ Furthermore, Treasury has yet to issue any final or temporary regulation defining “limited partner” under section 1402(a)(13).²⁴¹

Ultimately, it was the courts that undertook the task of determining how to address these various entities and the exclusion stipulated in IRC §1402(a)(13):

In 2011 we were called upon to determine the scope of the limited partner exception. We applied statutory construction principles to determine whether partners in an LLP should be considered limited partners under section 1402(a)(13). See *Renkemeyer*, 136 T.C. 137. In *Renkemeyer*, 136 T.C. at 150, we analyzed the legislative history of section 1402(a)(13) and concluded that its intent “was to ensure that individuals who merely invested in a partnership and who were not actively participating in the partnership’s business operations . . . would not receive credits towards Social Security coverage.” We further found that “[t]he legislative history . . . does not support a holding that Congress contemplated excluding partners who performed services for a partnership in their capacity as partners (i.e., acting in the manner of self-employed persons), from liability for self-employment taxes.” *Renkemeyer*, 136 T.C. at 150. Lastly, we held that the partners in that case were not limited partners for purposes of section 1402(a)(13) because their “distributive shares arose from legal services . . . performed on behalf of the law firm” and not “as a return on the partners’ investments.” *Renkemeyer*, 136 T.C. at 150.

In *Renkemeyer* we specifically applied a functional analysis test to determine whether the limited partner exception applied. But that case specifically dealt with an LLP and not a limited partnership as present here. While there have been subsequent opinions applying *Renkemeyer* to determine whether taxpayers in passthrough entities are limited partners under section 1402(a)(13), we have not addressed whether a limited partner in a state law limited partnership must satisfy a functional

²⁴⁰ *Soroban Capital Partners LP et al. v. Commissioner*, 161 TC No. 12, November 28, 2023

²⁴¹ *Soroban Capital Partners LP et al. v. Commissioner*, 161 TC No. 12, November 28, 2023

analysis test to be entitled to the limited partner exception. See, e.g., *Castigliola v. Commissioner*, T.C. Memo. 2017-62, at *7-14 (finding professional LLC members not limited partners for purposes of section 1402(a)(13)).²⁴²

The Court describes the basic dispute between the parties as follows:

Petitioner contends that Mr. Mandelblatt, Mr. Kapadia, and Mr. Friedman are state law limited partners and therefore their distributive shares of income are excluded from net earnings from self-employment under section 1402(a)(13). Petitioner argues that because Soroban is a state law limited partnership and its Limited Partnership Agreement identified Mr. Mandelblatt, Mr. Kapadia, and Mr. Friedman as limited partners, section 1402(a)(13) is satisfied.

The Commissioner disagrees, arguing that the distributive shares of income of limited partners in state law limited partnerships are not automatically exempt from self-employment income. He asserts that the Court must apply a functional analysis test, similar to the test outlined in *Renkemeyer* and subsequent cases, to determine whether individuals are limited partners pursuant to section 1402(a)(13).²⁴³

The Tax Court aligned with the IRS in this dispute, with its rationale significantly hinging on the inclusion of the “as such” clause in IRC §1402(a)(13):

Section 1402(a)(13) excludes from net earnings from self-employment “the distributive share of any item of income or loss of a *limited partner, as such*.” (Emphasis added.) Neither section 1402(a)(13) nor applicable regulations define the phrase “limited partner, as such.” Therefore, we use principles of statutory construction to ascertain Congress’s intent.²⁴⁴

The Court, in its opinion, emphasized the necessity to ascribe meaning to every word of the statute. It focused on Congress’ deliberate choice of words, noting that instead of broadly applying the exclusion to limited partners, Congress specifically referred to “limited partners as such.”

Under the canon against surplusage, we give effect to every clause and word of a statute. *United States v. Menasche*, 348 U.S. 528, 538-39 (1955). “When construing a statute, the Court must interpret it ‘so as to avoid rendering any part of the statute meaningless surplusage.’” *Groumark, Inc. & Subs. v. Commissioner*, No. 23797-14, 160 T.C., slip op. at 11 (May 16, 2023) (citing *15 W. 17th St. LLC v. Commissioner*, 147 T.C. 557, 586 (2016)); see also *Tucker v. Commissioner*, 135 T.C. 114, 154 (2010) (“[W]e decline to read words out of the statute; rather, we attempt to give meaning to every word that Congress enacted. . . .”), *aff’d*, 676 F.3d 1129 (D.C. Cir. 2012).

²⁴² *Soroban Capital Partners LP et al. v. Commissioner*, 161 TC No. 12, November 28, 2023

²⁴³ *Soroban Capital Partners LP et al. v. Commissioner*, 161 TC No. 12, November 28, 2023

²⁴⁴ *Soroban Capital Partners LP et al. v. Commissioner*, 161 TC No. 12, November 28, 2023

Turning to the statute in question, we find that the limited partner exception does not apply to a partner who is limited in name only. If Congress had intended that limited partners be automatically excluded, it could have simply said “limited partner.” By adding “as such,” Congress made clear that the limited partner exception applies only to a limited partner who is functioning as a limited partner.²⁴⁵

The Court dismissed the taxpayers’ efforts to reference various other documents, upholding what it determined to be the plain meaning of the statute.

Petitioner’s reliance on legislative history to overcome the plain meaning of the statute is unavailing. To the extent legislative history might be used to shed light on the meaning of the phrase “limited partner, as such,” it confirms our conclusion. Congress enacted section 1402(a)(13) to exclude earnings from a mere investment. It intended for the phrase “limited partners, as such” used in section 1402(a)(13) to refer to passive investors.

Petitioner points to H.R. Rep. No. 95-702, pt. 1, at 11, as reprinted in 1977 U.S.C.C.A.N. at 4168, as support, noting that it states that section 1402(a)(13) was intended “to exclude for coverage purposes certain earnings which are basically of an investment nature.” But Congress’s express text makes clear that it was looking to the nature of the earnings. Congress intended section 1402(a)(13) to apply to partners that are passive investors.

Next petitioner cites the Sense of the Senate Resolution for support. Through that resolution, the Senate expressed its view that Treasury’s attempt to define limited partner exceeded its authority. But Treasury’s proposed regulation had several criteria that might have led to a limited partner’s earnings’ being subject to self-employment tax, even if the person was a passive investor. One such example is merely being personally liable for partnership debts. Prop. Treas. Reg. § 1.1402(a)-2(h)(2)(i), 62 Fed. Reg. at 1704. The Senate’s concern was “that an individual meeting any one of these three criteria will be treated as a general partner.” H.R. 2014, 105th Cong., 143 Cong. Rec. S6694, S6774, S6819. The Senate’s concern about the criteria set forth in Treasury’s proposed regulation does not override the plain text of the statute.

Lastly, petitioner relies on a Joint Committee on Taxation report that states: “A special rule applies for limited partners of a partnership.” Staff of J. Comm. on Tax’n, 110th Cong., Present Law and Analysis Relating to Tax Treatment of Partnership Carried Interests and Related Issues, Part I, JCX-62-07, at 35. In a footnote from that sentence, that report explains that “limited partner status is determined under State law.” Id. at 35 n.64. We find this unpersuasive. The report addresses only the meaning of the words “limited partner” and not the phrase “limited partner, as such.” It is those latter words that narrow the scope of the limited partner exception, which the Joint Committee Report does not address. To

²⁴⁵ *Soroban Capital Partners LP et al. v. Commissioner*, 161 TC No. 12, November 28, 2023

the extent one might read the Joint Committee on Taxation Report more broadly, it does not constitute legislative history and carries no more weight than a law review article. *Gregory*, 149 T.C. at 55.²⁴⁶

Ultimately, the Court dismissed further attempts by the taxpayer to argue that the state law definition should prevail in this case:

Petitioner puts forth myriad other arguments to support its definition of limited partner, but none is persuasive. Petitioner cites section 469 and compares its rules and regulations with section 1402(a)(13), but we do not find the sections analogous. Petitioner cites dicta out of context. Lastly, petitioner points to the 2016 Instructions for Form 1065 at 2 and 2017 Instructions for Form 1065 at 3 as support for its definition. The instructions state: “A limited partner is a partner in a partnership formed under a state limited partnership law, whose personal liability for partnership debts is limited to the amount of money or other property that the partner contributed or is required to contribute to the partnership.” But this definition is provided as part of the “General Instructions” and “Definitions.” This is not, and does not purport to be, a definition for purposes of self-employment tax. In discussion of self-employment tax, the instructions state: “Generally, a limited partner’s share of partnership income (loss) isn’t included in net earnings (loss) from self-employment.” 2016 Instructions for Form 1065 at 34; 2017 Instructions for Form 1065 at 36. Use of the qualifier “generally” makes clear that it is not always true that a limited partner’s share of partnership income is excluded from net earnings from self-employment.²⁴⁷

Will the Decision Survive on Appeal?

The case seems poised for an appeal in a Court of Appeals. The certainty of the Tax Court’s reliance on the “as such” phrase and its interpretation that a partner must meet a functional test to qualify as a limited partner, rather than merely in name, remains uncertain for support in the appellate court. However, the potential for rejection is also unclear, especially considering the complications that could arise from treating LLC members as limited partners solely based on state law, as demonstrated in the *Renkemeyer* analysis.

²⁴⁶ *Soroban Capital Partners LP et al. v. Commissioner*, 161 TC No. 12, November 28, 2023

²⁴⁷ *Soroban Capital Partners LP et al. v. Commissioner*, 161 TC No. 12, November 28, 2023

NOTES

Unit 8

Business Updates

LEARNING OBJECTIVES

- Understand the impact of a potential rescheduling of marijuana on the tax status of state-legal cannabis businesses.

IRS REMINDS CANNABIS BUSINESSES THAT IRC §280E CONTINUES TO APPLY AS MARIJUANA REMAINS A SCHEDULE I DRUG FOR NOW

The IRS has released IR-2024-2024-177²⁴⁸ reminding taxpayers that marijuana remains a Schedule I substance for now, and that IRC §280E continues to apply until such time as the drug is removed from that schedule when and if the Justice Department finalizes the proposed rule. The news release states that:

Until a final federal rule is published, the Internal Revenue Service today reminded taxpayers that marijuana remains a Schedule I controlled substance and is subject to the limitations of Internal Revenue Code.²⁴⁹

The IRS notes that they are receiving improper claims for refund after the news broke about the Department of Justice proposing to move the substance off Schedule I.

The law with respect to the schedule or classification of marijuana has not changed. Taxpayers seeking a refund of taxes paid related to Internal Revenue Code Section 280E by filing amended returns are not entitled to a refund or payment.

Although the law has not changed, some taxpayers are filing amended returns. The grounds for filing such claims vary, but these claims are not valid. The IRS is taking steps to address these claims²⁵⁰

²⁴⁸ IRS News Release IR-2024-177, June 28, 2024, <https://www.irs.gov/newsroom/irs-marijuana-remains-a-schedule-i-controlled-substance-internal-revenue-code-section-280e-still-applies>

²⁴⁹ IRS News Release IR-2024-177, June 28, 2024

²⁵⁰ IRS News Release IR-2024-177, June 28, 2024

The IRS points out that prior to the publication of a final rule, the provisions of IRC §280E will continue to apply to cannabis businesses.

On May 21, 2024, the Justice Department published a notice of proposed rulemaking with the Federal Register to initiate a formal rulemaking process to consider rescheduling marijuana under the Controlled Substances Act. Until a final rule is published, marijuana remains a Schedule I controlled substance and is subject to the limitations of Internal Revenue Code Section 280E.²⁵¹

The release also states the impact of these limitations until such time as a final rule rescheduling the substance is issued.

Section 280E disallows all deductions or credits for any amount paid or incurred in carrying on any trade or business that consists of illegally trafficking in a Schedule I or II controlled substance within the meaning of the federal Controlled Substances Act.

This applies to businesses that sell marijuana, even if they operate in states that have legalized the sale of marijuana. Section 280E does not, however, prohibit a participant in the marijuana industry from reducing its gross receipts by its properly calculated cost of goods sold to determine its gross income.²⁵²

While generally agreeing that it is premature to file a standard claim for refund at this point for prior years, some tax counsel have been suggesting that it might be prudent to file protective claims for refund for years whose statute of limitations on claims for refund are expiring just in case the ultimate IRS guidance or later cases would provide for a retroactive application of the rescheduling and thus allow deducting expenses previously barred by IRC §280E.

While this seems unlikely to take place, the possibility cannot be totally dismissed, so the issue likely should be raised with clients that are potentially impacted and with their tax counsel. Such clients do need to be told, preferably in writing, that such a claim may eventually come to nothing as the hoped for guidance or court rulings may never come, so it will be their choice whether or not to spend the funds needed to prepare the various protective claims.

²⁵¹ IRS News Release IR-2024-177, June 28, 2024

²⁵² IRS News Release IR-2024-177, June 28, 2024

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