IRS Restructuring and Reform Act of 1998

(Training Supplement/Desk Guide)

Highlights of Significant Tax Law Provisions

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Introduction

Congress passed and the President signed into law the IRS Restructuring and Reform Act on July 22, 1998.

In keeping with our commitment to world-class customer service, we believe it is very important that each IRS employee be as informed as possible about the legislative changes that effect the way we do business.

This document is a summary of the highlights of the IRS Restructuring and Reform Act of 1998. Designed as a quick reference tool, it provides a brief background, changes, and selected questions and answers (Q & A) for each section summarized. Ideally, it should be distributed and used by local instructors in workshops and small group discussions.

Also included is a topical index that may be used to quickly locate information or specific subjects. For a complete reference, refer to the Act itself or to authorized explanations such as 1998 Tax Legislation: Law, Explanation, and Analysis, published by CCH Inc.

Sections of the Restructuring and Reform Act highlighted in this document are subject to change as additional clarification of the law is released.

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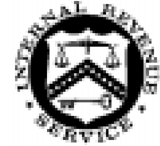

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Section 1102(c) Expansion of Authority to Issue Taxpayer Assistance Orders

Background

Prior law did not define "significant hardship" for the purposes of issuing Taxpayer Assistance Orders (TAO).

The Commissioner had delegated the authority to issue TAOs on issues not specifically covered in the prior law when a significant hardship existed.

Changes

The Taxpayer Advocate's title is changed to National Taxpayer Advocate.

Significant hardship is defined to include:
- An immediate threat of an adverse action by the Service
- A delay of more than 30 days in resolving taxpayer account problems
- The incurring by taxpayers of significant costs if relief is not granted
- Irreparable injury to or long-term adverse impact on a taxpayer if relief is not granted

The Taxpayer Advocate may consider issuing a TAO if there is either:
- Significant hardship as defined by law or under such other requirements as may be prescribed by regulation.
- A service employee has not or is not following applicable published administrative guidelines (including the Internal Revenue Manual (IRM)).

Q & A

Q1 What are some examples of a threat of an adverse action?

A1 When a taxpayer has received notification of actions such as a defaulted installment agreement, lien, levy, or seizure.

Q2 When does the 30 day period for delay begin?

A2 Thirty days after the taxpayer has been promised resolution or 30 days after the normal processing time for the issue involved.

Q3 What type of a situation would cause a taxpayer to incur significant costs wile waiting for relief from a Service action.?

A3 Situations where the Service is unable to make adjustments, process returns, release a lien etc, immediately and the taxpayer is going to have significant cost or expense due to this inability. Ex: Taxpayer made duplicate 941 deposits for same quarter, needs erroneous deposits returned. Otherwise he will need to obtain a loan to meet his payroll or pay large late fee to supplier.

Q4 What are considered irreparable injuries ?

A4 Irreparable injuries would be considered when the taxpayer or family may lose health, reputation, home, employment, etc. The reversal of the Service's actions or payment of damages would not reverse the injury suffered. Financial loss is never an irreparable injury.

Q5 Can you give me some examples of long-term adverse impact?

A5 Some examples of long-term adverse impact are:

- taxpayer unable to go for a job interview.
- business unable to bid on contract.
- detrimental credit report may cost taxpayer his/her job.

Section 2001 Electronic Filing of Tax and Information Returns

Background

Error rate for paper filed returns approximately 20 percent.

Error rate for electronically filed returns less than 1 percent.

Electronic returns receive confirmation of return receipt from Service.

Changes

Paperless filing must be promoted.

Long term goal: at least 80 percent of taxpayers filing electronically by the year 2007. The Service will develop a plan to increase taxpayer use of electronic filing.

The Service must maintain current processing times for paper returns.

By the year 2001 all returns prepared electronically must be filed electronically (when feasible).

Congress will receive an annual report on the progress in meeting the 80 percent goal.

Improvements will be made in the Telefile program and a similar program will be developed for the Internet.

Q & A

Q Is it true that the IRS may institute payments to the tax preparation community as an incentive for electronically filing returns?

A The Service has been authorized to implement procedures to provide for the payment of appropriate incentives for electronically filed returns. The Service has not yet decided whether such procedures will be implemented.

Section 2002(a) Due Date for Certain Information Returns

Background

Payors must supply taxpayers with copies of information returns by January 31 of the following calendar year.

Information returns must be filed with the Internal Revenue Service by February 28 of the following calender year, regardless of the method used to file.

Changes

Due date for information returns filed electronically will be extended to March 31 of the following calendar year.

A study will be conducted on the merits and disadvantages of extending the date for supplying taxpayers with copies of information returns from January 31 to February 15.

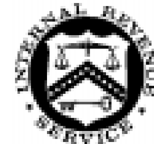
Forms W-2 will still be required to be furnished by January 31.

The change is effective for information returns required to be filed after December 31, 1999 (except Forms W-2).

Q & A

Q Does this effect the 1999 filing season?

A No. The extended due date for filing electronically is effective for information returns required to be filed after December 31, 1999.



Section 2003(d) Paperless Electronic Filing – Internet Availability

Background

Internal Revenue Service provides Internet access for certain forms, instructions and publications.

There was no legal requirement for the type and timeliness of the available documents.

Changes

The Service is required to make available all tax forms, instructions, and publications on the Internet in a searchable database.

This database must include all forms, instructions and publications created in the most current five year period.

Other forms of taxpayer guidance must be made available electronically in a searchable database on the Internet.

This provision is for tax periods beginning after December 31, 1998.

Q & A

Q1 How long after these forms, instructions and publications are published will they be found on the Internet?

A1 The provisions of this act call for these items to be placed on the Internet at approximately the same time the paper versions are available to the public.

Q2 Did the Act specify what other forms of taxpayer guidance should also be placed on the Internet?

A2 No, just that “other types of taxpayer guidance” should be available electronically approximately same time such information becomes available in paper form.

Section 2003(e) Paperless Electronic Filing – Procedures for Authorizing Disclosure Electronically

Background

Electronically filed returns must be filed with paper Form 8453, which contains the signature for the electronically filed return as well as the signature for the disclosure authorization.

A signature for disclosure authorization can not be submitted electronically.

Changes

Service will develop procedures for acceptance of digital or electronic signatures.

Until such procedures are implemented, the Act authorizes the Service to:

- waive signature requirements for selected types or classes of returns or documents.
- develop alternative methods of signing these items.

The Service will establish procedures allowing an electronic disclosure authorization to release taxpayer information to the preparer of the return.

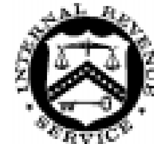
Q & A

Q1 When will the alternative methods to form 8453 be available?

A1 While this provision became effective on the date of enactment, the time period for the Service to develop these procedures has not been determined.

Q2 Are there any circumstances where a return is filed electronically and an 8453 is not required?

A2 Yes, a return filed with Telefile is an electronically filed return and the taxpayer is not required to send Form 8453.



Section 3001 Burden of Proof

Background

Taxpayers had the burden of proof in establishing their tax liability with few exceptions.

There were no specific burden of proof rules for proof of income by statistical averages and most penalties. The taxpayer bore the burden of proof for those issues also.

Changes

Three significant changes were made in the burden of proof in tax litigation. In general, the Service must bear the burden of proof in certain situations when the taxpayer qualifies. Additionally, the Service has additional responsibilities relative to proof of income and penalty assessments.

The general burden of proof is on the Service when the taxpayer shows that they have complied with all the substantiation requirements; have maintained all the records required by the Code; and cooperates with all the Service's reasonable request for witnesses, information, meetings, and interviews and the taxpayer meets certain net worth requirements.

The burden of proof will be placed on the Service when it is asserting an item of income based only on statistical information relating to unrelated tax payers. When the Service uses this method to assert income, the taxpayer will not be required to cooperate or maintain records and the burden of poof will be solely on the Service.

When the Service asserts penalties, additions to tax, or additional amounts, the Service must initially produce evidence with respect to the penalty before the general burden of proof rules apply.

Q & A

Q Is it possible that some taxpayers may interpret the provision to mean that they are no longer required to keep records or produce them when requested?

A That is a possibility, and the Service must educate the taxpayers on requirements for record maintenance and the production requirements whenever possible.

Section 3102 Civil Damages for Collection Action

Background

Previously, taxpayers could recover damages up to $1,000,000 under section 7433 for reckless or intentional disregard of the Code and regulations. Also, **it was not required** that all administrative remedies be exhausted before filing an action, although the courts could reduce the damages awarded if administrative remedies were not exhausted. **Third parties** and **debtors in bankruptcy** could **not** recover damages under Sections 7426 and 7433. Taxpayers could also recover economic damages for wrongful levies due to reckless or intentional disregard of the Code or regulations.

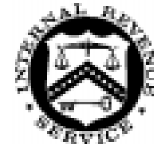
Changes

Now, **taxpayers** may recover:

- up to $100,000 in damages as the result of the negligent disregard of any provision of the IRC or Treasury Regulations by an IRS Officer or employee in connection with **the collection** of federal tax from the taxpayer (Code Sec. 7433(a) & (b)).
- **Third parties** may recover damages up to $1,000,000 for reckless or intentional disregard of the Code or regulations, or
- up to $100,000 for negligent disregard of the Code or regulations under section 7426(e).

Pertaining to **taxpayers in bankruptcy**:

- taxpayers may petition the bankruptcy court for damages up to $1,000,000 for willful violations of bankruptcy code section 362, automatic stay, and section 524, discharge injunction.
- for willful violations of section 524, discharge injunction, section 7433 is the exclusive remedy.
- for willful violations of section 362, taxpayers may elect to sue for damages under section 362(h). However, if damages are awarded under section 362(h), administrative and litigation costs may be awarded under section 7430.
- Recoverable administrative costs are only those which **are incurred on or after the date of filing the bankruptcy petition.**
- When a taxpayer sues in bankruptcy court for violation of either section 362 or 524, the standard is **willful** not **negligen**t or **reckless**.
- **All administrative remedies must be exhausted before a suit for damages can be filed**.



Q & A

Q1 What is the definition of "negligent disregard?"

A1 This has not been determined at this time and has been left to the courts to define.

Q2 If I make a mistake in answering a tax question over the telephone, am I subject to these provisions?

A2 No. This only applies if you are engaged in the collection of Federal tax.

Q3 What is meant by "reckless or intentional disregard?"

A3 This has not been determined at this time and has been left to the courts to define.

Q4 I'm not a Revenue Officer. I'm a CSR. Does this apply to me?

A4 Yes, this provision applies to any officer or employee of the IRS when engaged in the collection of Federal tax.

Q5 What is "wrongful levy?"

A5 A "wrongful levy" may or may not be the same as an "illegal levy" in which the IRS acted negligently. It may simply be a levy in which the IRS may have done everything right as far as could be known but maybe the bank turned over someone else's funds or provided funds which were not in the account.

Q6 If the "wrongful levy" is not the fault of the IRS, do these provisions still apply?

A6 The provisions apply but the extent of the penalties depend upon the particular case and whether the IRS was negligent.

Section 3103 Increase in Size of Cases Permitted on Small Case Calendar

Background

If a taxpayer's contested tax liability is $10,000 or less, he may choose to handle the controversy under small case procedures.

The Tax Court must concur with this choice.

Request may be denied if:

- if it is believed the contested liability will exceed the $10,000 limit.
- the case is unique or will impact other cases before the Tax Court.

Changes

Increases the size of cases to be handled on the small case calendar.

The amount of the contested liability can not exceed $50,000.

The Tax Court must carefully consider the following when determining whether a case that does not exceed the limits can not be heard on the small case calendar.

Internal Revenue Service's objection to the case being heard because of potential precedential value.

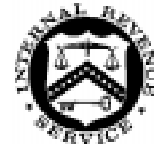
Financial impact to the taxpayer including the additional legal fees.

Q & A

Q1 What is the difference between claims filed on the small case calendar and regular tax court?

A1 Proceedings for small tax cases are much less formal. Briefs and oral arguments are not required. The strict rules of evidence are not applied here, and the taxpayer may, if he/she wishes, serve as their own representative.

Q2 Why can't a case under the dollar limit which could set a precedent be heard on small tax calendar?



A2 Decisions made under the small tax procedures can not be cited as a precedent nor can they be appealed by the government or the taxpayer.

Q3 How does a taxpayer request placement on the small tax calendar?

A3 The taxpayer should complete Petition, Form 2, leaving blank the block at the end of the Petition, Form 2. The form is a simple printed form. The form is supplied by the:

Clerk of the Court, U.S. Tax Court
400 Second St NW
Washington DC 20021

Section 3106 Civil Action for Release of Erroneous Lien

Background

Formerly, the provisions regarding refund suits pertained only to the taxpayer against whom the tax had been assessed and collected.

Changes

The third-party owner of property upon which the IRS has placed a lien may obtain a certificate of discharge by:

- Depositing with the IRS an amount of money equal the value of the United States' interest in the property as determined by the IRS, or
- Posting a bond covering the United States' interest in the property in a form acceptable by the IRS.

This procedural relief is only available to the third-party owner(s), not to the taxpayer whose unsatisfied liability gave rise to the lien.

If the IRS determines that the liability can be satisfied from other sources or the IRS redetermines the value of the property to be less than originally determined, the IRS will refund with interest the excess amount deposited and release the bond applicable to the property.

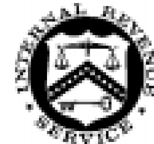
Within 120 days after the certificate of discharge is issued, the third-party owner may file a civil action against the United States in a U.S. District Court for a determination of whether the United States' interest in the property has less value than that determined by the IRS.

If the court rules in favor of the third-party owner that the IRS' valuation exceeds the governments actual interest in the property, the court will order a refund of the deposited amount plus interest and release of the bond. **Interest is to be paid from the time the IRS deposited the received amount to the date the refund is made**, not from the date of the determination.

If the third-party does not file a suit within 120 days after the discharge certificate is issued, the IRS must within 60 days after the 120 day period has elapsed:

- Apply the amount deposited, or
- Collect on the posted bond to the extent necessary to cover the unsatisfied liability secured by the lien

And



- Refund any amount not used to satisfy the liability with interest at the rate applicable to overpayments.

This action is the only action available to third-party owners seeking a determination of the value of the government's interest in their property.

The CSED is suspended from the date the IRS wrongfully seizes or receives a third-party's property to 30 days after the earlier of:

- the date the IRS returns the property under Code Sec. 6343(b), or
- the date upon which a judgement secured pursuant to Code Sec 7426 becomes final.

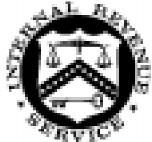
With respect to wrongful liens, the CSED is suspended from the time the third-party is entitled to a certificate of discharge of lien until 30 days after the earlier of:

- the date the IRS no longer holds any amount as a deposit or bond that was used to satisfy the unpaid liability, or
- the date that the judgement in a Civil Action under Code Sec 7426(b)(5) becomes final.

Q & A

Q What is meant by a "wrongful lien or levy?"

A "Wrongful" should not be confused with "willful" or "intentional." A situation to which this would apply would be where the IRS issued a levy on the taxpayer and the bank erroneously turned over money that wasn't the taxpayer's, either because there was actually no money in the bank or the bank tapped the wrong person's account.



Section 3201 Spousal Election to Limit Joint and Several Liability on Joint Return

Background

A taxpayer could request innocent spouse relief from joint and several liability if they met certain requirements. In order to meet the innocent spouse requirements, the taxpayer had to establish:

- A joint return was filed for the taxable year,
- The joint return contained a substantial understatement of tax attributable to a grossly erroneous item of the other spouse the taxpayer did not know,
- Had no reason to know, of the substantial understatement when he/she signed the joint return.

AND

- It would be inequitable to hold the taxpayer liable for the deficiency in income tax attributable to the substantial understatement.

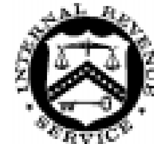
Changes

There are now three different types of relief from the joint and several liability associated with a joint return. If they qualify, taxpayers may (1) elect innocent spouse relief, (2) elect to allocate their liability, or (3) request equitable relief.

(1) **Election for Innocent Spouse Relief**: Section 6015(b) expanded innocent spouse relief from what was previously available under Section 6013(e) by relaxing the requirements as follows:

- The understatement does not have to be substantial or a gross understatement.
- When there is an understatement of tax attributable to an error by the other spouse, the innocent spouse can seek relief.
- A taxpayer may have been aware of an understatement but not of its extent. Relief may be sought on any portion of the tax that is attributable to the part of the understatement that he or she did not know or had no reason to know.

(2) **Election for Allocation of Liability**: Section 6015(c) allows a qualified taxpayer to elect to have the liability for any deficiency limited to the portion of the deficiency that is attributable to items



allocable to that taxpayer under special rules. In order to qualify, the taxpayer must meet one of the following requirements:

- At the time the election was filed, taxpayer was divorced or legally separated from the spouse with whom they filed the joint return; or
- The electing spouse did not live with the spouse with whom they filed the joint return at any time during the 12 months preceding the election.

(3) **Request for Equitable Relief**: If a taxpayer does not meet the requirements of Section 6015(b) and Section 6015(c), then the taxpayer may request equitable relief under Section 6015(f).

- This relief is not available until procedures have been developed by Treasury and the Service.
- It is expected that this relief will be available in the situation where a taxpayer does not meet the requirements of Section 6015(b) and Section 6015(c) because they have an underpayment associated with their joint return, as opposed to a deficiency.
- Equitable relief will also be available to married individuals who file separate return in a community property state under Section 66(c), as amended by Section 3201(b) of the Reform Act.

Section 3201 applies to all liabilities arising after July 22, 1998, and all liabilities arising before July 22, 1998, which were unpaid as of July 22, 1998.

An electing spouse may make an election under Section 6015 after being informed of a potential tax liability, however, the election must be made before 2 years after the first collection activity after July 22, 1998, against that electing spouse.

If the Service does not respond to a taxpayer’s request for relief within 6 months, the taxpayer may petition the Tax Court. If the Service responds by denying a taxpayer’s request for relief, the taxpayer may petition the Tax Court within 90 days after the Service mails the notice denying relief.

A levy cannot be issued from the date of the 6015 election until the end of the 90 day period. A taxpayer who files a petition may not be levied until the court decision becomes final.

The statute of limitations on collection is suspended for the period during which collection is prohibited and for 60 days thereafter.

Q & A

Q1 Does this mean that more taxpayers will qualify for innocent spouse status?

A1 This provision establishes three separate methods of relief:
- Expanded Innocent Spouse Relief
- Separate Liability Election
- Equitable Relief

These methods will allow more taxpayers to seek relief from joint liability.

Q2 Does this provision only apply to joint filers?

A2 No, taxpayers who were married and filed separate returns in community property states may be eligible for equitable relief under Section 3201(b).

Q3 If a taxpayer is in collection can he/she apply for relief under these provisions?

A3 Yes, a taxpayer in collection can apply for relief if there was an unpaid deficiency on the date of enactment (July 22, 1998). Such a taxpayer can apply for relief for two years following the date of the first collection activity against the electing spouse after July 22, 1998.

Q4 I need more information on Equitable Relief.

A4 At this time the procedures for Equitable Relief are being developed.

Section 3202 Suspension of Statute of Limitations on Filing Refund Claims During Periods of Disability

Background

Generally, a taxpayer had to file a refund claim within three years after filing the return or two years after paying the tax, whichever period expired later.

Changes

The suspension (tolling) of the statute of limitations on refunds is permitted for periods of time during which an individual taxpayer is unable to manage his or her financial affairs because of a medically determinable physical or mental impairment:

- that can be expected to result in death, or
- that lasts or can be expected to last for a continuous period of not less than 12 months.
- the normal RSED (Refund Statute Expiration Date) for the credit/refund being claimed has not expired before the date of enactment (July 22, 1998).
- the disability period (or at least part of the disability period) must occur within the normal RSED for the credit/refund being claimed.

A taxpayer will not be eligible for the suspension during the time period that the individual's spouse or any other person is authorized to act on behalf of the taxpayer in financial matters.

To claim the suspension, proof of the impairment will have to be submitted.

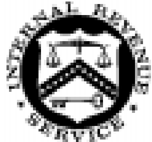
Impact

The suspension of the statute of limitations during a period of impairment will allow taxpayers to claim refunds outside the normal statutes.

Q & A

Q What is the effective date of the provision?

A The provision applies to periods of disability before, on, or after the date of enactment (July 22, 1998), but not to any claim for credit or refund which (without regard to the new provision) is barred as of the date of enactment.



Section 3301 Elimination of Interest Rate Differential on Overlapping Periods of Interest on Tax Overpayments and Underpayments

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Background

Taxpayers have paid higher interest rates on tax underpayments than the IRS has paid on tax overpayments.

Taxpayers could owe interest to the extent of the interest rate differential on overlapping periods of interest on underpayment and overpayments.

Changes

The interest rate differential is eliminated for overlapping interest periods.

This applies to periods of overlap beginning after the date of enactment.

Taxpayers can apply the zero rate to periods beginning before the date of enactment if BOTH of the following apply:

- The taxpayer identifies and establishes the periods of overlapping interest, and
- The taxpayer requests (on or before December 31, 1999) that the IRS apply the zero rate.

Impact

Procedures must be developed to provide for elimination of the interest rate differential.

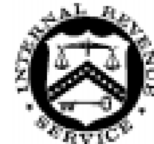
Procedures must be developed to assist taxpayers with requests for application of the zero rate.

Manual interest computations will be required.

Q & A

Q1 Taxpayer A elected to have his 1997 overpayment applied to his 1998 return. Prior to filing the 1998 return, a deficiency was assessed on his 1996 return. Would the 1997 overpayment be considered for netting with the deficiency?

A1 Since the 1997 overpayment is a credit-elect, no interest is allowed on it. There is no period for which interest is payable under



Section 3301 and allowable under Section 6611. Therefore, the zero rate is not applicable.

Q2 On September 1, 2001, Corporation B was determined to have an overpayment of $8,000 on its 1999 return as a result of an examination. During 2001, Corporation B determined it owed $13,000 for its year 2000 taxes. It paid the $13,000 plus interest on December 1, 2001. How is the interest on the overpayment determined?

A2 The overlapping interest period for both the overpayment and underpayment must be determined. This is March 15, 2001 (due date of 2000 return) until the payment date on September 1, 2001. For this period, the interest rate on $8,000 of the underpayment and the $8,000 overpayment must be equalized. Interest on $5,000 of the underpayment is not affected.

Q3 In 1998, I finally received my 1995 refund. It was filed on time and the IRS paid interest from April 15, 1996. Meanwhile, I owed money on my 1996 return and paid the tax with interest from April 15, 1997 to November 30, 1997. Is it right that I paid you interest while you owed me money? You owed me more than I owed you.

A3 From April 15, 1997, until November 30, 1997, you had an overlapping interest period. The interest rate on equivalent amounts of overpayment and underpayment for the overlapping period must be equalized. You must request on or before December 31, 1999, that the IRS apply the zero interest rate to the equivalent amounts of overpayments and underpayments for the overlapping interest period. You must reasonably identify and establish the overlapping interest period for which the zero interest rate applies.

Section 3302 Increase in Overpayment Rate Payable to Taxpayers other than Corporations

Background

Since 1986, the interest rate taxpayers pay on underpayments of tax has been higher than the interest the IRS pays on overpayments.

Changes

The Act increases the interest rate the IRS will pay on overpayments to the federal short-term rate plus three percentage points.

The increase is effective for interest paid in the second and succeeding calendar quarters beginning after enactment, i.e., January 1, 1999.

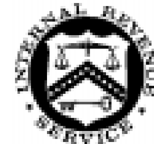
Impact

The interest rate applies to underpayments and overpayments for all returns except Form 1120.

Q & A

Q I'm a sole proprietor with employees. Will the interest rate on my Form 941 overpayment be changed?

A Yes, effective the first calendar quarter of 1999, the interest rate on overpayments will be the same as charged on underpayment for all returns filed except Forms 1120. This is the federal short-term rate plus three percentage points.



Section 3303 Mitigation of Penalty for Individual's Failure to Pay during Period of Installment Agreement

Background

Taxpayers who fail to pay the tax shown on a return by the due date of the return are subject to a penalty of 0.5 percent per month on the unpaid balance of tax up to a maximum penalty of 25%.

The failure to pay penalty is increased to 1% after certain notices relating to levy are given.

Changes

For individuals, the penalty amount for failure to pay is reduced to .025 percent for any month in which an installment agreement is in effect.

The failure to pay penalty is reduced only if the individual timely filed the return in question, including extensions.

The reduced rate only applies to Form 1040 returns.

Q & A

Q1 When does this take effect?

A1 The provision applies in determining additions to tax for months beginning after December 31, 1999.

Q2 Does the reduced rate of .025 percent apply if the 1% rate has been triggered?

A2 No.

Section 3304 Mitigation of Failure to Deposit Penalty

Background

The penalty for not timely depositing taxes ranges from two to fifteen percent of the underpayment.

Deposits and credits are credited to the oldest past-due underdeposits within the same return period.

The IRS can waive the failure to deposit timely penalty for inadvertent failures by certain first time depositors of employment tax.

Changes

Taxpayers may designate the application of a deposit within the return period to which the deposit applies.

Designation must be during the 90-day period beginning on the date of the IRS penalty notice for the specified tax period of the deposit.

Deposits required to be made after Dec 31, 2001, will be applied to the most recent period(s) within the specified tax period unless the taxpayer designates a different period.

The IRS may waive the penalty for the first deposit after a taxpayer is required to change the frequency of employment tax deposits if:

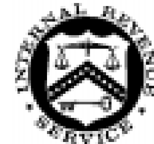
The related return is filed timely.

The taxpayer meets the net worth requirements applicable for an award of attorneys' fees.

Q & A

Q1 I filed my 941 return timely and made all my deposits. I made the deposits on time except the first one. I didn't understand the rules for this semiweekly schedule the IRS just put me on. Can the penalty be waived?

A1 Assuming you meet the net worth requirements, the penalty can be waived. Your 941 was filed timely and this was the first required deposit after you became a semiweekly depositor.



Q2 I am a monthly depositor of payroll deposits. My Form 941 was filed timely. I forgot to make my January deposit and made it April 20, 1999. My February deposit was made March 10, my March deposit was made April 8. The notice I just received says all my deposits were late and charges me penalties on all of them. What can I do?

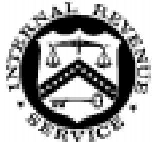
A2 Payments are generally applied to the oldest liability first. This resulted in multiple failure-to-deposit or cascading penalties. You are able to designate the application of each deposit since you have received the penalty notice and 90 days have not passed. This can eliminate all penalties except the penalty for the missed deposit for the January liability.

Q3 Have the rules changed for allowing penalties to be waived for inadvertent failure to deposit payroll tax for certain first-time depositors?

A3 No, Act Section 3304 extends the ability to waive the penalties for taxpayer who meet the net worth requirements and timely file the employment tax return. The penalty may be waived during the first quarter that employment tax deposits are required and, also, for the first deposit after the taxpayer is required to change the frequency of employment tax deposits.

Q4 What is the effective date of these provisions?

A4 The amendments apply to deposits required to be made after the 180th day after the date of enactment. However, the rules providing that a deposit be automatically applied to the most recent period to which the deposit relates apply to deposits required to be made after December 31, 2001 (Act Sec. 3304(d) of the IRS Restructuring and Reform Act of 1998).



Section 3305 Suspension of Interest and Certain Penalties Where Secretary Fails to Contact Individual Taxpayer

Background

Generally interest and penalties accrue when taxes are unpaid.

Accrual occurs whether or not the taxpayer is aware of a balance due.

Changes

Interest and penalties will be suspended on an individual income tax return after 18 months unless the IRS sends a notice within 18 months of the later of:

- The original due date of the return without regard to extensions, or
- The date on which the return is filed timely.

The notice must state the liability and the basis for the liability.

For tax years beginning after Dec 31, 2003, the 18 month period is shortened to 12 months.

The suspension will apply separately with respect to each item or adjustment.

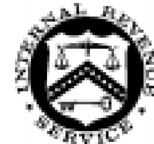
The suspension starts on the day after the end of the 18 (12) month period.

The suspension ends 21 days after the date on which the notice is provided.

The suspension does not stop the accrual of:

- Failure to pay and failure to file penalties (any penalty imposed by IRC 6651).
- Any interest, penalty, additions to tax, or additional amount in a case involving fraud.
- Any interest, penalty, addition to tax or additional amount with respect to any tax liability shown on the return.
- Any criminal penalty.

The suspension applies to tax years ending after July 22, 1998.



Impact

Certain individual taxpayers who are not sent a notice within the required time frame will have interest and penalties suspended.

The IRS must send out notices timely in order for interest and penalties to continue to accrue on timely filed returns.

Q & A

Q1 The taxpayer filed timely on April 15, 1999. She inadvertently failed to include $3,000 of income. Required notice was sent of July 1, 2001 and the balance due was paid October 1, 2001. For what periods is interest suspended?

A1 Interest accrues from April 15, 1999 through October 15, 2000. Interest is suspended from October 16, 2000, through July 21, 2001 (21 days after notice). Interest accrues from July 22, 2001 through October 1, 2001 (payment date).

Q2 When is the previous taxpayer's failure to pay penalty suspended?

A2 Failure to pay penalty is not able to be suspended. It continues to accrue until payment is made.

Q3 Suppose the previous taxpayer had an extension and filed timely on August 15, 1999. When is interest suspended?

A3 Interest accrues from April 15, 1999, until February 15, 2001. It is suspended from February 16, 2001, through July 21, 2001. It accrues from July 22, 2001, through October 1, 2001.

Q4 A taxpayer receives a first notice two years after his return was timely filed. The notice is informing him of a balance due that was shown on the original return. Is the suspension of interest applicable?

A4 No, the provision does not apply when the taxpayer has self assessed the tax.

Section 3306 Procedural Requirements for Imposition of Penalties and Additions to Tax

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Background

Notices sent by Internal Revenue Service that have penalties are not required to show the how penalty was computed.

Penalties can be imposed without supervisory approval.

Changes

Penalty notices must include:
- Name of the penalty
- Code section that authorizes the penalty
- Computation used to figure the penalty

Approval in writing by a supervisor of the employee making the determination is needed before the penalty can be assessed.

Exceptions to the requirement for supervisory approval are:
- Failure to file or pay
- Failure to pay estimated taxes
- Any penalty automatically computed through electronic means

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Q & A

Q1 My site has not informed me that I need prior supervisory approval?

A1 The new procedural requirements become effective on notices issued after December 31, 2000.

Q2 What if my immediate supervisor is not available to give approval?

A2 The act states that the Internal Revenue Service may designate a higher level official to approve the assessment of penalty

Section 3307 Personal Delivery of Notice of Penalty Under Section 6672

Background

Section 6672(b) of the Internal Revenue Code requires the Service to provide at least 60 days written notice to the taxpayer before assessing the trust fund recovery penalty. Notice had to be mailed to the taxpayer's last known address.

Changes

It was believed that if the Service could personally serve the notice required by this section, unnecessary disputes over whether the notice was properly addressed or received might be eliminated.

It was also believed that personal service might afford taxpayers and Service employees an opportunity to resolve trust fund recovery penalty cases at an earlier stage.

With this provision, the Service may personally deliver the written Section 6672(b) notice as an alternative to mailing the notice to the taxpayer's last known address.

Q & A

Q1 Does this mean that a Revenue Officer must personally deliver the notice?

A1 No. This officially provides the option of personal delivery. The notice may still be mailed. Congress felt that personal delivery may encourage earlier resolution without actual assessment of the penalty.

Q2 If a the notice is delivered in person, does it still have to be sent by mail?

A2 No, simply document in the file when the notice was personally given to the taxpayer.

Section 3308 Notice Of Interest Charges

Background

Taxpayers are required to pay interest on amounts owed to the IRS.

Changes

IRS balance due notices that include interest charges must include a detailed computation of the interest charged as well as the Code section under which the interest is imposed.

Q & A

Q1 What is the effective date of this provision?

A1 Notices issued after December 31, 2000 must contain this information.

Q2 What are the specific references for this information?

A2 Act Sec. 3308(a), (b), (c) and new Code Sec. 6631.

Q3 What is the Code Section that imposes interest for failure to timely pay tax?

A3 Code Sec. 6601.

Section 3309 Abatement of Interest on Underpayments by Taxpayers in Presidentially Declared Disaster Areas

Background

The Taxpayers Relief Act of 1997 provides that if the IRS extends the time to file income tax returns and to pay tax with respect to the return for individuals living in an area declared a disaster area by the President during 1997, no interest is charged for the duration of the extension period.

Changes

IRC Section 6404 is amended to provide that if the IRS extends the due date for filing income tax returns and for paying income tax for any taxpayer located in a Presidentially declared disaster area, the IRS will abate the interest that would otherwise accrue for the extension period.

Impact

The interest abatement provision applies to disaster areas declared after December 31, 1997, with respect to taxable years beginning after December 31, 1997.

Q & A

Q1 Why was this provision of the Act necessary?

A1 To amend the IRC to allow abatement of interest during extension periods for tax payers in a Presidentially declared disaster area.

Q2 Will there be a gap in relief between the 1997 Act and the new provision for individual taxpayers?

A2 No. Congress intended that no gap exist between the relief provided for 1997 Presidentially declared disasters and disasters declared after 1997.

Section 3415 Taxpayers Allowed Motion to Quash Third Party Summons

Background

"Third-Party Recordkeepers" are defined as persons other than the taxpayer under investigation to include:

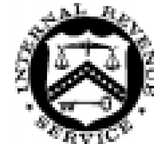
- Any mutual savings bank
- Cooperative bank
- Domestic building and loan association
- Other savings institution chartered and supervised as a savings and loan
- Any bank
- Any credit union
- Any consumer reporting agency
- Any person extending credit through the use of credit cards or similar devices
- Any broker
- Any attorney
- Any accountant
- Any barter exchange
- Any regulated investment company and/or any agent of a regulated investment company when acting as an agent thereof
- Any enrolled agent

Formerly, whenever the Service served a summons on these third-party recordkeepers both the taxpayer and any other person named in the description of records sought by the summons were entitled to be notified about the summons within three days of service, either by certified or registered mail.

They then had the right to intervene in any enforcement proceeding regarding that summons as well as the right to bring a motion to quash the summons within 20 days of notification.

If the taxpayer was successful, he could prevent that third-party recordkeeper from revealing the information sought by the IRS.

Certain types of summonses were exempt, including collection summonses.



Changes

The notice requirement now applies to any summons issued to any third party, not just third-party recordkeepers as previously defined in section 7609. A summons issued to determine Trust Fund Recovery Penalty liability is no longer exempt from the notice requirements. These notification requirements apply to summonses for testimony as well as records.

The IRS' ability to obtain information from other sources without using a summons are not limited by this provision.

Further, certain summonses remain exempt from these provisions:

- Summonses served on the person with respect to whose liability the summons is issued (the taxpayer) or any officer or employee of that person,
- Summonses issued to determine whether or not records of the business transactions or affairs of the taxpayer have been made or kept,
- Summonses issued to third parties who are not third party recordkeepers by a criminal investigator of the IRS in connection with the investigation of an offense connected with the administration or enforcement of the revenue laws.

The taxpayer and any other person identified in the body of any summons issued to a third-party, except those specifically exempt, must be given notice of the summons within 3 days of service or the summons. A summons regarding an investigation for the Trust Fund Recovery Penalty is no longer exempt. Anyone other than Criminal Investigation should make certain that the following change is made to the Form 2039 summons before sending it out:

> Strike out the words, "This certificate applies only to summonses served on third-party recordkeepers and not to summonses served on other third-parties or" and substitute for it the words, "This certificate does not apply to summonses served on."

Revenue Officers may continue to issue "collection" summonses, making certain they are so stated, with the exception of summonses issued for the investigation of the Trust Fund Recovery Penalty; these must follow the above notification procedures.

Special Agents may continue as they have and use Form 2039 without making any changes.

Q & A

Q1 Are summonses issued to gather information to prepare returns included in these provisions?

A1 If the summons is issued to the taxpayer, it does not come under these provisions. If it is issued to a third-party recordkeeper, then these provisions apply unless issued in the course of a criminal investigation.

Q2 Is it only the Form 2039 that is affected by these provisions?

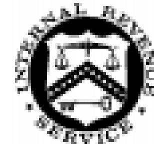
A2 No. Any summons issued on any form, comes under these provisions unless the summons is exempt. Whether a summons is exempt is determined by the reason for its issuance, not by the form used.

Q3 If we send a notice of summons to the potentially responsible person, do we also send a notice of the summons to the corporation or partnership?

A3 Yes, if the corporation or partnership is identified in the summons.

Q4 If we send notice to the corporation, should it be addressed to a corporate officer or simply to the corporation?

A4 When a summons is directed to a corporation. The service must be made upon a corporate officer, director, managing agent, or other person authorized to accept service of process for the corporation. If the responsible person is not known, it should be sent to the corporate officer who signed the return.



Section 3416 Service of Summons to Third Party Recordkeeper Permitted by Mail

Background

Formerly, a summons had to be served either by handing it to the person to whom it was directed or else leaving it at the person's usual place of abode. Service on third-party recordkeepers also had to be made personally.

Changes

Service employees may send a summons by certified or registered mail.

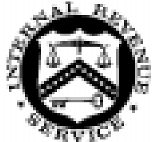
The previous methods of serving summonses still exist. The new procedures provide an additional method of service. The Form 2039 needs to be revised to reflect the new change.

Q & A

Q Does this mean we cannot use the Form 2039 until it is revised?

A No. Service employees may now serve summonses by registered or certified mail so long as the following pen and ink change is made to the relevant Certificate of Service forms in the "How the Summons Was Served" part of the form as follows:

> "I sent an attested copy of the summons by certified or registered mail to the last known address of the person to whom it was directed, that person being a third-party recordkeeper within the meaning of IRC 7603(b). The address is:_____________________________________."



Section 3417 Prohibition on IRS Contact of Third Parties Without Prior Notice

Background

Formerly, Service employees could contact persons other than the taxpayer under investigation to obtain information relating to either the determination or collection of tax. The taxpayer would not necessarily be informed about who the Service had contacted.

Changes

The new law imposes three obligations on the Service:

- The Service must give taxpayers a general warning at the beginning of the examination or collection process that the Service might contact third parties about the taxpayer's tax liabilities.
- The Service must keep track of the third parties that are contacted.
- The Service must provide that information periodically to the taxpayer as well as be prepared to release it upon the taxpayer's request.

Exceptions

The Service does not have to release the information:

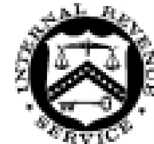
- If the contacts are made in the course of a criminal investigation, or
- The Service determines that releasing the information would jeopardize the collection or assessment of the liability, or
- The Service determines that releasing the information would subject the third parties, from whom the information came, to reprisals.
- The Service also does not have to release information on those contacts which the taxpayer has authorized.

Q & A

Q1 How are these records to be kept and who will have access to them?

A1 At present there are no policies and procedures developed for this provision. The service will have to develop them.

Q2 What is meant by a "contact?" Can this be via telephone or should it be in writing?



A2 The Service has not determined this as yet. The Service has to provide guidance to taxpayers on how to request the list of contacts, how often the lists can be requested, and whether or not one list should include contacts previously disclosed.

Q3 What is meant by "periodically provide?"

A3 This is also not defined at this time. The Service needs to determine if this is going to be provided on a scheduled basis, whenever third-parties are contacted, and whether to divulge that none were contacted.

Q4 What is meant by "jeopardy" and "reprisal?"

A4 Although these terms are currently in use, the Service has not stated that they will be utilized is the same context or whether they will have a more restrictive definition in this respect or not.

Q5 What will we need to do to comply with this provision?

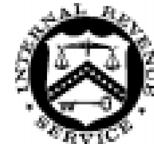
A5 Although there is very little guidance at this time, it is clear that Service employees must begin keeping records of third parties contacted during either the examination or collection process. They must be provided to taxpayers periodically and upon taxpayer request. Records of these are currently kept in the case files. Service employees must be aware that the taxpayer is entitled to this information upon request and the taxpayers must be notified that third parties may be contacted prior to the third parties actually being contacted. According to the Conference Committee report, it is intended that the pre-notification be made part of an existing IRS notice provided to taxpayers (such as Publication 1 or 594).

Q6 Is there anything we must do now to comply with this provision?

A6 This provision is effective 180 days after enactment, meaning late in January 1999. There are no interim procedures or record-keeping requirements, and field offices should not try to anticipate what guidelines the Service will issue.

Q7 Regarding tracking of third party contacts, how specific must the identification of "persons previously contacted" be? Would this include name, address, SSN – what? It is anticipated that if neighbors were requested to give their personal information to comply with this provision that it would interfere with the free flow of information – they would refuse to provide any information. Would just the address and identification as "a neighbor" be sufficient? Does "person previously contacted" include locator services such as DMV, credit bureaus, etc?

A7 These procedures have not yet been established. The Service has until 181 days after enactment to develop procedures and policies to implement this provision.



Section 3431 Modifications to Certain Levy Exemption Amounts

Background

The Service can levy on all non-exempt property of a taxpayer.
IRC Section 6334(a) lists the types of property which are fully or partially exempt from levy. This included the following as totally exempt from levy:

- Books and tools of a trade or profession totaling no more than $1,250, and
- Fuel, provisions, furniture, personal effects in the taxpayer's household, arms for personal use, livestock, and poultry totaling no more than $2,500.

Changes

The amounts exempt from levy are increased as follows and will be adjusted regularly for inflation:

- Books and tools of a trade or profession totaling not more than $3,125, and
- Fuel, provisions, furniture, personal effects in the taxpayer's household, arms for personal use, livestock, and poultry totaling no more than $6,250.

Q & A

Q1 When do these provisions go into effect?

A1 They are already in effect. They were effective July 22, 1998 when the President signed the Bill.

Q2 Are vehicles included within the definition of "personal effects" ?

A2 Vehicles were never deemed to be "personal effects" for purposes of the levy exemption under former law and are not included now. Section 6334(a)(2) describes "personal effects in the taxpayer's household." A vehicle would not fit within the common meaning of this phrase. In addition, the fact that the original exemption amount was only $500 provides support for the position that creating an exemption for a vehicle was never contemplated. There is nothing in the legislative history for section 3431 to indicate Congress intended to expand the types of property which are

exempt from levy. Section 3431 merely increases the dollar amounts that can be exempted.

Section 3434 Approval Required for Jeopardy & Termination Assessments and Jeopardy Levies

Background

Formerly, there was no requirement that Chief Counsel pre-approve jeopardy and termination assessments and levies made less than 30 days after notice and demand, although the IRM does instruct revenue officers to obtain Counsel's approval if there is time before such assessment and levies are made and it is the current practice for Counsel to conduct such reviews.

Changes

All jeopardy and termination assessment and jeopardy levies made less than 30 days after notice and demand must have written approval by the IRS Chief Counsel or his delegate.

Within 5 days or making the jeopardy or termination assessment or jeopardy levy, the IRS must provide the taxpayer with a written statement explaining the basis on which the IRS relied in making the assessment or levy.

The pre-levy due process procedures under section 3401 do not apply to levies made less than 30 days after notice and demand.

If prior Counsel approval is not obtained, the taxpayer is entitled to an abatement of the assessment or release of the levy. If the IRS fails to offer such relief, the taxpayer may appeal to IRS Appeals under the new due process review procedure for IRS collections and then to court.

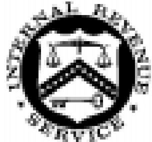
Q & A

Q1 What if the statute is imminent and there is not time to get Counsel's approval? Can I make the jeopardy levy?

A1 No. Approval by IRS Chief Counsel or his delegate is **mandatory.**

Q2 Counsel gave me approval via telephone. Can I document it and make the levy?

A2 No. The approval by Counsel or his delegate **must be written.**



Section 3435 Increase in Amount of Certain Property on which Lien not Valid

Background

Under IRC 6321, if any person liable for any tax fails to pay the tax after demand, a lien in favor of the United States automatically attaches to all of that person's real and personal property or rights to property.

The lien is not valid against "any purchaser, holder of a security interest, mechanic's lien, or judgement lien creditor" until the Service files a Notice of Federal Tax Lien (IRC 6323(a)).

However, the effect of a Notice of Federal Tax Lien is not valid against persons holding certain interests on property of the taxpayer that are specified in IRC 6323(b); these are known as "super-priorities." Two of these interest are limited by a specific dollar amount.

Formerly, the following were granted super-priority status (including code section and dollar amounts):

- IRC 6323(b)(4) Total sale less than $250
- Persons who purchased household goods, personal effects, and items exempt from levy under IRC 6334(a) from a taxpayer is a **casual sale**, such as a **yard sale**.
- IRC 6323(b)(7) Contract not more than $1,000
- Contractors, repairmen, and mechanics who had contracted with the taxpayer for **repairs or improvements** to be made to the taxpayer's owner-occupied personal residence.
- IRC 6323(b)(10) unlimited
- Banks and building and loan associations which made **passbook loans** to their customers, provided that those institutions retain the passbooks in their possession until the loan is completely paid off.

The seven other categories of "super-priorities" listed in IRC 6323(b) have not changed.

Changes

IRC 6323(b)(4)	Total sale less than $1,000
IRC 6323(b)(7)	Contract not more than $5,000
IRC 6323(b)(10)	Updated to show current banking practices, where a passbook-type loan may be made even though an actual passbook is not used.

Q & A

Q1 How can I know if the Service is not behind a super-priority?

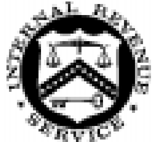
A1 It's not important to know that prior to filing a lien. As has been the practice, a lien should be filed as soon as it is deemed necessary to protect the government's interest and facilitate collection. The awareness of a "super-priority" is important when enforcement action needs to be taken.

Q2 If this is the only funds available, does this mean the government has no hope of recovery?

A2 No. Any amounts over the stated dollar amount has no "super-priority" status and would be retrievable by the government.

Q3 When is this effective?

A3 Now. It went into effect when the President signed the bill on July 22, 1998.



Section 3441 Prohibition of Sales of Seized Property at Less Than Minimum Bid

Background

IRC 6335(e) requires that a minimum bid price be established for seized property offered for sale.

To conserve the taxpayer's equity in the property the minimum bid price normally should be set at 80% or more of the forced sale of the property less the amount of any encumbrances having priority over the Federal Tax Lien.

Exceptions are also provided in the IRM if, due to the situation, the revenue officer with group manager approval needs to compute the minimum bid at a lower percentage.

The revenue officer must advise the taxpayer of the minimum bid price, how it was computed, and give the taxpayer 10 days to respond. The taxpayer may challenge the minimum bid price. If the minimum bid is set at the tax liability plus the expenses of sale, it is not necessary that the taxpayer agree to it.

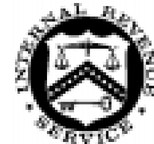
If no one offers the minimum bid price and the Service has determined that the purchase of the property by the United States would be in its best interest, the Service may bid-in and buy the property at the minimum bid price. If no one offers the minimum bid price and the Service determines that it would not be in the best interest of the United States to purchase it, the Service must release the property back to the taxpayer.

Although IRC 6335 did not suggest that seized property could be sold for less than the minimum bid price, it did not expressly forbid a sale for a lesser amount.

Changes

The Service must determine a minimum bid price below which the seized property must not be sold.

The IRS is expressly forbidden to sell property for less than the minimum bid price.



The sale of property for less than the minimum bid price is an unauthorized collection action and the taxpayer may sue for civil damages under IRC 7433.

Q & A

Q1 When is this provision effective?

A1 Now. It became effective when the President signed the bill on July 22, 1998, and applies to all sales after the date of enactment.

Q2 What about sales that are already in progress?

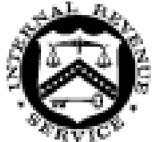
A2 Unless the sale was consummated prior to July 22, 1998, they are subject to these provisions.

Q3 Our sale was consummated after July 22, 1998, and we sold it at the best price we could get with managerial approval but it was less that the set minimum bid.

A3 Your sale was a prohibited collection action and the taxpayer can sue for civil damages under IRC 7433. Refer back to Section 3102.

Q4 If a determination must be made prior to seizure that there is equity after expenses, how is seizure of a safe deposit box handled where you don’t know the contents of the box, if any?

A4 The Act does not specifically address this issue nor specifics of many individual seizures. Congress has stated that a seizure cannot be done unless, based upon all of the information at hand, it can be shown that there will be equity after expenses. When there is doubt, the advice of District Counsel should be sought in the absence of local procedures.



Section 3442 Accounting of Sales of Seized Property

Background

The Service is authorized to seize and sell a taxpayer's property to satisfy an unpaid tax liability.

The Service is required to give the taxpayer written notice at least 30 days before seizure of the property (IRC 6331(d)), the taxpayer must be given notice of the sale of the seized property, publish a public notice of the sale (IRC 6335(b)) and the property must be sold no less than 10 days nor more than 40 days after the notice of the sale (IRC 6335(d)).

Although the Service is required to keep records of all sales of **real property**, including the proceeds and expenses associated with the sale (IRC 6340), there is no existing provision that requires the Service to inform the taxpayer of how the proceeds are applied.

There also is no requirement that the Service keep records of sales of personal property.

Changes

With this provision, IRC Section 6340(a) is amended to require the Service to keep a record of all sales of property, **including sales of personal property**, in the same manner as that previously kept for **real property**.

In addition, a new section, Section 6340(c), requires the Service to give the taxpayer a copy of the record showing the amount from each sale applied to the taxpayer's account and the remaining balance.

Therefore, **for all sales**, the IRS must keep records of:

- The delinquent tax,
- The dates of seizure and sale,
- The party assessed,
- The sale proceedings,
- The amount of expenses,
- The purchasers,
- And the date of any deed.

The Service must also the taxpayer whose property has been seized and sold or redeemed a copy of the record that the Service is required to keep

showing the amount from each sale applied to the taxpayer's account and the remaining balance.

The Service already has Form 2435. Pen and ink changes can be made to make this form usable for personal property until a separate form is created.

The Service already provides the taxpayer with Form 2436 which contains most of the information required to be given to the taxpayer. Pen and ink changes can make this form totally compliant by adding:

- The date on which a deed or certificate of sale was issued, and
- A statement as to the taxpayer's remaining outstanding tax balance, if any.
- Taxpayers are entitled to collect damages under IRC 7433 if the Service fails to comply.

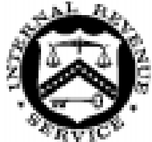
Q & A

Q1 Can we provide all of the required information to the taxpayer over the telephone?

A1 No, it must be written. The Service doesn't keep oral records and the provisions state that it must be a copy of the records the Service kept that is provided to the taxpayer.

Q2 When is this effective?

A2 This applies to all seizures made after the date of enactment, July 22, 1998.



Section 3444 Codification of IRS Administrative Procedures for Seizure of Taxpayer's Property

Background

The IRS provides guideline to its employees for the collection of unpaid tax liabilities including the seizure of property to satisfy those liabilities. In addition to providing guidelines for its employees, they also act to protect the taxpayer.

IRM 56(12)5.1 provides these general guidelines which include:

- A requirement to verify the taxpayer's liability,
- A requirement to determine whether the estimated expenses of levy and sale exceed the fair market value of the property. If they do, the property can not be seized,
- A requirement to determine whether the taxpayer has sufficient equity in the property to have money after expenses applied to the liability. If there is not and the property has already been seized, the property must be immediately released.

Before seizing the assets of a going business, all alternative methods of collection must be thoroughly considered. Reasonable forbearance should be exercised if a major disaster such as a flood, hurricane, drought, or fire has affected the taxpayer's business and affected the taxpayer's ability to pay the liability.

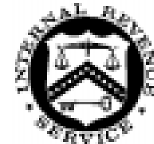
Changes

In order to assure that the IRS follows its own procedures which it has already given to its employees, these procedures are now made a mandatory part of the Code.

Q & A

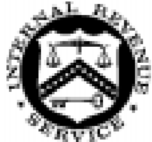
Q1 When is this effective?

A1 It is effective on the date of enactment, July 22, 1998, but should pose no new concern since this is the operating procedure of the IRS already. Codification provides for Congressional oversight, procedural disclosure, and assurance of consistent treatment.



Q2 If a determination must be made prior to seizure that there is equity after expenses, how is seizure of a safe deposit box handled where you don’t know the contents of the box, if any?

A2 The Act does not specifically address this issue nor specifics of many individual seizures. When there is doubt, the advice of District Counsel should be sought in the absence of local procedures.



Section 3445 Procedures for Seizure of Residences and Businesses

Background

If a taxpayer does not pay any tax within 10 days after notice and demand, the IRS may seize and sell property in which that taxpayer has an interest (IRC 6331(a)).

The IRS' authority to seize property is subject to certain procedural rules and limitations:

Principal Residence

- Unless collection of tax is in jeopardy, the principal residence of a taxpayer may not be seized without approval of an IRS District or Assistant District Director (IRC 6334(a)(13) & (e).
- There is no legal restriction on the seizure of a residence used by persons other than the taxpayer.
- There is no legal restriction on the seizure of the taxpayer's principal residence to satisfy small tax deficiencies.

Going Business

- It is the policy of the IRS to consider the facts of the case and alternative collection methods before seizing the assets of a going business (P-5-34), but this is not a statutory requirement.

Changes

In order to prevent undue disruption of the residents of any residence, the IRS may not seize any real property used as a residence by either the taxpayer, spouse, ex-spouse, or minor child, or real property of the taxpayer that is used as a personal residence by someone else, unless it is rental property, in order to satisfy a levy amount of $5,000 or less.

Further, the IRS may not seize the taxpayer's principal residence without the written approval of a U.S. District court judge or magistrate.

Unless collection of tax is in jeopardy, tangible personal property or real property, other than rented real property used in the taxpayer's trade or business, may not be seized without the written approval of an IRS District or Assistant District Director.

Such approval may not be given unless it is determined that the taxpayer's other assets subject to collection are not sufficient to pay the amount due and the expenses of the proceedings.

Effective July 22, 1998, the enactment of this Act, the Service CANNOT seize residences of any individual (except rental property) where the levy amount does not exceed $5,000, regardless of prior approval. Seizures of principal residences must now be approved judicially.

Effective July 22, 1998, the enactment of this Act, Revenue Officers CANNOT seize an individual's business assets as previously described unless the District Director or Assistant District Director personally approves such seizure in writing. There currently is no ability to delegate this authority.

District Directors and Assistant District Directors CANNOT grant such approval without first evaluating the availability of other assets.

Q & A

Q1 What is meant by "tangible personal property?"

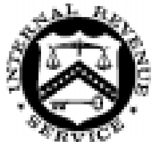
A1 "Tangible Personal Property" refers to visible and movable property such as an automobile, boat, furniture, or the like; usually property which may be depreciated that does not qualify as "real property."

Q2 What is meant by "other assets?"

A2 "Other Assets" include any asset other than the business assets for which seizure approval is being considered, and specifically includes future income that may be derived by a taxpayer from the commercial sale of fish or wildlife harvested under a state fish or wildlife permit.

Q3 I have obtained permission to seize a taxpayer's residence prior to the enactment but have not done so yet. Can I still proceed?

A3 Not without first complying with the new law. Upon enactment of this Act, the IRS **CANNOT** seize residences of any individual (except rental property) where the levy amount does not exceed



$5,000 regardless of prior approval. Seizure of principal residences must now be approved judicially.

Q4 There is a requirement in section 3445 to exhaust all payment options before seizure and to secure District Director approval before seizing tangible personal property or real property used in the trade or business of an individual taxpayer. Does the exhaustion of all payment options include requiring the taxpayer to secure a loan based upon the value of assets (including accounts receivable) or to convert assets to cash to apply to the delinquent tax?

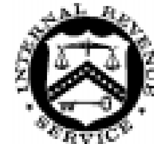
A4 Payment options may include the factors mentioned plus other payment alternatives dictated by circumstances of the case. The taxpayer's ability to secure a loan or discharge property from the lien to raise funds to pay **must** be considered. The key is that the reviewing/approving official must be satisfied that the case options have been explored.

Q5 Does "tangible personal property" include inventory?

A5 Business inventories of physical items are generally considered tangible personal property.

Q6 Is the fact that the taxpayer is continuing to accrue additional Form 941 trust fund employment taxes any sort of mitigating factor when considering seizure (assuming there is equity in assets)?

A6 The continuing nonpayment of Form 941 trust fund employment tax liabilities (pyramiding) **may** be a mitigating factor. However, revenue officers are not relieved of the legal **requirement** to explore payment options before seizure solely on the basis that the taxpayer is pyramiding the liability. The fact that the taxpayer is continuing to accumulate additional liabilities and all payment options have been reasonably exhausted should be a part of the supporting documentation for the request or seizure approval.



Section 3461 Procedures Relating to Extension of Statute of Limitations By Agreement

Background

Generally:

- The Service has three years from the date a return is filed to assess additional taxes.
- The Service generally has ten years from the date of assessment to collect the tax (IRC 6502(a)(1)).
- The taxpayer and the Service could agree in writing to extend the statute of limitations (IRC 6501(c)(4)).

To obtain an extension, the parties must complete a written consent before the statute period expires (3 years for assessment and 10 years for collection).

Taxpayers often agree to the extension believing it will be in their best interest, but they also have the right to refuse.

Congress believed many taxpayers were not being informed of their rights to refuse to extend the statute of limitations on assessment or to limit the scope of any such extension.

Congress also believed that all taxes should be collected within ten years without extension of the statute.

Changes

On December 31, 1999, the collection statute of limitations can no longer be extended.

Any extension already in effect on December 31, 1999, automatically expires on December 31, 2002, with the exception of installment agreements.

Taxpayers must be specifically informed of their right to refuse to extend the statute or limit the extension to particular issues or to a particular period of time.

If an extension is agreed to with the acceptance of an installment agreement, the extension should be for the period necessary to satisfy the tax liability under the installment agreement.

The period of limitations for extensions related to installment agreements will expire 90 days after the end of the extension period.

The collections period may continue to be extended after it has expired if:

- There has been a levy on any of the taxpayer's property before the statute expiration, and
- The extension is agreed to before the levy is released .

Each time the Service requests taxpayers extend the limitations period, the taxpayers must be advised of their right to refuse to extend or to limit the extension on the statute of limitations on assessment.

Except in the case of installment agreements, Collection 900 waivers cannot be solicited from any taxpayer after December 31, 1999. In cases other than those involving installment agreements, the Service cannot collect on any case where the statute of limitations has been extended beyond December 31, 2002.

Q & A

Q1 Is this effective as of the date of enactment (July 22, 1998)?

A1 No. This provision applies to all extension requests made after December 31, 1999.

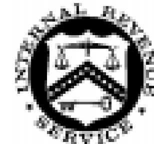
Q2 So, can I continue to request and accept extensions up until that date?

A2 Yes, but be aware that any request to extend the 10-year statute for collections made on or before December 31, 1999, regardless of the terms of the agreement, on the latest of:

- the last day of the original 10-year limitations period, or
- December 31, 2002, or
- in the case involving an installment agreement, the 90th day after the extension

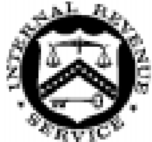
Q3 What effect does the new law have on extensions already in place, where the collection statute has been extended beyond December 31, 2002?

A3 The waiver of statute is terminated as of December 31, 2002.



Q4 Does the IRS have the authority to void existing agreements in light of the fact that the waivers required to get the agreement will expire prior to the agreed upon term?

A4 Not as long as the agreement is current. There should be no collection action if all other terms of the agreement are met.



Section 3462 Offers-in-Compromise

Background

The IRS has the authority to accept less than the full amount of a liability owed in a civil or criminal case prior to the case being referred to the Justice Department based upon one or both of the following criteria:

- doubt as to liability, or
- doubt as to collectibility

The basis of most offers is doubt as to collectibility.

An Offer-in-Compromise is a contractual agreement between the taxpayer and the IRS.

Formerly, the taxpayer would agree to a 60-month suspension of the collection statute and agree to remain fully compliant with the tax laws during the 60-month period.

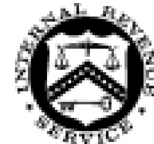
To have an offer considered, the taxpayer had to disclose detailed information regarding his assets and liabilities and be willing to pay over the net value of such assets plus the present value of total net disposable income available over the 60-month period.

To aid in computing the net disposable income, the IRS developed national standards for living expenses and local standards for measuring the costs of housing, utilities, and necessary transportation. Assets above these standard amounts would be used to satisfy the tax liability.

Congress believes the Service should be more flexible in working with taxpayers who are sincerely trying to satisfy their tax obligations and make it easier for taxpayers to enter into offers-in-compromise.

Many people have stated that the local and national standards have removed the revenue officers from case-by-case decision making which has made the process inequitable and harder to get an approved Offer-in-Compromise which was not the intent in setting up the standards.

Critics recommend that revenue officers be given discretion to recognize expenses on a case-by-case basis and the ability to recognize expenses such as educational expenses as being necessary (for example, families living in low-income urban areas who bear the expense of sending their children to parochial schools).



Others point to the prohibition against treating unsecured debt (except for court-ordered payments) as a necessary expense.

Tax writing committees have indicated taxpayer compliance is enhanced by the ability to compromise and make installment payments.

Changes

The IRS is required to develop employee guidelines for determining the adequacy of the offer.

The guidelines must include local and national allowances under which the IRS employees may determine on a case-by-case basis whether the use of the standard allowances is appropriate.

Local and national standards are not to be used to the extent that they would result in a taxpayer not having adequate means to provide for basic living expenses.

IRS employees may not reject an offer from a low-income taxpayer solely on the basis of the amount of the offer.

If the offer is based upon doubt as to liability, the IRS may **not** reject the offer solely because the IRS cannot locate a taxpayer's return or return information for verification purposes.

Anyone seeking an offer based upon doubt as to liability is **not** required to provide a financial statement.

IRS is urged to be flexible in finding ways to work with taxpayers who are sincerely trying to meet their tax obligations, for example by foregoing penalties and interest amounts that have accumulated while determinations of taxpayer liability were being made.

In addition, the Service cannot levy on he property of a taxpayer who has a pending offer-in-compromise or installment agreement, or

- during the 30 days following rejection of the requested offer-in-compromise or installment agreement
- during any time the rejection of a request for either an offer-in-compromise or an installment agreement is being appealed, provided the appeal is filed within 30 days of the rejection
- during any period for which an installment agreement is in effect
- during the 30 days after an installment agreement is terminated

- during the time an offer-in-compromise is being considered
- during the time an installment agreement offer is being considered

The prohibition does not apply if the taxpayer files a written notice waiving the levy prohibition.

The prohibition does not apply to any offset under IRC 6402 or to any levy predating the receipt of the offer-in-compromise or installment agreement.

The IRS is prohibited from initiating any court action with respect to the liability that is included in the offer with the exception of the counter-claims or any related proceedings.

The 10-year collection statute is suspended during the time the IRS is prohibited from making a levy or taking other collection measures while the offer-in-compromise is pending.

All rejected offers and installment agreements must undergo an independent administrative review before the rejection is communicated to the taxpayer. The IRS must establish procedures for this.

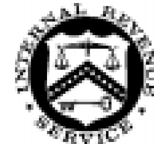
The taxpayer must be allowed o appeal any rejection of any proposed offer-in-compromise or installment agreement to the IRS Office of Appeals.

The IRS must prepare a statement informing the taxpayer of his/her rights and obligations with respect to offers-in-compromise and installment agreements which must be in simple non-technical terms and must advise the taxpayer:

- of the advantages of promptly notifying the Service of any address changes,
- that any non-compliant activity by one spouse or former spouse does not prevent the complying spouse or former spouse from having it reinstated upon application (with respect to married taxpayers who have entered into an offer-in-compromise), and
- if their offer-in-compromise was rejected, that they have the right to appeal to the IRS Office of Appeals.

Q & A

Q1 When are these provisions effective?



A1 Generally, these provisions apply to all offer-in-compromises and installment agreements submitted after the date of enactment (July 22, 1998). The provisions relating to suspension of collection by levy applies to offers-in-compromise pending on or after December 31, 1999.

Q2 What is the definition of a "low-income" taxpayer.

A2 The Act does not define this. This is one of the things the IRS must decide when creating its procedures and policies pertaining to these provisions.

Q3 Can the current local and national standards continue to be used for offer processing?

A3 They can be used, but authorization to do so would have to come via local procedures.

Q4 Can we still use the current Form 656?

A4 Yes, until form 656 is revised, with the addendum that provides for severability in the event of default by jointly liable taxpayers with joint offers.

The waiver provided in the current form will expire as of December 31, 2002. If the 10-year collection statute is still open on that date for the liabilities contained in the offer, the offer agreement may remain viable.

For offers pending after December 31, 1999, the statute will be suspended because of the Service's inability to collect by levy.

If a taxpayer submits an offer between the date of enactment and December 31, 1999, where the collection statute expires on or before December 31, 2002, collection action must stop as of that date.

Q5 Can the application of state tax refunds still remain as a condition of acceptance of an offer or installment agreement?

A5 Absolutely not. The Service is no longer allowed to condition the acceptance of an installment agreement on the taxpayer's waiver of the right to receive a state income tax refund. Any language on an installment agreement form authorizing the Service to levy on state income tax refunds as a condition of the agreement should be eliminated.

Q6 What does "independent administrative review" mean?

A6 This is not defined at this time but is a part of the establishment of policies and procedures for these provisions.

Section 3463 Notice of Deficiency to Specify Deadlines for Filing Tax Court Petition

Background

A taxpayer who wishes a redetermination of their tax liability before the Tax Court must file a Tax Court petition within 90 days after the deficiency notice has been mailed. Taxpayers outside of the United States have 150 days after the mailing. If the taxpayer does not file a petition within that time frame, the Tax Court can not consider the petition.

Changes

All deficiency notices must provide the date IRS has determined to be the last day for filing a petition with the Tax Court.

All petitions filed by the date stated on the deficiency notice will be considered filed timely.

Impact

Taxpayers will have a definite date for filing of the petition.

All deficiency notices mailed after December 31, 1998 must carry the last day for filing of the petition.

Q & A

Q Are there any changes to the regulations for filing a petition before the Tax Court?

A No, this act only concerns the requirement for the deadline date for the filing of the petition.

Section 3464 Refund or Credit of Overpayments before Final Determination

Background

Generally, the IRS cannot take any action to collect an account during the time that a taxpayer is petitioning the tax court regarding that account; no action can be taken until the court decision becomes final.

Refunds on the disputed period are also frozen and there is no authority for ordering the refund of any amount collected by the IRS during the prohibited period.

If the tax court determines that an overpayment has been made and a refund is due the taxpayer, no provision exists for the refund to be made prior to the court's decision becoming final.

Changes

The Act provides that any court having jurisdiction in the case, including the tax court, may order a refund of any amount that the IRS collected during the time the IRS was prohibited from collecting.

Further, the Service is also authorized to issue a refund of, or credit an overpayment that is not contested on appeal.

Q & A

Q When does this become effective?

A Upon the date of enactment, July 22, 1998.

Section 3466 Application of Certain Fair Debt Collection Procedures

Background

Taxpayers may bring damages action against the IRS if, in connection with a collections activity, an IRS employee recklessly or intentionally disregards any tax code provision or Treasury regulation (IRC 7433).

Formerly, the Fair Debt Collection Practices Act (P.L. 95-109) which restrict various collection abuses in the private sector, generally did not apply to the federal government.

Changes

This provision requires the IRS to comply with certain provisions of the Fair Debt Collections Practices Act.

IRS may not communicate with any taxpayer at an unusual or inconvenient time or place unless otherwise agreed to by the taxpayer or with consent by court order.

Unless otherwise agreed to, the IRS is to assume that the convenient time for communicating with taxpayers is between the hours of 8:00 am and 9:00 pm, as determined at the taxpayer's location.

IRS may not communicate with the taxpayer if the IRS knows that the taxpayer has obtained representation from a person authorized to practice before the IRS and the IRS knows or can readily obtain the representative's name and address. This requirement is void if the representative consents to direct communication with the taxpayer, or the representative fails to respond to IRS communications within a reasonable period of time.

The IRS is restricted from communicating with the taxpayer at the taxpayer's place of employment if the IRS knows or has reason to know that such communication is prohibited by the employer.

The IRS may not harass, oppress, or abuse any person in connection with any tax collection activity that would naturally lead to harassment, oppression, or abuse.

Examples of violations are as follows (the list is not exhaustive):

- The threat or use of violence or other criminal means to harm the physical person, reputation, or property of any person.
- The use of obscene, profane, or abusive language either verbally or in writing.
- The use of a telephone with the intent to annoy, abuse, or harass any person at the number called, whether through conversation or merely by repeated calling.
- Except as provided under 15 USC 1692b, placing telephone calls without meaningful disclosure of the caller's identity.

Q & A

Q1 What does "meaningful disclosure of the caller's identity" mean?

A1 Although this is presumed to mean that the employee is to give his/her name, employee number, and affiliation as required in Act section 3705, this is not specifically defined at this time.

Q2 The terms "harass," "oppress," and "abuse" are rather broad and subject to personal interpretation. What an upset taxpayer may term as "harass" may not be that at all from the revenue officer's viewpoint. Is there any guidance as to what the Service is holding as "harass," "oppress," or "abuse?"

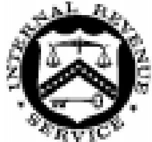
A2 Not at this time. Until the service defines these terms, local procures and guidelines should be used along with the provisions of the Fair Debt Collection Practices Act (P.L. 95-109) under which revenue officers are now bound.

Q3 Will there be any training provided for revenue officers regarding the Fair Debt Collection Practices Act?

A3 Revenue officers should see their managers for this; they should be well familiar with the Fair Debt Collection Practices Act provisions since they are responsible for adherence to it.

Q4 Is it safe to assume that "obscene, profane, or abusive language" is what is commonly meant?

A4 Although it may appear to be self-evident what the meaning of "obscene, profane, or abusive language" might be it should not be assumed since the civil courts have rendered differing opinions. Revenue Officers should look to their district's local procedures for guidance until the Service provides definitions.



Section 3467 Guaranteed Availability of Installment Agreements

Background

The Service is authorized but not required to enter into written agreements for the payment of taxes in installment payments.

Taxpayers do not have an absolute right to an installment agreement. The IRS director has discretion to accept or reject an installment agreement proposal.

However, the Service routinely grants requests for installment agreements to taxpayers who meet certain criteria (streamlined installment agreements).

These are granted to taxpayers without verification of the taxpayer's financial background if the amount owed is under $10,000.

Congress believes that the availability of installment agreements promotes voluntary compliance and that the Service should make it easier for taxpayers to enter into installment agreements.

Changes

Under certain conditions, the IRS' discretionary powers have been removed and the IRS is required to enter into an installment agreement when the taxpayer is an individual with an income tax liability.

- The taxpayer must not owe more than $10,000.
- Over the previous five years the taxpayer and/or his spouse, if the requested installment agreement is for a jointly filed return, cannot have failed to file an income tax return.
- Over the previous five years the taxpayer and/or his spouse, if the requested installment agreement is for a jointly filed return, cannot have failed to pay any income tax.
- Over the previous five years the taxpayer and/or his spouse, if the requested installment agreement is for a jointly filed return, cannot have entered into an installment agreement.

The taxpayer's absolute right to an installment agreement only applies if:

- The IRS determines that the taxpayer is unable to pay the liability in full when due.

- The taxpayer provides the IRS with requested financial information necessary to make such determination.
- The liability must be paid **in full** within three years.
- The taxpayer must agree to abide by the income tax laws while the agreement is in effect.

Q & A

Q When are these provisions effective?

A Upon enactment, July 22, 1998.

Section 3468 Prohibition on Requests to Taxpayers to Give Up Rights to Bring Actions

Background

Prior to the enactment of the IRS Restructuring and Reform Act of 1997, there were no restrictions on officers or employees of the federal government using their position of authority to persuade an unknowing and unrepresented taxpayer to waive his or her rights to bring civil action against the federal government or an officer or employee of the federal government.

Changes

The new law generally provides that an officer or employee of the federal government may not request a taxpayer to give up the right to sue any officer or employee of the federal government for any action taken in connection with the federal internal revenue laws unless: (1) the taxpayer has been sufficiently informed of his/her rights and the consequences of a waiver to those rights, or (2) if the taxpayer was competently assisted by an attorney or other representative.

Q & A

Q1 What are the specific references for this information?

A1 Act Sec. 3468

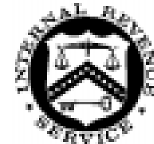
Q2 When does this go into effect?

A2 The act provided no specific date so the provision is considered effective as of July 22, 1998 (the date of enactment).

Q3 Are there situations where this rule will not apply?

A3 Yes, there are three specific exceptions.

- If the taxpayer knowingly and voluntarily gives up the right to sue.
- If the request is made by an IRS employee or officer in person and the taxpayer’s representative is present.
- If the request is made in writing to the taxpayer’s attorney or representative.



Section 3502 Explanation of Taxpayer's Rights in Interviews with the Internal Revenue Service

Background

Taxpayer's rights during interviews with the Internal Revenue Service are covered under Code Sec. 7521.

These rights are explained Part IV in IRS Publication 1 (Your Rights as a Taxpayer).

Taxpayer interview right's in a criminal investigation or relating to the integrity of a an IRS officer or employee are not covered under Code Sec. 7521.

Changes

The Publication 1 will be rewritten to clarify the taxpayer's rights.

The clarification will more clearly explain the taxpayer's rights:

- To be represented at interviews with the Internal Revenue Service by a representatives authorized to practice before the IRS.
- To suspend the interview pursuant to Code Sec. 7521(b)(2) which states that once the taxpayer indicates that the taxpayer wishes to consult with an attorney, accountant, enrolled agent, or any person permitted to practice before the IRS the interview must be suspended.

Q & A

Q Has there been a change or amendment in Code Sec. 7521 concerning the rights of a taxpayer during an interview?

A No, the provisions under this act call for clarifying the existing Code Sec 7521 in Publication 1. There is no change in the rights of the taxpayer.

Section 3506 Statements Regarding Installment Agreements

Background

Taxpayers wanting to satisfy their liabilities through an installment agreement (IRC 6159) must provide extensive financial background information.

An installment agreement is subject to review, modification, or termination by the IRS if the taxpayer meets the terms of the agreement.

IRS formerly had no obligation to provide the taxpayer with an annual accounting of the tax liability, how the payments were applied, and the remaining balance during the course of the agreement.

Changes

The IRS must provide the taxpayer and/or the taxpayer's representative with an annual statement with the following information:
- the taxpayer's beginning of the year balance
- all payments made during the year
- the remaining balance at the year's end

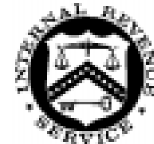
Q & A

Q1 When is this effective?

A1 No specific effective date is provided by the act, therefore it is presumed to be effective on the date of enactment, July 22, 1998.

Q2 What tax year are the statements to first go out on?

A2 The IRS must begin to provide the installment agreement statements no later than July 1, 2000.



Section 3601 Low-Income Taxpayer Clinics

Background

Some tax practitioner organizations and legal assistance clinics offer free or reduced rate assistance to taxpayers engaged in controversies with the IRS. In addition, some law, accounting and business schools programs allow students, under the supervision of an authorized tax practitioner, to represent taxpayers in administrative proceedings before the IRS. Many of these programs limit assistance to low income taxpayers. Congress wanted to increase the assistance available to low income taxpayers in controversies with the IRS in order to protect the rights of such taxpayers and ensure fair results.

Changes

Establishment of a matching grant fund for tax clinics that provide representatives for low-income or non-English speaking taxpayers.

Matching grants of up to $100,000 may be received by eligible clinics for the expansion, development or continuation of these type services.

The aggregate limit on the funds available for this project shall not exceed six million dollars annually, but will be "subject to the availability of funds" (Code Sec. 7526(a) as amended by the 1998 Act).

An eligible clinic can be a clinical program operated by:

- An accredited law school
- Business school
- Accounting school where students represent taxpayers
- Tax-exempt organizations that represent taxpayers before the Service or refer to outside qualified representatives, authorized to practice before the Internal Revenue Service.

Eligible clinics must:

- Operate on a nominal fee basis (not to include reimbursement of actual cost incurred)
- Represent low-income taxpayers in Internal Revenue disputes
- Offer programs for non-English speaking taxpayers that are designed to inform such individuals of their rights and responsibilities under the tax law.

Impact

The provisions in this act will allow low-income taxpayers to receive representation from tax professionals when engaged in controversies with the Internal Revenue Service. Also non-English speaking taxpayers can be informed about their rights and responsibilities under the tax laws.

Q & A

Q1 What is meant by "matching funds?"

A1 A clinic who receives funds under this program must match dollar for dollar the amount of the award provided.

Salaries of employees and the cost of equipment used in the clinic will be considered as matching dollars. Cost considered to be indirect expenses (example: overhead of the clinic's sponsoring organization) are not considered matching funds.

.

Q2 Must the clinic offer services to only low-income taxpayers?

A2 The client base of the clinic will meet this provision if 90% of the taxpayers they serve fall under the low-income definition.

Q3 What is the low-income definition?

A3 Income at or below 25% of the poverty level (Office of Management and Budget determination).

Section 3703 Payment of Taxes

Background

Currently, checks and money orders payable to the Internal Revenue Service may be used for payment of taxes .

Changes

The Act will allow payment of tax using checks and money orders made payable to the United States Treasury.

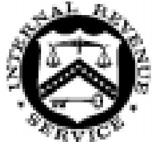
Q & A

Q1 I just mailed my 1998 estimated tax payment and it was payable to the Internal Revenue Service. Will the IRS cash it?

A1 Yes, the IRS will continue to accept checks and money orders made payable to the Internal Revenue Service.

Q2 When I pay my tax, to whom should I make my checks payable?

A2 Make checks payable to the United States Treasury.



Section 3705(a) IRS Employee Contacts

Background

Many notices sent by the Service do not contain an employee's name or a telephone number that can be contacted if the taxpayer has questions.

Changes

In order make the Internal Revenue Service more accessible to the taxpayer, the Service must:

- Include on all manually generated correspondence:
    - employee's name
    - unique identifying number
    - telephone number
- Provide during personal or telephone contact:
    - employee's name
    - unique identifying number
    - employee's name and telephone number must be "prominently disclosed" on correspondence
- Develop a system that allows a taxpayer to deal with a single employee

Impact

All employees will need a designated identifying number.

New procedures will need to be set in place to allow, to the greatest extent possible, the taxpayer to have deal with one employee from the beginning of the matter to resolution.

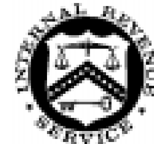
Taxpayers who have received correspondence and have questions will be able to reach the employee who issued the correspondence.

Q & A

Q1 What is meant by an unique identifying number?

A1 A unique identifying number is one that has been established by the Service for that employee.

Q2 What does prominently disclosed mean?



A2 It means that the name and number must be readily available, easy to notice. For a walk-in employee this may mean a name tag or desk sign, for a telephone assistor it may mean announcing your name and number at the beginning of the call, for correspondence it should be clearly written in a place on the correspondence that is not obscure.

Q3 My site has always required me to give an unique number along with my name, how is this different?

A3 Many local sites have established local procedures that may include provisions found in this section of the Act. You should continue to follow local procedures until your site issues new procedures.

Q4 When will these new provisions take place?

A4 Generally, these provisions take place 60 days after enactment,, the unique identifying number provision will be effective six months after enactment.

Q5 Will I be required to use my Social Security number as the unique identifying ?

A5 No, although your Social Security number is an unique identifying number, due to the Privacy Act , your Social Security number will not be used for this purpose.

Q6 What about my badge number?

A6 Your badge number is not a unique identifying number. When you leave the Service that number can be reassigned.

Section 3705(c) Telephone Helpline Options in Spanish

Background

Internal Revenue has instituted many programs to provide service to the taxpayer.

Toll-free sites are available six days a week and 16 hours a day

The Service offers recorded tax information and voice mail

Changes

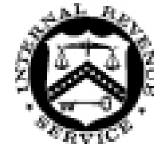
In order to meet the various needs of the diversified taxpaying public the Service will:

- Provide all Spanish speaking taxpayers reaching a call site the opportunity to have their questions answered in Spanish.
- Allow taxpayers calling within normal business hours the option to speak to an assistor in addition to other options.

Q & A

Q When will full service for Spanish speaking taxpayers be available on the Helpline?

A The effective date for the implementation of Act Section 3705(c) and (d) is January 1, 2000.



Section 3706 Use of Pseudonyms by IRS Employees

Background

An employee of the federal government could "register" a pseudonym (alternate name) with his/her supervisor. In order to register a pseudonym, an employee had to believe that the use of his/her unique name and/or the nature of the office location would allow identification of the employee.

Changes

The Act specifies that an IRS employee may use a pseudonym only if BOTH of the following apply:

- The employee must provide adequate justification for use of the pseudonym, such as personal safety, and
- Use of the pseudonym must be preapproved by the employee's supervisor.

Q & A

Q1 I have a pseudonym that is registered with my supervisor, may I continue to use that pseudonym?

A1 If that pseudonym was registered with your supervisor before the date of enactment, it has been "grandfathered in" and you may continue to use it.

Q2 What if I wish to use a pseudonym, but I didn't register with my supervisor before the date of enactment?

A2 The interim procedures established to implement Section 3706 should be followed by both non-bargaining and bargaining unit employees. The use of the interim procedures for bargaining unit employees has been approved by NTEU and will remain in effect until bargaining over final procedures is completed.

Q3 Why was this provision included in the Act?

A3 This provision was included to eliminate the perception that IRS employees were using pseudonyms in inappropriate circumstances.

Section 3707 Illegal Tax Protestor Designation

Background

Prior to enactment of the IRS Restructuring and Reform Act, individuals who met certain criteria were designated as illegal tax protestors. Individual Master Files for these individuals contained an illegal tax protestor designation.

Changes

The Act prohibits the IRS from designating taxpayers as illegal tax protestors or any similar designation.

Nonfiler designations are sill allowed in appropriate cases, but must be removed once the taxpayer has filed income tax returns for two consecutive years and paid all taxes on the returns.

The provision is effective on the date of enactment; however, removal of any illegal protestor designations from the Individual Master File is not required before January 1, 1999.

Q & A

Q Will this provision of the Act make any change to the potentially dangerous taxpayer (PDT) designation?

A No. Taxpayers who have made threats against IRS employees, have assaulted IRS employees, or who belong to a tax protestor group that advocates violence against IRS employees may be designated as potentially dangerous taxpayers. This designation remains unchanged under the Act.

Section 3709 Listing of Local IRS Telephone Numbers and Addresses

Background

The Internal Revenue Service generally does not list the phone number of local offices. Most telephone directories list only the 800 number, which does not always connect to a local office.

Changes

Service is now required to list the phone number and address of the local office.

The listing is not required to be published in more than one local directory.

Listings of local numbers in alternate language directories are permissible but not required.

Local listing are required as soon as possible.

Q & A

Q My area has many phone directories. Will the phone number and address be found in all of them?

A The phone number and address must be listed in at least one directory.

Section 3710 Identification of Return Preparers

Background

The IRC currently requires that any return or claim of refund contain the social security number of the return preparer.

Changes

The IRS is now authorized to approve alternatives to social security numbers to identify tax return preparers.

The provision is effective on the date of enactment.

Q & A

Q1 Why was this provision included in the Act?

A1 Congress was concerned that inappropriate use might be made of a return preparer's social security number.

Q2 Are income tax return preparers still required to furnish their social security numbers on returns prepared by them?

A2 Yes, the Act merely authorizes the IRS to accept alternative identification numbers. Until the IRS develops an alternative system, income tax return preparers must continue to furnish their social security numbers on all tax returns and claims for refund prepared by them.

Section 3711 Offset of Past-Due Legally Enforceable State Income Tax Obligations Against Overpayments

Background

IRC Section 6402 allows an overpayment to be applied to satisfy a taxpayer's past-due child support and debts owed to other Federal agencies.

Changes

IRC Section 6402 is amended to include past due legally enforceable state income tax debts. However, in order to offset a taxpayer's overpayment, the taxpayers federal return must show an address that is in the same state as the state requesting the offset.

Various notifications are required:

- The state must notify the IRS that a qualifying state income tax debt is owing.
- Upon offset the state will be notified of the taxpayer's name, TIN, address and amount collected.
- The taxpayer must be notified that an offset has taken place.

Q & A

Q1 What are the specific references for this information?

A1 Act Sec. 3711(a), (b), (c), (d) creates new subsection IRC 6402(e)

Q2 What is the effective date of this provision?

A2 The effective date is for refunds payable after Dec. 31, 1999.

Q3 What is the definition of a "Past due legally enforceable debt?"

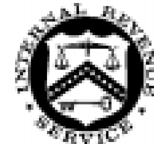
A3 A past due legally enforceable debt is:

- A debt which resulted from a court judgment that has determined the amount of state income tax due; or,
- A determination made after an administrative hearing which determined the amount of state income tax due; or,

- The result of a state income tax which has been assessed but not collected and has not been delinquent or more than ten years?

Q4 What is a definition of state income tax?

A4 State income tax is any local income tax administered by the chief tax administration agency of the state.



Section 5001 Elimination of 18-month Holding Period

Background

Under prior law, the lowest long term capital gains rates applied to capital assets held more than 18 months for sales and exchanges after July 28, 1997.

This created capital gains rules that were extremely hard to apply.

Changes

Effective for tax years ending after December 31, 1997, the 18-month holding period is eliminated.

The 10-percent, 20-percent, and/or 25-percent long term rates apply to most capital assets held more than 12 months.

Capital assets such as collectibles that are still subject to the maximum capital gains rate of 28-percent need only to be held more than 12 months.

Long term capital gain treatment is available for investments held more than 12 months, eliminating “mid-term gain.”

Q & A

Q1 I sold stock March 8, 1998, that I owned for 13 months. It was purchased before this new law. What is the most I can be taxed on this – 20% or 28%?

A1 The sale of the stock took place after December 31, 1997. The 12 month holding period for long term capital gains treatment is effective for tax years ending after December 3, 1997. The gain will be subject to a maximum 20 percent rate.

Q2 Last year the Form 1099-D and paper work I received for my mutual funds showed short term, midterm, and long-term gain. Every fund showed this differently. Will the same thing happen this year?

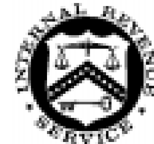
A2 It shouldn’t. Mid-term gain has been eliminated. Long term gains are those realized by the mutual funds after selling a capital gain asset held for more than 12 months.

Q3 It sounds as if the rate structure is close to what it was before the Taxpayer Relief Act of 1997. Is it that simple again?

A3 The rate structure is more complex than the earlier one. In addition to the maximum 10 percent, 15 percent, or 20 percent rates on most long-term capital gains, there are two major exceptions. The 25 percent rate continues to apply to gain on the sale of real estate attributable to depreciation. Gain on the sale of collectibles held more than 12 months is subject to a maximum 28 percent rate.

Q4 Will Schedule D of Form 1040 be as complicated as last year?

A4 The column for 28 percent rate gain or loss will be eliminated since long term treatment is applicable to capital assets held more than 12 months, and because the law is retroactive to sales after December 31, 1997. There will still be a tax computation section so that capital gains will be taxed at the maximum applicable rate.



Section 5002 Clarification of Exclusion of Meals for Certain Employees

Background

Generally, only 50% of business meals provided are currently deductible by the employer.

Meals that qualify as a de minimis fringe benefit are fully deductible.

Changes

Meals provided by the employer are fully deductible as a de minimis fringe benefit IF

- The meals are provided to employees on the employer's business premises in an employer-operated eating facility for employees, and
- More than half of the employees to whom meals are provided receive the meals for the convenience of the employer.

This does not include meals provided to highly compensated employees on a discriminatory basis. If more than half of the employees receiving meals on the premises receive them for the convenience of the employer, all of the meals are excludable from the employees income.

The provision is effective for tax years beginning on, before, or after the date of enactment.

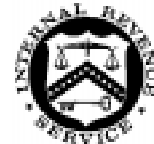
Q & A

Q1 My company serves dinner to 80 night shift employees in an employee cafeteria on its premises. The facts indicate that the meals are provided for the convenience of the company. Sixty day shift employees routinely stay for dinner which we provide as a bonus to them. Can the company deduct more than half the cost of their meals?

A1 Since more than half of the employees to whom the company provides meals in the employee cafeteria on the premises receive the meals for the company's convenience, all meals are fully deductible as a de minimis fringe benefit. The value of the meals will not be income to any employees.

Q2 The hospital where I work provides free meals to 50 employees at their cafeteria under facts that indicate they are provided for the convenience of the hospital. Fifty-two other employees, including myself, receive meals because we choose to eat there. The hospital says that since it can't deduct the full value of the meals as a de minimis fringe benefit, I have to report the value of the meals as income. Why? They say its because I eat there for my convenience, not theirs.

A2 In order for the hospital to fully deduct the value of your free meal as a de minimis fringe benefit, more than half of the employees to whom meals are provided must receive them for the employer's convenience. Since this is not the case, and since your meals are not specifically provided for the hospital's convenience, the value of the meals is fully included in your income.



Section 6003(a)(1) Child Credit Stacking Rules

Background

For 1998, taxpayers are entitled to a credit of up to $400 for each qualifying child under the age of 17. The credit is generally nonrefundable, but all or a portion may be refundable for a taxpayer with three or more qualifying children.

Nonrefundable credits cannot be used to reduce a taxpayer's tax liability below his or her tentative minimum tax. Special "Stacking Rules" are used to determine the order in which credits must be applied. They are as follows:

- Credit for Child and Dependent Care Expenses
- Credit for the Elderly or the Disabled
- Child Tax Credit
- Education Credits
- Adoption Credit
- Foreign Tax Credit
- Credit from Form 3800 (General Business Credit)
- Credit from Form 8396 (Mortgage Interest Credit)
- Credit from Form 8801 (Prior Year Minimum Tax)
- Credit from other forms
- Earned Income Credit
- Additional Child Tax Credit

Changes

The change clarifies that the refundable portion of the Child Credit (The Additional Credit) will be treated in the same manner as other refundable credits. Under the stacking rules, the order is nonrefundable credits without a carryforward, nonrefundable credits with a carryforward, and then refundable credits.

Q & A

Q1 What is the effective date of this provision?

A1 Tax years beginning after December 31, 1997

Q2 What are the specific references for this information?

A2 Act Sec. 6003(a), Code Sec. 24(d).

Q3 What is meant by "Stacking?"

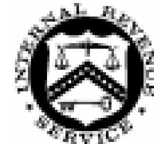
A3 "Stacking" is the order in which credits are applied.

Q4 What is the "Additional Credit?"

A4 The Additional Credit is the refundable portion of the child credit. It is allowable only if the taxpayer has 3 or more qualifying children.

Q5 Where can I find out more about the Child Credit?

A5 Publication 17



Section 6003(b) Coordination of Child and Supplemental Credit

Background

The Supplemental Credit was intended to be an additional part of the Child Credit.

The credit was intended to be computed on the Earned Income Credit worksheet.

The taxpayer's Earned Income Credit would be reduced by the amount of the supplemental Credit.

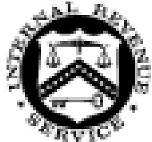
Changes

The Supplemental Credit is still included in the law. However, the Supplemental Credit will not be included in any of our forms, publications or instructions because there is not a tax benefit to the taxpayer since it only reduces a taxpayer's earned Income Credit dollar for dollar.

Q & A

Q Many taxpayers have already heard about the supplemental credit and will be calling us because they do not see it anywhere in the forms or instructions. What should I say?

A Advise taxpayers that since the new supplemental credit only reduced the amount of Earned Income Credit dollar for dollar, a decision was made to simplify things and remove all references to the supplemental credit from all forms, publications and instructions.



Section 6004(a) Reporting Requirements in Connection with Education Tax Credit

Background

As provided by the Taxpayer Relief Act of 1997, information returns have to be filed with the IRS by educational institutions that receive tuition and related expenses, and any person which, in the course of a trade or business, reimburses or refunds such expenses.

These institutions and persons must also provide statements to students and persons claiming them as dependents on or before January 31 of the year following the calendar year for which the information return is made.

Changes

Clarifies that IRC section 6050B requires institutions to report the total amount of payments made for each student for qualified tuition and related expenses without any amounts being subtracted for qualified scholarships or other tax-free educational assistance received with respect to the student.

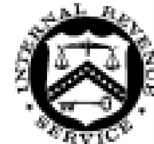
Requires that the amount of any grant received by the student for payment of costs of attendance and processed by the institution making the information return be reported as a separate item.

Clarifies that an institution must report only the total amount of reimbursements and refunds of qualified tuition and related expenses paid to a student by the institution (and not by any other party).

Clarifies that a person that is not an eligible educational institution is only required to file information returns if the person is in the trade or business of making reimbursements or refunds of qualified tuition and expenses to individuals *under an insurance arrangement.*

Impact

Until final regulations are adopted, no penalties will be imposed for failure to provide correct information returns or for failure to furnish correct statements to the required individuals. Even after final regulations are adopted, no penalties will be imposed for 1998 or 1999 if the institution made a good-faith effort to file information returns and to otherwise comply with Notice 98-46 and Notice 98-73.



Q & A

Q1 What is the effective date of this provision?

A1 This provision is effective for expenses paid in tax years after December 31, 1997, for education furnished in academic periods beginning after December 31, 1997.

Q2 What are the specific references for this information?

A2 IRC Section 6050S, as amended by Act Sec. 3712 and Act Sec. 6004. Act Sec. 6024 of the IRS Restructuring and Reform Act of 1998; Notice 97-73, 1997-51,16 IRB, and Notice 98-46 1998-36, IRB.

Q3 What form is used to report the payment of qualified tuition and expenses?

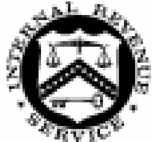
A3 Form 1098-T (Tuition Payments Statement).

Q4 If you are not an educational institution, can you be required to issue information returns?

A4 Only if you are in the trade or business of making reimbursements or refunds of qualified tuition and expenses to individuals *under an insurance arrangement.*

Q5 How can I find out more about tuition payments reporting requirements?

A5 See the 1998 Instructions for Form 1099, 1098, 5498, and W2-G for what a properly completed Form 1098-T must include. Also, see Notice 97-73, 1997-51, 16 IRB and Notice 98-46, 1998-36, IRB.



Section 6004(b)(1) Deduction For Student Loan Interest

Background

Beginning with the payments made in 1998, individuals may deduct interest paid during the tax year on any qualified education loan. A qualified education loan is any debt incurred to pay the qualified higher education expenses of the taxpayer, the taxpayer's spouse, or an individual who was the taxpayer's dependent at the time the debt was incurred. This includes refinancing of the debt. Debt owed to a related party is not deductible.

The maximum deductible interest amount is $1,000 in 1998. A deduction may be claimed only for the first sixty months in which interest payments are required. The original loan and all refinancings of the loan are treated as one loan for this purpose.

Changes

Clarifies that the debt must be incurred by the taxpayer solely to pay qualified higher education expenses.

Impact

Revolving lines of credit generally would not constitute qualified education loans unless the borrower agreed to use the line of credit to pay only qualifying education expenses.

The payer must be obligated for the debt under the loan agreement itself in order to be entitled to the deduction for student loan interest.

Q & A

Q1 What is the effective date of this provision?

A1 This provision applies to qualified education loans but only with respect to interest payments due and paid after December 31, 1997, and the portion of the 60-month period after December 31, 1997.

Q2 What are the specific references for this information?

A2 Act Sec. 6004(b)(1), amending Code Sec. 221(e)(1); Act Sec. 6004(b)(2), amending Code Sec. 221(d).

Q3 What are the maximum interest deductions for years after 1998?

A3 The maximum deductible amount of interest is $1,500 in 1999, $2,000 in 2000, and $2,500 in 2001 and thereafter.

Q4 Are there any deduction phase outs based on income?

A4 The amount of interest on a qualified education loan that may be deducted is phased out beginning at modified AGIs over $40,000 ($60,000 for joint filers), as adjusted for inflation after 2002.

Q5 Where can I find more information on student loan interest?

A5 Publication 17 and Publication 508.

Section 6004(c)(1) U.S. Savings Bonds Interest Exclusion

Background

Interest on certain U.S. savings bonds generally may be excluded from an individual's gross income if the individual redeems the bonds and uses the bond proceeds to pay for qualified higher education costs, at an eligible educational institution, for the individual, the individual's spouse, or the individual's dependents. The amount of excludable interest will be decreased if the bond proceeds are greater that the qualified higher education expenses paid during the year. Contributions of bond proceeds to a qualified state tuition program or to an education IRA are treated as payments of qualified higher education expenses.

The excludable amount is subject to phaseout at higher levels of modified AGI. Also, the expenses can be reduced by the amount of expenses used in computing the HOPE Scholarship or Lifetime Learning credits.

Changes

An "eligible educational institution" is now defined as an institution which includes accredited post secondary educational institutions offering credit toward a bachelor's degree, associate's degree, graduate or professional degree, or another recognized post secondary credential.

Provides that the expenses that are taken into account in determining the excludable amount of interest must be reduced by the amounts taken into account for the Education IRA, as well as the HOPE Scholarship, and/or the Lifetime Learning credit.

Impact

The definition of the term "eligible institution" now conforms with the definition used with respect to qualified state tuition programs and education IRAs.

Q & A

Q1 What is the effective date of this provision?

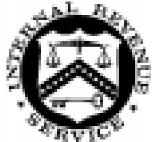
A1 The provision applies to tax years beginning after December 31, 1997.

Q2 What are the specific references for this provision?

A2 Act Sec. 6004(c)(1), amending Code Sec. 135 (c)(3), Act. Sec. 6004(d)(4), amending Code Sec. 135(d)(2), and Act. Sec. 6004(d)(9), amending Code Sec. 135 (c)(2)(C).

Q3 Where can I find out more about U.S. Bond Interest Exclusion?

A3 Publication 17, Publication 550, Publication 970, and Form 8815.



Section 6004(c)(2) and (3), 6004(d)(3)(B) Qualified State Tuition Programs

Background

These programs are generally exempt from tax. Distributions from the program are taxed under the annuity rules. Amounts in excess of contributions, i.e., earnings, are generally included in income unless excludable under another Code section. Earnings are included in the student's income if the distribution is used to pay education expenses. Earnings distributed that are not used to pay educational expenses are subject to a penalty and are included in the income of the distributee, i.e., the student or the account owner.

A change in beneficiaries is not treated as a distribution subject to tax as long as the new beneficiary is a member of the family of the previously designated beneficiary. Similar treatment applies to a distribution to a beneficiary that is rolled over within 60 days to the credit of a family member of the previously designated beneficiary.

Changes

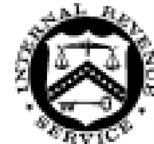
The technical correction clarifies that distributions are taxed as an annuity. Thus, distributions are treated as consisting of contributions that are generally not taxed and are recovered ratably over the period that distributions are made. The third Q and A illustrates how contributions are recovered ratably. The method used by the QSTP in calculating the earnings and contributions may differ from the illustration. For purposes of calculating earnings and contributions under Code Sec. 529, the account balance is valued at the end of the calendar year as required by Section 529(c)(3)(D)(iii).

The Act clarifies the definition of a family member to include the spouse of the original beneficiary. Thus, a member of the family with respect to any designated beneficiary includes:

1) the spouse of the beneficiary;
2) the son or daughter or a descendant of either; stepson or stepdaughter; brother, sister, stepbrother or stepsister; father or mother or ancestor of either; stepfather or stepmother; niece or nephew; aunt or uncle; son-in-law, daughter-in-law, father-in-law, mother-in-law, brother-in-law, or sister-in-law; and
3) a spouse of any of the individuals listed in (2) above.

Q & A

Q1 What is the effective date of this provision?



A1 This provision is effective on January 1, 1998.

Q2 What are the specific references for this information?

A2 Act Sec. 6004(c)(2), amending Code Sec. 529(c)(3)(A); Act Sec. 6004(c)(3), amending Code Sec. 529(e)(2); and Act Sec. 6004(d)(3)(B), adding Code Sec. 72(e)(9).

Q3 How are contributions recovered ratably?

A3 For example, the taxpayer is the beneficiary of a qualified state tuition program who receives a $2,000 distribution from the program to pay her qualified higher education expenses. On the close of the calendar year, the total account balance is $20,000, of which $15,000 represents contributions of principal and $5,000 represents earnings. The portion of the $2,000 distribution that is treated as a nontaxable return of contributions is $1,500 ($2,000 times ($15,000 divided by $20,000)).

Section 6004(d) Education Individual Retirement Accounts

Background

Education IRA's are used to accumulate funds for a designated beneficiary's qualified higher education expenses. Up to $500 of annual contributions per beneficiary may be made subject to a phase out that starts for joint filers with modified AGI of $150,000 and for others with MAGI of $95,000. Contributions to an Education IRA are not deductible.

Distributions are considered paid from taxed contributions and from earning on a pro rata basis. Earnings may be excludable if they are used to pay the beneficiary's qualified education expenses. If the expenses are at least as much as the aggregate from the education IRA, then no part of the distribution is includible in income.

A taxpayer who excludes a distribution from an Education IRA may not also claim the HOPE Scholarship credit or the Lifetime Learning credit in the same year.

Changes

A technical correction clarifies that the designated beneficiary of the IRA must be an *individual.*

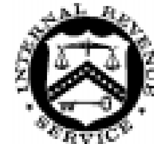
Clarifies that the new beneficiaries following a rollover of a distribution to another education IRA or a change in beneficiary must be under age 30 as of the date of such distribution or change.

Clarifies that the balance in an education IRA may be distributed to a named death beneficiary following the designated beneficiary's death.

Provides that the rule for survivors who acquire the original beneficiary's interest in an education IRA upon the beneficiary's death applies to the beneficiary's family members as well as to the beneficiary's spouse.

Clarifies that distributions from an education IRA are taxed under the annuity rules as an amount not received as an annuity.

Provides that *no* additional deduction or credit is allowed for expenses already used in the education IRA distribution exclusion.



The balance remaining in an education IRA must be distributed within 30 days after a beneficiary reaches age 30. This is in addition to the rule requiring distribution of the account balance within 30 days after the death of a beneficiary under age 30.

Distributions are treated as consisting of contributions which are generally not taxed and earnings which may be subject to tax on a pro rata basis, depending on the amount of qualified education expenses.

The 10-percent additional tax will not apply if the taxpayer elected to claim a HOPE Scholarship credit or Lifetime Learning credit instead of the education IRA exclusion.

The 10-percent additional tax also does not apply to certain distributions of excess contributions.

Q & A

Q1 What is the effective date of this provision?

A1 This provision applies to tax years beginning after December 31, 1997.

Q2 What are specific references for this information?

A2

Act Sec. 6004(d)(1)	amending Code Sec. 530(b)(1);
Act Sec. 6004(d)(2)	amending Code Sec. 530(b)(1)(E) and (d)(7) and adding Code Sec. 530(d)(8);
Act Sec. 6004(d)(3)	amending Code Sec. 530(d)(1) and 72(c)(9);
Act Sec. 6004(d)(6)	amending Code Sec. 530(d)(4)(B);
Act Sec. 6004(d)(4)	amending Code Sec. 135(d);
Act Sec. 6004(d)(5)	amending Code Sec. 530(d)(2);
Act Sec. 6004(d)(7)	amending Code Sec. 530(d)(4)(C);
Act Sec. 6004(d)(8)	amending Code Sec. 530(d)(5) and (6);
Act Sec. 6004(d)(10)	amending Code Sec. 4973(e)(1), striking Code Sec. 4973(e)(2)(B) and redesignating Code Sec. 4973(e)(2)(C) as (B).

Q3 How do you determine what portion of a distribution is treated as "paid from contributions?"

A3 You multiply the distribution by the ratio that the total amount of contributions bears to the total balance of the education IRA at the time the distribution is made.

Q4 Can you give me an example of that calculation?

A4 The taxpayer receives a $1,000 distribution. The total account balance on the distribution date is $10,000, of which $6,000 represents contributions and $4,000 represents earnings. The portion of the $1,000 distribution that is treated as a nontaxable return of contributions is $600 ($1,000 x ($6,000 divided by $10,000)).

Q5 What if the qualified higher education expenses are at least $1,000?

A5 Then the $400 portion of the distribution that represents earnings may also be excluded from income.

Q6 What if the qualified higher education expenses are only $750?

A6 Assuming the same facts as above, except for the expenses being $750, then only $300 of the $400 portion of the distribution from earnings may be excluded from income ($400 x ($750 divided by $1,000)). The remaining $100 must be included in income.

Q7 How does the education IRA impact the HOPE Scholarship credit, for example?

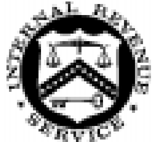
A7 A taxpayer who claims tax-favored treatment for education IRA distributions may not also claim the HOPE Scholarship credit or the Lifetime Learning credit in the same year.

Q8 What kind of penalties are imposed in connection with the education IRA accounts?

A8 A six percent excise tax may be imposed on excess contributions and an additional ten-percent tax imposed on distributions includible in income unless an exception applies.

Q9 Where can I get additional information related to education IRA's?

A9 Publication 17 and Publication 970 all have additional information in this area.



Section 6004(f) Cancellation of Student Loans

Background

An individual's gross income does not include forgiveness of student loans if the individual worked for a certain period of time in certain professions for any of a broad class of employers.

Loans by a tax-exempt organization to refinance such loans are also treated as student loans for this purpose. The work must be performed under the direction of a governmental entity or a tax-exempt organization and the student may not be employed by the lender.

Changes

Clarifies that the exclusion applies to discharge of loans made by certain tax-exempt organizations to refinance *any* existing student loan and not just loans made by educational organizations.

Clarifies that refinancing loans must be made under a program that requires the student to fulfill a requirement to work in occupations or areas with unmet needs.

Q & A

Q1 What is the effective date of this provision?

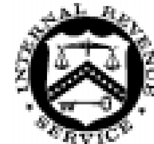
A1 This provision is applies to discharges after August 5, 1997.

Q2 What are the specific references for this information?

A2 Act Sec. 6004 (f)(1), amending Code Sec 108(f)(2); Act Sec. 6004(f)(2), amending Code Sec. 108(f)(3).

Q3 Where can I find out more about cancellation of student loans?

A3 Publication 17 and Publication 525.



Section 6004(g) Qualified Zone Academy Bond Credit

Background

Qualified zone academy bonds are bonds issued by a state or local government where a substantial portion of the funds raised are used to renovate, provide equipment to, develop course materials for, or train teachers and others at certain public schools that are located in empowerment zones or enterprise communities or that have a certain percentage of students from low-income families.

The credit is allowed to taxpayers holding a qualified zone academy bond on the credit allowance date, which is the anniversary of the issuance of the bond.

Changes

Clarifies that the credit may be claimed for corporate estimated tax purposes and is taken into account when determining whether a taxpayer has made an overpayment of tax.

Impact

The credit is includible in income as if it were an interest payment on the bond and may be claimed against regular income tax and AMT liability.

Q & A

Q1 What is the effective date of this provision?

A1 This provision is effective for obligations issued after December 31, 1997.

Q2 What are the specific references for this information?

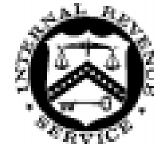
A2 Act Sec. 6004(g)(1), amending Act Sec. 226(a) of the Taxpayer Relief Act of 1997 (P.L.105-34); Act Sec 6004(g)(2), amending Code Sec 1397E(d)(4)(B); Act Sec. 6004(g)(3), adding Code Sec. 1397E(h); Act Sec. 6004(g)(4), amending Code Sec. 1397E(g); Act Sec. 6004(g)(5), amending Code Sec. 42(j)(4)(D); Act Sec. 6004(g)(6), amending Code Sec. 49(b)(4); Act Sec 6004(g)(7), amending Code Sec. 50(a)(5)(C).

Q3 How is the credit figured?

A3 The amount of the credit is equal to a credit rate set monthly by the IRS multiplied by the face amount of the bond.

Q4 Where can I find out more about the Qualified Zone Academy Bond Credit?

A4 Temporary Reg. Ss1.1397E-1T(a) and (b).



Section 6005(a) Deductible IRA Contribution Limits

Background

The $2,000 limit on deductible IRA contributions is gradually phased out for taxpayers filing a joint return who are eligible to participate in an employer plan.

For 1998 the phase-out range for joint filers is $50,000 to $60,000.

The $2,000 maximum deductible contribution for an individual who is not eligible to participate in an employer plan but whose spouse is eligible is $150,000 to $160,000.

Changes

The Restructuring Act clarifies that the phased-out dollar limitation for deductible IRA contributions applies whether a married individual or the individual's spouse is an active participant in an employer plan.

The Act further states that if the phase out rule applies to an individual solely because the individual's spouse is an active participant in an employer plan, the $2,000 maximum deductible IRA contribution for **that** individual is phased out if the adjusted gross income is between $150,000 and $160,000 (not $50,000 to $60,000).

Q & A

Q1 What is the effective date of this provision?

A1 This provision is in effect for tax years ending after December 31, 1997.

Q2 What are the specific references for this information?

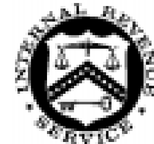
A2 Act Sec. 6005(a), amending Code Sec. 219(g)(1) and (7).

Q3 My husband is covered by a 401(K) plan. I am unemployed. We will file a joint return and our adjusted gross income is $120,000. Assuming all other qualifications are met, how much can I contribute and deduct?

A3 $2,000 because your AGI is below $150,000.

Q4 What if our AGI is $200,000?

A4 No deductible IRA contribution because adjusted gross income is over $160,000.



Section 6005(b)(1) and (9) Contribution Limit to Roth IRAs

Background

The Taxpayer Relief Act of 1997 stated that contributions to all of an individual's IRAs for a tax year could not exceed $2,000.

Changes

The Act clarifies that the maximum amount of contributions an individual may make to all IRAs is limited to a cumulative total of $2,000.

A simplified employee pension (SEP) or a SIMPLE IRA may not be designated as a Roth IRA.

Contributions to a SEP or SIMPLE IRA cannot be taken into account for purposes of the $2,000 contribution limit.

Q & A

Q1 I deposited $1,500 in a traditional IRA. How much can I put in my Roth IRA, assuming I meet all other requirements?

A1 $500

Q2 What are the specific references for this provision?

A2

Act Sec. 6005(b)(1)	amending Code Sec. 408A(c)(3)(A)
Act Sec. 6005(b)(8)(B)	amending Code Sec. 4973(b)
Act Sec. 6005(b)(9)	adding Code Sec. 408A(f)

Q3 What is the effective date of this Act Section?

A3 This provision is effective for tax years beginning after December 31, 1997.

Q4 I already have a SEP. Is my $2,000 yearly limit affected by my contributions to my SEP?

A4 No. The limitations for the Roth IRA are not impacted by the contributions to a SEP.

Section 6005(b)(2)(A) Clarification of Phase-Out Range

Background

The Taxpayer Relief Act of 1997 imposed phase-out limits. The $2,000 Roth IRA maximum contribution limit phase-out for married persons filing separately was intended to be $0 to $10,000, but this intent was not reflected in prior law.

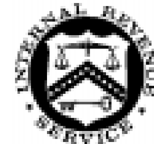
Changes

The IRS Restructuring and Reform Act of 1998 clarifies that the phase-out range for Roth IRA maximum contribution limit for a married person filing a separate return is AGI of $0 to $10,000.

Q & A

Q1 What is the effective date of this provision?

A1 The provision is effective for tax years beginning after December 31, 1997.



Section 6005(b)(2)(B) and (C)
Determination of AGI Limit for Conversions

Background

A taxpayer with modified adjusted gross income of $100,000 or less may convert a traditional IRA into a Roth IRA.

When determining whether the modified AGI threshold is exceeded, do not consider taxable amounts that result from converting to a Roth IRA.

Under the Taxpayer Relief Act of 1997, the deduction for a contribution to a traditional IRA was taken into account in determining modified AGI for the tax year.

Changes

The $100,000 modified AGI threshold for Roth IRA conversions is determined in the same manner as traditional IRAs, except taxable amounts that result from converting to a Roth IRA are not taken into account.

The deduction for a contribution to a traditional IRA is not taken into account.

For purposes of computing taxable income, the conversion amount is taken into account.

Q & A

Q1 To what year does the $100,000 threshold apply?

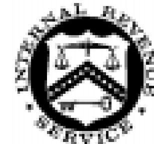
A1 The $100,000 modified AGI threshold applies for the year of the distribution to which the conversion relates.

Q2 What are the specific references for this provision?

A2 Act Sec. 6005(b)(2)(B) amending Code Sec. 408A(c)(3)(B)
Act Sec. 6005(b)(2)(C) amending Code Sec. 408A(c)(3)(C)(i).

Q3 Is the conversion amount taken into account for purposes of determining the $100,000 modified AGI threshold?

A3 No, only for purposes of computing taxable income.



Section 6005(b)(3)(A) Determination of Five-Year Holding Period

Background

Qualified distributions from a Roth IRA made after a 5-year taxable period are excludable from income.

The 5-year taxable period began with the first tax year for which an IRA contribution was made.

The 5-year taxable period for conversion contributions began with the taxable year in which the conversion contribution was made.

Changes

Under the Act, both regular Roth IRA contributions and conversion contributions are subject to a single 5-year taxable period.

The 5-year taxable period begins with the first taxable year for which a contribution is made to a Roth IRA.

The Act established the following ordering rules for amounts withdrawn from Roth IRAs that contain both conversion amounts and other contributions:

- Regular Roth IRA contributions
- Converted amounts (starting with amounts first converted that were included in income)
- Earnings

Q & A

Q1 How are multiple Roth IRAs treated?

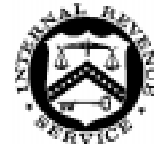
A1 For purposes of these rules, all Roth IRAs will be considered a single Roth IRA, even if they are maintained in separate accounts.

Q2 What is the effective date of this provision?

A2 These provisions are effective for tax years beginning after December 31, 1997.

Q3 What are the specific references for these provisions?

A3 Act Sec. 6005(b)(3)(A), amending Code Sec. 408A(d)(2)(B).
Act Sec. 6005(b)(5)(A), amending Code Sec. 408A(d)(4).



Section 6005(b)(4) IRA/Early Withdrawal of Converted Amounts

Background

A taxpayer with modified adjusted gross income of $100,000 or less may convert a traditional IRA into a Roth IRA.

The amount converted in 1998 is includable in income over a four-year period beginning in 1998. The four-year spread is mandatory, not elective.

The 10% additional tax on early withdrawals does not apply to conversions of traditional IRAs into Roth IRAs.

Changes

The four-year income spread is elective, not mandatory.

A taxpayer that withdraws converted amounts during the 4 year period will be required to include in income the amount otherwise includible under the four-year rule, plus the lesser of:

4) The amount of the withdrawal allocable to the 1998 conversion, or
5) The remaining taxable amount of the conversion.

The 10% additional tax on early withdrawals now applies to a Roth IRA distribution allocable to a conversion contribution as if that portion were includible in gross income, if the distribution is made within 5 taxable years of the conversion contribution. Hence, taxpayers under the age of 59-1/2 can no longer escape the 10% additional tax on early withdrawals by rolling over funds from a traditional IRA to a Roth IRA, and then immediately thereafter taking a distribution from the Roth IRA.

Q & A

Q1 When must the four-year spread election be made?

A1 By the due date for the first year of the income inclusion (including extension).

Q2 What is the effective date of this provision?

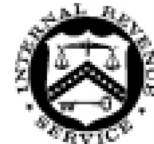
A2 Tax years beginning after December 31, 1997.

Q3 What are the specific references for this provision?

A3 Act Sec. 6005(b)(4)(A), amending Code Sec. 408A(d)(3)(A)(iii). Act Sec. 6005(b)(4)(B), adding Code Sec. 408A(d)(3)(E) and 408A(d)(3)(F). Act Sec. 6005(b)(6)(B).

Q4 Does the Taxpayer have to spread the income over a 4-year period?

A4 No, the Taxpayer can elect to have the entire amount converted included in income in the year of conversion.



Section 6005(b)(4)(B) Effect of Account Holder's Death During 4 Year Spread Period

Background

The Taxpayer Relief Act did not contain a specific rule in the event a taxpayer makes a conversion from a traditional IRA to a Roth IRA, and dies during the 4-year spread period for including the conversion amount in gross income.

Changes

Any amounts remaining to be included in income as a result of a 1998 conversion will be included in income in the final return of the deceased taxpayer.

If the surviving spouse is the sole beneficiary of the Roth IRA, the spouse may elect to continue the deferral by including the remaining amounts in his or her income over the remainder of the 4-year period.

Q & A

Ql My aunt converted a traditional IRA into a Roth IRA in 1998 and elected the four-year spread. She died in 2000. How is the remaining conversion amount reported?

A1 Any remaining amount will be reported on her final return for the year of death.

Q2 My spouse passed away before the four-year spread period was finished. Can I include the remaining amounts in my income over the remainder of the four-year period?

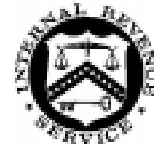
A2 Yes, you can make that election or report the entire remaining amount in the year of death on the final return.

Q3 What is the effective date of this provision?

A3 This provision is effective for tax years beginning after December 31, 1997.

Q4 What are the specific references for this provision?

A4 Act Sec. 6005(b)(4)(B), Adding Code Sec 408A(d)(3)(E)(ii).



Section 6005(b)(4)(G) Special Rule for Applying Section 72

Background

The Taxpayer Relief Act of 1997 did not provide a rule for imposing the additional 10 percent tax on early distributions under section 72 on conversion contributions distributed within a 5-taxable-year period beginning with the year the conversion contribution was made.

Changes

Under the IRS Restructuring and Reform Act of 1998, if any portion of a distribution is allocable to a conversion contribution, and such distribution is made within a 5-taxable-year period beginning with the taxable year the conversion contribution was made, then section 72 is applied as if that portion of the distribution were includible in gross income.

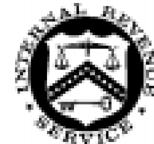
Section 6005(b)(5) Aggregation and Ordering Rules

Background

The Taxpayer Relief Act of 1997 did not provide specific aggregation and ordering rules for determining the taxability of a Roth IRA distribution.

Change

Under the IRS Restructuring and Reform Act of 1998, the taxability of a Roth IRA distribution is determined by: (1) treating all of an individual's Roth IRAs as one Roth IRA, and (2) treating the distribution as made from contributions, to the extent that the amount of the distribution, when added to all previous distributions, does not exceed the amount of aggregate contributions made to the Roth IRA. The distribution is treated as made first from regular Roth IRA contributions, and then from conversion contributions on a first-in, first-out basis.



Section 6005(b)(6) Taxpayer May Make Adjustments Before Due Date

Background

The Taxpayer Relief Act of 1997 did not provide a way for a taxpayer to adjust a conversion contribution that the taxpayer made to a Roth IRA before discovering that his or her modified adjusted gross income exceeds $100,000.

Change

Under the IRS Restructuring and Reform Act of 1998, a taxpayer may recharacterize a contribution by electing to transfer in a trustee-to-trustee transfer a contribution made to an IRA during such taxable year to another IRA by the due date (including extensions) of the taxpayer's return for the year of the contribution. The contribution is treated as having been made to the second IRA (and not the first IRA), provided that: (1) the contribution being transferred is accompanied by any net earnings allocable to it, and (2) no deduction is taken with respect to the contribution to the first IRA.

Q & A

Q1 What is the effective date of these provisions?

A1 These provision are effect for tax years beginning after December 31, 1997.

Q2 What are the specific references for these provisions?

A2 Act Sec. 6005(b)(6)(A). Act Sec. 6005(b)(7), adding Code Sec. 408A(d)(6) and 408A(d)(7).

Section 6005(c)(2) Eligible Rollover Distributions

Background

Generally, distributions received by an IRA owner before he or she reaches the age of 59-1/2 are subject to an additional 10% tax.

The 10% additional tax does not apply if certain exceptions are met, including:

6) IRA distributions used to pay qualified higher education expenses.
7) Up to $10,000 in qualified first time home buyers expenses.

The exception to the 10% additional tax do not apply to distributions (including hardship distributions), from employer sponsored plans.

Taxpayers could avoid the 10% additional tax by rolling over funds from a 401(k) or 403(b) plan into an IRA and then taking a distribution under the new law for higher education or first time home buyer expenses.

Changes

The Act provides that hardship distributions from 401(k) and 403(b) plans are not eligible rollover distributions and can not be rolled over into an IRA.

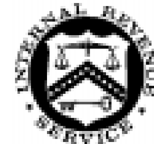
Q & A

Q1 What is the effective date of this provision?

A1 The effective date is for distributions occurring after December 31, 1998.

Q2 Will 401(k) and 403(b) hardship distributions be subject to the 20-percent withholding rate?

A2 No, the 20-percent withholding rate that is generally applicable to eligible rollover distributions that are not directly transferred to another plan or IRA does not apply.



Section 6005(d) Individual Capital Gains Rate Reductions

Background

Under the 1997 legislation, the rules for netting gains and losses from the various tax groups (20%, 25%, 28%) did not operate as Congress intended.

The 1997 legislation also failed to coordinate the new Code Section 1(h) with certain other provisions of the code.

Changes

The new legislation corrected and clarified the rules for netting capital gains and losses and coordinated the new IRC Section 1(h) with certain other provisions of the Code.

The netting procedure first requires netting within each group to reach a net gain or loss for the group.

Short-term capital losses (including carryovers) are applied first to reduce short-term capital gains.

A net short-term capital loss is first used to reduce net long-term capital loss from the 28-percent group, the 25-percent group, and then the 20-percent group.

Net long-term capital loss (including carryovers) from the 28-percent group is used first to reduce gain from the 25-percent group, then the 20-percent group.

Net loss from the 20-percent group is first used to reduce gain from the 28-percent group, then the 25-percent group,

Any net capital gain remaining that is in a particular rate group is taxed at that group's marginal rate.

The changes are retroactive to May 7, 1997.

Q & A

Q1 I have a long-term capital loss carryover of $5,000 from 1997. For 1998, I have a $500 short-term capital gain, $1,500 gain in the 28

percent group, $2,000 unrecaptured section 1250 gain, and $4,000 gain in the 20-percent group. How do I apply the loss?

A1 The loss is first applied to the gain in the 28 percent group, then the 25 percent unrecaptured section 1250 gain. The remaining $1,500 is applied to the gain in the 20% group. You will have $500 short-term capital gain and $2,500 long-term capital gain subject to 20-percent capital gains tax.

Q2 At the end of 1998, I had a short-term capital loss of $2,000, short-term capital gain of $600, a gain of $1,200 on the sale of collectibles that I held long-term, and a gain of $500 on stock that I held long-term. How is all this taxed?

A2 The $2,000 short-term loss is netted first against the short-term gain of $600. The remaining $1,400 is then used to reduce the gain from the collectibles. This leaves $200 to be applied to the $500 capital gain. The result is a net $300 long-term gain in the 20% group.

Q3 Our taxable income is $120,000, including a net capital gain of $90,000. Since we file jointly, that means our tax rate would have been 15% without the capital gains, so our capital gains are taxed at 10%, right?

A3 Assume we are using 1997 tax rates. Your assumption is not correct. The $30,000 of regular income is taxed at 15%. Of the adjustable net capital gain, $11,200 is taxed at 10% (the amount that would have been taxed at 15% if the maximum capital gains rate didn't exist). The remaining $78,800 of net capital gain is taxed at 20%, the maximum rate for adjusted net capital gain.

Q4 I have taxable income of $200,000, including net capital gain of $80,000. This net capital gain includes unrecaptured section 1250 gain of $20,000 and 28% rate gain of $15,000. How is this taxed?

A4 The unrecaptured section 1250 gain of $20,000 is taxed at 25%, the $15,000 of 28% rate gain is taxed at 28%, and the remaining

$45,000 of adjusted capital gain is taxed at 20%. The other $120,000 of your income is taxed at regular rates.

Q5 The only adjusted capital gains I have are $48 in capital gains distributions from my mutual fund. Why do I need to fill out a Schedule D?

A5 Schedule D needs to be filled out to insure that you pay no more tax than the law requires. Your capital gains distribution will be taxed at a lower rate than your marginal tax rate.

Section 6005(d)(2) Tentative Minimum Tax

Background

The 1997 legislation provided that the new capital gains rates would apply when computing an individual's alternative minimum taxable (AMT) liability.

Changes

The formula for computing the AMT on capital gains was reordered.

The rate ordering changed from:

1) 25% to 10%
- 10% to 20%, and
- 20% to 25%

Impact

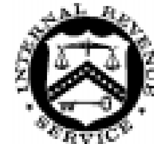
Even though net capital gains are subject to the lower capital gains tax rates when computing AMT, they are still fully includable in an individual's AMT income.

Taxpayers with large capital gains may be liable for AMT.

Q & A

Q What is the effective date for this change?

A The provision is effective for tax years after May 6, 1997.



Section 6005(e)(1) Sale or Exchange of Residence/Joint Returns

Background

Taxpayers who file joint returns may elect to exclude up to $500,000 for the sale or exchange of a personal residence sold after May 6, 1997 if:

- Either spouse owned the home for two of the last five years.
- Both spouses meet the two-year use test.
- Neither spouse is ineligible for the exclusion because he/she sold or exchanged a residence within the last two years.

Changes

If the $500,000 exclusion does not apply, the amount of the allowable exclusion will be the sum of the amount of the exclusion each spouse would have been entitled to if they had not been married.

Q & A

Q1 What is the effective date of this provision?

A1 The effective date of this provision is for sales/exchanges made after May, 6 1997

Q2 What are the specific references for this information?

A2 Act Sec. 6005(e)(1), amending IRC Section 121(b).

Q3 I got married in 1998. My spouse and I each owned a home. My spouse sold his/her home and we moved into mine eight months ago. We are planning on filing a joint return. Can we take up to $500,000 exclusion?

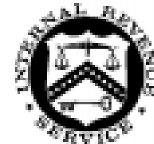
A3 No, since you will not meet the 2-year use test, the $500,000 exclusion does not apply. If your spouse meets the Section 121 requirements, up to $250,000 may be excluded.

Q4 My spouse and I each owned our own homes and did not live together before we got married in 1998. After we got married we each sold our homes. Do we qualify for the $500,000 exclusion?

A4 No, since you both do not satisfy the use requirements for the same home, the $500,000 exclusion does not apply. However, you will each be able to exclude up to the amount you would have each been entitled to if you were not married. If the requirements of Section 121 are met, gain up to $250,000 on each home may be excluded.

Q5 Where can I find more information on sale or exchange of personal residence?

A5 Publication 17, Publication 523 and Publication 530.



Section 6005(e)(2) Principal Residence/Exclusion Of Gain

Background

A taxpayer who sold or exchanged a personal residence on or after May 7, 1997, may exclude:

- Up to $250,000 of gain on the sale or exchange ($500,000 for certain joint returns), IF
- The taxpayer(s) owned and occupied the residence for at least two of the five years ending on the date of the sale or exchange.

A taxpayer is entitled to a reduced exclusion if the taxpayer:

- Fails to meed the ownership and use requirements, or
- Used the exclusion within the last 2 years and the sale or exchange is by reason of a change in health or employment.

Changes

The amendment clarified that is a taxpayer is entitled to a reduced exclusion, the excludable amount is based on the ***exclusion*** amount, not the ***realized gain*** amount.

Impact

Because the excludable amount is based on the exclusion rather than the gain amount, taxpayers may still not have any taxable gain on the sale or exchange.

Q & A

Q1 What are the specific references for this information?

A1 Act Sec. 6005(e)(2), amending IRC Section 121(c)(1).

Q2 How is the reduced exclusion calculated?

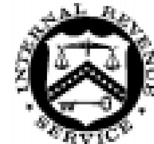
A2 The reduced exclusion is equal to the $250,000 or $500,000 exclusion (whichever applies) multiplied by the ration of:

- the shorter of:
  - the total periods that the property was owned and used as a principal residence during the five-year period ending on the date of the sale or exchange, or
  - the period after the date of the most recent prior sale or exchange to which the exclusion applied, over

2) two years (24 months).

Q3 Where can I find out more information regarding the sale or exchange of a personal residence?

A3 Publication 17, Publication 523 and Publication 530.



Section 6005(e)(3) Sale Or Exchange of Residence/Effective Date

Background

Taxpayers who sold their personal residence after May 6, 1997 may choose to apply the rules that applied to the sale/exchange of a personal residence sold before May 7, 1997 if:

- The home was sold before August 5, 1997, or
- After August 5, 1997 if a binding contract was in effect by August 5, 1997, or
- After August 5, 1997, if gain would not be recognized under the old sale of home rules because a replacement home was acquired on or before August 5, 1997 or a binding contract for the resident was in place on or before August 5, 1997.

Changes

A technical correction allows taxpayers to use the sale of home rules that applied to homes sold before May 7, 1997 on sales that took place **on** August 5, 1997, not just **before** August 5, 1997.

Impact

Taxpayers who sold or exchanged their home on August 5, 1997 and were required to use the new rules may want to consider amending their return if applying the old rules would be more favorable.

Q & A

Q1 What are the specific references for this information?

A1 Act Sec. 6005(e)(1), amending Sec. 312(d)(2) of the Taxpayer Relief Act of 1997.

Q2 I used the new rules because I sold my home on August 5th, 1997. What should I do?

A2 If it would be more beneficial for you to use the old rules, you must file an amended return by filing a form 1040X.

Q3 Where can I find more information on the sale of a personal residence?

A3 You can find more information on this topic in Publication 17, Publication 523 and Publication 530.

Section 6005(f) Rollover of Gain From Qualified Small Business Stock to Another Qualified Small Business Stock

Background

The 1997 legislation allowed an individual to elect to roll over gain realized from the sale of qualified stock if the stock is held by the individual for more than six months.

The gains may be rolled over into other small business stock, provided it is purchased during the 60 day period starting on the original sale date.

Changes

The Act replaces the word "individual" with the phrase "taxpayer other than a corporation."

This is effective for sales after August 5, 1997.

Impact

The Act makes clear that the rollover rule applies to certain partnerships and S Corporations.

The types of partners or stockholders the entity has is not limited.

Q & A

Q1 I am a partner in a partnership that has gain from the sale of qualified small business stock. I have been a partner the entire time the partnership held the stock. One of the other partners is a corporation. Is the partnership eligible for the tax free rollover provision?

A1 The partnership is eligible for the tax free rollover provision.

Q2 Will it flow through to the partners?

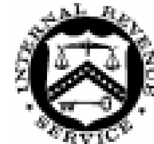
A2 The benefit will flow through to the noncorporate partners only.

Q3 What is the effective date for this provision?

A3 The provision applies to sales after August 5, 1997.

Q4 What are the specific references for this information?

A4 Act Sec. 6005(f), amending Code Sec. 1045(a) and Code Sec. 1045(b).



Section 6006(b) Accelerated Cost Recovery System

Background

For regular tax purposes, the 200 percent declining balance method may be used to calculate depreciation on certain short lived tangible property (e.g., cars, office furniture.)

For AMT purposes, property placed in service after December 31, 1998 had to be depreciated using the 150 percent declining balance method and the ADS class lives of Code Sec. 168(g).

Changes

Taxpayers can elect, for regular tax purposes, to depreciate tangible personal property that would otherwise qualify for the 200% declining balance method, by using the 150 percent declining balance method over the recovery period applicable for regular tax.

The election is irrevocable

The election applies to all property in the same class placed in service during the tax year of the election.

Impact

The need to make an AMT depreciation adjustment is eliminated.

Q & A

Q I'm buying a desk for my office in 1999. Do I have to depreciate it using different methods for my regular tax and AMT?

A No. You can make an irrevocable election to depreciate the desk by using the 150% declining balance method. This election must include all property in the same class placed in service in 1999.

Section 6008(a) Eligible Census Tracts

Background

Residents (business and individuals) of certain economically depressed census tracts within the District of Columbia are eligible for special tax incentives.

These census tracts are designated as the DC Enterprise Zone.

Changes

The determination of whether a census tract satisfies the applicable test is based on the 1990 census.

Impact

Data from the year 2000 census will not result in expansion or change in the DC Enterprise Zone.

Q & A

Q My street has really changed and in the 2000 census is sure to qualify as economically distressed. Will I get those special DC Enterprise Zone tax breaks then?

A No, If your census tract does not qualify based on 1990 data, there will be no change based on the 2000 census.

Section 6008(b) Qualified DC Zone Business

Background

A DC Zone business, for purposes of the zero-percent capital gains rate, is defined in a way that can be interpreted to mean only corporations and partnerships.

Changes

The definition of a DC Zone business has been clarified to include sole proprietors, corporations, and partnerships for purposes of the zero-percent capital gains rate.

Q & A

Q1 What was the effective date of this provision?

A1 The effective date of this provision is August 5, 1997.

Q2 I am a sole proprietor. Can I be considered a DC Zone business for purposes of the zero-percent capital gains rate?

A2 Yes, effective August 5, 1997, a sole proprietor can be a qualified DC zone business for the zero percent capital gains rate.

Section 6008(c) Zero-Percent Capital Gains Rate

Background

Certain qualified DC zone assets held for more than 5 years are subject to zero-percent capital gains rate.

In general the assets must be acquired after 1997 and before 2003.

There are special rules for property that was a qualified DC zone asset for a prior owner.

Only qualified capital gains attributable to the period from January 1, 1998 through December 31, 2007 are eligible.

Changes

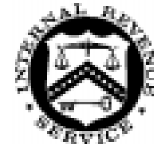
Property that is DC Zone business property and is acquired by a subsequent purchaser after January 1, 2003 can still qualify under the special rule.

The ending of the DC Enterprise Zone designation at the end of 2002 will not cause property to be ineligible for treatment as a qualified DC Zone asset for purposes of the zero-percent capital gains rate.

Q & A

Q I bought property in 1998 that is a qualified DC Zone asset. I plan to sell it in 2004. Since that is after the DC enterprise zone designation terminates, what capital gains rate will apply?

A Even though the DC enterprise zone designation terminates at the end of 2003, that by itself will not disqualify the property for purposes of the zero-percent capital gains rate. If all conditions are met, the capital gains rate will be zero-percent.



Section 6008(d) Homebuyer Credit

Background

First-time home buyers of a principal residence in the District of Columbia are eligible for a tax credit of up to $5,000 of the purchase price.

The residence must be purchased after August 4, 1997 and before January 1, 2001

The credit is phased out for individual taxpayers with AGI between $70,000 and $90,000 and joint filers with AGI between $110,000 and $130,000

Changes

The definition of first time homeowner is clarified.

The definition of purchase price is clarified.

The purchase date of a newly constructed residence is the date the taxpayer first occupies it.

The credit is a non-refundable personal credit claimed after the adoption credit and credit for interest on certain home mortgages.

The phaseout rules only apply in the year of the initial credit.

Provision is effective as of August 5, 1997.

Impact

The time requirement is based on when the taxpayer acquires title, not the contract date.

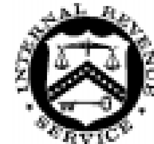
Q & A

Q1 I signed a purchase contract on August 1, 1997 on an otherwise qualified home. I took title on September 20, 1997. I meet all the qualifications for the District of Columbia first-time home buyers credit but am concerned about signing the contract before the law went into effect. Is there a problem?

A1 No, purchase date is when you acquired title, not when the contract was signed.

Q2 Do you re-apply the phaseout rules in subsequent years if the credit is carried forward?

A2 No, the phaseout of the credit for taxpayers above the specified AGI gross income levels applies only to the year the credit is generated.



Section 6009(c) Depreciation Limit for Electric Cars

Background

Limitations are placed on the annual depreciation that may be claimed on passenger cars used in business.

Annual depreciation limits are increased for vehicles primarily propelled by electricity placed in service after August 5, 1997, and before January 1, 2005.

Changes

Section 6009(c) clarifies that the maximum allowable deprecation amounts for electric cars is also increased in the years after the regular depreciation period.

Q & A

Q1 If I put an electric car in service in 1998 that has a basis of $50,000, what is the maximum annual depreciation allowable after the first three years of business use?

A1 For non-electric cars placed in service in 1998, the maximum allowable annual depreciation if $1,775 after the third year of business use. For electric cars, the rate is increased to $5,425.

Q2 What is the effective date for this provision?

A2 This provision applies to property placed in service after August 5,1997, and before January 1, 2005.

Q3 What are the specific references for this provision?

A3 Act Sec. 6009(c), amending Code Sec. 280f(a)(1)(C)(ii)

Section 6009(d) Montana Demonstration Project

Background

The 1997 law authorized a demonstration project between the IRS and the state of Montana to determine the feasibility and desirability of combined federal and state employment tax reporting.

Disclosure is limited to:
- taxpayer's name
- identification number
- signature

Implementation of the project was hindered by the fact that IRS was concerned that penalties for disclosure of information would apply.

Changes

The correction makes it clear that the usual restrictions regarding disclosure will not apply to information disclosed as part of the Montana Demonstration Project.

IRS employees who disclose information to the state of Montana as part of the demonstration project will not be subject to prosecution for unlawful disclosure.

Q & A

Q1 I am an IRS employee working with the state of Montana on the Montana Demonstration Project. Is it a disclosure violation to share taxpayer information with the state?

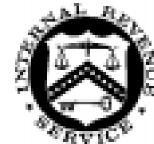
A1 No, but you may only disclose the taxpayer's name, identification number, and signature as part of the demonstration project. This is information common to the federal and state portions of the combined form.

Q2 What are the specific references for this provision?

A2 Act Sec. 6009(d), amending Code Sec. 6103(d)(5).

Q3 What is the effective date for this Act section?

A3 This provision is effective as of August 5, 1997.



Section 6010 Continuous Levies

Background

The IRS has the authority to issue a “continuous levy” on “specified payments” in order to collect unpaid taxes.

A continuous levy is one that would continually levy the taxpayer’s funds without further action.

Specified payments are:

- any Federal payments other than payments for which eligibility is based on the income or assets or both of a payee
- certain amounts that would otherwise be exempt from levy such as:
  - unemployment benefits
  - workers compensation benefits
  - wages
  - public assistance benefits
  - certain railroad annuity, pension, or unemployment benefits

The continuous levy applies to up to 15% of any specified payment including amounts otherwise exempt from levy.

Changes

Clarifies that a continuous levy is at the IRS’ discretion and must be specifically approved by an IRS group manager before the levy takes effect.

Q & A

Q1 If I levy once on the taxpayer’s bank account, does this mean that I have to have my manager’s approval before I can levy the bank account again?

A1 No. A bank levy is not a continuous levy. Each time bank funds are to be levied using Form 668-A, a separate levy must be issued, therefore it is not continuous. A wage levy using Form 668-W is one that continually levies the taxpayer’s funds until it is released and so would be termed a “continuous levy.”

Q2 When is this in effect?

A2 This provision applies to all levies issued after August 5, 1997. Since the Act was signed July 22, 1998, this provision is therefore retroactive.

Q3 Were all levy payments between August 15, 1997, and July 22, 1998, subject to the 15% limitation?

A3 No.

Q4 Should we do a search for those that were and refund any payments above 15%?

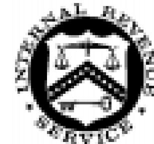
A4 No.

Q5 Since July 22, 1998, are Social Security benefits "specified payments" with respect to IRC 6331(h)?

A5 They are "specified payments" and have been since the Taxpayer Relief Act created IRC 6331(h). They **could** be levied under 6331(h), but no levies have been served that were designated as being under that Code provision and none will be until the computer match with the disbursing agency begins.

Q6 What is the proper approval process to make a Social Security levy a continuous levy?

A6 A 15% continuous levy under 6331(h) will be handled only in National Office.



Section 6010(p)(1) Earned Income Credit/Modified Adjusted Gross Income

Background

An eligible taxpayer with earned income which falls below a specified amount may qualify for a refundable earned income credit. The amount of the credit is determined by the taxpayer's:

- earned income
- modified adjusted gross income (MAGI)
- number of qualifying children

For purposes of the earned income credit, modified adjusted gross income is the taxpayer's adjusted gross income minus:

- Net capital loss (limited to $3,000)
- Net loss from trusts and estates
- Net loss related to nonbusiness rents and royalties
- For tax years beginning before 1998, 50 percent of net loss from trades or businesses determined separately with respect to:
  - Non-farming sole proprietorships
  - Farming sole proprietorships
  - Other trades or businesses
- For tax years beginning after 1997, 75 percent of net loss from trades or businesses determined separately with respect to:
  - Non-farming sole proprietorships
  - Farming sole proprietorships
  - Other trades or businesses
- For tax years beginning after 1997, tax exempt interest
- For tax years beginning after 1997, nontaxable distributions from pensions, annuities and IRAs (unless the distribution is a transfer or rollover distribution).

Changes

The Act clarifies that certain nontaxable amounts are added to AGI in determining MAGI.

Q & A

Q1 What is the effective date of this provision?

A1 Tax years beginning after December 31, 1997

Q2 What are the specific references for this information?

A2 Act Sec. 6010(p)(1), and 1085(b) and (d) of the Taxpayer Relief Act of 1997.

Q3 What is Modified Adjusted Gross Income (MAGI)?

A3 For EIC purposes, modified adjusted gross income in adjusted gross income increased by certain losses and certain nontaxable items. MAGI is computed differently for different purposes. This section discusses MAGI only as it relates to the earned income credit.

Q4 What is a Net Capital Loss for purposes of computing MAGI?

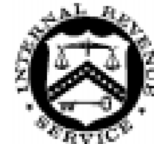
A4 A net capital loss is the excess of losses from sales or exchanges of capital assets over the gain from sales of capital assets, but limited to the amount of the capital loss deduction.

Q5 Are there any changes that affect how I assist a taxpayer on this issue?

A5 No, the Act only clarifies and reinforces things that we were already doing.

Q6 Where can I find out more about the earned income credit?

A6 You can find more information in Publication 17 and Publication 596.



Section 6012 Federal Employees on Temporary Duty Status

Background

Unreimbursed travel expenses while temporarily away from home for business are deductible. However, "temporary" is defined as being away for one year or less.

Changes

Travel expenses of federal employees who are traveling on temporary duty status in order to *prosecute* or to provide support services for the *prosecution* of a federal crime, as well as to investigate or to support the investigation of a federal crime, may be deductible even if they are away from home for more than one year.

Q & A

Q1 What is the effective date of this provision?

A1 The provision is effective for amounts paid or incurred with respect to tax years ending after August 5, 1997.

Q2 What are the specific references for this information?

A2 Act Sec. 6012(a), amending Code Sec. 162(a).

Q3 Are there any special certifications required?

A3 Yes, the travel must be certified by the Attorney General or his/her designee.

Q4 Where can I find additional information on travel expenses?

A4 Publication 17 and Publication 463 both have sections on travel expenses.

Section 6015(c) Police And Fire Department Employees/Disability Payments

Background

Certain payments received in 1989, 1990 or 1991 by full-time police or fire department employees or their survivors are treated as nontaxable compensation. The employee must have separated from service before July 1, 1992. The employee must have received the payments due to the state's workers compensation law that heart disease and hypertension are work-related illnesses.

Changes

The description of the state law to which the provision relates was clarified to be one that presumed work relatedness only for employees hired before July 1, 1992.

The exclusion was expanded to include amounts received by employees or their survivors who were eligible to receive payments under the following:

Any other statute, ordinance, labor agreement or similar provision received as a disability pension attributable to being a police officer or fire fighter but only if the employee was an individual referred to in the identified state law.

The normal statute of limitation to claim a refund does not apply if the claim was filed before August 5, 1998.

Q & A

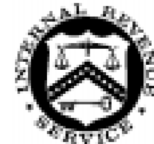
Q1 What is the effective date?

A1 August 5, 1997

Q2 What is the specific reference for this information?

A2 Act Sec. 6015(c)

Q3 Where can I find more information on workers compensation and disability payments?



A3 Publication 17, Publication 525 and Publication 575

Section 6018(f) Adoption Credit Carryovers

Background

Individuals may claim a nonrefundable adoption tax credit of up to $5,000 per child ($6,000 for a child with special needs) for qualified adoption expenses.

The credit is phased out for taxpayers with adjusted gross income between $75,000 and $115,000.

Code Sec. 26 generally limits the amount of nonrefundable credits that a taxpayer can claim to the amount by which his/her regular tax liability exceeds his/her tentative minimum tax liability.

Adoption expense credits not able to be used because of the Section 26 limit can be carried forward for up to five years. Any credit that cannot be used within five years is lost.

Changes

The phaseout of the adoption credit based on the taxpayer's AGI is applied without regard to any carryover of the credit.

Q & A

Q1 What is the effective date of this provision?

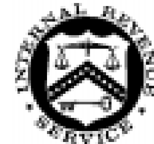
A1 Tax years after December 31, 1996

Q2 What are the specific references for this information?

A2 Act Sec. 6018(f)(1), IRC 23(b)(2)(A).

Q3 What are qualifying expenses?

A3 Qualifying expenses are reasonable and necessary adoption fees, court costs, attorney fees, traveling expenses and other expenses directly related to (and principally for) the legal adoption of an eligible child.



Q4 Can I claim the expenses for adopting my spouses child?

A4 No, a spouse's child is not a qualifying child.

Q5 What if I received money from the state or my employer to adopt the child?

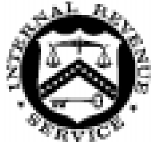
A5 You can not claim a credit for costs that you paid for with funds provided by your employer or by any state, federal or local program.

Q6 Where can I find more information on this subject?

A6 Publication 17, Publication 968, instructions for Form 8839.

Q7 How do I claim an amount that I am carrying over from a prior year?

A7 There is a worksheet in the instructions of Form 8839 for calculating out the amount of the carryover to claim on Form 8839.



Section 6019(c) Disclosure to Authorized Representatives of Divorced or Separated Spouses and of Persons Subject to the Trust Fund Recovery Penalty

Background

The Taxpayer Bill of Rights 2 provided authority to disclose tax return and return information to taxpayers subject to the Trust Fund Recovery Penalty and to taxpayers under certain circumstances with respect to joint returns.

If more than one person is liable for the Trust Fund Recovery Penalty, also known as the 100% Penalty, each person who actually paid the penalty is entitled to recover from the others who are liable for the penalty an amount equal to the excess of the amount paid by the person over the person's proportionate share of the penalty. Also, the IRS must disclose the names of the other taxpayers from whom it has attempted to collect the penalty. This disclosure was authorized only to a person determined to be a responsible person, and not the person's representative.

If a deficiency is assessed with respect to a joint return and the individuals who filed the return are divorced or no longer reside in the same household, the Service must disclose in writing certain information about the Service's collection activities with respect to the joint liability taken against the former spouse, to one of the former spouses, in response to a written request from the other former spouse. This disclosure authority provided for in Section 6103(e)(8) did not extend to the authorized representative of a former spouse.

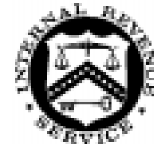
Changes

The IRS may now disclose information regarding other responsible persons, upon written request, to an attorney in fact who provides the IRS with written authorization from the responsible person.

A former spouse's representative may make a written request under Section 6103(e)(8) to obtain limited tax information regarding collection activity with respect to a joint liability.

Impact

The provision allowing for the disclosure of information to a responsible person's authorized representative is effective on the date of enactment.



The provision providing disclosure authority to an authorized representative of a divorced or separated spouse should have little impact because of existing disclosure authority allowing disclosure of tax information with respect to a joint return to either spouse or either spouse's authorized representative.

Q & A

Q1 What information can an authorized representative receive with respect to collection activity involving a joint liability?

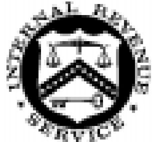
A1 If a specific request is made in writing referencing Section 6103(e)(8), the Service must disclose in writing whether or not the Service has attempted to collect the deficiency from the other former spouse; any amount collected from the other former spouse; the current collection status and if suspended, the reason. If a general written request is made by the taxpayer and/or the authorized representative, or an oral request is made, the Service should disclose those items of information described above, orally or in writing as appropriate under the circumstances.

Q2 What information can an authorized representative receive with respect to collection activity involving a Trust Fund Recovery Penalty?

A2 If a specific request is made in writing, the Service must disclose in writing:

- the name of any other person determined to be a responsible person with respect to the Trust Fund Recovery Penalty;
- whether the Service has attempted to collect from other responsible persons;
- the general nature of the collection activities;
- and the amount (if any) collected.

The Service cannot respond to an oral request under this provision.



Section 6020 Employer Social Security Credit

Background

Food and beverage establishments are eligible for a business tax credit for a portion of the employer social security taxes paid on employee tips.

The credit is classified as a general business credit.

Usually unused general business credits can only be carried forward 20 years (15 years if its origin was a tax year beginning before January 1, 1998).

Any unused carryforward was lost after the applicable period.

Changes

Any unused carryforward of the employer social security credit may be deducted the year after the expiration of the carry forward period.

Q & A

Q1 In 1996 the employer had an unused employer social security tax credit of $8,000. In 2011, the employer expects to have $3,000 in unused credit carry forward. How is this taken into account?

A1 The employer may claim a deduction in 2012 for $3,000, the full amount of the unused credit.

Q2 What is the effective date for this provision?

A2 This provision is effective for taxes paid after December 31, 1993.

Section 6021 Earned Income Credit Identification Rules

Background

In addition to other requirements for claiming the earned income credit, a taxpayer must provide:

- A valid social security number with no employment restrictions for the taxpayer and spouse.
- A valid social security number with no employment restrictions for each qualifying child.

The omission of a correct social security number is treated as a math error and the credit will be eliminated or reduced.

Changes

The Act clarifies that:

1) The identification requirements are separate from the definition of "eligible individual" and "qualifying child."
2) A taxpayer who has one or more qualifying children, but who does not identify them on Schedule EIC will not be allowed the earned income credit for taxpayers without a qualifying child.

Q & A

Q1 What are the effective dates of these provisions?

A1 The provision relating to the taxpayer and spouse is effective for returns due after September 21, 1996.

The provision relating to qualifying children is effective for tax years beginning after December 31, 1990.

Q2 What impact does this have on my work as a CSR?

A2 This was a technical correction only, and will not affect your job.

Section 7001 Clarification of Deduction for Deferred Compensation

Background

Vacation and severance pay is deductible by an employer in the year earned if it is paid to the employee within 2-1/2 months of the end of the tax year.

Vacation and severance payments made more than 2-1/2 months after the end of the tax year are considered deferred compensation and are not deductible in the year earned.

Changes

An employer may deduct vacation and severance pay in the year earned only if the employee actually received the pay on or before the day that is 2-1/2 months after the end of the tax year. The effect of the change is to limit an employer's ability to deduct accrued amounts for the year before the employee must report the income.

The provision is effective for tax years ending after July 22, 1998.

Any change in accounting method required by this provision does not require the advance consent of the IRS.

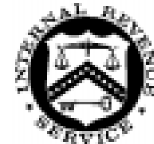
Q & A

Q1 At the end of 1998, my company has accrued vacation pay liability of $20,000. By March 10, 1999, the company issues a secured note to each employee for the employee's accrued vacation pay. The company will not actually pay the employee until after March 15, 1999. Can the company deduct the accrued vacation pay in 1998?

A1 Since the employees won't actually receive the accrued vacation pay by March 15, 1999, the company may not deduct it in 1998. It is considered deferred compensation.

Q2 How can we get the deduction for 1998 in the above situation?

A2 The employees must actually receive the payment on or before March 15, 1999.



Q3 What does "actually received" mean?

A3 "Actually Received" is not defined except by examples of what it does not mean. For example, securing an employer's promise with a letter of credit does not make the promised amount actually received by the employees. Nor does furnishing a note or letter or other evidence of indebtedness of the employer, even if it is guaranteed. Also, an amount set aside in a trust for employees is not considered to be actually received by the employees.

Q4 If the employer cannot claim the deduction, what effect does this have on the employee?

A4 This will not have any affect on when the employee must report the income.

Section 7004 AGI Limit and Minimum Required Distributions

Background

A taxpayer with modified adjusted gross income of $100,000 or less may convert a traditional IRA into a Roth IRA.

The $100,000 threshold amount includes amounts that are minimum required distributions from traditional IRAs or qualified plans.

Changes

For tax years beginning in 2005, the definition of modified AGI is amended to exclude minimum required distributions from the modified AGI threshold calculation for the purpose of determining eligibility to convert a traditional IRA to a Roth IRA.

Q & A

Q1 What is the effective date for this provision?

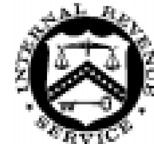
A1 For tax years beginning in 2005.

Q2 What are the specific references for this provision?

A2 Act Sec. 7004(a), amending Code Sec. 408A(c)(3)(C)(i).
Act Sec. 7004(b).

Q3 What impact will this Act section have on taxpayers over age 70-1/2?

A3 This change will allow more taxpayers to qualify for Roth IRA conversions since the amount of their required minimum distribution will not count toward the $100,000 modified AGI threshold.



Section 9010(a)(1) Exclusion for Transportation Fringe Benefits (Transportation Equity Act for the 21st Century)

Background

The value of qualified transportation fringe benefits provided to an employee is excluded from gross income and wages for income and employment tax purposes. Qualified transportation fringe benefits include transportation in a commuter highway vehicle if the transportation is in connection with travel between the employee's residence and place of employment (e.g. van pooling), a transit pass, or qualified parking.

Changes

After 1997, employers may generally offer employees a choice between cash and any qualified transportation fringe benefit without causing the employees to lose the exclusion for the qualified transportation benefit.

The maximum amount that is excludable for parking for 1998 is $175 per month. The other transportation fringe benefit exclusions cannot exceed a combined $65 per month in 1998.

The 1998 exclusion amounts were provided in Revenue Procedure 97-57.

Q & A

Q1 What is the effective date of this provision?

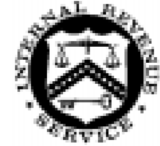
A1 The provision for choosing to take cash instead of transportation fringe benefits is effective for tax years beginning after December 31, 1997. The provision on increasing the base amounts for the exclusion for transportation benefits to $65 and $175 is effective for tax years beginning after December 31, 1997.

Q2 What are the specific references for this information?

A2 Act Sec. 9010 of the Transportation Equity Act for the 21st Century, amending Code Sec. 132; Section 1072 of the Taxpayer Relief Act of 1997, amending Code Sec. 132, and Rev. Proc. 97-57, 1997-52 IRB 20, for 1998 exclusions.

Q3 Where can I find out more about transportation fringe benefits?

A3 Transportation Equity Act for the 21st century; Publication 17, Publication 525, and Publication 535.



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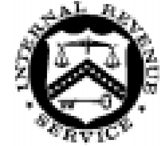

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