Recent Developments in Federal Income Taxation

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Shea Homes, Inc. v. Commissioner, 118 A.F.T.R.2d 2016-5593 (9th Cir. 8/24/16)

Outline: item A.1.a, page 4

- The taxpayer, a home builder engaged in developing planned residential communities:
  - Entered into contracts for the sale of houses and lots
  - Was obligated by contract and by state law to complete common improvements such as landscaping, parks and roads; this obligation was secured by performance bonds.
- The contracts were “home construction contracts” under § 460(e)(6), thus entitling the taxpayer to use the completed contract method of accounting
- Issue: is the subject matter of each sales contract only the house and lot, or instead the larger development?
- Held: The larger development, including amenities and common improvements.

Rev. Rul. 2016-15
2016-26 I.R.B. 1060 (6/10/16)
Outline: item A.1, page 7

- Issue: when may a real estate developer exclude cancellation of debt income under the qualified real property business indebtedness (QRPBI) exclusion in § 108(a)(1)(D)?
- Held:
  1. Indebtedness incurred or assumed in connection with property held as rental property qualifies as QRPBI because the property is depreciable.
  2. But property held for sale to customers is not depreciable, and therefore:
     - Indebtedness incurred or assumed in connection with property held for sale to customers is not QRPBI, and
     - Any cancellation of such debt is not excludable under the QRPBI exclusion.

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T.D. 9771
81 F.R. 37504 (7/26/16)
Outline: item A.2, page 7

- Final regulations under § 108 provide that, if debt of a grantor trust or disregarded entity is discharged, the determination whether the bankruptcy and insolvency exclusions apply is determined by looking to the owner.
  - For the bankruptcy exclusion to apply, the <u>owner</u> of the grantor trust or disregarded entity must be a debtor in bankruptcy.
  - For the insolvency exclusion to apply, the <u>owner</u> of the grantor trust or disregarded entity must be insolvent.
- If the owner of the grantor trust or disregarded entity is a partnership, these rules are applied at the <u>partner</u> level.
  - The <u>partners</u> must be insolvent or debtors in bankruptcy.

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Notice 2015-82
2015-50 I.R.B. 859 (11/24/15)
Outline: item B.2, page 8

- De minimis safe harbor in the 2013 final regulations on deduction and capitalization of expenditures related to tangible property. Reg. § 1.263(a)-1(f).
- The safe harbor permits a taxpayer to deduct currently, rather than capitalize, an amount paid for the acquisition or production of a unit of tangible property.
  - Must have a written accounting procedure
  - Must treat as an expense for financial accounting
  - The expense must not exceed a specified amount.
- Notice 2015-82 increases the specified amount for taxpayers *without* an applicable financial statement from $500 to $2,500.

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Brinks, Gilson & Lione P.C. v. Commissioner, T.C. Memo. 2016-20 (2/10/16)
Outline: item C.1, page 8

- The taxpayer, a law firm, zeroed out its book income each year with bonuses to the shareholder-attorneys.
- The taxpayer conceded that some of the compensation paid to shareholders was properly recharacterized as nondeductible dividends.
- Issue:
  - Can the taxpayer avoid accuracy-related penalties because it had either substantial authority for its position or had a reasonable basis for its position and acted in good faith?
- Held: No. Taxpayer had neither substantial authority nor a reasonable basis for its position.

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