

MEETINGS

Everyone welcome - Members, spouses, friends, non-members, subscribers, IRS & CDOR personnel and any other interested individuals!!

Your Board wants to see you!!! This month and in future months at our regularly scheduled dinner meetings. They are one of the best places to meet new members, share your ideas, learn new resources and actually have fun while earning CPE credits.

Reservations may be called into C.J. Whiteley at 303-819-3278 or email to cj.whiteley@comcast.net no later than the Sunday before the meeting.

No shows will be billed if a reservation is made.

DINNER MEETINGS

January 24, 2012

Meeting

Date: Tuesday, January 24, 2012

Time: 5:00 pm Board Meeting
6:00 pm Dinner
Meal-Jack Daniels
Craison Pork
7:00 pm Program

Place: Holiday Inn

Program: Overview of Cost Segregation

Speaker: Scott Zarret, KBKG Inc.

February 28, 2012

Meeting

Date: Tuesday, February 28, 2012

Time: 5:00 pm Board Meeting
6:00 pm Dinner
Meal-Honey Dijon Salmon
7:00 pm Program

Place: Holiday Inn

Program: Intro to IRS Appeals

Speaker: Linda S. Alden, IRS Appeals

Cost for Dinner & Program:

Members \$25.00
Non-members \$30.00
Program Only \$15.00

MAKE CHECKS PAYABLE TO CoSEA - **NO SHOWS WILL BE BILLED!**

MONTHLY MEETING LOCATION

Our meeting site is at the Holiday Inn at the Mousetrap. The address is 4849 Bannock Street, located northwest of the intersection of I-25 and I-70.

Here's how to get there: *Going east on I-70:* exit onto Pecos, go left (north) over the freeway to 48th Ave. Go right (east) to Bannock, turn left to 4849 Bannock. *Going west on I-70:* exit onto Pecos, turn right (north) to 48th, turn right (east) to Bannock, go left. *From I-25:* exit at 58th Ave., go west to 2nd light west of freeway, at Bannock, turn left (south).

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PRESIDENT'S MESSAGE

2012 – The New Year has started and tax season has arrived.



We had a great 2011. Your Board worked tirelessly to make the year a success. Two members are leaving the board. Jan Edwards, a director and Web Site Chair, did an excellent job of keeping our website up-to-date with our membership and other useful information. Debbie Lynn, Director and Program Chair, also did an excellent job of making our

monthly programs educational, with current topics and great speakers. I want to thank all of the members of the 2011 Board and Committees for their great work and efforts on behalf of CoSEA.

There are three new Board members for 2012. Already we are thinking of ways to expand our efforts to benefit CoSEA members. We look forward to having a very success 2012. Be a part of our ongoing success. Check out the last page and see if there is a committee that interests you and call the Chairperson to volunteer.

John Dundon and I went to the APEX meeting in Albuquerque, NM. We always get additional ideas for marketing, education, and member benefits. This year they did a section on social media. John was asked by the staff to give a presentation on his Blog.

Sponsors of CPE will have some new requirements. CoSEA will eventually be sending the list of attendees at our educational program/seminars directly to the IRS. These lists will include your name and PTIN. The sign in sheets and certificates will now ask for your PTIN number, so it is suggested that you keep the number with you when attending CPE programs.

Should you have suggestions or comments about the coming year, please contact a Board member. We look forward to working with all our members and making 2012 a grand year.

**HAPPY NEW YEAR!
HAVE A SUCCESSFUL TAX SEASON!**

Linda

Linda Ward, EA

linda13@lward.biz

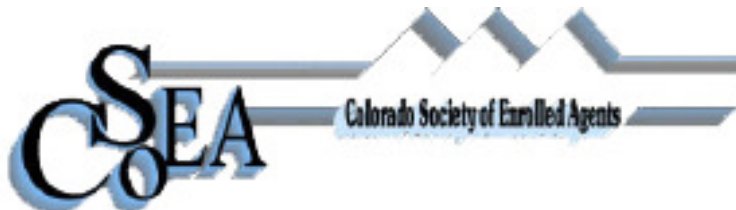
EA RENEWALS

If you are an EA with a SSN ending in 7, 8 or 9, now is the time to renew. The renewal period is from November 1, 2011- January 31, 2012. Use the online Form 8554 at www.pay.gov.

Pre-order the 2012 tax calendar now

The English version of the 2012 IRS Tax Calendar for Small Business and Self Employed, Publication 1518, will ship in late-November. The Spanish calendar (Pub 1518SP) will ship late-December.

Order on line (<http://www.irs.gov/businesses/small/article/0,,id=101169,00.html>) or call 1-800-829-3676.



Paul's Points to Ponder



We are trying out a slightly different format/layout of this newsletter. I would like to hear from the membership what your thoughts are – good, bad or indifferent. **I want to also welcome all of the new members who have joined in 2011. I hope you will find all of the benefits worthwhile and helpful.**

Other points I would like to mention [though not inclusive]:

1. Per the State of Colorado Department of Revenue, if you don't pay sales tax online, you must pay use tax with your 2011 Form 104 income tax return. See State Update (See page 8).
2. Last month's winners at the Dinner drawing:
 - a. Joe Coscia - \$25 gift certificate
 - b. Debbie Lynn – Free meeting dinner
3. Per November's dinner meeting with the IRS, PTIN numbers will be required for all sign-in sheets for all CPE classes starting January 1, 2012. Due to directions from OPR and RPO, attendance sheets must have signatures, printed name, and PTIN and EA #'s numbers. This information will be sent to RPO for their on-line database.
4. Remember, that returns filed for tax year 2011 in calendar year 2012 must be e-filed if you are filing 11 or more returns, with some exceptions.

5. There are several form changes – W-2, W-3, Form 1040, Schedule D, new Form 8938, Form 1099-K, Form 5884-B.
6. Those claiming the Earning Income Tax Credit **MUST** attach Form 8867 to the tax return.
7. I would like to especially thank John Dundon for his excellent article on Severance Payments [page 7] and thank Michael Merrion for his detailed analysis and article on this issue's tax question [pages 9 and 10]. Next issue, I will pick a less ambiguous question.

**HAVE A MERRY CHRISTMAS
AND A SAFE AND
HAPPY NEW YEAR**

Paul

You Are The Judge:

H and W Taxpayer file a joint return. In 2011 they purchased a rental property. Their attorney had them place the property in an LLC to protect them in the event of a lawsuit. Can the taxpayers report the rental activity on Schedule E of their Form 1040?

See the answer on page 8.

TAX AUDIT + APPEALS REPRESENTATION

John R. Dundon, Enrolled Agent 85353

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Have You Updated Your Profile Lately?

The details of your NAEA profile can impact whether you are matched with a potential new client. To update your profile, go to www.naea.org, log in (User name is your NAEA ID and password is your zip code) and click on “**View/Edit My Profile.**” You can change your login & password, see financial history, change your specialties and edit you contact information (click on “Edit” at bottom of screen). There you can change all your contact information and also enter a description of your practice in the “Supplementary Information” tab. In addition, please check and update your information on the Colorado website, go to www.taxproco.org. Use the same User name and password as for NAEA website.

Please send your updated contact information, *i.e.* addresses, phone numbers and/or e-mails to Richard Van Buren at (303) 660-2295 or email to rmvanb84@aol.com This will help your Board stay current and ensure that all notices, newsletters, etc. will be delivered to you in a timely manner. Please note that your newsletters are e-mailed to you by Joan Lipinski of Misteren Graphics, our printer. This is not spam, so please do not block this e-mail. As a Board we have been trying to stay on top of all changes submitted but would like your assistance in verifying that everything is correct for you.

The History of Enrolled Agents (E.A.)

By Robert Normandie
Upland, CA 91786

The history of Enrolled Agents dates back to 1884 when Congress authorized the Enabling Act of 1884, also known as the Horse Act of 1884. Congress recognized a need to regulate individuals representing citizens dealing with the Treasury Department about their claims against the U.S. This act gave the Secretary of the Treasury the authority to regulate who can represent these individuals.

Many people had claims for losses from the Civil War. The Treasury Department was being overwhelmed by some of the most dubious claims you can imagine. Horses were the number one reason for this act. It seemed as most of the horses in America were thoroughbreds. If the horses weren't thoroughbreds, then they were show horses. To make matters worse, there were more claims for horses than there were horses lost in the Civil War.

These comparisons weren't just limited to livestock. It seems as if suddenly and miraculously, everything turned from junk to perfection. Timber used for log cabins became milled black walnut. If it was made pot metal, it became disguised silver. Row boats were turned into yachts. And the claims became more and more ridiculous.

Congress recognized that a person wasn't making these claims, it was their agents who represented them. These agents would seek out people who might have a claim, right or wrong and for a percentage of what they could collect from the government, they would represent you. Most of these agents were confidence men or scam artists. Congress decided that these agents had to be regulated hence the Enabling Act of 1884. President Chester Arthur responded by signing the Act which was known as the

Horse Act of 1884. A standard was created, suitability checks, criminal records, moral character, all of these factors along with testing. The people who passed the requirements were known as Enrolled Agents.

Back in the 1880's, you didn't have to go to college or even graduate from high school to be a Doctor or Lawyer. You simply applied to the school of your choice and if accepted, off you went. No regulations. CPAs were non-existent. Again, because the standards for practice as an Attorney were so lax, they and CPAs, as they became evolved, were required to take and pass the enrolled agents exam, in order to practice before the IRS until 1936. Since 1965, with the strict State guidelines and regulations for members of the Bar & CPAs, the Treasury department automatically recognizes members of the Bar and legitimate CPAs.

Here is a interesting note concerning the E.A. exam. The exam was originally written by American Society of CPAs. It has become a controversy unto itself. The controversy is it's failure rate. Many critics think that the test was stacked so that very few would pass it regardless of their background. They are quick to point out that most CPAs would fail the test, lacking the necessary tax knowledge. When you look at the logic behind that, it may make sense. Eliminate the competition from the beginning. Some critics go as far to say they think there was collusion between the IRS and the CPA. IRS Agents, after a period of time in service are exempt from taking the test. Again the competition is eliminated. Regardless of whom you believe, the IRS is committed to make change, to make it fairer for all who take it.

In 1994, the initials E.A. were finally designated by the Treasury Department, as that of Enrolled Agent.

A Touch of Humor

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I want to join a armed group with little or no regard for the law... but the IRS isn't hiring.

=====

A businessman on his deathbed called his friend and said, "Bill, I want you to promise me that when I die you will have my remains cremated."

"And what," his friend asked, "Do you want me to do with your ashes?"

The businessman said, "Just put them in an envelope and mail them to the Internal Revenue Service and write on the envelope, "Now you have everything."

FEDERAL UPDATES

Continuing Education and Recordkeeping Requirements

By Irene Lawrence, EA

On June 3, the IRS issued its long-awaited revision of Circular 230. Most of the changes fall into three categories: the Return Preparer Office (RPO), a spin-off from the Office of Professional Responsibility (OPR); the introduction of Registered Tax Return Preparers (RTRPs) as practitioners governed by Circular 230; and changes in continuing education (CE) requirements for all, but especially for CE providers. This article will deal with the CE requirements mostly as they apply to us rank-and-file EAs, the consumers rather than the providers of continuing education.

A little background: in her remarks at the 2011 CSEA Super Seminars, OPR Director Karen Hawkins mentioned that OPR had been performing compliance checks on Enrolled Agents' continuing education, and that the EAs who were audited did not, in general, do particularly well in providing substantiation for the CE hours that they had claimed. Ms. Hawkins added that she personally thought that most of those EAs had indeed completed the hours they claimed, but their recordkeeping was not, to put it mildly, up to the usual EA standard of excellence.

With the spin-off of the new RPO to handle the administration of Circular 230 practitioners including the new RTRPs, OPR will be free to concentrate even more on ethical issues. It is only common sense to expect that in the future OPR will pay even more attention to CE compliance. Therefore, now might be a good time to check that our own recordkeeping is compliant and up to date.

First, a quick look at the changes as they affect us consumers of education:

We are now required to keep our records for four years (formerly three) from our date of renewal.

The CE provider (formerly, the "sponsor") is required to obtain a "continuing education provider number" and, for each program presented, a "continuing education provider program number." We as education consumers are required to keep a record of the program number (in addition to everything else).

As before, programs may be classes or self-study, face-to-face, written or electronic, and instructors may claim credit for preparation and teaching hours, although the maximum instruction credit hours allowed has been severely limited. However, practitioners may no longer claim CE credit for writing and publishing articles (such as this one).

As for the rest of the CE requirements, there has been no change in the CE hours required for renewal for EAs. To review, EAs must obtain 72 hours in the three-year cycle, with a minimum of 16 hours in any one year, and a minimum of two hours of ethics or professional conduct in each year. RTRPs, who apparently at this time must renew annually, must obtain 15 hours each year, including two hours of ethics or professional conduct and three hours of federal tax law updates. Every CE program for EAs and RTRPs must be a qualifying program "designed to enhance professional knowledge in Federal taxation or Federal tax related matters" and "be a qualifying continuing education program consistent with the Internal Revenue Code and effective tax

administration." Note that "Federal tax related matters" is usually construed to cover state taxes, but the issue does come up from time to time. Also note that Members and Associates of the California Society of Enrolled Agents and the National Association of Enrolled Agents are required to complete 30 hours of CE each year, although the "extra" hours may be in more peripheral subjects such as practice management.

The administrative requirements for a qualifying CE program also have not changed. They must include physical attendance and a qualified instructor/leader/speaker for "formal" programs, or registration and a measure of completion, usually an exam, for individual study programs; a certificate of completion; and written or electronic educational materials. Instructors can find their parallel requirements in §10.6(f)(2)(iii).

Once we have taken our qualifying courses, we have to keep substantiation — and that is where EAs have been weak. Again, the period is now four years following the date of renewal. Let's take as an example Emma Agent, EA, whose year of renewal is 2012. Her three-year period prior to renewal is 2009, 2010, and 2011. She completes all her required CE, distributed appropriately through the three years, and renews her enrollment in April 2012. She is required to keep her records from 2009, 2010, and 2011 until April 2016, four years after her renewal date of April 2012. Thus her oldest records may be seven years old before she may safely discard them.

RTRPs also must keep their substantiation for four years after renewal, but currently their renewals are annual rather than triennial. Thus an RTRP who renews in 2012 will have to keep until 2016 only substantiation for education claimed in 2011 and later.

Now, what information is Emma (and are we) required to keep? Our recordkeeping requirements are summarized in Circular 230, §10.6(h)(1). (Instructors can find their requirements in §10.6(h)(2).)

Recordkeeping Requirements:

- The name of the sponsoring organization;
- The location of the program;
- The title of the program;
- The qualified program number;
- A description of its content;
- Written outlines, course syllabi, textbook, and/or written or electronic materials provided or required for the course;
- The dates attended;
- The credit hours claimed;
- The name(s) of the instructor(s), discussion leader(s), or speaker(s), if appropriate; and
- The certificate of completion and/or signed statement of the hours of attendance obtained from the CE provider.

Customarily, this information is included on the Certificate of Completion that the provider issues. Presumably, providers will include the new program number on new versions of their certificates as the numbers begin to be required. Nevertheless, it is ultimately the practitioner's responsibility to keep all the required information—and find it again if audited!

FEDERAL UPDATES

Severance Payments and FICA Tax

Generally severance payments made to terminated employees have been held by the courts to be FICA wages mostly because the definition of “wages” for FICA purposes found in the Internal Revenue Code is so broad. “Wages” include all remuneration or money paid for employment with 23 listed statutory exceptions to the definition. However a Federal District Court case, *US v.*

Quality Stores, Inc. from the western district of Michigan provides a FICA exception for one small area of severance pay. Specifically, the federal court found a FICA exception for severance pay which constitutes “supplemental unemployment compensation benefits” within the meaning of [Section 3402\(o\) of the Internal Revenue Code](#) defined as amounts paid to an employee *because of an employee’s involuntary separation from employment resulting directly from a reduction in work force, the discontinuance of a plan or business operation.*

This one court decision should not be misconstrued as precedent by any means. Specifically what I am referring to is how we render advice as CoSEA members. In this particular example when you retire from employment your retirement is usually NOT considered involuntary and as such your severance pay is subject to FICA taxation presuming you have not hit the income threshold for the

tax year even if retirement is the consequence of workforce reduction. If you are advising taxpayers otherwise because of this one court decision it is imperative that you recognize the jurisdiction of the court in question as part of full disclosure when rendering an opinion. If not you are setting yourself up for a US Treasury Circular 230 complaint. Furthermore it is important to note that the IRS disagreed with the *Quality Stores* decision described above. On June 18, 2010, the IRS issued an opinion which refers to the *Quality Stores* decision by stating “the decision is not binding precedent,” and “the opinion runs counter to (a) Federal Circuit Court of Appeal’s 2008 decision.” From my perspective this means the IRS will dedicate resources to defending their position on this matter the next time a case like *Quality Stores* comes up. Basically most severance payments will more likely than not be subject to FICA tax.

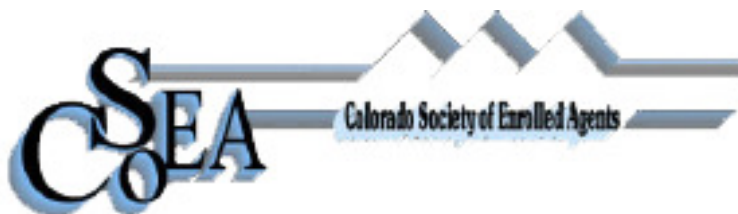
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Continuing Education and Recordkeeping Requirements *continued from page 5*

Because of the complexity and magnitude of the issues involved in setting up the RTRP program, the Treasury Department and the IRS have decided to delay implementing the continuing education program requirements for RTRPs for at least the first year of registration. But that doesn’t let EAs off the hook. The next time the Director of the Office of Professional Responsibility discusses EA educational compliance, let’s be the standard setters.

Irene Lawrence, EA, has her own practice, Lawrence Associates, now in Menlo Park, CA. Her tax specialties are personal income

taxes and expatriate taxes. She has been active in CSEA, first in the East Bay Chapter, then in the Mission Chapter, since she became an Enrolled Agent in 1987. She has served many years on the CSEA Ethics and Professional Conduct Committee, and was President of CSEA in 2006-2007. Her first career was as a teacher and professor; she holds a B.S. in mathematics from Stanford University, and a Ph.D. in theology and linguistics from the Graduate Theological Union in Berkeley, CA. She can be reached at irene@lawrencetax.com.



Visit our website at www.taxproco.org

FEDERAL UPDATES

THE NEW FORM 2848

POWER OF ATTORNEY AND DECLARATION OF REPRESENTATIVE

By EVAN S. GOLAR, EA, CPA

We are all aware that new model automobiles start rolling off the production line annually each September and the manufacturers begin their extensive new ad campaigns to promote their products. Their ads tend to make you feel you're not riding in style unless you're riding in the newest model.

Well guess what fellow EAs? Just after Thanksgiving 2011 – the Internal Revenue Service surprised us all by releasing a new version of Form 2848, circa October 2011.

Many critical changes have been made that Enrolled Agents should be aware of in order to not have rejected POA's when attempting to represent their clients before the Internal Revenue Service. They should be thought of in two distinct categories – changes to representative status and changes to form disclosure.

Changes to Representative Status

You need to keep in mind that the IRS will soon be granting Registered Tax Return Preparer licenses to those who qualify by passing an examination as well as obtaining a PTIN. The IRS has made provision for them in this new 2848 version. On P. 2, Part II – Declaration of Representative provides a new code – code “i” for Registered Tax Return Preparer – that briefly describes their status under section 10.4 of Circular 230 and highlights Notice 2011-6 for reference purposes. On page 2 of the 2848 instructions, there are three paragraphs of special rules for registered tax return preparers and unenrolled preparers.

There is also a new type of representative who is eligible to sign Form 2848. They are termed “student attorneys or student CPAs” – granted code “k”. In this case, the lead Attorney or CPA is also required to be listed as a representative. However, in the case of a POA by a student, the CAF record will be deleted 130 days after it is received whereas unless a POA is revoked earlier, CAF will generally delete POAs seven years after recording.

Changes to Form Disclosure

The very first item to be noticed is that previously there was line space for joint return filers to enter their respective names and Social Security Numbers. That is now history. The new version provides for only one name and only one Social Security Number – so joint filers must now prepare and sign their own separate POA. Although IRS has not disclosed the specific reason for it – it may be due to divorce/separation issues where the ex-spouses misuse or abuse the identification of the other.

In the Representative disclosure area, a checkbox has been provided to check if notices and communications are to be sent to the Representative. Up to two representatives may receive correspondence. If no box is checked, IRS does not mail correspondence. Also in this area a PTIN is requested. If no PTIN is assigned yet, you are to enter “Applied For”.

Line 3 – Matters – has some material new features.

Applicable matters now include Private Letter Rulings and Freedom of Information Act requests. If the tax form number or years/periods are not applicable, then you are to specifically describe the matter to which the POA pertains. Do not enter “Not Applicable”.

Line 5 – Acts Authorized – now has checkboxes to authorize a representative to perform acts not traditionally authorized by a 2848 form which include disclosure to third parties, signing a return, substitute or add representatives, or any other specific act the taxpayer wishes to authorize.

The IRS has not announced as of this writing, a specific date in which the prior 2848 version is no longer valid and the new version is required to be used. However, the IRS has created a page for Form 2848 and instructions at www.irs.gov/form2848 for posting future developments to the form.

Changes to Form 2848 (Rev. October 2011)

The IRS released a new version of Form 2848, *Power of Attorney*. Changes to the form include:

- Adding RTRP as a designation for limited practice before the IRS;
- No longer allowing joint return authorizations—authorizations are allowed for only one Taxpayer Identification Number and client signature;
- Requiring CPAs to indicate their CPA enrollment number for the state in which they are licensed to practice;

- Requiring practitioners to affirmatively select to be copied on client notices, if they choose to be;

- Eliminating the option to receive a client's refund check;
- Adding checkboxes to clearly authorize acts such as: disclosure of tax return information to third parties, practitioner authorization to sign a client return, and substituting or adding a representative.

It is recommended that practitioners file the new form to ensure proper processing.

STATE UPDATES

A reminder for Business owners with Colorado Tax Accounts, that each year, from October through December, Colorado sales tax and wage withholding coupon booklets [current calendar year 2011] are not available by mail to businesses because the Department of Revenue is in the process of preparing coupon booklets for the next year [2012].

Businesses can report tax and make payments at any time through Revenue Online at www.Colorado.gov/RevenueOnline even without a coupon booklet. To use Revenue Online, sign up to access your account. Then you may login to file and pay online and manage many aspects of your account, including making address changes, viewing payment and filing histories and filing protests.

If you cannot file through Revenue Online, you can download sales and wage withholding forms from the Colorado Web site.

Use Tax – Shoppers who take advantage of ‘Cyber Monday’ Internet sales on November 28th, or Green Monday or any other time, should remember to check receipts for sales tax charges and save those receipts where sales tax was not paid, so that they can pay consumer use tax. The Use tax for individuals on purchases made during 2011 is due by April 16, 2012.

When sales tax isn’t collected by the seller on a taxable item purchased from the Internet or mail order catalog, such as clothing, electronics, appliances or other tangible property, it is the purchaser’s responsibility to report and pay use tax. Colorado state use tax is 2.9 percent. Consumers should also be aware that some local special districts in Colorado have use tax.

Details about the tax may be found on the Colorado Taxation Consumer Use Tax Web page.

Apply for sales tax and withholding accounts online

New businesses can now apply for state sales and withholding accounts online through a consolidated, online service called [Colorado Business Express](#) (CBE). This service eliminates the need for new business owners to use paper forms to register separately with different state agencies. For the state tax accounts, the online service replaces the CR 0100 form.

Colorado Business Express leads applicants through the process of applying for a Colorado sales tax license, employee wage withholding account and/or an unemployment insurance account.

CBE reduces business registration processing time from hours or days to just minutes. In one transaction, this service consolidates business registration information required by multiple government departments and automatically updates state regulatory systems for the business filer.

The Colorado Department of Revenue, Department of Labor and Employment, Secretary of State, Statewide Internet Portal Authority and Colorado.gov all worked together to create Colorado Business Express.

The direct link to Colorado Business Express is www.Colorado.gov/ColoradoBusinessExpress

*Colorado Department of Revenue
Taxpayer Service Division*

Colorado Taxation Web Site: www.TaxColorado.com

Answer:

No, when a husband and wife establish an LLC for any reason, whether it is a trade or business or a rental activity, they are required to file Form 1065 ‘US Return of Partnership Income’, to report the income and expenses of the activity. Had they not placed the property into an LLC, they would have been able to elect out of partnership reporting and report the income and expenses of the rental on a separate Schedule E Form 1040 for each taxpayer. This treatment applies to jointly owned rental property. Co-ownership of rental property does not create a partnership for federal income tax purposes; however, electing out of partnership reporting is advisable. In addition, LLCs cannot elect out of partnership reporting, because the property is not owned by the co-owners. Instead it is owned by the LLC. Thus, a rental activity owned by an LLC with two members must be reported on a Form 1065 as a partnership. Due to questions which have arisen from this answer, Attorney Michael Merrion was kind enough to write a more detailed answer. Please see pages 9 and 10 for his excellent response.

COLORADO UPDATES

If you are not currently getting the Colorado Tax Professionals updates via email from the Taxpayer Service Division, you may sign up at tpspublicinfo@spike.dor.state.co.us and put SUBSCRIBE in the subject line.

You Are The Judge:

H and W Taxpayer file a joint return. In 2011 they purchased a rental property. Their attorney had them place the property in an LLC to protect them in the event of a lawsuit. Can the taxpayers report the rental activity on Schedule E of their Form 1040?

ALL RISE!

This question raises a number of collateral issues which are not readily apparent from the skeletal statement of facts, but which require some consideration when addressing the underlying issues.

Income from a rental property owned by one person is generally¹ reported on page 1 of Schedule E. The same is true if the rental property is owned by a husband and wife who elect to be treated as a single taxpayer by filing a joint return. However, if the property is owned by two or more persons who are not spouses, and who cannot therefore elect to file jointly, the reporting treatment depends upon the nature of the activity in the venture (addressed more fully below).

In the present case, however, the rental property is actually owned by the limited liability company which is, in turn, wholly owned by the spouses. This tiered ownership structure adds a level of complexity to the analysis. If only one spouse owned the entire LLC interest, then the LLC would be considered to be a “disregarded entity”² for tax purposes and the rental activity would still be reported on page 1 of the Schedule E. However, if the LLC is owned by two persons, it is not considered to be “disregarded” and the LLC would have a separate tax filing requirement. In that case, each “partner” would receive a form k-1, and the income from the venture (partnership) would be reported on page 2 of the taxpayers’ Schedule E.

But wait! What if the only owners of the LLC holding the rental property are spouses who elect to be treated as one taxpayer (by filing jointly). Are they entitled to any special consideration in determining whether the interests must be reported as a separate entity? Sadly, they are not. With one notable exception, an LLC owned by two persons, regardless of their relationship, is considered a separate entity for filing purposes.

With regard to the “notable exception” mentioned above, one should note that the above discussion assumes that the spouses are not living in a community property state. The IRS has acknowledged³ that spouses living in a community property state may elect to treat their co-ownership of a business entity formed under the laws of that state as a disregarded entity for federal tax purposes. In this limited instance, the spouses could elect to disregard the entity in the same manner as a sole member of an LLC in any other state, and report the income on page 1 of Schedule E.

That said, there are several provisions in the Code and Regulations that raise interesting possibilities and to which one might be drawn when counseling the taxpayers in this case. The tempting nature of these provisions warrant some additional discussion.

Anytime there is an association of persons engaged in an endeavor, and the participants have not taken the additional step of formalizing the terms of the venture, perhaps with formal organization (i.e., a corporation or LLC), or simply with a formal

document (partnership agreement, etc.), a certain amount of confusion must necessarily follow. It appears that the principal reason for the amount of confusion which typically accompanies an analysis of a client’s “joint venture” is the terminology itself. For tax purposes, the term “joint venture” has been defined as a “special combination of two or more persons, where in some specific venture a profit jointly sought without any actual partnership or corporation designation.”⁴ Thus, the tax compliance requirements which more naturally accompany the formal organization of a corporation or LLC, or even the imposition of a simple partnership agreement, become more obscure when dealing with a joint venture, or even mere co-ownership of property.

Under the “check-the-box” regulations⁵, the default classification of a joint venture is a partnership. It is encouraging, however, that those regulations also acknowledge that mere co-ownership of property does not necessarily create a separate entity. Something more is needed to raise the ownership to the level of a reporting partnership. For example, mere cost sharing arrangements, or even co-ownership of property that is maintained, kept in good repair and rented does not constitute a separate entity for tax reporting purposes. But if the venture is a trade or business, or is a co-ownership venture which also provides services in connection with a mere rental activity (whether directly or through an agent), the venture assumes the mantle of a reporting entity. The problem in the case before us, is that there is no co-ownership of the rental property. It is clearly wholly owned by the LLC. The co-ownership is of the LLC, which is treated in much the same manner as that of co-ownership of a corporation.⁶

Another tempting provision is contained in IRC §761(a), which provides a definition of what constitutes a partnership for federal tax filing purposes (including a “joint venture”), and also provides that members of an unincorporated organization may elect out of Subchapter K (partnership reporting requirements) in three limited instances,⁷ one of which arises where the venture is availed of for investment purposes only, and not for the active conduct of a business. This election requires⁸ that the co-owners (1) own the property as co-owners, (2) reserve the right separately to take or dispose of their shares of any property acquired or retained, and (3) do not actively conduct business (whether directly or through an agent). Again, the co-ownership requirement limits the application of the provision in this instance. The use of a state recognized entity such as a corporation or LLC⁹ disqualifies the taxpayer from using this provision.¹⁰

There has also been some confusion regarding the application of the “Qualified Joint Venture” (“QJV”) rules of IRC §761(f) which became effective for tax years beginning after 12/31/2006 and which allow a husband and wife to report a jointly owned trade or business on separate schedule C’s¹¹ rather than having to a separate file partnership return. This election is only available where (1) the only members of the joint venture are a husband and wife, (2) both spouses materially participate (within the meaning of IRC §469(h), i.e., the “passive activity rules”), and (3) both spouses elect the treatment. It also requires that the spouses be conducting a trade or business: mere joint ownership of property does not qualify for the election.¹² In addition, the election to be treated as a QJV is not available when the venture is held in the name of a state law entity such as a partnership or LLC.¹³

You Are the Judge *continued from page 9*

Thus, unless the owners elect some other entity classification under the “check-the-box” regulations, the spouses in our case will be required to file a partnership return for the LLC and each report their share of the financial activity of the LLC on page two of their joint Schedule E.

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(Footnotes)

¹ Presumably, if the amount of rent related activity rises to the level of a trade or business, even rental income would be seen to be a trade or business, reportable on schedule C and subject to SE tax.

² See Treas. Reg. 301.7701-2(c)(2)(i).

³ See Rev. Proc. 2002-69, 2002-2 CB 831 (10/9/2002).

⁴ See *Haley v. Commissioner*, 203 F.2d 815, 818 (C.A. 5, 1953);

Aiken Mills v. United States, 144 F.2d 23 (C.A. 4, 1944);

Tompkins v. Commissioner, 97 F.2d 396 (C.A. 4, 1938).

⁵ See Treas. Reg. 301.7701-1(a)(2).

⁶ One sees this argument particularly in connection with like kind exchanges under IRC §1031, in cases where the “partners” wish to liquidate the property and some want to utilize the §1031 deferrals, while others just want to “cash-out.” This is a problem as the like-kind exchange can only be accomplished by the owner (i.e., the LLC) and will impact all of the partners in the same manner.

⁷ We will ignore the other two instances where taxpayers can elect out of Subchapter K, as they are not relevant to this discussion.

⁸ See Treas. Reg. 1.761-2(a)(2).

⁹ An LLC owned by more than one person is treated as an “other business entity” pursuant to Treas. Reg. 301.7701-2(c), i.e., not a corporation and not a disregarded entity for tax purposes.

¹⁰ Treas. Reg. 1.761-2(a)(1) specifically excludes from this election out of Subchapter K “Any syndicate, group, pool, or joint venture which is classifiable as an association, or any group operating under an agreement which creates an organization classifiable as an association.”

¹¹ There is an additional collateral issue if QJV spouses elect to treat rental properties as QJV’s. Since they are, in essence, taking the position that the activity constitutes a business reportable on schedule C, the question arises as to whether the net rental income is then taxable for self-employment purposes. In a 2008 Chief Counsel Advice (CCA 200816030, 4/18/2008), the IRS, deferring to IRC §1402(a)(1), has clarified that if income is otherwise excludible from net earnings from self-employment under §1402(a), the election of QJV status does not convert such income to net earnings from self-employment.

¹² See CCS 200816030, *Ibid*.

¹³ See page 2 of the 2010 instructions for form 1065.

CONGRATULATIONS TO JANEEN RYAN, EA

The Internal Revenue Service announced the selection of seven new members to the Internal Revenue Service Advisory Council (IRSAC), which provides an organized public forum for IRS officials and representatives of the public to discuss key tax administration issues. Members are selected to represent the tax-paying public, tax professionals, small and large businesses, and the payroll community. The council provides the IRS commissioner and division leadership with important feedback, observations and suggestions. IRSAC members generally serve three-year terms with a possible one-year extension. The seven new members will join 17 returning members in 2012.

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| 8:15 – 9:05 | Federal Tax Updates | Gerry Malmberg (IRS) |
| 9:05 – 9:15 | Break | |
| 9:15 – 11:00 | Ethics | Mike Merrion |
| 11:00 – 11:55 | Colorado Tax Updates | Deb Towers (EA) |
| 12:00 – 1:00 | Lunch | |
| 1:00 – 2:50 | EFile and Eservices | Terry Donoghue (IRS) |
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NOTE FROM THE PROGRAM COMMITTEE:

Beginning immediately, the first request for reservations to our monthly meetings will be sent out no later than the 2nd Friday before the meeting. A second request will be sent out no later than the Wednesday before the meeting. The Program Committee asks that all reservations be received no later than the Sunday before the meeting. When we receive reservations late - or not at all, the hotel staff does not have ample time to set up an appropriate meeting room and, in addition, the chef needs to know how many meals to prepare.

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Thank You – Program Committee

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What Interests You? Know a Speaker?

The Program Committee needs your suggestions on topics and speakers.

Contact C.J. Whiteley at 303-819-3278 or email her at cj.whiteley@comcast.net

ANNOUNCEMENTS AND ACTIVITIES

NAEA recently added a toll free number. Of course, you can continue using the 202-822-6232 main line, but now you can also call 855 880 6232. All of the extensions work the same. For your convenience, here's a listing of staff and NAEA contact information. It's also posted on NAEA website under About NAEA, Staff Listing.

Executive Office:

Michael S. Nelson, CAE, Executive Vice President; mnelson@naea.org; Extension: 101

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Sam Matlick, CAE, Deputy Director; smatlick@naea.org; Extension: 106
Tori Martin, Assistant Director of Membership; tmartin@naea.org; Extension: 110
Clarise Diggs, Membership Coordinator; cdiggs@naea.org; Extension: 103
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By Paul Matonis, EA

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| <i>Client Tax Tools Series</i> Client Booklets (30 pack) | Quantity | Price | Cost |
|---|----------|----------------------|------|
| Pocket Calendars | x | \$48 \$41 | = \$ |
| Donation Trackers | x | \$48 \$41 | = \$ |
| Social Security/Medicare | x | \$48 \$41 | = \$ |

| STEP 2 Total Quantity and Cost Columns | | | |
|---|----------|------------|----------|
| Total Quantity of All Items | A | Total Cost | B |

Calculate Your Quantity Discount Here

| STEP 3 Calculate Quantity Discount (Total Quantity × Quantity Discount Per Item) | | | | | | | |
|---|----------------------------|--------------|--------------|--------------|--------------|--------------|-------------------|
| Total Quantity of All Items (from STEP 2) | Quantity Discount Per Item | | | | | | Quantity Discount |
| | 1 Item | 2 Items | 3-5 Items | 6-10 Items | 11-20 Items | 21+ Items | |
| (items) × | \$0.00/ item | \$3.00/ item | \$4.00/ item | \$5.00/ item | \$6.00/ item | \$7.00/ item | = \$ C |

| STEP 4 Calculate Shipping & Handling Charge (Total Quantity × S&H Charge Per Item) | | | | | | | |
|---|---|--------------|--------------|--------------|--------------|--------------|-----------------------------|
| Total Quantity of All Items (from STEP 2) | Shipping & Handling (S&H) Charge Per Item | | | | | | Shipping & Handling Charge* |
| | 1 Item | 2 Items | 3-5 Items | 6-10 Items | 11-20 Items | 21+ Items | |
| (items) × | \$5.75/ item | \$4.75/ item | \$4.25/ item | \$3.75/ item | \$3.25/ item | \$2.25/ item | = \$ D |

*Exclude *The Tax Library* Products. Please call for international orders.

| STEP 5 Calculate Order Cost (Total Cost - Quantity Discount + S&H Charge) | | | | | |
|--|---|---------------------------------|---|--|--------------|
| Total Cost (from STEP 2) | - | Quantity Discount (from STEP 3) | + | Shipping & Handling Charge (from STEP 4) | = Order Cost |
| B | - | C | + | D | = \$ |

| STEP 6 Finalize Your Order | | |
|-----------------------------------|--|------|
| Sales Tax | MN residents add 7.275% (Order Cost from STEP 5 × 0.07275) | = \$ |
| Order Total | Order Cost (from STEP 5) + Sales Tax | = \$ |

2011 ORDER FORM

MAIL CODE
265

Customer # _____

Company Name _____

Name _____

Address _____
(If P.O. Box, please include physical address)

City, State, Zip _____

Email _____
(Needed for order and shipping confirmation)

Day Phone _____ Billing Zip _____
(If different, needed for credit card orders)

PAYMENT OPTIONS Remember to include credit card number & expiration date.

Credit Card: MasterCard Discover Visa American Express

Expiration Date _____

3-Digit Security Code (optional) _____
AmEx (4 digits)

Your credit card will be charged separately for each shipment.

Cardholder's Signature _____
 Check or Money Order payable to: Tax Materials, Inc.

Orders are shipped first-in, first-out *starting* on the start ship date of the product.

Tax Materials, Inc.
Tax Materials, Inc.
15105 Minnetonka Ind. Rd.
Suite 221
Minnetonka, MN 55345

www.thetaxbook.com
Email: info@thetaxbook.com
Toll Free: 866-919-5277
Local: 952-746-5276
Fax: 952-746-5278

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