

Federal Tax Policy To Watch In The 2nd Half Of 2020

By Joshua Rosenberg

Law360 (July 13, 2020, 7:29 PM EDT) -- While the legislative agenda for the second six months of 2020 will likely be defined by the COVID-19 pandemic and the political limitations historically associated with election years, the Internal Revenue Service is poised to finalize guidance with long-term implications.

Here, Law360 takes a look at federal regulatory and legislative tax developments that appear in store for the year's second half.

COVID-19 Relief Redux

Individuals and businesses will be looking to Congress to see what relief measures it might pass in light of the pandemic and its economic fallout.

Congress passed the Coronavirus Aid, Relief and Economic Security Act in March, providing stimulus checks of \$1,200 to individual taxpayers and \$2,400 to couples filing joint tax returns, subject to income caps.

For individuals suffering from the economic fallout of the novel coronavirus, which causes the respiratory illness COVID-19, that federal assistance was indispensable, Steven Rosenthal, senior fellow at the Urban-Brookings Tax Policy Center, told Law360.

But with the virus spiking across the country, Congress should consider the question of "what's next?" as its focus of attention, Rosenthal said.

Congress was "effective at getting money out the door and into the economy, but did they get the money out sensibly?" Rosenthal said.

"What are we going to do come July, August and into the fall, when there are going to be additional amounts that we need to spend on really deserving individuals: people who are without jobs and perhaps without food and shelter," Rosenthal said. "How are they going to help them get by?"

Lawmakers hope to reach a compromise on COVID-19 relief measures in July, given that the expanded unemployment insurance enacted earlier this year expires at the end of the month and Congress typically adjourns in August.

Proposals on the table include passing refundable tax incentives for both businesses and workers, a tourism tax incentive and a payroll tax cut, which would go beyond and possibly supersede a payroll tax deferral enacted in the CARES Act. That deferral allows businesses to remit 2020 payroll levies in two installments in 2021 and 2022.

One issue businesses hope to see clarified is whether the relief the government provided under the Paycheck Protection Program, per the CARES Act, is tax-deductible. The Internal Revenue Service has issued guidance concluding that businesses may not take deductions for qualified expenses covered by PPP loans, including wages, rent, mortgage interest, employees' health care benefits and utilities.

But some lawmakers, including Senate Finance Committee Chairman Chuck Grassley, R-Iowa, and the committee's ranking member, Sen. Ron Wyden, D-Ore., sent a letter to Treasury Secretary Steven Mnuchin arguing that the IRS' notice was contrary to lawmakers' intent in exempting loan forgiveness from income.

Wyden, Grassley and others later introduced the Small Business Expense Protection Act, or S.B. 3612, which would ensure that Paycheck Protection Program loan recipients can deduct their business expenses, even if their loans are forgiven, to reflect the lawmakers' original intent, they said.

Deductibility of Penalties

Companies and their legal representatives await final guidance from the IRS on the deductibility of fines and penalties levied by government authorities.

The IRS recently proposed regulations on changes made by the 2017 Tax Cuts and Jobs Act to Internal Revenue Code Section 162(f), which addresses the deductibility of fines and penalties. The TCJA required that tax-deductible fines under the statute be reported to the IRS.

The IRS rules address the TCJA's stipulation that companies may not deduct penalties imposed by federal, state or local governments except those considered restitution or paid in order to achieve compliance with the law.

To qualify for those exceptions, both the businesses and government authorities involved would need to identify, in court orders or settlement agreements, which payments meet those standards. At that point, the government entities would report the determinations to the IRS, which has the capacity to challenge those characterizations.

As the IRS receives comments on the proposed rules, tax practitioners and their clients will be looking to see how the agency responds to them, according to S. Starling Marshall, a partner in Crowell & Moring LLP's tax and litigation groups.

"I'll be interested to see if the IRS makes any changes to those proposed regulations based on comments, and I think that'll be something for companies to watch," she said.

Final Carbon Capture Rules

Practitioners and environmental groups will be looking to see in finalized guidance whether the IRS provides more details on how companies will be judged when submitting life cycle assessments.

Carbon capture and sequestration is a process by which carbon oxides are seized at the point of emission — at power plants, for example — and then permanently stored, or sequestered, deep underground in saline reservoirs or in oil and gas fields. The aim is to reduce atmospheric greenhouse gases that contribute to climate change.

In recently proposed rules, the IRS definitively prescribed which avenues could be used to demonstrate secure geological storage for the purposes of Internal Revenue Code Section 45Q, which provides for a tax credit of up to \$50 per metric ton of carbon captured in qualified facilities. For the first time, the rules also provided details on when the credit could be recaptured.

The agency proposed a five-year recapture period, which would be in line with credits for renewable energy projects such as those in wind and solar energy.

Those proposed regulations will prove helpful in moving capital off the sidelines and into carbon capture projects, Peter Connors, a tax partner at Orrick Herrington & Sutcliffe LLP, told Law360. But he's looking forward to final regulations from the agency that could provide clarity on the life cycle assessment component of the regulations required for so-called utilized carbon, that used to create products. Specifically, practitioners are looking for guidance on the extent to which the life cycle analyses they'd submit would need to demonstrate the amount of atmospheric carbon mitigated by the use process.

For now, the IRS is accepting comments on how it can standardize the life cycle analysis process.

Cryptocurrency Information Reporting

Practitioners will be watching for IRS guidance on cryptocurrencies to address questions about compliance, including the calculation of basis, valuation and information reporting.

In a 2014 notice, the agency established the principle that cryptocurrencies should be treated as property for tax purposes. In 2019, the agency released a revenue ruling and frequently asked questions that said the splitting of a cryptocurrency blockchain under a so-called hard fork does not create taxable income if no new cryptocurrency is received, but that taxable income is generated by so-called airdrops. A hard fork occurs when the distributed ledger underlying a cryptocurrency is altered, resulting in a split from the former ledger; an airdrop, in contrast, delivers new coins and doesn't result in a split.

The agency later released cryptocurrency guidance on the treatment of hard forks and airdrops. Nevertheless, the IRS is aware that virtual currency users and tax practitioners have additional questions that need to be addressed, IRS Chief Counsel Michael Desmond said at a conference hosted by the Tax Policy Center in Washington, D.C., in 2019.

To that end, the agency has been composing additional guidance on cryptocurrencies to address questions about compliance, including the calculation of basis, valuation and information reporting, Desmond said.

Desmond and Internal Revenue Commissioner Chuck Rettig "are really interested in" and "focused on" the subject, said Marshall, of Crowell & Moring,

"There has been talk about some information reporting regulations that might be coming out," Marshall said. "That's something that could come out in the second half of the year."

--Additional reporting by Alan K. Ota. Editing by John Oudens and Joyce Laskowski.

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