Pilla Talks Taxes

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New Guidance On PPP Loans

IRS Issues Rulings on When Expenses Paid with PPP Loans Are Deductible

In the June 2020 issue of *PTT*, I covered the topic of whether business expenses paid with the proceeds of a Paycheck Protection Program (PPP) loan were tax deductible. There was—and still is—a great deal of confusion about this issue. I analyzed at length the reason for the confusion in the June issue of this newsletter. I will not revisit the debate here, except to say that I stand by my discussion, particularly in light of recent IRS guidance on the matter, which I discuss below.

As we approach the end of the year, with most businesses closing out their 2020 income and expense statements, it is vitally important to understand the rules for deducting expenses paid with PPP loans.

IRS ISSUES GUIDANCE

To help with this matter and to hammer home the points I made in the June article, the IRS has issued two specific guidance statements. The first is Revenue Ruling (Rev. Rul.) 2020-27, effective December 7, 2020; and the second is Revenue Procedure (Rev. Proc.) 2020-51, effective December 7, 2020. I address both statements here.

The Revenue Ruling. The Rev. Rul. expresses the IRS's position on the law as to whether business expenses paid with PPP loan proceeds are tax deductible. The IRS's position, as set forth in detail in the June article, is that such expenses are not deductible. The

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reason is that the law generally provides that otherwise deductible expenses paid with tax-exempt proceeds are in fact not tax deductible.

In the case of PPP loans, if one uses the proceeds to pay the qualified expenses for which the loan was intended, the loan is forgiven. We know that loan proceeds are tax-free in the first place. But the CARES Act further provides that forgiveness of a PPP loan expressly does not create a taxable event, as ordinarily would occur when a typical loan is forgiven. See my discussion of this in the June 2020 issue of *PTT*.

The Rev. Rul. goes even a step further in arguing why the payment of business expenses with PPP loans is not deductible. The IRS persuasively argues that a person with a "reasonable expectation" that his PPP loan will be forgiven is not entitled to a deduction for the business expenses paid with the loan proceeds. See: Rev. Rul. 2020-27, Analysis, pg 6.

We have two potential scenarios under which otherwise deductible business expenses paid with PPP loans are not deductible. In the first scenario, the taxpayer uses 100% of his PPP proceeds expressly as required by the CARES Act. In November 2020, he applies to the lender for forgiveness of his PPP loan. At the time of applying for the loan, he met all the requirements of law in order to have the loan forgiven. As of the end of 2020, the taxpayer has not been notified by the lender whether the loan will be forgiven.

In scenario 2, the taxpayer's facts are the same as above, except that he did not apply for forgiveness of his PPP loan before the end of 2020. However, the taxpayer in scenario 2, just as in scenario 1, meets all the legal requires to have his loan forgiven. Because of that, he intends to, and in fact will apply for forgiveness in 2021.

Both taxpayers in these scenarios have a reasonable expectation that their loans will be forgiven. In fact, because they meet all the requirements of the CARES Act and subsequent legislation regarding the use of PPP loans, forgiveness of the loans is entirely predictable; that is to say, forgiveness is "reasonably foreseeable." Because of that (and for other reasons), the Rev. Rul. declares that the business expenses paid by the taxpayers in each scenario "are not deductible…" See: Rev. Rul. 2020-27, Analysis, pg 6.

The Revenue Procedure. Rev. Proc. 2020-51 addresses what happens if a taxpayer (a) expects to obtain loan forgiveness but is denied, or (b) never applied for forgiveness because he knows he will be denied. In either case, the payment of the business expenses becomes tax deductible. The procedures addressed in the Rev. Proc. are referred to as a "safe harbor" for those who did not, or knew they would not, obtain PPP loan forgiveness.

In the case of a person whose application was denied in 2020, he can claim as a deduction the expenses paid with PPP loan proceeds on his 2020 tax return. Say he applies for loan forgiveness some time during 2020 and is notified in 2020 that his loan is not forgiven. In that case, he simply claims the deductions on his 2020 tax return as he normally would. If the taxpayer submitted an extension to file his 2020 return, he can claim the deductions on the timely filed return by the extended due date. See: Rev. Proc. 2020-51, §4.01. If the taxpayer already filed his 2020 return by the time his application is denied in 2021, he can also opt to amend his return (within three years of the filing date) to claim the deductions.

However, if the application is filed in 2020 but not denied until 2021, the taxpayer has an option. He can claim the deductions on the 2020 return (Rev. Proc. 2020-51, §4.01), or he can claim them on his 2021 return (Rev. Proc. 2020-51, §4.02). In either case, he must follow the procedures for making the election, explained below.

In the case of the taxpayer who never applied for forgiveness, and also did not claim his deductions on his 2020 return, he may claim a deduction for those expenses "for the subsequent taxable year." See: Rev. Proc. 2020-51, §4.02. Suppose you did not apply for loan forgiveness in 2020, and did not make the determination to forego applying for such forgiveness until after filing your 2020 return. In this case, you can opt to make an election to claim the deductions on your 2021 return.

MAKING THE ELECTION

The election to claim the expenses in 2020 (if your forgiveness application was denied in 2021), or on your 2021 tax return (if you withdrew your application after 2020), must be made on the tax return. The election is made by submitting a statement with the return that is titled “Revenue Procedure 2020-51 Statement.”

The statement must include the following:

1. Your name, address, and social security number or employer identification number,
2. A statement specifying that you are an eligible taxpayer under either §3.01 (application denied) or §3.02 (application withdrawn or not filed) of Rev. Proc. 2020-51,
3. A statement that you are applying §4.01 (deductions claimed in 2020) or §4.02 (deductions claimed in 2021) of Rev. Proc. 2020-51,
4. The amount and date of disbursement of your PPP loan,
5. The total amount of forgiveness that you were denied or decided not to seek,
6. The date you were denied or decided to no longer seek forgiveness, and
7. The total amount of eligible expenses and non-deducted eligible expenses that are reported on the return. See: Rev. Proc. 2020-51, §4.04.

PARTIAL FORGIVENESS

The Rev. Proc. is clear that the ability to deduct expenses is tied directly to the lack of forgiveness of a PPP loan. If the loan is entirely forgiven, there is no deductibility whatsoever. If forgiveness is completely denied, the expenses become fully deductible. In the case of partial forgiveness, the expenses are deductible only to the extent that forgiveness is denied or is not sought. See: Rev. Proc. 2020-51, §4.03.

For example, suppose you obtain a PPP loan for $50,000, but only $30,000 of the loan is forgiven. In that case, you cannot deduct more than $20,000 of the expenses paid with PPP proceeds.

THE AUDIT RISK

I’ve been talking about audit risks associated with PPP loans from day one, and in fact, in the August 2020 issue of this newsletter, I presented a full article discussing the PPP audit risks. The Rev. Proc. makes it quite clear that the IRS is ready, willing and able to audit various issues related to PPP loans. Among those issues are:

1. Whether expenses paid with PPP loan proceeds were claimed on the tax return,
2. Whether you can substantiate the amount and business purpose of any claimed deduction under otherwise established tax rules,
3. The extent to which your PPP loan was forgiven, and
4. Requiring proof of any of the elements set forth in the required statement explained in the previous section of this article. See: Rev. Proc. 2020-51, §4.05.

CONCLUSION

The tax consequences of the CARES Act pandemic relief will remain long after the affects of COVID-19 itself are just a bitter memory. I anticipate that, between the issues I raised in the June 2020 article and those that I address here, the IRS will be running PPP audits for many years to come.

What To Do Now About PPP Loans

Critical Year-End Planning Considerations

With 2020 winding to an end, there are a few important considerations for dealing with PPP loans before the end of the year. Here's what I'm talking about.

1. Separate accounting. You must ensure that you can separately account for your PPP expenditures—for two reasons. First, if you used PPP money only for the expenses authorized under the program (discussed further below), your loan is forgivable. Of course, your goal is to in fact get the loan forgiven. Therefore, you must be able to demonstrate to your lender (for sure) and to the IRS (if challenged) that the money was used only as authorized by law. Second, as you know from the lead article above, you cannot deduct PPP loans to the extent that the loan is forgiven. Thus, your accounting must be able to show that you did not include a deduction for expenses—payroll, for example—that were paid with PPP proceeds. The burden of proof is on you. And, as discussed in the next article, a potential IRS attack might not be limited to just a civil audit. The IRS has already opened hundreds of criminal investigations related to potential PPP loan fraud.

2. Organize your documents. In the August issue of this newsletter, I discussed the likely PPP audit issues. In anticipation of that, be sure you organize your documents to show that you qualified for a PPP loan in the first place, and that you used the proceeds as allowed by law. Keep in mind that PPP money can be used only as follows:

1. Payroll costs (at least 60% of your loan must be used for payroll),
2. Interest (but not principal) on a mortgage obligation existing as of February 15, 2020,
3. Rent on business property existing as of February 15, 2020, and
4. Utility payments on business property existing as of February 15, 2020.

In addition to the audit issues I identified in August, there are more potential audit issues as explained in the above article. The bottom line: don't be surprised by a PPP audit. Rather, assume you will be audited and be sure you have your documents lined up in advance.

3. Spend the money. The deadline for spending PPP proceeds is either: (a) 24 weeks from the date the loan was funded, or (b) December 31, 2020, whichever comes first. If you have not spent your PPP proceeds by the end of the year, you must do so, and spend it on one or more of the four items listed above. If you do not, you will not get forgiveness of your loan to the extent that you didn't spend the money within the time allowed by law. See the July 2020 issue for more discussion of the deadline for spending PPP proceeds.

4. Apply for forgiveness. You must apply for loan forgiveness within ten months of the deadline for spending PPP proceeds. Depending upon when your 24-week calculation expires, you might already be well into your application deadline. In any event, don't wait. I believe all SBA lenders are now processing forgiveness applications. In the August and October issues of *PTT*, I discuss the application process at length. Please review that material for further guidance. You should also check with your lender. They may have unique procedures or particular forms they require to facilitate the application/forgiveness process.

Criminal Investigation Division Targeting PPP Loans

Wide Spectrum of CARES Act Fraud Cases Now in the Mix

The massive COVID-19 relief package is, to my knowledge, the largest single-year government giveaway in the history of the United States. Between the CARES Act and the various other elements of federal government relief, especially PPP loans and the $1,200 economic impact payment to individuals, the cost of the pandemic bailout is well over $2 trillion—and I'm sure much more is yet to come. Simply unimaginable. See my detailed discussion of these costs in the July 2020 issue of *PTT*.

With all this "free money" pouring from government coffers, it's no wonder that fraud associated with these problems is likely to be rampant. For example, it didn't take sophisticated con artists long to realize that they could use email to bait unsophisticated citizens into claiming their purported COVID stimulus check by logging on to a fake IRS website to enter their financial details. Of course, the email, like the website, is a scam. I reported on this in the June issue of *PTT*, and included a copy of the scam email that was being sent out. I personally received one, and no, I didn't apply for my free refund.

You can be sure the fraud is not limited to con artists targeting innocent people with bogus emails. Like the vast fraud associated with the Earned Income Tax Credit, the various CARES Act programs will most certainly be leveraged by dishonest people—even purported "financial professionals"—in the hope of getting free money from the government.

You can also be sure that this fact is not lost on the IRS. The IRS's Criminal Investigation (CI) division is already targeting cases for potential criminal prosecution. They currently have hundreds of open investigations already pending, according to James Lee, the head of CI. Lee stated, "We think there's going to be some significant cases there, and our involvement increases monthly."

The cases CI is currently working run through the entire spectrum of CARES Act relief programs. These include fraudulent claims for the economic impact payment (the $1,200 refundable tax credit), Paycheck Protection Program loans, unemployment benefit fraud, fraud associated with the array of payroll tax credits created this year, and Economic Injury Disaster Loans issued through the Small Business Administration.

To aid the effort, CI is currently in the process of hiring and training new special agents. This will include as many as 288 new staff slated for hire in 2021.
As I said in the opening article, expect the IRS to be conducting PPP and related CARES Act enforcement activity for many years to come.

How You Can Ask Dan Pilla a Question

If you have questions or problems you'd like Dan Pilla to address, please write to Dan at:

215 W. Myrtle Street
Stillwater, MN 55082

or e-mail to:

expert@taxhelponline.com

Write the word "newsletter" in the subject line.

Biden's Promise is A Fantasy

His Plan Will Raise Taxes on Everybody

BY SCOTT MACPHERSON *

Biden's promise to raise taxes only on the rich cannot possibly be upheld if he is successful with the centerpiece of his plan. That, of course, is to repeal in its entirety the Tax Cuts and Jobs Act (TCJA), which was President Trump's tax plan that took effect in January 2018. The primary effect of the TCJA was to reduce taxes for Americans in the bottom 80% of the income earning strata. Said another way, only the top 20% of income earners did not get a tax cut under the TCJA. Americans those earning between about $40,000 to $80,000 per year saw the greatest benefits of the TCJA, and millions of additional citizens at the lowest income levels were taken off the tax rolls altogether.

Biden and a Democrat controlled House and Senate have pledged to reverse all that.

For example, Biden vows to eliminate the so-called "stepped up basis" rule for inherited property. This rule has been on the books forever; it was not a part of the TCJA and yet it is under attack by Democrats. Here's how it works.

Suppose your parents own a home worth $200,000. They purchased the home decades ago for, say $50,000. If they gift the home to you prior to their passing, your basis in the home is the same as theirs—$50,000. That means if you sell the home for its current value of $200,000, you must pay capital gains tax on the profit of $150,000.

However, if you inherit the home after their death, your basis becomes the fair market value of the property as of the date of death—in this example, $200,000. Now if you sell the property for $200,000, there is no capital gains tax because there's no gain.

This is what the law refers to as "stepped-up basis." And the rule does not apply only to "rich people." Every American taxpayer enjoys the benefit of stepped up basis on inherited property.

According to Gallup, as of 2017, 82% of Americans over age 65 own their own homes. That is the highest rate of home ownership for any age group. When these people die, their property passes to their heirs. If Biden and leftist Democrats have their way, the next four years will see a massive transfer of wealth—not from parents to children (as it should be)—but from parents to the federal government. This is just another example of the "tax the rich" fraud. The government will systematically steal the wealth created by your parents.

Let me lay out a planning consideration to take into account if leftists gain absolute control of the federal government. It involves senior citizens selling their homes now. They could avoid any capital gains on the sale of the house and pass the cash to their heirs tax free. Here's how that might work.

Under current law, a person can sell his primary residence free of capital gains tax (within limits) if (a) he owned the home for at least five years from the date of sale, and (b) he occupied the home as his principal residence for at least two of those five years. In that case, a single person can exclude up to $250,000 of capital gain from taxation, and a married filing jointly couple can exclude up to $500,000 of capital gain from taxation.

Using our example of the $200,000 house, consider this: If mom and dad sell their main home now, their capital gain would be $150,000. But since they are married, they can exclude from taxation up to $500,000 of gain on the sale of the home. As such, they incur no taxes whatsoever on the sale of the home. If they in turn die with that cash (or any portion of it) on hand, the money passes to their heirs tax free, assuming the total value of the estate is less than threshold at which the estate tax kicks in. The reason for this is that property inherited from a decedent is not taxed to the beneficiary. The estate pays the tax, if any is due; but for estates under the valuation threshold, there's no estate tax.

In 2021, estates valued under $11,700,000 are not subject to the estate tax. Note that if Biden has his way, that threshold will be cut at least in half. The pre-TCJA threshold was $5,490,000. As recently as 2001, the threshold was just $675,000. If leftists get control of the entire U.S. Government, expect the estate tax threshold to be slashed dramatically.

Of course, this strategy assumes that a federal government totally controlled by leftists will not change the law excluding capital gains on the sale of one's main home, as explained here. Believe me when I say I'm going to keep my eye on all proposed tax law changes. If a Biden Administration is capable of enacting the socialist programs they talk about—Medicare for all and cancellation of all student loans as examples—there will be massive tax increases across the board.

11th Circuit Renders Important Ruling In Tax Bankruptcy Case

Late-filed Return is a Return for Bankruptcy Discharge Purposes

BY SCOTT MACPHERSON *

Two years ago I reported in *Pilla Talks Taxes* on the case of In re Kline, 581 B.R. 597 (Bankr. W.D. Ark. 2018), where the court held that a late return is not a "return" for purposes of a bankruptcy discharge. The court held that a late-filed return fails the definition in *11 U.S.C. § 523(a).* That section requires that a return meet the requirements of "non-bankruptcy law," one of which is that the return must be filed on time. I chastised the court for basing its holding upon an objectively-false and irrational analysis. See the April-May 2018 issue of *PTT.*

Earlier this year, the panel of judges in the 11th Circuit case of *In re Shek,* 947 F.3d 770 (11th Cir. 2020), agreed with me, and agreed with the *amicus curiae* brief written by John A. E. Pottow, a renowned law school professor at the University of Michigan and author of a bankruptcy textbook. The panel decimated the argument supporting the *Kline* holding by way of reversing the holding of the case before it. The *Shek* court held that a late return can be a "return" for purposes of a bankruptcy discharge.

I should clarify that *Shek* concerned Massachusetts state income taxes, not federal taxes. However, I see nothing in the facts of Shek, or in the court's analysis, that makes the holding inapplicable to federal income taxes. In point of fact, the court discussed federal tax law.

One might notice that Massachusetts is not under the 11th Circuit. That discrepancy is explained by the simple facts of the case. Shek lived in Massachusetts. He filed his 2008 Massachusetts income tax return seven months late (in November 2009). He then moved to Florida, which is in the 11th Circuit. In 2015 he filed chapter 7 bankruptcy, and received a discharge order. The Massachusetts Dept. of Revenue resumed collection activities after the discharge order, so Shek file a motion with the bankruptcy court for a determination of dischargeability. Held: his state tax debt was discharged. Massachusetts appealed, arguing that because the tax return was late it failed the definition in the "hanging paragraph" of *§ 523(a)(19)* (that is, the unnumbered paragraph after (a)(19)), which means the tax debt was not discharged.

For reference, that portion of the statute reads:

> For purposes of this subsection, the term "return" means a return that satisfies the requirements of applicable nonbankruptcy law (including applicable filing requirements). Such term includes a return prepared pursuant to section 6020(a) of the Internal Revenue Code of 1986, or similar State or local law, or a written stipulation to a judgment or a final order entered by a nonbankruptcy tribunal, but does not include a return made pursuant to section 6020(b) of the Internal Revenue Code of 1986, or similar State or local law.

The government made two arguments. The first was that the phrase "applicable filing requirements" includes the relevant temporal deadline for filing a tax return: if a taxpayer does not timely file his return, then he did not comply with all "applicable filing requirements," Thus, the statutory definition fails, and as such, the tax debt is not discharged. This is the so-called "one-day-late rule" because it prohibits discharge of a tax debt with respect to which a return was filed even as little as one day late. *Shek* at 775.

That's a syllogism: a return must comply with "applicable filing requirements," and a filing deadline is an "applicable filing requirement." Therefore, a return that does not meet its filing deadline has not complied with "applicable filing requirements." "[This argument] has some force to it," the court said. "All three of our sister circuits to have considered this question have held that the plain language of the hanging paragraph requires DOR's interpretation." *Id.* at 775 (with citations to cases in the 1st, 5th, and 10th Circuits).

But the court dismantled that syllogism by denying that "applicable filing requirements" includes filing deadlines. The court could do that by application of the axiom that all words in a statute must have meaning:

> We must strive, if possible, to give meaning to every word of the Code. See, e.g., *United States v. Menasche,* 348 U.S. 528, 538-39, 75 S. Ct. 513, 99 L.Ed. 615 (1955). This means we must look for an interpretation of "applicable" that distinguishes the set of "applicable filing requirements" from the set of all "filing requirements." Any interpretation that does not account for this word risks rendering it superfluous. *Id*. at 776.

Said another way, if the phrase "filing requirements" without the adjective "applicable" encompasses the temporal deadline, and of course it does, then Congress must have had something else in mind when it included the adjective "applicable." The court found that other meaning in the dictionaries cited by the Supreme Court in *Ransom v. FIA Card Servs., N.A.,* 562 U.S. 61 (2011): "appropriate, relevant, suitable or fit."

For example, "applicable" filing requirements could refer to considerations like a return's form and contents—aspects of the putative return that have a material bearing on whether or not it can reasonably be described as a "return"—but not to more tangential considerations, like whether it was properly stapled in the upper-left corner, or whether it was filed by the required date. This approach makes common sense; in a definition of what constitutes a "return," it makes sense that the term "applicable" would relate to matters that are relevant to the determination of whether the document at issue can reasonably be deemed a "return." *Id*. at 776.

Rephrased, the government interpreted "applicable filing requirements" to mean those filing requirements that apply to a given taxpayer, but the court pointed out that, per the Supreme Court's definition, it could also mean those filing requirements that are "relevant" or "appropriate" to the task of defining a "return"—that is, those that deal with what a return is. "Statutory context, however, makes clear that only the latter interpretation accords with § 523 as a whole." *Id.* at 776.

The court continued:

> Statutory provisions are not written in isolation and do not operate in isolation, so we cannot read them in isolation. The plain meaning of a statutory provision derives not only from the "particular statutory language at issue," but also "the language and design of the statute as a whole." *Id.* at 776-77 (citing *K Mart Corp. v. Cartier, Inc.*, 486 U.S. 281 (1988)).

And further, the court, citing other authority, stated:

> "Because legal drafters should not include words that have no effect, courts avoid a reading that renders some words altogether redundant." *Reading Law* at 176. This surplusage canon obliges us, whenever possible, to disfavor an interpretation when that interpretation would render a "clause, sentence, or word … superfluous, void, or insignificant." *Id.* at 777; [internal citations omitted].

The government's reading of the hanging paragraph violated those principles, so the *Shek* court rejected the government's reading.

The court also pointed out that in 2005, when Congress added the hanging paragraph, it left § 523(a)(1)(B)(ii) unchanged. That portion of the statute provides that a late-filed return can qualify for discharge if the return is filed more than two years before the bankruptcy. "The one-day-late approach would render § 523(a)(1)(B)(ii) a near nullity. … There is a clear conflict between DOR's interpretation of the hanging paragraph and *§ 523(a)(1)(B)(ii)." Id.* at 777.

The government tried to argue that the one-day-late approach does not completely eradicate the statute, because *§ 6020(a)* returns and equivalent state-law returns would still fall into that statutory exception. Thus, according to the government, *§ 523(a)(1)(B)(ii)* is not surplusage because it still bars discharge of some returns. The Shek court was not impressed with that reasoning, because it knew that a § 6020(a) return is "atypical" and is made only in "the most unusual circumstances." It quoted the Supreme Court saying that the surplusage canon applies when an interpretation would render a clause, sentence, or word superfluous, void, or insignificant, which the government's reading does. Id. at 778 (quoting *TRW Inc. v. Andrews,* 534 U.S. 19, 31 (2001)). Thus, the one-day-late rule cannot be what Congress intended.

Lastly, the court noted that its interpretation of the hanging paragraph was in harmony with the principle that "exceptions to discharge should be confined to those plainly expressed." *Kawaauhau v. Geiger*, 523 U.S. 57, 58 (1998). And where possible, courts should always construe exceptions to discharge "in favor of the debtor, and recognize that the reasons for denying a discharge must be real and substantial, not merely technical and conjectural." *In re Miller,* 39 F.3d 301, 304 (11th Cir. 1994) (internal citations and quotations omitted).

The government then argued that Massachusetts tax law (which is "applicable nonbankruptcy law") defines "return" in part by reference to whether a putative return was "duly filed," and "duly filed" encompasses a temporal requirement. Thus, if a putative return is not timely filed, then it was not duly filed, so it fails the definition under state law. "Therefore, the 'applicable nonbankruptcy law' defines a 'return' as, in part, a timely filing." *Id.* at 779.

The court denied that "duly filed" necessarily includes timeliness. It noted that, per Black's Law Dictionary, the term means "in a proper manner; in accordance with legal requirements." The traditional legal adverb for "time sensitivity" is "timely." *Id.* at 780. But without explicitly accepting one definition over the other, the court took notice that Massachusetts has several statutes explicitly addressing late-filed returns, and the statutes all treat late-filed returns as "returns." Thus, the government's argument was false. *Id.* at 780.

All that analysis accomplished, the court deliberated over whether to apply the *Beard*-test definition of a "return" or the Massachusetts definition to this *state* income tax return. The court chose to dodge that question because the outcome was the same either way: under Massachusetts law a late return is still a return, and the parties stipulated the elements of *Beard* in the bankruptcy court, so both tests were met. For a discussion of the Beard elements, see page 176 of ***How to Get Tax Amnesty.***

Ultimately, Shek's return was deemed a return for purposes of § 523: "We hold that the bankruptcy court's discharge included Shek's tax return debt." *Id.* at 781. I find the question odd, though, in that a *state* income tax return is surely defined by *state* law. But, the important part is that the court concluded "that § 523 does not incorporate a mandatory precondition that a tax return must be timely filed to be dischargeable." *Id.*

Out of the eleven numbered circuit Courts of Appeal plus the District of Columbia, ten of them have now faced the question of discharging tax debts in bankruptcy where the tax return was late. The most recent cases in each jurisdiction are as follows:

1st Circuit: *Fahey*, 779 F.3d 1 (Feb. 18, 2015) (MA state tax; no discharge because late return violates the "shall be made on or before …" statutory due date and thus fails the hanging paragraph of § 523(a)(19)); *Pendergast*, 2015 WL 3388354 (May 1, 2015) (MA state tax; followed *Fahey* to deny discharges where returns were filed late).

2nd Circuit: no known case yet.

3rd Circuit: *Giacchi*, 856 F.3d 244 (2017) (federal tax; no discharge because late post-assessment return violates the *Beard* test).

4th Circuit: *Moroney*, 352 F.3d 902 (2003) (federal tax; no discharge because late post-assessment return violates the *Beard* test).

5th Circuit: *McCoy*, 666 F.3d 924 (2012) (MS state tax; no discharge because late return violates the "shall be filed on or before April 15th …" statutory due date and thus fails the hanging paragraph of § 523(a)(19)).

6th Circuit: *Hindenlang*, 164 F.3d 1029 (1999) (federal tax; no discharge because a late return that serves no tax purpose violates the *Beard* test).

7th Circuit: *Payne*, 431 F.3d 1055 (2005) (federal tax, pre-BAPCPA; no discharge because late post-assessment return violates the *Beard* test; strong dissent however).

8th Circuit: *Colsen*, 446 F.3d 836 (2006) (federal tax, winner, pre-BAPCPA; post-SFR late return counts as a return because on its face it appeared to be a return, and in fact the IRS accepted the late return and abated some of the debt according to what it showed).

But see *Kline*, 2018 WL 813313 (W.D. Ark. 2018) (AR state tax; explicitly rejected *Colsen*; no discharge because late return violates the "shall be filed as follows" statutory due date and thus fails the hanging paragraph of § 523(a)(19)).

9th Circuit: *Smith*, 828 F.3d 1094 (2016) (federal tax; no discharge because late post-SFR return violates the *Beard* test).

10th Circuit: *Mallo*, 774 F.3d 1313 (2014) (federal tax; no discharge because post-assessment late return does not comply with the tax-law filing deadline and thus it violates the hanging paragraph of § 523(a)(19)).

11th Circuit: *In re Shek*, 947 F.3d 770 (January 23, 2020) (MA state income tax; late return is a "return" under state law and therefore tax debt was discharged); but see also Justice, 817 F.3d 738 (2016) (federal tax; no discharge because late post-assessment return violates the *Beard* test).

D.C. Circuit: no known case yet.

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Small Business Auditors Set Up For Remote Work

Expect Business Audits to Get Back into Action

According to the IRS's deputy commissioner for examination in the Small Business and Self-Employed Division, the agency's team that focuses on small business audits is 90% operational. That is to say, 90% of IRS employees in that function are now able to work from home. That means audits of small businesses and self-employed people will kick back into high gear.

As of the time of the COVID shutdown orders last spring, only about 40% to 45% of employees were able to work from home. Between June and July, most other employees received their needed IT equipment, allowing them to get back to the work of harassing small business owners. I'm sure that comes as good news to all small business owners.

The 2020 Paul R. Tom Award

And the Winner Is…

As many of you know, we lost our good friend and colleague Paul Tom at the end of 2017. In our newsletter tribute to Paul in January 2018, I stated that his memory will live on in TFI through the annual presentation of the Paul R. Tom Award for Outstanding Contributions to the Mission and Goals of the Tax Freedom Institute. The 2018 Paul R. Tom Award—the very first—was presented to Paul posthumously through his wife, Melissa.

On Monday, October 26, 2019, on the first day of the Defense Conference, I presented the second annual Paul R. Tom Award.

The award winner was determined on the basis of the model that was created by Paul Tom himself. Paul was selfless in giving his time to those who needed help. He was willing and anxious to contribute articles to the newsletter, which he did often. He was a speaker at past conferences. And, he was always present on the list-serve answering questions and giving guidance. He loved TFI and its members. He was completely dedicated to our mission as evidenced by the fact that he never missed a single conference. He even attended the 2017 conference at a time when he was quite ill.

On top of all that, Paul was my friend. I greatly valued that relationship and his counsel, which I leaned on regularly. I miss him every day. But as we march on, please help me congratulate our second Paul R. Tom Award winner. We selected this person because he most closely resembles Paul's dedication and commitment to TFI.

AND THE WINNER IS…

Steven Klitzer, Attorney at Law and Consulting Member of TFI.
Member since 2000

TAX FREEDOM INSTITUTE, INC.

AN ASSOCIATION OF TAX PROFESSIONALS IN DEFENSE OF TAXPAYERS RIGHTS

Tax Freedom Institute

The Paul R. Tom Award

Given in Appreciation and Gratitude to

Steven N Klitzner

Attorney at Law

For Outstanding Contributions and Commitment to the Mission and Goals of the Tax Freedom Institute.

Daniel J. Pilla
Executive Director
October 23, 2020

It is my honor to present Steve Klitzner the 2020 Paul R. Tom Award. Thank you, Steve, for your dedication and commitment to this organization. Due to COVID, Steve was unable to attend the 2020 conference personally, but he did participate via the live feed. We were able to hear his comments when I announced the award.

Steve's email response reads as follows:

> Paul Tom was one of the foundations of the Tax Freedom Institute. He was always so generous in sharing his vast knowledge and experience. He was an inspiration to all of us to fight the good fight and exercise all taxpayers' rights. I miss the telephone conversations and Defense Conference dinners where we would talk about work and life. He could be so serious one minute and so funny the next. We lost a great warrior for the people and an even greater friend. It is an honor to receive an award named for Paul R. Tom, Attorney at Law.

And let me tell you Steve, it is a great honor to present you with this award!