PILLA TALKS TAXES

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White House Abandons Bank Reporting Plan...

...For Now

The wildly invasive plan to require banks, credit unions, and other financial institutions to report account data to the IRS on an annual basis was abandoned by the White House...for now. The plan would have required all financial institutions to file an annual report to the IRS on all accounts with "gross flows" of $600 or more per year. What that means exactly is if the total of your account's in-and-out transactions equals at least $600, your account activity would be reported to the IRS.

The White House claimed that this measure was necessary to track down rich people who don't pay their taxes. In an article published on the Treasury Department's web site last month, the argument was made that this reporting was necessary because we have a "two-tiered tax system." One tier allegedly applies to wage-earners whose income is reported to the IRS annually, and the other to rich people, who are often self-employed and whose income is therefore not necessarily reported to the IRS. For more on this, see my article in August/September issue of *PTT*, entitled "The Tax Gap Fraud."

The Biden administration and House Democrats came under heavy fire for this plan, and for good reason. The idea that we must report to the government all financial accounts the in-and-out flows of which exceed $600 in order catch rich tax cheaters in the highest 1 percent of the income strata is pure farce. Don't the financial accounts of rich people show gross flows of substantially

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ADS

more than $600?

As a result of pressure from me and others (for example, see my article, "Biden's Tax Plan Calls for Indiscriminate Spying," published by National Review on 9-27-2021), the administration floated the idea of an upward revision of the threshold. The revised spying scheme would require banks to report to the IRS only if the gross flow in a given account reached $10,000. But even the $10,000 threshold is a farce.

Think about this for a minute. According to the Department of Health and Human Services, poverty level income in the United States for an individual in 2021 is $12,880. That means those on the very bottom of the income strata would still very likely be subject to financial account reporting even at $10,000 per year. How is that any concession of the $600 threshold?

But rather than continue to push for the reporting requirement, even at the revised level of $10,000, as of October 28, the administration scrubbed the idea from the latest version of the tax and spend proposal working its way through Congress. That doesn't mean it can't be added back as negotiations continue, nor does it mean it won't be brought up in the future. The reality is that Big Government never gives up on the idea of gathering private data with as broad a dragnet as possible.

For example, a hidden provision in the Affordable Care Act was a law that required information reporting on essentially all corporate business-to-business payments that exceeded $600 per year. Suppose your small business corporation paid $600 or more in a year to, say, the phone company or a materials supplier. Your corporation would have to report those payments to the IRS on a Form 1099. The rule—enacted as part of the ACA—would have led to an explosion in the number of information returns filed with the IRS every year, just like the $600 (or even $10,000) gross-flows reports would have done.

The difference is that the $600 business-to-business provision actually became law. And once it did, it was met by an avalanche of opposition, led by me, which resulted in its repeal in 2012.

My point here is simple. The idea of IRS invasiveness into every area of your private life is not new—and *it's not going away*. They don't give up. And it doesn't seem to matter whether Democrats or Republicans control the White House or Congress. The wish list of information gathering tools comes from inside the IRS—from the career bureaucrats who spend their days thinking up more ways to gain access to your private personal and business financial details in the name of enforcing the tax laws.

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LOCATION:

Embassy Suites by Hilton, Nashville South, Cool Springs, Tennessee.

DATES:

Sunday Evening November 7
– TDI/TFI Members Only Business and Networking Meeting.
Monday and Tuesday November 8 & 9
– Taxpayers Defense Conference.

COST:

More details will follow on cost but it looks like the room cost is $149 a night which includes breakfast. Those who stay at the hotel will get an additional discount off the conference registration fee. The retail cost of the conference will be at least $795. For our current members, the cost will be $595 at most.

PLEASE EMAIL JEAN DIRECTLY

at *jean@taxhelponline.com* to say whether you are planning to attend in person. We are also planning to host it virtually (like we did last year) so let Jean know if that is what you are planning.

DEFENSE CONFERENCE THEME and TOPICS:

The IRS has made it perfectly clear that it intends to launch an attack on businesses. Because of that, our 2021 Defense Conference theme is Business Tax Audits. The topics include:

- An analysis of how this attack will look
- How the IRS attacks a business's reported income and deductions
- The law regarding the burden of proof on underreported income
- 6 ways to prove deductions
- An analysis of procedures relating to Notice CP2000 and ASFRs
- 2 ethics sessions to include billing practices and the essential elements of competency of counsel
- And don't forget our very educational live role playing and group debriefing sessions
- Finally, as always, we will have our popular and informative moderated discussion where all topics and problems are fair game.

The Taxpayers Defense Conference is widely regarded as simply the best tax seminar in the country—and for good reason. There is no place else you can go to get the up-to-date, cutting edge information you need to effectively represent your clients in taxpayers' rights and problems resolution issues. And that's a fact.

Watch your email and check the TDI/TFI website for more details.

Where We Stand With The Wealth Tax

Looks Like the “Billionaire’s Tax” Is Dead

Leftist Democrat Ron Wyden, Chairman of the Senate Finance Committee, recently pitched a revenue-raising idea that he called a “billionaire’s income tax.” But the fact is Wyden’s plan wasn’t an income tax at all. It was a wealth tax. Wyden’s plan was targeted against just 700 people—those at the very top of the mountain when it comes to wealth.

The plan was to impose a tax on the mere appreciation of assets, such as stocks, bonds and real estate, rather than on the gain realized on the sale of such assets. Wyden’s proposal was not substantially different than the wealth tax floated by Senators Elizabeth Warren and Bernie Sanders earlier this year. Really what we’re talking about here is effectively an estate tax, but one which is imposed without the hassle of having to wait until the taxpayer is actually dead before it can be assessed.

As clearly explained in Tom Giovanetti’s article below, Wyden’s plan would lead to massive complexity driven by the near impossibility of accurately valuing assets in the absence of a sale of those assets at fair market value. Thankfully, the plan appears to be dead.

In its place, Democrats are opting for an alternative in the form of surtaxes on high income individuals. While the current 37% top individual income tax rate would remain the same, there would be a 5% surtax on incomes above $10 million and an additional 3% on incomes above $25 million. This would effectively create two new tax brackets, with the “tippy-top” top bracket fixed at 45%. This way, high-income taxpayers would be punished for being successful but without all the complexity of trying to administer a wealth tax.

The surtax appears to be much more politically salable than the billionaire's income tax, and most certainly would not be the target of constitutional challenges that surely would have befallen any wealth tax.

The White House claims the tax will raise $230 billion over 10 years. However, this claim has not been tested by the Congressional Budget Office.

Moreover, the surtax would hit far more than just the 700 mega-rich individuals who were targeted by Wyden's wealth tax. To raise the trillions in new revenue the administration needs to deliver on the gravy train of spending promises, they are going to have to broaden the tax base immensely. There simply are not enough mega-rich people in the country from whom money can be extracted to raise the kind of revenue needed to satisfy the spending appetite of the Left.

What's really at stake here is the Marxist concept of income redistribution. In today's political rhetoric, the Left talks in terms of ending "income inequality." What that actually means is the confiscation through the tax code of the income and assets earned lawfully and peacefully by one group because it is thought (arbitrarily) that they have too much.

And frankly, the idea that such income would be directly redistributed to those who don't have as much is fantasy. What happens is the resources of the rich are confiscated by the government and used by the government as only the government sees fit to use them. It's undeniable that much of those resources are used to fund a growing gift basket of benefits to lower income people—Medicare, universal basic income, etc.—but this does not in any way raise the standard of living of low-income people. It only gives them further incentive not to produce, and in turn makes them even more dependent on government largess to survive to the next month. In any event, they certainly do not prosper.

Wyden is not giving up. He claims that he will continue to push the administration to attack mega-rich individuals who have managed to amass a portfolio of assets that he believes they should not own.

IRS To Blame For Its Own Delay

Sixth Circuit Spanks IRS in Fraudulent Conveyance Case

BY SCOTT MACPHERSON

In the case of *U.S. v. Holland*, 2020 WL 1146716 (6th Cir. 2020), the Sixth Circuit Court of Appeals upheld a recalcitrant songwriter's business structure against the IRS's accusations of nominee, alter ego, and fraudulent transfer. These three topics were covered in the 2019 Taxpayer Defense Conference.

The reason for the court's ruling is that the taxpayer paid adequate consideration for his business arrangement. As such, there was no evidence that his transfer of assets was done with the goal of thwarting the collection of taxes – even though he was a serial tax debtor. The effect of recognizing the business structure was to deny the IRS a judgment against the business assets.

And to make it even better, the court blamed the IRS for this holding, saying that if the IRS had not delayed its assessment for so long, the decision might have been different.

The taxpayer was Edward Holland, Jr., a musician who wrote or co-wrote about 80 hit songs on the UK charts and more than 140 hit songs on the US charts in the 60s, 70s, and 80s. He wrote for bands such as Martha and the Vandellas, The Supremes, The Four Tops, and The Isley Brothers. (The court noted as particular examples that he wrote "Stop in the Name of Love" and "Baby Love.") At some point Holland sold his song rights to music companies in exchange for the right to royalty payments. Those royalties thereafter served as Holland's primary source of income.

Unfortunately, he was not very good at staying current on income taxes. Between 1986 and 1990, the IRS levied approximately $1.5 million for back taxes. In June 1997, after the IRS informed him that it intended to levy for year 1996, Holland got an idea. He retained a team of professionals to prepare and execute a transaction described by the Sixth Circuit as "common enough in financial circles" by which he would convert his interest in future royalty payments into a present lump sum of cash. Specifically, Holland would create a partnership wholly owned by him, to which he would transfer title to the royalty assets, which were then worth about $23.3 million; the partnership would then borrow (by means of the issuance of notes) $15 million, for which the royalty assets would serve as collateral. Holland's representatives informed the IRS about the pending transaction in advance; the agency replied that Holland was free to "conduct his normal course of business" at that time. *Id.* at *1.

While Holland's advisers worked on the partnership, the IRS audited him for year 1995, and then expanded the audit to 1991-1994. In May 1998 "the IRS told Holland that it thought he owed about $1.8 million in taxes and penalties, as well as $2.1 million in interest, for his underpayments for the 1991—94 years. The IRS did not, however, record an assessment for that amount at that time." *Id.*. A few days after learning of the proposed assessment, Holland executed the transaction to monetize his royalty assets. At the close of the transaction, Bankers Trust (which served as a trustee of sorts for the deal) paid $8.4 million directly to Holland and about $5 million in fees to the lawyers and bankers who structured it. Bankers Trust also placed $1.7 million in escrow, which was then used to pay Holland's debts—notably including the entire amount (about $1.4 million, for the 1986 and 1990 years) of the IRS's assessments against Holland at that time. *Id.*. at *2.

Two facts in that historical recitation were crucial to the court's holding: Holland paid his professional team $5 million and Holland paid his assessed federal tax debts in full.

Four years later the IRS assessed him again. After that, Holland refinanced his partnership's loans with a new bank and obtained a line a credit secured by the royalty rights. The IRS later filed a notice of tax lien, and then initiated a suit to bring the lien to judgment. (That lawsuit was this case, on appeal to the Sixth Circuit.) In that lawsuit the government named as an interested party the bank that held a security interest in the royalty rights.

The government's argument was that Holland, not the partnership, actually owned the royalty rights on any of three alternative theories: nominee, alter ego, and fraudulent transfer. As a consequence, said the government, the tax lien had priority over the bank's security interest, so the IRS should get the money in the partnership's bank account.

And that is where the case gets interesting. All three of those theories were discussed at the 2019 Defense Conference, in Session 5. As explained at the conference,

"Nominee" means one who holds title to another's property,

"Alter ego" means that one is a mere extension of the taxpayer, and

"Fraudulent transfer" means a sham transfer to defeat a creditor's right to collect.

"Nominee" theory was also discussed in the article titled "Transferring Title to Assets" in the September 2019 issue of *Pilla Talks Taxes*. As explained both at the Defense Conference and in that article, an owner of property may be considered a mere nominee for someone else (known as "the true owner") and thus may be considered to hold only bare legal title to the property. In that situation, the property can be seized by the IRS in payment of a tax debt owed by the true owner. The critical issue in the nominee analysis is that of control: who actually controls the property? To answer the question of control, a court will consider numerous factors. The exact set factors can vary slightly according to state law, but it will be something like:

1. Whether inadequate or no consideration was paid by the nominee,
2. Whether the property was placed in the nominee's name in anticipation of a lawsuit or other liability while the transferor remains in control of the property,
3. Whether there is a close relationship between the nominee and the transferor,
4. Whether they failed to record the conveyance,
5. Whether the transferor retains possession, and
6. Whether the transferor continues to enjoy the benefits of the transferred property. See, e.g., *Spotts v. United States*, 429 F.3d 248 n. 2 (6th Cir. 2005).

In brief, the nominee theory focuses on the relationship between the taxpayer-debtor and the property, for the purpose of discerning whether a taxpayer has engaged in a legal fiction by placing legal title to the property in the hands of another while retaining all (or at least some) of the benefits of being the true owner.

The alter ego theory, in contrast, emphasizes the taxpayer's control over the entity that holds the property. In other words, the alter ego is an entity that holds the property, but it holds the property as an extension of the taxpayer, so that the taxpayer is still actually in control. There again, in deciding whether or not someone is the alter ego of another person, courts consider numerous factors such as:

1. Grossly inadequate capitalization,
2. Failure to observe corporate formalities,
3. Insolvency of the debtor corporation at the time the debt is incurred,
4. Shareholders holding themselves out as personally liable for certain corporate obligations,
5. Diversion of funds or other property of the company property for personal use,
6. Absence of corporate record, and
7. The fact that the corporation was a mere facade for the operations of the dominant shareholder(s). See, e.g., *U.S. v. Toler,* 666 F. Supp. 2d 872, 885 (S.D. Ohio 2009).

And, third, the focus of a fraudulent conveyance is on the intent of the seller. Per the Uniform Fraudulent Conveyances Act adopted by 40 states, a "fraudulent conveyance" occurs if:

1. There is a conveyance of property to third party,
2. There is intent to defraud, hinder, or delay creditors,
3. Debtor received no "reasonably equivalent value" and
4. Remaining assets would be "unreasonably small," or
5. Debtor knew or should have known he would incur debts beyond ability to pay.

That is, the court asks, did the owner get rid of his property at less than fair market value to avoid paying off his creditor(s)?

Restating all of the above, nominee theory looks at the taxpayer/debtor's relationship to the property, alter ego theory looks at the taxpayer/debtor's relationship to the entity that ostensibly owns the property, and fraudulent conveyance theory looks at how the property was sold.

The Sixth Circuit noticed that the three theories share a common ground: the IRS has to prove that, 1) there was inadequate consideration for the transfer, and 2) the transfer of assets was made with the goal of thwarting the collection of taxes. But, as for Holland, the IRS did not meet that burden:

> As for the adequacy of consideration, the transfer of assets itself in the 1998 transaction left Holland financially no worse off than he had been before, since he owned the partnership. Nor was the $15 million loan itself a device to thwart Holland's creditors: $8.4 million of the loan proceeds went back to Holland; another $1.7 million was used to pay off Holland's debts, including the entire $1.4 million of IRS assessments then pending against him. The remaining $5 million or so was used to pay the fees of the lawyers and bankers whom Holland retained to prepare and execute the transaction.

> The government is correct, of course, that those transaction costs "meant that the value of cash and partnership interests Holland ended up with was $5 million less than the value of the royalty assets he paid to the partnership." Gov't Br. at 27. That left $5 million less for Holland's creditors to collect from him. But Holland had just paid off substantially all of his extant creditors in that very transaction. And so far as consideration is concerned, Holland undisputedly received the benefit of those lawyers' and bankers' services in exchange for that $5 million.

Id. at *3.

Stated more succinctly, the Sixth Circuit ruled that even though Holland was a serial tax-debtor, the federal tax liens did not attach to his partnership because when he formed his partnership, 1) he paid the IRS and his other creditors in full, and 2) he paid adequate consideration for that business structure. The court even repeated the fact that Holland completely paid his assessed tax debts when he formed the partnership, and then emphasized that the IRS took more than four years to assess new tax debts against him, saying:

The IRS's more than four-year delay in making additional assessments against Holland—rather than the 1998 transfer of royalty assets itself—is to blame for the government's collection difficulties now.

Id. at *3.

It is refreshing to have a court actually hold that the IRS is to blame for its own failure.

Scott MacPherson *is a member of The MacPherson Group, tax attorneys and longtime members of TFI. Scott is a regular contributor to* PTT *and a speaker at the Taxpayers Defense Conference.*

The Global Warming Army

Another Way to Create More Federal Workers

On October 28, the Biden administration released the framework of its $1.75 trillion economic agenda that it says would raise nearly $2 trillion. Among the laundry list of spending proposals is the idea of $105 billion in new funding to create the so-called Civilian Climate Corps.

In case you might think that Leftists have run out of ways to create new government workers, you would be wrong. The Civilian Climate Corps is intended to be a 300,000-person army tasked to wage war against global warming.

The administration's plan refers to the proposed spending as "Funding to improve resilience to extreme weather, especially near coastal areas, forests, farms, and ranches." I'm not exactly sure what they will do; perhaps shadow-box high temps. Anyway, $105 billion more down the drain.

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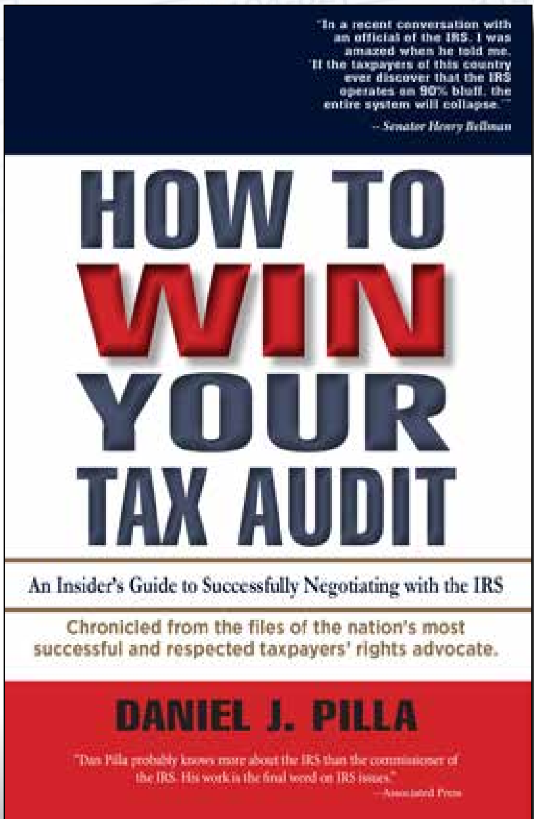

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It's Impossible to Accurately Tax Unrealized Gains

BY TOM GIOVANETTI

One of the useful functions of markets is in the determination of the actual value of a product or service. What is something truly worth? This is a question asked millions of times every day by every kind of participant in the economy.

Very often, the seller of a product or service has an inflated idea of its value, while a potential buyer may have a much different opinion. That's why we say that the true value of something is determined by a willing seller and a willing buyer, after full disclosure of all relevant facts. That negotiation, whether it happens in person, on-line, or in the aisle of a retail store, results in a critical piece of information: What is that thing worth, in its current condition, in this place, at this moment in time? The answer is: Whatever a willing buyer and seller agree to.

That's part of the genius of auction sites like eBay. We've probably all seen eBay sellers list something for a ridiculously high price, and it remains listed for weeks and weeks as the seller takes forever to come to terms with the fact that, because no one is bidding, he or she has overestimated its real value.

Conversely, these days residential real estate is often selling above the asking price. This indicates that the seller actually undervalued the property in the current market. What was the house worth? Whatever a willing buyer was willing to pay, and whatever a willing seller was willing to agree to.

Value cannot be accurately determined without a transaction between a willing buyer and a willing seller after full disclosure of all relevant facts. That's just one reason why the tax on unrealized gains proposed by some Democrats is such a terrible idea.

A gain is not "realized," that is to say, profits are not pocketed, until and unless there is a transaction between a willing buyer and a willing seller. So an unrealized gain simply cannot be accurately valued, and how can you accurately tax wealth that cannot accurately be valued?

You can't. And that's one of the reasons why every past discussion about even attempting to tax unrealized gains has gone absolutely nowhere.

Whether we are talking about a house, a stock or bond, a shopping center, a piece of art, or anything else, there is no accurate valuation unless there is a market transaction. Lacking such a transaction, how would the taxable value of an unrealized gain be determined?

In the case of publicly traded securities, you could just choose an arbitrary calendar date, such as December 31. But that in itself would cause market distortions through tax-motivated buying and selling. For other less liquid goods and non-publicly traded assets, who would determine the taxable value? The Treasury Department?

There are other reasons why a tax on unrealized gains is unworkable, such as the fact that it is almost certainly unconstitutional. But the silver lining of this ridiculous proposal is that it gives us an opportunity to remember the significance of markets in determining real value through voluntary transactions.

Tom Giovanetti *is the President of the Institute for Policy Innovation, Dallas, TX. Go to* www.ipi.org *for more information.*

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:

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Write the word "newsletter" in the subject line.