

TAX TALK

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FROM THE CHAIR

By Caroline D. Ciruolo

As we enter the 2009 legislative session, every day seems to bring more news of declining retirement funds, crashing housing markets, lay offs and bankruptcies. Many of our members are either looking for employment or hoping to maintain their current positions. Law school graduates that were so hopeful when they began their pursuit of a law degree in 2006 are now wondering if they will be able to find a job and repay student loans. Against this backdrop, I spend a lot of time wondering how the Taxation Section can help. While we can not solve the country's economic woes, I believe there are ways that we can help our members and those less fortunate in our communities.

To begin, we must remember that there are many individuals for whom the current economy is nothing new. They have been at the lowest rung of the economic ladder for years and, despite a strong work ethic and desire to improve their position, have been unable to achieve much of what we take for granted. Each year, the Maryland Volunteer Lawyers Service ("MVLS") provides free tax return preparation for low-income families and individuals through the Earned Income Tax Credit clinic as part of the Baltimore CASH Campaign. In 2008, MVLS volunteers prepared 652 federal and Maryland tax returns, resulting in federal tax refunds totaling \$1,100,000. The average Earned Income Tax Credit refund for MVLS clients was \$1,700. The program also helps low-income taxpayers avoid the high cost of predatory "refund anticipation loans" ("RALs"), that carry effective interest rates as high as 170%. The refunds come to those most in need and add much needed spending power to our communities.

MVLS receives no special funding for the tax return preparation clinic and is experiencing significant shortfalls in the clinic budget. In this time of financial crisis, I ask that you donate your time and, if at all possible, your funds to ensure that

this program continues. Please send your donations to Maryland Volunteer Lawyers Service, One North Charles Street, Suite 222, Baltimore, MD 21201. As a § 501(c)(3) nonprofit organization, all contributions to MVLS are tax deductible to the fullest extent allowed by law. For further information, you may contact MVLS Executive Director Bonnie Sullivan at 410-539-6800.

The Section has also formed Maryland's first U.S. Tax Court Pro Bono Program, which encourages members of the Maryland State Bar Association to offer pro bono consultation services to unrepresented taxpayers at U.S. Tax Court calendar calls, during settlement negotiations and in final trial preparation. The majority of taxpayers that file petitions in the U.S. Tax Court appear without representation and are dealing with an unfamiliar maze of rules and procedures. Through the efforts of Pro Bono Committee Chair Todd J. Bornstein and Committee members Robb A. Longman, W. Randolph Shump and Saul B. Abrams, the Section commenced this program in the fall of 2008, appearing at the November and December calendar calls in Baltimore. The Section will continue its efforts this spring and looks forward to expanding its volunteer base.

Next, while those of us fortunate enough to have a job may not have a current position available for a Section member looking for employment, we can still offer our time and our professional network. Take the time to talk to lawyers seeking employment. Learn about their area of practice and experience. Circulate their information to others who may be looking to fill a position. Invite applicants to social and networking functions, introduce them to your colleagues and get them involved in professional activities. It is important for someone looking for a job to stay involved in the legal

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FROM THE CHAIR...

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community, and any help you can offer in this regard will be greatly appreciated.

To this end, the Section sponsored several very successful events in 2008. The annual Advanced Tax Institute ("ATI") was held during the first week in November. The week-long program offered a wide variety of educational sessions. Attendees received updates from Maryland, New Jersey, Delaware and Pennsylvania as well as substantive programs on a wide variety of topics including federal and state procedures, exempt organizations, estates and trusts, real estate, and business transactions.

ATI was followed by the Section's annual Tax Networking Night on November 13, 2009. Despite the unexpected closing of our initial venue less than two weeks prior to the event, Member Services/Program Committee Chair Katrina Kamantauskas-Holder, Darwin Holder and our multi-tasking Secretary/Treasurer Catherine Mary Rafferty were able to relocate to a restaurant across the street from the original venue and host an evening that by all accounts was a resounding success. Thank you for a job extremely well done.

And to round out the year, on December 4, 2008, the Section sponsored its second Symposium at the University of Baltimore - "Expanding the Tax Base: Policy, Legality and Practicality." Drawing speakers from across the country (Joseph Crosby (COO and Senior Director of COST), Sheldon Laskin (counsel to the Multistate Tax Commission), Gerald Langbaum (former Counsel to the Comptroller of Maryland), and Wallace Hellerstein (author of State Taxation)), and across the aisle (State Senator David Brinkley (R) and State Delegate Sheila Hixson (D)), the Symposium offered the opportunity to discuss tax policy and various legislative proposals. The Symposium drew national attention to the Section and its members and an article in State Tax Notes - "House Panel Chair: No Combined Reporting Next Session," thanks to a great deal of time and effort by Jessica R. Lubar, our Section Chair-Elect, and moderators Jeffrey Markowitz, David De Jong and Karen Syrylo.

On March 12, 2009, the Section is sponsoring a joint program with the Real Property Section at 6:30 p.m. at That's Amore in Columbia, Maryland. The program will offer a networking reception followed by an educational program on issues of interest to both sections. There is no cost for this program and I hope you will attend. This is a great opportunity to invite a colleague that may be looking for employment. Introduce them to your fellow Section members and get them involved in Section activities. I look forward to seeing everyone there.

We have also added an Employment Opportunities page to the Section website (http://www.msba.org/sec_comm/

[sections/taxation/employment.asp](http://www.msba.org/sec_comm/sections/taxation/employment.asp)). Advertising is free to all Section members and the Section will remind members to view the site on a regular basis. Our first posting is from the Georgetown University Law Center's Tax Interview Program scheduled to occur this spring. If you have an available position, email the information to Katrina Kamantauskas-Holder at katrina.kamantauskas@holderlaw.com. I invite anyone seeking employment to visit the page and, while there, take a moment to review what the Section's been up to this year.

Taking a larger view, I encourage Section members to get involved in the legislative process. The Section's State Legislation and Regulatory Proposals Committee reviews tax bills as they are introduced and reports this information to the Section Council. If the issue warrants input from the Section, the Committee will prepare comments to the bill for submission to the General Assembly. Section members will often appear before the General Assembly to testify with respect to pending legislation. On January 28, 2009, Steven M. Gevarter represented the Section in Annapolis by testifying with respect to Senate Bill 94, which proposes a new 25% penalty on unpaid sales and use tax. A copy of the Section's comments is included in this edition of Tax Talk. The Section also proposes legislation on matters of interest to its members. For example, the Section has supported legislation drafted by Steven M. Gevarter opposing the extraordinary interest rate assessed by Maryland on unpaid tax liabilities. Maryland's current interest rate is thirteen percent (13%), eight percent (8%) higher than the current federal rate. Although the Comptroller has the authority to abate interest, this authority is rarely exercised. In this time of shrinking resources, convincing the General Assembly to pass legislation that would further reduce the State's collections is, to say the least, an uphill battle. Nonetheless, the Section will continue its efforts to reduce the exorbitant interest rate on behalf of Maryland taxpayers.

Looking back, I am proud of what the Section has accomplished thus far in its 2008/2009 year and I look forward to an active and productive spring. Some of the exciting programs ahead include the annual Irving Shulbank Memorial Dinner on May 14, 2009 at the Belvedere Hotel and the Section's Annual Program (tentatively titled "Losses, Bad Debts, Loan Forgiveness, Workouts, Bankruptcy-- In Bad Economic Times, How To Make The Internal Revenue Code Work For You") at the MSBA Annual Meeting in Ocean City in June.

If you have ideas for improving the Section – its programs or methods of communications – please do not hesitate to contact me. This is your Section and its success depends on your involvement. Thank you for continuing your membership and I look forward to working with each of you in 2009.

Visit www.msba.org/sec_comm/sections/taxation

JOINT SECTION NETWORKING EVENT AND PANEL DISCUSSION

Current Development in Real Estate and Taxation in the Changing Economic Times

Co-sponsored by the Maryland State Bar Association's
Real Property Section and Taxation Section

Location: **That's Amore**
10400 Little Patuxent Parkway
Columbia, Maryland 21044

Date/Time: **Thursday, March 12, 2009, 6:30-8:30 pm**

What: **One hour of networking followed by a one hour panel discussion**
Appetizers, non-alcoholic drinks, and a cash bar will be provided

Topics:

- **Real property tax assessments: appeals and other strategies**
- **Planning with conservation easements: tax benefits and creative planning**
- **Ways to protect yourself and your investors from title company failure**
- **Current developments in workouts and foreclosures**

Please join the Maryland State Bar Association's Real Property and Taxation Sections for a Joint Section Networking Event and Panel Discussion. More details and a list of speakers to follow.

The event is free to attend, however, reservations are required! Please RSVP to: Christopher A. Davis, cdavis@milestockbridge.com or 410-385-3611.

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Comments, contributions, and suggestions are greatly appreciated. Please direct them to the Editor.

Items contained in Tax Talk reflect the views of the individuals who prepared them and do not necessarily reflect the opinions of the MSBA Tax Section.

Calendar of Events for 2009

FEBRUARY

26th Estate and Gift Tax Study Group (Bank of America, Baltimore) - 12:30 PM

MARCH

8th Nominations due for 2009 Tax Excellence Award and 2009 J. Ronald Shiff Memorial Pro Bono Award

10th Tax Controversy Study Group (Rosenberg | Martin | Greenberg, LLP, Baltimore) - 9 AM

10th Employee Benefits Study Group (Whiteford Taylor, Baltimore) - 12 PM

11th Transactional Tax Study Group (Whiteford Taylor, Baltimore) - 12 PM

12th Joint Program with Real Estate Section (That's Amore, Columbia, MD) – 6:30 PM

17th State Tax Study Group (Ober | Kaler, Baltimore) - 8:30 AM

19th Montgomery / PG County Tax Study Group (Law Office of Mary Beth Beattie, Rockville) - 8 AM

26th Estate and Gift Tax Study Group (Bank of America, Baltimore) - 12:30 PM

APRIL

8th Transactional Tax Study Group (Whiteford Taylor, Baltimore) - 12 PM

16th Montgomery / PG County Tax Study Group (Fred B. Goldman, PA, Rockville) - 8 AM

21th State Tax Study Group (Ober | Kaler, Baltimore) - 8:30 AM

23th Tax Controversy Study Group (Rosenberg | Martin | Greenberg, LLP, Baltimore) - 9 AM

23th Estate and Gift Tax Study Group (Bank of America, Baltimore) - 12:30 PM

MAY

4th U.S. Tax Court calendar call (S cases) - MSBA U.S. Tax Court Pro Bono Program

12th Tax Controversy Study Group (Rosenberg | Martin | Greenberg, LLP, Baltimore) - 9 AM

12th Employee Benefits Study Group (Whiteford Taylor, Baltimore) - 12 PM

13th Transactional Tax Study Group (Whiteford Taylor, Baltimore) - 12 PM

14th Annual Irving Shulbank Memorial Dinner and Program (The Belvedere, Baltimore, MD) – 6-9 PM

20th State Tax Study Group (Ober | Kaler, Baltimore) - 8:30 AM

21th Montgomery / PG County Tax Study Group (Location TBA) - 8 AM

28th Estate and Gift Tax Study Group (Bank of America, Baltimore) - 12:30 PM

JUNE

8th U.S. Tax Court calendar call (regular cases) - MSBA U.S. Tax Court Pro Bono Program

10th Transactional Tax Study Group (Whiteford Taylor, Baltimore) - 12 PM

10th-14th MSBA Annual Meeting, Ocean City

18th Estate and Gift Tax Study Group (Bank of America, Baltimore) - 12:30 PM

26th 2009 Institute on Nonprofit Organizations (Ecker Business Training Center, Columbia, MD) - 8:30 a.m. - 4:30 p.m.

Have you visited the Tax Section website lately? If you are looking for something to do, check the main page for information on upcoming events, or visit the Study Groups page for schedules for each of the Tax Section Study Groups. If you are looking for a job, visit our new Employment Opportunities page (and if you have a position to offer, we will post it for you!). If you are looking for a government contact, the 2008 Maryland Tax Practitioner's Handbook is now online. And we have added additional resource materials such as the combined reporting regulations, handouts from IRS meetings, even a video! It all starts at www.msba.org/sec_comm/sections/taxation. Use the tabs at the top and right of the screen to access even more information.

ANNUAL IRVING SHULBANK MEMORIAL

DINNER AND PROGRAM

Thursday May 14, 2009



Reception: 6:00 p.m. ♦ Dinner: 6:45 p.m.
Belvedere Hotel, 1 E. Chase St., Baltimore, MD 21202
Keynote Speaker: **Doug Gansler**, MD Attorney General

Includes presentation of the **2009 Tax Excellence Award** and the
J. Ronald Shiff Memorial Pro Bono Award

CALLING FOR NOMINATIONS FOR THE J. RONALD SHIFF MEMORIAL PRO BONO AWARD

The Maryland State Bar Association's Section of Taxation is seeking nominations for the 2009 J. Ronald Shiff Memorial Pro Bono Award. The Award is presented annually to an attorney (whether in private practice, government, academia, public service or other area) who has demonstrated a commitment to providing legal services to low-income taxpayers. The Award will be presented to the recipient at the Section of Taxation's Annual Irving Shulbank Memorial Dinner and Program to be held on May 14, 2009, at the Belvedere Hotel.

If you know an individual who should be considered, please send your nomination by email (jrlubar@venable.com) or fax (410.244.7742) to Jessica R. Lubar, Chair of the Tax Excellence Award Committee. You must include a brief statement as to why you feel the nominee is worthy of consideration. Nominations forms are available on the Section's website www.msba.org/sec_comm/sections/taxation/. Nominations must be submitted on or before March 8, 2009.

Calling For Nominations For The Tax Excellence Award

The Maryland State Bar Association's Section of Taxation is seeking nominations for the 2009 Tax Excellence Award. The Tax Excellence Award is presented annually to an attorney, law school professor, public official or member of the judiciary who exemplifies professional, academic or public service excellence, integrity, compassion and commitment in the areas of practicing, teaching or developing tax law or tax policy. The Award will be presented to the recipient at the Section of Taxation's **Annual Irving Shulbank Memorial Dinner and Program** to be held on May 14, 2009, at the Belvedere Hotel.

If you know an individual who should be considered, please send your nomination by email (jrlubar@venable.com) or fax (410.244.7742) to Jessica R. Lubar, Chair of the Tax Excellence Award Committee. You must include a brief statement as to why you feel the nominee is worthy of consideration. Nominations forms are available on the Section's website www.msba.org/sec_comm/sections/taxation/. **Nominations must be submitted on or before March 8, 2009.**



Legal assistance for people in need

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December 16, 2008

Dear Tax Section Member:

Every year during tax season, Maryland Volunteer Lawyers Service (MVLS), with the help of many dedicated volunteers from our section, provides a vital service for low-income taxpayers. Between January and March, volunteer lawyers, accountants, paralegals and law students come together to prepare tax returns – *without charge* – for low-income families and individuals. Last year, over 65 MVLS volunteers prepared 652 federal and Maryland tax returns. Our clients received federal tax refunds totaling \$1.1 million!

MVLS undertakes this important project without special funding. Although the costs of running the tax clinic keep escalating, the unrestricted funds to support it keep shrinking. MVLS wants to continue the project, but will need additional funds to do so. **Therefore, I am writing to ask you to make a gift to the 2009 MVLS Tax Clinic.** At a time when so many people are struggling, even a small gift can:

- provide free tax preparation, which can save someone living paycheck-to-paycheck *as much as \$300* for commercial tax preparation;
- ensure that low-income taxpayers obtain the maximum gain from the Earned Income Tax Credit and other tax credits like those for dependent care. Last year, the average EITC refund for MVLS clients was \$1,700;
- help low-income taxpayers avoid high-cost “refund anticipation loans” (RALs) that commercial tax preparers offer, often at effective interest rates as high as 170%!

Please send in your donation today in the enclosed envelope. If you have ever volunteered for the tax clinic, you know what a difference this service makes in the lives of low-income taxpayers. As the economy continues to spiral downward, the MVLS Tax Clinic will make an even bigger difference for hardworking people in need.

Sincerely,

Caroline D. Ciralo, Chair
MSBA Taxation Section

As a 501(c)(3) nonprofit organization, all contributions to Maryland Volunteer Lawyers Service are tax deductible to the fullest extent allowed by law. A copy of our current financial statement is available upon request by contacting MVLS at One North Charles Street, Suite 222, Baltimore, MD 21201 or 410-539-6800. Documents and information submitted to the State of Maryland under the Maryland Charitable Solicitations Act are available from the Office of the Secretary of State, State House, Annapolis, MD 21401 for the cost of copying and postage. MVLS may not expend any funds for any activity prohibited by the Legal Services Corporation Act, 42 U.S.C. 2996 et seq. or by Public Law 104-134.

One North Charles Street / Suite 222 / Baltimore, MD 21201-3710 / info@mvlslaw.org
Administration 410-539-6800 / Intake 410-547-6537 / 800-510-0050 / Fax 443-451-4081





CAROLINE D. CIRAOLLO
Direct Dial: 410.547.7852
E-mail: cciraolo@rosenbergmartin.com

September 19, 2008

The Honorable John O. Colvin
United States Tax Court
400 Second Street, N.W.
Washington, D.C. 20217

**Re: *Taxation Section of the Maryland State Bar Association
U.S. Tax Court Pro Bono Program***

Dear Chief Judge Colvin:

Thank you for speaking with me at the 2008 Joint Fall Meeting of the ABA Section of Taxation in San Francisco about the Court's Pro Bono Program and the Low Income Taxpayer Clinics. I am writing on behalf of Taxation Section of the Maryland State Bar Association to provide the Court with the information requested in section 1.c of the Tax Court's Requirements for Bar-Related Pro Bono Programs.

1. The 2008/2009 Chair of the Pro Bono Committee of the Taxation Section of the Maryland State Bar Association is Todd Bornstein, Esquire, of Selzer Gurvitch Rabin & Obecnyc, Chtd., 4416 East West Highway, Fourth Floor, Bethesda, Maryland 20814-4568, phone: (301) 634-3104, email address: tbornstein@sgrolaw.com.
2. The current U.S. Tax Court Pro Bono Program Coordinator is Caroline D. Ciruolo, Rosenberg | Martin | Greenberg, LLP, 25 South Charles Street, Suite 2115, Baltimore, Maryland 21201, Tax Court Bar # KC0286, phone: (410) 547-7852, email address cciraolo@rosenbergmartin.com.
3. The city which will be served by the Pro Bono Program is Baltimore, Maryland.
4. The Taxation Section of the Maryland State Bar Association, Pro Bono Committee agrees to comply with the U.S. Tax Court Requirements for Bar-Related Pro Bono Programs.
5. Enclosed is a copy of the Pro Bono Program's Guidelines, as described in section 1.b of the Tax Court's Requirements for Bar-Related Pro Bono Programs.

The Honorable John O. Colvin
United States Tax Court
September 19, 2008
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6. This is the initial year of Taxation Section of the Maryland State Bar Association, Pro Bono Committee's U.S. Tax Court Pro Bono Program and, as such, we do not have any statistical information on petitioners with cases pending before the courts and practitioners associated with the pro bono program that have entered appearances and calendar calls. We will provide that information during the year as it becomes available.

The Taxation Section of the Maryland State Bar Association appreciates this opportunity to participate in the Court's Pro Bono Program. In accordance with section 1.d of the Tax Court's Requirements for Bar-Related Pro Bono Programs, the Section will immediately inform the Chief Judge of the Court of any material changes in the information provided herein.

Respectfully yours,



Caroline D. Ciralo
Chair, Taxation Section
Maryland State Bar Association

Enclosure

Rules Governing the Taxation Section of the Maryland State Bar Association

Tax Court Pro Bono Program

1. Goals

The goals of the Tax Court Pro Bono Program (the "Pro Bono Program") of the Taxation Section of the Maryland State Bar Association (the "Section") include the following:

- (a) To assist in the administration of justice in cases in the United States Tax Court by providing legal instruction to *pro se* petitioners in the small case sessions of the United States Tax Court;
- (b) To provide a way in which an individual can be referred to a lawyer participating in the Pro Bono Program;
- (c) To provide information about the availability of legal help that will aid *pro se* taxpayer in either settling or trying his case in the United States Tax Court; and
- (d) To provide general and legal information needed by the public.

2. Administration

(a) The Pro Bono Program shall be operated under these Rules, as amended from time to time. The Pro Bono Program shall be administered by the Pro Bono Committee of the Section (the "Pro Bono Committee"). The Pro Bono Committee shall have full authority to make or delegate all administrative decisions necessary in the operation of the Program.

(b) The Pro Bono Committee shall be composed of at least three (3) members. The Chair of the Pro Bono Committee will be selected by the Section Officers. The Chair of the Section will serve as an advisor to the Pro Bono Committee.

(c) The Chair of the Pro Bono Committee will designate a Pro Bono Program Coordinator, who must be a member of the Section and admitted to practice before the U.S. Tax Court. The Pro Bono Program Coordinator must attend each U.S. Tax Court session in Baltimore, Maryland or, in their absence, appoint a delegate to fulfill his or her responsibilities. The delegate must be a member of the Section and admitted to practice before the U.S. Tax Court.

(d) A quorum of two (2) or more members of the Pro Bono Committee must be present to conduct Pro Bono Committee business.

(e) The Pro Bono Committee shall have the responsibility of regularly reviewing the operation of the Pro Bono Program on at least an annual basis.

(f) The Pro Bono Committee shall meet at least once every six (6) months and, additionally, at the special call of the Chair of the Pro Bono Committee.

(g) The Pro Bono Committee shall periodically review these rules and make such additions and changes as may be deemed appropriate. Any changes recommended by the Pro Bono Committee shall be subject to the approval of the Council of the Section.

3. Participating Attorneys

(a) Participation in the Pro Bono Program shall be open to any member of the Section who has offices within the State and who satisfies the application requirements set forth herein. Such persons shall be referred to hereinafter as an "Applicant" and, once accepted, as a "Participating Attorney."

(b) Each Applicant shall submit his or her name to the Pro Bono Program Coordinator prior to each session of United States Tax Court in the State of Maryland. Each Applicant shall agree to do the following:

(i) Personally participate at the calendar call of the United States Tax Court for consultation that day, free of charge, to any person referred by the Pro Bono Program at the calendar call, unless he or she is unable to do so for ethical reasons;

(ii) Not solicit for hire the services of the Participating Attorney;

(iii) Abide by these Rules, as amended from time to time, and any rules relative to lawyer referral services in the State of Maryland; and

(iv) Waive any and all claims against the State Bar of Maryland, its Council, officers, Governors, members; or employees and against the Pro Bono Committee and its members from any liability for loss as a result of participation in the Pro Bono Program.

(c) The Program shall be operated through a solicitation of Participating Attorneys via e-mail request prior to a United State Tax Court calendar call.

(d) To qualify for participation, an Applicant must be admitted to practice before (or have filed an application to be admitted to practice before) the United States Tax Court at the time the Applicant volunteers.

(e) An Applicant shall be refused participation upon failure to meet any one or more of the requirements set forth herein. Rejected Applicants must be fully advised of the grounds of rejection.

4. Referral Procedure

(a) Assignment of *pro se* persons for advice shall be at the discretion of the Pro Bono Program Coordinator or his or her delegate, who shall strive to be impartial in the appointment process. The individual assigning *pro se* persons for advice shall, in all circumstances, consider referral of cases with non-English speaking *pro se* petitioners to a Participating Attorney who speaks the client's language.

(b) In the event that the Participating Attorney is unable to handle a matter due to conflict of interest, unfamiliarity with the subject matter, or other reasons that render it likely that a second referral may be appropriate, or if it is the Participating Attorney's opinion that representation of the client will not serve the purpose stated in paragraph 1(a) above, the Participating Attorney shall refer the client back to the Pro Bono Program Coordinator or his or her delegate, who will make a second referral (if appropriate).

(c) Each Participating Attorney is expected to handle *pro se* petitioners with the same courtesy and diligence as fee-based clients.

(d) It shall be the obligation of each Participating Attorney to whom a *pro se* petitioner is referred to determine at the outset whether a conflict of interest exists and, if so, to immediately report such determination to the Pro Bono Program Coordinator, or his or her delegate, to facilitate a further referral.

(e) No referral shall be made or refused on the basis of race, sex, age, religion, or national origin.

5. Fees

The Participating Attorney agrees to provide legal instruction free of charge for one day at the United States Tax Court calendar call. The Participating Attorney agrees not to solicit clients for a fee beyond the one-day pro bono period. Should exceptional circumstances arise, the Participating Attorney agrees to advise the Pro Bono Program Coordinator in writing of the circumstances that would result in more than legal advice for the stated one-day period.

6. Geographical Limits

The geographical area to be serviced by the Program shall be the County where the Tax Court proceedings are held within the State of Maryland, or such portion thereof, as may, from time to time, be delimited by the Pro Bono Committee.

7. Resignation, Suspension, and Removal

(a) Any Participating Attorney may resign at any time upon written notification to the Pro Bono Program Coordinator in advance of the United State Tax Court calendar call for the date on which the attorney agreed to participate.

(b) Any Participating Attorney may be removed from any or all participation in the Pro Bono Program, or suspended therefrom for:

- (i) Failure to maintain continuous eligibility under these Rules;
- (ii) Failure to handle Program cases with professional competence and diligence;

- (iii) Charging fees to Program-referred *pro se* petitioners;
- (iv) Falsification of any material statement made in the application for participation;
- (v) Violation of the applicable State Bar Act, Business and Professions Code, or of a Rule of Professional Conduct of the State Bar;
- (vi) Conviction of a crime involving moral turpitude;
- (vii) Failure to comply with these Rules; or
- (viii) Repeated discourtesy to *pro se* petitioners or Area Counsel attorneys.

(c) Before a Participating Attorney may be removed or suspended under Rule 7(b), such member shall be given written notice of the asserted grounds for suspension or removal, which notice shall further contain the date, time, and place of hearing on said matter, and which notice shall be given no less than twenty (20) days prior to said hearing; provided, however, that said hearing may be held on less than twenty (20) days' notice if the Pro Bono Committee determines that public interest is endangered by further delay.

(d) The Pro Bono Committee shall have jurisdiction to hear all matters involving suspension or removal under Rule 7(b) and shall render its written decision in any such matter within forty-five (45) days from the date of such hearing, unless the time is extended with the Participating Attorney's consent.

(e) Any Participating Attorney may appeal the decision of the Pro Bono Committee by giving written notice of appeal to the Pro Bono Committee within ten (10) days of being notified of suspension or removal.

8. Appeals

All decisions of the Pro Bono Committee may be appealed to the Council of the Section. Such Council may take whatever action it deems appropriate in light of the facts and circumstances of the particular appeal. Action by the Council shall be conclusive.

9. Forms, Records, and Reports

(a) The Pro Bono Program shall maintain records of its operations and shall adopt the necessary forms satisfactory to the Section including the following:

- (i) Rules of the Program.
- (ii) Attorney's Application.
- (iii) Accounting records as required.

(b) The Pro Bono Committee shall periodically review such forms and records and make such changes, additions, and deletions as appear appropriate.

(c) All Pro Bono Committee records shall be available for inspection by Pro Bono Committee members, the Officers and Council Members of the Section and qualified representatives of the State Bar of Maryland, at all reasonable times, but shall otherwise be treated as confidential.

(d) Upon request of the Chair of the Section, and in any event at least annually, the Pro Bono Committee Chair shall prepare and submit to the Chair of the Section a report of the activities of the Pro Bono Program.

10. Amendments

These Rules may be amended by vote of a majority of the members of the Pro Bono Committee, present and voting, subject to the approval of the Council of the Section.

**Agreement of Pro Se Participant
In the Taxation Section of the State Bar of Maryland Pro Bono Program**

I, the undersigned, agree and understand that Participating Attorneys in the Taxation Section of the State Bar of Maryland Pro Bono Program are volunteering their time free of charge to provide legal instruction to me related to my case pending before the United States Tax Court. I further understand that said Participating Attorneys are not being hired by me and will not be entering an appearance on my behalf in my case before the United States Tax Court. I understand and agree to the following:

- 1) I will not be charged for the legal instruction given to me during the day of the calendar call of my case before the United States Tax Court.
- 2) The Participating Attorney signing below is agreeing to help me evaluate any settlement offers from Area Counsel of the Internal Revenue Service; and, if a settlement cannot be achieved, to instruct me on procedural issues related to trying my case pro se before the United States Tax Court.
- 3) The Participating Attorney will not hold any discussions with Internal Revenue Service personnel regarding my case without me being present.
- 4) I am not hiring said Participating Attorney and agree not to bring any legal action related to the pro bono legal instruction given during the day of the calendar call of my case or thereafter.

Date: _____

Printed Name of Pro Se Petitioner: _____

Signature of the Pro Se Petitioner: _____

Printed Name of Participating Attorney: _____

Signature of Participating Attorney: _____

UNITED STATES TAX COURT

WASHINGTON, DC 20217

CHAMBERS OF
JOHN O. COLVIN
CHIEF JUDGE

September 29, 2008

Ms. Caroline D. Ciruolo
Rosenberg | Martin | Greenberg, LLP.
25 South Charles Street
Suite 2115
Baltimore, MD 21201

Dear Ms. Ciruolo:

Thank you for your letter dated September 19, 2008, indicating the agreement of the Taxation Section of the Maryland State Bar Association to comply with the Tax Court's requirements pertaining to bar-related pro bono programs.

Based on your letter, the Tax Court is pleased to recognize the Taxation Section of the Maryland State Bar Association through June 30, 2009.

You may contact the Court any time by letter, or via the "contact us" link that appears with the information for Clinics, Student Practice and Pro Bono Programs on our Web site (ustaxcourt.gov), if you have questions or comments regarding the Court's requirements relating to recognition of bar-related pro bono programs.

Please contact us again by February 15, 2009, if you wish to extend this recognition period beyond June 30, 2009.

Thank you again for your interest and response.

Sincerely,

John O. Colvin

John O. Colvin
Chief Judge

cc: Mr. Todd Bornstein, Esq.



Maryland State Bar Association, Inc.

CAROLINE D. CIRAULO
Direct Dial: 410.547.7852
E-mail: cciraolo@rosenbergmartin.com

January 28, 2009

The Honorable Ulysses Currie
Chair, Senate Budget and Taxation Committee
Maryland State Senate
Miller Senate Office Building, 3 West Wing
Annapolis, Maryland 21401

Re: Senate Bill 94

Dear Chairman Currie:

I am writing on behalf of the Taxation Section of the Maryland State Bar Association to provide comments with respect to Senate Bill 94 (the "Bill" or "SB 94"), which is scheduled for a hearing on January 28, 2009.¹ The Bill proposes to create a new penalty for an underpayment of the Maryland sales and use tax if that underpayment is due to gross negligence. The penalty is equal to 25% of the underpayment. The Bill also provides that an underpayment of 25% or more of the required sales and use tax is *prima facie* evidence of gross negligence.

Under current law, failure to pay a tax when due subjects a taxpayer to a penalty not exceeding ten percent (10%) of the unpaid tax. Tax-Gen. § 13-701. If the Comptroller proves by clear and convincing evidence that the taxpayer filed a false return with the intent to evade the payment of tax, the Comptroller is authorized to impose a penalty not exceeding one hundred percent (100%) of the tax due. Tax-Gen. § 13-703. In addition to these penalties, unpaid tax accrues interest at the *minimum* annual statutory rate of thirteen percent (13%). Tax-Gen. 13-604.²

With SB 94, the Comptroller seeks to establish an intermediate penalty limited to unpaid sales and use tax, to be imposed when the Comptroller is unable to carry its

¹ The comments in this letter are solely those of the Taxation Section Council of the Maryland State Bar Association. This letter is not being submitted on behalf of the Maryland State Bar Association.

² Maryland's statutory interest rate is well in excess of the current market rate and has been an issue of heated debate for years. It is the position of the Taxation Section Council that the interest on unpaid tax serves as an additional, severe penalty on all taxpayers.

Honorable Ulysses Currie
January 28, 2009
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burden of establishing that the taxpayer acted with a specific intent to evade but strongly believes that a penalty exceeding 10% of the unpaid tax should be imposed. The Comptroller proposes the imposition of this new penalty in cases involving gross negligence.

Should the General Assembly find that this additional penalty is warranted, it must consider several issues that the Bill fails to address and which, if ignored, will certainly result in contentious disputes and litigation.

1. The Bill fails to address whether the new penalty will be retroactive. Will the penalty be limited to those returns due after the effective date? Or will the penalty also apply to returns due prior to the effective date? And what about returns due prior to the effective dates but at issue in an audit or litigation pending after the effective date? In the interest of fairness, the Section recommends that penalty be limited to those returns due after the effective date.

2. The Bill also fails to address whether the new penalty may be imposed in addition to other penalties in the Tax General Article. Because the Comptroller is seeking this penalty as a means to address situations that do not support the fraud penalty, but call for a penalty greater than 10% of the tax due, it appears that the “stacking” penalties would be contrary to the intent of the Bill and patently unfair. The Section recommends that the Bill be amended to expressly prohibit the imposition of this penalty if penalties under § 13-701 and/or § 13-703 are assessed.

3. The Bill does not explain how the 25% threshold is calculated. Is there a certain number of periods for which a taxpayer must have underreported tax due by 25% prior to the penalty being imposed? Or will the Comptroller have authority to impose this increased penalty based on a single transaction that meets the 25% threshold? If the General Assembly believes this decision should be made by the Comptroller on a case-by-case basis, it should include a clear reasonable cause exception to penalty based on a taxpayer’s individual facts and circumstances. *See* paragraph 6 *infra*.

4. The Bill does not define “gross negligence,” nor does it offer a standard by which a taxpayer may rebut the *prima facie* presumption of gross negligence in cases involving a 25% or more underpayment. By establishing a *prima facie* presumption of gross negligence, the Comptroller is relieved of any obligation to offer evidence that the taxpayer acted with gross negligence. At a *minimum*, the Bill should attempt to define “gross negligence,” if for no other reason than to provide Maryland taxpayers with guidance as to the difference between negligence (calling for a 10% penalty), gross negligence (calling for a 25% penalty) and fraud (calling for a penalty up to 100% of the unpaid tax).

5. The Bill appears to expand the scope of corporate officer liability under the Code. Maryland law currently imposes strict liability for all unpaid sales & use tax, interest and penalties on *certain* corporate officers, members of limited liability companies and partners of limited liability partnerships.³ Tax-Gen. § 11-601(d). Under the current language of the Bill, liability for the new penalty will be imposed against *any* corporate officer, regardless of title or level of responsibility. In light of § 11-601(d), the language in the Bill regarding officer liability is unnecessary. Moreover, it seeks to broaden an already overbroad and often unfair statute. The Section recommends that this portion of the Bill be removed.

6. The Bill fails to guarantee abatement of the penalty if reasonable cause is established. The language of the Bill mirrors § 13-714 of the Tax General Article, which provides that, “[f]or reasonable cause, a tax collector *may* waive a penalty under this subtitle.” (emphasis supplied). This language grants the Comptroller “discretion” to impose a penalty even if a taxpayer establishes reasonable cause. By way of comparison, § 6664(c) of Internal Revenue Code provides that “no penalty shall be imposed. . . with respect to any portion of an underpayment if it is shown that there was reasonable cause for such portion and that the taxpayer acted in good faith with respect to such portion.” In other words, under federal law, a taxpayer has an opportunity to establish reasonable cause prior to a penalty being imposed, and the courts have rejected penalties where a taxpayer has offered such evidence. The Section recommends that the Bill be amended to provide that the penalty will not be imposed with respect to any portion of the underpayment if it is shown that there was reasonable cause for such portion and the taxpayer acted in good faith.

To summarize, if the General Assembly favors the creation of an intermediate penalty for sales and use tax, the Section recommends that:

1. SB 94 be amended to provide that the new penalty is only applicable to sales and use tax returns due after the date of enactment;
2. SB 94 be amended to clearly provide that the 25% penalty under § 13-703.1 is in lieu of, and not in addition to, the 10% penalty established under § 13-701 and/or the 100% penalty established under § 13-703;
3. SB 94 be amended to provide that a taxpayer has the right to challenge the calculation of the 25% underpayment threshold set forth in § 13-

³ For example, under § 11-601(d), any vice president of a company is strictly liable for his employer's tax liability even if his employment was completely unrelated to the company's taxes or financial affairs. The Bill would seek to impose an additional 25% penalty on that vice president if his employer is deemed to have been grossly negligent.

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703.1(a) and (b) based on the individual facts and circumstances of the case;

4. SB 94 be amended to define "gross negligence," or, at a minimum, offer guidance as to the different standards for imposing the 10% penalty under § 13-701, the 25% penalty under proposed § 13-703.1, and the 100% penalty under § 13-703;

5. SB 94 be amended to provide that the penalty *shall* be waived or abated if the taxpayer establishes reasonable cause; and

6. SB 94 be amended to remove any reference to individual or corporate officer liability.

Thank you for this opportunity to express the views of the Taxation Section. Should you have any questions, comments or concerns regarding any of the points set forth herein, please do not hesitate to contact me at (410) 547-7852.

Respectfully yours,



Caroline D. Ciraolo
Chair, Taxation Section
Maryland State Bar Association

FEDERAL TAX TREATMENT OF EMPLOYER-PROVIDED HEALTH INSURANCE FOR DOMESTIC PARTNERS

By Brian R. Della Rocca, Esq.

To fully understand the tax treatment of the receipt of employer-provided health benefits by an employee's domestic partner (regardless of the domestic partner's gender), one must first understand the tax treatment of the receipt of employer-provided health benefits by an employee¹, the employee's spouse, and the employee's dependents².

Employers can deduct the cost of employer-provided health insurance as a Section 162 ordinary and necessary business expense.

An employee's receipt of benefits from his/her employer constitutes income for purposes of Section 61 of the Internal Revenue Code of 1986, as amended (the "Code"). For example, but for a specific statutory provision, the cost of employer-provided health insurance coverage would be required to be included in an employee's gross income under Section 61(a)(1)³.

There are three specific scenarios that could give rise to inclusion of the receipt of employer-provided health benefits in an employee's gross income: (1) the receipt of employer-provided coverage (i.e., employer-paid premiums); (2) the receipt of benefits paid to or on behalf of an employee attributable to medical care received by the employee, the employee's spouse, or a dependent of the employee (i.e., medical expense payment/reimbursement); and (3) the receipt of benefits from the employer (i.e., short-term and long-term disability payments).

Section 106(a) excludes from the gross income of an employee the value of employer-provided coverage under an accident or health plan. An "accident or health plan" is an arrangement for the payment of amounts to employees, employees' spouses, and employees' dependents in the event of personal injuries or sickness⁴.

An employer's payment of all or a

portion of an employee's health insurance premiums or the contribution of an amount to a trust or a fund to be used specifically for reimbursement of the cost of accident and health benefits⁵ is excluded from gross income pursuant to Section 106(a).

Section 105(a) provides that, "except as otherwise provided," amounts received by an employee from accident or health insurance for personal injuries or sickness are taxable if paid by the employer or are attributable to employer contributions that have not been included in the gross income of the employee.

Section 105(b), however, provides that gross income does not include amounts referred to in Section 105(a) if those amounts are paid, directly or indirectly, to the employee to reimburse the employee for expenses incurred for the medical care of the employee, the employee's spouse, or a dependent of the employee. Any medical expense claimed as a Section 213 itemized deduction cannot be excluded pursuant to Section 105.

There lies much confusion between the seemingly small differences between 105(a) and 105(b) but, essentially, the exclusion from gross income is allowed for the reimbursement of medical expenses that have already been paid by the employee and not for an employer's direct payment of those expenses.

Section 104 excludes from gross income amounts received by an employee from accident or health insurance that the employee either paid for directly or are attributable to employer contributions that were includible in the employee's gross income.

Section 104 excludes the receipt of short-term and/or long-term disability benefits by an employee if: (1) the employer-paid premiums were included in the employee's gross income; or (2) the employee-paid the premiums

using after-tax dollars. Thus, if short or long-term disability benefits are paid with after-tax dollars, the benefit received is not included in that employee's gross income.

As most know, federal law does not recognize domestic partnerships (or any other form of non-married partnership, such as civil unions) even if recognized by an individual state or jurisdiction of the United States. The result of this non-recognition is the loss of the exclusions from gross income contained in Sections 104, 105, and 106 for the domestic partner. These exclusions apply solely to the receipt of coverage/benefits by an employee attributable to such employee, the employee's spouse, and the employee's dependents.

Section 7 of Title 1 of the United States Code defines "marriage" as the legal union between one man and one woman as husband and wife and defines "spouse" as a person of the opposite sex who is a husband or a wife (emphasis added). Domestic partners (whether same-sex or opposite-sex) do not "qualify" as a spouse under federal law.

Tax Treatment of Benefits for Domestic Partners

Federal law does not extend the exclusions from gross income described above to benefits received by the employee from his/her employer for the benefit of his/her domestic partner. The typical choice an employee must make is whether to provide the benefit to his/her domestic partner (assuming the employer allows domestic partner benefits) and include the value of those benefits in the employee's gross income or not provide benefits to the domestic partner. However, there may be more choices that are being overlooked.

The issue of employer-provided benefits for unmarried couples in gen-

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DOMESTIC PARTNERS...

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eral has been addressed by the IRS in several private letter rulings. If the employee's jurisdiction or residence recognizes common-law marriage, an opposite-sex domestic partnership can qualify as common-law spouses if the requirements of their jurisdiction are met. This is not available as an option in Maryland as common-law marriage is not recognized.

Opposite-sex domestic partners may be able to qualify for the exclusions as well by seeking dependent treatment of the other partner pursuant to Section 152. The IRS has recognized in a private letter ruling that, if the requirements of Section 152 are met and the partnership is not in violation of local law, a domestic partner can be treated as a dependent.

According to Section 152, a dependent is an individual who: (1) is considered a "qualifying relative" of the employee and has gross income for the taxable year less than the exemption amount of Section 151(d); (2) receives over one-half of his/her support from the employee; (3) has the same principal residence as the employee; and (4) is a member of the employee's household for the entire taxable year of the employee. State and local law determines whether or not domestic partners can be considered "a member of a household." Qualification as a dependent will then extend to the children of the domestic partner as well (assuming the children meet the other requirements of Section 152).

In 2008, legislation was introduced in Maryland giving to domestic partners visitation rights in hospitals and the right to make health care decisions for his/her domestic partner where a properly executed advance medical directive is not in place. This bill, which was approved by Governor O'Malley on May 22, 2008, as Chapter 590, contained a definition of a domestic partnership.

Section 6-101(a) of the Health-Gen. Article of the Maryland Code defines "domestic partnership" as "a

relationship between two individuals who: (1) are at least 18 years old; (2) are not related to each other by blood or marriage within four degrees of consanguinity under civil law rules; (3) are not married or in a civil union or domestic partnership with another individual; and (4) agree to be in a relationship of mutual interdependence in which each individual contributes to the maintenance and support of the other individual and the relationship, even if both individuals are not required to contribute equally to the relationship."

The domestic partner of an employee who is a Maryland resident is more likely to qualify as a dependent (assuming all other requirements are met) because of this newly enacted provision. If that is the case, the value of the employer-provided benefits received by the domestic partner of such employee will be excludible from the employee's gross income.

Conclusion

Many employers in Maryland (and throughout the United States) view providing domestic partner benefits as a way to entice new employees and retain old ones. Purchasing private health insurance can be expensive and is frequently denied if the individual seeking the benefit has a preexisting condition. Employer-provided coverage is typically much cheaper and the Health Insurance Portability and Accountability Act of 1996 ("HIPAA") imposes strict rules regarding preexisting conditions.

With the legal recognition of "domestic partnerships" in Maryland, it is likely that a domestic partner could qualify as a dependent. That being said, if the employee's domestic partner meets the qualifications of Section 152, the benefits provided to the domestic partner would be excludible from gross income pursuant to Section 104, 105 or 106. If the domestic partner does not qualify as a dependent, a fully informed employee may still choose to have his/her domestic part-

ner participate in employer-provided health insurance even with the added income tax burden to the employee.

An employer trying to determine whether to provide these benefits to its employees can rest assured knowing that the cost of providing benefits to the domestic partner benefits will likely qualify for the Section 162 deduction as an ordinary and necessary business expense.

Brian R. Della Rocca, Esq. is a member of the Estate Planning and Probate practice group at Stein, Sperling, Bennett, De Jong, Driscoll & Greenfeig, P.C., working out of the firm's Rockville, Maryland office. In addition to estate planning and probate, he advises clients on employee benefit and executive compensation matters. Mr. Della Rocca was chosen as one of Maryland's 2009 Rising Stars by Super Lawyer's Magazine.

Footnotes

¹For purposes of employer-provided benefits, including health insurance coverage, an "employee" is a common-law employee, including inactive employees, retired employees, former employees, laid-off employees, and employees on leaves of absence. Sole proprietors, partners, LLC members and shareholders in an S Corporation owning more than a 2% interest in the corporation are not employees.

²As defined in Section 152 of the Internal Revenue Code of 1986, as amended.

³Section 61(a)(1) defines "gross income" as "all income from whatever source derived, including... compensation for services, including fees, commissions, fringe benefits, and similar items."

⁴See Section 105(e).

⁵See Treasury Reg. Section 1.106-1.

⁶28 U.S.C.A. Section 1738C.

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PLANNING FOR LIKE-KIND EXCHANGES IN A DOWN MARKET – IS NOW THE TIME TO DROP BEFORE YOU SWAP?

By James G. Dattaro, Esq.

The on-going downward trend in the real estate market should not stop investors from planning to use a “like-kind” exchange when disposing of their real estate holdings. Rather, the current slow down in the market provides opportunities for implementing plans which can be utilized once market conditions improve and the pace of transactions increases. The purpose of this article is to both provide a “primer” of the basic requirements for implementing a like-kind exchange and to discuss planning opportunities in order to properly position clients for future transactions.

Background

Section 1031 of the Internal Revenue Code of 1986, as amended (the “Code”), contains the requirements which must be satisfied in order to execute a tax deferred like-kind exchange. To demonstrate the advantages of the leveraging made available through the use of a 1031 exchange, assume your client previously purchased commercial rental property with respect to which the client has an adjusted cost basis of \$1,000,000. Further assume that the property’s fair market value is now \$3,000,000 (down from a high \$3,500,000 a year ago but still with significant appreciation) and that the property is subject to an outstanding mortgage balance of \$500,000. If the client sold the property for \$3,000,000, the client would pay taxes of approximately \$400,000 on the realized gain of \$2,000,000 (i.e., assuming a combined state and federal capital gains tax of 20% on the \$2,000,000 gain). The actual amount of tax would likely be even greater as a portion of the gain would

in many instances be subject to depreciation recapture which is taxed at the higher ordinary income tax rates. For purposes of this article, a presumed 20% rate will be used in any examples. After paying off the mortgage, the client would have \$2,100,000 to reinvest

\$400,000 of deferred taxes could be used to acquire property worth an additional \$1,600,000. In today’s down markets, that additional leveraged amount would likely yield a high rate of return in the future.

The Basics.

In order to properly effect a like-kind exchange, there are a number of rules to which a taxpayer must adhere. In this regard, the requirements of Section 1031 should be regarded as absolute in that failure to strictly comply with its requirements will almost always result in the loss of the tax deferral.

Rule 1. All Properties Must be of Like-Kind. Both the property which your client sells (the “Relinquished Property”) and the property which the client acquires (the “Replacement Property”) must be of “like-kind” and either held for investment purposes or in connection with a trade or business (but not property held for sale to customers). Thus, for example, a developer generally cannot take advantage of Section 1031 when selling lots since the lots are in effect “inventory” and thus will not qualify. The “like-kind” requirements are, however, otherwise broadly applied with respect to real estate. Improved

or unimproved real estate, rental properties, commercial retail or office space, condominiums, certain long term leases and, under certain circumstances, beach houses and vacation homes which are held primarily for investment and not for personal use¹,

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in other property (\$3,000,000 sales proceeds, less \$500,000 debt and less \$400,000 of tax). By contrast, if the client was to set up an exchange to acquire other “qualifying property” worth at least \$3,000,000, the client could defer paying any of the \$400,000 in taxes. Assuming a willing lender would loan based on a 75% loan-to-value ratio, the

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all are considered to be of like-kind and thus may be exchanged for any of these types of properties. The Internal Revenue Service (the “Service”) has also ruled that development rights in a property may be exchanged for a fee interest in another property.²

Unlike real property, many other forms of investments do not qualify for exchange treatment. For example, stocks, bonds, securities and/or partnership and limited liability company interests are not considered to be “qualifying property” and are specifically excluded from exchange treatment even if the entity’s primary asset is real property.³ This can create significant problems where some of the members of a limited liability company want to reinvest the proceeds from a sale of the entity’s real property by exchanging into a new property, while the others prefer to pocket the cash. The issue arises because, in order to complete an exchange, the same taxpayer (i.e., the LLC) must both sell the Relinquished Property and acquire qualifying Replacement Property. Thus, if the entity were to sell the Relinquished Property, the individual members generally cannot then reinvest their respective shares of the proceeds in one or more Replacement Properties; nor may a member either exchange his LLC membership interest for a membership interest in another LLC or for a fee interest in qualifying real property (other than all of the membership interests in a single member LLC which owns the property).⁴ By carefully planning for a “drop and swap,” however, a member may nonetheless be able to execute an exchange. This will be discussed in greater detail below.

Rule 2. Timing Matters – A Lot. To affect a proper exchange, a taxpayer must both (1) identify one or more Replacement Properties within 45 days after the sale of the Relinquished Property (the “Identification Period”) and (2) acquire the Replacement Property within 180 days after the sale of the Relinquished Property (the “Replace-

ment Period”). The two periods run concurrently, generally from the closing date of the sale of the Relinquished Property, and should be considered to be absolutes, regardless of whether or not either date falls on a weekend or a holiday, and regardless of whether the taxpayer had seemingly valid reasons for his or her failure to comply (i.e., disability, overseas travel, and even death do not extend either deadline). Failure to meet either deadline will result in the loss of exchange treatment and tax will be payable on the sale of the Relinquished Property (either in the year of the sale or, in certain situations, the subsequent year in which the period expires without having been satisfied).

Rule 3. Identifying the Replacement Property. In order to assure compliance with the identification requirement, your client must “unambiguously” identify the potential Replacement Property, in writing, and should deliver the identification to the Qualified Intermediary (discussed below) or to the settlement company involved in the exchange. It is important to note that several Replacement Properties may be exchanged for a single Relinquished Property and vice versa. Once identified, Replacement Properties can be changed or supplemented at any time during the 45-day Identification Period, but not after it has expired. When identifying the Replacement Property or Properties, the following rules apply:

(1) the taxpayer can identify up to three properties without regard to their fair market values; or

(2) the taxpayer can identify any number of properties so long as their aggregate fair market value as determined at the end of the Identification Period does not exceed 200% of the fair market value of the Relinquished Property(ies) as of the date of sale of the Relinquished Property.

These rules are frequently referred to as the “3-property rule” and the “200% rule,” respectively. If a taxpayer violates the 200% rule, he or she will be deemed to have not identified any property and tax will be due on the sale of the Relinquished Property (unless the taxpayer acquires Replacement Property identified during the Identification Period which is valued at 95% or more of the aggregate fair market value of all identified properties – the “95% rule”). In addition, any property acquired by the taxpayer before the expiration of the Identification Period will be treated as having been properly identified.

Rule 4. How Much is Enough? In order to fully defer the tax otherwise due on the sale of the Replacement Property, the taxpayer must satisfy the following two requirements:

- (1) the taxpayer must maintain or trade up in value; and
- (2) the taxpayer must maintain or trade up in equity.

Failure to satisfy both requirements will not exclude the taxpayer from exchange treatment; however, any “shortfall” will be taxed on a “dollar for dollar” basis (but in no event will the taxpayer pay tax on more than the gain realized from the sale of the Replacement Property – in other words, you can’t end up worse off as a result of a failed exchange than if no exchange had been attempted).

Looking at the above example, in order to defer tax on the entire \$2,000,000 of gain, the taxpayer must acquire Replacement Property which in the aggregate has a purchase price of at least \$3,000,000 and the taxpayer must have at least \$2,500,000 of equity in the Replacement Property at the time of acquisition. If the taxpayer acquired property for \$2,500,000 with no debt, the taxpayer would pay taxes on a non-

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deferred gain of \$500,000. The deferred gain is carried over to the Replacement Property because a Replacement Property's basis is equal to its cost basis less any gain deferred on the first sale. In this case, the Replacement Property's basis would be \$1,000,000 (i.e., \$2,500,000 purchase price less \$1,500,000 of deferred gain). The results would be the same if the taxpayer acquired Replacement Property for \$3,000,000 with debt of \$2,000,000. The shortfall in equity is treated as though the taxpayer received \$500,000 of cash (i.e., taxable boot) which was not re-invested in the Replacement Property. There is, however, no requirement that the amount of debt be the same (i.e., the taxpayer could acquire a \$5,000,000 Replacement Property with debt of \$2,000,000 because the amount of equity has increased).

Rule 5. Use of a Qualified Intermediary. Under Section 1031, any boot (i.e., cash or other non-qualifying property) which the taxpayer received or is deemed to have received from the sale of the Relinquished Property will be subject to tax. In order to provide a method for holding the sales proceeds where the Replacement Property will not be acquired until some time after the sale of the Relinquished Property (as is almost always the case – a “deferred exchange”), the regulations provide a safe harbor where the proceeds will be held by a “qualified intermediary” (a “QI”). Under the legal fiction created by the regulations, the taxpayer assigns the contract to sell the Relinquished Property to the QI, which is then deemed to have sold that property and been paid the proceeds. After the taxpayer identifies and contracts to purchase the Replacement Property, the taxpayer assigns that contract to the QI. The QI then acquires the Replacement Property using the escrowed funds and conveys the Replacement Property to the taxpayer to complete the exchange. The regulations permit direct deeding from the taxpayer to the buyer of the Relinquished Property and from the

Replacement Property's owner to the taxpayer in order to avoid multiple assessments of transfer and recordation taxes were the properties required to actually be transferred through the QI.

To comply with the regulations, the taxpayer must enter into an exchange agreement with the QI before closing on the sale of the Relinquished Property. The QI cannot be a related party or affiliate of the taxpayer, nor an accountant or attorney which has provided professional services to the taxpayer during the 2-year period prior to the sale of the Relinquished Property. Typically, QI's are title companies, settlement attorneys or attorneys not otherwise having previous business with the taxpayer. The terms of the exchange agreement must not allow the taxpayer to have access to the funds before the end of the Replacement Period (or, earlier, at the end of the 45-day Identification Period if the taxpayer has failed to identify the Relinquished Property before that time). The escrowed funds may, however, be used by the QI to reimburse the taxpayer for any deposits required to be paid by the taxpayer under the Replacement Property purchase agreement.

Planning for a “Drop and Swap”

As mentioned above, care must be taken when attempting to structure a like-kind exchange of property held by a limited liability company where only some of the members desire to re-invest the sale proceeds in qualifying Replacement Property. The Service has frequently taken the position that Section 1031 will not apply where an entity either redeems out those members which want the cash prior to sale or distributes the Relinquished Property or Replacement Property to those Members who want to do the exchange either immediately before the sale of the Relinquished Property or after the acquisition of the Replacement Property so that some, but not all, of the members can elect (or not

elect) to do a like-kind exchange. The Service's argument is that the company is the taxpayer which sold the Relinquished Property and the member(s) are the taxpayer(s) which acquire(s) the Replacement Property (i.e., that there is no exchange since 1031 requires that the same taxpayer exchange the Relinquished Property for the Replacement Property). Alternatively, the Service has taken the position that either the members or the company, as applicable, did not “hold” the Relinquished Property or the Replacement Property for investment since the property was transferred shortly after receipt by the member or company).⁵

It should be noted that the Service has had mixed results in both the Tax Courts and in the Federal Courts of Appeal with respect to its position.⁶ To combat the Service's position, taxpayers frequently argue that the transactions involved two separate non-taxable events: first, a non-taxable distribution of LLC property to a withdrawing member⁷; and second, a tax deferred, like-kind exchange by that member. The taxpayer's success will depend on being able to establish that the taxpayer was acting on his or her own behalf in negotiating the sale of his or her share of the Relinquished Property. While there is no “bright line” test for establishing this position, the following factors have been recognized by both the courts and the Service as supporting the taxpayer's position:

- (i) Execution and recordation of a deed from the LLC to the withdrawing member of the member's co-tenancy interest in the Relinquished Property (a “TIC”) well in advance of the sale of the Relinquished Property. This tends to demonstrate that the distribution was made for reasons other than simply to accommodate the exchange;

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(ii) Evidence that, subsequent to the distribution of the TIC, the member truly acted as owner of his share of the Relinquished Property;

(iii) Acknowledgment by the buyer of the member's TIC (i.e., some recognition in either the sale documents or in the negotiation process that the buyer was dealing with both the LLC and the withdrawn member);

(iv) Evidence that the member was actively involved in negotiating the terms of the contract of sale;

(v) Evidence that the property's operating income was allocated between the withdrawing member and the LLC during the period of time from the date of distribution to the date of sale (i.e., evidence that income was not simply allocated on the LLC's books among all the members, including the withdrawing member);

(vi) Evidence that property expenses were paid by both the LLC and the withdrawing member between the time of distribution and the time of sale (including closing costs of the sale);

(vii) Evidence that the sales proceeds were allocated and paid to both the LLC and the withdrawn member (i.e., and not solely paid to the LLC and then divided among all of the members in accordance with their respective percentage interests); and

(viii) Acknowledgment by the other members of the direct ownership in the property by the withdrawing member (i.e., evi-

dence of authorizing resolutions, consents, etc.).

While no one factor will likely be determinative, one thing is clear – the passage of time will surely help.⁸ Actions taken immediately prior to or after one leg of the exchange will be given relatively little weight by either the Service or the courts. Thus, clients who are contemplating sales of property once the market improves should be counseled to take advantage of the current down turn in the market in order to better position themselves for future like-kind exchanges. Among the steps to be taken are the following:

1. Deeds should be prepared to distribute the TIC interests from the LLCs to members who want to participate in an exchange. Ideally, the deeds should be recorded. Thus, one must balance the cost of paying any applicable transfer and recordation taxes against the benefit of the tax deferral under Section 1031. It is worth noting that, in addition to putting more time between the “drop” and the “swap,” by distributing the TIC interests now the parties should be able to take advantage of today's lower real property values to reduce the amount of these transfer taxes.

2. The withdrawing members should immediately commence paying their respective pro rata shares of the Relinquished Property's operating expenses. When the Relinquished Property is ultimately sold, these members should also pay their respective pro rata shares of any closing costs (e.g., commissions, transfer taxes, etc.).

3. Any income derived from the Relinquished Property between

the time of withdrawal and the time of sale should be paid to the owners of the TIC's and the LLC as co-owners of the Relinquished Property.

4. All tax returns filed by the LLC and the members should reflect that the withdrawn members are no longer members of the LLC.

5. If there is a management agreement with an outside party, consideration should be given to amending it to reflect the separate TIC interests of the parties.

6. Authorizing LLC resolutions should be prepared whereby all of the members consent to and acknowledge the distribution of the TIC interests to the withdrawing members.

7. Once a purchaser of the Relinquished Property has been identified, that purchaser should be advised, in writing, of the identity of the withdrawn member(s) as co-owner(s) of the Relinquished Property and they should be injected into the negotiations concerning the sale. The purchaser should be instructed to address all future correspondence to both the withdrawn member(s) and to the LLC. The sale contracts and ancillary documents should also reflect all of the TIC interests in the Relinquished Property.

8. The settlement attorney or the title company handling the transaction should be notified to prepare settlement statements which reflect the joint ownership of the Relinquished Property. As a practical matter, this will be required any-

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HOUSE PANEL CHAIR: NO COMBINED REPORTING NEXT SESSION

By Karen Setze

Maryland lawmakers are not going to raise taxes or adopt combined reporting during the 2009 legislative session, House Ways and Means Committee Chair Sheila Hixson (D) said December 4 in Baltimore.

Hixson spoke as part of a panel on state tax policy jointly sponsored by the University of Baltimore Graduate Tax Program and the Maryland State Bar Association Taxation Section.

The question about combined reporting was raised by one of the discussion moderators, Karen Syrylo, a CPA and consultant on taxation to the Maryland Chamber of Commerce.

"Separate corporate reporting is simple if you simply close your eyes and let taxpayers do what they will," said panelist Walter Hellerstein, the Francis Shackelford Distinguished Professor of Taxation at the University of Georgia Law School. "Done well, arms-length separate reporting is much more complex [than combined reporting]."

Panelist Joe Crosby, chief operating officer and senior director of policy for the Council On State Taxation, responded that some audits in combined reporting states have taken many years to complete. By contrast, he said, "there is no separate return jurisdiction with audits older than five years."

Panelist Gerald Langbaum, who recently retired after 33 years with the Maryland Office of the Attorney General, including serving as counsel to the comptroller, said he knew little about combined reporting.

"That's why the legislature created the commission to do a study," Langbaum said.

Syrylo raised the issue of combined reporting in the context of the first meeting of the Maryland Business Tax Reform Commission, to which she was appointed to represent the cham-

ber. Syrylo said that one of the commission's charges is to consider combined reporting.

"Right now, nobody knows" how much revenue the state would generate from combined reporting, Langbaum said. The suggestion "that if we adopt combined reporting that \$ 200 million will appear in our coffers is foolish. Let's see what the likely economic result will be."



Another panelist, Sen. David Brinkley (R), a member of the Senate Budget and Taxation Committee, said the panel discussion was much more rational than those heard in Annapolis.

"The argument that we're always hearing is the emotional aspect: 'those evil corporations, they're not paying their share,'" Brinkley said.

Establishing a commission is a common action for the General Assembly, he said. "We do that all the time when we don't know what to do."

"We're studying [combined reporting] so hard, we're not going to meet again until June," said Hixson, a member of the commission.

The commission was established in 2007 and expanded in 2008 by companion bills HB 664 and SB 444, which also reduced the income tax data that corporations must submit to the Office of the Comptroller. (For HB 664, see Doc 2008-9751 or 2008 STT

91-15. For SB 444, see Doc 2008-9747 or 2008 STT 91-14.) The commission is charged with analyzing the submitted data and making tax reform recommendations to the General Assembly and the governor. The commission is required to make an interim report by December 15, 2010, and issue its final report by December 15, 2011.

Combined reporting is a "fairness issue," Hixson said, since some companies are paying corporate income tax and some aren't. "I've been in the legislature 30 years," and this solution to the problem has been raised many times.

"Combined reporting won't be acted on this session," she said, adding that lawmakers will wait for the commission's report.

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DOMESTIC PARTNERS...

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⁷ See PLRs 9603011, 9431017, 9231062, 9109060, and 9034048; See also PLR 200108010 (allowing exclusion from gross income of benefits to employee's domestic partner received from a voluntary employees' beneficiary association (VEBA)).

⁸ PLR 200339001.

⁹ Section 152(d).

¹⁰ The current personal exemption is \$3,650 and is subject to phase-out.

¹¹ See Section 152(d) and Treasury Reg. Section 1.152-1(b).

¹² See Section 152(f)(3).

¹³ Senate Bill 566 of 2008.

DOWN MARKET...

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way since the withdrawn member's share of the sale's proceeds must be held by a QI (and not paid to either the company or to the member directly) in order to qualify for Section 1031.

In closing, while real estate values have decreased recently, many properties still have significant appreciation which, with proper planning, can be sheltered from taxation through the use of a like-kind exchange. Steps should be taken now to best position clients who own real estate inside an entity.

James G. Dattaro, Esq. is a partner with Selzer Gurvitch Rabin & Obecny, Chartered, in Bethesda, Maryland. In addition to advising clients on structuring like kind exchanges, his areas of practice include taxation of pass through entities and their owners, federal and state tax protests and appeals, choice of entity planning, mergers, acquisitions and other transactions, and general business and tax planning.

Footnotes:

¹ Rev. Proc. 2008-16 (describing requirements for the safe harbor under which the IRS will not challenge whether a vacation home qualifies as investment property)

² PLR 200805012

³ IRC § 1031(a)(2)(D)

⁴ PLR 200118023 (an acquisition of all of the interests in a single member LLC which owns real property is treated as an acquisition of the underlying real property); PLR 200807005 (an acquisition of all of the partnership interests from all of the partners in a partnership which owns real property is treated as an acquisition of the underlying real property)

⁵ Rev. Rul. 77-337 (property distributed in liquidation of a corporation which was immediately exchanged by a shareholder was not held for investment); PLR 9645005; TAM 9818003 (property distributed immediately prior to exchange was not held for investment)

⁶ *Chase v. Commission*, 92 T.C. 874 (1989) (exchange treatment disallowed where distribution of an interest in real property was in contravention of the partnership agreement, partnership negotiated and executed all sale documents and partnership continued to operate the entire property prior to sale); *Bolker v. Commissioner*, 81 T.C. 782 (1983), affirmed 760 F.2d 1039 (9th Cir. 1985) (exchange treatment allowed where shareholder exchanged property three

(3) months after receipt in liquidation of corporation – taxpayer, not the corporation, negotiated the exchange); *Mason v. Commissioner*, TC Memo 1988-273 (court rejects Service's argument that the transaction was in substance an impermissible exchange of partnership interests for real property); *Magneson v. Commissioner*, 753 F.2d 1490 (9th Cir. 1985) (court allowed tax deferred exchange, holding that a contribution to or from a partnership is merely an allowable change in ownership). *Chase*, although decided against the taxpayer, is a particularly helpful case in laying out various elements which would support/undermine the taxpayer's claims.

⁷ IRC § 731 (distributions of property by partnerships to partners are generally tax free, but tax may be triggered if the property was contributed by one of the partners within seven (7) years of the distribution)

⁸ TAM 9645005 (exchange disallowed in connection with condemnation of property where the distribution was delayed until closing was imminent and an agreement with the taxpayer required reconveyance of property if condemnation did not occur)



PARTING SHOTS



Tax Networking Night, November 13, 2009; (from left to right) Darwin Holder, Katrina Kamantauskas-Holder, Jessica Lubar, Caroline Ciralo