



# Tax Dispute Resolution Quarterly

Summer 2018

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# Issue spotlight

## IRS extends CAP program—Modifying some rules and signaling more significant changes may lie ahead

**By Mike Dolan and Timothy McCormally, Washington National Tax**

On August 27, the IRS announced both the continuation of and changes to its Compliance Assurance Process (CAP) program for 2019. The highly lauded CAP program, begun as a pilot in 2005 and made permanent in 2011, provides for “real-time audits” of taxpayers—i.e., the review and resolution of tax issues through open, cooperative, and transparent interactions between the IRS and taxpayers *before the filing of a return*.

This September [article](#) provides an overview of the CAP program, performs a cost-benefit analysis from a taxpayer perspective, and makes some observations on the modifications made by the IRS in [IR-2018-174](#).



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# IRS practice and procedure

- ▶ Tax reform breathes new life into choice of entity decision  
Recent changes in tax rates have altered the “choice of entity” determination for [Read more](#)
- ▶ An excess of uncertainty: The new tax on tax-exempt compensation  
In this June 25 article in *Tax Notes* [Read more](#)
- ▶ Home equity interest may still be deductible  
The new tax law, originally known as the Tax Cuts and Jobs Act [Read more](#)



## Tax reform breathes new life into choice of entity decision

**By Deanna Walton Harris, Debbie Fields, and Barbara Rasch, Washington National Tax**

Recent changes in tax rates have altered the “choice of entity” determination for new and existing businesses. This July [article](#) describes some of the federal tax considerations involved when choosing or changing the tax classification of a closely held business entity and explains how changes to the taxation of income earned or distributed by business entities may affect those considerations. The article also illustrates the consequences of the choice if additional changes in the federal tax law make the entity selected less desirable in the future.

## An excess of uncertainty: The new tax on tax-exempt compensation

**By Alexandra O. Mitchell, Preston J. Quesenberry, and Randall S. Thomas, Washington National Tax**

In this June 25 [article](#) in *Tax Notes*, the authors examine the new excise tax imposed on remuneration exceeding \$1 million paid by tax-exempt organizations to some employees, and they discuss technical issues arising from the statute’s borrowing of several terms and concepts from section 162(m). The authors also explore numerous questions raised by other defined terms in the statute and offer possible interpretations for consideration.

## Accounting methods and credits considerations post-tax reform

The new tax law enacted in December 2017 brings a multitude of changes to the Internal Revenue Code. It not only reduced the corporate tax rate but has had an immediate impact on income and expense recognition, cost, recovery, and credits.

From increased expensing, income inclusion, mandatory repatriation, BEAT, to section 199 repeal, KPMG LLP’s [Accounting Methods and Credit Services \(AMCS\) team](#) can assist companies in all industries achieve greater tax efficiency. AMCS uses a multi-disciplinary approach and a consistent tax consulting methodology to help companies manage their cash taxes, effective tax rate, and tax risks.

## IRS tax tip: Here’s what taxpayers should know about penalty relief

A taxpayer may qualify for relief from some penalties under certain circumstances. On June 28, the IRS issued [Tax Tip 2018–100](#) advising the public on requesting the IRS to first consider the reasonable cause relief provision in order to preserve “first time abatement,” which the taxpayers can only use every 3 years.

# Home equity interest may still be deductible

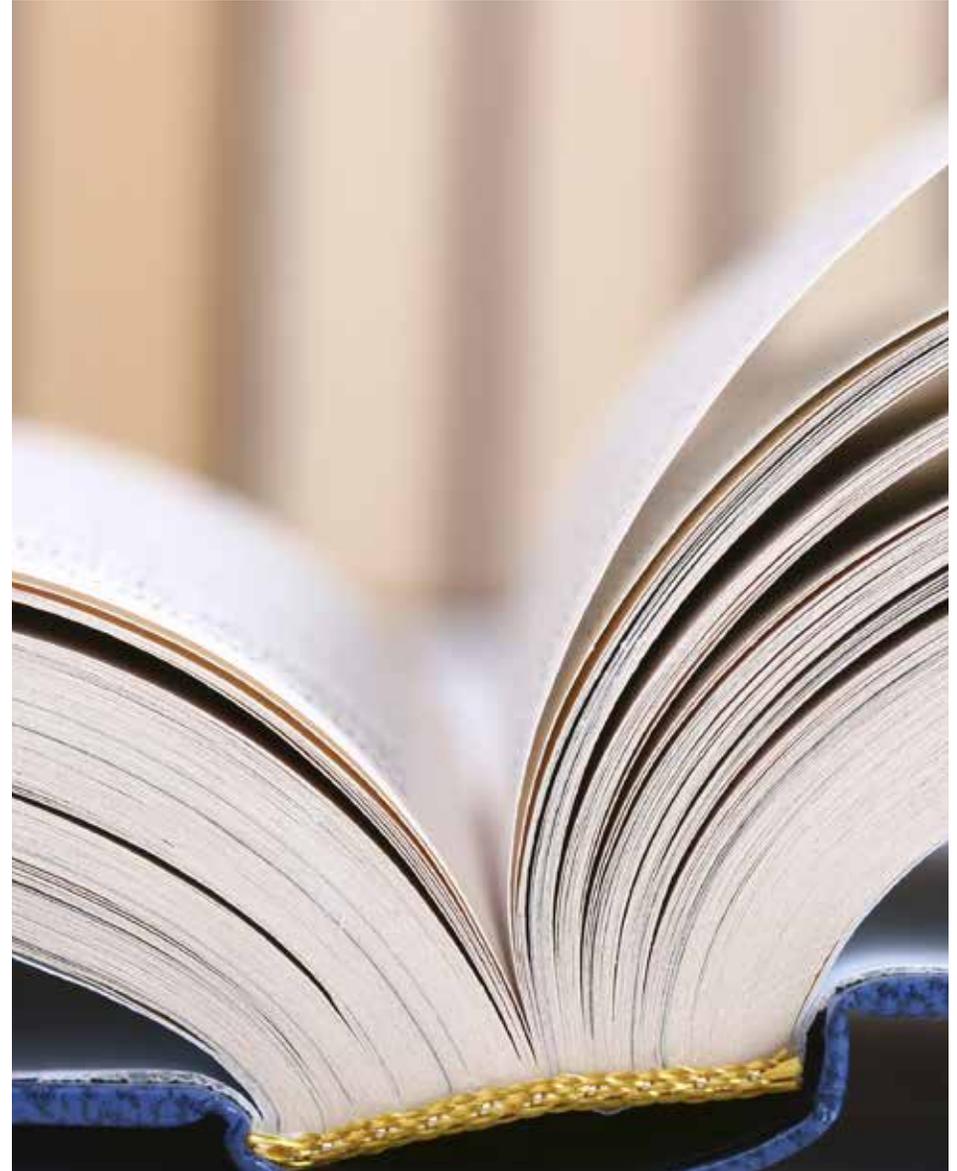
**By Liz L'Hommedieu and Chris Stroeer, Washington National Tax**

The new tax law, originally known as the Tax Cuts and Jobs Act, Pub. L. No. 115-97, includes substantial changes to the taxation of individuals and businesses of all sizes. Among these changes, certain aspects of an individual's deduction for home equity interest have been temporarily modified. For tax years beginning after Dec. 31, 2017, and before Jan. 1, 2026, an individual's deduction for qualified residence interest expense has been amended to disallow a deduction for interest on "home equity indebtedness." However, when it comes to home equity lending and borrowing, there is more than meets the eye for purposes of this deduction. "Home equity indebtedness" is a specifically defined term, and to the extent certain criteria are met, a taxpayer may still be able to deduct interest paid on a home equity loan, home equity line of credit, second mortgage, or similar product.

This [article](#) in the June 26 issue of Bloomberg BNA's *Daily Tax Report* details more about home equity interest under the new tax law.

## Webcast: International tax reform issues for banks

During this one-hour June 5 webcast, KPMG international tax and banking professionals provided insights into the current international tax landscape and the more common issues facing banking organizations. Topics covered include Global Intangible Low-Taxed Income (GILTI) and expense allocation considerations for banks, foreign tax credit "basket" for branch income, Base Erosion and Anti-abuse Tax (BEAT) and base erosion percentage considerations for banks and securities dealers, and the outlook on anticipated guidance.



# Enforcement trends

- ▶ Foreign information reporting penalties:  
Assessable or not?  
The IRS automatically assesses and collects monetary penalties under sections 6038 and 6038A—chapter 61 penalties. ([Read more](#))
- ▶ Tax Court sides with IRS, rejects captive's insurance company status  
In June, the U.S. Tax Court found that a corporation was not a captive insurance company, but rather a foreign corporation ([Read more](#))



## Foreign information reporting penalties: Assessable or not?

**By Erin Collins and Garrett Hahn, Tax Controversy Services**

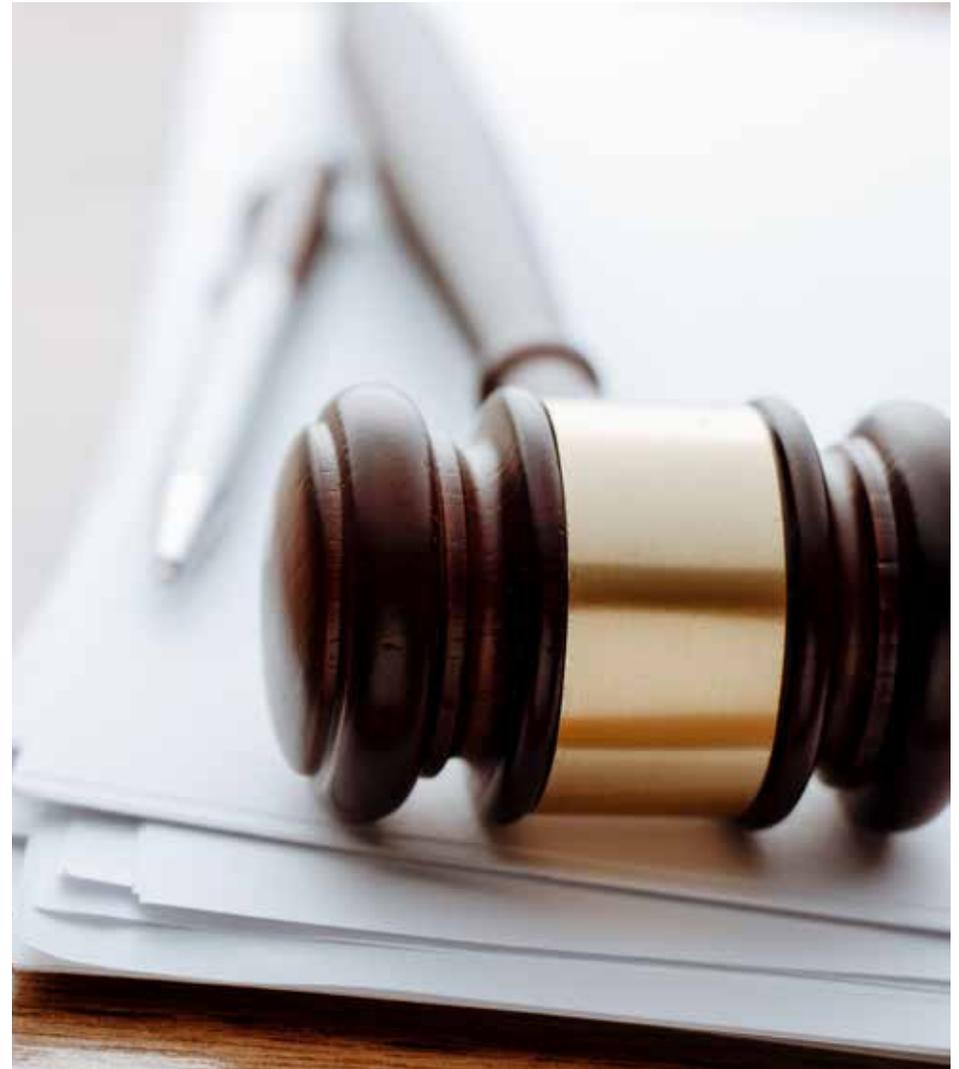
The IRS automatically assesses and collects monetary penalties under sections 6038 and 6038A—chapter 61 penalties. But where in the Code is its authority to treat these penalties as assessable? How are these chapter 61 penalties within the scope of “assessable penalties”? They don’t appear to fall under assessable penalties within chapter 68 and subchapter B. Tax practitioners, however, have generally assumed the IRS has authority to assess and collect penalties under sections 6038 and 6038A.

This [article](#) from the July 9 issue of *Tax Notes*, questions the IRS’s statutory authority to treat monetary penalties under sections 6038 and 6038A as assessable.

## Tax Court sides with IRS, rejects captive’s insurance company status

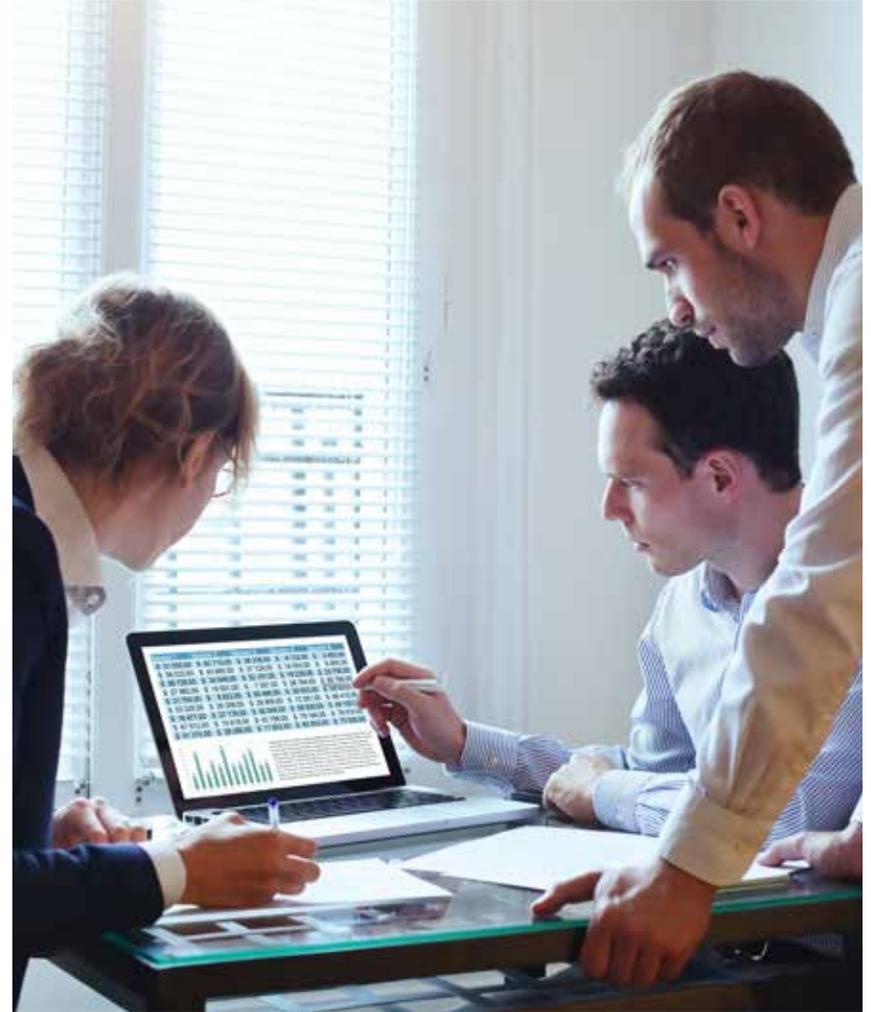
**By Sheryl Flum, Fred Campbell-Mohn, Liz Young, and Rob Nelson,  
Washington National Tax**

In June, the U.S. Tax Court found that a corporation was not a captive insurance company, but rather a foreign corporation subject to the 30% withholding tax on its “fixed or determinable annual or periodical” (FDAP) income imposed by section 881(a)(1). Read an overview and initial observations of the case, *Reserve Mechanical Corp. v. Commissioner*, T.C. Memo 2018-86 (June 18, 2018), in this June KPMG [report](#).



# State & local tax

- ▶ *Quill* overturned in *Wayfair* decision  
The U.S. Supreme Court on June 21 held in favor of the state in *South Dakota v. Wayfair, Inc.* ([Read more](#))
- ▶ Conformity Update 2018: An overview of 2018 corporate conformity bills  
By mid-June, most fixed-date states—those states that tie to the Internal Revenue Code ([Read more](#))
- ▶ State and local incentive arrangements from REIT perspective  
Nearly three years after taxpayer requests, the IRS issued on April 20, 2018, ([Read more](#))



## Quill overturned in Wayfair decision

The U.S. Supreme Court on June 21 held in favor of the state in *South Dakota v. Wayfair, Inc.*—a sweeping decision in which the Court concluded that the physical presence sales and use tax nexus rule last articulated by the U.S. Supreme Court in *Quill* is “unsound and incorrect.”

In the five-to-four decision authored by Justice Kennedy, the Court held that the Court’s earlier decisions in *Quill Corp. v. North Dakota*, 504 U.S. 298 (1992), and *National Bellas Hess, Inc. v. Department of Revenue of Ill.*, 386 U.S. 753 (1967), “should be, and now are, overruled.” The Court then vacated the South Dakota decision holding in favor of the taxpayers and remanded the case to the state court for “further proceedings not inconsistent with this opinion.”

- August 30 webcast: [What does the Supreme Court Wayfair decision mean for tax-exempt organizations?](#)
- July 12 KPMG report: [Financial reporting implications of Wayfair](#)
- June 26 webcast: [The wait for Wayfair is over – What’s next?](#)
- June 21 Tax News Flash: [U.S. Supreme Court: Initial impressions of Wayfair decision](#)

## Webcast: Recent developments affecting banking industry

During this August 22 [webcast](#), KPMG subject matter professionals from the Washington National Tax and State and Local Tax practices discussed recent federal and state tax developments, and the effects on the banking industry.

Topics included:

- *Wayfair* and key considerations for banks
- State developments, including NJ tax reform
- State tax considerations for qualified opportunity zones
- Proposed section 199A regulations and the implications for S corporation banks

## Conformity Update 2018: An overview of 2018 corporate conformity bills

### By the SALT group in Washington National Tax

By mid-June, most fixed-date states—those states that tie to the Internal Revenue Code as of a specific date—had acted in 2018 to update their conformity in response to the 2017 federal tax law. The only fixed-date states that had not acted at all to update their conformity are Arkansas, California, New Hampshire, and Texas. Certain of these states have unique conformity to the Code and California and Texas do not update each year.

In other fixed-date states, conformity legislation was proposed, but never made it across the finish line. In South Carolina, lawmakers failed to enact conformity legislation during the regular session, but conformity is on the agenda for a special session. In Maine and Minnesota, conformity was included in larger tax bills that failed to pass or were vetoed during the regular sessions and there are no (current) plans to hold special sessions. Lastly, at press time various bills containing conformity provisions have failed in Vermont.

And not to be outdone, several rolling conformity states—those states that tie to the Internal Revenue Code in effect for the year—also enacted legislation addressing various aspects of federal tax reform.

Because there are some complexities to the conformity bills enacted during Q2 and other legislation addressing tax reform, this June 2018 [article](#) summarizes the bills and any provisions in the bills that specifically address key federal corporate tax reform changes in lieu of including details in the checklist. This article includes the conformity bills enacted in Q1 and Q2.

## State and local incentive arrangements from REIT perspective

### By David Lee, Washington National Tax, and Orla O'Connor, Business Tax Services

Nearly three years after taxpayer requests, the IRS issued on April 20, 2018, three identical private letter rulings addressing whether the right to receive payments out of new tax revenue collected by a municipality as the result of a real estate development is a qualifying real estate investment trust (REIT) asset and whether the payments are qualifying REIT income.

An [article](#) in the July 11 issue of Bloomberg BNA's *Daily Tax Report* summarizes and contextualizes the three IRS rulings and relevant tax rules concerning tax treatment under the REIT rules for incentive payments from a municipality involving tax increment financing, and attempts to explain why the delay in issuing the rulings.

## 2018 second quarter summary of state, local tax changes

This [report](#), prepared by KPMG's State and Local Tax practice, provides a summary of state and local tax developments for the second quarter of 2018 in table format.

# Global tax disputes

## Corporate board oversight and governance

With the critical role that corporate culture plays in driving a company's performance and reputation, boards today are reassessing their approach to oversight of culture. KPMG's latest report, [Board oversight of corporate culture](#), shares highlights and takeaways from KPMG's Director Roundtable series.

The Financial Reporting Council has issued a revised United Kingdom Corporate Governance Code to reflect the changing business environment and focuses on long-term success, sustainability, and public trust in business. Read a [report](#) on it prepared by KPMG's Board Leadership Centre (UK).



## Global Tax Disputes Update— June 2018

With tax audit and dispute activity rising in almost every country, keeping up with developments is more important than ever. In this edition of *Global Tax Disputes Update*, you'll find briefings on key news, events, and thought leadership from Global Tax Dispute Resolution & Controversy professionals in KPMG member firms worldwide. Staying informed can be a crucial first line of defense as you manage your disputes around the globe.

Make sure to view our past issues of [Global Tax Disputes Update](#).



**Sharon Katz-Pearlman**

Head of KPMG's Global Tax Dispute Resolution & Controversy

# OECD & BEPS

## KPMG comments on future revisions to OECD transfer pricing guidelines

The Organisation for Economic Co-operation and Development (OECD) in May 2018 announced it was considering two new projects to revise guidance in the OECD's Transfer Pricing Guidelines—specifically possible changes to Chapter IV (administrative approaches) and Chapter VII (intra-group services).

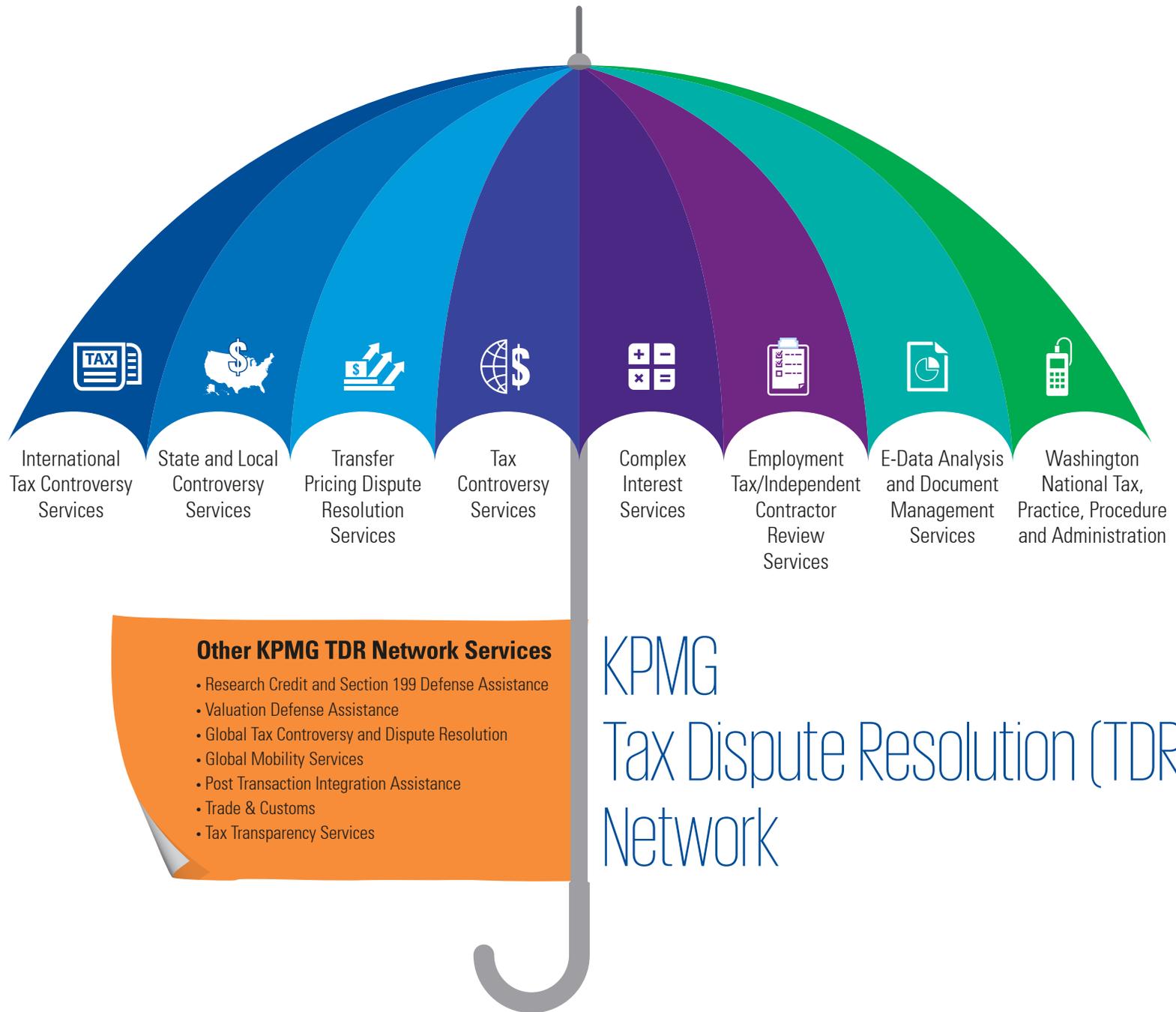
On June 20, 2108, KPMG's Transfer Pricing Services group submitted comments to the OECD on the potential amendments to the OECD Transfer Pricing Guidelines.

- [KPMG's comments](#) on the scope of the future revision of Chapter IV (administrative approaches) of the Transfer Pricing Guidelines
- [KPMG's comments](#) on the scope of the future revision of Chapter VII (intra-group services) of the Transfer Pricing Guidelines

## BEPS Action 13: Latest country implementation update

Updated weekly, this summary [report](#) in table format offers a snapshot of implementation of country-by-country (CbC) reporting and Master file/Local file documentation requirements around the world.





**Other KPMG TDR Network Services**

- Research Credit and Section 199 Defense Assistance
- Valuation Defense Assistance
- Global Tax Controversy and Dispute Resolution
- Global Mobility Services
- Post Transaction Integration Assistance
- Trade & Customs
- Tax Transparency Services

KPMG  
Tax Dispute Resolution (TDR)  
Network

# Contacts

## Tax Dispute Resolution– National Leader

Sharon D. Katz-Pearlman  
skatzpearlman@kpmg.com

## Business Unit Leader East Mid-South and Chesapeake

Michael P. Dolan  
mpdolan@kpmg.com

## New England

Thomas D. Greenaway  
tgreenaway@kpmg.com

## New York Metro/Short Hills

Sharon D. Katz-Pearlman  
skatzpearlman@kpmg.com

## Pennsylvania

Justin Donatello  
jdonatello@kpmg.com

## Short Hills

Miri Forster  
mcfoster@kpmg.com

## Business Unit Leader West Gateway West/North Heartland

Jeffrey S. Luechtefeld  
jluechtefeld@kpmg.com

## Chicago Metro/Mid-America

Kathleen C. Schlenzig  
kschlenzig@kpmg.com

## Dallas/Denver

Victoria J. Sherlock  
vsherlock@kpmg.com

## Pacific Northwest

Erin M. Collins  
emcollins@kpmg.com

David R. Unger

dunger@kpmg.com

## Contributors

### Fred Campbell-Mohn

fcampbellmohn@kpmg.com

### Erin Collins

emcollins@kpmg.com

### Mike Dolan

mpdolan@kpmg.com

### Debbie Fields

dafields@kpmg.com

### Sheryl Flum

sflum@kpmg.com

### Garrett Hahn

ghahn@kpmg.com

### Deanna Walton Harris

dwharris@kpmg.com

### David Lee

dwlee@kpmg.com

### Liz L’Hommedieu

elhommedieu@kpmg.com

### Timothy McCormally

tmccormally@kpmg.com

### Alexandra Mitchell

aomitchell@kpmg.com

### Rob Nelson

rsnelson@kpmg.com

### Orla O’Connor

orlaoconnor@kpmg.com

### Preston Quesenberry

pquesenberry@kpmg.com

### Barbara Rasch

brasch@kpmg.com

### Randall Thomas

randallthomas@kpmg.com

### Liz Young

epetrie@kpmg.com

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*KPMG’s Tax Dispute Resolution Services network helps companies prevent, prepare for, and respond to challenges by the varying tax authorities. The network is a national team of tax professionals, who assist companies in identifying, managing, and mitigating potential tax risks and exposures.*