

ATTACHMENT "B"

Frost & Associates, LLC
Attorneys at Law

ATTORNEYS

GLEN E. FROST**A
JESSICA R. MARINE
ELI S. NOFF
KAITLYN A. LOUGHNER**
ROBERT OWINGS
KRISTIN LECLAIR ZUROWSKI*
NICHOLAS E. BERGER
LEANNE FRYER BROYLES
REBECCA J. SHEPPARD
ROBERT HAMILTON**
MARY FRANCES LUNDSTEDT

888 Bridgeport Road, Suite 400 | Annapolis, MD 21403

Phone: 410-497-5947 | Fax: 866-235-9405

Additional Locations:

Columbia, MD | Washington, DC
Fairfax, VA | Miami, FL

www.FrostTaxLaw.com

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OF COUNSEL

DENNIS BOYLE***
JUSTIN HUGHES***

ENROLLED AGENTS

ALICIA L. CHIRY*

Also Member of DC Bar *
Also Member of FL Bar *
Also Member of PA Bar **
Also Member of NY Bar *
Also Member of VA Bar Δ
Also Member of AK Bar Ω
Also Member of NJ Bar α
Member of PA Bar Only *
Licensed to Practice Before the IRS*

Re: Information Regarding the Ruling and Members' Tax Returns

Attached is an outline to put the Ruling in context for your members.

If you have any additional questions, I can be reached at 410-497-5947. Thank you for your assistance with this important matter.

Respectfully submitted,


Justin Hughes, Esq.

Enclosures: Outline: "Information Regarding the Ruling & Your Taxes"

Information Regarding the Ruling & Your Taxes
August 18, 2017

This outline is to aid your tax professional in making an independent assessment of whether or not you can claim that the amount reported to you on Form 1099-C from ODCP can be excluded from taxable income. Please note, as discussed below, the only taxpayer that can directly rely on the ruling is the representative taxpayer that submitted the Ruling. Nevertheless, the Ruling can be used in determining whether there is "substantial authority" for your position on your federal income tax return.

1. Summary

- a. On August 4, 2017, the IRS granted the representative taxpayer's (the "Taxpayer") private letter ruling request regarding Form 1099-C from Office of D.C. Pensions ("ODCP") and issued a favorable ruling to the taxpayer (the "Ruling").
- b. *The ruling is premised on the fact that the taxpayer requesting the ruling had properly reported, on his prior federal income tax returns, all income reported to him on Form 1099-R for years in which he received distributions from the Office of D.C. Pensions.*
- c. A redacted copy of the Ruling will not be made publicly available by the IRS for several months. At this time, it is not known how the Ruling will be cited when disclosed to the public (e.g., PLR 2017XXXXXX). However, the Retired Police Offices and Retired Firefighters Associations (the "Associations") will make a redacted copy available for members' use in analyzing their tax position with respect to the Form 1099-C issued by Office of D.C. Pensions ("ODCP").
- d. This document and attachments should be shared with your tax return preparer. Should you or your preparer wish to contact Frost & Associates, LLC for additional consultation, you may do so. However, any fees or costs related to the consultation are the responsibility of the member who seeks Frost & Associates, LLC individual assistance.

2. Ruling Discussion

- a. Generally, the Ruling holds that, although ODCP was technically required to issue the Form 1099-C to the Taxpayer, the amount on Form 1099-C ("Total Overpayment Amount") did not give rise to cancellation of indebtedness income for federal income tax purposes. As discussed in more detail below, the IRS agreed with the desired ruling (i.e., the amount on Form 1099-C was not taxable) in the private letter ruling request, but IRS used a different technical analysis to reach the desired result. While this is the most important aspect of the ruling, we want to apprise Members of the technical analysis should an IRS agent or employee challenge the position.
- b. The IRS's technical position in the Ruling is that because the Taxpayer had already included the Total Overpayment Amount on his personal income tax

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return when previously reported to him on Form 1099-R, ODCP's waiver of the legal obligation to repay the Total Overpayment Amount did not give rise to cancellation of indebtedness income. This position is reached on general federal income tax principles. The IRS did not provide any citations to reach this conclusion. While this position has merit, it is difficult to support with precedent (i.e., case law, IRS rulings, etc).

- c. Our position in the private letter ruling request assumed that the Form 1099-C generated cancellation of indebtedness income. However, we believed that the cancellation of indebtedness income was subject to an exception which rendered the cancellation of indebtedness non-taxable. This position was provided in detail in a prior statement to the Associations on December 13, 2016, which is attached. The December 13, 2016 statement set forth the law and analysis that the private letter ruling request was based upon.

3. Precedential Value of Ruling

- a. The Internal Revenue Code provides that letter rulings may not be used or cited as precedent, except in very limited circumstances. However, private letter rulings may be considered in determining whether a taxpayer's position is supported by substantial authority (i.e., whether or not the position is subject to penalty for a substantial understatement). Thus, the Ruling should provide some comfort if your fact pattern is consistent with the facts set forth in the Ruling. **Specifically, in order to fit the fact pattern in the Ruling, you must have properly reported, on your prior federal income tax returns, all income reported to you on Form 1099-R for years in which you received distributions from the ODCP. Underreporting on prior returns will likely cause some or all of the amount on the Form 1099-C to be taxable.**

4. Considerations When Filing

- a. If you and your tax professional conclude that you have paid tax on all of the amounts reported to you on Form 1099-R from ODCP and you wish to take the position that the Form 1099-C does not give rise to taxable income on your return, we suggest that you and your tax professional consider:
 - i. When you file your tax return for the year including the Form 1099-C (either amended or original), that your preparer include Form 8275 to indicate the position that you are claiming on your tax return. Reference can be made to the Ruling and indicate if your situations matches the fact pattern in the Ruling. In referring to the Ruling, you can cite "PLR – CC:ITA:B04; PLR-105098-17, dated July 31, 2017". Note this is an internal IRS reference number, and it may not be the final citation that will be used when the Ruling is published by the IRS.

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- ii. Your tax return preparer should consider including the amount from Form 1099-C on Line 21 (as in an income inclusion), but also include an offsetting line item on Line 21 (e.g., "see Form 8275 - basis in previously reported income" or "see Form 8275" if your software does not provide sufficient space). This would report the item, but the net result should be zero. If you do not include the Form 1099-C amount, you are at increased risk of receiving an IRS matching notice.
- iii. If you have already filed your return, included the amount from Form 1099-C, and paid tax on that amount, then you will need to file an amended return. In most cases, under the statute of limitations, a claim for credit or refund must be filed within 3 years from the time the return was filed or 2 years from the time the tax was paid, whichever of such periods expires the later, or if no return was filed by the taxpayer, within 2 years from the time the tax was paid.

b. A copy of the redacted PLR should NOT be attached to your personal income tax return.

5. Summary of Form 8275

- a. Form 8275 is a preventative measure and does not automatically cause an IRS examination. Form 8275 is used by taxpayers and tax return preparers to disclose items or positions that are not otherwise adequately disclosed on a tax return to avoid certain penalties. The form is filed to avoid the portions of the accuracy-related penalty due to disregard of rules or to a substantial understatement of income tax for non-tax shelter items if the return position has a reasonable basis. It can also be used for disclosures relating to the economic substance penalty and the preparer penalties for tax understatements due to unreasonable positions or disregard of rules.