



## What The IRS Criminal Investigation Fiscal Year 2017 Annual Business Report Means For Tax Professionals And Taxpayers

By *Josh O. Ungerman, J.D., CPA*

### Comments on the State of IRS Criminal Investigation (CI)

The Internal Revenue Service Criminal Investigation (“IRS CI”) 2017 Annual Report (“Report”) reflects forward thinking vision of Don Fort, Chief, IRS Criminal Investigation. The numbers unmistakably demonstrate that years of congressional budget cuts have taken their toll. In the last five (5) years the number of investigations initiated by the IRS CI dropped an alarming 36%. The incarceration rate was down to 67%.

The statistics demonstrate diminishing resources to IRS CI are having a significant effect. Some tax professionals openly ask how low the resources to IRS CI will go before a percentage of the taxpaying public are no longer motivated to comply with the tax laws and, indeed, actively work to evade them. Many tax professionals believe a dangerous era of unchecked criminal noncompliance exists today.

IRS CI, with so few resources, must nonetheless succeed in its mission of having tax prosecutions directly impact voluntary compliance through criminal deterrence? The path is to increase the

IRS’s budget so the IRS can support a strong voluntary compliance tax system through increased examinations and investigations. For the time being, IRS CI will pursue high-impact cases. Through intense data analytics, IRS CI will identify high impact taxpayers in a very efficient and futuristic manner.

### Chief’s Message

The Chief’s message emphasizes IRS CI successes, noting that, when there is a sophisticated financial component to an investigation, prosecutors usually contact IRS CI for assistance.

The Chief tackles the budget crisis head-on, admitting that resource issues make it impossible to be involved in every investigation in which IRS CI is asked to participate. He discloses that IRS CI has the same number of special agents – around 2,200 – as it did 50 years ago. Despite low staffing, the Chief lays out that financial crime has not diminished during that time – in fact, it has proliferated in the age of the Internet, international financial crimes, and virtual currency. Regardless IRS CI continues to investigate some of the most complicated cases in the agency’s

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### Message from the Chair Anne Gordon

Dear Members of the Federal Bar Association Section on Taxation,



I am honored to serve as the chair of the Section for the 2018-2019 year and am pleased to update you all on the busy year the Section has had thus far, and to provide insight on our plans for the remainder of the year. It is my hope that this year will be the most consequential yet for the Section.

Significantly, the Section has continued to foster a relationship with the tax community outside Washington. The Section has long strived to benefit members across the country, and this year aims to continue that outreach. The Beyond the Beltway committee, led by Ryan Montgomery (Morgan Lewis & Bockius) & Alan Williams (I.R.S. Office of Chief Counsel), has already held events in a number of cities including Dallas, Chicago, New York, and Miami. These events have attracted many current and future members of the Section and have hosted Tax Court judges, government officials, and renowned private practitioners.

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history. The size of IRS CI directly affects the number of cases opened each year but has not affected the fact that the quality and the complexity of the cases continues to remain at a high level. The Chief warns “Criminals would be foolish to mistake declining resources for a lack of commitment in this area.”

The Chief is leveraging limited resources by publicizing the results of those cases and more efficiently utilizing of the massive amounts of data IRS CI has access through the Nationally Coordinated Investigations Unit. The Chief commits that IRS CI will “continue to stay one step ahead of the criminals.”

### **Nationally Coordinated Investigations Unit**

IRS CI launched the Nationally Coordinated Investigations Unit (NCIU) on May 1, 2017. The NCIU partners with agents and analysts to supplement the case development activities of each field office. The NCIU pivots IRS CI to a data-driven case selection process (Data Analytics/Artificial Intelligence) by developing and managing national initiatives approved by IRS CI leadership. The case selection is designed to be both high impact and national in scope.

The NCIU utilizes wide range of data to identify and develop areas of non-compliance and will operate by:

- 1.Ensuring appropriate geographic coverage to IRS CI investigative priorities and emerging non-compliance threats
- 2.Building and supporting investigations referred to field offices
- 3.Promoting bi-lateral accountability for both NCIU and field offices
- 4.Serving as a resource to field offices
- 5.Educating and training field offices on the program areas NCIU supports
- 6.Providing and coordinating targeted training to agents assigned to NCIU referrals
- 7.Identifying emerging threats to the tax administration and financial system
- 8.Partnering with DOJ tax and other litigation components to support efforts to litigate these investigations through prosecution

### **Investigative Areas**

Below is a list of the Investigative Areas outlined in the Annual Report:

#### *Tax Crimes*

1. Employment Tax Fraud
  2. Identity Theft
  3. Data Compromises
  4. General Tax Fraud
  5. Abusive Tax Schemes
  6. Refund Fraud Program
  7. Cyber-crimes (including virtual currency)
  8. Visual Currency
  9. International Tax Enforcement Group
- Non-Tax Crimes

1. Public Corruption
2. Corporate Fraud
3. General Fraud
4. Money Laundering
5. Organized Crime Drug Enforcement Task Force (OCDETF) / High Intensity Drug Trafficking Area (HIDTA), Transactional Organized Crime

#### V. IRS CI Business Results

One of the most talked about figures in the Report is the number of investigations initiated that plummeted. These figures represent an [11.1%] drop in investigations initiated from last year and an astronomical [43.2%] drop in the last five (5) years. Such a decrease in investigations is a major problem inside and outside of the IRS who view the drop as threatening the foundations of the voluntary tax system in the United States.

### **Tax Crimes**

“Criminal Investigation’s primary resource commitment is to develop and investigate Tax Crimes, both legal and illegal Source.” The Report emphasizes that prosecution of Tax Crimes supports the overall IRS compliance goals and enhances the voluntary compliance with tax laws.

#### Employment Tax Fraud

The damage from employment tax fraud can have a cascading effect, because many of the tax-evasion cases involve a multiple number of employees and their taxes. Typical methods of employment tax fraud include pyramiding, employee leasing, payment of employees in cash, false payroll tax returns, and simple failure to file payroll tax returns. The Report also identifies how some business owners are withholding taxes from employees’ paychecks and intentionally failing to remit the taxes to the IRS, while only paying their employees the amount of the net payroll check. The Report specifically identifies the scenario in which unpaid employment taxes are utilized for a business owner’s personal use. IRS CI criminally investigates and recommends prosecution for business and personal use of unpaid taxes; personal use is specifically identified in the Report. IRS CI will not tolerate taxpayers who fail to remit employment taxes and intentionally take full credit for the nonexistent withholding on their own W-2s.

#### *General Tax Fraud*

The Report acknowledges that general tax fraud investigations directly influence the public’s tax compliance and are the backbone of IRS CI’s enforcement program. The Report points out that the entire system depends heavily upon self-assessment by taxpayers of the correct amount of tax and the voluntary filing of tax returns, including paying the amount of tax owed. Taxpayers from all different sectors of the economy – including corporate executives, small business owners, self-employed and wage-earners – through willful noncompliance, fail to report and pay their fair share of taxes. The financial investigative skills of IRS CI Special Agents are of paramount importance to uncovering and

quantifying these cases. The following criminal behavior are identified in the Report:

1. Skimming by deliberately underreporting or omitting income
2. Maintaining dual sets of books
3. Creating false entries in books and records
4. Claiming personal expenses as business expenses
5. The use of false deductions or credits to decrease taxes
6. Hidden or transferred assets for the purposes of avoiding the payment of taxes

#### *Abusive Tax Schemes (Domestic and Offshore)*

The abusive tax schemes program focuses on promoters and taxpayers who willfully participate in schemes for the purpose of violating tax laws. These schemes include both domestic and offshore plans that typically include various layers of structures which are onshore and offshore and which are meant to give the appearance that the U.S. taxpayer is not the true owner of assets or the true earner of income. Many of these schemes also include very complicated structures utilizing entities such as trusts, foreign corporations and foreign partnerships which are designed to appear like a trustee, nominee, nonresident alien or other foreign entity owned assets and is the party for which income is attributable. In these structures, the domestic taxpayer is actually the proper recipient of the income.

#### *Refund Fraud Program*

The Report points out that refund fraud poses a significant threat to the tax system. Criminals are attempting to misuse the tax system to obtain large amounts of money from the government under false pretenses. The Report notes that in addition to the loss of much needed funds for vital programs, refund fraud directly impacts the confidence taxpayers have in the tax system and taxpayers' willingness to voluntarily meet their tax filing obligations. It is not uncommon to read or hear about violent criminal enterprises that have shifted their business model into organized tax refund theft.

#### *Virtual Currency*

As Virtual Currency becomes more mainstream, the threat to tax administration increases. IRS CI virtual currency concerns include a tremendous loss of transparency in transactions that historically produced a useful paper trail. The IRS CI expertise in Identity Theft transitions nicely into virtual currency investigations. IRS CI Virtual Currency topics range from the straightforward reporting of capital gains and use to pay for goods and services to the critical danger of taxpayers desiring to evade taxes using virtual currency as the new offshore bank accounts.

#### *International Tax Enforcement Group*

The Report describes how back in August 2013, IRS CI and DOJ (Department of Justice) Tax Division initiated the Swiss Bank Program (SBP) which included bringing IRS CI

Special Agents from across the country into Washington D.C. to work directly with attorneys assigned from DOJ. Since the inception the Report notes of the SBP, 80 Swiss banks have entered into Non-Prosecution Agreements (NPAs) paying over 1.3 Billion in penalties, with about 58 investigative leads being sent to various IRS CI field offices for investigation and action. Interestingly, the Report identifies over 18,000 leads not meeting criminal criteria were forwarded to IRS's LB&I Division for civil tax compliance action. IRS CI is utilizing an international tax enforcement group in IRS CI's Washington D.C. field office. This group's focus is to dismantle the most significant international tax plans that have been identified as systemic threats to the integrity and fairness of the tax administration. Investigations initiated by this group will be long-term in nature and utilize all tools at the Criminal Investigation Division's disposal.

Chief Fort is clear that the IRS CI is actively engaged in obtaining the identities of those with undisclosed foreign accounts with the use of information resources and increased data analytics. The new IRS CI elite international group is leveraging off of members with a high level of expertise in order to identify sophisticated noncompliant taxpayers. International tax issues continue to be a high priority for IRS CI.

#### **Undercover Operations**

The Report proudly states that IRS CI has utilized undercover techniques throughout its history and undercover techniques played a significant role in bringing public enemy No. 1, Al Capone, to justice. Undercover techniques have been used in numerous investigations involving organized crime, illegal gambling operations, tax shelter schemes, illicit money movers, investment scams and many others. The Report discloses that in fiscal year 2017, over 450 undercover operations were conducted.

#### **Conclusion**

IRS CI continues to focus on legal source cases. With respect to legal source income cases, one of the most powerful tools to avoid being part of the IRS's statistics is to take advantage of the IRS's domestic and offshore voluntary disclosure programs which were modified in December of 2018. The IRS has collected and analyzed the data from years of voluntary disclosure programs both in domestic and international matters. The IRS is using this data to pursue taxpayers who failed to participate in under one of the various IRS voluntary disclosure or remediation programs.

With fewer resources, IRS CI is committed to high impact/highly publicized cases that will likely be sourced from the use of Data Analytics/Artificial Intelligence using the huge trove of information already in the hands of IRS CI. IRS CI is jumping on the big data bandwagon and taxpayers who are not paying attention may find themselves in the data analytic crosshairs of the IRS. ☹

## Federal Bar Association Section on Taxation Announces 43rd Annual Tax Law Conference

The Section on Taxation is looking forward to hosting the 43rd Annual Tax Law Conference, which will be held on March 7-8 at the Ronald Reagan Building in Washington, D.C. As the tax community continues to work through all of the new tax reform provisions, this year's conference is sure to be our most important one yet. The Section thanks all of the chairs and vice-chairs of the conference for their work in preparing for the conference. ☘

### CHAIR continued from page 1

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For the remainder of 2019, we plan to host additional events in those cities as well as events in San Francisco, Boston, Atlanta, St. Louis, and Philadelphia.

In Washington, the Section continues to have its monthly steering committee meetings. Please reach out to me if you would like to attend (in person or via phone). In addition, the Section is continuing its efforts to attract younger members and has held happy hours and career panels to do just that. Elizabeth Kanyer (DOJ- Tax) and Joshua Savey (PwC) kicked off the year with a widely attended happy hour that Commissioner Rettig, Commissioner (Wage & Investment) Ken Corbin, and Deputy Commissioner (Wage & Investment) David Alito attended and met a number of younger members and students. The Section has also made an effort to give back to the community and held a volunteer morning at the D.C. Central Kitchen—an event organized by former Community Outreach chair Marissa Rensen (I.R.S. Office of Chief Counsel). Drew Cummings (Morgan Lewis & Bockius) and Nick Zemil (PwC) are planning an event with local schools to inform students about the law. The Women in Tax Law Committee led by Carina Federico (Crowell & Moring), Teresa Abney (Crowell & Moring), and Lisandra Ortiz (Miller & Chevalier) have put together popular networking events. For 2019, we have added a Diversity & Inclusion Committee, which Jacob Puhl (Facebook) has agreed to lead. Make sure you connect with the FBA on social media – Derek Berry (Schulte Roth & Zabel) continues to publicize all of our terrific programming on Facebook, LinkedIn, and Twitter.

Last but not least, the Section also looks forward to hosting its 43rd Annual Tax Law Conference, which will be held on March 7-8, 2019 at the Ronald Reagan Building in Washington. Matt Hicks (Caplin & Drysdale), Private Sector Chair and Robin Greenhouse (I.R.S. Large Business & International), Public Sector Chair are working diligently to put together a great conference. We are excited to expand the Conference to a day and a half of programming.

This year's conference is likely to be the most significant yet as the tax community grapples with the challenges posed by tax reform and the new regulatory regime.

With the implementation of tax reform and the enthusiasm of recently appointed Commissioner Rettig, this year is on track to be the Section's best yet. But, I ask each of you for a favor. To our long-time members, I ask that you stay involved in the Section for the benefit of our younger members, many of whom are just a couple years out of law school. Your experiences and guidance are invaluable to them. And to our newer and younger members, remember, involvement in the Section can drive your career, help you meet future colleagues and competitors, and will overall be a good experience.

Please do not hesitate to contact me at [anne.r.gordon@pwc.com](mailto:anne.r.gordon@pwc.com) or at 202-875-0716 if you would like to get more involved, have ideas for programming, or would like additional information about the Section. ☘

Best regards,  
Anne Gordon  
Chair, Section on Taxation (2018-2019)

## FBA Section of Taxation, New York Chapter, Hosts Judge Lauber in NYC

The FBA's Section on Taxation, NY Chapter hosted Judge Albert Lauber of the Tax Court at an informal reception at the New York Office of Kostelanetz & Fink on [date]. Members of the New York tax community had an opportunity to mingle and socialize with Judge Lauber and each other. Judge Lauber engaged in a wide-ranging conversation with attendees and took questions from the audience on varying subjects. Judge Lauber discussed recent Tax Court cases, and provided insight on the inner workings of the great work done by the Tax Court. ☘



## FBA Section of Taxation Volunteers at DC Central Kitchen

On August 12, 2018, eight volunteers worked at DC Central Kitchen preparing meals for local community members. The volunteers cut vegetables, filled buckets with salad, and tidied up the kitchen. Everyone enjoyed helping out! ☘



## FBA Section on Taxation Hosts Happy Hour in Dallas

On Wednesday, August 15, 2018, the Section's Dallas Chapter held a happy hour in conjunction with the IRS Counsel international technical training conference. The event was well attended by both IRS Counsel employees and private practitioners. ☘



## FBA Section of Taxation, Young Tax Lawyer, Holds Happy Hour



On October 25, 2018, the Young Tax Lawyers Group of the Section on Taxation held a happy hour for young practitioners and current tax students in the Washington, D.C. metro area. The happy hour brought together approximately 50 tax lawyers from both the public and private sectors, as well as many students from local law students. The event even included special guests, including IRS Commissioner Charles Rettig, Commissioner of the IRS Wage and Investment Division, Kenneth Corbin, Deputy Commissioner of the IRS Wage and Investment Division, David Alito, and Counsel to the Commissioner, Tom Cullinan. Those who attended received great happy hour drink specials and a variety of appetizers.

If you would like to learn more about the Young Tax Lawyers Group or be included in our email list, please contact Elizabeth Kanyer at [elizabeth.kanyer@gmail.com](mailto:elizabeth.kanyer@gmail.com) or Josh Savey at [joshsavey@gmail.com](mailto:joshsavey@gmail.com). ☘



## Recruiting Georgetown Law and NYU Law Tax LL.M. Students

Georgetown Law is again partnering with the New York University School of Law to sponsor the nation's premier recruitment program for graduate tax students, the Taxation Interview Program (TIP). TIP enables private and public sector employers to interview, on one day (March 1, 2019), and in one place (Embassy Suites by Hilton Crystal City National Airport), current LL.M. students from both schools. Employers can also participate in TIP through a resume collection option. Employer registration will start on November 30, 2018 and will remain open through January 18, 2019. For

more information about TIP, please visit the TIP website [<https://www.law.georgetown.edu/your-life-career/career-exploration-professional-development/for-ll-m-students/recruitment-programs/taxation-interview-program-tip/>] or contact Masha Khomenko of Georgetown Law at 202-662-4266 or at [taxrecruit@georgetown.edu](mailto:taxrecruit@georgetown.edu). ☘

## FBA Section on Taxation Hosts Judge Guy in Miami

On Tuesday, November 6th the Miami Chapter of the FBA Tax Section hosted a reception for United States Tax Court Judge Daniel A. Guy, Jr. in Miami at Morton's Steakhouse. A couple dozen practitioners joined Judge Guy in a lively discussion about the new passport certification proceedings under Rule 350 and the travel pitfalls clients in this area with tax liens are facing. Also discussed were the effects of the local pro bono calendar call and settlement day programs, the latter of which Miami has just recently started doing and it seems to be very effective in resolving cases for unrepresented petitioners. ☘



## FBA Section on Taxation Goes to Baseball Game

On July 31, 2018, the Section's Young Tax Lawyers group hosted a group outing to the Nationals v. Mets game. Several dozen people attended a record-setting game and enjoyed food and drink too! ☘

## FBA Section on Taxation Hosts CLE Breakfast at Eversheds Sutherland



On October 17, 2018, the Federal Bar Association's Section on Taxation and Eversheds Sutherland hosted a round table discussion on the proposed Treasury Regulations under section 951A. This conversation featured two of the drafters of the GILTI regulations, Jeffery G. Mitchell and Kristine A. Crabtree from the IRS Office of Chief Counsel (International), joined by Robb Chase, Daniel Nicholas, David Sites, and Daniel Strickland. The group discussed the basic GILTI calculations and transitioned into several examples, which were designed to highlight ambiguous aspects of the proposed regulations. The conversation was informative, with all of the panel taking notes as the others were speaking. This is the second successful panel discussion co-sponsored by the Section and Eversheds Sutherland. ☘

## Women in Tax Law Group Hosts Networking Reception

Women in Tax Law Group organized a networking reception on November 28, 2018, attended by roughly 30 female tax practitioners from the government and private sector. The reception was hosted at the DC showroom of MM.LaFleur. ☘

## Opportunity Zones: The good, the bad, and the yet to be defined.

*By Michael March, Rosenberg, Martin Greenberg, LLP*

The Tax Cuts and Jobs Act (“TCJA”) provided the most comprehensive update to the tax code in over two decades. Of the many changes the TCJA provided, Section 1400Z-1 and 1400Z-2 of the IRC are of the most heavily discussed and analyzed by taxpayers and tax practitioners. Collectively, these sections provide the opportunity for an eligible taxpayer to defer capital gains and obtain a step up in basis, when properly investing in an opportunity zone.

To qualify for these tax benefits, a taxpayer must obtain capital gains that are eligible for deferral. For a gain to be eligible for deferral, it must be recognized through a sale or exchange with an unrelated person.<sup>1</sup> After the sale, the taxpayer has 180 days to reinvest the gain into a Qualified Opportunity Fund (“QOF”).<sup>2</sup>

A QOF is an investment vehicle. Organized as a corporation or a partnership for the purpose of investing in Opportunity Zone Property (“OZP”). A QOF must hold at least 90% of its assets in OZP.<sup>3</sup> The corporation or partnership self-certifies on its tax return that it is a QOF. To date, there is no legal prohibition for a preexisting entity self-certifying as a QOF. Once the QOF is formed, it must acquire OZP after December 31, 2017 by purchase in an arms-length transaction.<sup>4</sup> OZP is property located in an economically distressed community that has been nominated for that designation by the state and confirmed by the Secretary of the U.S. Treasury.

After the QOF obtains OZP, it must substantially improve that property within 30 months, beginning after the date of acquisition of the tangible property.<sup>5</sup> To substantially improve such tangible property, the additions to the basis of the property must exceed an amount equal to the adjusted basis.<sup>6</sup> Alternatively, if the QOF obtains property for a new and original use, it does not have to substantially improve the property.<sup>7</sup>

The IRS has requested commentary to help identify what parts of the foregoing process require clarification. Prior to identifying some of the issues that require clarification, it is important to note the policy behind the creation of opportunity zones. Opportunity zones were created to facilitate economic development in historically distressed areas by offering investors tax incentives. Additionally, the TCJA required pre-existing capital gains to be used to obtain the tax incentives. From this, we infer that the Federal government’s intention was to shift capital from appreciated assets, to areas in which capital contributions would act as a catalyst for economic growth. With this background in mind, the next set of regulations must address a number of unresolved issues, but tax practitioners should also have an idea how the IRS will clarify some of the issues.

Of the unresolved issues, the original use requirement needs clarification. Specifically, what happens if property acquired by a QOF, and located within a QOZ, was abandoned for a substantial period of time before the purchase? Would the original use of the property relate back to the last time the property was in use, or is any new use of the property considered the original use?

26 U.S.C (“IRC”) § 1394 establishes a similar procedural construct and applies to enterprise zones facility bonds. Based on IRC § 1397, an enterprise zone facility bond is a tax exempt private activity bond issue. The proceeds of an enterprise zone facility bond may be used by certain businesses in empowerment zones or enterprise communities. Empowerment zones and enterprise communities are highly distressed urban and rural communities. Taxpayer’s who purchases the enterprise zone bonds receive interest income that is tax exempt. More importantly, the issuer of the bond is required to place property, whose original use, is in the empowerment zone.

To clarify the original use requirement in the enterprise zone context, the IRS issued Treasury Regulation 1.1394-1(h). The regulation provides that if property is vacant for at least a one year period, use prior to that period is disregarded for purposes of determining original use. Moreover, de minimis incidental uses of property such as renting the side of a building for advertising are disregarded.

The policy behind enterprise facility bonds is similar to QOZ. Although, the mechanism by which the economically distressed area receives capital is different, the overall goal of the program is the same, provide capital to an economically distressed area and receive tax incentives for doing so. As a result, it would be logical for the IRS to issue guidance adopting the rules as outlined above.

The IRS should also contemplate and provide guidance on the original use of property located in an opportunity zone that was used for multiple different purposes before being sold to a QOF. For example, a building that was used as a warehouse, grocery store, retail space, or other similar purposes within a short period of time before being purchased by a QOF. Based on these facts, it is difficult to determine the prior use of the property, and thus what would constitute original use of the property moving forward.

In December of 2005, the Gulf Opportunity Zone Act (“Gulf Act”) was signed into law. The Gulf Act, which in many ways mirrors QOF and QOZ, provided tax benefits to assist individuals recovering from Hurricanes Katrina, Rita and Wilma. Of the many tax benefits the Gulf Act provided

one was additional depreciation. Based on IRC § 1400N, property described in IRC § 168(k) was provided an additional 50% first year depreciation allowance under IRC § 167(a), if the property that was placed into a designated Gulf Zone, and it was the property's original use.

Internal Revenue Bulletin 2007-17, Notice 2007-36, clarified the original use requirement as it applied to the Gulf Act and determined that reconditioned or rebuilt property did not satisfy the original use requirement if the property had been previously used within the Gulf Zone. Moreover, the Court has also clarified the original use requirement as it relates to the Gulf Act. In *Blakeney v. Commissioner of Internal Revenue Service*, the Taxpayer purchased a yacht and placed it into service for the first time in a Gulf Zone. As this was the first time the yacht was placed into service in that specific Gulf Zone, the IRS accepted it as an original use, without analyzing the yacht's prior use in any other area.<sup>8</sup>

Tax practitioners hypothesize that the IRS will use a broad definition of original use to facilitate the greatest degree of economic growth. From this standpoint, only the last use of the property would be considered as outlined in the scenario above. Alternatively, a strict interpretation of the original use requirement would make it more difficult for QOF to operate in a QOZ because less entity choices would be available. Unfortunately, it is likely the IRS, and the Court, will adopt the strict interpretation of the original use requirement. As a result, all prior uses of the property within the QOZ will be taken into consideration when determining if the original use requirement is met.

Finally, further guidance is required to clarify the original use requirement when a QOF purchases only land, or land that has a structure which will be demolished. In Revenue Ruling 2018-29, the IRS stated "given the permanence of land, land can never have its original use in a QOZ commencing with QOF." Meaning, land must be substantially improved in order to qualify as QOZ property. In this context what constitutes the substantial improvement of land? Upgrading the land itself such as razing or leveling would constitute substantial improvement. However, would vertical improvements to

the land such as a building constitute an increase in basis to the land? From a policy perspective, allowing vertical improvement to substantially increase the basis of the property would facilitate economic prosperity. As a result, it would seem logical for the IRS to conclude that vertical improvements could qualify as a substantial improvements of the land itself.

In a similar scenario, what if an individual acquired OZP prior to December 31, 2017, and wanted to develop a building on the land now. Based on the statute, current land owners could not take advantage of the tax incentives because they were not acquired after December 31, 2017. In response, tax practitioners have conceptualized a leasing arrangement where owners of the land developed separate land and construction joint ventures with ground leases satisfying the statutes requirements. To date, regulations have not considered this planning technique. However, generally, for federal income tax purposes a lease does not qualify as an acquisition unless certain conditions are met.

In conclusion, the process to obtain the tax benefits associated with IRC § 1400Z-1 and 1400Z-2 are complicated, and at times in need of clarification. However, the construct from which these statutes are derived have been in existence for almost a decade, albeit on a much smaller scale. With just a quick glimpse into how the IRS and the Courts have handled these issues in the past, we can help clients obtain significant tax benefits in the future, and less headache for tax practitioners in the present.

#### Endnotes:

<sup>1</sup>26 U.S.C § 1400Z-2(a)(1).

<sup>2</sup>26 U.S.C § 1400Z-2(a)(1)(A).

<sup>3</sup>26 U.S.C § 1400Z-2(d)(1).

<sup>4</sup>26 U.S.C § 1400Z-2(d)(2)(D)(i)(I).

<sup>5</sup>26 U.S.C § 1400Z-2(d)(2)(D)(ii).

<sup>6</sup>Id.

<sup>7</sup>26 U.S.C § 1400Z-2(d)(2)(D)(i)(II).

<sup>8</sup>*Blakeney v. C.I.R.*, T.C. Memo 2012-289.

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## Georgetown Law & NYU Law Taxation Interview Program

Women in Tax Law Group organized a networking reception on November 28, 2018, attended by roughly 30 female tax practitioners from the government and private sector. The reception was hosted at the DC showroom of MM.LaFleur. ☘

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43rd Annual

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Federal Bar Association  
Section on Taxation  
1220 North Fillmore Street, Suite 444  
Arlington, VA 22201

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