Post Polak

Welcome to Edition 14 of The Newsletter from Scott H. Novak, Attorney at Law. The Newsletter is designed to bring timely and interesting topics to accountants and attorneys. Comments and suggestions are always welcome. Feel free to call or write at any time.

The Treasury Offset Program

If you do business with or work for the federal government, then you should know about the Treasury Offset Program (TOP). Under the TOP, if you owe money to a federal agency or a state, or owe child support, the federal government can offset or take in full your federal tax refund, or any other payment owed to you by the federal government. For example, if you are a contractor doing business with the federal government, they can retain any of the payments that are due to you from the government, irrespective of your other commitments (i.e., to suppliers, employees, etc.).

There are some rules. Among them is the amount the government is allowed to collect:

- Federal tax refund - up to 100% to collect federal nontax debts, child support, and state income tax and unemployment insurance debts
- Vendor and federal employee travel-related payments - up to 100% for all debts
- Federal salary - up to 15% of disposable pay for federal tax and nontax debts and up to 50-65% for child support debts
- OPM retirement - up to 25% for federal nontax debts and 15% for federal tax debts
- Social Security and Railroad Retirement benefits - up to 15% for federal tax and nontax debts
- State payments of all kinds - up to 100% for federal nontax debts

There are some exemptions. If you are in a situation where the state or federal government might offset a payment to cover a debt, do some research on this program before putting yourself in a very difficult position.

Partnership Audit Rules

We have now been living with the new partnership audit rules for more than a full tax year. You may already know a fair amount about this, but I thought I might take a few moments to remind you of some important items relative to this new law.

- The main point of the new law is to allow the IRS to conduct audits at the partnership level, rather than at the partner level. If there is a resulting adjustment, the partnership will then be taxed at the partnership level, which may result in higher taxes than if taxed at the partnership level.

- All partnership agreements and LLC operating agreements for partnership LLCs must be amended to reflect the new law. For example, someone must be designated as the Partnership Representative. There is no longer a Tax Matters Partner. The Representative need not be a partner. However, the Representative must have the ability to bind the partnership and the partners, and act on the partnership's behalf in relation to the IRS.
- Partnerships with 100 or fewer partners can elect out of these new rules, provided that all partners are "eligible partners." An eligible partner is an individual, C corporation, eligible foreign entity, an S corporation or the estate of a deceased partner. This election must be made ANNUALLY on a timely-filed tax return. If the partnership elects out of the new regime, the audit is conducted at the partner level. If the election is made, the partnership must notify each partner and provide the IRS with each partner's name or employer identification number.
- If the audit is done at the partnership level, the partnership may make an election to shift the responsibility back to the partners by issuing a statement within 45 days of receipt of the notice of adjustment from the IRS. The partnership must also issue a K-1 within 45 days of the IRS final notice of adjustment.
- Things can get complicated in situations where partners have left the partnership or joined the partnership after the year being audited. In the case where a partner leaves the partnership, an agreement ought to be considered that indicates that the partner will be responsible for his or her share of any adjustments that occur for tax years when that person was a partner.
- Things can further be complicated when there is a change of Partnership Representative. It is possible that the audit occurs for a year when one individual was the Partnership Representative, but that someone else is the Representative in the adjustment year.

Tax Liens and the Sale of Real Estate

I get many calls from people who have an IRS tax lien outstanding and they want to or have to sell their property. The latest one that I have involves a short sale where the property is being sold for less than the bank loan. In such a case, no money is left over for the IRS - their interest in the property is worthless. The form to use in this circumstance is Form 14135. It can be submitted by the seller (most common), the buyer, or someone else. There are certain things that the IRS must see in order to make a determination of whether to release the lien on the property. They must see a contract for sale, deed, title report, appraisal, secondary appraisal (usually done by a realtor), a proposed settlement statement and the tax liens. In the case of a short sale, they will also need to see the short sale letter from the bank.

Once all of this information is gathered, the package is sent to an IRS campus in Cleveland, which then routes it to an IRS office in Freehold, NJ (if the property is a New Jersey property). The IRS is quite aware that there are deadlines in real estate transactions and in my experience, they get the review done quickly, certainly within 30 days if all of the necessary information was provided and sometimes with two weeks. At this moment, however, the entire IRS is behind because of the shutdown that started last December, so it may take a bit longer than usual. What the IRS provides is a conditional letter of lien withdrawal. Some title companies see that and say that they will not close with a conditional letter. At that point, it must be explained that the conditional letter is as good as it gets until after the closing, at which point, the IRS is provided with documentation showing that the property did in fact transfer hands and that there was no additional money available for the IRS. It is at that point that the lien is fully released.

It should be noted that there are times when a buyer would like to buy a property that has been abandoned, but still has a tax lien outstanding. When asked about this situation, I generally will advise the buyer to go ahead with the sale. In such a case, the buyer can complete the necessary forms and submit them to the IRS. The process is fairly straightforward.

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