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From the Editor:

Supreme Court Review of Healthcare Could Cause Chaos

By Jeremy Scott — jscott@tax.org

The fate of President Obama's signature domestic achievement, healthcare reform, is now in the hands of the U.S. Supreme Court. The Court heard three days of oral arguments last week over the constitutionality of the Patient Protection and Affordable Care Act. The controversial individual mandate, which would impose a penalty on citizens who fail to secure health insurance, was at the center of the debate.

Before the oral arguments, most legal observers expected the Court to affirm the law, or at least to invoke the Anti-Injunction Act to avoid finding the mandate or the PPACA as a whole unconstitutional. But the nature of the questions from the justices has thrown that assumption into question. Justices seemed skeptical that the AIA barred them from considering the constitutionality of the law. And on the second day of arguments, Justice Kennedy, who usually functions as the swing vote on the Court, appeared very critical of the individual mandate. Many liberal commentators came away from the arguments thinking that Chief Justice Roberts might be the only hope of saving the individual mandate, an outcome that doesn't seem terribly likely. (For coverage, see p. 15. For analysis of the mandate, see p. 14.)

Healthcare reform was accomplished through two major pieces of legislation. One was the original Senate-passed bill, which the House was forced to accept without amendment after the election of Massachusetts Republican Scott Brown. The second was the strange reconciliation bill that was used by Democrats to partially modify elements of the Senate bill while avoiding a Republican filibuster in the Senate. The interaction of those two laws is complicated, and if the Supreme Court strikes down the PPACA, it is not clear what will happen to a host of individual provisions. Even if the Court simply strikes down the individual mandate, the ability of Obamacare to function will be called into question. Without the individual mandate, other provisions in healthcare reform could cause insurance costs to skyrocket (at least if the experience of several states is to be believed).

The tone of oral arguments can be misleading, and it is not at all clear that the Supreme Court will insert itself so brazenly into the legislative process by striking down a major piece of legislation like healthcare reform. But that outcome, which might produce administrative chaos, seems more likely now than it did two weeks ago.

Swiss Protocol

As the UBS scandal unfolded and U.S. enforcement efforts spread to other Swiss banks and bankers, Switzerland pushed hard to compromise with the United States. The Swiss appeared willing to cooperate with U.S. tax enforcement in an effort to preserve some of their bank secrecy regime. A protocol to the existing U.S.-Switzerland tax treaty was negotiated, and U.S. authorities lauded the end of bank secrecy. However, it is the Swiss who should be celebrating the agreement, according to Lee Sheppard. In her comprehensive look at the protocol, Sheppard finds that the terms are much closer to the old information disclosure regime than U.S. officials have claimed. The Swiss have managed to preserve a great deal of discretion over when and how to disclose account holders to the United States, she writes. (For her analysis, see p. 7.)

40th Anniversary

Tax Notes features two articles from 1984 in this week's 40th anniversary retrospective. In the first, Sheppard discussed the precedential value of private letter rulings, an issue that remains controversial today (p. 65). She wrote that tax practitioners use letter rulings in their research and cite them, and the IRS encourages the practice. As a result, she thought it would be inevitable that letter rulings would become precedent because of usage.

In the second selection, then-Senate Appropriations Chair Mark Hatfield put forward his own proposal for simplifying the U.S. tax system (p. 68). Hatfield's plan sought to broaden the tax base by replacing many deductions and credits with just five tax credits. He also called for lower rates. Like many commentators today, Hatfield cited the low U.S. savings rate as a reason for tax reform and decried the complexity of the current system.

Commentary

Treasury issued final partnership debt-for-equity regulations in November 2011. The regulations deny a creditor's loss on the contribution of indebtedness to a partnership in exchange for a partnership interest with a value less than the price of the

contributed indebtedness. Blake Rubin, Andrea Whiteway, and Jon Finkelstein write that there is no tax policy justification for the loss deferral and character conversion imposed on a creditor under the guidance (p. 81). In a previous article, they criticized the proposed regulations and suggested a bifurcation approach that would achieve consistency between the treatment of the partnership and the creditor in such an exchange. They reiterate that proposal in their special report and call for clarifications on the treatment of unpaid rent, royalties, and interest.

In the 1980s, the IRS suffered a series of defeats in cases in which it sought to treat transactions as disguised sales of property or property interests. In response to those setbacks, Congress enacted section 707(a)(2)(B), which grants the IRS expanded authority to recharacterize transactions as disguised sales. Peter Poulos writes that the IRS has taken advantage of its authority to attack disguised sales of property, but has made little use of its power in the area of disguised sales of partnership interests (p. 91). The IRS issued proposed regulations on disguised sales of partnership interests but withdrew the regs in 2009, Poulos writes. The withdrawal of the regulations means that partners continue to have the flexibility to structure the withdrawal of a partner as either a liquidation or a sale to the continuing members, he concludes.

In response to a transaction by May Department Stores, the IRS issued proposed regulations in 1989 that would prevent taxpayers from using a partnership to redeem stock with appreciated gain without recognizing corporate-level gain. Twenty years later, the regulations have yet to be finalized. It is time for the IRS to either revoke the regulations or finalize them, according to Monte Jackel and Audrey Ellis (p. 95). The status quo is not acceptable because it creates uncertainty that prevents legitimate tax planning, they argue.

A recent Tax Court decision suggested that an alternative characterization may have applied to an employee loan. In *Brooks*, the Tax Court stated that a loan to an employee might have been advance compensation, an argument that the taxpayer did not raise and that would have run counter to all the documentation in the case. Elizabeth Kessenides writes that the opinion is problematic and the court's reasoning is flawed because it encourages the taxpayer to take a position that contradicted the structure of the transaction (p. 99). In her opinion, the Tax Court is ignoring the taxpayer's duty of consistency.

House Budget Committee Chair Paul Ryan's budget proposal passed the House last week, despite the defection of 10 Republicans. (For coverage, see p. 34.) The budget would overhaul the U.S. tax system by lowering rates, moving the country to a territorial regime, and ending the AMT. It would also require sharp cuts in government spending, including entitlements. Diana Furchtgott-Roth writes that the House budget plan is very different from Obama's proposal, showing the vast philosophical differences between Republicans and Democrats (p. 105). She argues that the public is beginning to support changes to the structure of Medicare and that Ryan's budget is closer to a realistic blueprint than the president's plan.

IRS Commissioner Douglas Shulman has recently come under fire from Republicans because of the Service's treatment of Tea Party-backed exempt organizations. Kip Dellinger looks at how Democrats and liberal watchdog groups are attempting to use the IRS as a weapon in the 2012 campaign season, and he questions Shulman's response to allegations of IRS bias (p. 109). Dellinger also looks at the Service's attempts to assess gift tax on donors to some exempt organizations and its handling of applications to become 501(c)(4) organizations.

In his column this week, Robert Wood looks at joint bank accounts and tax ownership (p. 113). Along with Jamie Ogden, Wood discusses the legal and factual framework that informs common joint bank account fact patterns and how that framework might affect income tax and reporting regimes. ■

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