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Phishing Schemes Make IRS Dirty Dozen List of Tax Scams

Cross References

- IR-2018-39, March 5, 2018

Following continuing threats to taxpayers, the IRS has listed email phishing schemes as a top filing season concern and part of the annual listing of the Dirty Dozen tax scams for 2018.

The IRS warned taxpayers, businesses, and tax professionals to be alert to fake emails or websites looking to steal personal information. These attempts can expand during tax season and remain a major identity theft threat.

Compiled annually by the IRS, the Dirty Dozen lists a variety of common scams that taxpayers may encounter any time of the year, but many of these schemes peak during filing season as people prepare their tax returns or seek help from tax professionals.

To help protect taxpayers, the IRS is highlighting each of these scams on 12 consecutive days to help raise awareness. The IRS also urges taxpayers to help protect themselves against identity theft by reviewing safety tips prepared the Security Summit, a collaborative effort between the IRS, states and the private-sector tax community.

"We urge taxpayers to watch out for these tricky and dangerous schemes," said Acting IRS Commissioner David Kautter. "Phishing and other scams on the Dirty Dozen list can trap unsuspecting taxpayers. Being cautious and taking basic security steps can help protect people and their sensitive tax and financial data."

2018 Sees New Phishing Schemes

The IRS continues to see a steady onslaught of new and evolving phishing schemes as scam artists work to victimize taxpayers during filing season.

In a recent twist to a phishing scam, the IRS has seen thousands of taxpayers victimized by an unusual scheme that involves their own bank accounts. After stealing client data from tax professionals and filing fraudulent tax returns, the criminals use taxpayers' real bank accounts to direct deposit refunds. Thieves are then using various tactics to reclaim the refund from the taxpayers, including falsely claiming to be from a collection agency or representing the IRS. Phone calls, emails, and websites are used to make the scheme more elaborate. Versions of the scam may continue to evolve. The IRS encourages taxpayers to review some basic tips if they see an unexpected deposit in their bank account.

In addition, the IRS has seen email schemes in recent weeks targeting tax professionals, payroll professionals, human resources personnel, schools, as well as individual taxpayers.

In these email schemes, criminals pose as a person or organization the taxpayer trusts or recognizes. They may hack an email account and send mass emails under another person's name. Or they may pose as a bank, credit card company, tax software provider, or government agency. Criminals go to great lengths to create websites that appear legitimate but contain phony log-in pages. These criminals hope victims will take the bait and provide money, passwords, Social Security numbers and other information that can lead to identity theft.

Fake emails and websites also can infect a taxpayer's computer with malware without the user knowing it. The malware gives the criminal access to the device, enabling them to access all sensitive files or even track keyboard strokes, exposing login information.

For those participating in these schemes, such activity can lead to significant penalties and possible criminal prosecution. IRS Criminal Investigation works closely with the Department of Justice to shutdown scams and prosecute the criminals behind them.

Tax Pro Alert

Numerous data breaches in the past year mean the entire tax preparation community must be on high alert during filing season to any unusual activity. Criminals increasingly target tax professionals, deploying various types of phishing emails in an attempt to access client data. Thieves may use this data to impersonate taxpayers and file fraudulent tax returns for refunds.

As part of the Security Summit initiative, the IRS has joined with representatives of the software industry, tax preparation firms, payroll and tax financial product processors and state tax administrators to combat identity theft refund fraud to protect the nation's taxpayers.

The Security Summit partners encourage tax practitioners to be wary of communicating solely by email with potential or even existing clients, especially if unusual requests are made. Data breach thefts have given thieves millions of identity data points including names, addresses, Social Security numbers and email addresses. If in doubt, tax practitioners should call to confirm a client's identity.

What to Do With Phishing Attempts

If a taxpayer receives an unsolicited email that appears to be from either the IRS or an organization closely linked to the IRS, such as the Electronic Federal Tax Payment System (EFTPS), they should report it by sending it to phishing@irs.gov. Learn more by going to the Report Phishing and Online Scams page on IRS.gov.

Tax professionals who receive unsolicited and suspicious emails that appear to be from the IRS or related to the e-Services program also should report it by sending it to phishing@irs.gov.

It is important to keep in mind the IRS generally does not initiate contact with taxpayers by email to request personal or financial information. This includes any type of electronic communication, such as text messages and social media channels.

Bipartisan Budget Act of 2018

Cross References

- H.R. 1892

On February 9, 2018, the President signed into law H.R. 1892, the Bipartisan Budget Act of 2018, which extends federal funding for the government. The law also contains a number of tax provisions, including the extension of a number of provisions that had expired as of the end of 2016. These changes affect the preparation of 2017 tax returns. The following is our coverage of the new law.

Extension of Expiring Provisions

A number of tax provisions expired on December 31, 2016 and were not extended by the Tax Cuts and Jobs Act (Public Law 115-97) that was signed into law on December 22, 2017. The Bipartisan Budget Act of 2018 extends the following tax provisions for the 2017 tax year. All of these provisions now expire on December 31, 2017:

- Cancellation of qualified principal residence indebtedness exclusion (IRC §108).
- Mortgage insurance premiums deduction (IRC §163).
- Tuition and fees deduction (IRC §222).
- Indian employment credit (IRC §45A).
- Railroad track maintenance credit (IRC §45G).
- Mine rescue team training credit (IRC §45N).
- Race horse two years old or younger treated as 3-year property instead of 7-year property [IRC §168(e)(3)].
- Motor sports entertainment complexes treated as 7-year property [IRC §168(e)(3) and §168(i)(15)].
- Indian reservation property accelerated depreciation recovery periods [IRC §168(j)].
- Mine safety equipment expense election (IRC §179E).
- Special expensing rules for certain film, television, and live theatrical productions (IRC §181).
- Domestic production activities deduction for activities located in Puerto Rico (IRC §199). ***Note:*** The domestic production activities deduction for all activities was repealed by the Tax Cuts and Jobs Act for tax years beginning after December 31, 2017.

- Special rate for qualified timber gains (IRC §1201). ***Note:*** IRC section 1201 refers to AMT for C corporations which was repealed by the Tax Cuts and Jobs Act for tax years beginning after December 31, 2017.
- Empowerment zone tax incentives [IRC §1391(d)].
- American Samoa economic development credit [Public Law 109-432, section 119].
- Nonbusiness energy property credit (IRC §25C).
- Alternative motor vehicle credit for qualified fuel cell motor vehicles [IRC §30B(k)(1)].
- Alternative fuel vehicle refueling property credit (IRC §30C).
- Electric vehicle credit for highway-capable 2-wheeled vehicles (IRC §30D).
- Second generation biofuel producer credit [IRC §40(b)].
- Biodiesel and renewable diesel fuels credit (IRC §40A). ***Note:*** Excise tax incentives for biodiesel and renewable diesel fuels under IRC section 6426(c) are also extended and modified.
- Indian coal production credit [IRC §45(e)].
- Electricity production credit or investment credit in lieu of the production credit for non-wind renewable power facilities [IRC §45(d) and §48(a)].
- Energy efficient home credit (IRC §45L).
- Special depreciation allowance for second generation biofuel plant property [IRC §168(l)].
- Energy efficient commercial building property deduction (IRC §179D).
- Special rule for sales or dispositions to implement Federal Energy Regulatory Commission or state electric restructuring policy [IRC §451(k)].
- Alternative fuels excise tax credit [IRC §6426(d) and §6426(e)].

Extensions beyond 2017. The following provisions are extended and modified as follows:

- The residential energy efficient property credit under IRC section 25D is extended through December 31, 2021 and includes qualified solar electric property expenditures, qualified solar water heating property expenditures, qualified fuel cell property expenditures, qualified small wind energy property expenditures, and qualified geothermal heat pump property expenditures.
- The energy credits and credit phase-outs under IRC section 48(a) are extended to periods ending before January 1, 2022. This provision affects solar and thermal energy property, fiber-optic solar property, qualified fuel cell property, qualified small wind energy property, qualified microturbine property, and combined heat and power system property.
- The oil spill liability trust fund financing rate under IRC section 4611 is extended through December 31, 2018.

Amended returns. Taxpayers affected by these provisions who have already filed their 2017 tax return may file an amended return to take advantage of the extension of the expiration date of these provisions.

Other Provisions

The new law also contains the following provisions:

- Provides additional Hurricane Maria relief by increasing funding for Medicaid programs for Puerto Rico and the Virgin Islands.
- Modifies the credit under IRC section 45J for production from advanced nuclear power facilities.
- Extends and modifies the rum excise tax revenues to Puerto Rico and the Virgin Islands under IRC section 7652.
- Extends the waiver of the statute of limitations from one year to three years with respect to the exclusion from gross income of amounts received by wrongfully incarcerated individuals.
- Taxpayers are held harmless and allowed to re-contribute retirement plan benefits on wrongful levies. The re-contributed benefits are treated as a rollover. [IRC §6343(f)]
- Modifies the user fee requirements for installment agreements. (IRC §6159)
- The special rules for deducting attorney's fees and court costs for certain whistle-blowers is expanded to include awards under the Securities Exchange Act, a state false claims act, and the Commodity Exchange Act. The law also clarifies what is considered to be included in a whistleblower award.
- Clarifies that the excise tax under IRC section 4968 based on investment income of private colleges and universities applies to educational institutions with at least 500 tuition-paying students with more than 50% of the tuition-paying students being located in the United States.
- Provides a new exception from the Private Foundation excess business holding tax under IRC section 4943 for independently operated philanthropic business holdings.
- Modifies record-keeping rules under IRC section 5555 for certain excise taxes.
- Directs the IRS to modify the regulations for hardship distributions.
- Adds Puerto Rico as an opportunity zone for purposes of IRC section 1400Z-1.
- Modifies the rules for foreign persons for purposes of Form 1099-K payment card and third party network transactions under IRC section 6050W.
- Eliminates the requirement for C corporations with assets over $1 billion to increase their 2020 tax year 3rd quarter estimated tax payment by 8%.

- Modifies the credit for carbon dioxide sequestration under IRC section 45Q.

Interest on Home Equity Loans

Cross References

- IR-2018-32, February 21, 2018

Responding to many questions received from taxpayers and tax professionals, the IRS said in a recent news release that despite newly-enacted restrictions on home mortgages, taxpayers can often still deduct interest on a home equity loan, home equity line of credit (HELOC) or second mortgage, regardless of how the loan is labelled. The Tax Cuts and Jobs Act of 2017 suspends from 2018 until 2026 the deduction for interest paid on home equity loans and lines of credit, unless they are used to buy, build, or substantially improve the taxpayer's home that secures the loan.

Under the new law, for example, interest on a home equity loan used to build an addition to an existing home is typically deductible, while interest on the same loan used to pay personal living expenses, such as credit card debts, is not. As under prior law, the loan must be secured by the taxpayer's main home or second home (known as a qualified residence), not exceed the cost of the home and meet other requirements.

New dollar limit on total qualified residence loan balance. The new law imposes a lower dollar limit on mortgages qualifying for the home mortgage interest deduction. Beginning in 2018, taxpayers may only deduct interest on $750,000 of qualified residence loans. The limit is $375,000 for a married taxpayer filing a separate return. These are down from the prior limits of $1 million, or $500,000 for a married taxpayer filing a separate return. The limits apply to the combined amount of loans used to buy, build or substantially improve the taxpayer's main home and second home.

The following examples illustrate these points.

Example #1: *In January 2018, a taxpayer takes out a $500,000 mortgage to purchase a main home with a fair market value of $800,000. In February 2018, the taxpayer takes out a $250,000 home equity loan to put an addition on the main home. Both loans are secured by the main home and the total does not exceed the cost of the home. Because the total amount of both loans does not exceed $750,000, all of the interest paid on the loans is deductible. However, if the taxpayer used the home equity loan proceeds for personal expenses, such as paying off student loans and credit cards, then the interest on the home equity loan would not be deductible.*

Example #2: *In January 2018, a taxpayer takes out a $500,000 mortgage to purchase a main home. The loan is secured by the main home. In February 2018, the taxpayer takes out a $250,000 loan to purchase a vacation home. The loan is secured by the vacation home. Because the total amount of both mortgages does not exceed $750,000, all of the interest paid on both mortgages is deductible. However, if the taxpayer took out a $250,000 home equity loan on the main home to purchase the vacation home, then the interest on the home equity loan would not be deductible.*

Example #3: *In January 2018, a taxpayer takes out a $500,000 mortgage to purchase a main home. The loan is secured by the main home. In February 2018, the taxpayer takes out a $500,000 loan to purchase a vacation home. The loan is secured by the vacation home. Because the total amount of both mortgages exceeds $750,000, not all of the interest paid on the mortgages is deductible. A percentage of the total interest paid is deductible.*

Qualified Improvement Property Technical Error

Cross References

- IRC §168

Numerous sources are reporting on a glitch in the new law concerning qualified improvement property. Under prior law, nonresidential real property is generally depreciated under MACRS over 39 years. An exception applied for certain qualified real property. 15-year MACRS depreciation using the straight-line method was available for qualified leasehold improvement property, qualified restaurant property, and qualified retail improvement property. In addition, such property was also eligible to be expensed under IRC section 179 or written off under bonus depreciation. The definition of each of these three categories differed from each other in various ways.

Effective for 2018, the Tax Cuts and Jobs Act eliminates the separate definitions of qualified leasehold improvement, qualified restaurant, and qualified retail improvement property. Qualified improvement property is defined as any improvement to an interior portion of a building which is nonresidential real property if such improvement is placed in service after the date such building was first placed in service. Such term does not include any improvement for which the expenditure is attributable to the enlargement of the building, any elevator or escalator, or the internal structural framework of the building.

According to the Conference Report for the new law, qualified improvement property placed in service after December 31, 2017 was supposed to be depreciable over 15-years (under MACRS) using the straight-line method and half-year convention, without regard to whether the improvements are property subject to a lease, placed in service more than three years after the date the building was first placed in service, or made to a restaurant building. The problem is the actual Internal Revenue Code section for qualified improvement property makes no reference to the 15-year class life. As a result, qualified improvement property by default is nonresidential real property subject to 39-year straight-line depreciation.

The Conference Committee report clearly shows that Congress intended qualified improvement property to have a 15-year class life, but the Conference Committee report cannot overrule the clear language of the statute.

Without a technical correction, effective for 2018, qualified improvement property is subject to 39-year straight-line depreciation, does not qualify for bonus depreciation, and does not qualify for Section 179 expensing, because bonus depreciation and Section 179 are allowed only for property having a class life of 20 years or less.

Short-Term, Limited-Duration Insurance

Cross References

- REG-133491-17, February 21, 2018

The Secretaries of the Treasury, Labor, and Health and Human Services have issued new proposed regulations that amend the definition of short-term, limited-duration insurance for purposes of its exclusion from the definition of individual health insurance coverage.

Under President Trump's Executive Order dated October 12, 2017, within 60 days, the Secretaries were to consider proposing regulations or revising guidance to expand the availability of short-term, limited-duration insurance.

Under the Affordable Care Act (ACA), non-exempt individuals must maintain minimum essential health insurance coverage or pay a penalty tax (the individual shared responsibility payment). Short-term, limited-duration insurance is a type of health insurance coverage that was designed to fill temporary gaps in coverage that may occur when an individual is transitioning from one plan or coverage to another plan or coverage.

Prior guidance defined short-term, limited-duration insurance as health insurance coverage provided pursuant to a contract with an issuer that has an expiration date specified in the contract that is less than 12 months after the original effective date of the contract. After ACA, guidance was proposed that shortened the length to less than three months. This guidance also included a requirement that the following notice be prominently displayed in the contract and in any application materials provided in connection with enrollment in short-term, limited-duration insurance:

> *"This is not qualifying health coverage (minimum essential coverage) that satisfies the health coverage requirement of the Affordable Care Act. If you don't have minimum essential coverage, you may owe an additional payment with your taxes."*

The intent of this guidance was to limit the number of consumers relying on short-term, limited-duration insurance as their primary form of coverage and improve the individual market single risk pools. However, critics expressed concerns about restricting the use of short-term, limited-duration insurance because it provides an additional, often much more affordable coverage option than an insurance policy that complies with all of the requirements of the ACA. Individuals who do not qualify for premium tax credits and need temporary coverage, or who cannot afford COBRA continuation coverage, or who missed an opportunity to sign up during the open enrollment periods, might need to rely on short-term, limited-duration insurance coverage for three months or longer.

For example, a person with just a less-than 3-month policy who develops a health condition might have no coverage options for the condition after their coverage expires until the beginning of the plan year that corresponds to the next individual market open enrollment period.

Individuals who may be financially stressed may be faced with a choice between short-term, limited-duration insurance coverage and going without any coverage at all.

In light of the Presidential Executive Order, the new guidance proposes to amend the definition of short-term, limited-duration insurance so that it may offer a maximum coverage period of less than 12 months after the original effective date of the contract. This new guidance states that the expiration date specified in the contract takes into account any extensions that may be elected by the policyholder without the issuer's consent.

The new guidance also revises the required notice that must appear in the contract and any application materials for short-term, limited-duration insurance to say:

"This coverage is not required to comply with federal requirements for health insurance, principally those contained in the ACA. Be sure to check your policy carefully to make sure you understand what the policy does and doesn't cover. If this coverage expires or you lose eligibility for this coverage, you might have to wait until an open enrollment period to get other health insurance coverage. Also, this coverage is not minimum essential coverage. If you don't have minimum essential coverage for any month in 2018, you may have to make a payment when you file your tax return unless you qualify for an exemption from the requirement that you have health coverage for that month."