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The Surface Transportation and Veterans Health Care Choice Improvement Act of 2015: Important Changes Affecting Tax Filings for Individuals and for Trusts and Estates

By Arielle L. Buss, Ronni G. Davidowitz and Joshua S. Rubenstein

On July 31, 2015, President Obama signed into law the Surface Transportation and Veterans Health Care Choice Improvement Act of 2015 (the "Act"), which revised a number of different federal tax laws relevant to individuals, trusts and estates. This advisory highlights some of the more significant provisions of the Act affecting trusts and estates.

Changes Affecting Basis Reporting

The Act requires that the reported basis for any property acquired from a decedent be consistent with the final value of the property as determined by such decedent's federal estate tax return. Penalties will be assessed if a taxpayer thereafter reports a higher basis in inherited property than the value as finally determined by the federal estate tax return. This rule applies only to property the inclusion of which in the decedent's estate increased the estate tax liability.

Beneficiary Statements

The Act obligates the executors of any estate required to file a federal estate tax return to provide a statement to the Internal Revenue Service (IRS) and to each person inheriting any interest in property included in the decedent's gross estate for federal estate tax purposes. The statement must identify the value of each interest in the property as reported on the federal estate tax return, and must be provided no later than the earlier of 30 days after the estate tax return is required to be filed (including extensions) or 30 days after filing the return.

If there is an adjustment to the information required to be included on the statement after the statement has been filed, a supplemental statement must be filed no later than the 30 days after such adjustment is made. The statements are required to be filed with respect to all federal estate tax returns filed after July 31, 2015. As of yet, there is no guidance as to the form of the statement to be filed with the IRS and beneficiaries.

Penalties for Inconsistent Basis Reporting and Failure to File a Statement

If a taxpayer claims a basis in inherited property that exceeds the basis as finally determined on the federal estate tax return, the IRS will assess a penalty equal to 20 percent of the underpayment of tax due to the inconsistent basis reporting.

Penalties of $250 ($100 for filings due before January 1, 2016) will be assessed for each information statement that was not properly filed with the IRS or beneficiary, with a maximum penalty of $3 million ($1.5 million for statements required before 2016). The penalties are increased to $500 ($250 for filings due before January 1, 2016) per intentional failure to file a statement, or, if greater, 10 percent of the aggregate amount of items to be reported correctly. However, no penalty will be imposed if it is shown that such failure is due to reasonable cause and not willful neglect.

Six-Year Statute of Limitations for Overstatement of Basis

Generally, there is a three-year statute of limitations for the IRS to examine income tax returns measured from the time of filing. The Act now extends the statute of limitations to six years when the taxpayer omits from his or her gross income an amount that is greater than 25 percent of the amount of gross income reported in the return. The Act treats overstatement of unrecovered cost or basis as an understatement of gross income for purposes of this six-year statute of limitations period.

Tax Filing Changes

The Act addresses deadlines for various tax filings, and in certain cases, makes changes to the deadlines, as outlined below.

Trust-Related Filings. For returns for taxable years beginning after December 31, 2015, the Act addresses the following trust-related filings:

- The Act extends the maximum extension for the tax returns of trusts filing Form 1041 from September 15 to September 30 for calendar year taxpayers.
- The due date of Form 3520-A, Annual Information Return of a Foreign Trust with a US Owner, is the 15th day of the third month after the close of the trust's taxable year and the maximum extension for Form 3520-A is a six-month period.
- The due date of Form 3520, Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts, for calendar year filers is April 15, with a maximum extension for a six-month period ending on October 15.

Partnership and S-Corporation Filings. For returns for taxable years beginning after December 31, 2015, partnership tax returns and S-corporation tax returns made on the basis of the calendar year must be filed on or before March 15, and returns made on the basis of a fiscal year must be filed on or before the 15th day of the third month following the close of the fiscal year. Formerly, partnership tax returns were due on April 15. This change may ease the burden of individuals who have partnership interests and must wait for partnership income tax returns to file their personal tax returns, often until the last day to file.

Foreign Bank and Financial Account Filings. For filings of the FinCEN Report 114 ("FBAR") for taxable years beginning after December 31, 2015, such reports are now due April 15 and are allowed a maximum six-month extension. This is a change from the previous June 30 due date, with no extension permitted. For any taxpayer required to file an FBAR for the first time, any penalty for failure to timely request for, or file, an extension may be waived by the secretary.

Private Foundation Filings. For taxable years beginning after December 31, 2015, Form 990-PF will be eligible for an automatic six-month period extension, from a due date of the 15th day of the fifth month following the close of the foundation's accounting period, ending on November 15, for calendar year filers. Prior to the Act, the Form 990-PF had only been eligible for an automatic three-month extension.

Employee Benefit Plans Filings. For taxable years beginning after December 31, 2015, the maximum extension for the returns of employee benefit plans filing Form 5500 is an automatic 3.5-month period (formerly, a 2.5-month period), from a due date of the last day of the seventh calendar month after the end of the plan, ending on November 15 for calendar year plans.

We recommend that these reported tax filing changes be forwarded to your tax preparer to ensure awareness of such changes, and to ensure compliance with the new tax filing deadlines under the Act.

In addition to the above, IRS changes to IRC Section 2704 regulations are expected early this fall, which may impact the valuation of intra-family transfers of interests in closely held entities.

If you would like more details about any aspect of the new law or to discuss the anticipated laws, please do not hesitate to contact your Katten attorney or the following members of Katten's **Trusts and Estates** practice:

CHARLOTTE

A. Victor Wray, Partner	+1.704.444.2020	victor.wray@kattenlaw.com

CHICAGO

Charles Harris, Practice Head	+1.312.902.5213	charles.harris@kattenlaw.com
Michael O. Hartz, Practice Head	+1.312.902.5279	michael.hartz@kattenlaw.com
David M. Allen, Partner	+1.312.902.5260	david.allen@kattenlaw.com
Tye J. Klooster, Partner	+1.312.902.5449	tye.klooster@kattenlaw.com
Bonita L. Stone, Partner	+1.312.902.5262	bonita.stone@kattenlaw.com
Philip J. Tortorich, Partner	+1.312.902.5643	philip.tortorich@kattenlaw.com
Neil H. Weinberg, Partner	+1.312.902.5646	neil.weinberg@kattenlaw.com

LOS ANGELES – CENTURY CITY

Abby L. T. Feinman, Practice Head	+1.310.788.4722	abby.feinman@kattenlaw.com
Carol A. Johnston, Partner	+1.310.788.4505	carol.johnston@kattenlaw.com

NEW YORK

Joshua S. Rubenstein, National Practice Head	+1.212.940.7150	joshua.rubenstein@kattenlaw.com
Ronni G. Davidowitz, Practice Head	+1.212.940.7197	ronni.davidowitz@kattenlaw.com
Neil V. Carbone, Partner	+1.212.940.6786	neil.carbone@kattenlaw.com
Zvi Hahn, Partner	+1.212.940.8517	zvi.hahn@kattenlaw.com
Shelly Meerovitch, Partner	+1.212.940.8538	shelly.meerovitch@kattenlaw.com

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