Brager Tax Law Group

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Winter 2025 E-Newsletter

Happy Valentine's Day, Clients and Friends!

With this year having begun under the shadow of the devastating California fires, our hearts go out to all those affected. In times of adversity, the true spirit of love and community emerges as we support one another with resilience and compassion that define our collective character.

As we gear up for some important reads in the first edition of our 2025 newsletter, we explore the intertwining of sweet and bittersweet elements, much like a box of chocolates, where you never know what you're going to get, especially when it involves the IRS!

For those who think they can sidestep the painful consequences of IRS penalties, one of our former IRS attorneys, Guy Glaser, discusses the severe repercussions of not filing Form 5471 on page 2. It's another reminder that neglecting IRS forms can lead to some costly outcomes, making your Valentine's dinner date look like petty cash.

Are you thinking of expatriation as escaping abroad to be with a loved one? On page 3, Guy Glaser points out that it's not a bed of roses. The IRS ensures that the journey is lined with regulatory thorns to keep you vigilant about your tax obligations.

Similarly, while investing in cryptocurrency might spark the thrill of a new romance, it's not a simple affair as the IRS ensures a strict commitment to compliance. Discover the details on page 4, where we unpack the new tax rules.

2025 may have started turbulently all around the globe, but let's use this time to reinforce our solidarity and support, reminding us that together, we can overcome any challenge.

CHERYL R. FRANK
President
CPA, JD, Tax LLM

IN THIS ISSUE

VALENTINES DAY SEE's CANDIES GIVEAWAY

Since it's the month for love, we are giving away a box of chocolates from See's Candies valued at over $50 that will be personally delivered to one lucky reader. Its apt that we selected a box of decadence from See's Candies for our giveaway this month not only because of Valentines Day but more importantly that See's Candies is driving an initiative in partnership with the Red Cross to aid LA fire relief efforts.

Send an email with your name and contact details to our Director of Communications, Ana-Paula Ferreira: aferreira@bragertaxlaw.com before February 22nd, 2025. The draw will take place on February 25th, 2025.

CONTEST RULES:

- *Deadline is February 22nd 2025*
- *Regrettably no Brager Tax Law Group staff or their families may participate.*
- *Decisions are final.*
- *Prize is not transferable for cash.*

Penalty for Not Filing Form 5471

By Guy Glaser, Esq.

The penalties for not filing Forms 5471 are $10,000 for the initial failure to file the form, and an additional $10,000 for every 30-day period, or part thereof, after the IRS has notified the taxpayer of the failure to file, up to a maximum of $50,000, meaning that the IRS can assess penalties of up to $60,000 for each form. *See* I.R.C. §§ 6038(a) and (b).

In *Mukhi v. Commissioner*, 162 T.C. No. 8 issued on November 18, 2024, the Tax Court reaffirmed the decision it reached in *Farhy v. Commissioner*, 160 T.C. 399 (2023) rev'd and remanded 100 F.4th 223 (D.C. Cir. 2024), stating that the IRS lacks authority to assess penalties under section 6038(b)(1) for failure to file Form 5471. Instead, the IRS's sole remedy to enforce this international reporting penalty is to pursue civil action and file a suit under Section 2461(a) of Title 28 of the United States Code.

The significance of the Mukhi decision stems from the Tax Court's national jurisdiction. Although the D.C. Circuit reversed the holding in *Farhy v. Commissioner*, *supra*, that decision is binding only on taxpayers, which includes citizens living within Washington D.C. and those living outside of the United States. See I.R.C. § 7701(a)(39). Fortunately, most taxpayers can choose to litigate outside of the D.C. Circuit. At present, the IRS has not issued any administrative guidance on this issue, nor has it yet filed an appeal in the *Mukhi* case. But, given the implications of this decision, the government most likely will appeal.

But what is really significant about the *Mukhi* decision is the impact it appears to have on other foreign information reporting penalties sought by the Government. Specifically, it would appear that after the *Mukhi* decision penalties under section 6038 related to the following forms used for foreign information reporting purposes are also not directly assessable by the IRS: Form 8858 (U.S. person with an interest in a Foreign Disregarded Entity) and Form 8865 (U.S. person with an interest in a Foreign Partnership).

Also, given that section 6038 is part of Subpart A of Part III of Subchapter A of Chapter 61 of Subpart F of the Code, and that other penalties found in this Subpart A contain no language which would make them assessable by the Commissioner, such as the penalties found in sections 6038A (Form 5472), 6038B (Forms 926 and 8865), 6038C (Form 5472), 6038D (Form 8938), 6039F (Form 3520) and 6039G (Form 8854), then until the IRS issues further guidance on the matter, or the decision in *Mukhi* is overruled on Appeal, taxpayers facing such penalties should argue that the Commissioner has no authority to collect these penalties without first filing a lawsuit.

Call Brager Tax Law Group at 310-208-6200 for an initial complimentary 15-minute consultation and one of our former IRS attorneys is ready to assist you with any tax litigation issues, or visit www.bragertaxlaw.com for more information.

Breaking Free at a Cost: Navigating the IRS Exit Tax on Expatriation

By Guy Glaser, Esq.

So, you are fed up of paying taxes and want to relinquish your U.S. citizenship or lawful permanent resident status and leave the United States. All you need to is pack your bags and get on a plane and travel to somewhere exotic. Right? Wrong. Before you leave the United States and expatriate you may need to pay an exit tax.

So, what constitutes expatriation and what is this exit tax? Expatriation is the process of legally relinquishing one's U.S. citizenship or long term lawful permanent resident status and exiting the U.S. tax system. In addition to needing to comply with certain immigration laws, there are tax responsibilities that the expatriating individuals needs to comply with, including the filing of a final tax return with the Government. The tax responsibilities of expatriation are found in Internal Revenue Code Section 877A. And, the exit tax is a tax, but it is not a tax on wealth. Rather, it is a U.S. capital gains tax based on whether income or gains have accumulated while you were a U.S. Person but which have not been recognized/realized. Perhaps the best known examples of this involve the mark-to-market gains from stock (or other equities) or from specified tax deferred accounts (such as a traditional IRA but not a Roth IRA) you might own which are deemed sold or distributed at the time of expatriation. The exit tax you will need to pay is based upon the value of the asset you own which is treated as if it had been sold at fair market value the day before you expatriate.

For example, let's assume that Guy is a U.S. Citizen who owns 1,000 shares of Apple stock that he purchased for $50,000. On the day before he expatriates the stock is worth $250,000. Depending on whether he meets the necessary criteria to be considered a covered expatriate, Guy may have to pay an exit tax on the deemed sale of his stockholdings. But, contrast this with the situation involving Gary, Guy's brother. Gary is a U.S. Citizen who has $1,000,000 of cash in the bank. Even if Gary is considered a covered expatriate, he would not have to pay any exit tax because his assets are in cash. In another example, let's assume that Guy is a U.S. citizen who owns a traditional IRA (i.e., it has no tax basis since all the contributions were made with pre-tax dollars) that is worth $700,000. When Guy expatriates he may have to pay an exit tax on the $700,000 depending on whether he is considered an expatriate.

So, who may need to pay this exit tax? The exit tax only applies to "covered expatriates." Non-covered expatriates are not subject to the exit tax and can expatriate free of charge. A covered expatriate is either a U.S. Citizen who relinquishes his or her citizenship or a Long-Term Lawful Permanent resident who meets any one of the following three tests: (1) Their average annual net U.S. income tax liabilities for the five years preceding the year of expatriation exceeds $201,000; (2) Their Worldwide net worth (including home) on the day of expatriation equals $2 million or more; and (3) They are unable to certify via Form 8854 that US tax filings (including foreign reporting forms and FACTA requirements such as Foreign Bank Account Reports) have been fully satisfied for the five proceeding years.

And how much tax will you have to pay? Under section 877A, you will need to include in your gross income, and pay a tax on an amount, by which the fair market value of the property exceeds its adjusted basis as if you had sold such property at fair market value the day before you left the country. Fortunately, there are provisions found in section 877A whereby you may be able to elect to defer payment of the mark-to-market tax liability on a property-by-property basis until the relevant property is sold, you die, or you do not provide, or no longer have in place, "adequate security."

There are some exceptions to the above rules. A covered expatriate is not subject to the exit tax charge if they are a dual national from birth, continue to be a citizen of their second country and are taxed as a resident of that country. Also, US citizens who are under the age of 18½ or over the age of 18½ but have not been US tax resident for more than 10 taxable years can relinquish their citizenship tax free.

After you properly expatriate and, if needed, pay the exit tax, you will no longer have to comply with the US tax filing obligations of a citizen or a lawful permanent resident. Then, you can go back to your exotic retirement destination and sip margaritas on a beach while dipping your toes into the glistening blue waters of the ocean worry-free.

Call Brager Tax Law Group at 310-208-6200 for an initial complimentary 15-minute consultation and one of our former IRS attorneys is ready to assist you with your expatriation tax litigation issues, or visit www.bragertaxlaw.com for more information.

US citizens seeking to expatriate must attend an appointment at a US embassy or consulate, pay a fee of $2,350 and request a Certificate of Loss of Nationality. Green Card Holders/Long Term Lawful Permanent Residents must submit a Form I-407 (Record of Abandonment of Lawful Permanent Resident Status) or a written letter stating their intention to expatriate to the consular office. In either case, the Green Card should be enclosed with the submission and formally returned to the US Citizenship and Immigration Services. Simply letting your Green Card expire or will not be enough and will not end your US tax responsibilities.

Cryptocurrency Under the Microscope: IRS Introduces Strict Compliance Rules for 2025

By Guy Glaser, Esq.

On December 30, 2024, the IRS issued final regulations (2024-30496 (89 FR 106928)), effective starting in 2025, imposing a new tax compliance mechanism to help ensure that people who engage in the sale or exchange of digital assets pay the proper amount of tax due.

These final regulations require brokers who regularly provide services to clients involving the buying and selling of digital assets, such as bitcoin, on a centralized custodial exchange or crypto trading platform like Coinbase or Gemini, to prepare and send information returns to the IRS and furnish payee statements reporting such transactions.

These brokers will keep information concerning all the purchases and sales made in your trading account throughout the year and report them on a new form to the IRS (Form 1099-DA). For the 2025 year, this Form 1099-DA will only include information concerning the gross proceeds from your cryptocurrency transactions. But, starting with the 2026 tax year, the Form 1099-DA will also include information concerning the cost basis needed to determine your capital gains or losses from such transaction.

But, starting with the 2026 tax year, the Form 1099-DA will also include information concerning the cost basis needed to determine your capital gains or losses from such transaction.

For those who don't trade on centralized custodial exchanges – for example if you maintain custody of your cryptocurrency assets and trade them on decentralized platforms in peer-to-peer (i.e., wallet-to-wallet) transactions – these new third-party reporting requirements will not go into effect until the 2027 tax year. Furthermore, while those decentralized platforms will have to report the gross proceeds on your transactions, they will not have to report cost-basis information because they probably will not know the price at which you originally bought the digital asset.

Finally, please note that the above third-party reporting rules will also apply to spot bitcoin exchange-traded funds (ETFs) starting this year (2025). The ETF provider will issue you either a Form 1099-B or a Form 1099-DA.

If You need assistance in reporting your digital assets or have other questions concerning how the IRS taxes digital assets, please reach out to us at the Brager Tax Law Group on 310-208-6200 or visit www.bragertaxlaw.com for more information.

An 'IRS Love' Poem, by Our Editor

On Valentine's Day, as hearts align,
The IRS won't spare a dime.
Though Cupid's arrows fly,
Tax forms are piled sky-high,
But It's audits that will cost you,
not the roses and wine!