



South Carolina Bar

Continuing Legal Education Division

2026 SC BAR CONVENTION

Tax Law Section

“Tax Law Section Seminar”

Saturday, January 24

SC Supreme Court Commission on CLE Course No. 260146




South Carolina Bar

Continuing Legal Education Division

Recent Trends and Development in State and Local Tax

Jason Luther

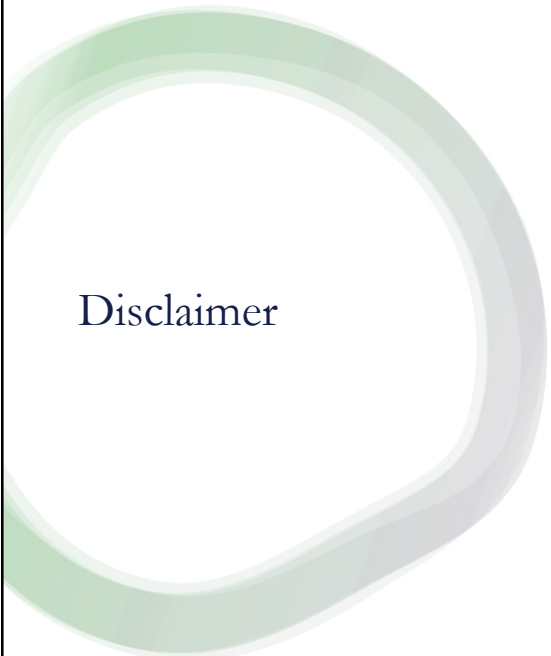


STATE AND LOCAL TAX
LITIGATION & LEGISLATION UPDATE

SOUTH CAROLINA BAR CONVENTION
JANUARY 2026

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Disclaimer

The opinions expressed in this presentation are the author's alone and should not be attributed to the South Carolina Department of Revenue.

Also...

"We must note here, as a matter of judicial knowledge, that most lawyers have only scant knowledge of the tax laws." *Bursten v. United States*, 395 F.2d 976, 981 (5th Cir. 1968).

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***Amazon Services, LLC v.
S.C. Dept. of Revenue,
442 S.C. 313 (Ct. App.
2024)***



Issue: Is Amazon the retailer for all items sold on its Marketplace, including items owned by third-party merchants?

- *ALC:* Yes
- *Court of Appeals:* Yes
- *Supreme Court:* Oral Argument on May 14, 2025

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***Amazon Services, LLC v. S.C. Dept. of Revenue,
442 S.C. 313 (Ct. App. 2024)***

- Oral argument discussions:
 - *Travelscape* and broad interpretations of a tax statute – limiting principle?
 - Can court find statute unambiguous without considering Amazon's contrary and reasonable interpretation?
 - *Alltel* and resolving (against the government) ambiguity in tax-imposition statutes



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CarMax Auto Superstores, Inc., Docket No. 21-ALJ-17-0182-CC (Amended Final Order Aug. 15, 2025)

- **Issue:** Does separate entity reporting fairly represent CarMax's business activity; if not, is combined unitary reporting a reasonable and equitable alternative apportionment method?
- *ALC:* No, Yes. Order Denying Second Motion to Reconsider (Sept. 20, 2024)
- *Court of Appeals:* awaiting oral argument



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CarMax Auto Superstores, Inc., Docket No. 21-ALJ-17-0182-CC (Amended Final Order Aug. 15, 2025)

- *Carmax Auto Superstores West Coast, Inc. v. SC Dep't of Revenue*, 411 S.C. 79 (2014) – Department has burden of proof when seeking alternative apportionment method
- *Carmax* (2014), Department failed to prove threshold issue that statutory formula did not fairly represent business activity in South Carolina



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CarMax Auto Superstores, Inc., Docket No. 21-ALJ-17-0182-CC (Amended Final Order Aug. 15, 2025)

- 2004 restructuring CarMax Business Services
 - CarMax West 93.5% ownership; CarMax East 6.5% ownership
 - East's business process intangibles and financing function
 - East assigned \$2B trademarks to West for no cost (just before CBS created)
- East and West pay CBS management fees; CBS distributes profits back to East and West based on ownership %
- East owns/operates 75%+ retail stores, generates 75% of group's revenue; gets 6.5% profits



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CarMax Auto Superstores, Inc., Docket No. 21-ALJ-17-0182-CC (Amended Final Order Aug. 15, 2025)

- Audit Period: East's South Carolina stores had total operating profit of \$90m, taxable income after apportionment was \$21m
- Income reported did not reflect true economic and business activity in the state



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Duke Energy Corp. v. S.C. Dep't of Revenue, 445 S.C. 499, 914 S.E.2d 873 (Ct. App. 2025), *reh'g denied* (May 12, 2025)

Issue: Is the investment tax credit in § 12-14-60 limited to \$5m annually or lifetime?

ALC: Lifetime.

Court of Appeals: Annual



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Duke Energy Corp. v. S.C. Dep't of Revenue, 445 S.C. 499, 914 S.E.2d 873 (Ct. App. 2025), *reh'g denied* (May 12, 2025)

SECTION 12-14-60. Investment tax credit.

(A)(1) There is allowed an investment tax credit against the tax imposed pursuant to Chapter 6 of this title for any taxable year in which the taxpayer places in service qualified manufacturing and productive equipment property.

(G) The credit allowed by this section for investments made after June 30, 1998, is limited to no more than five million dollars for an entity subject to the license tax as provided by Section 12-20-100.



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Duke Energy Corp. v. S.C. Dep't of Revenue, 445 S.C. 499, 914 S.E.2d 873 (Ct. App. 2025), *reh'g denied* (May 12, 2025)

- No time-specific language in Subsection (G)
- Subsection (G) refers to the credit allowed by subsection (A)(1); that credit is available in “any taxable year.”
- Income tax is a “yearly” tax
- “Absent language providing for a lifetime limitation, we find a credit against a yearly tax is claimable in any taxable year in which the statutory requirements are met.”
- Interpretation supported by purpose of credit, which is to encourage continued investment in this State



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Mastercard International, Inc. v. S.C. Dep't of Revenue, Docket No. 20-ALJ-17-0008-CC (Final Order June 3, 2024)

- **Issue:** Does Mastercard have income-producing activities (IPA) in South Carolina subject to income tax in the State?
- *ALC:* Yes
- *Court of Appeals:* Awaiting oral argument



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Mastercard International, Inc. v. S.C. Dep't of Revenue, Docket No. 20-ALJ-17-0008-CC (Final Order June 3, 2024)

- Section 12-6-2210(B): if taxpayer is transacting business partly within and without the State, SC “income tax is imposed upon a base which *reasonably represents* the proportion of the trade or business carried on within this State.”
- Section 12-6-2290: apportion income using this fraction for each taxable year:

$$\frac{\text{Gross receipts from within SC}}{\text{Total gross receipts from everywhere}}$$



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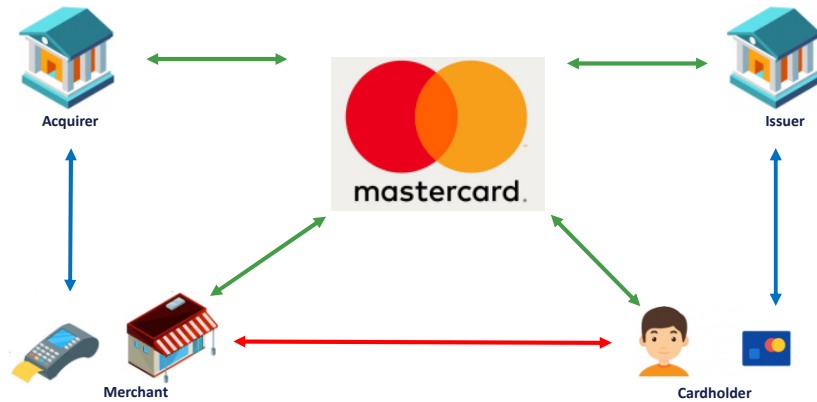
Mastercard International, Inc. v. S.C. Dep't of Revenue, Docket No. 20-ALJ-17-0008-CC (Final Order June 3, 2024)

- Gross receipts for service providers – Section 12-6-2295(A)(5):
“If the **income-producing activity** is performed partly within and partly without this State, sales are attributable to this State to the extent the **income-producing activity** is performed within this State.”
- What is the income producing activity?



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Mastercard International, Inc. v. S.C. Dep't of Revenue, Docket No. 20-ALJ-17-0008-CC (Final Order June 3, 2024)



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Mastercard International, Inc. v. S.C. Dep't of Revenue, Docket No. 20-ALJ-17-0008-CC (Final Order June 3, 2024)

Issues on appeal

- Is Mastercard's IPA the provision of its global payment systems network that facilitates cashless transactions?
- Does Department's ratio reasonably approximate Mastercard's business activity in SC?
- Did ALC abuse discretion to qualify expert in "consumer credit markets"?
- Did ALC err by declining to waive failure to file penalties?



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Synovus Bank v. South Carolina Dep't of Revenue, 444 S.C.
30 (Ct. App. 2024), cert denied (Jan 14, 2025)

Issue: Can a bank deduct NOL carryforwards when calculating its South Carolina bank tax liability?

ALC: No.

Court of Appeals: No

Supreme Court: Certiorari Denied

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Synovus Bank v. South Carolina Dep't of Revenue, 444 S.C.
30 (Ct. App. 2024), cert denied (Jan 14, 2025)

S.C. Code Ann. § 12-11-20:

A tax is imposed upon every bank engaged in business in the State which shall be levied, collected and paid annually with respect to the **entire net income** of the taxpayer doing a banking business within this State or from the sales or rentals of property within this State, computed at the rate of four and one half per cent of the entire net income of such bank or taxpayer.

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Synovus Bank v. South Carolina Dep't of Revenue, 444 S.C.
30 (Ct. App. 2024), cert denied (Jan 14, 2025)

Court of Appeals:

- Proper frame of reference: tax deduction
- No NOL deduction in Chapter 11
- NOL deduction is not inherent in definition of "entire net income"
- Adopting portions of Chapter 6 for administration, enforcement, etc. is not broad enough to include deductions and modifications to income
- History bears out a long and uniform recognition that the bank tax is not an "income tax," but is a franchise tax based on "financial income" instead of "taxable income."
- Facial and structural defects in the "IRC conformity" argument
- No constitutional issues with using book income as basis of "entire net income"

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Tractor Supply Company v. SCDOR, Docket
No. 19-ALJ-17-0416-CC (Jan. 3, 2024)

- **Issue:** Does separate entity reporting fairly represent TSC's business activity; if not, is combined unitary reporting a reasonable and equitable alternative apportionment method?
- *ALC:* Amended Final Order, Dec. 4, 2023; Order Denying Second Motion to Reconsider
- *Court of Appeals:* Oral argument on September 9

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SUPPLY CO.**

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Tractor Supply Company v. SCDOR, Docket No. 19-ALJ-17-0416-CC (Jan. 3, 2024)

- Allocation and apportionment seeks to impose income tax on a base that “reasonably represents the proportion of the [taxpayer’s] trade or business carried on within this State.” *See* Section 12-6-2210(B).
- If the standard apportionment formula does not fairly represent the taxpayer’s business activity in SC, Department can require other methods “to effectuate an equitable allocation and apportionment of the taxpayer’s income.” *See* Section 12-6-2320.
- *Carmax Auto Superstores West Coast, Inc. v. S.C. Dep’t of Rev.*, 411 S.C. 79 (2014)
- *Rent-A-Center West, Inc. v. S.C. Dep’t of Rev.*, 418 S.C. 320 (2016)



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Tractor Supply Company v. SCDOR, Docket No. 19-ALJ-17-0416-CC (Jan. 3, 2024)

- PwC “tax restructuring” in 2001; three affiliated entities
- Intercompany Agreements, including inventory procurement agreement (9.7% markup)
- Texas licenses trademarks for free
- TSC owns/operates almost all retail stores; 80% of group’s sales/inventory
- 82% of Texas’ income generated from intercompany transactions (\$400m from markup, cost of \$13m); because of intercompany transactions, receives 71% of group’s taxable income
- E.g., in 2014 TSC unitary group generated over \$6 billion in gross sales (\$135 million from SC stores); reported \$4.1 million in SC



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Watertoys, LLC d/b/a Tidalwave Watersports v. S.C. Dep't of Revenue, Docket No. 23-ALJ-17-0362-CC (Apr. 18, 2024)

- § 12-21-2420: imposes tax upon paid admissions to places of amusement
- § 12-21-2420(13) – exemption for “admissions to boats which charge a fee for pleasure fishing, excursions, sight-seeing and private charter.”
- “Amusement” undefined, but SCDOR Revenue Rulings from 1989 and 2005 provide longstanding definitions (dictionaries)



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Watertoys, LLC d/b/a Tidalwave Watersports v. S.C. Dep't of Revenue, Docket No. 23-ALJ-17-0362-CC (Apr. 18, 2024)

Examples of Places of Amusements Subject to the Admissions Tax

The following list of places of amusements is not all inclusive and is merely provided as guidance. Charges to enter or use these places, events, facilities and rides and all other amusement facilities are subject to the tax unless specifically exempted under Code Section 12-21-2420 or Code Section 12-21-2430.

SUBJECT: air shows
amusement parks
EFFECTIVE DATE amusement rides, shows and exhibits

pageants

paint ball or laser gun facilities

para sail rides

Introduction

The State of South Carolina provides as guidance:

balloon shows
baseball batting cages (See SC Revenue Ruling 91-14.)
basketball courts
boat cruises (See, however, Code Section 12-21-2420(13). Charges for cruises with entertainment, such as one in which patrons attempt to solve a murder mystery, do not come within the exemption in Code Section 12-21-2420(13).)
boat shows
botanical gardens
bowling alleys
bungee jumping



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Watertoys, LLC d/ b/ a Tidalwave Watersports v. S.C. Dep't of Revenue, Docket No. 23-ALJ-17-0362-CC (Apr. 18, 2024)

- Summary judgment (April 2024); Motion to Reconsider; Notice of Appeal
- Court of Appeals remand; Order on Remand (Sept. 2024)
 - Section 12-60-3370: Before appealing a decision to the court of appeals, a taxpayer must pay or post a bond for all taxes (not including penalties or civil fines) determined to be due by the ALJ
- Order granting Motion to Strike re: ROA



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Watertoys, LLC d/ b/ a Tidalwave Watersports v. S.C. Dep't of Revenue, Docket No. 23-ALJ-17-0362-CC (Apr. 18, 2024)

Issues on Appeal:

- Appellate jurisdiction – is deposit into Appellant's counsel's IOLTA account a bond under section 12-60-3370?
 - Does "all taxes" include interest?
 - "before appealing the decision"?
- Can ALC grant summary judgment without a hearing?
- Is parasailing exempt from admissions tax?
- *Chevron* and *Alltel*?



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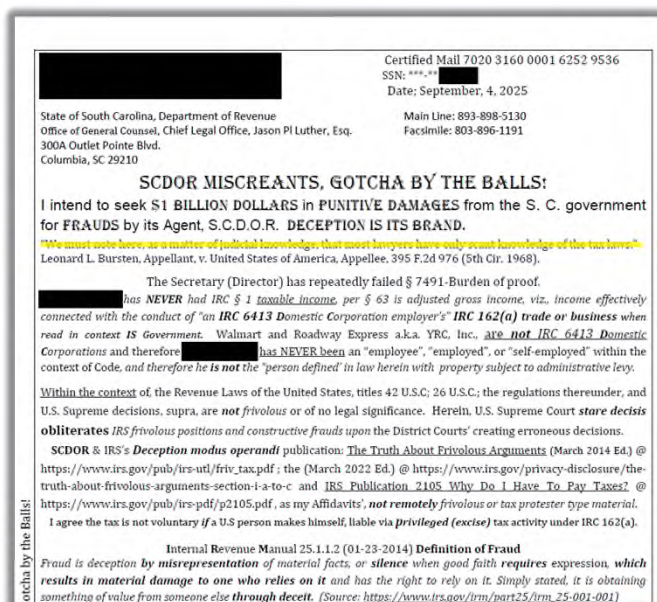
Audience Poll

Proper Written Protest under the Revenue Procedures Act?

- S.C. Code Ann. § 12-60-450
 - TP info
 - Tax info (period, nature/kind of tax in dispute)
 - Facts; statement outlining the reasons for the appeal, including law or other authority upon which the taxpayer relies; and
 - other relevant information the department may reasonably prescribe.

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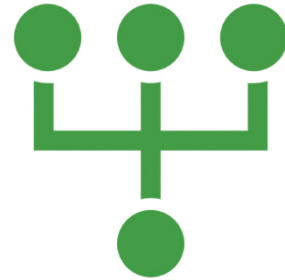
Audience Poll



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Agency Deference in SALT

- *Chevron* two-step
- *Kiamah Dev. Partners, II v. S.C. Dep't of Health & Env't Control*, 411 S.C. 16, 766 S.E.2d 707 (2014) (citing *Chevron*)
 - Interpreting and applying statutes and regulations administered by an agency is a two-step process.
 - **Step One:** court determines whether the language of a statute or regulation directly speaks to the issue. If so, the court must utilize the clear meaning of the statute or regulation.
 - **Step Two:** If the statute or regulation is silent or ambiguous on the specific issue, the court then must give deference to the agency's permissible interpretation of the statute or regulation.



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Agency Deference in SALT

- *Chevron* two-step
- *Kiamah Dev. Partners, II v. S.C. Dep't of Health & Env't Control*, 411 S.C. 16, 766 S.E.2d 707 (2014) (citing *Chevron*)
- Earliest cases involved tax matters:
 - *Read Phosphate v. SC Tax Commission* (1933)
 - *Hadden v. SC Tax Commission* (1937)
 - *U.S. Rubber Prods. V. SC Tax Commission* (1939)

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Agency Deference in SALT

Read Phosphate Co. v. South Carolina Tax Commission, 169 S.C. 314, 168 S.E. 722 (1933):

“The construction given to a statute by those charged with the duty of executing it is always entitled to the most respectful consideration, and ought not to be overruled without cogent reasons. . . The officers concerned are usually able men, and masters of the subject. Not unfrequently they are the draftsmen of the laws they are called upon to interpret.”

Quoting *U.S. v. Moore*, 95 U.S. 760 (1877)

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Loper Bright Enterprises v. Raimondo, 603 U.S. 369 (2024)

“*Chevron* is overruled. Courts must exercise their independent judgment in deciding whether an agency has acted within its statutory authority, as the APA requires. Careful attention to the judgment of the Executive Branch may help inform that inquiry. And when a particular statute delegates authority to an agency consistent with constitutional limits, courts must respect the delegation, while ensuring that the agency acts within it. But courts need not and under the APA may not defer to an agency interpretation of the law simply because a statute is ambiguous.”



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Colonial Pipeline Co. v. S.C. Dep't of Revenue, 443 S.C. 448, 905 S.E.2d 129 (Ct. App. 2024), *cert. denied* (Feb. 12, 2025)

"We are cognizant of the recent United States Supreme Court decision in *Loper Bright* . . . which overruled precedent requiring a reviewing court "to defer to 'permissible' agency [interpretations of the statutes those agencies administered,]" even when a reviewing court might read the statute differently, if " 'the statute [was] silent or ambiguous with respect to the specific issue' at hand." The Court in *Loper* concluded that "[c]ourts must exercise their independent judgment in deciding whether an agency has acted within its statutory authority." The Court explained independent judicial judgment is part of the "solemn duty" of courts to declare what the law is. The Court reminded us that "[t]he Framers appreciated that the laws judges would necessarily apply in resolving those disputes would not always be clear, but envisioned that the final 'interpretation of the laws' would be 'the proper and peculiar province of the courts.'" The Court overruled *Chevron*, which "demand[ed] that courts mechanically afford *binding* deference to agency interpretations" while leaving in place *Skidmore v. Swift & Co.*, 323 U.S. 134, 65 S.Ct. 161, 89 L.Ed. 124 (1944), which endorses "exercising independent judgment . . . consistent with the 'respect' historically given to Executive Branch interpretations."

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Agency Deference in SALT

Further, South Carolina's deference doctrine was adopted from United States Supreme Court precedent. In grounding its decision solely on deference to the Department of Revenue, the Administrative Law Court could not have anticipated that a month later, the United States Supreme Court drove a stake through the heart of "deference" when it struck down the *Chevron* doctrine, the federal version of the state "deference" standard relied on by the Administrative Law Court. In *Loper Bright Enterprises v. Raimondo*, ___ U.S. ___, 144 S.Ct. 2244 (June 28, 2024) (Opinion No.: 22-), the U. S. Supreme Court made the same point appellant makes here; to wit, that granting deference to agencies interpreting their own rules for their benefit are the precise circumstances in which such deference is least warranted: Under *Loper*, the *Chevron* is not entitled to deference.

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Tax Legislative Update for 2025

SOUTH CAROLINA DEPARTMENT OF REVENUE
TAX POLICY SERVICES

Legislation

Significant changes in tax law, by category:

- Income, Bank, Withholding, Corporate License = 14
- Property taxes = 10
- Sales & Use = 9
- Miscellaneous = 15

77% of changes via Act No. 69 (Appropriations Bill)

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Legislation

- Proviso 117.208 – suspends income tax rate reduction for 2025 (top marginal income tax rate 6%)
- Proviso 117.163 – Abandoned Textile Mills Credit
 - If Notice of Intent to Rehabilitate filed by June 30, 2025, then effective for any project if:
 - Between 50k - 55k square feet (began by June 30, 2022); or
 - Between 130k – 135k square feet; and
 - Estimated rehabilitation expenses of either
 - \$3m to \$3.5m, or
 - \$5.5m to \$6.5m

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Legislation

- Proviso 117.202 – political subdivision reimbursement
 - Section 12-37-220(52); exempts 42.8571% of property tax value of certain manufacturing property
 - Increased amount of reimbursement to political subdivisions for revenue loss, now up to \$300m (with balance expended from Trust Fund for Tax Relief)
- Proviso 109.14 – manufacturing property tax reduction disallowed
 - No tax reduction for property owned/leased by any utility, including solar farms

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Legislation

- Act No. 45 – durable medical equipment
 - Amends Section 12-36-2120(74) to apply to all providers who hold a South Carolina retail license.
 - Prior version (only for providers whose principal place of business was in SC) was held unconstitutional in *Orthofix, Inc. v. South Carolina Department of Revenue* and *KCI USA Inc., v. South Carolina Department of Revenue*, 443 S.C. 138, 903 S.E.2d 496 (2024).

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Legislation

- Act No. 42 (tort reform)
 - SCDOR to oversee alcohol server training; certify
 - Mandatory penalties for violations of section 61-4-580
 - Sale of beer/wine at “collegiate sporting venues”
 - Liquor liability risk mitigation (reduce total coverage of \$1m)
- Proviso 117.162 – athletic admissions tax revenue
 - Admissions tax revenue from athletic events of accredited colleges/universities are allocated back to college/university, to be used for supporting student-athletes

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Advisory Opinions

Topics

- 7 Revenue Rulings
- 2 Revenue Procedures
- 21 Information Letters
- Policy Manual – “Tax Incentives for Economic Development”
- National Tax Surveys
- Angel Investor Credit
- Capital Project Sales Tax – Compliance Audits, Paying Project Debt
- Collegiate Sporting Venues
- Tax Exemptions for Farmers
- Credit Against Corp. License Fee
- Durable Medical Equipment (Sales Tax)
- New Jobs Credit
- Sales of Trailers
- Textile Communities Revitalization Act
- Withdrawals for Use
- Per Capita Income Figures
- Tax Legislative Update for 2025

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South Carolina Bar

Continuing Legal Education Division

In the Air or at Sea: How to Prepare for an IRS Examination of Aircraft and Yacht Deductions

Katie Simmons



In the Air or at Sea:

How to Prepare for an IRS Examination of Aircraft and Yacht Deductions

Katie Simmons

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Agenda

1. The Tax Examination Landscape – An Update on the IRS Business Aircraft Campaign
2. Tax Considerations, Consequences and Reporting Requirements
3. What to expect when you get an Information Documentation Request
4. Overview of Yacht Examinations



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01

Section 01

The Tax Examination Landscape –**An Update on the IRS Business Aircraft Campaign**

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Tax Examinations – The General Landscape

- Large Business and International Business Aircraft Campaign launched February 2024
- Areas of emphasis:
 1. Qualified business use
 2. Personal use
 3. Fringe benefit inclusion
- The IRS continues its enhanced enforcement related to aircraft.
 - This began in earnest during the last administration and continues today.
 - The second tranche of aircraft have been selected, and taxpayers are being notified of the impending examinations.

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02

Section 02

Tax Considerations, Consequences and Reporting Requirements

5

Three primary income tax considerations

1. Qualified business use – Can I take accelerated depreciation?
2. Entertainment use – Can I deduct my expenses?
3. Personal use – Do I have to report income?

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Two Main Rule Structures Utilized by the IRS

- Employer-provided aircraft rules
 - Today's discussion will focus on these rules as they are the most commonly used
- Primary purpose aircraft rules
 - These are used when the aircraft ownership/usage is reported on a Schedule C
- Applies to all types of private aircraft usage
 - Full ownership
 - Fractional ownership
 - Fractional leasing
 - Jet card usage
 - Third party charter of the taxpayer's aircraft
 - Taxpayer's charter of someone else's aircraft
 - Interchange usage
 - Timeshare usage

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Income Inclusion for Personal Use of Aircraft

- Applied at the individual passenger level
- Income is generally determined using the Standard Industry Fare Level (SIFL) rules.
 - Computations include the need to understand and know:
 - The difference between "control" and "non-control" employees
 - The maximum certified takeoff weight (MTOW) of the aircraft utilized
 - The number of seats not occupied by crew and available for use on takeoff for each flight leg
 - The statute (not nautical) miles between the origin and destination for each flight leg (1NM = 1.15SM)
 - Whether reimbursements occurred for the personal use by passengers
- The imputed income is reported to the personal passengers or their hosts at least annually.
 - Using Forms K-1, W-2, or 1099-NEC depending upon the circumstances
 - The annual reporting periods allowed are November 1 – October 31 and January 1 – December 31

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Income Inclusion for Personal Use of Aircraft - Continued

- Additional special rules exist for:
 - Personal use by passengers under the age of 2
 - Flights that involve personal legs and business legs
 - Mileage computations when the aircraft stops for fuel stop, weather, customs, or mechanical reasons
 - Personal use by passengers when 50% or more of the seats available for passenger use are occupied by business use passengers
 - Passengers flying with security requirements
 - International travel for more than 7 days involving personal use and business use
- Alternative Methods of Personal Use Valuation
 - Charter rate method (when crew are provided with the aircraft)
 - Lease valuation method (when crew are not provided with the aircraft)
 - These methodologies generally are more expensive than SIFL
 - To the point that the IRS utilizes the charter rate method as the "penalty" for computing SIFL incorrect in some cases

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Expense Disallowance for Entertainment Use of Aircraft

- Applied at the individual passenger level
- Four methodologies exist to arrive at the disallowance percentage
 - Occupied seat hours and miles (OSH/OSM)
 - Flight by flight hours and miles (FBFH/FBFM)
 - Example - 1,000 SM, 1 flight hour with 5 passengers onboard
 - There are 5 OSH and 5,000 OSM
 - Each passenger is attributed .2 FBFH and 200 FBFM
- The disallowance percentage is applied against ALL aircraft related expenses
 - All expenses include non-operating costs such as interest expense and depreciation
- The method chosen is an annual elections without regard to prior years' elections
- The method chosen is applicable to the ENTIRE fleet of aircraft operated.

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Expense Disallowance for Entertainment Use of Aircraft - Continued

- Additional special rules exist for:
 - Ghosting passengers on deadhead flights
 - Maintenance and training flights
 - Aggregating costs and disallowance computations for aircraft with similar cost profiles, propulsion types, and number of engines
 - Costs related to third-party charter and dry lease operations for fair market value payment for services
 - The VERY beneficial election to disallow depreciation expense based upon the lesser of the annual:
 - Hypothetical straight-line depreciation computed over the alternative depreciation system life of the aircraft or actual depreciation allowed on the tax return annually

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Summarizing the 5 Main Passenger Classifications for the Income/Expense Rules

Classification	Deductible?	Imputes income?
Business	Yes	No
Business Entertainment	No	No
Personal Non-entertainment	Yes	Yes
Personal Entertainment	No (with SIFL offset)	Yes
Commuting	No (without SIFL offset)	Yes

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Bonus Depreciation

- The legislative landscape
 - The Tax Cuts and Jobs Act (TCJA) rules for bonus depreciation were in a phase-out period when The One Big Beautiful Bill Act (OBBBA) reinstated 100% bonus depreciation
 - Property placed in service in 2025 was generally eligible for 40% bonus depreciation (decreasing by 20% annually) or 60% for “certain aircraft” and “transportation property.”
 - OBBBA reinstated 100% bonus depreciation for property placed in service on or after January 20, 2025.

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Bonus Depreciation – Continued

- Many taxpayers try to avail themselves of the accelerated method of depreciation
 - Bonus Depreciation (Section 168(k))
 - Expensing (Section 179)
 - General Depreciation System - MACRS (Section 168)
- Aircraft ineligible for GDS must utilize ADS
 - ADS utilizes longer lives AND forces the straight-line methodology
- Eligibility for the accelerated methods of depreciation includes passing the Qualified Business Use (QBU) testing under Section 280F

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IRC Section 280F – The Listed Property Rules

- To be eligible for accelerated depreciation (including bonus) you must have >50% QBU of the aircraft.
 - QBU is defined as use in the trade or business of the taxpayer.
- However, it is the aircraft specific 25% test that really controls what happens for aircraft.
 - The 25% QBU test excludes certain types of usage:
 - Any personal use by 5% owners and their guests
 - Any personal use by a non-5% owner that is personal in nature and income was NOT imputed.
 - In the case of an ownership structure containing a “related party lease”...ANY use by a 5% owner is NOT QBU.
 - Leases between disregarded entities are also disregarded for this rule.
 - If the 25% QBU rule is successfully passed, the above restrictions are removed to compute the final 50% test.
 - The computations use the same methodologies as expense disallowance.
 - If the test is failed, the aircraft must utilize ADS depreciation.
 - Testing continues throughout the ADS depreciable life of the aircraft and if the test is failed in a year subsequent to the placed in service year, the accelerated depreciation previously taken is recaptured in the year of failure.

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IRC Section 280F – The Listed Property Rules - Continued

- The Section 280F 25% and 50% tests are also applicable for the lessee.
 - Since the lessee doesn't have depreciation, the rules call for a one-time addition to income in the year of failure.
- The most important things to remember here:
 - Structure planning is paramount prior to acquisition if the aircraft usage will cause Section 280F QBU testing failures.
 - Testing before the end of the year can give a taxpayer time to adjust the aircraft usage to achieve the desired results.

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More Possible Limitations

- IRC Section 162 – Trade or Business Expenses
- IRC Section 183 – Activities Not Engaged in for Profit (The Hobby Loss Rule)
- IRC Section 465 – Deductions Limited to Amount At-Risk (The At-Risk Rules)
- IRC Section 469 – Passive Activity Losses and Credits Limited (The Passive Loss Rules)
- Unreimbursed Partner Expenses (UPE) – An Extension of Section 162
- IRC Section 67(h) – 2% Floor on Miscellaneous Itemized Deductions - Unreimbursed Employee Expenses
- IRC Section 461(l) – Limitation on Excess Business Losses (EBL) of Noncorporate Taxpayers

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Section 03

What to expect when you get an Information Documentation Request

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Information Document Requests

- The IRS will issue an Information Document Request (IDR) requesting the following information for each aircraft in the taxpayer's fleet:
 - The tail number, type and model of aircraft, and number of seats certified for passengers for takeoff for each flight.
 - Flight logs for all operations of the aircraft including origin, destination, and flight time for each flight leg.
 - Airframe and engine maintenance logs.
 - Passenger listings for all operations designating which passengers are "specified individuals" and which are "control employees."
 - Names of the "5% owners" and designated "related parties" that are passengers for purposes of imputed income and Section 280F computations.
 - Flight type classifications for each individual passenger for each flight leg for all operations.
 - All dry lease agreements.
 - All aircraft management and charter management agreements.
 - All maintenance agreements.
 - All timeshare/interchange agreements.
 - Any aircraft use policy documents
 - The imputed income (SIFL), expense disallowance, and Section 280F computations

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Information Document Requests - Continued

- Contemporaneous documentation supporting the business purpose of all business flights will be requested after the initial IDR response is submitted.
- Examples:
 - Emails/calendar entries showing that the flights/events causing the flights were scheduled at the time
 - Presentation materials, marketing materials, or business cards
 - Meeting agendas and minutes

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Section 04

Overview of Yacht Examinations

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Tax Issues to Consider with a Yacht

- | | | |
|--|---|---|
| • Class Life
(IRC 167) | • Predominate Use
(IRC 168) | • Fringe Benefit Income
(IRC 61) |
| • Ordinary and Necessary
(IRC 162) | • Personal Use Limitations
(IRC 162/274) | • Activity Not For Profit
(IRC 183) |
| • Qualified Business Use
(IRC 280F) | • Dwelling Unit Used as a
Residence (IRC 280A) | • Passive Loss Limitations
(IRC 469) |

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Qualified Business Use (QBU)

- No 25% Test available; 50% Test only
- What is NOT QBU
 - Leasing to 5-percent owner or related
 - Treated as compensation to 5% owner or related
 - Investment (IRC 212) use
 - Any trips disallowed under IRC 274
- Fail QBU?
 - No accelerated depreciation allowed
 - Must use appropriate straight-line class life
 - Prior year accelerated depreciation recapture is calculated

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Class Lives

Asset Class 00.28

- Vessels, barges, tugs and similar transportation equipment
- 10 Year MACRS
- 18 Year SL

Asset Class 44.0

- Commercial water Transportation
- Carrying of Freight or Passengers
- 15 Year MACRS
- 20 Year SL

Asset Class 79.0

- Recreation
- 7 Year MACRS
- 20 Year SL

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Predominate Use

Property is used predominantly outside the United States if it is located outside the United States during more than 50 percent of the taxable year

The determination of whether property is used predominantly outside the United States during the taxable year shall be made by comparing the period of time during the year when the property is physically located outside the United States with the period of time during the year when the property is physically located within the United States.

• Exceptions:

- Shipping property to and from the United States
- Operated in the foreign or domestic commerce of the United States
- Used for the purpose of exploring for, developing, removing, or transporting resources from the outer Continental Shelf
- Used in international or territorial waters within the northern portion of the Western Hemisphere for the purpose of exploring for, developing, removing, or transporting resources from ocean waters or deposits under such waters

If the predominate use of a vessel is outside the U.S then accelerated depreciation is not allowed.

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IRC 280A Deduction Limitations

There are two deduction limitations under IRC 280A for dwelling units that are used personally and rented:

1. Expenses must be allocated under IRC 280A(e)(1) between personal and rental beginning with the first day of personal use. The rental use percentage is generally the number of days rented at Fair Rental Value (FRV) divided by the total days of use (personal days plus rental days).
2. After the allocation of expenses in step #1, IRC 280A(c)(5) limits the rental expenses to gross rental income if the dwelling is used by the taxpayer as residence during the taxable year. Under IRC 280A(d), a dwelling is used as a residence if personal use exceeds the greater of 14 days or 10% of the days

If the 14-day or 10% test in IRC 280A(d) is met, rental expenses are deductible only to the extent of gross rental income. No rental loss may be deducted. Gross rental income means gross rental receipts less expenses directly related to the rental (such as rental agency fees and advertising).

The ordering rules in Prop. Reg. 1.280A-3(d)(3) require allocable rental expenses to be deducted from gross rental income as follows:

1. Otherwise, allowable/deductible expenses: qualified home mortgage interest, real estate taxes, and casualty/theft loss
2. Operating expenses such as utilities, repairs, insurance, etc.
3. Depreciation

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Personal Use Disallowance

Same rules as for an aircraft

Deduction allowed for the amount treated as income to the individual

Usage includes time docked and at sea

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Documentation is Key

- Documentation must be contemporaneous
- No deduction allowed unless substantiated by adequate records or sufficient evidence corroborating the taxpayer's statement including
 - Amount of expense
 - Time and place of travel
 - Business purpose, and
 - Business relationship of persons using the yacht.

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South Carolina Bar

Continuing Legal Education Division

A Look at the New IRS

*Kristin Gutting
Karen Fleming
&
Caitlyn Meehan*



A Look at the New IRS

Kristin Gutting, Karen Fleming, & Caitlyn Meehan

South Carolina Bar Convention – Tax Law Section Seminar
January 24, 2026

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Agenda



- Reflection on the Current IRS Environment
- Hot Topics in IRS Exams
- Hot Topics in IRS Penalty & Procedures
- Advice on Practicing before the IRS
- Q&A

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Reflection on the Current IRS Environment

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*Reflection on the Current IRS Environment:
Uncertainty Looms*

- January 2025 - Over 102,000 employees
- February 2025 –
 - 4,000 to 5,000 IRS workers accepted a voluntary Treasury Deferred Resignation Program
 - 6,000 to 7,000 IRS workers were terminated
- April 2025 - Over 20,000 employees applied for second voluntary Treasury Deferred Resignation Program & over 13,000 were approved
- October 1, 2025 – Government shutdown
- November 12, 2025 - Government reopens
- December 2025 – Around 77,000 employees

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Reflection on the Current IRS Environment

IRS Exams

- Less experienced Revenue Agents
- More focused exams & fewer comprehensive exams
- Different procedural interpretations
- Phasing out LB&I Agreement of Facts Information Document Requests
- More complex taxpayers being audited by SBSE
- Continued focus – partnerships (BBA exams), wealthy individuals (Global Wealth), complex pass-through entities, and large corporations

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Reflection on the Current IRS Environment

Penalty & Procedure

Impact And Comparison To COVID Era

	Shutdown Delays and Impact	The IRS shutdown caused delays in critical processes, making resolution timelines unpredictable.
	Comparison to COVID Bottlenecks	Both the shutdown and COVID caused bottlenecks, but the current IRS posture is stricter, requiring more diligent actions.
	Recommended Practitioner Actions	Practitioners should obtain transcripts frequently, document all IRS interactions, and avoid relying on verbal commitments to mitigate risk.
	Consequences of Assumptions	Assumptions can lead to errors, emphasizing the need for a proactive not reactive approach.

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Reflection on the Current IRS Environment
Penalty & Procedure

Average Timeframes And Implications

PROCESS	AVERAGE TIMEFRAME
TAS Assignment	4-12 weeks
Domestic Penalty (Form 843)	General Income: 3-5 months Informational (1099): 4-6 months Informational (1094/1095): 12-14 months
International Penalty (Form 843)	12-16 months
CDP Hearing	3-5 months
Appeals	4-6 months (confirmation) + 3-4 months (assignment & hearing)

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Hot Topics In IRS Exams



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Hot Topics In IRS Exams: Key IRS Exam Focus Areas

- R&D Credit
- Solar & Wind
- Virtual Currency
- Aircrafts
- Travel, Meals, & Expense Documentation For Business Purposes
- Related Party Activities
- Basis Issues
- Employment Tax Checks

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Hot Topics In IRS Exams: ERC Claim Updates

- Processing Issues:
 - Wrong Signature Issues
 - Not Timely Filed For Q3 2021
 - Wrong Quarter
- Enforcement:
 - IRS Exams - Service Center Exams & Agent Exams
 - Denials – Letter 105c (Full) And Letter 106c (Partial)
 - Appeals Trends
- Considerations:
 - Extension To File Suit (Form 907)
 - Proactive

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Hot Topics in IRS Penalty & Procedure



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Hot Topics in IRS Penalty & Procedure IRS Evolving Positions



Stricter Reasonable Cause Claims

IRS now demands comprehensive documentation for Reasonable Cause claims, increasing scrutiny.



Accelerated Collections Activity

Collections, especially via ACS, have sped up with levy actions happening within 30 days of initial notices.



Practitioner Guidance

Advising clients on proactive payments and thorough communication and documentation is crucial during this enforcement shift.

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Hot Topics in IRS Penalty & Procedure: IRS Evolving Positions

Reasonable Cause



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Challenges & Best Practices

- **IRS Documentation Requirements**
 - The IRS now requires thorough timelines and supporting evidence for Reasonable Cause claims, increasing scrutiny compared to COVID-era leniency.
- **Best Practices for Claims**
 - Tie Reasonable Cause narratives to transcript data including transaction codes and dates and avoid generic hardship claims.
- **Building Strong Arguments**
 - Use verified facts and detailed records to support Reasonable Cause claims effectively and avoid generic or unsupported statements.

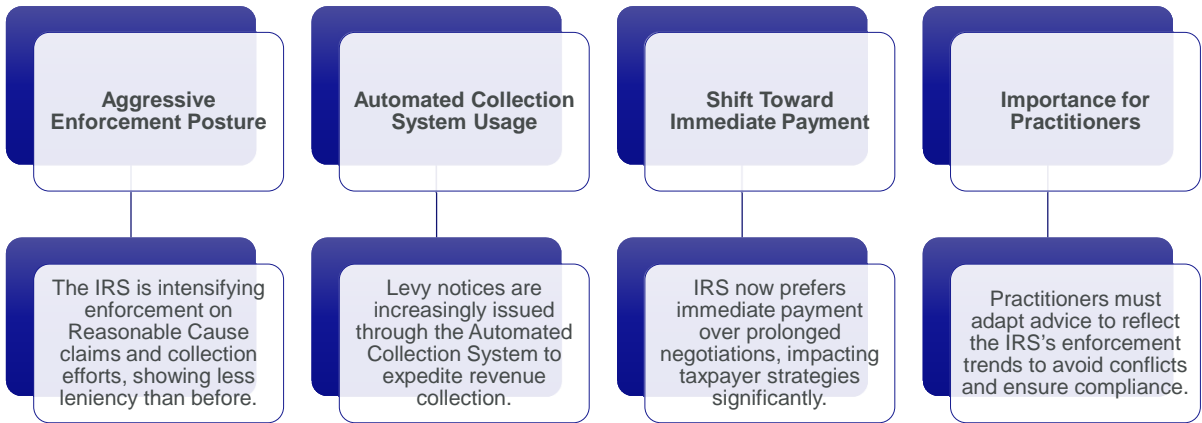
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Hot Topics in IRS Penalty & Procedure: IRS Evolving Positions

Collections



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Advice on Practicing Before the IRS



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Advice on Practicing Before the IRS: IRS Exam

Best Practices



Preparation & Diligence

Retain source documents

Ensure files are transferable & digital

Request monthly check-in calls with Revenue Agent



The IRS is More Virtual

Teams Meetings

TDC & Secure File Transfer



Assess Tenure & Personality of Revenue Agent

Assists in determining how to present information to Revenue Agent

Don't be afraid to request to speak with manager

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*Advice on Practicing Before the IRS:
Penalty & Procedures*

Best Practices



Maintain Current POAs

Ensuring POAs are current and properly filed is crucial for effective practice management.



Disciplined Transcript Reviews

Review transcripts before and after any IRS discussion for accuracy and to prevent issues.



Structured Call Scripts

Use structure during calls to confirm system information, clarify actions, and identify account confirmations.



Build Trust and Competence

Demonstrating these practices builds trust with clients and IRS representatives.

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Q & A



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