

Fishing Information Newsletter

News You Can Use from the Internal Revenue Service

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Message from the Coordinator

I would like to take this opportunity to welcome several new readers. Within the last few months we have added over 135 new subscribers to our distribution register. For those subscribers who are commercial fishing associations, I encourage you to pass this newsletter along to your members.

The purpose of this newsletter is to provide you, the reader, with pertinent tax information. Please do not hesitate to send us your topic ideas and questions to the addresses listed below.

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National Commercial Fishing Coordinator

Please send us your topic ideas and questions....

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Capital Construction Fund (CCF)

The Capital Construction Fund (CCF) was created under a Merchant Marine Act to assist fisherman to acquire fishing vessels or improve a current vessel. The National Oceanic and Atmospheric Administration (NOAA) and the Internal Revenue Service (IRS) jointly administer the CCF.

The CCF program allows taxpayers to defer taxable income by making contributions to a NOAA approved depository and eventually use the accumulated funds for purchasing or improving fishing vessels.

The December 1999 and January 2000 issues of this newsletter covered several aspects of the Capital Construction Fund including the eligibility requirements, procedures in opening a CCF account, the tax treatment of CCF deposits, how to claim a deduction, the tax treatment of CCF earnings and the tax treatment of qualified and non-qualified withdrawals.

Several readers have requested that we provide more detail with respect to what constitutes qualified and non-qualified withdrawals.

Qualified Withdrawals.....

General requirement: To acquire, construct, or reconstruct a new or used vessel or skiff, including but not limited to payments in direct acquisition or payments for a lease in excess of 5 years.

- If you are self-constructing your vessel, all capital costs, including travel, meals (deductible portion), and lodging are considered a capital expense if your project is away from your tax home and these expenses are incurred in connection with the inspection of vessel construction or reconstruction. Wages and other expenses deemed attributable to construction or reconstruction activities are also eligible.
- The overhaul of vessel machinery, including but not limited to rebuilding engines and generator sets, hydraulics and steering systems, if considered an integral part of the vessel.

- Upgrading or acquiring equipment, including but not limited to booms, blocks, reels and drums, if considered an integral part of the vessel.
- The upgrade of the vessel hull, including but not limited to reconstructing or expanding top house and lengthening the vessel.
- Upgrading or acquiring vessel electronics.
- Installation of safety equipment, including but not limited to life rafts, alarms, electronic navigation, communication equipment, electronic emergency beacon (EPIRP), fire control equipment and special non-skid coatings to vessel surface.
- Mortgage payments on a vessel mortgage (principle portion only).
- A qualified withdrawal also includes the earnings on investment (investment income). However, the withdrawal shall be considered as taxable, unless specifically excludable.

Non-Qualified Withdrawals.....

The general rule is that anything that is not a qualified withdrawal is a non-qualified withdrawal. The following examples fall under the category as non-qualified withdrawals:

- Payment of expenses that qualify for tax deductions in the current year (operating expenses), including but not limited to expenses for labor, materials, supplies, fuel, bait, auto expenses, legal and professional fees, supplies. Machinery and equipment that are not considered an integral part of the vessel.
- Fishing Permits and licenses.
- Fishing rights, including but not limited to set-net sites and vessel moratorium rights.
- Shore based capital assets, including but not limited to docks, real property, machinery, and vehicles.

- Other capital assets, including but not limited to set-net site survey and moorings.
- Payments for repairs.
- Payments of interest expense.
- Acquisition or reconstruction of fishing gear, including nets, pots, traps, long lines, and trawl net systems.
- Payments relating to personal living expenses.
- Amounts in fund after termination (voluntary or involuntary).
- Amounts withdrawn to pay vessel mortgage indebtedness that are in excess of vessel tax basis.
- Amounts not withdrawn after 25 years.
- Amounts in accumulation determined by the Internal Revenue Service that exceeds the plan objectives.
- Annual over-deposit in fund, not cured by either withdrawal or carry-over provisions.

(I would like to thank George Bousseilaire, Revenue Agent in Anchorage, Alaska, for providing the content for this article)

Limited Entry Permits

The following question was submitted by one of our readers:

The July issue article "Are the capitalized costs of limited entry fishing permits eligible for an amortization deduction under the Revenue Reconciliation Act of 1993," brings up the topic of "Anti-churning." Under "Wash Sales" rules one might be led to believe that there could be a 30 day period necessary between sale and purchase of a permit. Could you expand upon this, and any other options that might be available to a pre-July 25, 1991, permit holder?

Wash sales are covered in Internal Revenue Code section 1091, and they only apply to wash sales of

stock or securities. Since a limited entry fishing permit isn't a stock or security, the wash sale rules are not applicable.

IRC section 197 provides for the amortization of limited entry fishing permits (they are a government permit). Generally, limited entry fishing permits may only be amortized if they were acquired after August 10, 1993. However, at the election of the taxpayer, they may amortize all section 197 intangibles, including a fishing permit, if acquired after July 25, 1991.

The anti-churning rules were created to PREVENT taxpayers from converting existing section 197 intangibles, for which a depreciation or amortization deduction would not have been allowable under the law as it existed prior to enactment of section 197, into amortizable property under the new section 197 rules. "Existing section 197 intangibles" are intangibles held by the taxpayer on the date of enactment of the Revenue Reconciliation Act of 1993 (RRA '93), which is the law that created section 197 intangible amortization. Under the anti-churning rules, a limited entry fishing permit cannot be amortized if:

---the taxpayer or a related person held or used the fishing permit at any time during the period that begins on July 25, 1991, and ends on August 10, 1993, OR

---the taxpayer acquired the fishing permit from a person that held it at any time during the period that begins on July 25, 1991, and ends on August 10, 1993, and, as part of the transaction, the user of the fishing permit does not change, OR

---the taxpayer grants the right to use the fishing permit to a person (or a person related to such person) that held or used the fishing permit at any time during the period that begins on July 25, 1991, and ends on August 10, 1993.

In addition, Congress gave the Department of the Treasury the authority to issue regulations as may be appropriate to carry out the purposes of this section, including such regulations as may be appropriate to prevent avoidance of the purposes of this section through related persons or otherwise. The "anti-abuse" portion of the regs. state: "The rules in this section shall be interpreted and applied as necessary and appropriate to prevent avoidance of the purposes of section 197. If one of the principal pur-

poses of a transaction is to achieve a tax result that is inconsistent with the purposes of section 197, the Commissioner can recast the transaction for Federal tax purposes as appropriate to achieve tax results that are consistent with the purposes of section 197, in light of applicable statutory and regulatory provisions and the pertinent facts and circumstances."

Based upon all of this, it is doubtful that there is any possibility to convert a limited entry fishing permit that was owned pre-July 25, 1991, to an amortizable section 197 intangible.

How should the income from the emergency transfer of a limited entry permit be reported?

The answer to this question is dependent upon two things. First, is the rental of a limited entry fishing permit considered to be the continuation of the Schedule C business? If YES, it would be reported on the fishing Schedule C subject to self-employment tax. If NO, whether it would be reported on the front of the Form 1040 as "Other Income" (not subject to self-employment tax) or on the Schedule C (subject to self-employment tax) is dependent upon how long the emergency transfer lasts. If it is just one fishing season, it would be reported as other income not subject to self-employment tax. If two or more seasons, it is likely that the income will be reported on Schedule C, subject to self-employment tax.

Need Back Issues?

Back issues of the FIN are available. Please feel free to request them by Month or Volume Number by calling or e-mailing us.

If you change your E-mail Address.....

If you are receiving this newsletter electronically and you have changed your Internet provider, please remember to send us a quick note advising us of any change to your e-mail address.

Alternative Payment Options

The IRS's "Offer-in-Compromise" program is used to settle a taxpayer's debt that is in both the Government's and the taxpayer's best interest. The IRS

will accept an offer-in-compromise to resolve unpaid accounts for less than the amount owed when doubt exists as to whether you owe the liability or when there is doubt that the liability can be collected in full and the amount you offer reasonably reflects your ability to pay. In appropriate cases an offer in compromise may be an alternative for resolving your tax delinquency. To submit an offer-in-compromise you must complete Form 656. Complete instructions are provided on the form.

If the basis of an offer is doubt that you owe the liability (for example, a disputed assessment) you must provide a written statement to support your claim. The Service cannot accept a compromise where the liability has already been decided by a court.

If the basis of the offer is doubt that the liability can be collected in full, in addition to Form 656, you must submit Form 433A, *Collection Information Statement for Individuals*, or Form 433B, *and Collection Information Statement for Businesses*. These forms provide a statement of your income, expenses, assets, and liabilities.

The amount of a doubt as to collectibility offer should at least equal or exceed your equity in all assets. When reviewing a set offer, the IRS considers four factors:

- The amount collectible from your assets,
- The amount collectible from present and future income,
- The amount that can be collectible from 3rd parties; and
- Assets or income that are available to you but not generally subject to the Service's collection, such as assets that are outside of the U.S.

It is your responsibility to show how acceptance of the offer would be in the best interest of the Government.

Generally, the IRS will not accept an offer unless all returns are filed and you exhibit the ability to remain current in the payment of your tax. The acceptance of an offer by the IRS creates a "fresh start"; therefore, the terms of a doubt as to the collectibility offer require future compliance with all tax filing and paying requirements. Any refund due to you for

years prior to and including the year in which your offer is accepted will be offset against your tax liability. If you do not abide by all the terms of the offer, including the compliance requirement, the IRS may reinstate the entire tax liability.

Additional information about the Offer-in-Compromise can be found on Form 656, and in Publication 594, *Understanding the Collection Process*. Publications and forms may be downloaded from www.irs.gov or ordered by calling 1-800-829-3676.

Tax Assistance Hotline, Forms Hotline, Fax on Demand and Teletax

Taxpayer Assistance

Phone Numbers:

(800) 829-1040

Seven days a week, 24 hours a day

(800) 829-4059 TTY/TDD (Hearing Impaired)

Seven days a week, 24 hours a day

Call with general tax questions.

Tax Forms and Publications

(800) 829-3676, seven days a week, 24 hours a day.

Order free tax forms and publications.

IRS Internet Access

World Wide Web: www.irs.gov

The IRS Web Home Page allows convenient access to tax information 24 hours a day. The Web Site provides tax forms with instructions, publications, the latest tax law changes, and much more information for individuals and businesses.



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