

**REPORT TO THE
HOUSE COMMITTEE ON WAYS AND MEANS
CHAIRMAN RICHARD NEAL**

Prepared by staff
of the
JOINT COMMITTEE ON TAXATION



December 15, 2022

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By letter dated June 16, 2021, to Treasury Secretary Yellen and Commissioner Rettig, Chairman Neal, House Committee on Ways and Means, requested certain tax return information under section 6103(f) to evaluate the mandatory examination program for the returns of a sitting United States President (the “June 16th letter”). In particular, the June 16th letter requested the following returns and related Internal Revenue Service (“IRS”) audit materials of former President Donald J. Trump (“Mr. Trump”) for each of the tax years 2015 through 2020, including whether an IRS examination of the returns took place and the present status of the audits, the applicable statutes of limitations,¹ and the issues considered:

1. The Federal income tax returns of Donald J. Trump (Form 1040),
2. The Federal income tax returns of the Donald J. Trump Revocable Trust,²
3. The Federal income tax returns of DJT Holdings LLC (Form 1065),
4. The Federal income tax returns of DJT Holdings Managing Member LLC (Form 1120-S),
5. The Federal income tax returns of DTTM Operations LLC (Form 1065),
6. The Federal income tax returns of DTTM Operations Managing Member Corp (Form 1120-S),
7. The Federal income tax returns of LFB Acquisitions Corp (Form 1120-S),
8. The Federal income tax returns of LFB Acquisition LLC (Form 1065), and
9. The Federal income tax returns of Lamington Farm Club, LLC d/b/a Trump National Golf Club-Bedminster (Form 1120-S).

This report³ is a summary of our review of the examination of the Federal income tax returns received in response to the June 16th letter. It should be noted that our review was limited to the materials received from November 30, 2022, through December 11, 2022. The following discussion only includes a summary of noteworthy issues based on our review of such materials that we believe would have warranted examination. Any returns listed above that were received and reviewed but not mentioned below did not appear to have noteworthy issues. We did not have any investigatory powers (such as the ability to issue information document requests (“IDRs”) or to interview the IRS revenue agents assigned to the audits) that would have provided us with more insight into the accuracy of the returns and the rationale for the scope of the audits. Thus, we express no opinion regarding whether any adjustment, or increase or decrease in tax, would have resulted if these issues had been pursued on examination.

¹ See sec. 6501.

² As described below, this trust does not file a Form 1041 (U.S. Income Tax Return for Estates and Trusts); rather, its activity is reported as part of Mr. Trump’s Form 1040.

³ On November 29, 2022, House Ways and Means Committee Chairman Richard Neal designated certain members of the staff of the Joint Committee on Taxation as his agents under section 6103(f) for the purpose of assisting in reviewing materials received in response to the June 16th letter. All references herein to “our,” “us,” and “we” are references to the agents so designated.

The structure of the organization must be understood to understand the flow in which the tax items were reportable. Mr. Trump is the beneficiary of a revocable trust, noted as request number 2 above. The trust is characterized for Federal income tax purposes as a grantor trust, a disregarded entity for tax purposes. As a disregarded entity, the items of income, deduction, gain, loss, and credit accruing to the trust appear directly on the Federal income tax returns of Mr. Trump. The trust in turn has an ownership in various pass-through entities (partnerships and S corporations) and the items of income, deduction, gain, loss, and credit from these entities flow to the individual Federal income tax returns of Mr. Trump (because the trust is a grantor trust). These pass-through entities own interests in other pass-through entities, the income, deductions, gains, losses, and credits from which flow upwards to the owning entities. In short, the items from the lowest tier entities flow up to the next higher level of pass-through entities and keep flowing upwards, eventually appearing on Mr. Trump's Form 1040s.

Tax Year 2015

For 2015, Mr. Trump and Melania Trump filed a joint income tax return. The 2015 Form 1040 showed the following notable items:

Wages		\$14,141
Taxable interest		\$9,393,096
Ordinary dividends		\$1,729,897
Business income (loss) - Schedule C ⁴		(\$599,030)
Capital gain (loss)		\$35,835,453
Other gains (losses) - Form 4797		\$6,603,042
Taxable pensions		\$77,808
Rental real estate, royalties, partnerships, S corporations, etc. - Schedule E		(\$7,882,011)
Other income		(\$76,909,237)
Total income		(\$31,736,841)
Deductible part of self-employment tax		\$19,594
Adjusted gross income		(\$31,756,435)
Itemized deductions - Schedule A		\$7,997,882
Personal exemptions		<u>\$12,000</u>
Taxable income		\$0
Tax		\$0
Alternative minimum tax		\$2,127,670
Other credits - Form 3800	<u>\$1,485,739</u>	
Total credits		<u>\$1,485,739</u>
Net tax		\$641,931
Self-employment tax		\$39,188
Household employment taxes		\$48,030
Other taxes		<u>\$6,023</u>
Total tax		\$735,172
Federal income tax withheld	\$3,017	
2015 estimated tax payments and amount applied from 2014 return	\$10,756	
Credit for Federal tax on fuels - Form 4136	<u>\$14,276</u>	
Total payments		\$28,049
Amount owed (overpaid)		\$707,123

⁴ For 2015, 27 Schedule Cs were included with the Form 1040.

The 2015 Form 1065 filed by DJT Holdings LLC showed the following notable items:

Page 1	
Gross receipts or sales (net of returns and allowances)	\$25,108,115
Cost of goods sold	\$29,130,916
Gross profit	(\$4,022,801)
Ordinary income (loss) from other partnerships, estates, and trusts	(\$31,684,804)
Other income (loss)	\$26,290,043
Total income (loss)	(\$9,417,562)
Repairs and maintenance	\$510,412
Interest	\$995,740
Depreciation	\$8,290,276
Other deductions	\$14,932,733
Total deductions	\$24,729,161
Ordinary business income (loss)	(\$34,146,723)
Schedule K (Partners' Distributive Share Items)	
Box 11, other income (loss)	\$28,248,588
Box 13a, charitable contributions	\$21,081,511

The 2015 Form 1120-S⁵ filed by DJT Holdings Managing Member LLC showed the following notable items:

Page 1	
Other income (loss)	(\$357,526)
Total income (loss)	(\$357,526)
Taxes and licenses	\$3,076
Other deductions	\$3,791
Total deductions	\$6,867
Ordinary business income (loss)	(\$364,393)
Fuel credit (refunded)	\$109
Schedule K (shareholders' pro rata share items)	
Box 10, other income (loss)	\$282,486
Box 12a, charitable contributions	\$210,816

The 2015 Form 1040 was selected for examination by the IRS. The initial contact was in April 2019, and the opening conference was held in June 2019. At the opening conference, the taxpayer's representative provided an informal claim for refund (2015 Form 1040X) due to the carryback of an historic rehabilitation credit from 2016 of \$24 million. If the claim is approved, the amount of the carryback used (\$641,181) will eliminate the taxpayer's entire Federal income tax liability for 2015, except for \$750.

An examination was also initiated for the 2015 Form 1065 for DJT Holdings LLC. A request for supervisory approval to open a TEFRA⁶ examination for this partnership was made in

⁵ As amended.

⁶ TEFRA refers to the Tax Equity and Fiscal Responsibility Act of 1982 (Pub. L. No. 97-248). The TEFRA rules were enacted in 1982 to establish unified audit rules for certain partnerships, and apply to returns filed

June 2019, and approval was received. The IRS sent a letter to DJT Holdings LLC in July 2019, stating that it had been selected for examination. The examination began in September 2019.

As is typical during an examination, the IRS revenue agent (“agent”) did a preliminary risk analysis to determine the scope of the examination. The agent recommended a limited scope examination to be combined with tax year 2014 due to a short statute of limitations, case sensitivity, and the complexity of issues being contemporaneously worked for tax years 2009 through 2013. The agent also decided not to utilize the Specialist Referral System⁷ in the practice network unless absolutely needed (due to case sensitivity); hence, no specialists were assigned. The audit was limited to carryover items from prior cycles and carryover flow-through adjustments from the TEFRA entity, DJT Holdings LLC. As additional support for a limited examination, the agent noted that the taxpayer hires a professional accounting firm and counsel to prepare and file his tax returns, and those parties perform the necessary activities to ensure the taxpayer properly reports all income and deduction items correctly. A decision was made not to pursue the Seven Springs conservation easement deduction because no charitable contribution deduction was allowed in 2015 as a result of taxable income limitations on Mr. Trump’s Form 1040.⁸ Subsequently, a decision was made to pursue an audit of the Seven Springs conservation easement deduction. The audit file does not reveal the reason for the change in this decision.

No final Revenue Agent Report (“RAR”) has been issued for the 2015 tax year. The prior years’ tax liabilities have not been settled. Thus, although preliminary rollover adjustments are set forth, no final adjustments can be made in this regard until the earlier years are finalized. Regarding Seven Springs, the agent’s notes mention two alternative adjustments for disallowing part or all of the charitable contribution easement deduction. The first would disallow the entire \$21.1 million deduction based on the fact that the appraisal was not a qualified appraisal. The second would reduce the deduction to \$8.95 million based on a valuation adjustment. The agent’s notes suggest the possibility of the imposition of a section 6695A penalty (*i.e.*, the penalty for substantial and gross valuation misstatements attributable to incorrect appraisals).⁹ The issue has not been resolved. There was a site visit to Seven Springs on January 24, 2022,

for partnership taxable years beginning before 2018. For partnership taxable years beginning after 2017, the TEFRA rules were replaced with a centralized partnership audit regime enacted by the Bipartisan Budget Act of 2015 (Pub. L. No. 114-74).

⁷ The IRS Specialist Referral System enables IRS personnel to request an IRS specialist to examine specific issues as part of an audit team.

⁸ A charitable contribution of a conservation easement of \$21,078,900, which was made by Seven Springs LLC, ultimately flowed through to the 2015 Form 1040 (on December 11, 2015, Seven Springs LLC placed a parcel of land in Westchester County, NY, in a conservation easement). The June 16th letter did not request the Federal income tax returns for Seven Springs LLC; as a result, we did not receive nor review such returns.

⁹ A person who prepares an appraisal that he or she knows (or should know) will be used to support a tax position on a return or claim for refund is subject to a civil penalty if such appraisal results in a substantial or gross valuation misstatement within the meaning of the accuracy-related penalty provisions. The penalty is equal to the greater of \$1,000 or 10 percent of the understatement of tax resulting from a substantial or gross valuation misstatement, up to a maximum of 125 percent of the gross income derived from the appraisal, and may be assessed without opportunity for pre-payment judicial review, unlike the accuracy-related penalties. The statute provides an exception if the appraiser establishes that it was “more likely than not” that the appraisal value was the proper value.

and then a meeting was scheduled with the agents and appraisers on November 22, 2022. The agents asked the appraisers if they felt threatened by meeting with them, and the appraisers said no.

Our review of the 2015 returns noted above revealed certain issues we thought warranted examination. These are:

1. Charitable contributions.--Specifically, whether the conservation easement deduction of \$21.1 million and other large donations reported on the 2015 Schedule A (Form 1040) were supported by required substantiation.¹⁰ Even though the deduction was limited in 2015 as a result of Mr. Trump not having any taxable income, it still became part of the charitable contribution deduction carryforward amount (such that it may be deducted in future years if not subject to limitations) and, therefore, would warrant review.¹¹

2. Proper reporting of section 108(i) income deferral.--The 2015 Form 1040 reported (as part of other income on line 21) section 108(i) income of \$282,486 from DJT Holdings Managing Member LLC and \$27,966,102 from DJT Holdings LLC (for a total of \$28.2 million¹²). While a taxpayer generally must recognize cancellation of indebtedness (“COD”) income when a loan is forgiven or a debt is discharged for less than the issue price, a special rule applied to the reacquisitions of business debt at a discount during 2009 or 2010, under which a taxpayer could elect to defer the COD income for five years (2009 reacquisitions) or four years (2010 reacquisitions), and then recognize such deferred COD income ratably over five years. Details of the debt discharge should be examined, particularly since an inclusion in income of \$28.2 million in one year means that a total of \$141 million¹³ is being deferred.

3. Verification of the net operating loss carryover schedule.--The net operating loss carryover to 2015 was shown as \$105,157,825 as part of the other income reported on line 21 of

¹⁰ The Code and Treasury regulations set forth substantiation requirements that vary with the type and amount of the charitable contribution. See sec. 170 and the regulations thereunder. Conservation easement contributions have been an audit focus of the IRS, and the Treasury Department and IRS are in the process of issuing new regulations on the subject. See proposed REG-106134-22, Syndicated Conservation Easement Transactions as Listed Transactions (87 FR 75185, Dec. 8, 2022).

¹¹ For individuals, charitable contribution deductions are generally limited to a percentage of the taxpayer’s adjusted gross income without regard to any net operating loss carryback. The applicable percentage limit varies depending on the type of recipient organization and property contributed. Charitable contributions that exceed the applicable percentage limit may generally be carried forward for up to five years. Sec. 170(b) and (d).

¹² This amount equals the amount shown for box 11 of Schedule K for DJT Holdings LLC, noted above. In 2015, DJT Holdings LLC was owned 99 percent by Mr. Trump and 1 percent by DJT Holdings Managing Member LLC. Mr. Trump owns 100 percent of DJT Holdings Managing Member LLC.

¹³ \$28.2 million x 5 years = \$141 million.

the 2015 Form 1040. Verifying the net operating loss carryovers will ensure that the proper amount of net operating loss is utilized in future years.¹⁴

4. Unreimbursed partnership/S corporation expenses reported on the 2015 Form 1040.-- With respect to a partner in a partnership, unreimbursed business expenses generally are deductible only if required to be paid by the partner without reimbursement under the terms of the partnership agreement.¹⁵ In the case of an S corporation shareholder, the payment of unreimbursed business expenses is generally considered to be a contribution to capital of the S corporation unless the shareholder is an employee of the S corporation, in which case the shareholder may be able to treat such amounts as a miscellaneous itemized deduction (to the extent allowed).¹⁶ For 2015, the total unreimbursed business expenses reported (for all partnerships and S corporations flowing through to the Form 1040) were approximately \$4.9 million. We would suggest looking into these amounts, which would include reviewing each applicable partnership agreement.

5. Related party loans.--Interest income on the 2015 Form 1040 was reported from related party loans made to some of Mr. Trump's children (*i.e.*, Ivanka Trump, Donald Trump Jr., and Eric Trump), in the amount of approximately \$51,000, raising the question of whether the loans were bona fide arm's length transactions, or whether the transfers were disguised gifts that could trigger gift tax and a disallowance of interest deductions by the related borrowers.

6. Validity of sole proprietorship activities.--A majority of the Schedule Cs reported either no gross income (*i.e.*, only expenses), or gross income and expenses that almost entirely offset, raising the question of whether these were valid trade or business activities, or whether these Schedules contained costs derived from personal activities or hobbies.¹⁷ For example, 13 of the 27 Schedule Cs reported only expenses (no gross income). As another example, one Schedule C for Donald J. Trump (speaking) reported gross income of \$50,000, which was almost

¹⁴ Net operating losses arising in taxable years beginning before January 1, 2018, may generally be carried forward 20 years. Sec. 172(b).

¹⁵ Under section 162, a taxpayer generally may not deduct expenses paid on behalf of another. However, a partner may generally deduct expenses paid out of his own funds on behalf of a partnership for which he is not reimbursed if he is required to pay for such items under the partnership agreement. See, *e.g.*, Rev. Rul. 70-253, 1970-1 C.B. 31, and *Probrandt v. Commissioner*, T.C. Memo 2016-135. See also the Instructions for Schedule E (Form 1040).

¹⁶ A shareholder in an S corporation who is also an employee of the S corporation may generally deduct unreimbursed business expenses as a miscellaneous itemized deduction under section 67 (to the extent such amount exceeds two percent of adjusted gross income). If the shareholder is not an employee of the S corporation, then any unreimbursed business expenses are generally not deductible by the shareholder, but rather are treated as a contribution to the S corporation by the shareholder, with the expenditures taken into account by the S corporation. See *Vorreyer v. Commissioner*, T.C. Memo 2022-97 (2022); and Rev. Rul. 71-36, 1971-1 C.B. 51. For 2015, Mr. Trump does not appear to have been an employee of any of the S corporations in which he was a shareholder because we did not see any 2015 Form W-2s for him from any of such entities.

¹⁷ See secs. 162, 183 and 262.

entirely offset by \$46,162 of travel expenses. Audits of closely-held entities often find personal expenditures being improperly deducted as business expenses.

7. Passive versus nonpassive flow-through income and losses.--It should be determined whether the Schedule E losses reported on the 2015 Form 1040 were passive or active losses, which could change the amount of ordinary loss allowed for the year.¹⁸ The more than 400 pass-through entities flowing through to the Form 1040 reported total passive and nonpassive income of \$69.52 million, and total passive and nonpassive losses allowed (including section 179 expenses) of \$79.25 million, resulting in a net ordinary loss of \$9.73 million. It should also be determined whether Mr. Trump had sufficient basis in the entities reporting losses and was sufficiently at risk with respect to such entities to be able to claim the losses.¹⁹

8. Cost of goods sold deduction by DJT Holdings LLC.--The 2015 Form 1065 for DJT Holdings LLC reported a cost of goods sold deduction of \$29.1 million, without any description of the inventory method. It is not clear what DJT Holdings was selling from the face of return. However, based on the IRS audit files, this entity appears to be selling residential and hotel units. In general, real estate should not be treated as inventory and costs should not be recovered through a cost of goods sold reduction to gross income.²⁰ Further, the 2015 Form 1125-A (Cost of Goods Sold) for DJT Holdings LLC reported cost of labor of \$14.1 million (out of total cost of goods sold of \$29.1 million). We would recommend looking into whether sales of real estate, and related costs, are being properly accounted for by the partnership, including an analysis of the labor costs and whether the partnership should have been using the percentage of completion method²¹ to account for the income and costs related to these sales.

9. Hotel expense deduction by DJT Holdings LLC.--The 2015 Form 1065 for DJT Holdings LLC includes a deduction for hotel expenses of \$13.9 million (total deductions were \$24.7 million). We would have inquired about the nature and reasonableness of these costs, and whether any of such amount included capitalizable and/or personal expenses.²²

¹⁸ Section 469 restricts the amount of passive activity losses and credits that can be claimed in a tax year.

¹⁹ A taxpayer cannot deduct a flow-through loss unless the taxpayer has sufficient basis in the partnership or S corporation to absorb the loss. See secs. 704(d) and 1366(d). In addition, the at-risk limitations of section 465 limit the extent to which certain types of income can be offset by deductions or losses. The basis and at-risk limitations are applied before the passive activity limitations of section 469. See Temp. Treas. Reg. sec. 1.469-2T(d)(6)(i).

²⁰ While section 263A applies to require the capitalization of certain costs to real property produced or acquired for sale, real property is not eligible to be accounted for under the inventory rules of section 471. See, e.g., *Atlantic Coast Realty Co. v. Commissioner*, 11 B.T.A. 416 (1928); *W.C. & A.N. Miller Development Co. v. Commissioner*, 81 T.C. 619 (1983); *Homes by Ayres v. Commissioner*, T.C. Memo 1984-475, aff'd 795 F.2d 932 (9th Cir. 1986); *Pierce v. Commissioner*, T.C. Memo 1997-411; Rev. Rul. 69-536, 1969-2 C.B. 109; and Rev. Rul. 86-149, 1986-2 C.B. 67.

²¹ See sec. 460.

²² See secs. 162, 262 and 263(a).

10. Activities of DJT Holdings Managing Member LLC.--The 2015 Form 1120-S for DJT Holdings Managing Member LLC largely consists of flow-through items from lower tier partnerships and S corporations, which then flow through to Mr. Trump's Form 1040. Specifically, for 2015, DJT Holdings Managing Member LLC reported an ordinary loss from other pass-through entities of \$358,466 as part of its other income (loss) of (\$357,526). While it had no gross receipts or sales, it reported deductions of \$6,867 for taxes and licenses, auditing fees, legal expenses, and miscellaneous taxes. In addition, DJT Holdings Managing Member LLC reported a negative retained earnings as of December 31, 2015, of \$1,488,038 on its Schedule L balance sheet. We would recommend requesting an explanation of these items in connection with the trade or business activities carried on by DJT Holdings Managing Member LLC as they strike us as somewhat unusual because the S corporation does not appear to be engaged in an active operating trade or business during 2015.

Tax Year 2016

For 2016, Mr. Trump and Melania Trump filed a joint income tax return. The 2016 Form 1040 showed the following notable items:

Wages		\$978
Taxable interest		\$8,994,141
Ordinary dividends		\$337,938
Business income (loss) - Schedule C ²³		\$8,797,393
Capital gain (loss)		\$10,941,053
Other gains (losses) - Form 4797		(\$444,633)
Taxable pensions		\$77,808
Rental real estate, royalties, partnerships, S corporations, etc. - Schedule E		(\$15,939,523)
Other income		(\$44,955,324)
Total income		(\$32,190,169)
Deductible part of self-employment tax		\$219,505
Adjusted gross income		(\$32,409,674)
Itemized deductions - Schedule A		\$8,158,717
Personal exemptions		\$12,150
Taxable income		\$0
Tax		\$0
Alternative minimum tax		\$2,234,725
Other credits - Form 3800	\$2,233,975	
Total credits		\$2,233,975
Net tax		\$750
Self-employment tax		\$439,009
Household employment taxes		\$45,060
Other taxes		\$129,480
Total tax		\$614,299
Federal income tax withheld	\$168	
Amount paid with request for extension to file	\$1,000,000	
Credit for Federal tax on fuels - Form 4136	\$16,849	
Total payments		\$1,017,017
Amount owed (overpaid)		(\$402,718)
Amount applied to 2017 estimated tax		\$388,441
Estimated tax penalty		\$14,277

²³ For 2016, 21 Schedule Cs were included with the Form 1040.

The 2016 Form 1065 filed by DJT Holdings LLC²⁴ showed the following notable items:

Page 1	
Gross receipts or sales (net of returns and allowances)	\$43,910,246
Cost of goods sold	\$27,266,558
Gross profit	\$16,643,688
Ordinary income (loss) from other partnerships, estates, and trusts	(\$58,940,296)
Other income (loss)	\$0
Total income (loss)	(\$42,296,608)
Repairs and maintenance	\$484,626
Taxes and licenses	\$4,750
Interest	\$1,134,846
Depreciation	\$5,805,150
Other deductions	\$14,771,148
Total deductions	\$22,200,520
Ordinary business income (loss)	(\$64,497,128)

The 2016 Form 1065 filed by DTTM Operations LLC showed the following notable items:

Page 1	
Total income (loss)	\$807,444
Other deductions	\$142,457
Total deductions	\$142,457
Ordinary business income (loss)	\$664,987

The 2016 Form 1040 was selected for examination by the IRS. The initial contact was in September 2019. The opening conference was held in December 2019.

An examination was initiated for the 2016 Form 1065 for DJT Holdings LLC. The IRS sent a letter to DJT Holdings LLC in February 2020, stating that it had been selected for examination. The opening conference was held in July 2020.

As is typical during an examination, the agent did a preliminary risk analysis to determine the scope of the examination. The agent noted that the examination of the 2016 Form 1040 was a mandatory examination under Internal Revenue Manual 3.28.3.3.3.²⁵ The agent listed examination issues as including related party loans (although we did not see an audit trail for this item in the audit files), an active participation inquiry, the tracing of net operating losses, and the review of related entity returns for 2016. The agent also noted that the taxpayer hires a professional accounting firm and counsel to prepare and file his tax returns, and that the parties

²⁴ The 99 percent ownership of DJT Holdings LLC was transferred from Mr. Trump to the Donald J. Trump Revocable Trust in 2016.

²⁵ As cited in the audit files. The current Internal Revenue Manual (“IRM”) cite for the mandatory examination of the President’s individual income tax returns is I.R.M. 3.28.3.5.3 (11-17-2020). Based on our review, we did not see where the mandatory examination language was used by the IRS in connection with the audits of 2017 through 2019.

perform necessary activities to ensure taxpayer properly reports all income and deduction items from Schedule K-1s, Form 1099s, etc., that the taxpayer receives. The agent issued an IDR inquiring about Mr. Trump's active participation with respect to his nonpassive losses, and based on the taxpayer's response, the agent determined that Mr. Trump met the active participation requirements of section 469 as a result of meeting the 100/500 hour material participation test.²⁶ Notwithstanding the considerable amount of time spent by Mr. Trump in campaigning for the office of the President of the United States, the agent determined that he was still heavily involved with his business operations in 2016 and mathematically met the 100/500 hour requirements.

The agent's preliminary risk analysis for DJT Holdings LLC noted that depending on the outcome of prior cycle adjustments, there will be carryover adjustments to 2016 for the cost of sales-units deduction and depreciation deduction (*i.e.*, the section 743(b) carryover items²⁷). The agent also noted the need to obtain the partnership agreement, the operating agreement with the general partner, financial statements and trial balance detail, as well as general ledger detail for the cost of sales-units account and depreciation. Other items of interest noted by the agent included legal fees, flow-through items from other partnerships and S corporations, the rehabilitation credit reported by the Old Post Office LLC²⁸ on its 2016 Form 1065, and legal fees paid by the Trump Corporation²⁹ of \$284,839.

No final RAR has been issued for the 2016 tax year. The prior years' tax liabilities have not been settled. Thus, although preliminary rollover adjustments are set forth, no final adjustments can be made in this regard until the earlier years are finalized.

Our review of the 2016 returns noted above revealed certain issues we thought warranted examination. These are:

1. Charitable contributions.--Mr. Trump's 2016 Form 1040 Schedule A reported charitable contributions of \$1,191,210 (\$1,111,000 of cash contributions, and \$80,210 flowing through from Schedule K-1s). We would have inquired as to whether the large cash contributions were supported by required substantiation.³⁰ Even though the deduction was limited in 2016 as a result of Mr. Trump not having any taxable income, it still became part of

²⁶ An individual will be deemed to materially participate in an activity if the individual participates more than 500 hours in that activity, or the individual participates in more than 100 hours in that activity and this participation is not less than the participation of any other individual. See sec. 469(h) and Treas. Reg. Sec. 1.469-5T.

²⁷ Section 743(b) requires a write-down of basis in certain circumstances.

²⁸ The June 16th letter did not request the Federal income tax returns for the Old Post Office LLC; as a result, we did not receive nor review such returns.

²⁹ The June 16th letter did not request the Federal income tax returns for the Trump Corporation; as a result, we did not receive nor review such returns.

³⁰ The Code and Treasury regulations set forth substantiation requirements that vary with the type and amount of the charitable contribution. See sec. 170 and the regulations thereunder.

the charitable contribution deduction carryforward amount (such that it may be deducted in future years if not subject to limitations) and, therefore, would warrant review.³¹

2. Proper reporting of section 108(i) income deferral.--The 2016 Form 1040 reported (as part of other income on line 21) section 108(i) income of \$282,486 from DJT Holdings Managing Member LLC and \$27,966,102 from DJT Holdings LLC (for a total of \$28.2 million). While a taxpayer generally must recognize COD income when a loan is forgiven or a debt is discharged for less than the issue price, a special rule applied to the reacquisitions of business debt at a discount during 2009 or 2010, under which a taxpayer could elect to defer the COD income for five years (2009 reacquisitions) or four years (2010 reacquisitions), and then recognize such deferred COD income ratably over five years. Details of the debt discharge should be examined, particularly since an inclusion in income of \$28.2 million in one year means that a total of \$141 million³² is being deferred.

3. Verification of the net operating loss carryover schedule.--The net operating loss carryover to 2016 was shown as \$73,376,129 as part of the other income reported on line 21 of the Form 1040. Verification of the net operating loss carryover amounts will ensure that the proper amount of net operating loss is utilized in future years.³³

4. Unreimbursed partnership/S corporation expenses reported on the 2016 Form 1040.--With respect to a partner in a partnership, unreimbursed business expenses generally are deductible only if required to be paid by the partner without reimbursement under the terms of the partnership agreement.³⁴ In the case of an S corporation shareholder, the payment of unreimbursed business expenses is generally considered to be a contribution to capital of the S corporation unless the shareholder is an employee of the S corporation, in which case the shareholder may be able to treat such amounts as a miscellaneous itemized deduction (to the extent allowed).³⁵ For 2016, the total unreimbursed business expenses reported (for all

³¹ For individuals, charitable contribution deductions are generally limited to a percentage of the taxpayer's adjusted gross income without regard to any net operating loss carryback. The applicable percentage limit varies depending on the type of recipient organization and property contributed. Charitable contributions that exceed the applicable percentage limit may generally be carried forward for up to five years. Sec. 170(b) and (d).

³² \$28.2 million x 5 years = \$141 million.

³³ Net operating losses arising in taxable years beginning before January 1, 2018, may generally be carried forward 20 years. Sec. 172(b).

³⁴ Under section 162, a taxpayer generally may not deduct expenses paid on behalf of another. However, a partner may generally deduct expenses paid out of his own funds on behalf of a partnership for which he is not reimbursed if he is required to pay for such items under the partnership agreement. See, e.g., Rev. Rul. 70-253, 1970-1 C.B. 31, and *Probrandt v. Commissioner*, T.C. Memo 2016-135. See also the Instructions for Schedule E (Form 1040).

³⁵ A shareholder in an S corporation who is also an employee of the S corporation may generally deduct unreimbursed business expenses as a miscellaneous itemized deduction under section 67 (to the extent such amount exceeds 2 percent of adjusted gross income). If the shareholder is not an employee of the S corporation, then any unreimbursed business expenses are generally not deductible by the shareholder, but rather are treated as a contribution to the S corporation by the shareholder, with the expenditures taken into account by the S corporation.

partnerships and S corporations flowing through to the Form 1040) were approximately \$1.9 million. We would suggest looking into these amounts, which would include reviewing each applicable partnership agreement.

5. Related party loans.--Interest income on the 2016 Form 1040 was again reported from related party loans made to some of Mr. Trump's children (*i.e.*, Ivanka Trump, Donald Trump Jr., and Eric Trump), in the amount of approximately \$51,000, raising the question of whether the loans were bona fide arm's length transactions, or whether the transfers were disguised gifts that could trigger gift tax and a disallowance of interest deductions by the related borrowers.

6. Validity of sole proprietorship activities.-- A number of the Schedule Cs either had no gross income (*i.e.*, only expenses), or gross income and expenses that entirely (or almost entirely) offset, raising the question of whether these were valid trade or business activities, or whether these Schedules contained costs derived from personal activities or hobbies.³⁶ In 2016, out of the 21 Schedule Cs, two reported expenses equal to the amount of gross income, nine reported only expenses (no gross income), eight reported a net profit, one reported negative gross income and expenses, and one reported no gross income or expenses. For example, the 2016 Schedule C for DT Endeavor I LLC (aviation) reported gross income of \$680,886 and total expenses of \$680,886. Similarly, the 2016 Schedule C for DJT Aerospace LLC (aviation) reported gross income of \$376,493 and total expenses of \$376,493. Audits of closely-held entities often find personal expenditures being improperly deducted as business expenses.

7. Passive versus nonpassive flow-through income and losses.--It should be determined whether the Schedule E losses from partnerships and S corporations reported on the 2016 Form 1040 were passive or active losses, which could change the amount of ordinary loss allowed for the year.³⁷ The more than 400 pass-through entities flowing through to the Form 1040 reported total passive and nonpassive income of \$85.87 million, and total passive and nonpassive losses allowed (including section 179 expenses) of \$103.64 million, resulting in a net ordinary loss from partnerships and S corporations of approximately \$17.77 million. It should also be determined whether Mr. Trump had sufficient basis in the entities reporting losses and was sufficiently at risk with respect to such entities to be able to claim the losses.³⁸

8. General business credits, including a \$26.3 million rehabilitation credit.--The 2016 Form 3800 (Form 1040) reported a rehabilitation credit of \$26.3 million. Given the stringent

See *Vorreyer v. Commissioner*, T.C. Memo 2022-97 (2022); and Rev. Rul. 71-36, 1971-1 C.B. 51. For 2016, Mr. Trump does not appear to have been an employee of any of the S corporations in which he was a shareholder because we did not see any 2016 Form W-2s for him from any of such entities.

³⁶ See secs. 162, 183 and 262.

³⁷ Section 469 restricts the amount of passive activity losses and credits that can be claimed in a tax year.

³⁸ A taxpayer cannot deduct a flow-through loss unless the taxpayer has sufficient basis in the partnership or S corporation to absorb the loss. See secs. 704(d) and 1366(d). In addition, the at-risk limitations of section 465 limit the extent to which certain types of income can be offset by deductions or losses. The basis and at-risk limitations are applied before the passive activity limitations of section 469. See Temp. Treas. Reg. sec. 1.469-2T(d)(6)(i).

requirements for the rehabilitation credit, we think this item should have been audited to see if the rehabilitation credit requirements were satisfied.³⁹ Even though Mr. Trump was not able to fully utilize the credit in 2016 due to taxable income limitations, it became part of his general business credit carryback and carryforward, available for use in prior and subsequent years.⁴⁰

9. Cost of goods sold deduction by DJT Holdings LLC.--Similar to 2015, the 2016 Form 1065 for DJT Holdings LLC reported a cost of goods sold deduction of \$27.3 million. As noted above, real estate generally should not be treated as inventory and costs should not be recovered through a cost of goods sold reduction to gross income.⁴¹ Further, the 2016 Form 1125-A (Cost of Goods Sold) for DJT Holdings LLC reported cost of labor of \$13.5 million (out of total cost of goods sold of \$27.3 million). We would recommend looking into whether sales of real estate, and related costs, are being properly accounted for by the partnership, including an analysis of the labor costs and whether the partnership should have been using the percentage of completion method⁴² to account for the income and costs related to these sales.

10. Hotel expense deduction by DJT Holdings LLC.--The 2016 Form 1065 for DJT Holdings includes a deduction for hotel expenses of \$13.9 million (total deductions were \$22.2 million). We would recommend inquiring about the nature and reasonableness of these costs, and whether any of such amount included capitalizable and/or personal expenses.⁴³

11. DTTM Operations LLC (Form 1065).--We did not see any mention of DTTM Operations LLC in the audit files for 2016. However, upon reviewing the returns, we noted that DTTM Operations LLC began business in 2016, and in its first year reported total income of \$807,444, and total deductions of \$142,457 (which included legal expense of \$139,553), for ordinary business income of \$664,987. We would recommend inquiring about the nature of the legal fees, including whether any of such legal fees should have been capitalized and amortized as start-up expenditures (pursuant to section 195) or organizational expenses (pursuant to section 709).

³⁹ See sec. 47.

⁴⁰ Unused general business credits may generally be carried back 1 year and carried forward 20 years. See sec. 39. As noted above, an informal claim for refund (2015 Form 1040X) was provided to the IRS exam team to carryback the 2016 rehabilitation credit.

⁴¹ As noted above, while section 263A applies to require the capitalization of certain costs to real property produced or acquired for sale, real property is not eligible to be accounted for under the inventory rules of section 471.

⁴² See sec. 460.

⁴³ See secs. 162, 262 and 263(a).

2017 and 2018 Tax Years⁴⁴

For 2017 and 2018, Mr. Trump and Melania Trump filed a joint income tax return. The 2017 and 2018 Form 1040s showed the following notable items:

	2017	2018
Wages	\$373,629	\$393,957
Taxable interest	\$6,758,494	\$9,435,377
Ordinary dividends	\$21,984	\$60,254
Business income (loss) - Schedule C ⁴⁵	\$1,433,030	(\$430,408)
Capital gain (loss)	\$7,528,298	\$22,015,123
Other gains (losses) - Form 4797	\$33,740	\$0
Taxable pensions	\$84,351	\$86,532
Rental real estate, royalties, partnerships, S corporations, etc. - Schedule E	(\$16,746,815)	(\$11,992,220)
Other income	(\$12,306,111)	\$4,826,478
Total income	(\$12,819,400)	\$24,395,093
Deductible part of self-employment tax	\$97,548	\$55,397
Adjusted gross income	(\$12,916,948)	\$24,339,696
Itemized deductions - Schedule A	\$10,237,921	\$1,388,307
Personal exemptions	\$12,150	\$0 ⁴⁶
Taxable income	\$0	\$22,951,389
Tax	\$0	\$5,287,122
Alternative minimum tax	\$7,435,857	\$4,069,110
Foreign tax credits - Form 1116	\$0	\$1,264,257
Other credits - Form 3800	\$7,435,107	\$7,092,509
Total credits	\$7,435,107	\$8,356,766
Net tax	\$750	\$999,466
Self-employment tax	\$195,095	\$110,793
Household employment taxes	\$27,213	\$7,475
Other taxes	\$61,660	\$951,088
Total tax	\$284,718	\$2,068,822
Federal income tax withheld	\$97,455	\$87,310
2017 estimated tax payments and amount applied from 2016 return	\$388,441	\$4,431,776
Amount paid with request for extension to file	\$4,200,000	\$7,500,000
Excess social security tax withheld	\$83	\$63

⁴⁴ The IRS audit files included 2017 and 2018 in the same audit cycle, so we are presenting information for both years together for consistency with the related audit files.

⁴⁵ For 2017, four Schedule Cs were included with the Form 1040. For 2018, five Schedule Cs were included with the Form 1040.

⁴⁶ Personal exemptions are suspended for 2018 through 2025. See sec. 151(d)(5).

Credit for Federal tax on fuels - Form 4136	\$30,515		\$30,598	
Total payments		\$4,716,494		\$12,049,747
Amount owed (overpaid)		(\$4,431,776)		(\$9,980,925)
Amount applied to next year's estimated tax		\$4,431,776		\$9,980,925

The 2017 and 2018 Form 1065s filed by DJT Holdings LLC showed the following notable items:

Page 1	2017	2018
Gross receipts or sales (net of returns and allowances)	\$49,257,638	\$50,505,081
Cost of goods sold	\$24,486,894	\$22,678,392
Gross profit	\$24,770,744	\$27,826,689
Ordinary income (loss) from other partnerships, etc.	(\$51,625,181)	(\$48,404,917)
Other income (loss)	\$0	\$199,764
Total income (loss)	(\$26,854,437)	(\$20,378,464)
Salaries and wages	\$4,554,524	\$4,700,287
Repairs and maintenance	\$1,117,252	\$956,833
Rent	\$3,150,970	\$2,846,941
Taxes and licenses	\$423,402	\$397,575
Interest	\$1,402,402	\$1,816,128
Depreciation	\$4,698,590	\$4,586,469
Employee benefit programs	\$108,349	\$137,297
Other deductions	\$15,555,569	\$17,654,984
Total deductions	\$31,011,058	\$33,096,514
Ordinary business income (loss)	(\$57,865,495)	(\$53,474,978)

The 2017 and 2018 Form 1120-Ss filed by DJT Holdings Managing Member LLC showed the following notable items:

Page 1	2017⁴⁷	2018
Gross receipts or sales (net of returns and allowances)	\$23,021,014	\$17,541,357
Cost of goods sold	\$7,132,045	\$6,861,820
Gross profit	\$15,888,969 ⁴⁸	\$10,679,537
Other income (loss)	(\$418,749) ⁴⁹	(\$410,902)
Total income (loss)	\$15,470,220⁵⁰	\$10,268,635
Salaries and wages	\$4,380,562	\$4,493,701
Repairs and maintenance	\$283,997	\$318,435
Rent	\$62,308	\$75,761
Taxes and licenses	\$633,001	\$1,034,505
Interest	\$2,227	\$6,922
Depreciation	\$1,501,214	\$1,566,299
Advertising	\$91,626	\$90,959
Employee benefit programs	\$561,737	\$788,066
Other deductions	\$3,528,453	\$4,038,955
Total deductions	\$11,045,125⁵¹	\$12,413,603
Ordinary business income (loss)	\$4,425,095⁵²	(\$2,144,968)
Fuel credit (refunded)	\$1,727 ⁵³	\$1,505

The 2017 and 2018 Form 1065s filed by LFB Acquisition LLC showed the following notable items:

Page 1	2017	2018
Total income (loss)	\$17,390,799	\$13,856,524
Total deductions	\$20,833,034	\$14,971,077
Ordinary business income (loss)	(\$3,442,235)	(1,114,553)

⁴⁷ As amended.

⁴⁸ For 2015 and 2016, DJT Holdings Managing Member LLC reported no gross sales or gross receipts, or cost of goods sold.

⁴⁹ For 2015 and 2016, DJT Holdings Managing Member LLC reported other income (loss) of (\$357,526) and (\$644,972), respectively.

⁵⁰ For 2015 and 2016, DJT Holdings Managing Member LLC reported total income (loss) of (\$357,526) and (\$644,972), respectively.

⁵¹ For 2015 and 2016, DJT Holdings Managing Member LLC reported total deductions of \$6,867 and \$49,066, respectively.

⁵² For 2015 and 2016, DJT Holdings Managing Member LLC reported ordinary business income (loss) of (\$364,393) and (\$694,038), respectively.

⁵³ For 2015 and 2016, DJT Holdings Managing Member LLC reported a fuel credit (refunded) of \$109 and \$119, respectively.

During September 2020, the IRS met internally to discuss the risking of Mr. Trump's 2017 Form 1040, including the *New York Times* article published on September 27, 2020, discussing Mr. Trump's tax returns and financial dealings (the "*New York Times* article"),⁵⁴ as well as the voluminous number of returns that flow through to the Form 1040 (*i.e.*, over 400 Schedule K-1s). Based on the number of pass-through entities flowing through to the Form 1040 (many of which are owned 100 percent (directly or indirectly) by Mr. Trump), they discussed setting criteria for risking the returns to make the process manageable. Mention was made of the history of difficult negotiations between Mr. Trump's counsel and IRS personnel. In addition, due to sensitivity, it was noted that the revenue agents would not use the Specialist Referral System. Instead, they will directly request team members after discussing with the Territory Manager and Director of Field Operations.

In November 2020, the IRS examination team continued its preliminary risk analysis for issues to consider in the examination. Based on certain issues identified in the *New York Times* article (such as the fivefold increase in general and administrative expenses from 2016 to 2017 for Bedminster Golf Club), it was noted that risking should include the 2017 returns for Bedminster Golf Club and Seven Springs LLC, as well as the Form 1040s of immediate family members receiving both salary and non-salary compensation, while maintaining a high materiality threshold in order to avoid identifying immaterial risks. In addition, it was noted that they would review the 2017 return for COD income and determine the level of risk (the *New York Times* article mentioned that Mr. Trump took advantage of a special rule that allowed for the deferral of COD income from 2010).

The *New York Times* article also claimed that Mr. Trump took \$9.7 million of business investment credits, some of which relate to the Old Post Office hotel renovations. The IRS identified the credits as a potential issue for 2016 and 2017, but noted that the credits would need to be material to add to the in-process 2016 examination that was nearing closure. In response to the article's discussion of \$26 million of consulting fees paid from 2010 through 2018, the IRS noted that materiality will be assessed entity-by-entity, but that with nearly 500 entities, it is unlikely the issue will be material on most returns and that the resources needed to examine would far outweigh any potential benefits. With respect to the *New York Times* article's discussion of family members being paid as consultants and the payments being deducted by the paying entities (*e.g.*, Ivanka Trump's financial disclosure reported \$747,622 of consulting fees that matched deductions by Trump organizations for hotel projects in Vancouver and Hawaii), it was noted that the agent would consider reviewing the 2017 and 2018 returns for a potential collateral examination, but that the consulting fees appear to be a 2013 issue that is unlikely to be material enough to add to the older cycle. In addition, Ivanka Trump's then employment was outside of the Trump organizations.

The *New York Times* article also mentioned personal expenditures for fuel, meals, haircuts, makeup artists, etc., that were written off as business expenses. The IRS noted it would

⁵⁴ Russ Buettner, Susanne Craig and Mike McIntire, "Long-Concealed Records Show Trump's Chronic Losses and Years of Tax Avoidance," *New York Times*, September 27, 2020.

consider the aircraft issue on related returns,⁵⁵ and that while it was unlikely to be a significant issue on the Form 1040, it could be on other returns. The *New York Times* article further mentioned Seven Springs and the related property taxes deducted by Mr. Trump as business expenses. The agent was going to risk the item for the 2017 return, including potentially adding Seven Springs LLC to the examination. The \$21 million conservation easement contribution flowing from Seven Springs to Mr. Trump in 2015 was noted as a potential issue that was previously passed on due to Mr. Trump's taxable income limitation for 2015. The current focus was on catching up to examine the "Presidential" returns, and that no examination resources were currently being applied to examine the Trump Corporation (so legal fees paid by the Trump Corporation were not currently being examined).

The preliminary risk analysis also included a review of the net operating loss carryover schedule (including the charitable contribution deduction carryover), review of carryover basis adjustments from prior years, whether the amount of income (loss) from partnerships and S corporations should be adjusted as a result of related entity examinations, whether Mr. Trump materially participated in the activities reported as nonpassive losses, whether there was a technical termination of a partnership, and whether the tax treatment of the \$21 million payment and settlement of the Trump University⁵⁶ litigation was correct. In connection with the \$21 million settlement payment, the agent wanted to determine whether any deductions were barred by section 162(f),⁵⁷ the treatment of legal fees, the source of the settlement payment to determine whether there was a circular cash flow, whether Mr. Trump had adequate basis in his partnership interest to claim the deduction, and whether Mr. Trump received any insurance proceeds as reimbursement for the settlement payment. With respect to DJT Holdings LLC, there was also mention of examining the 2017 optional partnership adjustments of \$4.7 million.

The IRS audit files included an email dated November 18, 2020, which noted the issues to potentially consider as part of the examination cycle. Such issues included a general review of passive versus nonpassive activities since Mr. Trump was President during 2017 and 2018, reviewing whether Mr. Trump had adequate basis and was at risk for pass-through losses claimed, reviewing the most material pass-through entities (*i.e.*, those reporting the largest amount of losses), reviewing the Trump Corporation since it is likely the primary operating entity,⁵⁸ and setting a substantial materiality threshold for any issues to be added to older cycles.⁵⁹

⁵⁵ Although no detail is mentioned, we assume the agent was referring to personal use of the aircraft by Mr. Trump and related parties.

⁵⁶ The June 16th letter did not request the Federal income tax returns for Trump Entrepreneur Initiative LLC f/k/a Trump University LLC; as a result, we did not receive nor review such returns.

⁵⁷ Section 162(f) denies a deduction for certain fines, penalties, and other amounts.

⁵⁸ We did not see any further information regarding any examination of the Trump Corporation in the IRS audit files.

⁵⁹ It was noted that the examination team has a good relationship with the taxpayer's new representative, and there was concern that any attempt to establish issues on older cycles could diminish the current relationship.

Subsequently, the IRS held a team meeting in February 2021 to discuss the examination plan for the 2017 and 2018 Form 1040s and relevant pass-through entities. It was noted that the 2017 – 2018 examination cycle is expected to include 2019. There was also mention of reviewing Ivanka Trump’s 2018 financial disclosure OGE Form 278e,⁶⁰ reviewing changes in ownership between related parties (including below market sales), reviewing changes in partnership/LLC/S corporation ownership, considering foreign activities, and determining whether the issues identified would have any impact on Mr. Trump’s tax liability. Follow-up team meetings were held to review the analysis of the Schedule Es and 30 entities that were selected for review, to discuss the team’s initial impressions of returns to be selected for further examination, and to complete an analysis of the net operating loss carryforward amounts to 2017 that rest, in part, on the conservation easement deduction. We did not see any documentation in the audit file discussing any final decisions made. It was noted that consulting fees were difficult to examine unless they were found to be fraudulent payments, and that the IRS was not interested in examining Form 990-PF (return of a private foundation) or the rehabilitation credit.

The 2017 and 2018 Form 1040s were selected for examination by the IRS. The initial contact was during March 2021, and the opening conference was held in April 2021.

An examination was initiated for the 2017 and 2018 Form 1065s for DJT Holdings LLC. The IRS sent a letter to DJT Holdings LLC in March 2021, stating that it had been selected for examination, and the opening conference was held in April 2021 (as part of the opening conference for the 2017 and 2018 Form 1040s).

Around this time, Mr. Trump’s representative contacted the IRS team manager to discuss the examination team size (*i.e.*, the increase in team size from one to three agents) and security, concerns over new issues, transparency in transition between representatives, and restricted consent.⁶¹ The IRS team manager communicated to Mr. Trump’s representative that while the 2014 – 2016 examinations were limited issue examinations focused on rollover issues from prior cycles (*i.e.*, 2009 – 2013) and any significantly material issues, it had always been the IRS’s plan that the 2017 examination would not be a limited scope examination and might require additional team members. The IRS team manager explained that the team risked the 2017 Form 1040, and the Schedule E was determined to be high risk, requiring additional team members for the examination due to the over 400 flow-through entities being reported (and after considering the fact that it is a tiered pass-through structure, there are actually about 500 pass-through entity returns). Hence, three revenue agents were assigned to the 2017 examination cycle and this examination would represent most or all of their case load.

Mr. Trump’s representative also expressed concerns about the examination team adding conservation easement contribution issues late in the examination for 2014 and 2015.⁶² The IRS team manager explained that such issues were not examined because they would not impact Mr.

⁶⁰ Executive Branch Personnel Public Financial Disclosure Report.

⁶¹ In a restricted consent agreement, the taxpayer agrees to extend the statute of limitations, but only for those items agreed to in the restricted consent – not for all items in the return.

⁶² The June 16th letter did not request any Federal income tax returns for tax year 2014; as a result, we did not receive nor review any such returns.

Trump's tax liabilities when the risk was evaluated for those years. However, subsequent section 743(b) adjustments to those years could make the contributions deductible and made the contributions worthy of examination. Mr. Trump's representative also asserted that adding any new issues to the older cycles was a breach of the agreement with the prior representative that no new issues would be added as they moved towards the closure of the examinations. The IRS team manager noted that there was no breach of the agreement, and that while the older cycles were moving towards closure, the conservation easement contributions were material enough to request additional information (*i.e.*, each conservation easement contribution was between \$20 million and \$25 million, which is material). In addition, Mr. Trump's representative wanted a restricted consent to extend the statute of limitations to issues currently on the table. The IRS team manager documented that he did not feel comfortable entering into a restricted consent for any of the years because of the size of the return, which involved so many moving parts.

The senior revenue agent designed the examination plan in September 2021. IDRs were issued requesting a global tax organization chart, verification of Mr. Trump's basis in Trump Entrepreneur Initiative LLC f/k/a Trump University LLC, any related party management consulting services agreements (including any agreements, statements of work, engagement letters, etc. with all related parties, informal agreements made with related parties, and list of recipients of management/consulting fees with amounts paid/deducted), and verification of members and the tax matters partner for DJT Holdings LLC for 2017. While taxpayer responses were received in response to the IDRs, we did not see an RAR in the files; it is unclear if resolution has been reached or if any adjustments will be made with respect to any of these issues.⁶³ There was also mention of a notice of potential identity theft related to the filing of a Form 1040SR. In response, LB&I⁶⁴ was making inquiries, but we did not see any further information regarding the identity theft issue contained in the files.

With respect to 2018, the agent noted several "Large unusual questionable items" ("LUQs"), including a \$12.1 million loss from the Trump Corporation (2018 Form 1120-S) (which included \$3.3 million of legal and professional fees), loans and exchanges of \$800,000 included in current assets of the Trump Corporation's 2018 Schedule L (Balance Sheet per Books), a \$55.2 million loss for DJT Holdings LLC (2018 Form 1065), that includes a \$9.8 million flow-through loss from Trump Endeavor 12 LLC,⁶⁵ and a \$14 million flow-through loss from Trump Old Post Office LLC. The agent recommended a review of Mr. Trump's basis in the entities to be able to use the losses, as well as a review of Form W-2s and Form 1099s for payments to related parties.

With respect to DJT Holdings LLC, IDRs were issued asking for information about the partnership's books and records, tax preparation software, financial statements, etc., as well as

⁶³ While we did not see an RAR in the files, we did see documentation regarding the IRS's calculations and determination that Mr. Trump had adequate basis to claim losses on his 2017 Form 1040 from the Trump University loss flowing through to him.

⁶⁴ The Large Business and International division of the IRS.

⁶⁵ The June 16th letter did not request the Federal income tax returns for Trump Endeavor 12 LLC; as a result, we did not receive nor review such returns.

the section 743(b) basis adjustments for depreciation (related to hotel units that were reclassified from inventory to depreciable property).

Our review of the 2017 and 2018 returns noted above revealed certain issues we thought warranted examination. These are:

1. Charitable contributions.--Mr. Trump's 2017 and 2018 Form 1040 Schedule As reported charitable contributions of \$1.9 million and \$500,150, respectively. We would have inquired as to whether the large cash contributions were supported by required substantiation.⁶⁶ Even though the deduction was limited in 2017 as a result of Mr. Trump not having any taxable income, it still became part of the charitable contribution deduction carryforward amount (such that it may be deducted in future years if not subject to limitations) and, therefore, would warrant review.⁶⁷ Further, in 2018, Mr. Trump had taxable income, enabling him to benefit from a charitable contribution deduction.

2. Miscellaneous itemized deductions for 2017.⁶⁸--Mr. Trump's 2017 Form 1040 Schedule A reported a miscellaneous itemized deduction in the amount of \$4.1 million, most of which was described as being for expenses for the production of income, deductible under section 212. This amount warrants further review.

3. Proper reporting of section 108(i) income deferral.--The 2017 and 2018 Form 1040s reported section 108(i) income of \$282,486 and \$282,485, respectively, from DJT Holdings Managing Member LLC and \$27,966,103 and \$27,966,102, respectively, from DJT Holdings LLC (for a total of \$28.2 million each year). While a taxpayer generally must recognize COD income when a loan is forgiven or a debt is discharged for less than the issue price, a special rule applied to the reacquisitions of business debt at a discount during 2009 or 2010, under which a taxpayer was permitted to elect to defer reporting the COD income for five years (2009 reacquisitions) or four years (2010 reacquisitions), and then to begin to recognize such deferred COD income ratably over five years. Details of the debt discharge should be examined, particularly since an inclusion in income of \$28.2 million in one year means that a total of \$141 million is being deferred.⁶⁹

4. Verification of the net operating loss carryover schedule.--The net operating loss carryover to 2017 and 2018 was shown as \$44,979,682 and \$23,422,109, respectively, as part of

⁶⁶ The Code and Treasury regulations set forth substantiation requirements that vary with the type and amount of the charitable contribution. See sec. 170 and the regulations thereunder.

⁶⁷ For individuals, charitable contribution deductions are generally limited to a percentage of the taxpayer's adjusted gross income without regard to any net operating loss carryback. The applicable percentage limit varies depending on the type of recipient organization and property contributed. Charitable contributions that exceed the applicable percentage limit may generally be carried forward for up to five years. Sec. 170(b) and (d).

⁶⁸ For 2017, miscellaneous itemized deductions were deductible to the extent they exceeded 2 percent of adjusted gross income. Sec. 67(a). Miscellaneous itemized deductions are not deductible for 2018 – 2025. Sec. 67(g).

⁶⁹ \$28.2 million x 5 years = \$141 million.

the other income reported on line 21 of the Form 1040s. Verification of the net operating loss carryovers will ensure that the correct amount of net operating loss was utilized each year.⁷⁰

5. Unreimbursed partnership/S corporation expenses reported on Form 1040.--With respect to a partner in a partnership, unreimbursed business expenses generally are deductible only if required to be paid by the partner without reimbursement under the terms of the partnership agreement. In the case of an S corporation shareholder, the payment of unreimbursed business expenses is generally considered to be a contribution to capital of the S corporation unless the shareholder is an employee of the S corporation, in which case the shareholder may be able to treat such amounts as a miscellaneous itemized deduction (to the extent allowed).⁷¹ For 2017 and 2018, the total unreimbursed business expenses reported (for all partnerships and S corporations flowing through to the Form 1040) were approximately \$2.1 million and \$1.9 million, respectively. We would suggest looking into these amounts, which would include reviewing each applicable partnership agreement.

6. Related party loans.--Interest income on Form 1040 was again reported from related party loans made to some of Mr. Trump's children (*i.e.*, Ivanka Trump, Donald Trump Jr., and Eric Trump), in the amount of approximately \$51,000 in both 2017 and 2018, raising the question of whether the loans were bona fide arm's length transactions, or whether the transfers were disguised gifts that could trigger gift tax and a disallowance of interest deductions by the related borrowers.

7. Validity of sole proprietorship activities.-- A number of Schedule Cs either had no gross income (*i.e.*, only expenses), or gross income and expenses that entirely (or almost entirely) offset, raising the question of whether these were valid trade or business activities, or whether these Schedules contained costs derived from personal activities or hobbies.⁷² For example, the 2017 Schedule C for DJT Aerospace LLC (aviation) reported gross income of \$42,965 and total expenses of \$42,965, the second consecutive year this business showed an equal amount of gross income and expense.⁷³ In 2018, of the five Schedule Cs, three reported only expenses (no gross income), and two reported losses. For example, the 2018 Schedule C for Donald J. Trump (management services) reported no gross income, just taxes and licenses

⁷⁰ Net operating losses arising in taxable years beginning before January 1, 2018, may generally be carried forward 20 years. Sec. 172(b). The 2018 Form 1040 net operating loss carryover statement reported the net operating loss carryover as being fully utilized in 2018.

⁷¹ A shareholder in an S corporation who is also an employee of the S corporation may generally deduct unreimbursed business expenses as a miscellaneous itemized deduction under section 67 (to the extent such amount exceeds 2 percent of adjusted gross income). If the shareholder is not an employee of the S corporation, then any unreimbursed business expenses are generally not deductible by the shareholder, but rather are treated as a contribution to the S corporation by the shareholder, with the expenditures taken into account by the S corporation. See *Vorreyer v. Commissioner*, T.C. Memo 2022-97 (2022); and Rev. Rul. 71-36, 1971-1 C.B. 51. For 2017 and 2018, Mr. Trump does not appear to have been an employee of any of the S corporations in which he was a shareholder because we did not see any 2017 or 2018 Form W-2s for him from any of such entities. As noted above, unreimbursed job expenses are not deductible as a miscellaneous itemized deduction for 2018 through 2025.

⁷² See secs. 162, 183 and 262.

⁷³ The remaining three of the four Schedule Cs reported net profit in 2017.

expense of \$38,764. Similarly, the 2018 Schedule C for DJT Endeavor I (aviation) reported gross income of \$38,392 and expenses of \$312,773, for a net loss of \$274,381. Audits of closely-held entities often find personal expenditures being improperly deducted as business expenses.

8. Passive versus nonpassive flow-through income and losses.-- It should be determined whether the Schedule E losses from partnerships and S corporations reported on the Form 1040s were passive or active losses, which could change the amount of ordinary loss allowed for each year.⁷⁴ The more than 400 pass-through entities flowing through to the Form 1040s reported total passive and nonpassive income of \$80.64 million and \$75.04 million for 2017 and 2018, respectively, and total passive and nonpassive losses allowed (including section 179 expenses) of \$97.9 million and \$87.2 million for 2017 and 2018, respectively, resulting in a net ordinary loss from partnerships and S corporations of \$17.3 million and \$12.2 million for 2017 and 2018, respectively. It should also be determined whether Mr. Trump had sufficient basis in the entities reporting losses and was sufficiently at risk with respect to such entities to be able to claim the losses.⁷⁵

9. Foreign tax credits.--Since the 2018 Form 1040 reported taxable income, foreign tax credits could be utilized, and a foreign tax credit of \$1.3 million was claimed for 2018. Verification of the foreign tax payments made will ensure that eligible amounts are being claimed as a credit. We would recommend requesting receipts for foreign tax payments to countries with the largest amounts making up the foreign tax credit, including the foreign tax credit carryforwards (*e.g.*, foreign taxes paid over \$500,000 per country over the 10-year period ending in 2018).⁷⁶

10. General business credit carryover.--The general business credit carryover to the 2017 Form 1040 is shown as \$22.6 million, partly attributable to the 2016 rehabilitation credit. As noted above, given the stringent requirements for the rehabilitation credit, we think this item should have been audited to see if the rehabilitation credit requirements were satisfied.⁷⁷ Even though Mr. Trump was not able to fully utilize the credit in 2016, 2017, or 2018 due to taxable income limitations, it continues to be part of his general business credit carryforward, available for use in future years.⁷⁸ As noted above, an informal claim was made for 2015 to carryback the

⁷⁴ Section 469 restricts the amount of passive activity losses and credits that can be claimed in a tax year.

⁷⁵ A taxpayer cannot deduct a flow-through loss unless the taxpayer has sufficient basis in the partnership or S corporation to absorb the loss. See secs. 704(d) and 1366(d). In addition, the at-risk limitations of section 465 limit the extent to which certain types of income can be offset by deductions or losses. The basis and at-risk limitations are applied before the passive activity limitations of section 469. See Temp. Treas. Reg. sec. 1.469-2T(d)(6)(i).

⁷⁶ See secs. 901 and 904(c).

⁷⁷ See sec. 47.

⁷⁸ Unused general business credits may generally be carried back one year and carried forward 20 years. See sec. 39.

2016 rehabilitation credit. If any part of the claim is allowed, the amount carried forward to 2017 and beyond must be decreased.

11. Rental real estate income (loss) for DJT Holdings LLC 2017 Form 1065.--DJT Holdings LLC 2017 Schedule E included a commercial rental real estate property that reported a significant loss of \$949,123 (rents received of \$792,698 and total expenses of \$1,741,821), as well as a residential rental real estate property (single family home) with no rental income, but total expenses of \$137,111.⁷⁹ We would recommend inquiring about the reason for the significant loss on the commercial rental real estate property, as well as whether the residential rental real estate property was actually held for rent during 2017. If the property is not used in a rental real estate activity, it raises the question of whether the residence might be held for personal use, and the payment of the expenses would be a distribution (non-deductible) to the partner.⁸⁰

12. Cost of goods sold deductions by DJT Holdings LLC and DJT Holdings Managing Member LLC.--The 2017 and 2018 Form 1065s for DJT Holdings LLC reported a cost of goods sold deduction of \$24.5 million and \$22.7 million, respectively. As noted above, real estate generally should not be treated as inventory and costs should not be recovered through a cost of goods sold reduction to gross income.⁸¹ Further, the 2017 and 2018 Form 1125-As (Cost of Goods Sold) for DJT Holdings LLC reported cost of labor of \$12.8 million and \$11.4 million, respectively (out of total cost of goods sold of \$24.5 million and \$22.7 million, respectively). We would recommend looking into whether sales of real estate, and related costs, are being properly accounted for by the partnership, including an analysis of the labor costs and whether the partnership should have been using the percentage of completion method⁸² to account for the income and costs related to these sales.

Similarly, the 2017 and 2018 Form 1120-Ss for DJT Holdings Managing Member LLC reported a cost of goods sold deduction of \$7.1 million and \$6.9 million, respectively. However, for 2015 and 2016, this entity did not report any sales or cost of goods sold (it only reported losses from pass-through entities and deductions, plus refundable fuel credits). Further, the 2017 and 2018 cost of goods sold deduction calculation (as reported on Form 1125-A) included lot development costs of \$4.98 million and \$5.12 million, respectively. We would recommend inquiring about the change in business activities between 2016 and 2017 (*e.g.*, an explanation for the change from no sales to significant sales), as well as the nature of the lot development costs, why they were included in the cost of goods sold computation, and the methodology used to allocate such costs to sales.

⁷⁹ The same property was also reported, but with different amounts, on Schedule E of Form 1040 for 2017. It was also shown on the Schedule E of the Form 1040s for 2015 and 2016.

⁸⁰ See sec. 731. See also, secs. 262 and 280A.

⁸¹ As noted above, while section 263A applies to require the capitalization of certain costs to real property produced or acquired for sale, real property is not eligible to be accounted for under the inventory rules of section 471.

⁸² See sec. 460.

13. LFB Acquisition LLC (Form 1065).--We did not see any mention of LFB Acquisition LLC in the 2017 or 2018 audit files, but observed some noteworthy deductions after reviewing the partnership's returns. Specifically, management fees and general and administrative expenses were significantly higher in 2017 than in 2016 and 2018. LFB Acquisition LLC reported management fees of \$750,997, \$1,919,780, and \$707,786 in 2016, 2017, and 2018, respectively, and general and administrative expenses of \$549,607, \$2,846,420, and \$570,454 in 2016, 2017, 2018, respectively. We would recommend inquiring about the large increase in these deductions for 2017 when compared to other years.

2019 Tax Year

For 2019, Mr. Trump and Melania Trump filed a joint income tax return. The 2019 Form 1040 showed the following notable items:

Wages		\$393,928
Taxable interest		\$11,332,436
Ordinary dividends		\$71,921
Business income (loss) - Schedule C ⁸³		(\$225,560)
Capital gain (loss)		\$9,257,197
Taxable pensions		\$86,532
Rental real estate, royalties, partnerships, S corporations, etc. - Schedule E		(\$16,472,951)
Total income		\$4,443,503
Deductible part of self-employment tax		\$62,789
Adjusted gross income		\$4,380,714
Itemized deductions - Schedule A		\$1,405,541
Taxable income		\$2,975,173
Tax		\$558,780
Alternative minimum tax		\$0
Other credits - Form 3800	\$425,335	
Total credits		\$425,335
Net tax		\$133,445
Self-employment tax		\$125,578
Household employment taxes		\$4,720
Other taxes		\$197,234
Total tax		\$460,977
Federal income tax withheld	\$86,490	
2019 estimated tax payments and amount applied from 2018 return	\$10,980,925	
Excess social security tax withheld	\$56	
Credit for Federal tax on fuels - Form 4136	\$29,026	
Total payments		\$11,096,497
Amount owed (overpaid)		(\$10,635,520)
Amount applied to 2020 estimated tax		\$10,635,520

⁸³ For 2019, six Schedule Cs were included with the Form 1040.

The 2019 Form 1065 filed by DJT Holdings LLC showed the following notable items:

Page 1	
Gross receipts or sales (net of returns and allowances)	\$48,522,768
Cost of goods sold	\$23,357,170
Gross profit	\$25,165,598
Ordinary income (loss) from other partnerships, estates, and trusts	(\$35,046,425)
Other income (loss)	\$99,168
Total income (loss)	(\$9,781,659)
Salaries and wages	\$4,900,520
Repairs and maintenance	\$847,474
Rent	\$3,367,871
Taxes and licenses	\$383,122
Interest	\$1,801,896
Depreciation	\$3,842,370
Employee benefit programs	\$112,738
Other deductions	\$18,599,418
Total deductions	\$33,855,409
Ordinary business income (loss)	(\$43,637,068)

The 2019 Form 1120-S filed by DJT Holdings Managing Member LLC showed the following notable items:

Page 1	
Gross receipts or sales (net of returns and allowances)	\$14,563,803
Cost of goods sold	\$2,076,942
Gross profit	\$12,486,861
Other income (loss)	(\$118,116)
Total income (loss)	\$12,368,745
Salaries and wages	\$4,445,951
Repairs and maintenance	\$336,911
Rent	\$237,253
Taxes and licenses	\$794,388
Interest	\$2,621
Depreciation	\$1,583,303
Advertising	\$77,428
Employee benefit programs	\$1,021,871
Other deductions	\$4,509,539
Total deductions	\$13,009,265
Ordinary business income (loss)	(\$640,520)
Fuel credit (refunded)	\$1,546

During April 2022, the IRS sent a letter to Mr. Trump and Melania Trump notifying them that their 2019 Form 1040 had been selected for examination, as well as to DJT Holdings LLC, notifying it that its 2019 Form 1065 had been selected for examination.

In the audit files for 2019, the agent noted several LUQs, including an \$11.1 million loss from the Trump Corporation (which included \$3.3 million of legal and professional fees); loans and exchanges of \$1.5 million included in current assets of the Trump Corporation's 2019

Schedule L (Balance Sheet per Books); a \$43.4 million loss for DJT Holdings LLC (2019 Form 1065), that includes a \$4.7 million flow-through loss from Trump Endeavor, a \$15.8 million flow-through loss from Trump Old Post Office, and a \$4.7 million loss from Trump Ferry Point; and a final return that had been filed for Trump Organization, Inc., reporting no income.⁸⁴ The agent also recommended a review of Form W-2s and Form 1099s for related party payments.

Our review of the 2019 returns noted above revealed certain issues we thought warranted examination. These are:

1. Charitable contributions.--Mr. Trump's 2019 Form 1040 Schedule A reported charitable contributions of \$504,700. We would inquire as to whether the large cash contributions were supported by required substantiation.⁸⁵ Further, in 2019, Mr. Trump had taxable income, enabling him to benefit from a charitable contribution deduction.

2. Unreimbursed partnership/S corporation expenses reported on the 2019 Form 1040.--With respect to a partner in a partnership, unreimbursed business expenses generally are deductible only if required to be paid by the partner without reimbursement under the terms of the partnership agreement. In the case of an S corporation shareholder, the payment of unreimbursed business expenses is generally considered to be a contribution to capital of the S corporation, or non-deductible if the shareholder is an employee of the S corporation.⁸⁶ For 2019, the total unreimbursed business expenses reported (for all partnerships and S corporations flowing through to the Form 1040) were approximately \$11.2 million. We would suggest examining these amounts, which would include reviewing each applicable partnership agreement, particularly because this amount was significantly higher than what was reported in prior years (*e.g.*, \$1.9 million in 2018) and were incurred while Mr. Trump was President.

4. Related party loans.--Interest income on the 2019 Form 1040 was again reported from related party loans made to some of Mr. Trump's children (*i.e.*, Ivanka Trump, Donald Trump Jr., and Eric Trump), in the amount of approximately \$51,000 in 2019, raising the question of whether the loans were bona fide arm's length transactions, or whether the transfers were disguised gifts that could trigger gift tax and a disallowance of interest deductions by the related borrowers.

5. Validity of sole proprietorship activities.--A number of Schedule Cs either had no gross income (*i.e.*, only expenses), or income and expenses that entirely (or almost entirely) offset, raising the question of whether these were valid trade or business activities, or whether

⁸⁴ The June 16th letter did not request the Federal income tax returns for either Trump Ferry Point or Trump Organization, Inc.; as a result, we did not receive nor review such returns.

⁸⁵ The Code and Treasury regulations set forth substantiation requirements that vary with the type and amount of the charitable contribution. See sec. 170 and the regulations thereunder.

⁸⁶ For 2019, Mr. Trump does not appear to have been an employee of any of the S corporations in which he was a shareholder because we did not see any 2019 Form W-2s for him from any of such entities. As noted above, unreimbursed job expenses are not deductible as a miscellaneous itemized deduction for 2018 through 2025.

these Schedules contained costs derived from personal activities or hobbies.⁸⁷ In 2019, out of the six Schedule Cs, two reported net profits of zero, three reported losses, and one reported a net profit. For example, the 2019 Schedule C for Donald J. Trump (management services) reported gross income of \$94,017 and expenses of \$94,017. Similarly, the 2019 Schedule C for Melania Trump (modeling) reported gross income of \$3,848 and expenses of \$3,848. As another example, the 2019 Schedule C for DJT Operations II LLC (aviation) reported no gross income and expenses of \$7,382. Audits of closely-held entities often find personal expenditures being improperly deducted as business expenses.

6. Passive versus nonpassive flow-through income and losses.-- It should be determined whether the Schedule E losses from partnerships and S corporations reported on the 2019 Form 1040 were passive or active losses, which could change the amount of ordinary loss allowed for the year.⁸⁸ The more than 400 pass-through entities flowing through to the 2019 Form 1040 reported total passive and nonpassive income of \$57.99 million, and total passive and nonpassive losses allowed (including section 179 expenses) of \$74.61 million, resulting in a net ordinary loss from partnerships and S corporations of \$16.62 million. It should also be determined whether Mr. Trump had sufficient basis in the entities reporting losses and was sufficiently at risk with respect to such entities to be able to claim the losses.⁸⁹

7. General business credit carryover.--The general business credit carryover to the 2019 Form 1040 was \$12.4 million, partly attributable to the rehabilitation credit that was reported in 2016. As noted above, given the stringent requirements for the rehabilitation credit, we think this item should have been audited to see if the rehabilitation credit requirements were satisfied.⁹⁰ Even though Mr. Trump has not been able to fully utilize the credit in intervening years due to taxable income limitations, it continues to be part of his general business credit carryforwards, available for use in future years.⁹¹ As noted above, an informal claim was made for 2015 to carryback the 2016 rehabilitation credit. If any part of the claim is allowed, the amount carried forward to 2017 and beyond must be decreased.

8. Cost of goods sold deductions by DJT Holdings LLC and DJT Holdings Managing Member LLC.--The 2019 Form 1065 for DJT Holdings LLC reported a cost of goods sold deduction of \$23.4 million. As noted above, real estate generally should not be treated as inventory and costs should not be recovered through a cost of goods sold reduction to gross

⁸⁷ See secs. 162, 183 and 262.

⁸⁸ Section 469 restricts the amount of passive activity losses and credits that can be claimed in a tax year.

⁸⁹ A taxpayer cannot deduct a flow-through loss unless the taxpayer has sufficient basis in the partnership or S corporation to absorb the loss. See secs. 704(d) and 1366(d). In addition, the at-risk limitations of section 465 limit the extent to which certain types of income can be offset by deductions or losses. The basis and at-risk limitations are applied before the passive activity limitations of section 469. See Temp. Treas. Reg. sec. 1.469-2T(d)(6)(i).

⁹⁰ See sec. 47.

⁹¹ Unused general business credits may generally be carried back one year and carried forward 20 years. See sec. 39.

income.⁹² Further, the 2019 Form 1125-A (Cost of Goods Sold) for DJT Holdings LLC reported cost of labor of \$11.3 million (out of total cost of goods sold of \$23.4 million). We would recommend looking into whether sales of real estate, and related costs, are being properly accounted for by the partnership, including an analysis of the labor costs and whether the partnership should have been using the percentage of completion method⁹³ to account for the income and costs related to these sales.

Similarly, the 2019 Form 1120-S for DJT Holdings Managing Member LLC reported a cost of goods sold deduction of \$2.1 million. Further, the 2019 cost of goods sold deduction calculation (as reported on Form 1125-A) included developed lot costs of \$1.9 million. We would recommend inquiring about the nature of the developed lot costs, why they were included in the cost of goods sold computation, and the methodology used to allocate such costs to sales.

⁹² As noted above, while section 263A applies to require the capitalization of certain costs to real property produced or acquired for sale, real property is not eligible to be accounted for under the inventory rules of section 471.

⁹³ See sec. 460.

2020 Tax Year

For 2020, Mr. Trump and Melania Trump filed a joint income tax return. The 2020 Form 1040 showed the following notable items:

Wages		\$393,229
Taxable interest		\$10,626,179
Ordinary dividends		\$25,347
Taxable refunds, credits, or offsets of state and local income taxes		\$382,065
Business income (loss) - Schedule C ⁹⁴		(\$29,686)
Other gains (losses) - Form 4797		(\$501,255)
Taxable pensions		\$86,532
Rental real estate, royalties, partnerships, S corporations, etc. - Schedule E		(\$15,676,469)
Total income		(\$4,694,058)
Deductible part of self-employment tax		\$101,699
Adjusted gross income		(\$4,795,757)
Itemized deductions - Schedule A		\$915,171
Taxable income		\$0
Tax		\$0
Alternative minimum tax		\$0
Net tax		\$0
Self-employment tax		\$203,397
Household employment taxes		\$4,164
Other taxes		\$64,412
Total tax		\$271,973
Federal income tax withheld	\$85,649	
2020 estimated tax payments and amount applied from 2019 return	\$13,635,520	
Credit for Federal tax on fuels - Form 4136	\$19,397	
Total payments		\$13,740,566
Amount owed (overpaid)		(\$13,468,593)
Amount refunded		\$5,468,593
Amount applied to 2021 estimated tax		\$8,000,000

⁹⁴ For 2019, six Schedule Cs were included with the Form 1040.

The 2020 Form 1065 filed by DJT Holdings LLC showed the following notable items:

Page 1	
Gross receipts or sales (net of returns and allowances)	\$18,963,271
Cost of goods sold	\$10,924,840
Gross profit	\$8,038,431
Ordinary income (loss) from other partnerships, estates, and trusts	(\$48,520,173)
Other income (loss)	<u>\$17,491</u>
Total income (loss)	(\$40,464,251)
Salaries and wages	\$3,234,660
Repairs and maintenance	\$376,869
Rent	\$1,103,750
Taxes and licenses	\$291,682
Interest	\$1,156,699
Depreciation	\$3,173,787
Employee benefit programs	\$20,835
Other deductions	<u>\$10,122,899</u>
Total deductions	\$19,481,181
Ordinary business income (loss)	(\$59,945,432)
Schedule K (Partners' Distributive Share Items)	
Box 2, Net rental real estate income (loss)	(\$2,464,389)

The 2020 Form 1120-S filed by DJT Holdings Managing Member LLC showed the following notable items:

Page 1	
Gross receipts or sales (net of returns and allowances)	\$8,590,390
Cost of goods sold	\$1,145,682
Gross profit	\$7,444,708
Other income (loss)	(\$426,327)
Total income (loss)	\$7,018,381
Salaries and wages	\$3,602,756
Repairs and maintenance	\$281,399
Rent	\$160,594
Taxes and licenses	\$676,841
Interest	\$3,537
Depreciation	\$1,442,908
Advertising	\$42,506
Employee benefit programs	\$602,114
Other deductions	<u>\$3,855,137</u>
Total deductions	\$10,667,792
Ordinary business income (loss)	(\$3,649,411)
Fuel credit (refunded)	\$1,186

The 2020 Form 1065 filed by DTTM Operations LLC showed the following notable items:

Page 1	2020
Total income (loss)	\$26,726
Salaries and wages	\$22,861
Taxes and licenses	\$50
Other deductions	<u>\$762,365</u>
Total deductions	\$785,276
Ordinary business income (loss)	(\$758,550)

Based on our review of the IRS audit files, it does not appear that any of the 2020 Federal income tax returns have been risked or selected for examination by the IRS.

Our review of the 2020 returns noted above revealed certain issues we thought warranted examination. These are:

1. Unreimbursed partnership/S corporation expenses reported on the 2020 Form 1040.-- With respect to a partner in a partnership, unreimbursed business expenses generally are deductible only if required to be paid by the partner without reimbursement under the terms of the partnership agreement. In the case of an S corporation shareholder, the payment of unreimbursed business expenses is generally considered to be a contribution to capital of the S corporation, or non-deductible if the shareholder is an employee of the S corporation.⁹⁵ For 2020, the total unreimbursed business expenses reported (for all partnerships and S corporations flowing through to the Form 1040) were approximately \$5.4 million. We would suggest examining these amounts, which would include reviewing each applicable partnership agreement.

2. Related party loans.--Interest income on the 2020 Form 1040 was again reported from related party loans made to some of Mr. Trump's children (*i.e.*, Ivanka Trump, Donald Trump Jr., and Eric Trump), in the amount of approximately \$46,000, raising the question of whether the loans were bona fide arm's length transactions, or whether the transfers were disguised gifts that could trigger gift tax and a disallowance of interest deductions by the related borrowers.

3. Validity of sole proprietorship activities.--A number of Schedule Cs either had no gross income (*i.e.*, only expenses), or gross income and expenses that entirely (or almost entirely) offset, raising the question of whether these were valid trade or business activities, or whether these Schedules contained costs derived from personal activities or hobbies.⁹⁶ In 2020, of the six Schedule Cs, three reported expenses equal to the amount of gross income, two reported only expenses (no gross income), and one reported no gross income or expenses. For example, the 2020 Schedule C for Donald J. Trump (management services) reported gross

⁹⁵ For 2020, Mr. Trump does not appear to have been an employee of any of the S corporations in which he was a shareholder because we did not see any 2020 Form W-2s for him from any of such entities. As noted above, unreimbursed job expenses are not deductible as a miscellaneous itemized deduction for 2018 through 2025.

⁹⁶ See secs. 162, 183 and 262.

income of \$87,442 and expenses of \$87,442. Similarly, the 2020 Schedule C for DT Endeavor I LLC (aviation) reported gross income of \$160,144 and expenses of \$160,144. The 2020 Schedule C for DJT Operations I LLC (aviation) reported no gross income and expenses of \$3,239. Audits of closely-held entities often find personal expenditures being improperly deducted as business expenses.

4. Passive versus nonpassive flow-through income and losses.-- It should be determined whether the Schedule E losses from partnerships and S corporations reported on the 2020 Form 1040 were passive or active losses, which could change the amount of ordinary loss allowed for the year.⁹⁷ The more than 400 pass-through entities flowing through to the 2020 Form 1040 reported total passive and nonpassive income of \$65.99 million, and total passive and nonpassive losses allowed (including section 179 expenses) of \$81.75 million, resulting in a net ordinary loss from partnerships and S corporations of \$15.77 million. It should also be determined whether Mr. Trump had sufficient basis in the entities reporting losses and was sufficiently at risk with respect to such entities to be able to claim the losses.⁹⁸

5. General business credits carryover.--The general business credit carryover to 2020 Form 1040 was \$12.7 million, which was made up in part of the rehabilitation credit that was reported in 2016. As noted above, given the stringent requirements for the rehabilitation credit, we think this item should have been audited to see if the rehabilitation credit requirements were satisfied.⁹⁹ Even though Mr. Trump has not been able to fully utilize the credit in intervening years due to taxable income limitations, it continues to be part of his general business credit carryforward, available for use in future years.¹⁰⁰ As noted above, an informal claim was made for 2015 to carry back the 2016 rehabilitation credit. If any part of the claim is allowed, the amount carried forward to 2017 and beyond must be decreased.

6. Rental real estate income (loss) for DJT Holdings LLC.--DJT Holdings LLC 2020 Schedule E (Form 1065) reported a residential rental real estate property (single family home) with no rental income, but total expenses of \$342,182. We would recommend inquiring about the high level of expenses for the residential rental property, as well as whether such property was actually held for rent during 2020. If the property is not used in a rental real estate activity,

⁹⁷ Section 469 restricts the amount of passive activity losses and credits that can be claimed in a tax year.

⁹⁸ A taxpayer cannot deduct a flow-through loss unless the taxpayer has sufficient basis in the partnership or S corporation to absorb the loss. See secs. 704(d) and 1366(d). In addition, the at-risk limitations of section 465 limit the extent to which certain types of income can be offset by deductions or losses. The basis and at-risk limitations are applied before the passive activity limitations of section 469. See Temp. Treas. Reg. sec. 1.469-2T(d)(6)(i).

⁹⁹ See sec. 47.

¹⁰⁰ Unused general business credits may generally be carried back 1 year and carried forward 20 years. See sec. 39.

it raises the question of whether the residence might be held for personal use, and the payment of the expenses would be a distribution (non-deductible) to the partner.¹⁰¹

7. Hotel expense deduction by DJT Holdings LLC.--The 2020 Form 1065 for DJT Holdings includes a deduction for hotel expenses of \$7.2 million (total deductions were \$10.1 million). We would recommend inquiring about the nature and reasonableness of these costs, and whether any of such amount included capitalizable and/or personal expenses.¹⁰²

8. 2020 book-to-tax reconciliation for DJT Holdings Managing Member LLC (Form 1120-S).--The 2020 Schedule M-3 (Net Income (Loss) Reconciliation for S Corporations with Total Assets of \$10 Million or More) reported management fees expense of \$415,905 for book, but \$965,483 for tax (*i.e.*, a book-tax difference of (\$549,578)). We would recommend inquiring about why there is such a large book-tax difference.

9. 2020 Form 1065 for DTTM Operations LLC.--DTTM Operations LLC reported a net ordinary loss of \$758,550 for 2020, which included a deduction for “gift cards redeemed” of \$438,479. Further, the 2020 Schedule L (Balance Sheet per Books) reported a gift card payable liability of \$614,417 as of December 31, 2020, but indicated on page 1 of the return that it used the cash method of accounting. We would recommend inquiring about the amounts reported for gift cards, and whether such amounts are being properly accounted for under the partnership’s method of accounting.¹⁰³

¹⁰¹ See sec. 731. See also, secs. 262 and 280A.

¹⁰² See secs. 162, 262 and 263(a).

¹⁰³ See sec. 451 and Treas. Reg. sec. 1.451-8.

Closing Observations

The IRS audit files we reviewed indicated that the first year of the mandatory examination program began with the 2016 tax year. It is unclear if the 2020 tax year is part of the mandatory examination program since Mr. Trump's 2020 Form 1040 was filed after he left office (*i.e.*, during 2021). Although the 2015 tax year was not part of that program, we did have a few comments regarding the audit of that year based on the returns provided to us. We have set forth above a number of items that we think are worthy of examination, but again express no opinion whether the examination of those items would have resulted in any proposed tax increases for 2015. Regarding the audit workpapers, we must express disagreement with the decision not to engage any specialists when facing returns with a high degree of complexity in so many areas of taxation (such as those at issue). We also fail to understand why the fact that counsel and an accounting firm participated in tax preparation ensures the accuracy of the returns. We would assume this fact would be true of most, if not all, returns of high-net worth individuals, and do not believe such individuals should be subject to limited scope audits on this basis.

As noted above, the IRS audit files noted 2016 as being the first tax year for a mandatory examination of Mr. Trump's returns. Again, we express no opinion whether any of the issues we would have audited (as identified above) would have produced any tax increases. The issues examined by the IRS included related party loans, material participation (*i.e.*, in activities reported as nonpassive losses), tracing of net operating losses, and the review of related entity returns. Charitable contributions were noted as not being examined due to taxable income limitations for 2016. We think that failure to audit donations in the year of contribution may result in an unallowable charitable contribution being deducted in a future year. The IRS audit files again stated that the use of professionals to prepare the returns ensured accuracy. While the IRS delved into more issues in 2016 than in 2015, we are not comfortable with any reliance on professional tax preparation to ensure accuracy, and it does not appear any specialists were called in to assist. As the audit is not complete, we cannot comment on the results of the audit.

For the 2017 and 2018 tax years, we again noted items we thought were worthy of audit, and again express no opinion whether an examination of these items would produce any tax increases. The stated audit scope noted in the IRS audit files for these years is fairly broad in scope as can be seen from the issues noted in the narrative for these years. The IRS audit files show that numerous IDRs were issued and regular meetings between the IRS and Mr. Trump's counsel were held. It appears consistent with the audit strategy that one would expect to see in an audit that is part of the IRS global high wealth audit program. The audit has not yet been completed. Accordingly, we cannot comment on the resolution of any issues.

For the 2019 tax year, the IRS audit files set forth several large and questionable items, but did not otherwise disclose an audit plan that we saw. We did not find any IDRs, and like the prior years, there is no final RAR. We are not certain, but this would suggest a much more limited audit for 2019 than is currently being done for 2017 and 2018. If that is what is planned, it is unclear if that is consistent with the mandatory examination program. Again, we do not suggest that any items we would have audited would have led to any tax increases. We simply cannot be sure absent an actual examination of these items.

For the 2020 tax year, an audit has not yet begun (and it is not clear if 2020 will be part of the mandatory examination program), and we obviously express no opinion on any IRS audit or the result of an audit of any issues we would have examined.