The Tax Times

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September 2013

Wisconsin Society of Enrolled Agents

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www.wienrolledagents.org

President's Message

~Julie Molek, EA~

It hardly seems possible that we are heading for fall already. It is time to gear up for next tax season already. WSEA is bringing you another opportunity for CPE. I, personally, prefer to go to live presentations. I find that many times the material stimulates questions from the audience. It has always amazed me how many times these questions once answered and sometimes debated are issues that come up in my practice the very next tax season. We usually offer two levels of training at our seminars: one is geared for basic tax preparation and the other offers more advanced training. Depending on the content, I enjoy going to both. Our September Seminar offers Mickey Reedy speaking on Representation and Ethics on Thursday, September 19th. On Friday, September 20th, we will offer two choices. Session A will be a course on Schedule B and D taught by Mickey Reedy. For Session B, Pat Handlos and Don Wollersheim will be teaching a course on Entity Selection.

We are looking forward to seeing many of you at our joint conference with Minnesota Society of Enrolled Agents this month in La Crosse. The seminar notice and registration pages are available on our website www.wiwenrolledagents.org under seminars.

Did any of you have difficulty getting your license renewed from the IRS? This seems to be a common malady now that the process has gone online. There is great news for members of NAEA in good standing. One of our membership benefits is that there is someone in the National

President's Message

~Julie Molek, EA~

office who will assist in this matter. From personal experience I found this extremely helpful. Trying to go through the IRS by myself got me nowhere. I left several messages on a machine that promised a response within 48 hours, but never received a call back. NAEA put me in touch with a specific IRS employee who identified the error, told me how to correct it and where and how to send documentations of my CPE for the previous three years! While that was frustrating, it was a great deal better than unanswered telephone messages. Once everything transpired, I was issued my license again. It seems that I used the incorrect form when I applied for relicensing.

One comment I have received in lunch table discussions is that an Enrolled Agent automatically belongs to NATP. NATP and NAEA are mutually exclusive organizations and each has its own dues and benefits. As a matter of fact many Enrolled Agents belong to both reaping the benefits of both organizations. While both are geared toward professional education, the other benefits available are variable.

Welcome New and Renewing Members!

Michael Deininger of Kenosha

Suann Dombrowicki of De Pere

Tim Eiting of Little Chute

Geoff Fieldbinder of Glendale

Ruth Hoyt of Beaver Dam

Terry LaPorte of Superior

Brian Loeck of De Forest

Michael Napier of South Milwaukee

Marybeth Rabideau of Manitowoc

Trina Rahmlow of Oshkosh

Michelle Sparks of Land O Lakes

Eunice Stevens of Wautoma

Joel Wiggers of Cameron

WANTED

Information leading to the hiring of a Qualified Income Tax Practitioner for the 2013 Tax Filing Season in 2014

I am aware of a small Tax Preparation Business in South-Central Wisconsin now preparing about 1,500 tax returns who is looking for a Tax Professional able to prepare between 400 to 500 individual tax returns seasonally.

While an Enrolled Agent would be preferred for this position, a CPA or a RTRP Tax Professional with at least 3 years of prior Income Tax Preparation experience would be considered.

The owner of this business would also be willing to discuss an equity ownership in the business.

For Information and Details, Please Contact:

Dennis C. Alt, EA
Alt Financial Services, Inc.
1101 Joliet Street
Janesville, WI 53546

(608)756-5919 or dennis@alttax.net

Legal Same-Sex Marriages Ruling

On June 26th the Supreme Court invalidated part of the 1996 Defense of Marriage Act, as a result the IRS and Department of the Treasury were forced to rule that same-sex couples, legally married in jurisdictions that recognize their marriages, will be treated as married for federal tax purposes. This gives same-sex couples the rights of all other taxpayers filing Married Filing Joint. Some of these benefits include, the higher standard deduction, exemption amounts, employee benefits, IRA contributions, claiming of EIC and the Child Tax Credit.

This ruling does not apply to civil unions, registered domestic partnerships or other formal relationships that are recognized under state law.

Taxpayers that this ruling applies to are also able to amend any returns still open under the statute of limitations to change their returns to reflect this update.

Please note that taxpayers do not have to reside in a state where same-sex marriage is legal for them to qualify for this change. As long as they were married in a state in which their union is legal they would be permitted to file MFJ.

Wisconsin officially does not recognize same-sex marriages. For WI DOR's response to this ruling see page 7.

EAR & DA Officially Discontinued

As of September 2, 2013, the IRS officially "retired" the Electronic Account Resolution and Disclosure Authorization as services for those of us who use e-services. This is disappointing, but Form 2848 Power of Attorney can still be faxed to the CAF Unit at 801-620-4249. From experience it generally takes the CAF unit 3 business days to process the POA. If you prefer to send it snail mail the address it should be sent to is:

Internal Revenue Service
1973 N. Rulon White Blvd. MS 6737
Ogden, UT 84404

Net Investment Income Tax Form

A draft version of Form 8960 Net Investment Income Tax is now available at http://apps.irs.gov/app/picklist/list/draftTaxForms.html.

If you have the time, take a look at the form and be sure to review the rules for NIIT. Briefly, taxpayers with MAGI above a certain level will have to pay 3.8% tax on their investment income. Investment income includes, but is not limited to: interest, dividends, capital gains, rental and royalty income, non-qualified annuities, income from businesses involved in trading of financial instruments or commodities, and businesses that are passive activities to the taxpayer (within the meaning of IRC section 469). Further information can be found at http://www.irs.gov/uac/Newsroom/Net-Investment-Income-Tax-FAQs

The 2010 Patient Protection and Affordable Care Act and the Health Care Education Reconciliation Act has more changes that will be implemented for 2013 and beyond. The following is meant to be a summary of the changes the tax community should be aware of as employers and tax and accounting service providers.

2013 Provisions

- Employee Contributions to Medical FSAs are limited to the lesser of $2,500 or your companies' maximum.
- An Additional Medicare Tax will be figured on taxpayers with wages and self-employment income above $200,000 (single) and $250,000 (joint). The new form, Form 8959, that will need to be included with taxpayers returns is available as a draft at http://apps.irs.gov/app/picklist/list/draftTaxForms.html
- NIIT (Net Investment Income Tax) will begin with 2013 Income Tax Returns – see information on page 4 regarding NIIT.
- The threshold for the unreimbursed medical expense deduction taken on Schedule A will increase to 10% of AGI for individuals under age 65. It remains at 7.5% of AGI for those taxpayers 65 and older.
- Employers will no longer be allowed a deduction for drug benefits provided to employees eligible for Medicare
- Patient Centered Outcomes Research Institute Fees will be charged on insurance plans that include major medical, dental and vision plans, wellness programs, HSAs, FSAs, HRAs and Employee Assistance Programs
- All employers will be required to notify their employees of the availability of health insurance through the Marketplace at https://www.HealthCare.gov by October 1, 2013.

2014 Provisions

- The Small Business Credit for providing health insurance increases to 50% of the employer's contribution, tax exempt businesses increase to 35% of the employer's contribution. To qualify small businesses must purchase their health insurance through the new Marketplace.
- Individuals will be required to have health insurance for a minimum of 9 months of the year
- Individual penalty for not having health insurance will be the greater of $95 per adult or 1% of your annual income. Individuals with children can add an additional $47.50 onto the penalty, but will not be penalized more than $285.00. Please note that annual income is for the household and based upon anyone within the household that files an income tax return.
- There are exceptions to being assessed this penalty. Some of them include, being uninsured for less than 3 months of the year, having very low income and if you are not required to file an income tax return because your income is too low.

- There will be a Premium Assistance Tax Credit available to those taxpayers that meet the qualifications to help reduce to cost of providing their own health insurance coverage. This tax credit is refundable and can be received in advance. To qualify the taxpayers household income must be between 100% to 400% of the Federal Poverty Level. Additionally, to qualify taxpayers must have purchased their health insurance through the Marketplace.

2015 Provisions

- Employers who have over 50 Full Time Equivalent (FTE) Employees will be required to provide "affordable" health insurance coverage to their FTE staff or pay a penalty.
  - $2,000 penalty per FTE employee (above the first 30 employees) for not offering insurance
  - $3,000 penalty per non-covered FTE employee or per FTE employees who have unaffordable premiums or inadequate coverage and receive the Premium Assistance Tax Credit

There are more provisions that will go into effect in 2018. However, delayed provision implementation for the Affordable Care Act has been a pattern.

For more information on the Affordable Care Act and its provisions go to https://www.HealthCare.gov. For Small Business Owners with questions the Department of Health and Human Services has created a call center – 1-800-706-7893. Additionally, the IRS has developed Pub 5093 which is available at http://apps.irs.gov/app/picklist/list/formsPublications.html;jsessionid=rj3NpDgsOuEVE0lHDCpMzA__?value=5093&criteria=formNumber&submitSearch=Find.

The information provided herein is meant to be a guide, please refer to the resources listed in the article for complete information.

Wisconsin Estate Tax:

Per 2013Wisconsin Act 20 there will continue to be no estate tax for persons who pass in 2013. Officially, there is no estate tax for any deaths occurring in Wisconsin from January 1, 2008 through December 31st, 2013. Please remember this is only valid if there is no change to the federal law which currently provides no federal estate tax credit. Wisconsin estate tax was based upon this credit.

Upcoming Outages

My Tax Account, TeleFile and E-file will be unavailable due to system upgrades on Friday, September 13th, 5:00 pm through Sunday, September 15th, 5:00 pm.

Unemployment News

The approved 2013-15 budget provides $30 million to pay interest due on monies borrowed from the federal government to pay Unemployment Benefits. Thanks to the $30 million set aside in the budget employers will not be required to pay a special assessment this year.

That being said, if the outstanding loan balance in not paid off by November 2014 Wisconsin employers will again be subject to the federal reduction of FUTA tax. The rate for 2014 FUTA would be 1.8% instead of .6%.

For 2013 the FUTA rate for Wisconsin employers will be 1.5%.

Wisconsin Guidance for Individuals in a Same-Sex Marriage

In response to the IRS ruling allowing Same-Sex couples to file joint returns Wisconsin issued the following guidance. The full text is available at http://www.revenue.wi.gov/taxpro/news/130906.html

Wisconsin does not recognize same-sex marriages per Section 71.3(s)(d) Wis. Stats. As a result, if same-sex couples choose to file joint returns for federal purposes, for Wisconsin they must file using filing status Singe, or, if qualified, Head of Household. Additionally, they must include a new Wisconsin form, Schedule S, Allocation of Income to be Reported by Same-Sex Couples Filing a Joint Federal Return. This schedule allocates the income reported on the Federal return to each individual. Marital property law does not apply to this allocation.

Tax year 2012 returns and any late returns from prior years filed after September 16, 2013 must be paper filed.

These rules only apply to 2012 returns filed after September 16, 2013, late returns from prior years filed on or after September 16, 2013 and for all future returns, 2013 and forward.

Schedule S is currently not available, but WIDOR hopes to have it available by the end of September.

Wisconsin Update Seminars

If you are interested in attending WIDOR update seminars please keep the following dates and locations in mind.

October 7, Monday – Madison

October 9, Wednesday – Menasha (Updated)

October 11, Friday – Pewaukee

October 14, Monday – Eau Claire

October 15, Tuesday – Stevens Point

October 25, Friday – Madison

October 28, Monday – Pewaukee

Register by clicking here. Or you can contact WIDOR on the Practitioner Only Line at (608) 261-5199 or by email DORtaxpractitioners@revenue.wi.gov for more information.

Follow-Up on Previous Articles

~ David J. Fayram, EA ~

Penalty Abatements in EA Practice, December 2012

In this article I discussed first-time abatements and mentioned that a problem existed with the program in that people who were delinquent in filing returns and/or delinquent in paying taxes could still have penalties abated. It did not take long for the IRS to correct this problem.

The correction was accomplished by adding a sentence to IRM paragraph 20.1.1.3.6.1 as follows, "Penalty relief under FTA will be limited to those taxpayers that are current with filing and payment requirements." Also, a new requirement was added for a first-time abatement with new paragraph (1)(b) which reads as follows:

> b. Has filed, or filed a valid extension for, all currently required returns and paid, or arranged to pay, any tax due
>
> EXAMPLE: Consider the taxpayer current if they have an open installment agreement and are current with their installment payments
>
> NOTE: If the taxpayer is not currently in compliance per (1)(b) but all other FTA criteria are met, provide the taxpayer an opportunity to fully comply before considering reasonable cause.

I took the language from Advance Release SBSE-20-0413-0690 dated April 5, 2013.

Reimbursements of IRS Administrative Expenses, May 2013

I discovered that we have an expert on reimbursements of litigation expenses in our midst. Douglas H. Frazer, an attorney in Milwaukee, has been reimbursed for his own expenses at Appeals. In another case, he has pursued litigation against the IRS for his litigation expenses. He sent me a copy of his most recent appeal to the Seventh Circuit in Nancy Ellen Kovacs v. United States of America. By my count, there have been one trial and nine appeals stretching over a decade! The original dispute involved only a few thousand dollars in tax, but now the litigation fees are in the hundreds of thousands of dollars.

Douglas has read a lot about the subject over these years. He does not remember a single case involving a CPA or EA contesting administrative expenses. He agrees with my speculation that we have not been aggressive enough in claiming reimbursements. He says that most of the cases involving litigation expenses are pro se and that these are usually lost on procedural grounds. In his experience, the IRS will do everything it can to bully the claimant into submission.

Good luck to Douglas. I hope he will soon have an occasion to uncork the champagne!

Oh, That Income
That's Not My Income
~ Donald Wollersheim, EA ~

We've all seen it, more than once. Your client brings in a 1099-INT and tells you "That's not my income. This is from an investment I am holding in my name for my mother, an account I set aside for my kids, or this belongs to my bowling team." How do we handle joint bank accounts between unrelated parties or joint bank accounts between divorced spouses?

This is an information return that will show up on IRS records. Omitting this on the return may result in the IRS issuing a CP2000. We can't ignore it! The income must be reported on the return bearing the recipients social security or Federal ID number.

What do we do? We report the entire amount of income on our client's Schedule B and on the next line we take a deduction for the same amount labeled as Nominee Interest Distribution. But, we're not done. To document the subtraction we need to issue a 1099-INT to the party actually entitled to the income.

This is an easy example. One that is easy to identify and correct. But, sometimes the "pass through income" is not so conveniently reported and easy to identify. Sometimes, unless we are extremely vigilant, the pass through income is conveniently buried.

A recent case, *Azimzadeh and Ehsan v. Commissioner* T.C. Memo. 2013-169 Docket No. 17924-10, July 23, 2013, brings to light some interesting issues regarding the taxation of income received.

Azimzadeh operated Stevens Creek Auto Center. His friend Mr. Barghi was involved in Stevens Creek and also ran a separate auto business called Luxury for Less. Mr. Azimzadeh reported all of Stevens Creek's income and expenses on his personal return.

When additional taxes and penalties were assessed on audit, Mr. Azimzadeh claimed that Stevens Creek was actually a partnership with Mr. Barghi. The partnership strategy would reduce taxable income and penalties. The IRS argued that this was all his income and the "partnership" issue was a convenience after the fact.

The tax court agreed with the IRS. In concluding that this business relationship was not a partnership, the court looked at eight factors:

1. Their agreement and conduct.
2. The contributions made by each partner.
3. Each individual's control over income and capital, and their right to make withdrawals.
4. Whether they shared interests in profits and losses or whether one party was an agent or employee.
5. Whether the business was operated in their joint names.
6. Whether they filed partnership returns and said they were joint ventures.
7. Whether they kept separate books.
8. Whether they exercised joint control and had joint responsibilities.

There was only one bank account, which could have been a partnership account. Mr. Barghi had equal control of the check book and Mr. Barghi even signed many checks to himself. However, this was not clear evidence as to what Mr. Barghi's position in the business was.

Oh, That Income
That's Not My Income, Continued

It wasn't clear if Mr. Barghi was a supplier or a partner. There was no evidence as to how Mr. Barghi held himself out to third parties. All sales records listed Stevens Creek as the only seller. Neither Mr. Barghi nor Luxury for Less was indicated on the invoicing, even when cars from Luxury for Less were being sold. This was no clear partnership.

The tax court found that no partnership ever existed.

After all, Mr. Azimzadeh had reported all of the transactions on his original return.

When it comes to income and taxes, fingers point to others quickly. This is another example of income being taxed to the recipient of record. Sometimes there is no consideration as to who enjoyed the use of the income.

May 2013 Seminar Pictures

Amy King Session Thursday

Julie Molek, New WSEA President sworn in.

Michelle McBride New WSEA Vice President sworn in

WSEA Board Meeting

Section 530 and an IRS Mandate

~ David J. Fayram, EA ~

The Section 530 referred to in the title is not a part of the Internal Revenue Code.[1] Instead the section was included by Congress in passing the *Revenue Act of 1978* where it remains to this day.[2] Its purpose then as now is to make it more difficult for the IRS to reclassify independent contractors as employees. Over the past thirty-five years or so, the IRS has chipped away at these protections while the Congress has tried to reinforce them. Pro-taxpayer provisions were included in the *Tax Equity and Fiscal Responsibility Act of 1982*,[3] the *Tax Reform Act of 1986*,[4] and the *Small Business Job Protection Act of 1996*.[5]

In what follows, I will discuss some of the history of Section 530 and parts of three court cases which bear on the reporting consistency requirement for Section 530 relief. The emphasis will be on dangers for EAs in representing these taxpayers and on potential recovery of fees from the IRS by these same EAs. I included a number of endnotes so you will be able to trace the authorities in the event this issue actually turns up in your practice.

Mandatory Notification

Those of us who have experienced audits on this issue might be surprised to learn that IRS employees are under both statutory and administrative mandates to inform taxpayers about Section 530 at the beginning of the audit. The statutory basis for this mandate is at Section 1122 of P.L. 104-188, the *Small Business Job Protection Act of 1996*, which added the following to Section 530:

> (e) Special Rules for Application of Section.—
>
> (1) Notice of availability of section.—An officer or employee of the Internal Revenue Service shall, before or at the commencement of any audit inquiry relating to the employment status of one or more individuals who perform services for the taxpayer, provide the taxpayer with a written notice of the provisions of this section.[6]

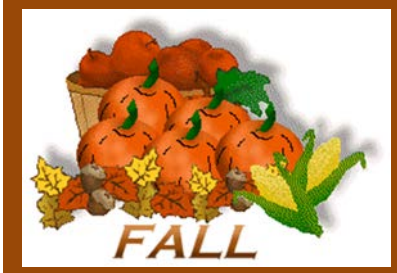
The conference committee report to this act emphasized this provision as follows:

> The conferees wish to clarify the notice that the IRS must provide to taxpayers at … the commencement of an audit inquiry involving worker classification issues.[7]

Both the words “shall” in the statute and “must” in the committee report indicate that this notification is not optional.

The administrative basis for the mandate is in the *Internal Revenue Manual*. Paragraph 4.23.5 is headed, “Technical Guidelines for Employment Tax Issues.”[8] After a short “Overview” section, the Manual proceeds to Section 530 at paragraph 4.23.5.2. The discussion covers about ten pages, but at the very beginning, at paragraph 4.23.5.2.1(1) we have:

> 1.Section 530 is a relief provision that **must** be considered as the **first step** in any case involving worker classification. [bolding in original]



Section 530 and an IRS Mandate, Continued

The fifth paragraph in this section reads as follows:

> 5. Publication 1976, Do You Qualify for Relief under Section 530?, must be provided before initiating any worker classification examination.

Finally, IRS training materials for revenue agents also describe the mandate.[9]

One would think, that, with all this emphasis, every taxpayer who has been audited over independent contractors would be familiar with Section 530. Unfortunately, I do not believe the message is getting through. I do not remember seeing *Publication 1976* in the few audits I have had. Also, I get about a call per year from EAs who are having their first employment audit. These EAs are usually at a loss when I mention Section 530. Section 530 has been around for thirty-five years and the specific mandate has been around for seventeen years. We need to be more careful about this.

Bruecher Foundation Services, Inc.

One William H. Bruecher, who owned Bruecher Foundation Services, Inc., is among those who were not notified about Section 530 by the revenue agent who audited him for employing independent contractors. His case was decided by the Fifth Circuit Court of Appeals on June 18, 2010.[10] There are some interesting issues concerning the Court's designation of the case as, "NOT FOR PUBLICATION," but my concern here is the obligation and mandate that the IRS **must** notify taxpayers about Section 530 and the implications for EAs. Since Mr. Bruecher was the only stockholder of Bruecher Foundation Services, Inc., I will refer to Mr. Bruecher and his corporation interchangeably.

The IRS conceded before trial that it had not provided Mr. Bruecher with the mandatory notice about Section 530. Mr. Bruecher argued that he deserved some remedy for this clear failure to meet a mandatory obligation. His proposals were two: that either the Court issue a verdict in his favor, or that it shift the burden of proof to the IRS. Neither of these got very far in the District Court or in the Fifth Circuit. Section 530 does not provide for any relief for taxpayers who are not informed. Perhaps this is a reason that the message is not getting through.

The Fifth Circuit cited several Supreme Court decisions to the effect that the Courts could not dream up remedies not specified in the statutes.[11] The Court then went on to say, "We do not mean to suggest that there can never be a remedy for the IRS's failure to comply with section 530(e)(1)." It then goes on to offer an example of another taxpayer who also lost on the issue and concludes with, "[Bruecher] was apprised of the IRS's determination as to the non-applicability of the Section 530 safe harbor at the conclusion of the audit, allowing [Bruecher] ample opportunity for administrative relief on those grounds." Apparently the fact that the IRS informed the taxpayer of its determination after the fact corrects its omission of notification at the beginning and justifies its determination without allowing the taxpayer to present any arguments. This is hardly what the Congress, the Conference Committee, and the *Internal Revenue Manual* intended. Oh, well.

Reporting Consistency

In order to gain relief from reclassification of independent contractors under Section 530, taxpayers must show three things: (1) The taxpayer filed information returns in a manner consistent with the worker's status as an independent contractor, ie 1099s (reporting consistency); (2) The taxpayer must have treated all other workers holding substantially similar positions as independent contractors (substantive consistency); and, (3) The taxpayer must have had a reasonable basis for treating the workers as independent contractors.

I will come back to the notification issue, but we need to discuss the 1099s ("reporting consistency"). The difficulty with Section 530 on reporting consistency is that it is silent as to when the 1099s must be filed.[12] The legislative history does mention the 1099s, but falls just short of saying the returns must be timely:

> The taxpayer shall be deemed to have acted in good faith only if all federal tax returns (including information returns) required to be filed by the taxpayer were filed on a basis consistent with the taxpayer's treatment of such individuals as independent contractors …[13]

What happens if a taxpayer is audited on the independent contractor issue; is properly informed by the IRS about Section 530; and immediately files all the required 1099s including delinquent forms? Does this taxpayer meet the reporting consistency prong of Section 530? If so, this might be another reason why the IRS is reluctant to inform taxpayers about Section 530.

Of course the IRS position is that these delinquent 1099s are not fair play. Several pronouncements make its position absolutely clear. Revenue Ruling 81-224 states that the 1099s must be filed timely in order to count. It imposed the same requirement in Revenue Procedure 85-18. Also in the 1980s, it issued a bunch of Technical Advice Memoranda with the same claim.[14] Finally, the IRM makes timely filing an absolute requirement for Section 530 relief. [15]

Medical Emergency Care Associates, S.C.

It happens that there is a Tax Court case with exactly these facts.[16] Medical Emergency Care Associates, SC hired people to provide emergency medical care services to hospitals in Chicago and treated them as independent contractors. The IRS audited the corporation and determined that it was qualified for Section 530 relief — except for the fact that the 1099s were not filed on time. That is, it had both substantive consistency and reasonable cause, but, according to the IRS, not reporting consistency. There are many great quotes in the decision. Here are a couple:

> Congress enacted Section 530 to "alleviate what it perceived as the 'overly zealous pursuit and assessment of taxes'" against employers who had, in

Section 530 and an IRS Mandate, Continued

> good faith, classified their workers as independent contractors.
>
> The plain language of section 530(a)(1)(B) denies relief only if the required filing was not made or if the required filing was made on a basis not consistent with treatment of the individual as not being an employee. As respondent [Commissioner] acknowledges, petitioner filed all required returns for 1996 on a basis consistent with the treatment of the reclassified physicians as not being employees. But there is nothing in the language of section 530(a)(1)(B) that requires timeliness along with consistent filing.

The Commissioner brought up all the pronouncements listed above and argued that the Court must accord them deference. The Court was not impressed with this argument:

> Rev. Proc. 85-18, however, provides no reason why it requires timely filing. Thus, we are unable to ascertain the thoroughness of the agency's consideration or the validity of its reasoning. Consequently, we do not defer to its requirement of timely filing as a prerequisite to Section 530 relief in this case.

Mr. Sheppard (see footnote 1 below) says that Mr. Bruecher did not raise Medical Emergency Care Associates at all in any of his pleadings. It was a "regular" decision of the Tax Court and therefore the Tax Court regarded it as precedential. It would not have been binding on the District Court or the Fifth Circuit where Bruecher was tried, but its arguments might have been persuasive. Mr. Sheppard thinks the failure to cite Medical Emergency Care Associates in Bruecher was a terrible blunder.

In order to refine the arguments, we must look at exactly when Medical Emergency filed its 1099s for the year 1996:

January 31, 1997	Due date for 1099s
January 21, 1997 to March 5, 1997	1099s mailed to service providers
February 28, 1997	Due date for 1096
May 20, 1997	1096 mailed to IRS (but IRS had no record of receipt)
December 22, 1998	1096 and 1099s flied for the second time
December 1998	IRS audit began
January 8, 1999	IRS issued letter saying the Section 530 relief was not available
May 14, 1999	IRS first provided Publication 1976 notifying taxpayer about Section 530

The most conservative reading of these dates is that taxpayers have reporting consistency if they file 1099s and 1096s before the IRS begins a worker-classification audit. The most liberal reading is that taxpayers have reporting consistency if they file the forms before the IRS concludes a worker-classification audit.

Section 530 and an IRS Mandate, Continued

***Bruecher* and Reporting Consistency**

What about Mr. Bruecher? Here is an abbreviated time line of what happened to him:

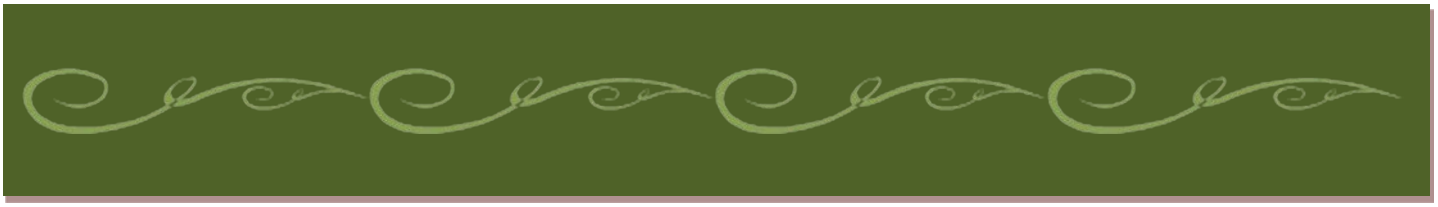
2002	IRS conducted a "general audit" of the corporation, but did not inform it of an employment audit
July 2, 2003	IRS sent a letter finding 16 workers from 2000 and 13 workers from 1999 were employees
December 2004	IRS Appeals issued a Notice of Determination allowing 90 days to appeal to Tax Court
June 6, 2005	IRS assessed taxes for 1999 and 2000
June 6, 2005	Bruecher paid some of the tax and filed a claim for refund
October 8, 2005	IRS denied the claim for refund
December 13, 2005	IRS levied against bank accounts
May 17, 2006	Bruecher filed 1096 and 1099s for 1999 and 2000
May 19, 2006	Bruecher filed a lawsuit in Federal District Court seeking a refund of taxes paid

We don't have a very sympathetic taxpayer here. The 1096 for 1999 would have been due around February 28, 2000, but was not filed until May 17, 2006. Not only was it filed after the audit began and after the audit concluded, but after the taxes were assessed. One wonders who represented the corporation during these six years. The result is bad for taxpayers seeking relief under Section 530 because the IRS now has a case supporting its position that the 1096 must be filed on time in order to support reporting consistency.

But there is a finer point to be made here about when the 1099s must be filed. The Fifth Circuit eloquently summarizes both sides of the argument as follows:

> At the outer boundaries of its argument, the United States would have us hold that a taxpayer's untimely filing of relevant informational returns *always* deprives that taxpayer of Section 530 relief, no matter how minimal the lateness of the filing. By contrast, BFS [Mr. Bruecher] argues that these administrative precedents are not entitled to deference and points us to other aspects of the legislative history and what it terms the plain language of the statute. BFS would have us hold that a taxpayer's untimely filing of the required returns *never* deprives the taxpayer of Section 530 relief, so long as the returns are at some point, filed. Both parties thus ultimately ask us to address the fundamental question of whether or not the Section 530 safe harbor implicitly requires that Form 1099s be timely filed.

After reading this paragraph, the expectant reader will be disappointed when the Court, "decline[s] to address the [fundamental] question of whether Section 530 requires the timely filing of the relevant Form 1099s." It found against Mr. Bruecher because he filed the 1099s after the government had completed the audit and assessed the tax. Even though the case was decided in favor of the government, we do not have a complete victory for the government. *Bruecher* can be read for the position that the 1099s must be filed before the IRS assesses the tax and no more. The Court explicitly declined to find that timely filing is required.



Section 530 and an IRS Mandate, Continued

Consequences for EA Practice

Let's start with a taxpayer who is representing themselves and who is not familiar with Section 530. Such a taxpayer could be substantially disadvantaged if the IRS does not notify them about Section 530 at the beginning of the audit because failure to file the 1099s immediately might cost them protection under Section 530. If the 1099s are not filed until after the assessment, according to the Fifth Circuit, it is too late. In addition, the taxpayer might be harmed by failing to present arguments on the other two prongs of section 530 (substantive consistency and reasonable cause).

What if the above taxpayer is represented by an EA? The crucial fact is the point at which the EA becomes involved. If it is at the beginning of the audit, then the failure of the IRS to provide notification should not damage the taxpayer at all. The reason is that the taxpayer should expect the EA, and not the IRS, to inform him or her about Section 530 and to be aggressive about arguing that the taxpayer should qualify for relief. Representation is what the taxpayer is paying the EA for. If the EA fails to make the arguments on behalf of the taxpayer, then the problem is with the EA!

What if the EA does not become involved until after the audit is over? Among the first things to be determined in this situation is if the IRS provided notice because one of the arguments going forward at Appeals is the extent of damages suffered by the taxpayer if the IRS did not provide the notice. One might start by asking the taxpayer about the notice, but it is a rare taxpayer who kept all the notices from the IRS, much less all the enclosures. If the revenue agent is still available, the EA should ask the revenue agent. Also, a transcript of the account might list the notification mailing. An Appeals Officer has authority to release the administrative file to the taxpayer and should be requested to do so. If none of this works, then a Freedom of Information Act request might be necessary.

Another kind of damage inflicted by failure to notify has to do with recoupment of administrative costs from the IRS. Among the hurdles to recovery is that the taxpayers must exhaust administrative remedies.[17] Taxpayers must have presented all of the relevant information under their control to the appropriate IRS personnel. A naive taxpayer (or a poorly represented one) might not know enough to do this without notification about Section 530 by the IRS. There is a case where attorney David P. Leeper recovered $16,087.50 in fees for representing a dance studio after the IRS maintained unreasonable positions with regard to Section 530 relief. Administrative representation expenses, in the amount of $1,650.00 were not allowed, but the reason for this is not clear because they were incurred after the equivalent of a 30-day letter was issued.[18]

As EAs, it is unlikely that we will be recovering litigation expenses because a lawyer will be representing the taxpayer in court. For that reason we are most interested, not in the $16,087.50, but rather the $1,650.00 which was not allowed. I tried to unravel what happened to this amount. Here is a time line:

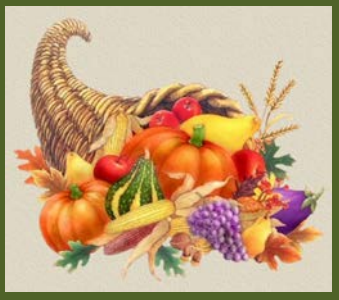
October 2, 2002	IRS issued 30-day letter
October 8, 2002	"Conference with new client-2.25 hours" (not allowed)
October 9, 2002	"Lengthy analysis of Federal tax laws per 3121, relief under Act 530, CSP , program relief, procedural circumstances-7.75 hours" (not allowed)

Section 530 and an IRS Mandate, Continued

October 16, 2002	"Draft of request for Appeals Office conference-.5 hours" (not allowed)
October 16, 2002	Protest mailed to revenue agent who refused to send it on to Appeals
October 24, 2002	"Draft of [second] request for Appeals Office conference-.25 hours" (not allowed)
October 29, 2002	"Draft of [second] request for Appeals Office conference-.25 hours" (not allowed)
February 20, 2003	Notice of Determination issued by IRS
February 28 to March 28	"Review and analysis of IRS Notice of Determination of Worker Reclassification, several conferences with client and her workers. Research of Federal tax laws and numerous cases-13.25 hours" (allowed)

Here is what the Judge offered in explanation of the disallowances:

> It appears the October 2002 fees were not in connection with the Court proceeding. However, petitioner's counsel's review of the notice of determination was in connection with this proceeding since petitioner had to draft its petition in response to the conclusions contained therein. See sec. 301.7430-4(c)(3)(i), (4), *Example* (1), Proced. & Admin. Regs.



Since this does not agree with my understanding of the statutes, I looked up his citation. Indeed, it contains the following:

> A's costs incurred in connection with the preparation and filing of a petition with the Tax Court are litigation costs and not reasonable administrative costs. Furthermore, A's costs incurred before the administrative proceeding date (date of the notice of deficiency as set forth in §301.7430-3(c)(3)), are not reasonable administrative costs.

My source for this material[19] has a prominent note in bold type as follows: "**Reg. §301-7430-4 does not reflect recent law changes.**" As it turns out, changes to these regulations were issued in proposed form on November 25, 2009 and are still outstanding! The example was changed to read as follows:

> A's costs incurred before the date of the mailing of the 30-day letter are not reasonable administrative costs because they were incurred before the administrative proceeding date. Similarly, A's costs incurred in connection with the preparation and filing of a petition with the Tax Court are litigation costs and not reasonable administrative costs.[20]

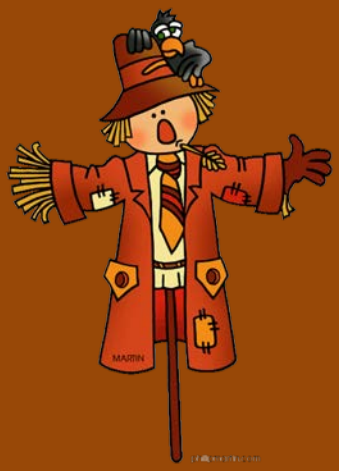
Thus, the disallowed costs were administrative costs and not litigation costs, but should have been reimbursed either way. In this specific case, EAs might have been able to recover fees after October 2, 2002 and before February 20, 2003. In addition, the lawyer might agree to allow an EA to make an appearance at Appeals, but these would be litigation expenses.

In summary, EAs might be able to recover administrative fees if the revenue agent did not notify the taxpayer about Section 530, did not consider taxpayer arguments, and took an unreasonable position in the 30-day letter.

One final thing on consequences of Section 530 for tax return preparers. What about the "employees"? That is, what if a business treated someone as an independent contractor. The IRS then audited the business and found that the independent contractor was an employee and also found that the business was protected by Section 530. How should one do the "employee's" return?

The income shown on Form 1099-MISC for this taxpayer should *not* be entered on Schedule C, Schedule SE, or as miscellaneous income on the 1040. The income can't support a self-employed retirement contribution for instance, or business expense deductions on Schedule C. The amount should be reported on the "Wages" line of Form 1040. It will be subject only to the "employee's" share of payroll taxes. Any deductions will go on Schedule A.

The IRS even has a form for this: Form 8919, "Uncollected Social Security and Medicare Tax on Wages." The instructions to Form 4137, "Social Security and Medicare Tax on Unreported Tip Income" say explicitly not to use Form 4137 if the 1099 results from Section 530 relief. Good luck!



Footnotes

[1] Hale E. Sheppard, *Must Taxpayers File "Timely" Form 1099 to Obtain Section 530 Relief? Unexpected Answers from a Recent Worker-Classification Case*, Journal of Tax Practice & Procedure, 15, 2, April-May 2013, at 39.

[2] Act § 530 of the *Revenue Act of 1978* P.L. 95-600, (1978).

[3] *Tax Equity and Fiscal Responsibility Act of 1982*, P.L. 97-248, (1982).

[4] *Tax Reform Act of 1986*, P.L. 99-514, (1986).

[5] *Small Business Job Protection Act of 1996*, P.L. 104-188, (1996).

[6] Act § 1122 of P.L. 104-188.

[7] H. Conf. R. 104-737, 104th Cong., 2d Sess., 204 (1996).

[8] If you come across an audit about these issues, then this part of the IRM is among the first things to read!

[9] IRS, *Independent Contractor or Employee? Training Materials*, Training 3320-102 (1996), at 1-5.

[10] *Bruecher Foundation Services, Inc. v. United States*, CA-5, 2010-1 USTC ¶ 50,476 (June 18, 2010), 383 FedAppx 381 (2010).

[11] For example, *United States v. James Daniel Good Real Prop.*, 510 U.S. 43, 63 (1993). "…[I]f a statute does not specify a consequence for [the government's] noncompliance with statutory timing provisions, the federal courts will not in the ordinary course impose their own coercive sanction."

[12] § 530(a)(1) reads as follows: "If for purposes of employment taxes, the [company] did not treat an individual as an employee for any period, and … all Federal tax returns (including information returns) required to be filed by the [company] with respect to such individual for such period are filed on a basis consistent with the [company's] treatment of such individual

as not being an employee, then, for purposes of applying such taxes for such period with respect to the [company], the individual shall be deemed not to be an employee unless the [company] has no reasonable basis for not treating such individual as an employee."

[13] S. Rep. 95-1263, 95th Cong., 2nd Sess. (1978).

[14] See TAM 8251012 (Sept. 7, 1982), TAM 8302008 (Sept. 28, 1982), TAM 8322005 (Feb. 21, 1983), TAM 8403002 (Sept. 9, 1983), TAM 8424005 (Feb. 24, 1984), and TAM 8703002 (Aug. 27, 1985).

[15] IRM ¶ 4.23.5.2.2.1(A) (Nov. 3, 2009).

[16] *Medical Emergency Care Associates, S.C., an Illinois Corporation v. Commissioner*, 120 TC No. 436, 120 TC No. 15 (May 19, 2003), CCH Dec. 55,154. The case was not published by CCH as a US Tax Case and therefore does not have a CCH case number.

[17] IRS § 7430(c)(4)(A), 2013(17), *Stand. Fed. Tax Rep.* (CCH), ¶ 41,740 (2012).

[18] *Images in Motion of El Paso, Inc. v. Commissioner*, 91 TCM 716 (2006), TC Memo. 2006-19, CCH Dec. 56,425(M).

[19] Reg. § 301.7430-4(c)(4), *Example 1*, 2013(15), *Stand. Fed. Tax Rep*. (CCH), ¶ 41,742D (2012).

[20] Prop. Reg. §301-7430-4(c)(4), *Example 1*, 2013(15). *Stand. Fed. Tax Rep*. (CCH), ¶ 41,742DC (2012).

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