

**INFORMATION REPORTING PROGRAM  
ADVISORY COMMITTEE**

**EMPLOYER INFORMATION REPORTING  
AND BURDEN REDUCTION  
SUBGROUP REPORT**

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## A. Electronic Transmittal of Employer Withheld IRS Tax Levy Proceeds

### Recommendations

IRPAC recommends that IRS provide an efficient method for employers to transmit employer withheld IRS tax levy proceeds electronically to the U.S. Treasury. The Electronic Federal Tax Payment System (EFTPS) is required to be utilized by employers to transmit federal payroll and corporate taxes to the U.S. Treasury. IRPAC's recommendation is to use EFTPS or a similar format to allow employers to transmit the withheld levy proceeds.

### Discussion

The current procedure, as instructed by Form 668-W (c) (DO), Notice of Levy on Wages, Salary, and Other Income, is to mail a physical check to the U.S. Treasury on the employee's payday. On the face of the check the employer is to record: the taxpayer's name, taxpayer's SSN, tax type and the words "proceeds of levy". This creates several issues for employers:

One issue that many employers face is that the payroll department must submit a check request to the accounts payable department for the amount withheld from the employee. For large employers with multiple employees with IRS tax levies, the employer either has to issue multiple checks to the U.S. Treasury or combine multiple employee withholdings into one check and include a listing of the taxpayer name and TIN. This is confidential information that should not be available in the accounts payable department. Many payroll departments receive the payroll check deduction amount information only a day or two before the employee's actual pay date. This does not give the employer enough time to get the accounts payable check(s) cut and mailed to Treasury by the employee's pay date. Many employers do not process accounts payable checks every day, some are on a weekly, biweekly or semimonthly accounts payable processing cycle, which may or may not coincide with the employee pay date. This means that technically the payments are not being made timely to the Treasury. In many companies once a check request has been submitted to the accounts payable department, it is processed and mailed by the accounts payable department which means that the payroll department does not have any way to know what has been recorded "on the face of the check", or any opportunity to get the required information onto the face of the check or to include a listing of the taxpayer names and TINs.

An additional issue is that most accounts payable systems do not have the capability to print the required information "on the face of the check" and therefore many checks are forwarded to Treasury with the taxpayer information printed on the check stub. Many times this becomes separated from the check before processing and applying the payment to the taxpayer account. If an employer is combining multiple taxpayer withholdings, the taxpayer information will be recorded on a separate attachment which also becomes separated from the check before processing. This leads to additional reconciliation work on the part of IRS to identify and apply levy

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proceeds correctly. There are times when Treasury will apply the amount to the employer's payroll tax account which results in an overpayment on the employer side and no credit to the actual taxpayer(s) who had the payroll deduction. This also leads to taxpayers being subjected to the levy deductions continuing longer than necessary and or penalties to the employer for not paying the funds to the correct accounts.

Another issue caused by submitting the proceeds via a physical check is that the Form 668-W directs the employer where to send the proceeds of the levy; many times the employer is required to send the payments to local IRS offices. With IRS offices closing, this leads to employers getting calls from IRS directing the employer to send the payments to another office. In some cases IRS will talk to whomever answers the phone so taxpayer confidentiality then becomes an issue. In other cases the employer does not receive a timely notice that an office has closed leading to payments not being properly credited to the taxpayer(s) accounts.

The IRPAC recommendation to provide an electronic payment method will ensure that withheld levy proceeds are efficiently, timely and correctly credited to the proper taxpayer(s) account. An electronic payment method will reduce processing time at IRS and Treasury and could significantly reduce the continuous burdensome communications and reconciliations necessary between the employer, the taxpayer, the IRS and the U.S. Treasury. An additional benefit of electronic transmission will be increased revenue because the proceeds will be deposited in the Treasury much sooner than the current process of handling physical checks.

## **B. Pensions and IRA Complications**

### **1. Withholding and reporting for pension payments to NRAs**

#### **Recommendation**

IRPAC recommends that the IRS clarify the withholding and information reporting requirements for certain pension plan distribution scenarios to nonresident aliens (NRAs). IRPAC believes it is important to focus on distributions including net unrealized appreciation (NUA) of employer securities, loan offsets, defaulted or deemed plan loans, and direct rollover payments to IRAs.

#### **Discussion**

IRPAC believes there are gaps in the withholding and information reporting guidance available to U.S. pension payors and IRA trustees when they must process and report certain common types of qualified plan payments to presumed or documented NRA plan participants. These gaps leave payors unsure if and when withholding under IRC § 1441 applies and how to accurately and clearly report amounts distributed or deemed to be distributed under IRC § 1461. As a result, IRPAC believes that the IRS is not receiving accurate and

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complete information and could be losing revenue. There is no such concern for U.S. payees, as Form 1099-R, Distributions From Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc., provides dedicated boxes and distribution codes to seamlessly report these transactions and the Chapter 61 withholding rules are covered clearly in the code and regulations.

Below are some common scenarios faced by payors and a sampling of the questions that IRPAC believes remain unclear:

- a. NRA plan participant requests an in-kind distribution of his/her employer securities that is eligible for net unrealized appreciation treatment.
  - o What portion of the in-kind distribution is subject to withholding under IRC § 1441? (all or just the cost basis)
  - o Are payors required to sell shares of the employer security to generate cash for withholding?
  - o What portion of the in-kind distribution is subject to reporting under IRC § 1461? (all or just the cost basis)
  
- b. NRA plan participant has a deemed loan transaction processed on his/her account. Generally, a deemed loan occurs when a plan participant defaults on a prior loan taken from his or her account balance (e.g., missed payments, loan amount exceeded statutory limit). In most cases, no cash is distributed during this transaction, but under IRC 72(p), the deemed loan is treated as a taxable distribution.
  - o What if any withholding obligation does a payor have under IRC § 1441?
  - o If there is a withholding obligation, how does the IRS view the payor's responsibility to aggregate any future cash payments with the deemed loan for the purpose of calculating withholding on that future distribution? While IRC § 1.1441-2(d) seems to require the aggregation with a future cash payment if that payment occurs prior to the filing of Form 1042, Annual Withholding Tax Return for U.S. Source Income of Foreign Persons, (including extensions), it does not provide a clear procedure when the future payment crosses tax years. Guidance is needed with respect to both Forms 1042 and 1042-S, Foreign Person's U.S. Source Income Subject to Withholding, reporting if these payments cross tax years.
  - o What if the future distribution is a direct rollover? Direct rollovers are not subject to federal income tax. Would a payor be required to aggregate the deemed loan with the direct rollover request to determine withholding on the prior deemed loan and withhold that amount against the direct rollover? How would the withholding be reported, since the withholding now becomes a taxable distribution from the plan?

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- c. NRA plan participant completes a direct rollover from a pension plan to an IRA.
  - o Is this a reportable transaction if paid to a presumed or documented NRA? Some payors may argue that since a direct rollover is an item of income that is excluded under a provision of the law without regard to the U.S or foreign status of the owner of the income, it is not FDAP income and thus, is not reportable.
  - o Other payors would argue that it is reportable since Treas. Reg. IRC §1.1461-1(c)(2) requires pension distributions, in general, be reported on Form 1042-S. What does the IRS view as the correct information return, if any? Many payors use Form 1099-R instead of Form 1042-S because Form 1042-S does not provide a mechanism to report the transaction as a direct nontaxable rollover to another tax deferred account. This could also apply to direct rollover payments from IRAs to qualified pension plans.

### 2. Reporting for IRA Assets Escheated to State Governments

#### Recommendation

IRPAC recommends that the IRS add a new Distribution Code to Box 7 on Form 1099-R to clarify that IRA assets escheated to state governments are IRA distributions includable in gross income and subject to information reporting.

#### Discussion

IRPAC has a concern that IRA trustees do not have sufficient guidance to properly withhold taxes and/or report IRA assets escheated to state governments. Through discussions with a sample of IRA trustees, IRPAC has learned that withholding and reporting procedures vary from no withholding and no Form 1099-R reporting to applying the 10% default withholding and reporting as a distribution on Form 1099-R. State governments that receive escheated IRA assets have indicated that they do not generate a Form 1099-R at the later date when the IRA assets are reunited with the IRA owner or beneficiary. This opens the potential for large amounts of IRA assets to be distributed from IRAs, yet never be reported as distributions to the IRS through the information reporting process.

IRPAC believes that the IRA assets escheated to state governments are distributions includable in gross income, as defined in IRC § 408(d)(1) and IRC § 1.408-4(a)(1), and that these distributions should be reported on Form 1099-R as required under IRC § 6047. To help alleviate the confusion that exists among IRA trustees and payors, IRPAC recommends that the IRS create a new Form 1099-R distribution code for Box 7, titled "IRA Assets Escheated to State". The requirement to report these transactions on Form 1099-R should also signal to IRA trustees that the 10% default withholding applies.

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Other important related issues that would be addressed through the implementation of this recommendation are:

- a. IRA owners would not face the 50% missed RMD excise tax found in IRC § 4974 that is levied on assets not distributed once the IRA owner attains age 70 ½.
- b. The default 10% withholding would help offset tax due by the IRA owner.
- c. IRS matching of underreported amounts and the resulting deficiency notice could alert the IRA owner about the escheated IRA assets and hasten their recovery of the money from the state.

### C. Publication 1586 Revision

#### Recommendations:

1. The next update to Publication 1586, Reasonable Cause Regulations and Requirements for Missing and Incorrect Name/TINs (including instructions for reading CD/DVDs and Magnetic Media) should include a reference in the “What’s New” section mentioning Form 1094-C, Transmittal of Employer-Provided Health Insurance Offer and Coverage Information Returns, Form 1095-B, Health Insurance Coverage and Form 1095-C, Employer-Provided Health Coverage
2. Publication 1586 should correctly reflect the requirements of annual solicitations made by mail.
3. Publication 1586 should include published guidance that provides taxpayer information on what/how reasonable cause can be established and obtain penalty relief.
4. Publication 1586 could be improved by clarifying the requirements for annual solicitations made by mail for information required to be reported on Form 1099-R and Form 5498, IRA Contribution Information .

#### Discussion:

1. Publication 1586 discusses issues related to information returns that contain errors including possible penalties and how taxpayers can establish reasonable cause for specific types of errors. Public Law 111-148 added IRC §§ 6055 and 6056 to the definition of information returns and IRS has created Forms 1095-B and Form 1095-C to meet the requirement of the statute. Publication 1586 was last updated in June 2012. The next update of the publication should include references to Form 1094-C, Form 1095-B and Form 1095-C in the “What’s New” section.
2. Errors made on information returns provided to IRS and to recipients are subjected to penalties imposed under §§ 6721 and 6722. IRC § 6724 provides

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that no penalties may be imposed if any failure is due to reasonable cause and not willful neglect. Rules for being able to demonstrate reasonable cause require acting in a responsible manner with respect to missing TINs and incorrect name/TIN combinations. Critical to the process of securing correct name and TIN information is the required process of requesting the information. The process of requesting correct names and TINs is termed solicitation. TIN solicitation rules for acting in a responsible manner are described in Treas. Reg. IRC § 301.6724-1(d) and the rules for missing TINs are described in Treas. Reg. § 301.6724-(1)(e). The manner of making solicitations includes a requirement that payees must be informed that they may be subject to a \$50 penalty imposed by the Internal Revenue Service per incorrect document.

Page 4 of Publication 1586 currently states that annual solicitations by mail must include a letter stating that the payee must provide an accurate TIN and that failure to do so may result in a \$50 penalty (\$100 for returns due on or after January 1, 2011) per incorrect document. IRC § 6723 sets forth the \$50 penalty, but was *not* amended to increase the penalty to \$100 for returns due on or after January 1, 2011. This error in Publication 1586 (i.e., stating that the penalty was increased to \$100 for returns due on or after 1/1//2011) is causing confusion relating to the process required to be able to demonstrate that a taxpayer has acted in a responsible manner.

IRPAC recommends that Publication 1586 be corrected to remove the parenthetical reference to a \$100 penalty for returns due on or after January 1, 2011.

3. The guidance on establishing “reasonable cause” and obtaining relief from penalties is set forth in the Internal Revenue Manual. These are crucial in the context of ACA related penalties as the ACA is one of the largest and most comprehensive pieces of legislation ever enacted by the Congress in the history of the country. IRPAC therefore recommends that the following sections be included in the Publication 1586 update:

IRM 20.1.1.3.2 states that reasonable cause is based on all the facts and circumstances in each situation and allows the IRS to provide relief from a penalty that would otherwise be assessed. Reasonable cause relief is generally granted when the taxpayer exercised ordinary business care and prudence in determining his or her tax obligations but nevertheless failed to comply with those obligations.

IRM 20.1.1.3.2.2 states that “ordinary business care and prudence” includes making provisions for business obligations to be met when reasonably foreseeable events occur. A taxpayer may establish reasonable cause by providing facts and circumstances showing that he or she exercised ordinary business care and prudence, (taking that degree of care that a reasonably

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prudent person would exercise), but nevertheless was unable to comply with the law.

IRPAC also recommends that the prior information reporting history of taxpayers be taken into account and be given greater weight in adjudicating requests for relief based on “reasonable cause”, as there is currently no ACA related reporting history.

4. Publication 1586 which discusses annual solicitations by mail could be improved by clarification of the requirements of annual solicitation by mail for purposes of information reported on Form 1099-R and Form 5498.

Page 4 of Publication 1586 states that “If the annual solicitation is for a missing or incorrect name/TIN required to be reported on Form 1099-R, then the Form W-4P, Withholding Certificate for Pension or Annuity Payment *may be included.*” (Emphasis added.)

If the individual taxpayer is sent a W-4P, a letter and a return envelope, do those three items together satisfy the annual solicitation requirement to support acting in a responsible manner according to Treas. Reg. IRC § 301.6724-1(f)?

A literal reading of page 4 is that annual solicitations must include three items: the required letter, Form W-9, Request for Taxpayer Identification Number and Certification and a return envelope; but for 1099-R purposes Form W-4P “may be included.” The items required for an annual solicitation for 1099-R purposes need to be clearly stated. The current wording “may be included” is not helpful because it could be interpreted two different ways: (1) include W-4P and do not send W-9, or (2) send W-9 but you have the option of also including W-4P.

IRPAC recommends that the ambiguity around the phrase “may be included” be removed from Publication 1586.

### **D. Theft of Business Taxpayer’s Identity**

The IRS has made an effort to track individual ID theft but has generally not taken into account how serious and sophisticated business identity theft is for the average business owner. Online ID theft and fraud have become common. With the increase in data breaches reported to date it is anticipated that more businesses could face financial hardship or ruin which will decrease further revenues which might otherwise have been due to Treasury. A more rigorous process to release personal data or refunds would help deter criminals from stealing personal information. In addition, this process would assist in protecting more taxpayers’ privacy rights. Revisiting and

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revising previously suggested safeguards and implementing new recommendations will help broaden efforts that prevent security infiltration.

IRPAC recognizes the Commissioner's willingness to reassess the IRS policies and assist those affected by tax related identity theft in 2015, such as agreeing with Senator Ayotte, to provide victims redacted copies of fraudulent tax returns filed on their behalf. IRPAC anticipates that the Commissioner will consider the IRPAC comments expressed herein in anticipation of fighting business identity theft.

## 1. Recommendation for Identity Theft Deterrence

- a. IRPAC recommends truncation of the issuer's Employer Identification Number (EIN) be permitted on payee information return statements as a means of preventing business identity theft. Although information provided in these forms by businesses is already available to the general public on other forms (e.g. W-2s), it is recommended, if possible, to limit additional EINs from being circulated. Even though EINs are already being mailed and e-mailed, truncation would reduce the opportunity for these numbers to be obtained by unnecessary third parties in the future.
- b. Form 1042-S instructions should clarify that the recipient's taxpayer identification number may be truncated on all 1042-S forms (not just when there is a reporting of bank deposit interest paid to certain nonresident aliens), to reduce opportunities for identity theft and tax fraud. It should be noted that this action is currently permitted by Rev. Proc. 2015-35 but has yet to be included in the form instructions.

## Discussion

Truncating EINs will help keep sensitive information from data mining thieves that could put businesses at greater risk for identity theft. Damage caused to small businesses by identity theft can be detrimental and can prevent them from obtaining credit or from expansion thus adding to the unemployment of today's workforces. IRPAC recommends truncating the issuer's EIN on recipient copies of information returns because truncation will allow companies that issue 1099s and other information returns to have less exposure to false information returns being filed using their EIN and legal name. Taking this precaution will diminish the chances of these businesses becoming victims of identity theft.

The new Forms 1095-B and 1095-C show the legal name and EIN of not only the issuer (the insurance company) but also the business that employs the insured individual, exposing more businesses to identity theft when that information is made accessible for a criminal to steal and fraudulently use to endanger the survival of an otherwise healthy business. IRPAC recommends truncation of the employer's EIN be permitted on Forms 1095-B and 1095-C.

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## 2. Recommendation for Business Master File and Form 8822-B

- a. IRPAC recommends IRS revise Revenue Procedure 2010-16 to state that an address change related to an EIN will only occur after receipt of IRS Form 8822-B (“Change of Address – Business”). Procedures should be implemented in all service centers to ensure the address for a large business is not updated when a tax return is filed that is not normally filed by the large business. Returns such as Form 1041, U.S. Income Tax Return for Estates and Trusts and 990-T, Exempt Organization Business Income Tax Return, should be rejected and sent back to the taxpayer that erroneously or fraudulently filed the return and is unconnected with the large business.
- b. IRPAC recommends revisiting the discussion of the process of issuing a change of address notification letter (CPs 148A and 148B) mailed to the last address and the new address when a mailing address on the Business Master File (BMF) is updated based on the requirements in Revenue Procedure 2010-16.
- c. IRPAC’s 2014 Public Report recommended that the prior representative’s name and TIN lines be eliminated from the Form 8822-B. We would like to thank the IRS for acting on this recommendation.

### Discussion

Over the last year several large businesses have experienced business and customer privacy breaches because the large business address has been updated in the BMF in error. Tax returns not normally filed by the large business such as Form 1041 and 990-T are being filed by taxpayers unconnected with the large business. The tax return contains the TIN of the large business but the business name on the filing is often not the large business taxpayer name. The large business address is being updated during the tax return processing without the proper authority from the large business, specifically a properly completed and filed Form 8822-B.

#### Business Master File

IRPAC recommended creating additional mailing address fields on BMF in 2013. We understand the challenges associated with this recommendation as it will be a monumental undertaking that may not be achievable in a short period. Please refer to the 2013 Public Report for a detailed discussion. We still feel strongly about providing additional address fields in BMF and we will continue to work with IRS until such time as resources become available to implement it.

Pursuant to Reg. § 301.6212-2(a) that states a “taxpayer’s last known address is the address that appears on the taxpayer’s most recently filed and properly processed Federal tax return,” the IRS has issued revenue procedures to determine which returns

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will result in the IRS changing the address based on the address included on the most recently filed return, as well as which notices must be mailed to that “last known address.” The current guidance is found in Revenue Procedure 2010-16 (2010-19 IRB 664, dated 04/16/2010).

The recommendations for BMF outlined above are achievable without having to overhaul the entire computerized BMF system. In addition, one of the above recommendations will result in a reduction of business taxpayer notices (such as B-notices that include TIN and customer name and account information) being delivered to an incorrect address. The result of these unnecessary notices being sent may result in increasing the risk of stolen identity in some cases, or erroneous penalties and interest being assessed against the information return filer for failure to respond in a timely manner.

We believe these recommendations would help prevent identity theft, allow companies to be forewarned if their withholding agent is not making payroll deposits, permit businesses to have specific tax correspondence directed to the appropriate group or person, and increase efficiencies by having the IRS receive timely responses to its inquiries and notices without repeated mailings.

We are aware that the IRS has been in the process of implementing and sending notices to taxpayers when address changes are deemed to occur because there is a different address on the tax return from the prior period’s return. Notices CP148A and CP148B have been sent to taxpayers filing employment tax returns with address changes as of January, 2015.

The IRS issues a notice of confirmation of an address change to both the former and new address of the business. A concern has been raised by IRPAC that numerous unnecessary notices are repeatedly being sent to taxpayers at the old address, thus providing confidential data to the wrong individual. In addition, duplicate reporting has resulted in repetitive telephone inquiries and unnecessary time for IRS staff responses.

Taxpayers have received unsolicited notices of change of address, CP148 - “We changed your mailing address”. Revenue Ruling Procedure 2010-16 needs to be changed to state that in relation to an EIN changes of address, this will only be changed after receipt of Form 8822-B, Change of Business Address for Businesses.

### Form 8822 – B

IRS issued final regulations in May, 2013 requiring every person obtaining an EIN to provide the IRS with updated information (T.D. 9617). Subsequently revised Form 8822-B was issued to accommodate the requirement set out in Reg. § 301-6109-1(d) (2) (ii) (A). This form is to be used to provide old and new mailing addresses, the new responsible party and the new responsible party’s SSN, ITIN or EIN.

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IRPAC reviewed this form and had a meeting with the W & I division of IRS and discussed Box 1 of the Form 8822-B, which currently lists many forms with a line description, e.g., employment, excise, income, and other business returns. We suggested that the box be expanded to 4 boxes to capture each type of return the box lists. We understand the actual address change cannot be accomplished based on these box types until such time as more address fields are implemented in BMF. Accordingly, we will continue to discuss how we can improve the form with this in mind.

We raised concerns relating to the required information for the old representative of the business. Many companies, especially the ones that have been in operation for a number of years, do not know which entity's or individual's name was put on the original Form SS-4, Application for Employer Identification Number, upon applying for the EIN. Often, the lawyers or accountants engaged in helping owners set up companies put their names and their address on the form, thus it is not that of the actual owners of the entity. Or, perhaps, they cannot locate the form as it may not be one that any business refers to on a regular basis. There is no reason to either have the old information if the purpose is to gather current information or treat the form as incomplete because the business cannot provide the old representative's name.

It is recognized and encouraging that the IRS understood our concerns and removed from Form 8822-B the lines pertaining to the old responsible party's information on the October 2014 Form 8822-B revision.

### **3. Form 940 & 941**

#### **Recommendation**

IRPAC recommends flagging a business when its Form 941, Employer's Quarterly Federal Tax Return, box on Line 15 of part 3, which states that a business has closed or stopped paying wages, has been checked. Moreover, two separate boxes should be created; one section stating "If your business has closed check here"; the alternate section should state "If you have stopped paying wages, check here". By adding these options, the IRS can close a FEIN, Federal Employer Identification Number, if the business has closed and prevent fraudulent future use of old FEINs.

#### **Discussion**

Information on line 15 part 3 of Form 941 is transcribed during processing at the Service Center Recognition/Image Processing System (SCRIPS) on forms filed prior to January 2004. SCRIPS generate an X in the related field. The information provided is primarily used for compliance in examinations and collections. However, these flags would alert the system if a W-2 comes in after the final date when wages were paid in inactive businesses and prevent ID theft. It can help identify early issues and prevent businesses from becoming a potential victim. Monitoring these forms for other than just collection and examination purposes can reduce the IRS liability and potential fraud losses.

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## E. Publications and Forms Changes

### Recommendations

IRPAC recommends the following to clarify for businesses and individuals what is needed on forms to lessen the burden on individual taxpayers and small business owners when filing information tax forms.

1. Add links from business forms and publications to the IRS web site “Am I Required to File a Form 1099 or Other Information Returns?”
2. Add to the back of the payer’s copy of Forms 1099 where to go to find how to correctly update the forms when an error was made.
3. Add the shareholders’ basis information to Form 1120S, Schedule K-1, Shareholder's Share of Income, Deduction, Credits, etc., similar to the information required on Form 1065, Schedule K-1, Partner's Share of Income, Deductions, Credits, etc. .
4. In the Form 8965, Health Coverage Exemptions instructions, divide the 4<sup>th</sup> (fourth) bullet in the Citizens living abroad and certain noncitizens’ section into two sections.
5. Add to Form W-4P information that asks the individual filing the form to certify under penalties of perjury that they are a U.S. person.
6. Add a link from Form 1040 Sch. B, question 7a to the FinCen 114 website.
7. Add the new Pub. 590-B, Distributions from Individual Retirement Arrangements (IRAs) to the individuals copy of 1099-R.
8. Add a description for Box 2 of the Form 1099-B.
9. Establish a free e-Service to the IRS website for small business payers to manually enter on-screen and electronically file with the IRS up to 100 Forms 1099.

### Discussion

**Discussion on Recommendation 1:** Small business owners who file their own returns need to be able to find a quick and easy way to determine if they need to file Forms 1099. To lessen the burden on small business owners, IRPAC is recommending adding links from the business entity forms (Form 1040 Sch. C, Form 1065, Form 1120-

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S, and Form 1120) to the IRS web site “Am I required to File a Form 1099 or Other Information Returns?” The tax forms ask the following questions:

- “Did the business make any payments in 201X that would require it to file Form(s) 1099?”
- If “Yes” did the business file or will it file required Forms 1099?”

To help small business owners understand the Form 1099 filing requirements and to help business owners prepare more accurate returns IRPAC is also recommending the following links:

- from Publications 334, Tax Guide For Small Business (For Individuals Who Use Schedule C or C-EZ), and 335, to the web site under the discussion of Forms 1099 in the publications under information returns, and
- IRS web sites that pertain to business expenses such as [http://www.irs.gov/Individuals/Self\\_Employed](http://www.irs.gov/Individuals/Self_Employed) and [http://www.irs.gov/Businesses/Small-Business-& Self\\_Employed](http://www.irs.gov/Businesses/Small-Business-& Self_Employed) to the information explaining if they need to file information returns.

**Discussion on Recommendation 2:** We would like to acknowledge that tremendous progress has been made in the past two years on some suggestions IRPAC has made on improving Form 1099-MISC, Miscellaneous Income. IRPAC is recommending the following wording that is found in the Instructions for Form 1099-MISC be added after the first paragraph on the back of Form 1099-MISC, copy C for payer:

“If you need to correct a paper Form 1099-MISC that you have already sent to the IRS, see the 2015 General instructions for Information returns, part H.”

Small Business Taxpayers often prepare and file their own Forms 1099-MISC to payees with income reported in the wrong field, payments reported to exempt payees, or they report payments that are not income to the payee. Inaccurate information reported to the IRS creates a burden on the small business and individual taxpayers.

Every year many taxpayers receive erroneous Forms 1099-MISC from small businesses. Small businesses that incorrectly prepare Forms 1099-MISC are often reluctant to file corrections because of the limitation on their time or are uninformed how to properly correct them. This issue is more evident in the small business owner who has very little time to do paper work. They are reluctant to read a whole publication, especially since there is a correction box on the Form 1099-MISC they feel they have corrected the problem without having to read further. If they fail to correct the erroneous Form 1099 filings, or make the corrections improperly, the problems become worse for the recipient taxpayer who now has to figure out how to correct the problem on their tax return; or the taxpayer doing their own return becomes vulnerable to IRS systems identifying erroneously reported amounts as taxable income. This results in unnecessary correspondence that absorbs resources of both the taxpayer and IRS.

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**Discussion on Recommendation 3:** The amount of a shareholder's stock and debt basis is very important. Each year the shareholder's stock and debt basis of the S corporation goes up or down based on the S corporation's operations. The shareholder's share of the income, loss and deduction items of the S corporation is shown on the shareholder's Form 1120S, Schedule K-1 but the beginning basis is not there for the shareholder to make the correct calculations to complete his or her personal return accurately.

IRPAC is recommending adding the basis calculation on the Form 1120S, Schedule K-1. The shareholder's basis in the S corporation is important for the following reasons:

- Stock and debt basis is the first level of the shareholder's loss limitations.
- Stock basis determines the amount of gain or loss upon disposition.
- Stock basis governs the amount of distribution that can be received from an S corporation free of tax.

The inability to determine basis is a great inconvenience to the shareholders whose Forms 1120S, Schedules K-1 show a loss since a shareholder must attach to his or her individual Form 1040 a calculation showing that he or she has enough basis to be able to deduct the losses shown on his or her Forms 1120S, Schedules K-1. IRC § 1366(d)(1) states "The aggregate amount of losses and deductions taken into account by a shareholder under subsection (a) for any taxable year shall not exceed the sum of - (A) the adjusted basis of the shareholder's stock in the S corporation (determined with regard to paragraphs (1) and (2)(A) of section 1367(a) for the taxable year), and (B) the shareholder's adjusted basis of any indebtedness of the S corporation to the shareholder (determined without regard to any adjustment under paragraph (2) of section 1367(b) for the taxable year)."

The shareholder does not always have his or her beginning stock and debt basis if the corporation has been in existence for some time. The lack of a beginning basis for the current year makes it impossible for the shareholder or their individual return preparer to comply with IRC § 1366, IRC § 465 at-risk rules and IRC § 469 passive activity loss limitations. The instructions for Form 1120S, Schedule K-1 do have a calculation worksheet for basis but the first line asks for the stock basis at the beginning of the year. Having the S corporation provide a calculation of stock and debt basis or some type of shareholder's accumulation of S corporation items would enhance the shareholder's ability to establish his or her stock and debt basis.

**Discussion on Recommendation 4:** IRPAC is recommending dividing the section on page 2 of Form 8965 instructions covering exemptions for citizens living abroad and certain noncitizens into two parts. The first three bullets address U.S. Citizens and resident aliens, the 4<sup>th</sup> bullet addresses a person who is not a U.S. Citizen or U.S. National, and not an individual lawfully present in the United States. A person looking to see if they qualify for an exemption would normally look at the titles of each section to see if they qualify for an exemption. The 4<sup>th</sup> bullet is not consistent with the

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other bullets and would be easy to overlook, especially for an individual for whom English is their second language.

**Discussion on Recommendation 5:** IRPAC is recommending adding to Form W-4P the following words “I am a United States Person, under penalties of perjury, I declare that I have examined this certificate and, to the best of my knowledge and belief, it is true, correct, and complete. A non-U.S. Person should not use Form W-4P.”

Not having this certification on the W-4P puts financial institutions issuing Forms 1099-R in the process of claiming reasonable cause abatement for Notice 972-CG incorrect TIN penalties due to having Forms W-4P on file instead of having both Form W-4P and Form W-9 on file per the instructions in Publication 1586.

**Discussion on Recommendation 6:** To lessen the burden on individuals for whom English is their second language, IRPAC is recommending having either a link to the FinCen114 Form from Schedule B or the Forms and Publication site with the caveat telling the taxpayer they are leaving the IRS web site. Although FinCen114 is not an IRS Form, IRS Form 1040 Schedule B Line 7a box 2 informs the taxpayer they must file FinCen114 Form if they checked the box “Yes”. Taxpayers must send the form separately electronically and not attach it to their Form 1040. It would be easier for the taxpayers to be able to electronically connect to the form if there is a link.

**Discussion on Recommendation 7:** We would like to thank IRS Forms personnel for adding the new Publication 590-B to the instructions on the back of the 2016 Draft Form 1099-R.

**Discussion on Recommendation 8:** Forms and Publications have added a description on the 2016 Draft Form 1099-B, Box 2. This will be helpful for the individual taxpayer to accurately complete their Form 1040 Schedule D.

**Discussion on Recommendation 9:** IRPAC is recommending again a program where small businesses can electronically file their Forms 1099 for free directly on line with the IRS. The current method of issuing Forms 1099 or correcting Forms 1099 is time consuming and confusing. Paper Form 1099-MISC filing requires issuers to file a “red ink” paper copy of the Forms 1099 and Form 1096 with their IRS service center if they are not electronically filing the forms. A small business has four options for compliance:

- order the “red ink” copies of the Forms 1099 and 1096 from the IRS well in advance;
- purchase a packet of at least 25 forms from a retailer (when they may need only a few Forms 1099);
- purchase a program that will electronically prepare and file the forms; or
- pay a tax professional to prepare the Forms 1099.

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If small businesses or their representatives could file original and corrected Forms 1099-MISC via a free on line service, the process would be easier and increase accuracy as well as reduce costs for IRS and Form 1099 issuers.

IRPAC recommends a secure system that allows a payer/filer to register and enter information into a form on the IRS website. An IRS e-file feature for Form 1099-MISC will give small-business Form 1099-MISC filers a service similar to the SSA free filing of Forms W-2 and W-2c on the ssa.gov website. If supported by public education efforts, a Form 1099-MISC small-business free e-file system will give the IRS a greater amount of usable information, make data available to IRS sooner for matching (compared to hand-written or typed paper forms that must be scanned), increase the number of Form 1099 e-filers, and improve the accuracy of Form 1099-MISC filings by reducing scanning input errors and linking to FAQs and TIN Matching. This concept may also be scaled up to increase the number of free e-file of Form 1099-MISC and to include other 1099 forms in the future.

Accurate information reporting is essential to assist taxpayers in filing correct tax returns, it encourages a greater level of compliance, allows the IRS to more economically and efficiently detect and pursue noncompliant taxpayers who underreport income or do not file tax returns. Incorrect filings of Form 1099-MISC are a burden to taxpayers, the IRS, and the recipients of payments.

### **F. Reporting by Insurance Companies and Third Parties under §6055 and §6056**

#### **Recommendations:**

1. Education of taxpayers about the importance of providing correct information to insurance companies is very important to the usefulness of information returns filed in 2016 and future years. The 2014 IRPAC Report recommended that the instructions for line 61 of Form 1040, U.S. Individual Tax Return, discuss the importance of providing social security numbers (SSNs) for responsible and covered individuals to insurance companies and employers as well as the consequence of not providing the SSN. This year IRPAC makes two additional specific recommendations:
  - a. The electronic instructions for line 61 of Form 1040 should be updated to contain a link to [www.irs.gov/Affordable-Care-Act/Questions-and-Answers-about-Reporting-Social-Security-Numbers-to-Your-Health-Insurance-Company](http://www.irs.gov/Affordable-Care-Act/Questions-and-Answers-about-Reporting-Social-Security-Numbers-to-Your-Health-Insurance-Company). (See Appendix C)

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- b. The “What’s New” Section of the Form 1040 instructions should also contain a reference in the paper edition and a link in the electronic edition to a discussion about the importance of this information.
2. The usefulness of information provided to IRS on Form 1095-B and Form 1095-C in 2016 and future years can be greatly improved by education about the specific details of error reports to be issued under the Affordable Care Act Information Returns System (AIR). IRPAC recommends additional webinars focused entirely on the error reports that will be created for Form 1095-B and Form 1095-C as a result of electronic filings with IRS. IRPAC also recommends advance testing of these error reports be completed with companies that submit files as part of 2014 voluntary filing.
3. Information provided on 2015 Forms 1095-B and Forms 1095-C in the initial year of filing will result in a large number of corrected forms being issued. The final instructions for Form 1095-B and Form 1095-C were issued on Sept. 16, 2015 to discuss corrections that are required. IRS is aware that insurance companies have concerns about large numbers of social security numbers that are missing and taxpayer names that may not match IRS records. IRPAC recommends that IRS share detailed information about categories of errors with industry groups in 2016 and modify existing correction guidance for the first two years of filing.

### Discussion:

1. IRC §§ 6055 and 6056 impose new information reporting rules on insurance companies and employers. These rules were initially to apply for 2014 but were delayed by Notice 2013-4, 2013-31 I.R.B.116 until 2015. Insurance companies have taken many steps to educate insured customers and self-funded employer groups about the importance of the new information reporting rules. Despite these efforts, it can be predicted that the usefulness of information provided to the IRS will be initially limited due to missing or inaccurate SSNs and mismatched name and SSN combinations.

The 2013 and 2014 IRPAC Reports noted the difficulty insurers were experiencing with gathering SSNs. The 2014 IRPAC recommended that instructions for line 61 of Form 1040 discuss the importance of providing SSNs for responsible and covered individuals to insurance companies and employers as well as the consequence of not providing the SSN. This change was not made in the paper or electronic instructions for line 61 of Form 1040. The difficulty experienced by insurance companies in getting SSNs continues today.

IRPAC appreciates the efforts of the IRS in providing guidance on this topic on the website under the section for Affordable Care Act Topics.

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However, the intended audience for understanding the importance of providing SSNs to insurance companies is highly unlikely to read the information buried deep on the website. The usefulness of the information could be greatly enhanced by adopting the suggestion from the 2014 IRPAC report that the instructions for line 61 of Form 1040 discuss this issue. A simple link to the information on the website in the electronic instructions would achieve the desired result.

2. During 2015 the IRS has conducted multiple webinars with details about the AIR system. This system is scheduled to be available for voluntary testing of 2014 information in July 2015 and mandatory testing of 2015 data in November 2015.

IRPAC applauds the development of this system and most importantly the fact that we understand the error reports will be issued to filers shortly after electronic files are provided to IRS. This is a giant improvement over the timing of error reports issued for other types of information returns and will provide useful information to insurance companies and employers to assist them in further improvement of data files used for information reporting under these rules.

To gain maximum advantage from these system improvements IRPAC recommends the creation of a webinar focused solely on the specific details of the error reports that will be provided and that this be done on an expedited basis.

Confusion exists about whether these new reports are intended to constitute notification as discussed below.

Treas. Reg. § 301.6724-1(f)(ii) provides rules explaining the requirements for acting in a responsible manner in certain situations where the payor has been notified of an incorrect TIN. The regulation provides in part that “Except as provided in paragraph (f)(5) of this section, a filer must undertake an annual solicitation only if the payor **has been notified of an incorrect TIN** and such account contains the incorrect TIN at the time of the notification” (emphasis added).

IRPAC recommends that the IRS announce in these webinars that the initial error reports provided for at least the first two reporting cycles will not start the clock running on the requirement for additional solicitations.

3. The new requirements imposed under IRC §§ 6055 and 6056, the requirement of the new AIR system and the increase in information reporting penalties imposed under the Trade Preference Extension Act of 2015 create significant risks for insurance companies and employers first required to file Form 1095-B and Form 1095-C in 2016 for the 2015 tax year.

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The final instructions for Forms 1095-B and Form 1095-C were issued on 9/16/15 that indicate specific instructions about corrections which are required.

Treas. Reg. §§ 301.6721-1(c) and 301.6722-2(b) provide a distinction in the rules for consequential and non-consequential errors. Errors that are never non-consequential include (but are not limited to) a taxpayer identification number, the surname of a payee, any monetary amount or a significant item in the address of the payee.

Filers are known to be confused about the need for corrections required initially because of inconsistency with rules for corrections resulting from a notification by IRS in CP2100 Notices. Page 10 of the instructions in Publication 1281 instructs filers to simply include the corrected information on future information returns rather than requiring corrections with IRS.

Filers of Forms 1095-B and Form 1095-C will be faced with a trifecta of reporting under IRC §§ 6055 and 6056 for the first time, filing under the new AIR system for the first time and information reporting penalties which were recently more than doubled by Congress. Relief from penalties will be provided to filers of incorrect 2015 information who demonstrate good faith efforts to comply.

IRS was faced with new information rules which impacted far fewer taxpayers for the very first time in implementation of rules under IRC § 6050W and Form 1099-K. Notice 2011-89, I.R.B. 2011-46 provided transitional relief from penalties imposed under IRC §§ 6721 and 6722 for payee statements made in 2012. Notice 2013-56, I.R.B., 2013-39 extended this transition relief from penalties for statements made in 2013 and 2014.

IRPAC recommends that new webinars be developed focused on the correction process and common errors noted in 2015 statements filed.

IRPAC further recommends that similar transition relief from penalties be extended to Forms 1095-B and Form 1095-C filed in 2017.

### **G. ACA Education**

The ACA information for tax professionals and individuals' pages on the IRS website should provide clear written guidance or FAQs on explaining issues where there is no information available in publications and form instructions. Without this reporting, confusion will likely result in errors.

### **Recommendations**

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The following questions from practitioners were suggested for FAQs on the IRS website:

1. When to deduct as a medical expense the repayment of the Premium Tax Credit (PTC)?
2. Is there a preparer penalty if a preparer leaves off a dependent on a client's tax return because the client does not want to pay the individual shared responsibility payment for that dependent who lived in their home all year and is a qualifying dependent?
3. Who pays the Premium Tax Credit if a dependent applies for the PTC and receives the credit? (This question has been answered on page 15 of Publication 974 issued March 2015.)
4. Can the individual shared responsibility payment be deducted on Sch. A as a medical deduction?

### Discussion

1. Individual taxpayers trying to prepare their own returns and tax professionals are confused about when to deduct as a medical expense the repayment of the PTC. Answers need to be in writing for the following:
  - a. If a taxpayer has to repay the PTC and the money reduces their current tax year refund, can they deduct the repayment amount as a Sch. A medical deduction in that year?
  - b. If the taxpayer has to pay the PTC by writing a check on April 15, is this deducted on the tax return that is being submitted or do they wait to deduct the amount paid with the tax return in the year paid?
2. Would a paid preparer receive a preparer penalty for leaving off a qualifying exemption on a tax return they are preparing because the client tells the preparer they do not want to pay the individual shared responsibility payment for someone? A taxpayer in a high tax bracket would pay less if the exemption is left off since they would not be paying the individuals shared responsibility payment for that person.
  - a. HealthCare.gov under who's included in your household states a household usually includes the tax filer, their spouse, if they have one, and their tax dependents.
    - 1) The website further says "If you won't claim them as a dependent, don't include them."

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3. A taxpayer's college age dependent went on the Marketplace and received the Premium Tax Credit. The parents provided the greater part of the student's support and are eligible to claim the exemption.
  - a. This question has been answered on page 15 of Publication 974 issued March 2015.
  
4. There is confusion by some individual taxpayers on whether an individual shared responsibility payment can be deducted on the personal income tax return as a medical or tax deduction. The individual taxpayer remembers that the United States Supreme Court on June 28, 2014, ruled that the individual responsibility payment required of individuals who do not maintain minimum health coverage under the "individual mandate" is not a penalty, but a tax under Congress's power to tax in Article 1 of the U.S. Constitution. The individual also knows that they can deduct taxes as an itemized deduction.

IRC §5000A(b)(1) is clear that a penalty is imposed with such failure as not to have health insurance but unfortunately the average taxpayer preparing their own return does not usually look at the Internal Revenue Code.

  - a. Can the individual shared responsibility payment be deducted on Schedule A as a medical deduction or as a tax? Individuals might decide to claim this as a medical or tax deduction on their tax return since the courts ruled this is not a penalty. The answer needs to be made clear in FAQs and in the publications and forms instructions.