



The Biweekly
Payroll
Compliance
Publication
Of The
American
Payroll
Association

PAYROLL CURRENTLY

Inside Washington

December 2008

Margaret Roark, CPP, Presides Over Public Meeting of IRS Advisory Council

Margaret Roark, CPP, completed her year as Chair of the IRS Advisory Council (IRSAC) by presiding over a public meeting of IRS executives (including the Commissioner) and taxpayer representatives (including Roark herself). Issues discussed included creating panels of taxpayers to review guidance from IRS before it is issued; helping companies make determinations of worker classification (employee vs. independent contractor); and dispelling myths that perpetuate the idea that there is a de minimis number of hours or minimum compensation which exempt an employer from the requirement to withhold income taxes and to pay and withhold employment taxes.

The public meeting marked the end of Roark's four years of representing APA and all payroll professionals on the IRS Advisory Council. She noted that it was an honor to serve on behalf of taxpayers everywhere, and said that taxpayers need to remember that "IRS doesn't make the laws, but they are tasked with administering them."

What is IRSAC?

IRSAC is made up of 27 volunteer representatives from various segments of the taxpaying public (e.g., payroll, tax return preparers, and investment firms). Its purpose is to advise the Commissioner on any current tax administration issues, explain how they affect the taxpaying public, and make suggestions toward meeting the IRS mission of *providing America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness.*

You can read all of IRSAC's recommendations in the report from the 2008 public meeting, which is at www.irs.gov/taxpros/article/0,,id=188458,00.html.

IRSAC has four subgroups. Three of them correspond to three of the four IRS operating divisions: Large and Mid-Size Business (LMSB), Small Business and Self-Employed (SBSE), and Wage and Investment (W&I). (The fourth operating division, Tax-Exempt and Government Entities, has its own advisory committee.) IRSAC's fourth subgroup is devoted to addressing the tax gap, the difference between the amount of tax that should be collected and the amount that is collected.

Improving worker classification compliance

The SBSE subgroup suggested that adherence to worker classification guidelines might be enhanced if IRS offered incentives to employers to reclassify their workers before an IRS examination takes place. The subgroup noted that "Worker classification is dependent upon a complex, difficult factual

analysis. A reclassification as a result of an examination for prior tax years often results in a liability that effectively renders the employer/service recipient insolvent."

IRS has a Classification Settlement Program (CSP) under which IRS examiners are able to offer businesses a settlement using a standard closing agreement that is then tailored to fit the situation. Under the provisions of the CSP, the business is assessed less tax than it otherwise would be, provided the business prospectively treats all the subject workers as employees for all future federal employment tax purposes. The program is only available to businesses that timely file Forms 1099.

These agreements help the IRS and employers save time and resources as opposed to going to Appeals or court to conclude a case. CSP procedures also ensure that the taxpayer relief provisions under section 530 of the Revenue Act of 1978 are properly applied. More information on CSP is available at www.irs.gov/irm/part4/ch21s07.html, and more information on section 530 relief is available at www.irs.gov/pub/irs-pdf/p1976.pdf.

The SBSE subgroup recommended:

(1) IRS should publicize the availability of the CSP to service recipients (i.e., companies with workers) whether under examination or not, allowing them to voluntarily apply for the CSP even in the absence of an employment tax examination.

(2) IRS should consider sending letters to companies in industries having a history of noncompliance, offering a way to avoid penalties through a voluntary disclosure and filing of amended returns and payment of the taxes and interest due. Service recipients may self-comply if they receive educational information regarding worker status and an opportunity to correct any filing errors rather than be subjected to a traditional examination.

(3) IRS should investigate whether the Trust Fund Recovery Penalty is appropriate whenever there are employment tax delinquencies for two consecutive calendar quarters. The Internal Revenue Code authorizes the imposition of this penalty against the responsible persons within a corporate entity who fail to take appropriate steps to assure payment of employment taxes. The amount of the penalty is equal to the unpaid balance of taxes.

(4) IRS should commence a National Research Program (NRP) focused on employment tax and independent contractor issues. Historical data seems to be out of date with the current Internet economy. The employment tax NRP would increase the ability of the IRS to focus limited resources within employment

tax compliance challenged industries.

(5) IRS should add employment tax/worker classification information to the Form SS-4 (*Application for Employer Identification Number*), including links to relevant publications and sites on irs.gov.

Christopher Wagner, the Commissioner of the SBSE division, expressed interest in these proposals, but noted a challenge with item 5, as some companies apply for and receive their EIN over the phone.

The de minimis question

The SBSE subgroup reviewed the fact that “[t]here is no de minimis number of hours or minimum compensation which exempts an employer from the requirement to withhold income taxes and to pay and withhold employment taxes.” However, IRS publications related to employment taxes and employee classification have limited guidance on this topic.

The subgroup pointed out the inadequacies in this regard of Publications 15 and 15-A, and suggested language to be included in all relevant publications, materials, and sections of the website: “For federal income tax withholding, social security, Medicare, and federal unemployment (FUTA) tax purposes, neither the number of hours worked nor amount earned alone determines the status of an individual as independent contractor or employee. For example, an individual can be an employee even though the individual works one hour a week or one day a year.”

Wagner expressed appreciation for these suggestions, saying “We are always looking for ideas to increase compliance.”

Improving the quantity and quality of IRS instructions to taxpayers

In reference to how the IRS develops guidance such as regulations, revenue procedures, and revenue rulings, the LMSB subgroup called for “more intense outside stakeholder group involvement at the front end of the guidance process.” Permitting more expansive front-end input “should help to assure the proper targeting and high technical quality of future guidance; and, among other things, improve the compliance and audit processes. As confidence in this approach builds, the IRS and Treasury should be able to generate more items of useful guidance, to do so more quickly, and to free up resources for other important work.”

Increasing IRS’s ‘commercial awareness’

Also from the LMSB subgroup: “It would be mutually beneficial to both the IRS and taxpayers if the IRS acquired a greater ‘commercial awareness.’ If the IRS became more ‘connected’ to the businesses it examines, it would gain a better understanding of matters from both a commercial and a tax perspective. This would provide the IRS with the knowledge and insight to efficiently enforce the tax laws with limited resources, and taxpayers would receive the benefit of expediting the resolution of tax controversies.”

The LMSB subgroup recommended, “The IRS should engage various taxpayer industry groups and other external stakeholders in order to establish educational programs to further develop commercial awareness and enhance industry-specific technical tax skills within LMSB.”

IRS website renovation and electronic commerce

“IRS.gov has 44,000 pages of web content and an equal number of pdf files,” according to David Williams, IRS Director for Electronic Tax Administration and Refundable Credits. The

IRS would like to “replace its portals and reorganize the website to allow easier navigation and easier understanding” on the part of the taxpayer, he said. “In addition, we want to support online transactions, but we have to balance convenience with data security. For example, we don’t want a fraudster to be able to change the mailing address for an IRS refund check.”

These comments were in response to recommendations from the W&I subgroup to improve the IRS website with more and easier-to-understand information about the Earned Income Tax Credit and easier access to, and more consistent information about, the “Where’s My Refund” function.

Although more than 23 million low-income workers receive the EITC each year, 20-25% of eligible taxpayers do not receive it, according to the subgroup. “[T]he complexity of the EITC can be difficult for taxpayers and tax preparers. The EITC has a high erroneous payment rate, estimated at 23-28% or \$10-12 billion in lost tax revenue. Since the irs.gov EITC website is a key EITC communication tool, enhancements that result in better communication and increased usage could have a positive effect on both increasing participation and reducing error” (W&I subgroup report).

With regard to the “Where’s My Refund” section of the website, the subgroup noted the number of pages a taxpayer has to click through before he or she may enter identifying information. In addition, various IRS publications and forms direct people to less-efficient phone lines instead of the website and provide conflicting information about the length of time to allow for receiving a refund.

Other business and individual income tax issues

In her overview of the IRSAC report, at the beginning of the meeting, Roark pointed out some other recommendations of interest to payroll professionals:

- Promoting the Advance Earned Income Tax Credit as a way to increase take home pay for eligible low income workers.
- Allowing refunds to be deposited into health savings accounts.
- Educating employers on various ways to give an employee a raise through employee benefits, such as health savings accounts, telecommuting, or flexible workweeks.
- Raising or eliminating the maximum income level on the Free File Program, allowing more taxpayers to take advantage of this program.
- Identifying all paid preparers of personal income tax returns through the use of a unique identification number, and finding a process to monitor, educate, and control them.

“Paid preparers annually assist over 80 million taxpayers to meet their federal income tax obligation. The IRS does not have a single database or other information source to identify the paid preparer community.” Paid preparers include both licensed and unlicensed persons. Only licensed persons (state-certified lawyers and certified public accountants, and federally enrolled agents) may represent taxpayers before the IRS, but both groups may prepare returns. However, “a Treasury Inspector General for Tax Administration report issued on September 3, 2008, found 61% of a limited sample of tax returns prepared by unlicensed persons contained errors resulting in a significant net understatement of tax.” IRSAC feels that knowing who the preparers are and conducting outreach to them could address this significant contribution to the tax gap. ■