



NCPA

Taxing Times

Monthly Newsletter for ncpeFellowship Members

Vol. 3 No. 1

January 2012

Remarks from Beanna

Happy New Year! 2012 is a year that has great promise and inspiration for those of us who represent America's taxpayers.

While 2012 lies ahead of us, our challenges do as well. They include:

- Staying well and healthy
- Striving to be the most knowledgeable in the business of tax
- Diligently serving taxpayers, providing quality service
- Fulfilling our obligation to assist America's taxpayers to file complete and accurate tax returns

The days ahead are filled with long days, short nights and opportunities to do great work! May all of our decisions be wise and solidly based on tax law, regulation and procedure.

The ncpeFellowship sends its wishes to you for a great filing season!

Beanna

Beanna@ncpefellowship.com

Contents

Page

Remarks from Beanna	1
Tax News	3
For First Time, Tax Court Approves Use of Geithner/Turbo Tax Defense	3
IRS Moves Forward With Real-Time Tax System to OK Returns Up Front	3
Undeniable Benefit—and Pitfalls	3
Time Needed for Resolution	4
Legality of Rejecting Returns	4
Refunds	4
Economists Fear US Recession Unless Tax Deal Agreed	4
No More 'Instant Refunds' from Tax Preparers After This Year	5
149% APR	6
The Competition For Your Tax Business Is Heating Up.	6
Aiming for the young	6
Digital vs. pen-paper	6
Interest Rates Remain the Same for the First Quarter of 2012	7
Standard Mileage Rates Starting January 1, 2012	7
People in the Tax News	7
Former Roni Lynn Deutch Clients to Receive Letter from Taxpayer Advocate Service	7
H&R Block Spent \$410,000 Lobbying in 3rd Quarter	7
Christie Brinkley: My \$500K Tax Debt Was a Result of an Error	8
Woman Claims 19 Non-Existent Children on Tax Returns, Now Facing 143 Years in Prison	8

(continued on page 2)

Contents	Page
H&R Block Competitor Ramps Up Wal-Mart Presence, Too	9
Delafield Firm's President Guilty of Tax Evasion	9
United Way Receives Tax Grant	10
IRS News	10
Tax Information for U.S. Citizens or Dual Citizens Residing Outside the U.S. FS-2011-13, December 2011	10
New IRS FAQs Ease Some Fears about Settlement Offer for Misclassified Workers	12
Newly Released Form 940 for 2011 Includes Final List of Credit Reduction States	13
IRS Modifies Safe Harbors for Ponzi Scheme Victims Claiming Theft Loss Deductions Rev Proc 2011-58, 2011-50 IRB	14
IRS Can Summons a Taxpayer's Original Electronic Data Files to Obtain Associated Meta Data Chief Counsel Advice 201146017	14
Overpayment and Underpayment Rates Remain the Same for the First Quarter of 2012 Rev Rul 2011-32, IR 2011-112	16
IRS and User Fees	16
IRS Releases Revised Audit Techniques Guide on Conservation Easements	17
Allowing Workers to Quit and Then Get Rehired to Salvage Benefit Would Disqualify Pension Plan PLR 201147038	18
IRS Gives Tax Professionals First Time Homebuyer Tool	19
IRS Makes Changes to Form 2848, Power of Attorney	19
IRS Seeks to Return \$153 Million in Undelivered Checks to Taxpayers; Recommends e-file, Direct Deposit to Avoid Future Delivery Problems	20
IRS Under Pressure to Police Refundable Tax Credits	21

Contents	Page
IRS Sends Letters to Identity Theft Victims	21
Proposed PAL Regs Ease Definition of Limited Partnership Interest, extend it to LLC interests	22
IRS Modifies Safe Harbors for Ponzi Scheme Victims Claiming Theft Loss Deductions Rev Proc 2011-58, 2011-50 IRB	23
IRS Offers Tips in Selecting A Trustworthy Preparer	23
Thoughts from the Ragin Cajun	24
How Seniors Can Guard Against Identity Theft	24
Tax Pros in Trouble	24
Houston Area Tax Return Preparer Pleads Guilty	24
Tax Preparer Sentenced; Stole from Clients	25
Kingston Tax Firm Owners Admit to Fraud	25
New Jersey Law Firm Barred From Preparing Returns	25
Gardena Tax Service Owner Gets 15 Months for Filing False Returns	26
Memphis Tax Preparer Gets More Than 5 Years	26
Bakersfield Tax Preparer Pleads Guilty To Presenting False Income Tax Returns	26
Columbus Tax Preparer Sentenced to 33 Months for Fraud Charges	26
Taxpayer Advocacy & Tax Professionals	27
IRS Can Summons a Taxpayer's Original Electronic Data Files to Obtain Associated Meta Data	27
Wayne's World	28
Tax Professionals and Conflict of Interest	28
Sponsor of the Month	29
Professional Liability Insurance for Tax Preparers from Target Insurance Services	29
Tax Quotes	29



National Center for Professional Education Fellowship

Visit our Website
ncpeFellowship.com

For First Time, Tax Court Approves Use of Geithner/Turbo Tax Defense



The Tax Court on Wednesday for perhaps the first time accepted a taxpayer's use of the Geithner/TurboTax defense in allowing a patent attorney to blame mistakes in his use of tax preparation software to excuse him for penalties for failing to report income on his return. *Olsen v. Commissioner*, T.C. Summ. Op. 2011-131 (Nov. 233, 2011):

Petitioner works as a patent attorney for the Department of Energy at a national laboratory, holds a Government security clearance, and is subject to detailed and periodic background investigations.

In 2007, petitioner's wife received interest income from a trust created by her mother's estate. The funds were attributable to litigation resolved in favor of the estate. As a beneficiary of the trust, petitioner's wife received a Schedule K-1, Beneficiary's Share of Income, Deductions, Credits, etc., reporting the interest income. Prior to this instance, the couple had never received a Schedule K-1 and were unfamiliar with the form.

Petitioner usually takes the lead in preparing the couple's joint Federal income tax returns. He prepared the couple's joint income tax return for 2007 using tax return preparation software. Because he had never dealt with a Schedule K-1 in the past, petitioner upgraded his tax preparation software to a more sophisticated version as a precaution to ensure proper treatment of the unfamiliar form.

Using the upgraded software's interview process, petitioner correctly entered the name and tax identification number of the trust, properly reporting the source of income. While transcribing the remaining information, however, he made a data entry error that prevented the amount of interest income from being correctly displayed on Schedule E, Supplemental Income and Loss, of his Federal tax return. Petitioner reviewed the Federal tax return before filing, including using the verification features in his tax preparation software, but did not discover the error.

This Court has observed that "Tax preparation software is only as good as the information one inputs into it." *Bunney v. Commissioner*, 114 T.C. 259, 267 (2000). An isolated transcription error, however, is not inconsistent with a finding of reasonable cause and good faith. Reg. § 1.6664-4(b)(1).

We found petitioner to be forthright and credible, and we credit his testimony at trial. We conclude that he made an isolated

error in transcribing the information from his wife's Schedule K-1 while using the tax return preparation software. [Fn.4] It is clear that his mistake was isolated as he correctly reported the source of the income, and he did not repeat any similar error in preparing his tax return.

We note that petitioner holds a Government security clearance and is subject to periodic background investigations, which, as he is well aware, provide substantial motivation for him to properly report income on his tax return.

The most important factor in deciding whether a taxpayer acted with reasonable cause and in good faith is the extent of the taxpayer's effort to assess the proper tax liability. Under the unique facts and circumstances of this case, we hold that petitioner acted with reasonable cause and in good faith within the meaning of § 6664(c)(1). Accordingly, petitioner is not liable for the accuracy-related penalty under § 6662(a) as determined by respondent in the notice of deficiency.

IRS Moves Forward With Real-Time Tax System to OK Returns Up Front

Internal Revenue Service Commissioner Douglas Shulman Dec. 8 took a major step forward in his quest to revamp the way individuals file their income tax returns, vetting the creation of a real-time tax system in which return information would be matched against other third-party data before returns are accepted by the IRS.

Under the plan, first announced by Shulman in April, IRS is exploring the possibility of embedding third-party information into its pre-screening filters so that mismatches between return information and data from W2s and Form 1099s could be identified prior to filing. Where there are mismatches, taxpayers would be given an opportunity to correct them. The objective is to get away from back-end auditing, Shulman told a large audience at an IRS public meeting on the subject Dec. 8. As it stands now, taxpayers file their returns at one time, and months, or even years, later the service discovers there are problems and begins working on them.

Undeniable Benefit—and Pitfalls

Speakers at the public meeting said the proposal has undeniable benefits, in terms of correcting potential discrepancies before returns are filed, allowing taxpayers to respond earlier, reducing identity theft, and curbing noncompliance with credits, such as the earned income tax credit.

At the same time, there are significant pitfalls, they said, in that tax refunds would be delayed, and CP 2000 notices showing proposed changes to income tax returns based on comparisons of information reported by employers, banks, businesses, and other payers could come months or years after a return has been accepted—with failure-to-file penalties accruing all the while.

"Even certain of the simplest information forms could present challenges to the IRS in the context of a real time tax system,"

Patricia Thompson, chair of the American Institute of Certified Public Accountants Tax Executive Committee and partner with Piccerelli Gilstein & Co., said. In addition, Congress's proclivity for year-end legislation would wreak havoc with a real-time tax system.

The greatest concerns revolved around what would happen to returns where taxpayers were unable to resolve mismatches with the IRS. Speakers were unanimous in saying the IRS should not reject those returns.

Time Needed for Resolution

Taxpayers may have to contact multiple parties to resolve issues, and originators of information may have to send corrected information to update the IRS's system, they said, all of which takes time.

A reasonable, relatively non-burdensome process for explaining discrepancies is needed, Thompson said, such as an IRS unit dedicated to the process. At the very least, Shulman said, if the proposal goes forward, many employees will be shifted into real-time resolution.

Others said the IRS should consider transitioning real-time in over a period of years, or for certain returns, such as the 1040 or 1040A. The IRS could also do "soft rejects" that give the filer a short window in which to change the return before processing it as filed.

Practically speaking, a real-time tax system is currently infeasible. IRS does not receive all the information return data in time to perform matching during the filing season, Lonnie Gary, partner in Young, Craig and Co., said on behalf of the National Association of Enrolled Agents. The initiative will require an aggressive due date for the information return data that is to be matched, he said.

A real-time system could require the tax season to be pushed back so that employers, financial institutions, and brokers have time to get all the necessary information to the IRS. Yet April 15 "has an iconic status for Americans," said Robert Weinberger, a long-time former H&R Block vice president of government relations. "It's baked into our DNA." Delaying the filing season, even just the mid-January starting date, is likely to be quite controversial and trigger opposition, especially if it means delayed refunds, he said.

Legality of Rejecting Returns

In a parlay with Shulman, Keith Fogg, Villanova Law School associate professor and Federal Tax Clinic director, said the IRS cannot reject a paper return that meets even minimal standards. "Once the document comes in, IRS has a return in its hands and it can't say, 'this is not the return we wanted, take it back and give us another one,'" he said. "You've got a return and you've got to do something with it."

Shulman quickly responded that the proposal is not necessarily to reject returns, acknowledging that, as a legal concept, that

might not work. There is quite a nuance around the term "rejecting" a return, he said, and IRS language on that point has shifted.

Fogg also said the difficult question of engaging with taxpayers as the IRS attempts to resolve issues will be even more difficult for low-income taxpayers. The IRS should shift the burden of correcting mismatches onto tax preparers who will be better able to deal with it, he said.

Refunds

Taxpayers hungry for their refunds are not likely to take well to delays due to IRS checking out mismatches, many speakers said.

"Many taxpayers rush to file their tax returns to quickly receive their refunds," Kathy Pickering, H&R Block vice president, said. "With an average refund of \$3,000, this is the largest lump sum of money many taxpayers receive all year." Receipt of it is important not only to them, but to the economy.

Pickering questioned if discrepancy cases, which represent less than 3 percent of the 140 million returns filed annually, warranted a change of the magnitude being considered.

Economists Fear US Recession Unless Tax Deal Agreed

Economists are warning US growth could stall and the United States could even tip back into recession if Congress fails to extend tax cuts and unemployment benefits before the end of the year.

It seems like round 12 of the tax and spending fight between Democrats and Republicans on Capitol Hill.

Yet with less than a year before voters adjudicate the winner, some are increasingly worried that spectators -- rather than one of the fighters -- is about to get knocked out.

A steady stream of economists has warned that letting a payroll tax cut expire at the end of the year -- along with benefits for the long-term unemployed -- would cause US growth to slow dramatically.

Unless Congress acts both measures will expire at the end of the year, withdrawing a roughly \$180 billion stimulus package from the US economy.

In practical terms from January 1 social security tax on employee wages would rise from 4.2 to 6.2 percent and the jobless would receive unemployment benefits for just 26 weeks rather than 99.

That is very bad news for the economy according to Michala Marcussen of Societe Generale.

"The baseline assumption behind our own 1.4 percent 2012 GDP growth forecast is that these measures will be extended,"

she recently told clients.

“Should no agreement be reached, this would bring a fiscal drag of 1 to 1.5 percentage points, almost certainly tipping the US into recession.”

And there is good reason for believing that the measures will not be extended.

The Congressional Budget Office estimates a one year extension to the tax cut alone would cost around \$110 billion. In an era of rediscovered fiscal probity, neither party is willing to spend that much unless savings are made elsewhere. But in the strange world of Washington politics it is no longer Republicans who are arguing for the tax cut, and no longer Democrats who are arguing against it.

Wall Street economists are looking to the failure of a bipartisan Congressional deficit cutting committee for their lead.

“Given the rhetoric against deficits, any stimulus measure needs to be paid for, and the failure of the Super Committee has created doubts over where these savings will come from,” said Rajiv Setia of Barclays Capital.

Democrats have proposed paying for the extension by introducing a surtax on incomes over \$1 million.

Republicans, who have long supported tax cuts across the board, say this one does not help stimulate the economy and do not want to tax the rich.

Barclays has predicted a failure to extend the measures could lead to a 1.5 percentage point drop in growth.

“Were these measures not to be extended, fiscal tightening would be pulled forward to 2012,” said Setia.

Goldman Sachs economists have predicted a similar impact early next year.

“We estimate each provision is worth roughly one-third of a percentage point,” said Alec Phillips, an economist for the bank.

Taking into account the knock on-effects, the impact could be “potentially up to one-half point each with multipliers,” he said. Democrats have pounced on that kind of claim.

President Barack Obama will visit Scranton, Pennsylvania on Wednesday to hammer the case for extensions of both measures.

But some are uncertain he has the power to force the Republican hand.

Speaking about the battle over temporary payroll tax cuts and extended unemployment benefits, Conrad DeQuadros and John Ryding of RDQ Economics said they expected a mixed bag.

“We think the former has a much greater chance of passing Congress than the latter,” they told clients.

“The fate of the extended unemployment benefits, which also expire at the end of this year, is less clear because the extension of these benefits at the end of last year was tied to a two-year continuation of the Bush-era tax rates.

“It is unclear what leverage the administration can use to renew extended unemployment benefits through the end of next year.”

Racing headlong toward elections next November both Congressional fighters may simply prefer to slug it out rather than show weakness by throwing in the towel.

“Ultimately, extension will depend less on the policy itself and more on whether the two political parties can agree on whether-or how-to offset the cost of a one-year extension,” said Alec Phillips, an economist for Goldman Sachs.

No More ‘Instant Refunds’ from Tax Preparers After This Year

Last bank offering high-cost refund anticipation loans forced to stop.



Consumer advocates are celebrating the end of high-cost refund anticipation loans (RAL), often presented as “instant refunds” by tax preparers.

The last bank offering the loans has been forced out of the business by a settlement with the Federal Deposit Insurance Corporation (FDIC).

The settlement between the FDIC and Republic Bank & Trust requires the bank to terminate its RAL program after the end of the next tax season -- April 30, 2012, in other words.

The FDIC’s agreement imposes a \$900,000 civil penalty on Republic. It also incorporates a plan for Republic to implement a system of verifications to ensure that its partner tax preparers operate their future tax settlement activities with appropriate safeguards.

Republic will have to review all advertising for tax settlement products at the partner preparer’s offices, and conduct audits, including surprise on-site visits and mystery shopper surveys,

at ten percent of preparer locations.

“Mark Pearce and his team at the FDIC have delivered a big win for low-income tax payers today. Their determined efforts to finish the job reflect a commitment to protecting consumers from predatory loan products,” said Peter Skillern of the Community Reinvestment Association of North Carolina.

“The FDIC action is an important step toward protecting families who struggle to make ends meet from unfair bank credit products and practices,” said Jean Ann Fox of the Consumer Federation of America.

149% APR

RALs are one- to two-week loans secured by the taxpayer’s refund. RALs can be expensive; this year, Republic Bank is charging \$61.22 for a RAL of \$1,500, which translates into an APR of 149%.

RALs target low-income taxpayers, especially recipients of the Earned Income Tax Credit, a special tax break for working poor families. In 2009, RALs skimmed over \$600 million from the refunds of 7.2 million American taxpayers.

“We are pleased see the last of the RAL banks forced out of the business,” said Chi Chi Wu of the National Consumer Law Center. “We also commend the FDIC for a settlement that includes a plan for

Republic to institute safeguards for its remaining refund anticipation check program.”

Going forward, consumer advocates expressed a desire for the FDIC to develop a regulatory standard for the sale of refund anticipation checks (RACs), particularly that the FDIC should be vigilant to make sure that pricing of RACs remains appropriate and consumers are not charged abusive extra fees by partner tax preparers.

Absent a decision to terminate those products as well, the key priority should be to establish a balance between the need to help people avoid paying out-of-pocket for tax preparation and being able to purchase a RAC at a fair price, the consumer groups said.

The Competition For Your Tax Business Is Heating Up.

H&R Block and TurboTax will both offer live online professional help in the coming tax season, aiming to draw customers nervous about making mistakes or missing out on refund money.

The two companies are also providing mobile applications that enable users to file their tax returns using smartphones and tablet computers, and reloadable prepaid cards to use to receive refunds.

The similarities reflect a more competitive business for tax customers as the economy continues to struggle. With high unemployment expected to linger, the total number of returns filed isn’t expected to grow much in coming years. And with most paper-and-pencil returns now converted to e-filing, the companies will increasingly have to compete for the same taxpayers to expand their customer base.

Aiming for the young

Younger taxpayers who file simple forms are the most specific target. Both companies hope to establish relationships with these customers that will last as their financial lives get more complex and their tax returns more expensive to prepare.

The two companies combined handled more than 45 million returns last tax season, a third of all returns filed.

TurboTax, the popular software produced by Intuit, has added certified public accountants, enrolled agents and tax attorneys to its ranks who will be available to answer customer questions as they prepare their returns.

The expert help, available via text-based online chat or by telephone, will be in addition to the Q&A available with other customers that the company has offered for years.

The professional assistance is designed to appeal to customers who have hired someone to handle their taxes in the past and are now trying the do-it-yourself software.

“This is one of the pain points that people who use a pro tell us they have,” said Bob Meighan Turbo Tax vice president. “Block Live,” which was unveiled last week at H&R Block’s investor conference in New York, goes a step further, offering live video chat with its tax professionals, in addition to text chat or telephone consultations.

CEO Bill Cobb said preparing taxes using video chat will duplicate the experience of going to one of the Kansas City, Mo.-based company’s 11,000 offices.

“It’s the natural evolution of our sweet spot, which is assisted tax prep,” he said in an interview. “It’s the same experience.” The offering is part of the Block’s aim to work with taxpayers in whatever medium they prefer.

But Cobb and other Block executives emphasized that the market for assisted tax preparation has not been overtaken by the digital do-it-yourself.

Digital vs. pen-paper

They cited Internal Revenue Service statistics to show that the growth in digital preparation, which has overwhelmingly benefitted TurboTax, has largely been at the expense of pen-and-paper preparation.

Assisted preparation has remained about 60 percent of the market for the past decade; do-it-yourself has stayed at 40

percent.

The two firms are competing most fiercely for 18- to 24-year-olds, hoping to hold onto them as their returns become more complicated and generate more revenue. Block said taxpayers under 34 account for 67 percent of the returns it handles, compared with 55 percent of the returns filed to the IRS.

New mobile applications from both companies are aimed at this market. TurboTax offered its “SnapTax” app for smartphones last year and added a tablet version. Block is debuting a smartphone and tablet version of its software.

With both companies’ apps, users can take pictures of W-2 forms and other documents, and the programs will extract the data and fill in tax forms.

Both companies also are providing reloadable prepaid cards for customers to use to receive their refunds. Block this year will not charge customers who use its Emerald Card an extra fee for delaying payment of their costs until their refund arrives. Block has 2.3 million Emerald Cards in circulation and aims to add 1 million more. Cobb aims to push more customers to use the cards throughout the year as a way to drive growth in Block’s financial services business. Block has a bank, which means it collects the fees merchants pay on purchases taxpayers make with the cards.

The prepaid market is expected to continue to grow dramatically as more customers leave banks to avoid expanding fees. TurboTax also is offering a prepaid card, issued by Wilmington, Del.-based Bancorp Bank.

Interest Rates Remain the Same for the First Quarter of 2012

The Internal Revenue Service today announced that interest rates will remain the same for the calendar quarter beginning Jan. 1, 2012. The rates will be:

- three (3) percent for overpayments [two (2) percent in the case of a corporation];
 - three (3) percent for underpayments;
 - five (5) percent for large corporate underpayments;
- and
- one-half (0.5) percent for the portion of a corporate overpayment exceeding \$10,000.

The 3 percent rate also applies to estimated tax underpayments for the first calendar quarter in 2012 and for the first 15 days in April 2012.

Under the Internal Revenue Code, the rate of interest is determined on a quarterly basis. For taxpayers other than corporations, the overpayment and underpayment rate is the federal short-term rate plus 3 percentage points. Generally, in the case of a corporation, the underpayment rate is the federal short-term rate plus 3 percentage points and the overpayment rate is the federal short-term rate plus 2 percentage points. The rate for large corporate underpayments is the federal

short-term rate plus 5 percentage points. The rate on the portion of a corporate overpayment of tax exceeding \$10,000 for a taxable period is the federal short-term rate plus one-half (0.5) of a percentage point. Further, the federal short-term rate that applies during the third month following the taxable year also applies during the first 15 days of the fourth month following the taxable year.

The interest rates announced today are computed from the federal short-term rate during October 2011 to take effect Nov. 1, 2011, based on daily compounding.

Standard Mileage Rates Starting January 1, 2012

Instead of using the business portion of the actual expenses of operating a vehicle, the IRS permits taxpayers to use a standard mileage rate. IRS has issued new rates that are effective for travel on or after January 1, 2012.

Business rate remains at 55.5 cents per mile. The depreciation portion of this rate is 23 cents per mile.

Charitable rate is 14 cents per mile and is set by Congress therefore does not change until Congress makes such a change.

Medical and moving rate is 23 cents per mile (down from the 23.5 cents per mile applicable for July 1-December 31, 2011 period).

People in the Tax News

Former Roni Lynn Deutch Clients to Receive Letter from Taxpayer Advocate Service

Due to State legal action and receivership resulting in the closing of the Roni Lynn Deutch (RLD) Tax Centers, the National Taxpayer Advocate will contact clients of the Tax Centers by letter advising them of actions they may need to take to resolve their tax problems. The letter provides taxpayers information on how to try to resolve their IRS tax debts, including how to contact the IRS and how to get assistance from Low Income Taxpayer Clinics (LITCs) and TAS. Many of these taxpayers may still be represented by employees (or former employees) of the RLD Tax Centers and have a Form 2848, Power of Attorney and Declaration of Representative (POA), on file with the IRS. To view the letter and additional information sent to the RLD clients, please follow the links below:

H&R Block Spent \$410,000 Lobbying in 3rd Quarter

H&R Block Inc. spent \$410,000 in the first quarter to lobby the federal government on the development of the Consumer Financial Protection Bureau and other issues, according to a disclosure report.

That's an 18 percent drop from the \$500,000 that the nation's largest tax preparer spent in the same period last year, but 36 percent more than the \$300,000 it spent in the second quarter of this year.

The Kansas City, Mo.-based company also lobbied the federal government on legislation involving regulation of tax preparers, tax simplification, policies relating to people who don't have bank accounts and refund anticipation loans, according to the report filed on Oct. 20.

Block said in September it will no longer offer refund-anticipation loans, which are short-term loans backed by expected tax refunds. The company was unable to offer them in 2011 tax season after regulators ordered the bank that provided the money to cease funding the loans. Demand dropped for the loans as the government was able to get refunds to taxpayers faster. Refund-backed loans accounted for 4 percent of Block's revenue in the 2010 season.

In the July-to-September period, Block lobbied Congress, the Internal Revenue Service, the Treasury Department and the Securities and Exchange Commission, according to the report filed with the House clerk's office.

Christie Brinkley: My \$500K Tax Debt Was a Result of an Error



Christie Brinkley claims that her tax debt was a result of an error. The Internal Revenue Service has, on November 21, filed a tax lien against the former Sports Illustrated model, claiming that she owes the government \$531,000 in back taxes. On Monday, December 5, she issued a statement in relation to the tax debt issue.

"I consider myself very lucky to have been employed since I was 17 years old," the 57-year-old supermodel said in the statement released via E! News. "I have never had an issue with the IRS or any tax liens in the past and I have dedicated my time to giving back as much and as often as possible."

"I was surprised to learn of the tax lien filing and took immediate steps to rectify this matter, which for most people is a private

matter. I discovered the tax lien was indeed the result of an error," she continued on before promising that her taxes will be paid in full by Wednesday, December 7. She added, "I expect the tax lien to be released immediately thereafter."

In conclusion, the former wife of musician Billy Joel stated, "I regret not paying more attention to my accounting, but I have been, and remain focused on my whole family as both my parents navigate serious health issues. I am grateful for the outpouring of understanding and support I have received."

The tax lien was filed on Christie's mansion in Bridgehampton on New York's Long Island. The model, who made her stage debut playing Roxie Hart in the long-running Broadway rival of "Chicago" in April, is reportedly worth an estimated \$80 million, mostly from real estate holdings in the Hamptons.

Woman Claims 19 Non-Existent Children on Tax Returns, Now Facing 143 Years in Prison

A former Los Angeles resident was sentenced this afternoon to 18 months in federal prison for filing fraudulent federal income tax returns that claimed deductions for 20 non-existent children who were supposedly all born on the same day.

Norma Coronel, 40, of Livermore, California, an undocumented immigrant from Mexico, was sentenced today by United States District Judge Manuel Real. In addition to the prison term, Judge Real ordered Coronel to pay \$302,186 in restitution to the Internal Revenue Service.

Coronel pleaded guilty in September to three felony counts – aiding and assisting in the preparation of fraudulent federal income tax returns, fraudulently using Social Security numbers obtained with false information, and theft of government property.

In a plea agreement filed in this case, Coronel admitted that in 2003 she applied for and obtained Social Security numbers for at least 20 fictitious children, falsely claiming that the children had been born to her at a Los Angeles hospital on December 11, 2002. Using these bogus identities, Coronel prepared and filed fraudulent federal tax returns for family members and friends that claimed dependent deductions and fraudulently sought refunds.

Coronel admitted in the plea agreement that she had frequently directed the IRS to send the refund checks to her own residence or to accounts that she controlled. Coronel either failed to provide the taxpayers with copies of the returns that she had filed, or gave them copies of fake returns that had never been filed. As a result, the taxpayers were not aware that Coronel had filed fraudulent returns in their names or that Coronel was using the returns to obtain the refunds for her own benefit.

Hers is not the only fraud case making headlines these days after it was discovered that a couple living in a \$1.2 million waterfront house was also on welfare.

People were outraged when they discovered David Silverstein and Lyudmila Shimonova received more than \$135,000 in welfare assistance while going on numerous trips across the globe.

Federal welfare fraud investigator Michael Radyshewsky found that since receiving federal assistance in 2003, Silverstein and Shimonova have taken trips to Moscow, the Dominican Republic, Mexico, France, Israel, and Turkey.

According to her welfare records, Shimonova claimed she lived alone with her two children and that her assets were less than \$5,000. Records also show that Silverstein, who was listed as her landlord, received monthly benefits of \$1,272. Shimonova received benefits under the federal Temporary Assistance for Needy Families program and Social Security.

H&R Block Competitor Ramps Up Wal-Mart Presence, Too

Jackson Hewitt (Pink Sheets: JHTXQ) announced that it signed an agreement to offer tax-preparation services at about 2,800 U.S. Wal-Mart locations during the upcoming tax season. During the past tax season, the Parsippany, N.J., company served 2,000 Wal-Mart locations.

“We are coming off of our best year ever in our Wal-Mart operations and look forward to building on our Wal-Mart success in the 2012 tax season by delivering outstanding tax-preparation service and convenience to clients and Wal-Mart associates in Wal-Mart U.S. store locations nationwide,” Jackson Hewitt CEO Phillip Sanford said in a release.

Overall, Jackson Hewitt will have about 6,500 locations nationwide for the upcoming tax season. It’s the second-largest U.S. tax preparer, behind Kansas City-based H&R Block (NYSE: HRB).

H&R Block announced in October that it would offer tax preparation services at 300 Wal-Mart locations nationwide, including three in the Kansas City area.

Overall, Wal-Mart Stores Inc. <http://www.bizjournals.com/> (NYSE: WMT) has 3,822 U.S. Wal-Mart stores. That means Jackson Hewitt will be represented in 73.3 percent of Wal-Mart’s locations and H&R Block in 7.9 percent.

H&R Block’s overall network includes 11,000 U.S. offices.

Delafield Firm’s President Guilty of Tax Evasion

James A. Stuart Jr., 68, claimed income of just \$631 for 2005 and didn’t file returns for 2006 and 2007, according to the U.S. attorney’s office. Stuart had been indicted in December 2010 and was tried this week in federal court in Milwaukee.

Stuart, president and majority owner of New Age Chemical in Delafield, actually earned more than \$900,000 those years

and owed more than \$200,000 in federal income taxes, according to the U.S. attorney’s office. A receptionist at the company said Friday that Stuart had retired a couple of years ago. He could not be reached for comment.

The same attorney who represented actor Wesley Snipes in his much publicized IRS battle in Florida, handled Stuart’s trial - with similar results.

“There have always been individuals who argue taxes are illegal. They use false, misleading or unorthodox tax advice to gain followers,” said Kelly R. Jackson, head of the IRS criminal investigation division.

According to court records, Stuart had filed normal tax returns until 2005, when he stopped, and also began filing amended returns from prior years seeking refunds of all taxes paid. About the same time, he began similar tax battles over his state income tax and Waukesha County property taxes.

After IRS agents raided New Age Chemical in 2009, Stuart sued to challenge the search warrant, arguing, without a lawyer, that federal agents only have jurisdiction in federal enclaves like the District of Columbia or a military base.

“We have called this theory ‘frivolous squared,’” said the U.S. 7th Circuit Court of Appeals, which upheld a lower court’s dismissal of Stuart’s action to recover what he claimed were valuable chemical formulas supposedly taken during the search.

Stuart tried to change his status at New Age from employee to consultant, retitled an \$80,000 1959 Corvette to his daughter, bought \$100,000 worth of gold and took other steps to avoid taxes, according to prosecutors.

In a trial brief, his attorney suggested that Stuart didn’t have the required intent to be guilty of tax evasion, because he honestly - if absurdly - believed the laws were wrong and didn’t apply to him.

“Equally, criminal tax laws do not exist to punish ‘frank difference of opinion’ about tax laws,” the brief states, quoting case law. “A ‘misunderstanding as to his liability for the tax’ does not make a man a criminal ‘by his mere failure to measure up to the prescribed standard of conduct.’“

Though he didn’t testify at trial, dozens of Stuart’s letters and filings to the IRS were introduced, Assistant U.S. Attorney Matthew Jacobs said. He said Stuart claimed he was a “sovereign citizen,” not subject to IRS jurisdiction, that only silver should be recognized for payments and similar claims. In fact, Stuart spent a couple of weeks in jail when first arrested because he refused to recognize the authority of the federal court. He eventually did, and then put up his home as security for his bail.

In 2007, the state Tax Appeals Commission had rejected Stuart’s claims as “tired tax protester legal arguments” that courts had consistently rejected.

Stuart is scheduled for sentencing in April. His attorneys at the Law Office of Robert Bernhoft, SC, did not return a call for comment.

The IRS will try to recover back taxes, penalties and interest, a spokesman said.

United Way Receives Tax Grant

United Way of Eastern La Salle County has received a 2012 Volunteer Income Tax Assistance Grant Award of \$12,500 from the IRS.

United Way was one of only five grant recipients in Illinois. The VITA Grant Program is an IRS initiative designed to promote and support free tax preparation service for underserved, low-income populations. These include elderly, disabled, limited-English-speaking, rural and native American taxpayers.

For tax season 2011, Eastern La Salle County VITA sites filed 542 returns with refunds totaling more than \$647,000. Earned Income Tax Credit claimed totaled more than \$196,000.

United Way's efforts in 2012 will focus on reaching rural and low-income residents by coordinating more one-day mobile tax sites this year through partnerships with social service

IRS News

Tax Information for U.S. Citizens or Dual Citizens Residing Outside the U.S.

FS-2011-13, December 2011

The IRS is aware that some taxpayers who are dual citizens of the United States and a foreign country may have failed to timely file United States federal income tax returns or Reports of Foreign Bank and Financial Accounts (FBARs), despite being required to do so. Some of those taxpayers are now aware of their filing obligations and seek to come into compliance with the law. This fact sheet summarizes information about federal income tax return and FBAR filing requirements, how to file a federal income tax return or FBAR, and potential penalties.

Note that penalties will not be imposed in all cases. As discussed in more detail below, taxpayers who owe no U.S. tax (e.g., due to the application of the foreign earned income exclusion or foreign tax credits) will owe no failure to file or failure to pay penalties. In addition, no FBAR penalty applies in the case of a violation that the IRS determines was due to reasonable cause.

This fact sheet is provided for information purposes only, and the topics discussed may or may not apply to a particular taxpayer's situation. The IRS continues to consider the

topics discussed in this fact sheet and will provide additional information as it becomes available.

1. U.S. income tax return filing requirement

As a United States citizen, you must file a federal income tax return for any tax year in which your gross income is equal to or greater than the applicable exemption amount and standard deduction. For information about whether you must file a federal income tax return for a particular tax year, including exemption amounts and standard deductions, see Publication 501 (Exemptions, Standard Deduction, and Filing Information) for that year. Generally, you are required to report your worldwide income on your federal income tax return. This means that you should report all income, regardless of which country is the source of the income. Generally, you only need to file returns going back six years.

2. Penalties imposed for failure to file income tax returns or to pay tax

If you are required to file a federal income tax return and fail to do so, or you fail to pay the amount of tax shown on your federal income tax return, you may be subject to a penalty under Internal Revenue Code (IRC) section 6651, unless you show that the failure is due to reasonable cause and not due to willful neglect. The penalty is 5 percent of the amount of tax required to be shown on the return. If the failure continues for more than one month, an additional 5 percent penalty may be imposed for each month or fraction thereof during which the failure continues. The total failure to file penalty cannot exceed 25 percent. Note that there is no penalty if no tax is due.

If you fail to pay the amount of tax shown on your federal income tax return, you may be subject to a penalty for failing to pay under IRC section 6651(a)(2), unless you show that the failure is due to reasonable cause and not due to willful neglect. The penalty begins running on the due date of the return (determined without regard to any extension of time for filing the return) and is 1/2 percent of the amount of tax shown on the return. If the failure continues for more than one month, an additional 1/2 percent penalty may be imposed for each additional month or fraction thereof that the amount remains unpaid. The total failure to pay penalty cannot exceed 25 percent. Note that there is no penalty if no tax is due.

Under IRC section 6651(c)(1), the failure to file penalty is reduced by the amount of the failure to pay penalty for any month in which both apply.

For more information regarding the failure to file penalty and the failure to pay penalty, see IRS Notice 746 (Information About Your Notice, Penalty and Interest).

Example 1: Taxpayer is a United States citizen who lived abroad in Country A for all of 2010, during which time Taxpayer worked as an English instructor. He maintained a checking account with a bank in Country A, and the highest balance in the account did not exceed \$10,000 in 2010. Taxpayer

complied with Country A's tax laws and properly reported all his income on Country A tax returns. Although Taxpayer earned income in excess of the applicable exemption amount and standard deduction, he did not timely file a federal income tax return for tax year 2010. After learning of his U.S. filing obligations, Taxpayer filed an accurate, though late, federal income tax return showing no tax liability after taking into account the section 911 foreign earned income exclusion and the foreign tax credit for taxes paid to Country A. Taxpayer is not liable for a failure to file penalty, since the amount of tax required to be shown on the federal income tax return is zero. Similarly, Taxpayer is not liable for a failure to pay penalty, since the amount of tax shown on the return is zero.

Whether a failure to file or failure to pay is due to reasonable cause is based on a consideration of the facts and circumstances. Reasonable cause relief is generally granted by the IRS when you demonstrate that you exercised ordinary business care and prudence in meeting your tax obligations but nevertheless failed to meet them. In determining whether you exercised ordinary business care and prudence, the IRS will consider all available information, including:

- The reasons given for not meeting your tax obligations;
- Your compliance history;
- The length of time between your failure to meet your tax obligations and your subsequent compliance; and
- Circumstances beyond your control.

Reasonable cause may be established if you show that you were not aware of specific obligations to file returns or pay taxes, depending on the facts and circumstances. Among the facts and circumstances that will be considered are:

- Your education;
- Whether you have previously been subject to the tax;
- Whether you have been penalized before;
- Whether there were recent changes in the tax forms or law that you could not reasonably be expected to know; and
- The level of complexity of a tax or compliance issue.

You may have reasonable cause for noncompliance due to ignorance of the law if a reasonable and good faith effort was made to comply with the law or you were unaware of the requirement and could not reasonably be expected to know of the requirement.

Example 2: Same facts as Example 1, except Taxpayer's federal income tax return showed a tax liability of \$2,100. Taxpayer is subject to the failure to file penalty, unless Taxpayer shows that the failure to file was due to reasonable cause and not due to willful neglect. Taxpayer is also subject to the failure to pay penalty, unless Taxpayer shows that the failure to pay was due to reasonable cause and not due to willful neglect. Since the failure to file penalty is reduced by the failure to pay penalty for any month during which both apply, the maximum failure to file penalty is \$472.50 (22.5 percent of \$2,100). The failure to pay penalty will accrue for 50 months before the 25 percent maximum is reached. The maximum failure to pay penalty is \$525 (25 percent of \$2,100). The penalties could

be lower depending on when Taxpayer filed the return and paid the tax shown on the return. The penalties also could be lower, or there could be no penalties at all, to the extent Taxpayer is able to show that the failure to file or failure to pay was due to reasonable cause and not due to willful neglect.

3. Possible additional penalties that may apply in particular cases

In addition to the failure to file and failure to pay penalties, in some situations, you could be subject to other civil penalties, including the accuracy-related penalty, fraud penalty, and certain information reporting penalties. For information regarding the accuracy-related penalty and the fraud penalty, see IRS Notice 746 (Information About Your Notice, Penalty and Interest). For information regarding information reporting penalties, see the instructions for the specific information reporting form. For example, see the Instructions for Form 3520-A for information on the penalty for failure to file Form 3520-A.

4. FBAR filing requirement

As a United States citizen, you may be required to report your interest in certain foreign financial accounts on Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts (FBAR). For information about FBAR reporting requirements, including reporting exceptions.

5. How to file an FBAR

If you learn you were required to file FBARs for earlier years, you should file the delinquent FBARs and attach a statement explaining why they are filed late. You do not need to file FBARs that were due more than six years ago, since the statute of limitations for assessing FBAR penalties is six years from the due date of the FBAR. As discussed below, no penalty will be asserted if IRS determines that the late filings were due to reasonable cause. Keep copies, for your record, of what you send.

6. Possible penalties for failure to file FBAR

If you fail to file an FBAR, in the absence of reasonable cause, you may be subject to either a willful or non-willful civil penalty. Generally, the civil penalty for willfully failing to file an FBAR can be up to the greater of \$100,000 or 50 percent of the total balance of the foreign account at the time of the violation. See 31 U.S.C. § 5321(a)(5). Note that this penalty is applicable only in cases in which there is willful intent to avoid filing. Non-willful violations that the IRS determines are not due to reasonable cause are subject to a penalty of up to \$10,000 per violation. There is no penalty in the case of a violation that IRS determines was due to reasonable cause.

Example 3: Same facts as Example 1, except that the highest balance in Taxpayer's checking account exceeded \$10,000 and, after reading recent press and thus learning of his FBAR filing obligations, Taxpayer filed an accurate, though late, FBAR. The FBAR was accompanied by a written statement

explaining why Taxpayer believed the failure to file the FBAR was due to reasonable cause. The IRS will determine whether the violation was due to reasonable cause based on all the facts and circumstances. Taxpayer's explanation for why he failed to timely file an FBAR appears reasonable in view of the facts and circumstances of the case. Since the IRS determined that the FBAR violation was due to reasonable cause, no FBAR penalty will be asserted.

Factors that might weigh in favor of a determination that an FBAR violation was due to reasonable cause include reliance upon the advice of a professional tax advisor who was informed of the existence of the foreign financial account, that the unreported account was established for a legitimate purpose and there were no indications of efforts taken to intentionally conceal the reporting of income or assets, and that there was no tax deficiency (or there was a tax deficiency but the amount was de minimis) related to the unreported foreign account. There may be factors in addition to those listed that weigh in favor of a determination that a violation was due to reasonable cause. No single factor is determinative.

Factors that might weigh against a determination that an FBAR violation was due to reasonable cause include whether the taxpayer's background and education indicate that he should have known of the FBAR reporting requirements, whether there was a tax deficiency related to the unreported foreign account, and whether the taxpayer failed to disclose the existence of the account to the person preparing his tax return. As with factors that might weigh in favor of a determination that an FBAR violation was due to reasonable cause, there may be other factors that weigh against a determination that a violation was due to reasonable cause. No single factor is determinative.

Current IRS procedures state that an examiner may determine that the facts and circumstances of a particular case do not justify asserting a penalty and that instead an examiner should issue a warning letter. The IRS has established penalty mitigation guidelines, but examiners may determine that a penalty is not appropriate or that a lesser (or greater) penalty amount than the guidelines would otherwise provide is appropriate. Examiners are instructed to consider whether compliance objectives would be achieved by issuance of a warning letter; whether the person who committed the violation had been previously issued a warning letter or has been assessed the FBAR penalty; the nature of the violation and the amounts involved; and the cooperation of the taxpayer during the examination.

Example 4: Taxpayer is a United States citizen who lives and works in Country B as a computer programmer. Taxpayer has checking and savings accounts with a bank that is located in the city where he lives. The aggregate balance of the checking and savings accounts is \$50,000 during the tax year. Taxpayer complied with Country B's tax laws and properly reported all his income on Country B tax returns. Taxpayer failed to file federal income tax returns and failed to file FBARs to report his financial interest in the checking and savings accounts. After reading recent press and thus learning of his federal

income tax return and FBAR reporting obligations, Taxpayer filed delinquent FBARs, reporting both foreign accounts, and attached statements to the FBARs explaining that he was previously unaware of his obligation to report the accounts on an FBAR. Taxpayer also filed federal income tax returns properly reporting all income and no tax was due. The IRS will determine whether the FBAR violation was due to reasonable cause based on all the facts and circumstances. Taxpayer had a legitimate purpose for maintaining the foreign accounts, there were no indications of efforts taken to intentionally conceal the reporting of income or assets, and no tax was due. Taxpayer's explanation for why he failed to timely file an FBAR appears reasonable in view of the facts and circumstances of the case. Since the IRS determined that the FBAR violation was due to reasonable cause, no FBAR penalty will be asserted.

7. New reporting requirement for foreign financial assets

A new law requires U.S. taxpayers who have an interest in certain specified foreign financial assets with an aggregate value exceeding \$50,000 to report those assets to the IRS. This reporting will be required beginning in 2012. Taxpayers who are required to report must submit Form 8938 with their tax return.

New IRS FAQs Ease Some Fears about Settlement Offer for Misclassified Workers

IRS has issued additional frequently asked questions (FAQs) providing guidance on the Voluntary Classification Settlement Program (VCSP) for employees that have been misclassified as independent contractors (or as other nonemployees). Among other things, the FAQs explain that VCSP participation won't trigger a federal audit and that IRS won't share information about participants with the Department of Labor (DOL) or state agencies.

Earlier this year, IRS launched a new VCSP that allows employers to prospectively reclassify—as employees—those workers that they have erroneously treated as independent contractors or as other nonemployees. The new program carries generous settlement terms and provides audit relief for previous years. The VCSP is available to taxpayers who are currently treating their workers (or a class or group of workers) as independent contractors or other nonemployees and want to prospectively treat the workers as employees. It is open to businesses, tax-exempt organizations, and government entities.

To be eligible, a taxpayer: (a) must have consistently treated the workers as nonemployees; (b) must have filed all required Forms 1099 for the workers for the previous three years; and (c) cannot currently be under audit by IRS, or currently under audit concerning the classification of the workers by the DOL or by a state government agency. A taxpayer that was previously audited by IRS or DOL about the classification of the workers will only be eligible if it has complied with the results of that audit.

A taxpayer accepted into the VCSP agrees to prospectively

treat the class of workers as employees for future tax periods and in exchange:

(A) Pays 10% of the employment tax liability that may have been due on compensation paid to the workers for the most recent tax year, determined under the reduced rates of Code Sec. 3509 ;

(B) Won't be liable for any interest and penalties on the liability;

(C) Won't be subject to an employment tax audit for the worker classification of the workers for prior years; and

(D) Agrees to extend the period of limitations on assessment of employment taxes for three years for the first, second and third calendar years beginning after the date on which the taxpayer has agreed under the VCSP closing agreement to begin treating the workers as employees.

In October, IRS issued 16 FAQs explaining the nuts and bolts of the VCSP program.

The new FAQs make the following clarifying points about the new VCSP:

- IRS's rejection of a VCSP application will not automatically trigger initiation of a Federal audit. The rejected taxpayer could be audited for another reason, but not as a result of filing Form 8952 (Application for Voluntary Classification Settlement Program (VCSP)). (FAQ 21)
- The VCSP concerns future years only. Thus, IRS won't make any determination with regard to prior years and a taxpayer that signs a VCSP isn't making any representation as to the workers' proper status for prior years for federal employment tax purposes. In other words, a taxpayer that signs a VCSP closing agreement is not admitting liability or wrongdoing for past periods. (FAQ 22)
- A taxpayer can't participate in the VCSP if its parent or subsidiary or another member of its consolidated group is under IRS audit. (FAQ 23)
- One of the threshold qualifications for the VCSP is filing Forms 1099 for the previous three years for affected workers. IRS says a taxpayer will be eligible for the VCSP if it files the required Forms 1099 within 6 months of their due date (including extensions), assuming the other eligibility requirements are met. Those that haven't previously filed required Forms 1099 or filed them more than 6 months after their due date (including extensions) are not eligible for the VCSP. (FAQ 20)

Other FAQs say IRS won't share information about VCSP participants with the DOL or state agencies (FAQs 18 and 19). IRS also clarifies that a worker's filing of Form SS-8 (Determination of Worker Status for Purposes of Federal Employment Taxes and Income Tax Withholding) isn't treated as an audit and won't bar the taxpayer from participating in the VCSP.

Newly Released Form 940 for 2011 Includes Final List of Credit Reduction States

IRS has posted the 2011 Form 940, Employer's Annual Federal Unemployment (FUTA) Tax Return, and the following two supporting schedules on its website: (1) Schedule A (Form 940), Multi-State Employer and Credit Reduction Information; and (2) Schedule R (Form 940), Allocation Schedule for Aggregate Form 940 Filers.

The 2011 version of Form 940 takes into account the elimination of the 0.2% federal unemployment tax (FUTA) surtax, effective beginning with wages paid on July 1, 2011. The surtax was part of the 6.2% gross unemployment tax rate that employers paid on the first \$7,000 of wages paid annually to each employee (6% permanent tax rate, 0.2% temporary surtax). The FUTA tax rate, before consideration of state unemployment tax credits, is 6.0%, effective with wages paid beginning July 1, 2011. Employers in 30 states are allowed to claim 5.4% in state unemployment tax credits (known as the "normal credit") against the FUTA tax rate if they timely pay their state unemployment taxes, making the net FUTA rate 0.6%, beginning with wages paid on July 1 (0.8% on wages paid from January 1 to June 30, 2011). The other 20 states are "credit reduction" states that aren't allowed to claim 5.4% in state unemployment tax credits against the FUTA tax rate.

The 2011 version of Form 940 has separate lines to compute the FUTA tax on wages paid before July 1, 2011 (lines 7b and 7c), and after June 30, 2011 (lines 7d and 7e). Employers should be separately tracking the FUTA wages paid before July 1, 2011, and after June 30, 2011.

IRS has created a Form 940 page on its website. Information about any future developments affecting Form 940 (such as legislation enacted after the release of the form) will be posted on this page.

The 2011 version of Schedule A lists the following states (and the Virgin Islands) as 0.3% credit reduction states: Arkansas, California, Connecticut, Florida, Georgia, Illinois, Kentucky, Minnesota, Missouri, North Carolina, New Jersey, Nevada, New York, Ohio, Pennsylvania, Rhode Island, Virginia, the Virgin Islands, and Wisconsin. Michigan employers will be subject to a 0.9% credit reduction, because of Michigan's failure to repay its outstanding federal loans for four consecutive years. Indiana employers will be subject to a 0.6% credit reduction, because of Indiana's failure to repay its outstanding federal loans for three consecutive years.

The format on the 2011 version of Schedule A is significantly different from the format on the 2010 Schedule A. The 2010 Schedule A only listed the three states that were subject to credit reduction. The 2011 Schedule A lists all 50 states, plus the District of Columbia, Puerto Rico, and the Virgin Islands. Employers will need to place an "X" in the box of every state in which they were required to pay state unemployment tax in 2011, even if the state is not a credit reduction state. IRS indicated on its October payroll industry conference call that it decided to list all of the states on the 2011 Schedule A

because so many more states could possibly be subject to a credit reduction than in previous years.

The Schedule A instructions include an example on how to complete the form. In the example, an employer paid \$20,000 in wages to each of three employees in a 0.3% credit reduction state in 2011. Only the first \$7,000 of wages paid to an employee is subject to FUTA. As a result, the employer should enter \$21,000 (i.e., \$7,000 × 3) in the “FUTA Taxable Wages” column on Schedule A for the state that is a credit reduction state, and \$63 (i.e., \$21,000 × .003) in the “Credit Reduction” column for that state. The \$63 will also be entered on Form 940, Part 3, line 11. The instructions caution employers not to include wages that employees in credit reduction states receive in excess of the \$7,000 wage base on the “FUTA Taxable Wages” line.

Schedule R is only filed by reporting agents acting on behalf of home care service recipients (clients) who have designated the agent under Code Sec. 3504 to report, file, and pay all of their FUTA taxes. On Schedule R, the agent allocates the aggregate information reported on Form 940 to each home care service recipient client. IRS must approve a person to act as an agent before an agent is allowed to file an aggregate Form 940. Agents request IRS approval on Form 2678, Employer/Payer Appointment of Agent, except for state and local government agencies acting as agents under the special procedures in Notice 2003-70, 2003-2 CB 916. Schedule R must be attached to Form 940 for every year in which an aggregate return is filed.

Some of the Schedule R references to line numbers on Form 940 and Schedule A have been revised because of the changes to Form 940 and Schedule A. Schedule R may be filed either electronically or on paper. However, reporting agents filing for 1,000 or more clients must file a paper return. Form 940 and its supporting schedules must be filed by Jan. 31, 2012. However, the deadline is Feb. 10, 2012, for employers that deposited all of their FUTA taxes on time.

IRS Modifies Safe Harbors for Ponzi Scheme Victims Claiming Theft Loss Deductions

Rev Proc 2011-58, 2011-50 IRB

In a revenue procedure, IRS has modified the definition of a “qualified loss” in Rev Proc 2009-20, which set out a number of safe harbors for Ponzi scheme victims, to address situations in which the death of a lead figure in a specified fraudulent arrangement has foreclosed the possibility of criminal charges. As modified, qualified investors won’t be prevented from using these safe harbors solely on account of the lead figure’s death.

In Rev Proc 2009-20, 2009-14 IRB 749, which was issued days after Bernard Madoff’s guilty plea, IRS provided several generous safe harbors for qualified investors who were victims of Ponzi schemes (aka “specified fraudulent arrangements” as defined in Rev Proc 2009-20, Sec. 4.01). The safe harbors were designed to eliminate uncertainty about (i) the year of

the loss, and (ii) how much was lost (i.e., because of problems in determining how much income that was reported in the scheme was fictitious and how much was real).

The safe harbors applied only to “qualified losses,” namely those resulting from a Ponzi scheme in which (a) the lead figure (or one of them, if more than one) was charged by indictment or information (not withdrawn or dismissed) with the commission of fraud, embezzlement or a similar crime that, if proven, would meet the definition of theft for loss purposes under the Code, under the law of the jurisdiction in which the theft occurred; or (b) the lead figure was the subject of a state or federal criminal complaint (not withdrawn or dismissed) alleging the commission of a crime described in Rev Proc 2009-20, Sec. 4.02(1) , and either (1) the complaint alleged an admission by the lead figure, or the execution of an affidavit by that person admitting the crime; or (2) a receiver or trustee was appointed with respect to the arrangement or assets of the arrangement were frozen.

Since publication of Rev Proc 2009-20 , the deaths of some lead figures in Ponzi schemes have foreclosed authorities’ ability to charge them with criminal theft, leaving qualified investors in these cases unable to meet the definition of a qualified loss in Rev Proc 2009-20, Sec. 4.02 , or use the optional safe harbors.

Rev Proc 2011-58 modifies the definitions of “qualified loss” and “discovery year” in Rev Proc 2009-20 as follows.

A qualified loss is a loss resulting from a specified fraudulent arrangement in which, as a result of the conduct that caused the loss:

a lead figure was charged by indictment or information under state or federal law with the commission of fraud, embezzlement, or a similar crime that, if proven, would meet the definition of theft for purposes of Code Sec. 165 under the law of the jurisdiction in which the theft occurred, and the indictment or information has not been withdrawn or dismissed (other than because of the death of the lead figure);

a lead figure was the subject of a state or federal criminal complaint alleging the commission of a crime described in Rev Proc 2009-20, Sec. 4.02(1) , that has not been withdrawn or dismissed (other than because of the death of the lead figure), and (a) the complaint alleged an admission by the lead figure or the execution of an affidavit by that person admitting the crime; or (b) a receiver or trustee was appointed with respect to the arrangement or assets of the arrangement were frozen; or

a lead figure, or an associated entity involved in the specified fraudulent arrangement, was the subject of one or more civil complaints or similar documents that a state or federal governmental entity filed with a court or in an administrative agency enforcement proceeding, and (a) the civil complaint or similar documents together allege facts that comprise substantially all of the elements of a specified fraudulent arrangement conducted by the

lead figure; (b) the death of the lead figure precludes a charge by indictment, information, or criminal complaint against that lead figure; and (c) a receiver or trustee was appointed with respect to the arrangement, or assets of the arrangement were frozen.

A qualified investor's discovery year is his tax year in which:

the indictment, information, or complaint is filed; or
the complaint or similar document is filed or the death of the lead figure occurs, whichever is later.

These changes apply to losses for which the discovery year is a taxable year beginning after Dec. 31, 2007.

IRS Can Summons a Taxpayer's Original Electronic Data Files to Obtain Associated Meta Data

Chief Counsel Advice 201146017

In Chief Counsel Advice (CCA), IRS has explored a number of issues concerning its ability to summon a taxpayer's original electronic data files or the backup files (referred to here as "original electronic data files") to obtain the associated meta data (data on data, including such information as who, when, and how the information was created).

IRS may examine "books, papers, records or other data," for purposes of ascertaining the correctness of any return, making a return if none has been made, determining the tax liability of any person, and collecting that liability. (Code Sec. 7602(a) (1)) IRS may issue a summons to the taxpayer or certain third parties that it feels may be able to assist in determining the taxpayer's tax liability. (Code Sec. 7602(a)(2))

To have a summons enforced, IRS must make a four-step prima facie showing that: (1) the investigation will be conducted pursuant to a legitimate purpose; (2) the inquiry may be relevant to the purpose; (3) the information sought is not already within IRS's possession; and (4) the administrative steps required by the Code have been followed. (U.S. v. Powell, (1964, S Ct) 14 AFTR 2d 5942)

Generally, meta data is information that describes how, when, and by whom a particular item or set of electronic information was collected, created, accessed, modified, and formatted. Taxpayers may keep their business records electronically with meta data automatically created as an integral part of the records. Often, IRS's examinations would be advanced by accessing meta data that identifies the original date a transaction was entered in the electronic records, the dates of any changes to the entries, and the username of the person who made the entries. The value inherent in an examiner's ability to obtain the date and source of recorded entries is self-evident: the information tends to support or undermine the credibility of the entries in the business records.

The CCA looked at several scenarios involving issues related

to meta data to determine the reach of IRS's summons power. It concludes that, while not unlimited, IRS's power to obtain meta data is indeed broad.

Issue: Can an IRS examiner summon a taxpayer's original electronic data files to obtain the associated meta data if the taxpayer offers to provide either paper printouts (e.g., spreadsheets) or a truncated or an altered copy of the data files that don't contain the meta data?

The CCA concluded that as long as the information in the meta data "may be relevant," within the broad Code Sec. 7602(a)(2) , to a proper purpose for which the examination is being conducted—such as ascertaining the correctness of the return—IRS may properly summon the taxpayer's original electronic data files containing the unaltered meta data. The CCA found that it was readily apparent that the phrase "books, papers, records, and other data" in Code Sec. 7602 was more than broad enough to encompass the compelled production of the meta data associated with electronic documents. It was also apparent that meta data associated with a taxpayer's electronic business records "may be relevant" because the nature of the information contained in the meta data, especially the dates on which the entries were made or modified and the identities of the persons entering the data, may support or undermine the credibility of the records offered to substantiate the accuracy of the return.

In addition, the taxpayer's offer to provide or actual production of copies that omit the meta data didn't restrict IRS's authority to summon the original, unaltered meta data. IRS was entitled to summon the original documents, even though it possessed copies. The original meta data associated with the electronic records could assure the accuracy of the documents reproduced.

Can an examiner summon the taxpayer's original electronic data files to obtain the recorded entries and associated, unaltered meta data for transactions that occurred before or after the periods being examined if the taxpayer offers to provide a copy of the data file showing only the recorded entries without the meta data for transactions that occurred during the periods being examined?

The CCA determined that when summoned information dates from a period outside of those being examined, IRS must be prepared to answer the question of why such information may be relevant to the periods being examined. As with any other summoned information, it was enough that the records sought might throw light on the tax inquiry at issue. So long as IRS could demonstrate the potential relevance of the meta data associated with the records, the meta data should be obtainable by summons.

Can IRS summon the taxpayer's original electronic data files from the taxpayer's accountant if the accountant recorded the entries of the business transactions into the electronic file and possesses the records?

The CCA determined that IRS can summon a third-party

witness, such as the taxpayer's accountant, to give testimony or produce information that may be relevant to the examination, including electronic data files and the associated unaltered meta data.

If a taxpayer provides IRS with an electronic data file on a CD or a thumb drive, must the examiner retain the original CD or thumb drive in the examination case file? Alternatively, may the examiner make an electronic copy of the file and include it in the examination file if the case is closed unagreed and the data file supports the examiner's conclusions (or the data file contains information that may be relevant to a separate criminal investigation)?

In any case in which a taxpayer voluntarily (i.e., without a court order) provides IRS with an electronic or paper copy of its books and records, the taxpayer can require IRS to return the original copy. Accordingly, the CCA advised that, upon receipt of the CD or thumb drive, the examiner should immediately copy the electronic records for inclusion within the examination file to avoid being forced to prematurely relinquish the only available copy. See Internal Revenue Manual §25.5.4.3(2) (advising examiners to immediately copy records upon receipt). The CCA warned that the only caveats to this approach lie in the restrictions and safeguards codified in Code Sec. 7612(c) for copying any software, including the computer software source code and the executable code.

Do the Federal Rules of Civil Procedure and the case law under it offer analogous support for summoning electronic records with intact meta data?

The CCA noted that Fed. R. Civ. P. Rule 34(a)-(b) specifically addressed the production of electronically stored information, including meta data. Recent case law supported the proposition that Rule 34 generally requires electronically stored information to be produced in the specified form or forms in which it was requested. (see *Genetically Modified Rice Litigation*, (E.D. Mo. June 5, 2007) 2007 WL 1655757) If a request does not specify a form for producing electronically stored information, then the information must still be produced in the form or forms in which it was ordinarily maintained or in a reasonably usable form or forms. The case law supported the required production of meta data associated with electronic records, when the specifically requested form included such meta data or when the meta data was necessary for the requested information to be reasonably usable under the circumstances.

Overpayment and Underpayment Rates Remain the Same for the First Quarter of 2012

Rev Rul 2011-32 ; IR 2011-112

IRS has announced that the interest rates for tax overpayments and underpayments for the calendar quarter beginning Jan. 1, 2012, will remain the same as for the fourth quarter of 2011. For noncorporate taxpayers, the rate for both underpayments and overpayments for the first quarter of 2012 will remain unchanged at 3%. The 3% rate also applies to estimated tax

underpayments for the first calendar quarter in 2012, and for the first 15 days in April, 2012.

For corporations, the overpayment rate for the first quarter of 2012 will remain at 2%. Corporations will receive .5% for overpayments exceeding \$10,000. The underpayment rate for the first quarter of 2012 for corporations will be 3%, but will be 5% for large corporate underpayments.

Interest factors for daily compound interest for an annual rate of 2%, 3%, and 5% are published in Tables 7, 9, 11, and 15 of Rev Proc 95-17, 1995-1 CB 556.

IRS and User Fees

Improved IRS guidance and documentation can likely strengthen the agency's periodic review of user fees, resulting in additional revenue for IRS, the Government Accountability Office (GAO) said in a report released on Nov. 22. (GAO-12-193) The agency reviews its user fees every two years. "Well-designed and well-implemented user fees can reduce taxpayer burden by funding portions of IRS services that provide special benefits to users beyond what is normally provided to the public," GAO said. The Obama administration's fiscal year (FY) 2012 budget request for IRS was \$13.6 billion, including \$204 million in spending funded by user fees. Collections are now expected to total \$309 million in FY 2012, GAO said. As described in the report, IRS charges user fees for activities such as assisting taxpayers in complying with their tax liabilities, clarifying the application of the Code to particular circumstances, and ensuring the quality of paid preparers of tax returns. In FY 2010, two fees—for installment agreements and income verification express service—comprised more than 80% of IRS user fee collections. "IRS has implemented several new user fees in recent years, but it may not be taking full advantage of its process for identifying new user fees," GAO concluded.

IRS's transition to its Modernized e-File (MeF) system, which is designed as the replacement for the Legacy e-File system, has hit bumps in the road, according to an audit released by the Treasury Inspector General for Tax Administration (TIGTA) on Nov. 29. (Audit Report No. 2011-40-131) As described in the audit, the MeF system provides real-time processing of tax returns and extensions that will improve error detection, standardize business rules, and expedite acknowledgments. "Processes used to test and monitor the MeF system do not ensure MeF system business rules designed to validate basic requirements on a tax return are working as intended," TIGTA said. Consequently, IRS still has only "limited assurance" that the system accurately processes individual tax returns, the audit continued. The audit also revealed that lower than expected tax return transmitter participation and tax return volumes "raise significant concerns" as to whether the MeF system will fully replace the Legacy e-File system in 2013. For example, IRS received only 8.7 million individual tax returns through the MeF system as of April 18, while it anticipated receiving 35 million such returns. "Since a growing number of Americans are filing their returns electronically, there is no room for error in IRS computer systems," said J. Russell

George, the inspector general. “The IRS must be relentless in its pursuit of excellence with regard to all aspects of the Modernized e-File system. Attention to system security, capacity, and performance accuracy is paramount.”

IRS Releases Revised Audit Techniques Guide on Conservation Easements

IRS has revised its Conservation Easement audit technique guide (ATG), which provides extensive insight into the statutory requirements for qualified conservation contributions, valuation issues, IRS examination procedures, penalties, and state tax credits associated with such contributions.

In general, Code Sec. 170(f)(3) bars a charitable contribution deduction for a contribution of an interest in property that is less than the taxpayer’s entire interest in the property, but an exception is made for a qualified conservation contribution, i.e., the contribution of a qualified real property interest to a qualified organization exclusively for conservation purposes. The interest in property conveyed by a facade easement must be protected in perpetuity for the contribution to be a qualified conservation contribution. (Code Sec. 170(h) , Reg. § 1.170A-14(b)(2))

Any interest in the property retained by the donor must be subject to legally enforceable restrictions that will prevent uses of the retained interest inconsistent with the conservation purposes of the donation. (Reg. § 1.170A-14(g)(1))

Under Reg. § 1.170A-14(g)(2) , if the property has a mortgage or other lien in effect at the time the easement is recorded, the easement contribution is not deductible unless the mortgagee or lien holder subordinates its rights in the property to the rights of the donee organization to enforce the conservation purposes of the easement.

The value of a conservation easement is its fair market value (FMV) at the time of contribution, as determined in a qualified appraisal (see below). Under Reg. § 1.170A-13(c)(2), which concerns any noncash charitable contribution exceeding \$5,000, the donor must: (1) obtain a qualified appraisal for the contributed property; (2) attach a fully completed appraisal summary (i.e., Form 8283) to the tax return on which the deduction is claimed; and (3) maintain records relating to the claimed deduction, as required by Reg. § 1.170A-13(b)(2)(ii).

A qualified appraisal must include a detailed description of the property and its physical condition, the valuation method used to determine the FMV, and the specific basis for the valuation. (Reg. § 1.170A-13(c)(3)(ii))

If the conservation organization requests a cash contribution from the donor of the conservation easement, the payment is deductible as a charitable contribution only if it is a voluntary transfer made with charitable intent. (Code Sec. 170) Charitable intent may exist if the transfer is made without the receipt of, or the expectation of receiving, a quid pro quo for the transfer. In general, if the benefits the transferor expects to receive are substantial, the transfer does not satisfy the

charitable intent requirement.

The ATG identified a number of issues frequently associated with deficient conservation easement contribution claims, including the following:

- failure to meet charitable contribution rules;
- noncompliance with substantiation requirements;
- inadequate documentation or lack of conservation purpose;
- failure to provide the donee organization with a right to proceeds in the event of termination;
- use of improper appraisal methodologies and overvalued conservation easements; and
- failure to report income from the sale of state tax credits.

Following is an overview of some of the key areas agents are instructed to examine, and steps they should take, when reviewing a return claiming a conservation easement deduction.

Before contacting the taxpayer, examiners should review the return, any attachments thereto, and internal and external sources of information. Form 8283, Noncash Charitable Contributions, is the “starting point” for examiners to gather information about the deduction. Examiners are instructed to inspect the form for a number of red flags, including:

- incomplete or missing information,
- missing appraiser or donee acknowledgments,
- inconsistent dates when compared to other documents,
- a short time period between the acquisition of the property and the donation date,
- high valuation of the easement in relation to the basis of the underlying property or the total acreage of the underlying land, and
- use of an appraiser who does not generally perform appraisals where the easement is located.

In some cases, taxpayers will also attach baseline studies, correspondence or other documents related to the easement donation. This information should be reviewed for unusual items or inconsistencies and ultimately compared to actual source documents.

Examiners should look for the following omissions, each of which may be a basis for disallowing the charitable contribution: lack of appraiser’s or donee’s signatures, failure to attach a qualified appraisal, and failure to include the \$500 façade filing fee for easements on buildings in registered historic districts for which a deduction of more than \$10,000 is claimed. Examiners are also instructed to determine whether there were any preexisting restrictions on the property such that granting the easement didn’t impose any new restrictions causing any loss in value.

The ATG also addresses complications that can arise in contexts where the donation originates from a flow-through entity.

Examiners are instructed to; if possible, conduct a joint

taxpayer interview with the IRS appraiser. If the taxpayer or representative won't consent to an interview, then the examiner should either issue a summons or develop the case based on third-party contacts, such as representative of the donee organization, the appraiser, the baseline study author, or other conservation experts.

Examiners are also encouraged to inspect the property, if possible, with the IRS appraiser. During the inspection, the examiner should note factors including the location of the significant or protected habitat or species, public access (both physical and visual) to the easement property, and any inconsistent use of the property. The examiner should ask the taxpayer or representative to point out the outdoor recreation areas, animals, plants, scenic views, or historic land and structures that contribute to the conservation purpose. If the examiner observes an absence of conservation attributes, lack of access, de minimis public benefit, or use inconsistent with the conservation purpose, the examiner should ask the taxpayer or representative for clarification and additional documentation.

The examiner and IRS appraiser should review documents such as the deed of conservation easement, subordination agreements, baseline study, appraisals, information provided by the qualified organization, and documents submitted to the National Park Service.

The deed of conservation easement should set out the property that is being encumbered, the conservation purpose, protection of the property in perpetuity, public access to the property, reserved rights, and provisions for subordination and allocation of proceeds. In particular, examiners should look for any language that negates or contradicts the perpetuity requirement, whether the taxpayer reserved any property rights that negate the conservation purpose, whether the taxpayer properly obtained a subordination agreement from any lender(s) prior to granting the easement, and whether the lender agreement provides for the donee organization to share in the proceeds in the event that the easement is extinguished (e.g., by condemnation or casualty).

Throughout the examination, the examiner should be developing relevant facts to determine what penalties may apply and whether waiver of the penalty may be appropriate (based on reasonable cause). In particular, examiners should be alert to any indication of fraud and should consult the Fraud Technical Advisor program analyst if badges of fraud are identified during the examination.

Most states with a conservation tax credit program determine the amount of the credit based on a percentage of the FMV of the donated easement. Some programs provide for a carryforward of unused tax credits over a number of years, and some have transferable tax credits that can be sold to third parties.

Although the issuance of the state tax credit, or use of same to reduce state tax liability, doesn't trigger federal gross income to a taxpayer, sale of a transferable state tax credit is

a taxable transaction that results in gain equal to the excess of the amount realized over the adjusted basis of the property (typically zero, since the taxpayer didn't pay anything to receive the credits). The Tax Court has also held that state tax credits are capital assets.

Although the charitable contribution of a conservation easement is likely the most significant issue on the return, examiners should nonetheless be alert to the related issue of taxpayers' failure to report income from the sale of state tax credits.

Allowing Workers to Quit and Then Get Rehired to Salvage Benefit Would Disqualify Pension Plan

PLR 201147038

IRS has privately ruled that a pension plan would cease to be qualified under Code Sec. 401(a) if it allowed workers to "retire" in order to lock in an unreduced pension benefit, and then immediately be rehired. The arrangement, which would suspend the unreduced pension benefit until affected workers actually retired, was proposed as part of a rehabilitation plan for a qualified plan in critical status.

Code Sec. 432(e) requires a rehabilitation plan to be adopted for a multiemployer plan that is in critical status. The plan sponsor must provide to the bargaining parties one or more schedules showing revised benefit structures, revised contribution structures, or both, which, if adopted, may reasonably be expected to enable the multiemployer plan to emerge from critical status in accordance with the rehabilitation plan. One schedule is designated as the default schedule and assumes that there are no increases in plan contributions other than the increase necessary to emerge from critical status after future benefit accruals and other benefits (other than benefits the reduction or elimination of which are not permitted under Code Sec. 411(d)(6)) have been reduced to the maximum extent permitted by law.

Under Reg. § 1.401-1(a)(2) and Reg. § 1.401-1(b)(1)(i), a qualified pension plan is one established and maintained by an employer to provide for the livelihood of the employees or their beneficiaries after the employees' retirement through the payment of benefits. The plan must be established and maintained by an employer primarily to provide for the payment of definitely determinable benefits for employees over a period of years, usually for life, after retirement.

After Plan's actuary certified that it was in critical status, Taxpayer wanted to present to the collective bargaining parties a default schedule that will eliminate all subsidized early retirement benefits, including unreduced service pensions. The default schedule will eliminate the ability of participants with 20 or more years of service to retire with an unreduced pension benefit. As a result, participants who have enough service to retire without a reduction in benefits will no longer be able to do so once the default schedule is in place.

As part of the default schedule, Taxpayer proposed to give participants notice 60 days before the date that the subsidized

service pension benefit is eliminated. Eligible participants who retire during this 60-day window would then return to employment and have their benefits suspended while working. The subsidized service pension benefit is an early retirement pension benefit and the plan's normal retirement age is 65. Thus, before eliminating the benefit (i.e., the ability of participants with 20 or more years of service to retire with an unreduced pension benefit), Taxpayer wanted to allow employees to "retire" on one day in order to qualify for the existing subsidized service pension benefit (i.e., before the default schedule is in place), and return to work the very next day or perhaps after a week has passed. Neither the employee nor the employer intend for these "retirees" to actually terminate employment and no longer perform services for the employer when they "retire" and qualify for their early retirement pension benefit.

Taxpayer asked IRS to rule on whether the plan would be disqualified under Code Sec. 401, if participants who are eligible for subsidized early retirement benefits are allowed to "retire" on one day in order to qualify for the early retirement subsidy, and then immediately return to work with payment of their early retirement pension benefit suspended until they actually retire.

IRS privately ruled that the proposed arrangement would cause the plan to be disqualified under Code Sec. 401. IRS interprets Reg. § 1.401-1(a)(2) and Reg. § 1.401-1(b)(1)(i), to provide that when an employee legitimately retires, he separates from service with the employer. Thus, if both the employer and employee know at the time of "retirement" that the employee will, with reasonably certainty, continue to perform services for the employer, a termination of employment has not occurred upon the "retirement" and the employee has not legitimately retired. IRS also said that under the regs dealing with severance of employment (Reg. § 1.410(a)-7(b)(2) and Reg. § 1.410(a)-7(b)(6)), an employee retires on a severance of service date, when his period of service ends.

To buttress its position, IRS cited:

A nontax Seventh Circuit opinion (*Meredith v. Allsteel*, CA 7, 1993) holding that the word "retire" means to leave employment after a period of service.

The Code Sec. 409A nonqualified plan rules and Rev Rul 79-336, 1979-2 CB 187 (dealing with special forward averaging of lump sum distributions), which IRS interprets as clarifying that an employee legitimately retires when he stops performing service for the employer and there is no explicit understanding between the employer and employee that upon retirement he will immediately return to service with the employer.

Proposed regs issued in 2004 on phased retirements (see Preamble to TD). The preamble provides that the proposed regs "specifically do not endorse a prearranged termination and rehire as constituting a full retirement."

IRS concluded that because a qualified pension plan

generally can't pay benefits before retirement, an employee who "retires" with the explicit understanding between him and the employer that he will immediately return to service has not legitimately retired and may not qualify for an early retirement benefit under Plan. Thus, under the proposed arrangement, IRS ruled that employees who "retire" on one day to qualify for a Plan benefit, with the explicit understanding that they are not separating from service with the employer, are not legitimately retired. Because such employees won't actually separate from service and stop working for the employer when they "retire," their supposed "retirements" wouldn't constitute a legitimate basis to allow participants to qualify for early retirement benefits (which then would be immediately suspended.) Such "retirements" would result in Plan's disqualification under Code Sec. 401(a).

However, IRS also pointed out that under Code Sec. 401(a) (36), employees who have attained age 62 upon benefit commencement may qualify for and receive an early retirement benefit under Plan while they continue in employment.

IRS Gives Tax Professionals First Time Homebuyer Tool

The IRS has created a web-based First-Time Homebuyer Credit Look Up tool that will allow taxpayers to look up their personal information about this credit. The Look Up tool will be available January 17, 2012;

In the Look Up tool, the taxpayer will need to self-authenticate by providing their SSN, date of birth, and complete address (same as Where's My Refund). The Look Up tool should then display the following taxpayer's information:

- Last 4 digits of their SSN
 - Original amount of credit claimed
 - Required annual repayment amount
 - Amount of credit already repaid
- Total Balance Left

ncpeFellowship member Bill Nemeth is credited with providing the above information – thanks Mr. Bill.

IRS Makes Changes to Form 2848, Power of Attorney

Last week, the IRS released changes to Form 2848, Power of Attorney -- the first changes to this form in nearly three and a half years. It made the changes in large part to accommodate a new class of tax practitioners: registered tax return preparers (RTRP). The IRS also took the opportunity to make other significant changes, such as:

- Adding RTRP as a designation for limited practice before the IRS
- Adding a place for RTRP holders to indicate their PTIN number
- No longer allowing joint return authorizations. Authorizations are allowed for only one Taxpayer

Identification Number and client signature. In past versions, the form allowed for both spouses' Social Security Numbers or for business Employer Identification Numbers in separate fields.

- Requiring CPAs to indicate their CPA enrollment number for the state in which they are licensed to practice
- Requiring practitioners to affirmatively select to be copied on client notices, if they choose to be. In the past, notices were automatically sent to the first representative listed on Form 2848.
- Eliminating the option to receive a client's refund check. (Note: Endorsing a refund check is not allowed under Circular 230, Section 10.31.)
- Adding checkboxes to clearly authorize acts such as:
 - Disclosure of tax return information to third parties
 - Practitioner authorization to sign a client return, and
 - Substituting or adding a representative

The IRS made many of these changes without soliciting practitioner comment, which caused confusion among practitioners.

What is still unknown is how long the IRS will continue to accept the previous version of Form 2848. Sources at the IRS are not clear on how to administer changes on the new version, particularly when it comes to joint returns. An IRS staff member at the Memphis, Tenn., CAF unit indicated that the unit was continuing to accept the previous version of Form 2848. However, because the IRS has not indicated any cut-off dates, it is recommended that practitioners file the new Form 2848 to ensure proper processing. The IRS is seeking comment on the updated Form 2848 at taxforms@irs.gov. Beyond415 makes it easy to keep up with changes to IRS practice and procedure. Our web-based application helps practitioners stay current, save time and improve workflow on issues that come up after tax filing, such as IRS notices and audits.

The award-winning system includes:

- A system to manage the process - from start to finish
- Guidance on more than 450 IRS notices and counting
- Hundreds of preformatted IRS forms and letters, kept current
- More than 120 audit workpaper templates spanning the four phases of an IRS audit
- The ability to reduce the time your firm spends on IRS issues by up to 50%

The IRS says it will give greater scrutiny to the Earned Income Tax credit for the coming tax year 2012. This comes after a government watchdog questioned the agency on billions of dollars worth of credit it gave out this year. In October, Congress approved an increase of the fine on paid tax preparers for not verifying the eligibility of those who apply for the Earned Income Tax credit from \$100 previously to \$500. The Earned Income Tax credit is the largest form of credit paid out by the IRS each year, amounting to more than \$55.1 billion in 2009, out of which \$11 billion was likely paid out wrongly, according

to IRS estimates.

The Treasury Inspector General for Tax Administration (TIGTA) J. Russell George wrote a stinging report in which he faulted the IRS for making potential improper payments involving two other refundable credit programs, one for higher education and the other for families with children in connection with the Earned Income tax credit. The report indicated that more than \$18 billion of the \$101 billion paid out under the 3 credits could have been done improperly.

The inherent danger in awarding the Earned Income tax credit is that as a refundable credit, it can be paid out in cash in excess of the tax owed, instead of offsetting part of the tax liability. As such, the Earned Income tax credit is always subjected to abuse.

IRS Seeks to Return \$153 Million in Undelivered Checks to Taxpayers; Recommends e-file, Direct Deposit to Avoid Future Delivery Problems

In an annual reminder to taxpayers, the Internal Revenue Service announced today that it is looking to return \$153.3 million in undelivered tax refund checks. In all, 99,123 taxpayers are due refund checks this year that could not be delivered because of mailing address errors.

Undelivered refund checks average \$1,547 this year.

Taxpayers who believe their refund check may have been returned to the IRS as undelivered should use the "Where's My Refund?" tool on IRS.gov. The tool will provide the status of their refund and, in some cases, instructions on how to resolve delivery problems.

Taxpayers checking on a refund over the phone will receive instructions on how to update their addresses. Taxpayers can access a telephone version of "Where's My Refund?" by calling 1-800-829-1954.

While only a small percentage of checks mailed out by the IRS are returned as undelivered, taxpayers can put an end to lost, stolen or undelivered checks by choosing direct deposit when they file either paper or electronic returns. Last year, more than 78.4 million taxpayers chose to receive their refund through direct deposit. Taxpayers can receive refunds directly into their bank account, split a tax refund into two or three financial accounts or even buy a savings bond.

The IRS also recommends that taxpayers file their tax returns electronically, because e-file eliminates the risk of lost paper returns. E-file also reduces errors on tax returns and speeds up refunds. Nearly 8 out of 10 taxpayers chose e-file last year. E-file combined with direct deposit is the best option for taxpayers to avoid refund problems; it's easy, fast and safe.

The public should be aware that the IRS does not contact taxpayers by e-mail to alert them of pending refunds and does not ask for personal or financial information through email.

Such messages are common phishing scams. The agency urges taxpayers receiving such messages not to release any personal information, reply, open any attachments or click on any links to avoid malicious code that can infect their computers. The best way for an individual to verify if she or he has a pending refund is going directly to IRS.gov and using the “Where’s My Refund?” tool.

IRS Under Pressure to Police Refundable Tax Credits

The Internal Revenue Service is under pressure to better police more than \$100 billion of refundable tax credits it issues annually after a government watchdog questioned billions of dollars in payments.

Congress passed in October legislation authorizing a five-fold increase, to \$500, in the penalty for paid tax preparers who don’t verify the eligibility of applicants for the earned income credit, by far the largest refundable tax credit.

Tax filers collected refunds of at least \$55.1 billion in 2009 from the earned income tax credit, and the IRS estimated that more than \$11 billion of that total was issued improperly, sometimes by mistake and sometimes as a result of fraud.

“The IRS is really stepping up enforcement,” Cindy Hockenberry, research supervisor for the National Association of Tax Professionals, said. The initial focus has been on the earned-income credit, but “they’re going to be branching out into other areas,” she said.

The association, based in Appleton, Wis., represents more than 21,000 tax preparers, accountants, attorneys and enrolled agents who work independently or for companies such as H & R Block Inc.

The IRS plans to give earned-income tax credit claims extra scrutiny during the 2012 tax filing season.

Oversight of refundable credits has become a political issue, with Republicans in particular demanding that the IRS do more to weed out ineligible recipients.

“We must balance the mandate to get refunds to those eligible as quickly as possible with ensuring that the money goes only to individuals who are eligible to receive it,” IRS deputy commissioner for services and enforcement, Steve Miller, told a House Ways and Means subcommittee hearing in May.

The earned income tax credit, passed by Congress in 1975 to offset the burden of Social Security taxes for the poor, has been expanded several times with bipartisan support, as an incentive to work.

However, Treasury Inspector General for Tax Administration J. Russell George criticized the IRS’s administration of the EITC and faulted the agency for potential improper payments involving two other refundable credit programs, one for higher education and the other for families with children.

George’s reports indicate that more than \$18 billion of \$101 billion for the three programs may have been improperly awarded.

Unlike a regular tax credit that offsets some or all of a tax liability, a refundable credit can include a cash payment in excess of the tax owed. As a result, refundable credits offer an incentive to defraud the government, George told the House Ways and Means subcommittee in May.

Legislation is pending to narrow eligibility for a refundable child tax credit. In a report in September, George’s investigators found that in 2009 about \$4.2 billion, or 15 percent of \$28.3 billion in additional child tax credits, had gone to people not authorized to work in the U.S.

The IRS declined George’s recommendation to seek more documentation of eligibility. In a statement at the time, the IRS said that the law authorizing the tax credit didn’t explicitly limit recipients to holders of a specific type of identification such as a Social Security number.

The IRS also took issue with George’s findings on the American Opportunity education tax credit, which helps low- and middle-income people pay for college. The credit, part of the 2009 stimulus law, was extended through December 2012 by legislation that also extended the tax cuts enacted under President George W. Bush.

In a report last month, George said 2.1 million taxpayers in 2009 received \$3.2 billion in American Opportunity and other education credits that may have been wrongly awarded. That’s about 17 percent of the \$18.7 billion of such credits distributed by the IRS.

The IRS disputed the findings, with spokesman Terry Lemons saying they were based on “a flawed and superficial analysis.”

IRS Sends Letters to Identity Theft Victims

Dear Taxpayer:

Our records show that you were previously a victim of identity theft. We have placed an identity theft indicator on your account to protect you when you file your federal tax return. We have a new program in place for the upcoming tax year that will help us make sure any tax return we receive with your identifying information is really from you. We will assign you a unique 6-digit number we call an Identity Protection Personal Identification Number (IP PIN) for use with your 2011 federal tax return. It is similar to a PIN for your ATM or bank account and will ensure that no one can file a tax return in your name.

In late December 2011, we’ll mail you a notice with your IP PIN. You’ll need to use this IP PIN when you file your 2011 tax return. If you use a professional tax return preparer or software to prepare your tax returns, you will be instructed on where to include your IP PIN on the returns.

It’s essential that you use your IP PIN when you file your 2011

tax return. Do not lose your IP PIN. If you do, you will only be able to file a paper tax return; you will not be able to E-file. Our walk-in offices and call centers will not be able to provide the IP PIN to you or provide a replacement.

If you have any questions about the IP PIN, please visit www.irs.gov/4868cs for information. You may also call 1-800-908-4490 extension xxxx. Thank you for your cooperation as we continue working to protect your identity and personal information.

Sincerely yours,

Proposed PAL Regs Ease Definition of Limited Partnership Interest, extend it to LLC interests

IRS has issued proposed regs that would provide a new definition of limited partnership interest for purposes of Code Sec. 469(h)(2), which treats limited partnership interests as passive interests for passive activity loss (PAL) purposes except as regs provide otherwise.

At the same time, the proposed regs would make it clear that an interest in a limited liability company (LLC) could be treated as a limited partnership interest for PAL purposes.

Under the Code Sec. 469 passive activity rules, passive activity losses cannot offset nonpassive activity income, such as wages, dividends, or profits from nonpassive activities. Passive activities include the conduct of trade or business activities in which the taxpayer doesn't materially participate and, generally, rental activities without regard to whether the taxpayer materially participates in them. (Code Sec. 469(c) , Reg. § 1.469-1T(e)(1))

Under Code Sec. 469(h)(1), a taxpayer materially participates in an activity only if he is involved in the activity's operations on a regular, continuous, and substantial basis, which generally requires him to meet one of seven tests carried in Reg. § 1.469-5T(a) . Under Reg. § 1.469-5T(a)(4) , one of these seven tests, (1) the activity must be a significant participation activity for the tax year, and (2) the individual's aggregate participation in all significant participation activities during the year must exceed 500 hours. An activity is a significant participation activity only if (a) the activity is a trade or business, (b) the individual participates in the activity for more than 100 hours during the year, and (c) the individual cannot establish material participation under any of the other material participation tests in the regs.

Under Code Sec. 469(h)(2), a limited partner's interest in a limited partnership isn't treated as an interest in an activity in which the taxpayer materially participates, except to the extent provided in the regs. Thus, Code Sec. 469(h)(2) treats losses from an "interest in a limited partnership as a limited partner" as presumptively passive. Reg. § 1.469-5T(e)(2) provides that a limited partner clears the material participation hurdle only if he meets one of three tests (instead of the generally applicable one of seven tests) in Reg. § 1.469-5T(a). The

more-than-500-hour test for significant participation activities in Reg. § 1.469-5T(a)(4) is not one of these three tests.

Reg. § 1.469-5T(e)(3)(i) provides that a partnership interest is treated as a limited partnership interest if:

the interest is designated a limited partnership interest in the limited partnership agreement or the certificate of limited partnership, without regard to whether the liability of the holder of the interest for obligations of the partnership is limited under the applicable state law; or

the liability of the holder of the interest for obligations of the partnership is limited under the law of the state in which the partnership is organized to a fixed amount. For example, state law could limit the liability of the partner to the sum of the partner's capital contributions to the partnership and contractual obligations to make additional capital contributions to the partnership.

However, under Reg. § 1.469-5T(e)(3)(ii) , a partnership interest isn't treated as a limited partnership interest for the individual's tax year if he is a general partner as well as a limited partner in the partnership during its tax year ending with or within the individual's tax year.

Several cases have held that an interest in an LLC is not a limited partnership interest for purposes of Code Sec. 469(h) (2)

Under the proposed regs, subject to an exception noted below, an interest in an entity would be treated as an interest in a limited partnership under Code Sec. 469(h)(2) if:

the entity in which the interest is held is classified as a partnership for Federal income tax purposes under Reg. § 301.7701-3; and

the holder of the interest does not have rights to manage the entity at all times during the entity's tax year under the law of the jurisdiction in which the entity was organized and under the governing agreement. (Prop Reg § 1.469-5(e)(3)(i))

Under the exception, an individual would not be treated as holding an interest in a limited partnership as a limited partner for his tax year if he also holds an interest in the partnership that is not an interest in a limited partnership as a limited partner, such as a state-law general partnership interest, at all times during the entity's tax year ending with or within his tax year (or the portion of the entity's tax year during which he directly or indirectly owns the interest). (Prop Reg § 1.469-5(e)(3)(i))

The preamble notes that Congress enacted Code Sec. 469(h) (2) to address the limitations on a limited partner's ability to participate in the control of the partnership's business. Under the Uniform Limited Partnership Act of 1916, limited partners could lose their limited liability protection if they participated in the control of the partnership.

The temporary regs had been drafted with these constraints in mind. Today, many states have adopted a variation of the Revised Uniform Limited Partnership Act of 1985 (RULPA). Under RULPA, limited partners may participate in the management and control of the partnership without losing their limited liability. As a consequence, limited partners under RULPA are now more akin to general partners and LLC members with respect to their rights in the management of the entity. Under the Uniform Limited Liability Company Act of 1996, LLC members of member-managed LLCs do not lose their limited liability by participating in the management and conduct of the company's business.

Recognizing that the original presumptions regarding the limitations on a limited partner's participation in the activities of the entity are no longer valid today, and also recognizing the emergence of LLCs, the proposed regs eliminate the temporary regs' reliance on limited liability for purposes of determining whether an interest is an interest in a limited partnership as a limited partner under Code Sec. 469(h)(2). Instead, the proposed regs would adopt an approach that relies on the individual partner's right to participate in the management of the entity.

The regs would apply to tax years beginning on or after the date they are finalized. (Prop Reg § 1.469-5(e)(4)).

IRS Modifies Safe Harbors for Ponzi Scheme Victims Claiming Theft Loss Deductions

Rev Proc 2011-58, 2011-50 IRB

In a revenue procedure, IRS has modified the definition of a "qualified loss" in Rev Proc 2009-20, which set out a number of safe harbors for Ponzi scheme victims, to address situations in which the death of a lead figure in a specified fraudulent arrangement has foreclosed the possibility of criminal charges. As modified, qualified investors won't be prevented from using these safe harbors solely on account of the lead figure's death.

In Rev Proc 2009-20, 2009-14 IRB 749, which was issued days after Bernard Madoff's guilty plea, IRS provided several generous safe harbors for qualified investors who were victims of Ponzi schemes (aka "specified fraudulent arrangements" as defined in Rev Proc 2009-20, Sec. 4.01). The safe harbors were designed to eliminate uncertainty about (i) the year of the loss, and (ii) how much was lost (i.e., because of problems in determining how much income that was reported in the scheme was fictitious and how much was real).

IRS Offers Tips in Selecting A Trustworthy Preparer

If you're planning to pay someone to do your taxes this year, the Internal Revenue Service cautions that you should make sure you know who you're entrusting with your records. Although most paid tax return preparers provide honest

and professional service, "there are some unscrupulous tax preparers out there," said IRS spokesman Dee Harris Stepter. "If it sounds too good to be true, it probably is, especially if they tell you they can get a bigger refund than other preparers. That should be a red flag.

"Be very, very careful when choosing someone to do your taxes," she said. "You're turning over all your financial information and Social Security numbers."

Usually, checking with the Better Business Bureau or friends who have used or are going to use a certain preparer is a good way to determine satisfaction, Stepter said. But even that is not always reliable.

Earlier this year, a scam that started along the East Coast moved into middle and southern Mississippi and northern Louisiana and within the past month into New Orleans. Unscrupulous tax preparers approached church ministers and got congregations to agree to allow them to prepare their taxes, giving them access to a large amount of personal identification.

The IRS warns that such scams usually result in the preparers stealing money and personal identity information that can be used in a number of illegal ways.

The taxpayer is legally responsible for any false claims made on a return filed by a paid preparer, Stepter points out, so any penalties for errors come back on the person who hired the preparer.

Another thing to check out, she said, is "how are they safeguarding your records for later?"

Any financial records presented to a preparer should be returned, and the taxpayer should insist on receiving a copy of the return to review before signing and a copy to keep.

The IRS warns that any preparer who suggests signing a blank return should not be trusted. Also, anyone who charges a percentage of the return, instead of a flat fee, is likely unscrupulous.

"Price may not be a good reason for choosing a preparer," Stepter cautions.

"Do your research," she said. "Check out the people" that will have access to your personal records. "Just because they do it part-time at home doesn't mean they're not a good tax preparer," but it's best to find out.

Paid preparers are required to register with the IRS and receive an identification number, known as a PTIN, which must be included on the return form. That's another thing to check for when reviewing a return.

The IRS is implementing a program that will require preparers to pass a competency test, which it says is another way to improve service for taxpayers.

The IRS website (IRS.gov) offers tips on choosing preparers. One of the precautions is “dishonest return preparers can cause big trouble for taxpayers who fall victim to their ploys. These fraudsters derive benefit by skimming a portion of their clients’ refunds, charging inflated fees for return preparation services and attracting new clients by making false promises.”

Stepter said many people with low and middle incomes up to \$59,000 can avoid any risk and file their returns free by using the IRS FreeFile option, which will become active on the website in mid-January.

Thoughts from the Ragin Cajun



How Seniors Can Guard Against Identity Theft

Identity theft continues to be a big problem in the United States affecting around nine million people every year – many are seniors.

Identity theft occurs when someone gets access to your Social Security Number, bank or credit card account number or other identifying information and uses it illegally.

While there is no iron clad protection against ID theft there are some things your Senior can do to minimize their risks. They include:

1. Guard their Social Security Number.
2. Be wary of emails and they should be told not to trust emails from the Social Security Administration or IRS.
3. Secure your mail; taxpayers should empty their mail boxes quickly or get a P.O. Box.
4. Destroy their trash; using a cross-shredder destroy all receipts and documents that identify the taxpayer.
5. Monitor your accounts reviewing monthly bank statements and other statements of accounts.
6. Watch your credit checking your credit accounts with the credit agencies.
7. Set up security freezes with the credit reporting companies to set limits and “stops” on new credit accounts.
8. Take action! Notify the credit reporting companies

and other agencies. Put fraud notifications in place and close any compromised accounts. File a report with your local police department and with the Federal Trade Commission at 877-438-4338. Also, notify the Internal Revenue Service.

Contact the credit reporting agencies at:

Equifax	800-685-1111
Experian	888-397-3742
TransUnion	877-322-8228

Serving Senior Taxpayers is an honor and part of our service must be in helping them keep the security of their identity.

Jerry

Tax Pros in Trouble

Houston Area Tax Return Preparer Pleads Guilty

Eddy Lovely of Tomball, Texas, pleaded guilty to three counts of aiding and assisting in the preparation of false tax returns, the Justice Department and Internal Revenue Service (IRS) announced. Lovely appeared before United States District Judge Nancy F. Atlas in Houston.

According to the plea agreement, Lovely owned and operated a Houston return preparation business, called “The Tax Master,” at which he prepared false income tax returns that included certain false Schedule A itemized deductions that the client did not make and fraudulent Schedule C business losses that the clients did not operate.

After Lovely was indicted in April 2011 on 14 counts of aiding and assisting in the preparation of false tax returns, he persisted in the preparation of false tax returns despite a court order requiring him not to prepare any tax returns while on release in the case. According to the plea agreement, after his release, Lovely aided and assisted in the preparation of materially false 2010 tax returns for two additional clients. These tax returns were materially false in that they featured fabricated Schedule C losses for businesses that the taxpayers did not own or operate, as well as false or inflated Schedule A deductions for charitable contributions and/or job search costs.

The tax loss associated with the three counts to which Lovely pleaded guilty is \$74,964. Lovely faces a maximum prison sentence of nine years and a fine of up to \$750,000. Judge Atlas set sentencing for February 29, 2012.

The case was investigated by IRS-Criminal Investigation and prosecuted by Trial Attorneys Tracy Gostyla and Kathryn Ward of the Justice Department’s Tax Division.

Tax Preparer Sentenced; Stole from Clients

An Avondale tax preparer has been sentenced to 18 months in prison after she pleaded guilty to wire fraud.

IRS investigators discovered that Cecilia Hidalgo, 48, had been stealing money from clients of her own tax return preparation business, La Esperanza Servicios Legales.

Many of Hidalgo's clients had limited English-language skills and were inexperienced about income tax matters, investigators said. For these clients, Hidalgo would prepare two sets of tax returns, one correct return to file with the IRS and another incorrect return with a lower refund amount to show the client, investigators said.

Hidalgo then provided the client with the incorrect return and the lower refund amount, but she filed the correct tax return with the IRS and kept the additional tax refund amount for herself, investigators said.

At sentencing, Judge David Campbell found that Hidalgo stole a total of \$97,728 from her clients, and that she victimized more than 50 different clients during the course of the scheme. The investigation was conducted by the Internal Revenue Service, Criminal Investigations Division.

Kingston Tax Firm Owners Admit to Fraud

The owners of a Kingston accounting and tax preparation firm raided by federal agents in 2010 have admitted to trying to defraud the United States government of hundreds of thousands of dollars in taxes, according to court documents filed.

Christopher Wartella and Jerome Pinkowski, both listed as owners of Broody Associates on Warren Avenue in the state's corporation database, signed the plea agreements in August, but they weren't made public until this week.

Prosecutors said Wartella failed to file tax returns in 2004 and 2005 and prepared fraudulent U.S. income tax forms in 2006, 2007 and 2008 that "substantially understated his taxable income."

All told, Wartella racked up \$441,352 in taxes and obligations, prosecutors said. He will plead guilty to tax evasion and faces a maximum of five years in prison, a \$250,000 fine, up to three years of supervised release and a \$100 assessment, according to court documents.

Wartella has agreed to cooperate with investigators by providing information about the "unlawful activities of others," prosecutors said. Court documents also indicated that because Wartella accepted responsibility for his actions and assisted authorities in the investigation, prosecutors will recommend a sentence at the lower end of the guideline range.

Prosecutors said Pinkowski conspired with Wartella to defraud the government of income and employment taxes from January 2004 until April 15, 2009. Pinkowski prepared

the personal tax returns for Broody Associates employees from 2004 to 2008, prosecutors said.

Pinkowski and Wartella under-reported employee wages to avoid paying income and employment taxes and told clients to "reclassify wages as distributions of income in order to evade the payment of employment taxes," according to court documents.

Pinkowski also allowed employees to charge personal expenses on business credit cards without reimbursement and in April 2008 helped prepare a fraudulent tax return for a client for the year 2007, prosecutors said. The return under-reported wages by about \$21,340 and resulted in the failure to pay about \$5,214 in taxes, according to court documents.

Pinkowski was charged with conspiracy to defraud the United States and with the filing of a false tax return as an aider and abettor. He faces a maximum of eight years in prison, a \$500,000 fine, \$200 assessment and supervised release of up to six years, according to court documents.

While prosecutors acknowledged Pinkowski accepted responsibility for his action, they did not make a recommendation for sentencing as they did for Wartella.

Both men agreed to make full restitution and file all delinquent and amended tax returns by their sentencing date. They also cannot withdraw their guilty pleas if they are dissatisfied with their sentences, according to court documents.

Agents for the Internal Revenue Service raided Broody Associates on April 16, 2010, the day after income tax returns were due to the federal and state governments. They refused to say why they were there, but piled boxes of documents on the porch of the business.

Wartella did not return a phone message left for him at his office, but a woman who answered the phone there said Pinkowski no longer worked with Wartella.

Philip Gelso and Frank Nocito, attorneys for Wartella, declined to comment.

Pinkowski could not be reached for comment. His attorney, Charles Coslett, declined to comment.

New Jersey Law Firm Barred From Preparing Returns

A federal court has permanently barred Carmen Gonzalez from preparing federal tax returns for others, the Justice Department announced. The civil injunction order, to which Gonzalez consented without admitting wrongdoing, was signed by Judge Joel A. Pisano of the United States District Court for the District of New Jersey. According to the government complaint, Gonzalez, of Allentown, Pa., operates Carmen Tax Services in New Brunswick, N.J.

The complaint alleged that Gonzalez repeatedly failed to

comply with due-diligence requirements imposed by federal law on tax preparers who claim the earned income tax credit (EITC) on their customers' returns. According to the complaint, Gonzalez also falsified deductions and listed bogus dependents on her customers' returns in order to claim the maximum EITC for them.

The court order requires Gonzalez to send a letter to all customers for whom she prepared a federal tax return since January 1, 2005, informing them that she has agreed to the injunction and is no longer permitted to prepare tax returns for others.

Gardena Tax Service Owner Gets 15 Months for Filing False Returns

Tax service owner sentenced for filing false returns: The owner of a Gardena tax preparation business was sentenced to 15 months behind bars for filing about 45 bogus returns with the Internal Revenue Service.

Simon Jenkins, owner of Jenkins Tax Service, also was sentenced by U.S. District Judge Stephen V. Wilson to one year of supervised probation when he is released from custody and was ordered to pay about \$240,000 in restitution to the IRS.

Jenkins, 70, of Bellflower previously admitted that during the 2005 through 2009 tax filing seasons, he prepared dozens of tax returns that overstated the amount of one or more claimed items, according to the IRS.

Jenkins acknowledged calculating returns that included false deductions, credits and expenses to obtain larger refunds with the IRS, according to the federal agency.

In his plea agreement, Jenkins admitted that he claimed around \$239,000 for customers, knowing that his clients were not entitled to that much money.

"Today's sentencing should serve as a reminder that all tax professionals must respect the law," said Leslie P. DeMarco of the

Memphis Tax Preparer Gets More Than 5 Years



A federal judge has sentenced a Memphis tax preparer to five years and four months in prison for lying about first-time home buyer tax credits on clients' returns and defrauding the government of more than \$3.4 million.

The U.S. attorney's office said Friday that James Burks ran a

Memphis tax shop named "Money In Your Hand Tax Service." Burks and other preparers falsely included first-time home buyer credits and other tax credits on more than 490 tax returns for 2008.

Burks received a cut of the false refunds by having the Internal Revenue Service electronically deposit part of the refunds into accounts that he controlled.

The IRS paid more than \$3.4 million in refunds that were not owed and deposited more than \$800,000 in illegal refunds into Burks' accounts.

Bakersfield Tax Preparer Pleads Guilty To Presenting False Income Tax Returns

United States Attorney Benjamin B. Wagner announced that Bertha Renell Vaughn, aka Bertha Renell Milton, 41, of Kern County, pleaded guilty today to four counts of aiding and assisting in the presentation of a false income tax return to the Internal Revenue Service.

According to the plea agreement, Vaughn owned and operated Nationwide Tax Solution, also referred to as Vaughn's Tax Service, a tax preparation business in Bakersfield. When Vaughn prepared clients' tax returns, she added fabricated items such as deductions, losses, income, wages, and withholdings that were not claimed by the taxpayers. She did this in order to charge higher fees for the more complicated tax return and also to have the IRS generate a refund to the taxpayer. The indictment alleges that more than 90 percent of the taxpayers using Vaughn's tax preparation services received a tax refund from the IRS.

This case is the product of an extensive investigation by the Internal Revenue Service, Criminal Investigation. Assistant United States Attorney Jeremy R. Jehangiri is prosecuting the case.

Vaughn is scheduled to be sentenced by United States District Judge Anthony W. Ishii on February 6, 2012. Vaughn faces a maximum penalty for each count of three years in prison, a \$250,000 fine, a period of supervised release, and restitution. The actual sentence, however, will be determined at the discretion of the court after consideration of any applicable statutory factors and the Federal Sentencing Guidelines, which take into account a number of variables.

Columbus Tax Preparer Sentenced to 33 Months for Fraud Charges

A Columbus man who plead guilty to 25 counts of tax fraud has been sentenced to 33 months in prison.

Gregory Carter changed his plea from not guilty to guilty in court back in June. He admitted to preparing fraudulent tax returns while he worked at Tax One on Buena Vista Road. Many of the fraudulent reports were filed for first time home buyer tax credits.

Carter's indictment was originally handed down in October of 2010 after the IRS raided the Tax One business in 2009. The IRS raid was part of an investigation which saw the IRS sue a total of 7 tax preparation companies across five states. After his 33 months in prison, Carter will be on a 1 year supervised release and will have to pay \$245,572 in restitution.

Taxpayer Advocacy & Tax Professionals

IRS Can Summons a Taxpayer's Original Electronic Data Files to Obtain Associated Meta Data

Chief Counsel Advice 201146017

In Chief Counsel Advice (CCA), IRS has explored a number of issues concerning its ability to summon a taxpayer's original electronic data files or the backup files (referred to here as "original electronic data files") to obtain the associated meta data (data on data, including such information as who, when, and how the information was created).

IRS may examine "books, papers, records or other data," for purposes of ascertaining the correctness of any return, making a return if none has been made, determining the tax liability of any person, and collecting that liability. (Code Sec. 7602(a) (1)) IRS may issue a summons to the taxpayer or certain third parties that it feels may be able to assist in determining the taxpayer's tax liability. (Code Sec. 7602(a)(2))

To have a summons enforced, IRS must make a four-step prima facie showing that: (1) the investigation will be conducted pursuant to a legitimate purpose; (2) the inquiry may be relevant to the purpose; (3) the information sought is not already within IRS's possession; and (4) the administrative steps required by the Code have been followed. (U.S. v. Powell, (1964, S Ct) 14 AFTR 2d 5942)

Generally, meta data is information that describes how, when, and by whom a particular item or set of electronic information was collected, created, accessed, modified, and formatted. Taxpayers may keep their business records electronically with meta data automatically created as an integral part of the records. Often, IRS's examinations would be advanced by accessing meta data that identifies the original date a transaction was entered in the electronic records, the dates of any changes to the entries, and the username of the person who made the entries. The value inherent in an examiner's ability to obtain the date and source of recorded entries is self-evident: the information tends to support or undermine the credibility of the entries in the business records.

The CCA looked at several scenarios involving issues related to meta data to determine the reach of IRS's summons power. It concludes that, while not unlimited, IRS's power to obtain meta data is indeed broad.

Can an IRS examiner summon a taxpayer's original electronic data files to obtain the associated meta data if the taxpayer offers to provide either paper printouts (e.g., spreadsheets) or a truncated or an altered copy of the data files that don't contain the meta data?

The CCA concluded that as long as the information in the meta data "may be relevant," within the broad Code Sec. 7602(a)(2) , to a proper purpose for which the examination is being conducted—such as ascertaining the correctness of the return—IRS may properly summon the taxpayer's original electronic data files containing the unaltered meta data. The CCA found that it was readily apparent that the phrase "books, papers, records, and other data" in Code Sec. 7602 was more than broad enough to encompass the compelled production of the meta data associated with electronic documents. It was also apparent that meta data associated with a taxpayer's electronic business records "may be relevant" because the nature of the information contained in the meta data, especially the dates on which the entries were made or modified and the identities of the persons entering the data, may support or undermine the credibility of the records offered to substantiate the accuracy of the return.

In addition, the taxpayer's offer to provide or actual production of copies that omit the meta data didn't restrict IRS's authority to summon the original, unaltered meta data. IRS was entitled to summon the original documents, even though it possessed copies. The original meta data associated with the electronic records could assure the accuracy of the documents reproduced.

Can an examiner summon the taxpayer's original electronic data files to obtain the recorded entries and associated, unaltered meta data for transactions that occurred before or after the periods being examined if the taxpayer offers to provide a copy of the data file showing only the recorded entries without the meta data for transactions that occurred during the periods being examined?

The CCA determined that when summoned information dates from a period outside of those being examined, IRS must be prepared to answer the question of why such information may be relevant to the periods being examined. As with any other summoned information, it was enough that the records sought might throw light on the tax inquiry at issue. So long as IRS could demonstrate the potential relevance of the meta data associated with the records, the meta data should be obtainable by summons.

Can IRS summon the taxpayer's original electronic data files from the taxpayer's accountant if the accountant recorded the entries of the business transactions into the electronic file and possesses the records?

The CCA determined that IRS can summon a third-party witness, such as the taxpayer's accountant, to give testimony or produce information that may be relevant to the examination, including electronic data files and the associated unaltered meta data.

If a taxpayer provides IRS with an electronic data file on a CD or a thumb drive, must the examiner retain the original CD or thumb drive in the examination case file? Alternatively, may the examiner make an electronic copy of the file and include it in the examination file if the case is closed unagreed and the data file supports the examiner's conclusions (or the data file contains information that may be relevant to a separate criminal investigation)?

In any case in which a taxpayer voluntarily (i.e., without a court order) provides IRS with an electronic or paper copy of its books and records, the taxpayer can require IRS to return the original copy. Accordingly, the CCA advised that, upon receipt of the CD or thumb drive, the examiner should immediately copy the electronic records for inclusion within the examination file to avoid being forced to prematurely relinquish the only available copy. See Internal Revenue Manual §25.5.4.3(2) (advising examiners to immediately copy records upon receipt). The CCA warned that the only caveats to this approach lie in the restrictions and safeguards codified in Code Sec. 7612(c) for copying any software, including the computer software source code and the executable code.

Do the Federal Rules of Civil Procedure and the case law under it offer analogous support for summoning electronic records with intact meta data?

The CCA noted that Fed. R. Civ. P. Rule 34(a)-(b) specifically addressed the production of electronically stored information, including meta data. Recent case law supported the proposition that Rule 34 generally requires electronically stored information to be produced in the specified form or forms in which it was requested. (see *Genetically Modified Rice Litigation*, (E.D. Mo. June 5, 2007) 2007 WL 1655757) If a request does not specify a form for producing electronically stored information, then the information must still be produced in the form or forms in which it was ordinarily maintained or in a reasonably usable form or forms. The case law supported the required production of meta data associated with electronic records, when the specifically requested form included such meta data or when the meta data was necessary for the requested information to be reasonably usable under the circumstances.



Tax Professionals and Conflict of Interest

conflict of interest n. a situation in which a person has a duty to more than one person or organization, but cannot do justice to the actual or potentially adverse interests of both parties. This includes when an individual's personal interests or concerns are inconsistent with the best for a customer, or when a public official's personal interests are contrary to his/her loyalty to public business. An attorney, an accountant, a business adviser or realtor cannot represent two parties in a dispute and must avoid even the appearance of conflict. He/she may not join with a client in business without making full disclosure of his/her potential conflicts, he/she must avoid commingling funds with the client, and never, never take a position adverse to the customer.

The National Taxpayer Advocate has released its 2007 Annual Report to Congress in IR 2008-4. The Advocate highlights the issues raised by newly amended Code Sec. 6694, the return preparer's penalty, and how it may affect the way tax preparers dispense advice. The Report says that new standard may, in some cases, lead to conflicts of interest between preparers and their clients.

Section 10.29 of Circular 230 Federal Code of Regulations Under Title 31 regulating the practice of Tax Professionals states "a practitioner should not represent a client...before the IRS if the representation involves a conflict of interest.

The procedures outlined in Circular 230 address the issue of "potential of conflict of interest". Once the potential for conflict is identified, the tax professional is required to notify the taxpayers involved in the potential conflict. If the taxpayers continue to want the tax professional to represent them, knowing of the potential for conflict, the taxpayers must each sign an acknowledgement, retained by the tax professional, stating they are aware of the potential of conflict and continue to want the tax professional to represent them.

To have a potential for conflict, two or more taxpayers must be represented but this is not just isolated to married or divorced taxpayers. Two related taxpayers could be a Partnership and the Partners, a Corporation and its shareholders, an Estate

or Trust and the Beneficiaries or Executor (trix) and Trustee.

A consideration for each tax professional is whether even with the written authorization of the taxpayers involved whether the potential of conflict would allow the zealous representation of both taxpayers.

Tax professionals must reconcile their obligations and their duties to zealously represent each taxpayer with whether they should recuse themselves from representing either or both taxpayers.

Wayne

Sponsor of the Month

Do not go into this tax filing season without Errors and Omissions Insurance – John Haugner will work for you to get you the best coverage and rate for your insurance needs.

Professional Liability Insurance for Tax Preparers from Target Insurance Services

**John Haugner, (262) 965-2441
or email jhaugner@wi.rr.com**

Tax Quotes

“How is a mugger different from the Internal Revenue Service? Both take your money, but the mugger doesn’t make you fill out forms.”

Jacob Sullum in Reason

“More than ever before, Americans are suffering from back problems: back taxes, back rent, and back auto payments.”

Robert Orben

“Taxation with representation ain’t so hot either.”

Gerald Barzan, humorist

“The term “tax humor” is no doubt an oxymoron to many people; to the more cynical, it is an apt description of the entire tax code.”

John F. Iekel

“You must pay taxes. But there’s no law that says you gotta leave a tip.”

Advertisement

“It’s income tax time again, Americans: time to gather up those receipts, get out those tax forms, sharpen up that pencil, and stab yourself in the aorta.”

D. Barry

“The wages of sin are death, but by the time taxes are taken out, it’s just sort of a tired feeling.”

Comedian

“A fool and his money are soon parted. It takes creative tax laws for the rest.”

C Bob Thaves

“Worried about an IRS audit? Avoid what’s called a red flag. That’s something the IRS always looks for. For example, say you have some money left in your bank account after paying taxes. That’s a red flag.”

Jay Leno

“Why can’t Americans do their own taxes? Because the federal Tax Code is out of control, that’s why. It’s gigantic and insanely complex, and it gets worse all the time. Nobody has ever read the whole thing. IRS workers are afraid to go into the same ROOM with it.”

Dave Barry

Next Edition of Taxing Times: February 1st, 2012