MARCH/APRIL 2023 VOL.41 NO.2

THE NATIONAL ASSOCIATION of ENROLLED AGENTS

EA JOURNAL

Exploring Tax Resolution Options

Story of a Worker Classification Case / Election Results / Inflation Reduction Act of 2022

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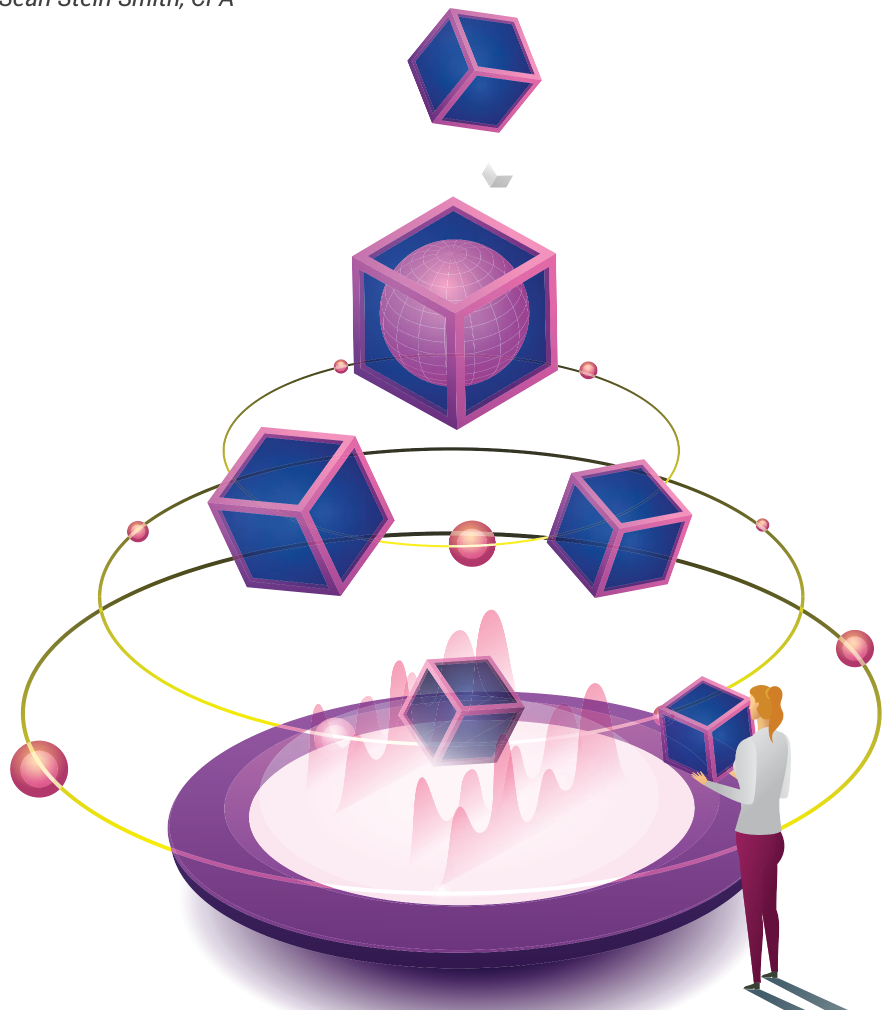

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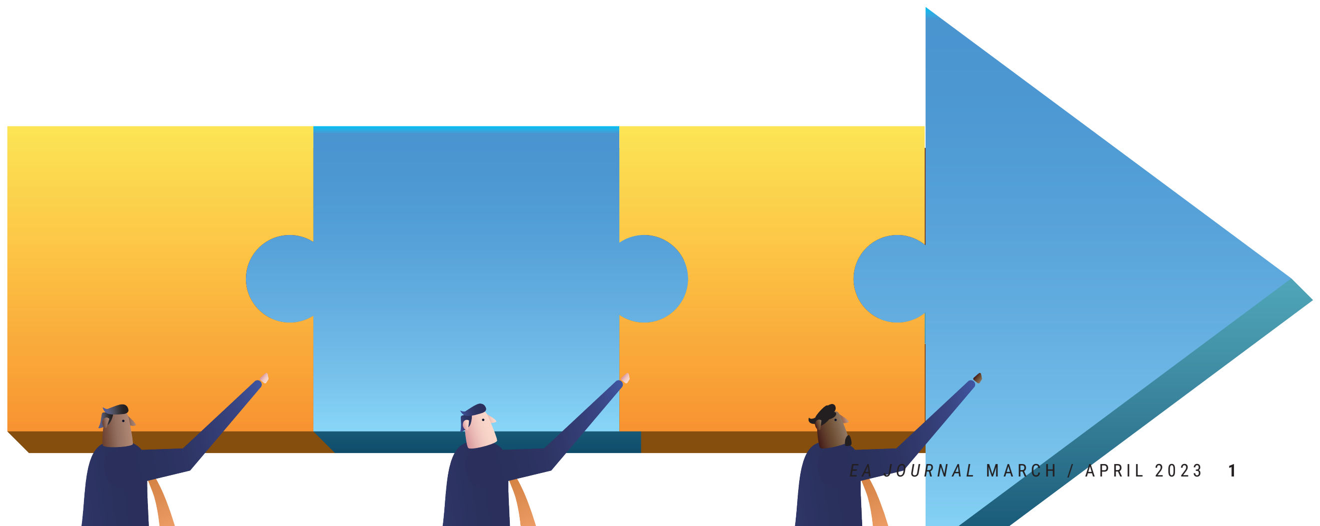

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If Anyone Is Familiar with Change, It Is NAEA Members

Tynisa (Ty) Gaines, EA (She/Her)

I am so very pleased to assume the position of editor-in-chief of the *EA Journal*. The *EA Journal* is an award-winning publication that provides expertise and insight on tax topics. It is an important part of National Association of Enrolled Agents' (NAEA) member services and serves as a vehicle to share thought leadership on the profession and features on NAEA members and activities.

Because the *EA Journal* is such a valued and respected publication, it is critical that we continue to ensure its ongoing success. That is why there will be some changes coming to the journal in 2023. This issue will mark the final bimonthly issue of the journal. The publication timeline will change from one issue every two months to one issue every quarter.

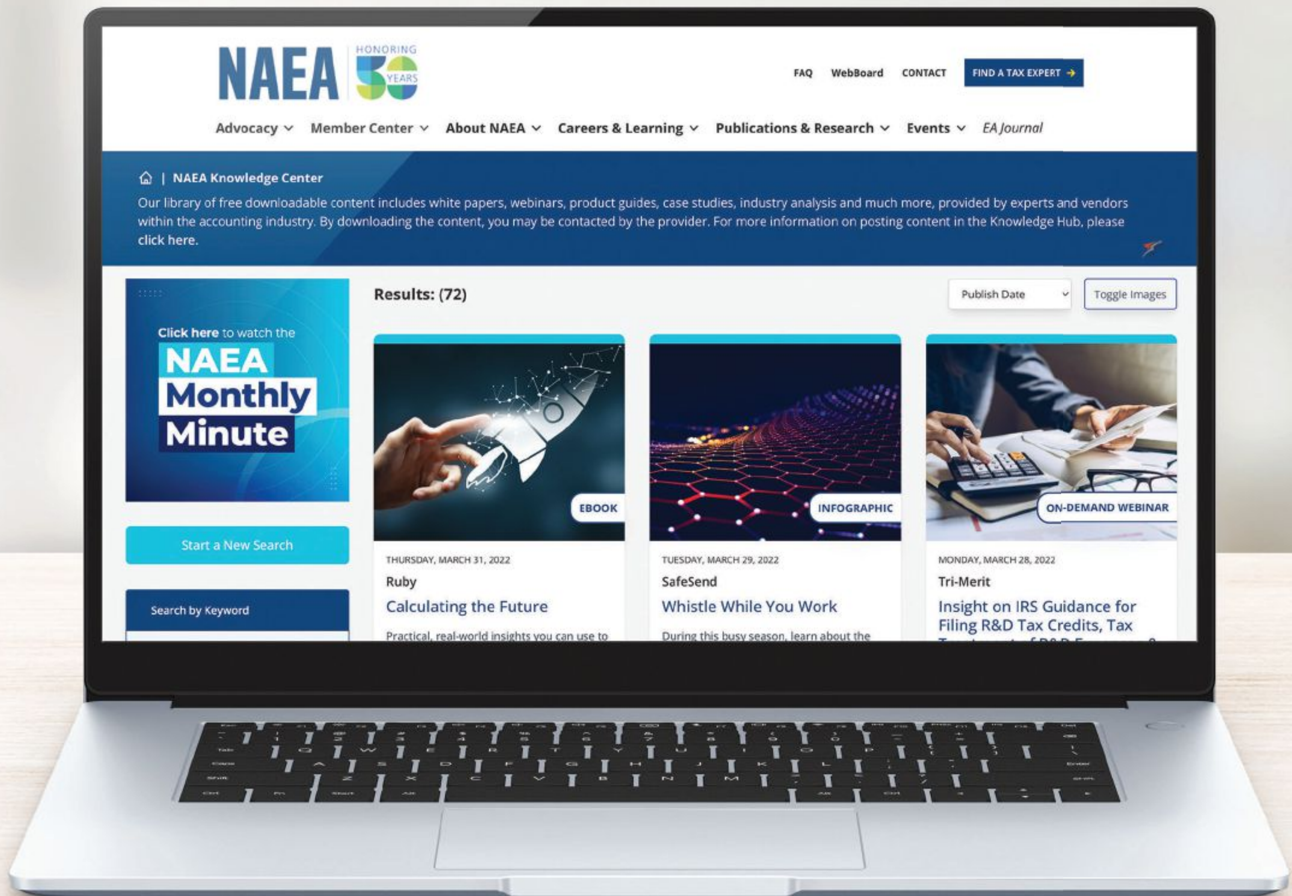
As with many print publications these days, the journal is competing with online sources for content, advertising, and readership. Increasing production costs and less advertising has had a negative impact on our economics. Reducing the frequency of the publication allows us more time to source relevant articles and subject matter experts and enhance the content of the journal by increasing the number of articles in each issue and expanding the number of continuing education (CE), as well as the inclusion of more nontechnical topics that are important to our readers. The technical pieces of the journal will remain, as will the test that so many of you utilize for your continuing education. The result of these changes will be a more robust publication that is less costly to produce and will remain a mainstay of NAEA services.

The result of these changes will be a more robust publication that is less costly to produce and will remain a mainstay of NAEA services.

I would like to thank Tom Gorczynski for his time as editor-in-chief. I was a member of the journal's inaugural editorial board, and I am honored to assume this responsibility from him and continue the great work he has done over the past few years.

Introducing

NAEA Knowledge Center



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What a Ride!

Kathy Brown, EA

I never would have dreamed when I arrived in Washington, DC, in 2008 to attend the National Association of Enrolled Agents (NAEA) Fly-In Day, that I would someday be the NAEA’s president. It was my first NAEA event. The first of many NAEA experiences that I look back on fondly as I write my last president’s column.

The organization has had its challenges, but I believe we’ve grown stronger and wiser. We are ready for new challenges and opportunities in the future. Most leaders strive to leave a place better than how they found it. This is not accomplished by just one individual, but a group of dedicated members who also strive towards that goal.

Most leaders strive to leave a place better than how they found it. This is not accomplished by just one individual, but a group of dedicated members who also strive towards that goal.

To quote part of NAEA’s strategic plan, *“NAEA is a home to a vibrant community of tax professionals who want to thrive and make a difference in their client’s lives. NAEA provides a collaborative space where members come together to help each other succeed and grow wherever they are in their professional journey.”*

While there have been many changes, there is one thing that remained a constant throughout my NAEA leadership journey – the members. Their enthusiasm and their support have been unwavering. I have never asked another member for advice or help and been turned down. Their mentorships have been invaluable to me as a leader, as a tax professional, and as a business owner. And their friendships have been priceless.

I have grown both professionally and personally since becoming a member of the NAEA, not only from the volunteering opportunities I’ve experienced, but also by meeting so many amazing enrolled agents (EAs) along the way who generously offer a hand whenever I’ve asked. The members that I have met along the way have helped mold the person I am today. NAEA’s membership community is like no other. We are members, volunteers, leaders, coaches, and most importantly, friends.

We are pleased to offer NAEA members and guests access to our monthly Tax Experts' Corner™ series of continuing education courses, curated for enrolled agents and tax professionals. Each course qualifies for 3 IRS CE hours and is offered to you at a 10 percent discount through NAEA (discount applied at checkout).

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Come for the CE, Stay for the Community

Megan Killian

I recently put out an SOS for assistance from our members. It was the beginning of tax season, and I knew it was a big ask. But I was in a bind, and it was something that only a tax expert could help with. Several members came to my aid, and they did it quickly and without complaint. This was really no surprise. Whether they are answering questions on the Web Board, serving as volunteers on committees, speaking at events, leading state affiliates, or, in this case, providing a tax novice like me with some technical assistance, National Association of Enrolled Agents (NAEA) members are very generous with their time and expertise.

This network of enrolled agents is one of the best benefits of being part of the NAEA. Membership gives access to thousands of tax experts who specialize in all areas of tax preparation and representation.

> Several members came to my aid, and they did it quickly and without complaint. This was really no surprise.

The NAEA Web Board is one place where our members provide invaluable assistance all year long. There were more than 20,000 discussions started in 2022, and more than 97,000 replies. This is an 8 percent increase in activity over the same time in 2021.

Christine Neubauer of Maryland sent me an email that said:
"The NAEA member forum is a lifeline for me. I am grateful for all of the members who offer their time in answering questions. Patrick Dimmitt takes the time to cite references which just saved my bacon, proverbially speaking."

If you haven't been on the Web Board in a while, you should know that it received a makeover a couple months ago and has a modernized look, additional features, and updated code of conduct. The enhanced search engine allows you to search through past posts, and you can use the directory to find and send a direct message to any NAEA member.

Creating and fostering a safe and reliable space for assistance is the responsibility of all of us who engage with the NAEA. For most successful online communities, being informative is essential, but being kind and courteous is just as important. As with all NAEA virtual participation, the adage remains true: "If you have nothing nice to say then don't say anything at all." I mean, after all, this isn't Twitter!

Take Note

Officers: Will serve a one-year term, beginning May 2023
- Cynthia Leachmoore, EA – President
- Twila Midwood, EA – President-elect
- Edward Ryan, Jr., EA – Treasurer

Directors: Will serve a two-year term, beginning May 2023
- Leslie Casteel, EA
- Kesha Dawson Harris, EA
- Julia Harvey, EA
- Dannie Lynn Murphy, EA
- John M. Perry III, EA, USTCP

The installation ceremony will take place on May 19, 2023. Registration details are available at www.naea.org.

2023 Calendar Dates

March 9
Webinar
March Solutions Room: S Corporation Basis Rules and Form 7203

March 30
Webinar
March Virtual Roundtable

April 6
Webinar
April Solutions Room

April 27
Webinar
April Virtual Roundtable

May 19
Board of Directors Installation Ceremony
Washington, DC

May 23–24
Capitol Hill Fly-In
Washington, DC

July 29–August 1
Tax Summit
Scottsdale, Arizona

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We understand how taxing taxes can be for our members. Take a moment for yourself to explore our wellness resources–including articles, music playlists, yoga activities, meditation, and more to support a thriving mind, body, and spirit. Visit **www.naea.org/taxprowellness.**

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The NAEA Education team is excited to announce that the very first all-access pass to the NAEA On Demand CE Library is now available for purchase! This new CE subscription will provide you with access to our on-demand library and *EA Journal* exams good for the year of 2023.* Choose from 150+ CE on a variety of topics including ethics, tax updates, and tax preparation. **Purchase your subscription today!**

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NAEA 2023–2024 Board of Directors

We are excited to welcome the following members to the board of directors of the National Association of Enrolled Agents (NAEA). Get to know this incoming group of hard-working, dedicated volunteers who are leading the NAEA in the 2023–2024 membership year.

PRESIDENT
Cynthia Leachmoore, EA
Soquel, California

Q: What do you do to relax?
A: Hike, succulent and cactus gardening, write music, and create organic skin care products

Q: Do you have any secret talents?
A: I am a former concert flutist.

Q: What was your first job?
A: McDonalds

PRESIDENT-ELECT
Twila Midwood, EA
Rockledge, Florida

Q: What do you do to relax?
A: Garden

Q: What motivates you?
A: My family

Q: What was the last book you read?
A: *Where the Crawdads Sing*

SECRETARY
Jennifer MacMillan, EA
Manitou Springs, Colorado

Q: What motivates you?
A: Anything that brings laughter and joy.

Q: What is your go-to snack?
A: Almonds, Fritos

Q: What was your first concert?
A: Dave Mason at the Santa Barbara County Bowl

TREASURER
Edward Ryan, EA
Rutherford, New Jersey

Q: What motivates you?
A: Helping clients meet their goals.

Q: What was your first concert?
A: The Who

Q: Star Trek or Star Wars?
A: Star Trek

IMMEDIATE PAST PRESIDENT
Kathy Brown, EA
Florence, Kentucky

Q: What motivates you?
A: Helping others - I love to see others succeed, especially our youth.

Q: Do you have any secret talents?
A: I am a clogger. I started years ago for the exercise and had the opportunity to perform in some amazing venues. My group was the opening act for many famous folks such as Reba McEntire and Clay Walker.

Q: What was your first concert?
A: Rick Springfield - still one of my favorites. I used to say I was going to marry a 6'0" Rick Springfield in cowboy boots.

DIRECTOR
Geri Bowman, EA
Mogadore, Ohio

Q: What motivates you?
A: The people in my life. They all motivate me to be the very best version of me.

Q: What's your go-to snack?
A: Doritos

Q: What was your first job?
A: Dairy Queen

DIRECTOR
Leslie Casteel, EA
Knoxville, Tennessee

Q: What motivates you?
A: Helping people

Q: What was your first concert?
A: Chicago – "Hard for Me to Say I'm Sorry" Tour

Q: What was your first job?
A: Federal Deposit Insurance Corporation (FDIC) liquidation specialist

DIRECTOR
Kesha Dawson Harris, EA
Orlando, Florida

Q: What motivates you?
A: Progress motivates me. If there is something that will progress me forward in life, I want to be a part of it.

Q: What is your go-to snack?
A: Hot Tamales and Peanut M&Ms

Q: What was your first job?
A: Ride operator at Enchanted Village in Federal Way, Washington

DIRECTOR
Susie DiMaggio, EA
Ventura, California

Q: What do you do to relax?
A: I love to lay around the pool and read or sit at the beach and watch the waves.

Q:What was your first concert?
A: Fleetwood Mac

Q: What was the last movie you watched?
A: "Encanto" with my granddaughter

DIRECTOR
Julia Harvey, EA
Vero Beach, Florida

Q: What motivates you?
A: I have a thirst for knowledge.

Q: Star Wars or Star Trek?
A: Star Wars

Q: What was your first job?
A: Waitress

DIRECTOR
Koreen Jervis, EA
New York, New York

Q: What do you do to relax?
A: I read and play word games.

Q: What was your first concert?
A: Mariah Carey in Atlantic City

Q: What was the last book you read?
A: *The Snow Leopard*

DIRECTOR
Michelle Lonsway, EA
Palm Bay, Florida

Q: What motivates you?
A: Healthy competition

Q: Do you have any secret talents?
A: Yodeling, baking

Q: What was your first job?
A: Babysitting

DIRECTOR
Michael Lawrence, EA
Jordan, New York

Q: What is your go-to snack?
A: Coffee

Q: What was your first concert?
A: James Taylor in 1968

Q: What was your first job?
A: Milking cows

DIRECTOR
Dannie Lynn Murphy, EA
Seattle, Washington

Q: What do you do to relax?
A: Reading, rowing, and traveling

Q: What's your go-to snack?
A: French burnt peanuts

Q: What was the last book you read?
A: *The Courtiers*

DIRECTOR
John M. Perry III, EA, USTCP
Oklahoma City, Oklahoma

Q: What motivates you?
A: Injustice

Q: Do you have any secret talents?
A: I sharpen knives.

Q: What was your first concert?
A: Simon and Garfunkel

Success or Failure at the IRS: What Will Make the Difference?

Charles O. Rossotti

For the first time, Congress has provided substantial long-term funding for the IRS. The unprecedented rebuilding program, which includes $80 billion of IRS funding over 10 years under the Inflation Reduction Act (IRA, P.L. 117- 169),[i] provides a once-in-a-century opportunity to restore a depleted IRS. It also presents serious risks for the Biden administration and the U.S. tax system if it fails.

What will make the difference between success and failure?

Appointing a Qualified Commissioner
To achieve success, the IRS needs a highly qualified, Senate-confirmed commissioner to lead it. The administration has taken the first step by nominating Daniel Werfel — an accomplished and experienced executive. It is critical for Congress to confirm him this year so that he can take the helm as well as ownership of the rebuilding program that Congress has funded. Until this position is filled, the entire rebuilding program is at serious risk of failure.

Congress has long recognized that implementing major change at the IRS requires a commissioner who can make hard management decisions. In 1998 it specified that the IRS commissioner appointment "shall be made from individuals who, among other qualifications, have a demonstrated ability in management."[ii] Congress also recognized that it takes time to make important changes and therefore provided a five-year term for the commissioner.[iii] Now it is important for the Senate to deliver what Congress itself demanded — a qualified commissioner confirmed for a five-year term.

Increasing Performance
When the new commissioner is in place, his major challenge will be improving the IRS's performance.

Congress has provided funds — and in a narrow accounting sense, the IRS has to say how it will spend the money. But that accounting exercise is not a strategy for making investments that will enhance operations. Only clear, regular improvements in the performance of the agency's mission will allow the new commissioner to win the confidence of the public and Congress. Money alone will not make that happen.

The risk is that the IRS will just do a little bit more of everything it is doing today. But that will not work, because despite many misleading statements about massive increases in the size of the agency, the new funding (even after 10 years) will bring the IRS to only about 75 percent of its size relative to the economy that it was in the 1990s.[iv]

Since I was the commissioner, I know that even then, the IRS's service to the public was inadequate, and the tax gap (taxes owed but not paid) was too big and growing.

Unless performance improves markedly, the IRS could end up 10 years from now having spent a lot of money to accomplish only marginally more. And without clear progress along the way, the rebuilding program will likely be declared a failure before the 10 years is up.

To realize the results that Congress and the public expect from the increased funding, strong and consistent

leadership will be essential to making and executing complex decisions in five key areas:

- setting strategic performance goals;
- setting rigorous priorities;
- organizing for results;
- defining and implementing effective compliance strategies; and
- communicating effectively with external and internal stakeholders.

Setting Strategic Performance Goals
Strategic performance goals are a statement of how the IRS will improve the way it serves all taxpayers.

These goals should be carefully and clearly defined to guide action that leads to measurable progress in the IRS's mission. The two essential strategic performance goals for the agency are (1) service: making every taxpayer interaction a high-quality, efficient one; and (2) compliance: increasing voluntary and enforced compliance to reduce the tax gap.

The IRS has a lengthy list of responsibilities and activities, such as protecting taxpayer data, hiring and training a diverse and competent workforce, and accounting for large sums of money from millions of taxpayers. Performing these activities should be thought of as the minimum required table stakes. They must be done, but they are not what drives the agency forward.

All interactions with taxpayers should be high quality and efficient, both in content and delivery method. The service goal should therefore include improving all forms of taxpayer interaction, not just routine inquiries such as when a refund will be paid or how to fill out a tax form.

The IRS receives separate appropriations for service and enforcement. Many taxpayer interactions (and some of the most important) occur as part of activities such as audits and collections that are funded by the enforcement appropriation. The IRS has approximately 677 million interactions with taxpayers every year through various channels, including correspondence, phone calls, and online transactions. About 175 million of these interactions are outbound notices from the IRS, many of which are part of an IRS enforcement program.[v]

In her report to Congress for 2018, National Taxpayer Advocate Nina Olson noted, "The IRS mailed over 175 million notices in fiscal year (FY) 2018, making notices one of the most frequent interactions between taxpayers and the IRS."[vi] In many cases, notices are the primary form of communication from the IRS to taxpayers concerning matters that have a significant effect on taxpayers' lives. The report also said, "In the three Most Serious Problems that follow, the National Taxpayer Advocate expresses concerns about IRS notices that fail to adequately inform taxpayers about their rights, responsibilities, and procedural requirements."[vii] The report recommended that the IRS use research to redesign its reports to be

more understandable and useful to taxpayers. As of this writing, none of these recommendations have been implemented.[viii]

The goal for improving all taxpayer interactions will require completely rewriting the content of notices to be clearer and more modern, with highly specific explanations of issues concerning taxpayer returns and data, and with links to references and accounts when appropriate.

These communications should provide taxpayers with a range of options for responding to the IRS, including the use of self-service accounts and secure online communications.

The compliance goal should be to reduce the tax gap by using a range of methods, many of which depend on the use of data and technology. Enforcement itself is not a goal, but it is one tool for achieving compliance.

This way of thinking is critical because just scaling up traditional audits will be inadequate. Even doubling the return from audits would reduce the tax gap over 10 years by less than 2 percent. That is 80 percent less than even the conservative estimates made by the Congressional Budget Office.[ix]

A key part of setting performance goals is to establish meaningful ways of measuring actual progress. What is not measured will almost never get done, and faulty measures can cause not only waste but real damage.

Congress recognized the importance of setting and measuring performance goals by twice passing the Government Performance and Results Act, most recently in 2010. Unfortunately, it is all too easy for this requirement to become merely a formal exercise, or to go awry and drive counterproductive behavior, as it did in the mid1990s when inappropriate enforcement goals were rolled out for the IRS.[x]

Serious work needs to be done in the IRS to develop indicators of actual progress for improving service in all taxpayer interactions and meaningfully reducing the tax gap.

The key guideline is to develop measures that are roughly right rather than precise but wrong, meaning that they indicate actual progress toward strategic performance goals even if they measure only partial results or do so imperfectly. By contrast, spending money and tracking activities like the number of audits are not adequate ways to measure progress on strategic goals.

As examples, measures of progress on the quality of taxpayer interactions can include traditional ones, such as telephone answering, but should also include measures of the results of those interactions, like whether a question was answered correctly or a problem was resolved. Answering a phone call in 10 seconds is good but not if it provides no useful answer to the taxpayer's question. Taxpayer feedback through short surveys is essential.

General measures of compliance should be done more frequently than in past compliance studies, the latest one of which was just issued for the years 2013-2016. In the interim, more frequent metrics on trends in key areas of noncompliance, such as for particular sources and kinds of business income, should be developed. In compliance reporting, indicators of trends in areas of noncompliance are more important than absolute metrics.[xi]

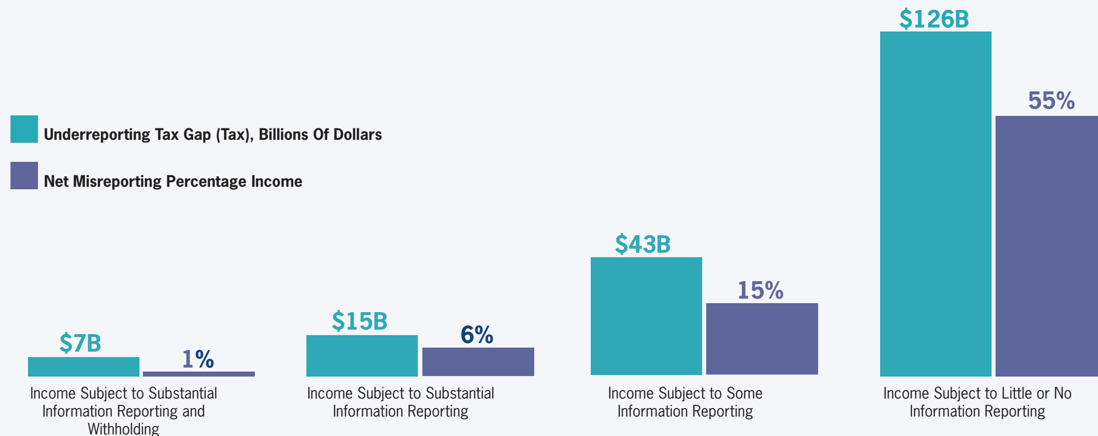
Setting Rigorous Priorities

The IRS needs to set rigorous priorities for action programs that clearly and timely make progress toward the performance goals, integrating technology into almost every program.

Making progress toward goals requires careful planning to break down long-term goals into practical projects that can be implemented and evaluated in reasonable periods, usually measured in months rather than years. Defining priorities requires strong leadership to allocate limited staff and financial resources to achieve the best results while managing risk. In the absence of rigorous decision-making, too many projects are likely to be approved, diluting resources and management attention and resulting in delays or outright failures. Still another risk is that projects will be defined too broadly with long time frames for implementation.

For example, projects already underway to improve taxpayer interaction include callbacks, secure electronic access to taxpayer accounts, self-service account updates for specified items (even including installment agreements), and secure electronic communication between IRS employees, taxpayers, and practitioners — all of which depend on technology. The technology to accomplish these initiatives is widely available but deploying them effectively at the IRS is a complex endeavor that includes training agency employees and communicating effectively with the public.

The elimination of most remaining paper filings is an essential part of improving the taxpayer experience as well as increasing efficiency at the IRS. Several techniques are available and have been recommended repeatedly over time, such as requiring barcoding on returns



produced on computers and submitted on paper. This recommendation was first proposed by the national taxpayer advocate in 2004.[xii]

The plan to accomplish this goal needs to incorporate available technology; include regulatory considerations; provide for consultation with taxpayers, practitioners, and tax software providers; and be implemented in well-defined steps.[xiii]

Organizing for Results

The IRS needs to make clear assignments of responsibility for the execution of priority programs.

At the top level, a governance process needs to be established that can make timely, firm decisions on a host of issues. This includes conflicts in priorities, competition for resources, and technical, procedural, or regulatory problems that always arise in the execution of change programs. Vetting important decisions with input from all key parts of the IRS will lessen the risk of major and expensive setbacks, such as those that recently occurred in the IRS's well-intentioned but flawed implementation of a project to provide more secure taxpayer online identification.[xiv]

Effective governance of the IRS rebuilding program will also require difficult decisions to adjust or even cancel initiatives that may not be achieving their goals. No major improvement program achieves success in every initiative, and it is normal and necessary to make those adjustments.

Improving performance also means changing long-established ways of doing business. Key leadership positions will have to be filled with individuals from inside and outside the IRS who are committed to improving the way the agency operates its core service and enforcement activities to reach performance goals. I believe that it is possible to recruit highly talented individuals for the IRS by stressing the unique opportunity that exists to rebuild one of the foundations of the American government — our tax administration system.

In most cases, the work to implement priority programs should be done by integrated teams that include legal, tax, data science, technology, and communication experts, all led by an empowered executive. They should usually include individuals with frontline experience who can provide a practical perspective on how the changes will work in the field.

IRS technology management will have to develop plans for executing longer-term technology renewal projects, such as the replacement of IRS master files. This decades long technology effort should not and need not impede near-term business improvement projects that also depend on deploying technology. Almost all large organizations have the problem of old but essential legacy systems that need to be replaced over time, but they do not and cannot allow them to undermine progress on necessary business improvements.[xv]

Effective Compliance Strategies

The IRS needs to define and implement compliance strategies that make far better use of data and technology to drive and support more productive enforcement actions and encourage voluntary compliance.

The tax gap has grown to over $600 billion per year. If nothing further is done, this loss will accumulate to more than $7 trillion over 10 years — considerably more than all the income taxes paid by 90 percent of all individual taxpayers.[xvi] About $140 billion per year of this lost tax revenue is from underreporting by passthrough businesses at the entity level, most of which is not even included in past IRS estimates of the tax gap.[xvii]

The reason for the continued growth in the biggest part of the tax gap is the lack of progress on income that is only reported on the tax return itself and not separately verified by third parties such as employers or payers. When the IRS has third-party data and uses that data effectively, the compliance rate is 94 to 99 percent. When it has no data, or has data but does not use it effectively, the rate is just over 50 percent, as shown in the figure, taken from the most recent IRS compliance study. These rates have not significantly changed in decades. The dollars lost just grow larger as the economy expands.[xviii]

The lack of progress in addressing the biggest and most lopsided part of the tax gap is extremely unfair to the vast majority of taxpayers who are paying all of what they owe.

The large amount of lost revenue is heavily concentrated among upper-income taxpayers.

By our estimate, at least half of the entire tax gap is attributable to underreporting by taxpayers reporting incomes over $160,000 (the top 10 percent of taxpayers), and at least 35 percent is from those reporting incomes over $400,000.[xix]

Today the IRS's main tool for addressing the large segment of lost tax on underreported income that has limited third-party reporting is traditional audits, which are too few and too inefficient

to have much effect. All of the IRS's audits collectively recover only about $10.5 billion per year, less than 2 percent of the tax gap. The auditing of passthrough businesses is negligible — about 0.06 percent or six audits out of 100,000 returns.[xx]

Because of the relatively modest revenue recovered through audits, there is scant evidence that they have much of a deterrent effect either, especially on upper-income taxpayers.[xxi]

The inefficiency of the IRS's approach to audits also imposes an unnecessary burden on compliant taxpayers because 21 to 73 percent of audits are "no change" audits, which means they did not need to be done at all.[xxii] The fraction of unnecessary audits would be even larger if those that recovered some tax, although an immaterial amount, were included in the data.

For the IRS to make progress on reducing the tax gap, new strategies that make much more use of data and technology will have to be applied on a larger scale. The IRS has had significant success in limited sectors with this approach — for example, in the Return Review Program that screens for inappropriate refunds and in parts of the Criminal Investigation division.[xxiii]

But the IRS has enormous amounts of data that it is not using and many more opportunities for new compliance approaches. In total, the IRS receives about two billion information reports per year from payers and employers who report a total of almost $18 trillion of income (yes, trillions).[xxiv] Only a fraction of this information is used in systematic, automated processes by the IRS.

Here are some examples of more efficient compliance strategies.

The IRS receives approximately 30 million Schedule K-1 (Form 1065), "Partner's Share of Income, Deductions, Credits, etc.," returns reporting over $1.2 trillion of income from passthroughs but makes no systematic use of this data unless an agent uses it in an audit.[xxv] With current technology, these returns could all be analyzed to identify and follow up on discrepancies.[xxvi]

In May 2020 the Treasury Inspector General for Tax Administration reported that high-income nonfilers owing billions of dollars in taxes were not being examined. The report noted that the IRS has the information necessary to identify these nonfilers from employers' Forms W-2, taxpayers' Forms 1099, and related and prior tax returns.[xxvii]

Similarly, in December 2020 TIGTA reported that billions of dollars in potential taxes were missed from taxpayers that received income reported on Form 1099-K, "Payment Card and Third Party Network Transactions."[xxviii] The report also noted that "numerous business and individual taxpayers with reporting discrepancies of at least $10,000 between the reported Tax Year 2017 income on the return and the Form 1099-K income were not identified by the IRS's underreporter programs, or were identified, but not worked."[xxix]

Separately, a study showed that just one small subsegment of business income — short-term rental income — likely accounts for $2 billion of unreported tax and is now reported on Form 1099-K but is not used by the IRS in any automated method.[xxx]

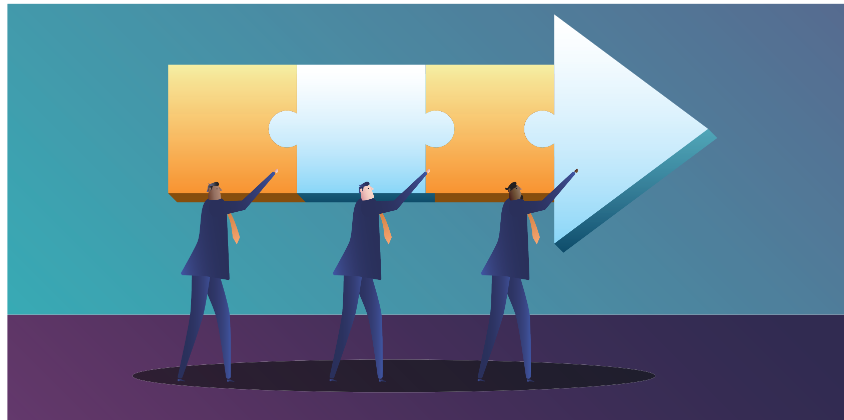
The Government Accountability Office performed an extensive study in 2007 of underreported tax by sole proprietors,

which are business owners that report their income directly on their individual tax returns. The GAO reported that 28 percent of the entire tax gap was caused by underreporting in this category of income and that 10 percent of the sole proprietor returns accounted for 61 percent of the underreported tax.[xxxi] In this and other studies, the GAO identified 22 options for addressing this part of the tax gap, but in a follow-up project, GAO said, "As of May 2021, Treasury has taken no action to address this recommendation and has not provided GAO with plans to do so."[xxxii]

Similar strategies must be developed and implemented for the huge and growing passthrough sector. Businesses in the passthrough sector now report total positive income exceeding $1 trillion, rivaling that of all corporations. Our independent estimate is that this passthrough sector accounts for approximately $140 billion per year of tax on underreported income at the business entity level, almost none of which is recovered by the IRS.

Also, new strategies will be required to address the tax lost by the underreporting of income from new parts of the economy, such as cryptocurrency transactions, which are not covered by official tax gap estimates since they barely existed when IRS compliance studies were done.

To make meaningful progress on reducing the tax gap and doing so efficiently, the IRS must transform its entire compliance approach to one that is driven by data and technology, supplemented by skilled and effective enforcement teams. Available data combined with machine-learning technology can vastly improve the efficiency of enforcement activity if used properly.[xxxiii]



The next IRS commissioner would be well served by setting up a small compliance strategy office, led and staffed by highly qualified experts in data science, statistical analysis, tax law, auditing, and technology, recruited from inside and outside the IRS

The next IRS commissioner would be well served by setting up a small compliance strategy office, led and staffed by highly qualified experts in data science, statistical analysis, tax law, auditing, and technology, recruited from inside and outside the IRS. All these disciplines, including auditing, are widely applied in the private sector as well as the IRS, and there is much to be learned from them.[xxxiv]

The IRS operating divisions, such as Large Business and International and Small Business/ Self-Employed, can execute a more effective strategy if provided with effective guidance, data, and tools.

As with all the major change programs in the IRS, the implementation of a modern compliance strategy will have to be led by an empowered and effective governance process with the commissioner as the ultimate decision-maker.

Communicating Effectively

The IRS deals directly with almost every family, business, and nonprofit entity in the United States — more than any other institution — and has a significant effect on those it serves. It is therefore appropriate that the agency be subject to substantial oversight. To this end, eight congressional committees have oversight jurisdiction over the IRS. They are supported by the GAO in the legislative branch and TIGTA. Together these bodies issue hundreds of reports on the IRS each year and investigate any suspected incidents of wrongdoing.

The Treasury Department is the IRS's parent agency and has responsibility for critical matters that greatly affect its performance, including approving budgets and issuing regulations and other forms of tax guidance. Close alignment with Treasury is essential.

Private sector groups consisting of practitioners, accountants, and lawyers regularly meet with and comment on the IRS, and they are the subject of continuous coverage by both specialized tax publications and general interest media.

The IRS Oversight Board, which was established by Congress to provide

independent private sector expertise and advice to the commissioner, has not been functioning because of a lack of appointees. A reconstituted board could provide valuable, forward-looking advice on matters such as resource allocation, internal organization and recruiting, strategic planning, technology management, and communications, which other auditing and oversight bodies generally do not provide.

Internally, the IRS employs more than 75,000 people who are spread across the United States, as well as many supporting contractors, all of whom must be motivated and trained to accomplish the agency's mission.[xxxv]

Communicating with these many stakeholders is a major job of the IRS commissioner. In my five-year term, I testified 48 times in congressional hearings and traveled almost every week to meet with employees and outside groups.

Honest, accurate, and meaningful communication in all these settings is essential to building credibility — internally and externally. Equally important is establishing reasonable expectations and realistically acknowledging challenges, risks, and setbacks — all of which inevitably occur. These challenges will only increase because of the long-term funding now available to the IRS. This funding will increase expectations for improved IRS performance since it can no longer be cited as a major constraint.

The Bottom Line: Success or Failure

With the passage of long-term funding for the IRS, Congress has provided an opportunity for the federal government to rebuild one part of America's critical infrastructure — our system for administering a tax system that accounts for approximately 20 percent of the economy and touches nearly every family, business, and institution. This system has been in decline for most of the past 25 years and is badly in need of transformation to one that taxpayers believe is fair and effective in the 21st century. The opportunity now exists to accomplish this vital goal, but it will require exceptional leadership and constructive forward-looking oversight to happen. If this opportunity is not seized and acted upon successfully, another chance will not soon occur, and the risk to the tax system will only increase.

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[i] *IRA, Title I, Subtitle A, Part 3.*

[ii] *IRS Restructuring and Reform Act of 1998.*

[iii] *Id. at Title I, subtitle B.*

[iv] *Shrink the Tax Gap, "STTG IRA Exhibit 1: IRS Resources Relative to Economy" (Nov. 10, 2022).*

[v] *Shrink the Tax Gap, "STTG IRA Exhibit 2: Taxpayer Interactions by Type" (Nov. 10, 2022).*

[vi] *National Taxpayer Advocate, "Annual Report to Congress 2018," at 170 (Feb. 2019).*

[vi] *Id. at 198.*

[viii] *Id. at 195.*

[ix] *Shrink the Tax Gap, "STTG IRA Exhibit 4: Enforcement Revenue From Auditing" (Nov. 10, 2022).*

[x] *Charles O. Rossotti, Many Unhappy Returns: One Man's Quest to Turn Around the Most Unpopular Organization in America 109 (2005).*

[xi] *For a more complete discussion of IRS metrics, see Shrink the Tax Gap, "STTG Goals, Metrics, Taxpayer Rights & Oversight" (Mar. 24, 2021).*

[xii] *Olson, "How Did We Get Here? 2-D Barcoding and the Paper Return Backlog — A Missed Opportunity," Procedurally Taxing, Feb. 24, 2022.*

[xiii] *For a more complete discussion of how technology can be used to improve all forms of service to taxpayers, see Fred Forman and Rossotti, "The Business Case for IRS Transformation," Shrink the Tax Gap ebook (Sept. 2021).*

[xiv] *Michelle Singletary, "Despite Privacy Concerns, ID.me Nearly Doubled the Number of People Able to Create an IRS Account," The Washington Post, Feb. 25, 2022.*

[xv] *For more discussion on how IRS improvement programs can be organized, see Rossotti and Forman, "Recover $1.6 Trillion, Modernize Compliance and Assistance: The How-To," Tax Notes Federal, Sept. 14, 2020, p. 1961.*

[xvi] *Shrink the Tax Gap, "STTG IRA Exhibit 3: Tax Gap Update" (Nov. 10, 2022) (Shrink the Tax Gap projected forward the estimates for the latest IRS compliance study, which covered years 2017-2019. Our estimate includes an estimate for taxes on underreported income at the passthrough business entity level, which are not included, except incidentally, in the IRS study.).*

[xvii] *Shrink the Tax Gap, "Appendix A: Methodology for Calculating Tax Gap From Underreporting of Passthrough Business Entities" (Oct. 28, 2022); and Shrink the Tax Gap, "STTG IRA Exhibit 5: Tax Gap From Underreported Income by AGI" (Nov. 10, 2022).*

[xviii] *IRS, "Federal Tax Compliance Research: Tax Gap Estimates for Tax Years 2014-2016," Pub. 1415 (Oct. 2019).*

[xix] *Shrink the Tax Gap, "STTG IRA Exhibit 5," supra note 17 (IRS statistics report distribution of income and tax paid classified by the amount reported by the taxpayer, so taxpayers who underreport are shown in a lower bracket. For example, a taxpayer reporting income of $190,000 who underreports by 55 percent (which is the average underreporting percentage for low-visibility income) actually has income of $422,000. Further, our estimates only account for underreporting of income tax, and do not include related underreporting of employment taxes.).*

[xx] *Shrink the Tax Gap, supra note 9.*

[xxi] *Phill Swagel, "The Effects of Increased Funding for the IRS," Congressional Budget Office Blog, Sept. 2, 2021.*

[xxii] *Shrink the Tax Gap, supra note 9.*

[xxiii] *Shrink the Tax Gap, "Appendix G: STTG Technology Paper Case Studies" (Aug. 18, 2021).*

[xxiv] *Shrink the Tax Gap, "STGG IRA Exhibit 6: Information Returns Filed for Calendar Year 2019" (Nov. 11, 2022).*

[xxv] *Id.*

[xxvi] *Forman and Rossotti, supra note 13.*

[xxvii] *TIGTA, "High-Income Nonfilers Owing Billions of Dollars Are Not Being Worked by the Internal Revenue Service" (May 29, 2020).*

[xxviii] *TIGTA, "Billions in Potential Taxes Went Unaddressed From Unfiled Returns and Underreported Income by Taxpayers That Received Form 1099-K Income" (Dec. 30, 2020).*

[xxix] *Id.*

[xxx] *Forman and Rossotti, supra note 13.*

[xxxi] *GAO, "Tax Gap: A Strategy for Reducing the Gap Should Include Options for Addressing Sole Proprietor Noncompliance," GAO-07-1014 (July 2007).*

[xxxii] *GAO, "Questionnaire on Policy Options to Improve Sole Proprietor Compliance" (Oct. 7, 2022).*

[xxxiii] *For a more complete discussion of how the IRS can use data and technology to address the tax gap more effectively, see Forman and Rossotti, supra note 13.*

[xxxiv] *Shrink the Tax Gap, supra note 23.*

[xxxv] *IRS Data Book 2021, Table 32.*

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Charles O. Rossotti co-founded American Management Systems in 1970 and is a former IRS commissioner. In this article, Rossotti examines the long-term and substantial funding provided for the IRS in the Inflation Reduction Act and explains how it could best be used to rebuild the agency and maximize its ability to collect taxes.

NAEA

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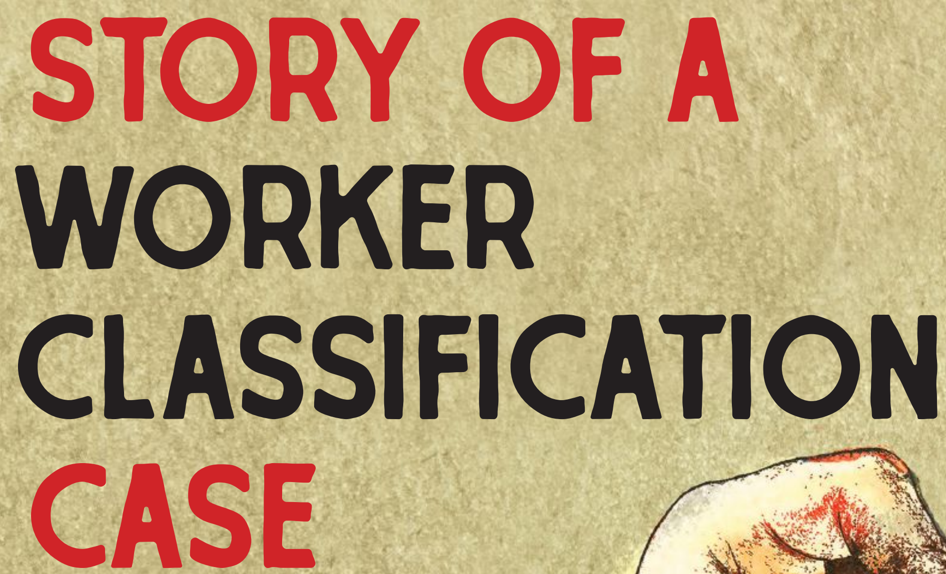
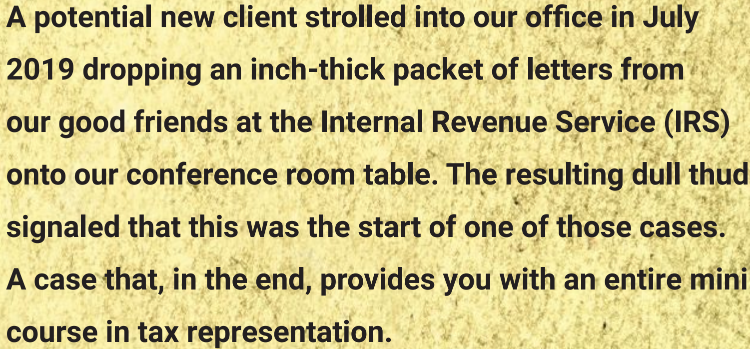


STORY OF A WORKER CLASSIFICATION CASE



A potential new client strolled into our office in July 2019 dropping an inch-thick packet of letters from our good friends at the Internal Revenue Service (IRS) onto our conference room table. The resulting dull thud signaled that this was the start of one of those cases. A case that, in the end, provides you with an entire mini course in tax representation.

John A. Mitchell, EA

At the very top of the stack was IRS Letter 3850[i] – dated from six months prior – notifying our potential new client of an examination of their employment tax returns for 2016, 2017, and 2018 along with Form 4564, *Information Document Request*,[ii] that ran for five pages, single-spaced. The Service notified us in due course that they were picking up the 2019 tax year as well.

PRACTICE TIP: It is certainly worth reminding clients to keep in mind their rights – especially their right to be represented. Anyone who has done representation work knows the pain and suffering of trying to undo the damage done to a case because inexperienced people went in with the best of intentions but ended up doing more harm to the case than good.

You can find the Taxpayer Bill of Rights[iii] in IRS Publication 1,[iv] and on the IRS.gov website by searching for "Taxpayer Bill of Rights" and, more specifically, the right to representation is detailed in IRS Tax Tip 2022-143, September 19, 2022,[v] stating among other things, *"Taxpayers have the right to retain an authorized representative of their choice to represent them in their dealings with the IRS."*

PRACTICE TIP: On the second page of the letter, several enclosures were listed. For years now, I have kept two rather large binders near my desk. One of them is full of these standard IRS publications which are kept by me for reference. The other binder has key research materials on frequently encountered issues. When I encounter a case that requires some research on my part, I frequently print out two copies of said research – one for the client's file and an extra for the binder which is tabbed and indexed for future quick reference.

The stakes were potentially high. This company was a successful construction company in the Houston area with gross revenues in the million-dollar range – per month. Their client list included nearly every high-profile home builder in the area, and they were regularly using the services of dozens of subcontractors at a time.

Misclassifying Workers

The IRS, in recent years, has issued several public warnings about properly classifying workers as either employees or independent contractors as this has become an enforcement priority for them. An example of this is IR-2021-186, September 15, 2021.[vi]

The potential consequences of misclassifying employees as independent contractors can be quite unpleasant for businesses. For example, businesses can face tax assessments for all of the withholdings that they "should have" held out of the (newly classified) employees' paychecks and the business cannot recover those withholdings from workers' pay after the fact. Criminal cases are not usually pursued but can be.

In two widely reported cases, the federal 9th Circuit Court of Appeals found in 2014 that FedEx Ground drivers in Oregon and California had been misclassified as independent contractors. FedEx lost those cases despite the fact that it had written contracts with all of its drivers in which the drivers agreed that they were independent contractors. That case cost FedEx over $225 million.

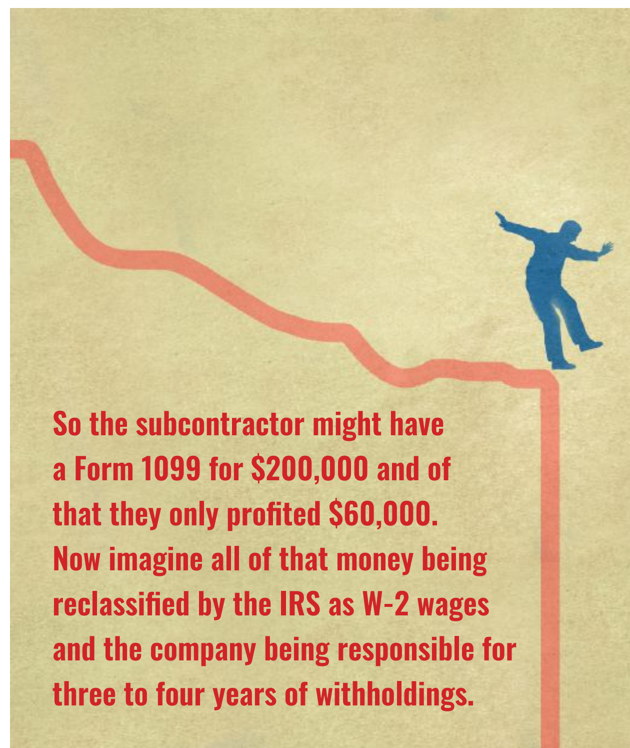
Our case was not nearly that large, but taking into account the four-dozen or so workers the IRS was seeking to potentially reclassify, multiplied by three (later four) years along with interest and penalties, the potential exposure to our soon-to-be client could easily have run into the low millions of dollars.

Our Case

Home builders will typically buy large tracts of land and plan out subdivisions, which will have different model homes built throughout. The home builders take of the high-level planning and then procure the services of general contractors and subcontractors. Different contractors will take care of different aspects of building a new home, such as pouring foundations, framing, roofing, electrical, plumbing, etc. Our soon-to-be client handles masonry work. The only detail is they had no employees working directly for their company that actually *did* any masonry work. They were "middle men" scheduling crews of subcontractors who would show up on the jobsites to actually install the masonry. This detail ended up being pivotal since we successfully argued that our client's business was not the masonry business, per se, but rather they were in the "project management" business. In effect, we argued (again, successfully) that our client made money by finding new construction work that needed to be done and putting that work together with subcontractors needing work and handling the backend details of carrying out the projects, like scheduling, ordering materials and supplies, and performing quality control functions. More on that later.

In any event, one of the reasons this case could have been so expensive was the way independent contractors are paid in the construction industry. This case was typical in that the masonry work for a new home to be built was bid to the subcontractors by my client. A gross amount would be paid for the entire job to the subcontractor, with a Form 1099 issued at the end of each year, typically under the Social Security number of the subcontractor. It was not unusual for the subcontractor to be paid between $10,000 and $15,000 for a particular job. It was also not uncommon for these subcontractors to do between 10 and 20 jobs for my client over the course of a year.

The problem comes about when you consider that the subcontractors have to pay expenses out of these gross amounts, including tools, equipment, transportation, insurance, and normally between one and four "helpers" which they were responsible for hiring, training, supervising, and paying.



So the subcontractor might have a Form 1099 for $200,000 and of that they only profited $60,000. Now imagine all of that money being reclassified by the IRS as W-2 wages and the company being responsible for three to four years of withholdings. For this reason, it was made clear to us in the beginning that our client *needed* us to win this case because (1) the financial impact would likely be crippling; and (2) if there were to be a precedent going forward where the client would be obligated to hire and pay subcontractors as W-2 employees, their cost structure versus other competitors in the market would be so skewed as to make them uncompetitive and likely cause them to go out of business.

One other factor was mentioned to us that is worth considering. Our client told us that the subcontractors strongly preferred their status as independent contractors and were unwilling to work as W-2 employees and that they were sure they would lose workers to other companies who would pay them in the manner they had become accustomed to. This is a bit anecdotal, but seemed quite plausible to me at the time and still rings true today.

PRACTICE TIP: My very best suggestion to enrolled agents (EAs) and really, any professional, is to not begin work without an adequate retainer and an engagement letter. Also, about filling out and filing Form 2848, I recommend getting them signed by the client in a version that covers more years than you expect to need power of attorney (POA) for. I almost always fill our my POAs to include years from 2000 to whatever the current year is plus two or three years. The Internal Revenue Manual at §21.3.7.5.2(4)[vii] specifies that three future years can be entered on the Form 2848.

After the engagement letter and retainer were squared away, it was time to fax the 2848 forms to the Centralized Authorization File (CAF) unit at the IRS as well as contacting the revenue agent to notify her that we were retained to represent the taxpayer and future communication should go through our firm and that we were making ourselves available to them and happy to reach a resolution of the examination engagement in as quick and efficient a manner as possible.

The IRS approached this case in a fairly aggressive manner. We got the sense, early on, that our client was of particular interest to the Service because of their relatively large size and relatively deep pockets. Indeed, in one of the first meetings I had with the revenue agent and her group manager I laid out all of our views on the case and the reasoning as to why these workers were properly classified as independent contractors. The group manager told me (in so many words) that they would not be giving in to our position because the IRS had “too much tied up into this case” to give up.

Worker Classification and Examinations of Same

The classification of a worker decides the obligation of an employer to withhold income taxes and contribute to Social Security, Medicare, and unemployment taxes based on the wages paid to the worker. According to standard laws, a worker is considered to be an independent contractor if the person or entity paying him or her has control only over the outcome of the work, but not the method or means used to attain that outcome.

There are various routes that can lead to a worker-classification audit. For instance, the IRS can be informed of misclassification by an employee. It can also stem from a state labor audit or a Department of Labor audit through information sharing agreements with the IRS. A worker-classification audit could also be triggered by a whistleblower, a civil lawsuit, or a random audit. With the current financial constraints faced by states and the federal government, it is expected that worker classification audits will increase in frequency.

The Internal Revenue Code in §3401[viii], defines an individual as an "employee" for employment tax purposes if he or she meets the criteria of an employee according to the common law rules used to determine the employer-employee relationship. The classification of a worker as an independent contractor or an employee is determined by evaluating the relevant facts and circumstances and applying common law principles. In making this determination, courts usually consider whether the worker meets the definition of an employee under common law.

Under Treasury regulations,[ix] the question of whether a worker constitutes an “employee” largely boils down the degree of control exercised by the employer over the individual. In this regard, it is not necessary that the employer actually direct or control the manner in which the services are performed; rather,

there is sufficient control if the employer has the right to do so. The right to discharge is also an important factor when considering the presence of an employment relationship.

The IRS analyzes the evidence of the degree of control and independence through three overarching categories:

Behavioral: Does the company control or have the right to control what the worker does and how the worker does his or her job?

Financial: Are the business aspects of the worker's job controlled by the payer? (How is the worker paid? Are expenses reimbursed? Who provides tools/supplies, etc.?)

Type of Relationship: Are there written contracts or employee-type benefits (i.e., pension plan, insurance, vacation pay, etc.)? Will the relationship continue and is the work a key aspect of the business?

Additionally, the IRS has historically applied what is commonly known as the "20-factor common law test"[x] for determining the status of workers. Ordinarily, the principal's right to control the manner in which the work is performed is the most important factor in determining whether there is an employer-employee relationship.

Businesses must weigh these factors when determining whether a worker is an employee or an independent contractor. No one factor stands alone in making this determination and the relevant factors will vary depending on the facts and circumstances.

Third-Party Summons and Interviews

One interesting thing that took place in the course of nearly 18 months of handling this case is that the Service wanted to interview nearly 30 of the the workers in a third-party summons. After conferring with our client and a good number of the workers, it was determined that I would represent the workers in each of their interviews. When I notified the revenue agent of this, I received a letter from the group manager citing potential conflict of interest rules as found in Circular 230[xi] and concluding that I "would not be allowed" to represent the workers. This fax came through late in the afternoon the day prior to the interviews. We were able to show case law which supported our position that the workers to be interviewed were entitled to hire me despite my representing the company and that the IRS must accept their decision to have me represent them. (See *Backer v. CIR,275 F 2d 141(5th Cir 1960)*.[xii]) Suffice to say that the chill in the room the next day was not due to the air conditioning in the IRS building. However, the group manager (who was present in every meeting thereafter – and flew in for said meetings from Los Angeles to Houston) was eventually assured that I was not present to impede or hinder their work but, rather, to facilitate. That part was actually true because we were happy to have the workers interviewed – we felt we had good facts on our side. In fact, we accepted the summons on behalf of most of the workers and coordinated the scheduling of the interviews making sure the workers arrived on time and prepared. Only two of the workers declined my presence in their interviews. In the end, I ended up with quite a good rapport with the agent and the manager.

Conclusion

So, how did the case end up? We ended up agreeing to reclassify exactly one worker from independent contractor to employee. Also, there were expenses paid by the company that were more properly classified as personal and therefore imputed wages for the owners of the company (an S corporation). In the end, the client was very happy to write a check in the neighborhood of $80,000.

The classification of workers presents a significant business hazard, including tax, labor, and civil litigation risks. If a business encounters worker classification exposure, it is advisable to seek the guidance of a tax professional as soon as possible, as there may be ways to eliminate the exposure. Our firm frequently provides clients with support for worker agreements and contracts, reducing risk exposure, representing them during audits, and, when required, serving as their legal counsel in litigation.

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[i] *https://www.irs.gov/irm/part4/irm_04-023-021*

[ii] *https://www.irs.gov/pub/irs-utl/form4564.pdf*

[iii] *https://www.irs.gov/taxpayer-bill-of-rights#representation*

[iv] *https://www.irs.gov/pub/irs-pdf/p1.pdf*

[v] *https://www.irs.gov/newsroom/every-taxpayer-has-the-right-to-retain-representation-when-working-with-the-irs#:~:text=Taxpayers%20have%20the%20right%20to,if%20they%20cannot%20-afford%20representation*

[vi] *https://www.irs.gov/newsroom/irs-reminds-business-owners-to-correctly-identify-workers-as-employees-or-independent-contractors*

[vii] *https://www.irs.gov/irm/part21/irm_21-003-007r#idm140005825049296*

[viii] *https://www.law.cornell.edu/uscode/text/26/3401*

[ix] *https://www.law.cornell.edu/cfr/text/26/31.3121(d)-1*

[x] *https://efte.twc.texas.gov/appx_d_irs_ic_test.html*

[xi] *https://www.irs.gov/tax-professionals/circular-230-tax-professionals*

[xii] *https://casetext.com/case/backer-v-cir*

John A. Mitchell, EA, holds a law degree and a Master of Science in Taxation. He began his tax journey by preparing 1989 tax returns in the 1990 filing season by hand. John is a foreign-licensed attorney and speaks Spanish at a "native speaker" level. John has been an enrolled agent since 2015 and is an NTPI Fellow®. He works at the law firm of Cantrell & Cantrell, PLLC in Houston, Texas, where he specializes in tax controversy. John is a husband, father of two children, stepfather of two children, and grandfather of two children. When not working, he enjoys books, movies, travel, and spending time with family. John can be reached for questions at (713) 333-0555 or jmitchell@cctaxlaw.com.

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Randall Brody, EA

Five Ways to Provide Peace of Mind to Your Clients with IRS Problems: Exploring Tax Resolution Options

There is no arguing the fact that the Internal Revenue Service (IRS) wants the money that is owed and heavily punishes delinquent taxpayers. Sometimes it feels as if the IRS wants people to stay indebted, to a point where the taxpayer winds up paying a lot more than originally owed through penalties and interest. That is on top of the intimidation tactics used by the IRS to get people to pay up. These taxpayers become your clients because they do not have the tools and skills to handle demands for payment from the IRS and look to you for peace of mind.

Owing money to the IRS is a source of stress for people who do not understand the tax resolution options available. You can help them relax by explaining that there is always a solution to the problem, the IRS will negotiate, and there are five common ways for settling IRS tax debt. There is nothing better than showing clients they can get the IRS off their backs and they do not have to be afraid of going to their mailboxes, much less worry about getting their bank accounts garnished.

The following is a look at how you can help your clients find normalcy once again while resolving their debt with the IRS. We are going to go through the following options at an introductory level that your clients can understand that include:

- Offer in compromise (OIC)
- Payment plan/partial payment installment agreement
- Currently non-collectible
- Bankruptcy
- Penalty abatement.

Read on to learn more about these IRS debt resolution options and how they create a binding contract between your client and the IRS to settle a debt and finally be free from collection harassment.

1 Offer in Compromise

The offer in compromise (OIC) touts an option to settle a tax debt for less than the full amount that is owed. Many times, this is for a fraction of what is owed. On the surface, getting an OIC accepted by the IRS seems easy, but if it were, everyone would be doing it. As a tax expert, this is where you come into the picture.

An OIC becomes an option when taxpayers cannot pay their entire tax liability as it would cause financial hardship. The IRS levies fines, penalties, and interest on an outstanding tax debt to the point that the total amount owed becomes a financial hardship. This can tilt the odds in the client's favor in terms of resolving the debt and closing out this particular chapter of the client's life.

The OIC comes into play when the offer amount is the most that the IRS can collect within a certain amount of time. The taxpayer must also explore all other payment options before the OIC is submitted.

For an OIC to be considered, the client must be eligible to apply. Factors for eligibility include:

- Filing of all outstanding tax returns, if any
- Not in a bankruptcy proceeding
- Extension for the current year's return is valid if applying for the current year.

The amount the IRS will settle for is based on the taxpayer's reasonable collection potential; a formula-driven process that must meet certain standards based on:

- Ability to pay the outstanding balance
- Income
- Expenses
- Equity in assets.

When an OIC is accepted, the client's payment options include a lump sum in cash or over time with periodic payments. The lump sum cash option requires an initial payment of 20 percent of the total offer amount and the remainder paid off in five or fewer months after acceptance of the offer. The periodic payment requires an initial payment and paying off the balance in monthly installments during the period the IRS considers the offer. If the offer is accepted, the payments continue until the offer balance is paid in full but not more than 24 months.

An OIC is done on Form 433-A (OIC) for individuals and Form 433-B (OIC) for businesses. More information can be found in the Form 656-B, *Offer in Compromise* Booklet.

2 Payment Plan

The payment plan, also known as an installment agreement, is the easiest way to get the IRS to accept payment for taxes owed. The basic concept behind a payment plan is one of agreeing with the IRS to make monthly payments for anywhere between 180 days to five to six years. Entering into a payment plan also stops the 10-year collection period from running out, which means you and your client need to be sure that the payments can be made regularly and prevent the IRS from taking more vigorous action.

To enter into a payment plan, the practitioner generally either goes online or makes a phone call to the IRS or completes IRS Form 9465 and submits it to the IRS. There are exceptions to this process. For example, when a taxpayer cannot meet the requirements of a streamlined installment agreement because he or she owes more than $50,000, a practitioner will need to submit an IRS Form 433-F, *Collection Information Statement*.

This can be a scary time for the client as he or she has to wait for the IRS to approve the plan; as long as the request is submitted, the IRS tolls all collection activity. That is, the IRS will not seek to collect money from your client while it reviews the request.

The IRS rarely rejects an installment agreement request as long as the form is correctly filled out; this is typically the quickest resolution option to receive approval. Your client may have to make payments on the outstanding debt while the agreement is under consideration.

Interest and penalties are assessed on the outstanding balance while the payment plan is active, but the interest rate is far lower than that of a credit card; the client can increase the payment amount to pay the debt sooner. All collection activities cease as long as the client maintains the payment plan by paying the amount owed monthly until the liability is paid.

Partial Payment Installment Agreement

The Partial Payment Installment Agreement (PPIA) is a relatively new payment plan the IRS offers. It is also known as the backdoor offer in compromise as it is similar to the OIC but has a different approach involving the collection statute expiration date (CSED). The CSED is the time period the IRS has to collect a debt from the date of assessment, which is 10 years. The client makes payments towards the outstanding debt but stops paying on the balance once the CSED expires.

To qualify for the PPIA, the client has to owe a minimum of $10,000 and have assets that cannot be easily liquidated to pay the outstanding debt. However, the IRS is not interested in basing the

Interest and penalties are assessed on the outstanding balance while the payment plan is active, but the interest rate is far lower than that of a credit card; the client can increase the payment amount to pay the debt sooner.

monthly payment on the net equity in assets, especially when the case is in the Automated Collection System (ACS). Instead, the IRS establishes the payment plan on the disposable income your client has available every month. The outstanding tax debt is paid until the 10-year CSED has expired. If there is an outstanding balance after the statute has passed, it becomes uncollectible.

The PPIA is by no means perfect, and the IRS is not doing a good job promoting the program as an alternative to other payment programs. This is where you will need to be an effective advocate for your clients by ensuring the IRS holds up its end of the bargain by allowing your clients to apply for PPIA, especially when they are qualified.

Another aspect of the PPIA is that it is not easy for the average taxpayer to get on his or her own. They have to fill out Form 9465 as well as Form 433-A or 433-B, which allows them to calculate the amount they can reasonably pay and offer to the IRS. However, this can cause taxpayers to get into financial trouble if they cannot pay the amount due for whatever reason. This is where you come in by helping your clients go over their finances to determine how much they can comfortably afford and determine how much time remains on the CSED.

The PPIA can be very favorable to a client who owes a large debt to the IRS and doesn't have the means to pay through a payment plan or OIC. Once the CSED period expires, your client becomes non-collectible, and the debt is erased. It is similar to the Chapter 13 bankruptcy process without the need to file for bankruptcy.

3 Currently Not-collectible

The status of currently not collectible (CNC) does not eliminate the tax debt, but it does stop the IRS from making collection attempts. Getting a client into CNC status requires filling out a collection information statement on Form 433-F, Form 433-A, or Form 433-B, along with proof of financial status. The proof may include information regarding assets, expenses, and income. It must show that the taxpayer has no available equity in his assets and that the income is not sufficient to cover allowable expenses.

Getting CNC status for a client should be considered a steppingstone unless the client is elderly or retired and on a fixed income. A client with no prospects for more income in the future benefits from CNC status and may never have to pay off the debt. However, for someone still employed with better future job prospects, CNC can be used as a steppingstone to obtaining an OIC or PPIA. You will have to use your best judgment when applying for this status on behalf of your client.

4 Bankruptcy

Certain types of tax debt can be eliminated through bankruptcy, but this option should only be used if your client has other financial issues. Bankruptcy is a nuclear option in that it eliminates more than tax debt; it also eliminates unsecured and secured debts in a wholesale fashion. Your client has to be at a point where taking this option makes sense, and he or she is willing to go through the process.

Bankruptcy is a nuclear option in that it eliminates more than tax debt; it also eliminates unsecured and secured debts in a wholesale fashion. Your client has to be at a point where taking this option makes sense, and he or she is willing to go through the process.

To wipe out tax debt through bankruptcy, the debt has to consist of federal personal income taxes. Any other type of outstanding tax, such as business tax, is ineligible. The tax debt in question has to be at least three years old, and the tax return for that year must be filed at least two years before filing for bankruptcy. Last, but not least, the tax debt has to fall under the 240-day rule wherein the IRS has determined the amount owed at least 240 days before filing a petition.

Provided the taxes owed align with these requirements, they can be eliminated through Chapter 7 bankruptcy and included in a payment plan under Chapter 13.

5 Penalty Abatement

Penalty Abatement (PA), also known as penalty relief, consists of the IRS removing or reducing the penalties applied to the debt based on either “first-time penalty abatement” or “reasonable cause” criteria. For a first-time penalty abatement, the IRS will remove penalties for the earliest year, but there are certain requirements that need to be met, such as for the prior three years there could not have been any failure to file or failure to penalties assessed and all returns were filed by the tax deadline or extended tax deadline.

For reasonable cause, the taxpayer has to show that he or she has been going through an extraordinary event but have been a responsible taxpayer outside of that event. The main thing is that whatever the event that gave rise has to coincide with the period to be abated.

The IRS does not consider a lack of funds a reasonable cause for failure to pay on time, but it does consider the reasons for lack of funds as part of the application for PA.

Reasonable causes considered by the IRS for the PA include:

- Natural disasters, fire, casualties, and other unexpected events
- Inability to obtain records through no fault of the taxpayer
- Serious illness, death, becoming incapacitated, or an unavoidable absence of the taxpayer or immediate family member
- Any other reason that demonstrates the taxpayer was unable to meet his or her tax obligation despite due diligence to do otherwise.

Conclusion

Clients in trouble with the IRS are dealing with a stressful situation that makes them feel like there is no hope. They turn to you as a tax professional to get help with resolving their debt and often are not aware of the payment programs that are available to them. Alternatively, a client may be aware of the payment programs but does not know how to take advantage of them, much less how to apply.

Your role is to reassure them that help is available, that their situation is not as dire as it seems, and that your job is to help them find a resolution with the IRS. If people paid their taxes promptly or followed the IRS rules, they would not need your help to begin with. As it stands, people make mistakes all the time, and you can help them correct their errors and avoid them going forward through the various payment options offered by the IRS.

Entering a client into an IRS payment program has the desired effect of resolving the debt equitably and enabling them to live their lives free from worry. You can be an effective advocate for your clients by examining their issues with the IRS, understanding their finances, and helping them get into a resolution plan that works best for their situation.

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The $80 Billion Question

On November 10, 2022, President Joe Biden nominated **Danny Werfel** to succeed Chuck Rettig as Commissioner of Internal Revenue.[i] Danny—or more formally, Daniel I.—Werfel testified on February 15, 2023, before the Senate Finance Committee, led by Chairman Ron Wyden (D-OR) and Ranking Member Mike Crapo (R-ID).[ii] The presumptive new commissioner in that three-hour session presented himself as polished, poised, appropriately deferential, and deft.[iii]

Robert Kerr, EA

Before focusing on the hearing itself and then on what it means, potentially, for tax practitioners, we will first scope the issue more broadly. While many federal leadership positions are presidentially appointed and Senate confirmed (or what we in Washington, DC, call PAS), the Internal Revenue Service (IRS) has only two such positions: Commissioner and chief counsel. **The purpose is to shield the agency from outsized political influence.**

The IRS Restructuring and Reform Act of 1998 codified (at 26 USC §7803(1)(B)) a five-year term for Commissioner. The first five-year term began November 13, 1997, with Commissioner Charles O. Rossotti, who remains the only person to serve a full term. Commissioner Rettig's term ended November 12, 2022.

The savvy reader will notice an issue: a November 10 nomination for a term beginning November 13 inevitably leaves the agency with an acting commissioner, which in the main is undesirable given his or her job is "responsible for establishing and interpreting tax administration policy and for developing strategic issues, goals and objectives for managing and operating the IRS...[and]...for overall planning, directing, controlling and evaluating IRS policies, programs, and performance."[iv]

Keeping in mind it is a truth universally accepted that the agency that has just found itself in possession of some $80 billion of additional funding (as well as a charge to build a plan to invest same) is in dire need of a commissioner, the timing of his nomination is less than perfect.[v] The fact that the Finance Committee pivoted smartly to this hearing is promising and demonstrates a welcome focus.

The Werfel Confirmation Hearing

The hearing was noteworthy first for what did not happen:

- **Interviewing:** No one questioned the nominee's bona fides. Werfel brings an impressively well-tailored resume to the position. He served in senior positions at the Office of Management and Budget (OMB), as acting IRS Commissioner in the wake of the Lois Lerner conflagration, and then as a partner and managing director at the Boston Consulting Group (BCG), focused on federal operations.[vi]

  Yet not a single direct question about his ability to manage an agency of 80,000 (plus or minus) or an annual budget of $12 billion. Only one question (from Senator Tom Tillis (R-NC)) on his BCG experience and one (from Senator Tom Carper (D-DE)) about his background broadly. Senator Bill Cassidy (R-LA) mentioned in passing he was impressed with Werfel's information technology (IT) history at OMB.
- **Fireworks:** The Hill has become an increasingly divided place, yet the Finance Committee largely continues its reputation for comity. A few members were outliers, but the grandstanding was by contemporary standards (such as they are) mild. Members on both sides of the aisle wished him luck on what many consider the worst job in DC.[vii]

Concerns and differences of opinion on how the agency should deploy some $80 billion in Inflation Reduction Act of 2023 (IRA23) funding consumed most but (by no means) all of the session. On audits in particular:

- **Who will be audited:** Out of the gate, Werfel pledged fealty to Treasury Secretary Yellen's directive that audit rates for those earning under $400,000 not increase "relative to historic levels."[viii] Still, no one pinned him down to what baseline he would be using.
- **How about those earning less than $400,000?** A conversation between Senator Tillis and Werfel prevents us from drawing the conclusion that no one believed anyone earning under $400,000 should be paying taxes. Senator Ron Johnson (R-WI) also asked, "Are we going to spend wrongly by ignoring those [who earn less than] $400,000?" The takeaway: The amount of enforcement attention those taxpayers receive should not increase, but the IRS should still be collecting the taxes.
- **What about the 87,000 agents with guns?** Senator Catherine Cortez Masto (D-NV) said she heard he was going to hire 87,000 agents "and sometimes I heard they were going to be armed." She asked him the pointed question, "Are you intending to hire 87,000 agents?" Werfel's response is equally pointed: "I am not. I think it is patently incorrect...I think the notion of armed agents is incorrect. I certainly have no intention of making that part of any plan going forward."[ix]
- **Complicated corporate/partnership returns:** On several occasions, Werfel indicated the agency needed help addressing complex returns.[x] In response to a question from Sen. Cortez Masto, he said, "The focus is to hire people with the understanding and capacity and talent to unpack very complicated and intricate returns, which is a capacity gap that exists today."[xi]

Outside of the focus on the $80 billion question, several topics are of note to tax practitioners, including:

- **True north:** During the hearing, Werfel promised to be "unyielding in following my true north to increase public trust" in the Service. He returned often in answering questions to public trust and to transparency, within the limits of a tax administration agency. Further, he was amenable to a proposal from Senators Chuck Grassley (R-IA) and John Thune (R-SD) to update the plan publicly.
- **Return preparer oversight:** More than one senator broached the issue, including Sherrod Brown (D-OH), who asked whether demonstrating a bare minimum of skill would help address error rates on refundable credits.[xii]
- **Technology:** Several senators asked insightful questions related to IRS technology. Senator Todd Young referenced a Treasury Inspector General for Tax Administration (TIGTA) audit concluding digital interactions with taxpayers cost $0.20, while telephone interactions cost $42, and interactions by correspondence cost $57.[xiii] He then asked, "Assuming the IRS had a working, fully digital platform for taxpayer inquiries and correspondence, how much less would the IRS have spent [in the last three fiscal years]?"

Sen. Cassidy went into the Wayback Machine to show the Service's modernization challenges are not new. He referenced the catastrophic 1985 processing season.[xiv] He also included in the "list of uglies" a 1986 modernization contract cancellation and 1982 assessment that the agency was "grossly short of capacity and modern, state-of-the-art efficiency."[xv] The fact that at least someone on the Committee is watching a 40-year window is interesting and telling.

Reading the Tea Leaves and Conclusion

This leaves the question of what the confirmation hearing tells tax professionals. The following observations are offered for the reader's consideration:

- The agency is—and has been—struggling for at least a decade. The reasonably timely installation of an obviously well-suited (at least on paper) person in the commissioner's chair bodes well for the medium and longer term.
- The first draft of the Service's IRA22 operations plan was due to Secretary Yellen immediately after his confirmation. Its delay days after Werfel's confirmation probably was not coincidental. Look for a delay long enough for him to lay eyes on it and modify. Once the plan is released, practitioners should be profoundly interested in its contents.
- Werfel returned consistently to establishing trust, providing transparency, and pledging to work collaboratively. Watch to see headway here because if this focus bears fruit, it will be a game changer.
- Higher earners should be on notice. While onboarding compliance staff is a challenge and training new revenue agents (and revenue officers) is time consuming, audit rates are going to increase.
- While collection did not receive much attention, any adjustments to compliance will necessarily include changes in how the agency addresses its accounts receivable. It will be interesting to see how the $400,000 earnings hurdle is handled here.

Wrapping up, while one never gets a second chance to make a good first impression, Danny Werfel inarguably does not need that second chance. He should be confirmed by the time this publication lands in the reader's mailbox. Practitioners and other stakeholders will be wishing him well and watching with high hopes and great expectations.

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[i] *The nomination sums Werfel's background nicely.*

[ii] *Readers may find of interest the prepared opening statement from Finance Committee Chairman Ron Wyden (D-OR) and Ranking Member Mike Crapo's (R-ID) prepared statement and Werfel's written testimony.*

[iii] *Chairman Wyden closed the hearing by stating Werfel had "accounted for [him]self very well with respect to key kinds of questions of fairness and professionalism." Werfel Confirmation Hearing (at 3:13.31).*

[iv] *The Internal Revenue Manual is a trove of information. In this case, IRM 1.1.5.1 encapsulates the Commissioner's duties.*

[v] *With apologies to Jane Austen, whose aphorism ("It is a truth universally acknowledged, that a single man in possession of a good fortune, must be in want of a wife.") is pressed into service.*

[vi] *Boston Consulting Group is considered among the most high-octane of consulting firms (along with McKinsey and Bain). This August 31, 2022 Fortune article reports $190,000 starting 2023 MBA salaries at the firm.*

[vii] *At a significant pay reduction, given the commissioner gig pays no more than the top end of the federal Executive Schedule, or $235,600.*

[viii] *Interested readers may access the full text of Treasury Secretary Janet Yellen's August, 10 2022 letter to then-Commissioner Chuck Rettig.*

[ix] *The reader may listen to the entire exchange at 2:43.41 of the Werfel Confirmation Hearing.*

[x] *His answer to Senator John Thune (R-SD) at 2:31.04 of the Werfel Confirmation Hearing is one example.*

[xi] *The reader may listen to the exchange at 2:44.19 of the Werfel Confirmation Hearing.*

[xii] *The full back-and-forth (at 1:59.44 of the Werfel Confirmation Hearing) is of interest for the framing (administrations of both parties have requested the legislation), the bouquet to former Commissioner Rettig, and Werfel's response.*

[xiii] *The November 14, 2022 TIGTA Audit Report, "More Should Be Done to Increase Use and Availability of the Taxpayer Digital Communication Tools," provides much greater detail.*

[xiv] *The 1985 processing season was infamous years later within the agency. A November 5, 1985, Washington Post article includes this stunner: "The disclosures of return-destruction in the Philadelphia, Kansas City and Austin service centers come during what even IRS officials admit has been their worst filing season in recent history. A new $103 million computer system delayed return-processing and mailing of refunds for millions of taxpayers...".*

[xv] *The reader may listen to the exchange at 1:54.54 of the Werfel Confirmation Hearing. For those interested in the longer arc of IRS' IT modernization struggles, Sen. Cassidy also references a March 5, 2022 commentary, "40 Years of Failure: IRS Unable to Fix Computer System," authored by Americans for Tax Reform (a politically conservative advocacy group founded by Grover Norquist).*

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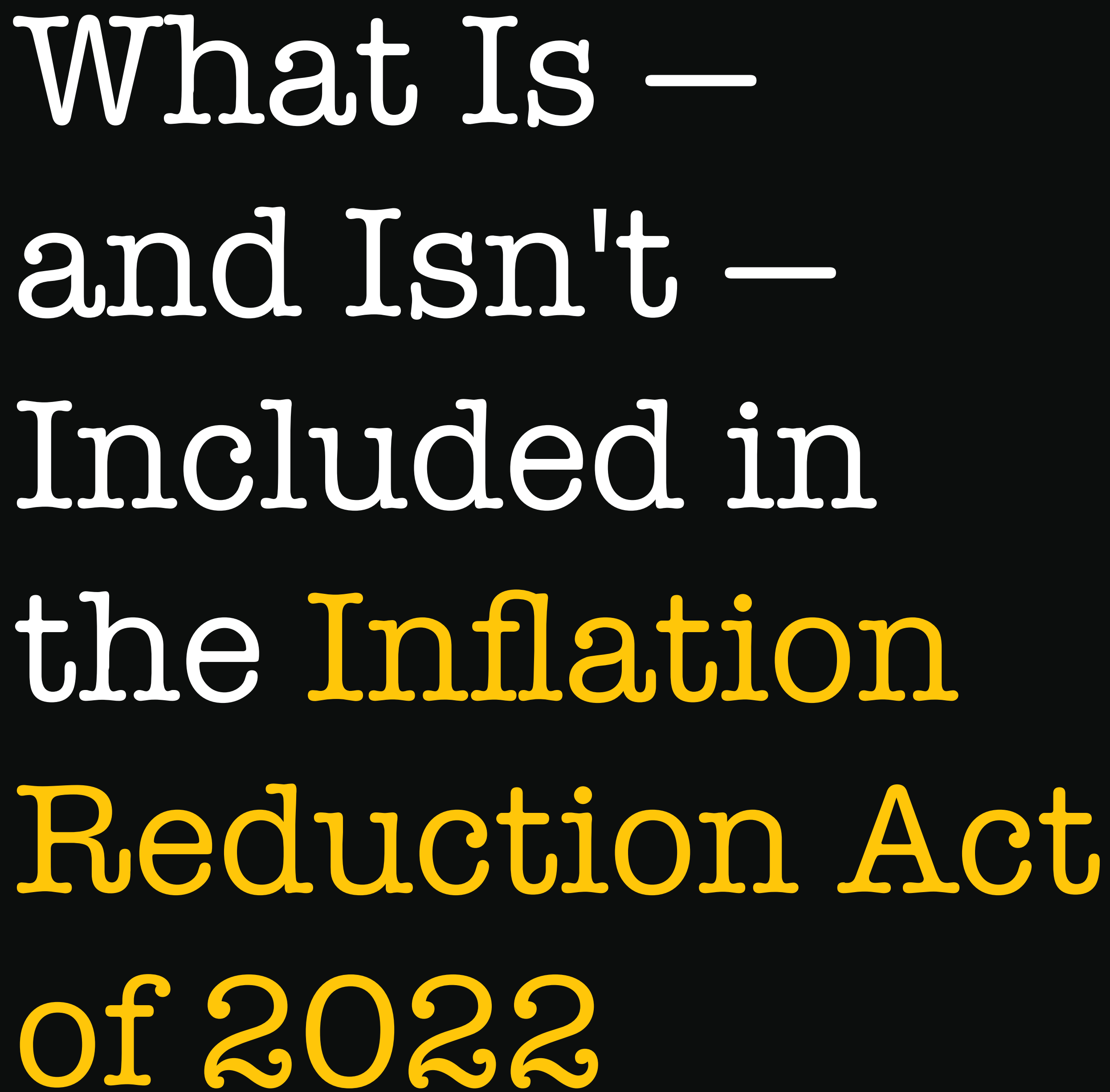

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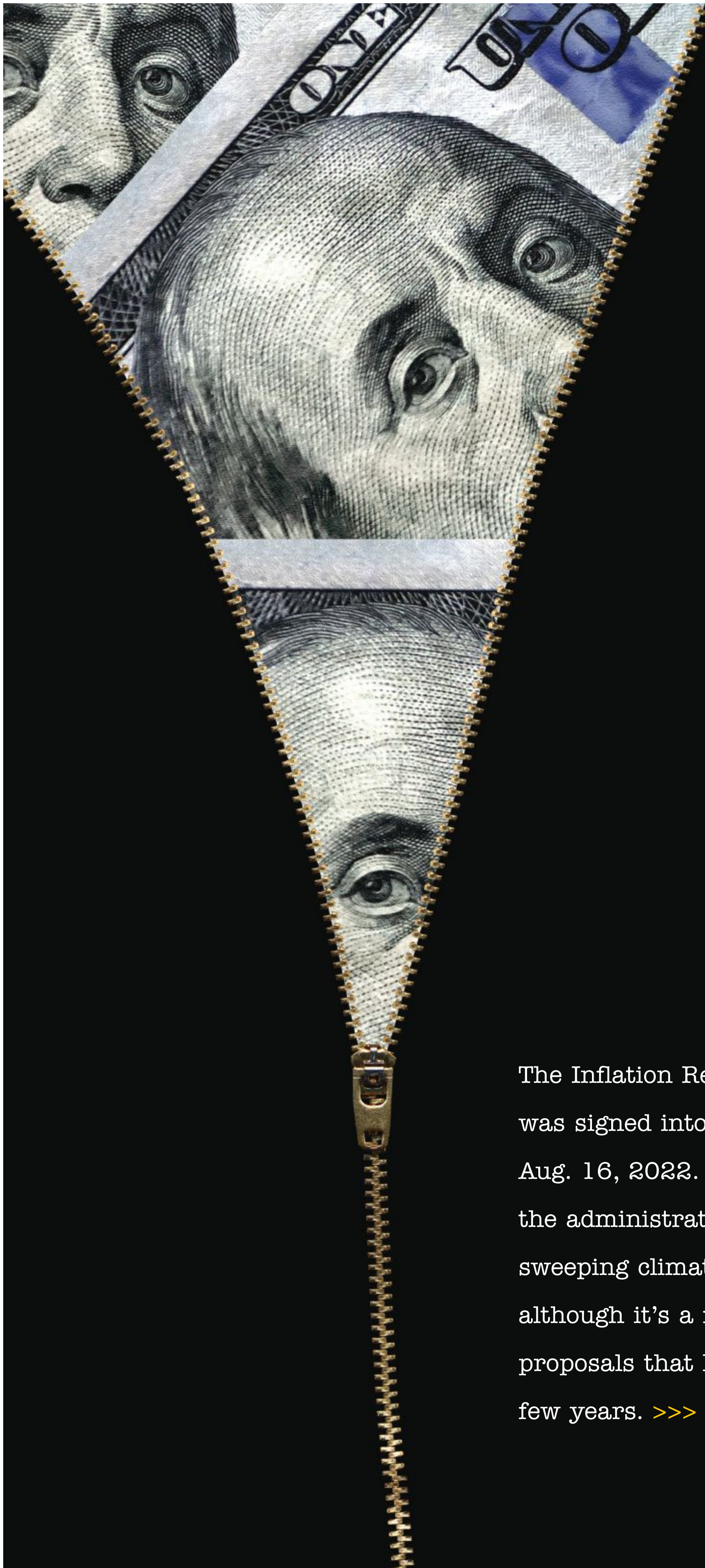

The Inflation Reduction Act of 2022 (IRA) was signed into law by President Biden on Aug. 16, 2022. It has been championed by the administration and Congress as the most sweeping climate and energy reform in history, although it’s a far cry from the various tax proposals that have been made over the past few years. >>>

The IRA provides for two major tax changes — a 15-percent corporate alternative minimum tax (AMT) and a 1-percent surtax on the repurchase of corporate stock. More importantly, the IRA allocates approximately $80 billion in funding to the IRS. However, any change to the taxation of carried interest is notably missing from the final version of the law.

Corporate Minimum Tax

The IRA imposes a new AMT on corporations (other than S corporations, regulated investment companies and real estate investment trusts) equal to 15 percent of their "adjusted financial statement income" (AFSI) if AFSI exceeds an average of $1 billion annually over a three-year period (i.e., the tax-year at issue and the prior two tax-years).

AFSI is defined under IRC § 56A as "the net income or loss of the taxpayer set forth on the taxpayer's applicable financial statement for such taxable year, adjusted as provided in this section." In general, an applicable financial statement is one that is prepared in accordance with generally accepted accounting principles and meets the requirements of IRC § 451(b)(3).

The corporate AMT is effective for tax years beginning after Dec. 31, 2022.

Stock Repurchase Surtax

The IRA imposes a 1-percent surtax on the fair market value of any stock in a publicly traded domestic corporation that is "repurchased" by such corporation through a redemption or economically similar transaction (see IRC § 4501). Of course, there are exceptions.

The IRA does not impose the surtax where the repurchase is:

- Part of a tax-free reorganization
- Contributed to an employer-sponsored retirement plan or employee stock ownership plan
- For less than $1 million (in the aggregate of all repurchases during the tax-year)
- Made by a dealer in securities in the ordinary course of business
- Made by a regulated investment company or real estate investment trust
- Treated as a dividend Like the corporate AMT, the new law applies to stock repurchases occurring after Dec. 31, 2022.

Like the corporate AMT, the new law applies to stock repurchases occurring after Dec. 31, 2022.

IRS Funding

It is no secret that the IRS has consistently struggled to perform. There are widespread reports of unanswered phone calls, millions of unprocessed paper returns, archaic technology and a workforce decimated by the COVID-19 pandemic. The IRA's distribution of approximately $80 billion in funding to the IRS over the next 10 years is expected to address these issues, increase productivity and capture foregone revenue. The IRA allocates the funds as follows:

The IRA allocates the funds as follows:

- $3.18 billion for taxpayer services
- $45.63 billion for enforcement
- $25.32 billion for operations support
- $4.75 billion for business system modernization
- $15 million for development of a new e-file system
- $403 million for general administration
- $104 million for tax policy
- $153 million for Tax Court
- $50 million for Treasury office expenses

The Inflation Reduction Act of 2022 (IRA) was signed into law by President Biden on Aug. 16, 2022. It has been championed by the administration and Congress as the most sweeping climate and energy reform in history, although it's a far cry from the various tax proposals that have been made over the past few years.

The Carried Interest Saga

The most interesting and controversial proposed tax change was eliminated from the bill at the eleventh hour to secure Senator Kyrsten Sinema's vote — taxation of carried interest.

Pooled investment vehicles like private equity (PE) funds are typically structured as a partnership made up of one general partner (the PE firm that manages the fund) and numerous limited partners ("silent" individual investors). The general partner raises capital to purchase a portfolio of several private companies with the intention of selling those interests for a profit by the end of the fund's term.

While the individual members of the PE firm may invest directly in the portfolio companies through "co-investment" vehicles, the PE firm itself generally makes little to no capital investment as the general partner. It is compensated with a management fee and a profits interest in the fund's performance. This profits interest is known as "carried interest" or simply "carry." While not used in every case, the "2

and 20" model is commonly used to structure these fees — a 2-percent management fee and a 20-percent carry in excess of any hurdle. The remaining profits are distributed to all the investing partners, pro rata, subject to any adjustments in the distribution waterfall.

When the fund sells a portfolio company, it generates a capital gain. Because the interest in the portfolio company would likely be held for more than three years before sale, the gain that flows through to the general partner and out to the members of the PE fund as carry qualifies for long-term capital gain (LTCG) treatment. Thus, carried interest is taxed at a much lower rate than ordinary income or short-term capital gain (STCG).

This tax treatment has received much opposition over the years by those who would like to see carry taxed at the higher ordinary income rates. Some headway was made by the opposition in 2017 when the Tax Cuts and Jobs Act enacted IRC § 1061, which governs the way carried interest is currently taxed. Sec. 1061 increased the required holding period for LTCG treatment of carried interest from one year to three years. In practice, however, it minimally affects carried interest for PE funds because portfolio companies are likely to be held by the fund for more than three years.

The proposed changes that did not make it into the IRA would have amended Sec. 1061 by affording LTCG treatment at the individual partner level to gain which is realized more than five years after the later of (1) the date on which the individual

When the fund sells a portfolio company, it generates a capital gain. Because the interest in the portfolio company would likely be held for more than three years before sale, the gain that flows through to the general partner and out to the members of the PE fund as carry qualifies for long-term capital gain (LTCG) treatment. Thus, carried interest is taxed at a much lower rate than ordinary income or short-term capital gain (STCG).

partner (the taxpayer) acquired substantially all of its interest in the general partner of the fund or (2) the date on which the fund acquired substantially all of its assets. This five-year rule would have instituted a significant hurdle for PE firms to receive LTCG treatment of carried interest, but for now, taxation of carried interest remains unchanged.

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Adam L. Sandler, JD, is the director of wealth planning at AJ Wealth LLC and can be reached at adam@ajwealthllc.com.

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Year-End Crypto Tips for Practitioners

Dr. Sean Stein Smith, CPA

The cryptoasset space continues to evolve and change rapidly, and there several major changes that tax practitioners need to be aware of as 2022 enters the home stretch.

The question about whether clients will be coming to practitioners with questions related to crypto has definitively shifted from an "if " question to a "when" scenario. While there are almost endless headlines to analyze and discuss, there are several fundamental items that practitioners should keep in mind as year-end rapidly approaches.

Ethereum Merge

Major technical changes have occurred. Something that might have gone unnoticed by practitioners not deeply immersed in the cryptoasset marketplace is the Ethereum merge which represents a seismic shift for the future of blockchain and crypto applications. Put simply, the Ethereum blockchain (the second largest blockchain and cryptocurrency) has replaced the Proofof-Work (PoW) consensus methodology with the Proof-of-Stake (PoS) option.

So, what does this mean? The energy required to process Ethereum-based transactions will be lower by as much as 99 percent, which should be a boon to environmental groups concerned about the carbon footprint of blockchain

technology. This also means that the number and breadth of Ethereum-based applications is set to rapidly increase, even in the face of lower crypto prices.

More applications and use cases mean the higher chance of questions coming into your inbox as the year comes to a close.

Tax-Loss Harvesting

Lower prices are creating a tax-planning opportunity that is unique to the crypto space. Clients who are sitting on unrealized losses, but who otherwise have capital gains, might benefit from a conversation explaining how these lower crypto prices can help them actually pay less in taxes. Tax-loss harvesting happens for all kinds of assets and does tend to peak during the last several months of the year, but crypto — under current tax laws — provides an additional benefit.

Under current tax law (as of this writing, several pieces of legislation are pending to change this) cryptoassets are exempt from wash sale rules, so clients can sell crypto that have incurred unrealized losses, recognize those losses and then repurchase the assets at that lower-cost basis.

This tax strategy, for now, should also apply to other cryptoassets that have recently achieved mainstream notoriety — non-fungible tokens (NFTs). It is true that the recent price declines for NFTs have definitely caused pain for investors, but these losses (if unrealized) might be able to be put to good use.

Cryptocurrency Regulations

Regulation is coming. There are numerous pieces of legislation that have rapidly moved to the marketplace that will — in short order — have a significant impact on the crypto landscape.

Key issues to consider:

- The Financial Accounting Standards Board (FASB) is finally getting into the conversation. Following years of clamoring from the profession, FASB has formally added some crypto accounting research and technical debate to its research agenda. While some crypto — notably NFTs and some stablecoins — will not be covered by this research, this is seen as a positive step forward.
- The IRS will be forced to decide some issues. The headlines around the Jarrett crypto staking case might have faded from view, but that should not reduce the importance of court cases and filings. Unclear tax laws, when combined with an uptick in enforcement, continues to create both headaches and opportunities for practitioners as tax planning and strategies come to forefront in Q4 2022.
- Crypto classification might be coming. Following the merge and pivot of the Ethereum blockchain from PoW to PoS, SEC Chair Gary Gensler has reignited a possible nightmare scenario for crypto investors. The same day that the merge finalized, chairman Gensler offered testimony that PoS crypto could qualify as securities under the Howey test. While that remains an open question, the fact that crypto is on the regulatory hotseat should be top-of-mind for all practitioners in the space.

Dr. Sean Stein Smith, CPA, is a professor at the City University of New York – Lehman College. He is a member of the NJCPA Board of Trustees and participates on several interest groups. Sean can be reached at sean.steinsmith@lehman.cuny.edu.

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STORY OF A WORKER CLASSIFICATION CASE

1. What is the main criterion the IRS uses to determine if a worker is an employee or an independent contractor?

A. The amount of control the payer has over the worker's behavior and financial aspects of the job.
B. The worker's level of education and experience in the field.
C. The worker's availability and flexibility in their work schedule.
D. The nature of the worker's job tasks and responsibilities.

2. Which of the following is not a factor the IRS considers when evaluating worker classification?

A. The worker's location and availability.
B. The type of relationship between the worker and the payer.
C. The method of payment and reimbursement.
D. The level of skill required for the job.

3. What is the difference between an employee and an independent contractor for tax purposes?

A. Employees are subject to payroll taxes, while independent contractors are not.
B. Independent contractors are entitled to more tax deductions than employees.
C. Independent contractors are responsible for paying their own income taxes, while employees are not.
D. There is no difference in tax treatment between employees and independent contractors.

4. How does a worker's classification affect their eligibility for employee benefits?

A. Independent contractors are generally eligible for the same benefits as employees.
B. Employees are eligible for more benefits than independent contractors.
C. Independent contractors are not eligible for any benefits.
D. Benefits eligibility is not affected by worker classification.

5. What are some potential consequences for misclassifying a worker as an independent contractor?

A. Fines and penalties from the IRS, as well as back taxes and interest owed.
B. The worker may sue the payer for employee benefits they were not provided.
C. The payer may be audited by the Department of Labor.
D. All of the above

6. If a worker provides services to multiple payers and is classified as an independent contractor by one payer, does that automatically mean they are an independent contractor for all payers?

A. Yes, the worker's classification is consistent across all payers.
B. No, each payer must evaluate the worker's classification independently.
C. It depends on the worker's level of experience and qualifications.
D. It depends on the nature of the work being performed for each payer.

7. Can a worker be classified as both an employee and an independent contractor for the same payer?

A.No, a worker can only be classified as one or the other.
B. Yes, as long as the worker performs different types of services for the payer.
C. Yes, but only if the worker is classified as an employee for the majority of their services.
D. Yes, but only if the worker is classified as an independent contractor for the majority of their services.

8. What is the IRS Form used to report non-employee compensation paid to independent contractors?

A. Form W-2
B. Form 1099-NEC
C. Form 1040
D. Form 941

9. What is the IRS's Voluntary Classification Settlement Program (VCSP)?

A. A program that allows employers to reclassify workers as employees going forward and pay reduced penalties for past misclassifications.
B. A program that allows independent contractors to voluntarily become employees of a payer.
C. A program that provides tax credits to employers who hire independent contractors.
D. A program that provides legal assistance to workers who have been misclassified as independent contractors.

10. Which of the following factors is least important in determining worker classification according to the IRS?

A. The worker's level of experience and qualifications.
B. The nature of the work being performed.
C. The method of payment and reimbursement.
D. The amount of control the payer has over the worker's behavior and financial aspects of the job.

FIVE WAYS TO PROVIDE PEACE OF MIND TO YOUR CLIENTS WITH IRS PROBLEMS: EXPLORING TAX RESOLUTION OPTIONS

11. Factors for offer in compromise eligibility include:

A. Filing of all outstanding tax returns, if any.
B. Not in a bankruptcy proceeding.
C. Extension for the current year's return is valid if applying for the current year.
D. All of the above

12. Reasonable Collection Potential is a formula-driven process based on:

A. Available cash and property
B. Ability to pay the outstanding balance, income, expenses, and equity in assets.
C. Income and expenses only
D. Equity in assets and income

13. A taxpayer can pay for an OIC:

A. Over 72 months
B. Lump sum in cash
C. Over time with periodic payments up to 24 months
D. B and C

14. A taxpayer may enter into an installment agreement with monthly payments up to:

A. 6 years
B. Until CSED expires
C. 10 years
D. 24 months

15. To qualify for a partial payment installment agreement, a taxpayer has to owe a minimum of:

A. $5,000
B. No minimum
C. $25,000
D. $10,000

16. To qualify for a discharge of tax debt under bankruptcy, the tax debt has to be:

A. At least two years old
B. At least three years old
C. More than five years old
D. At least one year old

17. What methods may a taxpayer qualify for penalty abatement:

A. Reasonable cause
B. IRS agent discretion
C. First-time penalty abatement
D. Both A and C

18. Information about the offer in compromise program can be found in:

A. Form 9465
B. Form 433-F
C. Form 656-B
D. None of the above

YEAR-END CRYPTO TIPS FOR PRACTITIONERS

19. Ethereum replaced its consensus methodology with which option?

A. Proof of Capacity (PoC)
B. Proof of Activity (PoA)
C. Proof-of-Stake (PoS)
D. Delegated Proof of Stake (DPoS)

20. How popular is the Ethereum blockchain blockchain and cryptocurrency?

A. Ethereum is the first largest.
B. Ethereum is the second largest.
C. Ethereum is the third largest.
D. None of the above

21. Due to the Ethereum merge, the energy required to process Ethereum-based transactions will be lower by as much as?

A. 99%
B. 10%
C. 100%
D. 50%

22. PoS crypto could qualify as securities under which test?

A. Dewey
B. Computer-assisted audit technique
C. Howey
D. Long-lived assets

23. What is a type of cryptoasset?

A. Wash sale
B. Bitcoin
C. Tether
D. Non-fungible tokens

WHAT IS—AND ISN'T—INCLUDED IN THE INFLATION REDUCTION ACT OF 2022

24. What does AMT stand for?

A. Alternative Minimum Tax
B. Advance Minimum Tax
C. Alternative Maximum Tax
D. Alternative Minimum Total

25. The IRA imposes a new AMT on corporations equal to 15 percent their adjusted financial statement income if it exceeds:

A. $1 Billion annually over a five-year period
B. $1 Million annually over a three-year period
C. $1 Million annually over five-year period
D. $1 Billion annually over a three-year period

26. The corporate AMT is effective for tax years beginning after:

A. December 31, 2021
B. December 31, 2022
C. December 31, 2023
D. December 31, 2024

27. When a publicly traded corporation repurchases stock through a redemption, they may be subject to a surtax of:

A. 10%
B. 5%
C. 1%
D. 0.5%

28. The IRS does not impose the surtax when:

A. The purchase is less than $1 million.
B. The purchase is treated as a dividend.
C. The purchase is part of a tax-free organization.
D. Any of the above

29. What is the amount of IRS funding that has been allocated to enforcement?

A. $45.63 billion
B. $45.63 million
C. $64.45 billion
D. $50 million

30. What is the amount of IRS funding that has been allocated for Tax Court?

A. $45.63 billion
B. $45.63 million
C. $64.45 billion
C. $153 million

31. $15 million of IRS funding has been allocated to:

A. Development of a new e-file system
B. Treasury office expenses
C. Operations support
D. Tax Court

32. The $80 billion in funding for the IRS would be distributed over what period of time?

A. 1 year
B. 5 years
C. 10 years
D. 20 years

33. The Tax Cuts and Jobs Act increased the holding period of long-term capital gains treatment of carried interest:

A. From one to five years
B. From one to three years
C. From two to five years
D. From three to four years

34. **The proposed tax change that was removed from the Inflation Reduction Act would have increased it further to:**

A. 5 years
B. 10 years
C. 15 years
D. 20 years

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Like Father, Like Son

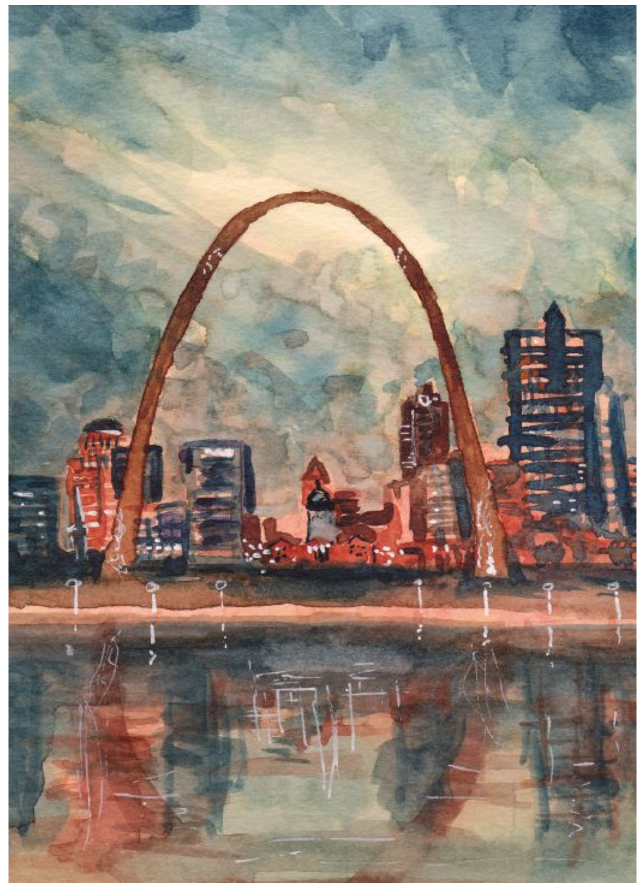
Brien G. Gregan, EA

My first tax season was in 2000 (the 1999 filing season). Three tax seasons later in September 2002 at 24 years old I became an enrolled agent. My father has been an enrolled agent for more than 40 years, so that is what started my interest in becoming an enrolled agent.

When I decided to take the Special Enrolled Examination (SEE), I sought out a preparation course that would help me prepare for the exam since I only had three tax filings seasons of experience. Christopher Bird, EA, was offering an enrolled agent preparation course in St. Louis, Missouri. I attended the course, and it helped me be prepared to pass the exam. I was fortunate to pass on my first attempt. Learning with others in a classroom setting and being isolated in the asphalt jungle (with nothing to do) of the part of St. Louis where the course was held was ideal for me.

I am now in the middle of my 23rd tax season and am grateful that I became an enrolled agent. I have been licensed to practice before the Internal Revenue Service (IRS) since May 2003, have 15 years of IRS and state representation experience, and 20 years of tax preparation experience. After joining the National Association of Enrolled Agents, I became a National Tax Practice Institute® (NTPI) fellow in 2009.

I have had the opportunity to help many taxpayers through Internal Revenue Service audits since I became an enrolled agent. It is a challenging profession that is constantly changing, and the past two tax seasons have been especially challenging with all of the COVID-19-related legislation. However, if you are preparing taxes, enjoy helping people, and are interested in tax law, I highly recommend taking the SEE. You won't regret it.



Brien G. Gregan, EA, is the president and founder of Tax Consultants, LLC.

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