

Scott Kauffman's...



# IRS Tax Advocate



A Legal Newsletter

*“Read About Taxpayers with IRS Problems & Learn Helpful Tips on How To End Them.”*

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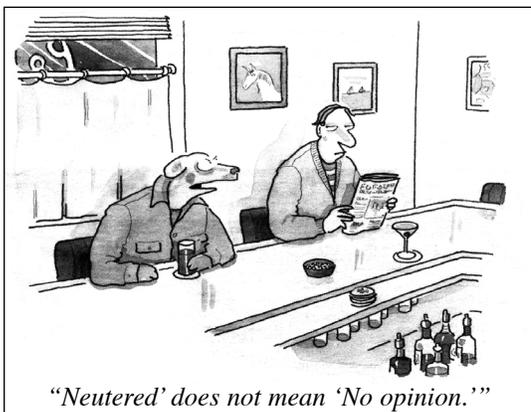
Learn How to Avoid

# IRS

problems and solve them if you find yourself with one!

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*“Neutered’ does not mean ‘No opinion.’”*

## THE GREAT TAX DROUGHT OF 2009

One reason this year’s deficit will set records? A big drop in revenue. Next year will be worse even if Congress fails to extend certain tax breaks. Much attention has been paid this year to the record-high spending and deficit accrued because of the financial and economic crisis Congress has inflicted upon us. But one of the driving factors that has gotten little notice is the plummeting tax revenue, which is a fallout of walloped company profits and savaged income streams. Through the end of August, the Federal government collected 25% less in tax revenue for the year that it did during the same period a year earlier due to a 56% drop in corporate income tax revenue and a 20% drop in individual income tax revenue.

## IRS TRAINS SIGHTS ON OFFSHORE EVADERS

The IRS is saying that more than 7500 taxpayers with undeclared offshore accounts stepped forward under its limited amnesty program that ended on October 15<sup>th</sup>. Now it is pushing to stop tax evaders from moving funds between foreign countries. The accounts ranged in size from \$10,000 to more than \$100 million in several hundred banks in 70 countries. The IRS says it is moving aggressively to identify funds moving out of European banks and into ones in Asia and the Caribbean and will be opening offices in Beijing, Sydney, and Panama City as well as adding staff in the Barbados and Hong Kong. The Obama budget calls for adding 800 additional agents.

## IRS TO FOCUS ON AUDITING THE RICH

A new IRS unit targeting the very wealthy is expected to help decode partnerships, offshore trusts, and other complex schemes used to hide income. The Global High Wealth Industry Group will launch a small number of audits with assets or income exceeding \$10 million. The creation of the group is in response to the complex web of entities and transactions many high net worth individuals use to manage their financial affairs.

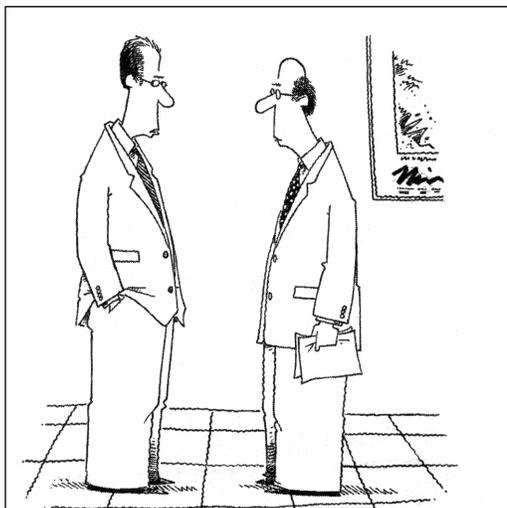
## HOME-BUYER CREDIT TEMPTS TAX CHEATS

Tens of thousands of taxpayers submitted suspicious – and possibly fraudulent – claims for a federal tax credit meant for first-time

*continued on page 2*

## INMATES BILK UNCLE SAM FOR MILLIONS

Officer Mark Lindback started his day off with a routine contraband check of a jail cell. He pulled up the inmate's mattress, ducked his head under the bed. No shanks or drugs, but he did find papers. Lots and lots of papers. The inmate immediately became irate. What Lindback found were tax forms along with instructions with social security numbers and birth dates. Investigators say Monroe County jail inmates in Key West had been filing false tax return forms for jobs they never had as far back as 2004 and getting thousands of dollars a pop in refund checks. By keeping their refunds to under \$5,000 a claim, the inmates thought they would fly under the radar, and they did so for years, passing around cheat sheets that showed line by line how to fill out the complicated forms. Federal investigators say the scam has been going on for decades in prisons.



*"One thing about prison, Ted: When that big iron door slams shut on you, your cell phone reception gets really crummy."*

homebuyers. At least 19,000 filers who had not bought homes claimed \$139 million in tax credits and were reimbursed. Treasury officials say they have discovered an additional 74,000 tax-credit claims valued at \$500 million, where evidence of previous home-ownership could make their claims invalid. More than 500 people under the age of 18, including a 4-year old child had their names on applications for credit. IRS says it is investigating more than 100 suspected criminal schemes involving the credit. One Jacksonville, Florida preparer was recently sentenced to 30 months in prison for preparing 15 tax returns that falsely claimed the homebuyer credit. IRS also says that is conducting more than 100,000 examinations that could require filers to give back the credit and pay civil penalties. IRS attributes the problems to a lack of safeguards including a lack of documentation.

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## “INDEPENDENT CONTRACTOR” LABEL CAUSING ISSUES

With the downturn in the economy, employers are avoiding hiring full-time employees by tapping contractors, and misclassification claims are rising. Revenue-strapped states are cracking down, seeking unpaid taxes. IRS has announced it will audit 6,000 random U.S. employers to quantify how many of them misclassify workers. Many employers, unfortunately, don't appreciate the risk with hiring contractors. From coal miners in the 1940's to Microsoft programmers in the 1990s, to Fed-Ex drivers recently, employers and the IRS have long sparred over the distinction. Contractors are not covered by minimum wage, overtime, and antidiscrimination laws, and employers do not need to pay unemployment insurance, workers' compensation, or Social Security taxes for them. IRS estimated in 1984 that employers misclassified 3.4 million workers, depriving the government of \$1.6 billion in tax revenue that year. The classification rules vary among the tax agencies, but boil down to the right to control the worker in the details of their actions. A class-action suit brought by exotic dancers in Massachusetts demonstrates how the recession is forcing the issue. Four current and former dancers at Ten's Showing Club in Salisbury are suing the club owners for misclassification and thereby depriving them of wages and benefits. Before the recession, the dancers could earn hundreds of dollars in tips per night, so they didn't object to not receiving an hourly wage and paying a small nightly house fee to dance. But business and tips are down, and managers have raised the house fee to as much as \$60 per night.

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## IRS DOESN'T WANT TO TALK TO YOU

The National Taxpayer Advocate says that an expanding slate of duties is stretching the IRS too thin, leading to poor customer service and undermining its ability to collect taxes. Even if the IRS meets its own goals, 29% of callers to the IRS's help line will not

## **STARVED STATES LEAVING NO STONE UNTURNED**

Financially strapped states are getting more aggressive, hoping that stepped-up enforcement and the posting of the names of delinquent taxpayers online will push more people to pay up. California, like other states, is mining IRS data for leads. Such efforts are designed to augment states' efforts to attack budget deficits that are projected to swell to \$55.5 billion for the fiscal year beginning July 1. California says that the difference between what is owed and what is paid is \$6.5 billion. The recession has caused a sharp drop in revenue. While California requires a balanced budget, the state has been cutting spending, increasing tax rates, and adding fees to eliminate deficits. These measures have not proved popular with voters, which poses problems for politicians in a year when 37 governor's seats are up for grabs. Collecting more of what taxpayers owe is less risky than again raising taxes and fees. California's efforts involve legal changes that compel agencies to work together as well as computer upgrades needed to sift through data. California, facing a \$20 billion budget deficit is considering requiring online retailers such as Amazon to collect sales taxes from customers in the state. California estimates it could collect \$150 million from the companies if the legislature passes the bill compelling payment. Amazon, however, abruptly ended its relationships with its marketing affiliates in Colorado after the state legislature passed a law requiring online retailers to collect sales tax or share information about purchases made by Colorado residents.

# **CHECK**

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# **IT OUT**

get through to a human being. Poor service will cause problems for the government and taxpayers alike because taxpayers will either give up and not file or make errors that must be resolved. IRS says it has been inundated with taxpayer calls in the past two years about temporary tax breaks passed by Congress to help revive the economy.

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## **IRS TO OVERSEE TAX FIRMS**

The IRS says it intends to regulate the thousands of tax-preparation companies. Under the new rules, tax-preparation firms will be required to pay a registration fee to the IRS, pass a competency exam, and have 15 hours of education a year. These requirements will apply to hundreds of thousands of independent preparers that offer tax preparation as one of several services. About 60% of taxpayers use tax preparers. The plan will take several years to implement, starting in 2011 when all preparers will have to register with the IRS and include an identification number on any returns they prepare. The basis for the regulation is that Government undercover visits found high levels of inaccuracies and distortions on returns. In 2006, the Better Business Bureau received almost 1500 complaints against tax preparers, ranking them 120 out of 3800 industry categories. In 2008, complaints jumped to 2,276, ranking the industry 80<sup>th</sup>.

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## **TAKE THE IRS TO COURT!**

Few taxpayers do and for good reason. Of the 300 cases argued by taxpayers without a lawyer, only 10% won. Many of the losers, though, were tax protesters who defended the filing of frivolous returns and were tilting at windmills. Others were simply on the wrong side of the law such as a horse enthusiast who wanted to deduct his hobby losses, an unsuccessful comedian who tried to classify his expenses as business losses, and a tax attorney who claimed \$100,000 in medical deductions for payments to prostitutes. One taxpayer who prevailed was a Maryland nurse who the Tax Court permitted to deduct \$15,000 in business school tuition. The audit process began with several rounds of confusing IRS correspondence including three requests for the same records, each with a different contact name. The IRS then summonsed her to Washington where she had to provide copies of her resume, a job description, and other records. The IRS still denied her deduction only to be reversed in the Tax Court.

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## **IRS COMES FIRST**

When working capital gets tight and your bank is slow to help with the taxpayer dollars its been receiving, it is tempting to borrow the payroll taxes withheld from your employees in order to kite the interval between payday and the day you are supposed to pay those amounts over to the IRS. Resist the temptation. Time and again I have seen those who make such a desperate gamble find them-

## UBS BANKER BEGINS PRISON TERM

Bradley Birkenfield, the key informant in the landmark U.S. case against the giant Swiss bank has reported to Federal prison in Pennsylvania to begin serving a 40-month sentence for helping UBS clients evade US taxes. Prosecutors have conceded that they would have had no case against UBS without Mr. Birkenfield's cooperation, but said they sought jail time because he was not forthcoming about his own role in the scheme. Mr. Birkenfield, however, is pressing the IRS for a rich payout as a whistleblower for exposing the Swiss bank's conduct. His claim could bring him tens of millions of dollars, but also take years to resolve. Maybe by the time he gets out.

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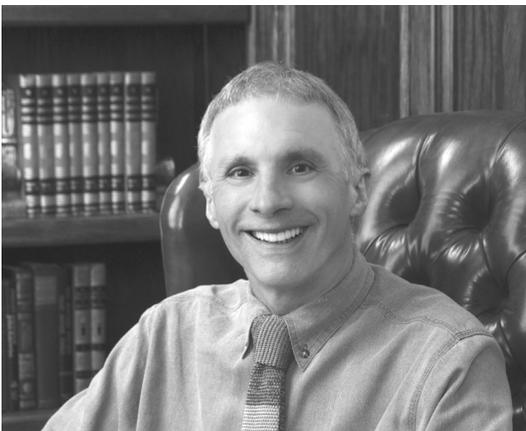
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## ***The Tax Advocate***



selves in deep trouble. First, there is personal liability. In addition, the civil penalty may be augmented by criminal prosecution. Employers are deemed to have withheld income and the employee's share of Social Security and Medicare taxes by paying their employees their wages, net of deductions. The withheld amounts are a fund the employers hold in trust for the government making it a trust obligation, not merely a debt. You cannot, however, be held personally liable for withheld taxes unless: (a) you are responsible for its collection and payment, whether as the owner of the business or a person authorized to handle its funds; and (b) your failure to collect the tax and pay it over are "willful." The person charged with personal liability has the burden of proving the absence of at least one of these elements. You do not have to be the owner of the business in order to be found responsible. The courts have made it clear that you can be found liable for the tax if you are in a position to exercise significant financial control – even if you do not have the final word – over the disbursement of funds. Whether your title is CFO or bookkeeper, if you are authorized to determine which creditors are to be paid and to issue checks you can be found responsible even if some payments are subject to a superior's approval. The easier question has to do with "willfulness." Failure to pay withholding taxes is willful if you pay other creditors when you don't have sufficient funds to pay the taxes you know to be due. Even an employee to whom you owe wages is regarded as just another creditor – the IRS comes first. If your company is teetering on the edge, you are better advised to close it down than to use the government's money as working capital. Liability imposed is not subject to discharge in bankruptcy and the statute of limitations for collections is ten years. The IRS comes first.

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