

# SCRIBNER, HALL & THOMPSON, LLP

SUITE 1050

1875 EYE STREET, N. W.

WASHINGTON, D. C. 20006-5409

(202) 331-8585

FAX (202) 331-2032

THOMAS C. THOMPSON, JR.  
MARK H. KOVEY  
STEPHEN P. DICKE  
PETER H. WINSLOW  
SUSAN J. HOTINE  
BIRUTA P. KELLY  
GREGORY K. OYLER  
LORI J. BROWN  
SAMUEL A. MITCHELL

FRED C. SCRIBNER, JR. (1908-1994)  
LEONARD W. HALL (1900-1979)

Writer's Direct Dial: (202) 434-9163

Writer's Email Address:

[kkosko@scribnerhall.com](mailto:kkosko@scribnerhall.com)

## Insurance Company Information Reporting and Withholding Update

October 2005

I.	Employer Issues and Employee Benefits . . . . .	1
II.	Employee Business Expenses . . . . .	1
III.	Other Matters . . . . .	3

## I. Employer Issues and Employee Benefits

### A. IRS Issues Proposed Regulations on Employment and Excise Taxes for Disregarded Entities

The IRS has issued proposed regulations (REG-114371-05) relating to employment and excise taxes for disregarded Subchapter S subsidiaries and single-owner eligible entities. The regulations would treat these entities that are currently disregarded as entities separate from their owners for federal tax purposes as separate entities for employment tax and related reporting requirement purposes. However, these entities generally would continue to be treated as disregarded entities for other federal tax purposes. Additionally, the new regulations would treat these disregarded entities as separate entities for the purposes of certain excise taxes. Thus, the new regulations impose liability on these disregarded entities for the payment of employment taxes and certain excise taxes.

Comments and requests for a public hearing are due by January 16, 2006, and should be sent to: CC:PA:LPD:PR (REG-114371-05), Room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Electronic comments may be submitted directly to the IRS via the IRS website at [www.irs.gov/regs](http://www.irs.gov/regs) or via the Federal eRulemaking Portal at [www.regulations.gov](http://www.regulations.gov).

### B. Employer-Provided Athletic Facility is not a Taxable Fringe Benefit

In response to a complaint, the IRS noted that employers may provide an athletic facility on premises owned or leased by the employer for the benefit of its employees. This facility would not be a taxable benefit even if the premises were not used by the employer for business purposes. The basic requirements for this exclusion are that the employer must operate the facility through its own employees or by contracting with a third party and substantially all of the use of the facility must be by employees, their spouses and dependent children. The complaint to which the IRS was responding charged that this exclusion was unfair since the same tax treatment was not available for independent athletic facilities.

## II. Employee Business Expenses

### A. IRS Explains Procedure to Determine Standard Business Mileage Rate

In a response to a Freedom of Information Act request, the IRS vaguely outlined its procedure for setting standard business mileage rates. An independent annual study of the fixed and variable costs of operating an automobile is conducted by an independent contractor who is

an expert in the cost analysis of business use of automobiles. The IRS declined to release further information since a court has ruled that the study's methodology, which is included in the report, constitutes a "trade secret" within the meaning of section 6110(c)(4) and, therefore, the study is exempt from disclosure.

B. Rules Updated for Substantiation of Traveling Employees' Lodging and Meal Expenses

The IRS issued updated rules for employees who are reimbursed for lodging, meals and incidental expenses, or for meal and incidental expenses only, which are incurred by the employee during business travel. Rev. Proc. 2005-67 updates Rev. Proc. 2005-10. The new rules provide guidance for the amount of ordinary and necessary business expenses which will be deemed substantiated when an employer or other party provides a per diem allowance or reimbursement under another expense allowance arrangement. The revenue procedure updates the list of high-cost localities and increases the per-diem rate for those locations to \$226 per day, up from \$204. The per diem rate for other localities not falling in the high-cost range was increased from \$129 to \$141.

Rev. Proc. 2005-67 also provides an optional method for employees and self-employed individuals who are not reimbursed to use in computing the deductible costs paid or incurred for business meal and incidental expenses, or for incidental expenses only if no meal costs are paid or incurred, during business travel. The IRS is not requiring taxpayers to use methods specified in this revenue procedure so long as they maintain adequate records or other sufficient evidence for proper substantiation.

C. No Business Mileage Deduction Without Proper Substantiation

In a summary opinion, the Tax Court held that a taxpayer would not be able to deduct the mileage expenses for his business use of his automobile, because he failed to properly substantiate those expenses.

Under section 162(a), a taxpayer may deduct ordinary and necessary expenses paid or incurred during the taxable year in carrying on a trade or business. A taxpayer may only take this deduction if it is substantiated by maintaining sufficient books and records. In the event that a taxpayer has incurred a deductible expense, but is unable to substantiate the exact amount, a court is permitted to estimate the deductible amount. An estimation of the deduction is only allowed when the taxpayer is able to submit sufficient evidence to establish a rational basis upon which the estimate can be made.

In Matthew P. Brown v. Commissioner, T.C. Summ. Op. 2005-155, Brown submitted weekly activity reports to his employer, which did not reflect the number of miles driven or other details about the specific business activity in which Brown was engaged. Furthermore, Brown maintained a day planner, but he lost the planner for 2001 and did not retain his 2002 planner. The court felt that the weekly activity reports did not rise to the level of substantiation required in order to be able to deduct the business mileage expenses. Additionally, the court held that Brown was liable for accuracy-related penalties under section 6662(a), which are equal to 20-percent of the portion of underpayment, which is attributable to the taxpayer's negligence or disregard of the rules and regulations.

### III. Other Matters

#### A. Hurricane Wilma Victims are Offered Tax Relief by IRS

The IRS announced on October 27 that deadlines for affected taxpayers to file returns and pay taxes among other things will be postponed to February 28, 2006, which is the same postponement granted for taxpayers affected by Hurricanes Katrina and Rita. The IRS postponed the deadlines for any tax return or payment with an original or extended due date falling on or after October 23. Furthermore, the IRS will waive the failure to deposit penalty for employment and excise deposits due before November 4, as long as the deposits are made by that date.

The IRS has requested that any taxpayer affected by the hurricane identify themselves by writing "Hurricane Wilma" in red ink at the top of any form or document filed with the IRS. For any questions regarding relief for the hurricane affected areas, the IRS has established a special disaster hotline at 1-866-562-5227.

#### B. IRS Releases Publication to Aid in Determining Work Status

The IRS released Publication 1779, Independent Contractor or Employee, which aims to help workers determine whether they would be classified as an independent contractor or employee. The publication focuses on three categories of facts to consider in determining work status: behavioral control, financial control and relationship of the parties. The publication also briefly discusses what it means to be designated either an employee or independent contractor.

#### C. IRS Discusses Idea of Information Clearinghouse

Darius Taylor, the director of Electronic Tax Administration development services for the IRS, addressed the attendees of a conference sponsored by the Council for Electronic Revenue Communication Advancement on October 26. In his speech, he noted that the IRS was in the

early stages of discussing plans for an “information document clearinghouse,” which would allow the IRS to create a repository of forms, such as Forms 1098, 1099 and W-2s, so that all information returns would be in one place for collection and dissemination. Audience members expressed concern regarding the potential security problems of a central document repository. Taylor acknowledged the concerns and noted that the IRS understands it is accountable for the protection of taxpayer information. Taylor expressed that it is a duty that is not taken lightly at the IRS. He again repeated that these discussions are in the very early stages, but the IRS has begun discussing the multiple layers of security measures that would need to be employed for this type of project.

D. Charters for IRPAC and IRSAC are Renewed for Two Years

The charters for the Information Reporting Program Advisory Committee (“IRPAC”) and the Internal Revenue Service Advisory Council (“IRSAC”) have been renewed for two-year periods beginning November 4. IRPAC advises the IRS regarding information reporting issues of mutual concern to both the private sector as well as the federal government. IRSAC serves as an organized public forum for discussions of relevant tax administration issues.

*IRS Circular 230 Disclosure:*

This memorandum is provided solely for informational purposes and is not intended to furnish legal advice with respect to the reader’s particular factual circumstances. In accordance with § 10.35 of IRS Circular 230 requirements, you are advised that any discussion of tax issues in this memorandum is not intended or written to be used, and cannot be used, to avoid penalties imposed under the Internal Revenue Code or to promote, market or recommend to another party any transaction or matter addressed herein. The persuasiveness of this memorandum with regard to the tax issues in question and a taxpayer’s good faith reliance on the memorandum will be determined under applicable provisions of the law and regulations (§ 10.35(f)).