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INSURANCE COMPANY INFORMATION REPORTING AND WITHHOLDING UPDATE

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Forms 1099, Backup And Foreign Payee Withholding, And Penalties

1. IRS Updates IRM Form 1042 Examination Procedures

The IRS recently updated Internal Revenue Manual section 4.10.21, *the Examination of Returns-U.S. Withholding Agent Examinations - Form 1042*. The IRM provisions provide extensive guidance relating to such examinations, including detailed procedures for U.S. financial and nonfinancial institutions that may have nonresident alien withholding tax and reporting related to their payment to foreign persons.

Last January, at the Foundation for Accounting Education's annual international taxation conference, Barry Shott, Deputy Commissioner (international) in the IRS Large and Mid-Size Business Division warned corporations that they may be overlooking withholding tax obligations under Treas. Reg. § 1.1441-7(a). Under Treas. Reg. § 1.1441-7(a)(1), a person is considered a withholding agent for purposes of section 1441 and its related provisions if the person has control, receipt, or custody of any amounts subject to withholding. Every withholding agent must file an information return, *Form 1042-S, Foreign Person's U.S. Source Income Subject to Withholding*, to report amounts paid during the preceding calendar year. Shott explained that tax executives may not be checking with their accounts payable office for payments fixed, determinable, and periodic income that trigger withholding requirements.

IRS examination of such payments is now part of the basic audit plan for revenue agents examining Form 1120 corporate tax filings. The new IRM provisions provide companies with a detailed view of the IRS examination procedures in connection with Form 1042 filings. Internal Revenue Manual section 4.10.21 can be viewed online at <http://www.irs.gov/irm/part4/ch09s24.html>.

Reporting Guidelines And Forms

2. IRS Updates Guidance for Substitute Forms

The IRS has issued Rev. Proc. 2008-36, 2008-33 I.R.B. 340 (superceding, Rev. Proc. 2007-50, 2007-31 I.R.B. 244) which provides requirements for reproducing paper substitutes and for furnishing substitute recipient statements for Forms 1096, 1098, 1099, 5498, W-2G, and 1042-S. Rev. Proc. 2008-36 will be reproduced as the next revision of Publication 1179. Changes include the following:

- **Where to file.** Information returns filed on paper will be filed with only two Internal Revenue Service Centers: Austin, TX, and Kansas City, MO. Do not file Form 1098-C at the Internal Revenue Service Center at Ogden, UT, after December 31, 2007.
- **Magnetic media filing no longer acceptable.** All references to magnetic media have been removed from Publication 1179 and from all forms to which the publication refer. Enterprise Computing Center-Martinsburg (ECC-MTB) will no longer accept tape cartridges for returns filed after December 1, 2008. After that date, electronic filing will be the only acceptable method for filing returns with ECC-MTB.
- **Form 1099-R.** The following changes were made to the Guide to Distribution Codes:
 - (1) For Distribution Code 1, reference to the qualified reservist distribution under section 72(t)(2)(G) has been deleted due to expiration of the provision.
 - (2) An exception was added to Distribution Code 2 for distributions that are permissible withdrawals under an eligible automatic contribution arrangement under section 414(w).
 - (3) New Distribution Code H, Direct rollover of a designated Roth account distribution to a Roth IRA, has been added.
 - (4) Distribution Codes B and D are a valid combination for 2008.
- **Form 1042-S.** The boxes on Form 1042-S have been changed and reconfigured for 2008. The major changes are to -
 - (1) Boxes 7 through 9. These boxes are used to show the amount withheld, the amount withheld by other withholding agents, and the total amount of tax withheld.
 - (2) Box 15. This box is used to show the recipient's foreign tax identifying number, if any.
 - (3) Box 22. This box is used to show the recipient's account number (optional).

Logos, slogans, and advertising

In addition to the above changes, guidance is provided in Rev. Proc. 2008-36, section 1.3.2, to respond to questions concerning whether substitute payee statements containing logos, slogans, or advertising were valid payee statements. (Guideline in the form of amended regulations was originally anticipated.) As we reported in last month's issue, the IRS announced that, with the exception of the electronic tax logo (i.e., the IRS e-file logo), the IRS has determined that slogans, advertising, and other logos will not be allowed on Forms 1096, 1098, 1099, 5498, W-2G, 1042-S, or any payee statements reporting amounts paid during the 2010 calendar year, and thereafter. See Rev. Proc. 2008-33, 2008-28 I.R.B. 93. The IRS e-file logo on the IRS official employee copies may be included, but it is not

required, on any of the substitute form copies. The new rules reflect the IRS' concern that some Forms 1098, 1099, 5498, W-2G, and 1042-S that include logos, slogans, and advertisements may be confused with questionable forms, and that a payee may not recognize the importance of the payee statement for tax reporting purposes due to the use of logos, slogans, and advertisements.

If you have comments about the prohibition against including slogans, advertising, and other logos on information returns and payee statements, send your comments to: Internal Revenue Service, Attn: Substitute Forms Program, SE:W:CAR:MP:T:T:SP, IR 6526, 1111 Constitution Ave., NW, Washington, DC 20224.

3. IRS Releases Draft Corporate and Partnership Tax Forms, And Requests Comments

The Internal Revenue Service has released for public comment draft revisions to Form 1120, *U.S. Corporation Income Tax Return*; Form 1065, *U.S. Return of Partnership Income*; and certain related schedules. See IR-2008-92. Included in the release are new Schedule B for Form 1120 and Schedule C for Form 1065. See IR-2008-92.

The major change to Form 1120 is to Schedule K and involves reporting direct and indirect ownership. The new Schedule B (Form 1120) is required of corporations that file Form 1120 Schedule M-3. Schedule B (Form 1120) will provide IRS information about allocations, transfers of interest, cost sharing arrangements, and changes in methods of accounting. Questions and comments regarding these changes *only should be e-mailed* to the IRS at Judith.A.McNamara@irs.gov by August 25, 2008. The draft forms are available on the IRS website at <http://www.irs.gov/businesses/article/0,,id=185271,00.html>.

4. IRS Denies FUTA Refund Based on Common Law Definition of Employer

In CCA 200827007 (March 10, 2008), the IRS concluded that the taxpayer, a staffing company, was not entitled to a Federal unemployment tax (FUTA) refund because it was not the employer for FUTA purposes. Then IRS reached this conclusion irrespective of whether the company was treated as the employer for state unemployment tax purposes or for purposes of section 3401(d), relating to FUTA withholding. In a heavily redacted memorandum, the IRS cited Rev. Rul. 57-471 and noted that the determination of employer status for FUTA purposes is based on common law. Thus, the status of the taxpayer as an employer for statutory purposes or for state unemployment tax purposes was not relevant. Because the IRS determined that "it is a fair assumption that the Taxpayer is not the common law employer," the IRS concluded that the FUTA refund should be denied even though the taxpayer was required to withhold pay over the FUTA tax liability under section 3401(d)(1), because it controlled the payment of wages.

Ask The Expert

What is the status of broker basis reporting proposals?

Despite broad-based opposition broker reporting rules by the financial community, two such provisions continue to be introduced. On July 24, Senate Finance Committee Chair Max Baucus (D-MT) introduced a revised energy and tax extenders bill, S. 3335, the “Jobs, Energy, Families and Disaster Relief Act of 2008.” The bill includes a provision to increase revenue by requiring broker reporting to the IRS of customers’ basis in securities transactions. A broker reporting provision was also included in the President’s fiscal year 2009 budget proposal, and appears to be included in Obama’s tax plan. *See* 2008 TNT 159-18, *Obama Campaign Releases Updated Summary of Tax Plan*, August 14, 2008 (Obama proposes increasing reporting of capital gains to close the tax gap).

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