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UPDATE…FROM THE NCCPAP PRESIDENT

ANDREW L. HULT, CPA

This message has three parts. First is an invitation to you to attend NCCPAP National's quarterly meeting in Washington, D.C. in May. Second, I touch on the state of the accounting/auditing profession. And finally, Executive Vice President Lana Kupferschmid reports to you on her activities for NCCPAP.

Part 1—NCCPAP on the Hill
Much of this *Journal* is devoted to the issues that NCCPAP will be discussing with the IRS and various congressmen. I just want to remind you that you are welcome to attend the meeting, the dates are May 11, 12 and 13, and the event will be held in the beautiful Madison Hotel in downtown Washington, D.C., at IRS headquarters, and on the Hill.

Part 2—It's Time to Change the Oil…
In my opinion, GAAP, GAAS and Peer Review all need work. (The following thoughts are mine, not NCCPAP's. If they strike a responsive chord, please consider joining NCCPAP National's Issues Committee to formally address them.)

Smaller firms are giving up their attest work because there's too much sludge. In other words, we've made attest work for smaller entities more complex than it needs to be. In turn, fees are higher than many smaller entities can afford, and practitioners' profit margins have shrunk to unacceptable levels. This doesn't need to be the case.

There is an unresolved tension between principals-based and rules-based accounting. In Hegelian terms, if one is the thesis, and the second is the antithesis, then we need a new synthesis, at least for private companies and small and mid-sized accounting firms.

There is a real need for rules-based accounting because our society is so litigious. Accountants need professional guidelines to protect themselves in the courts. Still, it feels as if we've gone too far. Some of the financial standards seem to address issues no more relevant to my practice than the medieval theological question, "How many angels can dance on the head of a pin."

With this in mind, I have hope for the "Private Company Financial Reporting" initiative sponsored by the AICPA. It calls for a different, more appropriate GAAP for privately held companies to be promulgated by a new board under FAF, but separate from the public-company-focused FASB. An AICPA representative will attend our Issues Committee meeting in Washington in May in order to explain the initiative. If you're interested and want to have input, please attend. We then look forward, in subsequent months, to working with the AICPA and other organizations to influence shape and content. The AICPA is actively seeking our help and input on this issue.

I have concerns, of course. Will "belt and suspenders" lenders accept financial statements prepared on the "Private Company Financial Reporting" basis? How much of a public relations effort might be required?

GAAS — I applaud the introduction of the risk-based approach to auditing. If I have it right, the concept is slick. Implementation is the sticking point. There are

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UPDATE...FROM THE NCCPAP PRESIDENT *(continued from page 1)*

too many checklists. And commercially available audit programs often are often excessive.

The risk-based audit approach is intended to focus audit effort on areas of highest audit risk. Perversely, it has spawned additional complex checklists to assess that risk. In the immortal words of Pogo the Conqueror, "We have met the enemy and they are us…." We've done it to ourselves again.

Strangely, I think that the Peer Review Program might share in the responsibility. Auditors in smaller firms will naturally desire assurance that a peer reviewer will accept their audit programs. Accordingly, they will tend to use audit programs that are themselves peer reviewed. And such programs will tend to be generalized, "one-size-fits-all," which may help to explain the current popularity of cumbersome, audit-cost inflating, commercially available audit programs.

What's the solution? I think that the auditing community needs to settle on, and promulgate widely, clear, concise criteria for audit programs in the smaller firm arena. And, there should be a consensus among auditors and peer reviewers as to what constitutes an appropriate approach to risk assessment. Small firm auditors need assurance that they and their peer reviewers are reading out of the same, professionally developed, playbook.

PEER REVIEW—I support peer review. The peer reviews that I have had have helped me become a better professional. However, there is room for improvement in the system.

As I understand it, a peer reviewer needs to assure himself or herself that there is a system in place and that that system will produce consistent results. One of my concerns is that, in some cases, there is not enough focus on the accuracy of the peer reviewed financial statements.

I am still haunted by the ENRON debacle. Clean peer review. Failed audit. Our profession can't tolerate this, and neither can the financial community. Think PCAOB.

If we went to a six-year cycle, could we find a better balance? The first peer review might focus on systems. Three years later, the second might focus on the accuracy of the work product.

I don't know the answer. I have discussed with Bob Goldfarb, Chair of the Issues Committee, and Frank Gallo, Chair of the Peer Review Committee, the need for a subcommittee to study this matter either independently or in conjunction with the AICPA Peer Review Committee. Please Bob or Frank if you would like to participate.

I take comfort in the fact that, while I and everyone I know finds the peer reviews burdensome, I have the utmost respect for the peer reviewers with whom I have had the privilege to work.

In sum, it seems as if we need not only an oil change but a new filter as well. Please share your insights and opinions. NCCPAP is practitioners helping practitioners. Let's work together to sort these things out. My telephone number is 516-565-1702. My e-mail is alhult@alhcompany.com.

Part 3—Report from the Executive Vice President

Over the past year and a half as Executive Vice President, I have been involved with many NCCPAP committees and chapters. Sometimes, I listen to the issues or help to resolve the problems of the President, other Vice Presidents and some Chapter Presidents. As founder of the

UPDATE...FROM THE NCCPAP PRESIDENT *(continued from page 2)*

New Jersey chapter, I have great concern for the growth and success of that chapter and work closely with Fred Bachmann, NJ Chapter President. I attended a meeting of the emerging Delaware Valley, Pennsylvania chapter and enjoyed talking with some potential members, along with executives of ADP who are anxious to work with us to help us expand our organization. As Chairperson of the Forward Planning Committee, I have been working with committee members to develop and implement a long-range plan. With the consent of the Executive Board, the last board meeting turned into a strategic planning session that really opened our eyes to our strengths, weaknesses and where we want to be in five years.

Over a year ago, our President, Drew Hult, asked me to look into updating and redesigning our web site. I spoke to many members who requested that our site become more user friendly and filled with information that will enable our members to succeed, plus provide NCCPAP with more online visibility. We developed a team, headed by Don Ingram, Chairman of the Technical Committee, and hired a web designer with marketing know-how, Deb Buckley of eMarketing4us. Week after week we have been teleconferencing along with the other dedicated team members, Ed Caine, David Rothfeld, Carol Markman and Bob Markman to transform our web site into a dynamic site that will enable our members to have access to information that will help them run their practices, inform our members of all NCCPAP events, and invite others to learn about our wonderful organization. Week after week, even through tax season, the team has held conference calls to coordinate our efforts. Soon we will bring our proposal to the board for approval so that we can launch the new site. We trust that our efforts will bring benefits for all of our members.

I urge you to share suggestions to help strengthen and improve our organization. Please feel free to email me at lanakcpa@aol.com. And don't forget to become a member of the NCCPAP group on Linkedin.com.

— Lana Kupferschmid, CPA Executive Vice President

NCCPAP
SUMMER CONFERENCE

SAVE THESE DATES!

Wednesday, August 3
Thursday, August 4
Friday, August 4

SOFITEL
Philadelphia, PA

2011 LONG ISLAND TAX PROFESSIONALS SYMPOSIUM

Wednesday, November 16
Thursday, November 17
Friday, November 18

Crest Hollow Country Club, Woodbury, NY

A GENTEEL GIANT

LEON D. ALPERN, CPA, passed away on January 12, 2011, at the age of eighty-nine. We will miss him.

Lee was a member of NCCPAP almost from its inception, and he played a mighty role in the development of the Nassau/ Suffolk Chapter. An account of the positions he held includes Chairman of five committees (Education, Tax Liaison, Nominating, Ethics, and By-Laws), Vice President, and, in 1992-93, President. However, this list doesn't even come close to capturing his essence. Steve Greenberg did that when he wrote the following:

> *"Lee was a rare combination of strength and professionalism mixed with kindness and compassion. Lee could listen to another point of view when he vehemently disagreed. Having worked together on bylaws, I can attest to his absolute attention to detail without losing sight of the big picture. Lee could make people feel welcome and part of the team. He never did anything half way. He could converse about many things equally well, including politics (*Meet the Press *was his favorite), the Yankees, his grandchildren or anything else. Most of all, Lee was a friend. Not because he said he cared but because you knew he cared. There was nothing phony or contrived, no excuses and no cover-ups. He called it the way he saw it, but without being hurtful. Needless to say, losing Lee was a big loss for me and almost anyone that knew him."*

Peter J. Ciccone reminisces:

> *Lee Alpern and I have been friends for more than thirty years. We met at a NCCPAP meeting and, in a word, I was very impressed. Not only had he built a successful accounting firm, but he was open, honest and a gentleman personified. Together, we worked on the National Tax Committee to investigate all of the "flat-tax" proposals that were being put forth in Congress.*
>
> *Lee showed me how a good accountant goes about learning and delving into the tax codes and how to dissect and evaluate the various proposals. To say he was a good accountant means very little because he was much more.*
>
> *Lee was a friend, a confidante and a person who was always willing to help and advise or just listen.*
>
> *I find it difficult to express my true feelings since I am limited by words. Suffice it to say he was the best and I will miss him.*

Sally, you and your family have our condolences. And Lee, NCCPAP will miss you while we honor your legacy.

Students Win Accounting Scholarships

by Lana Kupferschmid, CPA; Chair, NCCPAP Scholarship Committee

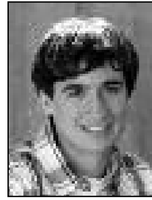
The National Conference of CPA Practitioners (NCCPAP) and the American Institute of Certified Public Accountants (AICPA) pooled their resources to offer scholarships to deserving high school seniors wishing to pursue a career in accounting. This year the scholarship program awarded eleven students $1,000 each. Our well-deserving students are:

Christa Allen will graduate from Huntingtown High School in Huntingtown, Maryland. In the fall she will proudly attend Meredith College in Raleigh, North Carolina. Her goal is to major in accounting, receive a master's degree in accounting and earn certification as a public accountant.

Mary Bailey will graduate from Bethel Park High School in Bethel Park, Pennsylvania with a 4.3 QPA. Her accounting studies includes an Independent Study Accounting (Honors) class. In DECA competition she placed first in the Accounting Application Individual Series Event (District Level), the first step towards competing at the International Development Conference. Mary plans to major in Accounting and possibly minor in Spanish. She is an Allegheny Mountain Swimming Scholastic All American and a National Honor Society member since her sophomore year.

Callie Bubb will graduate from Greenport High School on Long Island, New York. In the fall she will study Accounting and Finances at the University of Albany, University of Delaware or Fordham University at Rose Hill. Callie is a member of the National Honor Society and was editor of the yearbook. She was also in varsity cheerleading, varsity field hockey and varsity softball.

Michael Casias is in the top 5% of his class at North Stafford High School in Stafford, Virginia. He plans to attend Wharton School of Business and major in accounting. Michael has been a class officer for three years, in National Honor Society and Future Business Leaders of America. He was awarded the Virginia Society of CPA's Award of Achievement in his sophomore and junior years. A three-year varsity starter in football and captain twice, Michael will play football at University of Pennsylvania.



Jonathan Coppolino will soon graduate from Quabbin Regional High School in Barre, Massachusetts. He plans to study accounting at a four year university. He is a member of the National Honor Society, Blue/Gold Key Society and Spanish Club, and has participated in the varsity football and tennis teams.

Kim Jamros will graduate from Silver Creek High School in Sellersburg, Indiana and then major in Accounting at Bellarmine University or Indiana University Southeast. Kim is in charge of the Silver Creek student-run bank for students and staff, and is a member of the Silver Creek Academy of Finance, affiliated with the National Academy Foundation (NAF). She presented NAF's new "Monopoly Accounting" curriculum at their 2010 Conference, has attended the Business and Accounting Summer Education Camp, and participated in two years of Job Shadowing. She is president of the National Honor Society and was on the Academic All-State Team for Volleyball.

Kevin Krautscheid will graduate from Centennial High School in Gresham, Oregon, where he took every AP and advanced course given. Kevin plans to attend Santa Clara University or University of Portland, major in accounting and management and become a CPA. In Future Business Leaders of America (FBLA) he was chapter community service Chairman, Treasurer/ Secretary, and Executive Vice President, and VP of Oregon FBLA (Mt. Hood). Kevin won state championship titles in Accounting I and Community Service Project, after chairing a project that raised over $11,000 for March of Dimes. Kevin was also Student Body Treasurer, National Honor Society Treasurer, Freshman Mentor, and on the Cross-Country and Track & Field teams.

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Timothy Schloz will graduate with honors from Whitmer High School in Toledo, Ohio, in the top 15 of over 500 seniors, and will study accounting at University of Toledo. He is a member of National Honor Society, Mu Alpha Theta, and Speech and Debate. Tim is a four-year varsity cross country runner and a former Buckeye Boys State delegate.

Cameron Scotese will graduate from Washington Township High School in Sewell, New Jersey. Assisted by the NCCPAP/AICPA scholarship, Cameron will obtain a B.S. in Accounting and become a CPA. He is vice president of the Business Education Honor Society; Executive Board Member of DECA, where he participated in the NJ state competition; and a member of National Honor Society, German National Honor Society, National Society of High School Scholars, U.S. Achievement Academy, Positive Coaching Alliance and Regional Qualifier for FBLA. He plans to play soccer in college.

Edianí Ramírez Torres, who was born in Mayagüez, Puerto Rico, is a senior at the Colegio Episcopal San Andrés at Mayagüez, Puerto Rico. After graduation he is planning to attend the University of Puerto Rico, Mayagüez Campus, and work towards a bachelor's degree in Accounting.

Kelly Valentine will graduate from Point Pleasant Borough High School in Point Pleasant, New Jersey, where she is ranked in the top three percent of her class. Kelly plans to attend Rutgers University in the fall and pursue an MBA/CPA. Kelly is the current FBLA treasurer and a member of the National Honor Society, Leo Club, Yearbook Committee, School Newspaper, and Peer Mediation. She playing first base on the varsity softball team and has participated in the Challenger softball program.

NCCPAP and the AICPA wish these future CPA's a very successful future in college and beyond!

New York State Wage Theft Prevention Act:

What Does it Mean to Employers?

by Hadley C. Margolis

The New York State Legislature recently enacted the Wage Theft Prevention Act. The Act expands upon New York State Labor Law 195 passed in 2009 to provide new protections to employees and stiffer penalties to employers who fail to abide by the new regulations and fail to pay overtime or the minimum wage to employees. The Wage Theft Prevention Act will become effective April 12, 2011.

The New York State Labor Law already requires employers to notify all newly hired employees at the time of hiring, in writing, of their regular rate of pay, regular payday, and overtime rate of pay if they will be eligible for overtime. The Act now also requires employers to include the basis of the wage payment (e.g., whether paid by the hour, shift, day, week, salary, piece, or commission, or another basis) as well as the employer's intent to claim allowances (e.g., tip or meal allowances) as part of the minimum wage. These new and expanded notices must be provided in English AND in the language identified by EACH employee as his or her primary language. An entirely new notice must be provided each year on or before February 1st.

Employers must obtain signed and dated written acknowledgments of such notices from all employees, including executives, and must retain them for six years. The notice must be updated and provided again to the employee at least seven days prior to any changes to the employee's pay or other terms, unless such changes are reflected in the employee's wage statement (pay stub).

The Act now requires more information on the pay stub in addition to dates of work covered by the payment of wages, employee's name, rate of pay, gross wages, deductions, allowances, net wages. For non-exempt workers it includes their hourly and overtime rates of pay and the number of regular and overtime hours worked. The Act requires employer name, DBA (if applicable), address, phone number and corporate office address, if different.

If an employer fails to provide its employees with the information each payday, or fails to get his or her signature on the form acknowledging the pay rate, the employer could be sued by the employee or commissioner for $50 to $100 per week in violation. Also, employers could be fined or imprisoned for retaliation against the workers.

To summarize, although the new law does not radically change the employer's duties, it does add a number of new burdensome notice and record-keeping obligations. The Act does impose significant civil and criminal penalties for employers who violate the law.

Hadley Margolis is president of Best Payroll Services. He can be reached at Hadley@bestpayroll.net if you have any questions regarding the new law.

– Congressional Agenda –

REPEAL OF FORM 1099 REPORTING BURDEN UNDER SECTION 9006 OF THE PATIENT PROTECTIONS AND AFFORDABLE CARE ACT

BACKGROUND

For certain distributions made after December 31, 2011, pursuant to Section 9006 of the Patient Protections and Affordable Care Act, all businesses will be required to prepare and submit 1099-MISC forms to any and all businesses for both merchandise and services in excess of $600 per year.

PROBLEM

The law that was enacted places a significant burden on all businesses and business owners, especially small business owners. We do recognize the need to close the revenue and reporting gap that currently exists and are in favor of taking actions to do so. However, small businesses do not have the manpower nor the time or necessary resources to be able to meet the reporting requirements as enacted. In addition, the new rules will place an undue burden on CPAs and accountants, as it will place additional onus on them to assist in the preparation of these forms.

It should be noted, however, that the issuance of 1099-MISC (which reflects disbursements made on a calendar year basis) may be moot as many businesses operate on a fiscal year ending in months other than December. The matching process for these entities will prove to be useless as the information on Forms 1099 issued may be significantly different from what would be reported on their respective income tax returns.

It is not the position of the CPA to advise the client on how to not report income. We are only in a position to recommend that the business owner reports all income and expenses so that a true picture of a business may be presented, either on a tax return or a financial statement. Neither is it the responsibility of a business owner to ensure that those whom they do business with report all the income that is paid to them.

RECOMMENDATION

H.R. 5141 was introduced on April 26, 2010, by Representative Daniel Lungren (3-CA). Known as the "Small Business Paperwork Mandate Elimination Act," passage of this bill would eliminate the financial and administrative burdens for business owners as discussed above. Subsequent bills have been introduced into Congress since then, calling for the repeal of Section 9006 of the Patient Protections and Affordable Care Act, all of which have failed to obtain passage.

Due to significant hardships that would be placed upon small business owners, without a significant corresponding increase in revenue to be generated for the Treasury or a significant increase in reporting compliance, we recommend the immediate and total repeal of Section 9006 of the Patient Protections and Affordable Care Act.

INDEPENDENT CONTRACTOR ISSUES

BACKGROUND

There is a bill in Congress, S.3786 and HR.1234, "The Fair Playing Field Act of 2010," which addresses the issue of the independent contractor vs. the employee. Currently, the Treasury Department and the Internal Revenue Service are prohibited from issuing guidelines for the determination as to whether a worker is an independent contractor or an employee. This restriction is in effect under Section 530 of the Revenue Act of 1978.

PROBLEM

This bill is intended to ensure that workers are afforded protections already in the law and help the employers who play by the rules so that they are not forced to compete against those businesses that do not. The purposes of this Act are to permit the Secretary of the Treasury to provide guidance allowing workers and businesses to clearly understand the proper federal tax classification of workers, and to provide relief, allowing for an orderly transition to new rules designed to increase certainty and uniformity of treatment. The legislation requires the Secretary of the Treasury to issue prospective guidance clarifying the employment status of individuals for Federal employment tax purposes.

We find that there are several issues that place NCCPAP in the position to recommend that this bill should not be passed into law:

1. It is our belief that this will not help close the "Tax Gap." Certain employers will still make use of illegal workers who do not have social security numbers and are undocumented
2. While some state legislatures have passed similar laws regarding workers in their respective states, other states have not. Such legislation is in the process of being challenged within the state courts.
3. If state legislation contradicts with federal legislation, which law will the employer be required to follow?
4. This legislation, if passed, would require additional paperwork for employers as they would be required to provide a written statement to independent contractors notifying them of the Federal tax obligation, the labor and employment law protections that do not apply to independent contractors, and the right of such independent contractors to seek a status determination from the IRS.

We would like to point out that within our profession there are many practitioners who own their own corporations, and who do work for colleagues on a per diem basis as independent contractors. Payments for these services are paid to the corporation, not the practitioner directly. The relationship may be constant or infrequent, depending on the need of both the practitioner needing help and the one looking for additional work.

RECOMMENDATION

We understand the need for such legislation. However, we believe that should this become law, additional discussions are needed in order to make this truly effective. NCCPAP would welcome the opportunity to participate in such discussions, as a blanket policy would be unfair to those who operate within the current required parameters.

We agree that The Fair Playing Field Act of 2010 should:

- end the moratorium on Internal Revenue Service (IRS) guidance addressing worker classification;
- require the Secretary of Treasury to issue prospective guidance clarifying the employment status of individuals for Federal employment tax purposes;
- amend the provisions of the Tax Code that provide for reduced penalties for failure to deduct and withhold income taxes and the employee's share of FICA taxes;
- not require persons who contract independent contractors on a regular and ongoing basis to provide a written statement to each independent contractor of the Federal tax obligations of independent contractors, the labor and employment law protections that do not apply to independent contractors, and the right of the independent contractors to seek a status determination from the IRS; and
- require the Secretary of the Treasury to issue annual reports on unresolved worker misclassification issues.

We strongly believe that the federal legislation go one step further and have the classification apply to all state departments of taxations, attorneys general, labor departments (federal and state) and other jurisdictions. For example, in Senator Kerry's home state, employers are subject to different interpretations from the Internal Revenue Service, Massachusetts Department of Revenue and the Massachusetts Attorney General.

Taxpayers should be subject to the same Form SS-8 filing as employers.

Contracting entities should be given five years before any penalties are assessed. This will allow time for the IRS to release regulations and employers to review them for applicability.

Suggested guidelines for determination of employee or independent contractor status might include:

- Average hours worked per quarter over a certain period
- Percentage of total business of the independent contractor with contracting entity
- Structure of independent contracting unit — corporation, LLC
- Rules for independent contractor operating a business with partners, other shareholders and/or employees treated differently than sole providers
- Rules for different types of industries, occupations, and professions
- Safe harbor or unprotected occupations as outlined by the Internal Revenue Service Determination Unit

CHANGE IN DUE DATES FOR RETURNS

BACKGROUND

With the growth of tax and financial planning, there has in recent years been unprecedented growth in the creation of partnerships and trusts. Changes in tax law and the Internal Revenue Code have now allowed entities that were previously prevented from becoming co-owners, shareholders, or members of such, to do so. In addition, other changes have allowed for an expansion in the number of owners of these entities. This has, in turn, placed an additional burden on the tax return preparers in providing information to these owners on a timely basis.

Two years ago, the Internal Revenue Service made a modification in the due date for Partnership (Form 1065) and Fiduciary (Form 1041) Tax Returns. These returns with a due date for the return of April 15th had their period of extension shortened by one month, from October 15th to September 15th. This was done to allow the partners, or beneficiaries, to have their own tax returns prepared by October 15th, and these individuals would have to file either an incomplete return, to avoid the need for filing an amended tax return, or filing the completed return late, subjecting them to late filing penalty and interest charges.

PROBLEM

The due date for the various income tax returns has not changed. There is still an overwhelming burden on the tax return preparer to meet these deadlines. Despite the development of technology, the human factor — getting the information from the clients — is still a burden on the preparer. The taxpayer, be it a business entity or an individual, operates at his/her own pace, making the gathering of their information for the preparer difficult at times. Many a tax preparer has had a client come to them just before the due date for the tax return, expecting a return to be created immediately. In addition, simultaneous due dates make it difficult for returns to be completed on a timely basis. A business may hold an interest in a partnership, but may not be able to file a timely tax return as it is awaiting the information from the partnership to include in its tax return.

RECOMMENDATION

NCCPAP recommends that the following changes be made in due dates, both for an original filing and the extension, if necessary:

Form 1040 – April 15 and October 15
Form 1041 – March 15 and September 15
Form 1065 – March 15 and September 15
Form 1120 – April 15 and October 15
Form 1120S – March 15 and September 15

HEALTH INSURANCE PREMIUM DEDUCTIBILITY

BACKGROUND

Businesses operating as an unincorporated entity with a single owner report their income and expenses on Form 1040, Schedule C. Unlike an incorporated business, they do not have the ability to claim any health insurance premiums as a deduction against the income that this business generates. A corporation, operating either as a Subchapter S or a C Corporation is allowed to take health insurance premiums as a deduction in the determination of the entity's net income. An unincorporated business is not. In the Small Jobs Act of 2010, a sole proprietor is to take into account health insurance premiums as an additional deduction against unincorporated income (Form 1040 Schedule C and Form 1065) in the determination of the amount due for Self-Employment Tax for 2010 only.

PROBLEM

With both the Subchapter S and the C Corporations, the owner(s), who are also employees, are paid a salary. Employee benefits, such as the payment of health insurance, may also be provided by the corporation, and are taken as a deduction against income

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CONGRESSIONAL AGENDA *(continued from page 7)*

to the extent that is paid by the employer. With an unincorporated business, no such deduction may be taken. The operator of such a business may take the health insurance premium as an adjustment against income on Form 1040, but unlike the corporate owner/employee, the amount paid for health insurance premiums is still subject to Self-Employment Tax, as it is not an expense against business income. For example, an S Corporation owner has a salary of $100,000, and the S Corporation has no profit. The expenses of the S Corporation include $12,000 in health insurance premiums. While the premium is added to the shareholder's W-2, it is immediately deducted in the determination of Adjusted Gross Income, resulting in a net result of $100,000 AGI ($100,000 + $12,000 – $12,000). Using the same information, this time for an unincorporated business, the owner has to report $112,000 of income. While they also can claim the deduction for health insurance premiums, their Self-Employment Tax is calculated on $112,000, not $100,000.

RECOMMENDATION

Health insurance premiums should be allowed as a full deduction against income for an unincorporated business. There should be no difference in the treatment of the deduction based on the type of entity formed. However, under the new law, this is for the year 2010 ONLY. NCCPAP recommends that this provision should be made permanent.

OFFICE IN HOME — S CORPORATION SHAREHOLDERS

PRESENT LAW

Internal Revenue Code Section 280A(a) states generally that *"in the case of a taxpayer who is an individual or an S corporation, no deduction otherwise allowable under this chapter shall be allowed with respect to the use of a dwelling unit which is used by the taxpayer during the taxable year as a residence."*

Code Section 280A(c) provides for certain exceptions (deductions are allowed) when a portion of the dwelling unit *"is exclusively used on a regular basis…as a place of business which is used by patients, clients, or customers in meeting or dealing with the taxpayer in the normal course of his trade or business"* [280A(c)(1)(B)]. Accordingly, allocated expenses are deductible when one of the three exceptions provided under Section 280A(c) are met.

Code Section 280A(c) (3) provides an additional exception (deductions are allowed) to the extent that the deductions *"are attributable to the rental of the dwelling unit or portion thereof."*

Code Section 280A(c) (6) provides an exception to the exceptions, to wit *"deductions shall not apply to any item which is attributable to the rental of the dwelling unit (or any portion thereof) by the taxpayer to his employer during any period in which the taxpayer uses the dwelling unit (or portion) in performing services as an employee of the employer."*

The Committee Reports on P.L. 99-514 (Tax Reform Act of 1986) indicate that this law was structured in reaction to the Feldman Case 84 T.C. 1 (1985). The Committee Report states that: *"allowing employees to use lease arrangements with employers as a method of circumventing the restrictions on home office deductions might encourage some taxpayers to arrange sham transactions whereby a portion of salary is paid in the form of rent. Moreover, it is questionable whether lease transactions between an employer and employee are generally negotiated at arm's length… Accordingly, the committee believes that no home office deductions should be allowable…if the employee rents a portion of his or her home to the employer."*

PROBLEM

Some taxpayers have become the unwitting victims of Section 280A merely by their choice of entity which, in many cases, was made without knowledge or consideration of Section 280A. Specifically, a taxpayer—for example, a chiropractor—forms a corporation for his practice and makes an election to be taxed under Subchapter S. The practice operates in a portion of the home that is clearly used regularly and exclusively for business purposes. In fact, significant modifications have been made to the residence to accommodate the practice. While the tax code [Section 1372(a)] treats taxpayers that own more than 2% of the stock of an S Corporation as self-employed for fringe benefit purposes, no such language is provided with regard to the use of a home office.

Accordingly, S corporation shareholders are caught between various Code Sections. The individual cannot claim home office deductions on Form 8829 because there is no Schedule C associated with the tax return; therefore no qualified business use exists. However, if the corporation pays the owner rent for the use of the property, the individual can not claim a deduction Schedule E against the rental income due to the limitations provided under Section 280A.

One of our members has recently discussed this issue with a Revenue agent on audit. He was told to have the corporation make proportionate payments for mortgage, real estate taxes, utilities, maintenance, etc. with a separate corporate check, and the corporation can deduct those payments. We believe that this advice is contrary to the Tax Code for several reasons. Interest deductions are not allowed for payments on a loan for which the entity is not obligated. Principal payments are never deductible. The associated depreciation expense is not available because the corporation does not have an ownership interest in the property and Section 280A thwarts that treatment in its opening paragraph if the corporation did have an ownership interest. Furthermore, we believe that the payments made by the corporation directly would be properly classified as a distribution or compensation to the shareholder under the Tax Code.

If the entity had been formed as a single owner LLC instead, the business would be reported on Schedule C and all of the allowable home office deductions under Section 280A would be available. Section 280A was enacted prior to the existence of the LLC rules under state business laws. In many cases, corporations were formed prior to the availability of the LLC as a choice of entity or prior to the "check the box" regulations that delineate the proper treatment of a single owner LLC. Furthermore, the dissolution of the S Corporation and immediate reformation as an LLC would have a number of adverse tax consequences.

Accordingly, taxpayers in situations similar to this are denied fair and equitable treatment under the Tax Code.

RECOMMENDATION

Section 280A should be revisited. In general, we believe that Code Section 280A should be coordinated with the rules under

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Section 1372 for S corporation shareholders. Adverse consequences also exist when a taxpayer rents a portion of the residence to a closely held C Corporation pursuant to Code Section 280A(c)(6). A fair and equitable result could be achieved by requiring any rental to the employer to be made at fair market value. IRS has already used the reasonable compensation rules successfully to stop taxpayers from converting compensation into Subchapter S dividends. We understand the need of the IRS to collect a proper amount of FICA, Medicare, unemployment and withholding taxes. This need, however, should not obviate the need to provide fair and equitable tax administration to all taxpayers.

S CORPORATION INCOME SUBJECT TO SOCIAL SECURITY TAX

In a report titled "Additional Options to Improve Tax Compliance," issued August 3, 2006, the Joint Committee on Taxation (JCT) has proposed modifying the determination of income subject to employment, or self-employment tax for the partners in Partnerships and shareholders of S Corporations.

Prior to stating a position on this matter, we should first examine how income is currently treated for Unincorporated Business and Incorporated Businesses.

UNINCORPORATED BUSINESSES: PARTNERSHIPS AND SCHEDULE C

If a single individual operates an entity, the income is reported on Form 1040, Schedule C. If two or more individuals are involved, then the business is treated as a partnership and Form 1065 is used to report the income. In either of these business situations, the business entity does not pay federal income tax, but rather the sole proprietor business operator in the case of a Schedule C, or the partners of the partnership, report the income on their individual tax returns, self-employment tax (SECA) must be paid by the individuals if there is earned income.

INCORPORATED BUSINESSES

A corporation is an artificial, legal entity created by state law, which may be owned by one or more individuals. The corporation itself has two options under which it can be treated for tax purposes, a C Corporation, or an S Corporation. With a C Corporation, the entity reports income and expenses and pays income tax on its net income. In addition, if the C Corporation makes a dividend distribution to a shareholder, these monies are taxed a second time, when the shareholders report the income on their individual income tax returns. If the corporation elects to be treated as an S Corporation, then the corporation pays no federal income tax and the shareholders report their share of the income on their individual income tax returns, pro rata, regardless of whether they receive funds from the corporation or not. Any monies that they receive (distributions) may be received tax free because the income has already been taxed, subject to basis and at-risk rules.

THE ISSUE

In recent times, many individuals have gone into business for themselves. The S Corporation has become a very popular vehicle for small business in that it provides protection from liabilities while income is generally taxed once at the personal level. Salary from an S Corporation is reported on Form W-2 and is subject to FICA (payroll taxes) instead of self-employment tax. Net income passed through to S Corporation shareholders on Form K-1 is not subject to FICA or SECA taxes.

HISTORY

The Subchapter S of the IRS Code was enacted in the 1950s. In 1959, the Internal Revenue Service issued Revenue Ruling 59-221, which is the original revenue ruling that deals with the treatment of taxable income included in the gross income of shareholders of an S Corporation. The Internal Revenue Code of 1954, Section 1, Subchapter S, Sections 1371-1377 dealt with the taxable status of such corporations. Section 1373 of the Code specifically states that:

> "Each person who is a shareholder of an electing small business corporation on the last day of a taxable year of such corporation shall include in his gross income, for his taxable year in which or with which such taxable year of the corporation ends, the amount he would have received as a dividend, if on such last day there had been distributed pro rata to its shareholders by such corporation an amount equal to the corporation's undistributed taxable income for it taxable year."

The IRS did not envision how the use of the S Corporation would evolve. It is apparent that the IRS in their 1959 ruling envisioned a small group of investors forming a corporation and reporting the income. It was not envisioned that a single individual would open their own business, make the S election, report the income, but in doing so, not report any compensation subject to FICA tax for themselves.

REASONABLE COMPENSATION

The question is in the definition of reasonable compensation. It can be defined as:

> "The theoretical compensation required to hire an outside person to perform the same duties as the shareholder in a similar circumstance."

Some taxpayers may seek to pay unreasonably low or no salaries to themselves and artificially increase the net income in order to reduce their liability for FICA taxes. The IRS has the right to reclassify a distribution of profits as salary if it determines that compensation is not reasonable. However, the term "reasonable compensation" is a very subjective term. What may be reasonable in one part of the country might be considered to be excessive in another. Also, one entity might show greater gross revenue than another in the same field of business, and therefore provide a greater compensation. The IRS has determined that reasonable compensation is to be determined by "facts and circumstances" within each individual case.

PROBLEMS

There are several problems with the current situation.

First, there are S Corporations that have more than one

shareholder. In some of these cases, some of the shareholders may not be active participants in the business of the corporation. According to the Treasury Inspector for Tax Administration, a difficulty that the IRS has encountered in the examination of officer compensation is the determination of the level of shareholder services rendered to the corporation (TIGTA 202-30-125).

Second, whether a shareholder is active in the S Corporation or not, funds are not always available to be paid as wages even though the corporation has net income at the end of the year. A business entity may need the funds in order to meet its financial responsibilities for operating expenses, debt service, or they may have to use the funds to purchase inventory or other assets. This can result in what some call "phantom income," income that must be reported but is not received. While some funds may be available to be distributed to allow the shareholders to meet their tax responsibilities, adding SECA to this may prove to be an undue burden, both on the shareholder of the S Corporation, and the S Corporation itself.

Finally, some S Corporations have been formed to operate real estate ventures that employ professional managers who are not shareholders. The shareholders are passive investors and may not control the day-to-day operations of the corporation. This type of activity should not generate earned income subject to FICA or SECA tax.

NCCPAP POSITION

NCCPAP recognizes that this is a serious issue. As the population of the United States ages, the ratio of contributors to recipients of Social Security/ Medicare decreases. The strain on the Social Security system is real, but economic crisis should not generate unfair tax policy.

NCCPAP does not believe that classifying all K-1 income from S Corporations as subject to SECA or FICA tax is the answer. Instead, the concept of "reasonable compensation" needs to be revisited so that it can be applied fairly across all levels. This can be accomplished through tests of "active engagement" in the business activity and providing guidance about how the IRS will apply the facts and circumstances concept in practice. While it may be tempting to provide salary ranges for reasonable compensation, this would be a daunting task based on geographical location, special skills and corporation profitability

In addition, the tax preparer community, in advising their business clients who are S Corporation shareholders, should that the active shareholders ***MUST*** draw a reasonable salary.

This is an issue where the CPA profession and the federal government should work together, to achieve a proper balance.

THE ALTERNATIVE MINIMUM TAX (INDIVIDUALS)

BACKGROUND

The AMT was originally enacted in 1969 to address the concerns that persons with substantial economic income were paying minimal or no Federal income taxes due to the clever use of "tax sheltered" investments. The AMT today is affecting an originally unintended class of taxpayer, namely the middle class taxpayers, who are not using what we would call "deferral strategies."

The AMT is a tax that eliminates many of a taxpayer's deductions and leaves the taxpayer paying more tax, sometimes much more, than they were led to believe they would pay, especially in light of all of the tax cuts of recent years—many of which have been very well publicized.

The AMT is a special tax applicable only if the amount of alternately calculated tax due exceeds the regular income tax. Individuals must first calculate the regular tax and then modify the calculation with certain adjustments and add-backs before subtracting an exemption amount that is based on filing status and adjusted gross income.

The individual AMT requires a second tax calculation that is a major compliance burden without a significant policy justification. The failure of the AMT to achieve the purpose it was originally designed for is due to the numerous changes that have been made to the Internal Revenue Code since 1969, which have limited tax shelter deductions and credits that many of the wealthier taxpayers took advantage of for many, many years.

Today, the AMT affects well over five million tax returns, and within the next five years it will increase to about one-third of all taxpayers. Currently, it is projected that ninety percent of all households with an adjusted gross income in excess of $100,000 will be subject to the AMT.

PROBLEM

The failure of the AMT to achieve its original purpose can be traced to items that are "personal" in nature and not the result of shrewd, sophisticated tax planning. These items include the personal exemption, medical expenses, state and local income taxes and miscellaneous itemized deductions.

For a very long time most people outside of the professional tax preparer community did not even know that this so-called "second tax calculation" even existed. Today, as more and more middle class individuals are being snared into this trap, they exclaim, "What is an AMT?" when their tax preparer informs them of a much-less-than-anticipated refund or an amount that is due to the U.S. Treasury when a refund was expected. Individuals who prepare their own returns and are subject to the AMT are not prepared to calculate it and will eventually receive a bill for the underpaid tax—plus interest and penalties.

While the regular tax rates were reduced and adjusted for inflation over the past decade, the AMT tax rates have been unchanged and have not been indexed for inflation, although there have recently been minor adjustments enacted to account for inflation. As the gap between the AMT and the regular tax narrows, more people are subject to it.

The AMT is too complex and imposes a large compliance burden. In her annual reports to Congress, taxpayer Advocate Nina Olson has, since 2001, stated that the AMT now functions "randomly and no longer with any logical basis in sound tax administration." She believes that the AMT impacts the "wrong" taxpayers. We agree with Ms. Olson in this regard. The record-keeping requirement for two sets of records is burdensome and unfair. Tax simplification can be achieved by an immediate repeal of this tax.

RECOMMENDATION

The tax code should be amended to repeal the individual AMT. It will reduce the complexities associated with the calculations

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and allow all taxpayers to have their tax calculated fairly and on the same playing field.

Congress is well aware that the alternative minimum tax is affecting a much larger portion of the population than it was originally intended to.

If a total repeal is not possible because of revenue considerations, the law could be amended to exclude taxpayers with adjusted gross income below a certain threshold from having to calculate any potential AMT liability. Each and every "preference item" should be reviewed to determine whether or not the item really belongs as part of the AMT calculation. All miscellaneous deductions should be deductible for AMT purposes as well. The tax rate brackets and exemption amounts for the AMT should be indexed in the same manner as the regular tax.

COMMENTS

The National Taxpayer Advocate has recommended repeal of the AMT in her annual report to Congress every year since 2001. In addition, former President Bush's select committee on tax reform also advocated for repeal of the AMT. The rules for AMT are unnecessarily complex and result in affecting taxpayers not originally intended when the AMT was first enacted. Rather than a provision to prevent high-income taxpayers from avoiding tax through tax planning, the AMT has become a tax on the middle class, burdening certain parts of the country more than others. Repeal, adjustment or reorganization is desperately needed to restore equitable taxation to the middle-class taxpayer.

TAX PREPARATION AND REPRESENTATION FEES

HISTORY

The Internal Revenue Code and associated regulations, rulings, etc. have become extremely complex in recent years. A 2006 GAO report stated that over 80% of income tax returns filed with the SBSE division of the IRS were prepared by paid preparers, a greater portion of which were not regulated by Circular 230 (non CPA, Attorney, Enrolled Agent and Enrolled Actuary). Additionally, the National Taxpayer Advocate has reported that IRS studies have shown that a significant number of unlicensed preparers do not report all of their earnings and prepare less compliant returns. Since current law allows a deduction for preparer fees only as a miscellaneous itemized deduction, subject to a floor of 2% of Adjusted Gross Income (AGI), most taxpayers do not benefit from this deduction and do not insist on reporting it on their tax return. Additionally, since miscellaneous itemized deductions are not allowed for Alternative Minimum Tax, taxpayers may lose the deduction totally.

On January 4, 2010, Douglas Shulman, Commissioner of the Internal Revenue Service, issued the **Tax Preparer Regulation Proposal**, which requires all individuals who sign a federal income tax return as a paid preparer to register and obtain a preparer tax identification number (PTIN). In addition, paid preparers who are not CPAs, attorneys, or Enrolled Agents or supervised by a CAP, attorney or Enrolled Agent are required to pass a minimum competency test and complete continuing education requirements to maintain their registration.

On January 6, 2010, the Taxpayer Advocate released her Annual Report to Congress. While she complimented the IRS on the regulation proposal, it was pointed out that the regulation did not address the individual who prepares a tax return but fails to sign the return.

PROBLEM

The Internal Revenue Service has implemented the PTIN program effective January 1, 2011. While legitimate paid tax return preparers have registered and received a new, or refreshed an existing, PTIN, there is still the problem of the underground economy where people provide services for cash, and then do not report the income. There are many tax return preparers who do not sign tax returns, nor do they report the income generated by the provided service.

RECOMMENDATION

The deduction for tax preparation and representation fees should be deductible on Page 1 of Form 1040 as an adjustment to AGI, with the requirement that the preparers' ID number (SSN, EIN, PTIN) be listed in order to allow the deduction. This will generate a direct reduction to AGI and taxpayers will not lose the tax benefit due to the above-mentioned limitations. NcCPAp believes that more taxpayers would insist on deducting the fees if they were certain there would be a tax benefit. Furthermore, unlicensed tax preparers would be more likely to sign returns and report the fee income. As alimony payments are currently a Page 1 adjustment with the requirement of the recipient's Social Security Number for cross-referencing purposes, such a mechanism is already in place. It is our belief that the IRS should collect enough currently unreported revenue from non-reporting preparers to mitigate the potential loss of tax revenue lost by allowing these fees on Page 1 of Form 1040.

By implementing the NCCPAP proposal, the IRS will have a mechanism to track paid preparers as to signing and reporting the income from tax preparation work. By requiring the ID number of the preparer and placing the deductibility of the preparation fees on Page 1 of Form 1040, the taxpayer will be more aware of the deduction and demand that the required information be provided. Additionally, the preparers will now be more aware of the requirement to sign the return and will be subject to the Tax Preparation Regulation Proposal for registration, competency, and continuing education, thereby improving tax compliance.

UPDATE

The PTIN program is up and running, but it will take time to be fully implemented with regard to the CPE and testing requirements. The CPE requirement has been delayed until 2012 for initial implementation, and those who will have to submit to the testing have until December 31, 2013 to satisfy that requirement.

– IRS Agenda –

FORM 8879, E-FILE SIGNATURE AUTHORIZATION BANK INFORMATION

PROBLEM

The bank account information is currently listed on page 2 of Form 1040 near the signature page. However, with more taxpayers e-filing, which is being encouraged by the Internal Revenue Service, they no longer look at the signature page of Form 1040 but do look at and sign the Form 8879.

Although the tax return preparers include the bank information on tax organizers they provide to clients, or in their instruction letters, many times the client will forget that they are using a particular bank account for their taxes. Sometimes a month or two may go by between the time that the client confirms the bank account information and the time that the tax return is ready for submission. During this period of time, clients may switch banks or just close the account. Many tax return preparers verbally confirm the banking information when the client signs Form 8879, but the information should be on the form and not just confirmed verbally.

RECOMMENDATION

Place the bank account information on Form 8879, IRS e-file Signature Authorization. For purposes of protection from identity theft, only the last 4 digits really need to be placed on the form. Currently, there are many states that include banking information on their respective authorization forms.

FORM 8879 BURDEN

PROBLEM

The Internal Revenue Code requires that tax return preparers receive a completed, executed Form 8879 from a taxpayer/spouse, corporate officer or fiduciary before transmitting an electronically filed income tax return. This burden is increased in many states by state requirements that all preparers who prepare more than a minimal number of tax returns file all returns electronically. The time required to prepare, print and mail a tax return for approval, and then receive a signed authorization for electronic submission, has made timely filing very difficult as due dates approach.

The Worker, Homeownership and Business assistance Act of 2009, as modified, includes provisions that require mandatory e-filing by all preparers who prepare more than one hundred (100) individual income tax returns, including fiduciary returns for estates and trusts for returns filed after December 31, 2010 and eleven (11) returns filed after December 31, 2011.

BACKGROUND

During the 1990s the IRS began increasingly to encourage the electronic filing of income tax returns. The purpose of this promulgation (to reduce paperwork and increase IRS efficiency) was commended and is correct. Many states followed the lead of the IRS and subsequently encouraged the electronic filing of tax forms (including state specific tax and reporting forms). The state tax jurisdictions also required that preparers obtain an executed form from the taxpayer, similar to IRS Form 8879, acknowledging and authorizing the electronic filing of the form by the electronic return originator (ERO). This requirement was mandated in many states for all tax preparers who prepare more than a minimum number of tax returns, this number varying from state to state. For example, the Commonwealth of Massachusetts mandates electronic filing of all individual income tax returns by preparers who had prepared more than 100 individual income tax returns in the prior year.

Current conditions (e.g. multiple corrected tax reporting statements from brokerage firms) have caused information to arrive in the hands of taxpayers closer to the filing deadline than in the past. Preparers receive this information and have a very limited amount of time to review and process the information and prepare an income tax return. These forms must still be reviewed and accepted by the taxpayer before an electronic filing can be submitted. The acceptance (Form 8879) must be signed, returned to and retained by the preparer. The process for preparation, mailing and receipt of the acceptance form can easily take 7-10 business days. A timely prepared return can easily become late because of protracted processing systems. Preparers are now required to spend time approximately one week before tax form due dates contacting clients who do not return the Form 8879.

In our electronic age, most individuals have access to e-mail, fax machines (and of course, telephones). There are many alternatives to wet signature approval of tax returns for electronic filing. While the IRS permits taxpayers to transmit executed forms to the preparer by these alternative methods (and we commend the IRS for their effort in this regard), it still does not eliminate the problems encountered by the tax return preparer in actually obtaining the executed Form 8879 from the taxpayer or the additional time spent in obtaining the receipt of these forms from the taxpayer—at a time when we are already overburdened with other compliance responsibilities.

RECOMMENDATION

April 15th has become an untenable time for most tax preparers. NCCPAP would like to return the role of tax preparers to what it was prior to electronic filing. We should prepare tax returns, according to the rules prescribed under Circular 230, and turn them over to clients for filing. It would then be the responsibility of our clients to accept or reject the return and to verify their bank account information. Tax preparers would submit a tax return to the IRS on or before April 15th (or the extended due date). This will create an e-postmark. Taxpayers would then have an additional 15 days to log on to the IRS web site and accept the return or contact their preparer to have the return modified and re-submitted.

Precedent exits within the information return reporting system to give an extended due date to returns electronically filled versus those filed on paper. Paper information returns are generally due February 28th; electronically submitted returns, through the FIRE system, are due March 31st. This same rule could be easily applied to income tax reporting. The IRS would still receive the returns for processing on or before May 15th, a

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condition that they were more than willing to accept when returns were submitted on paper and then keypunched at a future date and time.

Implementing this procedure would return the responsibility of filing returns back to the taxpayer, where it should belong. It would further secure taxpayers' bank account information by leaving it to the taxpayer to enter. No preparer is comfortable retaining bank information in their files and electronic records. There are libraries and public access computers for those taxpayers who do not have access to the Internet. Return preparers can assist those taxpayers who either do not have access to computers, or are incapable of using one, with their "acceptance" procedure. This would be a significantly smaller burden than having to do it for each and every client.

LINE FOR FEDERAL ID (EIN) ON FORM 1040, SCHEDULE E, PAGE 1

PROBLEM

When a taxpayer starts a business or purchases rental property, he/she may apply for a Federal Employer Identification Number (EIN). Many of these situations involve the creation of a Limited Liability Company (LLC). A single member LLC can be a disregarded entity for income tax purposes and the information regarding income and expenses is reported on the appropriate schedule of Form 1040. A business operating as a single-member LLC is reported on Form 1040 Schedule C, Profit or Loss from Business (Sole Proprietorship). If the entity is involved in renting real estate, then the income or loss is reported on Schedule E, Supplemental Income and Loss (from Rental Real Estate, Royalties, Partnerships, S Corps, Estates, Trusts, REMICS, etc.). In situations involving real estate, when the taxpayer has obtained an EIN for the real estate entity, they may receive a Form 1098 for interest paid on a mortgage, with the EIN of the real estate entity. There is no place on Schedule E, Page 1, to indicate this EIN. Therefore, the taxpayer may receive a notice from the IRS indicating the reporting of an interest deduction, which does not match their Social Security Number (SSN).

Under the Patriot Act, when the taxpayer forms an LLC for liability protection, banks require an EIN that corresponds to that specific LLC in order to open a bank account.

RECOMMENDATION

A line for a federal identification number should be incorporated on Form 1040 Schedule E, Page 1 to avoid any confusion in the future, and provide the ability to match up federal identification numbers with the appropriate tax return to save time and expense to the IRS and the taxpayer.

MODIFICATION TO FORM 1098

PROBLEM:

Some residences are owned by more than one individual, who may or may not be married to each other. When the taxpayer(s) receive(s) the 1098 Form, reporting the amount of interest paid on a mortgage, or home equity line of credit, only the social security number of the primary individual on the loan documentation appears on the form. If the taxpayer(s) are filing a joint tax return, this is not a problem. However, should the taxpayer(s) not be filing a joint return, this can present a problem because one or more taxpayers are taking a deduction for which there is no official reporting of the expense to the Internal Revenue Service. This can result in IRS notices to the taxpayer disallowing deductions being claimed because the interest was not reported in their Social Security Number. This results in unnecessary and burdensome correspondence to resolve the matter.

RECOMMENDATION

Form 1098 should be modified to allow more than one social security number to appear, thereby allowing the taxpayer(s) to claim the deduction for interest on their respective tax returns.

SMALL BUSINESS OWNERS BURDEN

BACKGROUND

Starting in 2012, under Section 9006 of the Patient Protections and Affordable Care Act, all businesses will be required to prepare and submit 1099-MISC forms to any and all businesses for both merchandise and services in excess of $600.

PROBLEM

This law is not a problem at this time. However, when it takes effect, it will place a significant burden on all business owners, especially small business owners. They may not have the personnel and/or time to be able to meet this requirement and timely prepare the data to file the reports. In addition, it will place an undue burden on the CPAs, as it will place additional onus on them to assist in the preparation of these forms.

In addition, the issuance of 1099-MISC may be moot as many businesses are on a fiscal year ending in months other than December. The matching process for these entities will prove to be useless as the 1099 issued will represent only a portion of what would be reported on their respective income tax returns.

It is not the position of the CPA to advise the client on how to not report income. We are only in a position to recommend that the business owner reports all income and expenses so that a true picture of a business may be presented, either on a tax return or a financial statement. Neither is it the responsibility of a business owner to ensure that those whom they do business with report all that is paid to them.

RECOMMENDATION

H.R. 5141 was introduced on April 26, 2010, by Representative Daniel Lungren (3-CA). Known as the "Small Business Paperwork Mandate Elimination Act," passage of this bill would eliminate this burden for business owners. Subsequent bills have been introduced into Congress since then, calling for the removal of Section 9006 of the Patient Protections and Affordable Care Act, all of which have failed to obtain passage. It is our opinion that such legislated be passed and request that the IRS call upon Congress to support such legislation in the future.

HEALTH INSURANCE PREMIUMS FOR S CORPORATION SHAREHOLDERS

PROBLEM

The health insurance premiums paid on behalf of all S

Corporation shareholders with more than a 2% interest in the corporation are required to be reported on Form W-2 for that shareholder, with the amount being included on Line 1 – Gross Wages. In the case of many small, closely held businesses, payroll tax reports, and W-2 are usually prepared by an outside service, such as a payroll service, or the accounting firm that is engaged by the corporation's shareholders. Depending on the condition of the books and records, this information may not be readily available to the outside party at the time they are preparing the W-2 forms. In addition, this amount for health insurance is then deducted on Page 1 as an adjustment from Gross Income to Adjusted Gross income (Line 29 on the 2009 Form 1040) on the individual's tax return. This can be a burden on the preparer of the W-2 Forms as they will need to determine the amount of the health insurance premiums paid that needs to be allocated to the shareholders.

RECOMMENDATION

As stated above, the amount for health insurance premiums is taken in full as a Page 1 adjustment on Form 1040. Since it is taken in full, there is no reason for it to be incorporated with the shareholder's gross wages, as it will also be deducted on the same form. We recommend that health insurance premiums no longer be required to be incorporated in the shareholder's W-2 for this purpose since there is no tax impact to the current procedure and it is burdensome.

COLLECTION FINANCIAL STANDARDS

PROBLEM

The Internal Revenue Service has established national standards for certain expenses such as food, clothing, personal care products, out-of-pocket medical expenses, vehicle ownership costs, rent/mortgage, which are the same for everyone regardless of where they live. These standards are used by IRS representatives and agents for variable allowable cost of living calculations in order to determine a taxpayer's ability to pay the IRS for outstanding liabilities. Specifically, food and clothing allowances are based on national standards while housing allowances are based on state and county standards, and vehicle and transportation allowances are based on regional standards. These standards do not necessarily reflect regional and local differences, which may result in an understatement of allowable expenses for certain taxpayers. For example, the amounts allowed in South Florida for housing and utilities are much too low as compared to actual costs. Mortgage payments are higher in this region, as well as higher property taxes, flood, windstorm and homeowners' insurances.

BACKGROUND

The Internal Revenue Service developed national and regional expense standards to determine allowable living expenses that meet the necessary expense test and to ensure that taxpayers have adequate means of providing for basic living expenses. Regional standards, such as housing and utilities, vehicle operating expenses, and other expenses that meet the necessary expense test, such as health insurance, dependent care, etc., may be adjusted by geographical areas.

The IRS agent is permitted to allow the taxpayers a year of lower than calculated installment payments under the "One Year Rule" to give the taxpayer one year to modify their lifestyle. In many cases, the taxpayer will still be unable to make the higher installment payments one year later.

RECOMMENDATION

Since the IRS does not adhere to the Collection Standards, giving the taxpayer lower payments under the "One Year Rule," NCCPAP proposes that the local Housing & Utilities collection financial standards should be adjusted to more realistic and actual amounts, based on the geographic area's specific differentials. An example to follow could be the per diem rates for travel within the continental United States, or CONUS, which is published at least annually by the Service.

RECEIPT BY IRS OF OFFERS IN COMPROMISE

PROBLEM

A taxpayer makes an application for an offer in compromise to settle an outstanding tax liability. The IRS acknowledges the application, and a letter is sent to the taxpayer and/or their authorized representative. The letter indicates a target date as to when they should receive an official response from the Internal Revenue Service.

In many cases, the taxpayer does not receive the correspondence by the date indicated. This causes anxiety on the part of the taxpayer. The taxpayer will try to contact the IRS, or have their representative call in their stead in order to determine the status of the application. These calls are a burden to the taxpayer, their representative, and the IRS.

RECOMMENDATION

It is recommended that the IRS automatically send out update letters to OIC applicants, and their representative, at least every sixty (60) days. This will serve to keep the taxpayers and their representatives informed and less anxious. This will reduce calls to collections phone lines and the Practitioner Priority Line.

Furthermore, the IRS should not require updated financial information (Forms 433A and 433B) during the initial review process. Requests for updated filings from the time of the initial application, until an employee of the IRS reviews the application, places an undue hardship on applicants and further delays the process.

In general, the IRS should not request financial information more often than annually as this is a burden to taxpayers, except when the IRS has reason to believe that there has been a significant change in the taxpayer's income or net assets.

S CORPORATION INCOME SUBJECT TO SOCIAL SECURITY TAX

In a report titled "Additional Options to Improve Tax Compliance," issued August 3, 2006, the Joint Committee on Taxation (JCT) has proposed modifying the determination of income subject to employment, or self-employment tax for the partners in Partnerships and shareholders of S Corporations.

Prior to stating a position on this matter, we should first examine how income is currently treated for Unincorporated Business and Incorporated Businesses.

(continued on page 16)

IRS AGENDA *(continued from page 15)*

UNINCORPORATED BUSINESSES: PARTNERSHIPS AND SCHEDULE C

If a single individual operates an entity, the income is reported on Form 1040, Schedule C. If two or more individuals are involved, then the business is treated as a partnership, and Form 1065 is used to report the income. In either of these business situations, the business entity does not pay federal income tax, but rather the sole proprietor business operator in the case of a Schedule C, or the partners of the partnership report the income on their individual tax returns, self-employment tax (SECA) must be paid by the individuals if there is earned income.

INCORPORATED BUSINESSES

A corporation is an artificial, legal entity created by state law, which may be owned by one or more individuals. The corporation itself has two options under which it can be treated for tax purposes, a C Corporation, or an S Corporation. With a C Corporation, the entity reports income and expenses and pays income tax on its net income. In addition, if the C Corporation makes a dividend distribution to a shareholder, these monies are taxed a second time, when the shareholders report the income on their individual income tax returns. If the corporation elects to be treated as a S Corporation, then the corporation pays no federal income tax and the shareholders report their share of the income on their individual income tax returns, pro rata, regardless of whether they receive funds from the corporation or not. Any monies that they receive (distributions) may be received tax-free because the income has already been taxed, subject to basis and at-risk rules.

THE ISSUE

In recent times, many individuals have gone into business for themselves. The S Corporation has become a very popular vehicle for small business, in that it provides protection from liabilities while income is generally taxed once at the personal level. Salary from an S Corporation is reported on Form W-2 and is subject to FICA (payroll taxes) instead of self-employment tax. Net income passed through to S Corporation shareholders on Form K-1 is not subject to FICA or SECA taxes.

HISTORY

The Subchapter S of the IRS Code, was enacted in the 1950s. In 1959, the Internal Revenue Service issued Revenue Ruling 59-221, which is the original revenue ruling that deals with the treatment of taxable income included in the gross income of shareholders of an S Corporation. The Internal Revenue Code of 1954, Section 1, Subchapter S, Sections 1371-1377 dealt with the taxable status of such corporations. Section 1373 of the Code specifically states that:

> "Each person who is a shareholder of an electing small business corporation on the last day of a taxable year of such corporation shall include in his gross income, for his taxable year in which or with which such taxable year of the corporation ends, the amount he would have received as a dividend, if on such last day there had been distributed pro rata to it shareholders by such corporation an amount equal to the corporation's undistributed taxable income for it taxable year."

The IRS did not envision how the use of the S Corporation would evolve. It is apparent that the IRS in their 1959 ruling envisioned a small group of investors forming a corporation and reporting the income. It was not envisioned that a single individual would open their own business, make the S election, report the income, but in doing so, not report any compensation subject to FICA tax for themselves.

REASONABLE COMPENSATION

The question is in the definition of reasonable compensation. It can be defined as:

> "The theoretical compensation required to hire an outside person to perform the same duties as the shareholder in a similar circumstance."

Some taxpayers may seek to pay unreasonably low salaries to themselves and artificially increase the net income in order to reduce their liability for FICA taxes. The IRS has the right to reclassify a distribution of profits as salary if it determines that compensation is not reasonable. However, the term "reasonable compensation" is a very subjective term. What may be reasonable in one part of the country might be considered to be excessive in another. Also, one entity might show greater gross revenue than another in the same field of business, and therefore, provide a greater compensation. The IRS has determined that reasonable compensation is to be determined by "facts and circumstances" within each individual case.

PROBLEMS

There are several problems with the current situation.

First, there are S Corporations that have more than one shareholder. In some of these cases, some of the shareholders may not be active participants in the business of the corporation. According to the Treasury Inspector for Tax Administration, a difficulty that the IRS has encountered in the examination of officer compensation is the determination of the level of shareholder services rendered to the corporation (TIGTA 202-30-125).

Second, whether a shareholder is active in the S Corporation or not, funds are not always available to be paid as wages even though the corporation has net income at the end of the year. A business entity may need the funds in order to meet its financial responsibilities for operating expenses, debt service, or they may have to use the funds to purchase inventory or other assets. This can result in what some call "phantom income," income that must be reported but not received. While some funds may be available to be distributed to allow the shareholders to meet their tax responsibilities, adding SECA to this may prove to be an undue burden, both on the shareholder of the S Corporation, and the S Corporation itself.

Finally, some S Corporations have been formed to operate real estate ventures which employ professional managers who are not shareholders. The shareholders are passive investors and may not control the day-to-day operations of the corporation. This type of activity should not generate earned income subject to FICA or SECA tax.

NCCPAP POSITION

The National Conference of CPA Practitioners recognizes that this is a serious issue. As the population of the United States ages, the ratio of contributors to recipients of Social Security/ Medicare decreases. The strain on the Social Security system is real but economic crisis should not generate unfair tax policy.

NCCPAP does not believe that classifying all K-1 income from S Corporations as subject to SECA or FICA tax is the answer. Instead, the concept of "reasonable compensation" needs to be revisited so that it can be applied fairly across all levels. This can be accomplished through tests of "active engagement" in the business activity and providing guidance about how the IRS will apply the facts and circumstances concept in practice. While it may be tempting to provide salary ranges for reasonable compensation, this would be a daunting task based on geographical location, special skills and corporation profitability

In addition, the tax preparer community, in advising their business clients who are S Corporation shareholders, should indicate that the active shareholders ***MUST*** draw a reasonable salary.

This is an issue where the CPA profession and the federal government should work together, to achieve a proper balance.

INDEPENDENT CONTRACTOR ISSUES

BACKGROUND

There is a bill in Congress, S.3786 and HR.1234, "The Fair Playing Field Act of 2010," which addresses the issue of the independent contractor vs. the employee. Currently, the Treasury Department and the Internal Revenue Service are prohibited from issuing guidelines for the determination as to whether a worker is an independent contractor or an employee. This restriction is in effect under Section 530 of the Revenue Act of 1978.

PROBLEM

This bill is intended to ensure that workers are afforded protections already in the law and help the employers who play by the rules so they are not forced to compete against those businesses that do not. The purposes of this Act are to permit the Secretary of the Treasury to provide guidance allowing workers and businesses to clearly understand the proper federal tax classification of workers and to provide relief allowing for an orderly transition to new rules designed to increase certainty and uniformity of treatment. The legislation requires the Secretary of the Treasury to issue prospective guidance clarifying the employment status of individuals for Federal employment tax purposes.

We find that there are several issues that place NCCPAP in the position to recommend that this bill should not be passed into law:

1. It is our belief that this will not help close the "Tax Gap." Certain employers will still make use of illegal workers who do not have social security numbers and are undocumented
2. While some state legislatures have passed similar laws regarding workers in their respective states, other states have not. Such legislation is in the process of being challenged within the state courts.
3. If state legislation contradicts with federal legislation, which law will the employer be required to follow?
4. This legislation, if passed, would require additional paperwork for employers as they would be required to provide a written statement to independent contractors notifying of the Federal tax obligation, the labor and employment law protections that do not apply to independent contractors, and the right of such independent contractors to seek a status determination from the IRS.

We would like to point out that within our profession, there are many practitioners who own their own corporations, who do work for colleagues on a per diem basis as independent contractors. Payments for these services are paid to the corporation, not the practitioner directly. The relationship may be constant or infrequent, depending on the need of both the practitioner needing help, and the one looking for additional work.

RECOMMENDATION

We understand the need for such legislation. However, we believe that should this become law, additional discussions are needed in order to make this truly effective. NCCPAP would welcome the opportunity to participate in such discussions, as a blanket policy would be unfair to those who operate within the current required parameters.

We agree that The Fair Playing Field Act of 2010 should:

- end the moratorium on Internal Revenue Service (IRS) guidance addressing worker classification;
- require the Secretary of Treasury to issue prospective guidance clarifying the employment status of individuals for Federal employment tax purposes;
- amend the provisions of the Tax Code that provide for reduced penalties for failure to deduct and withhold income taxes and the employee's share of FICA taxes;
- not require persons who contract independent contractors on a regular and ongoing basis to provide a written statement to each independent contractor of the Federal tax obligations of independent contractors, the labor and employment law protections that do not apply to independent contractors, and the right of the independent contractor to seek a status determination from the IRS; and
- require the Secretary of the Treasury to issue annual reports on unresolved worker misclassification issues.

We strongly believe that the federal legislation to go one step further and have the classification apply to all state department of taxations, attorneys general, labor departments (federal and state) and other jurisdictions. For example, in Senator Kerry's home state, employer's are subject to different interpretations from the Internal Revenue Service, Massachusetts Department of Revenue and the Massachusetts Attorney General.

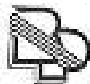
Taxpayers should be subject to the same Form SS-8 filing as employers.

Contracting entities should be given five years before any penalties are assessed. This will allow time for the IRS to release regulations and employers to review them for applicability.

Suggested guidelines for determination of employee or independent contractor status might include:

- Average hours worked per quarter over a certain period.

(continued on page 18)



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IRS AGENDA *(continued from page 17)*

- Percentage of total business of the independent contractor with contracting entity.
- Structure of independent contracting unit – corporation, LLC.
- Rules for independent contractor operating business with partners, other shareholders and/or employees treated differently that sole pro0viders.
- Rules for different types of industries, occupations, and professions.
- Safe harbor or unprotected occupations as outlined by the Internal Revenue Service Determination Unit.

AUTOMATIC COLLECTION HOLD BE INPUT BY IAT CREDIT TRANSFER TOOL

PROBLEM

Unnecessary collection notices are mailed to taxpayers for Form 941—even though the payments (credits) are pending in the Individual Master File (IMF) or Business Master File (BMF). The IAT CREDIT TRANSFER tool does not input a collection hold automatically.

For example: Notice CP 504B dated 11/8/2010, regarding a balance due on a Form 941 for the second quarter of 2010, was mailed to taxpayer using certified mail, while there were two credits totaling $1,884.00, in the taxpayer's second quarter of 2010 account which resolve the balance due.

Per CSR Ms. Karen Houston, id 1000144162, Ogden UT, on the Tax Practitioners Line, it takes two weeks to debit payments and three weeks to credit payments.

The prior IRS customer service representative on 11/1/10 had used the "IAT CREDIT TRANSFER" tool to transfer payment from Q3 to Q2. This tool does not automatically place a collection hold on the account, which suspends correspondence while the adjustment posts.

The "IAT CREDIT TRANSFER" tool is used to transfer (or move) payments, credit elect or other credits. For examples, credits arise when (a) if penalty has been paid and penalty is later voided, and (b) amended returns can result in credits.

Another tool is the IAT REQ54 tool used for adjustments. The IAT REQ54 tool inputs a collection hold automatically.

Unlike the IAT CREDIT TRANSFER tool which does not input a collection hold automatically.

RECOMMENDATION

The IAT CREDIT TRANSFER tool should be updated to include the input of a collection hold automatically.

It would reduce IRS costs—postage and labor of sending correspondence, and labor of responding to incoming phone calls and additional correspondence generated in response to IRS notices which were issued prematurely because the IRS notices are based upon IRS's incomplete processing of data.

Send Your E-MAIL ADDRESS to NCCPAP!

Like most national organizations, NCCPAP reaches out to members through e-mail. It is the best way for us to keep you up to date with our work in tax regulations, member accomplishments, upcoming events and everything NCCPAP does on behalf of the practicing CPA.

Our membership e-mail list is not 100% complete. Please send your name, firm name and e-mail address to the National office at execdir@NCCPAP.org. Do it now — before you forget, and before you miss out on another important piece of news from NCCPAP!

Join Your Friends and Colleagues!

NCCPAP ON THE HILL

Wednesday, May 11
Thursday, May 12
Friday, May 13

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CHAPTERS' CALENDAR OF EVENTS — MAY / JUNE 2011

NASSAU/SUFFOLK, NEW YORK

Contact: Chapter Office (516) 997-9500
Chapter Meetings:
Registration & Buffet Dinner - 5:30 p.m.; Seminar – 7:00 p.m.

Holiday Inn of Plainview, 215 Sunnyside Blvd., Plainview, N.Y. (exit 46 off the L.I.E.)

Thursday, May 17, Special Chapter Meeting
HOW TO CLOSE A DEAL – 2 CPE credits (Tax)
Crest Hollow Country Club, Woodbury, N.Y.

Wednesday, May 25, 8–10 a.m.
PROTECT YOUR CPA BUSINESS FROM FRAUD IN YOUR CLIENT'S BUSINESS – 2 CPE credits (MAP)
On Parade Diner, 7980 Jericho Tpke. Woodbury, N.Y.

Thursday, June 2, Chapter Meeting, Start time 5 p.m.
WHERE'S THE MONEY? – 3 CPE credits (A & A)

Thursday, June 23, 8 a.m. – 5 p.m.
ALL DAY–ACCOUNTING & AUDITING UPDATE – 8 CPE credits (A & A)

Wednesday, June 29, 8–10 a.m.
HOW TO SURVIVE YOUR CLIENT'S SALES TAX AUDIT – 2 CPE credits (MAP)
On Parade Diner, 7980 Jericho Tpke. Woodbury, N.Y.

LONG ISLAND EAST, NEW YORK

Contact: Chuck Pegler, CPA (631) 582-9090
E-mail: Chuck@PeglerCPA.com

Call for information.

NEW YORK CITY, NEW YORK

Contact: Jay Rosenbaum, CPA (212) 594-4610 ext 28
Please call to confirm all meetings as topics, times, and locations are subject to change due to attendance, speakers preference, etc.

May & June: To be announced.

Join us!

PHILADELPHIA GROUP EVENTS

Call 888-488-5400 for information.

May 10. **ESSENTIALS OF RISK MANAGEMENT** – 1 CPE credit (TAX) / 1 CPE credit (A & A)
June 14. **QUICKBOOKS FOR CPAs** – 2 CPE credits (A & A)

WESTCHESTER/ROCKLAND, NEW YORK

Contact: Chapter Office (914) 708-9404
DoubleTree Hotel, 455 South Broadway. Tarrytown, N.Y.

Tuesday, May 10, 7:30 – 9:15 a.m.
BUYING AND SELLING YOUR PRACTICE – 2 CPE credits

Tuesday, June 14, 7:30 – 9:15 a.m.
ETHICS – 2 CPE credits

NEW JERSEY

Contact: Fred Bachmann, CPA (973) 377-2009
E-mail: bachmanncpa@msn.com
Victor's Maywood Inn, 122-124 West Pleasant Ave, Maywood, N.J. Phone (201) 843-8022; E-mail: www.maywoodinn.com
6–8 p.m. – Dinner and Seminar

May & June: To be announced.

FLORIDA

Contact: Neil Fishman (561) 369-3228
New Meeting Location: Cypress Creek Country Club, 9400 Military Trail, Boynton Beach, FL
8:45 a.m. – 10:45 a.m., Registration at 8:30 a.m.

Thursday, May 5
IRS CRIMINAL INVESTIGATIONS – 2 CPE credits

Thursday, June 2
OFFERS IN COMPROMISE/OTHER OPTIONS – *2 CPE credits*

MASSACHUSETTS

Contact: Ronald Tockman, CPA (781) 341-2400 or
Jeff Winer, CPA (508) 879-0408
Sheraton Needham Hotel, 100 Cabot Street, Needham, Mass.

Thursday, May 5, 7:30 – 9:30 a.m.
SECTION 504 IMPROVEMENTS AND STATE TAX AND FILING UPDATE – 2 CPE credits

Wednesday, June 1, 7:30 – 9:30 a.m.
ETHICS – 2 CPE credits

HOUSTON

Call for Information: (888) 488-5400