

## Reporting Income Payments Using Form 1099-MISC

The IRS continues to increase its scrutiny of Form 1099 reporting by individuals and businesses. The IRS uses 1099s submitted to them to be sure Form 1099 recipients report the income on their income tax returns. Failure to comply with 1099 filing requirements may result in substantial penalties. Because of the *Small Business Jobs Act of 2010*, certain 1099-related penalties are more than double what they were in previous years.

The penalties increase the longer the 1099 filing failure continues or the longer it takes to correct 1099s filed incorrectly. Penalties range from \$30 to \$100 per form, with a maximum penalty of \$1.5 million. However, if the rules are intentionally disregarded, penalties increase to \$250 per 1099 with no maximum penalty.

Starting in 2011, IRS added two new questions on its individual and business tax forms to increase awareness of the 1099 filing requirements and add another opportunity to identify taxpayers that should be filing 1099s but are not. The individual tax forms reporting business income, rental income and farm income (Schedules C, E and F, respectively) have two additional questions:

1. "Did you make any payments that would require you to file Form(s) 1099?"
2. "If 'Yes,' did you or will you file all required Forms 1099?"

Similar questions also have been added to corporate and partnership returns.

Given the increased IRS focus on taxpayers' information reporting obligations, it is important to know when a Form 1099 filing is required.

### Who must file Form 1099-MISC?

- All entities engaged in a trade or business (sole proprietorships, partnerships and corporations)
- Landlords engaging in the business of renting property
- Nonprofit organizations, federal, state or local governmental agencies
- Trusts of qualified pension or profit-sharing plans of employers

### When is Form 1099-MISC Required?

Businesses will need to fill out a Form 1099-MISC for each person, vendor, subcontractor, independent contractor, and others in the following circumstances:

**\$600 or more per year is paid for** rents, services (including parts and materials), prizes and awards, medical and health care payments, crop insurance proceeds, cash payments to fishermen, proceeds paid to attorneys, and other types of payments not covered by another information reporting document.

Reporting such payments is required if the recipient of the payment **is not a corporation** - for example, when the recipient is an individual, estate, partnership, a limited liability company treated as a partnership or sole proprietorship. Payments made to corporations may be reported using Form 1099-MISC, but is not required.

#### *Exceptions:*

- **Payments to corporations for legal services.** The exemption from reporting payments made to corporations does not apply to payments for legal services. Therefore, you must report attorneys' fees (in box 7) or gross proceeds (in box 14) as described earlier to corporations that provide legal services.
- **Medical and health care payments** are reported on Form 1099-MISC even if made to corporations.
- **Payments of rent to real estate agents** do not have to be reported. But the real estate agent must use Form 1099-MISC to report the rent paid over to the property owner.

### Steps to Take to Prepare for 1099-MISC Forms

You should request that your vendors, contractors and other payment recipients submit to you a [Form W-9](#). The W-9 will provide you with the legal name, address and taxpayer identification number for the vendor, which is the information you will need when preparing any 1099-MISC forms.

You should also keep track of your payments in your bookkeeping system. You will need to know whether the payment falls under any of the categories listed above for reportable payments, whether your payments to a particular recipient reaches the \$600 threshold for reporting, and finally you'll need to know the exact amount you paid the recipient for the year.

### Backup Withholding Requirement Policy

Backup withholding is required on payments if TIN is not furnished by the payee. If you are required to withhold but fail to do so, you may be liable for the amount you should have withheld, unless the payee included the payments on a tax return.

## **1099-MISC Requirements for Landlords**

In the past couple of years Congress has been active in modifying filing requirements for informational returns, especially 1099s. All of these changes have left informational return filing requirements misconstrued, especially in the case of landlords on their individual tax returns.

The Patient Protection and Affordable Care Act (PPACAP), enacted in 2010, increased the 1099 filing requirements to include any payment of \$600 or more for goods or services rendered from any single vendor. On September 27, 2010, the Small Jobs Business Act (SBJA) was passed reclassifying any individuals receiving rental income as engaging in the business of renting property, and as a result, expanded the 1099 filing requirement by the PPACAP to all landlords. Prior to 2011 owners of rental real estate were generally not considered to be engaged in a trade or business and were therefore exempt from the 1099 reporting requirements.

In the spring of 2011 both the extensive 1099 filing requirements sanctioned by the PPACAP and the extension of these requirements to landlords under the SBJA were repealed by the Comprehensive 1099 Taxpayer Protection and Repayment of Exchange Subsidy Overpayments Act of 2011. This repeal has caused the misunderstanding that landlords are no longer required to file 1099s for services paid.

Although the act repealed the extensive reporting requirements in which landlords were included, the historical rules still apply, causing some landlords to still be obligated to file Form 1099. Landlords engaging in the business of renting property are still required to issue 1099s for vendors paid \$600 or more. A person engaging in a trade or business is defined as a person who is involved in the activity continuously and regularly and whose main motive in engaging in the activity is for income or profit. Thus these filing requirements will not apply to the owner of property who turns over management duties to an outside source, as he is not regularly and continuously involved in the activity.

To emphasize the matter of filing requirements, the IRS has modified Schedule E. At the top of Schedule E there are now two new questions, A and B. Question A asks, "Did you make any payments in 2012 that would require you to file Form(s) 1099?" Question B asks, "If 'yes,' did you or will you file all required Forms 1099?" For example, if a landlord pays \$600 or more to an attorney to collect unpaid rent on their behalf or to a handyman for various repairs in a rental unit over the course of 2012, the landlord would have to answer "yes" to both questions since it is a payment in the course of a trade or business and the payment amount is above the \$600 threshold.

It is also important to note that although the extensive filing requirements were alleviated with the repeal, the increase in penalties for not filing 1099s still pertains. Taxpayers are penalized \$250 for each 1099 intentionally not filed.