CribSheet 12-5
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IRS Form 1099

Businesses report wages and salaries on IRS Form W-2 and report certain other transactions on 1099 forms. The 2010 healthcare law originally expanded 1099 reporting requirements in ways that would have imposed enormous costs on small and large businesses. NFIB led a successful fight to repeal the expansion. Businesses still have to file other 1099s, however.

1099s report income to the IRS.

1099s were designed to increase tax compliance.

The Internal Revenue Service (IRS) tracks employee wages and salaries via W-2s in order to minimize tax evasion. 1099 forms similarly alert the IRS to other forms of income.

The "tax gap" led to 1099s.

1099s are designed to partially reduce the "tax gap" – the difference between taxes owed and taxes paid. For 2006, the IRS estimated a net tax gap of $385 billion – $450 billion unpaid minus $65 billion recovered later.

Evidence of the tax gap is sketchy.

There is little evidence concerning the extent of unpaid business taxes or the effectiveness of the 1099 program in reducing the tax gap. Under-reporting seems to result primarily from tax law complexity, and 1099s may exacerbate, rather than alleviate the problem.

"1099" refers to a series of 17 separate IRS forms.

The 1099 is a series of seventeen different forms.

They include the following. (Boldface means forms that are especially important to small business.)

- 1099-A: Acquisition or Abandonment of Secured Property
- 1099-B: Proceeds from Broker and Barter Exchange Transactions
- **1099-C: Cancellation of Debt**
- 1099-CAP: Changes in Corporate Control and Capital Structure
- **1099-DIV: Dividends and Distributions**
- 1099-G: Certain government Payments
- 1099-H: Health Coverage Tax Credit (HCTC) Advance Payments
- **1099-INT: Interest Income**
- **1099-K: Merchant Card and Third Party Network Payments**
- 1099-LTC: Long-Term Care and Accelerated Death Benefits
- **1099-MISC: Miscellaneous Income**
- 1099-OID: Original Issue Discount
- 1099-PATR: Taxable Distributions Received From Cooperatives
- 1099-Q: Payment from Qualified Education Programs (under Sections 529 and 530)
- 1099-R: Distributions from Pensions, Annuities, Retirement or Profit-Sharing Plans, IRAs, Insurance Contracts, etc.
- **1099-S: Proceeds from Real Estate Transactions**
- 1099-SA: Distributions From an HSA, Archer MSA, or Medicare Advantage MSA

The 1099-MISC is of special interest to small business.

Small businesses frequently use the 1099-MISC.

If a business spends $600 or more for services from an unincorporated business (S corps, LLCs, sole proprietors, etc.) during a tax year, the total is reported on a 1099-MISC. A large proportion of small businesses use the services of unincorporated businesses or are themselves unincorporated.

Small businesses must report purchases of services from unincorporated vendors.

Businesses file a 1099-MISC when purchasing services (not goods) from unincorporated vendors (not corporations). For example:

REPORT a $700 purchase of computer repair **services** from Jones's Computers (**independent contractor**).
DO NOT REPORT a $700 purchase of computer repair **services** from Best Buy (**corporation**).
DO NOT REPORT a $700 purchase of computer **equipment** from Jones's Computers (**independent contractor**).
DO NOT REPORT a $700 purchase of computer **equipment** from Best Buy (**corporation**).

1099 compliance is expensive.

Tax compliance costs a business roughly $74 per hour or, according to the Small Business Administration, $1,500 per employee. Each 1099-MISC involves copies for the purchaser, the vendor, the IRS, and some state governments.

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1099s require withholding.

If the purchaser is unable to provide the IRS with a vendor's Taxpayer Identification Number (TIN), the purchaser must withhold 28% of the amount of the transaction and forward it to the IRS.

Penalties are costly.

The IRS can issue a $50 fine for each missing 1099 form; before 2011, the fine was also applicable to submitted forms with inaccuracies, including an incorrect TIN. The IRS can double the fines if they judge the errors and omissions to be willful. Penalties can total $500,000 for businesses with gross receipts under $5 million or $1.5 million for businesses with gross receipts over $5 million.

PPACA was set to greatly expand 1099s.

The Patient Protection and Affordable Care Act (PPACA) originally added an avalanche of 1099s. A 1099-MISC is only required for purchases of *services* from *unincorporated* entities. PPACA **would have expanded** this to include purchases of goods and purchases from corporations. Businesses who currently file dozens of 1099s a year would have found themselves filing hundreds or thousands, instead.

Congress repealed the expansion.

NFIB successfully led a year-long battle to remove the 1099 provision from PPACA. As of May 2012, this remains the only successful effort to amend PPACA.

Businesses still must file Form 1099-MISC.

Repealing PPACA's 1099 expansion didn't eliminate the 1099. **Businesses must still file 1099s**, including the 1099-MISC, as before. The repeal simply means that the requirements still not be expanded to purchases of goods and purchases from corporations.

They were going to have to reconcile card receipts.

The IRS had planned to implement an ill-conceived requirement that small business owners record all of their "merchant card and third-party reporting payments" and reconcile them with a new Form 1099-K. These payments would have included credit card, PayPal, and certain other card-based transactions.

NFIB successfully lobbied against the card-receipt reconciliation.

NFIB was instrumental in persuading the IRS to drop the requirement to reconcile card receipts. The IRS dropped this requirement in February 2012. Since the amount reported on the 1099-K and the actual business income are usually different, this reconciliation would have forced small business owners to spend countless hours comparing the two.

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