MIND THE TAX GAP: HOW INCREASED REPORTING REQUIREMENTS EXPOSED THE POLITICAL AND PRACTICAL CHALLENGE OF COLLECTING SMALL BUSINESS TAX DEBT

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I. INTRODUCTION

According to the Congressional Budget Office, the Patient Protection and Affordable Care Act of 2010 ("PPACA") will reduce the federal budget deficit by an estimated $143 billion in the first decade after enactment.¹ One of the provisions intended to produce this effect is § 9006 of the PPACA, which expands business expenditure reporting requirements to the Internal Revenue Service ("IRS"), using the familiar Form 1099. By expanding the types of business expenditures that need to be reported annually to the IRS, Congress hopes to reduce unreported and underreported tax liabilities, and therefore increase tax revenue by revealing more collectible taxes.² This will reduce the federal budget deficit by reducing the “tax gap,” the difference between taxes legally owed and taxes actually paid. While reducing the deficit by collecting tax debts already owed is preferable to creating new tax debts by establishing new taxes, this particular effort comes at a cost to small businesses owners (and, to a lesser extent, to the IRS). This cost may outweigh the benefit of collecting previously uncollectible taxes. Because of this, small business tax advocates,³ members of the U.S. Senate, and even the Obama Administration⁴ argue that the law as enumerated in the PPACA either needs to be amended to some degree or repealed entirely, although there is little agreement as to the right way to change the new law. Whether or not the law changes before it takes force in January 2012, it is important to

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¹ Juris Doctor, The Ohio State University Moritz College of Law, expected 2012.
² Neil deMause, Health care law's massive, hidden tax change, CNN (May 5, 2010, 11:00 PM), http://money.cnn.com/2010/05/05/smallbusiness/1099_healthcare_tax_change/.
disclose the practical impact and high price the law will have on small businesses, and to prepare small business owners for efficient and cost-effective compliance with the new law, or whatever replacement small businesses might encounter down the road.

Sections II and III of this paper explain exactly what the tax gap is and why the small business community bears a fair amount of responsibility for its existence. Sections IV and V explain the current state of the law and the current taxpayer responsibilities for filing the Form 1099. Sections VI through IX explain the new law and new responsibilities, as introduced through I.R.C. § 6041 (the codified version of § 9006 of the PPACA), as well as reasons why the key players find the additions so disruptive. Sections X and XI highlight the recent congressional actions and attitudes towards the legislation and discuss the potential future faced by small business taxpayers if the provision is repealed. Finally, Section XII provides practical, preparatory advice for the small business owner in the face of an uncertain regulatory future. Ultimately, the goal of this article is to provide the reader with an understanding of why revenue provisions such as § 6041 are so often aimed at small business taxpayers, and why such provisions face political and practical failure.

II. WHAT IS THE TAX GAP?

Before delving into the specifics of the law, it is important to understand what the federal tax gap is and why the government is targeting small businesses in order to reduce it. According to the Treasury Department, "[t]he tax gap is defined as the aggregate amount of true tax liability imposed by law for a given tax year that is not paid voluntarily and timely." The IRS "developed the concept of the tax gap as a way to gauge taxpayers' compliance with their federal tax obligations. The tax gap measures the extent to which taxpayers do not file their tax returns and pay the correct tax on time." In other words, the tax gap boils down to deceptively simple arithmetic: the amount of taxes owed to the IRS minus the amount the IRS was able to collect. According to the Department of the Treasury, the IRS collected $2.7 trillion in 2008. That seems like a lot of money, but it does not represent all the money owed to the IRS. For the

5 Office of Tax Policy, U.S. Dep't of the Treasury, Update on Reducing the Federal Tax Gap and Improving Voluntary Compliance 32 (2009). The report went on to note potential reasons for the discrepancy: "For a variety of reasons, this amount often differs from the amount of tax that a taxpayer reports on a return. The taxpayer might not understand the law, might make inadvertent mistakes, or might misreport intentionally." Id.
7 Office of Tax Policy, supra note 5, at 2.
fiscal year 2001, the IRS estimates that the tax gap was in excess of $345 billion.\textsuperscript{8} Despite collecting $2.7 trillion in 2008, the IRS is still owed hundreds of billions of dollars.

The arithmetic supporting the tax gap estimate of $345 billion is deceptive for two reasons. First and most obvious,\textsuperscript{9} the $345 billion figure was calculated in 2005 using data from the fiscal year 2001.\textsuperscript{10} It is difficult to refresh this number frequently because it is an estimate comprised of three other smaller estimates, which will be discussed later in this section.\textsuperscript{11} Therefore, the number is based on estimated data that is nearly a decade old.\textsuperscript{12} While the IRS is ramping up its efforts to produce more current and more accurate data on the tax gap, that effort is unlikely to bear any fruit until 2011.\textsuperscript{13} The $345 billion figure is deceptive for a second reason: it is not possible to conclusively establish how much money each taxpayer actually owes. The IRS does not have a spreadsheet indicating the amount owed by each taxpaying entity before it starts collecting taxes for any given year. The onus is on the taxpayer to report this information by reporting personal or business income, payments made to suppliers, wages paid or received, and other taxable expenditures or gains. That does not always happen, as this paper will discuss; in fact, the Treasury Department estimates that only eighty-four percent of tax liabilities are voluntarily reported to the IRS.\textsuperscript{14} If the taxpayer underreports their tax liabilities, the government has to do the legwork to uncover that discrepancy. In the meantime, that discrepancy, when combined with all the other discrepancies taken from all the other taxpayers, is considered to be the tax gap. The IRS estimates that it was able to reduce the 2001 tax gap from

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  \item \textsuperscript{8} See id.
  \item \textsuperscript{9} While reading this article, it is important to carefully note the year or years being discussed.
  \item \textsuperscript{10} See OFFICE OF TAX POLICY, supra note 5, at 2.
  \item \textsuperscript{11} See id. at 4. This report contains a chart detailing the different elements of the tax gap. It is noteworthy that the chart identifies each sub-element of the tax gap and color-codes each sub-element as being supported by either “actual amounts,” “reasonable estimates,” or “weaker estimates.” Id. The tax gap itself is identified as a “weaker estimate.” Id.
  \item \textsuperscript{12} See id. at 2.
  \item \textsuperscript{13} See id.
  \item \textsuperscript{14} The use of the word “only” may be inappropriate. Eighty-four percent taxpayer compliance is actually higher than that experienced throughout much of the rest of the Western world, including Austria (74.8%), France (75.38%), Germany (67.72%) and Italy (62.49%). See Edward Christie & Mario Holzner, What Explains Tax Evasion? An Empirical Assessment Based on European Data (The Vienna Inst. for Int’l Econ. Studies, Working Paper No. 40, 2006).
  \item \textsuperscript{15} OFFICE OF TAX POLICY, supra note 5, at 2.
\end{itemize}
$345 billion to $290 billion through enforcement actions and by collecting late payments, but it was unable to collect the rest.\(^\text{16}\)

According to the IRS, the tax gap has three primary components: (1) underpayment of taxes, (2) non-filing of returns, and most significantly, (3) underreporting of income.\(^\text{17}\) Underreporting of income is the largest component of the tax gap, constituting eighty-two percent, or $285 billion, of the total tax gap.\(^\text{18}\) Underreporting of income occurs when a business earns taxable income but fails to report that income. Of the $285 billion in underreported income, non-corporate business income (i.e., individually-owned business income) contributed $109 billion.\(^\text{19}\) In other words, the tax gap is substantially comprised of the underreporting of income from non-corporate business activities.\(^\text{20}\) By comparison, corporations, both large and small, only owed an estimated $30 billion.\(^\text{21}\) Small businesses are responsible for nearly a third of the tax gap ($109 billion out of $345 billion) and are responsible for over three times as much of it as incorporated entities ($109 billion compared to $30 billion). This is why Congress, through legislation such as the amended I.R.C. § 6041, has focused on small businesses.\(^\text{22}\) Generally speaking, this is why efforts by Congress and the IRS focus on small businesses when they seek to reduce the tax gap.

Mark W. Everson, the IRS Commissioner in 2005, admitted that "no one should think we can totally eliminate the gap. That would take Draconian measures and make the government too intrusive. We have to strike the right balance."\(^\text{23}\) The Treasury Department agrees, recommending that, while closing the tax gap should be a priority, “enforcement activities should be combined with a commitment to taxpayer service,” and “policy positions and compliance proposals should be sensitive to taxpayer rights and maintain an appropriate balance between enforcement activity and imposition of taxpayer burden.”\(^\text{24}\) In other words, even with a $345 billion gap consisting of unpaid taxes rightfully owed to the government, consideration should still be given to keeping the burden on taxpayers manageable. We will see more of this “customer service”

\(^{16}\) See id.
\(^{17}\) See id. at 2–3.
\(^{18}\) Id. at 3.
\(^{19}\) See id. at 4.
\(^{20}\) See id.
\(^{21}\) See id.
\(^{22}\) See generally OFFICE OF TAX POLICY, supra note 5 (the conclusions and solutions in this report focus heavily on both collecting more taxes from small businesses and on mitigating the costs of those increased collection efforts).
\(^{24}\) OFFICE OF TAX POLICY, supra note 5, at 5.
mindset when we discuss the approach the IRS is taking to implement the
law and the approach the IRS might take if the law is repealed.

Furthermore, the Treasury Department realizes that small businesses
would be particularly hard hit by tougher measures (i.e., enforcement
measures, as opposed to “customer service” measures). In its report, the
Treasury Department emphasized seven considerations that should bear on
any legislation or regulatory changes addressing the tax gap. Only two of
these seven considerations suggested tougher enforcement. The rest of the
considerations address improving the IRS's own information systems and
procedures, improving IRS customer service, simplifying the law to assist
compliance, and working with organizations like the Small Business
Administration ("SBA") to further assist small businesses.

III. THE CULPABILITY OF SMALL BUSINESSES

Although the government recognizes that limiting the taxpayer burden
is a strong policy consideration, the federal government does have a strong
practical reason to reduce the tax gap. The tax gap consists of taxes owed
by taxpayers that have simply gone unpaid. In his March 29, 2005 news
release, Mr. Everson stated that:

[While] the vast majority of Americans pay their taxes honestly and accurately... [e]ven after IRS enforcement
efforts and late payments, the government is being shortchanged by over a quarter-trillion dollars by those
who pay less than their fair share. People who aren’t paying their taxes shift the burden to the rest of us.

It bears repeating: the tax gap does not represent taxes the government
wants to impose but has not; the tax gap represents unpaid tax liabilities
that are rightfully owed under the Internal Revenue Code. The best IRS
estimates place the liability of small businesses at approximately $109
billion. Whether the 1099 reporting requirements established in the
PPACA and the Small Business Jobs Act of 2010 overburden small
businesses, the measures are targeted at a culpable segment of taxpayers.
The measures are also aimed at reducing the tax gap in the category that
carries the single largest bulk of the tax gap: individual or small business
taxpayers engaging in small-scale business transactions that fail to report
those transactions for tax purposes. It is important to keep in mind that the “tax gap” refers to taxes that should have been paid, but were not.29

Clearly, small businesses that fail to pay their taxes are liable to the government. As a matter of fairness, they are culpable with regard to all other taxpayers who voluntarily and fully pay their taxes. In a 2009 report, the Treasury Department sought to better communicate what it knows about the intentional underreporting by taxpayers in general:

[T]he tax gap does not arise solely from tax evasion or cheating. It includes a significant amount of noncompliance due to tax law complexity that results in errors of ignorance, confusion, and carelessness. This distinction is important even though, at this point, the IRS does not have sufficient data to distinguish clearly the amount of noncompliance that arises from willful, as opposed to unintentional, mistakes. Moreover, the line between intentional and unintentional mistakes is often a grey one, particularly in areas such as basis reporting, where a taxpayer may know that his or her reporting is inaccurate but does not have ready access to accurate information. This is an area where additional research is needed to improve understanding.30

In other words, the IRS cannot say whether small business noncompliance (or any taxpayer noncompliance) is due to intentional noncompliance or due to mistake. As the IRS admits, additional research may improve the IRS’s understanding of the reasons why taxpayers generally, and small businesses specifically, fail to report their tax liabilities. That being said, the old 1099 reporting requirements, as well as the new ones, are intended to achieve the same end: supply the IRS with enough information to know what taxes it is owed and from whom.

IV. CURRENT REPORTING REQUIREMENTS

Under the pre-amendment law, required reporting using IRS Form 1099 is common but relatively straightforward, requiring businesses to submit a Form 1099 for specific types of transactions in which the business paid $600 or more to the same payee.31 Government Accountability Office (“GAO”) research revealed that currently, small businesses spend between three and five hours per year filing 1099 data manually, an effort the GAO

29 As discussed earlier, the tax gap figure includes unpaid taxes whether nonpayment was intentional or unintentional.
30 OFFICE OF TAX POLICY, supra note 5, at 32–33.
considers quite low. Small businesses typically file these forms manually, using in-house accounting software to track reportable payments. For taxpayers filing fewer than 250 Forms 1099, they may file by paper or electronically, while businesses filing more must file online through the IRS. Currently, the majority of transactions do not require the submission of a Form 1099. Only transactions involving the sale of services, such as those by an independent contractor, require the payor (the party that paid for the services) to submit a 1099. Additionally, in most cases, business-payors are not required to send a 1099 to corporate payees. Specifically, the payor must file a 1099-MISC for each payee (person the filer paid) where payments totaled $600 during the tax year for the following:

- Rents, services (including parts and materials), prizes and awards, other income payments, medical and health care payments, crop insurance proceeds, cash payments for fish (or other aquatic life) you purchase from anyone engaged in the trade or business of catching fish, or, generally, the cash paid from a notional principal contract to an individual, partnership or estate;
- Any fishing boat proceeds;
- Gross proceeds to an attorney.

Payments to corporations (with few exceptions) are not reportable. The same goes for payments to tax-exempt organizations. Most importantly, payments for merchandise (goods) are specifically exempted.

Here is how the process works: The buyer fills out the form and sends one copy to the seller and one copy to the IRS. This is so the buyer, the seller and the IRS can verify they all have the same information, or can be made aware that there is a discrepancy in the information. The purpose of the Form 1099-MISC is to give the IRS as much information as possible so that it may determine when a certain transaction resulted in taxable income.

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33 See id.
35 See I.R.C. § 6041.
36 See id.
37 See id.
39 See I.R.C. § 6041.
40 See id.
41 See id.
42 See id.

6 Ohio St. Entrepren. Bus. L.J. 103 2011
By requiring the buyer to submit the form to both the IRS and to the seller, the IRS is able to hold parties on both sides of a single transaction responsible for reporting that transaction. The seller, typically an independent contractor or unincorporated business operator, must report the income using a Form 1040. The IRS will match the information reported on the seller's Form 1040 and all of buyers' Forms 1099 to discover whether the seller is reporting all the income it should be for the tax year. For example, if ten buyers submit Form 1099 to the IRS for "Seller A," with each buyer reporting $600 in qualifying purchases from Seller A, then Seller A's Form 1040 should include the cumulative $6000 in income from its ten buyers. If Seller A reports an amount less than $6000, the IRS should notice and investigate the discrepancy.

The pre-amendment law targets transactions between independent contractors, sole proprietors and unincorporated businesses specifically because those types of transactions are relatively less likely to be properly reported. Unincorporated entities, such as the self-employed independent contractors, were the primary target under the old law.

V. INEFFICIENCIES EXIST EVEN UNDER THE CURRENT LAW

Government Accountability Office research reveals that, even under the old law, the IRS is inefficient at identifying business taxpayers that failed to file tax returns generally. "For tax year 2007, [the] IRS had identified almost 2 million businesses as potential nonfilers whose cases had not been resolved as of June 2009." These 2 million cases represent business nonfilers that the IRS has reason to believe should have filed, but the IRS is not certain that a filing was required. The GAO and IRS admit that many of these 2 million entities do not need to file, but the current information systems at the IRS do not reveal enough data to say one way or the other. These entities may not have to file for a number of reasons: they are no longer operating, they no longer have any employees, they no longer produce any revenue, or they have been merged with another entity that now reports on behalf of the non-reporting entity. In other words, the information the IRS currently possesses on these entities does not reveal taxable income or the existence of employees, but other data held by the IRS from other parties indicates that these entities are producing income and do have employees. The GAO made at least two recommendations to

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43 See IRS Form 1040 (2010).
45 See id. at 1.
46 See id.
47 See id.
48 See id. at 14.
49 See id.
the IRS regarding its current use of information: (1) improve its Business Master File Case Creation Nonfiler Identification Process ("BMF CCNIP") to better identify which businesses are most likely to fail to pay taxes, and (2) gather and use third-party data to reveal whether questionable entities truly need to file so the IRS can pursue those entities.50

The BMF CCNIP is the IRS’ current system for organizing nonfiling businesses in the order of the likelihood that they owe taxes.51 The IRS takes the available information for each entity on income and business activity and inserts it into this system.52 The BMF CCNIP assigns each case (nonfiling business) a code based on this data.53 According to the GAO, “[the] IRS uses the code to select cases to work with the goal of securing tax returns from nonfilers and collecting additional revenue.”54 The system boils down to targeting first those taxpayers with the most tax debt. Although the system shows great promise according to the GAO, the report identified two problems with this system. First, for nearly sixty-five percent of the businesses that the system identifies as “closed,” the BMF CCNIP results give no reason for why the business closed.55 This makes it difficult to establish a formula for accurately identifying closed businesses. For example, a business may have closed but failed to notify the IRS of the closure,56 or a business may have changed its corporate structure or may have terminated its employees due to seasonal business fluctuations.57 The inability to accurately and efficiently identify which non-filing businesses owe taxes costs the IRS an extraordinary amount of resources chasing business entities that don’t exist or don’t owe taxes.58 Erroneous IRS actions also cost taxpayers resources: when the IRS mistakenly pursues a taxpayer for taxes that the taxpayer does not owe, the taxpayer has to spend time and money defending an action that the IRS would have known was not necessary if it had better information.59 Current use of the BMF CCNIP section is inefficient in another respect: the IRS may be closing60 cases where, in reality, billions of tax dollars are owed.61 For the tax year 2007, IRS employees closed 39,931 partnership and corporation cases as "not

50 See id. at 1.
51 See id.
52 See id.
53 See id.
54 See id.
55 See id. at 13.
56 See id.
57 See id.
58 See id. at 21.
59 See id.
60 A “closed” entity is one that the IRS has concluded is no longer operating, and therefore no longer owes taxes.
61 See U.S. GOVT ACCOUNTABILITY OFFICE, supra note 44, at 15.
liable to file returns. These cases represented reportable income totaling over $193 billion. The GAO estimates that a large portion of this amount may have actually been owed, and the IRS may have incorrectly closed a large proportion of these cases. As the research presented above indicates, improved BMF CCNIP data would allow the IRS to more efficiently close cases where businesses owe no taxes, and more effectively avoid closing cases where businesses actually do owe taxes. The GAO concludes that deficiencies in the promising BMF CCNIP system are resulting in uncollected revenue from improperly closed cases, and wasted resources pursuing cases that should have been closed immediately.

The GAO also recommends that the IRS gather and use third-party data to reveal whether any of these 2 million non-filing entities have employees or produce income. The GAO references two third-party sources: industry reporting agencies such as Dunn & Bradstreet ("D&B"), and the federal Central Contractor Registration ("CCR") file, which is a file containing the names, revenues and employment numbers of entities that are seeking federal contracts. The GAO found that these two resources produced data that revealed income and employees that the IRS data does not show. For example, GAO research in California and Illinois for the tax year 2007 reviewed 39,920 cases closed by the IRS because IRS data indicated those businesses had no employees. D&B data indicated otherwise; 4185 of those businesses had a total of 16,869 employees and conducted $20.3 billion in business. These businesses may have owed billions in tax dollars. The IRS failed to find what D&B data easily found, and this data only represents improperly closed cases in two states.

The GAO also researched the federal CCR file, which contains businesses that register annually wishing to be awarded federal contracts. Businesses registering for the CCR must report revenue and employment data. This self-reported information would indicate clearly whether a business is really closed, and whether it owes taxes. Reviewing this register, the GAO found 3589 entities reporting revenue and 10,263 entities

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62 See id. at 15.
63 See id.
64 See id.
65 See generally id.
66 See id. at 7.
67 See id. at 18.
68 See id. at 19.
69 See id. at 18–19.
70 See id. at 18.
71 See id. at 17–18.
72 See id. at 19.
73 See id.
reporting employees, all entities the IRS had closed for the 2007 tax year. It is very likely that these businesses should have filed some sort of return to the IRS, but the IRS closed these cases because in-house information did not show this revenue or employee data. Therefore, the CCR represents a second third-party source of information for identifying liable entities. The GAO admits that the CCR is limited to use only for the 400,000 businesses registered on the CCR.

Given the GAO's findings, two related conclusions can be drawn regarding the IRS's current information systems under the old law. First, the IRS is already struggling to use the information it has available to it, either in-house or through readily-available third parties. Second, despite the shortcomings, the current information systems show promise, and if the IRS was given the time and resources to improve the BMF CCNIP and its use of third-party information, it would be able to more efficiently collect unpaid taxes without expanding the old 1099 reporting requirements.

VI. NEW REPORTING REQUIREMENTS ESTABLISHED IN 2010

The year 2010 saw the enactment of two critical pieces of legislation related to reporting under I.R.C. § 6041 of the tax code: § 9006 of the PPACA, which will become effective on January 1, 2012, and the Small Business Jobs Act of 2010, which has already gone into effect. Taken together, both pieces of legislation drastically broadened the scope and volume of reporting required under § 6041.

First, the variety of covered transactions has expanded to include the sale of goods and purchases by landlords in connection with the lease of

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74 See id. at 19.
75 See id.
76 See id.
77 See id. at 23.
79 See id.
their property. Additionally, corporate payees (sellers) will no longer be exempt, and small businesses will have to submit Forms 1099 to their large corporate suppliers and small independent contractors alike. According to the Treasury Department and the National Taxpayer Advocate, the new law would apply to nearly 26 million sole proprietorships, 6 million corporations, 3 million partnerships, 2 million farming businesses, 1 million charities and other tax-exempt organizations, and more than an estimated 100,000 federal, state, and local government entities. In other words, Forms 1099 must be filed for a much wider variety of transaction types, and for sellers of nearly every categorization. Corporations are no longer exempt, and neither are purchases of merchandise. These two changes alone vastly increase the number of Forms 1099 each taxpayer will have to file if they spend $600 or more with any single vendor.

Second, the laws have elevated the severity of the penalties for failing to file a 1099 where required. When a business fails to file a required 1099, the penalties for each failure to file by “persons generally” have doubled from $50 to $100. Additionally, the maximum “aggregate annual limitation” for penalties for persons generally under § 6041 has increased from $250,000 to $1,500,000. Whether the taxpayer is large or small, or the failure to file is accidental or willful, § 6721 raises the penalty amounts across the board. Compounded with the fact that businesses will be filing exponentially more Forms 1099, the small business owner’s exposure to penalty even for inadvertent failure has increased greatly.

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82 A corporate payee is defined by the IRS as an entity “formed under state law by the filing of articles of incorporation with the state.” See Definition of a Corporation, IRS, http://www.irs.gov/charities/article/0,,id=96118,00.html (last visited Mar. 30, 2011).
83 NAT’L TAXPAYER ADVOCATE, IRS, REPORT TO CONGRESS: FISCAL YEAR 2011 OBJECTIVES 10 (June 30, 2010).
84 See id. at 10.
86 See id.
87 See id.
88 See id.
89 NAT’L TAXPAYER ADVOCATE, supra note 83, at 12 (“The new volume of information reports could exacerbate underassessment of penalties in some cases and overassessment [sic] of penalties in others.”).
VII. THE RATIONALE BEHIND § 9006 AND THE SMALL BUSINESS JOBS ACT OF 2010

Besides the lingering threat of prison time, information reporting is currently the most powerful tool the IRS has in compelling compliance with tax obligations because the more taxable transactions the IRS is aware of, the more taxes the IRS can pursue. To make matters more difficult for legislators seeking to fund new proposals such as the PPACA, the federal budget deficit for the 2010 fiscal year is $1.294 trillion, leading Congress and the President to lean heavily on the IRS to collect every dollar owed in taxes. By uncovering taxes already owed to the government, Congress hopes to help pay for PPACA, without increasing the deficit, and without raising taxes.

The new laws increase the potential for revenue in two ways: first, by uncovering transactions that would have been unreported so those transactions may be taxed, and second, increasing the number of payments and amount paid in penalties for failure to file. The basic idea behind the new reporting requirement is to create a paper trail connecting both sides of each transaction and making mutual the responsibility for reporting each transaction. That way, inadvertent failures to report become much less likely, and intentional failures to report become harder to commit because the buyer is now responsible for reporting the transaction, not the seller (who may wish to hide the transaction in order to avoid paying taxes on the sale).

Additionally, because so many more transactions will be subject to reporting requirements, the likelihood of failing to report may increase. In fact, the IRS believes that the risk of over-penalizing taxpayers will grow as well. Even without over-penalization, one pundit estimates that “if every small-business in America missed just one 1099 it would generate an estimated $10 billion in revenue to the government every year.” By vastly increasing the number of 1099s that need to be submitted, and by also

90 I.R.S. News Release IR-2010-68 (May 27, 2010).
91 Joint Statement of Timothy Geithner, Secretary of the Treasury, and Jeffrey Zients, Acting Director of the Office of Management and Budget, on Budget Results for Fiscal Year 2010, TG-911 (Oct. 15, 2010).
92 I.R.S. News Release IR-2010-68, supra note 90.
93 Id.
94 Id.
95 Id.
96 Id. at 12.
increasing the number and variety of businesses required to submit them, there will undoubtedly be more opportunities to assess penalties for failing to file or for filing improperly. Experts expect that the greatest difficulties will stem from the accurate collection of Tax ID numbers ("TINs"). Whether a TIN is inaccurately recorded by the payer, or inaccurately relayed by the seller, either mistake will cost the filing party in penalties. These penalty provisions are expected to provide additional revenue to the government.

It is interesting to note that, although the idea of expanding the 1099 reporting requirements is included in PPACA, legislation drafted by top Democrats and President Barack Obama, the idea was originally conceived by the White House under George W. Bush. It is clear that closing the tax gap has been a concern of Presidential administrations and Congresses even before the consideration and passage of PPACA. The PPACA merely provided an opportunity to use the more stringent reporting requirements as a way to fund the healthcare provision without actually imposing new tax burdens.

VIII. THE PRACTICAL CHANGES TO THE SMALL BUSINESS OWNER'S DUTIES

If the law remains unchanged as enacted in PPACA and the Small Business Jobs Act of 2010, small business owners should expect the following changes to their routine. First, the number of Forms 1099 small businesses must generate and send to suppliers will increase by multitudes. Additionally, businesses that have never received Forms 1099 from their buyers can expect to start receiving them once the law takes effect. While the old 1099 reporting requirements were aimed at the category of individual / small business taxpayers, the new requirements are broadened to include payments to corporate sellers regardless of size.

Second, the TIN will become an incredibly important number in the daily course of business. To avoid a mountain of work at the beginning

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98 Nat'l Taxpayer Advocate, supra note 83.
100 Nat'l Taxpayer Advocate, supra note 83, at 11.
101 See id.
102 See Frequently Asked Questions about Backup Withholding, IRS, http://www.irs.gov/efile/article/0,,id=98145,00.html (last visited Mar. 30, 2011). The TIN may be any one of the following: a Social Security Number, Employer Identification Number, an IRS individual taxpayer identification number, or an Adoption Taxpayer Identification Number. Id.
103 See id.
of each year, TINs should be collected as a matter of course at the time of each transaction. By collecting TINs at the time of each transaction, businesses will not have to contact each and every supplier at tax time to request TIN information. Under the old requirements, waiting until tax time to collect TIN information would not have been as much of a burden because there were so few TINs to collect. Under the new requirements, since more transactions will be covered, more TIN numbers will have to be collected. Additionally, transaction records should now be organized by TIN so that the TIN can be more easily determined at the end of the year whether or not the $600 threshold was met, and whether or not the transactions need to be reported. Small business owners can expect to respond to regular requests for their own TIN as well, which presents another critical consideration: identity theft. As TIN numbers become more widely available and widely reported, it will become easier for an identity thief to find the TIN for a targeted small business. With the TIN (or a social security number, if the filing taxpayer is an individual), an identity thief can assume the identity of a legitimate taxpaying small business and file for a tax return as that small business and receive a refund in the name of that small business. Therefore, not only does it become a hassle to collect TIN data from sellers and submit TIN data to buyers, it also comes with an increased risk of identity theft.

Third, credit and debit card use in the daily course of business will increase. Credit and debit card purchases do not need to be reported under the new law because such purchases are reported using a separate system that puts the reporting duty on the bank. Small businesses will instantly recognize the value of making routine purchases using a credit card to avoid reporting minor transactions under this new law. Furthermore, small businesses that currently do not offer their own customers the ability to pay using a credit card will be under greater pressure to do so. Small businesses may require all employees to make purchases for the company using a credit card, especially employees who travel extensively for business and accumulate small expenses with vendors across the country. One caveat: businesses should still track these purchases with their non-credit card purchases, and should still collect all available TINs and match TINs to each purchase.

104 NAT'L TAXPAYER ADVOCATE, supra note 83.
105 See id.
106 See id. at 11.
109 NAT'L TAXPAYER ADVOCATE, supra note 83.
reportable purchases, even if the majority of its transactions were made with a credit card, and having the TIN on hand is still recommended. Additionally, increased credit card use always brings the risk of increased credit card debt. Small business owners should be prepared to manage this debt, and owners should not use credit cards to avoid new tax filing requirements if interest payments will harm the company’s bottom line.

Another practical effect will concern approximately one million entities identified as “tax-exempt” by the IRS, including non-profit organizations. Although the old reporting requirements did include non-profit organizations and did require such organizations to file Forms 1099 just like other small businesses, the same increased burden felt by small businesses will be felt by non-profit organizations.

Altogether, these practical effects illustrate that the cost of complying with the new 1099 reporting requirements will be high for all taxpayers, and will be disproportionately high for smaller organizations, many of which may not have an accounting department or regular accounting professional on staff or accounting software in use. Furthermore, smaller organizations that did not previously have to e-file their Forms 1099 because they produced fewer than 250 per year might have to learn how to do so, or may be compelled to pay a professional e-filing service to handle the extra load if they expect their quantity of required Forms 1099 to exceed 250. Additionally, the cost of compliance goes hand-in-hand with the price of non-compliance: because failure-to-file penalties have doubled in many cases and because the cap on potential penalties has been increased by multitudes, liability has also increased.

IX. COSTS BORNE BY THE GOVERNMENT

Small businesses are not the only ones concerned with the new provisions. Currently, the IRS is struggling to implement the new law, and

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110 See id.
112 NAT’L TAXPAYER ADVOCATE, supra note 83, at 10.
113 See id.
114 See id. at 11.
115 See id.
116 Unfortunately, these costs are difficult to estimate, but the government acknowledges their existence. See U.S. GOV’T ACCOUNTABILITY OFFICE, supra note 32 (“Current 1099-MISC requirements impose costs on the third parties required to file them. The magnitude of these costs is not easily estimated because payers generally do not track these costs separate from other accounting costs”).
has voiced concerns about its own ability to process the increased volume of information.\textsuperscript{118} First, the information systems at the IRS are not currently capable of matching the new information with existing information; this may lead to unnecessary action by the IRS.\textsuperscript{119} The IRS has a document matching system, the Automated Underreporter Program ("AUR"), that compares amounts submitted by the taxpayer to amounts submitted by others, such as buyers or sellers, in the case of Forms 1099.\textsuperscript{120} This document matching system is not capable of accurately identifying discrepancies where a seller declared income but a buyer did not file a Form 1099 because payments did not exceed $600.\textsuperscript{121} In that circumstance, neither party did anything wrong, but the AUR might still find a discrepancy. For example, if Seller A sells $500 in goods in one tax year to Buyer B, Buyer B will not file a Form 1099 for that year, but Seller A will still report the income. This creates a discrepancy. Although such a discrepancy would have existed under the old law, the number of discrepancies will be multiplied by the new law. Identifying and properly ignoring these types of discrepancies will become much more difficult for the IRS because so many more will be improperly flagged.

Second, if a buyer and a seller use different methods of accounting for returned goods or refunds on goods, the Form 1099 submitted by a buyer may not include payments made on a returned good, while the Form 1040 submitted by a seller may include that payment as income. This discrepancy also exists under the old law, but will also be multiplied in frequency of occurrence under the new law. The IRS already depletes extra resources identifying these types of discrepancies under the old law; under the new law, discrepancies will increase dramatically, forcing the IRS to spend even more.

The IRS request for public comment on the amendments to § 6041 reveal additional concerns.\textsuperscript{122} Aside from the effort to reduce duplicative reporting, the IRS sought public comment on the appropriate definition of certain terms in § 6041.\textsuperscript{123} The definition of what constitutes "property" for the purpose of a business transaction does not seem very flexible, and
covers just about everything, including consumer and professional goods. Congress could have chosen to use the word “goods,” which would have granted the IRS greater leeway in narrowing the types of purchases that would fall under the law. The IRS still believes that it might define the terms in § 6041 narrowly, including the definition of “property,” in order to narrow the reach of the amendments.

The IRS also sought comment on whether payments between two affiliated corporations would need to be reported.\textsuperscript{124} This request by the IRS exposed an interesting and probably unintended effect of the amendments: since corporations are no longer exempt from the 1099 reporting requirements, should affiliated corporations be required to report transactions made between said affiliated corporations? The IRS seems to think that an exemption or limitation on that reporting requirement would be reasonable.

Another variable under IRS consideration is the time and manner in which reporting to the IRS needs to take place, and whether the current requirements can be relaxed to include longer reporting timeframes or relaxed reporting form requirements.\textsuperscript{125} The IRS has requested practical recommendations on new deadline requirements, indicating a willingness to delay the assessment of penalties for a longer time than allowed under current law.

The IRS is also considering one of the primary issues brought to light by National Taxpayer Advocate Nina Olsen, discussed earlier in this paper, regarding the burden of collecting and reporting TINs.\textsuperscript{126} The IRS is acutely aware of the burden on collecting TINs as well as the accompanying privacy issues. A related issue concerns backup withholding

\textsuperscript{124} Id. ("Whether or how the expanded reporting requirements should apply to payments between affiliated corporations, such as payments related to intercompany transactions within the same consolidated group.").

\textsuperscript{125} Id. ("The appropriate time and manner of reporting to the Service, and what, if any, changes to existing practices for Form 1099 information reporting to the Service are needed to minimize burden in compliance with the new reporting requirements.").

\textsuperscript{126} Id.

What, if any, changes to Form W-9, Request for Taxpayer Identification Number and Certification, and the existing rules for soliciting taxpayer identification numbers (TINs) are needed to minimize the burden for payors to obtain TINs from payees, what are the privacy concerns with respect to TINs, and what are other concerns regarding identifying payees.

\textit{Id.}
requirements.\textsuperscript{127} A backup withholding is filed by the taxpayer (in this case, the small business) when the small business is unable to get the TIN from the seller.\textsuperscript{128} Either the TIN was improperly communicated, or the seller failed to supply it to the small business. The IRS is aware that the number of instances where small businesses are unable to get the seller’s TIN might increase under the new law, which will increase the number of instances where the payor simply files an automatic twenty-eight percent backup withholding, which in turn might cause the IRS to overtax the seller.

Ultimately, the IRS has broad administrative authority to implement the law, including the authority to exempt certain parties or transactions from reporting requirements.\textsuperscript{129} The exemptions the IRS ultimately chooses, if any, will dictate the real burden businesses feel under the law, and will determine whether lawmakers ultimately feel the need to change the law. The concerns listed above were all issued for public consideration and comment by the September 29, 2010 deadline.\textsuperscript{130} Interestingly enough, a great deal of public comment concerned not how the IRS should implement the law, but whether Congress should repeal the amendments entirely.\textsuperscript{131} For example, the American Institute of Certified Public Accountants (“AICPA”)\textsuperscript{132}, with the collective associations of the U.S. Chamber of Commerce,\textsuperscript{133} each sent letters to Congress urging the repeal of PPACA and Small Business Jobs Act amendments prior to enactment. While both organizations possess the expertise to comment on the concerns of the IRS, neither chose to do so, instead focusing on getting the law repealed. The discussion focused so much on repeal (as opposed to trying to make the law work) that some proponents of the bill have grown agitated. After the expiration of the September 29 deadline for public comment, Senator Olympia Snowe criticized the SBA’s Office of Advocacy for its failure to

\textsuperscript{127} Id. ("How should the backup withholding requirements for missing TINs under the expanded new reporting requirements be administered in order to minimize burden on payors.").

\textsuperscript{128} See IRS Instructions for Form 1099-MISC (2011), supra note 38. (The filing party (payor) must list a twenty-eight percent withholding on payments made to a seller that failed to provide the payor with a TIN.).

\textsuperscript{129} See I.R.C. § 6201 (2006).

\textsuperscript{130} See I.R.S. News Release IR- 2010-51, supra note 122.

\textsuperscript{131} See id.

\textsuperscript{132} See Letter from Alan Einhorn, Chair, Tax Executive Committee, American Institute of Certified Public Accountants, to members of the U.S. Senate (July 19, 2010), available at http://www.aicpa.org/Press/PressReleases/2010/Pages/AICPA SupportsRepealofBurdensomeTaxInformationReportingMeasure.aspx.

officially comment on the legislation.\textsuperscript{134} The Office of Advocacy responded to this criticism by arguing, first, that it had been very actively involved with the IRS during the comment period, but that, in the end, the Office of Advocacy determined that helping the IRS implement the law would not provide the greatest benefit to small business owners. Instead, the Office of Advocacy would ask Congress to change the law measurably (or repeal it) before the IRS would be asked to implement it.\textsuperscript{135} The Office of Advocacy concluded in its letter that, "[t]he roundtable participants suggested no alternative, short of legislative action, that would minimize the impact of the expanded Form 1099 reporting requirements,"\textsuperscript{136} extending its opinion that Congress should amend or repeal the amendments before asking the IRS to implement it.

X. CONGRESSIONAL ATTEMPTS TO AMEND § 6041 THUS FAR

In September 2010, while the IRS was taking public comment on the amendments to § 6041, the Democrats and the Republicans each made an attempt to repeal or amend the new law. The Republicans attempted to repeal the amendments entirely using a proposal sponsored by Senator Mike Johanns of Nebraska.\textsuperscript{137} The measure was opposed by Democrats because it would have made up for the repeal by exempting more people from the new health insurance mandate.\textsuperscript{138} In other words, the Republicans suggested leaving the tax code and 1099 reporting requirements as they were before PPACA and the Small Business Jobs Act of 2010, but suggested cutting costs by exempting more people from the mandate requiring individuals to obtain healthcare (so the federal government would not have to pay for health care for as many individuals) and eliminating the Prevention Trust Fund, a $15 billion fund in PPACA that provides access to preventive services, including cancer screenings and smoking cessation

\textsuperscript{134} See Press Release, U.S. Senate Comm. on Small Bus. & Entren., Snowe Blasts SBA Office of Advocacy’s Failure to Submit Comments on Burdensome 1099 Mandate (Oct. 6, 2010), available at http://sbc.senate.gov/public/index.cfm?p=PressReleases&ContentRecord_id=7270554e-db79-4d42-af8d-2f60143c5d0c&ContentType_id=4bf6d10b-f7c6-4d07-9c74-7aab32dd938&Group_id=0a5867cf-c34c-421f-969b-ea2a5b192a22&MonthDisplay=10&YearDisplay=2010.


\textsuperscript{136} Id.


programs, especially for those who have lost their health insurance. Democrats were understandably opposed to shedding healthcare benefits in order to make the bill cheap enough to abandon the 1099 reporting requirements, and the Johanns amendment was defeated. The Democrats' own amendment, sponsored by Senator Bill Nelson of Florida, would have kept the 1099 reporting requirements largely intact, and raised the reporting threshold from $600 to $5000 and exempted businesses with twenty-five or fewer employees from the new requirement. The Nelson amendment did not touch the healthcare benefits contained in the bill. The Nelson Amendment was defeated because it did not do much in the way of actually eliminating the reporting burden on small businesses. The accounting problems for small businesses would still exist because small businesses would still have to track all expenses because the small business would not know which payments to suppliers would equal or exceed $5000. Additionally, the twenty-five employee ceiling would have placed a false cap on small business size; hiring a twenty-sixth employee would be incredibly expensive because that hire would cue the 1099 reporting requirement. Both amendments failed in September, leaving the IRS to conclude its public comment period on the legislation without a change from Congress.

It is important to note that while Congress was in a state of disagreement on how changes to the amendments to § 6041 should appear, the Obama Administration supported at least some measure of change. The Obama Administration, including Treasury Secretary Tim Geithner and Health and Human Services Secretary Kathleen Sebelius, felt that the reporting requirements in the new § 6041 were well-intentioned toward reducing the tax gap, but concluded that the burden on taxpayers outweighs the potential tax gap reducing benefits. The Administration supported the Nelson amendment and opposed the Johanns amendment, but their support for one amendment and opposition for the other was not based on how each law addressed the tax problem, but how each law intended to make up for the revenue that would be lost if the amendments to § 6041 were amended or repealed. In other words, the White House conceded that the current

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140 Id.
142 WebCPA Staff, supra note 139.
143 Id.
144 Haberkorn, supra note 4.
145 See id.
amendments pose a problem for small businesses, a problem that Congress must address without draining any benefits from the PPACA.146

As of January 21, 2011, it appeared that Congress and the White House were united in repealing the 1099 provisions in full.147 This admission comes on the tail of the House Republicans' primarily symbolic attempt to repeal the PPACA in its entirety.148 While the full repeal was successful in the House, Senate Democrats vowed not to act on the repeal, which effectively killed it.149 At this time, House Republicans plan to take a "repeal and replace" strategy: original PPACA provisions would be repealed and then subsequently replaced by a newly-drafted provision.150 Four House committees are currently drafting the "replacement" legislation, with more attention towards the more politically-charged provisions, such as the health care mandate and protections for people with pre-existing conditions.151 It is unclear whether these committees are drafting "replacement" legislation in the case of § 6041. If § 6041 is repealed, it is not certain that there will be anything to replace it, at least not for the time being.

XI. WHAT WILL CONGRESS DO IF § 6041 IS REPEALED?

Section 6041 is going to prove difficult to repeal, despite nearly universal support for such a move.152 The reason for the difficulty is quite simple: the removal of a revenue-building provision as large as § 6041 requires either the addition of a replacement revenue provision, or the removal of a benefit provision.153 The competing Nelson/Johanns amendments made that much too clear. Republicans support the cutting the cost of amended § 6041 and cutting the benefits for which it pays. Removing a revenue provision and a benefit provision results in a smaller bill. Democrats support replacing the lost revenue (finding the revenue somewhere besides small businesses) since it keeps the benefits of the bill intact while reducing the tax burden on small businesses. Both efforts suffer from a crucial shortcoming: the tax gap, and the large chunk of it for which the small business community is responsible, remains unaddressed.

146 See id.
149 Id.
150 Id.
151 Id.
152 Haberkorn, supra note 4.
153 See The Impact of the New 1099 Reporting Provision, supra note 108. The provision is expected to increase tax revenue by $17 billion to help off-set the cost of the health care bill. Id.
A repeal of § 6041 would end the current 1099 reporting requirement issue, but would do nothing to address the tax gap and small business’ share of it. It is clear that the two issues are separate. Section 6041 was intended to fund the health care bill, not to close the tax gap. The tax gap presents an issue regardless of what happens to the PPACA generally. Even before PPACA was drafted, the small business tax gap was an issue for the IRS, and it will no doubt remain an issue regardless of what happens to PPACA. The question is: what will Congress and the IRS do to close the gap without § 6041?

It appears that the IRS’s first efforts will not involve increased reporting requirements. The Treasury Inspector General for Tax Administration released a report at the end of 2010, recommending a new effort to increase voluntary compliance among small business/self-employed filers by enhancing the customer service capabilities of the IRS. Here again we see a renewed attitude of “service” as opposed to “enforcement” at the IRS. Although the report does not weigh in on the reporting issue (and whether or not increased reporting requirements are needed in some form or another), the report does make a broad admission on behalf of the Treasury Department: the government needs to know more about small business taxpayers before it can recommend improvements to current customer service efforts of the IRS. This makes sense because it is difficult to serve customers about whom too little is known. The report recommends researching small business taxpayers in the same way it researches individual taxpayers, mainly using the survey method and following up with small business filers after they have taken advantage of one or more of the IRS’s programs. The tone of the report, generally speaking, is very amicable towards small business non-filers. The report takes the position that small business taxpayers would voluntarily comply at a greater rate if the process were easier, and if the IRS adopted an approach to tax collection with a greater focus on customer service. This friendly approach is completely at odds with the get-tough attitude of the embattled § 6041. This leaves a question for small business advocates regarding the

155 See TREASURY INSPECTOR GEN. FOR TAX ADMIN., U.S. DEP’T OF THE TREASURY, 2011-40-010, MULTIPLE CHANNELS ARE USED TO PROVIDE INFORMATION TO SMALL BUSINESS TAXPAYERS, BUT MORE INFORMATION IS NEEDED TO UNDERSTAND THEIR NEEDS (2010).
156 See id. at 3.
157 See id. at 11, 27.
158 See id. at 3.
159 See id. at 2.
long-term treatment the IRS will adopt on this issue once the political firestorm regarding § 6041 dies down.

Is it realistic to believe that the IRS will be able to close the $109 billion small business tax gap without getting tough on small businesses? Is it politically feasible for the IRS and Congress to get tough even if they wanted to? At this point, the answers to these questions may rely on little more than speculation, but speculation does not help the small business owner plan for the future. Fortunately, there are steps the small business owner can take now to prepare for the uncertain tax environment of the next few years.

XII. PRACTICAL ADVICE FOR SMALL BUSINESSES

First, proprietors should acquire a TIN from the IRS that is something other than their own Social Security Number, such as an Individual Tax Identification Number or an Employer Identification Number. This will allow the proprietor to more widely disseminate their TIN without fear of personal identity theft. This first step will make it easier for the proprietor to begin taking the next steps to preparing for 1099 reporting under the new requirements.

Second, proprietors should place their TINs on every invoice the proprietor creates. In doing so, proprietors will ensure that all buyers will have the proprietor’s TIN number. This will accomplish two things. First, it will ensure that all customers have the same TIN for the proprietor and will ensure that the TIN is accurate. If a proprietor’s customers file a 1099 that includes an incorrect or missing TIN number for the proprietor, the proprietor will be assessed the backup withholding penalty and ultimately charged more taxes for those transactions. Second, providing the proprietor’s TIN on all invoices will reduce or eliminate the number of customers contacting the proprietor at tax time requesting the TIN. This author recommends placing the proprietor’s TIN number on every invoice, regardless of whether the proprietor believes the customer will (or will not) accumulate $600 in purchases for the year. Doing so will alleviate the

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163 See U.S. Gov’t Accountability Office, supra note 32.
164 See IRS Instructions for Form 1099-MISC (2011), supra note 38. (the filing party (payor) must list a twenty-eight percent withholding on payments made to a seller that failed to provide the payor with a TIN).
uncertainty that exists when it is possible, but not certain, that a customer will eventually spend $600 or more with the proprietor in a given tax year.

Third, proprietors should collect the TIN information from every supplier when the proprietor makes a purchase. Furthermore, proprietors should instruct all employees to collect TIN information when they engage in a transaction on behalf of the company. If employees are permitted to file expense reports for personal expenses incurred while conducting business, those expense reports should include a conspicuous section where each supplier’s TIN should be recorded. The importance of collecting all available TIN data cannot be overstated. Missing or incorrect TIN data is one of the most critical oversights when preparing 1099s, resulting in unnecessary IRS action and taxpayer burden on both sides of the sales transaction. Additionally, the proprietor will have to collect all missing TIN numbers at tax time, which is one of the burdens opponents to the law most frequently invoke.

Fourth, the proprietor should organize all transactions by TIN number. Organizing both purchases and sales by TIN in a spreadsheet or database will make it much easier at tax time to ascertain whether a 1099 needs to be filed for a particular supplier, or whether the proprietor should expect a customer to file a 1099 on behalf of the proprietor.

Fifth, the proprietor should create a preferred supplier list and distribute the list to all employees. Such a list should establish a single supplier for all same-type transactions. For example, the proprietor should select a single supplier for all office equipment, a single supplier for vehicle fuel, and a single supplier for lodging or air travel. Employees should be instructed to conduct business on behalf of the company strictly with these suppliers whenever possible. This will reduce the overall number of suppliers for which the proprietor will have to file 1099s.

Sixth, the proprietor should file its 1099s online through the IRS. The IRS encourages taxpayers of all sizes to file online and makes it relatively easy to do. Filing manually using paper-based 1099s is difficult because the IRS requires the use of a special red ink pen and special composite forms that cannot merely be printed from the Internet.

Finally, the IRS has recommended reaching out to underserved taxpayers through social media websites, such as Facebook, YouTube and Twitter. Small business owners should turn first to the web for

165 See id.
166 See, e.g., NAT’L TAXPAYER ADVOCATE, supra note 83, at 11.
168 See id. at 17.
169 NAT’L TAXPAYER ADVOCATE, supra note 83, at 59.
instructional videos on filing procedures, filing requirements, the audit and appeals process and more. \(^{170}\) These tools will prove particularly useful for those speaking English as a second language, since the IRS anticipates releasing all of its educational content in a multilingual format. \(^{171}\)

These practical considerations will make the proprietor more efficient in filing its taxes, and will make it less likely that mistakes will occur. Taxpayers can use these considerations to reduce the burden of paying taxes, even while the 1099 reporting requirements become more burdensome and the penalties become more onerous.

**XIII. CONCLUSION**

The government is mounting a valid assault on the tax gap, and small businesses, right or wrong, are caught in the middle of it. The government provides conclusive evidence that the small business/small operator community is responsible for a large majority of the tax gap, $109 billion of the $345 billion estimated total simply by underreporting their liabilities. \(^{172}\) On the flip side, the government concedes that, by and large, most small businesses owners pay the taxes they owe. \(^{173}\) Small business advocates argue that it is unfair to lump the costs of compliance onto honest small business owners in order to catch the small percentage of taxpayers who do not fully disclose their tax liabilities. Moreover, even with the increased disclosure, greater enforcement is unlikely to entirely eliminate the tax gap, as the IRS concedes, \(^{174}\) and notwithstanding the additional costs levied on small businesses, the government’s own costs of enforcing the Code will increase as well. \(^{175}\) This note examined these costs and considerations, and the practical considerations the IRS is currently considering as it attempts to implement the amendments to § 6041. This note made clear that the IRS has the means and the need to reform itself and its information systems. Perhaps such an effort should take place before any replacement to the old § 6041 is put into effect.

Regardless of the regulations and recommendations the IRS ultimately issues, and regardless of whether the law is ultimately repealed or amended before the IRS has a chance to rule on it, small business owners, their counsel and their accounting staff should properly implement the recommendations suggested by small business leaders, the IRS and this author as described in this note.

\(^{170}\) Id. at 60.

\(^{171}\) Id. at 60–61.

\(^{172}\) OFFICE OF TAX POLICY, supra note 5, at 3.


\(^{174}\) See id.

\(^{175}\) See NAT’L TAXPAYER ADVOCATE, supra note 83, at 9.