



# **1099 Information Reporting Requirements and Penalties as Modified by the Patient Protection and Affordable Care Act and the Small Business Jobs Act of 2010**

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## Summary

Generally, taxpayers are more likely to report items of income on their tax returns if they know that a third party has reported it to the Internal Revenue Service (IRS); therefore, expanding information reporting requirements under the Internal Revenue Code (IRC) can improve the collection of federal tax revenue. However, as those requirements are expanded, those who must comply with the requirements generally will face an increased administrative burden. Recent expansions of the reporting requirements in IRC § 6041 have been met by protests that the changes impose too great a burden, particularly on small businesses.

The Patient Protection and Affordable Care Act (P.L. 111-148; PPACA) and the Small Business Jobs Act of 2010 (P.L. 111-240) both amended IRC § 6041, which requires payments totaling at least \$600 in a single calendar year to a single recipient to be reported to the IRS. The required returns are generally Form 1099s, which are prepared by the entity making the payment and show to whom payment was made, the amount of the payment, and the general reason for the payment. The form is filed with the Internal Revenue Service (IRS) and a copy is provided to the payee. The form is required only when the payer is considered to be engaged in a trade or business and has made the payment in connection with that trade or business.

Beginning with payments made in 2011, § 2101 of the Small Business Jobs Act makes most landlords subject to the reporting requirements of IRC § 6041 by stipulating that, for purposes of IRC § 6041(a), they are considered to be engaged in the trade or business of renting real property, with certain exceptions. Landlords generally have not been considered to be engaged in a trade or business and, therefore, have not been subject to IRC § 6041. The Small Business Jobs Act also increased the penalties for failure to file an information return (IRC § 6721) and the penalties for failing to provide a copy of the information return to the payee (IRC § 6722). These changes will apply to any information returns required to be filed after December 31, 2010.

Beginning with payments made in 2012, § 9006 of PPACA changes the reporting requirements in two ways. Payments to corporations will no longer be exempt from reporting. Additionally, § 9006 expands the types of payments that will trigger the reporting requirement. Until 2012, the type of payment that most commonly triggers the reporting requirement is payment for services. Beginning in 2012, IRC § 6041 will also require reporting of payments for goods or other property as well as gross proceeds.

Various groups have asserted that the reporting requirements will be too burdensome on both the payer and the payees. For payments made by credit card, the reporting burden may be eased somewhat by a recent change in the law that will require payment settlement entities to report credit card payments and payments through third party networks (e.g., PayPal). Under a new Treasury regulation, if reporting is required under that law, no reporting of the payment will be required under IRC § 6041 if payments are made after December 31, 2010.

In the 111<sup>th</sup> Congress, several attempts were made to either repeal or modify § 9006 of PPACA. A number of bills have been introduced in the 112<sup>th</sup> Congress to repeal that section (e.g. H.R. 4, H.R. 60, H.R. 144, H.R. 417, H.R. 584, H.R. 705, S. 12, S. 18, and S. 72). Some of these would also repeal the changes made by § 2101 of the Small Business Jobs Act. During consideration of S. 223, the Senate agreed to an amendment that would repeal § 9006. Recently, the House Committee on Ways and Means marked up and reported H.R. 4 and H.R. 705.

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As a general rule, taxpayers are more likely to pay taxes on income if the realization of that income has been communicated to the Internal Revenue Service (IRS). To encourage compliance with tax laws, the Internal Revenue Code (IRC) includes a number of information reporting requirements regarding payments that may result in taxable income for the payee. One such reporting requirement, contained in IRC § 6041(a), applies to certain payments made by persons in the course of a trade or business. Under IRC § 6041(a), if the total amount of payments made to a payee over a year equals at least \$600, the payer is required to file an information return with the IRS providing information identifying the payer, the payee, and the total amounts paid to that payee over the past calendar year. The information returns required to be filed under IRC § 6041 are typically versions of Form 1099.<sup>1</sup> A copy of this information return must also be provided to the payee. Although payees may receive copies of information returns, payees are not required to file any information returns under IRC § 6041.<sup>2</sup>

Section 6041 was amended twice in 2010: once by § 9006 of the Patient Protection and Affordable Care Act (PPACA)<sup>3</sup> and later by § 2101 of the Small Business Jobs Act of 2010.<sup>4</sup> Each of the amendments potentially increases the number of 1099s that will be filed in the coming years. The Small Business Jobs Act also revised the penalties that apply when a payer fails to file an accurate 1099 with the IRS or fails to provide an accurate copy of that report to the payee.

Since the passage of PPACA, numerous bills have been introduced to repeal or modify § 9006. Some of these would also repeal § 2101 of the Small Business Jobs Act.

This report discusses the amendments, objections to the amendments, and proposed legislation that may affect IRC § 6041. It also discusses procedures for and enforcement of the information reporting requirements. In both text and tables, this report outlines the penalties for failure to comply with the requirements of IRC § 6041, including changes to the penalties that were enacted by the Small Business Jobs Act. **Table A-1** is included in **Appendix A** as a reference for the enacted changes in the requirements for filing information returns. The table includes the dates those changes are scheduled to become effective. **Appendix B** contains a list of 10 questions that are representative of questions being raised by constituents.

## Section 9006 of the Patient Protection and Affordable Care Act

For payments made after December 31, 2011, § 9006 of PPACA amended the reporting requirement in IRC § 6041 in two principal ways. First, payments to corporations will no longer be automatically exempt from reporting requirements by virtue of the payee's corporate status, despite existing regulations to the contrary.<sup>5</sup> Second, the types of payments that can trigger the

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<sup>1</sup> Treas. Reg. § 1.6041-1(a)(2). Payments for trust distributions are made on Form 1096 and employee compensation is typically reported on Forms W-2 and W-3. *Id.*

<sup>2</sup> Payees, like most individuals, are required to report all income, whether reflected on a 1099 or not, on an annual federal income tax return if they have sufficient income to meet or exceed the filing threshold. Internal Revenue Code (IRC) § 6012(a).

<sup>3</sup> P.L. 111-148.

<sup>4</sup> P.L. 111-240.

<sup>5</sup> I.R.C. § 6041(h), as added by P.L. 111-148 § 9006(a), the Patient Protection and Affordable Care Act (PPACA).

reporting requirement will be expanded to include amounts paid in consideration of property and other gross proceeds.<sup>6</sup> The effect of this amendment is to require those engaged in a trade or business to report a broader range of payments made to a broader range of payees.

The purpose of this amendment appears to be to reduce the “tax gap”<sup>7</sup> because the existence of an information return generally encourages the voluntary reporting of taxable income and may also facilitate the enforcement and collection of taxes on income that is not voluntarily reported.<sup>8</sup> Although this provision is intended to raise revenue without increasing taxes, Congress has received significant feedback from constituents who anticipate that the increased reporting will impose an administrative burden on all payers. In particular, some have commented that the impact on small businesses will be significant because their bookkeeping systems may need to be modified to accommodate tracking the aggregate amounts paid to each payee to comply with the new requirements regarding the types of payments and payees that will trigger 1099 reporting. They add that the administrative burden is also anticipated to increase due to the time and expense involved in filing each newly required 1099.<sup>9</sup>

The \$600 reporting threshold has not changed since at least 1954 and is not currently slated to be increased by law. In contrast, some dollar amounts specified in the IRC have been legislatively increased over time or indexed for inflation. For example, the personal and dependent exemption amounts were \$600 in 1954, but over time have risen to \$3,650 for tax year 2010.<sup>10</sup> As the buying power of \$600 decreases, the number of transactions captured may increase as it becomes more likely that minor expenditures will aggregate to at least \$600 and trigger the reporting requirement.

## Payments to Corporations

Historically, although IRC § 6041 did not explicitly exempt payments to corporations from its reporting requirements, such payments were considered exempt under regulations promulgated by the IRS, if payments were made to

[a] corporation [as defined in the IRC] except with respect to payments made to a corporation after December 31, 1997 for attorneys’ fees, and except a corporation engaged in providing medical and health care services or engaged in the billing and collecting of payments in respect to the providing of medical and health care services. However, no

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<sup>6</sup> PPACA § 9006(b).

<sup>7</sup> See CRS Report R40219, *Tax Gap, Tax Enforcement, and Tax Compliance Proposals in the 111<sup>th</sup> Congress*, by James M. Bickley.

<sup>8</sup> GAO-09-238, *IRS Could Do More to Promote Compliance by Third Parties with Miscellaneous Income Reporting Requirements* (January 2009). The Joint Committee on Tax has estimated that this provision would raise \$17.1 billion between 2012 and 2019. JOINT COMM. ON TAX, *Estimated Revenue Effects Of The Amendment In The Nature Of A Substitute To H.R. 4872, The “Reconciliation Act Of 2010,” As Amended, In Combination With The Revenue Effects Of H.R. 3590, The “Patient Protection And Affordable Care Act (‘PPACA’),” As Passed By The Senate, And Scheduled For Consideration By The House Committee On Rules On March 20, 2010* at 1 (March 20, 2010).

<sup>9</sup> The IRS has estimated the average time needed to complete a single Form 1099-MISC at 16 minutes, although the actual time “will vary depending on individual circumstances.” IRS, *2010 General Instructions for Certain Information Returns* at 15, available at <http://www.irs.gov>. In addition to possible increased costs for paper, envelopes, filing software, and toner or ink, payers may also incur postage expense in providing each payee with the required copy of the 1099.

<sup>10</sup> Rev. Proc. 2009-50.19 (see 26 U.S.C. § 1 note).

reporting is required where payment is made to a hospital or extended care facility described in section 501(c)(3) which is exempt from taxation under section 501(a) or to a hospital or extended care facility owned and operated by the United States, a State, the District of Columbia, a possession of the United States, or a political subdivision, agency or instrumentality of any of the foregoing.<sup>11</sup>

PPACA § 9006 adds a new subsection (h) to IRC § 6041. For payments made after December 31, 2011, the new subsection provides that “[n]otwithstanding any regulation prescribed by the Secretary before the date of the enactment of this subsection, for purposes of this section the term ‘person’ includes any corporation that is not an organization exempt from tax under section 501(a).”<sup>12</sup>

PPACA § 9006 supersedes the IRS regulations. Thus, payments made to corporations after December 31, 2011, will no longer be automatically exempt from information reporting requirements unless the corporation is a tax-exempt entity.

## Amounts in Consideration of Property and Other Gross Proceeds

IRC § 6041(a) specifies a list of payments that can trigger its information reporting requirements. For payments made before January 1, 2012, these include “rent, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable gains, profits, and income.”<sup>13</sup> If the aggregate amount of these payments to a single payee equals \$600 or more, then IRC § 6041(a) requires the payer to report the amount of those payments and the identity of the payee to the IRS.

For payments made after December 31, 2011, PPACA § 9006 amended this list of payments to add “amounts in consideration for property” and other “gross proceeds.”<sup>14</sup> Because of these additions, reporting will be required for some payments that previously were not subject to reporting. For example, payments for merchandise, telegrams, telephone, freight, and storage have been exempt under IRS regulations.<sup>15</sup> However, those payments may be considered amounts in consideration for property or gross proceeds under the amended IRC § 6041(a) and could potentially be subject to reporting when the amended language goes into effect. As part of its general request for comments on guidance to be provided regarding the new reporting requirements, the IRS has specifically requested comments on the scope and interpretation of the terms “gross proceeds” and “amounts in consideration for property” so that the reporting burden is minimized and duplicate reporting is avoided.<sup>16</sup>

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<sup>11</sup> Treas. Reg. § 1.6041-3(p)(1).

<sup>12</sup> I.R.C. § 6041(h).

<sup>13</sup> I.R.C. § 6041(a).

<sup>14</sup> P.L. 111-148, § 9006(b). As amended, the language would read: “rent, salaries, wages, *amounts in consideration for property*, premiums, annuities, compensations, remunerations, emoluments, or other *gross proceeds*, fixed or determinable gains, profits, and income.” (emphasis added).

<sup>15</sup> Treas. Reg. § 1.6041-3(c).

<sup>16</sup> Notice 2010-51. Definitions of the terms were not included in PPACA § 9006. Additionally, property is not defined in the IRC. In a 1993 Field Service Advisory (FSA 1177), the IRS addressed the meaning of property for purposes of IRC § 351. It noted that in the absence of “specific Congressional indication to the contrary, statutory terms are generally given their ordinary meaning. ‘Property’ has been defined as ‘something owned or possessed.’ Merriam-Webster’s Collegiate Dictionary, (10<sup>th</sup> Ed. 1999). Case law has broadly defined ‘property’ to generally include assets; FSA 1177 (citing *E.I. DuPont de Nemours & Co. v. United States*, 471 F.2d 1211, 1218 (Ct. Cl. 1973)); or “whatever (continued...)”

## Section 2101 of the Small Business Jobs Act of 2010

Amidst proposals to repeal the expansion of the § 6041 reporting requirements enacted by the PPACA, § 6041 was amended again. Section 2101 Small Business Jobs Act expanded the payers who would be required to comply with the section's reporting requirements to include landlords.

Generally, those receiving rental income from real estate have not been considered to be engaged in a trade or business; however, the recent amendment of § 6041 will, barring further amendment or repeal, change this. Effective for payments made after December 31, 2010, and *solely* for purposes of § 6041(a), most landlords are to be considered to be engaged in the trade or business of renting real estate and, therefore, may be required to file Forms 1099 to report payments made in conjunction with their rental properties.

The amendment added a new subsection (h) to § 6041. The subsection includes three exceptions to its general rule that those receiving rental income from real estate will be considered engaged in the trade or business of renting real estate for purposes of § 6041(a).

The first exception is for those who receive substantially all of their rental income from renting their principal residence on a temporary basis would not be considered to be engaged in a trade or business. However, it appears that if an individual were receiving rent from both a principal residence and other properties, the individual would be subject to § 6041's reporting requirements for the expenses of all properties, including the rented principal residence unless the rental income from the other properties was very small.

A second exception provided in § 6041(h) is for an individual receiving "rental income of not more than the minimal amount, as determined under regulations prescribed by the Secretary."<sup>17</sup> Similarly, the third exception is somewhat undefined. It exempts individuals from being considered engaged in the trade or business of renting property if "the requirements of this section would cause hardship, as determined under regulations prescribed by the Secretary."<sup>18</sup>

## Exception for Credit Card and Third Party Network Payments

The changes made by PPACA and the Small Business Jobs Act may be affected by recently promulgated regulations<sup>19</sup> implementing IRC provisions that require reporting of credit card and third party network transactions.<sup>20</sup> For payments made after December 31, 2010, there is a regulatory exception to the IRC § 6041 requirements to file an information return with the IRS and provide a copy to the payee. Treasury Regulation § 1.6041-1(a)(1)(iv) states that any transaction that is subject to reporting under § 6050W, without regard to the third party network

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(...continued)

may be transferred"; FSA 1177 (quoting *H.B. Zachary Co. v. Commissioner*, 49 T.C. 73, 80 n.6 (1967)).

<sup>17</sup> *Id.*

<sup>18</sup> *Id.*

<sup>19</sup> Treas. Reg. § 1.6041-1(a)(1)(iv), (v), 75 *Federal Register* 49827, August 16, 2010.

<sup>20</sup> I.R.C. § 6050W (added by P.L. 110-289).

de minimus threshold, will not be reported under § 6041. Thus, if payments are made by credit card or through a third party network,<sup>21</sup> the payer generally will not be required to report them on an information return.

## Procedures

The deadline for filing an information return with the IRS is February 28 of the year following the calendar year in which payments were made, or March 31 if filed electronically. Copies of information returns must be provided to payees no later than January 31 of the year following the calendar year in which the payments were made.

Information returns must accurately identify both the payer and the payee of the payments as well as the total amount paid. The payees are required to provide their names, addresses, and taxpayer identification numbers<sup>22</sup> to payers in order to facilitate information reporting. The information return must include all of these as well as the address and telephone number of the payer. It is the payer's obligation to request information from the payee, and the payee is required to provide it.<sup>23</sup> The payer may use Form W-9 to request the information from U.S. persons. If the payee does not provide a taxpayer identification number, the payer is generally required to collect backup withholding from payments due to the payee. For 2010-2012, the backup withholding rate is 28%.<sup>24</sup> A payee is subject to a penalty of \$50 for each failure to provide the correct taxpayer identification number to a payer who has requested it.

## Enforcement

Both the failure to submit an accurate information return to the IRS and the failure to provide a copy of the information return to the payee are subject to monetary penalties assessed by the IRS. As a unique information return is required with respect to each payee, penalties are assessed on each deficient information return. Both § 6721 (pertaining to failure to file accurate returns with the IRS) and § 6722 (pertaining to failure to provide payees with correct copies of the information returns) of the IRC have been amended by the Small Business Jobs Act to revise the amounts of the penalties. Section 6722 has been amended to change the structure of the penalty so that it is similar to the structure of the § 6721 penalty. In so doing, the effect is that the amended penalty may be lower than it previously would have been where corrective action is taken. The changes to both sections are scheduled to become effective for returns required to be filed after December 31, 2010. Thus, the new penalty amounts are expected to apply to returns that report payments made during calendar year 2010.

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<sup>21</sup> See Treas. Reg. § 1.6050W-1((b)(3), (c)(3). One example of a third party network is PayPal.

<sup>22</sup> For individuals, the taxpayer identification number (TIN) is generally their social security number.

<sup>23</sup> Section 6041(c) of the IRC requires the recipient to provide both name and address upon demand by the person paying the income. IRC § 6109(a)(1) requires the payer to report the TIN of the recipient. IRC § 6109(a)(2) requires the recipient to provide the TIN to the payer.

<sup>24</sup> The backup withholding rate is currently defined in IRC § 3406 as being the fourth lowest tax rate under IRC § 1(c), making it 28% for 2010. This definition was enacted in § 101(c)(10) of P.L. 107-16, the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA). The provisions of EGTRRA, due to expire December 31, 2010, were extended by P.L. 111-312 through December 31, 2012. If allowed to expire at that time, on January 1, 2013, the backup withholding rate will revert to 31%—its pre-EGTRRA rate.



## Civil Penalties for Information Returns Due Before January 1, 2011

For information returns that are due before the amendments take effect, the penalty for failing to file a correct and timely return with the IRS is \$50 for each defective return not to exceed \$250,000 for a single payer.<sup>25</sup> If the deficiency is corrected within 30 days of the due date, the penalty is reduced to \$15 per return, not to exceed \$75,000. If corrected later than 30 days, but before August 1, the penalty is \$30 per return, not to exceed \$150,000.<sup>26</sup> No penalty will be assessed against a person if defects are corrected by August 1, and the total number of defective returns does not exceed the greater of 10 or one-half percent of the total number of information returns required to be filed by the person.

Some small businesses may be able to take advantage of reduced ceilings on aggregate penalties for payers with gross receipts of less than \$5 million. For these payers, the ceilings are \$100,000 (for uncorrected violations), \$25,000 (if corrected within 30 days), and \$50,000 (if corrected after 30 days, but on or before August 1). Higher penalties may also be assessed where persons intentionally disregard their duty to file an information return. (See **Table 1**.)

Failure to provide a correct and timely statement to a payee is also subject to a \$50 penalty per return, not to exceed \$100,000 per payer. Higher penalties may also be assessed where persons intentionally disregard their duty to provide a payee with a copy of an information return. (See **Table 2**.)

## Civil Penalties for Information Returns Due After December 31, 2010

Section 2102 of the Small Business Jobs Act modified the penalties for failing to provide information returns to the IRS or to the appropriate payee in a timely fashion. The penalties for failing to file information returns with the IRS were increased across the board, as described in **Table 1**. These amounts will also be updated in 2017, and every five years after, to account for inflation.

**Table 1. Penalties for Failure to File Information Return with IRS**

IRC § 6721

	Returns Due Before 2011	Returns Due After Dec. 31, 2010
Base penalty	Lesser of \$50/return or \$250,000 (\$100,000 for small businesses)	Lesser of \$100/return or \$1,500,000 (\$500,000 for small businesses)
Corrected within 30 days	Lesser of \$15/return or \$75,000 (\$25,000 for small businesses)	Lesser of \$30/return or \$250,000 (\$75,000 for small businesses)
Corrected by August 1	Lesser of \$30/return or \$150,000 (\$50,000 for small businesses)	Lesser of \$60/return or \$500,000 (\$200,000 for small businesses)
Due to intentional disregard	\$100/return without limit	\$250/return without limit

**Source:** Compiled by CRS

<sup>25</sup> I.R.C. § 6721(a)(1).

<sup>26</sup> I.R.C. § 6721(b).

**Notes:** As used in this chart, small businesses are those with gross receipts of not more than \$500,000 in the calendar year for which an information return is required. I.R.C. § 6721(d).

Section 2102 of the Small Business Jobs Act also modified the penalty scheme for failures to provide copies of information returns to payees. As described in **Table 2**, the amended penalties mirror the amounts that would be assessed for a failure to file information returns with the IRS and are similarly indexed for inflation. In addition to raising the base penalty, the amendments also provide reduced penalties if corrective actions are taken. Because the prior penalty scheme did not take corrective action into account, penalties under the amended provision may actually be less than what would have been assessed under the old scheme if corrective action is taken.

**Table 2. Penalties for Failure to Provide Information Return to Payee**  
IRC § 6722

	Returns Due Before 2011	Returns Due After Dec. 31, 2010
Base penalty	Lesser of \$50/return or \$100,000	Lesser of \$100/return or \$1,500,000 (\$500,000 for small businesses)
Corrected within 30 days	Same as base penalty	Lesser of \$30/return or \$250,000 (\$75,000 for small businesses)
Corrected by August 1	Same as base penalty	Lesser of \$60/return or \$500,000 (\$200,000 for small businesses)
Due to intentional disregard	\$100/return	\$250/return

**Source:** Compiled by CRS

**Notes:** As used in this chart, small businesses are those with gross receipts of not more than \$500,000 in the calendar year for which an information return is required. I.R.C. § 6722(d).

## Criminal Penalties in Cases of Willful Violations

It is a misdemeanor for any person to willfully fail to make an information return as required by law.<sup>27</sup> Persons convicted of this offense may be punished by a fine of up to \$25,000, imprisonment for up to one year, or both. A willful violation occurs when there is “a voluntary, intentional violation of a known legal duty.”<sup>28</sup> However, a violation that results from a good-faith misunderstanding of the requirements of the IRC is not a willful violation, as that term has been interpreted by the courts.<sup>29</sup> Neither the Small Business Jobs Act nor PPACA changed the criminal penalties applicable to the willful failure to make an information return.

<sup>27</sup> I.R.C. § 7203.

<sup>28</sup> *Cheek v. U.S.*, 498 U.S. 192, 200 (1991).

<sup>29</sup> *Id.* at 202.

## Responses to Changes to 1099 Information Reporting Requirements

Those in favor of the expanded 1099 reporting requirements argue that they are a means through which tax revenue can be generated without raising taxes.<sup>30</sup> At the same time, opponents to the measure have expressed concern about the potential financial and administrative burdens that businesses may experience. The following sections describe points that have been raised by various stakeholders in the debates surrounding these issues.

### Internal Revenue Notice 2010-51—Request for Comments

On July 1, 2010, the IRS announced its request for comments<sup>31</sup> on the expanded § 6041 reporting requirements that are to be effective for payments made after December 31, 2011. Within less than a week, reportedly “scores of taxpayers and certified public accountants”<sup>32</sup> had responded, calling for the repeal of the changes enacted by PPACA § 9006. Some expressed concern that they would need additional personnel to handle the recordkeeping needed to comply with the new requirements. Others referred to additional costs required to obtain and compile the required information—at least one indicated that businesses should not be required to undertake such reporting for free and proposed a refundable income tax credit that would be based on a per return processing fee.

Some, however, offered suggestions rather than simply expressing disapproval of the changes. These included suggestions as to what should be excluded from “gross proceeds” for reporting purposes and a staggered reporting process that would allow payers and payees to reconcile the reported payments before they were reported to the IRS.

A number recognized the intent to reduce the tax gap and encourage or enforce the reporting of income received. While several suggested increasing the reporting threshold from \$600, one suggested lowering it to \$100 to account for more otherwise unreported income.

### The National Taxpayer Advocate

The National Taxpayer Advocate’s office is an independent office within the Internal Revenue Service whose mission is to help resolve taxpayers’ problems with the IRS and recommend changes to eliminate problems. Each year, it must prepare an annual report identifying its objectives for the coming fiscal year. The June 30, 2010, Fiscal Year 2011 Objectives Report (Objectives Report) included examination of the administrative challenges presented by the expanded information reporting requirements. The report expressed concern “that the new

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<sup>30</sup> The Joint Committee on Tax has estimated that this provision would raise \$17.1 billion between 2012 and 2019. JOINT COMM. ON TAX, *Estimated Revenue Effects Of The Amendment In The Nature Of A Substitute To H.R. 4872, The “Reconciliation Act Of 2010,” As Amended, In Combination With The Revenue Effects Of H.R. 3590, The “Patient Protection And Affordable Care Act (‘PPACA’),” As Passed By The Senate, And Scheduled For Consideration By The House Committee On Rules On March 20, 2010 at 1* (March 20, 2010).

<sup>31</sup> IR-2010-79 (announcing Notice 2010-51).

<sup>32</sup> BNA Daily Tax Report, 128 DTR G-2 (July 7, 2010).

reporting burden, particularly as it falls on small businesses, may turn out to be disproportionate as compared with any resulting improvement in tax compliance.”<sup>33</sup>

Since 2004, the National Taxpayer Advocate has recommended including corporate service providers in the 1099 reporting requirements as a means of addressing the tax gap and the cash economy, but has not recommended extending the requirements to include vendors. Among the concerns expressed in the Objectives Report are issues involving collection of tax identification numbers (TINs). Sole proprietors who have no employees generally use their Social Security numbers as their TINs, opening the opportunity for identity theft. An additional concern involving TINs is the backup withholding requirement if a TIN is not provided. This presents issues involving administrative expenses on the part of the taxpayer who must collect the withholding and remit it to the IRS. Further, vendors who have refused to provide a TIN may then refuse to sell their products to anyone who does not pay the entire price (i.e., withholds the required 28% from the payment due).

Other concerns expressed in the Objectives Report involve the volume of information that will be received by the IRS. The report anticipates challenges in making productive use of the information reporting involving payments to vendors because amounts reported on the information returns may not match amounts reported on tax returns: vendors are required to report all income received, but payers are only required to report payments aggregating \$600 or more. Additionally, for goods, there is often a high rate of returned items. These returns and their refunds may not be adequately reflected in the payer’s records of payments made to the vendor.<sup>34</sup>

A final concern expressed in the Objectives Report is that the expanded reporting requirements could distort taxpayer behavior. If payers are able to get year end computer generated summaries of their purchases from vendors, they may be more likely to make their purchases at those vendors. Those vendors who do not have the ability to track customer purchases may lose customers, reducing local competition and favoring large, national vendors.

## **Trade Associations and Others**

The American Numismatic Association and the Numismatics United for Political Action called on coin collectors and dealers to contact their Members of Congress to repeal § 9006 of PPACA. They cited the burden the additional paperwork would impose on dealers as well as the potential for identity theft of those collectors who sell coins or collections.

The National Association of Realtors issued a “Call for Action” regarding proposals to treat those receiving income from renting real property as “engaged in a trade or business” for purposes of § 6041. The additional burden that the reporting requirements would impose on landlords, many with only one property, was cited as cause for opposition.

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<sup>33</sup> National Taxpayer Advocate, “Report to Congress: Fiscal Year 2010 Objectives,” 9 (June 30, 2010).

<sup>34</sup> Although not mentioned in the Objectives Report, another reason income tax returns may not match the payments reported on 1099s is because the 1099s are based on calendar year payments, but many companies report their income on a fiscal year basis. Discrepancies are also likely when the vendor is an accrual basis taxpayer and reports income when it is earned rather than when it is received.

On August 17, 2010, the U.S. Chamber of Commerce announced that “more than 1,099 local chambers of commerce, associations, and businesses of all sizes”<sup>35</sup> were sending a letter to Congress to call for the repeal of PPACA § 9006. The letter asserted that the new requirements would “impose substantial paperwork and reporting burdens on the backs of governments, nonprofits, and businesses—especially small businesses.”<sup>36</sup> The letter also stated that the reporting requirements would alter the behavior in the marketplace, potentially harming smaller merchants.

On January 25, 2011, the president of the National Association of Enrolled Agents (NAEA) sent a letter to the House Committee on Ways and Means encouraging passage of H.R. 4 to repeal § 9006 of PPACA, saying that the section “places an unprecedented burden on small businesses.”<sup>37</sup> The letter also addressed expressed concern about implementation of § 2101 of the Small Business Jobs Act of 2010, foreseeing non-willful compliance problems and suggesting either legislative or regulatory action to provide a transition period.

Other responses regarding the landlord provision in § 2101 have mentioned the possibility of identity theft. Some have expressed concern that contractors were going to be required to provide their personal information to the landlords and were concerned that individual landlords might not be trustworthy. Others are concerned that landlords must provide personal information on the 1099 that is issued to the payee. This information includes the address, taxpayer identification number, and phone number of the landlord. Those who have only one or two rental properties may not have a business address, business phone, or employer identification number. In those cases, the individuals would need to provide contractors with their home address, home (or cell) phone number, and their Social Security number.

## Legislative Proposals in Congress

### The 112<sup>th</sup> Congress

On February 17, 2011, the House Committee on Ways and Means marked up and reported two of the myriad bills that have been introduced to § 9006 of PPACA.<sup>38</sup> H.R. 4<sup>39</sup> and H.R. 705<sup>40</sup> would each repeal the changes § 9006 made to IRC § 6041. H.R. 705 would also repeal the changes made by § 2101 of the Small Business Jobs Act.<sup>41</sup> Unlike H.R. 4, which has no “pay for”

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<sup>35</sup> “U.S. Chamber Leads Effort to Repeal Burdensome Reporting Requirement Impacting Small Businesses,” press release, available at <http://www.uschamber.com/press/releases/2010/august/us-chamber-leads-effort-repeal-burdensome-reporting-requirement-impacting>.

<sup>36</sup> Letter “To the Members of the United States Congress,” September 2010, available at <http://www.uschamber.com/issues/letters/2010/national-sign-letter-repeal-1099-provision-health-care-law>.

<sup>37</sup> Letter from Gina Jones, EA, President, National Association of Enrolled Agents, to Representative Dave Camp, Chairman, Committee on Ways and Means, and Representative Sander Levin, Ranking Member Committee on Ways and Means (Jan. 25, 2011). Available at [http://www.naea.org/MemberPortal/Advocacy/Comments/Camp\\_Levin\\_Letter\\_01252011.htm](http://www.naea.org/MemberPortal/Advocacy/Comments/Camp_Levin_Letter_01252011.htm).

<sup>38</sup> *E.g.*, H.R. 4, H.R. 60, H.R. 144, H.R. 417, H.R. 584, H.R. 705, S. 12, S. 18, and S. 72.

<sup>39</sup> H.R. 4, § 2.

<sup>40</sup> H.R. 705, § 2.

<sup>41</sup> H.R. 705, § 3.

provision, H.R. 705 would amend IRC § 36B to increase the extent to which overpayments of health care credits could be recaptured, thus providing increased tax revenue.<sup>42</sup>

Other proposals have also included either spending cuts or alternative revenue sources to offset the cost of repealing § 9006.<sup>43</sup> During consideration of S. 223, the FAA Air Transportation Modernization and Safety Improvement Act, the Senate agreed to an amendment which would repeal § 9006 of PPACA.<sup>44</sup> The amendment would also rescind \$44 billion of unobligated, appropriated discretionary funds and directed the Director of the Office of Management and Budget to identify, within 60 days, from which accounts the rescinded funds would be deducted. However, the amendment also specifically provided that the rescinded funds could not come from unobligated funds of the Department of Defense, the Department of Veterans Affairs, or the Social Security Administration.

S. 12 proposes repeal of both § 9006 of the PPACA and § 2101 of the Small Business Jobs Act of 2010,<sup>45</sup> which required landlords to comply with the reporting requirements of § 6041 of the IRC for payments made after December 31, 2010. It differs from H.R. 705 in its “pay for” provision. The bill proposes rescission of unspent federal funds.<sup>46</sup>

H.R. 1, which does not propose repealing § 9006 of PPACA, instead would allow no funds made available through the bill’s Full-Year Continuing Appropriations for Fiscal Year 2011<sup>47</sup> to be used to implement or enforce the amendments to § 6041 that were made by § 9006.<sup>48</sup>

## The 111<sup>th</sup> Congress

After the passage of PPACA, there were a number of proposals to repeal or modify its § 9006, but there were also proposals to further expand the reporting requirements in IRC § 6041.

### Proposals to Repeal § 9006 of PPACA

Numerous bills were introduced in the 111<sup>th</sup> Congress that would have repealed § 9006 of PPACA. In addition to introducing a bill (S. 3578) to repeal the provision, Senator Johanns repeatedly introduced amendments to H.R. 5297 calling for repeal. However, that amendment was not included in the Senate’s substitute amendment to the bill. The bill was subsequently passed by the House and enacted as P.L. 111-240, the Small Business Jobs Act of 2010. Proposals to repeal § 9006 were also offered as amendments to S. 510, the FDA Food Safety Modernization Act.<sup>49</sup>

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<sup>42</sup> H.R. 705, § 4.

<sup>43</sup> *E.g.*, S. 18 (rescinding \$39 billion in unobligated, appropriated discretionary funds), S.Amdt. 9 (rescinding \$44 billion in unobligated, appropriated discretionary funds), and S.Amdt. 28 (amending tax provisions related to gas and oil production).

<sup>44</sup> S.Amdt. 9.

<sup>45</sup> S. 12, § 103(a).

<sup>46</sup> S. 12, § 103(b) (rescinding \$39 billion in unobligated, appropriated discretionary funds).

<sup>47</sup> H.R. 1, Div. B.

<sup>48</sup> H.R. 1, § 1516.

<sup>49</sup> *See* S.Amdt. 4702 and S.Amdt. 4713. Generally, repeal proposals have taken the form of repealing § 9006 of PPACA in its entirety. However, at least one proposal, S.Amdt. 4713 to S. 510, employed a more piecemeal approach, perhaps (continued...)

A review of bills that were introduced in the 111<sup>th</sup> Congress to repeal § 9006 appears to indicate bipartisan support in the House for repeal.<sup>50</sup> However, there was disagreement over how to pay for repeal.<sup>51</sup> S. 3946 would have repealed § 9006 of the PPACA without requiring either spending cuts or an alternative revenue source.

## Proposals to Modify Provisions of § 9006 of PPACA

There were two proposals to increase the \$600 reporting threshold in IRC § 6041(a). S. 3783 proposed increasing the threshold amount to \$5,000. A Senate amendment to H.R. 5297 proposed increasing the threshold amount to \$5,000, but only for “payments in consideration of property.”<sup>52</sup> The amendment also would have exempted certain small businesses<sup>53</sup> from the requirement to file 1099s to report property transactions. In addition, it would have provided a statutory exception to the § 6041 filing requirements for credit card transactions and would have allowed regulatory exceptions for transactions with low risk of noncompliance.

## Proposals to Expand Reporting Requirements in IRC § 6041

The TAX GAP Act of 2010<sup>54</sup> would have required information return reporting for certain government payments for property and services. Further, presumably to increase compliance with the requirements of IRC § 6041, the bill would have required sole proprietors<sup>55</sup> to include additional information on their Schedule Cs regarding both the 1099s they received and those they issued.<sup>56</sup>

Another bill<sup>57</sup> would have amended § 6041 to require information reporting of payments made to or on behalf of a person due to that person’s liability to pay punitive damages.<sup>58</sup> The change coordinated with the bill’s general purpose of disallowing the deduction of punitive damages and

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(...continued)

in an effort to accommodate the intervening amendments made by the Small Business Jobs Act. Despite this difference in approach, the end result would appear to be the same as a complete repeal of § 9006. All bill and amendment references are for the 111<sup>th</sup> Congress.

<sup>50</sup> See H.R. 6367, § 201; H.R. 6213, § 1; H.R. 5982; and H.R. 5141. All bill references are for the 111<sup>th</sup> Congress.

<sup>51</sup> Robb Mandelbaum, *Will Congress Repeal the 1099 Expansion? YOU’RE THE BOSS: THE ART OF RUNNING A SMALL BUSINESS* (November 18, 2010), <http://boss.blogs.nytimes.com/2010/11/18/will-congress-repeal-the-1099-expansion/?scp=1&sq=repeal%209006&st=cse>.

<sup>52</sup> S.Amdt. 4595 (the “Nelson Amendment,” authored by Senator Bill Nelson) (111<sup>th</sup> Congress).

<sup>53</sup> These businesses were defined as those that had no more than 25 employees at any time during the year.

<sup>54</sup> S. 3795 (111<sup>th</sup> Congress).

<sup>55</sup> It appears that single-member Limited Liability Companies (LLCs) choosing to be taxed as sole proprietors would be subject to the requirements that would have been imposed by the bill, but those single-member LLCs choosing to be taxed as corporations and multiple-member LLCs would not have been affected by the legislation since the bill did not extend the requirements to either corporate or partnership returns. Other entities filing as either corporations or partnerships apparently would not have been required to comply with these requirements.

<sup>56</sup> The required information would have included both the number of 1099s received and the total amount reported on them as well as the number of 1099s filed by the sole proprietor and the total amount reported on them. Taxpayers would have been required to state, under penalty of perjury, that they had filed all information returns required by IRC § 6041.

<sup>57</sup> H.R. 5994 (111<sup>th</sup> Congress).

<sup>58</sup> This amendment to § 6041 differed from others in that it would be the logical result of another provision in the bill that would disallow deduction of punitive damages and require amounts paid.

requiring inclusion in gross income of amounts paid “to or on behalf of a taxpayer as insurance or otherwise by reason of the taxpayer’s liability (or agreement) to pay punitive damages.”<sup>59</sup> Similar language was included in a Senate bill.<sup>60</sup>

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<sup>59</sup> H.R. 5994 § 2(b) (111<sup>th</sup> Congress).

<sup>60</sup> S. 3793 § 422(b)(2) (111<sup>th</sup> Congress).



## Appendix A. IRC § 6041 Reporting Requirements as Amended by PPACA and the Small Business Jobs Act

**Table A-1. Current Law and Scheduled Changes for Payments Made after 2010**

Changes to IRC § 6041 as Amended by P.L. 111-148 and P.L. 111-240

	Currently Applicable Law for Payments Made Before January 1, 2011	Changes Applicable for Payments	
		Made After December 31, 2010	Made After December 31, 2011
Who must file 1099 for reportable payments?	Persons engaged in a trade or business who, in the course of their trade or business, make reportable payments	Those who receive rental income from real estate are considered engaged in the trade or business of renting real estate and become subject to the reporting requirements in § 6041(a) of the Internal Revenue Code (IRC) <sup>a</sup>	Both the types of payments that are reportable and the payees for whom payments must be reported are expanded
What are “reportable payments”?	Payments aggregating at least \$600 during the calendar year per reportable payee if the payment is made for reportable purposes	Change in who must file (see above) <sup>b</sup>	Change in definition of “payments made for reportable purposes” (see below)
Who are “reportable payees”?	Generally, any individual or entity that is not a corporation and for whom payments are not otherwise reportable	No change	1099s must also be filed for payees that are corporations (unless they are organized under IRC § 501(c))
What are “payments made for reportable purposes”?	Payments for rents, premiums, annuities, compensation, or other fixed or determinable gains, profits, and income	No change	1099s must also be filed for payments for goods and other property and payments that are gross proceeds

**Source:** Compiled by CRS.

- a. There is an exception for property that is the taxpayer’s principal residence and is being rented on a temporary basis. Two other exceptions (for minimal rent and undue hardship) will be defined by regulation.
- b. Although not due to a change in § 6041, for payments made after December 31, 2010, information reporting under § 6041 will generally not be required if the payment was made by credit card (but not by “convenience check”) or through a third party network. Treas. Reg. § 1.6041-1(a)(1)(ii). The amounts of these transactions generally would be reported instead by the “payment settlement entity” that made payments to the vendor or service provider who had initially received payment via a credit card, etc. See IRC § 6050W (Added by the Housing Assistance Tax Act of 2008, P.L. 110-289 § 3091).

## Appendix B. Frequently Asked Questions About the Changes in the 1099 Information Reporting Requirements

1. I own two rental houses. Do I need to file 1099s for payments I made to plumbers, electricians, landscape services, etc., in calendar year 2010?

No. For calendar year 2010, you are not considered to be engaged in the trade or business of renting real estate. However, that will change for calendar year 2011 and beyond.

2. I own my own business and am confused by all the talk about what has to be reported and when the changes take place. Do I have to do anything differently for the amounts I paid in 2010 than I did for the amounts I paid in 2009?

Assuming that you complied with the existing law in reporting the payments you made in 2009, you will not have to do anything differently for payments made in 2010. The changes that will affect you begin with payments made in 2012.

3. I have a small business that I run out of my home. In 2011, I expect to spend more than \$600 for office supplies from one store. Will I need to file a 1099 to report those payments made in 2011?

No. Purchases of supplies in calendar year 2011 will not have to be reported on a 1099. However, that will change for calendar year 2012 and beyond. Treasury regulations create an exception for payments made by credit card (but not by “convenience checks”).

4. I’m the treasurer of a nonprofit organization. Do I have to file 1099s?

Yes. Nonprofit organizations are subject to the same reporting requirements as others who are engaged in a trade or business.

5. There are only two things that I need to file 1099s for. Surely the IRS doesn’t expect me to file just two 1099s. Isn’t there a minimum number that is a threshold?

There is no minimum threshold. If you made reportable payments to reportable payees within the calendar year, you must file a 1099 for each such payee, even if there is only one.

6. I know I’m supposed to put the payee’s “TIN” on the 1099, but I don’t know what that is. How do I get it?

For individual payees the TIN (Taxpayer Identification Number) may be the individual’s Social Security number (SSN). However, for any individual or business entity that has employees, the TIN is the Employer Identification number (EIN). You should request each payee’s TIN by providing a Form W-9 and asking that it be filled out and returned to you. This should be done before making the first payment to the payee.

7. What if someone doesn’t want to fill out a W-9? What do I do then?

Anyone who refuses to complete a W-9 is subject to “backup withholding.” This means that if a payee will not complete a W-9 after you have requested it, you must withhold 20% of the

amount that the payee is owed and submit it to the IRS. When you file the 1099, you will provide as much information as you have about the payee and show the backup withholding on the 1099. You will report 100% of the amount that was owed to the payee as income on the 1099. That is the 80% that you actually paid to the payee and the 20% that you withheld. You will also use the 1099 to report the amount that was withheld for the year.

8. I just contracted with an individual to paint my house. This will cost a lot more than \$600. Do I need to file a 1099 to report these payments?

Unless this is a house that you are renting out to someone else, you will not need to file a 1099 for the amount that you pay to have the house painted. If it is a rental house, you will need to file a 1099 if some portion of the contracted price is paid in 2011 and that portion is at least \$600.

9. I am a collector and buy a lot of stamps each year. Someone said that I'm going to have to start filing 1099s for the amounts that I pay for the stamps I collect. Is that true?

No. Those who are engaged in a trade or business will need to file 1099s for payments made in 2012 or later to purchase goods or property if the total amount paid during the year to a payee is at least \$600. However, those who are not engaged in a trade or business will not need to file 1099s for purchases. Thus, as a collector, you will not have to file 1099s. If you were to begin a business of buying and selling collectible stamps, you would become responsible for filing 1099s.

10. I'm a coin collector. Are these new rules on 1099s going to affect me?

It is possible that you may be affected by the new rules even though you are not engaged in a trade or business; however, you would not be required to file any 1099s. Instead, it is possible that you might receive a 1099 if you were to sell coins to a coin dealer. The dealer would be required to report the purchase of the coins if the total amount paid to you during the year was \$600 or more. You would report the amount on your tax return for the year, but would offset the sales price by your basis in the coins. Your basis is generally what you paid for the coins when you acquired them.

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