

Legal Times

Vol. 32, No. 6

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February 9, 2009

Points of View

SHOT IN THE FOOT

INCOME TAX MISTAKES ARE OFTEN MADE BY PEOPLE WHO THINK THEY'RE SO SMART.

In the midst of the financial crisis, when nerves seem rawer than ever, the most intense attention has been placed on nominees' tax records. Timothy Geithner, who was confirmed as secretary of the Treasury, would have lost his slot had the strident voices arguing his indispensability kept quiet. Former Sen. Tom Daschle was not deemed quite so essential as secretary for health and human services, so he had to bow out.

With all these tax issues popping up, Legal Times couldn't help but wonder if we--;or you--;didn't miss something last April. Legal Times' Eric Barendsen talked to local tax experts to ask: What are the common tax mistakes that lawyers and other high-income professionals make? Their answers have been edited for space.

MICHAEL LLOYD MEMBER MILLER & CHEVALIER

'The one thing that people always struggle with is noncash compensation. That is the one thing that seems to trip a lot of people up--;perks. Whether the perk is provided to a government employee or to an executive, it's always the perk.

'For example, Governor [Rod] Blagojevich and the use of the state aircraft for personal purposes, as well as the situation involving Senator [Tom] Daschle, where someone provided him, apparently, with an automobile and a driver, and he used it for personal purposes--;that's compensation. There are special rules for calculating the value of that compensation, but in order for an accountant to know that the issue exists, the taxpayer has to tell him. That, or the employer needs to withhold.

'I kind of regard the mistake by Treasury Secretary [Timothy] Geithner a little differently than I see the error by Senator Daschle. Treasury Secretary Geithner's error was a very discrete issue. He was a common-law employee and received a W-2. So he was presumably thinking of himself as an employee and not as a selfemployed person. And the software package that he used simply did not connect the dots.

'The reason for that is that 99 percent of the population does not work at the

[International Monetary Fund]. They don't even program the software for that. So I could see someone in his situation just being ignorant of how to report it, because he did report his income and he filed timely. In fact, before he was such a high-profile person, [the IRS] looked at his pattern and they abated the penalties thinking that he did not deserve to be penalized.

'Certainly, if you're a high-profile person, you shouldn't have been doing your own taxes. I have to say that I think that's ridiculous. On the other hand, these people are being played before our very eyes.

'It's almost cliché to say the tax code is too complicated. But there clearly are numerous traps for the unwary, and high-profile people should probably hire professionals to do their returns so that they can catch everything. Or they at least have an excuse.'

ALICE MARTIN THOMAS ASSOCIATE PROFESSOR OF LAW HOWARD UNIVERSITY SCHOOL OF LAW

'You have people who are very busy, very smart, who think they understand more than they understand. I'm a tax professor and have practiced tax law, and I hire a professional accountant to do my returns. Why? Because they spend all day and all night thinking about it. And there are things that I don't want to overlook.

'The other thing that makes wealthy and other individuals' tax reporting more complicated is that our lives are complicated. We have a high divorce rate, particularly lawyers, which means there may be alimony and maybe one party doesn't report it properly. There may be the issue of both parties claiming the [children] on their returns. Usually wealthy individuals have some type of retirement fund, and may move jobs. So you may be moving your retirement funds or withdrawing them early, experiencing the penalties from not properly rolling them over to another fund.

'Particularly wealthier people oftentimes have an entrepreneurial spirit. So they may have some business enterprise on the side, and they don't properly structure that enterprise. They don't keep good records. They don't keep a clear separation between personal and business expenses. They don't think about the right structure in which to place it.

'If you looked at each of these people--;Daschle, Geithner, and [Nancy Killefer, who was slated to be the president's chief performance officer]--; none of their issues were very complicated. Geithner's was: A professional told you what to do, and you didn't do it. The professional looked at your returns and said, 'Hey, you misreported these overnight camp expenses.' And he just didn't bother to admit his mistake and correct it. So even if you have a professional helping, it helps to pay attention to what the professional says to you.

'We've seen more than once before wealthier people having domestics and not doing the proper withholding on employment tax--;actually not paying them properly or

not doing the tax payments that go with having employees. They say, 'Well, I didn't know I was supposed to do all that.' I think it's happened enough that people are aware now.

'I can't imagine Daschle did not understand that when he received the, quote, gift from a business partner--;because you can't even make gifts of that kind in a business context--;it's income. I think wealthier people confuse that as well. There may be a personal element to a business relationship, but they don't make a clear distinction in their own minds. They kind of stay in that fuzzy tax mind.

'Daschle and Geithner and [Killefer], they're just the tip of the iceberg. People are pointing fingers on Capitol Hill, and I dare say that if we did an audit on a great deal of those returns, there'd be a whole lot of people scratching their heads saying 'Well, I didn't know.'

NEIL BUCHANAN ASSOCIATE PROFESSOR OF LAW GEORGE WASHINGTON UNIVERSITY LAW SCHOOL

'Like a lot of people, I get a laptop from my employer. The university officially owns it. But it's in my possession, and I use it when I go on research trips or to conferences. Of course, I use it at home as well. And it means that I don't have to buy my own laptop.

'From the standpoint of pure income tax theory, the question is whether that's income, and the answer is really easy. It's obviously income. Because anybody else would have to earn money and pay tax on it and then get a laptop.

'So there are two interesting questions. One is, would this occur to anyone [to declare the laptop]? And two, is there an exception to the very broad rule?

'In answer to the first question, it certainly didn't occur to me. I got the laptop Jan. 1, 2007, and filed my 2007 taxes without ever thinking about it, and I would have done the same thing this year, except that I happened to see something on the TaxProf Blog that brought this up. So I have to amend my taxes for 2007, and when I do my 2008 taxes I'll do them right going forward. In terms of the amount of underpaid tax, we're talking in the low hundreds at most, but it was wrong. And it's incumbent upon me to make it right.

'The code has--;this is one thing that we teach very early on in the basic tax law class--;some very extensive rules about fringe benefits. And what drives the students crazy, rightly, is that the rules are essentially ad hoc. Over the years Congress decides we're not going to bother to tax this, but we are going to tax that. Without looking at the Internal Revenue Code, there was no way for me to know whether or not [the laptop] was the type of income that Congress had said will be taxed or has been excluded from tax.

'A lot of it is just in response to situations like this where you say, 'Is this