

1099's: How to Avoid an Audit

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Processing 1099's can be confusing and frustrating. Admin Books enjoys passing on important information that will help you find your way through the requirements of 1099's. Here are some facts you need to know!



General Rule: If you **pay someone more than \$600 in a calendar year for services**, not material/product, then you are required to provide a 1099 showing the amount you paid. One tip is to **collect a W-9 at the time of payment** so you know if the business is a sole proprietorship, LLC or Corporation. If it is a corporation, then no 1099 is required. The 1099 is due January 31st and the required 1096 is due February 28th.

Addressing the 1099: If the person you paid uses their Social Security number as a tax ID number (which I don't recommend), then the person's full name must be on the **first line of the 1099**. If you list the business name by mistake, then you will receive a

letter from the IRS saying that the name and ID do not match. Then the IRS may require you to withhold money from future checks.

Reimbursed Expenses: If you pay a subcontractor for expenses incurred, **do NOT include that amount in box 7**. If you receive a 1099 from someone with reimbursed expenses, like travel or postage, don't worry. Show the full amount of income on your tax return and then show the full amount of expenses and it will net out the same. If you lower the 1099 amount on your return to "correct" it, that will trigger an audit.

Strict Classification Rules: If you hire a subcontractor, be sure that the **state won't deem the person as an employee**. A few indications to strengthen your case are:

- You have a contract agreement between parties.
- The subcontractor invoices the business.
- The subcontractor has a business license. The business does not tell the contractor **WHEN** to perform the work or **HOW** to do their job. The subcontractor uses their own equipment and materials.
- The subcontractor is available to be hired by other companies. Governor Brown signed a bill that starting 01-01-12 if any employer is found to willfully misclassify a worker as an independent contractor, they penalties will increase to \$10,000-\$25,000 per violation.

New 1099-K Rules: There has been a lot of confusion regarding the new 1099-K rules. All merchant companies that process credit card payments are required to issue 1099-K's to the seller. It can be for 1 transaction for any amount. The main reason for this new law is to capture payments going through eBay, PayPal and Amazon. However, now the common business owner will get a 1099-K as well if their clients/customers pay them with a credit card. Here is the confusing part: businesses will

provide a 1099-MISC for payments made with a check/cash and the merchant company will process 1099-K's made with a credit card. Let's give some examples to clarify:

Example 1 – You pay a subcontractor \$700 for services. If you paid them with a check, you issue them a 1099-MISC.

Example 2 – You pay a subcontractor \$700 with a check and \$800 with a credit card. You will issue them a 1099-MISC for \$700 and the subcontractor's merchant company will give them a 1099-K for the \$800.

Example 3 – You pay a subcontractor \$300 with a check and \$800 with a credit card. We recommend that you still issue a 1099-MISC for \$300 because the combine total payment to the subcontractor (check and credit card) was over the \$600 amount – this is the safe answer.

Oddball Clarifications: If the **contractor is NOT a US citizen and lives in another country**, have them fill out a W-8 and keep this on file. Prepare a 1099, but there will be no tax ID number on the form. If questioned by the IRS, show them a copy of the W-8.



If the 1099 comes back to you undelivered, keep a copy for your records to show the attempt.

If the contractor has already performed their services and you **cannot get the contractor to fill out the W-9**, keep a log of the attempts to contact them by phone, email or letter. The IRS has penalties for not sending the 1099 and if you show intent, hopefully there will be grace in the penalties.

If you find you made a mistake on the amount or tax ID number, you can always correct the form and re-send it by checking the "Corrected" box.

Corporations do NOT get 1099's, but some people are confused if they should send a 1099 to LLC's. Send a 1099 to single-member LLC's and multi-member LLC's (partnerships.)

1099's are **required to ALL attorneys** regardless of their entity!

If you have any clarifications, please contact our office. If you would like to delegate this project, we would be honored to help. Call our office at 408-782-9640 for 1099 pricing.

