January 6, 2023

Sent via email: pra.comments@irs.gov
Andres Garcia
Internal Revenue Service
Room 6526
1111 Constitution Avenue, N.W.
Washington, D.C. 20224

Re: Form 1098-F
OMB Control No. 1545-1276
Notice and Request for Comment on Form 1098-F, appearing in Federal Register, Vol. 87, No. 221 (Nov. 17, 2022).

Dear Andres Garcia:

On behalf of the Federation of Tax Administrators[1] (hereinafter "FTA") we appreciate this opportunity to provide comments on the proposed Form 1098-F. The Form 1098-F is the information collection form used to report the amounts paid as required by Internal Revenue Code (hereinafter "IRC") § 6050X to the Internal Revenue Service (hereinafter "IRS"). IRC § 6050X in turn is directly tied to the 2017 amendments to IRC § 162(f) prohibiting a deduction for certain payments to governments or governmental agencies in relation to a violation of the law or an investigation or inquiry into a potential violation of the law[2]. Clarifications and information provided to date by the IRS has been useful, but the burden of compliance with the reporting requirements by State revenue agencies (hereinafter "Agency" or "Agencies") will be substantially more efficient and less burdensome if more clarity were provided regarding the concerns contained herein.

Agencies routinely conduct audits and review the tax returns of thousands, if not millions, of businesses and individuals annually. These audits and reviews are part of the ordinary course

[1] The Federation of Tax Administrators serves the principal tax collection agencies of the 50 states, the District of Columbia, Philadelphia, and New York City. Part of its mission is to improve the quality of state tax administration. FTA serves as a source of information and expertise for state administrators and others on the workings of state tax agencies and systems as well as issues generally affecting tax policy and administration. FTA works with state tax agencies and the Internal Revenue Service to foster cooperative tax administration projects among states and with IRS.

[2] Whenever the term "violation of the law" is used that usage, unless otherwise stated, shall also encompass "an investigation or inquiry into a potential violation of the law."

of business and natural part of the voluntary compliance system under which the Agencies operate. For the most part, taxpayers, be they businesses or individuals, file tax returns that comply or are intended to comply with extremely complex tax statutes and regulations. Not surprisingly, tax filers make innocent errors on these returns which are identified by the Agencies, resulting in notices to the taxpayers of corrections made and, possibly, additional amounts due to the government. In addition, and, also, not surprisingly, there arise reasonable differences in the interpretation and application of these complex provisions to particular situations. There is substantial case law in both State and federal courts that have concluded such errors or good faith positions do not support subjecting a taxpayer to the most severe penalties allowed under a particular tax regime. Administrative penalties such as for late filing or late payment are, at most, all that is warranted. And often, even these administrative penalties are ultimately abated, in whole or in part, during the collection process.

The regulations for IRC §§ 162(f) and 6050X provide some but not enough clarity on whether, under the circumstances described above, in which an assessment notice would be issued, a "violation of the law" or "investigation or inquiry into a potential violation of the law" have occurred triggering the requirement to file a Form 1098-F. The examples provided in Code of Federal Regulation (hereinafter "CFR") § 1.162.21(f)(5), (6), do not provide the Agencies sufficient clarification. FTA recommends that the IRS clarify that assessment notices sent to individuals or businesses as part of the routine audit process not be classified as a violation of the law under IRC §§ 162(f)(1), 6050X(a)(1)(C), and/or CFR § 1.6050X-1(a)(1). Additionally, the FTA recommends that where a taxpayer in good faith takes a reporting position on the return that may be contrary to the position of the Agency, that such is not considered a violation of the law under IRC §§ 162(f)(1), 6050X(a)(1)(C), and/or CFR § 1.6050X-1(a)(1).

Alternatively, the FTA recommends that a determination of when a tax liability (including any associated penalties and interest) constitutes a violation of the law and is binding should take into consideration whether all appeals have been exhausted or the time for filing an appeal has expired. (*See* CFR § 1.6050X-1(b)(4) which states that the exhaustion of appeals and time for taking an appeal should **not** be taken into consideration.) As noted above, more often than not, tax assessments arise due to innocent errors, minor corrections, or reasonable disputes as to the interpretation and application of a statute or regulation. It is only after an assessment is appealed by a taxpayer and fully vetted that it can be determined that these circumstances are not the cause behind the tax deficiency but rather a violation of the law[3] has arisen prompting the requirement to file a Form 1098-F.

Like the situations above, it often occurs that a taxpayer will timely and properly file the tax return, reporting the proper amount of tax due, but will not remit the tax. The Agency will then file a notice of amount due, or deficiency notice or undertake other collection actions. The taxpayer will subsequently pay the amount due. The FTA recommends that such collection actions

[3] As those terms are used in IRC §§ 162(f)(1) and 6050X(a)(1)(C) and CFR § 1.6050X-1(a)(1).

should not be considered a violation of the law for purposes of IRC §§ 162(f)(1) and 6050X(a)(1)(C) or CFR § 1.6050X-1(a)(1). Likewise, the FTA recommends that the administrative type penalties such as for late filing and late payment not be considered a trigger for Form 1098-F reporting purposes. (FTA does not, by this recommendation, take any position contrary to current rules regarding the deductibility of such administrative penalties.)

As understood by FTA, the reporting requirements of IRC § 6050X are a tool for the IRS to have, should the occasion arise, to determine if a taxpayer has properly reported certain deductible expenses on the return as limited by IRC § 162(f)(1). To assuage any confusion, IRC § 162(f)(4) clearly states that the exclusions in IRC § 162(f)(1) do "not apply to any amount paid or incurred as taxes due." In other words, the amount of taxes paid or incurred, and the interest accrued and paid thereon, is a properly deductible expense (provided any limitations otherwise provided in IRC do not apply) per CFR § 1.162-21(c)(2). In addition, per that same regulatory provision, penalties, and the interest on such penalties, are not deductible under § 162(f)(1). Thus, per the plain language of the statute and regulation, taxes and interest on taxes due are excluded from § 162(f)(1) and should not be taken into consideration for reporting purposes under § 6050X. Consequently, the FTA recommends that the IRS clarify that for purposes of meeting the threshold amount of CFR § 1.6050X(f)(6), it is only the penalties and interest on those penalties for a violation of the law, determined at the time such imposition becomes binding, that must equal or exceed the threshold, and no other amounts should be considered. In so clarifying, the IRS should also provide that it is only the penalties and interest on those penalties that should be reported on the Form 1098-F.

There are many circumstances in which a taxpayer will be informed of a tax liability that is due and owing. At the time of such initial notification interest may not have been due, it becomes due only if the taxpayer does not pay before a certain date. Additionally, interest may accrue as the tax liability remains outstanding. Assuming there is a violation of the law at the point in time the notice is sent to the taxpayer, the instructions do not make clear what, if any, additional reporting obligations are required if the liability remains unpaid and subsequent notices are sent out. This could be especially problematic if, at the time of the first notice, the threshold amount was not met, but it was met at the time of the subsequent notice. FTA recommends that no additional reporting requirement should arise because of the subsequent notice to the taxpayer. At this stage, it is a collection matter and not a component of the violation of the law or the investigation or inquiry into a potential violation of the law.

Taking into consideration the above information, background, and recommendations, the FTA addresses the specific questions posed in the "Notice and Request for Comment on Form 1098-F" appearing in Federal Register, Vol. 87, No. 221 (Nov. 17, 2022). Answering in the order of appearance:

A. Is the collection of the information necessary for the proper performance of the functions of the agency, including whether the information shall have practical utility?

The FTA is unable to address whether the information that would be received from the Agencies is necessary for the proper performance of the functions of the IRS. That said, unless the clarifications requested herein are provided, the information that will be received from the Agencies will be of minimal practical utility. This is because the information will not necessarily reflect actual amounts paid by a taxpayer and may not accurately show the amounts paid for interest that is deductible and not deductible under IRC § 162(f)(1). The purpose of a third-party informational return is the production of independent documentation containing accurate information to test the accuracy of a tax return. If the informational return cannot be completed accurately due to unclear instructions and definitions, it can be of little utility.

Likewise, the inaccuracy of the Form 1098-F has consequences for the taxpayer as well. First, based on inquires the Agencies have been receiving, taxpayers and tax practitioners are already confused as to what they should be doing with this form upon receipt. Second, the taxpayers that this form was most likely intended to incentivize will not be so incentivized knowing the form is not necessarily accurate.

Additionally, despite whatever utility the form may have to the IRS, it could have a negative utility to an Agency if the form is required to be issued at the time of an assessment. In many cases, after an assessment is issued by an Agency, the Agency and taxpayer will enter into discussions regarding the basis of that assessment. The results of those discussions could be modifications and corrections to the assessment, withdrawal of the assessment, or a comprise, all of which could be finalized well after the Form 1098-F reporting deadline. Issuing the Form 1098-F using the initial assessment figures will not only be inaccurate for the IRS's purposes, but will negatively impact a taxpayer's willingness to cooperatively work with an Agency or reach a compromise in lieu of an administrative or judicial appeal.

B. The accuracy of the agency's estimate of the burden of the collection of information.

The IRS has estimated that 137,500 1098-F forms, each taking approximately 7 minutes to prepare will be filed annually. If the recommendations made herein are not implemented, the time estimated for the Agencies to prepare each Form 1098-F will be substantially more than the 7 minutes estimated. Each potential assessment issued by an Agency will have to be individually reviewed to determine if it is "binding under applicable law, determined without regard to whether all appeals have been exhausted or the time for filing an appeal has expired" as provided in CFR § 1.6050X-1(b)(4). In many circumstances this determination is not a simple bureaucratic function, nor a function which can be programmed into an automated system but requires a nuanced understanding of the applicable law and will require referral to Agency counsel and/or upper management of the Agency.

Ascertaining the appropriate figures to be reported on the return will require time. The figures on the notice that triggered the reporting requirement will not necessarily reflect the actual

amounts paid by the taxpayer. Additional interest may have accrued, or a lesser amount may have been accepted by the Agency in compromise. Again, this is not something that can necessarily be automated, but will require investigation and ascertainment vis-à-vis staff review.

In this same vein, the instructions for the Form 1098-F require certain codes be entered in box 9. Of specific concern to the Agencies is code "A" which is required if the taxpayer "has made or is obligated to make multiple payments." To determine what payments have been made is not a simple task. The Agencies will have to review the payment history of the taxpayer. Such payment histories could very well include information on payments received for multiple tax periods and multiple tax types. The Agencies will need to sift through this information to determine what, if any, payments a taxpayer has made for the tax agreement, suit, or order being reported on the particular Form 1098-F. Added complexity to discerning what is the proper code arises when multiple government agencies are involved and not only a revenue agency.

Agencies at both the state and local level of government will also expend time and resources on training and record keeping. This expenditure of time and resources will not occur in just the first year but will be an ongoing outlay. Whatever time it may take to actually complete the return, i.e. the "7 minute" estimate above, clearly does not factor in the ongoing administrative burden associated with the Form 1098-F.

C. Ways to enhance the quality, utility, and clarity of the information to be collected.

The FTA has proposed several clarifications and recommendations above. Those clarifications and recommendations are incorporated herein. In addition, FTA recommends that further clarification be provided defining what figures are reportable in which boxes of the Form 1098-F in the context of tax assessments. For instance, as noted above there is a clear distinction between interest on a tax due liability and interest on the penalty imposed arising from that tax liability. But where on the form each type of interest is reportable is unclear. If the form is to be of any utility, accurately reporting such figures in the correct location on the form is critical.

D. Ways to minimize the burden of the collection of information on respondents, including through the use of automated collection techniques or other forms of information technology.

The FTA refers you to the requests for clarification and recommendations contained elsewhere for the ways to minimize the burden upon the Agencies.

E. Estimates of capital or start-up costs and costs of operation, maintenance, and purchase of services to provide information.

It is not possible for the FTA to estimate what the start-up, maintenance, and purchase of services costs will be to comply with this reporting requirement. These costs will depend on numerous factors including, but not limited to: 1) will a particular Agency be responsible only for reporting on violations or the investigation and inquiry into potential violations of tax laws administered by that agency, or such as arise across all State agencies; 2) the current state of an

Agency's information technology system and the adaptability of that system; and 3) changes implemented year over year by the IRS.

Finally, the Agencies have already received numerous inquiries from tax practitioners and taxpayers asking what is to be done with the Form 1098-F. For example, they want to know if the form is to be attached to a return, whether they are required to report the figures on a return as they appear on the form, as well as where to report the figures on the return. These are questions that the Agencies are not qualified to address. The FTA strongly recommends that the IRS put information in the instructions and on its website providing more direction for taxpayers and tax practitioners and notifying taxpayers and tax practitioners whom they can contact to answer such questions. The FTA further recommends that a frequently asked question page be established on the IRS website, that is updated in real time, to keep interested parties informed and to provide consistency in understanding the requirements of Form 1098-F.

The FTA urges the IRS to promptly review these comments and publish the clarifications, modifications, and alterations to the Form 1098-F and its instructions necessary to the proper completion and filing of the form by the Agencies. Time is of the essence in that the deadlines for reporting and filing are fast approaching.[4] To comply with those deadlines Agencies need to start immediately gathering and reviewing information that they may be required to report. All this while in the midst of preparing for tax-filing season.

Thank you for the opportunity to provide comments on the Form 1098-F. FTA is hopeful that you will find these comments and recommendations helpful. FTA remains committed to its working relationship with the IRS on behalf of its members and to promoting the efficient and transparent administration of the States and federal revenue laws. Should you have any questions or require additional information please contact the undersigned at (202) 964-5861 or brian.oliner@taxadmin.org.

Sincerely,

Brian L. Oliner

Brian L. Oliner
General Counsel
Federation of Tax Administrators

[4] Per CFR 1.605X-1(c)(3), the Agencies are required to send a copy of the Form 1098-F to the taxpayer by January 31, 2023. Filings to the IRS are due on February 28, 2023, for paper filings, and March 31, 2023, for electronic filings.