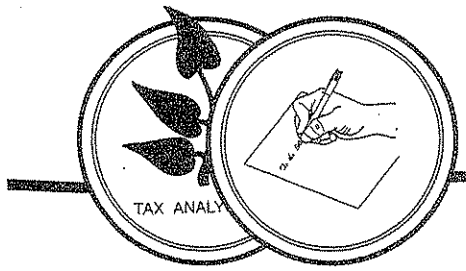

letters to the editor

Thoughts on the More Level Playing Field

To the Editor:

It is not helpful that otherwise knowledgeable tax writers perpetuate the IRS myth that self-employed individuals and small businesses engage in massive noncompliance. However, that is exactly what my good friend Bill Raby did in his recent article "'Spouse Employment Contract' — Loophole or Noose?," *Tax Notes*, Mar. 8, 1999, p. 1481.

The self-employed suffer from so much image bashing already that this comment will allow the government (IRS, Dept. of Labor, etc.) to continue to pursue their aggressive tactics against small businesses. Can this be shades of financial status auditing all over again? Bill also suggests that audits will be more intrusive because of the new law that shifts the burden of proof to the IRS. Nothing could be further from the truth. If the taxpayer complies with reasonable requests for information, the burden of proof shifts. What is a reasonable request? Let's look at independent contractor law, which states that the taxpayer must make a *prima facie* case to the government before the burden of proof shifts to the government. *"Prima facie"* is a low-level test. It means on its face — almost a common-sense approach. If the IRS wants to fight over the definition of reasonable requests — so be it. I believe the taxpayer who offers *prima facie* proof in an audit will win overwhelmingly should the IRS dispute the evidence proffered.

Taxpayers must remember — IRS fishing expeditions are not allowed. Taxpayers are required to substantiate their deductions using the *prima facie* standard. However, the taxpayer need not stand in fear that the very law that is designed to level the playing field (the shift of the burden of proof to the IRS) will boomerang and produce financial status-type intrusion audits. That is not what Congress intended and the American public should not stand for it.

Sincerely,

Michael J. Knight
Michael J. Knight & Company, CPAs
Fairfield, Conn.
April 4, 1999

Teaching Sanskrit Would Be Easier

To the Editor:

I read with interest "Recent Capital Gains Tax Legislation: Some Behavioral Research Observations," by Bruce Koch and Stewart Karlinsky, (*Tax Notes*, Mar. 1, 1999, p. 1369) in which they state that if " . . . Congress is trying to simplify the tax code, it has not done a very good job."

I couldn't agree more. However, they have picked only one example. My perspective is a little different from theirs. Theirs approaches the complexity issue from the preparer perspective. I approach the issue as an educator. A little background may be in order. I am, at heart, an educator. While I am an attorney (inactive) and a CPA (barely active), I am also a college professor teaching two undergraduate federal income tax courses. As anyone who has tried to teach these courses knows, these are very difficult subjects to teach.

The cited letter deals with the complexity of the capital gains provisions. Another overly complex subject to teach are the alimony recapture provisions. That is in part due to the fact that the alimony recapture calculations look more like a final exam question in calculus than they do something that sprang from Congress as part of the Internal Revenue Code. View them for yourself!

(1) Year 1 recapture is P1 - ((P2* + P3)/2) + $15,000)

(2) Year 2 recapture is P2 - (P3 + $15,000)

For these purposes:

P1 = Allowable alimony payments in year 1

P2 = Allowable alimony payments in year 2

P2* = P2 minus the recapture in number (2) above.

P3 = Allowable alimony payments in year 3

So, I guess when I accepted that teaching tax involved complicated concepts or arcane "theories" it made sense because surely there was a good justification for the apparent complexity. After all, without such calculations taxpayers could treat as alimony what was actually a property settlement with the goal of moving income from one ex-spouse to another, thereby reducing their combined income taxes. My gosh, would a divorced or divorcing couple really do that?

So what does Congress do for 1998? It created two new credits, the HOPE scholarship credit and the lifetime learning credit, apparently to reduce the cost of college and postsecondary education by providing a credit for the cost of tuition. Certainly a noble goal.

But can it be taught and more importantly, does the public understand it? I think the answer to both questions is no!

If it takes IRS Publication 970, Tax Benefits of Education, over three pages to explain these two credits, plus a full page chart and an example of the IRS tax form, Form 8863, what hopes do I have of teaching this in 10-15 minutes? After all, in the scheme of things this isn't even a theoretical issue, its simply a tax reduction by way of a credit. Moreover, it is not even refundable, as if I could explain to college juniors and seniors what the difference between a refundable and a nonrefundable credit is. And while I am on the subject of juniors and seniors, I guess I can skip the HOPE credit, because it is improperly named. Juniors and seniors have no hope of getting it, because it applies only to frosh (freshmen according to the IRS, but being sexist I will not call them that) and sophomores. Of course, since this is tax, it is not that simple. The credit actually applies to the first two years of postsecondary education, not to frosh and sophomores. Thus, I am confused! The government publication, clearly the source of all tax compliance advice anyone would need to fill out a tax return for a college student, does not appear to answer the real life questions of most students. If the student previously took part-time classes at a two-year college do those count? What if they go to trade school after high school? What if they are at a two-year college but have been there for three years because they changed majors?

I would go on to explain that if the juniors paid tuition as sophomores last semester that they could get a HOPE credit equal to 100 percent of the first $1,000 of qualified expenses and 50 percent of the next $1,000 for all payments made during 1998, or that if they were full-time students and that if they are juniors or later, they can still qualify for the lifetime learning credit, except that this applies only to payments after June 30, 1998, and the credit is equal to 20 percent of the qualified payments up to $5,000, and even then, there are phase-outs for students (or their parents) who make too much money; oh and did I mention that the credit must be coordinated with the use of education IRAs and scholarships, but, that might be a run-on sentence and I also teach Business Communications and what would those students think of a sentence such as this that is too long and that contributes to a one-sentence paragraph that looks more like an Internal Revenue Code section than a paragraph in a nationally distributed magazine?

Is it just me or is this far too complicated? The answer to that question can be seen in the following actual story. A student came to me and said she had just been to her tax preparer, a national chain. She has a W-2 and tuition payments. "That's all folks." So, she gave the information to the preparer who said that she doesn't qualify for an education credit. I don't remember why, but I think it was because she was a junior. Finally, the student convinced the preparer that she does qualify and lo and behold, a credit appeared on her tax return along with a bill for $92. So how much of the $92 was caused by the credit?

Another student came to my office, return in hand, Form 8863 prepared (properly I might add), and asked "Where do I enter the credit? There doesn't appear to be any place to put it on Form 1040EZ." I noted, trying not to be to sarcastic, "Unfortunately, you should have figured out that this credit isn't EZ. So, you can't use that form. You must go back to the library and get a Form 1040A." As long as I am on this subject, why are there three tax forms? Form 1040 EZ, Form 1040A, and Form 1040, not to mention Form 1040NR and Form 1040X.

So, I close with the following comment to whomever will listen. I've had it, I am mad as hell, and unfortunately, I do have to take it.

Sincerely,

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April 5, 1999