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Re: Mid-Year Tax Tips!

Dear Clients, Colleagues, and Friends:

Economics, the Law, and Reason (ELR) – Does it Pass the ELR Test?

We strive to work our projects to pass the ELR test. To increase efficiency, we are recommending that you send your documents to TheOffice@paulhburgess.com. It is an inbox that is being monitored daily and will assist us in keeping your projects moving forward. Of course, feel free to use our other emails too, especially for specific questions, comments, and concerns. If you have not already, please update your contacts with our new physical address and telephone number (see above) as well as our new email addresses: Paul@paulhburgess.com, Theresa@paulhburgess.com, Mackenzie@paulhburgess.com, and Melanie@paulhburgess.com. We are conveniently located in mid-town Tulsa with excellent parking, so feel free to drop by and see our new offices. They are unique and inviting. The rest of our Newsletter provides several helpful *Tax Tips!* that support the ELR process.

Document Your Tax Payments and Be Careful of Larger Overpayments. Tax agencies continue to struggle with their workloads. Three common problems taxpayers are experiencing include: (1) Checks cashed but posted late or incorrectly, (2) Checks not cashed for several months, and (3) Auto withdraw requests made with e-filed tax returns but posted late or not at all. To reduce the problems from these mishaps, consider these *Tax Tips!* (a) Pay your taxes online, (b) Check your bank accounts to verify the tax payment has been withdrawn, (c) Try to pay a week or so prior to the due date, (d) Combine smaller quarterly estimated tax payments into one payment, and (e) Procure your proof of payment just in case the dreaded tax and penalty notice arrives.

A similar tax problem is starting to arise...difficulty getting tax overpayments back or applied to subsequent years. In the past we generally recommended trying to be just a little bit overpaid. Our recommendations are shifting. In some cases, we are suggesting to perhaps err on the side of a small underpayment to reduce the probability of “wrestling down” an overpayment.¹ *Tax Tip!* If you are paying estimated tax payments based on the prior year, but the current year’s income is down, consider “pulling back” on your 4th quarter estimates. Generally, though, make sure Oklahoma is timely paid because it charges 15% interest plus a 5% late penalty.

Written Agreements Between Related Parties are Important to the IRS. In *Plentywood Drug, Inc. (PDI) v. [IRS]*, a written lease probably would have helped in their “self-rent” situation. PDI was renting its storefront from its shareholders. The IRS challenged the rent rate as too much.

¹ Starting July 1, 2022 the IRS is paying and charging 5% interest for individuals. Good if your overpayment arrives several months late and you don’t need the money, but an expensive interest rate for underpayments.

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Although PDI eventually prevailed, the Tax Court first noted “[the parties] set the terms by oral agreement...[and] did not [ever] put the [rent] terms into a formal written lease signed by themselves...as the owners of the pharmacy and then again as owners of the building.” The lesson in *Plentywood* is: draft and sign written agreements when you are personally leasing space to your business (usually an LLC or corporation). Typically in self-rent situations taxpayers should charge their business the high-end of a reasonable rent rate. The IRS likes those “self-rent” agreements in writing, and perhaps if PDI had one, the IRS might have backed down some and not taken PDI to court. **Tax Tip!** Draft self-rent agreements similar to 3rd party agreements and document your due diligence on how you ascertained your fair value rental rate.

Three Tax Tips! from the Recent Tax Court Alder Case.

Travel Receipts are Required. Mr. Adler worked for a division of NBC as a contract consultant. He would turn in his travel receipts and NBC would reimburse him. Mr. Adler apparently failed to get reimbursed for some of his travel, and instead he deducted “travel estimates” on his tax returns. The problem is there is an IRS statute disallowing “travel expenses” without a receipt. Using reasonable estimates per the *Cohan Rule* is allowed in many circumstances, but not for travel expenses. **Tax Tip!** Keep your business travel receipts.²

Refrain from Combining Accountings. Mr. Adler also started performing construction services for NBC. He reported his “construction business” on the same IRS schedule as his “consulting business.” The problem is construction projects generally have much lower net profits per gross income than consulting. Thus, Mr. Adler’s “consulting income” appeared to have significant expenses that consultants generally do not incur. Combining the two businesses probably triggered the audit.³ **Tax Tip!** Generally, prepare separate accountings for different types of businesses. In addition, for larger deductions, sometimes it is important to “spread the deduction out.” An example is a large automobile deduction, which might consist of Repairs and Maintenance, Insurance, Tires, and Fuel. These expenses may be best reported in the four respective categories.

Issue Forms 1099. Exasperating Mr. Alder’s tax mess, he deducted expenses for a sub-contractor to perform demolition and hauling but failed to issue the sub a Form 1099. Generally, the IRS’ position in an audit is that even if you can prove the contractor expense, no deduction is allowed without a Form 1099 issued. Accordingly, issue Forms 1099 or increase the risk you will be paying your sub-contractor’s taxes. **Tax Tip!** Call our office at (918) 901-9000 in early January to timely file your business’ Forms 1099.

Good News & Bad News re: the 2022 Meals Deduction. The IRS confirmed that the 100 percent business meals deduction for 2022 applies not only to meals on premises but also otherwise eligible takeout meals from restaurants. Restaurants for tax purposes are an establishment primarily serving meals for immediate consumption. But a restaurant is *not* takeout food from a grocery or convenience store even if the meals are ready for immediate consumption.

² Some taxpayers are eligible to use the IRS’ “per diem” travel rates instead. Nevertheless, proof is required for the time, place, and business purpose. Many times a receipt with notations on it can prove the three elements.

³ Expense to income ratios that are unusual may be the leading cause of audits. In Alder’s case, his tax return reported he was a consultant but it had construction firm deductions. Not Good.