

# Tax Preparer Mistakes You Should Know

I have great sympathy for tax return preparers. A nearly endless stream of virus-like complex tax laws and rules are making them ill. New, stiff penalties for preparers who don't have substantial authority are like the Internal Revenue Service standing on their oxygen hose. Throw in a dose of new, revised and confusing tax forms and we've got an epidemic.

Congress, the President and the IRS do not deserve all the blame for this epidemic, however. Many taxpayers exacerbate the situation by delivering information to their tax preparers at the last minute, then demanding that their returns be ready by April 15. Perhaps fewer preparers would fall victim to the epidemic's infection if they simply had more time and took more care in the preparation of the returns.



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Regardless, the epidemic is here. Watch for these symptoms.

**Forgotten Form 1045.** Infected tax preparers sometimes forget that an individual can have a business net operating loss that can be carried back or forward for tax refunds or savings in future years. Thanks to recent economic recovery legislation, a net operating loss from 2008 and 2009 can be carried back up to five years. This allows the taxpayer to get money back from the IRS out of taxes paid in better times. Preparers often forget to compute the business net operating loss because the Form 1040 scrambles non-business income and expenses with the business income and expenses. The Form 1045 is the unscrambler.

If an individual has a loss in a sole proprietorship (Schedule C), partnership, LLC, LLP, S Corporation, farm (Schedule F), or other pass-through entity, this loss flows back to the owners. Form 1045 starts with line 41 of the Form 1040; if that is a negative number the preparer needs to consider preparing the Form 1045 to see if there is a net operating loss that can be carried back for a refund. I have two clients where the infected preparers missed very large business net operating losses with refunds in six digits.

There is a three-year statute of limitations for computing the net operating loss and carrying it back or electing to carry it forward. If there is no money on the table in the past, the net operating loss can be carried forward for 20 years to offset future taxes. Don't let your beleaguered tax preparer miss this item. The Form 1045 for 2009 is good only through the rest of this calendar year and cannot be used for previous years. However, the Form 1040X can still be filed and the refunds claimed.

The good news is if there was a loss years ago, that loss may still be available to carry forward to the current or future years. Even if that tax year is closed by the statute of limitations, there is a possibility the loss may still be carried forward with the right facts.

**Forgotten Form 3800.** This lead form for claiming the General Business Credit is one monster dose of germs – and is easy to forget. Form 3800 is the lead sheet for claiming dozens of credits, each of which requires a separate form. Infected tax preparers may view this as a big waste of time. A great deal of detailed information is required, historically with little payback. But times have changed. There are some

significant credits available now.

While politicians may not be able to agree on health care or immigration policy, they all love tax credits. Some view a tax credit like a tax reduction, and others view credits as helping to stimulate the economy, create jobs and protect the environment – all good things. For the “sick” tax preparer, however, these nearly endless new credits are like being caught in a cold draft. She fears that she has to plow through the form and there may be no credit actually available at the end of the calculation. If she spends an extra hour or two and finds not a single dollar of credit, will she ever be able to bill for the time? Cough, cough. If she does find the credit, however, it may save money now or may be carried to years where it will save money.

Here are just a few of the credits that appear on Form 3800's long list: alcohol and biofuel; alternative motor vehicle; employer social security and Medicare taxes paid on certain employee tips; employer differential wage payments; employer-provided childcare facilities and services; increasing research activities; small employer pension plan startup costs; disabled access; empowerment zone and renewal community employment; energy efficient home; Indian employment; investment credit; low-income housing credit; new markets credit; work opportunity credit; and many more. Some of the credits for hiring new employees and even employees previously laid off are quite substantial. Owners of small businesses – including many law firms – should not overlook these potentially big tax benefits.

The above does not include state tax credits; California has a long list of credits as well. If your infected tax person doesn't claim it, you won't get it. Choke.

You may have missed these credits in years past. If the statute is still open, look into going back and getting them. You may be able to carry the credits backward and get money left on the table, or carry them forward for years and years until you use them all.

Failure to report foreign bank accounts, foreign trusts, or foreign controlled corporations. Some tax preparers don't even think of these as tax return forms. While they are only information reports, failure to file can be very expensive. The IRS has the power to impose significant



penalties for nondisclosure of a U.S. taxpayer's interest – even if it is only a contingent beneficial interest or signature authority over an account in which the taxpayer has no beneficial interest. One key form is the Report of Foreign Bank and Financial Accounts (FBAR) – Form TD F 90-22.1. There are yet other forms to disclose the foreign trust and foreign controlled corporations, and there also are boxes to mark on the Schedule B to Form 1040. Finally, don't forget Form 3520 to report the trust that owns your home in Mexico, or to report gifts to U.S. residents from foreign sources.

The penalties for failure to report can be horrible. They range from a mere \$10,000 per undisclosed item per year to confiscation of a large percentage of the account balance to criminal penalties. The recent UBS secret Swiss bank account fiasco has created tremendous awareness. I get frequent phone calls from confused and desperate taxpayers and tax preparers alike wondering what they should do about unfiled FBAR reports for the last several years.

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I strongly recommend that any taxpayer with nondisclosure issues consult with a tax lawyer who has expertise in this area, as the taxpayer will be able to avail himself of advice and counsel while protected by the cloak of the attorney-client privilege.

A local CPA acquaintance, apparently not yet infected by this epidemic, recently sent me her new client with big-time nondisclosure problems. At the end of our meeting he leaned forward, lowered his voice and asked, “Should my old accountant have told me about these disclosures?”

I leaned forward, lowered my voice and said, “Your former accountant was ill.”

*IRS Circular 230 Disclosure. IRS regulations generally provide that, for the purpose of avoiding federal tax penalties, a taxpayer may rely only on formal written advice meeting specific requirements. Any tax advice in this article does not meet those requirements and is not intended or written to be used, and cannot be used, for the purpose of avoiding federal tax penalties or promoting, marketing or recommending to another party any transaction or matter addressed herein.*