New Regulations Address 1099s for Lawyers' Fees

By Robert W. Wood

Robert Wood explains the new regulations for lawyers to report payments made to them on Form 1099 and the ongoing effort to ensure that attorneys meet their tax obligations.

For the better part of the past decade, the reporting of payments made to attorneys has garnered a fair amount of controversy. Recently, the IRS issued final regulations on this muddled subject, quelling debate and setting forth clarity in a field that seems increasingly known for uncertainty. Yet, it is difficult to discuss these new reporting rules for payments made to attorneys without reviewing a bit of history. The IRS has long been concerned about attorneys meeting their tax obligations, although formal programs to recognize this have not been widely discussed.

At one time, the IRS initiated a program called "Project Esquire," which implicitly recognized that lawyers needed particular tax scrutiny.[1] Moreover, given that lawyers are often involved in handling client moneys, it has occasionally been suggested that they may merit special audits. Independently, the IRS has also long had an interest in the tax treatment of litigation settlements, as well as judgments and lawyers' fees. The confluence of these ostensibly independent concerns coalesces nicely in reporting issues over attorneys' fees.

The mix of tax reporting has ramped up materially over the last several decades, and it often now seems that virtually any payment from anywhere, for anything, must be the subject of a Form 1099. This allows the government to match payee tax reporting with payor information reporting. The digital age allows the IRS to engage in computer matching, and that is something the IRS does well.

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In 1996, Congress took aim at taxpayers, amending Code Sec. 104 to dramatically narrow the scope of that exclusion to cover only "physical" injuries and "physical" sickness. Only a year later, in 1997, Congress changed its focus to the reporting of payments to attorneys. Code Sec. 6045(f) was added to the Code as part of the euphemistically named Taxpayer Relief Act of 1997.[2] Code Sec. 6045(f) generally requires information reporting for payments of gross proceeds made in the course of a trade or business to attorneys in connection with legal services.

Notably, this provision requires reporting whether or not the services are performed for the payor. In other words, there does not need to be an attorney-client relationship between the payor and the lawyer. To avoid needless duplication, though, Code Sec. 6045(f) requires no information reporting for the portion of any payment that is required to be reported under certain other information reporting provisions.

Specifically, Code Sec. 6045(f) obviates reporting to the attorney if the payment is already required to be reported under Code Sec. 6041(a) (dealing with payments made in the course of a trade or business), or under Code Sec. 6051 (relating to receipts for employees) or that would be required to be reported but for the $600 threshold. Significantly, Code Sec. 6045(f) overrides the general exception for reporting of payments to corporations.[3] Thus, the mere fact that the attorney is incorporated (or is part of an incorporated law firm) does not excuse any reporting that is otherwise required.

Fundamentally, Code Sec. 6045(f) requires Form 1099 reporting of monies paid to attorneys. That hardly sounds complicated, difficult or controversial. Yet, the regulatory history of Code Sec. 6045(f)

has been tortured. Proposed regulations under Code Secs. 6045(f) and 6041 were first published on May 21, 1999.[4] After considering practitioner comments and holding a hearing, the IRS and Treasury Department were evidently dissatisfied with their first foray. They went back to the drawing board and issued reproposed regulations on May 17, 2002.[5] Four years later, on July 12, 2006, the IRS adopted final regulations under Code Sec. 6045(f).[6] They generally follow the reproposed regulations, but there are some notable revisions.

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Middleman Regulations

Before embarking on a tour of the newly finalized attorneys' fee reporting regime, it is necessary to take a brief detour to highlight a separate, but parallel, reporting system that has been in place since 2003. The originally proposed Code Sec. 6045(f) regulations were controversial when they were first published in 1999, and on the whole, they remained controversial when revised and republished in 2002. However, at least lawyers could derive some comfort from the fact that these particular proposed regulations were not scheduled to become effective until two months after they were finalized.

Sometimes, though, dangers lurk in unexpected places. Final regulations issued under a *different* Code section in 2002, but effective on January 1, 2003, represented just such a danger.[7] These 2002 final regulations were published under Code Sec. 6041, and they were primarily aimed at escrow agents and others who make payments on behalf of third parties. However, with no fanfare, despite the controversy of attorney fee reporting, the IRS and Treasury Department literally slipped into these regulations much of the attorneys' fee reporting regime that remained so controversial in the two sets of proposed regulations under Code Sec. 6045(f). These final regulations literally are a back-door reporting regime. These regulations are known as the "Middleman" regulations.

Generally speaking, the Middleman regulations provide rules for reporting payments made on behalf of another. They include a rule for the amount a payor must report when a payee takes deductions from the payment.[8] Yet, many lawyers and payors were understandably surprised to find that the Middleman regulations contained reporting rules for payments by and to attorneys and client—payments that have little to do with escrow agents.[9]

Even with the issuance of the final regulations under Code Sec. 6045(f), the Middleman regulations remain in effect. In large part, the two sets of regulations compliment each other and rarely overlap. An overly simplified view of them may be that the new regulations control the reporting of payments *to* attorneys, and the Middleman regulations control the reporting of payments *by* attorneys. Practitioners, however, shouldn't place too much in this generalization. As Mark Twain reputedly said, "all generalizations are false, including this one."[10]

Basic Regulatory Rule

Turning back to the newest final regulations, we need to switch gears from Code Sec. 6041 to Code Sec. 6045(f). Code Sec. 6045(f) requires payors of money to attorneys to issue Forms 1099 to attorneys. The main question is, when this rule can be varied and, more importantly, when the payor must report not only to the lawyer, but to the client as well. This duplicate reporting feature, it turns out, has been the most controversial part of the rules.

The Code's basic mechanism requires that every payor engaged in a trade or business, who, in the course of that trade or business, makes $600 or more in payments during the year to an attorney, file a Form 1099. The rule is explicit that the Form 1099 is required whether or not any portion of the payment will be retained by the attorney.[11] Thus, a Form 1099 is required to be filed even if the lawyer will pay all of the money over to his client and keep nothing for himself.

As in the previously proposed regulations, the real guts of the rule concerns joint and multiple payees. If more than one attorney is listed as a payee on the check, the form must be filed reporting the payment to the payee attorney to whom the check is delivered. That means a check made payable to attorneys A, B and C, jointly, will not necessitate three Forms 1099. Rather, the payor is to issue a

single Form 1099 only to whichever of A, B and C actually *receives* the check.[12]

On the other hand, if there are multiple payees, but the check is delivered to someone who is *not* an attorney, the first named payee *attorney* on the check must receive the form.[13] In some cases, the recipient of the check may actually *not* be a named payee. For example, if two or more attorneys are payees on the check, but the check is delivered to someone who is not a payee, then the first listed payee is to receive the Form 1099.[14]

The final regulations also deal with at least some of the circumstances where attorneys must report payments they make to *other* attorneys. Here, the regulations helpfully use the concept of "tier 1" and "tier 2" attorneys. Suppose that an attorney receives a Form 1099 with respect to a payment made to him. But, the attorney has co-counsel, pays referral fees or otherwise needs to make distributions of some of the moneys represented by the check for which he receives a Form 1099.

Example: Lawyer 1 receives a check for $100,000 in fees and receives a Form 1099 for the same amount. Lawyer 1 owes his co-counsel, Lawyer 2, $40,000. Because Lawyer 1 is required to receive an information return for the $100,000 payment, Lawyer 1 must file a Form 1099 for any payment that he (as the tier 1 attorney) makes to any other (tier 2) payee attorney with respect to that check.[15] Notably, Lawyer 1 must determine his tier 1 status and his Form 1099 filing obligation prior to receiving a Form 1099 from the original payor.

In other words, Lawyer 1's obligation to issue a Form 1099 may hinge in part on whether he *receives* a Form 1099. If he receives a Form 1099 on January 31, can he reasonably also *issue* a Form 1099 to Lawyer 2 the same day? This timing trap could create problems down the road for all sorts of attorney payments.

Exceptions

There are some notable exceptions to the scope of these new attorneys' fee reporting rules. Information returns need not be filed under the authority of Code Sec. 6045(f) with respect to the following types of payments:

- payments of wages or other compensation paid to an attorney by the attorney's employer;
- payments of compensation or profits paid or distributed to its partners by a partnership engaged in providing legal services;
- payments of dividends or corporate earnings and profits paid to its shareholders by a corporation engaged in providing legal services;
- payments made by a person to the extent the person must report the payment to the same payee under certain other provisions (Code Sec. 6041(a) and Reg. § 1.6041-1(a), etc.);
- payments made to a nonresident alien individual, foreign partnership, or foreign corporation that is not engaged in a trade or business in the U.S., and does not perform any labor or personal services in the U.S.;
- payments to an attorney in the attorney's capacity as the person responsible for closing a transaction (as described in Reg. § 1.6045-4(e)(3)) for the sale, exchange or financing of real estate;
- payments to an attorney in the attorney's capacity as a trustee in bankruptcy under Title 11 of the U.S. Code.[16]

Expansion of Exceptions?

The Preamble to the final regulations notes that many of the comments to the proposed regulations were from practitioners who wanted broader exceptions to the reporting rules than those enumerated above. Yet, the IRS notes as a general matter that these reporting rules are meant to be broad and that few exceptions are warranted. For this, the IRS cites the legislative history to Code Sec. 6045(f).[17]

Many of the comments made during the proposed regulation stage concerned situations in which practitioners thought reporting should not be required. Some of these circumstances related to: (a) payments to trustees and other fiduciaries such as administrators of estates and settlement funds; (b) an expanded bankruptcy exception (that would go farther than the one ultimately adopted by the final regulations); and (c) an expanded exception relating to attorneys who conduct settlements for sales or exchanges of real estate, to encompass payments made in connection with refinancing, loan closings, *etc.*

As noted above, the IRS took a dim view of requests to expand the exceptions from reporting. Indeed, the Preamble even notes that one commentator had asked for an exception so that payments of life insurance proceeds made to an attorney on behalf of a client would not be considered received in con-

nection with the performance of legal services. The idea, of course, was to explicitly except such payments from Form 1099 reporting. That seems like a reasonable request.

Yet, the IRS answers this comment by noting that the IRS believes that reporting in this circumstance is required. In fact, the IRS says that a broad definition of legal services is appropriate. The IRS simply notes that, as in the fiduciary situation, information reporting is not required if the attorney is not the named payee of the life insurance.[18]

Nevertheless, there are two places where the final regulations did expand exceptions from reporting. There is a new exception relating to attorneys acting in the capacity of bankruptcy trustees.[19] There is also an expanded exception for attorneys receiving payments made in connection with sales or exchanges of real estate that now also encompasses the financing of real estate.[20]

Duplicate Reporting

Since Code Sec. 6045(f) was enacted and the first set of proposed regulations were promulgated in 1999, there has been a huge outcry concerning the risk of duplicate reporting. The Preamble to the final regulations notes the continuing concern expressed by commentators that duplicate reporting is required. Underlying the complaint is the notion that duplicate reports may subject the same dollar to multiple tax hits. At least some of the duplicate reporting concerns relate to misapprehension over Forms 1099 that report income, versus those that merely report gross proceeds. Many taxpayers are understandably nonplused at the idea that they will be taxed on money also reported to someone else, and even worse, that they may be tagged twice with the same "income."

Even more fundamentally, though, some commentators noted that duplicate reporting can cause administrative problems under automated systems for generating information returns. In many cases, they say, these systems are designed to generate only *one* Form 1099 per payment. Nonetheless, the IRS points out in the Preamble to the final regulations that it was Congress that provided for duplicate reporting by enacting both Code Secs. 6045(f) and 6041. Thus, in situations in which a payment is made to an attorney for the benefit of the client, Code Sec. 6041 requires reporting to the client, while Code Sec. 6045(f) requires reporting to the attorney. According to the IRS, each of these statutory reporting requirements serves an independent purpose.

One silver lining in the final rules is a delayed effective date. Following the gist of the proposed regulations, these final regulations apply to payments made in or after 2007.

For those who still think duplicate reports will gum up their information return systems, the IRS has an answer: You have time to implement the change, since those rules only affect payments that are made after 2006. That means the first payments (made in 2007) for which Forms 1099 are required under these rules will not be due to the taxpayer until January of 2008.

Who is the Payee?

Exactly how a check is made payable can be important when it comes to tax reporting. Yet, there can be questions about who is really the payee. In most cases, of course, this will be clear. The payee will often be one individual or one firm. There may be joint payees, such as "pay to the order of Client A and Attorney B."

However, sometimes there can be confusion, as when a check is made payable to a particular person, but in care of someone else. What if a check is made payable to the client, but "in care of" the attorney? What if a check is payable to the attorney's client trust account?

Regarding the latter situation, the final regulations are clear that the attorney is treated as the payee on a check written to the attorney's client trust account.[21] Sensibly, the regulations hinge on the requirement to issue a Form 1099 on the attorney's ability to negotiate the check. Thus, no Form 1099 to the lawyer would be required if the attorney cannot negotiate it. That would be the case, for example, where the check was made out to the client, but sent in care of the attorney.[22]

Penalties and Effective Dates

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these final regulations apply to payments made in or after 2007. That means the first batch of Forms 1099, to which these new regulations apply (for 2007 payments), will be due in January of 2008.[23]

Interestingly, the Preamble to the final regulations deals with penalties. In one sense, that seems odd, since penalties are imposed under *other* Code sections. Implicitly, the fact that penalties are mentioned should invite some taxpayers to consider the stakes of failures to file. Potential exposure to penalties may even color how one thinks about filing obligations in cases involving close calls. The final regulations note that no penalty relative to information reporting will be imposed with respect to a failure that is due to reasonable cause and not to willful neglect.[24]

But, what is reasonable cause? To show reasonable cause, the putative Form 1099 filer must establish that there are significant mitigating factors with respect to the failure, or that the failure arose from events beyond the filer's control and that the filer acted in a responsible manner.[25] These "significant mitigating factors" can include the fact that, prior to the failure, the filer was never required to file that particular type of return.[26]

Furthermore, "acting in a responsible manner" means that the filer must exercise reasonable care. Reasonable care is the standard of care that a reasonably prudent person would use under the circumstances in the course of its business in determining its filing obligations.[27]

Foreign Issues

There was some controversy over whether the attorney fee reporting rules would apply to payments to certain nonresidents, who are not engaged in a U.S. trade or business, and who do not perform any labor or personal services within the United States. Although the reproposed regulations contained an exception for certain such payments, commentators had suggested that the exception was too narrow. Indeed, one suggestion was that the IRS should allow a payor to rely (in failing to issue a Form 1099) on a signed statement by the attorney or law firm, to the effect that the services for which payment is made were performed outside the United States, as long as the payor does not know that such a statement is inaccurate.

Notwithstanding such commentary, the final regulations take a strict view of foreign reporting issues. The IRS notes in the Preamble that gross proceeds reporting under Code Sec. 6045(f) is intended to be broad. The legislative history to Code Sec. 6045(f) indicated that the IRS is to administer the provision "so that it will not apply to foreign attorneys who can clearly demonstrate that they are not subject to U.S. tax."[28]

Thus, to avoid reporting, foreign persons must demonstrate that the income would not be subject to U.S. tax if the foreign person were engaged in a trade or business within the United States and that the income is not effectively connected with a U.S. trade or business. Given the twin prongs of these rules, the IRS implements broad attorney gross proceeds reporting to foreign attorneys.

Examples

The final regulations contain a number of helpful examples, although some of them may be likely to provoke questions that the regulations do not explicitly answer. With only slight variations, here are the examples that are supposed to elucidate how taxpayers must report under the new regime.

Example 1. One Check–Joint Payees–Taxable To Claimant

> Eric Employee sues his employer for back wages. Eric is represented by Al Attorney. The employer settles for $300,000, and this all represents taxable wages to Eric. The employer writes a settlement check payable jointly to Eric and Al in the amount of $200,000, which is the full $300,000 settlement net of income and FICA tax withholding. The employer delivers this check to Al, who retains $100,000 of the payment as compensation for his legal services, and disburses the remaining $100,000 to Eric. The employer must file a 1099 with respect to Al for $200,000. The employer must also file an information return with respect to Eric under Code Secs. 6041 and 6051 (a Form W-2), in the amount of $300,000.[29]

This example raises some difficult problems. As it is stated, the $300,000 settlement represents wages to Eric. The example uses a single check with joint payees. Although its focus is on the attorneys' fee reporting, it states (as an assumption) that the employer is going to withhold on the *full* $300,000.

In my experience, even in cases like that posited in the example (that is, cases where 100 percent of the recovery constitutes wages), most employers will not

withhold on the attorneys' fees portion of the settlement. Of course, that generally is accomplished not by a joint check, but rather by one check for wages (in this case, payable solely to Eric) and a second check payable solely to the attorney (here, Al).

The difficult but not explicitly raised question on these facts is how this example would change if separate checks were issued to Eric Employee and Al Attorney, instead of a single check. The point of the example is that reporting is required on the attorneys' fees and on the wages, provided that the attorneys' fees are paid out of wages. This may sound like splitting hairs, but it may be simple enough to have a settlement agreement provide that attorneys' fees are not paid out of wages. In any event, if two checks were cut (one to Eric for $200,000 of wages and one to Al for $100,000 of attorneys' fees), taxpayers could certainly posture themselves so that the proper result would be that appropriate wage withholding should only be taken on the $200,000 check to Eric, and a Form W-2 should only be issued to Eric.

Under Code Sec. 6045(f) reporting, if a separate $100,000 check is cut by the employer to Al, there would be a separate Form 1099 for that check. Arguably, since the attorneys' fees represent gross income to Eric as well as to Al Attorney, there should be a duplicate Form 1099 for $100,000 sent to Eric. That means Eric would receive a Form W-2 for $200,000 (showing the withholding), plus a Form 1099 for the $100,000 of lawyers' fees. Al would receive a duplicate Form 1099 for $100,000.

An interesting conundrum here is whether there should be withholding on the money paid to the lawyer. It may depend on the procedural aspects of any court order or the language contained in a settlement agreement.[30] If the full settlement truly represents wages, perhaps theoretically there should be. Yet, I don't think most employers would withhold on this amount.

Example 2. One Check–Joint Payees–Excludable To Claimant

Harry Hurt, who sues Big Defendant corporation for damages on account of personal physical injuries, is represented by Larry Lawyer. Big Defendant settles the suit for a $300,000 damage payment that is excludable from Harry's gross income under Code Sec. 104(a)(2). Big Defendant writes a $300,000 settlement check payable jointly to Harry and Larry, and delivers the check to Larry Lawyer. Larry retains $120,000 of the payment as compensation for legal services, and remits the remaining $180,000 to Harry Hurt. Big Defendant must file an information return with respect to Larry Lawyer for $300,000. Big Defendant is not required to file an information return with respect to tax-free damages paid to Harry.

This is an important example, if for no other reason than it confirms that when a payment is made that is excludable under Code Sec. 104, no Form 1099 should be sent to the client. The instructions to Form 1099-MISC say this,[31] but I've had endless debates with defendants about the point.

Secondly, this example is important in showing that a joint check may not be the thing of the future for lawyers. Traditionally, plaintiffs' lawyers always wanted joint checks in resolution of cases because it was a way of maintaining control over 100 percent of the case proceeds. The lawyer would traditionally have the client endorse the check so funds could be deposited in the client trust account. Then, the lawyer would disperse the client's share to the client. Absolute control.

Here, though, this example shows that having a joint check results in the lawyer receiving a Form 1099 for the full $300,000. If, instead, there had been two checks (one to the client for $180,000, and one to the lawyer for $120,000), the lawyer would receive only a Form 1099 for $120,000. However, the conclusion of the example, with respect to the Code Sec. 104 payment, would still ring true. The client would not receive any Form 1099.

Whether the lawyer cares that he receives a Form 1099 for $120,000 or $300,000 may depend in part on the lawyer's handling of other cases, the lawyer's confidence that there is truly a difference between a "gross proceeds" Form 1099 and an "income" Form 1099, and conceivably other factors. Most lawyers, however, will probably prefer to receive a Form 1099 only for their *own* fees, not the total gross proceeds of the case.

Example 3. Separate Checks–Taxable to Claimant

Cathy Claimant, an individual plaintiff in a suit for lost profits against Payor Corporation, is represented by Alice Attorney. Payor settles the suit for $300,000, all of which will be includible in Claimant's gross income. Alice requests Payor to write two checks, one payable to Alice in the

amount of $100,000 as compensation for legal services, and the other payable to Claimant in the amount of $200,000. Payor writes the checks in accordance with Alice Attorney's instructions and delivers both checks to Alice. Payor must file an information return with respect to Alice Attorney for $100,000. Payor must also file an information return with respect to Claimant for the $300,000.

This example is slightly different from Example 2, both in the sense that separate checks are issued, and because the proceeds are taxable income, rather than excludable under Code Sec. 104. The point of this example is simply that writing two checks will limit the amount included on the Form 1099 issued to the lawyer. It will not, however, impact the amount included on the Form 1099 issued to the client. The client here receives a Form 1099 for the full $300,000. The lawyer only receives a Form 1099 for the $100,000 check he receives.

Example 4. Check Made Payable to Claimant, But Delivered to Nonpayee Attorney

Payor Corporation is a defendant in a suit for damages, in which Paul Plaintiff has been represented by Albert Attorney throughout the proceeding. Payor settles the suit for $300,000. Pursuant to a request by Albert, Payor writes the $300,000 settlement check payable solely to Paul Plaintiff and delivers it to Albert Attorney at Albert's office. Payor is not required to file an information return with respect to Albert Attorney because there is no payment to an attorney. Albert Attorney cannot negotiate the check.

I don't know how frequently this scenario occurs in real life. Yet, the point of this example is to illustrate variance between the payee of a check and its delivery recipient. The mere fact that a check is delivered to an attorney does not mean that the check has been "paid" to the attorney.

Example 5. Multiple Attorneys Listed as Payees

Payor Corporation, a defendant, settles a lost profits suit brought by Ivan Investor, for $300,000, by issuing a check naming Ivan's attorneys, A, B and C, as payees in that order. A, B and C do not belong to the same law firm. Payor delivers the payment to A's office. A deposits the check proceeds into a trust account and makes payments by separate checks to B, for $30,000, and to C, for $15,000, as compensation for legal services, pursuant to authorization from Ivan to pay these amounts. A also makes a payment by check of $155,000 to Ivan. A retains $100,000 as compensation for legal services. Payor must file an information return for $300,000 with respect to A. A, in turn, must file information returns with respect to B, for $30,000, and to C, for $15,000, (A is not required to file information returns under Code Sec. 6041 with respect to A's payments to B and to C because A's role in making the payments to B and to C is merely ministerial).[32] As described in Example 3, Payor must also file an information return with respect to Ivan.[33]

As with the prior example, I don't think the problem of multiple payee attorneys occurs all that frequently. The main point is to illustrate the duty of the payee attorney to file Forms 1099 with respect to the various payees to whom he or she cuts checks. Many attorneys will find this to be a new practice, since in my experience, many attorneys are notoriously bad about issuing Forms 1099.

Example 6. Amount of the Payment–Attorney Does Not Provide TIN

(1) Payor Corporation, a defendant, settles a suit brought by Clyde Claimant for $300,000. Payor will pay the damages by a joint check to Clyde and his attorney, Al. Al failed to furnish Payor with his (or his law firm's) TIN. Payor is therefore required to deduct and withhold 28-percent tax from the $300,000 under Code Sec. 3406(a)(1)(A) and Reg. §1.6045-5(e). Payor writes the check to Clyde and Al Attorney as joint payees, in the amount of $216,000. Payor must file an information return with respect to Al Attorney in the amount of $300,000. If the damages are reportable under Code Sec. 6041 because they are not excludable from gross income under existing legal principles and are not subject to any exception under Code Sec. 6041, Payor must also file an information return with respect to Clyde in the amount of $300,000.[34]

(2) Rather than paying by joint check to Clyde Claimant and Al Attorney, Payor will pay the damages by a joint check to Clyde Claimant and Big Firm, Al's law firm. Unfortunately, Big Firm failed to furnish its TIN to Payor. Thus, Payor is required to deduct and withhold 28-percent tax from the $300,000 under Code Sec. 3406(a)(1)(A) and Reg. §1.6045-5(e). Payor writes the check to Clyde and Big Firm, as joint payees, in the amount of $216,000. Payor must file an information return with respect to Big Firm in the amount of $300,000. If the damages are reportable under Code Sec. 6041 because they are not excludable from gross income under existing legal principles and are not subject to any exception under Code Sec. 6041, Payor must also file an information return, with respect to Clyde Claimant, in the amount of $300,000.[35]

This lengthy example should tell lawyers that failing to provide a taxpayer identification number may be disastrous. I do not believe this occurs frequently, but I do think that law firms are sometimes reluctant to provide taxpayer identification numbers on the theory that somehow they will be "tagged" with income.

Conclusion

The newly issued final regulations concerning the reporting of payments made to attorneys provide a plethora of new rules. Although the IRS probably hoped that these regulations would be the link that completed the Form 1099 chain, some questions remain unanswered. Moreover, these regulations appear to elevate form over substance. In an era in which the IRS and the Treasury have made clear that they think substance-over-form principles should be given significant weight, this seems a bit odd.

Perhaps it is not surprising that different reporting requirements arise, depending on who actually receives checks. This may give practitioners more control in effectuating settlements than anticipated. Yet, I see the real test and traps may be likely to arise from the interaction of these regulations with the Middleman regulations, especially since the Middleman regulations are filled with rules that are arguably subject to interpretation.[36] Perhaps such ambiguity is the genesis for the IRS including details of penalty relief in the Preamble. Needless to say, practitioners should tread carefully in this complex web of ever-changing reporting rules.

Endnotes

1 The IRS undertook Project Esquire during the 1990s to identify attorneys who failed to file federal income tax returns. Although most were given the opportunity to pay their taxes, some were criminally indicted. *See Attorney Nonfilers Still Targets in Service's Project Esquire*, 95 TNT 52-7 (March 16, 1995).

2 Taxpayer Relief Act of 1997 (P.L. 105-34).

3 *See* Reg. § 1.6041-3(p)(1).

4 64 Fed. Reg. 27730.

5 67 Fed. Reg. 35064.

6 T.D. 9270 (July 12, 2006).

7 T.D. 9010 (July 26, 2002).

8 Reg. §1.6041-1(f).

9 *See* Robert W. Wood, *The New (Final!) Form 1099 Reporting Regs: Attorneys' Fees Regs in Drag?*, 97 TAX NOTES 265 (2002).

10 There seems to be some dispute about this, with some sources attributing the quote to Voltaire. Perhaps both authors would have appreciated the irony of the generalization that Twain said it.

11 Reg. §1.6045-5(a)(1)(i).

12 Reg. §1.6045-5(b)(1)(i).

13 Reg. §1.6045-5(b)(1)(ii).

14 Reg. §1.6045-5(b)(1)(iii).

15 Reg. §1.6045-5(b)(2).

16 *See* Reg. §1.6045-5(c)(1)–(7).

17 *See* H.R. 105-220, at p. 546 (1997).

18 *See* Preamble of T.D. 9270, IRB 2006-33, 237.

19 Reg. §1.6045-5(c)(7).

20 Reg. §1.6045-5(c)(6).

21 *See* Reg. §1.6045-5(d)(4).

22 *See* Reg. §1.6045-5(d)(4).

23 Under normal information reporting rules, the Forms 1099 are due to the taxpayer by January 31 of the year following payment, and due to the IRS by February 28. *See* Code Sec. 6045(b) and Reg. §1.6045-1(j). For analogous rules under the Middleman Regulations, *see* Code Sec. 6041(d) and Reg. §1.6041-6.

24 Code Sec. 6724(a).

25 Reg. §301.6724-1(a).

26 Reg. §1.301.6724-1(b)(1).

27 Reg. §301.6424-1(d)(1)(i).

28 *See* Joint Committee on Taxation, *General Explanation of Tax Legislation enacted in 1997*, 105th Congress, First Session, p. 215 (1997).

29 *See* §§1.6041-1(f) and 1.6041-2.

30 *See* LTR 200244004 (June 19, 2002).

31 *See www.irs.gov/pub/irs-pdf/i1099msc.pdf,* at page 4.

32 *See* Reg. §1.6041-1(e)(1), (e)(2) and (e)(5) Example 7 for information reporting requirements with respect to A's payments to B and C.

33 Reg. §1.6041-1(a) and (f).

34 Reg. §1.6041-1(a) and (f).

35 Reg. §1.6041-1(a) and (f).

36 *See supra*, note 9.