

## 11 Tax Myths About IRS Form 1099

by Robert W. Wood



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In this article, Wood debunks some common myths about Form 1099, emphasizing its importance to both the IRS and taxpayers.

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Does anyone really like receiving an IRS Form 1099? Probably not, because it says that you received a payment — one you may have forgotten about or spent. A 1099 reminds you that you have to pay tax. If you're in business you probably don't especially like sending out the forms, either. Of course, many systems are automated, so if you are in business, you may not be bothered much by the process. Even so, sending out Forms 1099 is an administrative burden.

The forms may also prompt calls and complaints from recipients saying the information is wrong, they didn't receive the payments, the form should not have been issued for *this* kind of payment, and so on. Millions of Forms 1099 are sent out every year. The IRS relies on them heavily because they allow agency computers to easily keep tabs on the many millions of payments made to taxpayers.

Even though the IRS audits less than 1 percent of all individual tax returns, it matches nearly all Forms 1099 against Forms 1040, sending automated notices to pay up. Yet despite the

forms' importance, there are many myths about them.

### **Myth no. 1: You need a Form 1099 so you should request it.**

Actually, you don't need the form if you know about a payment. But it is surprising how many people ask for Forms 1099. Whether the form is reporting independent contractor pay, a legal settlement, or something else, if you know about the payment, you don't need the form. There is no mismatch on your tax return if you report a payment but didn't receive a Form 1099. Only the reverse is a problem.

Of course, keeping payers advised of your current address is a good idea, as is reporting errors to payers. But that's when I'd stop. If you don't receive a Form 1099 that you expect, don't ask for it. If you are expecting a Form 1099, you know about the income, so just report that amount on your tax return. The IRS computers have no problem with that.

Besides, in my experience, if you call or write the payer and raise the issue, you may be buying trouble. The payer may issue the 1099 incorrectly or you may end up with two of them, one issued in the ordinary course (even if it never got to you) and one issued because you called. The IRS computer might end up thinking you had twice the income you really did.

### **Myth no. 2: Every payment triggers a Form 1099.**

No, but it can sometimes seem like that. The basic Form 1099 rule is that each person engaged in business and making a payment of \$600 or more for services must report it on a Form 1099. The rule is cumulative, so while one payment of \$500 won't trigger the rule, two payments of \$500 to a single payee during the year require a Form 1099 for the full \$1,000.

Generally, businesses must issue the forms to any payee (other than a corporation) that receives \$600 or more during the year. And that's just the basic threshold rule; there are many exceptions. That's why you probably get a Form 1099 for every bank account you have, even if you earned only \$10 of interest income.

**Myth no. 3: All Forms 1099 are the same.**

No, there are many varieties of 1099. There's a 1099-INT for interest; 1099-DIV for dividends; 1099-G for state and local tax refunds and unemployment benefits; 1099-R for pensions and payouts from your individual retirement accounts; 1099-B for broker transactions and barter exchanges; 1099-S for real estate transactions, etc. In fact, there's a dizzying array. There are many categories, but the Form 1099-MISC (for miscellaneous) seems to prompt the most questions and covers the biggest territory. And the newest 1099 is Form 1099-NEC for payments to independent contractors.

**Myth no. 4: Reporting errors on Forms 1099 is a waste of time.**

Not at all. Reporting errors is wise, so don't just put arriving 1099s in a pile. Open them immediately. Suppose you get a 1099-MISC reporting \$8,000 of pay when you know you received only \$800? Tell the payer immediately. There may be time for the payer to correct it before sending the form to the IRS. If the payer has already dispatched the incorrect 1099 to the IRS, ask the payer to send in a corrected form.

There's a special box on the form to show it is correcting a prior 1099 — so the IRS doesn't just add the amounts together. The corrected form cancels the first one. Even if the payer doesn't fix it for you, keep a copy of your correspondence. It might help you convince the IRS you got only \$800.

**Myth no. 5: It doesn't matter if you get Form 1099-Misc or 1099-NEC.**

Actually, it matters a lot. For payments in 2020 and later years the IRS has a special form for independent contractors. Maybe the gig economy finally got to the IRS. New Form 1099-NEC is specifically for paying independent contractors. Starting in 2020, payers should not use Form 1099-MISC for that purpose: They should use Form 1099-NEC instead. The NEC form tips off the IRS

that it should get self-employment tax on top of income tax. Self-employment tax is equivalent to both halves of the employer and employee payroll taxes that apply to wages, which are reported on Form W-2.

Self-employment tax can add a whopping 15.3 percent on top of income taxes. That 15.3 percent applies up to the wage base of \$147,000, with a 2.9 percent tax on any excess over the base. There's no limit on that 2.9 percent, even if you earn millions. In short, self-employment tax is nothing to sneeze at.

A Form 1099-MISC is more neutral and just reports income without saying it is subject to self-employment tax. Box 3 of the 1099-MISC is the big one: other income. Before 2020, there were Box 3 and Box 7 for non-employee compensation — but Box 7 was made into its own form, Form 1099-NEC.

**Myth no. 6: Lawyers do not receive Forms 1099.**

Actually, they do. In fact, lawyers are singled out for special treatment. Nearly any payment to a lawyer is supposed to be reported, even if it's all the client's money. Case settlement proceeds count as gross proceeds, too. Say that a lawyer settles a case, with payment to the lawyer's trust account. Even if the lawyer splits 60/40 with the client, the lawyer gets a 1099 for 100 percent.

But lawyers get a break; they have Box 10 on 1099-MISC, "gross proceeds paid to an attorney." It is a special box only for lawyers, and unlike other 1099s, it does not count as income. But apart from the very good deal that gross proceeds reporting is for lawyers, in other ways lawyers are disadvantaged when it comes to Forms 1099. Lawyers receive and send more Forms 1099 than most people, in part because of tax laws that single them out.

Lawyers must issue Forms 1099 to expert witnesses, jury consultants, investigators, and even to co-counsel if the payment is \$600 or more. Moreover, any client paying a law firm more than \$600 in a year as part of the client's business must also issue a Form 1099. It applies to law corporations, too; even though corporations are generally exempt from receiving 1099s.

**Myth no. 7: Your mailing address on Form 1099 doesn't matter.**

Yes and no. It's true that regardless of whether the payer has your correct address, the information will be reported to the IRS (and your state) based on your Social Security number. But you want to see any forms that are issued, and that means by mail, so you have an interest in making sure payers have your correct address. Update your address directly with payers and put a forwarding order in with the U.S. Postal Service if you move. Seeing any forms the IRS sees is important knowledge, so don't miss out.

**Myth no. 8: If a Form 1099 is wrong, you can ignore it.**

Nope, not a good idea. The key to Forms 1099 is the IRS's computerized matching. Every Form 1099 includes the payer's employer identification number and the payee's Social Security (or taxpayer identification) number. The IRS matches the 1099 with the payee's tax return. If you disagree with the information on the form but you can't convince the payer you're right, explain it on your tax return. Suppose you received a \$100,000 payment from your car insurance company to cover medical expenses and pain from the whiplash you suffered in an accident.

A payment for personal physical injuries is excludable from income, and it shouldn't be the subject of a Form 1099. If you haven't succeeded in convincing your insurance company to cancel the 1099, try to explain it on your tax return. There's no perfect solution, but one thing is clear: If you receive a Form 1099, you can't just ignore it, because the IRS won't.

**Myth no. 9: You don't need to report each Form 1099.**

Actually, the reverse is true. No one likes a tax audit, and there are many tales about what will provoke one. This much is clear: If you forget to report the \$300 of interest you earned on a bank account or the \$6,000 consulting payment you received, the IRS will send you a computer-generated letter billing you for the tax due. If it's correct, just pay it. The IRS sends millions of these notices every year. Not many people may be audited, but these notices are low-hanging fruit and the IRS usually collects.

**Myth no. 10: Forms 1099 are always sent in January.**

Not always. Timing is everything, and businesses must indeed send out Forms 1099 on or before January 31 of each year for the prior calendar year. That means you should watch your mailbox carefully at that time of year. But some businesses send a Form 1099 at the same time they send you a check so they won't have to send you a form later.

That means you might receive a Form 1099 at any time of the year. Besides, some companies are late, so don't assume you're off the hook if you don't receive a Form 1099 by March or April. Even May is not unheard of, so keep a lookout for Forms 1099 at all times. When they arrive, open and check them, and then put them in a safe place.

**Myth no. 11: State tax authorities don't receive Forms 1099.**

Actually, your state will also get a copy, just like the IRS. And most states have the same kind of computer matching program as the IRS. That way, your state can spew out an automatic tax bill if you fail to report a Form 1099 on your state tax return. Most states have an income tax and will receive all the same information the IRS does. So if you failed to report a Form 1099 on your federal tax return, your state tax office will probably catch up with it, too.

**Conclusion**

Forms 1099 are a vital part of the IRS's computer matching program and nearly all of us have payments reported in this way. Take these forms seriously. I assure you the IRS does. ■