



letters to the editor

Musings on Reporting and Withholding

To the Editor:

I am writing with a few comments to the excellent article written by Farley Katz, "Reporting and Withholding Rules for Litigation Settlements & Judgments," which appeared in the December 7, 1998 *Tax Notes* (p. 1265). Mr. Katz has done a marvelous job of distilling a huge body of confusing and (as he points out) inadequately documented law concerning reporting. I have only a few observations.

I do not disagree with Mr. Katz that, based on the existing authority, payors should probably follow, to use Mr. Katz's words, a "when in doubt, don't report" principle. However, I don't see too much of this attitude in practice. Indeed, despite the logical case for such a policy that Mr. Katz lays out, I see more concern on the part of reporting issues today than ever before, surely as a result of the reporting requirements contained in the Taxpayer Relief Act of 1997 and, to a lesser extent, to the substantive changes to section 104 enacted in 1996. To support a "when in doubt, don't report" principle, I think Mr. Katz needs to discuss more thoroughly the applicable penalties, which he does turn to briefly at the very end of his article. With the discussion of penalties and indemnity, Mr. Katz's "when in doubt, don't report" policy might be more saleable to payors.

Second, I find that one of the bigger stumbling blocks in practice concerns withholding issues. Although Mr. Katz is correct that the employment tax regulations are quite stringent in their definition of wages, I believe he does not consider the rather substantial volume of case law in which private parties litigate the existence of withholding tax liabilities. This is important, especially since the "to withhold or not to withhold" inquiry has higher penalty stakes than the "to report or not to report" quandary. Perhaps the most famous case in which private parties have litigated the applicability of withholding laws is *Lisec v. United Airlines, Inc.*, 10 Cal. App. 4th 1500 (Cal. Ct. App. 1992), where the court concluded that some of an award might be gross income, but none of it constituted wages and therefore withholding was not appropriate. In my experience, some employers are well aware of the California holding in *Lisec*, and treat California settlements of employment actions differently from settlements in other states. This is just one example of the minefield of withholding obligations, where the stakes are higher than the 1099 reporting issues.

Anyway, such quibblings aside, I found Farley Katz's article to be helpful, covering an area that few have laid out and that virtually all professionals and businesspeople need to know more about.

Very truly yours,

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