

Tax Letter

Tax Scams and Traps

Dear clients and friends,

Early March, the Internal Revenue Service issued its annual tax scams and tax traps announcement (**IR-2012-23**). We believe it is beneficial for our readers to be reminded of these sets of tax scams and Traps. The following are excerpts from the IRS announcement:

Identity Theft

Topping this year's list of Scams is Identity Theft. In response to growing identity theft concerns, the IRS has embarked on a comprehensive strategy that is focused on preventing, detecting and resolving identity theft cases as soon as possible. In addition to the law-enforcement crackdown, the IRS has stepped up its internal reviews to spot false tax returns before tax refunds are issued as well as working to help victims of the identity theft refund schemes. The IRS is increasingly seeing identity thieves looking for ways to use a legitimate taxpayer's identity and personal information to file a tax return and claim a fraudulent refund.

An IRS notice informing a taxpayer that more than one return was filed in the taxpayer's name or that the taxpayer received wages from an unknown employer may be the first tip off the individual receives that he or she has been victimized.

Anyone who believes his or her personal information has been stolen and used for tax purposes should immediately contact the IRS Identity Protection Specialized Unit. For more information, visit the special identity theft page at www.irs.gov/identitytheft.

Phishing

Phishing is a scam typically carried out with the help of unsolicited email or a fake website that poses as a legitimate site to lure in potential victims and prompt them to provide valuable personal and financial information. Armed with this information, a criminal can commit identity theft or financial theft.

If you receive an unsolicited email that appears to be from either the IRS or an organization closely linked to the IRS, such as the Electronic Federal Tax Payment System (EFTPS), report it by sending it to phishing@irs.gov. It is important to keep in mind the IRS does not initiate contact with taxpayers by email to request personal or financial information. This includes any type of electronic communication, such as text messages and social media channels.

Return Preparer Fraud

Questionable return preparers have been known to skim off their clients' refunds, charge inflated fees for return preparation services and attract new clients by promising guaranteed or inflated refunds. Taxpayers should choose carefully when hiring a tax preparer. Federal courts have issued hundreds of injunctions ordering individuals to cease preparing returns, and the Department of Justice has pending complaints against many others. In 2012, every paid preparer needs to have a Preparer Tax ID Number (PTIN) and enter it on the returns he or she prepares.

Hiding Income Offshore

Over the years, numerous individuals have been identified as evading U.S. taxes by hiding income in offshore banks, brokerage accounts or nominee entities, using debit cards, credit cards or wire transfers

to access the funds. Others have employed foreign trusts, employee-leasing schemes, private annuities or insurance plans for the same purpose.

The IRS uses information gained from its investigations to pursue taxpayers with undeclared accounts, as well as the banks and bankers suspected of helping clients hide their assets overseas. The IRS works closely with the Department of Justice to prosecute tax evasion cases.

While there are legitimate reasons for maintaining financial accounts abroad, there are reporting requirements that need to be fulfilled. U.S. taxpayers who maintain such accounts and who do not comply with reporting and disclosure requirements are breaking the law and risk significant penalties and fines, as well as the possibility of criminal prosecution.

The IRS has collected \$3.4 billion so far from people who participated in the 2009 Offshore Voluntary Disclosure (OVDP) Program, reflecting closures of about 95 percent of the cases. On top of that, the IRS has collected an additional \$1 billion from up front payments under the 2011 program. That number will grow as the IRS processes the 2011 cases. Moreover, this OVDP Program will be kept open for an indefinite period until further notice.

Scams Involving Social Security

Flyers and advertisements for free money from the IRS, suggesting that the taxpayer can file a tax return with little or no documentation, have been appearing in communities around the country. These schemes are also often spread by word of mouth as unsuspecting and well-intentioned people tell their friends and relatives. For example, scammers have been known to lure the unsuspecting with promises of non-existent Social Security refunds or rebates. In another situation, a taxpayer may really be due a credit or refund but uses inflated information to complete the return.

False Form 1099 Refund Claims

In this ongoing scam, the perpetrator files a fake information return, such as a Form 1099 Original Issue Discount (OID), to justify a false refund claim on a corresponding tax return. In some cases, individuals have made refund claims based on the bogus Information Returns filed with the IRS. Don't fall prey to people who encourage you to claim deductions or credits to which you are not entitled or willingly allow others to use your information to file false returns. If you are a party to such schemes, you could be liable for financial penalties or even face criminal prosecution.

Abuse of Charitable Organizations and Deductions

IRS examiners continue to uncover the intentional abuse of 501(c)(3) organizations, including arrangements that improperly shield income or assets from taxation and attempts by donors to maintain control over donated assets or the income from donated property. The IRS is investigating schemes that involve the donation of non-cash assets — including situations in which several organizations claim the full value of the same non-cash contribution. Often these donations are highly overvalued or the organization receiving the donation promises that the donor can repurchase the items later at a price set by the donor. The Pension Protection Act of 2006 imposed increased penalties for inaccurate appraisals and set new standards for qualified appraisals.

Misuse of Trusts

For years, unscrupulous promoters have urged taxpayers to transfer assets into trusts. While there are legitimate uses of trusts in tax and estate planning, some highly questionable transactions promise reduction of income subject to tax, deductions for personal expenses and reduced estate or gift taxes. Such trusts rarely deliver the tax benefits promised and are used primarily as a means of avoiding income tax liability and hiding assets from creditors, including the IRS.

NOTE: According to the IRS, Illegal scams can lead to significant penalties and interest and possible criminal prosecution.