



# Form 1099 Information Reporting Requirements as Modified by the Patient Protection and Affordable Care Act

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## Summary

Under § 6041 of the Internal Revenue Code (IRC), persons engaged in a trade or business who make payments totaling at least \$600 to another person in a single year are required to file an information return (typically a Form 1099) with the Internal Revenue Service (IRS) and to provide the payee with a copy. For payments made after December 31, 2011, § 9006 of P.L. 111-148, the Patient Protection and Affordable Care Act (PPACA), expanded the information reporting requirements contained in IRC § 6041. Under the amended provision, most payments to corporations will no longer be exempt from reporting and the types of payments that can trigger the reporting requirement will include gross proceeds and amounts received by a payee in consideration for property.

A payer's failure to file a timely and accurate information return with the IRS can result in monetary fines; criminal sanctions may be applicable where such failure is willful. Payers may also be penalized for failing to provide a timely and accurate copy of an information return to their payees.

In the 111<sup>th</sup> Congress, several bills and amendments have been introduced that would repeal the modifications made to IRC § 6041 by PPACA § 9006. Both versions of the Small Business Paperwork Mandate Elimination Act, S. 3578 and H.R. 5141, would repeal PPACA § 9006 entirely. Similar provisions have also been proposed in Senate amendments to H.R. 5297 and in § 1 of H.R. 5982.

Legislation has also been proposed to require landlords to file information returns for payments made with respect to their rental properties and to increase the penalties for failing to file an information return. The House passed such a provision in H.R. 4849. A provision with similar language was passed by the Senate in its consideration of a different bill, H.R. 4213. However, this language was ultimately struck by a House amendment in the nature of a substitute while resolving differences with the Senate.

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**A**s a general rule, taxpayers are more likely to pay taxes on income if the realization of that income has been communicated to the Internal Revenue Service (IRS). To encourage compliance with tax laws, the Internal Revenue Code (IRC) includes a number of information reporting requirements regarding payments that may result in taxable income for the payee. One such reporting requirement, contained in IRC § 6041(a), applies to certain payments made by persons in the course of a trade or business. Under IRC § 6041(a), if the total amount of payments made to a payee over a year equals at least \$600, the payer is required to file an information return with the IRS providing information identifying the payer, the payee, and the total amounts paid to that payee over the past calendar year. Outside of employment or distributions to beneficiaries of a trust or an estate, the information returns required to be filed under IRC § 6041 are typically versions of Form 1099.<sup>1</sup> A copy of this information return must also be provided to the payee. Although payees may receive copies of information returns, payees are not required to file any information returns under IRC § 6041.<sup>2</sup>

This report discusses the modifications to IRC § 6041 made by § 9006 of the Patient Protection and Affordable Care Act (PPACA) and briefly discusses the penalties that can be imposed on persons that do not comply with these information reporting requirements. Although this report discusses certain aspects of the information reporting requirement in IRC § 6041, it is not intended to be a complete reference regarding the requirements of that provision. Legislation that has been introduced that would either further modify IRC § 6041 or repeal PPACA § 9006 is also briefly discussed.

## Section 9006 of the Patient Protection and Affordable Care Act

For payments made after December 31, 2011, § 9006 of PPACA amended the reporting requirement in IRC § 6041 in two principal ways. First, payments to corporations will no longer be automatically exempt from reporting requirements by virtue of the payee's corporate status, despite existing regulations to the contrary.<sup>3</sup> Second, the types of payments that can trigger the reporting requirement will be expanded to include amounts paid in consideration of property and other gross proceeds.<sup>4</sup> The effect of this amendment is to require those engaged in a trade or business to report a broader range of payments made with respect to a broader range of payees.

The purpose of this amendment appears to be to reduce the "tax gap" because the existence of an information return generally encourages the voluntary reporting of taxable income and may also facilitate the enforcement and collection of taxes on income that is not voluntarily reported.<sup>5</sup>

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<sup>1</sup> Treas. Reg. § 1.6041-1(a)(2).

<sup>2</sup> Payees, like most individuals, are required to report all income, whether reflected on a 1099 or not, on an annual federal income tax return if they have sufficient income to meet or exceed the filing threshold. Internal Revenue Code (IRC) § 6012(a).

<sup>3</sup> I.R.C. § 6041(h), as added by P.L. 111-148 § 9006(a), the Patient Protection and Affordable Care Act (PPACA).

<sup>4</sup> PPACA § 9006(b).

<sup>5</sup> GAO-09-238, *IRS Could Do More to Promote Compliance by Third Parties with Miscellaneous Income Reporting Requirements* (Jan. 2009). The Joint Committee on Tax has estimated that this provision would raise \$17.1 billion between 2012 and 2019. JOINT COMM. ON TAX, *Estimated Revenue Effects Of The Amendment In The Nature Of A Substitute To H.R. 4872, The "Reconciliation Act Of 2010," As Amended, In Combination With The Revenue Effects Of H.R. 3590, The "Patient Protection And Affordable Care Act ('PPACA')," As Passed By The Senate, And Scheduled* (continued...)

Although this provision is intended to raise revenue without increasing taxes, Congress has received significant feedback from constituents who anticipate that the increased reporting will impose an administrative burden on all payers. In particular, some have commented that the impact on small businesses will be significant because their bookkeeping systems may need to be modified to accommodate tracking the aggregate amounts paid to each payee to comply with the new requirements regarding the types of payments and payees that will trigger 1099 reporting. They add that the administrative burden is also anticipated to increase due to the time and expense involved in filing each newly required 1099.<sup>6</sup>

Also potentially affecting the administrative burden on payers is because the \$600 threshold, which triggers the reporting requirement, has remained constant over time, since at least 1954. In contrast, other dollar amounts specified in the IRC have been legislatively increased over time or indexed for inflation. For example, the personal and dependent exemption amounts were \$600 in 1954, but over time have risen to \$3650 for tax year 2010.<sup>7</sup> As the buying power of \$600 decreases, the number of transactions captured may increase as it becomes more likely that minor expenditures will aggregate to at least \$600 and trigger the reporting requirement.

## Payments to Corporations

Although IRC § 6041 did not explicitly exempt payments to corporations from its reporting requirements, such payments were considered exempt under regulations promulgated by the IRS, if payments were made to

[a] corporation [as defined in the IRC] except with respect to payments made to a corporation after December 31, 1997 for attorneys' fees, and except a corporation engaged in providing medical and health care services or engaged in the billing and collecting of payments in respect to the providing of medical and health care services. However, no reporting is required where payment is made to a hospital or extended care facility described in section 501(c)(3) which is exempt from taxation under section 501(a) or to a hospital or extended care facility owned and operated by the United States, a State, the District of Columbia, a possession of the United States, or a political subdivision, agency or instrumentality of any of the foregoing.<sup>8</sup>

PPACA § 9006 adds a new subsection (h) to IRC § 6041. For payments made after December 31, 2011, the new subsection provides that “[n]otwithstanding any regulation prescribed by the Secretary before the date of the enactment of this subsection, for purposes of this section the term “person” includes any corporation that is not an organization exempt from tax under section 501(a).”<sup>9</sup>

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(...continued)

*For Consideration By The House Committee On Rules On March 20, 2010* at 1 (Mar. 20, 2010).

<sup>6</sup> The IRS has estimated the average time needed to complete a single Form 1099-MISC at 16 minutes, although the actual time “will vary depending on individual circumstances.” IRS, *2010 General Instructions for Certain Information Returns* at 15, available at <http://www.irs.gov>. In addition to possible increased costs for paper, envelopes, filing software, and toner or ink, payers may also incur postage expense in providing each payee with the required copy of the 1099.

<sup>7</sup> Rev. Proc. 2009-50.19 (see 26 U.S.C. § 1 note).

<sup>8</sup> Treas. Reg. § 1-6041.3(p)(1).

<sup>9</sup> I.R.C. § 6041(h).

PPACA § 9006 effectively supersedes the IRS regulations. Thus, payments made to corporations after December 31, 2011, will no longer be automatically exempt from information reporting requirements unless the corporation is a tax-exempt entity.

## Amounts in Consideration of Property and Other Gross Proceeds

IRC § 6041(a) specifies a list of payments that can trigger its information reporting requirements. For payments made before January 1, 2012, these include “rent, salaries, wages, premiums, annuities, compensations, remunerations, emoluments, or other fixed or determinable gains, profits, and income.”<sup>10</sup> If the aggregate amount of these payments to a single payee equals \$600 or more, then IRC § 6041(a) requires the payer to report the amount of those payments and the identity of the payee to the IRS.

For payments made after December 31, 2011, PPACA § 9006 amended this list of payments to include “amounts in consideration for property” and other “gross proceeds.”<sup>11</sup> Because of this expansion of the categories of payments that can give rise to the information reporting requirement, reporting will be required for some payments that previously were not subject to reporting. For example, payments for merchandise, telegrams, telephone, freight, and storage have been exempt under IRS regulations.<sup>12</sup> However, those payments may be considered amounts in consideration for property or gross proceeds under the amended IRC § 6041(a) and could potentially be subject to reporting when the amended language goes into effect.

## Procedures and Enforcement

The deadline for filing an information return with the IRS is February 28 of the year following the calendar year in which payments were made, or March 31 if filed electronically. Copies of information returns must be provided to payees no later than January 31 of the year following the calendar year in which the payments were made.

Information returns must accurately identify both the payer and the payee of the payments as well as the total amount paid. The payees are required to provide their names, addresses, and taxpayer identification numbers<sup>13</sup> to payers in order to facilitate information reporting. The information return must include all of these as well as the address and telephone number of the payer. It is the payer’s obligation to request information from the payee, and the payee is required to provide it.<sup>14</sup> The payer may use Form W-9 to request the information from U.S. persons. If the payee does not provide a taxpayer identification number, the payer is generally required to withhold 28% from all subsequent payments due to the payee. A payee is subject to a penalty of \$50 for each failure to provide the correct taxpayer identification number to a payer who has requested it.

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<sup>10</sup> I.R.C. § 6041(a).

<sup>11</sup> P.L. 111-148, § 9006(b). As amended, the language would read: “rent, salaries, wages, *amounts in consideration for property*, premiums, annuities, compensations, remunerations, emoluments, or other *gross proceeds*, fixed or determinable gains, profits, and income.” (emphasis added).

<sup>12</sup> Treas. Reg. § 1.6041-3(c).

<sup>13</sup> For individuals, the taxpayer identification number (TIN) is generally their social security number.

<sup>14</sup> Section 6041(c) of the IRC requires the recipient to provide both name and address upon demand by the person paying the income. IRC § 6109(a)(1) requires the payer to report the TIN of the recipient. IRC § 6109(a)(2) requires the recipient to provide the TIN to the payer.

Both the failure to submit an accurate information return to the IRS and the failure to provide a copy of the information return to the payee are subject to monetary penalties assessed by the IRS. As a unique information return is required with respect to each payee, penalties are assessed on each deficient information return. The penalty for failing to file a correct and timely return with the IRS is \$50 for each defective return not to exceed \$250,000 for a single payer.<sup>15</sup> If the deficiency is corrected within 30 days of the due date, the penalty is reduced to \$15 per return, not to exceed \$75,000. If corrected later than 30 days, but before August 1, the penalty is \$30 per return, not to exceed \$150,000.<sup>16</sup> No penalty will be assessed against a person if defects are corrected by August 1, and the total number defective returns does not exceed the greater of 10 or one-half percent of the total number of information returns required to be filed by the person.

Some small businesses may be able to take advantage of reduced ceilings on aggregate penalties for payers with gross receipts of less than \$5,000,000. For these payers, the ceilings are \$100,000 (for uncorrected violations), \$25,000 (if corrected within 30 days), and \$50,000 (if corrected after 30 days, but on or before August 1). Higher penalties may also be assessed where persons intentionally disregard their duty to file an information return.

Failure to provide a correct and timely statement to a payee is also subject to a \$50 penalty per return, not to exceed \$100,000 per payer. Higher penalties may also be assessed where persons intentionally disregard their duty to provide a payee with a copy of an information return.

It is a misdemeanor for any person to willfully fail to make an information return as required by law.<sup>17</sup> Persons convicted of this offense may be punished by a fine of up to \$25,000, imprisonment for up to one year, or both. A willful violation occurs when there is “a voluntary, intentional violation of a known legal duty.”<sup>18</sup> However, a violation that results from a good-faith misunderstanding of the requirements of the IRC is not a willful violation, as that term has been interpreted by the courts.<sup>19</sup>

## Proposed Legislation Affecting Information Returns

In the 111<sup>th</sup> Congress, legislation has been introduced in both houses to repeal PPACA § 9006. At the same time, other legislation has been introduced that would further expand the reach of IRC § 6041 by making those who receive rents from real estate subject to the reporting requirements.

### Repeal of PPACA § 9006

Several bills and amendments have been introduced that would repeal the amendments made to IRC § 6041 by PPACA. The Small Business Paperwork Mandate Elimination Act, S. 3578 and H.R. 5141, would repeal PPACA § 9006. Similar language was proposed in amendments to H.R. 5297,<sup>20</sup> and in § 1 of H.R. 5982.<sup>21</sup>

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<sup>15</sup> I.R.C. § 6721(a)(1).

<sup>16</sup> I.R.C. § 6721(b).

<sup>17</sup> I.R.C. § 7203.

<sup>18</sup> *Cheek v. U.S.*, 498 U.S. 192, 200 (1991).

<sup>19</sup> *Id.* at 202.

<sup>20</sup> S.Amdt. 4455, S.Amdt. 4513, and S.Amdt. 4531.



## Extension to Landlords

Generally, those who make real estate available for rental are not considered engaged in a trade or business so long as the average rental period is at least 30 days. Because IRC § 6041 only imposes a reporting requirement when payments are made in the course of a trade or business, landlords generally have not been required to provide 1099s for payments made for expenses for their rental real estate properties. H.R. 4849, the Small Business and Infrastructure Jobs Tax Act of 2010, was passed by the House on March 24, 2010. Two days later, it was referred to the Senate Committee on Finance. Section 304(a) of the bill proposed amending IRC § 6041 to add new subsection (h), which reads, “For purposes of subsection (a), a person receiving rental income from real estate (other than a qualified residence) shall be considered to be engaged in a trade or business of renting property.” Subsection (a) is the part of IRC § 6041 that generally requires reporting of income. The bill provides an exclusion for the rental of one’s principal residence and one other residence (such as a vacation home or second home); therefore, those who rent out their principal residence while trying to sell it or rent out their second home when they are not using it would not be considered to be engaged in a trade or business for purposes of the information reporting requirements of IRC § 6041(a).

Although H.R. 4849 has not yet been voted on by the Senate, the Senate has passed a provision similar to that in H.R. 4849. On March 10, 2010, the Senate passed H.R. 4213 with an amendment in the form of a substitution that included a provision that would have treated landlords as engaged in a trade or business for purposes of IRC § 6041(a).<sup>22</sup> The bill included an exception for those whose rental income was derived from renting their principal residence on a temporary basis. It did not explicitly provide an exception for those who rented out a second home. Instead, there was an exception for an individual receiving “rental income of not more than the minimal amount, as determined under regulations prescribed by the Secretary.”<sup>23</sup> When the bill returned to the House, the House passed its own substitute amendment, which did not include the provision to treat landlords as being engaged in a trade or business.<sup>24</sup>

## Increased Penalties

Both H.R. 4849<sup>25</sup> and H.R. 4213<sup>26</sup> as first passed by the Senate included provisions to increase the penalties for failure to file correct information returns with the IRS. Each provision would increase the penalty for each incorrect (or unfiled) return as well as increasing the maximum penalty that could be assessed to one payer. An inflation adjustment was also proposed that would allow for adjustment of all dollar amounts in IRC § 6721. Neither bill would increase the penalty assessed for failure to provide a correct and timely copy of the information return to the payee.

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<sup>21</sup> On July 30, 2010, the House unsuccessfully attempted to pass H.R. 5982 under suspension of the rules.

<sup>22</sup> H.R. 4213 § 603 (Engrossed Amendment Senate (hereinafter “EAS”)).

<sup>23</sup> H.R. 4213 § 603 (EAS) in proposed paragraph (2)(B).

<sup>24</sup> H.R. 4213 was passed by both houses of Congress in July 2010 as the Unemployment Compensation Extension Act of 2010—P.L. 111-205. Most of the provisions included in earlier versions of the bill were not included in the enrolled bill.

<sup>25</sup> H.R. 4840 § 308.

<sup>26</sup> H.R. 4213 § 605 (EAS).



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