

IRS' DIRTY DOZEN

By Reg P. Wydeven
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In 1967, *The Dirty Dozen* was released, establishing what many Hollywood critics cite as the blueprint for today's action movies. Lee Marvin stars as an army major responsible for training a squad of army criminals made up of an all-star cast including Charles Bronson, Donald Sutherland, Telly Savalas, George Kennedy, Ernest Borgnine, and Jim Brown. In exchange for being pardoned, the soldiers must complete a suicide mission that parachutes them into Nazi-occupied France.

Although not all of the soldiers survive, the mission is a success and the movie has a relatively happy ending. Each year, the IRS unveils its own "Dirty Dozen" list of tax scams, however, taxpayers who encounter one of these twelve typically don't have a happy ending.

For 2005, the IRS's Dirty Dozen includes the following:

- 1. Trust Misuse.** Many scam artists encourage taxpayers to transfer their assets into trusts they sell to reduce income tax, take deductions for personal expenses, or reduce estate or gift taxes. Many of these trusts, however, do not deliver the promised tax benefits.
- 2. Frivolous Arguments.** Some income tax urban legends include the following myths: the 16th Amendment, concerning congressional power to collect income taxes, was never ratified; wages are not income; filing a return and paying taxes are voluntary; and being required to file Form 1040 violates the 5th Amendment right against self-incrimination or the 4th Amendment right to privacy.
- 3. Return Preparer Fraud.** Many tax preparers attract new clients by promising large refunds. Some then skim fees off improperly taken refunds and overcharge for preparing the return.
- 4. Credit Counseling Agencies.** The IRS aggressively audits these organizations, which are intended to provide education to low-income customers with debt problems, because many charge large fees while providing little or no counseling.
- 5. "Claim of Right" Doctrine.** In this scheme, taxpayers are advised to file a return and incorrectly take a deduction equal to the entire amount of their wages as "a necessary expense for the production of income."
- 6. "No Gain" Deduction.** Similarly, taxpayers using this scheme attempt to eliminate their entire adjusted gross income (AGI) by deducting it on Schedule A under "Other Miscellaneous Deductions," claiming there was "No Gain Realized."
- 7. Corporation Sole.** Promoters of this scheme advise their clients to improperly claim they are a "bishop" or "overseer" of a one-person, phony religious organization or society, entitling them to exemption from federal income taxes as a nonprofit, religious organization.
- 8. Identity Theft.** Taxpayers have been defrauded by schemes where scam artists send bank customers fictitious correspondence and IRS forms in an attempt to trick them into disclosing their personal financial data. Similarly, some scammers pose as the IRS itself and send emails to taxpayers informing them they are "under audit" and can set matters right by divulging sensitive financial information on an official-looking Web site.
- 9. Abuse of Charitable Organizations and Deductions.** Some taxpayers move assets or income to a tax-exempt charity but maintain control over the assets or income, then incorrectly take a tax deduction without actually 'transferring' the benefit to the charity.
- 10. Offshore Transactions.** Many taxpayers illegally hide income in offshore bank and brokerage accounts.

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11. Zero Return. Taxpayers are instructed to enter all zeros on their tax return.

12. Employment Tax Evasion. Employers are instructed not to withhold federal income tax or other employment taxes from their employees' wages, based on an incorrect interpretation of §861 of the Internal Revenue Code.

If you are wary of a potential tax scam, the IRS has some great advice: if it sounds too good to be true, it probably is.