

Phishing Scams, Frivolous Arguments Top the 2008 "Dirty Dozen" Tax Scams

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Podcast: 2008 Dirty Dozen

WASHINGTON — The Internal Revenue Service today issued its 2008 list of the 12 most egregious tax schemes and scams, highlighted by Internet phishing scams and several frivolous tax arguments.

Topping this year's list of scams is phishing, which encompasses numerous Internet-based ploys to steal financial information from taxpayers. New to the "Dirty Dozen" this year is a scheme, which IRS auditors discovered, that relates to unreasonable and/or excessive fuel tax credit claims.

"Taxpayers should be wary of scams and promises to avoid paying taxes that seem too good to be true," Acting IRS Commissioner Linda Stiff said. "There is no secret formula that can eliminate a person's tax obligations. People should be wary of anyone peddling any of these scams."

Tax schemes can lead to problems for both scam artists and taxpayers. Tax return preparers and promoters also risk significant penalties, interest and possible criminal prosecution.

The IRS urges taxpayers to avoid these common schemes:

1. Phishing

Phishing is a tactic used by Internet-based thieves to trick unsuspecting victims into revealing personal information they can then use to access the victims' financial accounts. These criminals use the information obtained to empty the victims' bank accounts, run up credit card charges and apply for loans or credit in the victims' names. Phishing scams often take the form of an e-mail that appears to come from a legitimate source. Some scam e-mails falsely claim to come from the IRS. To date, taxpayers have forwarded more than 33,000 of these scam e-mails, reflecting more than 1,500 different schemes, to the IRS. The IRS never uses e-mail to contact taxpayers about their tax issues. Taxpayers who receive unsolicited e-mail that claims to be from the IRS can forward the message to a special electronic mailbox, phishing@irs.gov, using instructions contained in an article titled "How to Protect Yourself from Suspicious E-Mails or Phishing Schemes." Remember: the only official IRS Web site is located at www.irs.gov.

2. Scams Related to the Economic Stimulus Payment

Some scam artists are trying to trick individuals into revealing personal financial information that can be used to access their financial accounts by making promises relating to the economic stimulus payment, often called a "rebate." To obtain the payment, eligible individuals in most cases will not have to do anything more than file a 2007 federal tax return. But some criminals posing as IRS representatives are trying to trick taxpayers into revealing their personal financial information by falsely telling them they must provide information to get a payment. For instance, a potential victim is told by phone or e-mail that he or she is eligible for a rebate but must provide a bank account number (or similar information) to get the payment. If the target is unwilling, the victim is then told that he cannot receive the rebate unless the information is provided. Individuals should remember that the only way to get a stimulus payment is to file a 2007 tax return. The IRS urges taxpayers to be extra-vigilant. The IRS will not contact taxpayers by phone or e-mail about their stimulus payment.

3. Frivolous Arguments

Promoters of frivolous schemes encourage people to make unreasonable and unfounded claims to avoid paying the taxes they owe. Most recently, the IRS expanded its list of frivolous legal positions that taxpayers should stay away from. Taxpayers who file a tax return or make a submission based on one of these positions on the list are subject to a \$5,000 penalty. The most recent update of the list of frivolous positions includes: misinterpretation of the 9th Amendment to the U.S. Constitution regarding objections to

military spending, erroneous claims that taxes are owed only by persons with a fiduciary relationship to the United States, a nonexistent "Mariner's Tax Deduction" related to invalid deductions for meals and the misuse of the fuel tax credit (see below). The complete list of frivolous arguments is on the IRS Web site at IRS.gov.

4. Fuel Tax Credit Scams

The IRS is receiving claims for the fuel tax credit that are unreasonable. Some taxpayers, such as farmers who use fuel for off-highway business purposes, may be eligible for the fuel tax credit. But some individuals are claiming the tax credit for nontaxable uses of fuel when their occupation or income level makes the claim unreasonable. Fraud involving the fuel tax credit was recently added to the list of frivolous tax claims, potentially subjecting those who improperly claim the credit to a \$5,000 penalty.

5. Hiding Income Offshore

Individuals continue to try to avoid paying U.S. taxes by illegally hiding income in offshore bank and brokerage accounts or using offshore debit cards, credit cards, wire transfers, foreign trusts, employee leasing schemes, private annuities or life insurance plans. The IRS and the tax agencies of U.S. states and possessions continue to aggressively pursue taxpayers and promoters involved in such abusive transactions.

6. Abusive Retirement Plans

The IRS continues to uncover abuses in retirement plan arrangements, including Roth Individual Retirement Arrangements (IRAs). The IRS is looking for transactions that taxpayers are using to avoid the limitations on contributions to Roth IRAs. Taxpayers should be wary of advisers who encourage them to shift appreciated assets into Roth IRAs or companies owned by their Roth IRAs at less than fair market value. In one variation of the scheme, a promoter has the taxpayer move a highly appreciated asset into a Roth IRA at cost value, which is below annual contribution limits even though the fair market value far exceeds the amount allowed.

7. Zero Wages

Filing a phony wage- or income-related information return to replace a legitimate information return has been used as an illegal method to lower the amount of taxes owed. Typically, a Form 4852 (Substitute Form W-2) or a "corrected" Form 1099 is used as a way to improperly reduce taxable income to zero. The taxpayer also may submit a statement rebutting wages and taxes reported by a payer to the IRS. Sometimes fraudsters even include an explanation on their Form 4852 that cites statutory language on the definition of wages or may include some reference to a paying company that refuses to issue a corrected Form W-2 for fear of IRS retaliation. Taxpayers should resist any temptation to participate in any of the variations of this scheme.

8. False Claims for Refund and Requests for Abatement

This scam involves a request for abatement of previously assessed tax using Form 843, "Claim for Refund and Request for Abatement." Many individuals who try this have not previously filed tax returns. The tax they are trying to have abated has been assessed by the IRS through the Substitute for Return Program. The filer uses Form 843 to list reasons for the request. Often, one of the reasons given is "Failed to properly compute and/or calculate Section 83-Property Transferred in Connection with Performance of Service."

9. Return Preparer Fraud

Dishonest tax return preparers can cause many problems for taxpayers who fall victim to their schemes. These scam artists make their money by skimming a portion of their clients' refunds and charging inflated fees for return preparation services. They attract new clients by promising large refunds. Some preparers promote the filing of fraudulent claims for refunds on items such as fuel tax credits to recover taxes paid in prior years. Taxpayers should choose carefully when hiring a tax preparer, especially one who promises something that seems too good to be true.

10. Disguised Corporate Ownership

Some people are going as far as forming domestic shell corporations in certain states for the purpose of disguising the ownership of a business or financial activity. Once formed, these anonymous entities can be used to facilitate underreporting of income, non-filing of tax

returns, engaging in listed transactions, money laundering, financial crimes and even terrorist financing. The IRS is working with state authorities to identify these entities and to bring the owners of these entities into compliance.

11. Misuse of Trusts

For years, unscrupulous promoters have urged taxpayers to transfer assets into trusts. They promise reduction of income subject to tax, deductions for personal expenses and reduced estate or gift taxes. However, some trusts do not deliver the promised tax benefits. As with other arrangements, taxpayers should seek the advice of a trusted professional before entering into a trust.

12. Abuse of Charitable Organizations and Deductions

The IRS continues to observe the misuse of tax-exempt organizations. Misuse includes arrangements to improperly shield income or assets from taxation, attempts by donors to maintain control over donated assets or income from donated property and overvaluation of contributed property. In addition, IRS examiners are seeing an upturn in instances where taxpayers try to disguise private tuition payments as contributions to charitable or religious organizations.

IRS Watches Scams That Fall Off the List

While the IRS has seen a decline in the occurrence of some of these scams, other problems, such as abuse of the American Indian Employment Credit and misuse of structured entity credits, continue to be areas of concern. The absence of a particular scheme from the Dirty Dozen should not be taken as an indication that the IRS is unaware of it or not taking steps to counter it.

How to Report Suspected Tax Fraud Activity

Suspected tax fraud can be reported to the IRS using IRS Form 3949-A, Information Referral. Form 3949-A is available for download from the IRS Web site at IRS.gov. The completed form or a letter detailing the alleged fraudulent activity should be addressed to the Internal Revenue Service, Fresno, CA 93888. The mailing should include specific information about who is being reported, the activity being reported, how the activity became known, when the alleged violation took place, the amount of money involved and any other information that might be helpful in an investigation. The person filing the report is not required to self-identify, although it is helpful to do so. The identity of the person filing the report can be kept confidential.

Whistleblowers also could provide allegations of fraud to the IRS and may be eligible for a reward by filing Form 211, Application for Award for Original Information, and following the procedures outlined in Notice 2008-4, Claims Submitted to the IRS Whistleblower Office under Section 7623.