

## Beware of IRS' 2010 "Dirty Dozen" Tax Scams

### Videos

Dirty Dozen: [English](#)

Message for Tax Preparers: [English](#) | [ASL](#)

Choosing a Tax Preparer: [English](#) | [Spanish](#) | [ASL](#)

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IR-2010-32, March 16, 2010

WASHINGTON — The Internal Revenue Service today issued its 2010 "dirty dozen" list of tax scams, including schemes involving return preparer fraud, hiding income offshore and phishing.

"Taxpayers should be wary of anyone peddling scams that seem too good to be true," IRS Commissioner Doug Shulman said. "The IRS fights fraud by pursuing taxpayers who hide income abroad and by ensuring taxpayers get competent, ethical service from qualified professionals at home in the U.S."

Tax schemes are illegal and can lead to imprisonment and fines for both scam artists and taxpayers. Taxpayers pulled into these schemes must repay unpaid taxes plus interest and penalties. The IRS pursues and shuts down promoters of these and numerous other scams.

The IRS urges taxpayers to avoid these common schemes:

### Return Preparer Fraud

Dishonest return preparers can cause trouble for taxpayers who fall victim to their ploys. Such preparers derive financial gain by skimming a portion of their clients' refunds, charging inflated fees for return preparation services and attracting new clients by promising refunds that are too good to be true. Taxpayers should choose carefully [when hiring a tax preparer](#). Federal courts have issued injunctions ordering hundreds of individuals to cease preparing returns and promoting fraud, and the Department of Justice has filed complaints against dozens of others, which are pending in court.

To increase confidence in the tax system and improve compliance with the tax law, the IRS is [implementing a number of steps](#) for future filing seasons. These include a requirement that all paid tax return preparers register with the IRS and obtain a preparer tax identification number (PTIN), as well as both competency tests and ongoing continuing professional education for all paid tax return preparers except attorneys, certified public accountants (CPAs) and enrolled agents.

Setting higher standards for the tax preparer community will significantly enhance protections and services for taxpayers, increase confidence in the tax system and result in greater compliance with tax laws over the long term. Other measures the IRS anticipates taking are highlighted in the IRS [Return Preparer Review](#) issued in December 2009.

### Hiding Income Offshore

The IRS aggressively pursues taxpayers involved in [abusive offshore transactions](#) as well as the promoters, professionals and others who facilitate or enable these schemes. Taxpayers have tried to avoid or evade U.S. income tax by hiding income in offshore banks, brokerage accounts or through the use of nominee entities. Taxpayers also evade taxes by using offshore debit cards, credit cards, wire transfers, foreign trusts, employee-leasing schemes, private annuities or insurance plans.

IRS agents continue to develop their investigations of these offshore tax avoidance transactions using information gained from over 14,700 [voluntary disclosures](#) received last year. While special civil-penalty provisions for those with undisclosed offshore accounts expired in 2009, the IRS continues to urge taxpayers with offshore accounts or entities to voluntarily come forward and resolve their tax matters. By making a voluntary disclosure, taxpayers may mitigate their risk of criminal prosecution.

## Phishing

Phishing is a tactic used by scam artists to trick unsuspecting victims into revealing personal or financial information online. IRS impersonation [schemes](#) flourish during the filing season and can take the form of e-mails, tweets or phony Web sites. Scammers may also use phones and faxes to reach their victims.

Scam artists will try to mislead consumers by telling them they are entitled to a tax refund from the IRS and that they must reveal personal information to claim it. Criminals use the information they get to [steal the victim's identity](#), access bank accounts, run up credit card charges or apply for loans in the victim's name.

[Taxpayers who receive suspicious e-mails](#) claiming to come from the IRS should not open any attachments or click on any of the links in the e-mail. Suspicious e-mails claiming to be from the IRS or Web addresses that do not begin with <http://www.irs.gov> should be forwarded to the IRS mailbox: [phishing@irs.gov](mailto:phishing@irs.gov).

## Filing False or Misleading Forms

The IRS is seeing various instances where scam artists file false or misleading returns to claim refunds that they are not entitled to. Under the scheme, taxpayers fabricate an information return and falsely claim the corresponding amount as withholding as a way to seek a tax refund. Phony information returns, such as a [Form 1099 Original Issue Discount \(OID\)](#), claiming false withholding credits usually are used to legitimize erroneous refund claims. One version of the scheme is based on a false theory that the federal government maintains secret accounts for its citizens, and that taxpayers can gain access to funds in those accounts by issuing 1099-OID forms to their creditors, including the IRS.

## Nontaxable Social Security Benefits with Exaggerated Withholding Credit

The IRS has identified returns where taxpayers report nontaxable Social Security Benefits with excessive withholding. This tactic results in no income reported to the IRS on the tax return. Often both the withholding amount and the reported income are incorrect. Taxpayers should avoid making these mistakes. Filings of this type of return may result in a \$5,000 penalty.

## Abuse of Charitable Organizations and Deductions

The IRS continues to observe the misuse of tax-exempt organizations. Abuse includes arrangements to improperly shield income or assets from taxation and attempts by donors to maintain control over donated assets or income from donated property. The IRS also continues to investigate various schemes involving the donation of non-cash assets including situations where several organizations claim the full value for both the receipt and distribution 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 definitions of qualified appraisals and qualified appraisers for taxpayers claiming charitable contributions.

## Frivolous Arguments

Promoters of frivolous schemes encourage people to make unreasonable and outlandish claims to avoid paying the taxes they owe. If a scheme seems too good to be true, it probably is. The IRS has a list of [frivolous legal positions](#) that taxpayers should avoid. These arguments are false and have been thrown out of court. While taxpayers have the right to contest their tax liabilities in court, no one has the right to disobey the law or IRS guidance.

## Abusive Retirement Plans

The IRS continues to find abuses in retirement plan arrangements, including Roth Individual Retirement

Arrangements (IRAs). The IRS is looking for transactions that taxpayers use to avoid the limits on contributions to IRAs, as well as transactions that are not properly reported as early distributions. Taxpayers should be wary of advisers who encourage them to shift appreciated assets at less than fair market value into IRAs or companies owned by their IRAs to circumvent annual contribution limits. Other variations have included the use of limited liability companies to engage in activity that is considered prohibited.

### **Disguised Corporate Ownership**

Corporations and other entities are formed and operated in certain states for the purpose of disguising the ownership of the business or financial activity by means such as [improperly using a third party](#) to request an employer identification number.

Such entities can be used to facilitate underreporting of income, fictitious deductions, non-filing of tax returns, participating 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 with the law.

### **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. Filings of this type of return may result in a \$5,000 penalty.

### **Misuse of Trusts**

For years, unscrupulous promoters have urged taxpayers to transfer assets into trusts. While there are many legitimate, valid uses of trusts in tax and estate planning, some promoted 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 to avoid income tax liability and to hide assets from creditors, including the IRS.

The IRS has recently seen an increase in the improper use of private annuity trusts and foreign trusts to shift income and deduct personal expenses. As with other arrangements, taxpayers should seek the advice of a trusted professional before entering into a trust arrangement.

### **Fuel Tax Credit Scams**

The IRS receives claims for the fuel tax credit that are excessive. Some taxpayers, such as farmers who use fuel for off-highway business purposes, may be eligible for the fuel tax credit. But other 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 is considered a frivolous tax claim and potentially subjects those who improperly claim the credit to a \$5,000 penalty.