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COMPLETING FORM W-4, EMPLOYEES WITHHOLDING ALLOWANCE CERTIFICATE How Hard Can it Be?

The 2019 filing season brought into sharp focus—much more so than in past years—just how few Americans understand how to complete Form W-4, *Employees Withholding Allowance Certificate*. For example, the news media was apoplectic over reports in February showing that tax refunds were down about 9% over last year's numbers. A hysterical cry went out that such data was proof that the Tax Cuts and Jobs Act was nothing more than tax cuts for the rich. After all, if your refund is down, it must mean your tax hit went up.

There were a number of problems with these reports. For starters, only about 25 million individual tax returns, out of the expected 152 million, were filed by the time the reports were issued. Thus, the sample size of returns was too small to draw any firm conclusions. Most notably, however, was the fact that effective January 2018 (one year *before* the filing season began) the IRS changed the withholding tables to reflect the fact that most taxpayers would in fact pay less tax in 2018 than they did in prior years because of the Jobs Act. Said another way, people were getting their tax refunds every month in their pay checks rather than at the end of the year.

Finally, by the time we were at the high tide of filing

season and well over 100 million returns were filed, it came to light that the average tax refund was actually up a few points over last year. There was no corresponding celebration by the media to acknowledge that the Jobs Act indeed did cut taxes for most citizens.

In the background of this discussion is a point that I've been making for years: people either don't pay attention to filling out their Form W-4, or they just don't know how to do it. I rather believe more of the latter element drives the issue. In light of the firestorm of controversy, the IRS redesigned Form W-4 so people might more accurately set their withholding. Now there's backlash over whether the IRS created a document that, like just about every other tax form, is way too complicated for the average person to read, comprehend and complete.

My response is that this just isn't that complicated.

Understanding Exemptions and Allowances

Let's start with understanding the very basics of the form. It is titled (and has been for decades), *Employees Withholding Allowance Certificate*. It calls for the citizen to inform his employer of the number of withholding *allowances* he wishes

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to claim for withholding purposes. The fewer allowances claimed, the more money is withheld. The opposite is also true. The greater the allowances claimed, the less is taken.

Likewise, a person declares on the form his tax return filing status, whether single, married (filing jointly or separately), or head of household. Your tax return filing status impacts whether more or less is taken. For example, if you are a single person with one withholding allowance, more will be withheld than if you are married filing jointly with one allowance. That is a function of the different tax tables that apply to the various filing categories.

Suppose you are married with two children. Prior to the Jobs Act, you were entitled to claim an exemption on your tax return for yourself and each dependent. Thus, in this example, you would get four exemptions on your tax return. These exemptions operated to reduce your tax liability because each exemption reduced taxable income by about \$4,500. Since most people believe that exemptions and allowances are the same thing, they claimed only four allowances on their W-4. Because this misunderstanding caused over withholding, about 80% of all taxpayers overpaid their taxes, leading to a refund of about \$3,000, on which the IRS paid no interest whatsoever.

But as I said, allowances and exemptions are not the same thing. An allowance is defined as any tax return item that reduces your tax liability. That certainly includes exemptions but is by no means limited to them. For example, standard or itemized deductions also reduce your tax liability. So do tax credits and retirement fund contributions. All of these (and more) need to be included in calculating allowances. I explain this further below.

IRS Redesigns the W-4

In the wake of the confusion and controversy of the 2019 filing season, the IRS redesigned Form W-4. Actually, it's not the form so much as the worksheet that goes with the form that was redesigned. In my opinion, it's for the better. The worksheet more clearly walks the reader through the process of figuring allowances. The new design is intended to get people closer to their ideal withholding amount so their withholding better matches their tax debt. That is to say, they do not over-withhold and thus end up with a big refund (and no interest); nor do they under-withhold and (worse) end up with an unfunded surprise tax debt they can't pay.

A Walk Through the Form

The remarkable difference between past W-4 instructions and the current version is the way it addresses exemptions. Under the Jobs Act, all personal and dependent exemptions are suspended through 2025. You didn't claim such exemptions on your 2018 tax return and will not claim them for the foreseeable future. Instead, the standard deduction for all filing

categories is about double and there is a new tax credit for certain dependents.

In light of that, the instructions provide a worksheet that guides you through calculating your allowances. The worksheet factors the following items:

- Your filing status and marital status,
- Whether you're entitled to any child tax credits,
- Figuring allowances for other dependents,
- Figuring allowances based on either itemized deductions or the standard deduction (whichever is greater), and finally,
- Splitting allowances in the case of two-earner married couples, or persons with multiple jobs.

The form and instructions are reproduced at the end of this article.

Some critics claim that people will need to seek the help of a tax professional to complete the form. I find that claim to be a bit hyperbolic. It is true there are a number of steps in the worksheet, but no single step appears to be unduly complicated.

W-4 is a Living Document

Most people file their W-4 upon getting hired for a new job and then forget it. This is one big reason so many people get large refunds. But it is not a file-and-forget form. It's a living document. It must change as your circumstances change. You must review your W-4 every year, preferably just after filing your past year's tax return. If you got a large refund or owed money you didn't expect to owe, you must re-figure your allowances so that going forward, your withholding better matches your tax liability.

Moreover, you should change your W-4 at any point during the course of the year if there are substantial changes to your circumstances. For example, if you:

- Get married or divorced,
- Have a new baby or a child moves out,
- Stop or start paying for deductible education costs,
- Buy or sell a home,
- Begin a new business or close one down,
- Begin or stop paying substantial medical expenses or charitable contributions,
- Begin making deductible retirement fund contributions,
- Being drawing taxable retirement fund benefits, or
- Change any other behavior that will affect the bottom line on your taxes.

But I Want a Large Refund

People tell me all the time they want over-withholding

because they want a large refund. They claim that it's the way they "save money." The fact is that it is the world's worst way to save money. As we all know, the IRS pays you no interest on the over-withholding. Second, you can't get access to the money on an as-needed basis. You have to file your tax return in order to get the money, and you don't file the return until March or April of the following year. And finally, when you do file the return, you don't get all your money back because you are also over-withheld for the first three or four months of the following year, which money you will not get back for a whole additional year later, when you finally file that return. In other words, the IRS always has more of your money than you owe.

But there's another element of the "savings" plan that is particularly bothersome. We know that about 80% of all taxpayers get a refund. The average refund in 2019 (for tax year 2018) was just north of \$3,100. That means those people paid \$258 per month in taxes they didn't owe. Now, we also know that about one-third of all Americans live pay check to pay check. They usually don't have enough money to get them through to the next month. For these people, getting a flat tire constitutes a financial crisis. For the life if me, I don't understand why these people want the IRS to hold their money. It only deprives them of the ability to ease their monthly financial stress.

I wonder. How much money do such people pay in late fees and interest on credit card debts? How much do they pay in fines for late utility bills or in added fees to reinstate disconnected utilities? How many are being eaten alive by costly car repairs because they don't have a reliable car? The fact is that \$258 per month pays for a reasonably priced, reliable vehicle, which in turn insures that a person can get to work every day, or perhaps even take a better job that he might not otherwise get because the job is off public transportation routes.

Americans need financial restoration now more than ever before. The process starts with knowing where your money is going, and making decisions with that money to put you on the track to recovery. The first step in that process for most people is to stop paying taxes you don't owe.

IRS WITH THE BURDEN TO PROVE MAILING Failure Will Lead to Abatement of Assessment By Scott MacPherson

Sometimes the simplest argument is the right solution for a client. The recent cases of *United States v. Birdsong*, 122 A.F.T.R.2d 2018-6804, 2018 WL 6330112 (D. Mont. Dec. 12, 2018) and *U.S. v. Meyer*, 914 F.3d 592 (8th Cir. March 26, 2019), remind us of this.

In *Birdsong*, the district court granted the government's motion for summary judgment, thereby reducing to judgment Birdsong's federal tax debt. The case is noteworthy not for the holding but for the argument that Birdsong raised in his defense: "Birdsong argues that the action is barred because the United States failed to send the notice of deficiency in the form required by law." *Id.* at 81. Likewise, in *Meyer* the appellate court affirmed summary judgment in favor of the government, thereby affirming tax assessments against Meyer. But Meyer, like Birdsong, argued that those assessments were invalid because the IRS did not mail a notice of deficiency before assessing those liabilities. *Meyer* at 594.

It sounds too simple to be useful, right? For one, both of these taxpayers lost. But ignoring that unfortunate detail, it is important to understand that in order to obtain an assessment beyond that reported on an individual's tax return, the IRS must send a notice of deficiency to a taxpayer's last known address either by certified or registered mail. If the IRS fails to do that, any subsequent assessment is null and void. This is a matter of settled law. See: IRC §6212. And indeed, both courts straightforwardly acknowledged that. See: *Birdsong* at *1; *Meyer* at 594.

For a full discussion of the so-called deficiency procedures, see chapters 4 and 8 of Dan's book, *The Taxpayers' Defense Manual*.

So, why, then, did they lose? And why would I think these cases are useful?

As to the first question, in *Birdsong*, for evidence of the required mailing the government produced a copy of an envelope bearing a certified mailing label and said that the notice of deficiency was mailed in that envelope. *Birdsong* at *2. The court held that the photocopy of the envelope was sufficient proof of the mailing required by law. (The government also produced the Certificate of Assessment for the tax years at issue to prove that a subsequent assessment occurred.)

Continued on page 8.

Form W-4 (2019)

Future developments. For the latest information about any future developments related to Form W-4, such as legislation enacted after it was published, go to www.irs.gov/FormW4.

Purpose. Complete Form W-4 so that your employer can withhold the correct federal income tax from your pay. Consider completing a new Form W-4 each year and when your personal or financial situation changes.

Exemption from withholding. You may claim exemption from withholding for 2019 if **both** of the following apply.

- For 2018 you had a right to a refund of **all** federal income tax withheld because you had **no** tax liability, **and**
- For 2019 you expect a refund of **all** federal income tax withheld because you expect to have **no** tax liability.

If you're exempt, complete **only** lines 1, 2, 3, 4, and 7 and sign the form to validate it. Your exemption for 2019 expires February 17, 2020. See Pub. 505, Tax Withholding and Estimated Tax, to learn more about whether you qualify for exemption from withholding.

General Instructions

If you aren't exempt, follow the rest of these instructions to determine the number of withholding allowances you should claim for withholding for 2019 and any additional amount of tax to have withheld. For regular wages, withholding must be based on allowances you claimed and may not be a flat amount or percentage of wages.

You can also use the calculator at www.irs.gov/W4App to determine your tax withholding more accurately. Consider

using this calculator if you have a more complicated tax situation, such as if you have a working spouse, more than one job, or a large amount of nonwage income not subject to withholding outside of your job. After your Form W-4 takes effect, you can also use this calculator to see how the amount of tax you're having withheld compares to your projected total tax for 2019. If you use the calculator, you don't need to complete any of the worksheets for Form W-4.

Note that if you have too much tax withheld, you will receive a refund when you file your tax return. If you have too little tax withheld, you will owe tax when you file your tax return, and you might owe a penalty.

Filers with multiple jobs or working spouses. If you have more than one job at a time, or if you're married filing jointly and your spouse is also working, read all of the instructions including the instructions for the Two-Earners/Multiple Jobs Worksheet before beginning.

Nonwage income. If you have a large amount of nonwage income not subject to withholding, such as interest or dividends, consider making estimated tax payments using Form 1040-ES, Estimated Tax for Individuals. Otherwise, you might owe additional tax. Or, you can use the Deductions, Adjustments, and Additional Income Worksheet on page 3 or the calculator at www.irs.gov/W4App to make sure you have enough tax withheld from your paycheck. If you have pension or annuity income, see Pub. 505 or use the calculator at www.irs.gov/W4App to find out if you should adjust your withholding on Form W-4 or W-4P.

Nonresident alien. If you're a nonresident alien, see Notice 1392, Supplemental Form W-4 Instructions for Nonresident Aliens, before completing this form.

Specific Instructions

Personal Allowances Worksheet

Complete this worksheet on page 3 first to determine the number of withholding allowances to claim.

Line C. Head of household please note: Generally, you may claim head of household filing status on your tax return only if you're unmarried and pay more than 50% of the costs of keeping up a home for yourself and a qualifying individual. See Pub. 501 for more information about filing status.

Line E. Child tax credit. When you file your tax return, you may be eligible to claim a child tax credit for each of your eligible children. To qualify, the child must be under age 17 as of December 31, must be your dependent who lives with you for more than half the year, and must have a valid social security number. To learn more about this credit, see Pub. 972, Child Tax Credit. To reduce the tax withheld from your pay by taking this credit into account, follow the instructions on line E of the worksheet. On the worksheet you will be asked about your total income. For this purpose, total income includes all of your wages and other income, including income earned by a spouse if you are filing a joint return.

Line F. Credit for other dependents. When you file your tax return, you may be eligible to claim a credit for other dependents for whom a child tax credit can't be claimed, such as a qualifying child who doesn't meet the age or social security number requirement for the child tax credit, or a qualifying relative. To learn more about this credit, see Pub. 972. To reduce the tax withheld from your pay by taking this credit into account, follow the instructions on line F of the worksheet. On the worksheet, you will be asked about your total income. For this purpose, total

----- Separate here and give Form W-4 to your employer. Keep the worksheet(s) for your records. -----

Form W-4 Department of the Treasury Internal Revenue Service		Employee's Withholding Allowance Certificate		OMB No. 1545-0074 2019
► Whether you're entitled to claim a certain number of allowances or exemption from withholding is subject to review by the IRS. Your employer may be required to send a copy of this form to the IRS.				
1 Your first name and middle initial		Last name		2 Your social security number
Home address (number and street or rural route)			3 <input type="checkbox"/> Single <input type="checkbox"/> Married <input type="checkbox"/> Married, but withhold at higher Single rate. Note: If married filing separately, check "Married, but withhold at higher Single rate."	
City or town, state, and ZIP code			4 If your last name differs from that shown on your social security card, check here. You must call 800-772-1213 for a replacement card. <input type="checkbox"/>	
5 Total number of allowances you're claiming (from the applicable worksheet on the following pages)				5
6 Additional amount, if any, you want withheld from each paycheck				6 \$
7 I claim exemption from withholding for 2019, and I certify that I meet both of the following conditions for exemption. <ul style="list-style-type: none"> • Last year I had a right to a refund of all federal income tax withheld because I had no tax liability, and • This year I expect a refund of all federal income tax withheld because I expect to have no tax liability. If you meet both conditions, write "Exempt" here ►				
Under penalties of perjury, I declare that I have examined this certificate and, to the best of my knowledge and belief, it is true, correct, and complete.				
Employee's signature (This form is not valid unless you sign it.) ►				Date ►
8 Employer's name and address (Employer: Complete boxes 8 and 10 if sending to IRS and complete boxes 8, 9, and 10 if sending to State Directory of New Hires.)			9 First date of employment	10 Employer identification number (EIN)

income includes all of your wages and other income, including income earned by a spouse if you are filing a joint return.

Line G. Other credits. You may be able to reduce the tax withheld from your paycheck if you expect to claim other tax credits, such as tax credits for education (see Pub. 970). If you do so, your paycheck will be larger, but the amount of any refund that you receive when you file your tax return will be smaller. Follow the instructions for Worksheet 1-6 in Pub. 505 if you want to reduce your withholding to take these credits into account. Enter “-0-” on lines E and F if you use Worksheet 1-6.

Deductions, Adjustments, and Additional Income Worksheet

Complete this worksheet to determine if you’re able to reduce the tax withheld from your paycheck to account for your itemized deductions and other adjustments to income, such as IRA contributions. If you do so, your refund at the end of the year will be smaller, but your paycheck will be larger. You’re not required to complete this worksheet or reduce your withholding if you don’t wish to do so.

You can also use this worksheet to figure out how much to increase the tax withheld from your paycheck if you have a large amount of nonwage income not subject to withholding, such as interest or dividends.

Another option is to take these items into account and make your withholding more accurate by using the calculator at www.irs.gov/W4App. If you use the calculator, you don’t need to complete any of the worksheets for Form W-4.

Two-Earners/Multiple Jobs Worksheet

Complete this worksheet if you have more than one job at a time or are married filing jointly and have a working spouse. If you

don’t complete this worksheet, you might have too little tax withheld. If so, you will owe tax when you file your tax return and might be subject to a penalty.

Figure the total number of allowances you’re entitled to claim and any additional amount of tax to withhold on all jobs using worksheets from only one Form W-4. Claim all allowances on the W-4 that you or your spouse file for the highest paying job in your family and claim zero allowances on Forms W-4 filed for all other jobs. For example, if you earn \$60,000 per year and your spouse earns \$20,000, you should complete the worksheets to determine what to enter on lines 5 and 6 of your Form W-4, and your spouse should enter zero (“-0-”) on lines 5 and 6 of his or her Form W-4. See Pub. 505 for details.

Another option is to use the calculator at www.irs.gov/W4App to make your withholding more accurate.

Tip: If you have a working spouse and your incomes are similar, you can check the “Married, but withhold at higher Single rate” box instead of using this worksheet. If you choose this option, then each spouse should fill out the Personal Allowances Worksheet and check the “Married, but withhold at higher Single rate” box on Form W-4, but only one spouse should claim any allowances for credits or fill out the Deductions, Adjustments, and Additional Income Worksheet.

Instructions for Employer

Employees, do not complete box 8, 9, or 10. Your employer will complete these boxes if necessary.

New hire reporting. Employers are required by law to report new employees to a designated State Directory of New Hires. Employers may use Form W-4, boxes 8, 9,

and 10 to comply with the new hire reporting requirement for a newly hired employee. A newly hired employee is an employee who hasn’t previously been employed by the employer, or who was previously employed by the employer but has been separated from such prior employment for at least 60 consecutive days. Employers should contact the appropriate State Directory of New Hires to find out how to submit a copy of the completed Form W-4. For information and links to each designated State Directory of New Hires (including for U.S. territories), go to www.acf.hhs.gov/css/employers.

If an employer is sending a copy of Form W-4 to a designated State Directory of New Hires to comply with the new hire reporting requirement for a newly hired employee, complete boxes 8, 9, and 10 as follows.

Box 8. Enter the employer’s name and address. If the employer is sending a copy of this form to a State Directory of New Hires, enter the address where child support agencies should send income withholding orders.

Box 9. If the employer is sending a copy of this form to a State Directory of New Hires, enter the employee’s first date of employment, which is the date services for payment were first performed by the employee. If the employer rehired the employee after the employee had been separated from the employer’s service for at least 60 days, enter the rehire date.

Box 10. Enter the employer’s employer identification number (EIN).

Personal Allowances Worksheet (Keep for your records.)

A	Enter "1" for yourself	A	_____
B	Enter "1" if you will file as married filing jointly	B	_____
C	Enter "1" if you will file as head of household	C	_____
D	Enter "1" if: } <ul style="list-style-type: none"> • You're single, or married filing separately, and have only one job; or • You're married filing jointly, have only one job, and your spouse doesn't work; or • Your wages from a second job or your spouse's wages (or the total of both) are \$1,500 or less. 	D	_____
E	<p>Child tax credit. See Pub. 972, Child Tax Credit, for more information.</p> <ul style="list-style-type: none"> • If your total income will be less than \$71,201 (\$103,351 if married filing jointly), enter "4" for each eligible child. • If your total income will be from \$71,201 to \$179,050 (\$103,351 to \$345,850 if married filing jointly), enter "2" for each eligible child. • If your total income will be from \$179,051 to \$200,000 (\$345,851 to \$400,000 if married filing jointly), enter "1" for each eligible child. • If your total income will be higher than \$200,000 (\$400,000 if married filing jointly), enter "-0-" 		
F	<p>Credit for other dependents. See Pub. 972, Child Tax Credit, for more information.</p> <ul style="list-style-type: none"> • If your total income will be less than \$71,201 (\$103,351 if married filing jointly), enter "1" for each eligible dependent. • If your total income will be from \$71,201 to \$179,050 (\$103,351 to \$345,850 if married filing jointly), enter "1" for every two dependents (for example, "-0-" for one dependent, "1" if you have two or three dependents, and "2" if you have four dependents). • If your total income will be higher than \$179,050 (\$345,850 if married filing jointly), enter "-0-" 		
G	<p>Other credits. If you have other credits, see Worksheet 1-6 of Pub. 505 and enter the amount from that worksheet here. If you use Worksheet 1-6, enter "-0-" on lines E and F</p>		
H	Add lines A through G and enter the total here		H _____

For accuracy, **complete all worksheets that apply.**

- If you plan to **itemize** or **claim adjustments to income** and want to reduce your withholding, or if you have a large amount of nonwage income not subject to withholding and want to increase your withholding, see the **Deductions, Adjustments, and Additional Income Worksheet** below.
- If you **have more than one job at a time** or are **married filing jointly and you and your spouse both work**, and the combined earnings from all jobs exceed \$53,000 (\$24,450 if married filing jointly), see the **Two-Earners/Multiple Jobs Worksheet** on page 4 to avoid having too little tax withheld.
- If **neither** of the above situations applies, **stop here** and enter the number from line H on line 5 of Form W-4 above.

Deductions, Adjustments, and Additional Income Worksheet

Note: Use this worksheet *only* if you plan to itemize deductions, claim certain adjustments to income, or have a large amount of nonwage income not subject to withholding.

1	Enter an estimate of your 2019 itemized deductions. These include qualifying home mortgage interest, charitable contributions, state and local taxes (up to \$10,000), and medical expenses in excess of 10% of your income. See Pub. 505 for details	1	\$ _____
2	Enter: } <ul style="list-style-type: none"> \$24,400 if you're married filing jointly or qualifying widow(er) \$18,350 if you're head of household \$12,200 if you're single or married filing separately 	2	\$ _____
3	Subtract line 2 from line 1. If zero or less, enter "-0-"	3	\$ _____
4	Enter an estimate of your 2019 adjustments to income, qualified business income deduction, and any additional standard deduction for age or blindness (see Pub. 505 for information about these items)	4	\$ _____
5	Add lines 3 and 4 and enter the total	5	\$ _____
6	Enter an estimate of your 2019 nonwage income not subject to withholding (such as dividends or interest)	6	\$ _____
7	Subtract line 6 from line 5. If zero, enter "-0-". If less than zero, enter the amount in parentheses	7	\$ _____
8	Divide the amount on line 7 by \$4,200 and enter the result here. If a negative amount, enter in parentheses. Drop any fraction	8	_____
9	Enter the number from the Personal Allowances Worksheet , line H, above	9	_____
10	Add lines 8 and 9 and enter the total here. If zero or less, enter "-0-". If you plan to use the Two-Earners/Multiple Jobs Worksheet , also enter this total on line 1 of that worksheet on page 4. Otherwise, stop here and enter this total on Form W-4, line 5, page 1	10	_____

Two-Earners/Multiple Jobs Worksheet

Note: Use this worksheet *only* if the instructions under line H from the **Personal Allowances Worksheet** direct you here.

- 1 Enter the number from the **Personal Allowances Worksheet**, line H, page 3 (or, if you used the **Deductions, Adjustments, and Additional Income Worksheet** on page 3, the number from line 10 of that worksheet) **1** _____
 - 2 Find the number in **Table 1** below that applies to the **LOWEST** paying job and enter it here. **However**, if you're married filing jointly and wages from the highest paying job are \$75,000 or less and the combined wages for you and your spouse are \$107,000 or less, don't enter more than "3" **2** _____
 - 3 If line 1 is **more than or equal to** line 2, subtract line 2 from line 1. Enter the result here (if zero, enter "-0-") and on Form W-4, line 5, page 1. **Do not** use the rest of this worksheet **3** _____
- Note:** If line 1 is **less than** line 2, enter "-0-" on Form W-4, line 5, page 1. Complete lines 4 through 9 below to figure the additional withholding amount necessary to avoid a year-end tax bill.
- 4 Enter the number from line 2 of this worksheet **4** _____
 - 5 Enter the number from line 1 of this worksheet **5** _____
 - 6 **Subtract** line 5 from line 4 **6** _____
 - 7 Find the amount in **Table 2** below that applies to the **HIGHEST** paying job and enter it here **7** \$ _____
 - 8 **Multiply** line 7 by line 6 and enter the result here. This is the additional annual withholding needed **8** \$ _____
 - 9 **Divide** line 8 by the number of pay periods remaining in 2019. For example, divide by 18 if you're paid every 2 weeks and you complete this form on a date in late April when there are 18 pay periods remaining in 2019. Enter the result here and on Form W-4, line 6, page 1. This is the additional amount to be withheld from each paycheck **9** \$ _____

Table 1				Table 2			
Married Filing Jointly		All Others		Married Filing Jointly		All Others	
If wages from LOWEST paying job are—	Enter on line 2 above	If wages from LOWEST paying job are—	Enter on line 2 above	If wages from HIGHEST paying job are—	Enter on line 7 above	If wages from HIGHEST paying job are—	Enter on line 7 above
\$0 - \$5,000	0	\$0 - \$7,000	0	\$0 - \$24,900	\$420	\$0 - \$7,200	\$420
5,001 - 9,500	1	7,001 - 13,000	1	24,901 - 84,450	500	7,201 - 36,975	500
9,501 - 19,500	2	13,001 - 27,500	2	84,451 - 173,900	910	36,976 - 81,700	910
19,501 - 35,000	3	27,501 - 32,000	3	173,901 - 326,950	1,000	81,701 - 158,225	1,000
35,001 - 40,000	4	32,001 - 40,000	4	326,951 - 413,700	1,330	158,226 - 201,600	1,330
40,001 - 46,000	5	40,001 - 60,000	5	413,701 - 617,850	1,450	201,601 - 507,800	1,450
46,001 - 55,000	6	60,001 - 75,000	6	617,851 and over	1,540	507,801 and over	1,540
55,001 - 60,000	7	75,001 - 85,000	7				
60,001 - 70,000	8	85,001 - 95,000	8				
70,001 - 75,000	9	95,001 - 100,000	9				
75,001 - 85,000	10	100,001 - 110,000	10				
85,001 - 95,000	11	110,001 - 115,000	11				
95,001 - 125,000	12	115,001 - 125,000	12				
125,001 - 155,000	13	125,001 - 135,000	13				
155,001 - 165,000	14	135,001 - 145,000	14				
165,001 - 175,000	15	145,001 - 160,000	15				
175,001 - 180,000	16	160,001 - 180,000	16				
180,001 - 195,000	17	180,001 and over	17				
195,001 - 205,000	18						
205,001 and over	19						

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Continued from page 3.

In *Meyer*, the 8th Circuit forthrightly said, “Before assessing liability for unpaid taxes, the IRS must send a NOD to the taxpayer’s last known address by certified mail or registered mail.” *Id.* at 594. And the government “bears the burden of proving that the IRS properly mailed a NOD by competent and persuasive evidence.” *Id.* at 594. But the government gets a rebuttable presumption of proper mailing, the court said, if it, a) shows that the notice of deficiency existed, and b) produces a properly completed Postal Form 3877, *Certified Mail Log*, or the equivalent. *Id.* at 594.

That is where Meyer lost. The government did not produce a Form 3877, so the presumption did not apply. However, for one of the tax years at issue the government did produce a Form 4340 and a copy of the notice of deficiency. *Id.* at 595. The court held that because the Form 4340 showed the dates when the NODs were mailed and the dates when the IRS assessed the deficiencies against Meyer, and the IRS had a note explaining that those assessments were made “per default of 90 day letter,” and because the government produced a copy of the notice of deficiency, that the government proved that the notice was in fact mailed. *Id.* at 595.

As for the other tax year at issue, the government did not produce a copy of the notice but it produced a Form 4340 and a “Case History Report” that detailed the steps taken by the IRS officer assigned to Meyer’s case in drafting and mailing a notice, and assessing the debt afterwards. The court held that this, too, was sufficient. *Id.* at 595.

As to why I think these cases are useful – not everyone loses on this argument, and that is the point I want to drill into throughout the rest of this article. Even though neither of the above courts cited it, both Birdsong and Meyer were using an argument that goes back decades, at least to the case of *Pietanza v. Commissioner*, 92 T.C. 729 (1989). In that case, a husband and wife successfully (yes, successfully!) argued that their assessment should be entirely abated because the IRS did not mail them a notice of deficiency. Their success is my point.

The Pietanzas filed their petition in Tax Court late (because they did not receive the notice), so the IRS of course moved to dismiss for lack of jurisdiction based on that untimely petition. The Pietanzas filed a cross-motion to dismiss for lack of jurisdiction based on there being no notice of deficiency at all. They won because (queue the laughter!) the IRS lost their administrative file. The court explained:

Respondent is unable to locate his administrative file in this matter, and accordingly, is unable to provide the Court (or petitioners) with a copy of a notice of deficiency for 1980. Further, there is no indication in this record, other than the bare existence of postal service Form 3877, that a notice of deficiency is, or ever was, in existence. We know only that a draft of a

notice was prepared. *Id.* at 731.

More specifically, the IRS in *Pietanza* provided: 1) a Form 3877, postal service mailing form, indicating that something (supposedly the notice of deficiency) was mailed, 2) a draft notice of deficiency, emphasis on “draft,” and 3) affidavits of two employees attesting that a notice of deficiency was prepared. *Id.* at 733. But the only notice of deficiency provided to the court, or to the petitioners in discovery, was a draft notice that was neither dated nor signed. And it was obviously only a draft, not the final version, because it did not include the negligence penalty assessed against the Pietanzas. *Id.* at 734. Said the court:

The most we can conclude from the record placed before us is that a draft of a notice of deficiency was prepared. We cannot conclude that the sample notice presented to us was, in fact, the notice of deficiency. *Id.* at 734.

The court then considered whether, as a matter of law, a Form 3877 standing *alone* can support an assessment—emphasis on *alone*. It held “no.” *Id.* at 742. And the normal presumption of official regularity in favor of the IRS was trumped by the documented history of unresponsive replies by the IRS to the Pietanzas’ repeated requests. *Id.* at 739.

So why did Birdsong and Meyer lose after the Pietanzas won? The winning (yes, winning) case of *Butti v. Commissioner*, T.C. Memo. 2008-82, explains why. Butti repeated the Pietanzas’ success on very similar facts. That case was an appeal from a Collection Due Process Hearing, where the hearing officer sustained a levy. The court held that the determination was in error and an abuse of discretion “because respondent [IRS] failed to show that respondent issued a notice of deficiency before assessing petitioner’s taxes.” *Id.* at *4.

As a starting point for its discussion, and with reference to §6212, the court recognized that the IRS cannot proceed with collection unless it first issued a notice of deficiency. *Id.* at *3. Further, “Respondent bears the burden of proving by competent and persuasive evidence that the notice of deficiency was properly mailed.” *Id.* And that is where Butti won:

Where the existence of the notice of deficiency is not in dispute, a properly completed Form 3877 by itself is sufficient, absent evidence to the contrary, to establish that the notice was properly mailed to a taxpayer [citations omitted]. However, where, as here, the existence of the notice of deficiency is in dispute, we have previously rejected the Commissioner’s reliance on the presumption of regularity based solely on the Form 3877 under circumstances similar to those present here. *Id.* at *3.

The court was referring to the *Pietanza* case:

In *Pietanza*, as here, the Commissioner, (1) lost the administrative file, (2) had no copies of a notice of deficiency, (3) did not establish that a final notice of deficiency ever existed, (4) relied on a Postal Service

Form 3877, and (5) did not introduce evidence showing how the Commissioner's personnel prepare and mail notices of deficiency.

The Commissioner in *Pietanza* produced a draft copy of the notice of deficiency but did not establish that a final notice ever existed. Here, the Appeals officer testified that he saw a copy of the notice of deficiency, but he did not say whether it was a final version. Further, his testimony is curious in the light of the contemporaneous entry in his log, which states only that the administrative file indicates that a defaulted notice of deficiency is in the administrative file. We do not understand why the Appeals officer would have chosen that language if he had seen the notice of deficiency. *Id.* at *4.

The case of *Galluzzo v. Commissioner*, T.C. Memo. 2013-136, mirrored the facts of *Pietanza*, and the court again held for the taxpayer. As before, husband and wife petitioned the Tax Court late, the IRS moved to dismiss for lack of jurisdiction, and the petitioners argued that they never received the notices of deficiency. As a starting point for its analysis, and with citation to *Pietanza*, the court said, "Respondent [IRS] has the burden of establishing both the existence of a notice of deficiency as well as the date of mailing." *Id.* at *1. Going on, the court said:

In *Pietanza*, we held that a Form 3877, standing alone, was not sufficient in the circumstances of that case to prove that a notice of deficiency was mailed to the taxpayers. Respondent has not shown that the facts present in this case differ in any material way from those in *Pietanza*. In *Pietanza*, as here, the Commissioner (1) lost the administrative file, (2) had no copies of a notice of deficiency, (3) did not establish that a final notice of deficiency ever existed, (4) relied on a Form 3877, and (5) did not introduce evidence showing how the Commissioner's personnel prepare and mail notices of deficiency. *Id.* at *2.

But it gets even worse. In *Pietanza*, the IRS at least produced a draft copy of the notice, and affidavits from two employees.

In our case [*Galluzzo*], respondent presented no such evidence; he has not produced a draft copy of the notices of deficiency or any testimony from IRS employees who assisted in the preparation of the notice of deficiency. Thus, there is nothing in the case, apart from the Form 3877 itself, to support a presumption of regularity by the IRS. *Id.* at *2.

Case dismissed on the grounds that the IRS did not issue a notice of deficiency.

And still more recently, the winning case of *Knudsen v. Commissioner*, T.C. Memo. 2015-69, again illustrates the viability of this argument. Knudsen was a non-filer for two tax years. He argued at a Collection Due Process levy hearing

that the assessments were illegal because the IRS never mailed a notice of deficiency. The hearing officer sustained the levy, Knudsen appealed, and in the Tax Court the government moved for summary judgment. The court began its discussion with a statement of the law:

Petitioner's contention that respondent [IRS] never mailed the notices of deficiency to him, if true, would be fatal to respondent's proposed levy. If respondent's assessments of petitioner's 2004 and 2006 tax liabilities were not preceded by the mailing of notices of deficiency to petitioner as required by section 6213(a), the assessments would be invalid. *Knudsen* at *15.

Notice the use of the word "fatal."

The IRS did not produce a copy of the alleged notice of deficiency. Instead it produced a Form 3877 that contained certain flaws of omission. There was: 1) no indication of the number of items the IRS delivered to the U.S. Postal Service, 2) no required signatures of the U.S. Postal Service employees who received the items to mail, 3) no identification of the listed items as actually being notices of deficiency, and 4) no identification of the tax years to which the mailed documents related. *Knudsen* at *14-15. The Tax Court held that these flaws were enough to raise a factual issue concerning whether the IRS mailed the required notice of deficiency. Thus, summary judgment was inappropriate. *Knudsen* at 16 & 17. (The parties subsequently settled, rather than go to trial.)

As we see, sometimes the very simple rule that there is no assessment unless the IRS sends a notice of deficiency can save the day. But notice again why Birdsong and Meyer lost, when other taxpayers won. In *Pietanza*, *Butti*, *Galluzzo*, and *Knudsen*, the existence of the notice of deficiency was disputed and the IRS only had a Form 3877 (its internal certified mailing form) for proof that a notice was mailed. In *Birdsong*, however, the IRS had a copy of a certified mailing envelope and a declaration of an employee attesting that the notice of deficiency was mailed in that envelope. Taken together, those two pieces of evidence were enough to prove that a notice of deficiency was mailed. And in *Meyer*, the IRS produced a Form 4340 and a copy of the notice of deficiency for one tax year, and a Form 4340 and Case History Report for the other tax year. These pieces of evidence, in combination, were enough to prove that a notice of deficiency was mailed.

And that raises the clarifying question: what *exactly* does the IRS have to prove when the mailing of a notice of deficiency is disputed? The circuit court in *Welch v. United States*, 678 F.3d 1371 (Fed. Cir. 2012) summarized the test clearly. *Welch* is a mixed-bag case in that the taxpayer won for one year but lost for another year because the evidence for the two years was different. The court stated the legal test in this way:

1. "First, where the IRS has, a) established the existence of a notice of deficiency, and b) produced a properly

completed PS Form 3877 certified mail log, it is entitled to a presumption of mailing. At that point, the burden shifts to the taxpayer to rebut that presumption by clear and convincing evidence.”

2. “Second, in the absence of proof of a notice of deficiency and a properly completed Postal Form 3877 certified mail log, the IRS may meet its burden with evidence that is ‘otherwise sufficient.’” *Id.* at 1377.

Those prongs raise the question of what sort of evidence is sufficient. The court answered that question by saying that the evidence must be “competent and persuasive.” *Id.* at 1378. In *Birdsong* the IRS had that—in the form of a photocopy of a mailing envelope plus a declaration by an IRS employee. In *Meyer*, the IRS had a copy of the notice of deficiency for one year, and a Case History Report detailing the notice of deficiency for the other year.

Again, the *Welch* court said, “Where the parties dispute the existence of the notice of deficiency itself, the government bears the burden of establishing both the existence of the notice itself, as well as timely mailing of that specific notice. ... Evidence of a mere mailing absent corroboration that the notice of deficiency was actually created is insufficient to meet the government’s burden.” *Id.* at 1379. This is precisely what the IRS had in *Birdsong*, but not in *Pietanza*, *Butti*, *Galluzzo*, or *Knudsen*. But where the existence of a notice is not in dispute, the presumption of official regularity can establish the validity of the notice’s contents.

In the absence of a Form 3877, the IRS must present other evidence corroborating an actual timely mailing. “The evidence presented to prove timely mailing may include documentary evidence as well as evidence of mailing practices corroborated by direct testimony.” *Welch* at 1377; *Meyer* at 594. But when a Form 3877 is used, the presumption of official regularity can be invoked to establish mailing. *Welch* at 1379; *Meyer* at 594.

On these same points see also: *Kamps v. Commissioner*, T.C. Memo. 2011-287 (decision for the government where the IRS provided a Form 3877 showing taxpayer’s correct mailing address and a date of mailing the notice of deficiency); *Clarkson v. Commissioner*, 664 Fed.Appx. 265 (3rd Cir. 2016) (decision for the government where the Form 3877 was missing the name of the issuing IRS employee and the number of pieces received at the post office, but it was appropriately signed and it showed the mailing date of the notice of deficiency, and the IRS produced a copy of the notice of deficiency).

In short, the reason *Birdsong* and *Meyer* lost actually proves the fundamental rule of law that there is no assessment without a self-assessment or valid notice of deficiency. If you do not have either one, then you might be able to get the assessment declared null and void in court. Remember that the *Pietanzas*, *Butti*, *Gulluzzo*, and *Knudsen* all won on this very point of law.

None of the above cases mentioned the IRS’s problem of the assessment statute of limitations (“SOL”). However, the assessment SOL is at the heart of the defense. If your client filed a non-fraudulent tax return, it is important to request a court judgment expressly stating that there was no notice of deficiency. The reason for this is that the usual three-year assessment SOL will almost certainly have expired by the time the court case is resolved. Note, however, that there is no assessment SOL if no return was filed (that is the reason *Knudsen* settled after summary judgment was denied), or if the return was fraudulent. The assessment SOL is six years if more than 25% of gross income was not reported on the return. See Code §6501 for the exact law and see the detailed discussion of these rules in *How to Win Your Tax Audit*.

As a practical matter, most if not all of the SOL will be eaten up by the time the court issues its holding. Consequently, in all likelihood there will be no way for the IRS to properly assess your client after the Tax Court dismisses the case. Ultimately, that is why *Pietanza*, *Butti*, *Galluzzo* and *Knudsen* are great cases for taxpayers.

Scott MacPherson is a second-generation member of TFI. He is located in Phoenix, AZ.

LESSONS FOR DEMOCRATS FROM THE SOCIAL SECURITY TRUSTEES' REPORT

by Dr. Merrill Matthews

Several of the 2020 Democratic presidential candidates will propose increasing the Social Security benefit for current retirees. They'll suggest paying for it by increasing the Social Security payroll tax and eliminating the current cap on income (\$132,900) that's affected by the tax. Those candidates need to take a long, hard look at the latest annual report from the Social Security trustees.

(The report is available at: <https://ipi.us2.list-manage.com/track/click?u=236713c0eb5508a7a8a8c680e&id=efad22d322&e=2ab411db23>.)

There are important lessons in that report, if only Democrats will learn them.

Lesson 1: A strong, private sector economy improves the Social Security trust funds.

The trustees tell us that the 75-year actuarial deficit—i.e., the amount Social Security will have to pay out above its expected revenue—improved slightly, from 2.84% of taxable payroll in the 2018 report to 2.78%.

However, the reason for that slight improvement, even as Social Security had to pay more benefits—\$946 billion cited in the 2018 report to \$994 billion in the current report—is the strong economy with historically low unemployment rates.

More people working in the private sector means more payroll tax revenue. It might not be enough to make a major difference in the trust funds, since the unfunded liabilities are too large, but at least it makes a small positive difference.

Lesson 2: Social Security is still headed for bankruptcy.

The Old-Age and Survivors Insurance (OASI) Trust Fund that covers about 53 million mostly seniors is still scheduled to be depleted by 2034—just 15 years from now.

At that point the trustees estimate that Social Security will only be able to pay about 75 cents on the dollar. And that's only if you believe that the trust funds, with a reported \$2.9 trillion in assets, really exist.

Congress has borrowed all of that money and spent it. Congress can only replace those funds by taking other tax revenue or borrowing more money. In other words, that \$2.9 trillion in the trust funds should be considered a liability, not

an asset.

Lesson 3: The financial challenges will only worsen.

Democrats will say they can solve the problem by raising taxes. But the trustees claim that the increase would have to be 2.78% of payroll. And that's just to keep the status quo. Democrats want to increase current benefits—by 2% in one proposal.

And the population continues to age, which means that fewer workers will be available to support each retiree.

Even as most private sector companies have transitioned their pension plans to 401(k) accounts to improve their financial stability and avoid long-term liabilities, Democrats want to move in the opposite direction.

The best lesson Democrats could learn from the trustees' report is that all the tweaking of Social Security's taxes and benefits over 80 years have only made the financial challenges worse. It is time to follow the private sector's 401(k) approach and solve the problem for good.

Dr. Merrill Matthews is a resident scholar with the Institute for Policy Innovation. See: ipi.org.

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