New rules for Form 1099-K...
and what to do if you receive one

Background. The American Rescue Plan Act of 2021 modified reporting for Form 1099-K. Payment settlement entities (PSEs), such as banks, and third-party settlement organizations (TPSOs) such as PayPal, CashApp and Venmo, that settle cash and credit card transactions, are responsible to report payment information to the IRS, and provide Form 1099-K to recipients. Eventually, payments for goods and services, rents, gifts, personal settlements, and other transactions through PSEs and TPSOs of $600 or more will require some reporting. A reportable payment transaction for Form 1099-K includes a *payment card transaction* or a *third-party network transaction*.

A *payment card transaction* is any transaction in which a payment card, or any account number or other identifying data associated with a payment card, is accepted as payment. Payment cards include credit cards, debit cards, gift cards, flexible spending arrangement cards and health reimbursement arrangement cards. A TPSO is the central organization that has the contractual obligation to make payment to the participating payees of third-party network transactions. Additionally, a *third-party network transaction* is any business transaction that is settled through a third-party payment network.

Transition rules. Calendar years 2022, 2023 and 2024 are regarded as transition periods for purposes of implementation, and IRS enforcement and administration. For calendar years beginning before January 1, 2024, a TPSO is not required to report payments in settlement of third-party network transactions with respect to a participating payee unless the gross amount of aggregate payments to be reported exceeds $20,000 and the number of such transactions with that participating payee exceeds 200. The IRS will not assert penalties for TPSOs failing to file or failing to furnish Forms 1099-K unless the gross amount of aggregate payments to be reported exceeds $20,000 and the number of transactions exceeds 200.

For 2024, the IRS is planning for a threshold of $5,000 as part of the phase-in. Beginning in 2025, the threshold for filing is substantially reduced to $600 for gross payments of goods or services, and there is no threshold on the number of transactions. **Many PSEs and TPSO's have already established processes to report 2023 transactions of $600 or more, and may begin sending Forms 1099-K at the lower thresholds in January 2024.**

Form 1099-K includes the gross amount of all reportable payment transactions. The gross amount of a reportable payment does not include any adjustments for credits, cash equivalents, discount amounts, fees, refunded amounts, or any other amounts. The dollar amount of each transaction is determined on the date of the transaction.

The IRS is currently working to clarify which transactions are and are not reportable on Form 1099-K. More guidance is expected in the coming months.

Backup withholding requirements. Beware. Certain payers are required to perform backup withholding by deducting and withholding income tax from a reportable payment when, among other circumstances, the payee fails to furnish his/her taxpayer identification number (TIN) to the payer, or the IRS has notified the payer that the TIN furnished by the payee is incorrect. Any amounts withheld by the payer are included on a box within Form 1099-K.

What to do if you receive Form 1099-K

First, take time to verify all reported information is correct, including name and TIN. Verify the amounts reported on Form 1099-K, including all components that aggregate to the numbers. Recipients may need to contact the issuer (or payer) of the Form 1099-K to obtain transaction details, or correct errors. With support, errors may also be corrected on tax returns.

It is important to understand that amounts reported on Form 1099-K may, or may not, constitute

taxable income to the recipient. Form 1099-K reports the gross amount of payments. The gross amount from Form 1099-K is reported in your income tax return. Discounts, service fees, refunds and other costs should not reduce the gross amount reported. Costs and expenses are offsets, and are reported as deductions (or as cost basis reductions) in tax returns.

For many recipients, only a portion of the total amount reported on Form 1099-K is taxable. For example, the sale of a personal item may not be entirely taxable, as only gain, if any, is taxable. It is also possible that none of the amount reported is taxable. For example, private transactions including friend and family transactions, transfers, gifts, or reimbursements, are likely not taxable.

Recordkeeping becomes much more important to help separate and support the components reported on Form 1099-K and any offsets to arrive at taxable income. Documents should identify "who, what, where, when and why" and support all amounts (or gross proceeds) reported on Form 1099-K, and any direct offsets. In other words, taxpayers must keep contemporaneous records (i.e., invoices, receipts, contracts and other documents) of income, and offsetting costs and expenses.

IRS rules surrounding Form 1099-K state that personal transfers from family and friends should not be reported on Form 1099-K. However, many apps and payment processors (such as PSEs and TPSOs) are not able to distinguish personal transactions from reportable transactions. So the burden is on recipients to support non-taxable transactions and deductions.

Businesses. It is important that your business books and records reflect all your business income accurately, including details of amounts reported on Forms 1099-K. You must report on your income tax return all income you receive. In most cases, your business income will be in the form of cash, checks, wire transfers, and debit/credit card payments. Forms 1099-K will likely report a portion of your business income. Additionally, you should maintain documentation to support both business income and deductions you report on your income tax return. Again, Forms 1009-K may or may not report taxable transactions. Businesses are now required coordinate (or reconcile) Forms 1099-K with their business tax returns.

You should be aware that Form 1099-K reports transactions by month. Individuals and businesses should ensure that their transactions are reported with proper dates within their records, books and ultimately financial statements. Is possible that the IRS will use the monthly reporting from Forms 1099-K to ensure that estimated income tax payments are made timely, and in the proper period.

We are here to assist.

Please contact your tax return preparer if you would like assistance understanding Form 1099-K.

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