

Everything is not fine

A few years ago, I testified as an expert witness in a case where a physician was in an abusive 401(k) plan with life insurance. It had a so-called “springing cash value” policy in it. The IRS calls plans with these types of policies “listed transactions.” The judge called the insurance broker “a crook.”

Keeping that in mind, you should know that the IRS is cracking down on small business owners who participate in tax reduction insurance plans and the brokers who sold them. Some of these plans include defined benefit retirement plans, IRAs, or even 401(k) plans with life insurance.

Who is involved

For the business owner, the motivation is a large tax deduction. For the insurance broker and the insurance carrier, the motivation is a substantial commission. Thus, the IRS is cracking down on accountants, insurance brokers and others.

If your client is (or was) in a 412(i), 419, captive insurance, or Section 79 plan, then you may be in big trouble.

If you are an accountant and signed a tax return for a client in one of these plans, you are probably what the IRS calls a “material adviser”

and subject to a maximum \$200,000 fine.

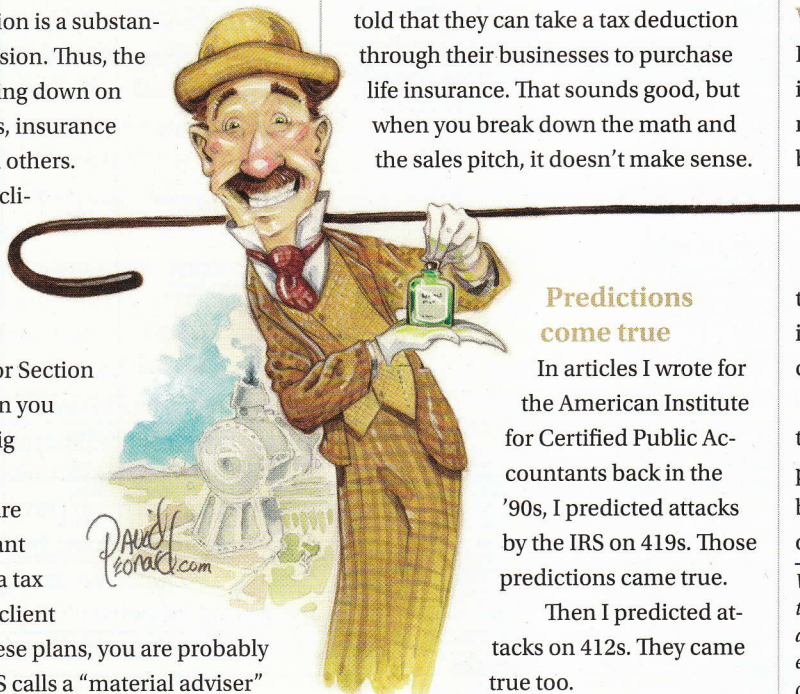
If you are an insurance professional that sold or advised on one of these plans, the same holds true for you.

What happened

Both business owners and brokers need to file properly under Section 6707A or face large IRS fines. In many cases, the accountant filed the appropriate forms, but the IRS still levied the fine because the accountant made a mistake when filling out the form.

The improper preparation of these forms usually results in the client being fined more quickly than if the form were not filed at all. My office has reviewed many forms and we have not yet seen one that was filled out properly.

The IRS will be soon attacking Section 79 scams as well, I am told. In Section 79 scams, small business owners are told that they can take a tax deduction through their businesses to purchase life insurance. That sounds good, but when you break down the math and the sales pitch, it doesn't make sense.



Predictions come true

In articles I wrote for the American Institute for Certified Public Accountants back in the '90s, I predicted attacks by the IRS on 419s. Those predictions came true.

Then I predicted attacks on 412s. They came true too.

Now I'm predicting that these Section 79 scams will be attacked.

How to act

To protect themselves, everyone in these Section 79 plans should file protectively under Section 6707A, and anyone who has not filed protectively in a 419 or 412(i) had better get some good advice from someone who knows what is going on and has extensive experience filing protectively.

The IRS has its task forces auditing these plans now; after that, they will move on to the Section 79 scams and the brokers who sold them.

I have been an expert witness in a lot of cases involving 412(i) and 419 issues. They rarely go well for brokers, accountants, plan promoters, or insurance companies.

Watch your back

If you are an insurance professional, it's important to understand that you should not count on your insurance company to back you up.

Based on what I have seen, insurance companies are more likely to stab you in the back. In an IRS investigation, the insurance companies settle first, leaving the brokers hanging. Then, in many cases, they fire the brokers.

So be careful. If you sold plans, gave tax advice, or signed a tax return and got paid a certain amount of money, you may be a material adviser, and subject to a fine of up to \$200,000. **EBA**

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