

IRS 1099 Reporting Requirements for Attorneys

This article explains why attorneys might receive a Form 1099 reporting certain amounts paid to them in the course of their practice, and why it is a “Big Deal.”

What Is a Form 1099?

A Form 1099 is an “Information Return” used to report payments of certain items of income. This form notifies the recipient that the specified amounts paid to them during the calendar year are being reported to the IRS. There are 20 different types of 1099 forms used to report various items of income. A common example is Form 1099-INT, which reports interest earned by the recipient during the calendar year.

When Is a Form 1099 filed?

Form 1099 reporting is based on a calendar year. The reporting entity must issue a copy (1) to the recipient by January 31 following the calendar year-end or February 15 following the calendar year-end for gross proceeds paid to attorneys; and (2) to the IRS on paper by the last day in February following the calendar year-end, March 31 following the calendar year-end if filing electronically, or January 31 following the calendar year-end if any payments for nonemployee compensation are reported in Box 7 on Form 1099-MISC. Electronic filing may be mandated, depending on several factors concerning the quantity of the reporting entity’s other required filings with the IRS.

Who Must File 1099-MISC Forms?

Any individual, corporation, partnership, limited liability company, or limited liability partnership *engaged in a trade or business* must file a Form 1099-MISC for certain payments made in the course of its trade or business to another person or a noncorporate business entity in any calendar year. However, a reporting entity must also file a Form 1099-MISC for *payments to all attorneys*, even if the attorney’s law practice is incorporated.

What Types of Payments to Attorneys Must Be Reported?

Payments of \$600 or more in a calendar year strictly for legal services must be reported by the payor (business entity) on Form 1099-MISC (in Box 7). Payments of \$600 or more in a calendar year to an attorney that contain any amount of settlement proceeds must be reported on Form 1099-MISC (in Box 14).

So What’s the Big Deal?

The big deal concerns settlement payments (gross proceeds) payable to attorneys. Pursuant to Internal Revenue Code Section 6045(f), when an attorney or law firm is the payee on a payment containing gross proceeds in connection with legal services, (i.e., a payment containing settlement proceeds in addition to legal services) the

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payor (usually an insurance company) must report the entire amount in Box 14 of Form 1099-MISC as gross proceeds paid to the attorney/recipient. This is required even if the attorney is not the sole payee. Consequently, the attorney must carefully track the receipt and disposition of these types of combined payments to clearly reflect on the firm's tax return the proper amount of income. One possible approach is to show the gross amount received as income, corresponding to the amount reported on the Form 1099-MISC in Box 14, and then show the amounts disbursed to the client and others as either Returns and Allowances or as a specific line item of Expense. Another option is to have the insurance company issue two separate checks – one to the attorney for attorney fees and costs, and the other to the claimant for the settlement award. A third possibility is to have the insurance company issue only one check payable to the claimant, out of which the claimant pays the attorney for legal services rendered and costs advanced.

Here are some examples to help illustrate these points:

Example 1. Attorney (A) receives a settlement check for \$300,000 from Payor (P) jointly payable to (A) and Client/Claimant (C). From this amount, A will subtract her fee and case costs and will pay the balance to C as net settlement proceeds. P will report the entire amount of \$300,000 on Form 1099-MISC (in Box 14) as paid to A. On A's records and tax returns, A will separately reflect the entire proceeds received and the related disbursements. The net income resulting should equal the fees retained for the matter. If the award is taxable income to C, then P will also issue a Form 1099-MISC in the amount of \$300,000 to C. C will then account for the income and related legal expense on C's tax return. If the settlement is a nontaxable award for personal physical injuries, then P will not issue a Form 1099-MISC to C.

Example 2. At A's request, P issues two checks that are delivered to A. One check is payable solely to A for \$100,000, representing compensation for legal services. The other check is payable solely to C in the amount of \$200,000. P will report only the \$100,000 on Form 1099-MISC (in Box 7) as paid to A. A only needs to record this amount on the firm's records and tax returns. P will also file a Form 1099-MISC reporting \$300,000 as paid to C. (Current law requires the claimant to report the entire amount of the settlement payment – \$300,000 in this case – as income, and then deduct the attorney fees as an itemized deduction, to the extent allowable.)

Example 3. P delivers a check in full payment of the settlement to A's office. The check is payable solely to C. P does not file a Form 1099-MISC reporting payment to A

because A is not a payee. P will, however, file a Form 1099-MISC reporting the full amount of the payment to C.

More complicated situations, such as those involving multiple attorneys as payees, are beyond the scope of this article. You should consult with your tax advisor regarding any scenarios involving receipt of settlement proceeds and related fees.

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