

The IMLA Municipal Attorney List—The IRS Cometh

by Warren Kraft

Not too many months ago, we completed an annual ritual of spring: filing our federal income tax returns (there's also state and local returns for those lucky enough to double or triple their annual dive into math, rules, and forms). Historically, an IRS invitation to personally visit one of its offices generates, in some folk, a nervous attack of significant proportions. Professional tax-return preparers often tout their willingness to defend their work on another's behalf in front of an auditor. Jokes and humorous anecdotes abound, and try to mask a taxpayer's nervousness, like the letter that begins:

> Dear IRS,
> I am responding to your letter denying the deduction for two of the three dependents I claimed on my 1998 Federal Income Tax Return.
> Thank you. I have questioned whether these are my children or not for years. They are evil and expensive.

But when the auditor comes knocking at the municipality's front door, well, it becomes serious business.

Needing Quick, Reasoned Guidance

Earlier this year, in at least one of IMLA's member communities, the dread visit occurred, with this request posted to the MCC/IMLA attorney listserve:

> Dear Friends,
> The IRS has sent us a letter telling us they are going to audit our practices as an employer, from city-owned vehicles to cell phones to you name it. I think we are in fair shape. Occasional posts to the listserv have helped us look at our practices these past few years. Thanks for those.
> Are there any big pointers or subtle points you would pass along to us to assure that our experience is a positive one for both us and the IRS? Thanks again.

Within a few hours, a colleague welcomed the poster "to the club," as his community was also being audited. Another asked if the municipal attorney could provide a copy of the audit letter, with several posting similar requests. Still another, who also represents a state municipal league, suggested a notice be prepared to send out to member communities. "A lot of us would be interested in seeing what the IRS is doing," added another respondent.

Check the Attachments!

The transmittal letter in question asked for "only" three categories of information from 2008: Forms 941 from all four quarters, Form W-2s, and Forms 1099 (the latter two preferably in electronic format). The fourth bullet point referenced the five-page attachment which added ten more items to the request. (Proof that nothing is ever simple.) The municipal attorney is now off and running to ensure that every responsible department can produce the requested documents.

Not surprisingly, the attorney for the other community that received a similar letter replied that he, too, was busily collecting information and assembling documents: copies of policies dealing with employee benefits and reimbursements, all employment contracts and internal control procedures, disbursement/accounts payable records, independent financial audit reports, and so on.

In this rather unpleasant scenario, one can take comfort in the fact that commiserating at its best and electronically involves many more colleagues from across the country than in the olden days of telephone solicitations for help and guidance.

The End Result

About a month after the original post to the listserve, the municipal attorney provided this update to those inquiring minds:

> Dear Friends:
> I recently asked about other cities that were facing an imminent IRS audit of their fringe benefits to employees. I recall this striking a chord with quite a number of you. I thought I would report what we experienced so the rest of you may be as prepared as you can get to be....

The message contained assessments concerning cell phones, same-day meal per diem amounts, fixed cash employee incentives, clothing allowances, on-call employee use of municipal vehicles, the proper classification of a particular employee (whether or not a truly independent contractor), and a wage-claim settlement. It concluded with this message:

> Overall, we took the approach that this was an opportunity for us to learn about our accounting practices and to get them right. With the IRS making the calls, there isn't much lobbying that an employee or group of employees can do to request that we record any of these transactions as nontaxable events. It is what the IRS says it is. The auditor was equally proactive and we think we have a better relationship with the IRS as a result, and that we also have better accounting practices.

Akin to the general practitioner trained to diagnose both simple and

complex medical issues in a patient, the municipal attorney becomes the first stop for all legal matters facing the governing entity. It is not every day the IRS audits all taxpayers, or every municipality, but it is good to know that the everyday practical experience of others, widely shared through the MCC/IMLA listserve, will enable the municipal attorney to better respond, defend and protect the entity.

For those of you who would like to join the listserv, go to http://www.municode.com and select the *Listservs* link to get the page on *Mailing Lists*. Click on *Municipal Attorneys* to bring up the subscription page. Fill it out and hit *Subscribe*. To sign up for the Water Cooler, send an e-mail to MunicAttyWaterCooler@yahoogroups.com that identifies you and the local government you represent. You will get a response from YahooGroups asking if you want to join. Respond to the message as directed. **M**

Warren Kraft is an Assistant City Attorney/Director of Human Resources for the City of West Bend, serves as of counsel to the Murphy-Desmond law firm of Madison and as attorney for the Village of McFarland, WI. A 2006 IMLA Local Government Fellow, he is a commissioned lay pastor, an active Scout leader, and a substitute lifeguard at the local YMCA.

INTERNATIONAL MUNICIPAL LAWYERS ASSOCIATION

IMLA CAREERS



JOBS! In 2008, IMLA introduced an online job board, IMLA Careers, aimed specifically at serving the needs of the local government legal community. See http://careers.imla.org (or click on Careers on the IMLA homepage, www.imla.org). Rates are posted on the site—and IMLA members are entitled to discounted rates for using the site!



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