

Fishing Information Newsletter

News You Can Use from the Internal Revenue Service

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Message from the Editor

It is our goal to make this newsletter the most useful and informative to you as possible. If there is a topic that you would like addressed in an upcoming newsletter, or if you have a fishing-related question you would like answered, please send us your topic ideas and questions and we will make certain they are addressed in future issues.

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Please send us your topic ideas and questions....

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Tax Form Reminders – What forms to have on hand during the fishing season

If you employ crewmembers/sternmen in your fishing operation, you are required to file either Forms 1099-MISC or employment tax forms (Forms 940, 941, and W-2). In order to complete these forms you will need the crewmember/sternman's name, address, and social security number. Use Form W-9 (Request for Taxpayer Identification Number and Certification) to secure the necessary information to complete Form 1099-MISC. Conversely, use Form W-4 (Employee's Withholding Allowance Certificate) to complete Form W-2.

Certain fishermen who work on a fishing boat are considered to be self-employed for purposes of employment and self-employment taxes. A fisherman

is considered self-employed if he meets all of the following conditions:

1. He receives a share of the catch or a share of the proceeds from the sale of the catch.
2. His share depends on the amount of the catch.
3. He receives his share from a boat (or from each boat in the case of a fishing operation involving more than one boat) with an operating crew that is normally made up of fewer than 10 individuals. This requirement is considered to be met if the average number of crew members on trips the boat made during the last 4 calendar quarters was less than 10.
4. He does not get any money for his work (other than his share of the catch or of the proceeds from the sale of the catch), unless the pay meets all of the following conditions.
 - a. He does not get more than \$100 per trip.
 - b. He is paid only if there is some minimum catch.
 - c. He is paid solely for additional duties (such as for services performed as mate, engineer, or cook) for which additional cash payments are traditional in the fishing industry.

If the above conditions are met, the fisherman is considered self-employed and must receive a Form 1099-MISC. He reports his income on a Form Schedule C. The crewmember/sternman must provide his name, address and social security number to the employer. This information may be secured on Form W-9.

If the above conditions are not met, the fisherman is an employee and must receive a Form W-2. He reports his income on Line 7 of Form 1040. The crewmember/sternman must provide his name, address, social security number, and withholding allowances to the employer. This information must be secured on Form W-4.

The applicable Form (W-2 or 1099-MISC) **must** be 1) furnished to the crewmember/sternman no later

than January 31st, and 2) filed with the IRS no later than February 28th of the year following the calendar year of the payment(s). Forms 941 are due quarterly, and Forms 940 are due January 31st.

The law provides a penalty of \$50 for each Form 1099-MISC that is not *furnished* to an individual who provided service. There is also a penalty of \$50 for each Form 1099-MISC that is not *filed* with the Internal Revenue Service when it is due.

If you are unable to secure the social security number of any person you pay in the course of commercial fishing or other business activities, the law requires you to withhold income tax at the rate of 31%. If you were required to withhold 31% and did not, you may be held liable for the required withholding. The tax may be assessed against you and collected from you personally.

If a crewmember/sternman fails to furnish a correct social security number to the requester, he may be assessed a penalty of \$50 for each such failure.

For further information see Publication 15 (Circular E, Employer's Tax Guide), Instructions for Form 1099, and Publication 595 (Tax Highlights for Commercial Fishermen). **Forms W-9 and W-4 should be kept on the vessel or hiring office.**

"Cash" Payments for Fish Purchases - Form 1099-MISC Requirements

Persons in the trade or business of purchasing fish for resale must report total cash payments of \$600 or more paid during the year to any person who is engaged in the trade or business of catching fish. They are required to keep records showing the date and amount of each cash payment made during the year, and they must report the total amount paid for the year on Form 1099-MISC.

"Fish" means all fish and other forms of aquatic life.

"Cash" means (1) U.S. and foreign coin and currency and (2) a cashier's check, bank draft, traveler's check, or money order. Cash does not include a check drawn on the fish purchaser's personal or business account.

If you are in the trade or business of purchasing fish for resale, you must report total "*cash*" payments of \$600 or more paid during the year to any person who is engaged in the trade or business of catching fish.

In the reverse, if you are in the trade or business of selling fish, any "cash" buyers purchasing fish from you should be issuing you a Form 1099-MISC for "*cash*" payments of \$600 or more that they paid to you during the year. Since the "cash" buyer was only required to report total "cash" sales, only the "cash" sales will be reflected on the Form 1099-MISC. "Non-cash" payments that you received for fish will not (generally) be included on Form 1099-MISC. These "non-cash" payments for which no Form 1099-MISC was received are still taxable to you. Your return must report total gross fish sales received from all sources and in all formats (i.e. all "cash" and "non-cash" sales proceeds must be reported).

If you have received a Form 1099-MISC from one or more "cash" buyers and all the transactions you had with these buyers were in the form of "cash" sales, you should reconcile your fish tickets with the Forms 1099-MISC and report the correct amount of total gross fish sales from all sources on your return.

If you have received a Form 1099-MISC from a "cash" buyer and there were other transactions you had with this buyer, such as your cannery account was credited with fish deliveries and you later received a settlement check(s), you should reconcile your fish tickets and the Form 1099-MISC with year-end cannery statement(s) and report the correct amount of total gross fish sales from all sources on your return.

When reconciling, keep in mind that if you provided services to a fish buyer (other than as an employee) and received payments of \$600 or more during the year for these services, you should also receive a Form 1099-MISC for this income. If completed properly, the payor will designate these payments as "nonemployee compensation" in box 7 of Form 1099-MISC. Nonemployee compensation is reportable on Schedule C, Profit or Loss from Business, and is subject to self-employment tax.

If you only reported the amounts reflected on the Forms 1099-MISC for “cash” sales of fish and also had “non-cash” sales of fish, you must file an amended return (Form 1040X) to correct the error and fully report your fish sale income.

Your Questions Answered

Estimated Tax Payments Penalty – Special Rules for Fishers

Q If I incorporate my fishing business and elect to be taxed as a Subchapter S corporation, will I still be eligible for the special rules for farmers and fishers when determining my required estimated tax payments?

A Publication 505, Tax Withholding and Estimated Tax, provides the answer to this question on page 22. A fisher who has at least two-thirds of gross income from fishing only has one estimated due date for the 2000 tax year, which is January 15, 2001. Assuming a fisher has at least two-thirds of their gross income from fishing, the January 15, 2001 estimated tax payment is not required as long as the 2000 return is filed by March 1, 2001, and all taxes owed are paid by this date.

When determining if at least two-thirds of a fisher’s gross income is from fishing, include the following amounts as fishing income:

- 1) Income from services as an officer or crew member of a vessel while the vessel is engaged in fishing.
- 2) Your share of a partnership's or S corporation's gross income from farming.
- 3) Income from services normally performed in connection with fishing. This includes shore service as an officer or crew member of a vessel engaged in fishing and services that are necessary for the immediate preservation of the catch, such as cleaning, icing, and packing the catch.

If a fisher is a 100% shareholder of an S corporation, all net income earned by the S corporation and all of the other items that must be separately stated on the Schedule K-1 will be reported on the fisher’s Form 1040 return. If the fisher owns less than 100% of the S corporation, only the fisher’s share of the S corporation's items flow to the fisher’s return.

In determining whether the individual fisher’s gross fishing income is at least two-thirds of the fisher’s total gross income, the fisher’s share of each type of S corporation gross income (i.e., fishing and non-fishing) will be included in the computation. If the total gross fishing income is at least two-thirds of the total gross income, the fisher is allowed to use the special “fishing” methodology of determining estimated tax payment requirements as discussed above.

The mere fact of incorporating a Schedule C fishing business into an S corporation will not affect the fisher’s estimated tax payment requirements unless, as a whole, the fisher’s gross income from fishing sources falls below the two-thirds requirement.

Bad Debt from Bankrupt Fish Buyer

Q I am a fisherman who sold salmon to a buyer who never paid us and subsequently went bankrupt. Can you tell me how to incorporate that loss into my taxes?

A The answer to your question depends upon the accounting method used for your business.

Most individuals and many small businesses with no inventory use the cash method of accounting. However, if an inventory is necessary to account for your income, you must use an accrual method of accounting for at least sales and purchases.

Under the cash method, you include all items of income actually or constructively received during the year in gross income for that year. Under the cash method of accounting, you must generally deduct expenses in the tax year in which you actually pay them. However, an expense paid in advance can be deducted only in the year to which it applies.

Under the accrual method of accounting, income is generally reported in the year earned and expenses are deducted or capitalized in the year incurred. The purpose of this method of accounting is to match income and expenses in the correct year.

The accounting method is chosen when you file your first return for your business. Changing your

accounting method can only be done with the consent of the IRS.

The loss you have experienced is considered a business bad debt. Whether or not you can deduct the bad debt depends upon your accounting method and whether you have previously included the fish sales in your business income. For credit sales, in order to claim a bad debt deduction you must have previously included the credit sales in your business income.

Cash method taxpayers only include in income amounts actually or constructively received. Since you did not receive the fish sale income, if you are using the cash method of accounting you would not have previously included this in your business income. As a result, when the income isn't received, there is no deductible business bad debt. You still have experienced a loss and have a bad debt, it just isn't a type of bad debt that can be deducted on your tax return.

On the other hand, an accrual method taxpayer would normally have included the fish sales in their business income in the year it was earned (i.e., the year the fish were sold). Assuming that you were on the accrual method and assuming you actually did include these fish sales in your income in the year of the sale, then a business bad debt is allowed in the year the debt becomes worthless.

If a bad debt is allowable, it is claimed on the appropriate line on the return. For schedule C taxpayers, it is deducted on Line 9; Form 1065 (partnership) filers, on line 12; Form 1120 (corporation) filers, on line 15; and Form 1120S (Subchapter S corporation) filers, on line 10.

Upcoming Newsletter Topics ...

- Per Diem Issues
- Self-Employment Tax Issues
- Collection Due Process Procedures
- Appropriate Salary Payments for S Corporation Shareholders/Crewmen

Tax Assistance Hotline, Forms Hotline, Internet Access

Taxpayer Assistance

Phone Numbers:

(800) 829-1040 Seven days a week, 24 hours a day
(800) 829-4059 TTY/TDD (Hearing Impaired)
Seven days a week, 24 hours a day

Tax Forms and Publications

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Order free tax forms and publications.

IRS Internet Access

World Wide Web: www.irs.gov

The IRS Web Home Page allows convenient access to tax information 24 hours a day. The Web Site provides tax forms with instructions, publications, the latest tax law changes, and much more information for individuals and businesses.

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