MSP #14 SHARING ECONOMY: Participants in the Sharing Economy Lack Adequate Guidance From the IRS

RESPONSIBLE OFFICIAL

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- *The Right to Quality Service*
- *The Right to a Fair and Just Tax System*

DEFINITION OF PROBLEM

The "sharing" economy (also known as the gig economy) can be described as "collaborative consumption" or a "peer-to-peer market" that links a willing provider to a consumer of goods or services (coordinated through a community-based online service). Typically, there are three parties involved in a sharing economy transaction. Here, we will refer to them as *service providers* (the freelancers who provide the goods or services), *service recipients* (the consumers of such good or services), and *service coordinators* (the third-party platforms that facilitate the transactions).

A 2016 survey of members of the National Association of the Self-Employed (NASE) revealed that:

- 34 percent of those who reported earning income in the sharing economy did not know they needed to file quarterly estimated tax payments;
- 36 percent did not understand what records they would need to maintain as a small business for tax purposes;
- 43 percent did not set aside money to meet their tax obligations or know how much they owed; and
- 69 percent did not receive any tax information from the sharing economy platform they used to earn their income.[2]

These results demonstrate both the need for guidance from the IRS and the opportunity to create a culture of tax compliance among participants in the sharing economy from the outset. Establishing the tax compliance norms for this emerging sharing economy industry in its infancy will assist the IRS as this segment of taxpayers grows.

1 *See* Taxpayer Bill of Rights (TBOR), http://www.TaxpayerAdvocate.irs.gov/Taxpayer-Rights. The rights contained in the TBOR are now listed in the Internal Revenue Code (IRC). *See* Consolidated Appropriations Act, 2016, Pub. L. No 114-113, Division Q, Title IV, § 401(a) (2015) (codified at IRC §7803(a)(3)).

2 Written statement of Caroline Bruckner, Managing Director, Kogod Tax Policy Center (May 17, 2016). In this survey, 22 percent of respondents reported earning income in the sharing economy. The statistics reported above are percentages of those who reported earning income in the sharing economy. *See* Caroline Bruckner, *Shortchanged: The Tax Compliance Challenges of Small Business Operators Driving the On-Demand Platform Economy* (May 2016).

ANALYSIS OF THE PROBLEM

Proponents of the sharing economy believe it promotes marketplace efficiency by enabling individuals to generate revenue from assets while the assets are not being used personally. For example, a vacation home owner may rent out her home while she is not using it. Peer-to-peer services not only include short-term home rentals (Airbnb) and shared car services (Uber and Lyft), but also:

- Sharing a back seat with strangers (Hitch);
- Short-term car rentals (Relayrides);
- Selling handmade or vintage items (Etsy);
- Providing household errands (TaskRabbit); and
- Providing cleaning and greeting services to Airbnb properties (Happy Host).

Service providers in the sharing economy may not fit the mold of the traditional employee who works "9-to-5" for a singular boss and receives a Form W-2, *Wage and Tax Statement*, from an employer. Rather, they may view themselves as contingent workers or freelancers, serving hundreds of service recipients but with no set schedule. The sharing economy often includes an additional party in transactions — the service coordinator — which may or may not provide a Form 1099-MISC, *Miscellaneous Income*, to the service provider.

Scope of the Sharing Economy

According to a 2016 Pew Research Center survey, nearly a quarter of the U.S. population earned money from the sharing economy.[3] About eight percent of Americans earned money using digital platforms to perform a job or task; 18 percent earned money selling something online, and one percent rented out properties on a home-sharing site.[4] Revenue from the sharing economy is projected to increase from $15 billion internationally in 2013 to $335 billion by 2025.[5]

Although it may be growing at a healthy rate, the sharing economy may not be lucrative for all or most service providers in the sector. On the contrary, data show that the vast majority of gig workers — 85 percent — make less than $500 per month.[6] When taxpayers take on multiple gigs to help make ends meet, it makes tax compliance even more difficult; they receive information returns from multiple sources, so it may be difficult to track and allocate expenses.

Establishing the tax compliance norms for this emerging sharing economy industry in its infancy will assist the IRS as this segment of taxpayers grows.

3 Pew Research Center, Gig Work, Online Selling and Home Sharing (Nov. 17, 2016), www.pewinternet.org/2016/11/17/gig-work-online-selling-and-home-sharing/.

4 *Id.*

5 Pricewaterhouse Coopers, *The Sharing Economy* 14 (2015), https://www.pwc.com/us/en/technology/publications/assets/pwc-consumer-intelligence-series-the-sharing-economy.pdf.

6 Washington Post, *Side Hustles Are the New Norm* (July 3, 2017).

There are many reasons why the sharing economy has grown as much as it has.

- **Cost.** It is often less costly for service recipients to use services offered by providers who identify as independent contractors than to use services offered by traditional businesses with employees. Employers are required to pay employment taxes for employees, and many offer costly benefits to full-time employees (such as retirement plans, paid leave, and health insurance). By classifying service providers as independent contractors, service coordinators in the sharing economy can avoid these expenses and pass the savings along to service recipients.
- **Technology.** With mobile networks and smartphone apps, a sharing economy can tap pools of latent labor supply, allowing service providers to deliver in real-time. Service providers in the sharing economy can select engagements based upon how each job fits their own priorities and skills.
- **Lifestyle.** Service providers in a sharing economy enjoy greater flexibility, control, and variety than their full-time employed counterparts. For example, an Uber driver has the ability to work only when it makes sense for his schedule, whereas a full-time taxi driver may have to adhere to rigid schedules set by the employer.

Participants in the Sharing Economy May Not Fully Understand Their Tax Obligations

Understandably, many of the new service providers in a sharing economy may not fully comprehend their tax filing obligations or have any experience with the requisite tax record-keeping. These new entrants to the sharing economy will need to spend significant time learning about their tax compliance obligations and to devote many hours to recordkeeping. For example, the IRS estimates that it takes taxpayers nearly 40 hours to learn about depreciation methods, keep records, and report the depreciation to the IRS.[7] Yet, according to a recent survey conducted by NASE, 69 percent of entrepreneurs who participate in the sharing economy received absolutely no tax guidance from the companies with which they work.[8]

When looking at noncompliance, it is important to distinguish between the various types of noncompliance the IRS encounters. Not all noncompliant taxpayers are willfully noncompliant; many of them are tripped up by "unknowing" or "lazy" noncompliance.[9] That is, some taxpayers are simply unaware of their tax compliance obligations. The NASE survey results underscore the importance of educating sharing-economy entrepreneurs and merchants that they are operating a self-employed, small business and need to understand certain basic tax obligations (*i.e.*, making required quarterly estimated payments throughout the year to avoid penalties).

Much of the compliance burden can be alleviated if tax is collected by third parties and reported to the IRS and to the service providers. This works well for workers in an employee/employer relationship — the employer withholds income and employment taxes throughout the year and provides a Form W-2 to

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7 *See* 2016 Instructions to Form 4562, *Depreciation and Amortization*. The IRS makes the following estimates for completing this form:
Recordkeeping .... 30 hr., 22 min.
Learning about the law or the form .... 4 hr., 16 min.
Preparing and sending the form to the IRS .... 4 hr., 58 min.

8 National Association of the Self-Employed (NASE), http://www.nase.org/about-us/Nase_News/2016/04/29/nase-releases-new-survey-data-on-sharing-economy. The survey was sent in March 2016 to more than 40,000 small businesses and received over 500 responses, mainly from the self-employed, about their participation in the sharing economy.

9 Leslie Book, *The Poor and Tax Compliance: One Size Does Not Fit All*, 51 U. Kan. L. Rev. 1145 (2003).

the employer and the IRS after the close of the year. In fact, IRS tax gap data shows that 99 percent of wages subject to withholding and third-party information reporting is reported by taxpayers to the IRS.[10]

For workers who fall outside the parameters of a traditional employee/employer relationship, the process may get more complicated. A driver of a shared car service may receive a Form 1099-MISC in January, reporting the gross amount received in fares for the prior year, but the issuer of the Form 1099-MISC typically has not done any withholding. The service provider may not have been aware of the consequences of being classified as a non-employee and may not have set aside money for self-employment tax or made quarterly estimated payments. Other service providers in a sharing economy may not receive any information reporting from the service coordinators.[11] A 2016 survey found that only 32 percent of sharing economy service providers receive information reporting via Form 1099-K, *Payment Card and Third Party Network Transactions*, or Form 1099-MISC from their service coordinators — perhaps because coordinators are wary of being classified as employers.[12]

Service Providers in the Sharing Economy Have Turned to Online Forums for Tax Advice

The IRS has not issued industry-specific guidance outlining the common tax issues faced by participants of the sharing economy. Because of this vacuum, many service providers have turned to the internet to ask tax-related questions.

For example, many Uber drivers engage in an online forum where they can share information about or solicit advice on a wide range of topics.[13] There is even a sub-forum dedicated to tax compliance, focused on "1099 income, deductions, and the IRS."[14] Similarly, Airbnb hosts have created an online forum where hosts can share advice with other hosts, and there is a sub-forum dedicated to "Regulations/Tax Issues."[15]

There are certain advantages that these online forums enjoy over traditional sources of tax content. First, internet discussion forums can provide a real-time picture of the tax and related issues that concern ridesharing drivers. There is instantaneous reaction to an online post from other forum members who may have had similar experiences. Second, the anonymous nature of these forums may cause forum participants to be more candid and forthright than they might be in face-to-face discussions. Third, the back-and-forth nature of the discussion can flesh out and identify related issues, more so than a static IRS publication could.

However, there are some major risks for service providers in the sharing economy in relaying on information or advice gleaned from online forums. The information or advice may be incorrect, yet accepted by the group as correct. This can easily occur when the facts of one taxpayer's circumstances

10 IRS, *Tax Gap Estimates for Tax Years 2008-2010* (Apr. 2016).

11 The IRS requires payors to issue Form 1099-K, *Payment Card and Third Party Network Transactions*, only when the total number of transactions exceed 200 and the aggregate value exceeds $20,000 in a calendar year. *See* IRC § 6050W(e). Senator John Thune recently introduced legislation that would lower the threshold to $1,000 for payors to report payments on Form 1099-K, while raising the threshold for reporting payments to service providers on Form 1099-MISC to $1,000 (up from $600). *See* New Economy Work to Guarantee Independence and Growth Act of 2017, S. 1549, 115th Cong. (2017).

12 *See* Caroline Bruckner, *Shortchanged: The Tax Compliance Challenges of Small Business Operators Driving the On-Demand Platform Economy* 10 (May 2016). The National Taxpayer Advocate has proposed legislative recommendations to allow voluntary withholding on payments made to independent contractors. *See* Legislative Recommendation: *Amend Internal Revenue Code Section 3402(p) to Allow Voluntary Withholding for Independent Contractors*, *infra*; National Taxpayer Advocate 2007 Annual Report to Congress 493-94; National Taxpayer Advocate 2005 Annual Report to Congress 69.

13 *See* www.uberpeople.net (last visited Nov. 28, 2017).

14 *See* http://uberpeople.net/forums/Taxes/ (last visited Nov. 28, 2017).

15 *See* http://airhostsforum.com/c/regulations-tax-issues (last visited Nov. 28, 2017).

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differ in a slight, but significant, way from the situation discussed in an online forum. Furthermore, anti-government/anti-IRS sentiment may skew the forum discussion, to the point where high-risk tax-avoidance techniques may be accepted as norms.

Rather than ignore the existence of these online forums and the benefits they provide, the IRS should take an active role in such discussions. Certainly, the IRS could not provide specific tax advice through online forums and discussion groups, but it could answer general questions, link to the IRS website for relevant information, and provide the phone number for IRS assistors when appropriate. If the IRS wants to be really bold and proactive, it could designate a representative to respond to questions on a Reddit forum for Airbnb or Uber users. A benefit of these exchanges is that the IRS will learn about specific challenges and issues facing this segment of the economy and thereby do a better job of tailoring its guidance for both taxpayers and IRS employees. It is clear there is a segment of the sharing economy that seeks guidance on how to comply with their tax obligations. By proactively engaging in the discussion, the IRS can positively shape the norm for participants in the sharing economy.

The IRS Should Expand Its Education and Outreach to Sharing Economy Participants

If we operate under the premise that most taxpayers want to comply with the law, the IRS needs to expand its presence within the sharing economy to enable that compliance. Providers of services want to be educated about what is expected of them. There are many ways the IRS can provide improved taxpayer service to this growing sector.

The IRS could get more creative in repackaging existing content and tailoring it for participants in a sharing economy. For example, the IRS currently releases Publication 527, *Residential Rental Property*,[16] and Publication 463, *Travel, Entertainment, Gift, and Car Expenses*,[17] each year. While these publications contain helpful information, an Airbnb host would have to sift through the 24-page Publication 527, and an Uber driver would have to navigate through the 50-page Publication 463, and they still might not understand how these rules apply to themselves as service providers in a sharing economy.

This new publication for sharing economy participants need not be long and all-encompassing, but it should at a minimum provide a checklist of issues that first-time, self-employed persons participating in the sharing economy should be aware of. For example, this new publication should include information about the need to make estimated payments of income and employment taxes. It should also explain that self-employed persons pay both the employee and employer shares of employment taxes. The new publication should mention that self-employed persons generally need to file a Schedule C and generally may deduct expenses (*e.g.*, actual vehicle expenses for Uber drivers, or a standard vehicle expense based on mileage), provided they keep contemporaneous and accurate records. This new sharing economy publication should cross reference other IRS publications that provide more detail on these and a

16 *See* https://www.irs.gov/pub/irs-pdf/p527.pdf.

17 *See* https://www.irs.gov/pub/irs-pdf/p463.pdf.

few other issues that are relevant to service providers in a sharing economy. To be evenhanded, the publication should also briefly explain the factors underlying worker classification and cross-reference other IRS materials on that topic.

In addition, the IRS should consider developing a one-page brochure that touches on some very basic points relevant to service providers in a shared economy. For example, this brochure can point out the significant difference in tax treatment when a home is rented out for 14 days or less per year versus a home that is rented by an Airbnb host for more than 14 days.[18] This brochure could contain a link to the new publication on the sharing economy. The IRS should require third-party service coordinators to provide this brochure to service providers at the same time they receive the Form W-9, *Request for Taxpayer Identification Number and Certification*, along with the taxpayer identification number from the service provider.

The IRS recently created a dedicated web page containing tax tips for participants in a sharing economy.[19] The IRS could develop a series of webinars on topics of interest to participants in the sharing economy, and host them on the sharing economy web page. The IRS should develop a Frequently Asked Questions (FAQs) section that is updated periodically. The IRS should also designate liaisons to monitor online forums to identify emerging issues for the sharing economy and address them via FAQs while the IRS develops more formal guidance. (FAQs should not be a substitute for formal guidance.)

If the IRS wanted to be even more helpful, it could create and host an online "wizard" — a tool that could be extremely helpful to participants in the sharing economy. TAS is exploring doing just that, but we would welcome IRS involvement. Such an online wizard could walk taxpayers who are newly self-employed through the various steps one needs to take (*e.g.*, obtain an employer identification number, make estimated payments, keep books and records). It could contain a downloadable mileage log app for taxpayers to use, with pre-populated mileage rates for a given year. The IRS could develop a user-friendly calendar function that permits taxpayers to add the estimated tax payment due dates to their smartphone calendars. In past Reports to Congress, we have suggested that the IRS work with the Electronic Federal Tax Payment System to make it more user friendly (*e.g.*, allow taxpayers to schedule estimated tax payments with greater frequency).[20] There are many ways the IRS can embrace technology to deliver services that taxpayers need.

Taxpayers who attempt to reach the IRS with tax law questions should be able to speak to someone about their substantive tax issue. Driving taxpayers to online content may be the desired goal of the IRS's "Future State" plan, but there are times when a taxpayer needs to speak to a live assistor. Congress needs to provide the resources for the IRS to properly staff its phone lines to achieve an acceptable level of service, and it needs to hold the IRS accountable for answering tax law questions via the phone all

18 For someone using a dwelling unit for both rental and personal purposes, the tax treatment of the rental expenses depends on how many days the dwelling unit was rented out during the year. If the property is rented less than 15 days during the year, income from the rental shall not be included in the gross income of the taxpayer (and rental expenses may not be deducted). *See* IRC § 280A(g); IRS, Publication 527, *Residential Rental Property* 3.

19 *See* www.irs.gov/sharing (last visited Nov. 28, 2017).

20 National Taxpayer Advocate 2007 Annual Report to Congress 43-44.

year round. There should be no reason for such questions to be deemed "out of scope."[21] We are asking taxpayers to voluntarily comply with their tax obligations, and the IRS should be there to pick up the phone and answer questions.

RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Develop and publicize new guidance for sharing economy participants that includes a publication and a checklist of issues of which first-time, self-employed persons participating in the sharing economy should be aware.
2. Create a one-page brochure touching on some basic points relevant to service providers in a sharing economy and containing a link to the resources available for sharing economy participants.
3. Require third-party service coordinators to provide the one-page brochure on the service economy to service providers at the same time they receive the Form W-9, *Request for Taxpayer Identification Number and Certification*, from the service provider.
4. Partner with TAS to develop an online wizard for taxpayers in the sharing economy, which may include interactive online tools such as a mileage log app or an estimated tax payment calculator.
5. Designate liaisons to participate in online forums to identify emerging issues for sharing economy participants.

21 Internal Revenue Manual (IRM) 21.1.1, *Accounts Management and Compliance Services Operations, Accounts Management and Compliance Services Overview* (Oct. 1, 2017), provides instructions regarding the kinds of questions IRS customer service representatives may answer. IRM 21.1.1.3.1 (Jan. 15, 2016) provides that "the areas discussed below are beyond the level of service (out of scope) that CAS, Accounts Management will provide:
- Tax form and schedule preparation
- Tax planning
- Legal opinions
- Highly complex tax issues (limited service)."

Exhibit 21.1.1-1 (Oct. 1, 2017) contains a list of out-of-scope topics and forms. Out-of-scope items include entity classification, e-commerce, depreciation and amortization (including Section 179 deductions), and questions about tax software.