



INTERNAL AUDIT

Follow-up Report of 1099 Reporting

R-23-03

November 20, 2024

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Rating Matrix

Descriptor	Guide
High	Matters considered being fundamental to the maintenance of internal control or good corporate governance. These matters should be subject to agreed remedial action within three months.
Medium	Matters considered being important to the maintenance of internal control or good corporate governance. These matters should be subject to agreed remedial action within six months.
Low	Matters considered being of minor importance to the maintenance of internal control or good corporate governance or that represents an opportunity for improving the efficiency of existing processes. These matters should be subject to agreed remedial action and further evaluation within twelve months.

Distribution List

Title	For Action	For Information	Reviewed prior to release
Executive Director		*	*
Chief Financial Officer		*	*
Comptroller	*		
Assistant Comptroller	*		
Accounting Supervisor	*		*

Executive Summary

Introduction

The Audit Committee directed Internal Audit (IA) to conduct a preliminary assessment to determine if controls and processes over the issuing and reporting Internal Revenue Service (IRS) 1099 forms are designed adequately and operating effectively to ensure compliance with internal policies and procedures as well Internal Revenue Service (IRS) requirements and standard. The Audit Plan was approved by the Audit Committee on December 12, 2022.

IA completed the preliminary assessment phase on August 25, 2023. We completed the work in accordance with the International Standards for the Professional Practice of Internal Audit, published by the Institute of Internal Auditors (“IIA”). Due to the specialized nature of 1099 reporting and tax filings IA outsourced the final conclusions of this follow-up to High Impact CPA and received their final report on October 8, 2024. IA performed preliminary testing in this follow-up to prepare data for the CPA’s review. The full report from High Impact CPA can be seen on Attachment B of this report.

Background and Functional Overview

Initial Phase Background Information:

UTA’s Accounting department is responsible for the preparation and transmission of IRS forms 1099-MISC and 1099-NEC. Entities are required to complete Form 1099-NEC by January 31 to report payments of \$600 or more made in the previous tax year to each non-employee who performed services. Entities file a Form 1099-Misc by March 31, if filing electronically, to report payments of \$600 or more for items such as rent or medical and health care payments made to non-employees and certain vendors in the previous tax year.

Most payments made to entities organized as a corporation do not need to be reported on a form 1099-Misc. However, the IRS has given direction that payments made to corporations must be reported on Form 1099-Misc if the payments were medical and health care payments or gross proceeds paid to an attorney.

Starting in Tax Year 2022 Nonemployee Compensation (“NEC”) should be reported on Form 1099-NEC. Non-employee compensation refers to the money an entity pays to an independent contractor who performs contingent work. Therefore, non-employee compensation includes fees, commissions, prizes, and awards for any services completed.

Key features of this process include:

- Identifying which vendors to include in 1099 reporting
- Bulk Taxpayer Identification Number (TIN) matching
- 1099-MISC & 1099-NEC preparation
- Printing and mailing 1099 forms to vendor recipients
- Electronic reporting (E-File) final 1099 report to the IRS

Objectives and Scope

Initial Phase Scope:

The period of the preliminary assessment phase focused on payments made to vendors between January 1, 2022, to December 31, 2022, with the coinciding IRS reporting occurring in the spring of 2023. Additional periods were reviewed, as necessary.

The primary areas of focus for the audit were:

- Governance
- TIN Accuracy Testing
- 1099 Forms issued for claims paid UTA
- Similar Vendors Testing

Follow-up Phase Scope:

The period of the follow-up phase focused on payments made to vendors between January 1, 2023, to December 31, 2023, with the coinciding IRS reporting occurring in early 2024. IA limited the focus of the follow-up to the findings from the Preliminary Assessment.

- Finding R-23-03-1: Required 1099 Forms were not issued
- Finding R-23-03-2: Claims vendors, physicians and attorneys were not sent a 1099 Form

Summary

Initial Summary:

Audit testing found approximately 60 vendors that should have been issued a 1099 form but were not. The majority were paid medical claims and payments to attorneys. Management was not aware of the IRS' renewed emphasis on reporting these categories. Additional 1099 forms not reported were simply missed. This points to a need for a defined process, resources and emphasis, and training for staff.

Finance management took immediate action to disclose noncompliance with proper taxing authorities. As of May 2024, UTA legal counsel confirmed there is no outstanding noncompliance with the IRS or Utah State Tax Commission.

IA would like to thank management for their diligence and attention completing the engagement.

Follow-up Summary:

In follow up testing IA found that 35 vendors should have had form 1099 filed with the IRS by the Accounting department. IA provided this information to High Impact CPA for final testing and confirmation. The CPA concluded that 34 of the vendors required a 1099. The one that did not require a 1099 was a pharmacy.

Attachment A: Current Status of Recommendations

Audit Finding R-23-03-1

Required 1099 Forms were not issued

Risk Level: Medium

Preliminary Assessment Status

Criteria:

The IRS requires that entities report payments made to contractors totaling \$600 or more on form 1099 NEC "Non Employment Compensation."

Instructions for form 1099 NEC indicate that it should be used to report all payments for services performed for a trade or business by people not treated as its employees. Examples: fees to subcontractors, directors, and golden parachute payments.

Condition:

IA conducted testing of 1099 compliance on a sample of 15 vendors containing “LLC” in the name of the company. Nine of these vendors were eligible for a 1099 but were reported on a form 1099. Additionally, testing was conducted on vendors with similar names to determine if 1099s were missed due to aggregation errors. While there were no aggregation errors, IA did note two additional vendors that should have been issued a 1099 but were not.

Underlying Cause:

Eight of the nine vendors from the ‘LLC Test’ had a form W-9 saved in JDE, meaning UTA had the information necessary to properly report taxable amounts. This indicates that Accounts Payable has underdeveloped processes for identifying which vendors would need to receive a Form 1099 within the accounting system. In further detail:

- a. AP has historically operated lean and lacked the resources to develop and maintain a robust control process. The team is currently at six and now better resourced to implement controls.
- b. A former employee performed or was believed to have performed 1099 reporting. This process was not adequately passed on to the successor.
- c. The AP team did not receive sufficient training or instruction on properly validating if vendors would need to receive a Form 1099.

Effect:

Entities who information returns are not filed or not filed timely are subject to penalties from the IRS. The penalty varies from \$50 to \$280 per form in 2022, depending on how long past the deadline the business issues the form. If an entity intentionally disregards the requirement to provide a correct payee statement, there is no maximum penalty¹.

Recommendations:

- 1. Management should coordinate with Legal Counsel to develop a disclosure and mitigation strategy for unreported forms 1099.
- 2. Additional research should be conducted by management to identify if other vendors who received payments from UTA should have had a 1099 sent to them.
- 3. Accounts Payable staff should receive training on Form 1099 reporting procedures.

Management Response and Action Plan:

See Management Response for R-23-03-2.

Target Completion Date:

See Target Completion Date for R-23-03-2.

Current Status: See Current Status for R-23-03-2.

Audit Finding R-23-03-2 Claims vendors, physicians and attorneys were not sent a 1099 Risk Level:

Performance Audit Status

Criteria:

¹ Internal Revenue Service, “Information Return Penalties”, irs.gov, Internal Revenue Service, Last Revised 10-May-2023, <https://www.irs.gov/payments/information-return-penalties>

IRS instructions for Form 1099-Misc state that a company must file form 1099-Misc for each person in the course of your business to whom you have paid the following during the year.

At least \$600 in:

- *Rents (box 1);*
- *Prizes and awards (box 3);*
- *Other income payments (box 3);*
- *Generally, the cash paid from a notional principal contract to an individual, partnership, or estate (box 3);*
- *Any fishing boat proceeds (box 5);*
- ***Medical and health care payments (box 6);***
- *Crop insurance proceeds (box 9);*
- ***Gross proceeds paid to an attorney (box 10) (see Payments to attorneys, later);***
- *Section 409A deferrals (box 12); or*
- *Nonqualified deferred compensation (box 15).*

(Emphasis added by IA).

Additional instruction from the IRS indicates that the following are reportable payments to corporations; emphasis added by IA to indicate what applies in this situation.

The following payments made to corporations must generally be reported on Form 1099-MISC,

- *Cash payments for the purchase of fish for resale reported in box 11.*
- ***Medical and health care payments reported in box 6.***
- *Substitute payments in lieu of dividends or tax-exempt interest reported in box 8.*
- ***Gross proceeds paid to an attorney reported in box 10.***

*Payments to attorneys. The term “attorney” includes a law firm or other provider of legal services. **Attorneys' fees of \$600 or more paid in the course of your trade or business are reportable in box 1 Form 1099-NEC, under section 6041A(a)(1).***

Gross proceeds paid to attorneys. *Under section 6045(f), report in box 10 payments that:*

- *Are made to an attorney in the course of your trade or business in connection with legal services, but not for the attorney's services, for example, as in a settlement agreement;*
- *Total \$600 or more; and*
- *Are not reportable by you in box 1 of Form 1099-NEC.*

(Emphasis added by IA).

Further guidance can be found within IRS *General Instructions for Filing 1099 Misc and NEC Forms*.

Condition:

IA identified 53 medical practitioners and attorneys identified as “VC” vendors within JDE, indicating that the payments were made as part of a settlement with the Claims department. These vendors should have all received a 1099 Misc form and been included in what was reported to the IRS.

Underlying Cause:

UTA was not aware of the recent changes made to the Form 1099 Misc which added specific areas for reporting Medical payments and Gross Proceeds paid to Attorneys. Many “VC” vendors did not have a W-9 form collected.

Effect:

Entities who information returns are not filed or not filed timely are subject to penalties from the IRS. The penalty varies from \$50 to \$280 per form in 2022, depending on how long past the deadline the business issues the form. If an entity intentionally disregards the requirement to provide a correct payee statement, there is no maximum penalty

Recommendations:

1. Management should coordinate with Legal Counsel to develop a disclosure and mitigation strategy for unreported forms 1099.
2. Accounts Payable should require a completed W-9 before issuing any future claims payments.
3. Accounts Payable or the Accounting Supervisor should maintain an IRS e-news subscription to receive future updates to the Form 1099 reporting process².

Management Response and Action Plan:

Accounting management is aware of the need for internal processes and controls to ensure compliance with Internal Revenue Service (IRS) requirements specifically regarding the issuance of Form 1099. Audit Finding R-23-03-1 Required 1099 Forms were not issued Risk Level: Medium; and Audit Finding R-23-03 Claims vendors, physicians and attorneys were not sent a 1099 Risk Level: Medium; are both related to 1099 forms that should have been issued due to payments coming out of Claims and Insurance either for Personal Injury Protection claims or workers' compensation claims. In addition to reviewing internal processes related to 1099 issuance, management also sought counsel from our internal and external legal partners. We are also in the process of creating a Finance SOP between the Claims & Insurance and Accounting departments for IRS Form W9 Requirements for Claims Settlements which will help by triggering Accounting to determine the need for a 1099. Finally, we have added two new accounts payable analysts positions to the Accounting department to assist with the improved workflow and increased workload. Two staff members are subscribed to IRS alerts to make sure we insure timely implementation of changes like 1099 requirements.

Target Completion Date:

July 2024

Current Status: In progress

High Impact CPA identified 34 vendors that were not issued a 1099 but were required to under IRS guidelines. We recommend that the Accounting department consult with UTA's legal counsel on disclosure and remediation of the missed filings with the IRS. Further, Accounting should investigate why these filings were missed and make corrections to the control environment ahead of the 2025 filing period.

Management Response and Action Plan:

Accounting management is aware of the need for internal processes and controls to ensure compliance with Internal Revenue Service (IRS) requirements specifically regarding the issuance of Form 1099. Audit Finding R-23-03-1 Required 1099 Forms were not issued Risk Level: Medium; and Audit Finding R-23-03 Claims vendors, physicians and attorneys were not sent a 1099 Risk Level: Medium; are both related to 1099 forms that should have been issued due to payments coming out of Claims and Insurance either for Personal Injury Protection claims or workers' compensation claims. In addition to reviewing

² Management can subscribe to IRS alerts at the following website: <https://www.irs.gov/newsroom/e-news-subscriptions>

internal processes related to 1099 issuance, management also sought counsel from our internal and external legal partners. A Finance SOP between the Claims & Insurance and Accounting departments for IRS Form W9 Requirements for Claims Settlements has been drafted and reviewed. This will help trigger Accounting to determine the need for a 1099 by requiring a W9 from everyone receiving a payment. Finally, we have added two new accounts payable analysts positions to the Accounting department to assist with the improved workflow and increased workload. As of November 25th [sic] AP will be fully staffed. Two staff members are subscribed to IRS alerts to make sure we insure timely implementation of changes like 1099 requirements.

Target Completion Date: December 2024

Attachment B: High Impact CPA Report

Attachment begins on the following page.



High Impact CPA
Consultation Report – Utah Transit Authority 1099 Analysis
October 8th, 2024

High Impact CPA
1154 W. Fremont Ave
Salt Lake City, UT 84104
(435) 669-0718

Mike Hurst, Internal Audit Director

Utah Transit Authority

669 W. 200 S.

Salt Lake City, UT 84104

Dear Mr. Hurst,

We have completed our analysis of 2023 payment transactions processed by Utah Transit Authority (“UTA”) that were identified by the UTA Internal Audit Division where the payee should have potentially been issued an IRS form 1099-MISC or 1099-NEC. We performed our engagement within the professional standards set by the American Institute of Certified Public Accountants *Statements on Standard’s for Consulting Services No. 1*. We note this was not an assurance engagement, and thus offer no opinions on the financial condition of UTA.

Scope of Consulting Engagement

The scope of this engagement is limited to performing an independent, 3rd party analysis of transactions identified by UTA’s Internal Audit Division that occurred in calendar year 2023 to determine if any payees should have been issued either a Form 1099-MISC or 1099-NEC as defined by Internal Revenue Code Section 6041 and accompanying IRS publications and instructions. The scope of our engagement was only to determine reportability and is not a full recalculation of transactions.

Intended Users of Report

This report is intended for use by UTA’s Internal Audit Division and UTA’s management for internal decision-making purposes only. We do not authorize this report to be used or relied upon by any 3rd parties.

Methodology

We examined a total of 54 transactions paid to a mix of 35 different payees where single or aggregate payments exceeded \$600 during 2023. For each transaction we analyzed the characteristics of the transaction to determine if it could qualify as reportable on a Form 1099. We also reviewed w9’s submitted by payees to UTA to determine if any of the transactions should be excluded based on both the characteristics of the transaction and the legal and/or tax structure of the payee. Where w9’s were not available we relied on the characteristics of the transaction and our professional judgment in the interpretation of *IRC Section 6041* and the IRS *Instructions for Forms 1099-MISC and 1099-NEC (Rev. January 2024)*.

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Conclusion

We determined that 34 of 35 payees identified by the Internal Audit Division should have been issued a Form 1099. We found three primary reasons why these payees should have been issued a 1099:

1. Payments made to attorneys.

According to the IRS instructions for Form 1099-MISC and 1099-NEC:

“Generally, you are not required to report the claimant’s attorney’s fees. For example, an insurance company pays a claimant’s attorney \$100,000 to settle a claim. The insurance company reports the payment as gross proceeds of \$100,000 in box 10. However, the insurance company does not have a reporting requirement for the claimant’s attorney’s fees subsequently paid from these funds. These rules apply whether or not:

- *The legal services are provided to the payer;*
- *The attorney is the exclusive payee (for example, the attorney’s and claimant’s names are on one check); or*
- *Other information returns are required for some or all of a payment under another section of the Code, such as section 6041.*

For example, a person who, in the course of a trade or business, pays \$600 of taxable damages to a claimant by paying that amount to a claimant’s attorney is required to:

- *Furnish Form 1099-MISC to the claimant, reporting damages pursuant to section 6041, generally in box 3; and*
- *Furnish Form 1099-MISC to the claimant’s attorney, reporting gross proceeds paid pursuant to section 6045(f) in box 10.”*

We analyzed 15 payments for legal claims made to attorney’s or law firms on behalf of a claimant. Therefore, based on the final two bullet points in the instructions it is our opinion that 1099’s should have been issued.

2. Payments made for medical or healthcare purposes.

According to the IRS instructions for Form 1099-MISC and 1099-NEC, Box 6. Medical and Health Care Payments:

“Enter payments of \$600 or more made in the course of your trade or business to each physician or other supplier or provider of medical or health care services. Include payments made by medical and health care insurers under health, accident, and sickness insurance programs...”

We analyzed 29 payments made by UTA for medical or healthcare payments and determined that 1099’s should have been issued.

3. Payments to other individuals or businesses that should have been issued based on the information provided on Form w9 furnished to UTA by the payee.

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We reviewed the w9's submitted for five vendors and determined they should have been issued a 1099 based on the fact they were not S-Corporations or C-Corporations as defined by the internal revenue code.

4. Payees not requiring a 1099.

The one payee we determined should be exempt from receiving a 1099 was identified as a pharmacy that received five payments in the population provided. The IRS instructions for Form 1099-MISC, Box 6. Medical and Health Care Payments explicitly states that *"you are not required to report payments to pharmacies for prescription drugs."* We recommend UTA consult further with a tax attorney to help ascertain the IRS purpose for this exclusion and to ultimately determine the 1099 treatment for that vendor.

A list of vendor numbers and the determination of reportability can be seen in Appendix A of this report.

We sincerely appreciate the opportunity to work with UTA's Internal Audit Division and Management. If there are any questions regarding the content of this report, please reach out to High Impact CPA for further clarification.

Sincerely,

A handwritten signature in black ink that reads "David E. Lewis, CPA". The signature is written in a cursive style.

David E. Lewis, CPA

Principal, High Impact CPA

1154 W. Fremont Ave.

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Appendix A. Payee Analysis by Transaction

Transaction	Payee ID	Amount	Purpose	1099 Required
1	1462437	162.73	Pharmacy	No
2	1462437	162.97	Pharmacy	No
3	1462437	210.66	Pharmacy	No
4	1462437	163.19	Pharmacy	No
5	1462437	13.42	Pharmacy	No
6	1507528	1,699.50	Medical	Yes
7	1509009	600.00	Per w9	Yes
8	1514566	663.10	Per w9	Yes
9	1512242	75,000.00	Legal	Yes
10	1513143	3,000.00	Legal	Yes
11	1509628	21,255.00	Legal	Yes
12	1510638	32,000.00	Legal	Yes
13	1510811	3,000.00	Legal	Yes
14	1512241	57,491.90	Legal	Yes
15	1507464	700.00	Per w9	Yes
16	1510902	15,498.74	Legal	Yes
17	1510902	11,538.07	Legal	Yes
18	1513001	4,776.81	Legal	Yes
19	1515124	17,500.00	Legal	Yes
20	1515125	22,500.00	Legal	Yes
21	1515127	35,000.00	Legal	Yes

22	1515128	40,000.00	Legal	Yes
23	1515819	35,000.00	Legal	Yes
24	1516333	3,000.00	Legal	Yes
25	1457724	76.87	Medical	Yes
26	1457724	268.24	Medical	Yes
27	1457724	154.82	Medical	Yes
28	1457724	236.61	Medical	Yes
29	1497485	180.78	Medical	Yes
30	1497485	96.29	Medical	Yes
31	1497485	92.38	Medical	Yes
32	1497485	54.81	Medical	Yes
33	1503168	102.47	Medical	Yes
34	1503168	102.47	Medical	Yes
35	1503168	479.21	Medical	Yes
36	1506275	1,123.80	Medical	Yes
37	1508158	1,397.76	Medical	Yes
38	1508158	2,271.36	Medical	Yes
39	1508716	4,169.33	Medical	Yes
40	1509314	153.90	Medical	Yes
41	1509314	153.90	Medical	Yes
42	1509314	163.80	Medical	Yes
43	1509314	222.30	Medical	Yes
44	1510809	5,170.00	Medical	Yes

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45	1513571	5,479.00	Medical	Yes
46	1513766	202.99	Medical	Yes
47	1513766	747.30	Medical	Yes
48	1513767	586.72	Medical	Yes
49	1513767	255.86	Medical	Yes
50	1514034	691.65	Medical	Yes
51	1514562	3,000.00	Medical	Yes
52	1101615	5,161.20	Medical	Yes
53	1514470	16,325.00	Per w9	Yes
54	1205731	5,220.63	Per w9	Yes

Subtotals by Payee ID

Payee ID	Transaction Count	Transaction Total	1099 Required
1101615	1	5,161.20	Yes
1205731	1	5,220.63	Yes
1457724	4	736.54	Yes
1462437	5	712.97	No
1497485	4	424.26	Yes
1503168	3	684.15	Yes
1506275	1	1,123.80	Yes
1507464	1	700.00	Yes
1507528	1	1,699.50	Yes
1508158	2	3,669.12	Yes

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1508716	1	4,169.33	Yes
1509009	1	600.00	Yes
1509314	4	693.90	Yes
1509628	1	21,255.00	Yes
1510638	1	32,000.00	Yes
1510809	1	5,170.00	Yes
1510811	1	3,000.00	Yes
1510902	2	27,036.81	Yes
1512241	1	57,491.90	Yes
1512242	1	75,000.00	Yes
1513001	1	4,776.81	Yes
1513143	1	3,000.00	Yes
1513571	1	5,479.00	Yes
1513766	2	950.29	Yes
1513767	2	842.58	Yes
1514034	1	691.65	Yes
1514470	1	16,325.00	Yes
1514562	1	3,000.00	Yes
1514566	1	663.10	Yes
1515124	1	17,500.00	Yes
1515125	1	22,500.00	Yes
1515127	1	35,000.00	Yes
1515128	1	40,000.00	Yes

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1515819	1	35,000.00	Yes
1516333	1	3,000.00	Yes
Totals	54	435,277.54	

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