

Tom Rhodus Quoted on Taxes Discrepancies

Texas Lawyer

March 9, 2009

[Tom Rhodus](#), a Member of Gray Reed & McGraw, was quoted in the March 9, 2009 edition of Texas Lawyer on discrepancies in U.S. trade representative nominee Ron Kirk's taxes.

Beginning his practice with seven years of experience as a trial attorney with the Tax Division of the U.S. Department of Justice, Tom is an expert in navigating the confusing landscape of federal regulation and law enforcement. Combining his experience in government and private practice, Tom has taught courses in federal tax procedure as an adjunct professor at SMU's Dedman School of Law for over 25 years. Tom has also been privileged to represent some of the largest physician groups in Texas on an on-going basis in the numerous business, tax and regulatory issues that arise in their practices. He routinely represents clients in civil and criminal matters stemming from examinations conducted by the IRS, the Department of Health and Human Services, and other federal and state agencies. He has tried numerous cases the United States District Courts, the U.S. Tax Court, and the state courts.

Kirk's Stumbles Highlight Common Tax Pitfalls

By Miriam Rozen, Texas Lawyer

The U.S. Senate Finance Committee disclosed March 2 that a team of its staff members had found discrepancies in some of U.S. trade representative nominee Ron Kirk's tax records and returns. After poring over three years' worth of tax returns for Kirk — a partner in Vinson & Elkins and a former Dallas mayor — they found he owed the Internal Revenue Service nearly \$10,000, in part because he failed to report as income speaking fees that he gave to charity and did not have proper records for deducting some business entertainment expenses for Dallas Mavericks games.

Six Texas tax lawyers agree that Kirk's tax issues highlight the challenges facing firm partners who must tackle the substantive parts of a practice while maintaining bookkeeping standards detailed enough to evaluate and abide by all the intricacies of the federal tax laws.

"I don't think what Ron Kirk did showed any bad intent. I have no doubt that many law partners could be doing some of the same things," says G. Tomas Rhodus, a shareholder in the Dallas office of Gray, Reed & McGraw who previously served as a trial lawyer for the Tax Division of the U.S. Department of Justice.

J. Rob Fowler, a partner in Houston's Baker Botts who focuses on tax and employee compensation issues, agrees anyone can be tripped up by the complexity of the Internal Revenue Code and the rigors of complying with it, particularly as it applies to questions related to a law practice.

"There are a lot of areas for law firm partners that raise questions about how you are supposed to report something to the IRS," Fowler says.

William D. "Bill" Elliott, a Dallas tax solo who has served as chairman of the State Bar of Texas Section of Taxation, characterizes Kirk's errors as "small change." He does not believe Kirk did anything wrong but rather was snagged by technicalities.

In its March 2 release, the Senate Finance Committee notes the following: Its staff members submitted questions to Kirk on Feb. 6 related to his tax returns for 2005, 2006 and 2007. Kirk supplied written responses on Feb. 17. The committee staff asked Kirk about his speaking fees, which he routinely "assigned" to his undergraduate alma mater, Austin College, to fulfill his pledge for a scholarship fund at the school. Kirk assumed those fees weren't taxable, an assumption with which his tax preparer agreed. The speaking fees totaled \$37,750 for 2004, 2005, 2006 and 2007. The release says Kirk has determined that he should have reported the fees as income and then deducted them as charitable donations, adding approximately \$5,800 to his tax bill.

According to the release, in 2005, 2006 and 2007, Kirk deducted as business entertainment expenses \$17,382 worth of Dallas Mavericks basketball tickets. But he substantiated only \$9,900 as qualifying entertainment expenses, triggering another tax return amendment and incurring about \$2,600 more in taxes. He owes the additional tax because he didn't have proof he used the tickets for business entertainment.

Speaking generally, Bryan Camp, a Texas Tech University School of Law professor who teaches tax, says IRS substantiation requirements include providing receipts and information about the amount, time, place, business purpose and business relationship between the tax filer and the person or people being entertained.

Kirk also will amend his tax returns and pay an extra \$1,000 for deducting too high a percentage of his tax and accounting fees in 2005, 2006 and 2007.

In the three-page release, the committee noted Kirk has agreed to promptly file amended tax returns reflecting adjustments that will total approximately \$9,975.

Kirk did not return a telephone call seeking comment before press time on March 5. V&E spokesman Mark Curriden writes in an e-mail that the White House is handling media inquiries about Kirk. The White House press office did not return a telephone call seeking comment.

Camp says the errors Kirk made "are not in the same league" as those of former Health and Human Services secretary nominee Tom Daschle, who withdrew his nomination after an uproar over his taxes.

Daschle, the Finance Committee staff noted in a Jan. 31 statement, had benefited from the use of a car service as part of a business relationship in 2005, 2006 and 2007 — a service valued at \$255,256 for all three years. He initially had not reported the benefit as compensation and therefore had to amend his taxes.

Kirk's mistakes "are not necessarily minor," Camp says, "because you want people to do things right." But they are commonplace mistakes probably discovered only because of the "über-vetting" of Cabinet-level nominees, Camp says.

Elliott says lawyers are notoriously distracted record-keepers, who are too busy practicing law to worry about the level of detail the Internal Revenue Code seeks.

Rhodus believes few lawyers can truly follow all the stipulations of the tax code as it pertains to substantiating business expenses such as Kirk's Mavericks' deductions.

"The IRS regulations dealing with business entertainment expenses are exceedingly exacting. I hate to say the law is unrealistic, but even IRS agents recognize that there would probably be nobody who keeps the records the regulations require," Rhodus says.

Lawyers file taxes differently depending on whether they are partners, shareholders or associates. Nonetheless, all must substantiate that business entertainment expenses qualify under IRS rules in order to deduct them from their income, say Rhodus, Elliott and Camp.

Generally, there are three ways lawyers can handle business entertainment expenses: the firm pays for the entertainment; the lawyer pays and seeks reimbursement from the firm; or the lawyer pays and deducts the expenses from his income on his tax return.

At his 100-lawyer firm, Rhodus says, management policy is to step in to help the lawyers by having them seek reimbursement from the firm for business entertainment expenses. This way, the firm — not the lawyer — is responsible for filing for the deductions related to business expense.

"It's up to the law firm to serve as the gatekeeper for business entertainment expenses," Rhodus says. He says his firm requires lawyers incurring business entertainment expenses to seek repayment from the firm. The substantiation they give to the firm includes receipts and information about where the entertainment took place, with whom and what business purpose it served. The firm then deducts 50 percent of those expenses from its income, and the individual lawyers don't have to deal with it.

When it comes to season tickets for sporting events, however, a drawback is cost: Federal tax law bars any tickets that go unused from being submitted as a business-entertainment expense. So if the firm or an individual lawyer purchases tickets in advance, there may be a cost disadvantage in the long run.

At Baker Botts, Fowler says, the firm has a specified budget for business entertainment, but there are some partners who prefer to incur costs related to rainmaking on their own.

"There is a real effort to have the firm pay," Fowler says. Not only does that mean people will keep up with their paperwork, as the tax laws require, but also firm management knows what's going on.

Fowler concedes, however, that some partners may want to manage their own rainmaking budget and incur the costs and tax responsibilities, precisely because they consider those events as more linked to their own careers, rather than the firm's. "In a large portion of the cases, that is not the case, though," he says.

In general, some lawyers who pay for their own business entertainment expenses and deduct them from their tax returns may prefer to keep their book of business private from their firms.

Unlike Rhodus, Elliott says that few firms today handle business entertainment expense deductions.

"The partners have to do it at most firms. The idea of firm management serving as a gatekeeper is great in theory but not in practicality," he says. At his own solo operation, he says, he holds his secretary responsible for getting his tax-related documents to his accountant. "I don't want to see it. I have too much else to do," Elliott says. At large firms though, management has too much else to track to bother with business entertainment expenses for each lawyer. The lawyers at big firms are more and more often on their own, he says.

And if those lawyers are audited, Elliott warns, watch out. As far as business entertainment expenses, he says, the IRS considers those "hanging fruit in an orchard, just ready for the picking." Rarely, Elliott says, would any law-abiding American have met the IRS's "slavish" substantiation requirements.