

# Client Alert

Data, Privacy & Security and Tax Practice Groups

February 9, 2016

For more information, contact:

**Phyllis B. Sumner**  
+1 404 572 4799  
[psumner@kslaw.com](mailto:psumner@kslaw.com)

**Abraham Shashy (Hap)**  
+1 202 626 5614  
[hshashy@kslaw.com](mailto:hshashy@kslaw.com)

**John A. Drennan**  
+1 202 626 9605  
[jdrennan@kslaw.com](mailto:jdrennan@kslaw.com)

**King & Spalding**  
*Atlanta*  
1180 Peachtree Street, NE  
Atlanta, Georgia 30309-3521  
Tel: +1 404 572 4600  
Fax: +1 404 572 5100

**Washington, D.C.**  
1700 Pennsylvania Avenue, NW  
Washington, D.C. 20006-4707  
Tel: +1 202 737 0500  
Fax: +1 202 626 3737

[www.kslaw.com](http://www.kslaw.com)

## Tax Relief for Identity Protection Services

In 2015, following numerous customer data security breaches at major U.S. companies, the IRS announced special tax relief to breach victims who were provided identity protection services as a result of the breach. In January 2016, the IRS has extended that relief a step further. Specifically, in response to comments solicited in connection with the 2015 announcement, the IRS has provided special tax relief to individuals who receive no-cost identity protection services *before* a data breach.<sup>1</sup>

In their remarks to the IRS regarding the 2015 announcement, commenters pointed out that data security is a major concern for many organizations and cited statistics showing a significant increase in the number of data breaches that result in unauthorized access to information systems containing the personal information of employees and other individuals. Commenters also noted that some organizations are making security decisions based on the belief that breaches of their information systems are inevitable. In addition, commenters made the case that an increasing number of organizations are combating data breaches by providing identity protection services to their employees or other individuals *before* a data breach occurs.

Citing these considerations as the basis for extending the tax relief it had provided for identity protection services in 2015, the IRS's new Announcement 2016-02 provides that the IRS will not assert—

- that an individual must include in gross income the value of identity protection services provided by the individual's employer or by another organization to which the individual provided personal information (for example, name, social security number, or banking or credit account numbers), or
- that an employer providing identity protection services to its employees must include the value of such services in the employees' gross income and wages.

Notably, the IRS also will not assert that the value of such a service needs to be reported to the IRS or the service recipients on information returns such as Forms W-2 or 1099. However, this relief does not apply to cash that an individual may receive in lieu of identity protection services, or to proceeds received under an identity theft insurance policy.

## Recommendations

This guidance is undoubtedly welcome news for employers that want to offer identity protection services to employees as part of their data security strategy. Companies may now offer these services without increasing federal tax liability for themselves or their employees.

But the good news goes beyond the employment context. In addition to an individual's employer, the guidance also provides that "the IRS will not assert that an individual must include in gross income the value of identity protection services provided by ... *another organization* to which the individual provided personal information." The guidance bolsters this broad language by singling out the Form 1099-MISC—the informational form appropriate for a wide variety of payments individuals may receive, such as rent, royalties, prizes and awards, and, presumably, the value of identity protection services— as containing the kind of information that no longer need be reported to the IRS. Thus, for example, if a customer gives a retailer personal information and the retailer provides the customer with identity protection services, the IRS will not treat that as a reportable event.

We urge companies to contact their attorneys about the tax and other implications of providing identity protection services to individuals such as employees and customers. We note the IRS's announcement concerns only federal taxation. Companies should be aware of state and/or local tax consequences of providing identity protection services.

\* \* \*

## King & Spalding's Data, Privacy Practice

King & Spalding is particularly well equipped to assist clients in the area of privacy and information security law. Our Data, Privacy & Security Practice regularly advises clients regarding the myriad statutory and regulatory requirements that businesses face in the U.S. and globally when handling personal information and other sensitive information and addressing cybersecurity requirements. This often involves assisting clients in developing comprehensive privacy and data security programs, responding to data security breaches, complying with breach notification laws, avoiding potential litigation arising out of internal and external data security breaches, defending litigation, whether class actions brought by those affected by data breaches, third party suits, or government actions, and handling both state and federal government investigations and enforcement actions. With more than 60 Data, Privacy & Security lawyers in offices across the United States, Europe, Russia, and the Middle East, King & Spalding is able to provide substantive expertise and collaborative support to clients across a wide spectrum of industries and jurisdictions facing privacy and data security-based legal concerns.

## King & Spalding's Tax Practice

King & Spalding's Tax Practice Group provides advice that is technically sophisticated, practical, and policy-aware. Our practice covers the full range of federal income tax issues presented in planning and executing complex business transactions in both domestic and cross border settings, including acquisitions, dispositions, joint ventures, financings, restructurings, and investment fund formations. In addition to advising on corporate, partnership, and international tax matters, we provide advice on the employee benefits and executive compensation aspects of business transactions and post-transaction integration. Our group also helps clients resolve tax controversies as favorably as possible, whether in examinations, administrative appeals, the courtroom, or alternative dispute resolution processes.

*Celebrating more than 130 years of service, King & Spalding is an international law firm that represents a broad array of clients, including half of the Fortune Global 100, with 900 lawyers in 18 offices in the United States, Europe, the Middle East and Asia. The firm has handled matters in over 160 countries on six continents and is consistently recognized for the results it obtains, uncompromising commitment to quality and dedication to understanding the business and culture of its clients. More information is available at [www.kslaw.com](http://www.kslaw.com).*

*This alert provides a general summary of recent legal developments. It is not intended to be and should not be relied upon as legal advice. In some jurisdictions, this may be considered "Attorney Advertising."*

---

<sup>i</sup> See IRS Announcement 2016-02 (available at <https://www.irs.gov/pub/irs-drop/a-16-02.pdf>).