



Nordlander CPA, PLLC
WHEN YOU WANT ANSWERS



ERASE THE **PENALTY**

A TAX PROFESSIONAL'S
GUIDE TO ABATEMENT



Who Is Your Presenter?

He is a retired special agent with the Internal Revenue Service, Criminal Investigation (IRS-CI). He has over 20 years of experience conducting federal criminal investigations to include tax evasion, money laundering, and other white-collar crimes.

After a successful law enforcement career, he started a boutique forensic accounting and tax resolution firm. He speaks nationally on topics regarding forensic accounting, criminal tax investigations, and solving IRS problems.

He is a CPA and CFE. He has a Bachelor's degree in Accounting and a Master's degree in Business Administration.

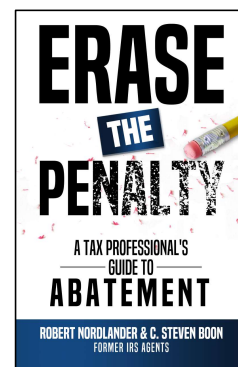
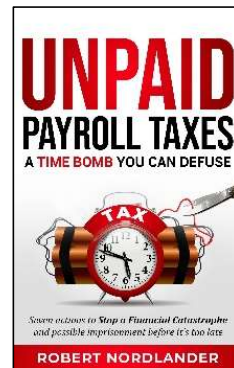
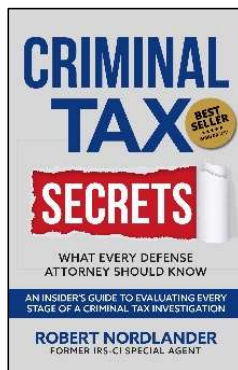
He is an author of three books (available on Amazon).



Robert Nordlander, CPA, CFE





Principal member of
Nordlander CPA, PLLC, a forensic
accounting and tax resolution firm

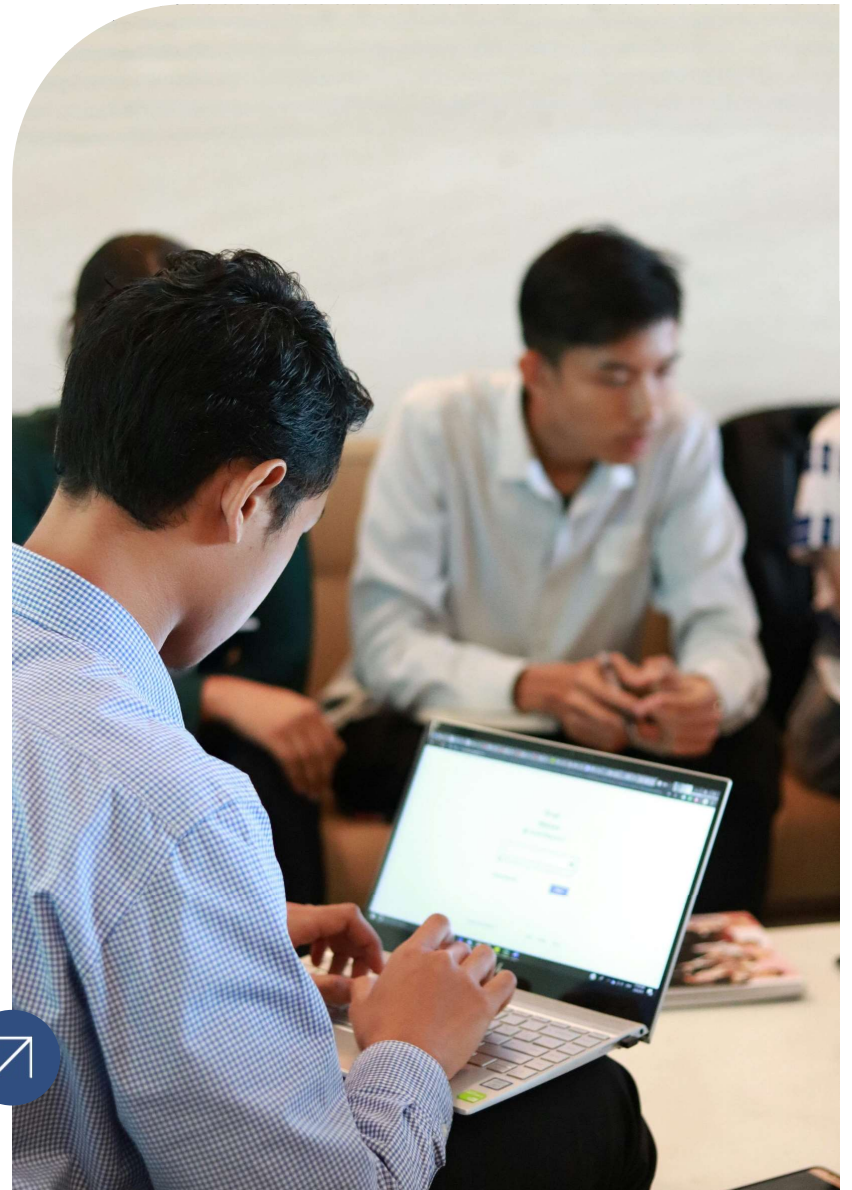
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LEARNING

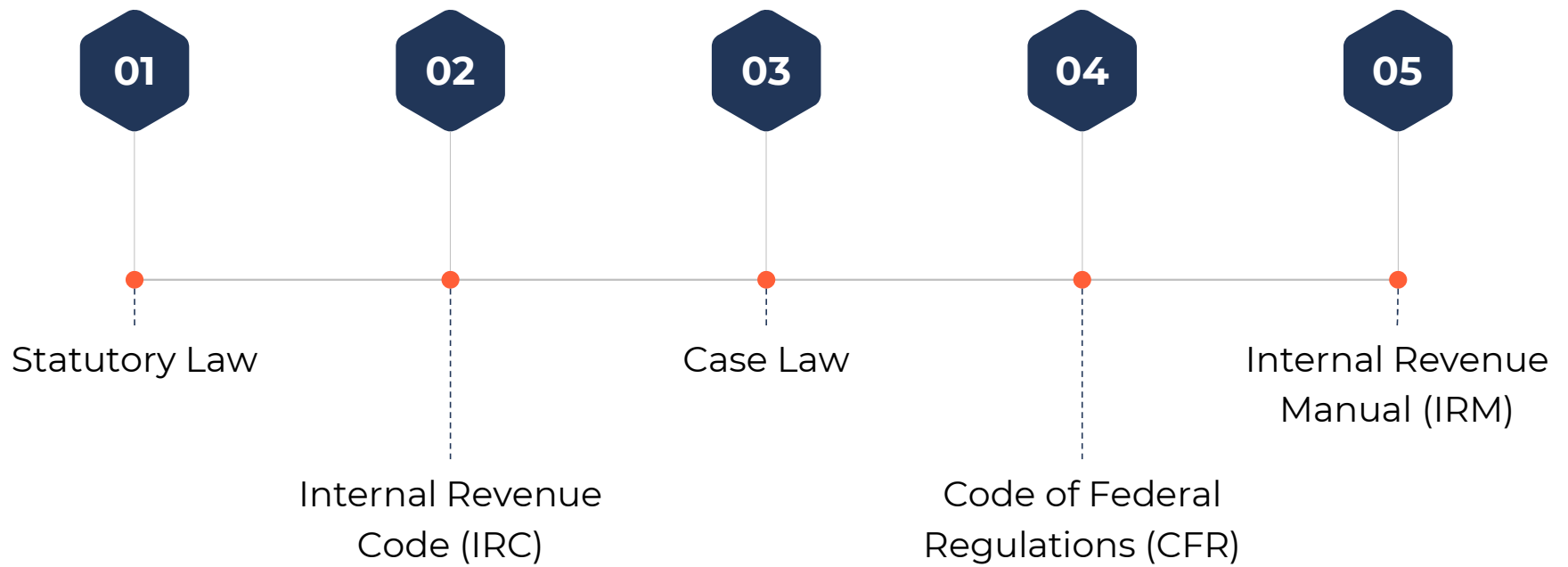
OBJECTIVES

-  Identify the authority of the IRS to assess penalties
-  Recognize the common types of penalties that can be abated
-  Develop a plan to request penalty abatement
-  Review real examples of successful penalty abatements





KEY TERMS





AUTHORITY OF THE IRS TO ASSESS PENALTIES



In 1955, 14 penalties in Internal Revenue Code (IRC)



In 2011, approximately 140 penalties (IRM Section 20.1.1.1)



IRC 7801 creates the IRS



IRC 7803 creates the commissioner position to administer tax laws



Penalties have two purposes (IRM 20.1.1.2)

- Encourage voluntary compliance by supporting standards of behavior
- Preparing an accurate and timely return with timely payment



Many instances, IRS supervisor must sign off on penalty (IRC 6751(b))

RECOGNIZE THE **COMMON** TYPES OF PENALTIES THAT CAN BE ABATED



Failure to file
(IRC 6651(a)(1))



Failure to pay
(IRC 6651(a)(1)
and (2))



Failure to file
information
returns (IRC 6652)



Estimated Tax
Penalty
(IRC 6654)



Accuracy related
penalty
(IRC 6662)

FAILURE TO FILE AND FAILURE TO PAY



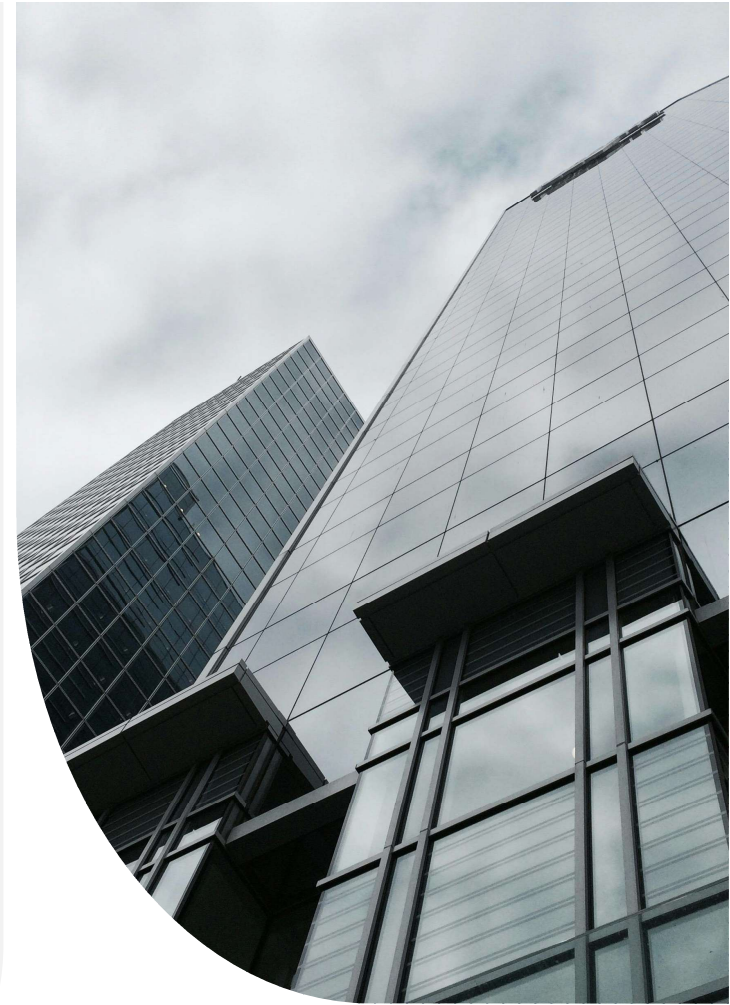
Failure to file (IRC 6651(a)(1))

- Tax returns with a tax due
- 5% per month; top at 25%



Failure to pay (IRC 6651(a)(1) and (2))

- .5% per month; top at 25% (50 months)
- Can be assessed simultaneously





FAILURE TO FILE INFORMATION RETURN

Failure to file information returns (IRC 6652)

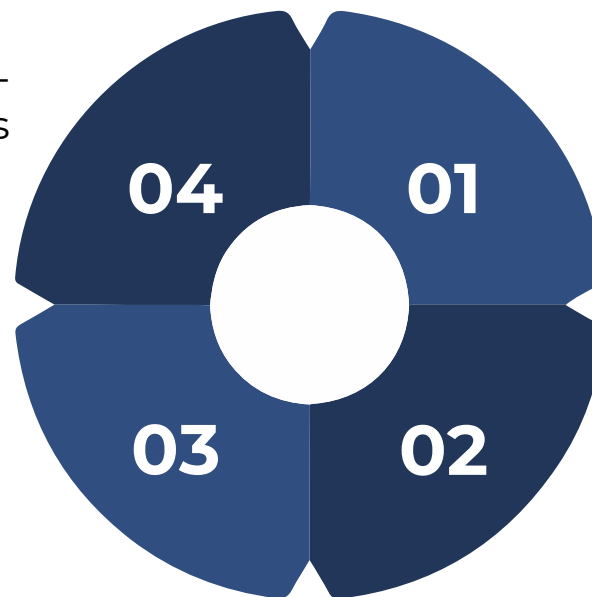
- ✓ Form 990
 - Can be between \$20 to \$120 per day
- ✓ Form W-2
 - Can be \$50 per form up to \$290
- ✓ Form 1099
 - Can be \$60 per form up to \$310
- ✓ Form 1098
 - Can be \$30 per form

ESTIMATED TAX PENALTY



Usually violated by self-employed business owners

Estimated Tax Penalty (IRC 6654)



Based on IRS wants its money now, like a W-2 federal withholding

Complicated formulas



01

Accuracy related penalty (IRC 6662)

02

Substantial understatement

- Penalty if tax exceeds **\$5,000** or **10%** of actual tax
- Math formula

03

Various circumstances

- Negligence of the rules/regulations
- Understatement of income tax
- Valuation misstatement
- Undisclosed foreign financial asset understatement



01

**Most penalties require supervisor approval
IRC § 6751(b)**

02

**Documentation is required to be maintained
in case file**

03

**Common penalties NOT requiring approval
IRC § 6751(b)(2)**

- Failure to file
- Failure to pay tax
- Failure to pay estimated income tax (individual and corporate)
- Any penalties calculated through electronic means

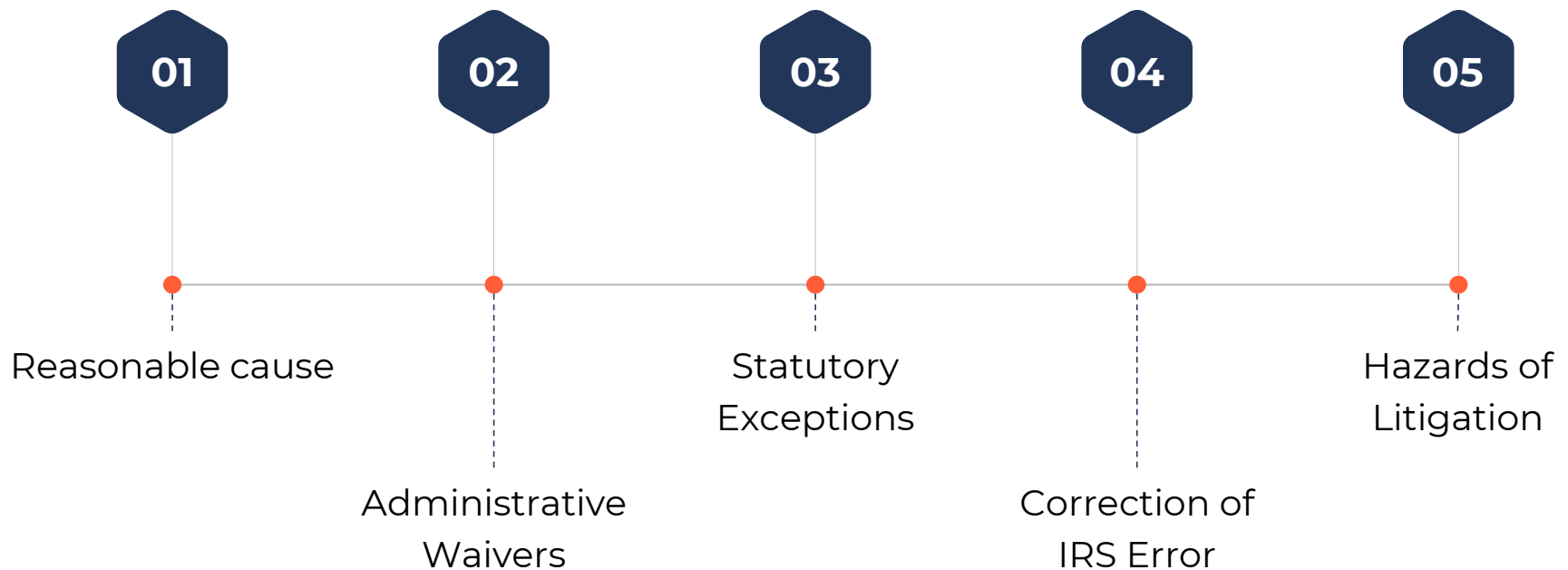
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2023 Tax Court case on IRS backdating
Lakepoint Land II, LLC v. Commissioner, T.C. Memo. 2023-111



DEVELOP A PLAN TO REQUEST PENALTY ABATEMENT

There are four main ways for the IRS to abate penalties [IRM 20.1.1.3 (10-19-2020)], with a fifth option for appeals



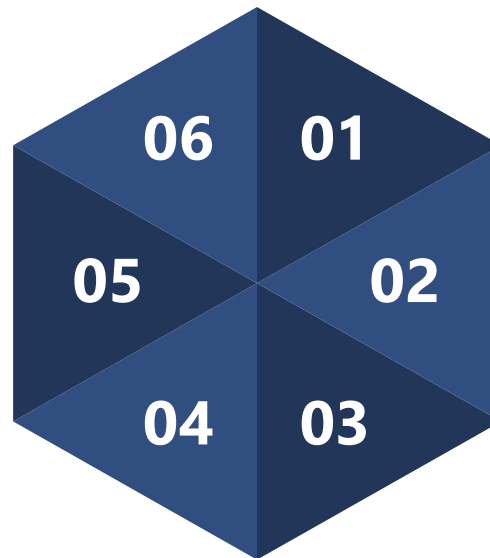


REASONABLE CAUSE

Courts don't consistently agree

Exercised ordinary business care and prudence, but unable to comply

IRS uses "all facts and circumstances"



Written directly into tax law

Example, failure to file or pay (IRC 6651)

- Penalty will be assessed "unless it is shown that such failure is due to reasonable cause and not due to willful neglect."

IRS has leeway to interpret "reasonable cause"



HOW THE COURTS INTERPRET

✓ United States vs Boyle,
469 USC 241, 245 (1985)

- Taxpayer has burden of proving both
 - No willful neglect
 - Reasonable cause

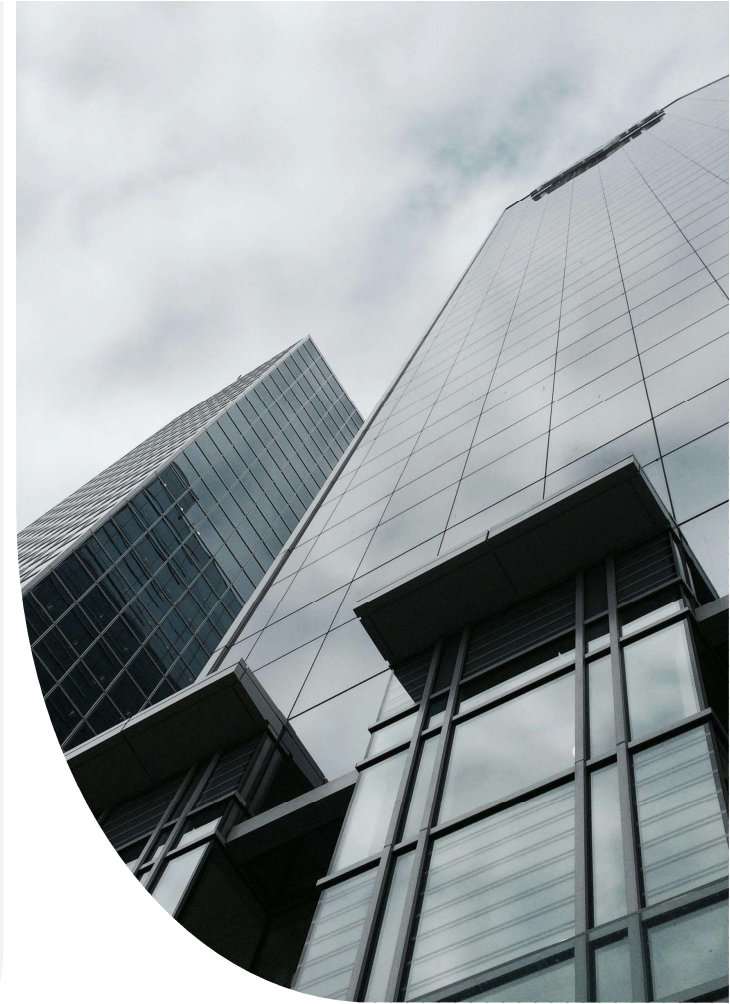


Reasonable cause isn't
defined in regulations



CFR 301.6651-1(c)(1)

- "The taxpayer has made a satisfactory showing that he exercised ordinary business care and prudence in providing for payment or his tax liability and was nevertheless unable to pay the tax or would suffer an undue hardship . . . if he paid the tax on time."



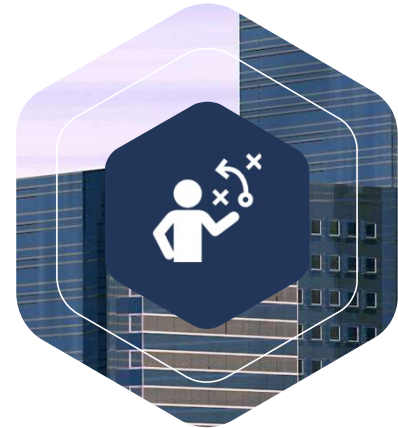
HOW THE COURTS **INTERPRET**



Is Not A Magic Wand
To Be Waved



IRS Looks At Client's
Filing History



Part Storyteller, Part Strategist,
Part Number Cruncher

EXAMPLE OF REASONABLE CAUSE



Death or serious illness

- Can be immediate family (spouse, sibling, parents, grandparents, child)
- If corporation, related to individual having sole authority
- IRM 20.1.1.3.2.2.1 (11-25-2011)

“

Where a taxpayer's disability is raised as part of a reasonable cause defense, we have looked to the severity of the disability and the impact it had on the taxpayer's life.

*Jones v. Commissioner,
T.C. Memo. 2006-176*

”



Won't work if taxpayer can continue business operations

“[A] taxpayer's selective inability to perform his or her tax obligations, while performing their regular business, does not excuse failure to file.”

*Watts v. Commissioner,
No. 9289-98 (T.C. Dec. 23,
1999)*

RELIANCE ON TAX PROFESSIONAL



- ✓ **Difference between tax advice and tax filings. Determine what penalty is relevant.**
-

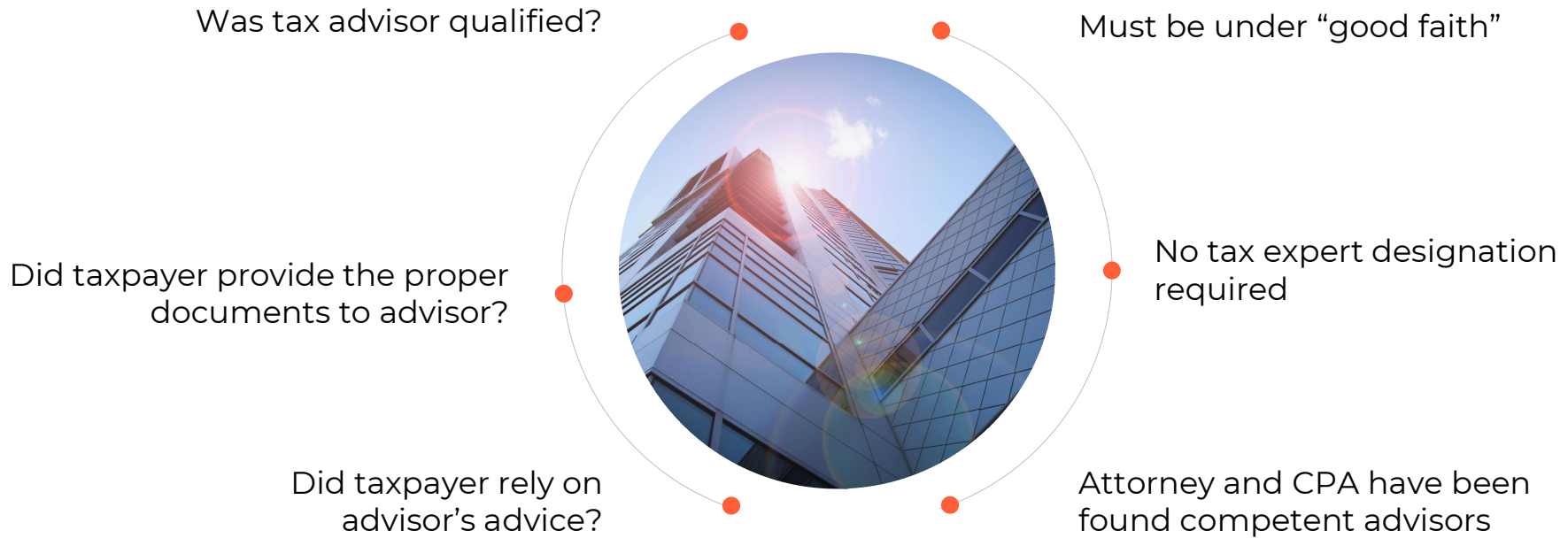
- ✓ **Bad advice can be reasonable cause.**

- Neonatology Associates, P.A. v Commissioner, 115 T.C. 43 (2000) allowed reasonable cause if -
 - 1) Tax professional was competent; 2) taxpayer provided information; 3) taxpayer relied on advisor.
-


- ✓ **Tax shelters won't work for reliance on tax professional**


- Unreasonable to rely on tax attorney who was tax shelter promoter - *Stobie Creek Investments, LLC v. U.S.*, 82 Fed. Cl. 636, aff'd, 608 F.3d 1366 (Fed. Cir. 2010);


TAX PROFESSIONAL RELIANCE



DELEGATED TO SOMEONE ELSE?

-  Filing a tax return has been declared as non-delegable duty - *Boyle v. Commissioner*, 469 U.S. 241 (1985)

-  Taxpayer is not excused for delegating responsibility to family member or tax professional.

-  Some courts allow reasonable cause if the due date of estate tax return was unknown. *Rohrbaugh v. U.S.*, 611 F.2d 211 (7th Cir. 1979); *Gray v. U.S.*, 453 F. Supp. 1356 (W.D. Mo. 1978).

LACK OF OVERSIGHT?



Lack of oversight or forgetfulness generally is not reasonable cause



However, some courts disagree, if lack of oversight was based on illness, etc.



Employee embezzlement?

No, unless it incapacitated the business

UNABLE TO OBTAIN RECORDS



✓ Unable to obtain records - IRM 20.1.1.3.2.2.3 (12-11-2009)

- Failure to make deposit or pay trust fund taxes when unable to access records
- Failure was caused by civil disturbance
- Show proof of inability to get records.

✓ IRS Will Consider

- Why were the records needed?
- Why records were unavailable?
- When did taxpayer become aware?
- What other avenues were pursued?
- Prompt compliance once information was received.





OTHER EXCUSES?

✓ Lack of necessary return information is not reasonable cause

- Courts want best estimate

✓ Ignorance of the Law

- Inadvertent error of failing to mail timely was reasonable cause
- Erroneous belief that no tax due – not reasonable cause
- Inexperienced administrator, attorney was reasonable cause
- Mistaken belief from not a competent professional – not reasonable cause



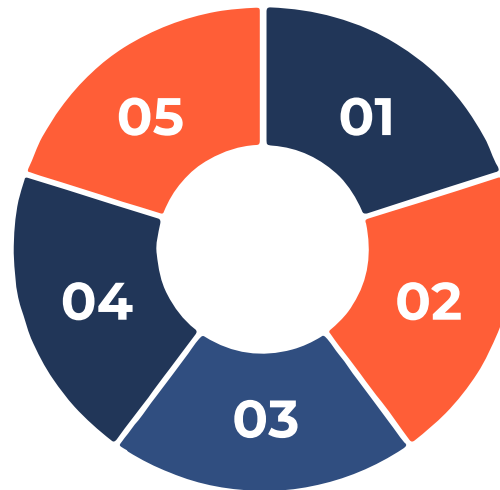
TAXPAYER IGNORANCE



IRS doesn't like ignorance, but will consider it (IRM 2.1.1.3.2.2.4)

Taxpayer's education, previous penalty, recent changes in tax law, complexity, and good faith effort (IRM 20.1.1.3.2.2.6)

Supporting documentation



When and how mistake was made?

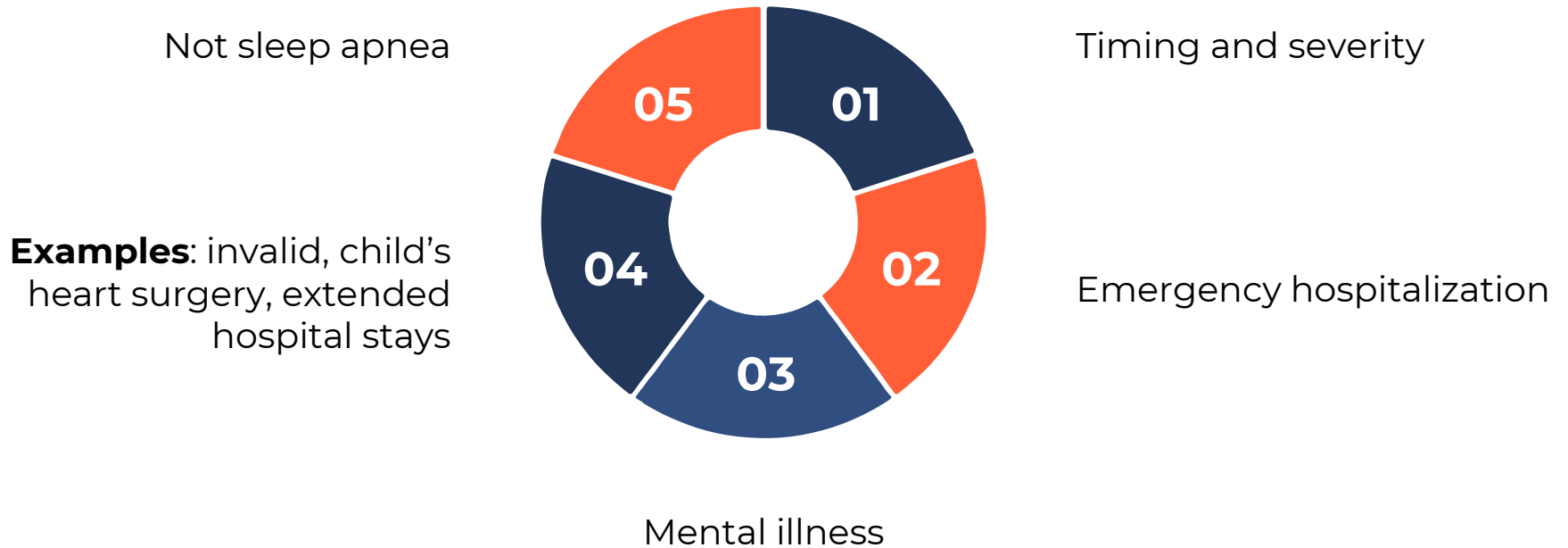
Correction taken when discovered

Relationship between taxpayer and subordinate

HEALTH PROBLEMS?



Stress, overworking?



NOT REASONABLE CAUSE



01

Constitutional or
religious objections

02

Just didn't care

03

Personal problems
Marital problems
Financial distress



LACK OF FUNDS



✓ Usually not reasonable cause

✓ But, possible under Failure to Pay penalty

- If exercised ordinary business care
- Couldn't pay according to facts and circumstances
- Lavish lifestyle, speculative assets, illiquid assets are not.
- "Undue Hardship" has been defined differently by the courts
 - Second, Third, and Ninth Circuits of Appeals agree that financial hardship is reasonable cause





UNDUE HARDSHIP

- ✓ Custom Stairs & Trim, Ltd., Inc. v. Commissioner, T.C. Memo. 2011-155 (2011) (holding that taxpayer exercised ordinary business care by cutting benefits and payroll, attempting to sell real property, the economic recession, and the result of Hurricane Ivan.)



- ✓ CFR §1.6161-1(b) defines the term “undue hardship” as more than an inconvenience to the taxpayer. It must appear that substantial financial loss (e.g., loss due to the sale of property at a sacrifice price) will result to the taxpayer for making tax payments on time.) CFR §301.6651-1(c)(2) allows stringency on the type of tax.
- ✓ Glenwal-Schmidt, DC-DC, 78-2 USTC ¶9610 (1978)
Pool & Varga, Inc., BC-DC-MI, 86-1 USTC ¶9445, 60 BR 722 (1986)
Slater Corporation, BC-DC-FL, 96-1 USTC ¶50,043, 190 BR 695 (1995)

DEFINING FINANCIAL HARDSHIP



Harvey and Sons, Inc 94 A.F.T.R.2d 2004-7258 (D. Mass 2004)

Real choice between making tax payments or going out of business

Not strongly favoring other creditors vs IRS

Duration of the financial crisis was limited in time

Not unfairly enriching themselves

Occurrence of one or more specific contingencies

Taxpayer prioritized creditors



ADMINISTRATIVE WAIVERS



IRS has authority to administer waivers for penalty abatement

Common waiver is First Time Penalty Abatement (FTA).

IRM 20.1.1.3.3.2.1

Can be applied multiple times and balance due

Criteria

- Not the same penalty within last three years
- Current in filings and payments

Types of penalties

- Failure to file (tax returns, partnerships, and S-Corps)
- Failure to pay
- Failure to deposit



STATUTORY EXCEPTIONS



Created in tax law



Examples are

01

Military in
combat zones

02

Severe disasters

03

Mailed return
on time



CORRECTION OF IRS ERROR



✓ When IRS makes a mistake

✓ Reliance on incorrect written advice from IRS

HAZARDS OF LITIGATION



- ✓ IRS Appeals can determine if litigating the penalty is worth the effort in tax court.

THE **PROCESS THE IRS** USES TO EVALUATE PENALTY ABATEMENTS



“Reasonable cause” is
the most common

Is there documentation
to corroborate?

FTA availability?

What happened after
non-compliance?

What caused the penalty?

What good faith was
done by taxpayer?





HOW TO **REQUEST** PENALTY ABATEMENTS



Form 843

- One page form
- Identifiers, type of penalty, and explanation
- Sometimes, require to be in writing and signed under penalties of perjury (Regs. Secs. 301.6651-1(c)(1) and 301.6724-1(m))



Phone call

- Dollar threshold
- Employee competency
- Reasonable Cause Assistant (RCA) software





BEST PRACTICES IN REQUESTING PENALTY ABATEMENT, INCLUDING APPEALS



Phone call

- Lesser amounts (like less than \$2,000) for reasonable cause
 - Can request FTA vs reasonable cause
 - Have Form 2848 available
-



Form 843

- Best avenue for penalty abatement
- IRS will analyze FTA first, then reasonable cause
- Letter of explanation (less than 2 pages)
- Documentation cited in letter (invoices, medical records, doctor's note, photos, police report, etc.)
- 3 ring binder with tabs (no originals, only copies)
- Read CFR and IRM regarding your penalty
- Appeal, if necessary



EXAMPLES OF SUCCESSFUL PENALTY ABATEMENTS



Business failed to file insurance forms



IRS misapplied federal tax payments



Key personnel unavailable due to sickness

LEARNING

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