

**SACEA**

**September 20, 2011**

**Penalty Abatement and Reasonable Cause**

**Jeri L. Cantrell  
Enrolled Agent**

#### Failure to File penalty

- A. Generally, the FTF penalty is 5% of the net amount due per month (or part of a month) not to exceed five months.
- B. When the FTF penalty and the FTP penalty under IRC section 6651(a)(2) apply at the same time, the 5% FTF penalty rate is reduced by the  $\frac{1}{2}$ % FTP penalty rate under IRC section 6651(a)(2). In other words, FTF is then assessed at a rate of  $4\frac{1}{2}$ % a month and FTP at  $\frac{1}{2}$ % a month. When both FTF and FTP apply for five months, the maximum FTF penalty rate is  $22\frac{1}{2}$ %.

#### Failure to Pay penalty

1. Determine the penalty period. The penalty period for the FTP penalty under IRC section 6651(a)(2) is the number of months (including a part of a month) from the return due date—not including extensions—until the tax is paid or the maximum 25% rate has been applied. ( See IRM 20.1.2.1.2.4. for the definition of a month.)
  2. The penalty rate is  $\frac{1}{2}$ % per month (or part of a month) on the net amount due until the tax is paid in full or the maximum 25% rate has been applied
1. IRC section 6651(d) increases the FTP penalty rate under IRC section 6651(a)(2) or IRC section 6651(a)(3) from  $\frac{1}{2}$ % to 1% of the tax at the start of the month beginning after:
- 10 days after the date of notice of intent to levy ( IRC section 6331(d)(1)), or
  - The day on which notice and demand for immediate payment is given in the case of jeopardy ( IRC section 6331(d)(3)).

#### Failure to Deposit Penalty

##### 20.1.4.2.1 (05-22-2009)

##### Time Sensitive Four Tier Penalty System

1. There is a time sensitive four-tier penalty system for late deposits. The penalty rate assessed depends on the number of days a deposit is late, as shown below:
  - A. 2 percent for deposits 1—5 days late,
  - B. 5 percent for deposits 6—15 days late,
  - C. 10 percent for deposits made more than 15 days late. Also applies to amounts paid within 10 days of the date of the first notice the IRS sent asking for the tax due.
  - D. 10 percent for deposits made at an unauthorized financial institution, paid directly to the IRS, or paid with the tax return.
  - E. 10 percent for amounts subject to electronic deposit requirements but not deposited using EFTPS.
  - F. 15 percent (actually, a 5 percent addition to the 10 percent for late payment in (c) above) for all amounts still unpaid more than 10 days after the date of the first notice that the IRS sent asking for the tax due or the day on which the taxpayer received notice and demand for immediate payment, whichever is earlier.

**Table 17. Civil Penalties Assessed and Abated, by Type of Tax and Type of Penalty, Fiscal Year 2010 [1]**

[Money amounts are in thousands of dollars.]

Type of tax and type of penalty	Civil penalties assessed		Civil penalties abated [2]	
	Number	Amount	Number	Amount
	(1)	(2)	(3)	(4)
<b>Civil penalties, total</b>	<b>37,055,841</b>	<b>28,055,115</b>	<b>4,874,920</b>	<b>10,025,544</b>
<b>Individual income tax:</b>				
<b>Civil penalties, total [3]</b>	<b>27,106,767</b>	<b>14,525,188</b>	<b>3,039,087</b>	<b>4,109,484</b>
Accuracy [4]	469,321	1,069,785	58,107	241,645
Bad check	152,225	14,212	6,770	4,791
Delinquency	3,529,203	5,871,164	804,058	2,195,182
Estimated tax	7,412,249	1,617,298	263,299	267,794
Failure to pay	15,538,896	5,828,731	1,901,839	1,346,024
Fraud	2,218	123,458	236	48,255
Other [5]	2,655	539	4,778	5,794
<b>Business income tax:</b>				
<b>Civil penalties, total</b>	<b>1,145,931</b>	<b>1,770,628</b>	<b>263,261</b>	<b>776,088</b>
Accuracy [4, 6]	3,840	334,558	148	47,825
Bad check [6]	1,826	164	111	137
Delinquency [6]	639,251	758,432	173,326	421,878
Estimated tax [6]	213,035	231,940	12,349	106,221
Failure to pay [6]	269,950	374,144	72,123	183,134
Fraud [6]	161	14,334	7	662
S corporation/partnership information [7]	18,022	54,685	1,607	8,611
Other [6]	46	2,371	3,592	7,819
<b>Employment taxes:</b>				
<b>Civil penalties, total [8]</b>	<b>7,838,423</b>	<b>5,778,753</b>	<b>1,376,063</b>	<b>2,477,757</b>
Accuracy [4]	1,786	8,827	218	529
Bad check	33,613	2,199	1,476	194
Delinquency	1,646,392	1,461,043	292,063	524,462
Estimated tax	3,688	12,723	726	6,680
Failure to pay	4,135,675	1,176,674	672,498	316,886
Federal tax deposits	2,016,966	3,108,562	409,049	1,628,555
Fraud	290	8,137	28	445
Other	13	587	5	6

16% 38% abated  
 11.2% - 28% abated

22%

Fiscal Year 2009 [1]

[Money amounts are in thousands of dollars.]

Type of tax and type of penalty	Civil penalties assessed		Civil penalties abated [2]	
	Number	Amount	Number	Amount
	(1)	(2)	(3)	(4)
<b>Civil penalties, total</b>	<b>36,228,339</b>	<b>29,820,693</b>	<b>5,140,094</b>	<b>15,939,535</b>
<b>Individual income tax:</b>				
<b>Civil penalties, total [3]</b>	<b>26,387,032</b>	<b>14,997,997</b>	<b>3,303,495</b>	<b>3,924,645</b>
Accuracy [4]	410,338	888,560	55,560	232,527
Bad check	181,144	17,429	9,710	8,088
Delinquency	3,805,227	6,189,019	775,789	2,238,966
Estimated tax	7,565,037	2,167,017	271,984	279,104
Failure to pay	14,437,722	5,833,923	2,183,511	1,143,044
Fraud	2,305	119,283	235	18,285
Other [5]	5,259	2,765	6,706	6,632
<b>Business income tax:</b>				
<b>Civil penalties, total [6]</b>	<b>970,098</b>	<b>1,853,961</b>	<b>232,837</b>	<b>1,014,539</b>
Accuracy [4]	3,318	286,811	d	d
Bad check	1,691	241	186	3,904
Delinquency	410,262	649,719	127,140	420,876
Estimated tax	243,852	433,078	21,336	220,752
Failure to pay	297,386	380,175	81,043	231,758
Fraud	140	14,093	d	d
S Corporation/Partnership Information [7]	13,398	89,196	1,919	14,642
Other	51	649	1,100	7,446
<b>Employment taxes:</b>				
<b>Civil penalties, total [8]</b>	<b>7,918,580</b>	<b>7,064,177</b>	<b>1,410,603</b>	<b>4,621,747</b>
Accuracy [4]	2,862	12,840	139	439
Bad check	36,846	2,571	1,966	441
Delinquency	1,686,977	1,570,520	290,668	1,457,850
Estimated tax	4,545	26,661	1,170	34,318
Failure to pay	4,182,740	1,215,132	680,496	457,011
Federal tax deposits	2,004,152	4,222,112	436,130	2,671,118
Fraud	412	14,307	15	553
Other	48	32	19	16

### 20.1.1.2 (02-22-2008)

#### Purpose of Penalties

1. Penalties exist to encourage voluntary compliance by supporting the standards of behavior required by the Internal Revenue Code.
2. For most taxpayers, voluntary compliance consists of preparing an accurate return, filing it timely, and paying any tax due. Efforts made to fulfill these obligations constitute compliant behavior. Most penalties apply to behavior that fails to meet any or all of these obligations.
3. The following factors support the public conviction that the tax system is fair and the penalty is in proportion to the severity of the noncompliance. Penalties encourage voluntary compliance by:
  - Defining standards of compliant behavior,
  - Defining consequences for noncompliance, and
  - Providing monetary sanctions against taxpayers who do not meet the standard.

### 20.1.1.2.2 (02-22-2008)

#### Fair and Consistent Approach to Penalty Administration

1. The IRS's approach to penalty administration must ensure:
  - A. **Consistency:** The IRS should apply penalties equally in similar situations. Taxpayers base their perceptions about the fairness of the system on their own experience and the information they receive from the media and others. If the IRS does not administer penalties uniformly (guided by the applicable statutes, regulations, and procedures), overall confidence in the tax system is jeopardized.
  - B. **Accuracy:** The IRS must arrive at the correct penalty decision. Accuracy is essential. Erroneous penalty assessments and incorrect calculations confuse taxpayers and misrepresent the overall competency of the IRS.
  - C. **Impartiality:** IRS employees are responsible for administering the penalty statutes and regulations in an even-handed manner that is fair and impartial to both the government and the taxpayer.
  - D. **Representation:** Taxpayers must be given the opportunity to have their interests heard and considered. Employees need to take an active and objective role in case resolution so that all factors are considered.

### 20.1.1.3.2 (12-11-2009)

#### Reasonable Cause

1. Reasonable cause is based on all the facts and circumstances in each situation and allows the IRS to provide relief from a penalty that would otherwise be assessed. Reasonable cause relief is generally granted when the taxpayer exercises ordinary business care and prudence in determining their tax obligations but nevertheless failed to comply with those obligations.
2. In the interest of equitable treatment of the taxpayer and effective tax administration, the non-assertion or abatement of civil penalties based on reasonable cause or other relief provisions provided in this IRM must be made in a consistent manner and should conform with the considerations specified in the IRC, Treasury Regulations (Treas. Regs.), Policy Statements, and IRM Part 20.1.
3. Reasonable cause relief is not available for all penalties; however, other exceptions may apply.
  - A. For those penalties where reasonable cause can be considered, any reason which establishes that the taxpayer exercised ordinary business care and prudence, but nevertheless was unable to comply with a prescribed duty within the prescribed time, will be considered.
  - B. If a reasonable cause provision applies only to a specific Code section, that reasonable cause provision will be discussed in the IRM 20.1 section relating to that specific IRC section. See Exhibit 20.1.1-2, *Penalty Relief Application Chart*.
  - C. When considering the information provided in the following pages, remember that an acceptable explanation is not limited to those given in IRM 20.1, *Penalty Handbook*. Penalty relief may be warranted based on an "other acceptable explanation", provided the taxpayer exercised ordinary business care and prudence but was

nevertheless unable to comply within the prescribed time. See *IRM 20.1.1.3.2.2, Ordinary Business Care and Prudence*.

4. The wording used to describe reasonable cause provisions varies. Some IRC penalty sections also require evidence that the taxpayer acted in good faith or that the taxpayer's failure to comply with the law was not due to willful neglect. See specific *IRM 20.1* sections for the rules that apply to a specific IRC section. See *IRM 20.1.1.1.2, Organization of IRM 20.1*.
5. Taxpayers have reasonable cause when their conduct justifies the non-assertion or abatement of a penalty. Each case must be judged individually based on the facts and circumstances at hand. Consider the following in conjunction with specific criteria identified in the remainder of this subsection:
  - What happened and when did it happen?
  - During the period of time the taxpayer was non-compliant, what facts and circumstances prevented the taxpayer from filing a return, paying a tax, and/or otherwise complying with the law?
  - How did the facts and circumstances result in the taxpayer not complying?
  - How did the taxpayer handle the remainder of their affairs during this time?
  - Once the facts and circumstances changed, what attempt did the taxpayer make to comply?
6. Reasonable cause does not exist if, after the facts and circumstances that explain the taxpayer's noncompliant behavior cease to exist, the taxpayer fails to comply with the tax obligation within a reasonable period of time.

#### 20.1.1.3.2.2 (02-22-2008)

#### Ordinary Business Care and Prudence

1. Ordinary business care and prudence includes making provisions for business obligations to be met when reasonably foreseeable events occur. A taxpayer may establish reasonable cause by providing facts and circumstances showing that they exercised ordinary business care and prudence (taking that degree of care that a reasonably prudent person would exercise), but nevertheless were unable to comply with the law.
2. In determining if the taxpayer exercised ordinary business care and prudence, review available information including the following:
  - A. **Taxpayer's Reason:** The taxpayer's reason should address the penalty imposed. To show reasonable cause, the dates and explanations should clearly correspond with events on which the penalties are based. If the dates and explanations do not correspond to the events on which the penalties are based, request additional information from the taxpayer that may clarify the explanation ( See *IRM 20.1.1.3.2, Reasonable Cause*).
  - B. **Compliance History:** Check the preceding tax years (at least three) for payment patterns and the taxpayer's overall compliance history. The same penalty, previously assessed or abated, may indicate that the taxpayer is not exercising ordinary business care. If this is the taxpayer's first incident of noncompliant behavior, weigh this factor with other reasons the taxpayer gives for reasonable cause, since a first-time failure to comply does not by itself establish reasonable cause.
  - C. **Length of Time:** Consider the length of time between the event cited as a reason for the noncompliance and subsequent compliance ( See *IRM 20.1.1.3.2, Reasonable Cause*). Consider: (1) when the act was required by law, (2) the period of time during which the taxpayer was unable to comply with the law due to circumstances beyond the taxpayer's control, and (3) when the taxpayer complied with the law.
  - D. **Circumstances Beyond the Taxpayer's Control:** Consider whether or not the taxpayer could have anticipated the event that caused the noncompliance. Reasonable cause is generally established when the taxpayer exercises ordinary business care and prudence, but, due to circumstances beyond the taxpayer's control, the taxpayer was unable to timely meet the tax obligation. The taxpayer's obligation to meet the tax law requirements is ongoing. Ordinary business care and prudence requires that the taxpayer continue to attempt to meet the requirements, even though late.

**1.2.12.1.2 (Approved 12-29-1970)**  
**Policy Statement 2-7**

1. **Reasonable cause for late filing of return or failure to deposit or pay tax when due**
2. Any sound reason advanced by a taxpayer as the cause for delay in filing a return, making deposits under the Federal Tax Deposit System, or paying tax when due, will be carefully analyzed to determine whether the applicable penalty should be asserted. Examples of sound causes for delay which, if established, will be accepted as reasonable cause are shown below:
  - A. Death or serious illness of the taxpayer or a death or serious illness in his/her immediate family. In the case of a corporation, estate, trust, etc., the death or serious illness must have been of an individual having sole authority to execute the return or make the deposit or payment or of a member of such individual's immediate family.
  - B. Unavoidable absence of the taxpayer. In the case of a corporation, estate, trust, etc., the absence must have been of an individual having sole authority to execute the return or make the deposit or payment.
  - C. Destruction by fire or other casualty of the taxpayer's place of business or business records.
  - D. Taxpayer was unable to determine amount of deposit or tax due for reasons beyond the taxpayer's control. However, this cause will be acceptable for taxpayers required to make deposits or payments of trust fund taxes only when the taxpayer was unable to have access to his/her own records.
  - E. The facts indicate that the taxpayer's ability to make deposits or payments has been materially impaired by civil disturbances.
  - F. Lack of funds is an acceptable reasonable cause for failure to pay any tax or make a deposit under the Federal Tax Deposit System only when a taxpayer can demonstrate the lack of funds occurred despite the exercise of ordinary business care and prudence.
3. **Other explanations may be acceptable**
4. Acceptable explanations of delinquency are not limited to the examples given above, since any reason for delinquency in filing or making deposits or payments which established that the taxpayer exercised ordinary business care and prudence but was nevertheless unable to comply within the prescribed time will be accepted as reasonable cause.
5. **State or local law interpretations as prohibiting advance payment of taxes withheld not acceptable**
6. For agencies or instrumentalities of a State or political subdivision thereof, interpretation of State or local laws as prohibiting advance payment or deposit of taxes withheld is not acceptable as reasonable cause for delay in making deposits or payments.

**20.1.5.6.3 (07-01-2008)**

**Experience, Knowledge, Sophistication and Education of Taxpayer**

1. Circumstances that may suggest reasonable cause and good faith include an honest misunderstanding of fact or law that is reasonable in light of the facts, including the experience, knowledge, sophistication and education of the taxpayer. The taxpayer's mental and physical condition, as well as sophistication with respect to the tax laws at the time the return was filed, are relevant in deciding whether the taxpayer acted with reasonable cause. See *Kees v. Commissioner*, T.C. Memo. 1999-41.
2. If the taxpayer is misguided and unsophisticated in tax law, but acts in good faith, a penalty is not warranted. See *Collins v. Commissioner*, 857 F.2d 1383 (9th Cir. 1988).

The mission of Appeals is to resolve tax controversies, without litigation, on a basis that is fair and impartial to both the Government and the taxpayer, and in a manner that will enhance voluntary compliance and public confidence in the integrity and efficiency of the Service.

From IRM Section 8, Appeals:

#### **8.11.1.5.2.1 (04-13-2010) Applying Reasonable Cause**

1. Penalty cases handled in Appeals involve more complex and questionable reasonable cause issues.
2. Decisions are made based on fact and the law, taxpayer circumstances and compliance history, and hazards of litigation.
3. Refer to IRM 20.1 for reasonable cause criteria guidelines.
4. The following questions are used to determine if the taxpayer has established reasonable cause:
  - A. Do the taxpayer's explanations directly relate to the penalty that was assessed?
  - B. Do the dates and times coincide with the taxpayer's explanation?
  - C. Could the noncompliance have been anticipated and/or prevented?
  - D. Did the taxpayer make an honest mistake?
  - E. Has the taxpayer provided sufficient detail (dates, relationships, documents) to determine if ordinary business care and prudence was exercised?
  - F. Is the taxpayer an individual, third party such as a reporting agent, accountant or lawyer?
  - G. Is there a history of the taxpayer being assessed the same penalty?
  - H. Were there prior abatements of the same or similar penalties?
5. The above questions should be considered in your the final determination and the decision must be clearly documented in your ACM. The facts and circumstances must support the decision.

## APPEALS – TODAY and TOMORROW

### Want To Learn More About Appeals and Its Processes?

To help you understand the Appeals organization and the Appeals process, we have created an educational tool utilizing video streaming technology. The video stream is designed for practitioners, taxpayers, and others that have an interest in learning more about Appeals.

To view the video, go to Internet address: [www.irs.gov](http://www.irs.gov) Keyword = Appeals

The following is just a small sample of the topics covered by this video stream:

- The Role of Appeals
- Overview of the Appeals Process
- Introduction to Exam & TEGE Cases
- Introduction to Collection
- Introduction to Alternative Dispute Resolution

Windows Media Player version 7 or greater is required to view the videos.



## OTHER USEFUL RESOURCES

Appeals website:  
[www.irs.gov](http://www.irs.gov) Keyword=Appeals

IRS website:  
[www.irs.gov](http://www.irs.gov)

Taxpayer Advocate Service:  
**1-877-777-4778**

TTY/TTD:  
**1-800-829-4059**

IRS Toll Free:  
**1-800-829-1040**

Forms and Publications:  
**1-800-TAX-FORM**



Department of the Treasury  
Internal Revenue Service

[www.irs.gov](http://www.irs.gov)

Publication 4227 (Rev. 11-2005)  
Catalog Number 37142N

Welcome

# Appeals

- MISSION
- OVERVIEW
- EXPECTATIONS
- RESOURCES

[www.irs.gov](http://www.irs.gov) Keyword=Appeals

## MISSION

The mission of Appeals is to resolve tax controversies, without litigation, on a basis which is fair and impartial to both the Government and the taxpayer and in a manner that will enhance voluntary compliance and public confidence in the integrity and efficiency of the Service. Today, alternative dispute resolution instead of litigation is widely valued and applied in many areas of our society. Customers expect more dispute resolution options, and Appeals has adapted its approach to keep up with the new methods and developments.

Our vision is to explore and apply innovative techniques to ensure customer confidence and meet customer and employee expectations regarding independent resolution services. Our goal is to increase confidence in the overall fairness of the tax system by providing an efficient, independent administrative appeal process for all taxpayers.

## OVERVIEW OF APPEALS PROCESS

If you disagree with the IRS findings in your tax case, you can appeal your case to the Appeals Office of the IRS. The local Appeals Office is separate from and independent of the IRS office that proposed the adjustment. An Appeals or Settlement Officer will review the strengths and weaknesses of the issues in your case and give them a fresh look. Appeals Office reviews are conducted in an informal manner, by correspondence, telephone or at a personal meeting. Most differences are settled in these appeals without expensive and time-consuming court trials. Appeals will consider any reason you have for disagreeing, except for moral, religious, political, constitutional, conscientious objection, or similar grounds. Our goal is to provide a forum for us to work together to resolve the tax dispute.

You can deal with Appeals by yourself, and you may bring a person with you to support your position. If you want to be represented by someone else, you must choose a person who is an attorney, a certified public accountant, or an enrolled agent authorized to practice before the IRS. If you plan to have your representative talk to us without you being present, we need a copy of a completed Form 2848, Power of Attorney and Declaration of Representative.

If you provide significant new information on a major issue, we generally ask the examiner for their opinion in writing and will share their comments with you. When there is a need for further clarification from the examiner, we may contact or invite you to participate in a conference call or a meeting with them.

## EXPECTATIONS

Our commitments to you are to:

- Explain your appeal rights and the Appeals process
- Listen to your concerns
- Be courteous and professional
- Be responsive (and allow you reasonable time to respond to any requests for information)
- Be fair and impartial

It is your responsibility to:

- Listen to our explanation of your appeal rights and the Appeals process
- Give us a statement as to how you understand the facts and the law, listing all issues with which you disagree and why
- Give us any additional information or documentation that will help your case
- Tell us when and how you think your case should be resolved
- Let us know the best time to contact you

**Internal Revenue Service**  
IRS Office of Appeals  
Appeals:MS 8000  
4041 N. Central Ave, Suite 112  
Phoenix, AZ 85012

**Department of the Treasury**

**Person to Contact:**

Theresa Nesbitt  
Employee ID Number: 0359716  
Tel: 602-636-9572  
Fax: 602-636-9565

**Refer Reply to:**

AP:FW:PHX:TAN

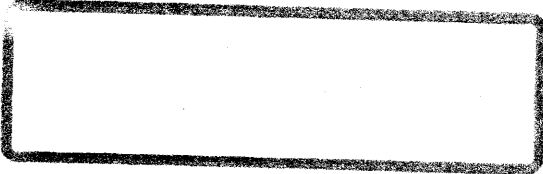
**In Re:**

Trust Fund Recovery Penalty

**Tax Period(s) Ended:**

09/2008 12/2008 03/2009 09/2009  
12/2009

Date: March 25, 2011



Dear Mr. 

This letter is our acknowledgement that we received your case for consideration in our Phoenix Appeals Office on March 9, 2011.

In this letter we will explain who we are, what we do, how we do it, who you can talk to, and what you can expect.

**Who We Are, What We Do, and How We Review Cases**

Appeals is separate from - and independent of - the division of the Internal Revenue Service proposing the action. What we do is review and resolve disputes. We do this in a fair and impartial manner by using the law and judicial decisions to weigh the facts. We conduct our reviews by: (1) telephone, (2) mail, and/or (3) personal interviews. If you prefer your hearing to be a face-to-face conference at the Appeals Office closest to your residence/business address, please let us know immediately so your case can be transferred to the appropriate field office for consideration.

**What You Can Expect**

We will make every attempt to contact you as quickly as possible. You can expect the "Person to Contact" listed above to consider the facts in your case and try to resolve the dispute. This person may also ask for additional information to specifically explain or support the information in your file.

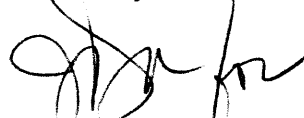
If our office determines that you owe the IRS, the law requires a charge for interest until you pay the amount you owe in full. If the amount determined that you owe includes penalties, additional penalty amounts may accrue until you pay in full.

**What You Can Do**

- Respond quickly if asked to send additional information.
- If you wish to stop or reduce interest on part or all of the proposed balance due, you can make payments toward the tax at the address listed above.

- You may be represented by an attorney, certified public accountant, or a person enrolled to practice before the Internal Revenue Service. However, your representative must submit a Form 2848, *Power of Attorney*, or similar written authorization. If you need more information about the requirements for representing taxpayers, you may obtain a copy of Treasury Department Circular 230 available at most IRS offices.
- Communicate with the "Person to Contact" listed above with any questions about the Appeals process or how you can prepare for your hearing.
- Research our website at [www.irs.gov/appeals](http://www.irs.gov/appeals) for more information.

Sincerely,



Angela Carmouche  
Appeals Team Manager

Enclosures:

Publication 4227 Welcome to Appeals

Publication 4167 Introduction to Alternative Dispute Resolution

cc: Jeri Cantrell

Jane Doe – PENALTY APPEAL

DRAFT:

**Internal Revenue Service**  
Kansas City Service Center  
Penalty Appeals Coordinator  
Kansas City MO 64999-0028

**RE: Jane Doe 123-45-6789**

Dear Sirs:

This firm represents Jane Doe (Power of Attorney Form 2848 attached). We are in receipt of Letter 3064C dated June 24, 2010 (attached) regarding our client.

The letter denies our request for abatement of the accuracy penalty charged for the Form 1040 for tax year 2006. The letter, however, did not advise us of appeal rights. Upon calling the number you provided, we spoke with Ms. Smith (ID#89XXXX) who assured us that the taxpayer has appeal rights. She advised that our appeal should be directed to the office that issued the above letter, however we are requesting a hearing with the Phoenix Office of Appeals.

We are requesting that the accuracy-related penalty of \$1724.00 that was assessed under IRS Section 6662(a) for tax year 2006, be abated due to reasonable cause.

The reasonable cause criteria in the Internal Revenue Manual provides that reasonable cause will be determined by considering “all of the facts and circumstances in each situation.” The following information will substantiate our abatement request.

**Reasonable cause for abatement of a penalty could exist if a taxpayer reasonably relied on the advice of their tax professionals (IRM 20.1.1.3.2.4).**

Ms. Doe is 88 years old and an inexperienced layperson. She does not exhibit tax expertise and depends on professional assistance for the preparation of her tax returns. Ms. Doe received income from a trust in 2006, however the CPA who prepared the return did not include it in her income. This was an inadvertent error on the CPA’s part due to his computer system not linking the K-1 information with the income on the individual tax return. This was a technological problem that Ms. Doe had no knowledge or control over.

In U.S. v. Boyle, the Supreme Court defined “willful neglect” as a “conscious or intentional failure or reckless indifference.” U.S. v Boyle, 469 U.S. 241, 245 (1985). At her advanced age, Ms. Doe did not recognize that an error had been made when she signed the return and clearly there was no willful neglect, intentional failure or reckless indifference on her part to omit this income. She depended on the expertise of a CPA

**EXAMPLE A**

who has been a reliable advisor in the past and who quite simply made an inadvertent error.

When Ms. Doe was advised by the Internal Revenue Service that additional tax was due, she immediately made payment of the tax and interest but we are requesting this penalty be abated due to reasonable cause.

In *Spies v. United States* the Court noted that "it is not the purpose of the law to penalize frank difference of opinion or innocent errors made despite the exercise of reasonable care....such errors are corrected by the assessment of the deficiency in tax and its collection with interest for the delay." 317 U.S. 492, 496 (1943). The Internal Revenue Manual further provides that penalties exist to encourage voluntary compliance and not for the purpose of bringing additional revenues into the Treasury or for imposing remedial charges against taxpayers. Requiring the taxpayer to pay the assessed penalties will not further the purpose of the penalty provisions

In conclusion, we believe that the above statement of facts establishes a cause for delinquency that a person of ordinary care and prudence would find to be reasonable and not due to willful neglect. The taxpayer's omission of income for the tax period was not intentional or willful but caused by a technical error made by the accounting firm that prepared the return. Ms. Doe, though advanced in age, has an impeccable record of being compliant with filing and paying her taxes and should be afforded consideration.

We respectfully request that the accuracy-related penalty be abated as a one time consideration to an elderly taxpayer.

Your assistance is greatly appreciated.

Sincerely,

Attached: Form 2848  
L3064C

Dear Taxpayer:

Thank you for your correspondence dated 04/27/2010.

We reviewed the information you sent to us. It did not state the reasonable cause necessary to waive the accuracy related penalty.

The law requires you to accurately report on your tax return all income you receive. A tax preparer's system failure does not constitute reasonable cause. Therefore, we must deny your request.

If you need forms, schedules, or publications, you may get them by visiting the IRS website at [www.irs.gov](http://www.irs.gov) or by calling toll-free at 1-800-TAX-FORM (1-800-829-3676).

If you have any questions, please call us toll free at 1-800-829-0922.

If you prefer, you may write to us at the address shown at the top of the first page of this letter.

Whenever you write, please include this letter and, in the spaces below, give us your telephone number with the hours we can reach you. Also, you may want to keep a copy of this letter for your records.

Telephone Number (    ) \_\_\_\_\_ Hours \_\_\_\_\_

**Certified Mail Return Receipt Requested**

Internal Revenue Service  
Attention: Barry Phillips  
2525 Capitol St Ste 108  
Fresno, CA 93721

**Re: Jane Smith**

12345 Some Street  
Phoenix, AZ 85014  
EIN: 33-1234567  
Letter dated January 14, 2009  
Letter 950-D (7-2006)  
Tax Years: 941: 2003-2007 All Quarters  
940: 200312, 200412, 200512, 200612,  
200712

Dear Mr. Phillips:

As attorney in fact for Jane Smith the undersigned hereby protests the findings of the Internal Revenue Service that Jane Smith is liable for \$100,523.08\* for the Failure to File, Failure to Pay and Failure to Deposit penalties (hereinafter "penalties") for the all quarters of 2003-2007 tax years and taxable periods ending December 31, 2003, December 31, 2004, December 31, 2005, December 31, 2006 and December 31, 2007 (hereinafter "taxable periods"). The Taxpayer hereby requests that the Internal Revenue Service not assert the above-noted penalties as the failure to timely file, pay and deposit employment taxes was due to reasonable cause and not due to willful neglect.

Enclosed please find a copy of my Power of Attorney, Form 2848, authorizing me to represent the taxpayer. The undersigned hereby formally requests that a hearing in this matter be granted before the Phoenix Appeals Division of the Internal Revenue Service.

The penalties at issue arise under Sections 6651 and 6656 of the Internal Revenue Code. These provisions specifically provide that penalties will not be assessed where the taxpayer can demonstrate that the failure to timely file tax returns and make federal tax payments is due to reasonable cause. The facts and circumstances in this case will establish reasonable cause.

## FACTS

In a letter dated January 14, 2009, a copy of which is enclosed, the Internal Revenue Service proposed a tax in the amount of \$287,208.63, penalties in the amount of **\$100,523.08 for the taxable periods**. The taxpayer contends that the penalties should not be assessed as the failure to file, pay and make deposits was due to reasonable cause and not due to willful neglect.

**The taxpayer is a former housewife with no business experience.** She, by virtue of an inheritance has become a devoted philanthropist. The taxpayer focused her efforts on a charity that she founded named, Foundation Good Works. Due to her lack of business experience, she surrounded herself with trusted advisors. In particular, the taxpayer hired **Izzie N. Expert, Certified Public Accountant, whom she has known for more than 25 years.** Mr. Expert advised the taxpayer on financial decisions, filing requirements and tax planning strategies. The taxpayer provided Mr. Expert with all financial and tax information in order for him to properly prepare her tax returns. **Mr. Expert, as a Certified Public Accountant, assured the taxpayer that she had properly filed and paid all tax returns each year.**

The taxpayer has employed various individuals to assist her with several needs. She pays these individuals a salary and they receive a W-2 each year. **Mr. Expert's firm prepared the W-2's and prepared her Individual Income Tax Returns.** Mr. Expert advised the taxpayer that she has met all tax filing and paying requirements, including the requirements with respect to her employees. The taxpayer believed that she had properly reported and paid the employment taxes. **The taxpayer knew that Forms W-2 were issued to the employees and she was reassured by Mr. Expert that he had properly filed all necessary tax returns.**

In 2008, the taxpayer was contacted by the Internal Revenue Service with respect to her employment tax return filing. The taxpayer immediately contacted Mr. Expert to assist with this issue as she believed that all required tax returns were filed and paid. Mr. Expert determined that his firm had made an error. He believed that **Schedule H was included on the taxpayer's Individual Income Tax Return in order to report and pay employment taxes for the employees while other members of his firm who assisted with the taxpayer's returns believed that Forms 941 and 940 were being filed by Mr. Expert.** As a result, the employment tax returns were never filed by Mr. Expert and the taxes were unpaid. **The taxpayer did not know that Mr. Expert made this error until she was contacted by the Internal Revenue Service.** The taxpayer has since

terminated Mr. Expert as her accountant and advisor and has retained a new accountant.

This inexperienced taxpayer who was completely unaware of the employment tax filing requirements reasonably relied on the advice of her CPA and trusted advisor, Mr. Expert, to properly file her employment tax returns. She reasonably believed that she was properly filing and paying all required taxes based on Mr. Expert's advice. The fact that Mr. Expert did issue W-2's led her to conclude that she had met her tax obligations with respect to her employees.

### LEGAL ANALYSIS

Section 6651 and 6656(a) of the Internal Revenue Code imposes additions to the tax shown on a return for failure to file, failure to pay and failure to deposit. These provisions expressly contain an exception – “unless it is shown that such failure is due to reasonable cause and not due to willful neglect.” I.R.C. § 6651(a) and 6656(a). The Treasury Regulations define “reasonable cause” as when the “taxpayer exercise[s] ordinary business care and prudence,” and is “nevertheless unable to file the return [or pay the tax] within the prescribed time.” 26 C.F.R. § 301.6651-1(c)(1). In *U.S. v. Boyle*, the Supreme Court defined “willful neglect” as a “conscious, intentional failure or reckless indifference.” *U.S. v. Boyle*, 469 U.S. 241, 245 (1985). The following information will substantiate the taxpayers' penalty abatement requests.

#### **Reasonable Cause**

The taxpayer's failure to file, pay and deposit employment taxes for the taxable periods was due to reasonable cause as the taxpayer exercised ordinary business care and prudence. I.R.M. 20.1.1.3.1 states:

1. Reasonable cause is based on all the facts and circumstances in each situation and allows the IRS to provide relief from a penalty that would otherwise be assessed. Reasonable cause relief is generally granted when the taxpayer exercises ordinary business care and prudence in determining their tax obligations but nevertheless is unable to comply with those obligations.
2. In the interest of equitable treatment of the taxpayer and effective tax administration, the non-assertion or abatement of civil penalties based on reasonable cause or other relief provisions provided in this IRM must be made in a **consistent** manner and should conform with the considerations specified in the Internal Revenue Code (IRC),

Regulations (Treas. Regs.), Policy Statements, and IRM Part 20.1

5. Taxpayers have reasonable cause when their conduct justifies the non-assertion or abatement of a penalty. Each case must be judged individually based on the facts and circumstances at hand. Consider the following in conjunction with specific criteria identified in the remainder of this section, *See IRM 20.1.1.3.*

- What happened and when did it happen?
- During the period of time the taxpayer was non-compliant, what facts and circumstances prevented the taxpayer from filing a return, paying a tax, and/or otherwise complying with the law?
- How did the facts and circumstances prevent the taxpayer from complying?
- How did the taxpayer handle the remainder of their affairs during this time?
- **Once the facts and circumstances changed, what attempt did the taxpayer make to comply?**

Reasonable cause for abatement of the penalties could exist if the taxpayer reasonably relied on the advice of their tax professionals. I.R.M. 20.1.1.3.2.4

Whether a taxpayer's reliance on the advice of their tax professional is a valid basis for the abatement or non-assertion of the penalties is contingent on three factors:

- (1) **Knowledge of the tax law and filing requirements;**
- (2) Whether the taxpayer makes full disclosure of all relevant facts to the professional he/she relies upon and maintains contact with the professional for time to time; and
- (3) Whether the taxpayer has otherwise exercised ordinary business care and prudence. *Rohrbaugh v. United States*, 611 F.2d 211, 214 (1979).

The facts which favor the non-assertion of the penalties for the taxable periods due to reasonable cause for the taxpayer are as follows:

The taxpayer is an inexperienced lay person, who does not exhibit business or tax expertise. As a result, the taxpayer surrounded herself with people who could advise her on these issues and ensure that she is making good business decisions and complying with all tax laws. She hired Mr. Expert, whom she has known for over 25 years.

In *Rohrbaugh v. United States*, the court emphasized that the type of tax would have a bearing on the matter of ordinary business care and prudence when determining whether an inexperienced taxpayer is wholly unaware of the filing requirements. *Id.* at. 214. An inexperienced taxpayer would have **considerable difficulty in demonstrating an unawareness of the due date of an annual income tax return.** *Id.* In the above-noted matter, the taxpayer is inexperienced and unaware of the employment tax filings. She truly believed that Mr. Expert properly filed all required tax returns. This is not a case where a taxpayer is trying to **claim that she was not aware of the due date of her income tax returns.** It is clear, that an inexperienced taxpayer and inexperienced business person would not have the requisite knowledge to know the filing requirements for employment taxes.

**The taxpayer believed that she had selected a competent tax expert** and she supplied him with all necessary information and requested that he prepare all necessary tax returns. Mr. Expert was not only the taxpayer's tax advisor but he was involved in other financial and business decisions that the taxpayer made. He was extremely involved in **her major financial and business decisions and her day-to-day operations.** The taxpayer was in constant contact with Mr. Expert, as often as once a week. Mr. Expert had all necessary information, however, he failed to properly file the taxpayer's employment tax returns.

**The taxpayer is aware that she lacks expertise in the area of business, finances and tax requirements.** As such, she knew it would be prudent to retain competent and recognized experts in these areas. She retained Mr. Expert, with whom she had a long-time business relationship and who had a reputation of being a tax expert. She relied **on these advisors to assist her in planning and managing her finances in order to ensure she was meeting all legal and tax requirements.** Specifically, the taxpayer reasonably relied on the advice of Mr. Expert to see that her tax returns were properly prepared and that she had met all tax filing and payment requirements.

Lastly, once the taxpayer became aware of the error made by her trusted tax expert, she terminated her relationship with him and has taken all necessary steps to ensure that she is in fact meeting all of her tax filing and paying requirements.

### **Willful Neglect**

The taxpayer's failure to file, pay and deposit the employment taxes was not due to willful neglect. As previously mentioned, "willful neglect" is defined as a "conscious, intentional failure

or reckless indifference.” *U.S. v. Boyle*, 469 U.S. 241, 245 (1985). As previously discussed in detail, the taxpayer was completely unaware of the employment tax filing requirements and believed that her Certified Public Accountant and trusted advisor had properly filed all tax returns. **The taxpayer was aware that she did not have the expertise in business or tax requirements, which is why she found people she believed she could trust, like Mr. Expert, to advise her and prepare her tax returns. Clearly, the taxpayer did not exhibit a conscious intentional failure or reckless indifference which would constitute willful neglect.**

The Internal Revenue Service’s stated purpose of delinquency penalties such as failure to file, failure to pay and failure to deposit, is to “encourage voluntary compliance by supporting standards of behavior expected by the Internal Revenue Code.” I.R.M. 20.1.1.2(1). **“Penalties encourage voluntary compliance by: Defining standards of compliant behavior, Defining remedial consequences for noncompliance, and Providing monetary sanctions against taxpayers who do not meet the standard.”** I.R.M. 20.1.1.2(3). As part of this policy of encouraging voluntary compliance, **penalty relief is granted upon the taxpayers’ showing a reasonable cause for such failure to file or pay.** Penalty relief for reasonable cause supports the notions of fairness and effectiveness of the tax system. I.R.M. 20.1.1.2.1. The mistake that was made by her Certified Public Accountant and his office was inadvertent and without the taxpayer’s knowledge. Her income tax filing and paying history coupled with her active solicitation of advisement from tax and financial experts clearly suggest that monetary sanctions are not appropriate under these circumstances.

### **SUMMARY**

Ms. Smith is an inexperienced taxpayer who had never previously had employees and who was completely unaware of the filing requirements for employment taxes. She selected someone she had trusted for over 25 years who she believed was a competent tax professional to prepare all necessary tax returns. **Further, she provided her advisor with all documentation and information with respect to her financial affairs. Her advisor was not only her accountant but he was intimately involved in all of her financial and business decisions, he was personally aware of all of her financial affairs and assisted her in making financial decisions. Finally, the taxpayer exercised business care and prudence, by retaining advisors who she thought to be competent to assist her with her financial, legal and tax decisions due to her lack of knowledge and experience in these areas. She met all other tax filing and paying obligations.**

Accordingly, for settlement purposes and consistent with the government's stated purposes for the penalties, we respectfully request that the penalties for the taxable periods not be asserted.

**If you have any questions about this, please do not hesitate to contact me.**

Sincerely yours,