Failure to Provide Information
Returns and Litigation

ABA May Meeting
Friday, May 10, 2019
11:30am-12:30pm
Grand Hyatt, Washington, DC
Panelists

• Moderator:

• Panelists:
  – Scott E. Fink, Esq., Greenberg Traurig, LLP, New York, NY
  – Mary E. Wood, Esq., Meadows, Collier, Reed, Cousins, Crouch & Ungerma, L.L.P., Dallas, TX.
  – Jonathan R. Black, Esq., IRS Office of Chief Counsel
Information Reporting

• I.R.C. § 6724(b): any penalty imposed shall be paid on notice and demand by the Secretary;
• I.R.C. § 6724(d) defines information returns and payee statements.
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Income Information Returns

• I.R.C. § 6041 requires payments of $600 or more made in the course of a trade or business to be reported on an annual return;

• Information required includes: amount of gains, profits, and income, and the name and address of the recipient of such payment.
Income Reporting Forms

• Form 1099, Miscellaneous Income;
  – Due January 31 of the following year;
  – Must file electronically if filing more than 250;

• Form W-2, Wage and Tax Statement;
  – Must file by January 31 of the following year;
  – Multi-part Form:
    • Copy A to Social Security Administration, via Form W-3, Transmittal of Wage and Tax Statement;
    • Copies B, C, and 2 to employee;
    • Keep Copy D for own records, with copy of Form W-3.
Form 8300

- Form 8300, *Report of Cash Payments Over $10,000 Received in a Trade or Business*;
  - I.R.C. § 6050I
  - Due by the fifteenth day after receipt;
  - Must provide statement to person giving cash;
  - Must contain:
    - Name, address, taxpayer identification number of person providing cash;
    - Amount received;
    - Date and nature of transaction; and
    - Other information as Secretary may prescribe.
Form 1042-S

• Form 1042-S, *Foreign Person’s U.S. Source Income Subject to Withholding*;
  – Reporting U.S. source income to foreign persons;
  – I.R.C. § 1441 requires 30% withholding on foreign aliens;
  – Withholding agent must file even if did not withhold due to a treaty or I.R.C. provision;
  – 2019 Form 1042-S due March 16th.
Form 8805

• Form 8805, Foreign Partner’s Information Statement of Section 1446 Withholding Tax;
  – I.R.C. § 1446 requires withholding on the ECI allocable under I.R.C. § 704 to a foreign partner;
  – Withholding amount equal to the applicable percentage of the ECI of the partnership allocable to foreign partners;
    • Applicable percentage is the highest rate of tax under I.R.C. § 1 & 11(b);
  – File on 15th day of the 3rd month following close of partnership’s tax year.
Form 8966

• Form 8966, *FATCA Report*;
  – Used to report on certain foreign financial accounts and withheld payments;
  – Financial institution must file electronically and all others must file electronically if over 250;
  – Filed on April 1.
Form W-2G

• Form W-2G, *Certain Gambling Winnings*;
  – Due February 28 (by paper) or March 31 (electronically) sent with Form 1096;
  – Following will be reported on W-2G:
    • Bingo or slot winnings of $1,200 or more (not reduced by wager);
    • Keno winnings (reduced by wager) of $1,500 or more;
    • Poker winnings (reduced by wager or buy-in) of $5,000 or more;
    • Winnings (other than those above) reduced by wager of:
      – $600 or more;
      – 300x the wager; or
    • Winnings subject to federal income tax withholding.
Failure to File/Provide Payee Statement

- I.R.C. § 6721(a): failure to file, failure to include all information required or the inclusion of incorrect information will subject filer to a penalty of $250 for each failure, not to exceed $3,000,000 per calendar year;

- I.R.C. § 6722(a): same as above with regard to payee statements.
Penalty Reductions/Exceptions

• Reduced Penalties:
• De Minimis failures;
• Gross receipts limitation; and
• Inconsequential errors or omissions.
Reduced Penalties

• Corrections made within 30 days;
  – $50/$545,500 (83% reduction) or $50/$191,000 (82%).

• Corrections made without 30 days but by August 1st.
  – $100/$1,637,500 (50%) or $100/$545,500 (50%).
De Minimis

- Information return is filed;
- Failure to provide all information required or incorrect information due to reasonable cause;
- Failure corrected by August 1st. I.R.C. § 6721(c)(1).
- Limitation on number of returns, not to exceed 10 or .05% of returns required to be filed. I.R.C. § 6721(c)(2).
De Minimis Safe Harbor

• De minimis safe harbor (no correction required):
  – There are one or more de minimis errors relating to an incorrect dollar amount;
  – No single amount in error differs from the correct amount by more than $100; and
  – No single amount reported for tax withheld on the information return differs from the correct amount by more than $25. I.R.C. § 6721(c)(3).
Gross Receipts

• Taxpayers with gross receipts under $5,000,000 per year will be subject to reduced penalties:
  – Average annual gross receipts of such person for the most recent three taxable years ending before the calendar year at issue do not exceed $5,000,000 (subject to I.R.C. § 448(c)(2) & (3)).
Inconsequential Error or Omission

• An inconsequential error or omission is not considered a failure to include correct information. Treas. Reg. § 301.6721-1(c).

• An inconsequential error or omission is **any failure** that does not prevent or hinder the Internal Revenue Service from **processing the return**, from **correlating the information required to be shown on the return**, or from **otherwise putting the return to its intended use**. The following errors or omissions are never inconsequential:
  – A taxpayer identification number;
  – A surname of a payee; and
  – Any monetary amounts.
Substantial Compliance?

- International information reports (such as Form 5471 and 5472) can be satisfied by substantial compliance;
- “whether the requirements relate ‘to the substance or essence of the statute.’” Taylor v. Commissioner, 67 T.C. 1071, 1077 (1977).
- Is inconsequential error really substantial compliance?
Failure Due To Intentional Disregard

• A failure is due to intentional disregard if it is a *knowing or willful failure* to file timely or to include correct information.

• Facts to consider:
  – Failure is part of a pattern of conduct;
  – Correction was promptly made;
  – Correction within 30 days after request from IRS; and
  – Amount of penalty is less than the cost of compliance or to include correct information.

• Exceptions do not apply!
## Penalties With Inflation

<table>
<thead>
<tr>
<th>When Filed</th>
<th>Gross Receipts Under $5,000,000</th>
<th>Gross Receipts Over $5,000,000</th>
</tr>
</thead>
<tbody>
<tr>
<td>After August 1st or Not at All</td>
<td>$270/</td>
<td>$270/</td>
</tr>
<tr>
<td></td>
<td>$3,275,500</td>
<td>$1,091,500</td>
</tr>
<tr>
<td>Not More Than 30 Days Late</td>
<td>$50/</td>
<td>$50/</td>
</tr>
<tr>
<td></td>
<td>$545,500</td>
<td>$191,000</td>
</tr>
<tr>
<td>31 Days Late to August 1st</td>
<td>$100/</td>
<td>$100/</td>
</tr>
<tr>
<td></td>
<td>$1,637,500</td>
<td>$545,500</td>
</tr>
<tr>
<td>Intentional Disregard</td>
<td>Greater of $540 or 10% aggregate amount of items required to be reported/ No Max</td>
<td>Greater of $540 or 10% aggregate amount of items required to be reported/ No Max</td>
</tr>
</tbody>
</table>
First Time Abatement

• I.R.M., pt. 20.1.1.3.3.2.1(Nov. 21, 2017): provides for the administrative waiver of a penalty if:
  – taxpayer has filed (or is on extension) for all required returns;
  – taxpayer has paid (arrange to pay) any tax currently due; and
  – Taxpayer has not been penalized in preceding three years.

• Not available for I.R.C. § 6721(a) or (e). I.R.M., pt. 4.19.4.3.1(1)(Mar. 28, 2019), only reasonable cause is available.
Reasonable Cause

• I.R.C. § 6724(a): no penalty shall be imposed if due to reasonable cause and not willful neglect.

• Reasonable cause requires:
  – Significant mitigating factors; or
  – The failure arose from events beyond the filer’s control; and
  – Filer acted in a responsible manner before and after the failure occurred. Treas. Reg. § 301.6724-1(a).
Significant Mitigating Factors

• Taxpayer is a first time filer and was not previously required to file this type of return or furnish this particular type of statement; or

• Filer has an established history of complying with the information reporting requirements with respect to which the failure occurred. History of compliance can be established by showing:
  – whether the filer has incurred any penalty under I.R.C. §§ 6721, 6722, or 6723 in prior years for the failure; and
  – if the filer has incurred any such penalty in prior years, the filer’s success in lessening the error rate from year to year. Treas. Reg. § 301.6724-1(b).
Event’s Beyond Filer’s Control

• Unavailability of certain business records;
  – Unavailable under such conditions, in such manner, and for such period as to prevent timely compliance; and
  – Must have been caused by a supervening event.
  • Casualty that damages or impairs business records or system;
  • Statutory or regulatory change that directly impacts data processing; or
  • Unavoidable absence (death or serious illness) of the person with sole responsibility for filing the statements.

• Under economic hardship relating to magnetic media;
  – Failure due to lack of necessary hardware;
Event’s Beyond Filer’s Control (cont’d)

• Actions of Internal Revenue Service;
  – Failure due to filer’s reasonable reliance on the erroneous written information of IRS;
  – Service must be aware of all facts prior to providing written information.

• Actions of Agents; and
  – Filer exercised reasonable business judgment in contracting with the agent; and
  – Agent satisfied the reasonable cause criteria.

• Actions of Payees.
  – Failure to due payee failing to provide information; or
  – Failure of payee to provide correct information.
Responsible Manner

- Filer exercised reasonable care: standard of care that a reasonably prudent person would use under the circumstances in determining the filing obligations and handling the account information;
- Filer undertook significant steps to avoid or mitigate any failure:
  - Requesting appropriate extensions to file;
  - Attempting to prevent a foreseeable impediment;
  - Acting to remove impediment once it has occurred; and
  - Rectifying the failure as promptly as possible once the impediment was removed.
Reasonable Cause Examples

• **Erickson v. Commissioner**: disabled taxpayer did not have reasonable cause because he did not provide all information necessary and did not follow up.

• **In re ACME Music Co., Inc.**: reliance upon the advice of an accountant constitutes reasonable cause for I.R.C. § 6722 purposes. Joint ventures do not give rise to an I.R.C. § 6041(a) filing requirement.
Managerial Approval

• Does the I.R.C. § 6721(a) penalty require managerial approval under I.R.C. § 6751(b)?
  – I.R.M., pt. 4.19.25.5(2) (July 26, 2018): The Notice 972CG determines and calculates (through electronic means) the IRC 6721(a) penalty for failure to file an information return. As a result, the **initial Notice 972CG is exempt from written managerial approval.** Once the taxpayer responds to the Notice 972CG, the tax examiner’s evaluation of the response, regardless of whether or not the taxpayer specifically addresses the penalty, means the exception no longer applies and written managerial approval is needed.
Practical Issues: Examination & Deductions

- How should expenditures without corresponding income information returns be treated during examination?
  - “Section 6721(a) prescribes a monetary penalty for neglecting that obligation, not disallowance of a deduction for the payment that should have been reported. . . . issuance of such forms is not a prerequisite to the deduction of salaries and wages.” Holden v. Commissioner, T.C. Memo. 2015-131, at *13.
  - Cohan rule?
  - Education credit under I.R.C. § 25A(g)(8).
Practical Issues: Trust Fund Recovery Penalty

- I.R.C. § 6672 imposes personal liability on any person required to collect, truthfully account for, and pay over taxes;
  - Liability is equal to amount of tax evaded, not collected, or not accounted for and paid over;
- Both I.R.C. § 6721 and 6672 penalties can be brought at same time (see United States v. Spence, 2010 WL 1463482; see also United States v. Davis, 2014 WL 7272221);
  - Is the I.R.C. § 6721 penalty a pile on in this situation?
Litigation

• Refund
  – Flora v. United States
  – I.R.C. § 6721 and 6722 are divisible.

• CDP
  – I.R.C. § 6320 and 6330: can challenge the underlying liability if no notice of deficiency and did not have an opportunity to dispute.

• Notice of Deficiency
  – Chapter 68 penalties are not brought by notice of deficiency.
  – Not additional amount or addition to tax.

• I.R.C. § 7434; Czerw v. Lafayette Storage & Moving Corp., 2018 WL 5859525 (W.D.N.Y. Nov. 9, 2018);
Relevant Cases (Taxpayer Friendly)

• **Scott Labor, LLC v. Commissioner**: Form 941s and W-2s were off by $2,000,000+. No intentional disregard found due to lack of pattern and taxpayer’s normal practice was to have accountant meet with his bookkeeper to ensure legal compliance.
Relevant Cases (Taxpayer Friendly)

- **American Vending Group, Inc. v. United States**: taxpayer issued W-2s but failed to file with SSA via Form W-3. Taxpayer was provided with Form W-3 for filing but it was left oh his “horribly messy” desk. Taxpayer’s hiring of outside personnel to help with compliance was indicative of his desire to comply.
Relevant Cases (Government Friendly)

• **Steven Technologies, Inc. v. Commissioner**: despite company’s apparent troubles, it was able to operate but for filing its tax returns, paying its taxes, or making deposits. The failure was “a deliberate choice to focus on business matters rather than on tax compliance.”
Relevant Cases (Government Friendly)

• **Bale Chevrolet Co. v. United States:** pattern existed because taxpayer had previously been audited for the same issue-failure to file Form 8300. Although there was only one previous violation, that violation coupled with facts were sufficient for an intentional disregard penalty.