SUBCOMMITTEE REPORT: LEGISLATIVE AND ADMINISTRATIVE DEVELOPMENTS

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LEGISLATIVE AND ADMINISTRATIVE DEVELOPMENTS

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1. Legislative Developments

There does not appear to have been any significant, new enactments or proposed legislation relating to criminal or civil tax penalties since October 2018.

2. IRS Criminal Investigation Releases Fiscal Year 2018 Annual Report

According to its 2018 Annual Report, released November 14, 2018, the IRS Criminal Investigation (CI) division initiated 2886 investigations in fiscal 2018, including 80 cases involving abusive tax schemes, 224 cases involving abusive tax return preparers, 207 cases concerning employment tax, 164 cases of identity theft, and 254 cases regarding nonfilers.

3. Voluntary Disclosures (Domestic and Offshore)

The IRS issued a memorandum (LB&I-09-1118-014) updating the process for all voluntary disclosures (domestic and offshore) following the closing of the 2014 offshore voluntary disclosure program on September 28, 2018. Taxpayers with no exposure to criminal liability can continue to correct past mistakes using other procedures described in the memo or by filing an amended or past due tax return. The procedures described in the memo are effective for all voluntary disclosures received after the closing of the 2014 OVDP on September 28.

A. Updated Criminal Investigation Procedures

- CI Screening: CI will screen all voluntary disclosure requests whether domestic, offshore, or other to determine if a taxpayer is eligible to make a voluntary disclosure.
  - All taxpayers wishing to make a voluntary disclosure must submit a preclearance request on a forthcoming revision of Form 14457. Under the new procedures, preclearances are required.
  - IRM 9.5.11.9 will continue to serve as the basis for determining taxpayer eligibility.

- Request Preclearance: Taxpayers must request preclearance from CI via fax or mail.

- Submission of Voluntary Disclosure Documents: For all cases where CI grants preclearance, taxpayers must then promptly submit to CI all required voluntary disclosure documents using a forthcoming revision of Form 14457.
Once CI has received and preliminarily accepted the taxpayer’s voluntary disclosure, CI will notify the taxpayer of preliminary acceptance by letter and simultaneously forward the voluntary disclosure letter and attachments to the LB&I Austin unit for case preparation before examination.

- Civil Processing by LB&I Austin: Once the LB&I Austin unit receives information from CI, LB&I will route the case as appropriate. The LB&I Austin unit will establish the most recent tax year covered by the voluntary disclosure for examination.
- Case Assignment for Civil Examination: The LB&I Austin unit will forward cases for case building and field assignment to the appropriate Business Operating Division and Exam function for civil examination. Civil examiners receiving the disclosure will establish any additional controls necessary on IRS systems.
- Case Development: All voluntary disclosures handled by examination will follow standard examination procedures.

### B. Civil Resolution Framework

For all voluntary disclosures received after September 28, 2018, the IRS will apply a civil resolution framework, which includes specific guidance related to the assessment of penalties. At the IRS’s discretion, this framework may extend to non-offshore voluntary disclosures that have not been resolved but were received on or before September 28, 2018.

- The “civil fraud penalty” will apply to the one tax year with the highest tax liability. The “civil fraud penalty” refers to the civil penalty under (i) IRC §6663 for fraud or (ii) IRC §6651(f) for the fraudulent failure to file income tax returns.
  - In limited circumstances, examiners may apply the civil fraud penalty to more than one year in the six-year scope (up to all six years) based on the facts and circumstances of the case, for example, if there is no agreement as to the tax liability.
  - Examiners may apply the civil fraud penalty beyond six years if the taxpayer fails to cooperate and resolve the examination by agreement.
- Willful FBAR penalties will be asserted in accordance with existing IRS penalty guidelines under IRM 4.26.16 and 4.26.17.
- A taxpayer is not precluded from requesting the imposition of accuracy related penalties under IRC §6662 instead of civil fraud penalties or non-willful FBAR penalties instead of willful penalties. Given the objective of the voluntary disclosure practice, granting requests for the imposition of lesser penalties is expected to be exceptional. Where the facts and the law support the assertion of a civil fraud or willful FBAR penalty, a taxpayer must present convincing evidence to justify why the civil fraud penalty should not be imposed.
- Penalties for the failure to file information returns will not be automatically imposed.
- Penalties relating to excise taxes, employment taxes, estate and gift tax, etc. will be handled based upon the facts and circumstances with examiners coordinating with appropriate subject matter experts.
- Taxpayers retain the right to request an appeal with the Office of Appeals.

### 4. Estimated Tax Penalty Waived for Some Exempt Organizations
- **Affected Taxpayers:** Tax Exempt organizations offering qualified transportation fringe (QTF) benefits that were not required to file a Form 990-T for the tax year immediately preceding the organization’s first tax year ending after December 31, 2017. The relief is limited to tax-exempt organizations that timely file Form 990-T and timely pay the amount reported for the tax year for which relief is granted.
- Taxpayers who do not qualify for relief may avoid an addition to tax for underpayment of estimated income tax if they meet one of the statutory safe harbor or exception provisions under section 6654 or section 6655.

The IRS announced (Notice 2018-100) that it will provide estimated tax penalty relief in 2018 to tax-exempt organizations that offer QTF benefits, but underpaid their taxes due to changes in the treatment of some QTFs under the Tax Cuts and Jobs Act (TCJA) (P.L. 115-97). The TCJA added section 274(a)(4), which prohibits employers from deducting expenses for qualified transportation fringes provided to employees. The TCJA also added section 512(a)(7), which requires tax-exempt organizations to increase unrelated business taxable income (UBTI) by the amount of the expenses that are no longer deductible and that are paid or incurred for any QTFs and any parking facility used in connection with qualified parking.

The provisions in section 512(a)(7) may result in some tax-exempt organizations owing UBTI and having to pay estimated income tax for the first time; however, these organizations are not eligible for a safe harbor under section 6655 (that would allow them to calculate the required annual payment of estimated income tax based on their return for the preceding tax year).

Because these taxpayers may need more time to develop the knowledge and processes to comply with estimated income tax payment requirements, the IRS will waive the section 6655 addition to tax for failure to make estimated payments otherwise required to be made before December 18, 2018.

5. **Preparer Due Diligence Penalty (No Substantive Change to July 2018 Proposed Regs)**

The IRS issued final regulations on tax return preparer penalties, which adopted—without substantive change—the proposed regulations published in July 2018.

6. **IRS Updates Accuracy-Related Penalty Guidance (No Substantive Changes)**

Non-substantive, editorial changes were made to Rev. Proc. 2019-9, which provides guidance on whether disclosure of a position taken on a tax return is adequate for purposes of reducing the section 6662(d) accuracy-related penalty and section 6694(a) return preparer penalty. Rev. Proc. 2019-9 applies to any income tax return filed on 2018 tax forms for a tax year beginning in 2018 and to any income tax return filed in 2019 on 2018 tax forms for short tax years beginning in 2019.

7. **New Guidance on Assessment of IRC §6715(a)(2) Dyed Fuel Penalties**

The IRS Small Business/Self-Employed Division issued interim guidance (SBSE-04-1018-0026) on (i) establishing the presence of dye in a fuel sample subject to a penalty assessed under section 6715(a)(2) and (ii) addressing situations in which a penalty may be assessed without a
sample. To confirm the presence of dye, the fuel compliance officer or agent (FCO/FCA) will obtain a fuel sample for analysis if the fuel is subject to an IRC §6715(a)(2) penalty is observed during the screening process. In a situation where the FCO/FCA visually detects that the fuel in the vehicle or storage tank is dyed but is unable to obtain a sample using an approved sampling method, an IRC §6715(a)(2) penalty may still be assessed under very limited circumstances. See IRM 4.24.15 for the approved fuel sampling methods.

To assess the penalty, the FCO/FCA must obtain written evidence, such as a fuel delivery ticket, verifying conclusively that the fuel in the tank is dyed. The FCO/FCA must, as with all penalties assessed under IRC §6715, determine the number of gallons subject to the penalty. The IRS may not default to assessing a $1,000 penalty without considering the number of gallons involved. If the FCO/FCA did not inspect the tank, he or she must calculate the penalty based on records and oral or written testimony to determine the number of gallons in the tank at the time of the inspection.

8. **Interim Guidance on Processing §6201(a)(4) Interest and Penalty Additions in CDP Cases with Restitution-Based Assessments**

The IRS provided interim guidance (AP-08-1118-0014) to Appeals technical employees on processing §6201(a)(4) interest and penalty additions in collection due process cases with restitution-based assessments in light of the Tax Court’s decision in *Klein v. Commissioner*, 149 T.C. No. 15 (2017). The guidance will apply to cases in collection due process (CDP) and Equivalent Hearings (EH) that include one or more restitution-based assessments with interest and penalty additions.

In *Klein*, the court held that §6201(a)(4) does not authorize the IRS to assess and collect underpayment interest and “failure-to-pay” additions to tax on the amount of restitution a couple was ordered to pay as a result of their tax crime convictions. Restitution ordered in a criminal tax case is designed to compensate the IRS for the loss caused by the defendant’s wrongdoing, but that award does not purport to reflect the defendant’s actual civil tax liability. Thus, the court held that the IRS could perform a civil examination of the couple’s returns if it wished to collect interest and additions to tax.

9. **Due Diligence Penalty Assessed Against Co-Owner May Bring Hazards**

In emailed advice (ECC 201845006), the IRS described the law regarding application of the section 6695(g) due diligence tax return preparer penalty and determined that there will likely be legal hazards if the penalty is asserted against the 25 percent owner of an S corporation because the co-owner does not directly employ the return preparers.

10. **Revised Standard Explanation for Disallowance of EIC**

The IRS Small Business/Self-Employed Division issued interim guidance (SBSE-04-1218-0031) to revise the standard explanation for the “failure to file” penalty for the 2018 and 2019 tax years. The penalty for tax returns due after January 1, 2018 will be the lesser of $210 or the tax due.