



# **LIBERTYTAX<sup>®</sup>**

**Penalty Abatement: First Time Guidelines Reasonable Cause**

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**1 Credit Hour, CLE and CPE**

# Objectives

- Identify the statutes authorizing the IRS to abate penalties based on 1st time guidelines or reasonable cause
- Compare and contrast a client's reasonable cause facts to existing case law and factors cited in IRM
- Accurately complete and submit the required documentation by following the advocacy tips presented
- Empower clients to make informed decisions through education
- Know the administrative remedies available when request(s) are denied, i.e. appeals, mediation, and tax court

# Important Legal Distinction

Internal Revenue Code (IRC)

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The IRC is a federal statute, meaning it is law enacted by Congress (codified in Title 26 of the United States Code).

## Content:

- Substantive tax laws that govern federal tax obligations
- Outlines rules and regulations for tax collection, rates, deductions, credits, and penalties

## Authority:

- Force of law
- Binding on taxpayers & IRS

## Amendments:

- Only through legislative action by Congress.

# Important Legal Distinction

## Internal Revenue Manual (IRM)

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The IRM is an internal document used by the IRS (compilation of guidelines, procedures, and policies).

## Content:

- Detailed instructions to IRS employees on how to administer and enforce tax laws
- Provides procedural guidance on administrative processes, i.e., audits, collections, appeals...

## Authority:

- No force of law but intent is to ensure consistency and efficiency within the IRS
- Not binding on taxpayers

## Amendments:

- IRS may update and revise as needed.

# Statutory Law

**IRC grants IRS the authority to assess AND abate:**

- IRC §6651(a)(1) – Late Filing
- IRC §6651(a)(2) – Late Payment

**Treasury Regulations provide interpretation of IRC (binding law)**

- Treas. Reg. §301.6651-1(c) - what constitutes reasonable cause for failure to file or pay taxes

**IRM provides procedural requirements for assessing and abating**

- IRM 20.1 Penalty Handbook - criteria for relief from certain penalties



# **Administrative Waiver: First Time Abatement (FTA)**

20.1.1.3.3.2.1 (03-29-2023) First Time Abate (FTA)



# Administrative relief from three penalty types, only:



**Failure to File**



**Failure to Pay**



**Failure to Deposit IRC**

# Elements Necessary to Approval:

1. Filed a return or had no filing requirement for the preceding 3 years
2. Modules do not have any type of unreversed penalty for the preceding 3 years

\*except estimated tax penalty

# Reasonable Cause

IRM 20.1.1.3.2 (11-21-2017)

**Based on all the facts and circumstances in each situation**

**Exceptions apply to certain penalties for public policy and equitable reasons, i.e., Civil Penalties.**

**Granted if the taxpayer exercised ordinary business care and prudence.**

**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.**

## Consider the following in conjunction with specific factors we cover next (re: Slide 13):

**1.**

What happened and when did it happen?

**2.**

During the time taxpayer was non-compliant, what facts and circumstances prevented the taxpayer from filing/paying and/or otherwise complying?

**3.**

How did the facts and circumstances result in the taxpayer not complying?

**4.**

How did the taxpayer handle the remainder of their affairs during this time?

**5.**

Once the facts and circumstances changed, what attempt did the taxpayer make to comply?

# Ordinary Business Care and Prudence

**20.1.1.3.2.2 (02-22-2008)**

**In determining if the taxpayer exercised ordinary business care and prudence, review available information including the following:**

- a. Taxpayer's Reason:
- b. Compliance History:
- c. Length of Time:
- d. Circumstances Beyond the Taxpayer's Control

# Statutory Criteria/Factors

## (based on specific reasonable cause)

- 20.1.1.3.2.2.1 (11-25-2011) Death, Serious Illness, or Unavoidable Absence
- 20.1.1.3.2.2.2 (10-19-2020) Fire, Casualty, Natural Disaster, or Other Disturbance-Reasonable Cause
- 20.1.1.3.2.2.3 (12-11-2009) Unable to Obtain Records
- 20.1.1.3.2.2.4 (12-11-2009) Mistake Was Made
- 20.1.1.3.2.2.5 (11-21-2017) Erroneous Advice or Reliance
- 20.1.1.3.2.2.6 (11-25-2011) Ignorance of the Law

# Death, Serious Illness, or Unavoidable Absence

## 20.1.1.3.2.2.1 (11-25-2011)

Factors and information to consider (not inclusive):

- a. The relationship of the taxpayer to the other parties involved.
- b. The date of death.
- c. The dates, duration, and severity of illness.
- d. The dates and reasons for absence.
- e. How the event prevented compliance.
- f. If other business obligations were impaired.
- g. If tax duties were attended to promptly when the illness passed, or within a reasonable period of time after a death or return from an unavoidable absence.

**Fire, Casualty,  
Natural Disaster,  
or Other  
Disturbance**  
20.1.1.3.2.2.2 (10-19-2020)

**Factors to consider include the following:**

- a. Timing
- b. Effect on the taxpayer's business
- c. Steps taken to attempt to comply
- d. If the taxpayer complied when it became possible



# Unable to Obtain Records

20.1.1.3.2.2.3 (12-11-2009)

## Factors and information to consider (not inclusive):

- a. Why the records were needed to comply.
- b. Why the records were unavailable and what steps were taken to secure the records.
- c. When and how the taxpayer became aware that he or she did not have the necessary records.
- d. If other means were explored to secure needed information.
- e. Why the taxpayer did not estimate the information.
- f. If the taxpayer contacted the IRS for instructions on what to do about missing information.
- g. If the taxpayer promptly complied once the missing information was received.
- h. Supporting documentation such as copies of letters written and responses received in an effort to get the needed information.



# Mistake Was Made

20.1.1.3.2.2.4 (12-11-2009)

Factors and information to consider (not inclusive):

- a. When and how the taxpayer became aware of the mistake.
- b. The extent to which the taxpayer corrected the mistake.
- c. The relationship between the taxpayer and the subordinate (if the taxpayer delegated the duty).
- d. If the taxpayer took timely steps to correct the failure after it was discovered.
- e. The supporting documentation.

# Erroneous Advice or Reliance

20.1.1.3.2.2.5 (11-21-2017)

- The taxpayer may try to establish reasonable cause by claiming they relied on another party to comply on their behalf.
- Generally, this is not a basis for reasonable cause, particularly for filing or paying obligations, since the taxpayer is responsible for meeting their tax obligations and that responsibility cannot be delegated. However, other factors to consider include:
  - Was the taxpayer unable to comply because they did not have access to their own records? See IRM 20.1.1.3.2.2.3, Unable to Obtain Records.
  - Was the failure to comply due to a change in the tax law the taxpayer could not reasonably be expected to know? See IRM 20.1.1.3.2.2.6, Ignorance of the Law.

# Ignorance of the Law

20.1.1.3.2.2.6 (11-25-2011)

## Factors:

- The taxpayer's education.
- If the taxpayer has previously been subject to the tax.
- If the taxpayer has been penalized before.
- If there were recent changes in the tax forms or law which a taxpayer could not reasonably be expected to know.
- The level of complexity of a tax or compliance issue.
- The taxpayer may have reasonable cause for noncompliance due to ignorance of the law if the following are true:
  - A reasonable and good faith effort was made to comply with the law, or
  - The taxpayer was unaware of a requirement and could not reasonably be expected to know of the requirement.

# Case Law - Reliance on Tax Advice from Expert

United States v. Boyle, 469 U.S. 241 (1985)

## **Holding U.S. Supreme Court:**

Reasonable Cause denied, reliance on attorney did not relieve taxpayer of duty to file timely. Attorney forgot to calendar estate return deadline, so it was filed late.

## **Facts:**

Estate return was filed three months late, apparently because of a clerical oversight in omitting the filing date from the attorney's calendar.

## **Reasoning:**

While engaging an attorney to assist in probate proceedings is plainly an exercise of the "ordinary business care and prudence" that the relevant Treasury Regulation requires the taxpayer to demonstrate to excuse a late filing, this does not answer the question presented here. To say that it was "reasonable" for respondent to assume that the attorney would meet the statutory deadline may resolve the matter as between them, but not with respect to the respondent's obligation under that statute.

It requires no special training or effort on the taxpayer's part to ascertain a deadline and ensure that it is met. That the attorney, as respondent's agent, was expected to attend to the matter does not relieve the principal of his duty to meet the deadline.

# Case Law - Reliance on Counsel as Reasonable Cause

Thouron v. United States, No. 13-1603 (3d Cir. May 13, 2014)

## **Holding Third Circuit:**

Reliance on Counsel may Relieve Penalties for Late Payment of Taxes.

## **Facts:**

In his will, the decedent appointed a friend as executor of the estate and the friend hired a tax attorney to advise the estate on tax matters. Relying on the advice of the attorney, the estate timely filed an extension for time to file the estate return and remitted a partial payment but did not file for an extension to pay the remainder of the tax due. The estate claimed its attorney advised it that the extension to pay was not due until the return was filed and that the tax due would be deferred under I.R.C. section 6166 because the bulk of the estate's assets were illiquid.

## **Reversed and Remanded:**

Distinguishing Boyle because it involved reliance on an adviser for merely the ministerial task of filing, the court noted the distinction drawn in Boyle between relying on an expert's clerical action and relying on the expert's advice: "taxpayers may rely on the advice of an expert but may not, for purposes of completing their statutory duty, rely on an agent to perform the task of filing and paying."

# Best Practice and Procedure

IRS loves their forms, in the case we look to 843,  
Claim for Refund and Request for Abatement.

- One form per tax form and year/qtr (no 2014-2016)
- Write the USC citation for the type of penalty
- Attach an extra page for your explanation and computation

\*\*\*Include PROOF – the IRS is not going to just take our word at face value. The burden of proof is on US/Taxpayer.

- medical/hospital records, police reports, bankruptcy or court documents, obituary, etc.





# Sample Language for 1st Time

- Based on the information provided, it is TAS's position that \$(insert dollar amount or "all" as applicable) of the (insert type) penalty is eligible for abatement based on first-time abate guidelines. (Insert an explanation of why the supporting documentation supports such a position.) We recommend you abate the penalty for reasons explained above. If you disagree and intend to sustain the penalty, contact me with an explanation and allow me three work days to review your reasoning before you sustain the penalty, per the Service Level Agreement (SLA)."

▶ See separate instructions.

Use Form 843 if your claim or request involves:

- (a) a refund of one of the taxes (other than income taxes or an employer's claim for FICA tax, RRTA tax, or income tax withholding) or a fee, shown on line 3,
- (b) an abatement of FUTA tax or certain excise taxes, or
- (c) a refund or abatement of interest, penalties, or additions to tax for one of the reasons shown on line 5a.

**Do not** use Form 843 if your claim or request involves:

- (a) an overpayment of income taxes or an employer's claim for FICA tax, RRTA tax, or income tax withholding (use the appropriate amended tax return),
- (b) a refund of excise taxes based on the nontaxable use or sale of fuels, or
- (c) an overpayment of excise taxes reported on Form(s) 11-C, 720, 730, or 2290.

Name(s) <b>First Last; SpouseFirst Last (make sure the primary Taxpayer is listed first)</b>		Your social security number <b>123-45-6789</b>
Address (number, street, and room or suite no.) <b>Clients address</b>		Spouse's social security number <b>987-65-4321</b>
City or town, state, and ZIP code <b>Client's address</b>		Employer identification number (EIN)
Name and address shown on return if different from above <b>**Make sure this is completed if the current address is different from the address on the tax return in question.</b>		Daytime telephone number <b>client #</b>
<b>1</b>	<b>Period.</b> Prepare a separate Form 843 for each tax period or fee year. From <b>20**/12</b> to <b>20**/12</b>	<b>2</b> <b>Amount to be refunded or abated:</b> \$ <b>All if not processed/no AT</b>
<b>3</b>	<b>Type of tax or fee.</b> Indicate the type of tax or fee to be refunded or abated or to which the interest, penalty, or addition to tax is related. <input type="checkbox"/> Employment <input type="checkbox"/> Estate <input type="checkbox"/> Gift <input type="checkbox"/> Excise <input checked="" type="checkbox"/> Income <input type="checkbox"/> Fee	
<b>4</b>	<b>Type of penalty.</b> If the claim or request involves a penalty, enter the Internal Revenue Code section on which the penalty is based (see instructions). IRC section: <b>6651(a)</b>	
<b>5a</b>	<b>Interest, penalties, and additions to tax.</b> Check the box that indicates your reason for the request for refund or abatement. (If none apply, go to line 6.) <input type="checkbox"/> Interest was assessed as a result of IRS errors or delays. <input type="checkbox"/> A penalty or addition to tax was the result of erroneous written advice from the IRS. <input checked="" type="checkbox"/> Reasonable cause or other reason allowed under the law (other than erroneous written advice) can be shown for not assessing a penalty or addition to tax.	
<b>b</b>	Date(s) of payment(s) ▶	
<b>6</b>	<b>Original return.</b> Indicate the type of fee or return, if any, filed to which the tax, interest, penalty, or addition to tax relates. <input type="checkbox"/> 706 <input type="checkbox"/> 709 <input type="checkbox"/> 940 <input type="checkbox"/> 941 <input type="checkbox"/> 943 <input type="checkbox"/> 945 <input type="checkbox"/> 990-PF <input checked="" type="checkbox"/> 1040 <input type="checkbox"/> 1120 <input type="checkbox"/> 4720 <input type="checkbox"/> Other (specify) ▶	
<b>7</b>	<b>Explanation.</b> Explain why you believe this claim or request should be allowed and show the computation of the amount shown on line 2. If you need more space, attach additional sheets.	

The taxpayer(s) respectfully requests abatement of the failure to file and failure to pay penalties pursuant to IRM 20.1.1.3.3.2.1 (03-29-2023) First Time Abate (FTA). The taxpayer(s) has filed all currently required returns and paid, or arranged to pay, any tax due. The taxpayer(s) have not previously been required to file a return or has no prior penalties for the preceding three (3) years on the same MFT.  
Computation of the amount shown on line 2:

# Sample – First Time Abatement

## Sample: Reasonable cause, Fire

**Suggested language:** “A fire in the taxpayer’s home destroyed records needed to file a return. See the supporting documentation provided. It is TAS’s position that the entire FTF and FTP penalty is eligible for abatement due to reasonable cause (casualty destroyed records) as the taxpayer filed the return with full payment two months after the fire. The two-month delay represented the time it took Attachment the taxpayer to recreate the records necessary to file an accurate return. We recommend you abate the penalties for the reasons explained above. If the RCA conclusion is to sustain either penalty or to utilize FTA, please suspend the case, contact me with an explanation, and allow me three work days to review your reasoning before you sustain the penalty, per the Service Level Agreement (SLA).”

## **Sample: Reasonable Cause, Unavoidable Absence/Illness**

**Suggested language:** “The taxpayer was hospitalized unexpectedly from April xx through May xx, preventing him from filing and paying his taxes timely. The doctor’s statement verifies hospitalization through the dates indicated. The taxpayer filed and paid the tax in full promptly once released from the hospital. The taxpayer states there was no one to handle his affairs. It is TAS’s position that all of the FTF and FTP penalties are eligible for abatement due to unavoidable absence. We recommend you abate the penalties for the reasons explained above. If the RCA conclusion is to sustain either penalty, please suspend the case, contact me with an explanation, and allow me three work days to review your reasoning before you sustain either penalty, per the Service Level Agreement (SLA).”

# Advocacy Tips – Reasonable Cause Assistant (RCA)

## The RCA Conclusion

The RCA will reach one of five possible conclusions for the MFT and the tax period reviewed (listed in order of priority):

- Abate - reasonable cause established; remove penalty.
- Suspend - insufficient information; no conclusion reached.
- Sustain - reasonable cause not established.
- Mixed - abate one penalty/sustain the other.
- Other - not a reasonable cause issue. For example, a taxpayer disputes how the IRS computed a penalty.

# Administrative Remedies

## The RCA Conclusion

- Submit 843
- At any level of disagreement, it may be more productive for the taxpayer to raise the issue in Appeals, rather than continuing to dispute the abatement denial with the OD/Function. Appeals can consider case law and hazards of litigation.
- If the issue is grey or mixed, Appeals may be a better option for settlement. Discuss this with the taxpayer or his or her representative, and if the taxpayer decides to go to Appeals, the taxpayer must file an appeal to the denial of penalty relief.

# Questions?