

# ***DEFENDING TAX PENALTIES***

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# *DEFENDING TAX PENALTIES*

- INTERNATIONAL PENALTIES
  - > 31 U.S.C. §5321(a)(5) – Penalty for failing to file a foreign bank account report
    - \$10,000 per violation or
    - Penalty is 50% of the total balance of the foreign financial account per violation
    - Reasonable cause/willful analysis
  - > IRC §6038D – Penalty for failing to file an information return
    - \$10,000 per violation
    - Form 8938
    - Statute of limitations problem
    - Additional \$10,000 added for each month the failure continues after taxpayer notified up to \$50,000 maximum
    - Reasonable cause defenses

# *DEFENDING TAX PENALTIES*

- **INTERNATIONAL PENALTIES (CONT'D)**
  - > IRC §6039F – Failure to report transactions involving foreign trusts
    - Form 3520
    - Failing to file (or incomplete reporting) is the greater of \$10,000 or 35% of the gross reportable amount
    - For gifts the penalty is 5% of the gift per month up to max of 25%
    - Reasonable cause
  - > IRC §6048(b) – Transactions – Failure to report ownership interests in a foreign trust with U.S. owner
    - Form 3520-A
    - \$10,000 or 5% of the gross value of the trusts' assets
    - Reasonable cause

# ***DEFENDING TAX PENALTIES***

- **INTERNATIONAL PENALTIES (CONT'D)**

- > IRC §§6035, 6038 and 6046 – Penalty for failing to file information return for certain U.S. persons who own interests in foreign corporations
  - Form 5471
  - \$10,000 per information return with additional \$10,000 added for each month the failure continues 90 days after taxpayer notified by IRS, up to maximum of \$50,000 per return
  - Reasonable cause
- > IRC §6038B – Penalty for failure of U.S. person to report transfer of property to U.S. corporation
  - Form 926
  - \$100,000 per return with no limit if intentional

# *DEFENDING TAX PENALTIES*

- **INTERNATIONAL PENALTIES (CONT'D)**
- > IRC §§6038, 6038B and 6046A – Penalty for U.S. persons who fail to report certain interests, transfers, acquisitions, disposition in foreign partnerships
  - Form 8865
  - \$10,000 per return up to \$50,000 after demand/notice of failure by the IRS, and 10% of the value of the property not reported
  - Subject to a \$100,000 limit
  - Reasonable cause

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  - Form 5471
  - \$10,000 per information return with additional \$10,000 added for each month the failure continues 90 days after taxpayer notified by IRS, up to maximum of \$50,000 per return
  - Reasonable cause
- > IRC §6038B – Penalty for failure of U.S. person to report transfer of property to U.S. corporation
  - Form 926
  - \$100,000 per return with no limit if intentional

# *DEFENDING TAX PENALTIES*

- **DELINQUENCY PENALTIES**

- > IRC §6651 – Failure to File or Pay

- §6651(a)(1) – failure to file return (FTF)
- §6651(a)(2) – failure to pay tax (FTP)
- §6651(a)(3) – failure to pay tax within 10 days of notice and demand (FTPN&D)
- FTF and FTP are each a maximum of 25% of unpaid tax but FTF is reduced by each month's FTP --- total of 47.5%
- Reasonable cause

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- **ACCURACY RELATED PENALTIES**

- > **IRC §6662(a) – Negligence- 20% of underpayment**
  - **§6662(a) – Negligence**
  - **§6662(d) – Substantial understatement penalty**
  - **§6662(e) – substantial valuation misstatement penalty**
  - **§6662(f) – substantial overstatement of pension liabilities**
  - **§6662(g) – substantial estate or gift tax valuation understatement**
  - **§6662(h) – increase in penalty in case of “gross valuation misstatements” from 20% to 40%**
  - **§6662(i) – increase in penalty for non-disclosed noneconomic substance transactions from 20%-40%**
  - **§6662(j) – undisclosed foreign financial asset understatement**
    - **failures on information returns required under IRC §§6038, 6038B, 6038D, 6046A or 6046**
    - **Increase from 20% to 40%**

# ***DEFENDING TAX PENALTIES***

- **REASONABLE CAUSE EXCEPTION (IRC §6664(c)(1))**
  - Good faith
  - Ordinary care and prudence
  - Reasonable reliance on advice
  - Qualified appraisal
  - Disclosure on return
  - Conflicts of interest
  - Mistakes
  - Qualified amended returns – Rev. Proc. 94-69
  - Administrative waivers by Service Center – first time offense
  - Lack of significant business purpose
  - Education, competence or sophistication of taxpayer
  - Tax shelters
  - Substantial authority
  - Death, illness, injury of the taxpayer
  - Natural disasters, fire, etc.

**[See also Reg. 1.6664-4(a) and IRM 20.1.5.6.1]**

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- **MORE PENALTIES**

- IRC §6694 – Return preparer penalties
- IRC §6666 – Erroneous claims for refund – 20% penalty on the “excessive amount” of the refund
- IRC §6654 – Failure to pay estimated tax
- IRC §6656 – Failure to deposit
- IRC §6651(f) and §6663 – Civil Fraud Penalties
  - 75% of the underpayment
  - Unlimited statute of limitations
  - Burden of proof on the IRS to show:
    - Understatement
    - Badges of fraud – intent

# ***DEFENDING TAX PENALTIES***

**The End!**

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