AGOSTINO & ASSOCIATES

November 2018

Monthly Journal of Tax Controversy

Contents

Upcoming Events

2018 IRS Representation Conference
November 29-30 RSVP: https://irsrepconference.com/
Mohegan Sun Casino & Resort, CT

Tax Settlement Programs—NJ Tax Amnesty, NJ Closing Agreements, IRS Voluntary Disclosures and OIC
December 4 RSVP: conta.cc/2EEJ1AN
Hackensack, NJ

Representing the Innocent Spouse—Proving Abuse
December 13 RSVP: conta.cc/2E76avI
Las Vegas, NV

IRS Problem Solving Day
December 13-14 RSVP: conta.cc/2EGiJOM
Las Vegas, NV

THE INTERNATIONAL INFORMATION REPORTING PENALTIES: IS THE IRS'S FAILURE TO EMBRACE A ONE-STOP SHOPPING PARADIGM INEFFICIENT AND STATUTORILY DEFICIENT?

By Frank Agostino, Esq. and Phillip J. Colasanto, Esq.[1]

This article is a follow-up to Erin Collins's and Garrett Hahn's article titled *Foreign Information Reporting Penalties: Assessable or Not?* published in Tax Practice's Tax Notes, on July 9, 2018.

The Internal Revenue Service's ("IRS" or "Service") bifurcation of income tax and international information return examinations has created an inefficient and expensive procedure for examining income tax returns of taxpayers with offshore income and assets. This article focuses on why penalties for failure to file international information returns must be processed under deficiency procedures, rather than the procedures created for assessable penalties.

The article examines the statutory authority for three of the most frequently asserted international penalties under Sections 6038B, 6038, and 6038D of the Internal Revenue Code (the "Code").[2] These penalties relate to the failure to file, comply, or substantially comply with instructions for Forms 926, *Return by a U.S. Transferor of Property to a Foreign Corporation*, 5471, *Information Return of U.S. Persons With Respect to Certain Foreign Corporations*, and 8938, *Statement of Specified Foreign Specified Foreign Financial Assets*.

Specified Foreign Financial Assets. Like Collins and Hahn, we conclude there is nothing in the Code that prohibits the simultaneous examination, appeal, or trial of the domestic and foreign issues related to these returns. The common law doctrine of res judicata, coupled with the statutory prohibition of unnecessary and repetitive examinations, Appeals hearings, and tax court trials, suggests that tax professionals should be more proactive in resisting unnecessary bifurcation and processing of international examinations and the IRS should reconsider their inefficient and statutorily questionable processing of these cases.

I. Assessable Penalties v. Deficiency Procedures

The litigation of the shared responsibility penalty in *NFIB v. Sebelius*, 132 S.Ct. 2566 (2012) reminded tax professions that whether an item is a penalty or a tax is a matter of substance not title. For purposes of this article, items used to calculate a taxpayer's income tax liability for a particular tax year will be considered a tax and any additional amounts or additions to the tax will be considered penalties. The Service generally assesses penalties through summary assessment or deficiency procedures.

Penalties subject to summary assessment procedures are primarily found in Sections 6671 through 6720C. Summary assessments are made without a deficiency determination and "shall be paid upon notice and demand . . . and collected in the same manner as taxes."[3] Assessments record the tax liability[4] and the taxpayer's name and address.[5] Once a penalty is assessed, the taxpayer is sent a notice and demand for payment. Assuming the penalty is not paid, the Service will either issue a notice of intent to levy or to file a notice of federal tax lien.[6] The notice of federal tax lien[7] and notice of intent to levy[8] inform the taxpayer of the right to a collection due process ("CDP") hearing. If a CDP hearing is not requested, the lien will stay in effect until the IRS forecloses and/or forces the sale of the taxpayer's property or levies the taxpayer's property to satisfy the outstanding liability.

Deficiency procedures are employed when the Service determines that non-compliance affected a deficiency in tax. Common penalties associated with deficiency actions include Section 6662 accuracy-related penalties and Section 6651 failure-to-file penalties.[9] Before the Service can assess additional tax it must issue a notice of deficiency.[10] The notice of deficiency will inform the taxpayer of the tax periods involved, the deficiency, the taxpayer's options, a statement showing how the deficiency was computed, and an explanation of the adjustments.[11] The notice of deficiency will also inform the taxpayer of the last day to petition the United States Tax Court for pre-assessment and pre-payment review.[12]

In short, deficiency procedures require the Service to determine a deficiency and allow the taxpayer to petition the Tax Court for a redetermination of the deficiency prior to making an assessment and initiating any collection action. Assessable penalties, on the other hand, are assessed before the taxpayer is given notice and a right to challenge the penalties. The Service's focus with such penalties is on the collection.

Although there are differences between how assessable penalties and deficiencies are imposed, challenged, and collected, some penalties can be subject to either the deficiency procedures or can be summarily assessed, depending on the situation. Failure-to-file and failure-to-pay penalties can be summarily assessed or determined through the deficiency procedures, depending on whether there is a deficiency in tax.[13] If there is no deficiency on the return, such penalties can be summarily assessed and a notice and demand for payment can be sent to the taxpayer. Otherwise, the penalties must be brought as part of the deficiency proceedings.

II. Forms and Code Sections

A. Form 926

Form 926 is an international information return required by Section 6038B. Section 6038B requires that a U.S. person who transfers property to a foreign corporation, as part of an exchange, or to a foreign partnership, as part of a contribution, or who distributes to a person who is not a U.S. person, provides "information with respect to such exchange or distribution [.]"[14]

Failure to file Form 926 results in a penalty "equal to 10 percent of the fair market value of the property at

the time of the exchange" or "in the case of a contribution * * * such person shall recognize gain as if the contributed property had been sold for such value at the time of such contribution."[15] If a taxpayer is forced to recognize gain as if the property was sold at fair market value then that deficiency in tax must go through the deficiency procedures.

Failure to file a Form 926 can also result in an increased accuracy-related penalty. Section 6662(j) applies a 40% penalty for any undisclosed foreign financial asset understatement, which "means, for any taxable year, the portion of the understatement of such taxable year which is attributable to any transaction involving an undisclosed foreign financial asset."[16] Any property not included on a Form 926 can cease to be property for use in the active conduct of a trade or business.[17] Section 6662(j) penalties are additional amounts and additions to tax that apply to an understatement of tax. Understatements of tax generally, if not always, result in an income tax deficiency, which must be assessed through the deficiency procedures. Thus, if the Service has determined a recognized gain or an accuracy-related penalty, deficiency procedures are the appropriate means of assessment.

Form 926 is to be filed with the U.S. person's income tax return for the year in which the transfer of property occurred.[18] The statute of limitations for assessment on a failure to file Form 926 is "3 years after the date on which the Secretary is furnished the information required to be reported under such section."[19]

Failure to file Form 926 can result in multiple actions against the taxpayer. First, if the taxpayer fails to file Form 926 and has transferred property to a foreign corporation or partnership, the taxpayer will be penalized 10% of the fair market value of the property. This requires a determination of fair market value. The 10% penalty is not an understatement of tax and will be summarily assessed and collected by the Service through either a lien or levy notice. Second, if the taxpayer recognizes gain from the contribution then there will be an income tax deficiency, which will be separately assessed through the deficiency procedures (which can also include the 40% accuracy-related penalty, if appropriate). Thus, for the same transfer a taxpayer can receive a notice of deficiency and notice of intent to lien or levy. Although both penalties arose from the same transaction and have identical facts and arguments, the taxpayer is forced to litigate on two separate fronts, with potential inconsistent determinations of value.

B. Form 5471

Form 5471 is required by Sections 6038 and 6046. Section 6038 requires U.S. persons to furnish information "with respect to any foreign business entity which such person controls [.]"[20] Section 6038 requires the corporation's basic information (name of company, country of incorporation), its undistributed earnings, a balance sheet, and information regarding any transactions between: the foreign corporation and the U.S. person, or any entity controlled or 10%-owned by the U.S. person.[21]

Section 6046, likewise, requires filing of Form 5471 for a U.S. citizen or resident, who is also a U.S. person, who owns or purchases 10% or more of the total combined voting power of all classes of stock or of the total value of stock of a foreign corporation.[22]

Failure to file Form 5471 under Section 6038 results in a $10,000 penalty, a continuation penalty with a $50,000 maximum, a potential 10% reduction of any foreign tax credit claimed and/or deemed paid to any foreign country, and a 5% per three-month period continuation penalty. The reductions are not to exceed the greater of $10,000 or the income of the foreign business entity for the taxable period.[23]

Failure to file Form 5471 as required by Section 6046 is penalized under the provisions of Section 6679.[24] Section 6046 contains a cross-reference to Section 6679, which authorizes a $10,000 penalty for failure to file or submission of an incomplete filing. This penalty also includes a continuation penalty with a $50,000 maximum.[25] Section 6679 also provides that deficiency procedures do not apply.[26] Like Section 6038B penalties, there is an increased accuracy-related penalty of 40%, which is applied to any undisclosed foreign financial asset understatement on the corresponding income tax return.[27]

Failure to file Form 5471, pursuant to Section 6038, can lead to both a deficiency notice and a summarily assessed penalty. In such cases, the Service will summarily assess a $10,000 failure-to-file penalty and the

send a notice and demand for payment. If the penalty is not paid, the Service will send a notice of lien and/or levy and proceed with collection. At the same time, the Service will send the taxpayer a notice of deficiency for the reduction of the foreign tax credit, which increases the tax owed by the taxpayer. Thus, much like Form 926, Form 5471 violations can result in litigation on multiple fronts with inconsistent determinations.

C. Form 8938

Section 6038D requires any individual holding any interest in a specified foreign financial asset (worth over $50,000 in the aggregate) to provide information on foreign financial asset or assets by attaching the appropriate information to the income tax return.[28] Specified foreign financial assets include any financial asset maintained by a foreign financial institution or any stock, security, financial instrument, or interest in a foreign entity not held by a financial institution.[29] The information required is generally a description of the asset, where the asset originated from or is maintained, and the maximum value of the asset.

Failure to file Form 8938D will result in a $10,000 penalty, and a corresponding continuation penalty not to exceed $50,000.[30] Further, like Sections 6038 and 6038B, there is an increased accuracy-related penalty (40%) for an undisclosed foreign financial asset understatement, which is not properly reported on the income tax return.[31]

Much like violations under Sections 6038 and 6038B, a Section 6038D violation can lead to both a penalty assessment and income tax deficiency. Failure to file Form 8938 will result in a $10,000 penalty, which the IRS will summarily assess and collect. Additionally, failure to file Form 8938 will result in a deficiency because of income from the undisclosed foreign financial asset, such as interest or dividend income earned from a foreign bank or investment account. With all three forms, the taxpayer can be subject to litigation of the same issues for the same tax years in separate forums, which is both costly and time-consuming.

III. Reasonable Cause Defense

The consequences of failure to file under Sections 6038, 6038B, or 6038D can be avoided with a showing of reasonable cause.[32] Similarly, a Section 6662(j) penalty can be abated with a showing of reasonable cause.[33] Generally, the taxpayer can establish reasonable cause by showing that despite the exercise of ordinary business care and prudence he or she was unable to comply with the law.[34]

One basis for establishing reasonable cause which often pertains to international information returns is the inability to obtain records. Inability to obtain records due to circumstances beyond the taxpayer's control, despite the exercise of ordinary business care and prudence, may satisfy reasonable cause.[35] This is particularly relevant to Form 5471 filing requirements that stem from attribution rules of Section 318.[36] Under Section 318, a taxpayer whose spouse or sibling owns a foreign corporation must file information on a foreign corporation with which he or she has no connection. In such situations, the inability to obtain records may be satisfactory reasonable cause.

IV. Assessable Penalties, Additions to the Tax, and Additional Amounts:

Title 26, Subtitle F, Chapter 68, Subchapter B, titled *Assessable Penalties*, allows the Service to assess and collect certain penalties "in the same manner as taxes."[37] These penalties "shall be paid upon notice and demand by the Secretary."[38] Title 26, Subtitle F, Chapter 68, Subchapter A, titled *Additions to the Tax and Additional Amounts*, allows the IRS to impose penalties for failing to file or pay tax, understatements or underpayments of tax, and penalties for fraudulent behavior.[39]

Although assessable penalties, additional amounts, and additions to tax are not identical, they often lead to the same result: the taxpayer must pay more than just the outstanding tax liability and interest. Most of these "penalties" are included in Chapter 68 of the Code.

There are, however, some "penalties" that are not included in Chapter 68. For penalties outside of Chapter

68, there is usually either a cross-reference to a Code section within Chapter 68 or a Code section authorizing the penalty will have a provision allowing the Secretary to assess. The following chart depicts some of the "penalties" not included in Chapter 68 and the corresponding assessment authority:

Code Section (Chapter of Code)	Code Authority for Assessment
6011 (Chapter 61)	Section 6707A(a): "Any person who fails to include on any return or statement any information with respect to a reportable transaction which is required under section 6011 to be included with such return or statement shall pay a penalty in the amount determined under subsection (b)."
527 (Chapter 1)	Section 527(j)(1)(B): "For purposes of subtitle F, the amount imposed by this paragraph shall be assessed and collected in the same manner as penalties imposed by section 6652(c)."
9707 (Chapter 99)	Section 9707(f): "For purposes of this title, the penalty imposed by this section shall be treated in the same manner as the tax imposed by section 4980B."
7519 (Chapter 77)	Section 7519(f)(1): "Except as otherwise provided in this subsection or in regulations prescribed by the Secretary, any payment required by this section shall be assessed and collected in the same manner as if it were a tax imposed by subtitle C."
6039F (Chapter 61)	Section 6039F(c)(1)(B): "such United States person shall pay (upon notice and demand by the Secretary and in the same manner as tax) an amount equal to 5 percent of the amount of such foreign gift for each month for which the failure continues (not to exceed 25 percent of such amount in the aggregate)."
6043 (Chapter 61)	Section 6043(d) "For provisions relating to penalties for failure to file–(1) a return under subsection (b), see section 6652(c), or (2) a return under subsection (c), see section 6652(1)."
6046 (Chapter 61)	Section 6046(f): "For provisions relating to penalties for violations of this section, sections 6679 and 7203."
6046A (Chapter 61)	Section 6046A(e): "For provisions relating to penalties for violations of this section, see sections 6679 and 7203."
5000A (Chapter 48)	Section 5000A(g)(1): "The penalty provided by this section shall be paid upon notice and demand by the Secretary, and except as provided in paragraph (2), shall be assessed and collected in the same manner as an assessable penalty under subchapter B of chapter 68."

This list of penalties not included in Chapter 68 is not all-inclusive but demonstrates how the Code deals with penalties not included in Chapter 68. The statute will either cross reference another section within Chapter 68 (such as Section 6046) or the Section will state that the penalties are to be assessed like tax, or as in Chapter 68 (such as Sections 6039F and 5000A).

Sections 6038, 6038B, and 6038D, however, have no cross reference and do not specifically state that the penalties can be assessed like tax.

Code Section	Penalty Provision and Cross References
6038	Section 6038(b)(1): If any person fails to furnish, within the time prescribed under paragraph (2) of subsection (a), any information with respect to any foreign business entity required under paragraph (1) of subsection (a), such person shall pay a penalty of $10,000 for each annual accounting period with respect to which such failure exists. Section 6038(f) Cross References: (1) For provisions relating to penalties for violations of this section, see section 7203. (2) For definition of the term "United States person", see section 7701(a)(30).
6038B	Section 6038B(c)(1): If any United States person fails to furnish the information described in subsection (a) at the time and in the manner required by regulations, such person shall pay a penalty equal to 10 percent of the fair market value of the property at the time of the exchange (and, in the case of a contribution described in subsection (a)(1)(B), such person shall recognize gain as if the contributed property had been sold for such value at the time of such contribution).
6038D	Section 6038D(d)(1): In general, if any individual fails to furnish the information described in subsection (c) with respect to any taxable year at the time and in the manner described in subsection (a), such person shall pay a penalty of $10,000.

Sections 6038, 6038B, and 6038D do provide the Service with authority, either via cross reference or the language of the statute, to assess the penalties upon notice and demand as if they were taxes. The only cross reference in Section 6038(f) is to Section 7203. Section 7203 is a criminal provision, which provides that taxpayer who fail to file, supply information, or pay tax shall "in addition to other penalties provided by law, be guilty of a misdemeanor and, upon conviction thereof, shall be fined not more than $25,000 ($100,000 in the case of a corporation), or imprisoned not more than 1 year, or both, together with the costs of prosecution." Section 7203 is focused solely upon the criminal repercussions for failure to file and does provide for summary assessments of Section 6038 penalties. Without a express authority to do so, the Service should not summarily assess penalties under Section 6038, 6038B, and 6038D.

V. Deficiency Procedures

Sections 6038, 6038B, and 6038D should be subject to deficiency proceedings. Because these "penalties" are not assessable and Forms 926, 5471, and 8938 are intertwined with income tax returns, it is more appropriate to consider them additional amounts or additions to the tax under Section 6214 than penalties. Section 6214 specifically provides that the U.S. Tax Court, as part of its authority to determine a deficiency, can also "determine whether any additional amount, or any addition to the tax should be assessed [.]"[40]

First, Sections 6038, 6038B, and 6038D can each trigger a Section 6662 accuracy-related penalty. Section 6662(j) allows for a 40% penalty to be asserted on "any portion of an underpayment which is attributable to any undisclosed foreign financial asset understatement [.]"[41] Section 6662 "penalties" are in Title 26, Subtitle F, Chapter 68, Subtitle A- Additions to the Tax and Additional Amounts. Section 6662 additions to the tax and additional amounts are based upon information reported on the income tax return.

Second, the connection between the forms and the income tax return compels the conclusion that the forms and the return should not be considered as separate forms. These forms must be filed with the income tax

return, including extensions of time to file. Also, it is our experience that Section 6038D penalties will be reported on the IRS Transcripts of Account for the Form 1040, *U.S. Individual Income Tax Return*, as opposed to Section 6038 penalties which are only reported on the Civil Penalty Transcripts. Therefore, these forms do not differ from any other form or schedule required to be filed with the income tax return.

Third, the statute of limitations for examining these penalties is directly connected with and may impact the income tax return. Section 6051(c)(8)(A), which provides the statute of limitations for items required under Sections 6038, 6038B, and 6038D, states that "the ***time for assessment of any tax imposed by this title with respect to any tax return***, event, ***or period to which such information relates*** shall not expire before the date which is 3 years after the date on which the Secretary is furnished the information required to be reported under such section."[42]

Section 6501(c)(8)(A) is telling because it shows just how intertwined these forms are with the income tax return, where failing to provide foreign financial information can allow for an indefinite statute of limitations regarding examination of the income tax return ("with respect to any tax return") or of any tax year ("or period to which such information relates"). Failing to provide foreign financial information is so critical to submitting a complete income tax return that the statute of limitations on the return will remain open until the reporting requirements are satisfied. Thus, failure to file an information return may indefinitely keep the entire tax year open for examination.

Fourth, Sections 6038, 6038B, and 6038D provide for "penalties" and directly affect the taxpayer's income tax return. For instance, Section 6038 allows for the reduction of the foreign tax credit, which can then create an underpayment of tax, and Section 6038B requires that the taxpayer "recognize gain as if the contributed property had been sold for such value at the time of such contribution," which may lead to an increase in taxable income. Because of the direct connection to income tax returns, Section 6038, 6038B, and 6038D "penalties" are more like Section 6651 additions to tax than they are to assessable penalties. Section 6651 additions to tax are not independent grounds for petitioning the Tax Court but they can be included as part of a deficiency determination,[43] which is exactly how Sections 6038, 6038B, and 6038D penalties should be treated. Although Section 6651 additions to tax can also be summarily assessed, this is only because they are found within Chapter 68. This is not the case for Section 6038, 6038B, and 6038D penalties.

The U.S. Tax Court should have jurisdiction over international penalty determinations because the Court's jurisdiction is based upon the tax year and because the Court may redetermine additional amounts or additions to the tax.[44] The Tax Court, however, has tried to abstain from resolving conduct based penalties in deficiency proceedings. In *Smith v. Commissioner*,[45] the Tax Court determined that it did not have jurisdiction to redetermine a Section 6707A penalty as part of the deficiency proceeding. Nonetheless, whether redetermination of Section 6038, 6038B, or 6038D penalties by the Tax Court is appropriate has not yet been resolved.

Penalties under Sections 6038, 6038B, and 6038D are also not similar to Section 6707A penalties. In *Smith v. Commissioner*, the Court determined that Section 6707A penalties are in Chapter 68, subchapter B of the Code and are, therefore, summarily assessable penalties. Assessable penalties are often, but not always, not includible in deficiency procedures. Section 6707A, however, did not contain such a limitation. Although an assessable penalty can be subject to deficiency procedures, the Court in *Smith* stated: "this Court has never exercised jurisdiction over an assessable penalty that was not related to a deficiency, even absent Congress' explicitly circumscribing our jurisdiction."[46] This language does not mean that the Tax Court does not or cannot have such jurisdiction but rather that it abstained from determining jurisdiction. This leaves the door open for future challenges.

Additionally, unlike the statute of limitations for Sections 6038, 6038B, and 6038D, Section 6707A does not reference the tax return or tax period. The omission of a reference to the tax return or period indicates that Section 6707A is only concerned with the assessment of any tax regarding a specific transaction, as opposed to any tax for a specific tax period.

Section 6707A violations also do not give rise to accuracy-related penalties, unlike Section 6038, 6038B,

and 6038D violations. Accuracy-related penalties are directly connected with and to the income tax return. Therefore, the holding in *Smith* is not applicable to the present penalties and, even if it were, the Court's decision that it did not have jurisdiction must be revisited.

VI. CDP Problems with Existing System

If Section 6038, 6038B, and 6038D "penalties" are treated as assessable, rather than as subject to deficiency procedures, several issues may arise during the collection due process ("CDP") proceedings.

First and foremost, the ability to challenge the underlying liability of a summarily assessed penalty in a CDP hearing only exists "if the person did not receive any statutory notice of deficiency for such tax liability or did not otherwise have an opportunity to dispute such tax liability."[47] Thus, if the taxpayer's failure to file Form 5471 leads to both a summarily assessable penalty and a notice of deficiency, the taxpayer may not be able to challenge that summarily assessed penalty in a CDP hearing because (a) the notice of deficiency was sent and (b) the taxpayer previously had the ability to dispute such tax liability. Therefore, as an initial matter, these Section 6038, 6038B, and 6038D penalties may not be subject to review in a CDP hearing if there is an accompanying deficiency procedure.

Additionally, Sections 6320 and 6330, which give rise to CDP hearing rights for notices of lien and levy, respectively, entitle a person "to only one hearing under this section with respect to the taxable period to which the tax specified in subsection (a)(3)(A) relates."[48] This one-hearing requirement may preclude taxpayers from challenging penalty assessments for a tax year if a hearing has already been held for the same year because of administrative res judicata.

Res judicata, however, can cut both ways. On one side, the taxpayer can argue that the Service cannot assess additional penalties for a tax period once a hearing for that tax period has been completed. The taxpayer should argue that Appeals does more than just verify the Service's actions and should conduct a de novo review of the tax year. Upon completion of a hearing for a particular tax year, all outstanding issues for that tax year should be resolved. Once Appeals conducts a de novo review and issues a notice of determination, the taxpayer should argue that the determination is final and no other assessments should be made for that tax year. Conversely, the Service may argue that once a hearing has been conducted the taxpayer should be precluded from requesting another to challenge the newly assessed penalty. The Service may further argue that the taxpayer would not be entirely foreclosed from challenging the penalty because he or she has the option to pay the penalty and sue for a refund.

The Service has issued regulations that conflict with this one-hearing per period limitation.[49] These regulations allow for additional hearings for different types of tax or situations where the same taxes for the same period is involved but the tax has changed.[50] This position, however, directly conflicts with the statute. The statute provides taxpayers with "only one hearing." As a matter of statutory construction, it is significant that "only" was used in connection with "one," indicating that "one hearing" was insufficient and to be further limited by "only." The Service cannot modify or expand the statute through regulations. These regulations can be challenged as arbitrary under *Chevron*.[51]

These regulations are of particular importance because international information returns have their own statute of limitations (discussed in more detail below) which allow for the assessment of penalties for three years after the required information is provided.[52] The extended limitations period makes penalty assessments after a particular tax year has already been examined more probable. In such cases the applicability of res judicata is crucial.

VII. Res Judicata & Collateral Estoppel Concerns

As discussed above, there are res judicata and collateral estoppel concerns. If a taxpayer receives a notice of deficiency for a particular tax year and then is assessed an international information return penalty for that same tax year the taxpayer may be precluded from: 1) challenging the merits of the assessed penalty in a CDP hearing; and 2) from seeking a redetermination by the Tax Court of the penalty. The Tax Court's jurisdiction is based on the tax year. Thus, if a tax year is resolved without inclusion of the summarily as-

sessed penalty, the Service may argue that the Court no longer has jurisdiction over that year. The taxpayer's only recourse would be to pay the penalty and seek a refund.

Additionally, even if res judicata does not fully preclude a taxpayer from litigating a previously resolved tax year, collateral estoppel, or issue preclusion, may apply. For instance, if a penalty for the failure to file a Form 8938 is assessed and a notice of deficiency is issued for failure to report income stemming from a foreign financial asset, which is accompanied by a section 6662(j) accuracy-related penalty, the taxpayer may, and probably will, have the same reasonable cause for failure to file. If the reasonable cause defense has already been denied by the Tax Court then the taxpayer may not be able to raise it again due to collateral estoppel. Thus, it is imperative that these matters be litigated together, otherwise taxpayers may not be able to properly challenge the subsequent assessments and/or determinations.

Finally, difficulties arise when there is both an ongoing deficiency proceeding in the Tax Court and a summarily assessed penalty is being collected by the Service for the same tax year and issue. The Service simultaneously levying while litigating the same issue in the Tax Court is not only distracting but also creates a hardship for the taxpayer. A taxpayer focused upon their ongoing litigation may not have the resources and/or wherewithal to also file a CDP hearing request and to conduct a separate Appeals/CDP hearing. In such situations, the taxpayer's representative should consider filing a motion under Rule 55 of the Tax Court Rules of Practice and Procedure to restrain the Service from the assessment and collection of tax. This will ensure that there is one battle being fought and that the Service cannot use the pressure of collection to influence the taxpayer.

VIII. Statute of Limitations Considerations

Generally, the statute of limitations for assessing any tax, including interest and penalties, for a particular tax year is three years from the date the return was filed.[53] The Service contends that international information returns have a separate statute of limitations, which raises two questions: 1) does the statute of limitations require the filing of a specified form or is it satisfied by providing the requisite information to the Secretary; and 2) does the statute of limitations provision authorize and/or provide for the penalties associated with the failure to file Forms 926, 5471, and 8938 and, if not, does the catchall five-year statute of limitations under 28 U.S.C. § 2462 apply?

A. Providing Information Versus Filing the Form

Section 6501(c)(8)(A), which provides the statute of limitations for international information returns, focuses upon "the date on which the Secretary is furnished ***the information required to be reported under such section***."[54] Compare this to the general statute of limitations, found in Section 6501(a), which provides: "the amount of any tax imposed by this title shall be assessed within 3 years ***after the return was filed***."[55] The inclusion of the term "return" in Section 6501(a) and the failure to include either "return" or "form" in Section 6501(c)(8)(A) leads to the conclusion that Sections 6038, 6038B, and 6038D can be satisfied without the filing of the forms prescribed by the Service.

The distinction between filing the form and providing the required information is important for penalties assessed under Section 6038D because it requires filing information related to foreign financial assets. If the foreign financial asset is a bank account, filing a FinCen Form 114 (FBAR) and properly reporting the account information on Schedule B of the Form 1040 may begin the running of the statute of limitations. Additionally, if the FBAR and Schedule B provide the information required by Section 6038D, filing of Form 8938 may not be required for the statute of limitations to run.

One position is that the statute and statute of limitations require that information be provided and so long as such information is provided the taxpayer has satisfied the filing requirements. Although sound, this position has not yet been successfully litigated or approved by any court. Thus, tax professionals should keep this distinction in mind and make the argument when appropriate, but should not rely on this position for not filing international information returns in the future. On a quasi-related note, the furnishing of information requirement is a re-establishment or re-affirmation of the lessons taught in *Beard*. *Beard* stands for the proposition that a filing can constitute a valid return, for triggering the running of the statute of limitations, even if it

is not provided on the specifically designated form. Here, Section 6501(c)(8)(A) does not require a form to be filed but rather that information to be provided. Therefore, *Beard* is also relevant to international information returns.

Section 6501(c)(8)(A) and *Beard* are important to know and understand because the failure to provide the information required under Sections 6038, 6038B, and 6038D can create an indefinite statute of limitations for an income tax return. Section 6501(c)(8)(A) provides that "the time for assessment of ***any tax*** * * * ***with respect to any tax return***, event, or ***period*** to which such information relates shall not expire before the date which is 3 years after the date on which the Secretary is furnished the information required to be reported under such section."[56] Thus, if a taxpayer fails to file Form 926, 5471, or 8938 then the time for assessment on any tax (including income) and regarding any tax return (Form 1040) or period (the tax year) will not expire until three years after the required information is furnished. Essentially, failure to file the required international information return leaves the statute of limitations for the tax liability and entire tax period open indefinitely.

B. The Statute of Limitations for Assessment of Section 6038, 6038B, and 6038D Penalties

Upon a close reading Section 6501(c)(8), it is unclear whether the statute of limitations provision actually applies to the penalties imposed under Sections 6038, 6038B, and 6038D. Section 6501(c)(8)(A) provides:

> In the case of any information which is required to be reported to the Secretary pursuant to an election under section 1295(b) or under section 1298 (f), 6038, 6038A, 6038B, 6038D, 6046, 6046A, or 6048, ***the time for assessment of any tax imposed by this title with respect to any tax return, event, or period*** to which such information relates shall not expire before the date which is 3 years after the date on which the Secretary is furnished the information required to be reported under such section.[57]

The plain language of the statute does not provide for the assessment of the penalties imposed under Section 6038, 6038B, and 6038D. The statute extends the time for assessment regarding "any tax * * * with respect to any tax return, event, or period" but it does not specifically state that the penalties imposed under Sections 6038, 6038B, or 6038D are also extended. There is an argument to be made that the term "any tax" includes, as it does in certain portions of the Code, additional amounts, additions to tax, and penalties but that is not made abundantly clear.

It is unclear is Sections 6038, 6038B, and 6038D penalties are included in "any tax." However, Sections 6501(a) and 6501(c)(8) can work and live in harmony as one provides the statute of limitations for the income tax return and any forms included therewith, while the other focuses upon information that was not provided and affects the taxpayer's income tax liability. Alternatively, if Section 6501(c)(8) does not provide the statute of limitations for the Section 6038, 6038B, and 6038D penalties, the catchall five-year statute of limitations, found in 28 U.S.C. § 2462, applies and limits the time to assess such penalties to five years from "the date when the claim first accrued[.]"[58]

28 U.S.C. § 2462 provides that:

> Except as otherwise provided by Act of Congress, an ***action, suit or proceeding*** for the ***enforcement of any civil fine, penalty***, or forfeiture, pecuniary or otherwise, shall not be entertained ***unless commenced within five years from the date when the claim first accrued*** if, within the same period, the offender or the property is found within the United States in order that proper service may be made thereon.

28 U.S.C. § 2462 is a catch-all statute of limitations that prevents taxpayers from the undue harm and prejudice that can arise from an indefinite statute of limitations. The plain language of the statute makes it clear that it is applicable to penalties assessed under Sections 6038, 6038B, and 6038D.

The statute provides that "an action [or] proceeding for the enforcement * * * of any penalty * * * shall not be entertained unless commenced within five years from the date when the claim first accrued[.]" The assessment process is part of the proceeding for the enforcement of Section 6038, 6038B, and 6038D penalties. Assessment is the beginning of the proceeding that will eventually lead to the collection of the penalty and is crucial to the penalty enforcement regime.

Therefore, if the Section 6501(a) three-year statute of limitations does not apply then the five-year catchall statute of limitations may apply. Again, this has not been argued or decided but it is a position that tax practitioners should be aware of and raise when available.

IX. **Conclusion**

The current system for assessment of penalties associated with international information returns ineffective and is not supported by statutory text. Litigation will determine whether the penalties should be subject to deficiency proceedings.

This article should be read in connection with the Form 5471 (October 2018), Form 926 (August 2018), and Form 8938 (July 2018) articles published in the Agostino & Associates Newsletter.

As always, if you have questions, please contact the attorneys at Agostino & Associates, P.C.

Endnotes:

1. Frank Agostino, Esq. is the principal of, and Phillip J. Colasanto, Esq. is an associate at, Agostino & Associates, P.C.
2. All references to "Section" numbers are to sections of the Internal Revenue Code of 1986, as amended.
3. I.R.C. § 6671(a).
4. I.R.C. § 6203.
5. IRM, pt. 35.9.2.1(1) (Aug. 11, 2004).
6. See IRM, pt. 5.11.1.3.2(1) (Nov. 9, 2017); see also I.R.M., pt. 5.12.7.3.1(4) (Sep. 21, 2017).
7. IRM, pt. 5.12.7.6.6(1) (Sep. 21, 2017).
8. See IRM, pt. 5.11.1.3.2(1) & (5) (Nov. 9, 2017).
9. See I.R.C. § 6212(a).
10. IRM, pt. 4.8.9.2.1 (Aug. 11, 2016).
11. IRM, pt. 4.8.9.8(1) (July 9, 2013).
12. See IRM, pt. 4.8.9.10.2(1) & (3) (July 9, 2013).
13. See I.R.C. § 6651.
14. I.R.C. § 6038B(a).
15. I.R.C. § 6038B(c).
16. I.R.C. § 6662(j)(1).
17. Treas. Reg. § 1.367(a)-2(a)(2); I.R.M., pt. 20.1.9.7.4(1) (July 8, 2015).
18. See Treas. Reg. § 1.6038B-1(b); Instructions to IRS Form 926, *Return by a U.S. Transferor of Property to a Foreign Corporation*, (2017) available at https://www.irs.gov/pub/irs-pdf/i926.pdf.
19. I.R.C. § 6501(c)(8).
20. I.R.C. § 6038(a).
21. *Id.*
22. I.R.C. § 6046(a).
23. I.R.C. § 6038(b) & (c).
24. I.R.C. § 6046(f).
25. I.R.C. § 6679(a).
26. I.R.C. § 6679(b).
27. I.R.C. § 6662(j).
28. I.R.C. § 6038D(a).
29. I.R.C. § 6038D(b).
30. I.R.C. § 6038D(d).

31. I.R.C. § 6662(j).
32. I.R.C. §§ 6038(c)(4), 6038B(c)(2), 6038D(g).
33. Treas. Reg. § 1.6662-1.
34. IRM, pt. 20.1.1.3.2.1 (Nov. 21, 2017).
35. IRM, pt. 20.1.1.3.2.2.3 (Dec. 11, 2009).
36. I.R.C. § 6038(e)(2).
37. I.R.C. § 6671(a).
38. *Id.*
39. I.R.C. §§ 6651, 6662, & 6663.
40. I.R.C. § 6214(a).
41. I.R.C. § 6662(j).
42. I.R.C. § 6501(c)(8)(A) (emphasis added).
43. IRM, pt. 8.17.7.1.1(3) (Sep. 24, 2013).
44. *Commissioner v. Sunnen*, 333 U.S. 591 (1948); I.R.C. § 6214(a).
45. *Smith v. Commissioner*, 131 T.C. 424, 429 (2009).
46. *Id.*
47. I.R.C. § 6330(c)(2)(B).
48. I.R.C. §§ 6320(b)(2) & 6330(b)(2).
49. See Treas. Reg. §§ 301.6320-1(d)(2)(Q&A-D1) and 301.6330-1(d)(2)(Q&A-D1).
50. See Treas. Reg. §§ 301.6320-1(d)(2)(Q&A-D1) and 301.6330-1(d)(2)(Q&A-D1).
51. See *Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837 (1984).
52. I.R.C. § 6501(c)(8)(A).
53. I.R.C. § 6501(a).
54. I.R.C. § 6501(c)(8)(A).
55. I.R.C. § 6501(a) (emphasis added).
56. I.R.C. § 6501(c)(8)(A) (emphasis added).
57. I.R.C. § 6501(c)(8)(A) (emphasis added).
58. 28 U.S.C. § 2462.

FORM 8865: U.S. PERSONS WITH INTEREST IN FOREIGN PARTNERSHIPS

By Frank Agostino, Esq. and Joseph A. Stackhouse, Jr.[1]

I. Introduction

The Internal Revenue Service ("IRS") generally uses international information returns to analyze how taxpayers interpret the Internal Revenue Code ("IRC" or "Code"),[2] guard against abuse of tax provisions, and start investigations into tax evasion. In the November 2018 Public Report the IRS Advisory Council identified Form 8865, *Return of U.S. Persons with Respect to Certain Foreign Partnerships*, as an important tool for analyzing high level transfer pricing risk and conducting economic and statistical analysis. This article examines Form 8865 and explains the categories of taxpayers that must file Form 8865, the transactions that must be reported, the consequences of failure to file, and how non-filers can become compliant.

II. Taxpayers Use Form 8865 to Report Information on Certain Transactions with Foreign Partnerships

Form 8865 pertains to U.S. persons who have interest in foreign partnerships. Generally, a partnership issues Schedule K-1 (Forms 1065) to each partner, which reports each partner's distributive share of capital, losses, and profits. Each partner then reports and pays tax on his or her share of the partnership's profits and losses to the IRS. However, the items reported on Schedule K-1 do not tell the whole story. Form 8865 supplements Schedule K-1 by disclosing certain reportable transactions that frequently lead to abuse of the Code.[3]

The IRS does not use Form 8865 to assess tax but rather to gain more information about items reported on the taxpayer's income tax return. If, based on information provided on the filed Form 8865, the IRS believes something is wrong on a taxpayer's tax return, the IRS can initiate an audit or issue an administrative summons.[4]

Accordingly, the IRS mandates that the following four categories of taxpayers report foreign partnership transactions using Form 8865:

> Category 1: A U.S. person having control over a foreign partnership;
> Category 2: A U.S. person owning a 10% or greater interest in a foreign partnership while U.S. persons owning a 10% or greater interest controlled the partnership;
> Category 3: A U.S. person contributing property to a foreign partnership for an interest in the partnership; and
> Category 4: A U.S. person who acquires, disposes of, or has a change in his proportional interest in a foreign partnership.[5]

For purposes of Form 8865, a "U.S. person" is a citizen or resident of the United States, a domestic partnership, a domestic corporation, an estate, and certain trusts.[6] Under Section 6038(e)(3)(2) "control" means owning, or being attributed, directly or indirectly, at least 50% of the capital interest, profit interest, or deduction or losses of the foreign partnership.

All Form 8865 filers must report personal information and the partnership's name, principal place of business, business activities, and country of incorporation.[7] All filers must also report the name, address, and U.S. taxpayer identification number of the person(s) whose interest the filer constructively owns and all partnerships in which the foreign partnership has a direct or indirect 10% interest on Schedules A and A-2, respectively. However, the schedules that must be filed with Form 8865 and the transactions that must be reported are different for each filer category. A taxpayer who falls into more than one category is required to file only one Form 8865 but must attach the appropriate schedule for each category he or she falls into. There is a minor exception to this rule discussed below.[8] In addition, the taxpayer must assign a Unique

Reference Identification ("URI") number to each foreign partnership requiring a Form 8865.[9]

U.S. Persons who engage in similar transactions with foreign corporations are subject to comparable reporting requirements.[10] Instead of filing Form 8865, corporate taxpayers must file Form 5471, *Information Return of U.S. Persons With Respect To Certain Foreign Corporations*. Sections 6038 and 6046 lay out four categories of filers that must report to the IRS using Form 5471. Forms 5471 and 8865 use the same definition of control and U.S. person and have similar filing exceptions and penalties. While many of the same Code sections apply to both forms, this article will identify important differences between Form 5471 and Form 8865 filing requirements.

III. Category 1 Filers: U.S. Persons Having Control over a Foreign Partnership at Any Time during the Partnership's Taxable Year

Under Section 6038, any U.S. person who had a controlling interest in a foreign partnership at any time during the partnership's taxable year must file Form 8865 as a Category 1 filer. Category 1 filers must provide:

1. A list of all U.S. partners owning at least a 10% interest in the foreign partnership (Schedule A-1);
2. An income statement (Schedule B);
3. The partner's share of capital, profits, losses, etc. (Schedule K or Schedule K-1);
4. A Balance Sheet (Schedule L);
5. A Balance Sheet for the taxpayer's interest allocation (Schedule M);
6. A statement reconciling the income or loss reported on the partnership's books with the income or loss reported on the return (Schedule M-1);
7. An analysis of the partner's capital accounts (Schedule M-2);
8. Transactions between the foreign partnership and the partner (Schedule N); and
9. A gain or loss calculation (Schedule D).[11]

Under Section 6038(a)(1)(B), Form 5471 filers will also need to report undistributed earnings. If any foreign corporation is treated as a controlled foreign corporation, the IRS may require any of the corporation's shareholders to file Form 5471.[12]

Under Section 267(c), a taxpayer indirectly owns an interest in a foreign partnership if the taxpayer has an interest in a corporation, partnership, trust, or estate which has an interest in a foreign partnership; or the taxpayer has a sibling, spouse, ancestor, or lineal descendant who has an interest in the foreign partnership.[13] A taxpayer's interest in a foreign partnership through another entity will be proportionate to his interest in that entity. If a taxpayer is required to file Form 5471, different attribution rules will apply. Section 318 (a)(1) attribution rules should be used to determine whether a particular taxpayer has an interest reportable on Form 5471.

If a taxpayer owns an interest in a foreign partnership indirectly through another entity, his interest is attributable to his family members.[14] However, if a taxpayer indirectly owns an interest in a foreign partnership through a family member, his interest is not attributable to other family members.[15] Also, Taxpayers cannot attribute their interests to entities, trusts, estates, or other partners.[16]

For example, U.S. taxpayer ("UST") purchases a 35% interest in a foreign partnership ("FP"). UST's brother ("USB") has a 15% interest in FP, and UST's sister ("USS") has no interest in FP. UST has a 50% interest in a U.S. corporation ("USC") which has a 40% interest in FP. Under Section 267(c), UST owns a 70% interest in FP (35% directly, 15% indirectly through USB, and 20% indirectly through USC). USB owns 70% of FP (15% directly, and 55% indirectly through UST's personal and corporate interests). USS would own 70% of FP (15% indirectly through USB and 55% indirectly through UST).

A. Exception for Multiple Partners with a Controlling Interest and Partner's with Only an Indirect Interest

In the above scenario, UST, USB, and USS would all be Category 1 filers because they all own a controlling interest in FP. However, the IRS requires only one Category 1 filer to file Form 8865 for the foreign partnership.[17] The taxpayers with an interest in the partnership must decide amongst themselves who will file Form 8865. However, a taxpayer who has a controlling interest in the foreign partnership's losses and deductions can only file Form 8865 if there are no filers with a controlling interest in profits or capital.[18] A Category 1 taxpayer not filing Form 8865 must file a statement with his or her tax return which provides:

1. a statement that the taxpayer is a Category 1 filer but is not filing Form 8865 because another Category 1 filer is filing with respect to the foreign partnership;
2. the name, address, and taxpayer identification number (if any) of the foreign partnership;
3. a statement that the requirement has or will be satisfied;
4. the name and address of the person filing Form 8865;
5. the IRS Center where the designated filer has or will file Form 8865; and
6. any other information that Form 8865 requires.[19]

The IRS does not require Category 1 filers who have no direct interest in the foreign partnership (USS from our example above) to file Form 8865 if they submit a "Controlled Foreign Partnership Reporting" statement along with their income tax returns. The statement must provide:

1. a representation that the taxpayer is a Category 1 filer but is not filing Form 8865 under the constructive ownership exception;
2. the name and address of the U.S. person whose interest the taxpayer constructively owns;
3. the name and address of the foreign partnership; and
4. any other information Form 8865 requires.[20]

B. Penalties on Category 1 Filers for Failing to File Form 8865

The penalty for failing to file a complete or substantially complete Form 8865 is $10,000 for each year the taxpayer does not file.[21] Substantially complete returns are discussed more fully below. If the IRS sends a notice to the taxpayer stating he is delinquent in filing Form 8865 and the taxpayer does not comply within 90 days of the date of such notice, there will be an additional $10,000 penalty for each 30-day period, or portion thereof, in which the form is not filed.[22] This continuation penalty cannot exceed $50,000.[23]

The IRS may also reduce the taxpayer's Foreign Tax Credit by 10% for each taxable year the taxpayer did not file form 8865.[24] If the IRS sends a 90-day notice to a taxpayer stating that he is delinquent in filing Form 8865 and the taxpayer does not comply, the IRS may reduce the taxpayer's Foreign Tax Credit by an additional 5% for every 3-month period the taxpayer is delinquent in filing.[25] This reduction cannot exceed the lesser of $10,000 or the amount of the foreign partnership's income for that taxable year. The failure-to-pay penalties explained above will also reduce foreign tax credit penalties.[26]

IV. Category 2 Filers: U.S. Persons Owning 10% or Greater Interest in a Foreign Partnership while U.S. Persons Owning a 10% or Greater Interest Controlled the Partnership

Under Section 6038, any U.S. person who directly or indirectly owned a 10% or greater interest in a foreign partnership, at any time during the partnership's taxable year, when U.S. persons with a 10% or greater interest controlled the foreign partnership must file Form 8865 as Category 2 filers. Category 2 filers must provide:

1. the partner's share of income, losses, deduction credits, etc. (Schedule K); and
2. transactions between the foreign partnership and the partner (Schedule N).[27]

There can be no Category 2 filers if, at any time during the partnership's taxable year, the partnership had a Category 1 filer.[28] Section 267(c) attribution rules also apply.

Using the example above, assume UST, USB, and USS are all unrelated U.S. persons. UST does not have an interest in USC, and USS has a 10% interest in FP. UST, USB, and USS all have a 10% or greater interest in FP. Together, UST, USB, and USS have a 60% interest in FP. UST, USB, and USS are all Category 2 filers because they each own a 10% or greater interest in FP and together they have a 50% of greater interest in FP.

Now assume UST has a 50% interest in USC. UST, USB, and USS all have a 10% or greater interest in FP and together have a greater than 50% interest in FP. However, UST now has a greater than 50% interest in FP. Therefore, USB and USS are no longer Category 2 filers, and USB is a Category 1 filer.

A. Exception for Partners with Only an Indirect Interest

Just like Category 1 filers, if a Category 2 filer's only interest in a foreign partnership is an indirect interest, he or she should file a Controlled Foreign Partnership reporting statement instead of Form 8865. However, unlike Category 1 filers, all Category 2 filers must file Form 8865 regardless of whether any other Category 2 taxpayer files the form.[29]

B. Penalties on Category 2 Filers for Failing to File Form 8865

Category 1 and 2 filers face the same penalties under Section 6038(b): a $10,000 penalty for each failure to file and an additional $10,000 penalty for each 30-day period the taxpayer fails to comply within 90 days of the IRS mailing a notice of delinquency. Category 2 filers also face a 10% reduction in their Foreign Tax Credit with an additional 5% reduction for each 3-month period if the taxpayer fails to file within 90 days of the IRS mailing a notice of delinquency. These penalties have the same limitations as those imposed on Category 1 filers.

V. Category 3: U.S. Persons Who Contribute Property to a Foreign Partnership in Exchange for an Interest in the Foreign Partnership

Under Section 6038B, any U.S. person who contributes property to a foreign partnership for an interest in the partnership, under Section 721,[30] must file Form 8865 as a Category 3 filer if he or she: 1) owned at least a 10% interest in the foreign partnership after the contribution; or 2) if the fair market value of the contributed property exceeded $100,000 in the 12-month period ending on the date of the transfer.

Category 3 filers must provide:

1. A list of all U.S. partners owning at least a 10% interest in the foreign partnership (Schedule A-1); and
2. A description of the transaction between the U.S. partner and the foreign partnership including the transferred property and its fair market value (Schedule O).[31]

The IRS also requires taxpayers to file Form 8865 if in a 12-month period a taxpayer makes multiple Section 721 property contributions that aggregate to more than $100,000.[32] If a U.S. partnership contributes property to a foreign partnership, the IRS treats the partners of the domestic partnership as contributing property with a fair market value proportionate to their interests in the domestic partnership.[33] Taxpayers receiving an indirect interest, under Section 267(c), because a relative or partnership contributed property to a foreign partnership, are also Category 3 filers. However, some of these taxpayers may use the constructive ownership exception described above.

Using the same example as above, if UST contributes a truck to FP every month for 10 months during UST's taxable year, and the fair market value of each truck is $30,000, then UST is a Category 3 taxpayer because he contributed property to FP that aggregates to more than $100,0000 in a 12-month period.

Assume, however, that USP contributed the trucks instead of UST, and UST has a 20% ownership interest in USP. UST would not be a Category 3 filer because the IRS deems UST to have contributed only $60,000 worth of property to FP (20% of the value of the property USP contributed).

A. Category 3 Filers Must Report Dispositions of Property

If a foreign partnership disposes of the Category 3 filer's property while the filer is still a partner and the property has a built-in gain, the filer must report that disposition on Form 8865.[34] However, if the foreign partnership substitutes the Category 3 filer's property with other property in a non-recognition event and the substituted property has a built-in gain, the Category 3 filer must file Form 8865 only when the foreign partnership disposes of the substituted property.

B. Penalties on Category 3 Filers for Failing to File Form 8865

The IRS penalizes Category 3 filers who fail to file Form 8865 in the amount of 10% of the property's fair market value at the time of the transfer.[35] The IRS does not allow the taxpayer to treat the transfer as a Section 721 exchange and requires the taxpayer to pay capital gains tax on the transfer. Unless the taxpayer's failure to file was due to an intentional disregard for the filing requirement, the IRS will not assess more than $100,000 in penalties. Form 5471 does not have a transaction of interest similar to Category 3.

VI. Category 4 Filers: U.S. persons who acquire a certain interest in, dispose of a certain interest in, or experience a change in proportional interest in a foreign partnership

Under Section 6046A, any U.S. person who holds a 10% direct interest either before or after the acquisition or disposition of an interest in a foreign partnership or who has a 10% or greater change in direct interest in a foreign partnership must file Form 8865 as a Category 4 filer. Category 4 filers must provide a list of the person(s) who acquired, disposed of, or had a change in ownership interest and the percentage acquired, disposed of, or changed (Schedule P).[36] Unlike Category 1, 2, and 3 filers, the attribution rules under Section 267(c) do not apply to Category 4 filers. Section 6046A only concerns direct interest holders.

A Category 4 filer has a reportable transaction under Section 6046A if he or she had less than a 10% interest in a foreign partnership before acquiring more interest and had at least a 10% interest after the acquisition.[37] For example, UST owns a 6% interest in FP. If UST purchases another 5% interest in FP, UST will be a Category 4 filer because the interest in FP is 10% or more after an acquisition.

The taxpayer must also file Form 8865 if the interest increased 10% or more through an acquisition.[38] Using the above example, UST has an 11% interest in FP. If UST purchased another 11% interest, he would be a Category 4 filer because he acquired a 10% or greater interest.

The rules apply inversely when the taxpayer disposes of an interest in a foreign partnership.[39] For example, using the above facts, if UST were to dispose of 10% of interest, he would be a Category 4 filer because a 10% or greater interest in FP was disposed. In this scenario, UST would have an 11% interest in FP. If UST were to dispose of an additional 3% interest, he would be a Category 4 filer because he had an interest greater than 10% which is now lower than 10%.

Finally, if a partner withdraws from the foreign partnership, if a partnership agreement requires that a partner's interest change at a certain date, or if another transaction changes a U.S. partner's interest, such changes would be reportable only if the U.S. person's interest increased or decreased by at least 10%.

For example, UST has a 25% interest in FP, his brother ("USB") has a 25% interest in FP, and his sister ("USS") has a 50% interest in FP. If USS were to withdraw from the partnership, UST and USB would each be Category 4 filers because each of their interests increased by 10% or more (each would own 50% of FP). USS would also be a Category 4 filer, but she would be one because she disposed of an interest in a foreign partnership that was 10% or more.

A. Exception to Filing Form 8865 when Taxpayer is Both a Category 3 and Category 4 Filer

If a taxpayer is both a Category 3 and Category 4 filer, he only needs to file Form 8865 as a Category 3 filer.[40] However, if he fails to file Form 8865 as either a Category 3 or Category 4 filer, he will be subject to both Category 3 and Category 4 penalties.[41] For example, assume UST owned a 15% interest in FP and contributed machinery worth $60,000 in exchange for an additional 10% interest in FP under Section 721. UST would be a Category 4 filer because he acquired a 10% or greater interest in a foreign partnership. However, UST would also be a Category 3 filer because he contributed property in exchange for a 10% or greater interest in a foreign partnership. UST would only file one Form 8865, and he would file as a Category 3 filer.

B. Penalties on Category 4 Filers for Failing to File Form 8865

Section 6679 codifies penalties the IRS imposes on Category 4 filers, which are like penalties the IRS assesses against Category 1 and 2 filers. The IRS imposes a $10,000 penalty for each failure to file Form 8865 and an additional $10,000 penalty for each 30-day period if the taxpayer fails to file within 90 days of the IRS mailing a notice of delinquency. Additions to penalties shall not exceed $50,000. Unlike Category 1 and 2 filers, the IRS will not reduce a Category 4 filer's foreign tax credit for failing to file Form 8865. Taxpayers should note that deficiency procedures codified under Chapter 63 Subchapter B of the IRC do not apply to Category 3 penalties.

We briefly note that Form 5471 has a transaction of interest similar to Category 4, however, its authority is under section 6046 not section 6046A.

VII. Criminal Penalties for Willfully Failing to File Form 8865

Under Section 7203, it is a misdemeanor for any filer, regardless of category, who is required to file Form 8865 to willfully not file Form 8865. Besides the civil penalties previously described, taxpayers who willfully fail to file Form 8865 will face a penalty not exceeding $25,000, up to a year in prison, or both.

VIII. Statute of Limitations and additional Penalties

The IRS has 3 years from the date it deems the return filed to assess penalties on Form 8865, known as the statute of limitations. If a taxpayer files his tax return before its due date, the IRS deems the return filed on the return's due date. The statute of limitations on late-filed returns begins to run on the actual filing date. The statute of limitations will never run out if a taxpayer does not file Form 8865. Thus, unless Form 8865 is filed, the IRS will have unlimited time to assess civil and criminal penalties against a taxpayer for failure to file. In addition, as of March 18, 2010, any item reported on the taxpayer's Form 1040, *U.S. Individual Income Tax Returns*, which relates to Form 8865 will be held open until three years after the Form 8865 is filed.[42]

For example, a taxpayer has a controlling interest in a foreign partnership (Category 1 filer) from 2008 through 2011. He timely filed his 2008 through 2011 Forms 1040 without attaching Form 8865. His 2008 through 2011 tax returns reflect his share of partnership losses. The taxpayer later realized he needs to file Form 8865 and filed all missing forms in 2012. The IRS may audit and assess his share of partnership losses, reported on the 2008 through 2011 Forms 1040, until 2015 because those losses were part of his Form 8865 filing requirement. Also, Section 6662(j) states that any understatement or underpayment of income tax attributable to a foreign asset reportable on Form 8865 is subject to an additional penalty equal to 40% of the understatement or underpayment.

The statute of limitations will not run if an incomplete Form 8865 is filed. The statute of limitations will only run when a substantially complete return is filed.[43] However, neither the Code nor the Treasury Regulations define what substantially complete means. In *Beard v. Commissioner*, 793 F2d. 139 (6th Cir. 1986), the Court created a test for determining whether a return is substantially complete to start the statute of limitations running ("Beard Test"). A return passes the Beard Test and is substantially complete if:

1. the return provides sufficient data to calculate a tax liability;
2. the return purports to be a return;
3. the taxpayer made an honest and reasonable attempt to satisfy the tax law; and
4. the taxpayer signed the return under penalty of perjury.

The IRS will deem any Form 8865 that does not meet all four requirements as incomplete. Incomplete Forms 8865 have the same penalties as listed above.

The IRS generally treats penalties related to the filing of Form 8865 as assessable penalties.[44] This means that the penalties are not subject to deficiency procedures.[45] While penalties on transactions described in Sections 6046 and 6046A have been expressly deemed assessable under section 6679, there is widespread debate on whether penalties on transactions described in sections 6038 and 6038B are assessable. An in-depth analysis of this issue and the ongoing debate is provided in this month's newsletter article entitled *The International Information Reporting Penalties: Is the IRS's failure to embrace a one-stop shopping paradigm inefficient and statutorily deficient?* by Phillip Colasanto, Esq. and Frank Agostino, Esq.

IX. Form 926

Under Treas. Reg. § 1.6038B–2, Category 3 filers who transferred property to foreign partnerships between January 1, 1998, and January 1, 1999, must file Form 926 along with Form 8865. Category 3 filers should modify their Form 926 reporting to reflect a partnership transferee as opposed to a corporation transferee.

X. Form 8865 Audit and Appeals Process

It is important for taxpayers to note that Form 8865 is subject to the same audit selection procedures as individual income tax returns.[46] The IRS collects information through Information Document Requests ("IDR") and Formal Document Requests ("FDR").[47] The IRS first uses IDRs to collect information from taxpayers regarding their interests in foreign partnerships. If a taxpayer fails to provide the requested information, the IRS will use a FDR to obtain information from overseas.[48] The IRS will review the information and then come to a conclusion which may include income adjustments, deduction or credit limitations, or penalty assessments. Although subject to the same audit procedures, international transactions and transfer pricing is the subject of IRS campaigns and the IRS has published training materials instructing examiners to look for Form 8865 non-compliance.[49]

Adjustments to income tax and deductions are typically subject to deficiency procedures. The IRS will send the taxpayer a 30-day letter alerting the taxpayer it has reached a conclusion and there is additional tax owed. The 30-day letter also informs the taxpayer of appeal rights. The 30-day letters are followed by 90-days letters which state that the IRS will enforce its determination unless the taxpayer files a petition in U.S. Tax Court within 90-days.

The IRS generally treats Form 8865 penalties as assessable penalties, meaning it can enforce the penalty determination without first giving the taxpayer the opportunity to appeal its determination. Nonetheless, I.R.M., pt. 20.1.9.2(11) states that audit examiners should inform the taxpayer before assessing penalties.[50] Notice letters allow taxpayers to dispute the IRS determinations by providing information to prove that there was no filing requirement or reasonable cause for not filing exists.

Taxpayers that receive a 30-day letter need not appeal the IRS's ruling before petitioning the United States Tax Court. They may ignore the 30-day letter and wait for the IRS to issue a 90-day letter, or they may request that the IRS issue a 90-day letter. The 90-day letter is the taxpayer's "ticket to Tax Court." However, taxpayers subject to assessable penalties do not receive 30-day or 90-day letters and must get a ruling from the IRS Office of Appeals before they can petition the Tax Court for a redetermination.

Under Sections 6320 and 6330, taxpayers may appeal the IRS's penalty assessment by filing Form 12153, *Request for a Collection Due Process or Equivalent Hearing*, within 30 days of receiving the notice. Section 6330 provides that a taxpayer may challenge the underlying liability in a Collection Due Process ("CDP") hearing if he did not receive a notice of deficiency or was not given an opportunity to appeal the IRS's de-

termination.[51] Taxpayers that disagree with outcome of the CDP hearing, may petition the Tax Court but will only have 30 days to file.[52]

Taxpayers that disagree with the Tax Court's ruling or are unable to appeal a CDP ruling to the Tax Court, may file a refund claim in the U.S. District Court or the Court of Federal Claims. Because these are refund forums, the taxpayer must pay the liability before filing the claim for refund. A claim may be filed within 3 years from the date the return was filed or 2 years from the date the liability was paid, whichever is later.

For a more in-depth look at the IRS audit and appeals process read *Form 5471*, *Information Return of U.S. Persons with Respect To Certain Foreign Corporations*, by Frank Agostino, Esq. and Alec Schwartz, Esq. from the October 2018 Agostino & Associates, P.C. Newsletter.

XI. Taxpayers Who Are Delinquent in Filing Form 8865 Should Take Advantage of a Voluntary Disclosure Program

The IRS has created options for taxpayers who are delinquent in filing Form 8865 and wish to become compliant without facing hefty penalties or criminal charges.

A. The Streamlined Filing Compliance Procedures

Taxpayers who did not willfully fail to file Form 8865 and owe tax on their share of partnership income can become compliant under the Streamlined Filing Compliance Procedures ("SFCP").[54] The SFCP allow taxpayers to file amended or delinquent returns and resolve any tax debt without imposing penalties or criminal liability.

To take advantage of the SFCP, a taxpayer must have a valid Taxpayer Identification Number ("TIN").[55] U.S. Citizens and resident aliens will typically use their Social Security numbers ("SSN") as their TIN. Non-resident aliens and other taxpayers who are not eligible for an SSN may complete Form W-7, *Application for IRS Individual Taxpayer Identification Number* ("ITIN"), to receive a TIN. Taxpayers may submit an application for an ITIN along with their SFCP filing.[56] Taxpayers who are not eligible for an SSN or ITIN cannot take advantage of SFCP.[57] Additionally, taxpayers under civil examination or criminal investigation are ineligible for the SFCP regardless of whether the examination or investigation related to the taxpayer's investment in a foreign partnership.[58]

Under SFCP, taxpayers must submit returns for the previous three tax years along with a statement certifying that their failure to report all income, pay all tax, and submit all required information returns was due to non-willful conduct. The IRS defines non-willful conduct as "conduct that is due to negligence, inadvertence, or mistake or conduct that is the result of a good faith misunderstanding of the requirements of the law."[59]

The IRS treats returns submitted under SFCP the same as any other tax return, which means they have the same audit selection process as any other return. If the IRS determines that the taxpayer's returns are in order, the taxpayer will not be subject to failure to file penalties. If the IRS selects a return for audit, it will not assess penalties unless the taxpayer's failure was willful or the return was fraudulent.[60]

B. Delinquent International Information Return Submission Procedures (DIIRSP)

The requirements for eligibility under the Delinquent International Information Return Submission Procedures ("DIIRSP") are similar to those for the SFCP. Failure to file must not have been willful and the taxpayer cannot be under criminal investigation or civil examination.[61] Taxpayers can take advantage of DIIRSP regardless of whether they have unreported income or not.[62]

Under the DIIRSP, taxpayers must file amended returns and attach their delinquent Forms 8865 along with a reasonable cause statement certifying that the taxpayer's failure to file was non-willful and the foreign partnership was not engaged in tax evasion.[63] Taxpayers must attach a separate reasonable cause statement to each delinquent Form 8865.[64] Similar to SFCP submissions, DIIRSP submission will be subject to

the same processing and audit selection procedures as regular returns.[65]

XII. Conclusion

U.S. citizens who have interests in foreign partnerships need to be aware of Form 8865 filing requirements. Taxpayers looking to come into compliance with their Form 8865 filing obligations should take advantage of SFCP or DIIRSP to reduce possible interest and penalties for failing to file. If the IRS has already notified a taxpayer of his delinquency and has assessed penalties, the taxpayer can request FTA or penalty relief for reasonable cause.

Endnotes:

1. Frank Agostino, Esq. is the principal of, and Joseph A. Stackhouse, Jr. is a law clerk at, Agostino & Associates, P.C. in Hackensack, New Jersey.
2. All references to "Section" numbers are to the Internal Revenue Code of 1986, as amended.
3. IRS, *Abusive Tax Shelters and Transactions*, https://www.irs.gov/businesses/corporations/abusive-tax-shelters-and-transactions (last updated Nov. 7, 2018).
4. Id.
5. IRS, *2017 Instructions for Form 8865*, *available at* https://www.irs.gov/pub/irs-pdf/i8865.pdf [hereinafter *Form 8865 Instructions*].
6. I.R.C. § 7701(a)(30).
7. I.R.C. § 6038.
8. Edward J. Jennings, *Tax, Exemption, and Filing Issues of Alternative Investments*, 18 Tax'n Exempts 67, 72 (2006).
9. Daniel Martinez, *Untangling the Constructive Ownership Rules for Foreign Entity Information Returns,* 117 J. Tax'n 155, 163 (2012).
10. Frank Agostino and Alex Schwartz, *Form 5471*, *Information Return of U.S. Persons with Respect To Certain Foreign Corporations*, discusses the specific filing requirements for Form 5471, as well as its exceptions and penalties.
11. *Form 8865 Instructions*, *supra* note 4.
12. IRC §6038(a)(4).
13. Treas. Reg. § 1.6308-3(b)(4).
14. I.R.C. § 267(c)(5).
15. *Id.*
16. Daniel Martinez, *Untangling the Constructive Ownership Rules for Foreign Entity Information Returns,* 117 J. Tax'n 155, 163 (2012).
16. Treas. Reg. § 1.6038-3(c).
18. *Id.*
19. Treas. Reg. § 1.6038-3(c)(1)(ii)(B).
20. Treas. Reg. § 1.6038-3(c)(2)(ii)(B).
21. I.R.C. § 6038(b)(1).
22. I.R.C. § 6038(b)(2).
23. *Id.*
24. I.R.C. § 6038(c)(1).
25. *Id.*
26. I.R.C. § 6038(c)(3).
27. *Form 8865 Instructions*, *supra* note 4.
28. *Id.*
29. I.R.C. § 6038(a)(5).
30. I.R.C. § 721(a): No gain or loss shall be recognized to a partnership or any of its partners in the case of a contribution of property to the partnership in exchange got an interest in the partnership.
31. *Form 8865 Instructions*, *supra* note 4.
32. Treas. Reg. § 1.6038B-2(a)(1)(ii).
33. Treas. Reg. § 1.6038B-2(a)(2).
34. Treas. Reg. § 1.6038B-2(a)(4)(i).
35. I.R.C. § 6038B(c)(1).

36. *Form 8865 Instructions*, *supra* note 4.
37. Treas. Reg. § 1.6046A-1(b)(1)(i)(A).
38. Treas. Reg. § 1.6046A-1(b)(1)(i)(B).
39. Treas. Reg. § 1.6046A-1(b)(1)(ii)(A)-(B).
40. Treas. Reg. § 1.6046A-1(f)(1).
41. Treas. Reg. § 1.6046A-1(f)(1).
42. Meghan L. Brackney, *Reporting Foreign Partnerships*, Tax Controversy Corner, May 2015, availble at: https://d3n8a8pro7vhmx.cloudfront.net/kflaw/pages/961/attachments/original/1438295012/Reporting_Foreign_Partnerships.pdf?1438295012
43. For more information on the IRS's process for determining whether a return is substantially complete see IRS, *The Meaning of "Substantially Complete" with Reference to International Information Returns*, *available at* https://www.irs.gov/pub/int_practice_units/iga_c_17_03_01_02.pdf (last updated May 31, 2017).
44. See I.R.M. Exhibit 20.1.9-4.
45. Sullivan & Cromwell, LLP, *IRS Allows International Appeals Prior to Payment* (September 13, 2010), available at: https://www.sullcrom.com/siteFiles/Publications/SC_Publication_IRS_Allows_Appeals_of_International_Penalties_Prior_to_Payment.pdf.
46. For more information on the IRS's process for auditing Form 8865 see IRS, *Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty*, *available at* https://www.irs.gov/pub/int_practice_units/FEN9434_01_10R.pdf (last updated Sept. 9, 2015).
47. IRS, *LB&I International Practice Unit, Issuing a Formal Document Request When a US Taxpayer is Unresponsive to an IDR*, *available at* https://www.irs.gov/pub/int_practice_units/IGA9460_02_02.pdf (last updated Aug. 29, 2014).
48. *Id.*
49. IRS, *LB&I International Practice Unit*, *Monetary Penalties for failure to timely file a complete and Accurate Form 8865 – Category 1& 2 Filers*, *available at* https://www.irs.gov/pub/int_practice_units/iga_p_17_4_01.pdf (last updated Jan. 9, 2017).
50. I.R.M., pt. 20.1.9.2 (11) (Nov. 30, 2015).
51. I.R.M., pt. 8.22.8.3(1) (Aug. 8, 2017).
52. I.R.C. § 6330(d)(1).
53. I.R.C. § 6532(a)(1).
54. IRS, *Streamlined Filing Compliance Procedures*, https://www.irs.gov/individuals/international-taxpayers/streamlined-filing-compliance-procedures (last updated June 5, 2018).
55. *Id.*
56. *Id.*
57. *Id.*
58. *Id.*
59. *Id.*
60. *Id.*
61. *Id.*
62. IRS, *Delinquent International Information Return Submission Procedures*, https://www.irs.gov/individuals/international-taxpayers/delinquent-international-information-return-submission-procedures (last updated June 18, 2018) [hereinafter *IDR Procedures*].
63. Kathy Sikora, *Relief from Penalties for Late Filing of Foreign Business Forms,* WithumSmith+Brown, P.C., https://www.withum.com/kc/relief-penalties-late-filing-foreign-business-forms.
64. *IDR Procedures*, *supra* note 60.
65. *Id.*

FIRM NEWS

Upcoming Speaking Engagements:

Frank Agostino, Esq., Michael Wallace, EA, and Caren Zahn, EA will be speaking at the 2018 IRS Representation Conference, held on November 29-30 at Mohegan Sun Casino & Resort, CT.

Valerie Vlasenko, Esq. will be discussing collectability as a litigation tool at the 2018 Low Income Taxpayer Representation Workshop on December 3 in Washington, DC.

Frank Agostino, Esq., Caren Zahn, EA, and Valerie Vlasenko, will be speaking on federal and state Tax Settlement Programs, including the new NJ Tax Amnesty program, NJ Closing Agreements, and the IRS Voluntary Disclosure program. This program will be held on December 4 at Bergen Community College.

Frank Agostino, Esq., Jeffrey Dirmann, Esq., Michael Wallace, EA., and Phillip J. Colasanto, Esq. will be speaking at the upcoming 35th Annual Institute on Criminal Tax Fraud and Eighth Annual National Institute on Tax Controversy, held on December 13-15, at the Encore at Wynn Las Vegas.

If you would like additional information on any of these speaking engagements please see the attached flyers or contact Joann Kozlowski at JKozlowski@AgostinoLaw.com.

UPCOMING UNITED STATES TAX COURT CALENDAR CALLS

All Calendar Calls Are Held at:

Jacob K. Javits Federal Building
26 Federal Plaza
Rooms 206, 208
New York, NY 10278

November 26, 2018

December 17, 2018

SECTION 139F PRO BONO PROJECT

Hello, Friends:

Two years ago at this time, we were working round the clock with Jon Eldan of After Innocence in San Francisco to file refund claims under Section 139F by December 18, 2016. I am really proud of the results achieved to date for our extraordinary, pro bono exoneree clients, and am so grateful for all of the assistance that Keith and his students at Harvard have provided to this effort as well over the past two years. This work has resulted in our doing additional tax-related, pro bono work for exonerees beyond the Section 139F claims. We have worked closely with Jon Eldan and the Innocence Project Network over the past two years as the only group of tax practitioners working to assist Exonerees. It has been incredibly important and significant work for us.

As you all know, the extender bill (which we provided much education on in terms of the normative refund statute) that was passed back in February gave us an additional two years from the original claim filing date. Since that time, Jon and myself and a team of summer associates and volunteer attorneys from Reed Smith have worked to locate almost 300 remaining possible Section 139F refund claimants, including, many military exonerees (these individuals are those left from our search two years ago, where we worked to locate hundreds of other possible Section 139F refund claimants). As a result of working to locate these individuals, preliminary review of each's facts and circumstances, Jon informed me today of 12 potential pro bono refund cases to review and assist with by the deadline of December 17, 2018.

I am writing to ask for your help in either you or your firm assisting us in taking on one or more of these cases.

Many thanks to you all. Happy to answer any questions and I welcome your thoughts about this work and how to best match these potential clients (and possibly, others to be identified in the next week or so) with pro bono counsel.

Best,

Kelley C. Miller
Direct 215.851.8855 – Mobile 215.704.3046 - Fax 215.851.1420
kmiller@reedsmith.com

AGOSTINO & ASSOCIATES, P.C. CONTACT INFORMATION

(201) 488-5400

Frank Agostino, Esq. Fagostino@agostinolaw.com	Ext. 107
Adam Brown, Esq. Abrown@agostinolaw.com	Ext. 125
Phillip Colasanto, Esq. Pcolasanto@agostinolaw.com	Ext. 105
Jeffrey Dirmann, Esq. Jdirmann@agostinolaw.com	Ext. 119
Eugene Kirman, Esq. Ekirman@agostinolaw.com	Ext. 142
Dolores Knuckles, Esq. Dknuckles@agostinolaw.com	Ext. 109
Victor Nazario, Esq. Vnazario@agostinolaw.com	Ext. 123
Alec Schwartz, Esq. Aschwartz@agostinolaw.com	Ext. 118
Malinda Sederquist, Esq. Msederquist@agostinolaw.com	Ext. 130
Christina Sierra, Esq. CSierra@agostinolaw.com	Ext. 120
Caren Zahn, EA Czahn@agostinolaw.com	Ext. 103
Joseph Stackhouse Jstackhouse@agostinolaw.com	Ext. 131
Valerie Vlasenko, Esq. Vvlasenko@agostinolaw.com	Ext. 112
Michael Wallace, EA Mwallace@agostinolaw.com	Ext. 143

TAXPAYERS ASSISTANCE CORPORATION - OF COUNSEL

Desa Lazar, Esq.	Lazar@tac-nj.org

IRS News Release

Internal Revenue Service
Media Relations Office
Washington, D.C.
Media Contact: 202.317.4000
Public Contact: 800.829.1040
www.irs.gov/newsroom

10 | 30 | 2018

Get Ready for Taxes:
Learn how the new tax law affects tax returns next year

IR-2018- 209

WASHINGTON –The Internal Revenue Service today advised taxpayers about steps they can take now to ensure smooth processing of their 2018 tax return and avoid surprises when they file next year.

This is the first in a series of reminders to help taxpayers get ready for the upcoming tax filing season. Additionally, the IRS has recently updated a special page on its website with steps to take now for the 2019 tax filing season.

New IRS Publication 5307 helps individuals understand Tax Cuts and Jobs Act
Major tax reform that affects both individuals and businesses was approved by Congress and signed by the President on Dec. 22, 2017. It's commonly referred to as the Tax Cuts and Jobs Act, or TCJA, or tax reform. Throughout 2018, the IRS has been working closely with partners in the tax return preparation and tax software industries to implement the new law and ensure taxpayers can count on the IRS, tax professionals and tax software programs when it's time to file their returns. Now there is a new publication that will help taxpayers learn how tax reform affects their taxes. IRS Publication 5307, Tax Reform Basics for Individuals and Families, is now available on IRS.gov/getready. While the Tax Cuts and Jobs Act law includes tax changes for individuals and businesses, this publication breaks down what's new for the 2018 federal tax return individual taxpayers will be filing in 2019.

This new publication provides important information about:

- increasing the standard deduction,
- suspending personal exemptions,
- increasing the child tax credit,
- adding a new credit for other dependents and
- limiting or discontinuing certain deductions.

Taxpayers can access Publication 5307 at IRS.gov/getready, along with other important information about steps taxpayers can take now to ensure smooth processing of their 2018 tax return and avoid surprises when they file next year.

Because of the many changes in the tax law, refunds may be different than prior years for some taxpayers. Some may even owe an unexpected tax bill when they file their 2018 tax return next year. To avoid these kind of surprises, taxpayers should perform a Paycheck Checkup to help determine if they need to adjust their withholding or make estimated or additional tax payments now.

Gather documents
The IRS urges all taxpayers to file a complete and accurate tax return by making sure they have all the needed documents before they file their return, including their 2017 tax return. This includes year-end Forms W-2 from employers, Forms 1099 from banks and other payers, and Forms 1095-A from the

Marketplace for those claiming the Premium Tax Credit. Confirm that each employer, bank or other payer has a current mailing address for you. Typically, these forms start arriving by mail in January. Check them over carefully, and if any of the information shown is inaccurate, contact the payer right away for a correction.

To avoid refund delays, taxpayers should avoid using incomplete records and instead wait to file until they have gathered all year-end income documentation. This will minimize the chances they will need to file an amended return later which is extra work for taxpayers and can take up to 16 weeks to process once the IRS receives it.

Taxpayers should keep a copy of any filed tax return and all supporting documents for a minimum of three years. Having your prior year return will make it easier to fill out your 2018 tax return next year. In addition, taxpayers using a software product for the first time may need the Adjusted Gross Income (AGI) amount from their 2017 return to properly e-file their 2018 return. Learn more about verifying identity and electronically signing a return at Validating Your Electronically Filed Tax Return.

For a faster refund, choose e-file
Electronically filing a tax return is the most accurate way to prepare and file. Errors delay refunds and the easiest way to avoid them is to e-file. Using tax preparation software is the best and simplest way to file a complete and accurate tax return. The software guides taxpayers through the process and does all the math. The IRS is working with the tax community to incorporate the tax law changes and form updates. Nearly 90 percent of all returns are electronically filed.

There are several e-file options:

- IRS Free File,
- Volunteer Income Tax Assistance and Tax Counseling for the Elderly programs,
- Commercial tax preparation software, or
- Tax professional.

Use Direct Deposit
Combining Direct Deposit with electronic filing is the fastest way for a taxpayer to get their refund. With Direct Deposit, a refund goes directly into a taxpayer's bank account. There's no reason to worry about a lost, stolen or undeliverable refund check. This is the same electronic transfer system now used to deposit nearly 98 percent of all Social Security and Veterans Affairs benefits. Nearly four out of five federal tax refunds are Direct Deposited.

Direct Deposit also saves taxpayer dollars. It costs the nation's taxpayers more than $1 for every paper refund check issued but only a dime for each Direct Deposit.

Renew expiring ITINs
Some people with an Individual Taxpayer Identification Number (ITIN) may need to renew it before the end of the year. Doing so promptly will avoid a refund delay and possible loss of key tax benefits.

Any ITIN not used on a federal tax return in the past three years will expire on Dec. 31, 2018. Similarly, any ITIN with middle digits 73, 74, 75, 76, 77, 81 or 82 will also expire at the end of the year. Anyone with an expiring ITIN who plans to file a return in 2019 will need to renew it using Form W-7.

Once a completed form is filed, it typically takes about seven weeks to receive an ITIN assignment letter from the IRS. But it can take longer — nine to 11 weeks — if an applicant waits until the peak of the filing season to submit this form or sends it from overseas. Taxpayers should take action now to avoid delays.

Taxpayers who fail to renew an ITIN before filing a tax return next year could face a delayed refund and may be ineligible for certain tax credits. For more information, visit the ITIN information page on IRS.gov.

Refunds held for those claiming EITC or ACTC until mid-February

By law, the IRS cannot issue refunds for people claiming the Earned Income Tax Credit (EITC) or Additional Child Tax Credit (ACTC) before mid-February. The law requires the IRS to hold the entire refund — even the portion not associated with EITC or ACTC. This law change, which took effect at the beginning of 2017, helps ensure that taxpayers receive the refund they're due by giving the IRS more time to detect and prevent fraud.

As always, the IRS cautions taxpayers not to rely on getting a refund by a certain date, especially when making major purchases or paying bills. Be aware that some returns may require additional review for a variety of reasons and may take longer. For example, the IRS, along with its partners in the state's and the nation's tax industry, continue to strengthen security reviews to help protect against identity theft and refund fraud.

-30-

Internal Revenue Service
Media Relations Office
Washington, D.C.
Media Contact: 202.317.4000
Public Contact: 800.829.1040
www.irs.gov/newsroom

Newly revised publication helps taxpayers understand changes to backup withholding

IRS Tax Reform Tax Tip 2018-168
October 30, 2018

The IRS urges taxpayers who make payments or receive payments to check out Publication 1281, Backup Withholding for Missing and Incorrect Name/TIN(s). The newly revised publication helps taxpayers understand how tax reform affects backup withholding. Backup withholding can apply to most kinds of payments reported on Form 1099.

Last year's Tax Cuts and Jobs Act dropped the backup withholding tax rate from 28 percent to 24 percent. This affects taxpayers who make and receive payments. Taxpayers who make payments are known as "payers," while those who receive payments are known as "payees."

Backup withholding can apply to payments such as:

- Interest payments
- Dividends
- Patronage dividends, but only if at least half of the payment is in money
- Rents, profits or other income
- Commissions, fees or other payments for work performed as an independent contractor
- Payments by brokers and barter exchange transactions
- Certain portions of payments by fishing boat operators
- Payment card and third-party network transactions
- Royalty payments
- Gambling winnings that aren't subject to regular gambling withholding
- Taxable grants and agriculture payments

Here are some situations when a payee may be subject to backup withholding. They:

- Fail to give a taxpayer identification number to the payer
- Give an incorrect TIN
- Supply a TIN in an improper manner
- Underreport interest or dividends on their income tax return
- Fail to certify that they're not subject to backup withholding for underreporting of interest and dividends

To stop backup withholding, the payee must correct any issues that caused it. They may need to give the correct TIN to the payer, resolve the underreported income and pay the amount owed, or file a missing return.

A TIN can be a:

- Social Security number
- Employer identification number
- Individual taxpayer identification number
- Adoption taxpayer identification number

The newly revised Publication 1281 is packed with useful information. It will help any payer who is required to impose backup withholding on any of their payees.

More information:
The Backup Withholding page
Publication 505, Tax Withholding and Estimated Tax
Publication 1335, Backup Withholding Questions and Answers
Form 945, Annual Return of Withheld Federal Income Tax
Publication 15, Employer's Tax Guide

Subscribe to IRS Tax Tips

Internal Revenue Service
Media Relations Office
Washington, D.C.
Media Contact: 202.317.4000
Public Contact: 800.829.1040
www.irs.gov/newsroom

Here's how tax reform affects farmers and ranchers

IRS Tax Reform Tax Tip 2018-169
October 31, 2018

Many farmers and ranchers will benefit from tax law changes brought about by last year's Tax Cuts and Jobs Act. Here are some of those changes along with details about how they will affect farmers and their bottom line:

Net Operating Losses:

- These can now be carried forward indefinitely. Under prior law, they could only be carried forward 20 years.
- NOL deductions are limited to 80 percent of taxable income.
- They can be carried back for two years for farm and ranch businesses. Under prior law, NOLs could be carried back five years.

Qualified Business Income Deduction:

- For tax years beginning after Dec. 31, 2017, taxpayers other than corporations may be entitled to a deduction of up to 20 percent of their qualified business income from a qualified trade or business, including income from a passthrough entity, but not from a C corporation, plus 20 percent of qualified real estate investment trust dividends and qualified publicly traded partnership income.
- The deduction is subject to multiple limitations such as the type of trade or business, the taxpayer's taxable income, the amount of W-2 wages paid with respect to the trade or business, and the unadjusted basis immediately after acquisition of qualified property held by the trade or business.
- The deduction can be taken in addition to the standard or itemized deductions. In some cases, patrons of horticultural or agricultural cooperatives may be required to reduce their deduction. The IRS will be issuing separate guidance for co-ops.

Accounting method changes:

- Under the new law, more farm corporations and partnerships can now use the cash basis of accounting for tax purposes. This includes small business taxpayers, such as:
    - Farmers and ranchers with average annual gross receipts of $25 million or less in the prior three-year period.
- Farmers can refer to IRS guidance for more information about the process that eligible small business taxpayers may use to change accounting methods.

Subscribe to IRS Tax Tips

Internal Revenue Service
Media Relations Office
Washington, D.C.
Media Contact: 202.317.4000
Public Contact: 800.829.1040
www.irs.gov/newsroom

Tax reform changes to depreciation deduction affect farmers' bottom line

IRS Tax Reform Tax Tip 2018-170
November 1, 2018

Last year's Tax Cuts and Jobs Act made changes to how farmers and ranchers depreciate their farming business property.

Depreciation is an annual income tax deduction. It allows a taxpayer to recover the cost or other basis of certain property over the time that they use it. When figuring depreciation, taxpayers consider wear and tear, and deterioration of the property, as well as whether it's now obsolete.

Here is information about how the tax law changes to depreciation affect farmers and their bottom line:

- New farming equipment and machinery is five-year property. This means that for property placed in service after Dec. 31, 2017, the recovery period is shortened from seven to five years for machinery and equipment.
- The shorter recovery period does not apply to grain bins, cotton ginning equipment, fences and other land improvements.
- Used equipment remains seven-year property.
- Property used in a farming business and placed in service after Dec. 31, 2017, is not required to use the 150-percent declining balance method. Farmers and ranchers must continue to use the 150-percent declining balance method for property that is 15 or 20 years old to which the straight-line method does not apply and for property that the taxpayer elects.
- New and certain used equipment acquired and placed in service after September 27, 2017, qualifies for 100 percent first-year bonus depreciation for the tax year in which the property is placed in service.
- A taxpayer may elect to expense the cost of any section 179 property and deduct it in the year the property is placed in service. The new law increased the maximum deduction from $500,000 to $1 million. It also increased the phase-out threshold from $2 million to $2.5 million. For taxable years beginning after 2018, these amounts of $1 million and $2.5 million will be adjusted for inflation.
- The new law increases the bonus depreciation percentage from 50 percent to 100 percent for qualified property acquired and placed in service after Sept. 27, 2017. The bonus depreciation percentage for qualified property that a taxpayer acquired and placed in service before Sept. 28, 2017 remains at 50 percent. Special rules apply for longer production period property and certain aircraft.
- The definition of property eligible for 100 percent bonus depreciation was expanded to include used qualified property acquired and placed in service after Sept. 27, 2017, if several factors are met.
- Farming businesses that elect out of the interest deduction limit must use the alternative depreciation system to depreciate any property with a recovery period of 10 years or more. This is property such as single purpose agricultural or horticultural structures, trees or vines bearing fruit or nuts, farm buildings and certain land improvements. This provision applies starting in tax year 2018.

Subscribe to IRS Tax Tips

NYCLA - U.S. Tax Court Calendar Call Pro Bono Program

Calendars through December 2018

Date	Presiding Judge	RSVP to Volunteer/Observe
November 26, 2018	The Honorable Michael B. Thornton	https://www.eventbrite.com/e/us-tax-court-calendar-nyc-november-26-2018-judge-michael-b-thornton-tickets-48042215560
December 17, 2018	The Honorable Lewis R. Carluzzo	https://www.eventbrite.com/e/us-tax-court-calendar-nyc-december-17-2018-judge-lewis-r-carluzzo-tickets-48042276743

The U.S. Tax Court Calendar Call Pro Bono Program provides counseling to self-represented taxpayers seeking advice in tax law at calendar call sessions of the U.S. Tax Court conducted in New York. Self-represented taxpayers are advised by volunteers while appearing pro se before the U.S. Tax Court.

Volunteers may be asked to consult with pro se petitioners regarding the merits of their cases and evaluate any settlement proposals from the Internal Revenue Service, act as a communicator or mediator between the parties to assist in resolving the case and provide procedural advice to pro se petitioners who proceed to trial. Individuals thinking of volunteering for the program and volunteers who are new to the program who would like to observe the calendar call session and client counseling are encouraged to attend.

For those of you interested in volunteering in the Tax Court, PLEASE feel free to attend the calendar, observe and give moral support to the volunteers and unrepresented taxpayers. Volunteers should arrive at the court (Rooms 206/208, Jacob B. Javits Federal Building, 26 Federal Plaza) and check in with NYCLA no later than 9:30 AM. Please allow sufficient time to clear the building's security screening.

TAXPAYERS ASSISTANCE CENTER

AGOSTINO & ASSOCIATES
COUNSELLORS AT LAW

TAXPAYERS ASSISTANCE CORPORATION

Tax Settlement Programs - NJ Tax Amnesty, NJ Closing Agreements, IRS Voluntary Disclosures and Offers-in-Compromise

Three (3) Free NY & NJ CLE*, CPE†, and EA CE Credits

Tax Professionals that attend the seminar are encouraged to accept a pro bono tax controversy case assignment from NYCLA, an ABA-sponsored Tax Court Pro Bono program or a NY or NJ Low-Income Tax Clinic

WHEN	WHERE
Tuesday, December 4, 2018 Registration/Pizza @ 5:30 PM **Seminar: 6:00 PM – 9:00 PM**	**Bergen Community College** **Ciarco Learning Center** 355 Main Street Room 102/103 Hackensack, NJ 07601

Learning Objective

This class will review procedures for resolving tax disputes without litigation

Procedures for New Jersey Tax Amnesty **NJ Form 906 - Closing Agreements** **NJ Voluntary Disclosures**	**New IRS Guidelines for All Voluntary Disclosures** **IRS Offers in Compromise - Forms 656**

Tilesha McCall & Christina Quinones from the New Jersey Division of Taxation will be available to answer your questions

Moderators and Panel, may also include

Frank Agostino	**Phil Colasanto**	**Jeffrey Dirmann**	**Malinda Sederquist**	**Valerie Vlasenko**

RSVP @ http://conta.cc/2jdF4oM	Questions: Contact Alec Schwartz @ **ASCHWARTZ@AGOSTINOLAW.COM**	CE IRS-APPROVED CONTINUING EDUCATION PROVIDER

This seminar is available via Live Stream - there are no continuing education credits offered for the live stream.

---

* This program has been approved by the Board on Continuing Legal Education of the Supreme Court of New Jersey for 3 hours of total CLE credit. Of these, 0 qualify as hours of credit for ethics/professionalism, and 0 qualify as hours of credit toward certification in civil trial law, criminal trial law, workers compensation law and/or matrimonial law. This course or program has been approved in accordance with the requirements of the New York State Continuing Legal Education Board for a maximum of 3 credit hours.

† Based upon our interpretation of the regulations by the New York and New Jersey State Boards of Accountancy, this event will qualify for CPE credit. Our New Jersey CPE Sponsorship number is 20CE00213700. Our New York CPE Sponsorship number is 002405. Our Office of Professional Responsibility Sponsor Number is QVGWD.

Representing the Innocent &/or Injured Spouse Demonstrating Abuse under Sections 61, 6013 and 6015

Two (2) Free NY, NJ, & NV CLE*, NY & NJ CPE†, and EA CE Credits

Thursday, December 13, 2018 **Registration & Sign-In @ 12:00 NOON** **Seminar from: 12:15 PM to 2:15 PM**	**Encore at Wynn Las Vegas** **3131 Las Vegas Blvd S** **Las Vegas, NV 89109-1967**	RSVP @ https://conta.cc/2E76avl Please contact Jeff Dirmann at Jdirmann@AgostinoLaw.com with questions

The goal of this training is to review best practices for proving emotional and physical abuse for purposes of determining whether:

- **a spouse voluntarily signed a joint return for purposes of IRC § 6013,**
- **a spouse should be relieved from joint and several liability under IRC § 6015,**
- **a spouse should be considered a victim, nominee or conduit for any other section of the Code, and**
- **the role of mental health professionals in tax controversies.**

This outreach is part of the *ABA's 35th National Institute on Criminal Tax Fraud and Eighth Annual National Institute on Tax Controversy*. There is no charge to attend the pro bono outreach. Attendees are encouraged to volunteer to represent a pro bono taxpayer in connection with the ABA's U.S. Tax Court Calendar Call Pro Bono Program or an Low-Income Tax Clinic. For more information about the ABA Criminal Tax Fraud institute:

https://shop.americanbar.org/ebus/ABAEventsCalendar/EventDetails.aspx?productId=334691944

Panelists, Include

Frank Agostino, Esq	**Jennifer Breen, Esq**	**Jeffrey Dirmann, Esq.**	
Janice R. Feldman, Esq	**Francine Lipman, Esq**	**Michael Wallace, EA**	**Lipika Wadhwa, Psy.D**

IRS-APPROVED CONTINUING EDUCATION PROVIDER

Las Vegas Outreach Partners include

Asian American Advocacy Clinic
Asian Bar Association of Las Vegas
DreamBig Nevada
Las Vegas Filipino Veterans Group
Las Vegas Latino Bar Association
Make the Road Nevada
Nevada Bar Association Tax Section
Nevada Legal Services
The Rosenblum Family Foundation Tax Clinic

Have a tax problem you haven't been able to resolve with the IRS? The Taxpayer Advocate Service will assist taxpayers in person at its upcoming

Problem Solving Day

Questions about IRS Problem Solving
https://conta.cc/2EGiJOM

---

* This program has been approved by the Board on Continuing Legal Education of the Supreme Court of New Jersey for 2 hours of total CLE credit. Of these, 0 qualify as hours of credit for ethics/professionalism, and 0 qualify as hours of credit toward certification in civil trial law, criminal trial law, workers compensation law and/or matrimonial law. This course or program has been approved in accordance with the requirements of the New York State Continuing Legal Education Board for a maximum of 2 credit hours.

† Based upon our interpretation of the regulations by the New York and New Jersey State Boards of Accountancy, this event will qualify for CPE credit. Our New Jersey CPE Sponsorship number is 20CE00213700. Our New York CPE Sponsorship number is 002405. Our Office of Professional Responsibility Sponsor Number is 772.

Jeremy Oswald

Local Taxpayer Advocate, Las Vegas invites you to a

Problem Solving Day

TAXPAYER ADVOCATE SERVICE

YOUR VOICE AT THE IRS

Have a tax problem you haven't been able to resolve with the IRS? The **Taxpayer Advocate Service** will assist taxpayers in person at its upcoming

Problem Solving Day

TAXPAYER ADVOCATE SERVICE
YOUR VOICE AT THE IRS

Las Vegas Outreach Partners include
Asian American Advocacy Clinic
Asian Bar Association of Las Vegas
DreamBig Nevada
Las Vegas Filipino Veterans Group
Las Vegas Latino Bar Association
Make the Road Nevada
Nevada Bar Association Tax Section
Nevada Legal Services
The Rosenblum Family Foundation Tax Clinic @ UNLV

Jeremy Oswald, the Local Taxpayer Advocate, Las Vegas and the Taxpayer Advocate Service (TAS) will be available to help tax professionals with their unresolved IRS tax problems. TAS will provide one-to-one guidance, direction on next steps, and case building ideas. If a tax professional's client's problem meets the TAS criteria, TAS will assign a Case Advocate to work with the tax professional to resolve the taxpayer's issue.

Tax Professionals looking to take advantage of Problem Solving Day, please bring an executed IRS Form 2848 "Power of Attorney and Declaration of Representative."

December 13 & 14, 2018

Registration & Sign-In @ 9:00 AM
Problem Solving from: 9:00 AM to 3:00 PM

Encore at Wynn Las Vegas

3131 Las Vegas Blvd S
Las Vegas, NV 89109-1967

This outreach is part of the *ABA's 35th National Institute on Criminal Tax Fraud and Eighth Annual National Institute on Tax Controversy*. For more information about the Criminal Tax Fraud institute:

https://shop.americanbar.org/ebus/ABAEventsCalendar/EventDetails.aspx?productId=334691944

For Questions About the Pro Bono Training:

Representing the Innocent Spouse: Demonstrating Mental Abuse under Sections 61, 6013 and 6015

RSVP @ https://conta.cc/2E76avl. Please contact Jeff Dirmann at Jdirmann@AgostinoLaw.com with questions

TAXPAYERS ASSISTANCE CENTER

AGOSTINO & ASSOCIATES COUNSELLORS AT LAW

TAXPAYERS ASSISTANCE CORPORATION

2019 TAX CONTROVERSY SEMINAR SERIES

Bergen Community College, Ciarco Learning Center, 355 Main Street, Room 102/103, Hackensack, NJ

Three Free NY & NJ CLE[1], CPE[2], and EA CE Credits per Class

This series is free. However, A&A asks that each attendee volunteer for 3 hours of pro bono service per class.

Date & Time	*Topic*	*RSVP*
January 8, 2019 6:00 PM - 9:00 PM	The IRS Examination, Responding to Document Requests, Interview Requests, Summonses and Third Party Contacts	https://conta.cc/2RpI6Xb
February 12, 2019 6:00 PM - 9:00 PM	International Tax Controversies, Including the LB&I Campaigns and Offshore Voluntary Disclosure	https://conta.cc/2RkBjhl
May 7, 2019 6:00 PM - 9:00 PM	Employment Tax Controversies, Including Worker Classification and Trust Fund Recovery Penalty	https://conta.cc/2RkwVPn
June 11, 2019 6:00 PM - 9:00 PM	IRS Collection, IRS Collection Alternatives and Collection Due Process	https://conta.cc/2RmkYsy
July 9, 2019 6:00 PM - 9:00 PM	Valuation, the Role of Forensic Analysis and/or Expert Witnesses	https://conta.cc/2KEJP8l
August 13, 2019 6:00 PM - 9:00 PM	The IRS Office of Appeals	https://conta.cc/2RjSY8J
September 10, 2019 6:00 PM - 9:00 PM	Civil and Criminal Tax Penalties	https://conta.cc/2Rm9nte
October 8, 2019 6:00 PM - 9:00 PM	Representing the Innocent Spouse and/or Injured Spouse	https://conta.cc/2RkWY94
November 12, 2019 6:00 PM - 9:00 PM	Tax Consequences of the Choice of Entity	https://conta.cc/2Rm9J32
December 10, 2019 6:00 PM - 9:00 PM	Representing the Whistleblower and Preparing the Reward Application	https://agostinoandassociates-representingthewhistleblower.eventbrite.com

[1] This program has been approved by the Board on Continuing Legal Education of the Supreme Court of New Jersey for 3 hours of total CLE credit. Of these, 0 qualify as hours of credit for ethics/professionalism, and 0 qualify as hours of credit toward certification in civil trial law, criminal trial law, workers compensation law and/or matrimonial law. This course or program has been approved in accordance with the requirements of the New York State Continuing Legal Education Board for a maximum of 3 credit hours.

[2] Based upon our interpretation of the regulations by the New York and New Jersey State Boards of Accountancy, this event will qualify for CPE credit. Our New Jersey CPE Sponsorship number is 20CE00213700. Our New York CPE Sponsorship number is 002405. Our Office of Professional Responsibility Sponsor Number is QVGWD. ‡CFP CE Credit will be provided.