LAW OFFICES OF
DANIEL N. PRICE, PLLC

July 3, 2023

Electronically submitted via www.regulations.gov

Internal Revenue Service
Room 5203
P.O. Box 7604
Ben Franklin Station
Washington, DC 20044

Re: Proposed Regulations under I.R.C. § 6751
REG-121709-19

Dear Sir or Madam:

We appreciate the opportunity to comment on the proposed regulations under I.R.C. § 6751. We have not been engaged by a client to make this submission. Rather, we make this submission out of concern for taxpayer rights. These comments focus on one aspect of the proposed regulations, the proposed definition of "immediate supervisor."

In the "Explanation of Provisions" published with the proposed regulations, the government acknowledges that the 1998 Senate Finance Committee Report intended for "immediate supervisor" to mean "IRS management." The proposed regulations define "immediate supervisor" in a manner inconsistent with Congressional intent and so broadly that nearly any IRS employee could be considered an immediate supervisor for penalty approval purposes.

We first address the proposed definition of "immediate supervisor." Second, we address the unique circumstances of penalty approval in IRS submission processing centers or campuses. Third, we propose specific changes to the proposed regulations to adjust the proposed regulations to align with Congressional intent. Fourth, we provide an additional suggestion related to these topics.

Proposed Definition of "Immediate Supervisor"

The proposed regulations define "immediate supervisor" as follows:

> The term immediate supervisor means any individual with responsibility to approve another individual's proposal of penalties, as defined in paragraph (a)(3)(i) of this section, without the proposal being subject to an intermediary's approval.

Phone: 210-960-2920 dan@pricetaxlaw.com Fax: 210-714-7646

As drafted, the proposed regulations define "immediate supervisor" too broadly and would allow non-managerial, non-supervisory personnel to approve penalties. The proposed definition encompasses any IRS employee reviewing a penalty approval regardless of supervisory or managerial status. Arguably, the proposed definition deviates so substantially from the statute that if implemented in final regulations, the proposed definition will be subject to judicial challenge. The proposed definition converts the statutory requirement of "supervisory approval" to "any IRS worker approval."

Penalties Assessed by Examination Personnel v. Campus Personnel

The proposed regulations appear to be drafted from the perspective of examinations and penalties arising from examinations. Exam personnel, typically revenue agents, generally determine penalties during the course of gathering facts from interaction with taxpayers or taxpayer representatives. The examination process generally culminates in a revenue agent proposing specific penalties, including alternative penalties, on a penalty approval lead sheet (Lead Sheet 300). Then, the revenue agent forwards the penalty approval lead sheet to his/her manager for approval. Both revenue agents and supervisory revenue agents are generally higher-graded government personnel on the GS scale. The proposed regulation's definition of "immediate supervisor" makes sense in the context of an examination by a revenue agent. But contrast penalties determined as a result of an examination with penalties assessed in a campus environment.

IRS submission processing centers, or campuses, are designed to handle huge volumes of paper submissions. Most campus workers are loyal and hard working federal employees, but most campus workers perform mechanical tasks quickly and repetitively. Campuses are designed for speed and volume. Many IRS workers at campuses hold positions on the GS scale much lower than revenue agents and are given task-specific training with little latitude in handling their assignments.

Yet, campus personnel are responsible for assessing various international information return penalties. IRS campus personnel routinely make systemic penalty assessments for perceived foot-faults and perceived tardiness involving Forms 3520 and 3520-A. Those campus personnel routinely make penalty determinations of millions of dollars for perceived late-filed or substantially incomplete Forms 3520 and 3520-A.

Especially in the context of penalty determinations that routinely involve significant sums, written supervisory approval of such penalties becomes crucial. An IRS manager or supervisor must approve in writing those penalty determinations. An approving manager or supervisor must be more than a fellow IRS worker approving the initial penalty determination by another IRS worker. As drafted, the proposed regulations

would classify a bargaining unit[1] reviewing worker as an "immediate supervisor." That does not accord with Congressional intent and runs contrary to the text of § 6751(b)(1) requiring written supervisory approval of penalties.

Specific Changes to the Proposed Definition of Immediate Supervisor

We recommend that the final regulations define "immediate supervisor" as follows:

> The term immediate supervisor means the manager or supervisor (including an acting manager or supervisor with a valid written delegation of authority) who directly supervises the work of the individual who proposes penalties. In general, one who directly supervises work is responsible for preparing performance evaluations and addressing any personnel issues of a subordinate. For purposes of this section, an IRS manager or supervisor must hold a "non bargaining unit" position in the IRS or a have a valid written delegation of authority as an acting manager or supervisor.

We believe the suggested language in this letter better fits Congressional intent underlying § 6571(b)(1).

Additional Suggestions

Beyond the suggested language for the definition of "immediate supervisor," we also recommend additional procedural safeguards be implemented in either the final regulations or the IRM.

1. Based on our review of various cases involving systemic penalty assessments by IRS campus personnel, it does not appear that IRS campus personnel currently use an established IRS form or lead sheet to document supervisory approval of penalties. At least the IRS has never produced any in response to FOIA requests. We recommend that IRS campus operations adopt the use of IRS Lead Sheet 300 for documenting penalty assertion and supervisory approval. This will promote compliance with I.R.C. § 6751(b)(1) and more uniformity across IRS operations.

[1] In the unionized environment of the IRS, employees are designated as "bargaining unit" ("BU") or "non-bargaining unit" ("NBU"). See generally 2019 National Agreement – Internal Revenue Service and National Treasury Employees Union, page 3. https://www.irs.gov/pub/irs-utl/2019_national_agreement_irs_nteu.pdf BU personnel are covered by the NTEU-IRS contract, whereas NBU personnel are not. One key distinction between BU and NBU is that managers, supervisors, executives and a few other positions are all classified as NBU.

2. Based on our review of various cases involving systemic penalty assessments by IRS campus personnel, it is practically impossible to identify by name IRS campus personnel involved in proposing and approving penalty assessments. The IRS uses, among other systems, the Correspondence Imaging System (CIS) to record key data points for campus penalty assessments and attempting to comply with I.R.C. § 6751(b)(1). For example, CIS generally includes key dates relating to campus penalty assessments, extremely brief notes, and employee numbers. But the employee numbers in CIS are not the same as employee badge numbers or employee numbers in the IRS business directory known as the "Discovery Directory." The employee numbers used in the CIS system make it impossible to link specific IRS workers with penalty proposals and written supervisory approval of penalties. We recommend that the IRS modify CIS to include the employee names for penalty proposals and supervisory approval of penalties. We have included a redacted sample of a CIS record for reference. This sample relates to a penalty imposed for the late filing of a Form 3520. Eventually, the penalty was fully conceded by the Independent Office of Appeals on the basis of reasonable cause.

3. For campus assessments of Form 3520 and Form 3520-A penalties exceeding $250,000, we recommend requiring approval by a supervisor or manager with a grade of IR-13/GS-13 or higher. Review of substantial proposed penalties relating to Forms 3520 and 3520-A by higher graded IRS employees might eliminate penalties imposed for timely filing where IRS workers misconstrue timeliness. Review by a higher graded IRS supervisor may also contribute to the IRS considering reasonable cause statements prior to assessment. See generally, Andrew Velarde, "Commentators Line Up to Critique Foreign Trust Penalty Operation," TAX NOTES, March 6, 2023. We have included a copy of the article for your reference. We encourage you to read the various public comments the article references to understand the dysfunction of campus based systemic penalties and background for this proposal.

4. We recommend increasing transparency about how IRS campuses are (or are not) complying with the requirement under I.R.C. § 6751(b)(1) to secure written supervisory approval of penalties before assessment.

We appreciate the hard work by personnel in Treasury, the Office of Chief Counsel, and the IRS.

Sincerely,

Daniel N. Price
Managing Member
Law Offices of Daniel N. Price, PLLC

Enclosures:

1. Redacted sample CIS record
2. Andrew Velarde, "Commentators Line Up to Critique Foreign Trust Penalty Operation," TAX NOTES, March 6, 2023

CC: David Bergman to david.j.bergman@irscounsel.treas.gov

Welcome to the Correspondence Imaging System. If you are utilizing assistive technologies, click the following link to skip repetitive navigation links at the top of each page. Skip Navigation

Correspondence Imaging System Help Logoff

Case Notes

Case Assigned To: 0433972885
Case ID: [redacted]

Case Notes

Return to Case

Note Description	Employee	Date
Case closed	0433972885	2021/02/25
Approved to assess F3520[redacted] civil penalty per IRM 21.8.2.19.2, ME, Manager	0433084679	2021/02/11
3520 penalty per IRM 21.8.2.19.2 659 for[redacted]	0433972885	2021/02/09
Case marked as statute searched	0433972885	2021/02/09
2MGR command executed by user.	0433972885	2021/02/09
Case Assigned from 0436000005 to 0433972885	0433548082	2021/02/05
Case Assigned	SYSTEM	2019/12/27

-1:vp2smemjbaams04:cii-ui-app04-1:03.17.2022 09:35:35.0093

03/17/2022

Commentators Line Up to Critique Foreign Trust Penalty Operation

Posted on Mar. 6, 2023

By Andrew Velarde

After requesting comments on foreign trust and gift reporting forms, the IRS received significant input from practitioners, with many comments going beyond recommendations on form changes and challenging the agency's implementation of related penalties.

In December 2022 the IRS asked the taxpayer community for feedback on forms 3520, "Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts," and 3520-A, "Annual Information Return of Foreign Trust With a U.S. Owner." The previous Office of Management and Budget recertification of the forms expired on February 28. Although there is disagreement over the exact number of taxpayers that must file the forms, it is substantial. The IRS previously estimated the annual time burden spent by taxpayers on the forms at 95,000 hours.

Several of the commentators were critical of the IRS's estimates of the number of annual responses for forms 3520 and 3520-A. The agency pegs it at 1,820, but both Daniel Price, a former IRS official, and the American Institute of CPAs suspect that to be well short of the true number, with Price labeling it "grossly understated." Historical data show that more than 27,000 Forms 3520 were filed in 2012, and Price surmises that the lower estimate is a "clerical holdover" from a previous OMB recertification. Given that awareness of the forms has grown considerably over the last decade, Price estimates that the true number of annual filers is closer to 60,000.

Price, now with the Law Offices of Daniel N. Price PLLC, told *Tax Notes* that the OMB recertification process is usually quite mechanical, with the last write-up from three years prior becoming the template for the new submission.

"It appears that the IRS, instead of securing current data, is just relying on what was done in the last round, which was outdated, which was based on the prior submission, which was outdated," Price said. "It's critical for the IRS to submit to OMB accurate data based on actual filings instead of just using your last submission as a go-by."

For several years, practitioners have decried how the IRS handles penalties and relief related to Forms 3520 and 3520-A, particularly its systemic and summary assessment of international information reporting penalties. It had long been suspected that the IRS was not reading reasonable cause statements that would excuse some of those penalties, and Price confirmed those suspicions last year. Some have argued that training materials from the IRS Independent Office of Appeals indicate that the agency may be misapplying case law to avoid reasonable cause relief and assert that hazards of litigation do not exist for cases involving penalties related to forms 3520 and 3520-A.

Penalties connected to filing failures on the forms can be high. Failure to file Form 3520 carries a penalty equal to the greater of 35 percent of the gross reportable amount or $10,000 and is also subject to $10,000 in continuation penalties. For Form 3520-A, the U.S. owner is subject to penalties of the greater of $10,000 or 5 percent of the gross value of the trust's assets they own. Additional continuation penalties also apply.

Out-of-Scope Consideration

Commentators reinforced hammered home some of the previous criticism of penalty operations. In their separate comments, Price, the AICPA, and the Florida Bar Tax Section are bluntly critical of the IRS's policy and communication on the systemic assessments of the penalties.

"The IRS' silence and lack of transparency on its practice of assessing systemic penalties at maximum rates all the while advertising the Delinquent International Information Return Procedures does not reflect the IRS' commitment to transparency," the AICPA letter states.

Echoing an argument Price previously made, the Texas Society of CPAs asserts that the systemic assessment of the penalties, which are not automatic penalties, is subject to section 6751(b)(1), which requires the initial penalty assessment to be approved by a supervisor. The IRS's penalty practice may thus not be following the law be unlawful, it says.

Price told *Tax Notes* that comments that don't relate directly to the forms themselves or their burdens but to IRS penalty operations could be considered out of scope. Out-of-scope comments on forms aren't unheard of, Price said, noting that the IRS received them on Form 14457 for voluntary disclosure and for streamlined filing forms. They aren't necessarily doomed to the waste bin.

"During my tenure at chief counsel, even out-of-scope comments were considered internally and given thoughtful consideration. . . . A lot of it depends on who is the technical owner of the form," Price said, referring to the IRS divisions.

Price noted that the forms are processed in the IRS campus environment, which is typically the jurisdiction of the Wage and Investment Division or the Small Business/Self-Employed Division. He said those business operation units would be lessinterested in the out-of-scope comments, but that they could ask for advice from branch 1 of the associate chief counsel international, which hasthe technical subject matter jurisdiction over the law governing the forms.

Do the Right Thing

The AICPA recommends that the IRS allow e-filing of forms 3520 and 3520-A, which could lessen the number of incorrectly assessed penalties.

Price told *Tax Notes* he agrees.

"The fact that the IRS is still forcing practitioners and taxpayers to paper-file these submissions to Ogden [Utah] is increasing [taxpayer] burden. . . . E-filing is the solution that will improve efficiencies

across the board," Price argued, adding that e-filing could also assist the IRS in reading reasonable cause statements by speeding up retrieval and access to them.

Price's comments to the IRS argue that systemic assessment without consideration of reasonable cause is contrary to IRS penalty policy, as it requires taxpayers to use professionals when penalty disputes wind up at the IRS Independent Office of Appeals.

Treasury regulations require taxpayers to exercise ordinary business care and prudence to claim reasonable cause for their failure, in order for them to be excused from penalties.

Price emphasized to *Tax Notes* the high cost of representation that taxpayers facing systemic penalties incur.

"That seems to be a factor the IRS puts blinders on and just doesn't acknowledge," Price said. "There may be textbook reasonable cause, but the amount of time and effort it takes to get a case into Appeals and then resolved is tremendous. That's a huge economic burden on taxpayers that are trying to do the right thing."

The Texas Society of CPAs said the IRS's review of reasonable cause statements needs to be "substantially revised." It arguedthat by assessing penalties before the reasonable cause exceptions are reviewed, the IRS's practice contradicts the statutory language of sections 6677 and 6039F. Those sections state that no penalty will be imposed or the penalty shall not apply if reasonable cause is shown.

"The statutes use the words 'imposed' and 'shall not apply' rather than 'refund' or 'abate,' which makes clear that Congress intended for the IRS to review a taxpayer's reasonable cause claim BEFORE imposing the penalty," the Texas Society of CPAs' comments state. "Current IRS practice not only contradicts this intent by assessing and collecting penalties first and asking questions later, but also potentially violates a taxpayer's due process rights. Our system of justice presumes innocence until proven otherwise, which necessarily requires governmental agencies to establish guilt before penalizing citizens."

The letter also argues that IRS agents need proper training to review reasonable cause statements and should consider assigning more experienced personnel to handle processing of forms 3520 and 3520-A.

Practitioners have disparaged how the IRS trains its Appeals employees on forms 3520 and 3520-A, finding those materials wanting when compared with other international information reporting forms.

If the IRS decides not to allow e-filing, it should consider moving the form processing to the Austin, Texas, campus and having Large Business and International Division personnel stationed there consider reasonable cause, Price said. He noted that there are higher-graded personnel in Austin who have handled voluntary disclosures and streamlined filing compliance procedures. Staffing considerations would still need to be considered, however, he added.

In addition to asking for greater clarity on what constitutes reasonable cause, the Florida Bar requested that the IRS extend its first-time abatement policy so that it includes avoidance of penalties on forms 3520 and 3520-A without the need to show reasonable cause. It insists that first-time abate relief should apply to all tax years the taxpayer filed during the initial reporting period.

"This will reduce the chilling effect on compliance and reporting as taxpayers will not be fearful of penalties being assessed for multiple years when trying to come into compliance for the first time," the Florida Bar argued. "The purpose of penalties is not to create fear of reporting to the government what Congress has determined to be valuable information. Instead, penalties are meant to be a punishment in appropriate situations and where it will help rehabilitate a taxpayer toward future voluntary compliance. In this regard, the automatic application of penalties to all situations does not meet this goal and, in fact, the current system has the opposite effect."