

Offshore Programs: Background, History and Current Procedures.

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IRS Office of Chief Counsel, SB/SE working under the Direction of the (b)(6)

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Reasonable cause

- Two types
 - Reasonable cause
 - No professional advice
 - Self-prepared
 - Reasonable cause/reliance
 - Reliance on professional advice

General Rules on Reasonable Cause

- ▶ To avoid penalty, taxpayer must show he acted with “reasonable cause” and in “good faith.”
- ▶ I.R.C. § 6664(c)(1).
- ▶ “Reasonable cause” requires the taxpayer to exercise ordinary business care and prudence to the disputed item.
- ▶ “Good faith” has no precise definition but means an honest belief and intent to perform all lawful obligations.

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Considerations

- ▶ Reasonable cause is established on a case-by-case basis.
- ▶ Review all pertinent facts and circumstances.
- ▶ Review the taxpayer's knowledge and experience.
- ▶ Consider if there is an honest mistake of fact or law.
- ▶ Consider the taxpayer's efforts to assess the proper liability.

Three-Prong Test

▶ Once the taxpayer has shown “advice” was given, the taxpayer must meet a three-prong test to establish reliance on a professional.

▶ The taxpayer selected a competent advisor with sufficient expertise to justify reliance.

▶ The taxpayer supplied the adviser with the necessary and accurate information.

▶ The taxpayer actually relied in good faith on the adviser’s judgment.

▶ Neonatology Assocs., P.A. v. Commissioner, 115 T.C. 43,99 (2000), aff’d, 299 F.3d 221 (3d Cir. 2002).

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Boyle
469 us 241, 105 s Ct 687

UNITED STATES v. BOYLE, Executor of the Estate of Boyle.
469 us 241, 105 s Ct 687

Taxpayer = executor of his mother's estate

Taxpayer relied on estate attorney to file estate return

Opinion = taxpayers cannot delegate filing

Boyle opinion

- *Held:* The failure to make a timely filing of a tax return is not excused by the taxpayer's reliance on an agent, and such reliance is not "reasonable cause" for a late filing under [§ 6651\(a\)\(1\)](#). While engaging an attorney to assist in probate proceedings is plainly an exercise of the "ordinary business care and prudence" that the relevant Treasury Regulation requires the taxpayer to demonstrate to excuse a late filing, this does not answer the question presented here. To say that it was "reasonable" for respondent to assume that the attorney would meet the statutory deadline may resolve the matter as between them, but not with respect to the respondent's obligation under that statute. **It requires no special training or effort on the taxpayer's part to ascertain a deadline and ensure that it is met.** That the attorney, as respondent's agent, was expected to attend to the matter does not relieve the principal of his duty to meet the deadline. Pp. 690-693.

Chief Justice BURGER delivered the opinion of the Court.

We granted certiorari to resolve a conflict among the Circuits on whether a taxpayer's reliance on an attorney to prepare and file a tax return constitutes "reasonable cause" under [§ 6651\(a\)\(1\) of the Internal Revenue Code](#), so as to defeat a statutory penalty incurred because of a late filing.

Ability to exercise reasonable cause.

“Because the respondent here was fully capable of meeting the required standard of ordinary business care and prudence, **we need not decide the issue** of whether and under what circumstances a taxpayer who presents evidence that he was *unable* to adhere to the required standard might be entitled to relief from the penalty.” *Post*, at 695.

Boyle quote

This case is not one in which a taxpayer has relied on the erroneous advice of counsel concerning a question of law. Courts have frequently held that “reasonable cause” is established when a taxpayer shows that he reasonably relied on the advice of an accountant or attorney that it was unnecessary to file a return, even when such advice turned out to have been mistaken. See, e.g.... This Court also has implied that, in such a situation, reliance on the opinion of a tax adviser may constitute reasonable cause for failure to file a return. See (remanding for determination whether failure to file return was due to reasonable cause, when taxpayer was advised that filing was not required).

(... = cases cited removed to add space)

Boyle quote

When an accountant or attorney *advises* a taxpayer on a matter of tax law, such as whether a liability exists, it is reasonable for the taxpayer to rely on that advice. **Most taxpayers are not competent to discern error in the substantive advice of an accountant or attorney (emphasis added)**. To require the taxpayer to challenge the attorney, to seek a “second opinion,” or to try to monitor ****693** counsel on the provisions of the Code himself would nullify the very purpose of seeking the advice of a presumed expert in the first place. See [Haywood Lumber, supra, at 771](#). “Ordinary business care and prudence” do not demand such actions.

Justice Brennan wrote his opinion yet concurred with the majority.

Because the respondent here was fully capable of meeting the required standard of ordinary business care and prudence, we need not decide the issue of whether and under what circumstances a taxpayer who presents evidence that he was *unable* to adhere to the required standard might be entitled to relief from the penalty. As the Court has expressly left this issue open for another day, I join the Court's opinion.

What does Boyle do and what does Boyle not do?

States that reasonable cause is based on facts and circumstances of each case.

Taxpayer's are not required to second guess or verify the professional's opinion.

Explicitly does not address reasonable cause in general, only that taxpayers cannot delegate the actual filing of a return to someone else.

Does not define "Qualified Professional", references accountants and attorney without additional qualifiers, e.g., CPA or tax attorney.

Contrast “Reliance on Advice” With “Delegation of Filing Duty”

Not preparing a return can be implied advice that nothing is required if the taxpayer provided all critical facts to an expert and asked him to prepare whatever forms are required.

- Hatfried v. Commissioner, 162 F.2d 628 (3rd Cir. (1947).

But if you know a return is required you can't just hand your information to a professional and rely on him to file on time.

- United States v. Boyle, 469 U.S. 241, 246 (1985).

HATFRIED, Inc. v. COMMISSIONER, 162 F.2d 628

Who is qualified?

Previously we pointed out that the Treasury Department has long given sanction to the practice of taxpayers in enlisting the aid of accountants in the preparation of their tax returns. To this may be added that the Treasury Department regularly admits accountants to practice before it in representation of taxpayers and the Tax Court does the same.

To accord the status of 'experts' on the tax laws to accountants for representation purposes and then to hold that taxpayers who entrust to them the task of preparing their tax returns run the risk of paying heavy penalties should they err in the discharge of their assignment creates an absurd situation.

To hold that a taxpayer who selects as his agent a certified public accountant (to whom as a class the Treasury Department and the Tax Court itself accord recognition as 'experts' and as 'counsel') has failed to exercise 'ordinary business care and prudence' and becomes liable for the error of his advisor as 'agent' is an inconceivable proposition.

HATFRIED, Inc. v. COMMISSIONER, 162 F.2d 628

useful quotes

- We approach the problem, whether there was any substantial basis for the Tax Court's finding, with these principles in mind: (1) 'Reasonable cause means nothing more than the exercise of ordinary business [**10] care and prudence'. 1. and (2) the penalties imposed under the revenue laws were designed to attach to conduct of a taxpayer 'which is intentional, or knowing, or voluntary, as distinguished from accidental' 2. as evidenced by the words in Section 291 'and not due to willful neglect.'
- Certainly the mere failure to comply with the provisions of the revenue laws is not a per se 'without reasonable cause' violation. That is manifest in the Lane-Wells Co. case, supra, where, although there was a failure to file a personal holding company return, the Supreme Court remanded to the Tax Court with directions to ascertain whether there was any reasonable cause.
- Further, it is well-settled that in the application of penalties 'all questions in doubt must be resolved in favor of those from whom the penalty is sought.' Crawford, Statutory Construction, Section 140, page 462.

Separate quotes



Streamlined Filing Compliance Procedures- Issues for Appeals

(b)(6)

(b)(6)

January 2020



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Contrast Objective and Subjective Standards

For fraud or criminal willfulness we use a subjective test:

(b)(3):26 U.S.C. § 6103; (b)(7)(E)

But for reasonable cause we use an objective test:

(b)(3):26 U.S.C. § 6103; (b)(7)(E)



Reliance on Paid Professional

- One way a taxpayer can establish reasonable cause is to show reliance on the advice of an independent professional such as a tax advisor, lawyer, accountant or the IRS.
- The advice can be written or oral. However, oral advice from the IRS does not guarantee penalty relief. See IRM 20.1.1.3.3.4.2.
- There are distinct, objective showings that the taxpayer must establish.



What is “Advice”?

The taxpayer must first show that “advice” on the disputed item was given.

Advice must be based on all pertinent facts and circumstances and the law as it relates to those facts and circumstances. Treas. Reg. § 1.6664-4(c)(i)

Advice may not be based on unreasonable factual and legal assumptions or unreasonably rely on facts supplied by third parties. Treas. Reg. § 1.6664-4(c)(ii)

Advice is any communication “setting forth the analysis or conclusion” of the advisor upon which the taxpayer relies with respect to the I.R.C. § 6662 penalty. Treas. Reg. § 1.664-4(c)(2)

(The regulation sets forth additional criteria for tax shelters and section 482 cases.)



What is “Advice”?

(b)(3) 26 U.S.C. § 6103; (b)(7)(E)

- Woodsum v. Commissioner, 136 T.C. 585 (2011).

(b)(3) 26 U.S.C. § 6103; (b)(7)(E)

- Neonatology Associates, P.A. v. Commissioner, 115 T.C. 43, 100 (2000).

Not to be used or cited as precedent.



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Consider

(b)(3) 26 U.S.C. § 6103; (b)(7)(E)

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Three-Prong Test

Once the taxpayer has shown “advice” was given, the taxpayer must meet a three-prong test to establish reliance on a professional.

1. The taxpayer selected a competent advisor with sufficient expertise to justify reliance.
 2. The taxpayer supplied the adviser with the necessary and accurate information.
 3. The taxpayer actually relied in good faith on the adviser’s judgment.
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Competence of Advisor

Prong 1: The taxpayer selected a competent advisor with sufficient expertise to justify reliance.

Did the advisor have international tax expertise or does it look like the taxpayer selected the advisor because he was unsophisticated?

- Patin v. Commissioner, 88 T.C. 1086 (1987).

Did the taxpayer change advisors?

What if the taxpayer relied on advice from an advisor in a foreign country?

What if the advice came from the taxpayer's banker?

- Mayflower Investment Company v. Commissioner, 24 T.C. 729 (1955).



Reasonable Cause in FBAR context

Jarnagin v. U.S., case number 15-1534T, Court of Federal Claims (opinion and order issued November 30, 2017)

Jarnagin involved the assessment of nonwillful FBAR penalties, and reasonable cause is a defense to nonwillful FBAR penalties. Jarnagin looked to the body of law concerning reasonable cause in tax cases in this context because of the dearth of caselaw interpreting reasonable cause for nonwillful FBAR cases. The taxpayers asserted they reasonably relied on their accountants in failing to report foreign bank accounts.

Not to be used or cited as precedent.



Jarnagin (cont'd)

But the Jarnagin court noted that:

“[W]hile the Jarnagins relied upon their accountants to fill out their tax returns, the record contains no evidence that they otherwise sought advice (legal or otherwise) concerning any obligations that they might have had to file reports or make disclosures concerning their foreign assets or businesses.”

Id. at 12.

In other words, the taxpayers in Jarnagin made no effort to seek advice from their accountants on how to report their foreign bank accounts.



Consider

(b)(3)26 U.S.C. § 6103; (b)(7)(E)

Not to be used or cited as precedent.



Disclosure of Facts

Prong 2: The taxpayer supplied the adviser with the necessary and accurate information.

Failure to disclose critical facts to advisor renders reliance unreasonable

- Yale Avenue Corporation v. Commissioner, 58 T.C. 1062 (1972).
- Leonhart v. Commissioner, 414 F.2d 749 (4th Cir. 1969).
- Diaz v. Commissioner, T.C. Memo 2012-280.

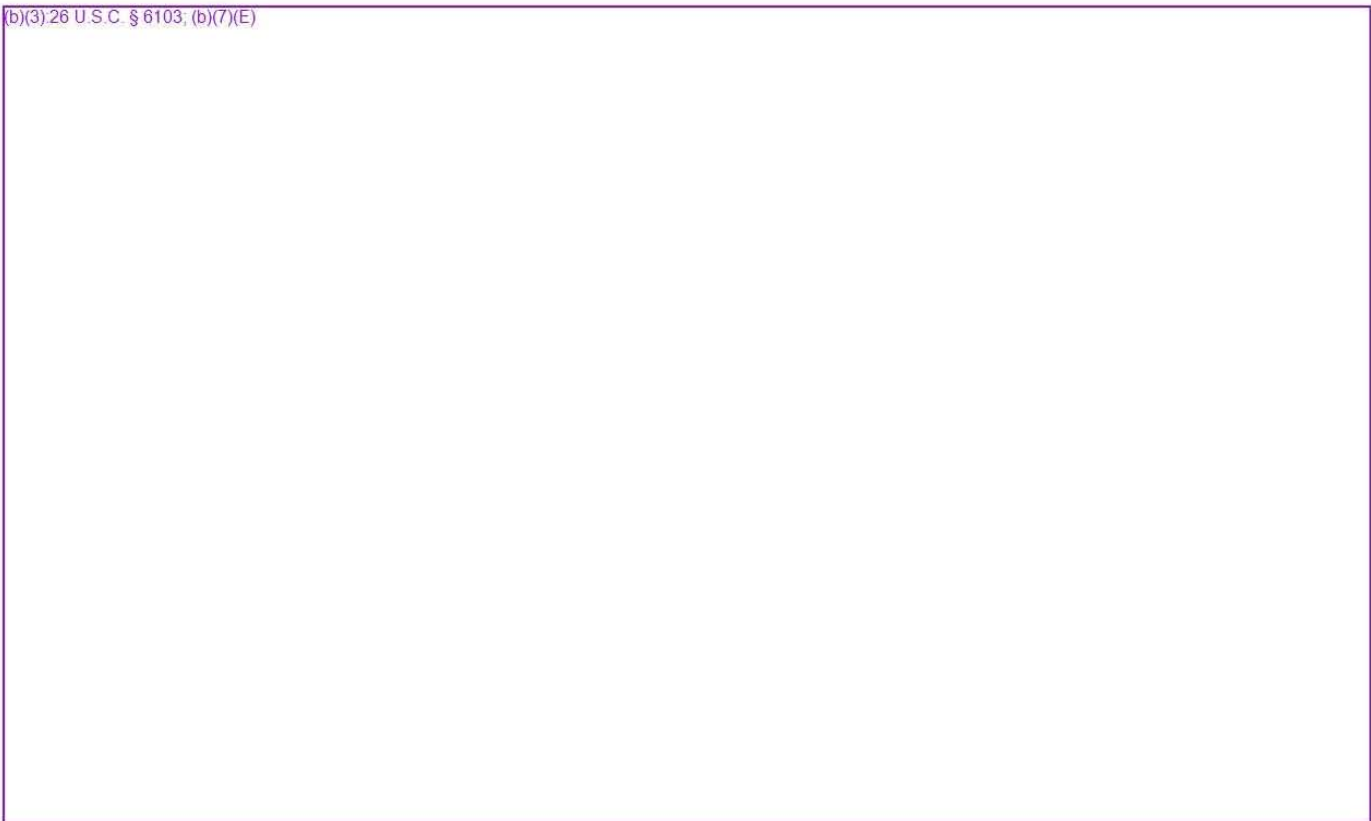
The burden is on the taxpayer to prove that all facts were disclosed

- Fourth & Railroad Realty Co. v. Commissioner, 25 T.C. 458 (1955).
- InterTAN, Inc. v. Commissioner, T.C. Memo 2004-1.

Not to be used or cited as precedent.



(b)(3)26 U.S.C. § 6103; (b)(7)(E)



Not to be used or cited as precedent.



Good Faith Reliance

Prong 3: The taxpayer actually relied in good faith on the adviser's judgment.

- Do the circumstances show that the taxpayer actually relied on the advice?
 - Estate of Young v. Commissioner, 110 T.C. 297 (1998).
- Negligent mistake of preparer is not reasonable cause, if taxpayer was in a position to notice the error on reviewing the return
 - Pritchett v. Commissioner, 63 T.C. 149 (1974).

Not to be used or cited as precedent.



Consider

(b)(3); 26 U.S.C. § 6103; (b)(7)(E)

Not to be used or cited as precedent.



Reliance in Filing Context

Ignorance of a filing requirement is not reasonable cause unless the taxpayer made inquiry of a knowledgeable expert and was misinformed.

- Henningsen v. Commissioner, 243 F.2d 954, 958 (4th Cir. 1957).
(income tax return)
- Janpol v. Commissioner, 102 T.C. 499, 504-05 (1994).
(returns of excise tax on profit sharing trust prohibited transactions)
- N.Y. State Assn. Real Est. Bd. Group Ins. Fund v. Commissioner, 54 T.C. 1325, 1336 (1970).
(exempt org business income tax returns)
- Heman v. Commissioner, 32 T.C. 479, 490 (1959).
(domestic trust returns)
- Coshocton Securities Co. v. Commissioner, 26 T.C. 935, 939 (1956).
(personal holding company returns).

Not to be used or cited as precedent.