

Penalties and Interest

When clients make initial contact with a tax resolution provider regarding their tax concerns, one of the first questions they ask is “can you remove the penalties and interest that has been assessed toward my delinquent taxes?” To be perfectly clear, you will most likely not be successful in removing interest. Interest generated from delinquent taxes will not be abated with the exception of a few extraordinary circumstances. In order to abate interest the taxpayer must prove that he or she was caused an unwarranted delay that was directly caused by the actions of an IRS employee; and, the delay itself caused the interest to be charged. The IRS and State taxing agencies have a steadfast policy that interest will be charged on delinquent taxes. There are other ways such as Offers in Compromise and Partial Pay Installment Agreement to remove or reduce the necessity to pay interest but simply asking for the interest to be removed will be unsuccessful. That being said, if you are able to abate penalties and/or have tax liabilities reduced, you can in turn reduce the interest that has accrued on said penalties and tax.

Having penalties waived (removed) on the other hand is a different story. There are several steps you can take to have penalties waived. Assuming you have the ability to have penalties waived, the question remains as to whether or not it makes economic sense to complete the work necessary to remove said penalties. For example, if a taxpayer owes \$500,000 in back taxes, and the possibility exists to have a \$10,000 penalty waived, should said taxpayer pay a professional to have the penalty removed? If the taxpayer has the ability to full-pay their liability within the statute of limitations, the answer would most likely be “yes”. However, if the taxpayer is earning minimum wage and has not assets to speak of, he or she would be spending their limited funds more wisely to address the \$500,000 liability as opposed to reducing it to a \$490,000 liability and still having to address the same concerns.

There are certain things you must know if you wish to have penalties abated. First and foremost, the IRS will typically not abate a penalty unless it has already been paid. Beyond the necessary to prepay a penalty and related interest on a liability, it can be advantageous for a taxpayer to do so because it will stop the additional interest that continues to accrue if the penalty is ultimately not removed.

As a general rule of thumb, you may request an abatement of penalty if you show cause. A taxpayer who voluntarily steps forward and corrects a deficiency in a previously filed return is often successful in requesting penalty abatement. A taxpayer will most likely not be successful in requesting an abatement of a penalty that was assessed as a result of an audit.

The most common way to request that a penalty be abated is write a letter to the IRS office that issued the initial notice. The chances of having the abatement granted increase if the letter is in response to the first notice received and not sent once collection activity has commenced.

Correspondence to the IRS requesting the abatement should be clear and concise, including both a detail of the cause of the penalty assessment, as well as providing supporting documentation showing why the penalty should be removed.

What kinds of interest and penalties will I be charged for filing and paying taxes late?

Answer:

Interest is compounded daily and charged on any unpaid tax from the due date of the return (without regard to any extension of time to file) until the date of payment.

- The interest rate is the federal short-term rate plus 3 percent.
- That rate is determined every three months.

In addition, if you didn't pay your tax on time, you'll generally have to pay a late payment penalty.

- The late payment penalty is one-half of one percent of the tax (0.5%) owed for each month, or part of a month, that the tax remains unpaid after the due date, not exceeding 25 percent.
- The one-half of one percent rate increases to one percent if the tax remains unpaid after several bills have been sent to you and the IRS issues a notice of intent to levy.
- If you filed a timely return and are paying your tax via an installment agreement, the penalty is one-quarter of one percent for each month, or part of a month, that the installment agreement is in effect.

If you did not file on time and owe tax, you may owe an additional penalty for failure to file unless you can show reasonable cause.

- The combined penalty is 5 percent (4.5% late filing, 0.5% late payment) for each month, or part of a month, that your return was late, up to 25%.
- The late filing penalty applies to the net amount due, which is the tax shown on your return and any additional tax found to be due, as reduced by any credits for withholding and estimated tax payments.
- After five months, if you still have not paid, the 0.5% failure-to-pay penalty continues to run, up to 25%, until the tax is paid.
- The total penalty for failure to file and pay can be 47.5% (22.5% late filing, 25% late payment) of the tax owed.

If your return was over 60 days late, however, the minimum failure-to-file penalty is the smaller of \$135 (\$100 for returns required to be filed before January 1, 2009) or 100% of the tax required to be shown on the return

Determining Income Tax Interestⁱ

20.2.6.1 (06-18-2010)

Method and Rates Used

1. The methods and rates for computing interest are:
 - Prior to February 1, 1980, simple annual interest was computed on a Year, Year, Month, Month, Day, Day (YYMMDD) basis.
 - Beginning February 1, 1980, the method changed to calculate total days times the daily factor.
 - On January 1, 1983, the method changed to daily compounding of interest (i.e., interest computed on interest).

20.2.6.2 (10-15-2011)

Compound Interest

1. The Service is required to compound interest on a daily basis per IRC 6622(a). This results in a daily recalculation of the principal amount **plus** accrued interest.
 - Principal amount (P)
 - Daily interest rate (R)
 - Number of days (T)
 - Interest (I)
2. The principal amount on which interest is compounded includes tax, penalties (at the point they become subject to interest per IRM 20.2.5.3, *Interest on Penalties and Additions to Tax*), additions to tax and all accrued interest.
3. The formula to compute interest is as follows:
 - Interest (I) equals principal (P) times the daily interest rate (R) or $I = P \times R$.
 - New principal (New P) equals interest plus principal or $New P = I + P$ and continues over the number of days (T) until the principal/new principal amounts are paid.

20.2.6.4 (10-15-2011)

Interest Computation Tools

1. IDRS Command Code (CC) COMPA is used for non-complex interest computations. C C INTST is used if the module is not restricted (-I Freeze Code is one indicator of module restriction). In addition to these command codes, the IRS supports the use of a Commercial Off The Shelf (COTS) software program called InterestNet, commonly referred to as the Automated Computational Tool (DMI/ACT), which can be used for most interest computations, and is recommended for more complex interest computations. This software program is available to all employees, particularly those involved with the calculation of restricted interest. IRM 20.2.8.6, *Reasons for Restriction*, lists some of the reasons interest may need to be restricted on a tax module.
2. See IRM 2.3.39, *Command Code FTPIN*, for an explanation of CC FTPIN. See IRM 2.3.40, *Command Code PICRD*, for an explanation of CC PICRD. See IRM 2.3.29, *IDRS Terminal Input, Command Codes INTST, ICOMP, and COMPA*, for definers and examples using CC COMPA.
3. Occasionally, CC INTST does not match the Master File (i.e., CFOL) interest and/or penalty computation. Therefore, before CC INTST results are used, compare total penalty and interest with CFOL command codes BMFOLT or IMFOLT (as appropriate) with total penalty and interest on INTST, computed to the interest date reflected on IMFOLT

or BMFOLT. If unable to reconcile computational differences between CFOL and CC INTST, a manual computation must be made to determine which one is correct. If there is a systemic interest problem, send the results to the appropriate person per local procedures (consult your manager or lead), so that either programming can be corrected or an advisory can be issued. If there are no local referral procedures, then send to the Office of Servicewide Interest analyst responsible for programming problems. For contact information see <http://sbseservicewide.web.irs.gov/interest/contacts/213.aspx>.

Caution:

C C INTST does not update or cause an accurate interest computation on a tax module to be performed when interest is restricted. If the tax module is restricted, a manual interest computation **must** be done. Whenever possible, use a non-restricting TC 340. See IRM 20.2.8.11, *Non-Restricting TC 340*.

20.2.6.5 (10-15-2011)

Computer Generated Interest Computations

1. Master File calculates interest by sorting all money amount transactions in effective date order and computing interest on balances from transaction to transaction (running module balance).
 - A. When all transactions are sorted and a liability is established, interest is computed on that liability to the date of the next transaction.
 - B. That transaction amount is added to the unpaid liability plus interest, and interest on this new balance is computed to the next transaction date and so on, through all transactions posted, to the current posting (23C) date.
 - C. Master File compares the total interest accrued to the net amount of all posted interest transactions in the module and assesses or abates the difference with TC 19X or 33X as appropriate.
 - D. No additional penalty or interest accrues on amounts paid within 21 calendar days of notice and demand (10 business days if the amount in the notice is \$100,000 or more). See IRM 20.2.5.4, *Notice and Demand and Debit Interest*.

Penalty for Paying Income Taxes After They Were Due

Whether or not you can afford to pay your tax liability, you are better off filing your tax returns timely. If you fail to file your Federal income tax return in a timely manner, you will be charged an additional 5% of the overall liability per month for the first 5 months after the taxes are due. This equates to paying an additional 25% above the original tax liability plus other less significant penalties and interest on both the tax and penalties.

For this reason, a taxpayer would be foolish not to file an extension of time to file (Form 4868) giving them an extra 6 months or 180 to prepare and file their tax return. The 4868 is a 1-page form requiring relatively little information.

Keep in mind that filing a 4868 does not extend the time necessary to pay the tax owed. That being said, it is still worth saving 25% of the overall tax liability in penalties. In order to avoid a late-payment penalty when filing an extension, a taxpayer must pay at least 90% of the amount they by the due date of the return which is typically April 15th

Example 1: if a taxpayer owes \$11,000, they would be required to pay \$9,900:

$$\$11,000 \times 0.90 = \$9,900$$

If said taxpayer did not pay at least \$9,900 when they filed their extension, the IRS would assess a late-payment penalty. The penalty is ½% of the amount you owe per month. This penalty continues to accrue until it reaches the prescribed maximum amount equaling 25%.. Using the example above, the late-payment penalty would be:

Example 1a: $\$11,000 \times 0.005 = \55 charged per month (this amount would continue to accrue until it reached \$2,750 which is 25% of \$11,000)

To sum up, the sooner a taxpayer is able to satisfy an outstanding balance, the less they will pay in penalties. If a taxpayer files their return on time and enters into a voluntary installment agreement, the IRS will reduce their late-payment penalty by $\frac{1}{4}\%$ per month.

Example 1c: $\$11,000 \times 0.0025 = \27.50 (in this case the \$55 penalty would be reduced to \$27.50 which is $\frac{1}{2}$ of the original)

In this same example, if the taxpayer does not file an extension, the late-filing payment fee would be 4.5% of the unpaid tax per month up to five months.

Example 1d: $\$11,000 \times 0.045 = \495 per month

In addition to accruing penalties for failure to pay timely, any additional tax owed after the due date of the return will also accrue interest. Interest assessed for taxes is compounded daily and will continue to accrue as long as the tax is owed.

The interest rate for unpaid taxes is determined by adding 3% to the federal short-term rate. As of the second quarter of 2008, the interest rate on unpaid individual income taxes is 6%.

Example 1e: monthly interest amount would be \$660,

$$\$11,000 \times .06 = \$660$$

and the penalty would be \$55 which combined would be

$$\$660 + \$55 = \mathbf{\$715 \text{ (penalty and interest)}}$$

So the taxpayer would continue to accrue \$715 for each month that they failed to pay the original \$11,000 they owed in taxes to the IRS. Keep in mind that this example is simple in that it fails to account for interim payments that may have been made as well as interest accruing on penalties and interest accruing on interest.

Payroll Tax Interest and Penalties

If a business has employees, it is the business's responsibility to collect and submit via tax deposits to the IRS and local taxing agencies, the employee's income tax withholding as well as the employee's payroll taxes as well as the employer's matching share of payroll taxes. Unless an employee is exempt, an employer must withhold and submit, usually via electronic deposits, the items described above within a given time frame. If an employer fails to remit income tax withholding as well as payroll tax withholding and the employer's matching share, they will face severe consequences.

In addition to the employee's Federal income tax withholding IRS payroll taxes are made up of two parts: Social Security tax and Medicare tax. An employer is required to match the amount paid of each of these taxes. If the payroll tax liability is under \$2,500, the employer may make tax deposits quarterly when they prepare and file their payroll tax returns (Form 941s). If the liability is over \$2,500, the deposits must be made sooner (i.e. semi-monthly or monthly).

While most employers are required to make Federal payroll tax deposits semi-monthly or monthly, if they reported taxes greater than \$50,000 for the look-back period, they are a semiweekly schedule depositor, and generally must deposit your employment taxes based on the following scheduleⁱⁱ:

1. The employment taxes on payments made to their employees on Wednesday, Thursday, and/or Friday, must be deposited by the following Wednesday.
2. The employment taxes on payments made to their employees on Saturday, Sunday, Monday, and/or Tuesday, must be deposited by the following Friday.

If any of the 3 weekdays after the end of a semiweekly period is a legal holiday, you will have an additional day for each day that is a legal holiday to make the required deposit. Regardless of whether an employer is a monthly schedule depositor or a semiweekly schedule depositor, if they accumulate taxes of \$100,000 or more on any day during a deposit period, they must

deposit the tax by the next business day. If this happens, they become a semiweekly depositor for at least the remainder of the calendar year and for the following calendar year.

Since 2012, the IRS determines the late filing penalty based upon the number of days that has passed since the payroll taxes were due. For example, if an employer makes their Federal tax deposit within five days of being due, the IRS will assess a 2% penalty of the total amount. If they deposit is made within 6-15 days of the due date, the penalty increases to 5%. If the tax is more than 15 days late, the penalty increases to 10%. Note that if you outsource your payroll tax duties to a payroll service provider, the IRS holds you responsible for tax errors that the third party makes.

It is important to remember that payroll tax penalties and interest are not only assessed to the business but also to those considered by the IRS to be “Responsible” for determining that the funds withheld to pay the government were earmarked for other items (see *Trust Fund* and *Civil Penalty*).

100% Penalty (Trust Fund Recovery Penalty)

As mentioned above, section 6672 of the Internal Revenue Code allows the IRS to charge any “responsible party” who refuses or fails to collect and pay mandated federal taxes a 100% personal liability “Civil” penalty. The responsible person/s may be a corporate officer or someone who controls the employer’s finances or has an authorized signature on the payroll account and will be jointly and severally liable if more than one person is found “Responsible”

The withholding process occurs as follows:

1. Employee’s income taxes, Social Security taxes, and Medicare taxes are withheld from the employee’s pay.
2. They amounts that were withheld are then paid (usually via electronic tax deposits).
3. The amounts withheld and the deposits that were made are reported via payroll tax returns.
4. At the end of the year, forms W-2 are prepared for each employee and submitted to the Social Security Administration (“SSA”) along with a summary of all of the W-2’s called Form W-3.
5. The SSA then forwards the reported withholding data to the IRS.

If an employer fails to satisfy the requirements set forth above, the employee may face issues that arise from the employer’s actions or lack thereof.

Statute of Limitations

There is no statute of limitations to assess penalties and interest on a return that has not been prepared. There is also no statute of limitations for penalties and interest stemming from the failure to file and report payroll taxes (Social Security, Medicare, Unemployment, withheld income taxes). In addition, there also is no statute of limitations on assessment of tax, penalties and interest when a false tax return is filed.

Penalty Reference Chartⁱⁱⁱ

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Limited Liability Company (LLC) Fee Estimate Penalty	None	17942(d)(2)	Underpayment of estimated fee.	10% of the underpayment.
			Exceptions - Safe harbor-100% of prior year.	
Tax on Joint Return Exceeds Tax on Separate Returns	6013(b)(5)	18530	Tax on a joint return exceeds tax shown on separate returns, due to negligence or intentional disregard of rules, or fraud. In lieu of penalties provided by Section 19164(a) and (b).	75% of excess if attributable to fraud.
			20% of total amount of excess if attributable to negligence/intentional disregard of rules.	
Information Return From Owner of Real Property	6045	18642	Owners and transferors failing to file information return relating to interest in real property by the due date.	Penalty under 19183 applies. If information return not filed within 60 days of due date, the deduction of certain property-related expenses are disallowed.
			Exceptions - Reasonable cause and not willful neglect.	
Withholding Penalties	3403, 1461	18668(a)	Any person required to withhold tax, but fails to do so.	The greater of: <ul style="list-style-type: none"> • The actual amount withheld or • Payee's total tax liability (before application of any payments and credits), not to exceed the required 7% withholding amount.

			Exceptions - Reasonable cause.	
Withholding Penalties – Real Estate	3403, 1461	18668(d)	Any person required to withhold tax from the sale of real property when properly notified, but fails to do so.	The greater of: <ul style="list-style-type: none"> • \$500 or • 10% of the amount required to be withheld.
				Exceptions - Reasonable cause.

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Withholding Penalties – Real Estate Escrow Person		18668(e)(1)	Any real estate escrow person failing to provide written notification of withholding requirement to a transferee/buyer of a California real property interest.	The greater of: <ul style="list-style-type: none"> • \$500 or • 10% of the amount required to be withheld.
				Exceptions - Reasonable cause.
Withholding Penalties – Real Estate False Certificate		18668(e)(5)	Any transferor of California real property who knowingly files a false exemption certificate (Form 593-C, <i>Real Estate Withholding Certificate</i>) to avoid withholding.	The greater of: <ul style="list-style-type: none"> • \$1,000 or • 20% of the amount required to be withheld.
				Exceptions - Reasonable cause.
Withholding Penalties	None	18669	Successor on a sale, transfer, or disposition of a business for failing to pay required amounts or failing to withhold or to pay withheld amounts.	10% of amount not paid or personal liability for amounts not withheld or withheld amounts not paid.
				Exceptions - None.
Electronic Funds Transfer (EFT) Penalty	6302	19011(c)	Any person required to remit payment by EFT, but who makes payment by other means.	10% of the amount paid by non-EFT.
				Exceptions - Reasonable cause and not willful neglect.
Electronic Payment Requirements for Individuals	None	19011.5	Failure by individuals, whose tax liability is greater than \$80,000 or who make an estimated tax or extension payment that exceeds \$20,000, to remit their tax payments electronically.	1% of the amount paid.
				Exceptions - Reasonable cause and not willful neglect.

Failure to File a Return/Late Filing Penalty	6651	19131	Any taxpayer who is required to file a return, but fails to do so by the due date.	5% of the tax due, after allowing for timely payments, for every month that the return is late, up to a maximum of 25%. For fraud, substitute 15% and 75% for 5% and 25%, respectively. For individuals and fiduciaries, minimum penalty is the lesser of: <ul style="list-style-type: none"> • \$135 or • 100% of the tax required to be shown on the return.
			Exceptions - Reasonable cause and not willful neglect.	

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Failure to Pay Tax/Late Payment Penalty	6651	19132	Taxpayer failing to pay tax by the due date. This penalty is not imposed if, for the same tax year, the sum of Sections 19131 and 19133 penalties are equal to or greater than this penalty.	5% of the total tax unpaid plus 1/2 of 1% for every month the payment of tax was late up to 40 months. Not to exceed 25% of the total unpaid tax.
			Exceptions - Reasonable cause and not willful neglect.	
Failure to Provide Information Requested/ Failure to File a Return Upon Demand	None	19133	Any taxpayer for failing to provide requested information, or failing to file a return after notice and demand.	25% of total tax liability assessed without regard to any payments or credits.
			Exceptions - Reasonable cause and not willful neglect.	
Penalty for Failure to Make a Small Business Stock Report	6652(k)	19133.5	Taxpayer for failing to make a small business report.	\$50 for each report. \$100 per report if the failure is due to negligence or intentional disregard.
			Exceptions - Reasonable cause and not willful neglect.	
Dishonored Payments	6657	19134	Any taxpayer who makes a payment by check that is dishonored. Includes payments made by credit card or EFT.	For payments received after January 1, 2011: <ul style="list-style-type: none"> • An amount equal to 2% of the amount of the dishonored payment, or • If the amount of the check is less than \$1,250, \$25 or the amount of the check, whichever is less.
			Exceptions - Reasonable cause and good faith.	

Unqualified or Suspended Corporation Doing Business in this State	None	19135	Any foreign corporation which fails to qualify to do business, or whose powers have been forfeited, or any domestic corporation which has been suspended, and is doing business in this state, within the meaning of Section 23101.	\$2,000 per taxable year.
			Exceptions - Reasonable cause and not willful neglect.	

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Underpayment of Estimated Tax (Addition to Tax)	6654	19136 et seq., 19142-19151	Any taxpayer who fails to pay estimated tax in the required installments.	An amount determined by applying the underpayment rate specified in Section 19521 to the amount of the underpayment for the period of the underpayment.
			Exceptions - (1) Safe harbors under 6654 as modified. (2) Underpayment created or increased by any provision of law that is chaptered during and operative for the taxable year of the underpayment (3) underpayment was created or increased by the disallowance of a credit under Section 17053.80(g) or 23623(g).	
Large Corporate Understatement of Tax	None	19138	When a corporation has an understatement of tax for: Tax years beginning January 1, 2003, through December 31, 2009, that exceeds \$1 million. Tax years beginning January 1, 2010, that exceeds the greater of: <ul style="list-style-type: none"> • \$1 million. • 20% of tax shown on original return or shown on amended return filed on or before original or extended due date of return for taxable year. 	20% of the understatement of tax.

			Exceptions - Understatement is attributable to (1) a change in law after earlier of date return is filed or extended due date of return or (2) reasonable reliance on legal ruling by the Chief Counsel.	
Corporation Officer Statement Penalty	None	19141	Upon certification by the Secretary of State, penalty for taxpayer's failure to provide a Statement of Information.	\$250 upon certification by the Secretary of State under Corporations Code Sections 2204 and 17653. \$50 upon certification by the Secretary of State under
			Exceptions - None.	

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Information With Respect to Certain Foreign Corporations (IRS Form 5471, Information Return of U.S. Persons With Respect To Certain Foreign Corporations)	6038	19141.2	Failure to file and furnish certain information about certain foreign corporations.	\$1,000 for each annual accounting period. \$1,000 for each 30-day period up to a maximum of \$24,000 when failure continues after 90-day of notification.
			Exceptions - Reasonable cause and not willful neglect.	
Failure to File and Furnish Information About Foreign-Owned Corporations (IRS Form 5472, Information Return of a 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business)	6038A	19141.5	Failure to file and furnish information or to maintain required records about foreign-owned corporations, under IRC Section 6038A.	\$10,000 for each taxable year for which the taxpayer fails to file required information or fails to maintain the required records. \$10,000 for each 30-day period when failure continues after 90-day of notification.
			Exceptions - Reasonable cause.	

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Failure to File - Notice of Certain Transfers to Foreign Corporation (IRS Form 926, Return by a U.S. Transferor of Property to a Foreign Corporation)	6038B	19141.5	Failure to file/furnish information records about transfers or distributions to foreign-owned corporations, under IRC Section 6038B.	10% of fair market value at time of exchange, not to exceed \$100,000 unless failure due to intentional disregard. Plus recognition of gain required as if property sold based on that value.
			Exceptions - Reasonable cause and not willful neglect.	
Failure to File or Furnish Information About Foreign Corporations Engaged in U.S. Business (IRS Form 5472)	6038C	19141.5	Failure to file and furnish information or to maintain required records about a foreign corporation engaged in a trade or business within the U.S., under IRC Section 6038C.	\$10,000 for each taxable year for which the taxpayer fails to provide the required information or fails to maintain the required records. \$10,000 for each 30-day period, when failure continues after 90-day of notification.
			Exceptions - Reasonable cause.	
Failure to Retain Unitary Records Penalty	None	19141.6	Any taxpayer engaged in a unitary business that fails to maintain records relating to unitary combination, apportionment and allocation, and application of federal law.	\$10,000 for each year that the taxpayer fails to maintain or causes another to fail to maintain the required records. If the failure continues beyond 90 days of notice from us, an additional penalty of \$10,000 for each 30-day period is imposed up to a maximum of \$50,000 if the taxpayer's conduct is not willful.

Exceptions - None.

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Accuracy Related Penalty	6662	19164	Any underpayment of tax required to be shown on a return, attributable primarily to negligence or disregard of rules and regulations or a substantial understatement of income tax.	20% of the underpayment of tax. 40% unless certain exceptions apply for amnesty eligible years, which are tax years prior to January 1, 2003.
			Exceptions - The defenses to an accuracy related penalty include (1) substantial authority, (2) adequate disclosure and reasonable basis or (3) reasonable cause and good faith, depending on the grounds for imposing the penalty. In addition, see underlying regulation regarding unitary and business and nonbusiness income determinations.	
Accuracy Related Penalty – Substantial Valuation Misstatement	6662(e)(1)	19164	A substantial valuation misstatement exists when the value (or adjusted basis) of any property claimed on a return is 150% or more of the correct amount. Transactional Penalty – The price reported for any property or services claimed on a return is 200% or more (or 50% or less) of the correct figure. Net Adjustment Penalty – When the transfer price of any property or services increases the taxable income for the taxable year by the lesser of \$5 million or 10% of the taxpayer's gross receipts.	20% of the portion of the underpayment of tax attributable to the misstatement. No penalty imposed unless the portion of the underpayment exceeds \$5,000 (\$10,000 for corporations other than S corporations or personal holding companies).
			Exceptions - Reasonable cause and good faith. (See Treasury Regulation Section 1.6664-4 and 1.6662-6 for special rules.) There is no disclosure exception to this penalty. Treasury Regulation Section 1.6662-5(a). When there is an underpayment due to overstated charitable deduction property, there are special rules for reasonable cause under IRC Section 6664(c) for returns filed after January 1, 2010.	

Accuracy Related Penalty - Increase in Penalty in Case of Gross Valuation Misstatements	6662(h)	19164	A gross valuation misstatement exists if: The value (or adjusted basis) of any property on a return is 200% or more of the correct amount, or The price for any property or service claimed on a return is 400% or more (or 25% or less) of the correct price, or The net Section 482 adjustment exceeds the lesser of \$20 million or 20% of the taxpayer's gross receipts.	40% of the portion of the underpayment of tax attributable to the misstatement. No penalty imposed unless the amount of the underpayment exceeds \$5,000 (\$10,000 for corporations other than S corporations or personal holding companies).
			Exceptions - Reasonable cause and good faith. (See Treasury Regulation Section 1.6664-4 and 1.6662-6(d).) There is no disclosure exception to this penalty. Treasury Regulation Section 1.6662-5(a). When there is an underpayment due to overstated charitable deduction property, there are special rules for reasonable cause under IRC Section 6664(c) for returns filed after January 1, 2010.	

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Fraud Penalty	6663	19164	When there is clear and convincing evidence to prove that some part of the underpayment of tax was due to civil fraud. Such evidence must show the taxpayer's intent to evade tax that the taxpayer believed to have owed.	75% of the underpayment attributable to civil fraud.
Exceptions - Reasonable cause and good faith.				
Reportable Transaction Accuracy Related Penalty - Disclosed Reportable Transaction	6662A	19164.5	Any disclosed reportable transaction understatement for tax years beginning on or after January 1, 2005.	20% of the understatement attributed to the reportable or listed transaction if the transaction is adequately disclosed on the return.
Exceptions - Chief Counsel relief for reportable transactions other than listed transactions. The standards in R&TC Section 19772 apply.				
Reportable Transaction Accuracy Related Penalty - Undisclosed Reportable Transaction	6662A(c)	19164.5	Any undisclosed reportable transaction understatement for tax years beginning on or after January 1, 2005.	30% of the understatement attributed to the reportable or listed transaction if the transaction is not adequately disclosed on the return.
Exceptions - Chief Counsel relief for reportable transactions other than listed transactions. The standards in R&TC Section 19772 apply.				

Preparer Penalty	6694(a)(1)	19166(a)	When a preparer completes a return or claim for refund that results in the taxpayer's understatement based on an unreasonable position and the preparer knew or reasonably should have known of the unreasonable position.	Greater of: \$250 or 50% of income derived (or to be derived) by the tax preparer with respect to each return or claim.
			Exceptions - The preparer can avoid the penalty (1) if the position is adequately disclosed and has a reasonable basis; (2) if the position is not disclosed and is not a tax shelter and there is substantial authority for the position; or (3) for a tax shelter transaction defined in IRC Section 6662(d) or a reportable transaction under IRC Section 6011, if the preparer reasonably believes that the position is more-likely-than-not correct. Also reasonable cause and good faith. If preparer pays at least 15% of the penalty within 30 days of the bill and files a claim for refund, the preparer may file an action in court within 30 days of the claim denial or deemed denial.	

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Preparer Penalty - Reportable Transactions, Listed Transactions or Gross Misstatements	6694	19166(b)(2)	When a preparer completes a return or claim for refund that results in the taxpayer's understatement based on an undisclosed reportable transaction, a listed transaction, or a gross misstatement.	\$1,000 or 50% of the income derived (or to be derived) with respect to each return or claim.
			Exceptions - Standard to avoid the penalty is more-likely-than-not. If preparer pays at least 15% of the penalty within 30 days of the bill and files a claim for refund, the preparer may file an action in court within 30 days of the claim denial or deemed denial.	
Understatement of a Taxpayer's Liability by Tax Preparer - Willful or Reckless Conduct	6694(b)	19166(a)	If the understatement of the taxpayer's tax is due to the preparer's willful attempt to understate the liability or any reckless or intentional disregard of rules or regulations.	The greater of \$5,000 or 50% of the income derived (or to be derived) with respect to each return or claim.
			Exceptions - A preparer is not considered to have recklessly or intentionally disregarded a rule or regulation if the position has a reasonable basis and is adequately disclosed. If a regulation is at issue, there must be a good faith challenge. If the position is contrary to a revenue ruling or notice, the substantial authority standard applies. The same rules of paying 15% and filing a claim and suit in court apply.	
Additional Penalties - Failure to Furnish Copy	6695(a)	19167(a)	Failure to furnish a completed copy of return or claim.	\$50 per failure, not to exceed \$25,000 during any calendar year.

to Taxpayer			Exceptions - Reasonable cause and not willful neglect.	
Additional Penalties - Failure to Furnish Identifying Number	6695(c)	19167(b)	Failure to include on a return or claim the identifying number of the preparer, employer or both.	\$50 per failure, not to exceed \$25,000 during any calendar year.
			Exceptions - Reasonable cause and not willful neglect.	
Additional Penalties - Failure to Retain Copy or List	6695(d)	19167(c)	Failure to retain a completed copy of a return or claim for 3 years or a list with the taxpayer's name and identifying number and make the return or list available for inspection by FTB.	\$50 per failure, not to exceed \$25,000 during any calendar year.
			Exceptions - Reasonable cause and not willful neglect.	

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Additional Penalties - Failure to Register as a Tax Preparer with California Tax Education Council (CTEC)	None	19167(d)(1) and (2)	Failure to register with the CTEC.	\$2,500 for first failure to register. \$5,000 for other than first failure.
			Exceptions - Reasonable cause and not willful neglect. The penalty may be waived if the preparer provides proof of registration to us within 90 days of mail date of notice. Certain persons are exempt from the requirement to register, such as licensed certified public accountants (CPA) and licensed attorneys.	
Negotiation of Taxpayer's Check by Tax Preparer	6695(f)	19169, 20645.7	If the tax preparer endorses or otherwise negotiates a check for the refund of tax that is issued to a taxpayer, if the person was the preparer of the return or claim that gave rise to the refund check.	\$250 for each endorsement or negotiation of a check.
			Exceptions - The preparer will not be considered to have endorsed a check solely as a result of putting the taxpayer's name to a check for the purpose of depositing the check into the taxpayer's account, if authorized by the taxpayer.	
Failure to File Electronically	None	19170	If a preparer that is subject to R&TC Section 18621.9 fails to file returns electronically.	\$50 for each failure.
			Exceptions - Reasonable cause and not willful neglect. Reasonable cause can be established by the taxpayer electing not to file electronically.	

Failure of Partnership to Comply with Filing Requirements	6698	19172	<p>If a partnership: Fails to file a timely return (FTB 565 <i>Partnership Return of Income</i>/ FTB 568, <i>Limited Liability Return of Income</i>), including any extensions, or</p> <p>Files a return (FTB 565/568) that fails to include information required under R&TC Section 18633 or 18633.5.</p>	\$18 multiplied by the number of persons who were partners/members during any part of that taxable year for each month during which that failure continues, not to exceed 12 months.
			Exceptions - Reasonable cause.	

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Failure of S Corporation to Comply with Filing Requirements	6699	19172.5	<p>If an S Corporation: Fails to file a timely return, including extensions, or</p> <p>Files a return that fails to include information required under R&TC Section 18601.</p>	\$18 multiplied by the number of persons who were shareholders during any part of that taxable year for each month during which that failure continues, not to exceed 12 months.
			Exceptions - Reasonable cause.	
Failure to Comply With Request to Provide Lists - Reportable Transactions	6708	19173(a)	<p>Failing to provide lists of advisees with respect to reportable transactions (other than a listed transaction) to FTB within 20 business days after FTB requests the list.</p>	\$10,000 for each day of such failure after the 20th business day.
			Exceptions - Chief Counsel relief for reportable transactions other than listed transactions.	
Failure to Comply With Request - Material Advisors With Respect to Listed Transactions	None	19173(b)	<p>Material advisors who fail to meet the requirements of R&TC Section 18648(d)(1) with respect to a listed transaction.</p>	\$100,000 or 50% of gross income that the material advisor derived from that activity whichever is greater.
			Exceptions - The penalty does not apply if it is shown that the additional information required was not identified in our notice prior to the date the transaction/shelter was entered into. No Chief Counsel review for listed transactions.	
Failure to Report Personal Service Remuneration	None	19175	<p>Any person or entity who fails to report amounts paid as remuneration for personal services may be liable for a penalty.</p>	<p>The maximum personal income tax rate multiplied by the unreported amounts paid as remuneration for personal services.</p> <p>In addition, at our discretion, we may disallow the deduction for amounts paid as remuneration.</p>
			Exceptions - None.	

Statement That Results in Under-Withholding	6682	19176	Statement that results in a decrease in amounts deducted and withheld, if there was no reasonable basis for the statement.	\$500 for the statement.
			Exceptions - Penalty may be waived if the tax paid by the individual for the taxable year is equal to or less than the sum of both certain credits allowed and payments of estimated tax.	

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Promotion of Abusive Tax Shelter	6700	19177	Any person who engages in the organization of, or sale of any interest in, a partnership or other entity, an investment plan or arrangement, or any other plan or arrangement, if the person makes, furnishes, or causes another person to make or furnish: A false or fraudulent tax benefits statement as to a material matter; or A gross valuation overstatement as to a material matter.	\$1,000 or 100% of the gross income derived (or to be derived) by the person from the activity whichever is less. If the activity on which the penalty is imposed involves a false or fraudulent statement as to any matter pertaining to the tax shelter plan or arrangement, the penalty is 50% of the gross income the promoter derived (or was to derive) from promoting the activity.
			Exceptions - If a penalty is imposed with respect to a gross valuation overstatement, the penalty may be waived on a showing that there was a reasonable basis for the valuation and the valuation was made in good faith.	
Aiding and Abetting Understatement of Tax Liability	6701	19178	Aiding and abetting understatement of tax.	\$1,000. \$10,000 if the tax liability relates to a corporation.
			Exceptions - None.	
Filing Frivolous Return	6702(a)	19179(a) and (b)	Filing a frivolous return.	\$5,000 if the return does not contain sufficient information or is based on a frivolous position or reflects an attempt to delay or impede administration of the tax laws.
			Exceptions - Chief Counsel relief.	
Frivolous Submissions	6702(b)	19179(d)	Filing a specified frivolous submission.	\$5,000 for "specified frivolous submissions."
			Exceptions - Chief Counsel relief.	

Failure to Comply With Original Issue Discount Reporting Requirements	6706	19181	Failing to comply with original issue discount reporting requirements.	<p>\$50 for each failure to show information on debt instrument.</p> <p>1% of the aggregate issue price of each issue, up to a maximum of \$50,000 for each issue for failure to furnish information to taxing agency.</p>
			Exceptions - Reasonable cause and not willful neglect.	

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Failure to Furnish Information Regarding Reportable Transaction	6707	19182	A material advisor who fails to file a return with respect to any reportable transaction before the date prescribed or who files false or incomplete information with respect to such transactions.	\$50,000; for listed transactions, equal to the greater of: \$200,000 or 50% (or 75% if failure is intentional) of the gross income derived by such a person.
			Exceptions - Penalty will not apply if it is shown that the additional required information was not identified in our notice issued prior to the date of the transaction. Chief Counsel relief for reportable transactions other than listed transactions.	
Failure to Disclose Quid Pro Quo Contributions	6714	19182.5	For each contribution where the organization fails to make the required disclosure.	\$10 for each contribution, but the total penalty with respect to a particular fundraising event or mailing shall not exceed \$5,000.
			Exceptions - Reasonable cause. No penalty imposed if requirements under IRC Section 6115 are met.	
Failure to File Correct Information Return	6652, 6721-6724	19183(a)	Failing to file information returns or failure to include all required information.	<p>\$50 for failure to file correct information returns, with respect to which such a failure occurs.</p> <p>Shall not exceed \$250,000 during any calendar year;</p> <p>\$100,000 for persons with gross receipts of not more than \$5 million.</p> <p>Higher penalties (without reduction for correction) apply in the case of intentional disregard, depending on type of information return.</p>
			Exceptions - De minimis failure exception. Reasonable cause and not willful neglect.	

Failure to File Correct Information Return	6721(b)(1)	19183(a)	Reduction in failure to file correct information return penalty when corrected within 30 days.	\$15 for failure to file correct information returns, with respect to which such a failure occurs. Shall not exceed \$75,000 during any calendar year. \$25,000 for persons with gross receipts of not more than \$5 million.
			Exceptions - Reasonable cause and not willful neglect.	
Failure to File Correct Information Return	6721(b)(2)	19183(a)	Reduction in failure to file correct information return penalty when corrected on or before August 1.	\$30 for failure to file correct information returns, with respect to which such a failure occurs. Shall not exceed \$150,000 during any calendar year. \$50,000 for persons with gross receipts of not more than \$5 million.
			Exceptions - Reasonable cause and not willful neglect.	

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Failure to File Correct Information - Failure to Furnish Correct Payee Statements	6722(a)	19183(b)(1)	Failure to furnish correct payee statements.	\$50 for each statement, up to a maximum of \$100,000 for each calendar year. \$100, or, if greater, 5% or 10% of the aggregate amount of the items required to be reported correctly, depending on the type of return required, with respect to each such failure for intentional disregard. The \$100,000 limitation in IRC Section 6722(a) shall not apply.
			Exceptions - Reasonable cause and not willful neglect.	
Failure to File Correct Information - Failure to Comply With Other Information Reporting Requirements	6723	19183(c)	Failure to comply with other information reporting requirements.	\$50 for each such failure, up to a maximum of \$100,000 for each calendar year.
			Exceptions - Reasonable cause and not willful neglect.	
Failure to File Correct Information - Failure to Provide Written Explanation to Recipients of Distributions Eligible for Rollover Treatment.	None	19183(e)	Failure to provide written explanation to recipients of distributions eligible for rollover treatment pursuant to IRC Section 402(f).	\$10 for each failure, up to a maximum of \$5,000 for each calendar year after notice and demand.
			Exceptions - Reasonable cause and not willful neglect.	

Failure to File Report Regarding Tax Deferred Savings Accounts	6693	19184	Failure to file report regarding tax deferred savings accounts.	\$50 for each failure.
			Exceptions - Reasonable cause.	

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Failure to File Report Regarding Tax Deferred Savings Accounts - Overstatement as to Amount Designated Nondeductible Contributions	6693	19184(b)(1)(B)	Overstating the amount designated as nondeductible contributions for any taxable year.	\$100 for each overstatement.
			Exceptions - Reasonable cause.	
Failure to File Report Regarding Tax Deferred Savings Accounts - Failure to File a Form Required for Nondeductible Contributions to Individual Retirement Accounts (IRA)	6693	19184(b)(2)	Failure to file a form required for nondeductible contributions to IRAs.	\$50 for each failure.
			Exceptions - Reasonable cause.	
Substantial and Gross Valuation Misstatements on Appraisal	6695A	19185	Knowingly preparing an appraisal to be used in connection with a return or claim and the claimed value results in a substantial valuation misstatement, or gross valuation misstatement.	For returns or submissions filed on or after January 1, 2011: 125% of gross income from the preparation of the appraisal. Or, if less: 10% of the amount of underpayment attributable to misstatement, but not less than \$1,000.

			Exceptions - Established value in the appraisal was more likely than not the proper value.	
Fraudulent Identification of Exempt Use Property	6720B	19186	Knowingly misidentifying applicable property (charitable deduction property) as having exempt use.	\$10,000.
			Exceptions - None.	

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Financial Institution Record Match (FIRM)	None	19266(g)	Any financial institution that willfully fails to comply with rules and regulations for the administration of delinquent tax collections.	\$50 for each record not provided up to \$100,000 per calendar year.
			Exceptions - Reasonable cause.	
Suspension or Disbarment From Practice Before FTB	None	19523.5	Failure to notify the Franchise Tax Board within 45 days of the issuance of a final order disbaring or suspending the person to practice.	\$5,000.
			Exceptions - None.	
Failure to Provide Information Concerning State Licenses Penalty	None	19528	Licenses failing to provide identification numbers upon demand.	\$100 after 30-day notice and demand.
			Exceptions - None.	
Frivolous Proceedings; Failure to Exhaust Administrative Remedies	6673	19714	Taxpayer's action at the State Board of Equalization (BOE) or in court that was instituted or maintained by the taxpayer for delay, or that the position was frivolous or groundless, or that administrative remedies were not pursued.	Not more than \$5,000.
			Exceptions - None.	
Business Conducted After Suspension or Forfeiture of Corporate Rights	None	19719	Anyone who attempts or purports to exercise the powers, rights, and privileges of a corporation that has been suspended or forfeited.	Minimum \$250 and not exceeding \$1,000.
			Exceptions - Not applicable to any insurer or insurer's counsel.	

Failure to Include Information on Reportable Transactions	6707A	19772	Failure to include reportable transactions information with a return.	\$15,000, \$30,000 if listed transaction.
			Exceptions - Chief Counsel relief only for reportable transactions other than listed transactions.	

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Noneconomic Substance Transaction Understatement	6662(b)(6) and (i)	19774	Understatement of a noneconomic substance transaction.	40% of understatement. Reduced to 20% if relevant facts adequately disclosed in the return.
			Exceptions - Chief Counsel relief.	
Interest-Based Penalty for Listed Transactions, et al.	None	19777	Taxpayer contacted by FTB concerning an abusive tax avoidance transaction.	100% of the interest payable for the period beginning on the due date of the return and ending on the date the NPA is mailed.
			Exceptions - None.	
Amnesty Program Interest Penalties	None	19777.5	An addition to tax for each tax year that was eligible for amnesty, but amnesty was not requested, and there was an unpaid amount due on March 31, 2005, (i.e., 50% Interest-Based penalty). The penalty is also imposed where FTB mails a notice of proposed assessment or a notice of tax due or where a taxpayer self assesses additional tax for an amnesty eligible tax year after the end of the amnesty period (i.e., Post-Amnesty Penalty).	The 50% Interest-Based Penalty is calculated as an amount equal to fifty percent of the interest that accrued on the unpaid daily balance from the original due date of the tax to March 31, 2005. The Post-Amnesty Penalty is calculated as an amount equal to fifty percent of the interest computed on the additional amount from the original due date of the tax year to March 31, 2005.
			Exceptions - No claim for refund allowed except on the grounds that the penalty was not properly calculated.	
150% Interest Penalty	None	19778	Amended return filed after April 15, 2004, but before taxpayer is contacted by FTB regarding a potentially abusive tax shelter.	Interest accrues at a rate of 150% of the adjusted annual rate.
			Exceptions - None.	
Relief From Contract Voidability	None	23305.1	The period for which relief from voidability of the contract is granted.	\$100 daily for each day of the period for which relief from voidability is granted, not to exceed a total penalty equal to the amount of the tax for the period for which relief is requested.
			Exceptions - None.	

Failure of Exempt Organizations and Trusts to Pay Filing Fee	6033, 6072(e)	23772(a)(3)	Failure to pay fee on or before due date (determined with regard to any extension of time for filing) for filing exempt organization or trust return.	Filing fee increased to \$25.
Exceptions - Reasonable cause.				

Penalty Name	IRC Section	R&TC Section	Penalty Reason	Computation
Failure of Exempt Organizations and Trusts to File Annual Information Return	6033, 6072(e)	23772(c)(1)	The period in which the exempt organization or trust fails to file a return after the due date.	On notice and demand \$5 for each month or fraction thereof during which the failure to file a return continues, but the total amount imposed on any organization for the failure to file shall not exceed \$40.
			Exceptions - Reasonable cause.	
Failure of Private Foundation to File on Demand	6033, 6072(e)	23772(c)(2)	The period in which a private foundation fails to file a return after receiving a demand for a return from FTB.	\$5 for each month or fraction thereof during which the failure to file a return continues, but the total amount imposed on any organization for the failure to file shall not exceed \$25 in addition to penalty provided in 23772(c)(1).
			Exceptions - Reasonable cause.	
Real Estate Investment Trust (REIT) Failure to Comply With Ascertainment of Ownership Rules	857(f)	24872.7	Failure to comply with federal regulations to ascertain ownership rules.	Penalty imposed only, and in same amount, if penalty is imposed for federal purposes: \$25,000. Intentional disregard is \$50,000. Failure to comply after notice an additional penalty of either \$25,000 or \$50,000.
			Exceptions – Reasonable cause and not willful neglect, as	
Failure to Supply Information Penalty	None	25112	Taxpayer engaged in a unitary business that fails to supply requested information.	\$1,000 for each taxable year. Additional penalty of \$1,000 for each 30-day period up to \$24,000 if failure continues for more than 90 days after we notify the taxpayer.

i www.irs.gov

ii See www.irs.gov/taxtopics/tc757.html

iii Courtesy of the Franchise Tax Board (FTB”) Use this chart for reference purposes only. We list penalty codes by Revenue and Taxation Code (R&TC) sections and reference comparable Internal Revenue Code (IRC) sections. These penalties reflect the law as enacted on September 21, 2011, for taxable years beginning on or after January 1, 2011.