

Part III - Administrative, Procedural, and Miscellaneous

New Penalty Section 6707A and Rescission Authority

Notice 2005-11

The purpose of this notice is to alert taxpayers to new section 6707A of the Internal Revenue Code. This notice announces that the Internal Revenue Service and the Treasury Department will issue regulations under section 6707A, which will apply to returns and statements the due date for which is after October 22, 2004, and provides guidance regarding the imposition and rescission of penalties under section 6707A. This notice also invites comments from the public regarding rules and standards relating to section 6707A.

BACKGROUND AND PRIOR LAW

Section 6011 and the regulations thereunder require a taxpayer that has participated in a reportable transaction to disclose certain information with respect to the reportable transaction with its tax return. Section 1.6011-4(b) of the Income Tax Regulations describes six categories of reportable transactions. One category of reportable transactions is a transaction that is the same as, or substantially similar to, one of the types of transactions that the Internal Revenue Service has determined to be a tax avoidance transaction and identified by notice, regulation, or other form of published guidance as a “listed transaction.” Section 1.6011-4(b)(2).

Section 1.6011-4(d) requires that a taxpayer file a disclosure statement on Form 8886, Reportable Transaction Disclosure Statement, for each reportable transaction in which the taxpayer participated. Section 1.6011-4(e)(1) provides that a reportable transaction disclosure statement is due when the taxpayer files an original or amended return that reflects the taxpayer's participation in a reportable transaction. The taxpayer also must send a copy of the disclosure statement to the IRS Office of Tax Shelter Analysis (OTSA) at the same time that the taxpayer first files a disclosure statement with a return. In certain circumstances, a taxpayer may be deemed to have satisfied its disclosure obligations by filing Schedule M-3, Net Income (Loss) Reconciliation for Corporations With Total Assets of \$10 Million or More, as provided by Rev. Proc. 2004-45, 2004-31 I.R.B. 140 (August 2, 2004).

Section 6011 also requires the disclosure of listed transactions under section 20.6011-4 of the Estate Tax Regulations, section 25.6011-4 of the Gift Tax Regulations, section 31.6011-4 of the Employment Tax Regulations, section 53.6011-4 of the Foundation and Similar Excise Tax Regulations, section 54.6011-4 of the Pension Excise Tax Regulations, and section 56.6011-4 of the Public Charity Tax on Excess Lobbying Expenditure Regulations.

Prior to the enactment of section 6707A, there was no monetary penalty for the failure by a taxpayer to disclose a reportable transaction.

THE AMERICAN JOBS CREATION ACT OF 2004

The American Jobs Creation Act of 2004, P.L. 108-357, 118 Stat. 1418 (the Act) was enacted on October 22, 2004. Section 811 of the Act added section 6707A to the

Code to provide a monetary penalty for the failure to include on any return or statement any information required to be disclosed under section 6011 with respect to a reportable transaction.

Section 6707A(b)(1) provides that the penalty for failure to include information with respect to a reportable transaction, other than a listed transaction, is \$10,000 in the case of a natural person, and \$50,000 in any other case. Section 6707A(b)(2) provides that the penalty for failure to include information with respect to a listed transaction is \$100,000 in the case of a natural person, and \$200,000 in any other case.

Section 6707A(d)(1) grants the Commissioner authority to rescind all or a portion of any penalty imposed by section 6707A if (1) the violation relates to a reportable transaction that is not a listed transaction and (2) rescission of the penalty would promote compliance with the requirements of the Code and effective tax administration.

Section 6707A(d)(2) provides that the Commissioner's determination whether to rescind the penalty may not be reviewed in any judicial proceeding. The legislative history to section 6707A provides that "the IRS Commissioner or his delegate can rescind (or abate) the penalty." H.R. Conf. Rep. No. 755, 108th Cong., 2d Sess. at 373 (2004).

Section 6707A(e) also provides that a person that is required to file periodic reports under section 13 or 15(d) of the Securities Exchange Act of 1934, or required to be consolidated with another person for purposes of those reports, must disclose the requirement to pay the following penalties in the reports to the Securities and Exchange Commission for the periods specified by the Secretary: (1) the penalty under section

6707A for failure to disclose a listed transaction; (2) the 30 percent penalty under section 6662A for an understatement attributable to an undisclosed listed transaction or undisclosed reportable avoidance transaction; and (3) the 40 percent penalty under section 6662 for a gross valuation misstatement if the 30 percent penalty under section 6662A would have applied, but for the application of section 6662A(e)(2)(c)(ii). Section 6707A(e) also provides that the failure to make a disclosure on reports filed with the Securities and Exchange Commission as required by the Secretary shall be treated as a failure to include information with respect to a listed transaction for which the penalty under section 6707A applies.

The penalty under section 6707A is in addition to any other potentially applicable penalties, including accuracy-related penalties under sections 6662 and 6662A. The penalty under section 6707A will be imposed regardless of whether the transaction results in an underpayment of tax.

Section 6707A is effective for returns and statements the due date for which is after October 22, 2004.

INTERIM GUIDANCE

The Internal Revenue Service and the Treasury Department intend to issue regulations providing rules under section 6707A. Because section 6707A is effective for returns and statements the due date for which is after October 22, 2004, however, the Service and Treasury are providing the following interim guidance regarding the imposition and rescission of penalties under section 6707A. These interim rules will apply until further guidance is issued.

A. Imposition of the Section 6707A Penalty

The Service will impose a penalty under section 6707A with respect to each failure to disclose a reportable transaction within the time and in the form and manner provided by section 6011 and the regulations thereunder. Accordingly, a taxpayer will be subject to a penalty under section 6707A for: (1) the failure to attach a reportable transaction disclosure statement to an original or amended return; or (2) the failure to provide a copy of a disclosure statement to OTSA, if required. A taxpayer that fails to attach a reportable transaction disclosure statement to an original or amended return and fails to provide a copy of a required disclosure statement to OTSA will be subject to a single penalty under section 6707A. The following examples illustrate this provision:

Example 1: Taxpayer T was required to attach a Form 8886 to its original return for the 2005 taxable year and to send a copy of the Form 8886 to OTSA at the time it filed its original return. T failed to attach the Form 8886 to its return and failed to send a copy of the Form 8886 to OTSA. Taxpayer T is subject to a penalty under section 6707A for a failure to disclose because Taxpayer T failed to comply with both of the disclosure requirements. A penalty under section 6707A also would apply if T had failed to comply with either of the two requirements.

Example 2: Same as Example 1, except that T subsequently filed an amended return for 2005 that reflects Taxpayer T's participation in the reportable transaction. Taxpayer T failed to attach a Form 8886 to the amended return as required by section 1.6011-4(e)(1). Accordingly, Taxpayer T is subject to an additional penalty under section 6707A for failing to disclose a reportable transaction.

The penalty under section 6707A applies to each failure to provide a disclosure statement that is required to be attached to an original or amended return filed after October 22, 2004 (with a copy sent to OTSA, if required), regardless of whether the original return was due on or before October 22, 2004. Under section 1.6011-4(e)(1), a

reportable transaction disclosure statement is due upon the filing of a return or amended return reflecting a taxpayer's participation in a reportable transaction.

Accordingly, a penalty under section 6707A will not be imposed until a taxpayer fails to provide the required disclosure statement with an original or amended return, or fails to provide a copy to OTSA, if applicable, even if the return is filed after the due date. In addition, a penalty under section 6707A will not be imposed if the disclosure statement is attached to a return that is filed after the due date for filing the return unless the taxpayer fails to provide a copy of the disclosure statement to OTSA, if applicable.

B. Rescission Authority

If it has been determined that a taxpayer failed to disclose a reportable transaction and a penalty is imposed under section 6707A, section 6707A(d) authorizes the Commissioner to rescind all or any portion of a penalty imposed under section 6707A only if (1) the violation relates to a reportable transaction other than a listed transaction and (2) rescission of the penalty would promote compliance with the requirements of the Code and effective tax administration. In determining whether rescission would promote compliance with the requirements of the Code and effective tax administration, the Commissioner (or his delegate) will take into account all of the relevant facts and circumstances, including: (1) whether the taxpayer has a history of complying with the tax laws; (2) whether the violation results from an unintentional mistake of fact; and (3) whether imposing the penalty would be against equity and good conscience. The Commissioner's determination whether to rescind a penalty in whole or in part is not reviewable by the IRS Appeals Division or any court.

REQUEST FOR COMMENTS

The Service and Treasury invite interested persons to submit comments regarding rules and standards relating to section 6707A, including the factors that should be considered in exercising the rescission authority under section 6707A(d). Comments are also requested on how voluntary, but untimely disclosures (e.g., if a taxpayer failed to make a required disclosure upon filing a return, but subsequently submits the required disclosure statement) should be treated in applying the section 6707A penalty. Comments are encouraged to be submitted by February 28, 2005, to: Internal Revenue Service, CC:PA:LPD:PR (Notice 2005-11), room 5203, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044. Submissions also may be hand delivered Monday through Friday between the hours of 8 a.m. and 4 p.m. to: CC:PA:LPD:PR (Notice 2005-11), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue N.W., Washington, DC. Alternatively, taxpayers may submit electronic comments directly to the IRS e-mail address:

notice.comments@irs.counsel.treas.gov.

DRAFTING INFORMATION

The principal author of this notice is Matthew S. Cooper of the Office of Associate Chief Counsel (Procedure and Administration), Administrative Provisions and Judicial Practice Division. For further information regarding this notice contact Matthew S. Cooper at 202-622-4940 (not a toll-free call).