

[4830-01-p]

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 301

[TD 9545]

RIN 1545-BG75

Interest and Penalty Suspension Provisions Under Section 6404(g) of the Internal Revenue Code

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Final regulations and removal of temporary regulations.

SUMMARY: This document contains final regulations regarding the suspension of interest, penalties, additions to tax, or additional amounts under section 6404(g) of the Internal Revenue Code. The final regulations explain the general rules for suspension and exceptions to those general rules, and incorporate a special rule from Notice 2007-93, 2007-48 IRB 1072, regarding the effective date of the changes to section 6404(g) made by the Small Business and Work Opportunity Tax Act of 2007. The final regulations affect taxpayers who file timely individual income tax returns and who fail to receive notification from the IRS of additional tax liability within the time period prescribed by section 6404(g).

DATES: Effective Date: These regulations are effective on **[INSERT DATE OF PUBLICATION OF THIS DOCUMENT IN THE FEDERAL REGISTER]**.

Applicability date: Section 301.6404-4(a)(5) applies to notices under section 6404(g)(1)(A) that are provided by the IRS on or after November 26, 2007, and that relate to individual Federal income tax returns that were timely filed before that date.

FOR FURTHER INFORMATION CONTACT: Nathan Rosen, (202) 622-3630 (not a toll-free number).

SUPPLEMENTARY INFORMATION:

Background

This document amends the Procedure and Administration Regulations (26 CFR part 301) by adding rules relating to the suspension of interest, penalties, additions to tax, or additional amounts under section 6404(g). Section 6404(g) was added to the Code by section 3305 of the Internal Revenue Service Restructuring and Reform Act of 1998, Public Law 105-206 (112 Stat. 685, 743) (RRA 98), effective for taxable years ending after July 22, 1998. Section 6404(g) was amended by section 903(c) of the American Jobs Creation Act of 2004, Public Law 108-357 (118 Stat. 1418, 1652) (AJCA), enacted on October 22, 2004, and by section 303 of the Gulf Opportunity Zone Act of 2005, Public Law 109-135 (119 Stat. 2577, 2608-09) (GOZA), enacted on December 21, 2005. Section 8242 of the Small Business and Work Opportunity Tax Act of 2007, Public Law 110-28 (121 Stat. 190, 200), extended the eighteen-month period within which the IRS can, without suspension of interest, contact a taxpayer regarding possible adjustments to the taxpayer's liability to thirty-six months, effective for notices provided after November 25, 2007.

On June 21, 2007, the Treasury Department and the IRS published in the **Federal Register** a notice of proposed rulemaking and notice of public hearing (REG-149036-04), 2007-34 IRB 411 (72 FR 34199), corrected at (72 FR 41045) (July 26, 2007), under section 6404(g). The proposed regulations provided guidance regarding the suspension of interest, penalties, additions to tax, or additional amounts under section 6404(g). No comments were received in response to the notice of proposed rulemaking and no public hearing was requested or held. Therefore, the proposed

regulations are adopted as amended by this Treasury decision. The revisions are discussed in this preamble.

On June 21, 2007, the Treasury Department and the IRS also published a separate set of temporary regulations (TD 9333), 2007-33 IRB 350 (72 FR 34176), corrected at 72 FR 41022, and a notice of proposed rulemaking by cross-reference to temporary regulations (REG-149036-04), 2007-33 IRB 365 (72 FR 34204), corrected at 72 FR 41045, under section 6404(g) concerning the suspension of interest, penalties, additions to tax, or additional amounts with respect to listed transactions or undisclosed reportable transactions. Those temporary and proposed regulations are not the subject of this Treasury decision, and were published as final regulations on June 16, 2010 (TD 9488), 2010-28 IRB 51 (75 FR 33992).

Explanation of Revisions

The final regulations include new §301.6404-4(a)(5) to address the matters that were the subject of Notice 2007-93. In general, section 6404(g) provides that if an individual taxpayer files a Federal income tax return on or before the due date for that return (including extensions), and if the IRS does not timely provide a notice to that taxpayer specifically stating the taxpayer's liability and the basis for that liability, then the IRS must suspend any interest, penalty, addition to tax, or additional amount with respect to any failure relating to the return that is computed by reference to the period of time the failure continues and that is properly allocable to the suspension period. A notice is timely if provided before the close of the 18-month period (36-month period, in the case of notices provided after November 25, 2007, subject to the provisions of §301.6404-4(a)(5)) beginning on the later of the date on which the return is filed or the due date of the return without regard to extensions. The suspension period begins on the day after the close of the 18-month period (or 36-month period) and ends 21 days

after the IRS provides the notice. This suspension rule applies separately with respect to each item or adjustment.

Notice 2007-93 set forth a special rule for notices under section 6404(g)(1) that (i) are provided by the IRS on or after November 26, 2007, and (ii) relate to individual Federal income tax returns that were timely filed before that date. Under the special rule:

1. If, as of November 25, 2007, the 18-month notification deadline had passed and the IRS had not provided notice to the taxpayer, the suspension described in section 6404(g)(1)(A) would begin on the day after the close of the 18-month period. The suspension would end 21 days after the date on which the notice was provided.

2. In all other cases, the suspension would begin on the day after the close of the 36-month notification period described in section 6404(g)(1)(A) and end 21 days after the date on which the notice was provided.

The final regulations incorporate substantially without change the special rule of Notice 2007-93 at §301.6404-4(a)(5).

In addition, §301.6404-4(b)(2) was revised to remove the reference to section 6501(c)(1) and the meaning of fraud, as fraud is not defined in section 6501(c)(1) but is instead generally described under case law and other guidance. Thus, fraud for purposes of §301.6404-4(b)(2) has the same meaning as that provided in case law and other guidance.

Finally, minor editorial changes were made to clarify the terms of section 6404(g) and to modify a reference to official IRS forms.

Effect on Other Documents

The following publication is obsolete as of **[INSERT DATE OF PUBLICATION OF THIS DOCUMENT IN THE FEDERAL REGISTER]**:

Special Analyses

It has been determined that this Treasury decision is not a significant regulatory action as defined in Executive Order 12866. Therefore, a regulatory assessment is not required. It has also been determined that section 553(b) of the Administrative Procedure Act (5 U.S.C. chapter 5) does not apply to these regulations, and because these regulations do not impose a collection of information on small entities, the Regulatory Flexibility Act (5 U.S.C. chapter 6) does not apply.

Pursuant to section 7805(f) of the Code, the notice of proposed rulemaking preceding these regulations was submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Drafting Information

The principal author of these regulations is Nathan Rosen of the Office of Associate Chief Counsel (Procedure and Administration).

List of Subjects in 26 CFR Part 301

Income taxes, Penalties, Reporting and recordkeeping requirements.

Adoption of Amendments to the Regulations

Accordingly, 26 CFR part 301 is amended as follows:

PART 301--PROCEDURE AND ADMINISTRATION

Paragraph 1. The authority citation for part 301 continues to read in part as follows:

Authority: 26 U.S.C. 7805. * * *

Par. 2. Section 301.6404-0 is amended as follows:

1. Revise the introductory text.
2. Revise entries for §301.6404-4(a) and (b)(1) through (b)(4).

3. Revise entries for §301.6404-4(c) and (d).

The revisions read as follows:

§301.6404-0 Table of contents.

This section lists the paragraphs contained in §§301.6404-1 through 301.6404-4.

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§301.6404-4 Suspension of interest and certain penalties when the Internal Revenue Service does not timely contact the taxpayer.

(a) Suspension.

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(ii) Amended returns that show a decrease in tax liability.

(iii) Amended returns and other documents as notice.

(iv) Joint return after filing separate return.

(3) Separate application.

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(5) Certain notices provided on or after November 26, 2007.

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(iii) Examples.

(8) Providing notice.

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(b) Exceptions.

(1) Failure to file tax return or to pay tax.

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(i) Description.

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* * * * *

(c) Special rules.

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(2) Election under section 183(e).

(i) In general.

(ii) Example.

(d) Effective/applicability date.

§301.6404-0T [Removed]

Par. 3. Section 301.6404-0T is removed.

Par. 4. Section 301.6404-4 is amended as follows:

1. Add paragraphs (a) and (b)(1) through (b)(4).
2. Add paragraph (c).
3. Paragraph (d) is amended by adding a second sentence.

The additions and revisions read as follows:

§301.6404-4 Suspension of interest and certain penalties when the Internal Revenue Service does not timely contact the taxpayer.

(a) Suspension.--(1) In general. Except as provided in paragraph (b) of this section, if an individual taxpayer files a return of tax imposed by subtitle A on or before the due date for the return (including extensions) and the Internal Revenue Service does not timely provide the taxpayer with a notice specifically stating the amount of any increased liability and the basis for that liability, then the IRS must suspend the imposition of any interest, penalty, addition to tax, or additional amount, with respect to any failure relating to the return that is computed by reference to the period of time the failure continues to exist and that is properly allocable to the suspension period. The notice described in this paragraph (a) is timely if provided before the close of the 18-month period (36-month period in the case of notices provided after November 25, 2007, subject to the provisions of paragraph (a)(5)) beginning on the later of the date on which the return is filed or the due date of the return without regard to extensions.

(2) Treatment of amended returns and other documents.--(i) Amended returns filed on or after December 21, 2005, that show an increase in tax liability. If a taxpayer, on or after December 21, 2005, provides to the IRS an amended return or one or more

other signed written documents showing an increase in tax liability, the date on which the return was filed will, for purposes of this paragraph (a), be the date on which the last of the documents was provided. Documents described in this paragraph (a)(2)(i) are provided on the date that they are received by the IRS.

(ii) Amended returns that show a decrease in tax liability. If a taxpayer provides to the IRS an amended return or other signed written document that shows a decrease in tax liability, any interest, penalty, addition to tax, or additional amount will not be suspended if the IRS at any time proposes to adjust the changed item or items on the amended return or other signed written document.

(iii) Amended returns and other documents as notice.--(A) As to the items reported, an amended return or one or more other signed written documents showing that the taxpayer owes an additional amount of tax for the taxable year serves as the notice described in paragraph (a)(1) of this section with respect to the items reported on the amended return.

(B) Example. An individual taxpayer timely files a Federal income tax return for taxable year 2008 on April 15, 2009. On January 19, 2010, the taxpayer mails to the IRS an amended return reporting an additional item of income and an increased tax liability for taxable year 2008. The IRS receives the amended return on January 21, 2010. The amended return will be treated for purposes of this paragraph (a) as filed on January 21, 2010, the date the IRS received it. Pursuant to paragraph (a)(2)(iii) of this section, the amended return serves as the notice described in paragraph (a)(1) of this section with respect to the item reported on the amended return. Accordingly, because the filing of the amended return and the provision of notice occur simultaneously, no suspension of any interest, penalty, addition to tax or additional amount will occur under this paragraph (a) with respect to the item reported on the amended return.

(iv) Joint return after filing separate return. A joint return filed under section 6013(b) is subject to the rules for amended returns described in this paragraph (a)(2). The IRS will not suspend any interest, penalty, addition to tax, or additional amount on a joint return filed under section 6013(b) after the filing of a separate return unless each spouse's separate return, if required to be filed, was timely.

(3) Separate application. This paragraph (a) shall be applied separately with respect to each item or adjustment.

(4) Duration of suspension period. The suspension period described in paragraph (a)(1) of this section begins the day after the close of the 18-month period (36-month period, in the case of notices provided after November 25, 2007, subject to the provisions of paragraph (a)(5)) beginning on the later of the date on which the return is filed or the due date of the return without regard to extensions. The suspension period ends 21 days after the earlier of the date on which the IRS mails the required notice to the taxpayer's last known address, the date on which the required notice is hand-delivered to the taxpayer, or the date on which the IRS receives an amended return or other signed written document showing an increased tax liability.

(5) Certain notices provided on or after November 26, 2007. If the IRS provides the notice described in paragraph (a)(1) of this section to a taxpayer on or after November 26, 2007, and the notice relates to an individual Federal income tax return that was timely filed before that date, the following rules will apply:

(i) Eighteen-month period has closed. If, as of November 25, 2007, the 18-month period described in paragraph (a)(1) of this section has closed and the IRS has not provided the taxpayer with the notice described in that paragraph (a)(1), the suspension described in paragraph (a)(1) of this section will begin on the day after the close of the 18-month period. The suspension will end on the date that is 21 days after the notice is provided.

(ii) All other cases. In all other cases, the suspension described in paragraph (a)(1) of this section will begin on the day after the close of the 36-month period described in that paragraph (a)(1) and end on the date that is 21 days after the notice described in paragraph (a)(1) of this section is provided.

(6) Examples. The following examples, which assume that no exceptions in section 6404(g)(2) to the general rule of suspension apply, illustrate the rules of this paragraph (a).

Example 1. An individual taxpayer timely files a Federal income tax return for taxable year 2005 on April 17, 2006. On December 11, 2007, the taxpayer mails to the IRS an amended return reporting an additional item of income and an increased tax liability for taxable year 2005. The IRS receives the amended return on December 13, 2007. On January 16, 2008, the IRS provides the taxpayer with a notice stating that the taxpayer has an additional tax liability based on the disallowance of a deduction the taxpayer claimed on his original return and did not change on his amended return. The date the amended return was received substitutes for the date that the original return was filed with respect to the additional item of tax liability reported on the amended return. Thus, the IRS will not suspend any interest, penalty, addition to tax, or additional amount with respect to the additional item of income and the increased tax liability reported on the amended return. The suspension period for the additional tax liability based on the IRS's disallowance of the deduction begins on October 17, 2007, so the IRS will suspend any interest, penalty, addition to tax, and additional amount with respect to the disallowed deduction and additional tax liability from that date through February 6, 2008, which is 21 days after the IRS provided notice of the additional tax liability and the basis for that liability. The suspension period in this example begins 18 months after filing the return (not 36 months) because, as of November 25, 2007, the 18-month period beginning on the date the return was filed had closed without the IRS giving notice of the additional liability. Thus, under the rules in paragraph (a)(5) of this section, the suspension period begins 18 months from the April 17, 2006 return filing date.

Example 2. An individual taxpayer files a Federal income tax return for taxable year 2008 on April 15, 2009. The taxpayer consents to extend the time within which the IRS may assess any tax due on the return until June 30, 2013. On December 20, 2012, the IRS provides a notice to the taxpayer specifically stating the taxpayer's liability and the basis for the liability. The suspension period for the liability identified by the IRS begins on April 15, 2012, so the IRS will suspend any interest, penalty, addition to tax, and additional amount with respect to that liability from that date through January 10, 2013, which is 21 days after the IRS provided notice of the additional tax liability and the basis for that liability.

(7) Notice of liability and the basis for the liability.--(i) In general. Notice to the taxpayer must be in writing and specifically state the amount of the liability and the basis for the liability. The notice must provide the taxpayer with sufficient information to identify which items of income, deduction, loss, or credit the IRS has adjusted or proposes to adjust, and the reason for that adjustment. Notice of the reason for the adjustment does not require a detailed explanation or a citation to any Internal Revenue

Code section or other legal authority. The IRS need not incorporate all of the information necessary to satisfy the notice requirement within a single document or provide all of the information at the same time. Documents that may contain information sufficient to constitute notice, either alone or in conjunction with other documents, include, but are not limited to, statutory notices of deficiency; examination reports (for example, Form 4549, *Income Tax Examination Changes* or Form 886-A, *Explanation of Items*); Form 870, *Waiver of Restriction on Assessments and Collection of Deficiency in Tax and Acceptance of Overassessment*; notices of proposed deficiency that allow the taxpayer an opportunity for review in the Office of Appeals (30-day letters); notices pursuant to section 6213(b) (mathematical or clerical errors); and notice and demand for payment of a jeopardy assessment under section 6861.

(ii) Tax attributable to TEFRA partnership items. Notice to the partner or the tax matters partner (TMP) of a partnership subject to the unified audit and litigation procedures of subchapter C of chapter 63 of subtitle F of the Internal Revenue Code (TEFRA partnership procedures) that provides specific information about the basis for the adjustments to partnership items is sufficient notice if a partner could reasonably compute the specific tax attributable to the partnership item based on the proposed adjustments as applied to the partner's individual tax situation. Documents provided by the IRS during a TEFRA partnership proceeding that may contain information sufficient to satisfy the notice requirements include, but are not limited to, a Notice of Final Partnership Administrative Adjustment (FPAA); examination reports (for example, Form 4605-A or Form 886-A); or a letter that allows the partners an opportunity for review in the Office of Appeals (60-day letter).

(iii) Examples. The following examples illustrate the rules of this paragraph (a)(7).

Example 1. During an audit of Taxpayer A's 2005 taxable year return, the IRS questions a charitable deduction claimed on the return. The IRS provides A with a 30-day letter that proposes to disallow the charitable contribution deduction resulting in a deficiency of \$1,000 and informs A that A may file a written protest of the proposed disallowance with the Office of Appeals within 30 days. The letter includes as an attachment a copy of the revenue agent's report that states, "It has not been established that the amount shown on your return as a charitable contribution was paid during the tax year. Therefore, this deduction is not allowable." The information in the 30-day letter and attachment provides A with notice of the specific amount of the liability and the basis for that liability as described in this paragraph (a)(7).

Example 2. Taxpayer B is a partner in partnership P, a TEFRA partnership for taxable year 2005. B claims a distributive share of partnership income on B's Federal income tax return for 2005 timely filed on April 17, 2006. On October 1, 2007, during the course of a partnership audit of P for taxable year 2005, the IRS provides P's TMP with a 60-day letter proposing to adjust P's income by \$10,000. The IRS previously had provided the TMP with a copy of the examination report explaining that the adjustment was based on \$10,000 of unreported net income. On October 31, 2007, P's TMP informs B of the proposed adjustment as required by §301.6223(g)-1(b). By accounting for B's distributive share of the \$10,000 of unreported income from P with B's other income tax items, B can determine B's tax attributable to the \$10,000 partnership adjustment. The information in the 60-day letter and the examination report allows B to compute the specific amount of the liability attributable to the adjustment to the partnership item and the basis for that adjustment and therefore satisfies the notice requirement of paragraph (a). Because the IRS provided that notice to the TMP, B's agent under the TEFRA partnership provisions, within 18 months of the April 17, 2006 filing date of B's return, any interest, penalty, addition to tax, or additional amount with respect to B's tax liability attributable to B's distributive share of the \$10,000 of unreported partnership income will not be suspended under section 6404(g).

(8) Providing notice.--(i) In general. The IRS may provide notice by mail or in person to the taxpayer or the taxpayer's representative. If the IRS mails the notice, it must be sent to the taxpayer's last known address under rules similar to section 6212(b), except that certified or registered mail is not required. Notice is considered provided as of the date of mailing or delivery in person.

(ii) Providing notice in TEFRA partnership proceedings. In the case of TEFRA partnership proceedings, the IRS must provide notice of final partnership administrative adjustments (FPAA) by mail to those partners specified in section 6223. Within 60 days of an FPAA being mailed, the TMP is required to forward notice of the FPAA to those partners not entitled to direct notice from the IRS under section 6223. Certain partners

with small interests in partnerships with more than 100 partners may form a Notice Group and designate a partner to receive the FPAA on their behalf. The IRS may provide other information after the beginning of the partnership administrative proceeding to the TMP who, in turn, must provide that information to the partners specified in §301.6223(g)-1 within 30 days of receipt. Pass-thru partners who receive notices and other information from the IRS or the TMP must forward that notice or information within 30 days to those holding an interest through the pass-thru partner. Information provided by the IRS to the TMP is deemed to be notice for purposes of this section to those partners specified in §301.6223(g)-1 as of the date the IRS provides that notice to the TMP. A similar rule applies to notice provided to the designated partner of a Notice Group, and to notice provided to a pass-thru partner. In the foregoing situations, the TMP, designated partner, and pass-thru partner are agents for direct and indirect partners. Consequently, notice to these agents is deemed to be notice to the partners for whom they act.

(b) Exceptions.--(1) Failure to file tax return or to pay tax. Paragraph (a) of this section does not apply to any penalty imposed by section 6651.

(2) Fraud. Paragraph (a) of this section does not apply to any interest, penalty, addition to tax, or additional amount for a year involving a false or fraudulent return. If a taxpayer files a fraudulent return for a particular year, paragraph (a) of this section may apply to any other tax year of the taxpayer that does not involve fraud. Fraud affecting a particular item on a return precludes paragraph (a) of this section from applying to any other items on that return.

(3) Tax shown on return. Paragraph (a) of this section does not apply to any interest, penalty, addition to tax, or additional amount with respect to any tax liability shown on a return.

(4) Gross misstatement.--(i) Description. Paragraph (a) of this section does not apply to any interest, penalty, addition to tax, or additional amount with respect to a gross misstatement. A gross misstatement for purposes of this paragraph (b) means:

(A) a substantial omission of income as described in section 6501(e)(1) or section 6229(c)(2);

(B) a gross valuation misstatement within the meaning of section 6662(h)(2)(A) and (B); or

(C) a misstatement to which the penalty under section 6702(a) applies.

(ii) Effect of gross misstatement. If a gross misstatement occurs, then paragraph (a) of this section does not apply to any interest, penalty, addition to tax, or additional amount with respect to any items of income omitted from the return and with respect to overstated deductions, even though one or more of the omitted items would not constitute a substantial omission, gross valuation misstatement, or misstatement to which section 6702(a) applies.

* * * * *

(c) Special rules.--(1) Tentative carryback and refund adjustments. If an amount applied, credited or refunded under section 6411 exceeds the overassessment properly attributable to a tentative carryback or refund adjustment, any interest, penalty, addition to tax, or additional amount with respect to the excess will not be suspended.

(2) Election under section 183(e).--(i) In general. If a taxpayer elects under section 183(e) to defer the determination of whether the presumption that an activity is engaged in for profit applies, the 18-month (or 36-month) notification period described in paragraph (a)(1) of this section will be tolled for the period to which the election applies. If the 18-month (or 36-month) notification period has passed as of the date the section 183(e) election is made, the suspension period described in paragraph (a)(4) of this

section will be tolled for the period to which the election applies and will resume the day after the tolling period ends. Tolling will begin on the date the election is made and end on the later of the date the return for the last taxable year to which the election applies is filed or is due without regard to extensions.

(ii) Example. In taxable year 2007, taxpayer begins training and showing horses. On January 4, 2011, the taxpayer elects under section 183(e) to defer the determination of whether the horse-related activity will be presumed (under section 183(d)) to be engaged in for profit. Accordingly, under section 183(e)(1), a determination of whether the section 183(d) presumption applies will not occur before the close of the 2013 taxable year. Assume that in 2014, the IRS is considering issuing a notice of deficiency for taxable year 2009 regarding tax deductions claimed for the horse-related activity. Pursuant to paragraph (c)(2)(i) of this section, the 36-month notification period under paragraph (a)(1) of this section will be tolled with respect to taxable year 2009 for the period to which the section 183(e) election applies. This tolling of the notification period begins on January 4, 2011 (the date the taxpayer made the section 183(e) election) and ends on the later of April 15, 2014, or the date the taxpayer's return for taxable year 2013 is filed.

(d) Effective/applicability date. * * * Paragraphs (a), (b)(1) through (b)(4), and (c) are effective on **[INSERT DATE OF PUBLICATION OF THIS DOCUMENT IN THE FEDERAL REGISTER]**.

Steven T. Miller

Deputy Commissioner for Services and Enforcement.

Approved: July 15, 2011

Emily S. McMahon

Acting Assistant Secretary of the Treasury (Tax Policy)

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