



DEPARTMENT OF THE TREASURY  
INTERNAL REVENUE SERVICE  
WASHINGTON, D.C. 20224

OFFICE OF  
CHIEF COUNSEL

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INTERNAL REVENUE SERVICE NATIONAL OFFICE SERVICE CENTER ADVICE

MEMORANDUM FOR ASSISTANT DISTRICT COUNSEL, KANSAS-MISSOURI  
DISTRICT, KANSAS CITY  
CC:MSR:KSM:KCY

FROM: Acting Assistant Chief Counsel (Income Tax & Accounting)  
CC:DOM:IT&A

SUBJECT: Significant Service Center Advice

This responds to your request for Significant Advice dated July 26, 1999, in connection with a question posed by the Kansas City Service Center. The Service Center requested guidance with respect to the increase of the failure to pay penalty under § 6651(a)(2) of the Internal Revenue Code as provided under § 6651(d) on a substitute for return (SFR) prepared by the Service.

Issues

1. Whether the increased rate to the addition to tax under § 6651(a)(2) (failure to pay tax as shown on the return) as provided under § 6651(d) applies to assessments made under the SFR program.

Assuming the increased rate under § 6651(d) applies to the § 6651(a)(2) penalty for an SFR, the following issues may arise.

2. Whether the increased rate to the § 6651(a)(2) penalty, currently in effect for an amount unpaid on an SFR, continues at the increased rate for an amount of unpaid tax shown on a delinquent return (other than a joint return) filed by the taxpayer for the same tax year as the SFR.

3. Whether the answer to issue number two is different if the taxpayer files a delinquent joint return.

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4. Whether a spouse who files a delinquent joint return with a taxpayer currently liable for the increased rate to the § 6651(a)(2) penalty on an SFR is also liable for the increased rate to the § 6651(a)(2) penalty for the unpaid liability on the delinquent return.

### Conclusions

1. The increased rate to the § 6651(a)(2) penalty under § 6651(d) applies to all returns prepared by the Service under the SFR program.

2. The increased rate to the § 6651(a)(2) penalty under § 6651(d) will continue at the increased rate after a taxpayer files a delinquent return (single, married filing separate, or head of household) when the increased rate is already in effect on an SFR for the same tax year.

3. The increased rate to the § 6651(a)(2) penalty under § 6651(d) will continue at the increased rate after a taxpayer has filed a delinquent joint return when the increased rate is already in effect on an SFR for the same tax year.

4. Because a spouse who files a delinquent joint return with a taxpayer liable for the increased rate to the § 6651(a)(2) penalty in effect for an SFR for the same year has not received the required notice under § 6331, the spouse is not liable for the increased rate for the unpaid liability on the joint return.

### Facts

The Service currently prepares income tax returns for individuals who fail to file returns or who file fraudulent returns, under the authority of § 6020(b) of the Code. These returns are prepared using the Substitute for Return (SFR) procedures. Under the SFR procedures, the Service establishes a taxpayer account on the computer and simultaneously prepares and mails a thirty-day letter to the taxpayer. If the taxpayer fails to respond to the thirty-day letter, the Service mails a statutory notice of deficiency to the taxpayer. Both the thirty-day letter and the notice of deficiency issued for a return prepared under the SFR procedures include the § 6651(a)(2) penalty. If the taxpayer does not petition the United States Tax Court, the Service will assess the tax liability determined in the notice of deficiency.

When the taxpayer does not pay the assessed liability, the Service issues the usual notice and demand letters to the taxpayer for payment of the liability. If payment is not received by the Service for the liability listed on the notice and demand letter, the Service issues a notice of intent to levy as provided under § 6331. Pursuant to § 6651(d), the failure to pay penalty under § 6651(a)(2) will increase from 0.5 percent to 1 percent per month after the final notice of intent to

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levy is issued. However, the computer program for the SFR procedures does not compute the increased rate to the § 6651(a)(2) penalty on an SFR; the lower initial rate is always in effect.

After an SFR has been prepared and assessed against a taxpayer, the taxpayer sometimes elects to file a delinquent return in lieu of the SFR. In most instances the Service accepts the delinquent return as correct and makes the proper adjustments to the taxpayer's liability on the computer system. The SFR usually has a filing status of single or married filing separate. Sometimes the delinquent return filed by the taxpayer has a different filing status than the SFR (i.e., married filing jointly).

### Discussion

Section 6020(b) of the Code provides that the Service may execute a return for a taxpayer who fails to make any return required by any internal revenue law or regulation at the time prescribed, or who makes, willfully or otherwise, a false or fraudulent return.

Section 6651(a)(2) of the Code imposes a penalty for failure to pay the amount shown as tax on a return on or before the due date prescribed for payment of such tax (with regard to extensions), unless it is shown that such failure is due to reasonable cause and not due to willful neglect. The amount of the penalty is 0.5 percent of the amount of unpaid tax if the failure is for not more than one month, with an additional 0.5 percent for each additional month or fraction thereof during which the failure continues, not exceeding 25 percent in the aggregate. Except as provided under § 6651(g), the addition to tax under § 6651(a)(2) only applies if a return is filed by the taxpayer. Section 6651(g) of the Code provides that for purposes of § 6651(a)(2), a return prepared by the Service under § 6020(b) is treated as a return filed by the taxpayer.

Section 6651(d) of the Code provides, in part, that the additions to tax under § 6651(a)(2) will increase from 0.5 percent to 1 percent per month if the notice under § 6331(a) or § 6331(d) is given. The increased rate under § 6651(d) begins at the beginning of the month after the earlier of: (1) the day which is 10 days after the date on which notice is given under § 6331(d); or (2) the day on which notice and demand for immediate payment is given under the last sentence of § 6331(a).

Section 6331 of the Code generally provides rules for levy and distraint. The last sentence of § 6331(a) provides that in a jeopardy situation, notice and demand for immediate payment may be made and collection by levy is lawful without regard to the period of days provided under § 6331(d). Section 6331(d) of the Code provides that 30 days prior to any levy the Service must provide notice to the taxpayer of the Service's intent to make such levy.

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### Issue 1

The increased rate to the failure to pay penalty under § 6651(a)(2) as provided under § 6651(d) applies to all returns prepared by the service under the SFR program. Returns prepared under the SFR program are returns prepared under the authority of § 6020(b). See Significant Service Center Advice (October 20, 1999) (attached). Thus, because § 6651(g) provides that a § 6020(b) return is treated the same as a return filed by a taxpayer for purposes of § 6651(a)(2), an SFR is subject to the same increased rate to the § 6651(a)(2) penalty as a return filed by the taxpayer.

### Issue 2

The increased rate to the § 6651(a)(2) penalty as provided under § 6651(d) continues at the increased rate after the taxpayer files a delinquent return (single, married filing separate, head of household) when the increased rate is already in effect for an SFR liability on the same year. The legislative history to § 6651(d) states that the purpose of the increased rate to the § 6651(a)(2) penalty is to compensate the Service for the increased cost of collection methods, such as telephoning or visiting the taxpayer, which generally occur after the notice of intent to levy under § 6331(d) is issued to the taxpayer. See H.R. Rep. No. 99-426, at 832 (1985). Even though the taxpayer files a delinquent return after an SFR has been filed, it is most likely in direct response to the more expensive collection methods that the Service switched to after issuing the notice of intent to levy. Additionally, because the taxpayer still has a tax liability from the delinquent return, the Service will remain involved in the more expensive methods of collection for the liability. In adhering to the purpose of the legislative history and because the Code does not indicate otherwise, the increased rate to the § 6651(a)(2) penalty that is in effect for an SFR will continue in effect even after a taxpayer has subsequently filed a delinquent return.

### Issue 3

The increased rate to the § 6651(a)(2) penalty under § 6651(d) continues at the increased rate even after the taxpayer files a delinquent return when the increased rate is already in effect on an SFR for the same tax year. The taxpayer in this situation is similar to the taxpayer under issue two, except that the taxpayer has filed a joint return. Although the spouse who files the joint return with the taxpayer has not received the § 6331(d) notice (as required under § 6651(d) for the increased rate to be in effect), the taxpayer has received the § 6331(d) notice. Thus, for the same reasons as provided under issue 2, the increased amount to the § 6651(a)(2) penalty remains in effect even after the taxpayer has subsequently filed a joint return.

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Issue 4

A spouse who files a delinquent joint return with a taxpayer liable for the increased rate to the § 6651(a)(2) penalty on an SFR is not liable for the increased rate on the delinquent joint return. In this situation the spouse has not received a notice under § 6331 as required by § 6651(d). Thus, until a notice under § 6331 has been issued to the spouse, the increased rate to the § 6651(a)(2) penalty can not be imposed on the spouse. Although the spouse is not legally liable for the increased rate of the § 6651(a)(2) penalty that has already accrued on the liability, we see no reason to separate the liability on the computer system unless a specific request is made by the spouse.

If you have any questions or concerns regarding this memorandum, please contact Brad Taylor at (202) 622-4940.

HEATHER C. MALOY

By: \_\_\_\_\_  
JUDITH M. WALL  
Chief, Branch 4

Attachment: Copy of Significant Service Center Advice (October 20, 1999)(199950033).