

Office of Chief Counsel
Internal Revenue Service
memorandum

CC:PA:01:MEHara
POSTS-135837-15

UIL: 6723.00-00

date: November 2, 2015

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Tax Forms and Publications
SE:W:CAR:MP:T:B:T

from: Bridget Tombul
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subject: Inflation Adjustments to Information Return Penalties

This memorandum responds to your request for assistance. This advice may not be used or cited as precedent.

ISSUE

Are information return penalties applicable to Schedule K-1 (Form 1041), *Beneficiary's Share of Income, Deductions, Credits, etc.*, that have an incorrect taxpayer identification number (TIN) subject to an inflation adjustment?

CONCLUSION

There is no inflation adjustment for I.R.C. § 6723, which is the appropriate penalty for the failure to provide a required TIN on a Schedule K-1 (Form 1041) that is filed with the Service. In contrast, there is an inflation adjustment for I.R.C. § 6722, which is the appropriate penalty for the failure to provide a required TIN on a Schedule K-1 (Form 1041), that is furnished to a beneficiary.

BACKGROUND

A Form 1041 must be filed by an estate if it has a gross income of \$600 or more,¹ or there is a nonresident alien beneficiary.² A Form 1041 must be filed by a trust if it has a

¹ I.R.C. § 6012(a)(3).

gross income of \$600 or more during the trust tax year, if there is any taxable income,³ or there is a nonresident alien beneficiary.⁴ Schedule K-1 (1041) is used to report a beneficiary's share of income, deductions, and credits from a trust or estate.⁵ The fiduciary must file Schedule K-1 with the Internal Revenue Service for each beneficiary.⁶ The fiduciary must also provide the beneficiary with a copy of his or her K-1.⁷

Section 806 of the Trade Preferences Extension Act of 2015, P.L. No. 114-27, signed into law on June 29, 2015, (TPEA) amends penalties applicable under I.R.C. § 6721, Failure to File Correct Information Returns, and I.R.C. § 6722, Failure to Furnish Correct Payee Statements. The amendments apply to returns and statements required to be filed after December 31, 2015.

TPEA increases the penalties under sections 6721 and 6722 from \$100 to \$250 per return or statement, and the annual cap or limit on penalties per calendar year under each section is increased from \$1,500,000 to \$3,000,000. Additionally, if the failure to file information returns or payee statements is a result of intentional disregard, TPEA increases the penalties under section 6721 and under section 6722 from \$250 per return/statement to \$500 per return/statement; or, if greater, 10% of the aggregate amount required to be reported correctly.

All of the above penalties are adjusted for inflation under sections 6721(f) and 6722(f).

You have asked whether TPEA affected the penalty for "Failure to Provide a Required TIN" and whether the \$250 and \$500 amounts increase to \$260 and \$520 for inflation adjustments.

LEGAL ANALYSIS

Section 6723 is the Appropriate Penalty for Filing an Incorrect Schedule K-1 (Form 1041) with the Service

The section 6721 penalty applies to failures to timely file a correct information return with the Service. Section 6724(d)(1) provides definitions for information returns that are subject to the section 6721 penalty, based upon the Code section that requires the filing

² I.R.C. § 6012(a)(5).

³ I.R.C. § 6012(a)(4).

⁴ I.R.C. § 6012(a)(5).

⁵ See 2014 Instructions for Form 1041 and Schedules A, B, G, J, and K-1, at 36; 2014 Instructions for Schedule K-1 (Form 1041) for a Beneficiary Filing a Form 1040, at 1.

⁶ See 2014 Instructions for Form 1041 and Schedules A, B, G, J, and K-1, at 36.

⁷ I.R.C. § 6034A(a).

of those returns. The definitions in section 6724 do not include I.R.C. 6012, the Code section that requires the filing of Form 1041. For this reason, the penalty under section 6721, for failing to timely file a correct information return, would not be the appropriate penalty to assert for an incorrect Schedule K-1 (Form 1041) filed with the Service.

The section 6723 penalty applies to failures to timely comply with a specified information reporting requirement. I.R.C. § 6724(d) provides definitions that apply to sections 6721, 6722, and 6723. Section 6724(d)(3)(B) provides a definition for "specified information reporting requirement" that applies to section 6723 which includes "any requirement contained in the regulations prescribed under section 6109 " for a person to include his TIN or that of another person on a "return, statement, or document (other than an information return or payee statement)." Treasury Regulation Section 301.6109-1(c) provides that "every person required to make a return, statement, or other document must furnish such taxpayer identification number of s of other U.S persons and foreign persons ... as required by the forms and accompanying instructions." Part II of Schedule K-1 requires including the identification number of the beneficiary. For this reason, the penalty under section 6723, for failing to timely comply with a specified information reporting requirement, is the appropriate penalty to assert for a Schedule K-1 (Form 1041) with an incorrect TIN filed with the Service.

There is no Inflation Adjustment for Section 6723

Section 806 of the TPEA amended I.R.C. § 6721 and 6722, but not section 6723. That penalty remains at \$50 for each failure, not to exceed \$100,000.

Section 6722 is the Appropriate Penalty for Furnishing an Incorrect Schedule K-1 to a Beneficiary

The section 6722 penalty applies to failures to timely provide payees with correct payee statements. Section 6724(d)(2) provides a definition for "payee statement" that applies to section 6722. The definition includes at subsection 6724(d)(2)(A), any statement required to be furnished under section 6034A. Section 6034A, Information to Beneficiaries of Estates and Trusts, requires the fiduciary of an estate or trust required to file a return under section 6012(a) to furnish an information return to any beneficiary who receives a distribution from an estate or trust or to whom any item is allocated during the taxable year. The requirement to file a Form 1041, *U.S. Income Tax Return for Estates and Trusts*, derives from section 6012(a). For this reason, the penalty under section 6722, for failing to timely furnish a correct information return, would be the appropriate penalty for an incorrect Schedule K-1 (Form 1041) furnished to a beneficiary.

There is an Inflation Adjustment for Section 6722

TPEA Section 806 increased the penalties under section 6722 from \$100 to \$250 per return or statement, and the annual cap or limit on penalties per calendar year under this section was increased from \$1,500,000 to \$3,000,000. Additionally, if the failure to furnish correct payee statements is a result of intentional disregard, the Legislation increases the penalties under section 6722 from \$250 per return or statement to \$500

per statement; or, if greater, 10% of the aggregate amount required to be reported correctly.

The penalty is adjusted for inflation under section 6722(f). Accordingly, for returns required to be filed after Dec. 31, 2014, the \$250 and \$500 amount is increased to \$260 and \$520 as a result of inflation adjustments.

If you have any further questions regarding the inflation adjustments as it affects fiscal year filers, please contact William Ruane, Income Tax and Accounting, (202) 317-4718.

Please call (202) 317-5417 if you have any further questions for issues within the jurisdiction of Procedure and Administration.