

LB&I International Practice Service Process Unit – Audit

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Volume	12	Pass-Thru Entities	Level 1 UIL	9434
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Chapter	12.1.2	Partnership Information Reporting Issues	Level 3 UIL	9434.01
Sub-Chapter	12.1.2.1	Form 8865 - Information Return Filing Requirements	–	–

Unit Name	Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty
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Process Overview

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Process Description

A U.S. person (USP) who has an ownership interest in a foreign partnership may be required to file a Form 8865 - Return of U.S. Persons With Respect to Certain Foreign Partnerships.

The Form 8865 is used to report information required under IRC §6038 (Information Reporting With Respect to Certain Controlled Foreign Partnerships), Internal Revenue Code (IRC) §6038B (Reporting of Certain Transfers to Foreign Partnerships), and IRC §6046A (Reporting of Acquisitions, Dispositions, and Changes in Foreign Partnership Interests).

Form 8865 requires substantially the same information contained on a U.S. Form 1065, U.S. Return of Partnership Income, including schedules for identification of partners, net profits, capital gains, partnership distributions, beginning and end of the year balance sheets, capital accounts, changes in the ownership interest of partners, and transactions between the partnership and its partners and related entities. The Form 8865's instructions are an integral part of the Form 8865.

Form 8865 is required to be filed only by those USPs described as Category 1, 2, 3, or 4 filers, with several exceptions to these filing requirements. The instructions specify the required schedules, depending on the category of filer. In general, with respect to Category 1 and 2 filers, a Form 8865 is required only when the foreign partnership (FP) is controlled by one or more USPs. See Treas. Reg. §§1.6038-3(a), and (b)(1)-(3).

For those required to file, the USP must attach Form 8865 to their United States (U.S.) income tax return for the year during which the FP accounting period ends. If the USP is not required to file a tax return, but is required to file a Form 8865, the Form 8865 must be filed separately with the IRS at the time and place they would be required to file a U.S. income tax return (or, if applicable, a partnership or exempt organization return). The USP files Form 8865 for the annual accounting period of the FP that ends with or within USP's tax year. See IRC §6038(a)(2).

Process Overview (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Process Description

The statute of limitations with respect to the penalties for failure to file, and with respect to the underlying adjustments attributable to the FP, does not expire before three years following the date on which a complete and accurate Form 8865 is filed. IRC §6501(c)(8); Treas. Reg. §1.6038-3(k)(5).

Penalties For Failure To File Form 8865.

Penalties under IRC §6038 may apply when the USP, fails to file a Form 8865, files a delinquent Form 8865 or files a substantially incomplete Form 8865.

If any of these failures exist an Initial Penalty of \$10,000 per form, per year applies, IRC §6038(b)(1). Where the failure continues for more than 90 days from the date the Service notifies the USP of the failure to file a complete Form 8865, a Continuation Penalty of \$10,000 applies for each 30 day period (or fraction thereof) that the failure continues.

The Continuation Penalty continues to accrue until the USP cures the failure, or until the maximum Continuation Penalty of \$50,000 has been incurred. [IRC §6038(b)(2)] These are assessable penalties, and are not subject to the deficiency procedures provided for by IRC §6213.

In addition to the monetary penalty, the Service may also reduce the amount of the USP's applicable foreign tax credit, IRC §6038(c). The procedures for reducing the USP's foreign tax credit is discussed in another unit.

Example Circumstances Under Which Process Applies

This process may apply when the taxpayer is determined to be a category 1 or 2 filer of a foreign partnership, as defined later, and:

- Filed a delinquent Form 8865
- Failed to file a Form 8865
- Filed a substantially incomplete Form 8865

Determination of Process Applicability

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Certain U.S. partners are required to file Form 8865 to report information with respect to certain FPs. The information required to be furnished varies based on the USP's filing category.

Criteria	Resources	6103 Protected Resources
<p>The statute of limitations for assessing IRC §6038 penalties does not expire before 3 years from the date the Service receives a complete and accurate Form 8865.</p>	<ul style="list-style-type: none"> • Director, LB&I-IIC – Memo (1/9/2013) -Statute Of Limitations on Assessment of Foreign Information Return Penalties • Statute of Limitations Desk guide 	
<p>Currently, there are four active categories of Form 8865 filers:</p> <ul style="list-style-type: none"> ▪ Category 1 - a USP who owned a controlling interest in a FP at any time during the partnership's tax year ▪ Category 2 - a USP who owned a 10% or greater interest in a controlled foreign partnership ▪ Category 3 - a USP who contributed property to a FP in exchange for a partnership interest ▪ Category 4 - a USP that had a reportable event per IRC §6046A (acquisition, disposition or change in proportional interest in a FP) 	<ul style="list-style-type: none"> ▪ IRC 6038(a)(1) – Requirement in general ▪ Treas. Reg. 1.6038-3(a)(1) ▪ See definitions on Slide 6 ▪ Treas. Reg. 1.6038-3(a)(2) ▪ See definitions on Slide 6 ▪ IRC 6038B ▪ Practice Unit “Failure to File the Form 8865 – Category 3 Filer - Monetary Penalty” ▪ IRC 6046A ▪ Practice Unit, “Failure to File the Form 8865 – Category 4 Filer – Monetary Penalty” 	

Determination of Process Applicability (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Certain U.S. partners are required to file Form 8865 to report information with respect to certain FPs. The information required to be furnished varies based on the USP's filing category.

Criteria	Resources	6103 Protected Resources
<p>Entities Qualifying as a Partnership:</p> <p>In general, the Form 8865 must be filed for any foreign flow-through entity that would be treated as a partnership under U.S. tax law. This includes a limited partnership, group or unincorporated organization through which any business, financial operation or venture is carried on, other than a corporation, trust, estate, or sole proprietorship.</p> <p>Category 1 Definitions</p> <ul style="list-style-type: none"> ▪ U.S. person <ul style="list-style-type: none"> – citizen or resident of the U.S., – domestic corporation, – domestic partnership, or – estate or trust that is not a foreign estate or trust. ▪ Control - ownership of more than a 50% interest in the partnership at any time during the FP's tax year 	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.6038-3(b)(7) ▪ IRC 7701(a)(2) Partnership ▪ IRC 7701(a)(5) Foreign Partnership ▪ See Category 1 description on Slide 5 ▪ Treas. Reg. 1.6038-2(d) – USP ▪ IRC 7701(a)(30) – United States person ▪ IRC 7701(a)(31) – Foreign estate or trust. ▪ Practice Unit, “Check the Box Rules for Foreign Entities,” DCN: FEN/9433.01_TBD ▪ IRC 6038(e)(3) – Control of partnership 	

Determination of Process Applicability (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Certain U.S. partners are required to file Form 8865 to report information with respect to certain FPs. The information required to be furnished varies based on the USP's filing category.

Criteria	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ 50% interest <ul style="list-style-type: none"> – 50% of the capital, or – 50% of the profits, or – 50% of the deductions or losses <p>When determining control, the constructive ownership rules of IRC §267(c)(1), (2), (4) and (5) apply.</p> <p><u>Constructive Ownership Rules:</u> Generally, under the constructive ownership rules of IRC §267, an individual is considered to own an interest directly or indirectly by his or her family, including that individual's spouse, siblings, ancestors and lineal descendants. An interest owned directly or indirectly by or for a corporation, partnership, estate, or trust shall be treated as if it is owned in proportion to the interest of its owners, partners, or beneficiaries</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.6038-3(b)(2) – 50% interest ▪ IRC 267(c)(1), (2), (4) and (5) ▪ Treas. Reg. 1.6038-3(b)(4) – Constructive Ownership Rules 	

Determination of Process Applicability (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Certain U.S. partners are required to file Form 8865 to report information with respect to certain FPs. The information required to be furnished varies based on the USP's filing category.

Criteria	Resources	6103 Protected Resources
<p>Category 2 Definitions</p> <ul style="list-style-type: none"> ▪ U.S. person ▪ 10% interest <ul style="list-style-type: none"> – 10% of the capital, – 10% of the profits, or – 10% of the deductions or losses ▪ Controlled Foreign Partnership (CFP) - a FP in which 10% U.S. partners own more than 50% of the interests. ▪ When determining ownership interest, the constructive ownership rules of IRC §267(c)(1), (2), (4) and (5) apply. 	<ul style="list-style-type: none"> ▪ See Category 2 description on Slide 5 ▪ See definition on Slide 6 ▪ Treas. Reg. 1.6038-3(b)(3) – 10% interest ▪ Treas. Reg. 1.6038-3(a)(2) – Controlling 10% partners ▪ Treas. Reg. 1.6038-3(b)(4) – Constructive Ownership Rules ▪ IRC 267(c)(1), (2), (4) and (5) ▪ See definition on page 7 	

Determination of Process Applicability (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Certain U.S. partners are required to file Form 8865 to report information with respect to certain FPs. The information required to be furnished varies based on the USP's filing category.

Criteria	Resources	6103 Protected Resources
<p>Exceptions to Filing - General</p> <ul style="list-style-type: none"> ▪ More than one controlling 50% partner <ul style="list-style-type: none"> – There may be more than one controlling partner with more than 50% control due to the definition for measuring control (capital account, profits or loss deduction allocation) – Only one controlling partner must file Form 8865. – Category 1 filer with a greater than 50% interest in deductions or losses must file only if no Category 1 filer with greater than 50% interest in capital or profits exists. – The filing Category 1 partner must file some additional information with respect to the non-filing Category 1 partner. – The non-filing Category 1 partner must attach a statement to its return regarding the CFP. ▪ 10% partners when the CFP has a controlling 50% partner <ul style="list-style-type: none"> – When a controlling 50% partner is required to file Form 8865 as a Category 1 filer, no U.S. 10% partners are required to file Form 8865 as Category 2 filers. 	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.6038-3(c)(1) – Exceptions when more than one U.S. person is required to file Form 8865 pursuant to IRC 6038 ▪ Instructions for Form 8865 ▪ Treas. Reg. 1.6038-3(a)(2) – Controlling 10% partners 	

Determination of Process Applicability (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Certain U.S. partners are required to file Form 8865 to report information with respect to certain FPs. The information required to be furnished varies based on the USP's filing category.

Criteria	Resources	6103 Protected Resources
<p>Foreign partnership files Form 1065 or 1065-B for its tax year</p> <ul style="list-style-type: none"> ▪ Form 8865 is required for Category 1 and 2 filers, even if the CFP files a Form 1065-B. However the Category 1 and 2 filers may use the completed Form 1065 or 1065-B schedules in place of the equivalent schedules as outlined in the instructions to Form 8865. 	<ul style="list-style-type: none"> ▪ <i>Treas. Reg. 1.6038-3(j) – Overlap w/IRC 6031</i> ▪ <i>Instructions for Form 8865</i> ▪ <i>Form 1065-B, U.S. Return of Income for Electing Large Partnerships</i> ▪ <i>Form 1065 U.S. Return of Partnership Income</i> 	

Determination of Process Applicability (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Certain U.S. partners are required to file Form 8865 to report information with respect to certain FPs. The information required to be furnished varies based on the USP's filing category.

Criteria	Resources	6103 Protected Resources
<p>Exceptions to Filing – Constructive Owners</p> <p>A USP that does not own a direct interest in a FP and is required to file Form 8865 solely by reason of constructive ownership is not required to file Form 8865 if -</p> <ul style="list-style-type: none"> ▪ The USP whose interest the indirect partner constructively owns reports all of the required information AND ▪ The indirect partner files with its income tax return a statement titled “Controlled Foreign Partnership Reporting” containing the following information: <ul style="list-style-type: none"> – A representation that the indirect partner was required to file Form 8865, but is not doing so pursuant to the constructive owner exception; – The names and addresses of the USP whose interests the indirect partner constructively owns; – The name and address of the FP with respect to which the indirect partner would have had to have filed Form 8865 but for this exception; and – Any additional information that Form 8865 and the accompanying instructions require. 	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.6038-3(c)(2) Certain constructive owners excepted from filing ▪ IRC 267(c) ▪ Treas. Reg. 1.6038-3(b)(4) Constructive Ownership rules 	

Summary of Process Steps

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty	
Step 1	Verify Fact of Filing
Step 2	Penalty Case File Controls
Step 3	Penalty Determination
Step 4	Penalty Application/Closing Procedures

Step 1

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

You have determined that the taxpayer had a requirement to file a Form 8865 as outlined previously in the Process Applicability section. Before commencing a penalty case file, you must first determine whether the taxpayer actually filed a timely and accurate information return Form 8865. The related income tax return may have been late filed with the Form 8865(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 8865(s)

Considerations	Resources	6103 Protected Resources
<ul style="list-style-type: none"> ▪ Due when USP's income tax return is due, including extensions ▪ Filed with the USP's income tax return. ▪ As discussed in detail previously there are several exceptions to filing that may apply: <ul style="list-style-type: none"> – More than one controlling 50% partner – 10% partners when the CFP has a controlling 50% partner – Constructive Owners (with required disclosure) ▪ Even with the above filing exceptions, certain information with respect to the FP may be required to be filed. ▪ There is no separate Master File Transaction (MFT) in Integrated Data Retrieval System (IDRS) for Form 8865 filings ▪ Penalties may be asserted when the related income tax return is filed late or when substantially complete Forms 8865 are not timely filed with the related income tax return, or when Form(s) 8865 are not substantially complete. 	<ul style="list-style-type: none"> ▪ IRC 6038 ▪ Determination of Process Applicability Section ▪ IRM 2.3.17.5 General Information for CC ESTABD to request original actual tax return 	

Step 1 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

You have determined that the taxpayer had a requirement to file a Form 8865 as outlined previously in the Process Applicability section. Before commencing a penalty case file, you must first determine whether the taxpayer actually filed a timely and accurate information return Form 8865. The related income tax return may have been late filed with the Form 8865(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 8865(s)

Considerations	Resources	6103 Protected Resources
<p>As you identify Forms 8865 that were required, but not filed, for the exam year(s), consider reviewing whether those forms were required, but not filed, in earlier tax years. The statute of limitations for assessing and collecting penalties under IRC §6038 does not expire before three years after a substantially complete Form 8865 was filed.</p>	<ul style="list-style-type: none"> ▪ Director, LB&I-IIC – Memo (1/9/2013) -Statute Of Limitations on Assessment of Foreign Information Return Penalties 	
<ul style="list-style-type: none"> ▪ Penalties under IRC §6038 may also be asserted for related income tax returns (prior or subsequent) without opening the returns for examination. 		

Step 1 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

You have determined that the taxpayer had a requirement to file a Form 8865 as outlined previously in the Process Applicability section. Before commencing a penalty case file, you must first determine whether the taxpayer actually filed a timely and accurate information return Form 8865. The related income tax return may have been late filed with the Form 8865(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 8865(s)


Considerations	Resources	6103 Protected Resources
<p>Determining if the Return was filed late</p> <ul style="list-style-type: none"> ▪ When the last day for filing a return was a Saturday, a Sunday, or a legal holiday in the District of Columbia, filing timely occurred when the return was mailed on the next succeeding day which was not a Saturday, Sunday, or a legal holiday. ▪ If a return was postmarked on or prior to the due date and received after the due date, the due date is treated as the filing date. ▪ The Official IRS Received Date stamped on page one of the return indicates when it was received by an IRS Campus or other IRS Office. Compare the stamped date to the due date based on the tax year end and, if applicable, the extended due date. 	<ul style="list-style-type: none"> ▪ IRC 7503 and Treas. Reg. 301.7503-1 – Time for performance of acts where last day falls on Saturday, Sunday of legal holiday. ▪ Rev. Rul. 81-269 ▪ IRC 7502 and Treas. Reg. 301.7502-1 – Timely mailing of documents and payments is treated as timely filing and paying 	

Step 1 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

You have determined that the taxpayer had a requirement to file a Form 8865 as outlined previously in the Process Applicability section. Before commencing a penalty case file, you must first determine whether the taxpayer actually filed a timely and accurate information return Form 8865. The related income tax return may have been late filed with the Form 8865(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 8865(s)

Considerations	Resources	6103 Protected Resources
 <p>DECISION POINT: If the U.S. partner's income, partnership or exempt organization was filed late then by definition the attached Forms 8865 were not timely filed. Consider whether to prepare a pattern letter to notify USP of their failure to timely file Form 8865.</p>	<ul style="list-style-type: none"> ▪ See Step 2 	
<p>Identify whether all required Form 8865s were attached to the return</p> <p>The following items are helpful in determining whether all required Form 8865s were filed:</p> <ul style="list-style-type: none"> ▪ U.S. partner's returns for previous and subsequent years; ▪ Forms 8832, <i>Entity Classification Election</i>; ▪ tax organization chart, including previous and subsequent years; ▪ legal entity chart including previous and subsequent years; ▪ statements of other U.S. filers of Form 8865 for same partnership. <p>The above tools can be used to analyze, compare and resolve questions to identify missing Form 8865(s). All or some of the tools can be used depending on the number of foreign partnerships owned by the USP. (If necessary, a more experienced agent could provide guidance on how to use these tools.)</p>		

Step 1 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

You have determined that the taxpayer had a requirement to file a Form 8865 as outlined previously in the Process Applicability section. Before commencing a penalty case file, you must first determine whether the taxpayer actually filed a timely and accurate information return Form 8865. The related income tax return may have been late filed with the Form 8865(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 8865(s)

Considerations	Resources	6103 Protected Resources
<p>If you determine the USP had a Form 8865(s) filing requirement but did not file Form 8865(s) or failed to file substantially complete Form 8865(s), then prepare a notice letter to notify the USP of the failure. The term substantially complete (substantial compliance) is discussed on the following slides.</p> <p>Note: The prior year income tax returns do not have to be open and under control in Exam for the Service to impose the penalty for the failure to file Form 8865 per IRC §6038.</p>	<ul style="list-style-type: none"> ▪ Step 2 – Notice Letter ▪ IRM 20.1.9.3.2 ▪ IRM Exhibit 20.1.9-7 Pattern Letter for failure to file Form 8865 	

Step 1 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

You have determined that the taxpayer had a requirement to file a Form 8865 as outlined previously in the Process Applicability section. Before commencing a penalty case file, you must first determine whether the taxpayer actually filed a timely and accurate information return Form 8865. The related income tax return may have been late filed with the Form 8865(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 8865(s)

Considerations	Resources	6103 Protected Resources
<p>Review Forms 8865 attached to return for completeness</p> <ul style="list-style-type: none"> ▪ Treas. Reg. §1.6038-3 and the instructions for Form 8865 detail the information required to be filed for each category of filer. A USP is required to furnish all required information on Form 8865 even though the information required may not affect the amount of any tax due under the Internal Revenue Code. ▪ Review USP's Form(s) 8865 to determine whether any schedule required (based on the filing category indicated on Page 1, Item A) was not completed. ▪ Compare current year Form 8865 to previous year: <ul style="list-style-type: none"> – Is identifying information on Page 1, Item F the same as prior year? This includes the EIN, Reference ID, Country under whose laws the entity is organized, and Principal business activity. – Compare current balance sheet (Schedule L) beginning year balances to prior year ending balances – Compare current balance sheet for Interest Allocation (Schedule M) beginning year balances to prior year ending balances 	<ul style="list-style-type: none"> ▪ Form 8865 ▪ Form 8865 - Instructions - for listing of required schedules by filer category 	

Step 1 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 1: Verify Fact of Filing

You have determined that the taxpayer had a requirement to file a Form 8865 as outlined previously in the Process Applicability section. Before commencing a penalty case file, you must first determine whether the taxpayer actually filed a timely and accurate information return Form 8865. The related income tax return may have been late filed with the Form 8865(s) attached or the related income tax return may have been filed timely but without a substantially complete Form 8865(s)

Considerations	Resources	6103 Protected Resources
<p>Review Forms 8865 attached to return for completeness</p> <p>The most common reasons for noncompliance with IRC 6038 include the following:</p> <ul style="list-style-type: none"> ▪ Stating that required information will be furnished upon request or audit, ▪ Providing computer generated Form 8865(s) that were not IRS approved and did not conform to requirements, ▪ Failure to complete all required schedules of the Form 8865 ▪ Consolidating two or more foreign partnerships onto one Form 8865 <p><u>Partnership Wind-Up Situations:</u> Significant transactions often occur during the business wind-up phase, even though the balance sheet reflects zero ending balances on the final Form 8865. (Note: Final year is determined by review of the beginning and ending dates at the top of Form 8865.)</p> <p># [REDACTED]</p> <p>[REDACTED] #</p>		

Step 2

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter.

Considerations	Resources	6103 Protected Resources
<p>Establish a penalty case file</p> <ul style="list-style-type: none"> ▪ Establish controls and prepare a penalty case file. This file must include the information that supports the requirements to file and establishes the Forms 8865 have not been filed or not filed substantially complete. ▪ Submit Form 5345-D for managerial approval to establish controls: <ul style="list-style-type: none"> – Check box for “Control Penalty Investigation.” – MFT = PR, Activity Code = 586, Source Code = 99 – For Initial Penalty – MFT = PQ, Activity Code = 586, Source Code = 99, - For Continuation Penalty – ASED will default to 01/31/YY+4. Upon receipt of delinquent information returns, update ASED to three years from receipt date. – Reason for Request is “To control penalty investigations for Form 8865 returns not filed” ▪ Examiners charge time to the penalty case file. ▪ Issue the Notice Letter as discussed on the following slides. 	<ul style="list-style-type: none"> ▪ IRM 20.1.9.2 – Assessment Procedures for Penalties Not Subject to Deficiency Procedures ▪ Exhibit 20.1.9-4 ▪ Exhibit 20.1.9.1 – Quick Reference Guide to International Penalties ▪ IRM 20.1.9.2(10) ▪ Form 5345-D ▪ IRM 20.1.9.2(11) ▪ IRM 20.1.9.2(12) 	

Step 2 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter.

Considerations	Resources	6103 Protected Resources
<p>Supporting a Form 8865 Penalty Assessment</p> <p><u>When completed, the case file should include the following information:</u></p> <ul style="list-style-type: none"> ▪ Evidence that the taxpayer had a duty to file a Form 8865 ▪ Evidence that the taxpayer failed to timely file a the required Form 8865, or the reasons that the Form 8865 which was filed is incomplete ▪ Evidence that that any reasonable cause claim asserted by the taxpayer is insufficient to excuse the failure. 	<ul style="list-style-type: none"> ▪ IRM 20.1.9.2(11) ▪ IRM 20.1.9.2(12) ▪ IRM 20.1.9.2(15)) 	

Step 2 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter.


Considerations	Resources	6103 Protected Resources
<p>Notice Letter Issuance</p> <p>Once you have opened the file and suspect that the reporting requirements of IRC §6038 have not been met, a Pattern Letter for Failure to File Form 8865 must be issued to the USP.</p> <p>The pattern letter notifies USP that it failed to file a Form 8865 (i.e., filed late or not filed at all), or that the form filed was substantially incomplete. It states that an Initial Penalty will be imposed absent showing a reasonable cause (or) showing that no Form 8865(s) is required. It also states, a Continuation Penalty will apply if the Service does not receive a complete and accurate Form 8865(s) within 90 days of notification. The pattern letter directs USP to Treas. Reg. §1.6038-3(k)(4), for the reasonable cause provision. The pattern letter must be <u>addressed to the U.S. partner required to file Form 8865</u>. If the U.S. partner is a subsidiary corporation included in a consolidated corporate income tax return, the Service can address the pattern letter to the partner (U.S. sub) or the parent (U.S. consolidating entity named on the Form 1120 income tax return).</p> <p>The Service may issue one pattern letter where USP failed to file multiple Form(s) 8865. The letter must list the complete legal names of the specific entities for which the USP has failed to file a Form 8865. If necessary, a list of these legal names can be attached as page two.</p>	<ul style="list-style-type: none"> ▪ IRM Exhibit 20.1.9-7 – Pattern Letter for Failure to File Form 8865 ▪ Treas. Reg. 1.6038-3(k)(4) – Reasonable cause provision 	

Step 2 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter.

Considerations	Resources	6103 Protected Resources
 <p># [REDACTED]</p> <p>[REDACTED] #</p>		
<p>Notice Letter Issuance</p> <ul style="list-style-type: none"> ▪ The pattern letter should include the name of the revenue agent to whom the taxpayer should reply. ▪ Notice letters must be signed by an examination group manager in SB/SE or a revenue agent in LB&I. ▪ Mail the notice letter to the person required to file as soon as possible for two reasons: 1) to obtain the information early to effectively conduct the exam; and 2) to start the 90-day notice period required by IRC §6038(b)(1) and (c)(1). Typically, USPs will provide corrected Form 8865(s) as soon as possible after receipt of the notice letter to avoid accumulating Continuation Penalties. 	<ul style="list-style-type: none"> ▪ IRM 20.1.9.2 (13) ▪ Treas. Reg. 1.6038-3(k)(3)(i)(B) 	

Step 2 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter.

Considerations	Resources	6103 Protected Resources
<p>Notice Letter Issuance</p> <ul style="list-style-type: none"> ▪ Per the regulations, the notice letter must be mailed to the person required to file, not its representative. # [REDACTED] ▪ [REDACTED] # Use registered or certified mail “return receipt requested” to provide evidence that the notice letter was received. If hand delivered to the USP, it is important to have USP sign and date a receipt to show acknowledgement of delivery. Also, specifically document delivery in the case file or the reasons for USP’s refusal to acknowledge receipt. ▪ Keep a copy of all notice letters issued, and the certified or registered return receipts, in the case file. <p>The pattern letter may be delivered to a representative with a valid Power of Attorney for IRC §6038 civil penalties. However, the Form 2848 for the income tax examination does not cover IRC §6038 penalties. In order for the Form 2848 to be valid for penalties under IRC §6038, the Form 2848 must include language similar to “Civil Penalties” or “IRC §6038 Penalty” or “Chapter 61 Penalties” for Item #3 “Description of Matter.”</p>		

Step 2 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter.

Considerations	Resources	6103 Protected Resources
<p>Notice Letter Issuance</p> <p>Review Forms 2848 <i>Power of Attorney and Declaration of Representative</i> to determine if the representative has authorization to represent the USP on the civil penalties. If not, consider suggesting that USP issue a separate Form 2848. Although you cannot discuss the civil penalties with an unauthorized representative, you may <u>obtain</u> information from the representative to proceed with the penalty development. The representative may have details about the Form 8865(s) that are helpful regarding their compliance with IRC §6038 and enable you to effectively develop the penalty.</p> <p># [REDACTED] # [REDACTED]</p>		

Step 2 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter.

Considerations	Resources	6103 Protected Resources
<p><u>Reasonable Cause:</u> Consider referring USP or its authorized representative to Treas. Reg. §1.6038-3(k)(4), which sets forth the requirements for a valid reasonable cause statement. This regulation <u>does not</u> apply as potential reasonable cause defense for the Continuation Penalty.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.6038-3(k)(4) – Reasonable cause limitation 	
<p>Review Forms 8865 submitted in response to the notice letter</p> <p>Date stamp the late filed or amended Form 8865(s) when they are received. If the late filed Form 8865(s) are substantially correct, the stamped date will determine whether the Continuation Penalty applies and the amount of the penalty.</p> <p>Review subsequently filed Form 8865(s) to determine whether they substantially comply with IRC §6038. The Continuation Penalties begin to accrue 90 days following the mailing of the notice letter, and continue to accrue until the Service receives complete and accurate Form 8865(s), or until the maximum penalty is accrued.</p>		

Step 2 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter.

Considerations	Resources	6103 Protected Resources
<p>Review Forms 8865 submitted in response to the notice letter</p> <p># [REDACTED]</p> <p>[REDACTED] #</p>		

Step 2 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter.

Considerations	Resources	6103 Protected Resources
<p data-bbox="99 586 1156 615">Review Forms 8865 submitted in response to the notice letter (cont'd)</p> <div data-bbox="99 672 1328 1016" style="background-color: black; width: 100%; height: 241px; position: relative;"># #</div>		

Step 2 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter.

Considerations	Resources	6103 Protected Resources
<p>Review Forms 8865 submitted in response to the notice letter (cont'd)</p> <p># [REDACTED]</p> <p>[REDACTED]</p> <p>[REDACTED] #</p>	<ul style="list-style-type: none"> ▪ IRM Exhibit 20.1.9-12 (04-22-2011) Pattern Letter for Failure to File Form 8865 Schedule O ▪ IRM Exhibit 20.1.9-14 (04-22-2011) Pattern Letter for Failure to File Form 8865 Schedule P 	
<div style="display: flex; align-items: center;"> <p>CAUTION: There is no statutory provision under IRC §6038 that would allow for an extension to the 90 day response period for the imposition of the Continuation Penalty</p> </div>		

Step 2 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 2: Penalty Case File Controls

You have determined that the taxpayer has failed to file a timely and accurate information return, the next step is to establish a penalty case file and prepare and issue the notice letter.

Considerations	Resources	6103 Protected Resources
<p>Review Forms 8865 submitted in response to the notice letter (cont'd)</p> <p>Note: For application of the Initial \$10,000 Penalty for the initial failure to file, there is no need to further advise the person responsible for filing that a substantially complete Form 8865 was not filed. With respect to the Continuation Penalty, there is no statutory requirement that you notify the USP of the continued failure.</p>		

Step 3

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the taxpayer, and initial revised Form 8865(s) may or may not have been filed, and those initial or revised Forms 8865 may not be substantially correct. Now you must determine what penalties apply, how they are computed, and whether or not the taxpayer has a valid reasonable cause argument for failure to file or lack of completeness.

Considerations	Resources	6103 Protected Resources
<p>Penalty Structure</p> <p>If Form 8865(s) are not filed on or before the due date (including extensions) of the individual's income tax return, or if the applicable form does not include all the information required, or includes incorrect information, then Initial and Continuation Penalties may be applicable as follows:</p> <p>The penalty per IRC §6038(b) for failure to furnish all the required information timely on a Form 8865 is:</p> <ul style="list-style-type: none"> ▪ \$10,000 per Form 8865 that the U.S. partner fails to file ▪ If the information is not filed within 90 days after notice of the failure is mailed to the USP, additional penalties of \$10,000 apply per failure to file for each 30-day period, or fraction thereof, during which the failure continues. The maximum additional penalty for each Form 8865 is \$50,000. ▪ The maximum total penalty for each failure to file Form 8865 is \$60,000 (\$10,000 Initial Penalty and the \$50,000 Continuation Penalty). <p>There is also a penalty under IRC §6038(c) which results in the reduction of foreign tax credits, but this is beyond the scope of this IPS unit and will be addressed elsewhere.</p>	<ul style="list-style-type: none"> ▪ IRC 6038(a) ▪ IRM 20.1.9.3.4 ▪ IRC 6038(b) ▪ IRC 6038(c) 	

Step 3 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the taxpayer, and initial revised Form 8865(s) may or may not have been filed, and those initial or revised Forms 8865 may not be substantially correct. Now you must determine what penalties apply, how they are computed, and whether or not the taxpayer has a valid reasonable cause argument for failure to file or lack of completeness.

Considerations	Resources	6103 Protected Resources
<p>Reasonable Cause Exception</p> <p>No penalty shall be imposed under IRC §6038(b) for any failure which is shown to be due to reasonable cause and not due to willful neglect. Reasonable cause is not defined in IRC §6038 nor the regulations thereunder. It is based on the facts of each case on a case by case basis.</p> <p>A reasonable cause defense for the failure to file a complete and accurate Form 8865 must be asserted in writing and must provide all of the facts alleged as reasonable cause.</p> <p>The IRM provides that reasonable cause will not be considered until the USP is in full compliance with reporting requirements. Determine whether USP is in full compliance with IRC §6038 reporting and record keeping i.e., has filed all delinquent forms and returns requirements for all tax years open under the statutes. Request USP to file, furnish, report or maintain the information required under IRC §6038 before considering any reasonable cause requests.</p>	<ul style="list-style-type: none"> ▪ IRC 6038(c)(4)(B) ▪ Treas. Reg. 1.6038-3(k)(4) - Reasonable cause ▪ IRM Exhibit 20.1.9-5 Reasonable Cause Relief ▪ IRC 6038(c)(4)(B) Special rules 	

Step 3 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the taxpayer, and initial revised Form 8865(s) may or may not have been filed, and those initial or revised Forms 8865 may not be substantially correct. Now you must determine what penalties apply, how they are computed, and whether or not the taxpayer has a valid reasonable cause argument for failure to file or lack of completeness.

Considerations	Resources	6103 Protected Resources
<p>Reasonable Cause Exception (cont'd)</p> <p>Regarding the facts alleged to support reasonable cause, determine whether USP's supporting documents (and events) related to those facts were dated (or occurred) after the latest date that reasonable cause was relevant.</p> <p>As previously discussed, there are two different penalties: the Initial Penalty and the Continuation Penalty. While both penalties are described within IRC §6038(b), only the Initial Penalty can be considered for the reasonable cause exception. There is no reasonable cause exception for the Continuation Penalty.</p>	<ul style="list-style-type: none"> ▪ IRM 20.1.9 - International Penalty Handbook ▪ IRM 20.1.9.3.5 	
<p>Review the definition and factors of reasonable cause</p> <p>Neither IRC §6038, nor the regulations thereunder, defines "reasonable cause" for the failure to timely file a substantially complete Form 8865. The Committee Reports on the Omnibus Budget Reconciliation Act of 1989 stated that "reasonable cause exists if significant mitigating factors are present, such as the fact that a person has an established history of complying with the information reporting requirements."</p>		

Step 3 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the taxpayer, and initial revised Form 8865(s) may or may not have been filed, and those initial or revised Forms 8865 may not be substantially correct. Now you must determine what penalties apply, how they are computed, and whether or not the taxpayer has a valid reasonable cause argument for failure to file or lack of completeness.

Considerations	Resources	6103 Protected Resources
<p>Review the definition and factors of reasonable cause</p> <p>The Code provides “reasonable cause” as a defense to several penalties. For example:</p> <ul style="list-style-type: none"> ▪ IRC §6651(a) - Failure to file tax return, ▪ IRC §6652 - Failure to file certain information returns, and ▪ IRC §6679 - Failure to file returns including foreign corporations. <p>However, those statutes do not define “reasonable cause” either.</p> <p>IRC §6651(a) provides that the penalty may be avoided if USP demonstrated that the failure was attributed to reasonable cause and not due to willful neglect.</p>	<p>IRC 6651(a) IRC 6652 IRC 6679</p>	

Step 3 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the taxpayer, and initial revised Form 8865(s) may or may not have been filed, and those initial or revised Forms 8865 may not be substantially correct. Now you must determine what penalties apply, how they are computed, and whether or not the taxpayer has a valid reasonable cause argument for failure to file or lack of completeness.

Considerations	Resources	6103 Protected Resources
<p>Review the definition and factors of reasonable cause</p> <ul style="list-style-type: none"> ▪ In <i>U.S. v. Boyle</i>, the Supreme Court noted that Treas. Reg. §301.6651(c)(1) (1984) required the USP to demonstrate that it exercised ordinary business care and prudence but nevertheless was unable to file the return within the prescribed time. And thus, the Service's correlation of “reasonable cause” with “ordinary business care and prudence” is consistent with Congress' intent, and over 40 years of case law as well.” ▪ In Field Service Advice (FSA) 1997 WL 33381431, relying on <i>U.S. v Nordbrock</i> and <i>Firestone v. Howerton</i>, it was noted that in the absence of a definition, courts generally agree that similar terms appearing in different sections of a statute should be interpreted the same way. The FSA states that there was no reason to define reasonable cause under IRC §6038 differently than in other contexts e.g., exercising ordinary business care and prudence but nevertheless being unable to file a substantially complete Form 5471. 	<ul style="list-style-type: none"> ▪ <i>U. S. v. Boyle</i>, 469 U.S. 241(1985) ▪ FSA 1997 WL 33381431 (02/14/97) ▪ <i>U.S. v. Nordbrock</i>, 38 F. 3d 440 (9th Cir. 1994) ▪ <i>Firestone v. Howerton</i>, 671 F. 2d 317, 320 n. 6 (9th Cir. 1982). 	

Step 3 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the taxpayer, and initial revised Form 8865(s) may or may not have been filed, and those initial or revised Forms 8865 may not be substantially correct. Now you must determine what penalties apply, how they are computed, and whether or not the taxpayer has a valid reasonable cause argument for failure to file or lack of completeness.

Considerations	Resources	6103 Protected Resources
<p>Review the definition and factors of reasonable cause (cont'd)</p> <ul style="list-style-type: none"> ▪ In <i>Congdon v. U.S.</i>, the court provided an explanation of what is needed for reasonable cause analysis regarding Form 5471. The court referred to the IRM and the Code and stated that, “The elements that must be present to constitute reasonable cause are a question of law, but whether those elements are present in a given situation is a question of fact. To demonstrate reasonable cause, the plaintiff must show that he exercised ordinary business care and prudence.” <p>The IRM provides factors to consider to determine whether USP exercised ordinary business care and prudence. Examples of what might be reasonable cause include:</p> <ul style="list-style-type: none"> ▪ Erroneous advice or reliance, ▪ Unable to obtain records, and ▪ Death, serious illness, or unavoidable absence 	<ul style="list-style-type: none"> ▪ <i>Congdon v. United States</i>, 108 AFTR2d 2011-6340 ▪ IRM 20.1.1.3.2.2.5 ▪ IRS CCN-CC 2004-036 (09/22/04) ▪ IRM 20.1.1.3.2.2.3 ▪ IRM 20.1.1.3.2.2.1 	

Step 3 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the taxpayer, and initial revised Form 8865(s) may or may not have been filed, and those initial or revised Forms 8865 may not be substantially correct. Now you must determine what penalties apply, how they are computed, and whether or not the taxpayer has a valid reasonable cause argument for failure to file or lack of completeness.


Considerations	Resources	6103 Protected Resources
<p>Review the definition and factors of reasonable cause (cont'd)</p> <p>Reasonable cause is determined by considering the USP's actual situation. Accordingly, you must obtain background information regarding the taxpayer's facts and circumstances. Ignorance of the law, by itself, is not reasonable cause. However, in conjunction with other factors, it might be. Such other factors to consider include: USP's education, if USP was penalized before, if USP could not reasonably be expected to know of recent changes in the tax law or forms, and the level of complexity of a tax or compliance issue in light of the USP's experience, education and intellect.</p>	<ul style="list-style-type: none"> ▪ IRM 20.1.1.3.2.2.6 	
<p>The fact that a foreign jurisdiction would impose a civil or criminal penalty on the taxpayer (or any other person) for disclosing the required information and/or refusal on the part of a foreign trustee to provide information for any other reason does not constitute reasonable cause.</p> <p>Generally, the most important factor in determining whether USP has reasonable cause and acted in good faith was the extent of USP's effort to comply with the reporting requirements and report the proper tax liability.</p>	<ul style="list-style-type: none"> ▪ Treas. Reg. 1.6664-4(b)(1) ▪ IRM 20.1.9.22.5(3) Reasonable Cause 	

Step 3 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 3: Penalty Determination

The penalty case file has been established, the Notice Letter has been mailed to the taxpayer, and initial revised Form 8865(s) may or may not have been filed, and those initial or revised Forms 8865 may not be substantially correct. Now you must determine what penalties apply, how they are computed, and whether or not the taxpayer has a valid reasonable cause argument for failure to file or lack of completeness.

Considerations	Resources	6103 Protected Resources
 CONSULTATION: Contact Counsel for assistance in evaluating whether USP had reasonable cause.		

Step 4

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 4: Penalty Application/Closing Procedures

Now that the Notice Letter has been issued and you understand the penalty determination factors, the final steps in this process are penalty application or non-application, and case closing procedures

Considerations	Resources	6103 Protected Resources
<p>Application of Penalties – Initial Penalty</p> <p>Now that you understand the penalty structure and reasonable cause considerations as discussed in step 3, let us discuss how these penalties are applied. Examiners must first take steps to secure documentation to support the USP is required to file the returns and keep the information in the penalty file. Second, when the examiner secures a delinquent Form 8865, the examiner must determine whether it provides all required information and is accurate. If inaccurate or incomplete, the examiner must inform the taxpayer that the return is not considered filed until it is complete and accurate, and that Continuation Penalties will continue to accrue.</p> <p>Once it is determined penalties are applicable, the penalties imposed by IRC §6038 are asserted on Form 8278 <i>Assessment and Abatement of Miscellaneous Civil Penalties</i>.</p> <p>The Initial Penalty is asserted using Penalty Reference Number (PRN) 623.</p>	<ul style="list-style-type: none"> ▪ See Steps 1-3 ▪ IRM 20.1.9.3.4 ▪ IRM 20.1.9.3.3 ▪ IRM Exhibit 20.1.9-3 	

Step 4 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 4: Penalty Application/Closing Procedures

Now that the Notice Letter has been issued and you understand the penalty determination factors, the final steps in this process are penalty application or non-application, and case closing procedures

Considerations	Resources	6103 Protected Resources
<p>Application of Penalties – Continuation Penalty</p> <ul style="list-style-type: none"> ▪ If the Continuation Penalty applies, the Continuation Penalties are asserted on Form 8278 using PRN 619. ▪ Remember: The maximum Continuation Penalty for IRC §6038(b) is \$50,000 per required Form 8865. This is in addition to the Initial Penalty, making the total possible penalty \$60,000 per required form. 	<ul style="list-style-type: none"> ▪ Slide 4 ▪ IRM 20.1.9.3.4 ▪ IRM Exhibit 20.1.9-3 	
<p>Form 8278 – Assessment and Abatement of Miscellaneous Civil Penalties</p> <ul style="list-style-type: none"> ▪ This is the assessment document for international penalties. ▪ If a Continuation Penalty is proposed in conjunction with an Initial Penalty, a separate Form 8278 is required for each type of penalty. Enclose a computation of the penalty and the applicable code section for each penalty. ▪ Prepare a separate Form 8278 for each tax period. Calculate the total penalty due per year. ▪ The examiner will enter the dollar amount of the penalty on Form 8278 and attach Form 886-A, <i>Explanation of Items</i>. ▪ The taxpayer's signature is <i>not</i> required with respect to these penalties. ▪ Manager's signature is <i>required</i> in block 11a to meet the provision of IRC §6751. 	<ul style="list-style-type: none"> ▪ Form 8278 ▪ IRM 20.1.9.3.4 	

Step 4 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 4: Penalty Application/Closing Procedures

Now that the Notice Letter has been issued and you understand the penalty determination factors, the final steps in this process are penalty application or non-application, and case closing procedures

Considerations	Resources	6103 Protected Resources
<p>Form 886-A – <i>Explanation of Items</i></p> <ul style="list-style-type: none"> ▪ Prepare Form 886-A - for failure to file Form 8865. ▪ Form 886-A should contain sections for: <ul style="list-style-type: none"> – Facts - include all pertinent information to establish that the USP had a Form 8865 filing requirement and the USP failed to timely file or filed an inaccurate and incomplete form. – Law – Provide all relevant law, including IRC Sections, Treas. Regulations and court cases. – Taxpayer's Position - including any reasonable cause request – Service's Position - including a detailed determination on reasonable cause ▪ It is important to include all relevant information on Form 886-A. Form 886-A will be sent to the Campus for the penalty assessment or will be forwarded to Appeals if USP chooses to appeal the penalty. Pre-Post Assessment appeals processes are available. ▪ A copy of Form 886-A should be provided to USP. 	<ul style="list-style-type: none"> ▪ IRM 20.1.9.2.2 	

Step 4 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 4: Penalty Application/Closing Procedures

Now that the Notice Letter has been issued and you understand the penalty determination factors, the final steps in this process are penalty application or non-application, and case closing procedures

Considerations	Resources	6103 Protected Resources
<p>Payments</p> <ul style="list-style-type: none"> ▪ Use Form 3244, <i>Payment Posting Voucher</i>, to record the payment amount, with Transaction Code (TC) 640 if the payment is received prior to assessment or with TC 670 if the payment is received after the assessment. Include the appropriate Designated Payment Code per IRM 21.3.4.7.1.3. ▪ The payment will be posted to MFT 55 for Individuals and MFT 13 for entities. 	<ul style="list-style-type: none"> ▪ IRM 20.1.9.2(21) Payments ▪ IRM 21.3.4.7.1.3 Designated Payment Codes 	
<p>No filing requirement or accepting the filing without penalties</p> <ul style="list-style-type: none"> ▪ If the examiner determines that there is no filing requirement or that reasonable cause exist, do not prepare Form 8278. Document in the civil penalty file case history all reasonable cause provided by the taxpayer for not asserting the penalty. Advise the group secretary that no penalties were asserted and Disposal Code 02 should be used to decontrol the case. 	<ul style="list-style-type: none"> ▪ IRM 20.1.9.2.1 (3) 	

Step 4 (cont'd)

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Step 4: Penalty Application/Closing Procedures

Now that the Notice Letter has been issued and you understand the penalty determination factors, the final steps in this process are penalty application or non-application, and case closing procedures

Considerations	Resources	6103 Protected Resources
<p>Miscellaneous Case Closing Considerations</p> <ul style="list-style-type: none"> ▪ The case file should contain all work papers, correspondence, an activity record, the Form 8278 and Form 886-A. ▪ The civil penalty is <u>directly assessable</u> and not subject to deficiency procedures. ▪ The case file will be closed separate from the income tax case file using Form 3198. ▪ The case file will be sent to the Campus for assessment. (Update to MFT 13 for entities or MFT 55 for individuals.) ▪ NOTE: The ERCS P9 record may have to remain open if it represents other penalties besides those associated with a Form 8865. If so, ensure the earliest expiring penalty statute is reflected in ERCS. 		

Other Considerations / Impact to Audit

Failure to File the Form 8865 – Category 1 and 2 Filers – Monetary Penalty

Considerations	Resources	6103 Protected Resources
<p>Specific Powers of Attorney or Authorization to Disclose Tax Information:</p> <p>A Form 2848 <i>Power of Attorney and Declaration of Representative</i> (POA) is required prior to discussing penalty issues with a person other than the USP subject to the IRC §6038 penalty or required to file Form 8865 returns. The POA secured for the income tax examination is <u>NOT valid</u> for the penalty issue. A separate Form 2048 can be secured for the IRC §6038 penalty considerations.</p> <p>Form 2848 Item #3 “Description of Matter” should include words similar to “Miscellaneous Penalty Under IRC 6038” or “Civil Penalties” or “IRC 6038 Penalty” or “Chapter 61 Penalties.”</p>	<ul style="list-style-type: none"> ▪ Form 2848 ▪ Form 2848 Instructions 	

Training and Additional Resources

Chapter 12.1.2 Foreign Partnerships Information Reporting Issues

Type of Resource	Description(s) and/or Instructions for Accessing	References
Online treatise	<p>IRC § 6038 discussions of reporting requirements for USP with interest in foreign partnerships.</p> <p>The treatise is included in LB&I's Westlaw subscription in the International resources section. Expand the section to show all resources to find Bittker & Lokken: <u>Federal Taxation of Income, Estates and Gifts</u>. Click on:</p> <ul style="list-style-type: none"> ▪ Table of Contents, ▪ Part 9 (Foreign Income and Foreign Taxpayers), and ▪ Chapter 65 (International Tax Enforcement). <p>Then, scroll to ¶ 65.5.4 Reporting Requirements for U.S. Persons with Interests in Foreign Corporations and Partnerships.</p>	Fed. Tax'n Inc, Est and Gift

Glossary of Terms and Acronyms

Acronym	Definition
CCN	Chief Counsel Notice
CFP	Controlled Foreign Partnership
FP	Foreign Partnership
FSA	Field Service Advice
IDRS	Integrated Data Retrieval System
IRC	Internal Revenue Code
LB&I	Large Business & International
MFT	Master File Transaction
POA	Power of Attorney
PRN	Penalty Reference Number
TC	Transaction Code
U.S.	United States
USP	United States Person

Index of Related Issues

Issue	Associated UIL(s)	References
Failure to File the Form 8865 – Category 3 Filer Penalty (IPS Unit in production)	9434.01	<ul style="list-style-type: none"> ▪ To be developed
Failure to File the Form 8865 – Category 4 Filer Penalty (IPS Unit in production)	9434.01	<ul style="list-style-type: none"> ▪ To be developed
Information Gathering's Considering a reduction to the foreign tax credits of a U.S. shareholder that did not file Form 8865 for a foreign partnership corporation (IPS Unit in production)	9560.04	
Information Gathering's Considering penalties when a U.S. partner did not file Form 8865, Schedule P to report their acquisitions, dispositions or change in proportional interest in a foreign partnership (IPS Unit in production)	9560.15	
Information Gathering's Considering penalties when a U.S. partner did not file Form 8865, Schedule O for assets contributed to a foreign partnership in exchange for a partnership interest (IPS Unit in production)	9560.07	
Foreign Partnership Taxation	9434.01	FEN/9434.01_08(2013)
Check the Box Rules for Foreign Entities	9433.01	To be developed