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IRS concept unit on accuracy-related penalties, tax professionals urge caution

The IRS Large Business and International (LB&I) Division yesterday publicly released a “concept unit” on accuracy-related penalties under Internal Revenue Code section 6662.

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The concept unit is meant to provide instruction to IRS examiners dealing with penalty issues, but it appears to contain several significant errors.

Read the [concept unit](#) [PDF 149 KB] as posted on the IRS practice unit webpage on July 29, 2020. The IRS subsequently removed the concept unit from the IRS website (August 3, 2020).

KPMG observation

KPMG tax professionals reviewed this concept unit, and have concluded that it contains several significant errors. As a result, taxpayers and tax practitioners need to be cautious—and even hesitant—in relying on this IRS concept unit as an accurate statement regarding the rules for the accuracy-related penalties.

Some believe the most significant error is the concept unit’s misstatement of the reasonable basis standard. The reasonable basis standard may provide a defense against certain accuracy-related penalties, and is also incorporated into professional standards on return preparation and practice, including Circular 230 and the AICPA’s Statements on Standards for Tax Services. The reasonable basis standard is commonly understood as requiring that a position must have a greater than 20% likelihood of being upheld on its merits if challenged. By contrast, the concept unit states (erroneously) that reasonable basis requires a greater than 50% chance of being upheld, thereby confusing the reasonable basis standard with the higher “more likely than not” standard.

The concept unit also appears to misstate the formula for determining the amount of an underpayment. Specifically, it adds amounts previously assessed or collected to the amount of the underpayment, whereas such amounts reduce the amount of an underpayment when applying the statutory penalty computation.

In addition, the concept unit may contain other errors. As a result, taxpayers and tax practitioners need to exercise caution in relying on the concept unit as an accurate statement regarding accuracy-related penalties.

The errors described above are particularly unfortunate in that examiners following this incorrect guidance might refuse to accept valid taxpayer defenses and/or apply penalties based on an inflated underpayment amount.

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