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DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 301

REG-141669-02

RIN 1545-BB41

Waiver of Information Reporting Penalties - Determining Whether Correction is Prompt

AGENCY: Internal Revenue Service (IRS), Treasury.

ACTION: Notice of proposed rulemaking and notice of public hearing.

SUMMARY: This document contains proposed regulations relating to waiver under section 6724 of the Internal Revenue Code (Code) of a penalty imposed by section 6721 for failure to file a correct information return. The proposed regulations provide guidance on the requirement of prompt correction of the failure to file or file correctly. The proposed regulations provide that the IRS will deem information returns promptly corrected if corrected within 30 days of the required filing date, or by August 1 following that required filing date. After August 1, a correction is prompt if made by the time announced by the IRS in published guidance. The proposed regulations do not change the rules for determining reasonable cause for waiving the penalty for failure to furnish correct

payee statements under section 6722 or the time to comply with other information reporting requirements under section 6723.

DATES: Written and electronic comments are due by October 7, 2003. Requests to speak (with outlines of topics to be discussed) at the public hearing scheduled for October 21, 2003, are due by September 30, 2003.

ADDRESSES: Send submissions to: CC:PA:LPD:PR (REG-141669-02), Room 5207, Internal Revenue Service, POB 7604, Ben Franklin Station, Washington, DC 20044. Commenters may hand deliver submissions Monday through Friday between the hours of 8 a.m. and 4 p.m. to: CC:PA:LPD:PR (REG-141669-02), Courier's Desk, Internal Revenue Service, 1111 Constitution Avenue, NW., Washington, DC. Alternatively, commenters may submit comments electronically to the IRS Internet site at www.irs.gov/regs. The public hearing will be held in the IRS Auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW., Washington, DC.

FOR FURTHER INFORMATION CONTACT: Concerning the proposed regulations, contact Robert A. Desilets, Jr. at (202) 622-4910; concerning submissions of comments, the hearing, and/or to be placed on the building access list to attend the hearing, Treena Garrett at (202) 622-3401 (not toll-free numbers).

SUPPLEMENTARY INFORMATION:

Background

This document contains proposed amendments to the Procedure and Administration Regulations (26 CFR part 301) under section 6724(a) of the Code. Section 301.6724-1(d)(1)(ii)(D) of the proposed regulations will clarify when a correction of an information return is prompt for purposes of establishing reasonable cause to waive the penalty under section 6721 of the Code. Existing §301.6724-1(d)(1)(ii)(D), adopted on December 31, 1991 (56 FR 67178), provides in pertinent part that a correction is prompt if it occurs on the earliest date of a regular submission of corrections, defining regular submissions as occurring at intervals of 30 or fewer days. Many information return filers have urged the IRS to replace the 30-day correction interval with an interval corresponding to the schedule for tiered penalties.

Explanation of ProvisionsI. Section 6721

Section 6721 imposes penalties on failures to file, or file correct, information returns. Section 6721 creates a three-tiered penalty structure to encourage timely filing and prompt correction of errors in previously filed returns. Congress enacted the three-tiered penalty structure in the

Omnibus Budget Reconciliation Act of 1989 (Public Law 101-239, 103 Stat. 2388, 2389). Section 6721 generally imposes a penalty in the amount of \$50 for each return with respect to which a failure occurs, but not to exceed \$250,000 per person per calendar year. However, if a filer corrects a failure within 30 days after the required filing date, the penalty with respect to such return shall be \$15 in lieu of \$50, but not to exceed \$75,000 per filer per calendar year. Moreover, if a filer corrects a failure more than 30 days after the required filing date, but before August 1 of the calendar year in which the required filing date occurs, the penalty with respect to each return shall be \$30 in lieu of \$50, but not to exceed \$150,000 per filer per calendar year. Section 6721 provides these penalties to encourage prompt corrections of failures to file, or file correct, information returns. H.R. Rep. 101-386, at 648-649 (1989).

II. Section 6724

Section 6724(a) provides for a waiver of information reporting penalties under sections 6721 through 6723 if the failure giving rise to such penalties was due to reasonable cause and not willful neglect. Under §301.6724-1(a) of the regulations, to prove reasonable cause for a failure, the filer must establish either that there are significant

mitigating factors with respect to the failure or that the failure arose from an event beyond the filer's control (an impediment). In addition, the filer must have acted in a responsible manner both before and after the failure.

Under §301.6724-1(d) of the regulations, a filer is considered as acting in a responsible manner if the filer exercises reasonable care, i.e., the care that a reasonably prudent person would use under the circumstances in the course of business in determining filing obligations and in handling account information such as account numbers and balances. Section 301.6724-1(d) of the regulations also refers to the promptness of correction, i.e., when the filer undertook significant steps to avoid or mitigate the failure.

Section 301.6724-1(d)(1)(ii)(D) currently provides, in part, that a correction is considered prompt if it is made within 30 days after the date of removal of an impediment or discovery of a failure, or on the earliest date thereafter on which a regular submission of corrections occurs. Submissions are regular only if they occur at intervals of 30 days or fewer. Under the 30-day rule, a filer of a large number of information returns that discovers errors over a period of several months would be required to submit multiple corrections in a series of filings. Information return filers

have urged the IRS to allow filers to "bundle" their corrections, i.e., submit the corrected information returns less frequently according to a defined timetable. The IRS agrees that the current rule may be burdensome and that bundling should be permitted.

The proposed regulations provide that a correction of an information return is prompt if the filer makes the correction within 30 days of the required filing date, or by August 1 following that required filing date. After August 1, a correction is prompt if the filer makes the correction by the date or dates announced in guidance governing the electronic or magnetic filing of information returns, or in other guidance including forms and instructions. It is anticipated that the date or dates will be in November and/or December of the calendar year in which the required filing date occurs. After the dates announced in the guidance, the proposed regulations provide that a correction is prompt if it is made within 30 days after the date the impediment is removed or the failure is discovered.

The proposed regulations apply solely for the purpose of determining whether there is reasonable cause for waiving the penalty for failure to file correct information returns imposed by section 6721. The proposed regulations do not

apply for the purpose of determining whether there is reasonable cause for waiving the penalties imposed by sections 6722 and 6723. The IRS and Treasury Department believe that a filer should correct promptly a failure to furnish a correct payee statement or a failure to satisfy the reporting requirements described in section 6724(d)(2) and (3) with regard to sections 6722 and 6723, respectively. Therefore, the proposed regulations retain the 30-day correction period for waiving the penalties imposed by sections 6722 and 6723.

The proposed regulations do not affect or alter the tiered penalty rate schedule of section 6721. To ensure that a reduced penalty amount under section 6721 will apply, in the event that the IRS does not grant a reasonable cause waiver, a filer should file correct information returns with the IRS within 30 days after the required filing date, or before August 1 of the calendar year in which the required filing date occurs.

Proposed Effective Date

The proposed regulations apply to corrections of information returns made after the date of publication of a Treasury decision adopting the proposed regulations as final regulations in the **Federal Register**. However, filers may cite these rules for purposes of requesting a reasonable cause

waiver prior to the date that the proposed regulations become final.

Special Analyses

It has been determined that this notice of proposed rulemaking 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 proposed regulations, and because the proposed 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, this notice of proposed rulemaking will be submitted to the Chief Counsel for Advocacy of the Small Business Administration for comment on its impact on small business.

Comments and Public Hearing

Before adoption of these proposed regulations as final regulations, the IRS will consider any electronic or written comments (a signed original and eight (8) copies) that a commenter submits timely (in the manner described in the **ADDRESSES** portion of this preamble) to the IRS. The IRS and the Treasury Department request comments on the clarity of the

proposed regulations and how they can be easier to understand. All comments will be available for public inspection and copying. Written comments on the proposed regulations are due by October 7, 2003.

A public hearing has been scheduled for October 21, 2003, beginning at 10 a.m. in the IRS Auditorium, Internal Revenue Building, 1111 Constitution Avenue, NW., Washington, DC. All visitors must present photo identification to enter the building. Because of access restrictions, visitors will not be admitted beyond the immediate entrance area more than 30 minutes before the hearing starts. For information about having your name placed on the building access list to attend the hearing, see the **FOR FURTHER INFORMATION CONTACT** portion of this preamble.

The rules of 26 CFR 601.601(a)(3) apply to the hearing. Persons who wish to present oral comments must submit electronic or written comments and an outline of the topics for discussion and the time for each topic (a signed original and eight (8) copies) by September 30, 2003. Each person making comments will have 10 minutes to present comments. The IRS will prepare an agenda showing the scheduling of the speakers after the deadline for reviewing outlines has passed. Copies of the agenda will be available free of charge at the

hearing.

Drafting Information

The principal author of these proposed regulations is Robert A. Desilets, Jr., Office of the Associate Chief Counsel (Procedure and Administration), Administrative Provisions and Judicial Practice Division. However, other personnel from the IRS and the Treasury Department participated in their development.

List of Subjects in 26 CFR Part 301

Employment taxes, Estate taxes, Excise taxes, Gift taxes, Income taxes, Penalties, Reporting and recordkeeping requirements.

Proposed Amendments to the Regulations

Accordingly, 26 CFR part 301 is proposed to be amended as follows:

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

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

Par. 2. Section 301.6724-1 is amended by:

1. Revising paragraph (d)(1)(ii)(D).
2. Adding paragraph (d)(3).

The revision and addition read as follows:

§301.6724-1 Reasonable cause.

* * * * *

(d) * * *

(1) * * *

(ii) * * *

(D) Correcting the failure as promptly as possible upon removal of the impediment or discovery of the failure. A person may correct a failure by filing or correcting the information return, by furnishing or correcting the payee statement, or by providing or correcting the information to satisfy the specified information reporting requirement with respect to which the failure occurs. This paragraph

(d)(1)(ii)(D) does not apply with respect to information that specific information reporting rules prohibit the filer from altering. See §1.6045-4(i)(5) of this chapter. In the case of a waiver of a penalty imposed by section 6722 or 6723 of the Internal Revenue Code, correction is prompt if it is made within 30 days after the date of removal of the impediment or discovery of the failure. For purposes of section 6721 of the Internal Revenue Code, a correction is prompt if the Internal Revenue Service receives the correction--

(i) On or before 30 days after the required filing date;

(ii) On or before August 1 following that required filing

date;

(iii) On or before the date or dates announced in guidance governing the electronic or magnetic filing of information returns;

(iv) On or before the date or dates announced in other guidance including forms and instructions; or

(v) Within 30 days after the date the impediment is removed or the failure is discovered if the correction is not submitted within the time frames set forth in paragraphs (d)(1)(ii)(D)(i) through (iv).

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(3) [Reserved] For further guidance, see §301.6724-1T(d)(3).

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Robert E. Wenzel,

Deputy Commissioner for Services and Enforcement.