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IRS representation & resolution

Department of Treasury
Internal Revenue Service
Ogden, UT 84201-0002

6/19/2024

RE: Raju Pusapati & Vidyavathi Bhupathiraju
607-17-0964 & 415-89-3060
30 201812
CP3219A, February 14, 2022

Request for reasonable cause penalty abatement – Accuracy Related Penalty

Reasonable Cause: IRS Error, IRS incorrectly processed TP's amended return. [Footnote 9]

To Whom It May Concern:

We respectfully request that that the Accuracy Related Penalty be abated based on the IRS's reasonable cause criteria.

Taxpayer meets the following reasonable cause criteria [Footnote 9]

Correction of Service Error

IRM 20.1.1.3.4

(3) Other IRS error examples include the following:

c. Any other error, when it can be shown that; (1) the taxpayer did in fact comply with the law, and (2) the IRS did not initially recognize that fact.

Unable to Obtain Records

IRM 20.1.1.3.2.2.3

(3) . . . Reasonable cause may be established if the taxpayer exercised ordinary business care and prudence, but due to circumstances beyond the taxpayer's control, they were unable to comply.

FACTS:

A full 18 months (06/27/2022) after he filed the 1040X, he was assessed additional tax [Exhibit 3d] and an accuracy related penalty [Exhibit 3e].

TP had a 401k through from his employer, Deloitte Services, LP. The 401(k) was managed by Great-West Trust Company, LLC. He also had a loan against the 401(k) for ~\$40,187. In 2018 he changed employment.

Unbeknownst to him, Great-West converted the loan to a distribution. Great-West reported the conversion to the IRS, but TP did not receive a 1099 from the brokerage or his employer.

TP timely filed 30 201812^[Exhibit 1 & 3a]

On November 2, 2020, the IRS sent CP2000^[Exhibit 4].

This was TP's first indication of a problem and on 12/08/2020 he filed an amended return ^[Exhibit 2 & 3b] with a check to full pay the 1040X balance of \$9,062^[Exhibit 3c]. He also included a letter of explanation ^[Exhibit 7] and request for First Time Abatement.

The IRS "forwarded the return for processing" ^[Exhibit 3b] and processed the payment ^[Exhibit 3c].

On July 27, 2021, the IRS sent LTR 2626C ^[Exhibit 6].

TP responded to that request for an explanation, resending his original explanation and return with amendment and request for First Time Abatement.

On July 6, 2021, IRS received 30 201812X again ^[Exhibit 3h]. This return was recorded twice ^[Exhibit 3g]. Both times it was "forwarded for processing".

IRS sent LTR 4314C ^[Exhibit 10] on September 20, 2021, requesting an additional 90 days to process his reply that they received on August 16, 2021.

On November 10, 2021, IRS sent LTR2626C ^[Exhibit 9] denying TP's request for "reasonable cause abatement" of penalty. His request was for a *First Time Abatement*. TP did not know that First Time Abatement was not available for accuracy related penalties. He had sent an explanation of what happened but had not requested a *Reasonable Cause Abatement*.

REASONABLE CAUSE:

TP now comes requesting a Reasonable Cause Abatement for the justifications set forth below.

Whether the accuracy-related penalty is applied because of negligence or disregard of rules or regulations, or a substantial understatement of tax, section 6664 provides an exception to imposition of the accuracy-related penalty if the taxpayer establishes that there was reasonable cause for the understatement and that the taxpayer acted in good faith with respect to that portion. Sec. 6664(c)(1); sec. 1.6664-4(b), Income Tax Regs.; see *United States v. Boyle*, 469 U.S. 241, 242 (1985). Although not defined in the Code, "reasonable cause" is viewed in the applicable regulations as the "exercise of ordinary business care and prudence". Sec. 301.6651-1(c)(1), *Proced. & Admin. Regs.*; see *United States v. Boyle*, *supra* at 246.

The determination of whether a taxpayer acted with reasonable cause and in good faith is made on a case-by-case basis, taking into account all the pertinent facts and circumstances. Sec. 1.6664-4(b)(1), *Income Tax Regs.* Generally, the most important factor is the extent of the taxpayer's effort to assess the proper tax liability, including reliance on facts that, unknown to the taxpayer, are incorrect. ^[Footnote 7]

1. TP had reasonable cause. He had a loan against his 401(k). He filed his return with the facts that he was aware of. It was unknown to him that those facts were incorrect because he had never been provided with a 1099.

He had no way of knowing that loan would be converted to a distribution. Also, he was never made aware that it had been converted.

2. The taxpayer's effort to report the proper tax liability is the most important factor in determining reasonable cause. TP acted in good faith in regard to the portion of income being assessed the penalty. He timely filed his return with all known income sources and, once he was made aware of the conversion, promptly filed an amended return with payment in full.

TP is a conscientious taxpayer. With the 10 years prior and 5 years after this incident, he has had no issues and has timely filed & paid all taxes. Additionally, the event that started the issue was a loan on his 401(k) with employer. When TP changed employers, he had no way of knowing that the balance of that loan would be reported as a disbursement. TP had not received a 1099 for said "disbursement" before he filed and had no reason to expect one.

3. The IRS committed errors in the case. TP's transcripts show that his amended return was received 2 different times, on 12/08/2020 and 07/06/2021. Both times the returns were "forwarded for processing" and are in fact, still not processed. The IRS assessed additional tax on 06/27/2022, a full 18 months after the first filing & 12 months after the second.

This was the height of COVID 19 and when TP filed his amendment the first time, the IRS had a backlog of almost 12 million returns [Footnote 8]. This likely explains the delays in TP's amended return being processed. But as understandable as that is, that issue should weigh in the consideration for TP's good faith and attempts to comply. If the amended return had been timely processed, he would not have had the additional assessment & subsequent accuracy related penalty. The fact is, TP corrected the return as soon as he was aware of the error, including full paying the additional tax, and well before the IRS made the assessment.

In summary, taxpayer used ordinary business care & prudence in filing his 2018 1040 tax return. Upon discovery of the conversion from loan to distribution, TP immediately filed amended return & fully paid the additional tax. Because the IRS didn't process the amendment, they assessed additional tax & assessed accuracy related penalty.

In view of the foregoing, we request that taxpayer be held not liable for the accuracy-related penalty pursuant to section 6662.

If you have any questions or require further information, please feel free to contact me anytime.



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Footnotes:

1. IRC 6662Ae
 - a. (3) Special rule for amended returns. Except as provided in regulations, in no event shall any tax treatment included with an amendment or supplement to a return of tax be taken into account in determining the amount of any reportable transaction understatement if the amendment or supplement is filed after the earlier of the date the taxpayer is first contacted by the Secretary regarding the examination of the return or such other date as is specified by the Secretary.
2. IRM 20.1.5.17.5 (12-13-2016)
 - (2) The accuracy-related penalty under IRC 6662A does not apply with respect to any portion of a reportable transaction understatement if, pursuant to IRC 6664(d), it is shown that there was reasonable cause and the taxpayer acted in good faith with respect to that portion of the understatement. A taxpayer does not have reasonable cause and did not act in good faith unless:
 - a. The relevant facts affecting the tax treatment of the item are adequately disclosed in accordance with the regulations prescribed under IRC 6011 or the IRC 6707A penalty for failure to disclose is rescinded in full;
 - b. There is or was substantial authority for the treatment of the item; and
 - c. The taxpayer reasonably believed that its treatment of the item was more likely than not the proper treatment.
3. 4.10.6.2.1 (05-14-1999)
 - a. (1) A component of the accuracy-related penalty involves taxpayer's negligence or disregard of rules or regulations — Per IRC section 6662 (c), "negligence" is defined as any failure to make a reasonable attempt to comply with the provisions of this title, and the term "disregard" includes any careless, reckless or intentional disregard.
4. 33.1.2.8.1 (04-12-2013)
 - a. (3) Reasonable cause exception: The accuracy-related penalty does not apply if the taxpayer has reasonable cause and acted in good faith, i.e., if an error was due to an honest misunderstanding of the facts or the law and the taxpayer took reasonable steps to comply with the law.
5. 20.1.1.3.4 (08-05-2014) Correction of Service Error
 - a. (3) Other IRS error examples include the following:
 - a. A math error when manually computing a penalty.
 - b. An extension of time to file that did not post to the Master File (and manual input of a TC 460 did not, or will not, result in an automatic penalty reversal, if input of a TC 460 is appropriate in accordance with IRM 20.1.2.2.3.1.1, Extension of Time to File Not Found).
 - c. Any other error, when it can be shown that; (1) the taxpayer did in fact comply with the law, and (2) the IRS did not initially recognize that fact.
6. 5.1.15.16.4 (03-09-2021) Penalty Relief Denial and Appeals Exhibit 5.1.15-2
IRS Error Taxpayer claims that an IRS error caused the non-compliance; IRM 20.1.1.3.4, Correction of Service Error.
Records Unobtainable The taxpayer was unable to obtain or reconstruct records. IRM 20.1.1.3.2.2.3, Reasonable Cause.
7. Monte, Daniel F. v. Comm.; T.C. Summ. Op. 2005-77, 06/07/2005
8. TIGTA Report Number 2021-46-023, March 22, 2021; Results of the 2020 Filing Season and Effects of COVID-19 on Tax Processing Operations