Office of Chief Counsel
Internal Revenue Service

memorandum

CC: CC:TEGE:EOEG:EO1:AMacKenzie

date: August 5, 2008

to: David L. Fish
Manager, EO Technical Guidance & Quality Assurance
SE:T:EO:RA:G

from: Michael B. Blumenfeld
Senior Technician Reviewer, Exempt Organizations Branch 1 (Tax Exempt & Government Entities) CC:TEGE:EOEG:EO1

subject: Request for Opinion on the Assertion of a Penalty under I.R.C. 6652(c)(1)(A)

ISSUE

This is in response to your May 21, 2008 memorandum requesting our opinion on whether the failure to file penalty of section 6652(c)(1)(A) may be applied when a taxpayer files an outdated version of Form 990 instead of the redesigned version of the form.

CONCLUSION

The failure to file penalty of section 6652(c)(1)(A) may be applied when a taxpayer files an outdated version of the Form 990 instead of the redesigned version of the form because this will constitute (a) a failure to file in the manner prescribed, section 6652(c)(1)(A)(i), and/or (b) a failure to include all of the required information required to be shown on the return, section 6652(c)(1)(A)(ii).

FACTS

On December 20, 2007, the Internal Revenue Service released a redesigned version of the Form 990, Return of Organization Exempt from Income Tax. The form was redesigned to keep pace with the changes to the laws that apply to tax-exempt organizations and the increasing size, diversity and complexity of the sector. With the exception of certain smaller organizations for which there is a graduated transition period, tax-exempt organizations are required to use the redesigned form for the 2008 tax year.

You are concerned that some tax-exempt organizations will file the old version of the form rather than the redesigned version of the form, and that they may refuse to comply with subsequent direction for them to file the redesigned version of the form. In addition, you are concerned that you may receive filings that contain the redesigned version of the core form with the old versions of the schedules and vice versa.

You note that the redesigned version of the Form 990 requests different information and is in a completely different format than the former version of the form. Further, you note that your system for processing the form has been adjusted to accommodate the revised version of the form, and that it will be impossible as a practical matter for you to process the former version of the form. If tax-exempt organizations file versions of the form that you cannot process, it will impede your ability to perform your oversight function.

LAW and ANALYSIS

Section 6033(a)(1) states that every organization exempt from taxation under section 501(a) shall file an annual return, stating specifically the items of gross income, receipts, disbursements, and such other information for the purpose of carrying out the internal revenue laws as the Secretary may by forms or regulations prescribe. Section 1.6033-2(a)(2)(i) of the Income Tax Regulations provides, in part, that every tax-exempt organization, with exceptions not noted here, shall file its annual return on Form 990.

Section 6033(b) lists 14 specific items that must be reported on an annual return by organizations exempt from taxation under section 501(c)(3). Section 6033(b)(14) specifically provides that organizations shall furnish in the annual return "such other information for purposes of carrying out the internal revenue laws as the Secretary may require."

Section 6652(c)(1)(A) provides:

> In the case of--
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> (i) a failure to file a return required under section 6033(a)(1)... on the date and in the manner prescribed therefor (determined with regard to any extension of time for filing), or
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> (ii) a failure to include any of the information required to be shown on a return filed under section 6033(a)(1)...,
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> there shall be paid by the exempt organization $20 for each day during which such failure continues [$100 per day for organizations with gross receipts exceeding $1,000,000].[1]

Section 6652(c)(4) provides that "[n]o penalty shall be imposed under this subsection with respect to any failure if it is shown that such failure is due to reasonable cause."

The section 6652 penalty for failure to file a return was enacted in 1969. The 1969 version of the penalty applied if an organization failed to file a return required under sections 6033, 6034 or 6043(b).[2] Congress added this civil penalty because the existing sanctions for failure to file

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[1] The maximum penalty with respect to any one return is the lesser of $10,000 or 5 percent of the organization's gross receipts [$50,000 for organizations with gross receipts exceeding $1,000,000]. Id.

[2] The original 6652 penalty was found at IRC section 6652(d)(1) and read, in its entirety:

> (d) RETURNS BY EXEMPT ORGANIZATIONS AND BY CERTAIN TRUSTS.—
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> (1) PENALTY ON ORGANIZATION OR TRUST.—In the case of a failure to file a return required under section 6033 (relating to returns by exempt organizations), section 6034 (relating to returns by certain trusts), or section 6043(b) (relating to exempt organization), on the date and in the manner prescribed therefore (determined with regard to any

information returns – revocation or criminal penalties – were so great that they were never enforced. H.R. Rep. 91-413 at 37, reprinted in 1969-3 C.B. at 224. The primary purpose of the penalty, according to the legislative history, is to provide the Service with the information it needs to enforce the revenue laws. The legislative history also reflects a concern with the timeliness of the information, that more information should be made readily available to the public and State officials, and that effective administration requires obtaining complete annual information returns.

The 1969 version of the penalty provided a penalty only in the case of a "failure to file a return." See note 2, supra. In Rev. Rul. 77-162, 1977-1 C.B. 400, the Service held that a failure to file a return for purposes of applying the section 6652 penalty occurs when an organization files an incomplete return by omitting material information. In support of the holding, the Service reasoned that an incomplete return hinders the Service's ability to administer the internal revenue laws, and seriously impairs the public's right to obtain meaningful information about tax-exempt organizations via the public inspection requirements. Thus, the Service concluded that when material information is omitted from the return, a return is not filed in the manner prescribed.

Following the revenue ruling, our office has consistently advised that an organization has "failed to file a return" as described in 6652(c)(1)(A)(i) where the organization files a form but omits information on the form that the Service needs to properly administer the tax laws and to perform the duties and responsibilities placed on it by Congress; that is, when the organization has failed to report material information. The duties and responsibilities that may have been hindered include making exempt organization returns available for public inspection and conducting audits of exempt organizations to determine their compliance with statutory provisions. See GCM 39861 (1991); GCM 39805 (1989); GCM 38943 (1982); GCM 38760 (1981); and GCM 37785 (1978).[3]

We also have consistently noted that whether an item is material is an administrative rather than a legal question. The materiality depends upon what the Service requires to administer the tax laws and is a matter of judgment to be exercised by the Service. See IRC § 6033(b)(14). Thus, the materiality of specific items of information is not a matter where the Service can rely on specific legal authorities.

In GCM 39072, our office addressed the issue of filing the wrong version of a form involving employee plans. The Service required Forms 5500-C or 5500-K ("long forms") to be filed only

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> extension of time for filing), unless it is shown that such failure is due to reasonable cause there shall be paid (on notice and demand by the Secretary or his delegate and in the same manner as tax) by the exempt organization or trust failing so to file, $10 for each day during which such failure continues, but the total amount imposed hereunder on any organization for failure to file any return shall not exceed $5,000.

[3] We have stated that case law regarding omissions from tax returns is distinguishable from omissions on information returns. See, e.g., GCM 36372 (1975). Whereas failing to provide certain information on a tax return may not impact the Service's ability to compute the tax liability, omissions on an annual information return will prevent the Service from carrying out the responsibilities placed on it by Congress, including making available complete copies of filed Form 990s to the public. Thus, information requested on the Form 990 might be material, for example, to administer the tax laws by verifying whether the organization is in compliance with the exemption and other related provisions; to capture enough meaningful information about exempt organizations for the public, including state officials, grant making entities, and individual donors; and to respond to and inform Congress.

once every three years; the Form 5500-R ("short form") was to be filed for the other two remaining years. The Employee Plans Division requested our advice concerning whether the timely and complete filing of a third Form 5500-R could be treated as an incomplete return and, if so, whether assessment of a 6652 penalty was appropriate. GCM 39072 stated that the Form 5500-R did not contain many of the items contained on the long forms, and "[a]s a result, even if completed in full, the Form 5500-R would not contain all of the critical items necessary to constitute a complete return of the 5500-C or 5500-K variety." The GCM expressed concern about a good faith filing of the return and an automatic computer generated penalty, but concluded that "the return may be treated as incomplete from the time the taxpayer is notified that the return is incorrect. Thereafter, a refusal to file the proper form or a delay (not due to reasonable cause) in filing the proper form, would result in assessment of the penalty."

Section 6652 was amended in 1987 to add part (ii), a penalty for failure to include "any of the information required to be shown on a return filed under section 6033(a)(1)."[4] The budget committee report stated:

> [T]he present-law penalty applicable to exempt charitable organizations and charitable trusts for failure to file an information return required in section 6033 should also apply where the organization fails to include required information or to show the correct information on Form 990 or 990-PF. The mere filing of a return without fully and accurately furnishing the required information does not serve the enforcement and accountability objectives of the return requirement.

H.R. Rep. No. 100-391, 1617 (1987) (emphasis added). The conference report clarified that:

> The amendment to section 6652 expands the scope of the penalty provisions to apply to cases where a tax exempt organization files an annual information return but, without reasonable cause, fails to furnish on the return any required information, or furnishes incorrect information.

H. Rep. No. 495, 100th Cong., 1st Sess. 1015 (1987) (emphasis added).

It is apparent that part (ii) provides an additional ground for asserting the penalty. As amended, section 6652(c)(1)(A) imposes a penalty in cases where an organization fails to file an information return as well as in cases where an organization files a return but fails to report all of the information required on the return. As stated in GCM 39861, the penalty under subsection (i) applies even when a return is filed but material information is omitted, because this is not considered a return. "The penalty under subsection (ii) applies where the return contains all the material information but omits information required to be shown on a return filed under section 6033." Id. After the 1987 amendments, it appears that § 6652(c)(1)(A) provides a basis for imposing the penalty when any required information is omitted, whether or not that information is material.

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[4] In 1986, section 6652(d)(1) was redesignated as section 6652(c)(1), although the wording did not change. In 1987, section 6652(c)(1) was narrowed to deal only with annual returns under section 6033 [annual returns under sections 6034 or 6043(b) were moved to section 6652(c)(2), and the reasonable cause exception was moved to 6652(c)(3)]. In addition, the 1987 Act split section 6652(c)(1)(A) into (i), which contained the original wording regarding failure to file a return on the date and in the manner prescribed therefor, and (ii), which contained the added language regarding a failure to include any of the information required to be shown on a return filed under section 6033, or to show the correct information. This is substantially the same language found in section 6652(c)(1)(A) today, although the monetary amount of the penalty has since been increased.

The IRS released a redesigned Form 990, *Return of Organization Exempt From Income Tax,* on December 20, 2007. With the exception of certain smaller organizations for which there is a graduated transition period, organizations must begin using the redesigned form for the 2008 tax year (returns filed in 2009). You have stated that the revised 2008 Form 990 is in a completely different format from the old 2007 Form 990. Not only is different information sought in the new Form 990, but the similarly requested information is now located in different parts of the form. The Service's processing system for the Form 990s (such as transcription of certain parts of the form) has been adjusted to accommodate the complete revision to the form, and it will be impossible as a practical matter for the Service to process an old version of the Form 990 once these new changes are in place. Thus, a failure to file the redesigned version of the Form 990 will hinder the Service in performing the duties and responsibilities placed upon it by Congress for proper administration of the revenue laws. It is our understanding that the Service would effectively be denied all the information on the return, including many items the Service would view as material. Therefore, under these circumstances, the section 6652(c)(1)(A) penalty could be applied on the basis that the organization had failed to file a return in the manner prescribed.

In addition, the Secretary has required new information on the 2008 Form 990 that was not requested on the 2007 Form 990. Congress gave the Secretary broad power to decide what information is needed for the proper administration of the revenue laws that apply to tax-exempt organizations. 6033(b)(14). That power may be implemented by issuing forms or regulations. IRC § 6033(a)(1). A tax-exempt organization that files an old version of the form will fail to provide some "information required to be shown on a return filed under section 6033(a)(1)." Therefore, whether or not the materiality of the missing information or the processing obstacles would support the conclusion that the organization has failed to file a return, the section 6652(c)(1)(A) penalty could be applied to an organization which filed an older version of the Form 990 and not the 2008 version on the basis that it failed to include information required to be shown on a return.

We note that you intend to request that an organization file the redesigned form before you apply the section 6652(c)(1)(A) penalty. The policy objective behind the section 6652(c)(1)(A) penalty is securing compliance with the section 6033 information reporting requirements. While corresponding with the organization is not a prerequisite before imposing the penalty, it is consistent with the policy objective behind the provision. In addition, we believe this practice would place the Service in a more favorable light upon judicial review. Thus, corresponding with the organization before imposing the penalty is a sound administrative practice, and may also enhance the prospects that a court would sustain the assessment of the penalty.

LITIGATING HAZARDS

In the absence of case law on the section 6652(c) penalty, and because the phrase "required information" in section 6652(c)(1)(A)(ii) is not defined by the statute, a court's approach to the application of the penalty with respect to missing information that the IRS does not consider material is likely to be affected by the reasonableness of the IRS's process in securing use of the correct form and by the significance of the problems the IRS faces in meeting its tax administration responsibilities. This memo addresses only the circumstance where an organization files an old version of the Form 990 rather than the redesigned form. Thus, it addresses a circumstance in which multiple pieces of information solicited by the correct form have not been provided, and the return submitted cannot be processed. Under that circumstance, we believe the Service can demonstrate to a court that it has taken a reasonable

and measured approach and that the burden on tax administration is significant if the Service cannot secure a return on the correct form. This advice does not address the potential litigation hazards we may face under different circumstances, such as where the taxpayer has used the correct form but has failed to provide certain potentially non-material information on the return.

If you have any questions, please contact Amber MacKenzie or me at (202) 622-6070.