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## How to Deal with IRS Penalties

If you have infringed the tax law, you will be liable to an IRS penalty. There are various penalties for differing types of offences, so in this article I explain some of the most common ones and how to deal with them.

### 1. Late Filing Penalty

If you are late in filing your return (including extensions), you may have to pay a penalty of 5% for each month or part of a month that a return is late, not to exceed 25%. For this reason, you should file your tax returns on time even if you cannot afford to pay the tax bill.

### 2. Late Payment Penalty

If you miss the deadline to pay your taxes, you will be penalized 0.5% per month or part of the month after your deadline. If you applied for an extension, the extension is granted for filing, not for payment. You will be typically granted a 6 month extension and you will not be penalized for late payment if you have paid at least 90% of your tax due on or before the due date and pay the balance upon filing your return.

If you arrange to pay your taxes in installments, the IRS will charge you only 0.25% of the unpaid balance.

### 3. Late Filing and Payment Penalty

If you file your returns and make your payments late, your penalty would be the difference between the late filing penalty and the late payment penalty.

If you are more than two months (60 days) late in filing and paying, the minimum penalty is the smaller of \$135 or 100% of the remaining tax owed at the time of filing.

### 4. Underpayment Penalty

If you underpaid your taxes, you will be penalized. Underpaying can be due to a variety of reasons, such as poor record keeping, blatant disregard for the rules, under-declaring your income, you erroneously claim tax benefits or you did not disclose a foreign financial asset such as an overseas source of income.

Your penalty in such cases would be 20% of the underpaid amount. But it can be raised to 40% if the reason for underpayment is failure to disclose a foreign financial asset or an undisclosed noneconomic substance transaction. A transaction of economic substance would be one that changes in a meaningful way the taxpayer's economic position, and one in which the taxpayer has a substantial purpose for entering into such transaction.

### 5. Underpayment of Estimated Tax Penalty

You need to fill in Form 2210 to determine the amount of this penalty. The rate can be as small as .00008 or as high as .02383.