

Not Quite Sick Enough: The Court of Federal Claims Looks at Taxpayer Disability.

Section 6651(a)(1) of the Internal Revenue Code imposes a significant penalty for the failure to file a tax return: five percent of the tax due per month, up to a total of twenty-five percent.

There is also a failure to pay penalty of 0.5% per month under Section 6651(a)(2).

But what if the taxpayer was sick? That can make a difference, since both penalties are subject to a reasonable cause defense, and courts have recognized that a serious illness can create reasonable cause. The question is how sick does the taxpayer have to be, which the Court of Federal Claims recently addressed in *Stine v. United States*, 2012 U.S. Claims LEXIS 1258 (Fed. Cl. Oct. 23, 2012).

In September 2008, Margaret Stine filed a gift tax return for 2007, tendering payment for the tax due; because the return was late she was assessed with a penalty of \$450,000, along with interest of \$21,500. *Id.* at *2. After an unsuccessful administrative appeal, she paid the penalties and interest and filed for a refund. When the IRS did not act on her refund claim, Ms. Stine filed suit in the Court of Federal Claims.

The Court began its analysis with the language of Section 6651, which provides that a taxpayer will be subject to penalty for failure to timely file or pay “unless it is shown that such failure is due to reasonable cause and not due to willful neglect.” Next, the Court adopted an Eleventh Circuit standard, which provides that a taxpayer should not be penalized if he “convincingly demonstrates that a disability beyond his control rendered him unable to exercise ordinary business care.” *Id.* at *10 (quoting *In re Sanford*, 979 F.2d 1511, 1514 n.8 (11th Cir. 1992)).

The Court then examined the types of illnesses that have qualified for relief from penalties, noting that they tend to involve hospitalization or prolonged periods of disability. *Id.* at *12. Evidence that the taxpayer was able to conduct other business affairs also counts against relief. *Id.* On the facts before it, the Court concluded that a brief hospital stay for knee surgery, upper respiratory infections and some adverse reactions to medication were not sufficient to establish sufficient disability to excuse Ms. Stine’s failure to timely file her return and pay her gift tax. The Court placed particular weight on a tax court opinion (*Williams v. Comm’r*, 16 T.C. 893 (1951)) that held that the disability period should be of a similar duration to the failure to file. *Id.* at *17-*20. Given a record that reflected only limited periods of incapacity, the Court granted the government summary judgment on the refund claim.

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