

Department
of the
Treasury

Internal
Revenue
Service

Office of
Chief Counsel

Notice

N(35)000-172

UIL# 6404.00-00

March 22, 2000

SUSPENSION OF INTEREST UNTIL INCORPORATION
Subject: UNDER SECTION 6404(g) **Cancellation Date:** INTO THE CCDM

Purpose

I.R.C. § 6404(g), enacted by the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA 98), Pub. L. No. 105-206, provides for the suspension, subject to certain exceptions, of any interest, penalty, addition to tax, or additional amount on any tax liability due from an individual taxpayer unless notice of such liability has been provided to the taxpayer within a prescribed time period. For taxable years ending after July 22, 1998, and before January 1, 2004, the prescribed period is 18 months. The 18-month period begins on the day the return was filed or the due date of the return without regard to extensions, whichever is later. The suspension period begins on the day after the close of the 18-month period and ends on the date which is 21 days after the date on which notice of the liability is provided to the taxpayer. Section 6404(g)(3). For taxable years beginning after December 31, 2003, the suspension period will begin on the day after the close of the 1-year period after the day the return was filed or the due date of the return without regard to extensions, whichever is later. Id.

Background

Pursuant to section 6404(g)(1)(A), interest, penalties, additions to tax, and additional amounts will be suspended on any tax liability due from an individual who timely filed his or her return unless the Service has provided notice of the increased liability and the basis for such liability to the taxpayer within a prescribed time period. Section 6404(g) is applied separately with respect to each item or adjustment. Section 6404(g)(1)(B). Accordingly, a notice provided to the taxpayer within the prescribed time period will not prevent the suspension of interest, penalty, addition to tax, or additional amounts on an item or adjustment not described in such notice.

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The suspension, however, only applies if the taxpayer is an individual and it does not apply to:

1. Any penalty imposed by section 6651;
2. any interest, penalty, addition to tax, or additional amount in a case involving fraud;
3. any interest, penalty, addition to tax, or additional amount with respect to any tax liability shown on the return; or
4. any criminal penalty.

Section 6404(g)(2).

What Constitutes Notice to the Taxpayer for Purposes of Section 6404(g)

For purposes of section 6404(g), the Service provides notice of the tax liability to the taxpayer if it sends a writing to the taxpayer at his or her last known address and that writing includes the amount of the liability, the basis for that liability, and sufficient information or explanation regarding the adjustment to enable the taxpayer to challenge the adjustment.¹ Math error notices, Underreporter Program (URP) notices, revenue agent reports (RARs), 30-day letters with accompanying RARs, and statutory notices of deficiency with accompanying Form 886A, Explanation of Items, generally will be sufficient notices for purposes of section 6404(g). This list is not exclusive, and notice may be provided by letter or other writing that satisfies the statutory requirements. Audit letters that only state which items are under examination, however, are not sufficient to constitute notice for purposes of section 6404(g).

In the case of an adjustment resulting in an increased deficiency in a Tax Court proceeding, service of the pleading affirmatively alleging the increased deficiency will constitute notice of the liability. If the increased deficiency is not raised in the pleadings, but is agreed to by the parties in a stipulated decision, the stipulated decision and a letter transmitting such decision to the petitioner for signature will constitute notice of the liability. Therefore, if the increased deficiency was not affirmatively raised in the pleadings, the letter transmitting the proposed decision document to the petitioner must include the information needed to constitute a notice under section 6404(g), *i.e.*, the amount of the liability, the basis for that liability, and sufficient information or explanation regarding the adjustment to enable the taxpayer to challenge the adjustment.²

¹ Issues with respect to notices relating to an adjustment to a partnership item should be directed to the Procedural Branch of the Field Service Division.

² If the proposed decision document is prepared and transmitted to the petitioner by Appeals, the District Counsel attorney should coordinate with the appropriate Appeals Officer to ensure that this information is included in the transmittal letter.

Application of Section 6404(g)

Example 1. H and W are married taxpayers who filed their 1999 joint income tax return on April 15, 2000. On July 13, 2000, the IRS mailed to the last known address of H and W a math error notice under section 6213(b)(1) informing H and W that they had an increased tax liability of \$100 resulting from an error in the subtraction of total itemized deductions from adjusted gross income. Penalties were found not to apply.

The math error notice constitutes a notice under section 6404(g) because it states the amount of the liability and provides sufficient information and explanation regarding the error in subtraction to enable H and W to challenge the adjustment. Inasmuch as the math error notice was provided before the close of the 18-month period prescribed in section 6404(g)(1)(A), interest is not suspended with respect to the \$100 item referred to in the notice.

Example 2. T, an individual taxpayer, filed his 1998 individual income tax return on April 15, 1999. The IRS informed T that an examination of his return would be conducted. The audit was completed on January 8, 2001, when, at a closing conference, the IRS presented to T an RAR which explained in detail various adjustments to T's return, resulting in a proposed deficiency of \$5,250. The section 6651(a)(3) penalty was imposed on T for failure to pay an amount required to be shown on a return, and the section 6662(b) penalty was imposed on T for the substantial understatement of income tax.

The RAR constitutes a notice under section 6404(g) because it states the amount of the liability and provides sufficient information and explanation regarding the adjustments to T's return to enable him to challenge the adjustments. Because the RAR was provided after the close of the 18-month period prescribed under section 6404(g)(1)(A), interest on the deficiency is suspended beginning on October 17, 2000. (The 18-month period ends on Monday, October 16, 2000, because section 7503 provides that, when the last day prescribed under authority of the internal revenue laws for performing any act falls on Saturday, Sunday, or a legal holiday, the performance of the act shall be considered timely if performed on the next succeeding day which is not a Saturday, Sunday, or a legal holiday.) Interest that accrued on the deficiency during the preceding 18-month period is not abated. The last day for the suspension of interest is January 29, 2001, which is the 21st day after the day on which the RAR was provided (January 8, 2001).

Under section 6404(g), the section 6651(a)(3) penalty is not suspended for T even though the IRS failed to provide a notice within the time period prescribed in section 6404(g)(1)(A). Interest on the section 6651(a)(3) penalty is not suspended because, under section 6601(e)(2)(A), interest is imposed on the penalty from the date of notice and demand. Thus, any interest that may accrue on the section 6651(a)(3) penalty will do so only after the suspension period because the suspension period ends prior to notice and demand. In addition, section 6404(g) does not apply to the section 6662(b) penalty because the penalty is, in general, 20% of the taxpayer's underpayment and is not computed by reference to the period of time a failure relating to the return continues to exist. Therefore, the section 6662(b) penalty is not suspended for T. Under section

6601(e)(2)(B), interest is imposed on the section 6662(b) penalty from the date on which the return is required to be filed (including extensions) until the date the penalty is paid. Therefore, interest on the section 6662(b) penalty is suspended for T during the suspension period (October 17, 2000, to January 29, 2001).

Example 3. T, an individual taxpayer, filed his 1998 individual income tax return on April 15, 1999. On December 4, 1999, the IRS mailed to T's last known address an Underreporter Program (URP) notice proposing that T had a deficiency of \$150 resulting from the underreporting of interest income, which was detected through the computerized matching of Forms 1099 INT. Penalties were found not to apply with respect to this adjustment. The URP notice included a list of the Forms 1099 submitted to the IRS for T by a particular payor and revealed that the interest income reported by the payor was greater than the interest income shown on T's return. T's return was also selected for examination, and on October 19, 2000, the IRS mailed to T's last known address a 30-day letter with an RAR proposing that T had an additional deficiency of \$350 resulting from the disallowance of deductions for travel and entertainment, professional fees, and subscriptions to trade publications due to a lack of substantiation. Penalties were found not to apply with respect to these adjustments.

The URP notice is a notice under section 6404(g) because it states the amount of the liability and provides sufficient information and explanation regarding the underreporting to enable T to challenge the adjustment. Inasmuch as the notice was provided before the close of the 18-month period prescribed in section 6404(g)(1)(A), interest on the deficiency resulting from the underreporting of interest income is not suspended under this section. The 30-day letter is also a notice under section 6404(g) because it provides sufficient information and explanation regarding the disallowance of the deductions to enable T to challenge the adjustment. The 30-day letter, however, was provided after the close of the 18-month period prescribed in section 6404(g)(1)(A). The URP notice, which was issued prior to the close of the 18-month period prescribed in section 6404(g)(1)(A), pertained only to the underreporting of interest income and does not prevent the suspension of interest for other items not in the URP notice. Thus, interest on the deficiency resulting from the disallowance of deductions, as set forth in the 30-day letter, is suspended beginning on October 17, 2000. Interest that accrued on the deficiency during the preceding 18-month period is not abated. The last day for the suspension of interest is November 9, 2000, which is the 21st day after the day on which the notice was provided (October 19, 2000).

**Tax Court Litigation Involving a
Tax Year Ending After July 22, 1998**

The stipulation portion of a stipulated Tax Court decision generally includes a waiver paragraph and a paragraph acknowledging the government's right to interest on deficiencies in tax, addition(s) to tax, and penalties. In light of section 6404(g), the stipulation portion of a stipulated decision in a Tax Court case with respect to the tax liability of an individual taxpayer for a year or years ending after July 22, 1998, should also include a paragraph setting forth the period(s) for which interest is suspended under section 6404(g). We note, however, that the paragraph is not mandatory and Counsel may execute a stipulated decision without its inclusion if the petitioner refuses to stipulate to the suspension period(s). Petitioners should nevertheless be provided with a statement apprising them of the suspension periods determined in accordance with section 6404(g) at the time decision documents are provided to them for signature. Also, if the petitioner did not stipulate to the suspension period(s) under section 6404(g), or the Tax Court entered its own decision in which a deficiency is determined, Counsel attorneys should apprise Appeals of the suspension periods when the decision is transmitted to Appeals for assessment.

If you have any questions regarding this notice, please contact the Procedural Branch of the Field Service Division at (202) 622-7940.

/s/ DANIEL J. WILES for
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Associate Chief Counsel
(Domestic)