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Penalty Provisions (Replaces RAB 89-53)

(Replaced by RAB 90-25 & RAB 91-16)

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STATE OF MICHIGAN

DEPARTMENT OF TREASURY

TREASURY BUILDING

LANSING, MICHIGAN 48922

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REVENUE ADMINISTRATIVE BULLETIN 1990-5

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PENALTY PROVISIONS

(Replaces Revenue Administrative Bulletin 1989-53)

RAB-90-5. The purpose of this Bulletin is to advise and illustrate the discretionary and non-discretionary penalty provisions of the Revenue Act effective July 1, 1986.

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DEFINITIONS

Negligence:	Lack of due care in failing to do what a reasonable and ordinarily prudent person would have done under the particular circumstances.
Intentional Disregard:	Knowingly and willfully disregarding the laws, rules and instructions published and/or administered by the Department of Treasury without the intent to commit fraud or evade payment of tax.
Fraud:	Knowingly and willfully acting in a manner to commit fraud, such as: failing or refusing to file a return, or filing a false return with the intent to evade payment of tax or part of a tax; claiming a false refund or a false credit; or aiding, abetting or assisting another in an attempt to evade payment of a tax or part of a tax, claim a false refund or claim a false credit.
Information Return:	Any tax return required by the Department that does not, by law, require the payment of a tax liability. However, this definition specifically excludes an informational return wherein, as a result of reconciliation, a tax is determined due. In such cases, the tax return is treated like a non-informational return.
Non-Negotiable Remittance:	A remittance by a taxpayer on an instrument that is not legally capable of being transferred by endorsement or delivery.
Discovery:	Any deficiency or delinquency identified solely as a result of efforts by the Department, based on information already in the Department's possession or supplied by third parties. Discovery does not include a deficiency or delinquency brought to the Department's attention by the taxpayer, when the Department made no overt effort, directed either at the specific disclosure or in general at the taxpayer involved, that may have persuaded the taxpayer to disclose.
Discretionary:	A collective term that addresses the negligence, intentional disregard and fraud penalties as judgmental in application and distinctly separate from the obvious errors of failure to file and failure to pay. The application of these penalties requires the reviewer to evaluate facts, circumstances, degrees of action or omission and apply penalty accordingly.
Frivolous:	A term that describes a taxpayer's attempts to avoid or delay the payment of tax by raising arguments that are clearly insufficient or have been repeatedly found to have no merit in prior litigation.

9. Taxpayer supplies a false W-2 form showing withholding tax in excess of what was actually withheld by the employer.

10. Taxpayer supplies a false or altered property tax bill or false rent receipts to support a false claim for tax credit.

11. Taxpayer claims false Schedule C business losses on a non-existent business.

12. Taxpayer, as part of a scheme, files an excessive number of false credit claims.

Intentional Disregard

The determining factor for intentional disregard is the taxpayer's intent. When applying this penalty, the issue is whether the taxpayer has intentionally disregarded the tax laws, rules or instructions. While the intent of a taxpayer is difficult to discern, such intent will be presumed when a taxpayer has received specific instructions from the Department as to the proper reporting of an item of income or deduction, but fails to do so.

Examples of intentional disregard:

1. Taxpayer has been advised of correct reporting by either an office review or audit, but fails to report correctly in a subsequent filing.

2. Taxpayer failed to file an amended return within 120 days after a final determination by the Internal Revenue Service which affected the taxpayer's single business tax liability.

Negligence

A reasonable, prudent person will read the instructions for filing tax returns before making a determination of tax liability. If a taxpayer fails to file a tax return in accordance with instructions, negligence is presumed. Except for the no penalty situation discussed below, or where intentional disregard or fraud exists on a portion of the liability, a negligence penalty may be added to the remaining tax deficiency.

Examples of negligence:

1. The single business tax forms and instructions clearly require the addback of depreciation to the tax base, but the taxpayer fails to report or understates the amount of depreciation.

2. The income tax forms and instructions clearly require the addback of the married couple deduction to the tax base, but the taxpayer either fails to report or understates the amount of the deduction.

3. The sales tax rules, forms and instructions clearly define exempt sales to educational institutions, but the taxpayer overstates this deduction on the annual sales tax return.

4. The single business tax instructions clearly require the prepayment of at least 85% of the annual tax, but the taxpayer (without intentional disregard) remits established payments of less than 50% of the annual tax.

5. A taxpayer fails to file an income tax amended return within 120 days, as required by law, after a final alteration, modification, recomputation or determination of a deficiency under the provisions of the Internal Revenue Code.

No Penalty Situations

Certain deficiency situations occur in spite of the taxpayer's good faith effort to comply with the tax laws.

Examples of no penalty situations:

1. Taxpayer in good faith accepts a claim for sales tax exemption from an unrelated third party that proves to be wrong.

2. A business taxpayer establishes and maintains an accounting system which minimizes the likelihood of mathematical errors or mispostings.

3. An individual taxpayer makes simple transpositions or mathematical errors.

4. A taxpayer (generally within 30 days of the due date of the return) takes action to hire a different tax preparer or bookkeeper or otherwise remedy the problem when the preparer or bookkeeper:

   A. Does not submit returns to the taxpayer to be filed on time, or

   B. Does not suitably prepare returns for the taxpayer to be filed.

NON-DISCRETIONARY PENALTIES

The failure to file/pay penalties are found in the Revenue Act, MCL 205.24.

How Failure to File/Pay Penalties Are Applied

Every case involving a return and/or payment filed after the due date must be reviewed as to whether late penalties apply.

Failure to file tax return	- 5% per month (maximum 50%)
Failure to pay a tax	- 5% per month (maximum 50%)
Failure to file informational return	- $10.00 per day (maximum $400.00)
Failure to file an amnesty return	- 50%

Except for the informational returns, these penalties are a percentage of tax due after subtracting credits and prepayments.

The maximum penalty of 50% is a combined maximum for failure to file and/or pay.

The penalties for failure to file/pay are applied at the stated rate per month or fraction of a month.

Types of Non-Discretionary Penalties

Failure to File

This penalty of 5% of the tax due per month (maximum) 50%) is applied to any monthly, quarterly or annual return, or any other tax return required by law that is filed after the prescribed due date for the return or an authorized extended due date. If adjustments are made that increase the tax due, then the total tax due is subject to this penalty. The additional tax due may be subject to the discretionary penalties.

Failure to Pay

When a taxpayer has filed a return but fails to pay the tax due, the penalty of 5% of the tax due per month (maximum 50%) is added. This penalty is also applied to assessed taxes until the aggregate of 50% of the tax due has been applied.

Transitional Rule. The maximum penalty for a failure to pay or failure to file was 25% prior to July of 1986. The additional penalty maximum up to 50% will be phased in at 5% per month beginning with the month of July of 1986.

Example of transitional rule:

> The Department discovered a delinquent 1984 income tax return, and an Intent to Assess was issued August 25, 1986. The penalty for failure to pay is 35% (25% + 10% for July and August) and will continue to accrue at 5% per month until 50% is applied.

Failure to File Informational Returns

Since there is no tax due on these returns, this penalty is the only penalty applied in this situation.

A penalty of $10.00 per day for each day for each separate failure or refusal may be added. The total penalty for each separate failure or refusal shall not exceed $400.00.

Examples of information returns:

1. Annual sales tax reconciliation showing no tax due.
2. Fiduciary income tax return reporting beneficiary information showing no tax due.

WAIVER REQUEST

Any taxpayer may request, in writing to the Revenue Commissioner, a waiver of penalty. The taxpayer must be prepared to offer facts and circumstances that demonstrate acceptable reasons why the penalty should not apply.

TAXPAYER-INITIATED DISCLOSURE

A negligence penalty of 10% of the tax due will be added in lieu of other applicable penalties or prosecution when a taxpayer, agent, or personal representative of an estate discloses to the Department a tax deficiency and/or a non-filing of a return and:

1. There has been no prior contact by the Department,
2. The taxpayer is not under investigation by the Department, and,
3. The taxpayer or agent pays the tax deficiency plus applicable penalty and interest without any further action by the Department of Treasury,

FRIVOLOUS PROTEST

A penalty (the greater of $25.00 or 25% of the tax due) may be imposed when a taxpayer attempts to avoid or delay payment of tax by raising arguments that are either not valid on the surface of the argument or have repeatedly been found to have no merit in prior litigation. The Commissioner or authorized agent will apply this penalty when a taxpayer uses this tactic to delay paying a Michigan tax.

Examples include:

1. Fifth Amendment (self-incrimination) objections:
   A. Taxpayer engaged in unlawful activities.
   B. Taxpayer failed or refused to file a return with another taxing authority.
2. Unconstitutionality of the tax, asserting a basis that has repeatedly been found to be without merit:
   A. Gold and Silver Standard.
   B. 16th Amendment to the U.S. Constitution.
3. Arguing that payment received for labor (salaries and wages) is a return of capital and not income.

Additionally, Section 21(2) of the Revenue Act states the following:

> "If the taxpayer serves written notice upon the Department within 20 days after receipt of the notice to the taxpayer and remits the uncontested portion of the liability, the taxpayer may request an informal conference on the question of liability for the assessment." (Emphasis added)

Therefore, a taxpayer is required to remit payment on the uncontested portion of the tax due within 20 days of receiving the billing. If results of the conference indicate that any portion of the unpaid liability is uncontested, the frivolous penalty will apply to that uncontested portion.