Office of Chief Counsel
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Memorandum

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subject: Interest on taxes due under section 4958(a)

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ISSUE

When does interest begin to accrue on taxes due under section 4958(a)?

CONCLUSION

Interest begins to accrue on the date the return reporting the section 4958(a) tax was due, the due date of the Form 4720. In general, that date is May 15 of the year following the close of the taxable year in which the excess benefit subject to tax under section 4958(a) was provided to the disqualified person.

FACTS

Section 4958(a) imposes an excise tax on an excess benefit transaction (EBT), described in section 4958(c), between a disqualified person, described in section 4958(f)(1), and an applicable tax-exempt organization (ATEO), described in section 4958(e). The tax is reported on Form 4720, "Return of Certain Excise Taxes Under Chapters 41 and 42 of the Internal Revenue Code." A disqualified person and an ATEO engaged in an EBT; however, Form 4720 was not filed. Upon audit, the taxpayer

agreed to liability for tax on the excess benefit, signed a Form 4549-E, "Income Tax Discrepancy Adjustment," to signify that agreement, and paid the amount of the adjustment reflected on the Form 4549-E. The Service then assessed interest on the 4958(a) tax, pursuant to section 6601(a). The taxpayer objected, stating that because section 4958(a) is a penalty, section 6601(e)(2) applies and interest should not accrue until after notice and demand. The taxpayer asserted that in his case no interest should have accrued because the liability was paid with the Form 4549-E. The person's tax year was a calendar year.

LAW AND ANALYSIS

Section 6601(a) states that "[i]f any amount of tax is not paid on or before the last date prescribed for payment, interest on such amount shall be paid from the last date prescribed for payment until the date paid." For taxes required to be reported on a return, the "last date prescribed for payment" is the time fixed for filing the return, without regard to any extension of time for filing. I.R.C. 6151(a). In particular, Chapter 42 taxes shown on a return are required to be paid at the time the return is required to be filed, *without assessment or notice and demand*. Treas. Reg. § 53.6151-1 (emphasis added).

Taxes due under section 4958(a), which is part of Chapter 42, are required to be reported on an annual basis on Form 4720. Treas. Reg. § 53.6011-1(b). Form 4720 is due on the 15th day of the fifth month after the person's taxable year. Treas. Reg. §53.6071-1(f). Because the taxpayer's taxable year was a calendar year, the taxpayer had until May 15th of the year following the year of the excess benefit transaction to file Form 4720, report the transaction, and pay the tax due under section 4958(a). Interest on the 4958(a) tax began to accrue when the taxpayer failed to pay the tax by May 15.

Section 6601(e) is an exception to the general rule of Section 6601(a). Under section 6601(e), interest accrues on assessable penalties, additions to tax, and additional amounts if they are not paid within 21 calendar days after notice and demand for payment. Section 6601(e) does not apply to the present case because, for the reasons mentioned above, section 4958(a) is a tax, not a penalty.

There is no case law which addresses whether section 4958(a) is a tax or penalty. However, Latterman v. United States, 872 F.2d 564 (3d Cir. 1989), analyzed a parallel excise tax provision, section 4975, finding that the excise tax was a tax rather than a penalty, and that interest began accruing on last date prescribed for payment, rather than after the Internal Revenue Service issued notice and demand for payment. The taxpayer in Latterman argued that the statute imposed a penalty, not a tax, because of its underlying penal purpose. Id. at 569. The court disagreed: "We conclude that such an amount due should be treated as a "tax" because Congress denominated the §4975(a) assessment as a "tax," and because amounts due under §4975(a) are self-assessing." Id. at 568-69. The court regarded a tax as self assessing when, pursuant to statutory authority, the IRS provides forms and instructions on how to pay the tax.

The Latterman case is analogous to the taxpayer's situation. Section 4958(a) imposes a 25 percent tax on excess benefit transactions. The statute and its regulations use the word "tax," not "penalty." Section 4958(a) is self-assessing – it is required to be reported on a return, Treas. Reg. § 53.6011-1(b), and must be paid "without assessment or notice and demand." Treas. Reg. § 53.6151-1. Therefore, section 4958(a) is not a penalty for purposes of section 6601. Instead, section 4958(a) is a tax and section 6601(a) controls, as discussed above.

As the Latterman opinion noted, other cases that found certain Chapter 42 taxes to be penalties can be distinguished because they generally pertain to narrow issues, not applicable here, such as whether these taxes receive favorable priority in bankruptcy.. See, e.g., Rockefeller v. United States, 718 F.2d 290 (8th Cir. 1983); Farrell v. United States, 484 F. Supp. 1097 (E.D. Ark. 1980); In re Unified Control Systems, Inc., 586 F.2d 1036 (5th Cir. 1978); In re Kline, 403 F. Supp. 974 (D. Md. 1975). Latterman distinguished both Kline and Unified Control because those cases interpreted section 57(j) of the Bankruptcy Act rather than provisions of the Internal Revenue Code. "[Section] 57j made the penal nature of a tax assessment control the outcome…; it required that courts examine whether a tax assessment serves a penal or revenue-generating purpose. Section 6601 of the tax code… mandates no such inquiry." Latterman, 872 F.2d at 570. Because Rockefeller and Farrell were grounded in the analysis of Kline and United Control, they are also distinguishable. Latterman, 872 F.2d at 570.

Additionally, unlike Latterman, none of these other cases addressed the fundamental difference between self-assessing taxes, such as those under section 4958(a), that are due without notice and demand, and penalties that are due only after notice and demand. We believe Latterman was correct that the relevant inquiry to determine when interest begins to accrue under section 6601 has little to do with the purpose of the assessment, but involves the timing of a tax's due date. Id. at 567. As explained above, that inquiry leads to the conclusion that section 4958(a) imposes a tax for purposes of section 6601.

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