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THE TAX LAWYER

Jun. 20 2011 – 8:18 am

### IRS Penalties Despite Accountant's Mistake

Blaming someone else for your tax problems is understandable. No, I don't mean the government, as tempting as that might be. I mean tax advisers. Who understands taxes, anyhow?

Even members of [Congress](#)—who propose and vote on new tax laws all the time—don't even **try** to do their own taxes. Like the rest of us, they have to hire experts. So if your accountant handles it, shouldn't that fact **by itself** get you out of IRS penalties?

Not hardly. See [Relying On Tax Advisers May Not Prevent Penalties](#). Much depends on who did and said what and whether you acted reasonably. See [IRS Penalties Despite Reliance on Adviser](#), describing a [recent tax case](#) distinguishing outside tax advisers—penalties abated—from in-house tax advisers—penalties applied.

When the IRS changes your tax return it usually adds penalties and interest. Interest generally can't be waived, but "I relied on my tax adviser" is a common defense to penalties. Still, it doesn't always work.

The taxpayer may be penalized even though the adviser arguably made the mistake. The latest in the "my accountant made me do it" defense is [Woodsum v. Commissioner](#). This case involved a not exactly downtrodden taxpayer who failed to report a small little item—\$3.4 million in income—from a Deutsche Bank swap transaction.

Oops! Not only that, but [Mr. Woodsum](#) received an IRS [Form 1099](#) for the \$3.4 million. You might think the Form 1099 would prompt reporting. See [The Truth About IRS Forms 1099](#).

Plainly, Mr. Woodsum had to pay tax and interest on the \$3.4 million error. That was clear. But should he also have to pay a \$104,000 penalty for failing to report it? He argued he shouldn't have to pay since his accountant failed to put it on the return or discuss it with Mr. Woodsum.

Nevertheless, the Tax Court upheld the penalty, noting the Mr. Woodsum was no slouch in the financial arena. In fact, Mr. Woodsum himself had triggered the income by intentionally terminating the swap early because it was not performing satisfactorily as an investment. When it came to his own income, the Tax Court said he was alert and careful.

On the other hand, when he was signing his tax return and reporting his tax liability, it was a different story. He was so laissez-faire that a half million dollars in taxes slipped through the cracks. The court wasn't willing to attribute this to reasonable cause and good faith.

The court could not answer yes to each of these questions based on Mr. Woodsum's facts:

1. Was the adviser a competent professional with sufficient expertise to justify the reliance?
2. Did the taxpayer provide the adviser with necessary and accurate information?
3. Did the taxpayer actually rely in good faith on the adviser's judgment?

For more, see:

[Relying On Tax Advisers May Not Prevent Penalties](#)

[IRS Penalties Despite Dead/Embezzling Accountant!](#)

## More Tax Defenses: “I Forgot!”

### Care With Forms 1099 Helps Audit-Proof Tax Returns

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