Smith v. Comm'r, 133 T. C. 424 (2009)

In *Smith v. Comm'r*, the U. S. Tax Court ruled it lacks jurisdiction to review penalties assessed under Section 6707A of the Internal Revenue Code in deficiency proceedings. This decision clarifies that such penalties, imposed for failing to disclose participation in tax avoidance transactions, are not subject to the Tax Court's deficiency jurisdiction, impacting how taxpayers can challenge these penalties.

Parties

Sydney G. and Lisa M. Smith, the petitioners, challenged the Commissioner of Internal Revenue, the respondent, in the U. S. Tax Court. The Smiths were residents of Hawaii at the time of filing the petition.

Facts

The Commissioner issued the Smiths a notice of deficiency for tax years 2003 through 2006, determining deficiencies in income tax and assessing accuracy-related penalties under Sections 6662 and 6662A of the Internal Revenue Code. Subsequently, the Commissioner assessed additional penalties under Section 6707A for the years 2004 through 2006, totaling $300,000, for the Smiths' failure to report involvement in a listed transaction. The Commissioner also issued similar notices and assessments to Sydney G. Smith, MD, Inc. , a corporation solely owned by Mr. Smith, which resulted in a separate case.

Procedural History

The Smiths timely filed a petition with the U. S. Tax Court contesting both the deficiency notice and the Section 6707A penalty assessments. The Commissioner filed a motion to dismiss for lack of jurisdiction and to strike the Section 6707A penalties from the petition, arguing that the Tax Court does not have jurisdiction to review these penalties in a deficiency proceeding. The parties agreed that the Tax Court had jurisdiction over the issues presented in the deficiency notice but disagreed on the court's jurisdiction over the Section 6707A penalties.

Issue(s)

Whether the U. S. Tax Court has jurisdiction to redetermine a taxpayer's liability for penalties assessed under Section 6707A of the Internal Revenue Code in a deficiency proceeding?

Rule(s) of Law

The U. S. Tax Court is a court of limited jurisdiction, authorized only to the extent provided by Congress. *Naftel v. Commissioner*, 85 T. C. 527, 529 (1985). The court's jurisdiction in deficiency proceedings is governed by Sections 6211 through 6214 of

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the Internal Revenue Code, which define a “deficiency” as the amount by which the tax imposed exceeds the amount shown by the taxpayer on their return. Section 6707A penalties are assessable penalties under subchapter B of chapter 68 of the Code, which do not fall within the definition of “deficiency. “

Holding

The U. S. Tax Court lacks jurisdiction to redetermine penalties assessed under Section 6707A of the Internal Revenue Code in a deficiency proceeding. The court concluded that these penalties, which are imposed for failure to disclose participation in a reportable transaction, do not depend on a deficiency and are thus outside the scope of the court’s deficiency jurisdiction.

Reasoning

The court’s reasoning centered on the statutory definition of “deficiency” and the nature of Section 6707A penalties. The court noted that these penalties are assessable penalties, which can be imposed even if there is an overpayment of tax, and are not related to a deficiency. The court examined its historical jurisdiction over assessable penalties, finding that it has never exercised jurisdiction over such penalties unrelated to a deficiency, even absent explicit Congressional limitation. The court also reviewed the legislative history of Section 6707A, which was enacted to combat tax shelters by requiring disclosure of reportable transactions. The court concluded that the absence of an explicit exemption from deficiency procedures in Section 6707A did not confer jurisdiction, as other assessable penalties without such exemptions have been held not subject to deficiency procedures. The court’s interpretation was guided by principles of statutory construction and precedent, including cases such as *Shaw v. United States*, *Medeiros v. Commissioner*, and *Judd v. Commissioner*. The court acknowledged the concerns raised by the National Taxpayer Advocate regarding the impact of these penalties but noted its current jurisdictional constraints.

Disposition

The U. S. Tax Court granted the Commissioner’s motion to dismiss for lack of jurisdiction and to strike the Section 6707A penalties from the petition. The court retained jurisdiction over the Smiths’ deficiencies and the accuracy-related penalties under Sections 6662 and 6662A.

Significance/Impact

The decision in *Smith v. Comm’r* clarifies the jurisdictional limits of the U. S. Tax Court regarding Section 6707A penalties, affecting taxpayers’ ability to challenge these penalties through deficiency proceedings. Taxpayers must seek alternative avenues for judicial review, such as paying the penalties and seeking a refund in a different court or challenging the penalties in a collection due process hearing. The

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ruling underscores the importance of understanding the distinct procedural pathways for contesting different types of tax penalties and the implications for tax planning and compliance strategies. Subsequent cases have cited *Smith* to delineate the scope of Tax Court jurisdiction over assessable penalties, influencing the development of tax litigation strategies.

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