Oropeza v. Commissioner, 155 T. C. No. 9 (2020)

In Oropeza v. Commissioner, the U. S. Tax Court ruled that the IRS failed to secure timely supervisory approval for penalties asserted against the taxpayer, as required by IRC Section 6751(b)(1). The court found that the initial determination of penalties occurred when the IRS sent the taxpayer a Letter 5153 and Revenue Agent Report (RAR), not when the notice of deficiency was issued. This decision underscores the importance of timely supervisory approval in the penalty assessment process and impacts how the IRS must proceed in similar cases.

Parties

Jesus R. Oropeza, the Petitioner, filed a petition in the U. S. Tax Court against the Commissioner of Internal Revenue, the Respondent, challenging the imposition of penalties for the 2011 tax year. The case was designated as Docket No. 15309-15 and was filed on October 13, 2020.

Facts

The IRS opened an examination of Jesus R. Oropeza's 2011 tax year. On January 14, 2015, as the period of limitations was about to expire, a revenue agent (RA) sent Oropeza a Letter 5153 and a Revenue Agent Report (RAR). The RAR proposed adjustments increasing Oropeza's income and asserted a 20% accuracy-related penalty under IRC Section 6662(a), citing four potential bases for the penalty: negligence, substantial understatement of income tax, substantial valuation misstatement, and transaction lacking economic substance. Oropeza declined to extend the limitations period or agree to the proposed adjustments. On January 29, 2015, the RA's supervisor signed a Civil Penalty Approval Form authorizing a 20% penalty for a substantial understatement of income tax. On May 1, 2015, the RA recommended a 40% penalty under IRC Section 6662(b)(6) for a nondisclosed noneconomic substance transaction, which was approved by the supervisor. The IRS issued a notice of deficiency on May 6, 2015, asserting the 40% penalty and, in the alternative, a 20% penalty for negligence or substantial understatement.

Procedural History

Oropeza timely petitioned the U. S. Tax Court for redetermination of the deficiency and penalties. The Commissioner filed a motion for partial summary judgment, contending that timely supervisory approval was obtained for the 40% and the alternative 20% penalty for a substantial understatement. Oropeza filed a cross-motion arguing that timely approval was not obtained for any penalties. The Tax Court granted Oropeza's motion and denied the Commissioner's cross-motion, finding that the IRS failed to secure timely supervisory approval for the penalties.

Issue(s)

Whether the IRS's supervisory approval of the 20% penalty under IRC Section

© 2025 SCOTUSreports.com. All rights reserved.

6662(a) and the 40% penalty under IRC Section 6662(i) was timely as required by IRC Section 6751(b)(1)?

Rule(s) of Law

IRC Section 6751(b)(1) requires that no penalty shall be assessed unless the initial determination of such assessment is personally approved in writing by the immediate supervisor of the individual making such determination. The initial determination is considered to be embodied in the document by which the IRS formally notifies the taxpayer that the Examination Division has completed its work and made a definite decision to assert penalties.

Holding

The Tax Court held that the IRS did not satisfy the requirements of IRC Section 6751(b)(1) because written supervisory approval was not given for any penalties until after the Letter 5153 and RAR had been issued to Oropeza. Consequently, the court granted Oropeza's motion for partial summary judgment and denied the Commissioner's cross-motion.

Reasoning

The Tax Court reasoned that the initial determination of the penalties was made when the Letter 5153 and RAR were sent to Oropeza on January 14, 2015, not when the notice of deficiency was issued on May 6, 2015. The court relied on the precedent set in Belair Woods, LLC v. Commissioner, where the initial determination was considered to be embodied in the document that formally notified the taxpayer of the Examination Division's definite decision to assert penalties. The court found that the RAR asserted a 20% penalty on four alternative grounds, including a substantial understatement of income tax and a transaction lacking economic substance, and that no timely supervisory approval was obtained for these penalties. Furthermore, the court clarified that IRC Section 6662(i) does not impose a distinct penalty but increases the rate of the penalty imposed under IRC Section 6662(a) and (b)(6). Since the base-level penalty under Section 6662(a) and (b)(6) was not timely approved, the IRS could not later secure approval for the rate increase under Section 6662(i). The court emphasized the importance of timely supervisory approval to prevent the unapproved threat of penalties being used as a bargaining chip.

Disposition

The Tax Court granted Oropeza's motion for partial summary judgment and denied the Commissioner's cross-motion, ruling that no penalties could be assessed due to the lack of timely supervisory approval.

Significance/Impact

© 2025 SCOTUSreports.com. All rights reserved.

This decision reaffirms the strict requirement of timely supervisory approval under IRC Section 6751(b)(1) and clarifies that the initial determination of a penalty occurs when the IRS formally communicates a definite decision to assert penalties to the taxpayer. It has significant implications for IRS penalty assessment procedures, particularly in cases involving the assertion of alternative penalties and rate enhancements. The ruling also underscores the importance of clear communication to taxpayers regarding penalty determinations and reinforces the statutory intent to prevent the use of penalties as a negotiation tool.

© 2025 SCOTUSreports.com. All rights reserved.