

Tax Penalties Information Guide

Understanding IRS Tax Penalties

When you fail to file or pay your taxes on time, the IRS may impose penalties. Understanding these penalties can help you make informed decisions about tax extensions and payment options.

Types of Common Tax Penalties

Failure to File Penalty

This penalty applies when you don't file your tax return by the due date (including extensions).

Penalty Rates by Entity Type: For S Corporations and Partnerships:

- \$210 per month (or part of a month) per partner/shareholder - Maximum penalty: 12 months (total of \$2,520 per partner/shareholder)

For C Corporations and Individuals: - 5% of unpaid tax per month (or part of a month) - Maximum penalty: 25% of unpaid tax (reached after 5 months)

Example: If an S Corporation with 3 shareholders files 2 months late, the penalty would be: $\$210 \times 3 \text{ shareholders} \times 2 \text{ months} = \$1,260$

Failure to Pay Penalty

This penalty applies when you don't pay the taxes you owe by the due date, even if you've filed an extension.

Penalty Rates:

- 0.5% of unpaid tax per month (or part of a month)
- Maximum penalty: 25% of unpaid tax (reached after 50 months)
- Rate increases to 1% per month if the IRS issues a notice of intent to levy and you don't pay within 10 days

Example: If you owe \$10,000 in taxes and pay 3 months late, the penalty would be: $0.5\% \times \$10,000 \times 3 \text{ months} = \150

Combined Penalties

If both the failure to file and failure to pay penalties apply in the same month, the failure to file penalty is reduced by the amount of the failure to pay penalty for that month.

Example: If you owe \$10,000, file 3 months late, and don't pay during those 3 months: - Failure to file: $5\% \times \$10,000 \times 3 \text{ months} = \$1,500$ - Failure to pay: $0.5\% \times \$10,000 \times 3 \text{ months} = \150 - Combined penalty: $\$1,500 - \$150 + \$150 = \$1,500$ (not \$1,650)

Interest on Penalties

In addition to penalties, the IRS charges interest on both the unpaid tax and on the penalties themselves. The interest rate is determined quarterly and is the federal short-term rate plus 3%.

How to Avoid Penalties

File and Pay on Time

The simplest way to avoid penalties is to file and pay your taxes by the original due date.

File an Extension if You Can't File on Time

If you can't file by the due date, file an extension: - Form 4868 for individuals - Form 7004 for businesses

Remember: An extension gives you more time to file, but not more time to pay.

Pay What You Can

If you can't pay the full amount, pay as much as you can by the due date to reduce penalties and interest.

Set Up a Payment Plan

If you can't pay in full, consider setting up an installment agreement with the IRS.

Relief from Penalties

First Time Abatement (FTA)

If you have a clean compliance history for the past three years, you may qualify for the First Time Abatement program. See our detailed First Time Abatement Guide for more information.

Reasonable Cause

If you had a legitimate reason for not filing or paying on time (such as a serious illness, natural disaster, or inability to obtain records), you may qualify for penalty relief under "reasonable cause."

Statutory Exceptions

Certain situations, such as incorrect written advice from the IRS, may qualify you for statutory penalty relief.

Conclusion

Understanding tax penalties can help you make better decisions about filing extensions and paying your taxes. If you've incurred penalties, explore your options for penalty relief, including the First Time Abatement program.

Remember that filing an extension by the original due date will help you avoid the failure to file penalty, but you still need to pay your estimated taxes by the original due date to avoid the failure to pay penalty and interest.