

# Why it's important to meet the tax return filing and payment deadlines

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The May 17 deadline for filing your 2020 individual tax return is coming up soon. It's important to file and pay your tax return on time to avoid penalties imposed by the IRS. Here are the basic rules.

## Failure to pay

Separate penalties apply for failing to pay and failing to file. The failure-to-pay penalty is 1/2% for each month (or partial month) the payment is late. For example, if payment is due May 17 and is made June 22, the penalty is 1% (1/2% times 2 months or partial months). The maximum penalty is 25%.

The failure-to-pay penalty is based on the amount *shown* as due on the return (less credits for amounts paid through withholding or estimated payments), even if the actual tax bill turns out to be higher. On the other hand, if the actual tax bill turns out to be lower, the penalty is based on the lower amount.

For example, if your payment is two months late and your return shows that you owe \$5,000, the penalty is 1%, which equals \$50. If you're audited and your tax bill increases by another \$1,000, the failure-to-pay penalty isn't increased because it's based on the amount *shown* on the return as due.

## Failure to file

The failure-to-file penalty runs at a more severe rate of 5% per month (or partial month) of lateness to a maximum of 25%. If you obtain an extension to file (until October 15), you're not filing late unless you miss the extended due date. However, a filing extension doesn't apply to your responsibility for payment.

If the 1/2% failure-to-pay penalty and the failure-to-file penalty both apply, the failure-to-file penalty drops to 4.5% per month (or part) so the total combined penalty is 5%. The maximum combined penalty for the first five months is 25%. After that, the failure-to-pay penalty can continue at 1/2% per month for 45 more months (an additional 22.5%). Accordingly, the combined penalties could reach 47.5% over time.

The failure-to-file penalty is also more severe because it's based on the amount *required to be shown* on the return, and not just the amount shown as due. (Credit is given for amounts paid via withholding or estimated payments. So if no amount is owed, there's no penalty for late filing.) For example, if a return is filed three months late showing \$5,000 owed (after payment credits), the combined penalties would be 15%, which equals \$750. If the actual tax liability is later determined to be an additional \$1,000, the failure to file penalty ( $4.5\% \times 3 = 13.5\%$ ) would also apply for an additional \$135 in penalties.

A *minimum* failure to file penalty will also apply if you file your return more than 60 days late. This minimum penalty is the lesser of \$210 or the tax amount required to be shown on the return.

### **Reasonable cause**

Both penalties may be excused by IRS if lateness is due to "reasonable cause." Typical qualifying excuses include death or serious illness in the immediate family and postal irregularities.

As you can see, filing and paying late can get expensive. In addition, in particularly abusive situations involving a fraudulent failure to file, the late filing penalty can reach 15% per month, with a 75% maximum. Please contact us if you have questions.

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