



TaxNewsFlash

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Second Circuit: Early distribution 10% exaction is tax, not a penalty requiring written supervisory approval; Tax Court affirmed

The U.S. Court of Appeals for the Second Circuit today affirmed an opinion of the U.S. Tax Court that the written supervisory approval requirement under section 6751(b)(1) does not apply with regard to the section 72(t) exaction on early distributions from a qualified retirement plan because the amount under section 72(t) is a “tax” and not a “penalty,” “addition to tax” or “additional amount.”

The case is: *Grajales v. Commissioner*, No. 21-1420 (2d Cir. August 24, 2022). Read the Second Circuit’s [decision](#) [PDF 184 KB]

Background

The taxpayer received early distributions from a qualified retirement plan. The IRS determined that under section 72(t), the taxpayer was liable for a 10% exaction on these distributions.

The taxpayer argued that she was not liable for the section 72(t) exaction because the IRS’s initial determination lacked “written supervisory approval,” as required under section 6751(b)(1). In other words, she claimed that written supervisory approval was required because the section 72(t) exaction was either a penalty or an “additional amount” within the meaning of section 6751(c). The IRS admitted that there was no such written supervisory approval, but nevertheless argued that none was required because the section 72(t) exaction is not a “penalty,” “addition to tax” or “additional amount” within the meaning of section 6751(b) and (c), but instead is a “tax.”

The Tax Court agreed with the IRS and held that the section 72(t) exaction is a “tax” rather than a “penalty,” “addition to tax” or “additional amount” and thus is not subject to the written supervisory approval requirement of section 6751(b). Read [TaxNewsFlash](#)

Second Circuit

The Second Circuit today affirmed the decision of the Tax Court, finding that “the plain and unambiguous language” of section 72(t) establishes that the section 72(t) exaction is a tax, not a penalty, an additional amount, or an addition to tax within the meaning of section 6751(c) that requires written supervisory approval.

As noted by the appellate court:

Here, the statute at issue is not ambiguous; the plain language of Section 72(t) properly considered in the context of the Code establishes that the Exaction is a tax. The purpose of the Exaction, as a result, is not determinative. What matters is the meaning Congress ascribed to it. And that meaning was clearly a tax, not a penalty.

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