



Volume 1

NATIONAL TAXPAYER ADVOCATE

# Annual Report to Congress

2018

[www.TaxpayerAdvocate.irs.gov/2018AnnualReport](http://www.TaxpayerAdvocate.irs.gov/2018AnnualReport)

*This report is dedicated to  
the employees of the  
Internal Revenue Service and  
the Taxpayer Advocate Service,*

*who, despite experiencing economic hardship and anxiety  
during the recent government shutdown,  
returned to work with energy and dedication;*



*to my staff  
who worked night and day  
to get this report out in record time  
on their return from the shutdown.*

*I am forever grateful.*

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 Compilation of Legislative Recommendations to Strengthen Taxpayer Rights  
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## NATIONAL TAXPAYER ADVOCATE 2019 PURPLE BOOK Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration

## **PREFACE: Introductory Remarks by the National Taxpayer Advocate, Including an Analysis of the Initial Effects of the Government Shutdown**

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I respectfully submit for your consideration the National Taxpayer Advocate's 2018 Annual Report to Congress. Section 7803(c)(2)(B)(ii) of the Internal Revenue Code (IRC) requires the National Taxpayer Advocate to submit this report each year and in it, among other things, to identify at least 20 of the most serious problems encountered by taxpayers and to make administrative and legislative recommendations to mitigate those problems. The statute requires the National Taxpayer Advocate to submit the report by December 31, 2018; however, as I discuss later in this preface, the lapse in IRS funding meant that no TAS employees were excepted to work on finalizing the report. Thus, I am submitting the report in February 2019.

This report was conceived, back in February 2018, as a baseline representation of the IRS at that point in time. We thought it would be a helpful document for both Congress and the new Commissioner—to know where things stood, from the perspective of the taxpayers' advocate, on the eve of the first filing season under a new tax law. We wanted to reflect the taxpayer's journey as he or she navigates the tax system, from obtaining answers to tax law questions before filing to litigating tax issues in court. Hence the title of the Most Serious Problems section—"The Taxpayer's Journey"—and the organization of that section reflecting phases of the taxpayer's experience with the IRS, along with a section of "roadmaps" depicting that journey.<sup>1</sup> One of our goals in creating these roadmaps was to help readers understand the complexity of the taxpayer journey. It was challenging for us to create these roadmaps and will probably be difficult for readers to follow them, which hints at the extreme frustration many taxpayers experience when they must interact with the IRS. IRS employees also experience that a frustration as they try to navigate the system. For every step shown on the roadmaps, I note there are multiple sub-steps and detours that we did not represent, for fear of getting ourselves and everyone else completely lost.<sup>2</sup>

Then came the longest government shutdown in the history of the United States. The Annual Report staff was furloughed, along with most of TAS. On January 28, when my office reopened, it was clear that the IRS baseline had changed. The five weeks could not have come at a worse time for the IRS—facing its first filing season implementing a massive new tax law, with a completely restructured tax form. As I outline below, the IRS is entering the filing season inundated with correspondence, phone calls, and inventories of unresolved prior year audits and identity theft cases.

Lurking under all of these are profound Information Technology (IT) systems issues. The IRS systems that constitute the official record of taxpayer accounts—the Individual Master File and the Business Master File—are the oldest in the federal government and for the last 25 years the IRS has tried—and been unable—to replace them. Taxpayer information is stored in over 60 separate case management systems, so the IRS has no 360-degree view of taxpayer data. The IRS has no enterprise case selection system, so it can't be sure it is focusing on the right taxpayers or the right issues in its outreach, audit, and collection activities.

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1 See *The Taxpayer's Journey: Roadmaps of the Taxpayer's Path Through the Tax System*, *infra*.

2 We hope to convert the roadmaps into an electronic version this year, so taxpayers can input a notice or letter number and see where they are on their "journey."

The IRS desperately needs to replace its antiquated technology systems. Indeed, this is the agency's #1 need. Last year, the IRS experienced a systems crash on the final day of the tax-filing season, forcing the IRS to extend the filing season by a day. The crash prompted talk of the risk of a catastrophic systems collapse, and that risk does, indeed, exist. But there is a greater risk: IRS performance already is significantly limited by its aging systems, and if those systems aren't replaced, the gap between what the IRS should be able to do and what the IRS is actually able to do will continue to increase in ways that don't garner headlines but increasingly harm taxpayers and impair revenue collection.

And that matters a great deal because the IRS is effectively the accounts receivable department of the federal government. In fiscal year (FY) 2018, it collected nearly \$3.5 trillion on a budget of \$11.43 billion—a return on investment of about 300:1. Yet funding for IRS technology upgrades—provided through the Business Systems Modernization (BSM) account—has been very limited in both absolute and relative terms. As the following chart shows, BSM funding was reduced by 62 percent from FY 2017 (\$290 million) to FY 2018 (\$110 million) and constituted just one percent of the agency's overall appropriation in FY 2018.

**FIGURE 1, IRS Appropriations – Fiscal Years 2017–2019<sup>3</sup>**

Fiscal Year	BSM Funding	Total IRS Funding	BSM as % of Total IRS Funding
2017	\$290 M	\$11.24 B	2.6%
2018	\$110 M	\$11.43 B	1.0%
2019 (House Bill)	\$200 M	\$11.62 B	1.7%
2019 (Senate Bill)	\$110 M	\$11.26 B	1.0%

Congressional funding for the BSM account has been limited in part because the IRS has not done a good job of planning and executing technology upgrades in the past. More funding should be made available subject to accountability measures. But given the additional revenue and improved taxpayer service state-of-the-art technology is likely to bring in, I believe spending for new systems going forward should be measured in billions—not millions. In this report, our #1 legislative recommendation is that Congress provide the IRS with additional dedicated, multi-year funding to replace its core IT systems—pursuant to a plan that sets forth specific goals and metrics and is evaluated annually by an independent third party so that Congress is not merely writing the agency a blank check.

But that is forward-looking. In recent years, modernization efforts have started and stopped, in part because of funding fluctuations and in part because constant legislative changes have absorbed almost half of the IRS's IT bandwidth during the last six years, according to IRS officials. In short, the IRS is stretched to its breaking point.

This is the IRS's baseline. Because our Report was written before the shutdown, in this preface I shall attempt to describe some of the initial effects of the shutdown on the IRS, including TAS, and on U.S.

3 For fiscal year (FY) 2017 IRS funding levels, see Consolidated Appropriations Act, 2017, Pub. L. No. 115-31, Division E, 131 Stat. 135, 331-334 (2017). For FY 2018 IRS funding levels, see Consolidated Appropriations Act, 2018, Pub. L. No. 115-141, Division E (2018). At this writing, the FY 2019 appropriations act that funds the Treasury Department has not been finalized. For House-proposed funding levels, see H.R. REP. No. 115-792, at 14 (2018) (accompanying H.R. 6258, which was subsequently incorporated into and passed by the House as H.R. 6147, Division B, at 168-176, 115th Cong. (2018)). For Senate-proposed funding levels, see S. REP. No. 115-281, at 25 (2018) (accompanying S. 3107, at 12-19, 115th Cong. (2018)).

taxpayers. (The full effect will become clearer months, and even years, down the road.) I will also point out where the shutdown exacerbated trends we already identified in the Most Serious Problems section of this report. I will discuss the impact of these interruptions on IRS IT modernization efforts and advocate for multi-year funding for those efforts. And I will recommend that Congress at the very least exempt the IRS from the operation of the Anti-Deficiency Act.

Before I discuss these issues, I want to express my deep appreciation to, and admiration for, the IRS workforce, including but not limited to employees in the Taxpayer Advocate Service. Most IRS employees experienced financial challenges as a result of missing two pay checks. Some employees could not pay their bills and others were deeply worried they would miss payments if the shutdown continued for much longer. Yet when the shutdown ended, IRS employees returned to work with energy and generally hit the ground running, eager to make sure the agency could deliver the filing season as well as achieve its broader mission. The IRS faces many challenges as an agency—and this report documents many of them—but the dedication of the IRS workforce is a notable bright spot.

### IRS Operations Before the Shutdown

On December 21, 2018, the day before the shutdown, the IRS was already struggling with its inventory of work. During 2018, the IRS shuffled resources around to meet the challenge of implementing the new tax law while wrestling with record inventory levels of unresolved cases in its fraud detection programs.<sup>4</sup> In addition, the IRS was directed to replace all the existing Individual Income Tax Return forms—the 1040, 1040A, and 1040EZ—with a single new Form 1040. This new form was reduced to the size of a postcard, two half pages in length, on which it is estimated approximately 47 million taxpayers (32 percent) could meet their filing requirements. By reducing the 1040 to a postcard size, however, this redesign necessitated the creation of an additional six schedules, some containing only three lines of information. Thus, for approximately 70 percent of taxpayers—nearly 102 million—the six new schedules increase the number of already existing schedules, such as A, B, C, D, or E, that taxpayers must complete.<sup>5</sup> While many taxpayers will use software to complete the return, the new schedules will force some taxpayers to cross-reference and transfer data such as credits, deductions, and income, increasing the potential for errors to occur since the tax information is dispersed over many pages and needs to be tracked down and reported on different schedules and forms.

The new tax law also required a “surge” of tax instructions and publications, as well as notices, FAQs, and regulations. IRS functions were asked to detail employees to the IRS Forms and Publications office for six months and longer to enable it to keep up with the demand and schedule. Chief Counsel guidance projects that were long scheduled and anticipated were put on hold while Counsel attorneys focused on interpreting major provisions of the new tax law. Once again, as with the Patient Protection and Affordable Care Act (ACA)<sup>6</sup> and the Foreign Account Tax Compliance Act (FATCA)<sup>7</sup>, key IT personnel were moved from ongoing modernization or enhancement efforts to work on delivery of the

4 See Most Serious Problem: *False Positive Rates: The IRS’s Fraud Detection Systems Are Marred by High False Positive Rates, Long Processing Times, and Unwieldy Processes Which Continue to Plague the IRS and Harm Legitimate Taxpayers*, *infra*.

5 TAS research estimates that 68 percent of taxpayers will need to file one or more schedules of the 2018 Form 1040 based on tax year (TY) 2016 tax return filing data. IRS Compliance Data Warehouse (CDW), Individual Returns Transactions File, TY 2016. For example, using the new 1040, a taxpayer with unemployment compensation, student loan interest deduction, and child and dependent care expenses will now have to file Schedules 1 and 3, whereas with the 2017 1040, they only needed to file the main form, which was two pages.

6 See Patient Protection and Affordable Care Act (ACA) of 2009, Pub. L. No. 111-148, 124 Stat. 119 (2010), as amended by the Health Care and Education Reconciliation Act (HCERA) of 2010, Pub. L. No. 111-152, 124 Stat. 1029 (2010).

7 See Hiring Incentives to Restore Employment Act, Pub. L. No. 111-147, 124 Stat. 71 (2010) (adding Chapter 4 of Internal Revenue Code (IRC) §§ 1471-1474; 6038D), collectively referred to as the Foreign Account Tax Compliance Act (FATCA).

new tax law and forms. Because of the revamp of the tax forms, the electronic filing requirements were not issued to private tax software vendors and electronic return originators until September 2018, much later than in previous years.

While the 2018 filing season went well for millions of taxpayers (excluding the filing glitch on April 17, 2018, which led to the IRS extending the filing season by a day), the IRS's fraud detection system wreaked havoc for hundreds of thousands of taxpayers and created manual rework for IRS employees. The IRS's fraud detection filters and models identify questionable refund returns. As we recount in the Most Serious Problem *Fraud Detection: The IRS's Fraud Detection Systems Are Marred by High False Positive Rates, Long Processing Times, and Unwieldy Processes Which Continue to Plague the IRS and Harm Legitimate Taxpayers*, however, the part of the process that was supposed to recycle returns back through the wage database as new wage data came in from employers and the Social Security Administration completely failed, requiring the IRS to *manually upload* wage data and *manually process* frozen returns through the system. It was not until late July 2018 that the IRS had waded through all the frozen refund returns and determined which were legitimate and which were not.

The result of this process was an 81 percent False Positive Rate (FPR). *That is, of all the returns initially frozen by this system as suspect, 81 percent were legitimate.* Of the returns still unreleased one month after the initial freeze, 64 percent were legitimate. Not surprisingly, taxpayers did not take this lying down. TAS cases involving this issue increased by 287 percent from January 2018 through September 2018, and for the first time ever, the NTA Case Intake line experienced two-hour wait times, as taxpayers called desperate to figure out when their refunds would be released.<sup>8</sup>

The fraud detection debacle had another consequence—frozen refund returns with Earned Income Tax Credit (EITC) claims were sent to the examination function, which was not prepared for this onslaught of cases. Thus, on December 21, 2018, the day before the shutdown, the IRS had not worked through its inventory of tax year (TY) 2017 EITC audits, meaning it was starting the 2019 filing season already behind in that category of work.

Meanwhile, the perennial staffing declines—well documented in past Annual Reports—continued to negatively affect the IRS's ability to deliver its audit and collection workplans, leading to across-the-board efforts to “streamline” audits and collection.

- With respect to the IRS examination function, we show in this report that the IRS's field audit selection is deeply flawed, resulting in no change rates on average of 23 percent for audits conducted by the Small Business/Self-Employed Division (SB/SE) and 32 percent for audits conducted by the Large Business and International Operating Division (LB&I).<sup>9</sup>
- The IRS correspondence examination function, which conducts 71 percent of all audits (individual and business), has the highest no response and lowest agreement rates of any audit type, and none of the audit streams measure the future compliance of the taxpayers who were audited, or whether those taxpayers understood what they did wrong.<sup>10</sup>

<sup>8</sup> Taxpayer Advocate Management Information System; TAS, Aceyus Phone Reporting System (Feb. 20, 2018).

<sup>9</sup> IRS, CDW, AIMS FY 2010 through FY 2018 (Dec. 2018). Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process. For a detailed discussion of the field audit process, see Most Serious Problem: *Field Examination: The IRS's Field Examination Program Burdens Taxpayers and Yields High No-Change Rates, Which Waste IRS Resources and May Discourage Voluntary Compliance*, *infra*.

<sup>10</sup> See Most Serious Problem: *Correspondence Exam: The IRS's Correspondence Examination Procedures Burden Taxpayers and are not Effective in Educating the Taxpayer and Promoting Future Voluntary Compliance*, *infra*.

In fact, a study we publish in this report shows that, overall, taxpayers in the study who experienced audits reported higher levels of fear, anger, threat and caution when thinking about the IRS and felt less protected by the IRS.<sup>11</sup> Taxpayers who experienced correspondence exams report a lower level of perceived justice compared to those who underwent office and field exams. A 2015 TAS study found that self-employed taxpayers filing a Schedule C who experience a no change audit reduced their reported income by 37 percent three years after the audit.<sup>12</sup> How the IRS conducts audits clearly has an effect on taxpayers' willingness to comply.

In collection, the IRS is *actively* discouraging and avoiding person-to-person conversations with taxpayers. It is intentionally not placing phone numbers on its correspondence or burying that information on the last page of multi-page communications.<sup>13</sup> Instead, it is pushing taxpayers to the internet to enter into “streamlined” installment agreements (IAs). It has expanded these streamlined IAs to six- and seven-year terms—that is, the taxpayer can agree to make monthly payments by dividing the tax debt by 72 or 84 months, without any financial analysis as to whether a taxpayer can actually afford to make these payments.<sup>14</sup>

No surprise, then, that TAS research found that in FY 2018:

- About 40 percent of taxpayers who entered into streamlined IAs within the Automated Collection System (ACS) had incomes at or below their Allowable Living Expenses (ALEs), meaning these taxpayers entered into IAs when they could not afford to pay their basic living expenses, according to the IRS's own definition.<sup>15</sup>
- About 39 percent of streamlined IAs within ACS involving taxpayers with income at or below their ALEs defaulted in FY 2018.<sup>16</sup>
- This sad situation is reproduced in the Private Debt Collection initiative, which utilizes the IRS's streamlined IA authority. In FY 2018, 37 percent of taxpayers defaulted on IAs entered into while assigned to the Private Collection Agencies (PCAs) and 40 percent of taxpayers who entered into PCA IAs had incomes below their ALEs.

All this taxpayer harm is driven by a lack of resources, and they are justified by the IRS as “efficiencies” and “Future State” initiatives. But these approaches are neither efficient nor effective. They represent a failure to conduct effective tax administration by not engaging with and educating the taxpayer and promoting future voluntary compliance.

This, then, was the state of affairs as of December 21, 2018, when the IRS shut down.

11 See Brian Erard, Matthias Kasper, Erich Kirchler, and Jerome Olsen, Research Study: *What Influence do IRS Audits Have on Taxpayer Attitudes and Perceptions? Evidence from a National Survey*, *infra*.

12 National Taxpayer Advocate 2015 Annual Report to Congress, vol. 2, 88 (Research Study: *Audit Impact Study*).

13 See Most Serious Problem: *Collection Due Process Notices: Despite Recent Changes to Collection Due Process Notices, Taxpayers Are Still at Risk for Not Understanding Important Procedures and Deadlines, Thereby Missing Their Right to an Independent Hearing and Tax Court Review*, *infra*.

14 See Most Serious Problem: *IRS's Automated Collection System (ACS): ACS Lacks a Taxpayer-Centered Approach, Resulting in a Challenging Taxpayer Experience and Generating Less Than Optimal Collection Outcomes for the IRS*, *infra*.

15 *Id.*

16 TAS Research analysis of the Individual Master File and Individual Returns Transaction File on installment agreements established in FY 2018. This figure assumes taxpayers have one IRS-allowed vehicle ownership and operating expense, and a second operating expense if they were married filing jointly. If we assume the taxpayers did not have vehicle ownership expenses, the default rate would be about 32 percent.

### A Brief Primer on the Anti-Deficiency Act

Article I of the Constitution provides that “No Money shall be drawn from the Treasury, but in Consequence of Appropriations made by Law.”<sup>17</sup> The Anti-Deficiency Act (ADA) implements this provision.<sup>18</sup> Specifically, 31 U.S.C. § 1341(a)(1)(B) forbids any officer or employee of the United States government or of the District of Columbia government to involve his or her respective government employer in a contract or obligation for the payment of money before an appropriation is made unless authorized by law. A significant exception to this rule is provided in 31 U.S.C. § 1342, which permits such government activity “for emergencies involving the safety of human life or the protection of property.”

A 1981 Attorney General opinion clarified that two factors must be present for this exception to apply:

1. A reasonable and articulable connection between the obligation (the opinion involved a contract or grant) and the safety of life or the protection of property; and
2. Some reasonable likelihood that either the safety of life or the protection of property would be compromised to some significant degree by failure to carry out the function in question—and that the threat to life or property can be reasonably said to be near at hand and demanding of immediate response.<sup>19</sup>

A 1995 Department of Justice opinion reiterated the two-prong analysis and interpreted the 1990 amendment to the ADA, noting the emergencies exception only applies where the threat is “near at hand and demanding of immediate response.”<sup>20</sup> It further concluded the threat must be significant in nature.

OMB guidance from 1981 excepts tax-related activities of the Treasury.<sup>21</sup> The way in which the IRS interprets this exception—not always consistently—can be seen in its shutdown plans. In 2011, some of the activities that the IRS included in the category of necessary for the safety of human life or protection of property were: processing of tax returns, taxpayer service centers and call sites, and protection of statute expiration, bankruptcy, liens and seizure cases.<sup>22</sup> The IRS excepted 57 TAS employees under this category in 2011. It also excepted 1,263 ACS employees to handle levy release calls from taxpayers.<sup>23</sup> In 2013, however, the IRS did not consider taxpayer service centers and call sites necessary for the safety of human life or protection of property exceptions, nor did it except any ACS employees to handle levy release calls from taxpayers. And no TAS employees, including the National Taxpayer Advocate, were excepted under the 2013 shutdown.

The IRS Office of Chief Counsel has adopted the position that the exception for protection of life and property applies only to prevent imminent loss of life or property and the protection of property exception applies only to *government* property.<sup>24</sup> Furthermore, Chief Counsel attorneys concluded that activities related to preventing significant hardship to individual taxpayers do not fit the exception. “The types of activities the [National Taxpayer Advocate] performs to prevent taxpayer hardship are

17 U.S. CONST. Art. I, § 9, cl. 7.

18 Pub. L. No. 97-258, 96 Stat. 923 (1982).

19 43 U.S. Op. Atty. Gen. 293, 302 (Jan. 16, 1981).

20 Office of Management and Budget (OMB), Memorandum M-95-18 Assistant Attorney General Walter Dellinger, *Memorandum for Alice Rivlin, Director, Office of Management and Budget* 9 (Aug. 16, 1995).

21 OMB, *Memorandum for Heads of Executive Departments and Agencies* 2 (Nov. 17, 1981).

22 *IRS FY 2011 Shutdown Contingency Plan (During Lapsed Appropriations)* 6 (Apr. 7, 2011).

23 *Id.* at 38.

24 Office of Chief Counsel, General Legal Services, *Points on Government Shutdown Issues Pertaining to National Taxpayer Advocate* (Sept. 27, 2013).

not the types of activities related to protecting the public welfare that OMB has identified.”<sup>25</sup> Upon questioning by the National Taxpayer Advocate, Chief Counsel personnel maintained that “safety of life” applied only in the context of public health, such as meat inspectors. Thus, neither of these exceptions would allow personnel to be excepted to issue a refund or release a levy in order to allow the taxpayer to obtain access to funds to receive a life-saving operation, for example. Nor could the IRS use resources to release a levy where it is depriving the taxpayer of funds to pay for basic living expenses, even if the levy could leave the taxpayer homeless.

### IRS 2018 Non-Filing Season Lapse Plan

On November 29, 2018, in anticipation of a lapse in funding, Treasury issued *IRS FY2019 Lapsed Appropriations Contingency Plan (Non-Filing Season - December 8-31, 2018)* that would apply in the event of a shutdown due to a lapse in appropriations outside the filing season. The plan identifies 9,946 employees, 12.5 percent of the IRS workforce, who would not be furloughed.

According to the plan:

- 3,337 IT employees would work during the shutdown, 1,457 of whom are in the Associate Chief Information Officer (ACIO) Enterprise Operations function, which is part of the Deputy Chief Information Officer for Tax Reform and Filing Season office. Of these 1,457 employees, 555 are in the Enterprise Computing Center (ECC) Division, which maintains IRS computer applications and prevents IRS computer processing from shutting down completely.
- Another 414 Small Business/Self-Employed (SB/SE) employees would be needed under the nonfiling season plan, 310 of whom work in collection, most often in field collection (165). Among other things, these employees process tax returns which include remittances, protect the government’s interests in the context of statute expirations, bankruptcy, liens, and seizure cases, handle budget matters related to the lapse in appropriations, and administer contracts.
- Another 2,241 Wage and Investment (W&I) employees would be needed under the nonfiling season plan, of whom 1,029 are submission processing employees, to process tax returns that contain remittances; 374 W&I accounts management employees would also be needed to process remittances and for statute protection.

Under the plan, the National Taxpayer Advocate and Local Taxpayer Advocates (LTAs) would be excepted for purposes of periodically checking mail and processing payments. They would not be authorized to intake cases, issue Taxpayer Assistance Orders (TAOs), or take other actions to address significant hardships and emergencies, including ordering the release of liens or levies.

### IRS 2019 Filing Season Lapse Plan

On January 15, 2019, the IRS issued the *IRS FY2019 Lapsed Appropriations Contingency Plan (Tax Year 2018 Filing Season)* to apply in the event of a shutdown due to a lapse in appropriations at any time during the TY 2018 filing season (January 1-April 30, 2019). The plan identifies 46,052 employees, 57.4 percent of the IRS workforce, who would not be furloughed.

25 Office of Chief Counsel, General Legal Services, *Points on Government Shutdown Issues Pertaining to National Taxpayer Advocate* 3 (Sept. 27, 2013).

According to the filing season plan 3,766 IT employees would work during the shutdown.

- The number of excepted employees in ACIO Enterprise Operations remained the same (1,457), but excepted employees in the ACIO User and Network Services increased to 627 from the nonfiling season plan level of 308. Among other things, these employees provide day-to-day maintenance of the IRS tax infrastructure.
- The number of excepted employees in ACIO, Applications Development, increased to 958 from the nonfiling season plan level of 798. These employees work to prevent loss of data in process and revenue collections, provide application support for critical systems, manage code, perform builds, process transmittals, and complete and test filing year programs.

The filing season shutdown plan calls for 2,938 excepted SB/SE employees, of whom 2,614 are collection employees.

- The number of excepted field collection employees remained the same as in the nonfiling season shutdown plan.
- The number of excepted campus collection employees increased from 64 employees in the nonfiling shutdown plan to 2,229. Most of these employees (1,839) are collection representatives, who respond to taxpayers who have received a collection notice through ACS, assist taxpayers with setting up installment agreements for tax payments, assist taxpayers with general collection processes, serve as the gateway for transferring taxpayers to Accounts Management for appropriate filing season inquiries, and provide assistance with releasing levies and liens as required by law. However, consistent with IRS Chief Counsel's position, later guidance clarified that these employees *are not* authorized to release levies and liens.<sup>26</sup>

In addition, the filing season shutdown plan provides for an SB/SE Mail Plan, for which 560 employees are needed.

- Of these, 250 collection employees protect statute expiration or assessment activities, protect bankruptcy or other revenue generating issues, oversee the collection of taxes and processing of returns, process tax returns which include remittances, complete computer operations necessary to prevent loss of data in process and revenue collections, handle budget matters related to the lapse in appropriations, and administer contracts.
- An additional 310 SB/SE Exam employees carry out similar tasks.

The filing season shutdown plan provides for 34,357 excepted W&I employees.

- Of these, 17,644 are accounts management employees (compared to 374 accounts management employees excepted under the nonfiling season plan). Of these employees, 17,520 are needed to process Form 1040X's and remittances, provide statute protection, support the Tax Cut and Jobs Act, and staff call sites.
- 13,469 submission processing employees are excepted (compared to 1,029 in the non-filing season plan). Of these, 13,000 are needed to process tax returns, Form 1040X remittances, and refunds.

<sup>26</sup> See IRS SERP Alert #19A0017, *Release of Levy and Release of Lien* (Jan. 23, 2019) (“While there is a lapse in funding during the partial shutdown we are not authorized to take this action. We may do so once we are fully opened, so please call us back at that time. Please apologize to the taxpayer and explain we are not authorized to release the levy or lien due to the partial government shutdown. Explain that they may call us back after we are fully reopened.”).

### Treatment of Taxpayers Experiencing Economic Hardship Under the Lapse Plans

Under the 2018 and 2019 Lapse Plans, the National Taxpayer Advocate, Deputy National Taxpayer Advocate, and LTAs are excepted to check mail in order to process payments. However, with respect to the 2019 Filing Season Plan, Chief Counsel has opined that TAS acts “derivatively” in solving refund problems and addressing collection issues and therefore cannot conduct those activities during a shutdown.<sup>27</sup> Thus, despite the requirement under IRC § 6343(a)(1)(D) that the IRS release any levy that creates an economic hardship for a taxpayer, and the explicit charge in IRC § 7811(b)(1) that the National Taxpayer Advocate may issue a TAO “to release property of the taxpayer levied upon” where the taxpayer is experiencing significant hardship, no IRS or TAS employee, including the National Taxpayer Advocate, was excepted to work these cases.

Moreover, the Treasury Department determined that the completion and issuance of the statutorily-mandated National Taxpayer Advocate’s Annual Report to Congress, which identifies at least 20 of the most serious problems facing taxpayers, did not meet the ADA exception as “authorized by necessary implication from the specific terms of duties that have been imposed on, or of authorities that have been invested in, the agency.”<sup>28</sup>

Thus, during the first part of the shutdown, no IRS employees were authorized to answer the telephone lines, issue refunds, release liens and levies, enter into installment agreements, or review pending IRS actions. On January 22, under the 2019 Filing Season plan, IRS employees were excepted to answer the phone lines, issue refunds, and enter into installment agreements. They were not, however, authorized to release liens and levies, nor were TAS employees authorized to advocate on behalf of taxpayers who were experiencing significant hardship as a result of the IRS’s actions or inactions.

### Impact of the Shutdown on IRS Operations

As described earlier, on December 21, 2018, the IRS was already in a position of entering the filing season with a backlog of items and with its resources stretched thin. Figure 2 presents the state of various types of key work and measures on three key dates: December 22, 2018 (the first day of the shutdown); January 26, 2019, (the end of the fifth week of the shutdown when some employees were called back to work under the 2019 Filing Season Lapse Plan); and February 2, 2019 (the end of the first week of the filing season after the shutdown ended).

27 The IRS Office of Chief Counsel opined as follows:

We have determined that TAS may continue to issue manual refunds and enter into streamlined installment agreements, because TAS has authority to take these actions on behalf of IRS.

In contrast, there are a number of functions listed in the Plan where TAS acts derivatively, serving as a conduit or advocate for action by other business units. This includes, for example, fixing refund issues and assisting with general collection processes. As to these derivative functions, we have concluded that there is insufficient evidence that Congress intended for the functions to continue during a lapse in appropriations. In reaching this conclusion, we relied on guidance from the Office of Legal Counsel (OLC). OLC has stated that there is implied authority for an unfunded function to continue during a lapse if the function is “necessary to the effective execution of” a function that has funding or is excepted, “such that suspension of the [unfunded] function[] ... would prevent or significantly damage the execution of [the funded or excepted] function[.]” OLC, *Effect of Appropriations for Other Agencies*, 19 Op. OLC 337, 338 (Dec. 13, 1995). Upon considering TAS’s role and its statutory mandates, we do not believe that Congress has implied that suspension of TAS’s derivative functions would prevent or significantly damage IRS’s execution of its tax collection and refund issuance functions.

Email from Senior Counsel, General Legal Services to Deputy National Taxpayer Advocate (Jan. 17, 2019).

28 See Op. Attorney Gen. 293, 296-301 (1981). “Page 97 of the revised plan shows a number of Taxpayer Advocacy [sic] Service employees excepted to prepare the annual TAS report to Congress. Even though there is a specific statutory deadline for the report, we do not consider a reporting deadline of this type sufficient to create an implied exception to the Anti-Deficiency Act. Therefore, the exception on this basis will need to be removed before I can clear the plan as legally sufficient.” Email from Deputy Director, Office of Emergency Preparedness, U.S. Department of Treasury (Nov. 30, 2018).

On January 24, 2019, the IRS had over 5 million pieces of mail that had not been batched for processing; it had 80,000 responses to FY 2018 Earned Income Tax Credit audits that had not been addressed; it had 87,000 amended returns waiting to be processed.<sup>29</sup> During the shutdown, the National Distribution Center's (NDC) inventory grew to about 170,000 orders.<sup>30</sup> Despite employees working overtime to process about 11,000 orders a day, the IRS announced that orders for Forms W-2 and W-3 were backlogged and would not be finished shipping out until mid-February. By law, employers are required to file these information returns by January 31; the IRS therefore suggested that employers consider requesting filing extensions.

At key points in the return processing pipeline, inventories were up over 100 percent over the same time in 2018. For the week ending January 26, 2019 (the last week of the shutdown), the level of service (LOS) on the Accounts Management phone lines was 36.8 percent and the average speed of answer (ASA) was 32 minutes. The LOS and ASA for the Installment Agreement/Balance Due phone lines was abysmal—12.8 percent and 93 minutes respectively. By February 2, 2019, the end of the first week after the shutdown ended—that is, the first week of the filing season—most levels only slightly improved. There was one significant exception: the LOS for the Balance Due/Installment Agreement line was 6.7 percent. *This means for that week 93.3 percent of the taxpayers calling to make payment arrangements were unable to speak to a live assistor.*

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29 IRS Senior Leadership Appropriations Lapse Daily Call (Jan. 25, 2019).

30 Email from Commissioner, Wage & Investment (W&I) Operating Division, to National Taxpayer Advocate (Jan. 24, 2019).

**FIGURE 2, Selected IRS Inventories and Levels of Service Pre-Shutdown and Post-Shutdown**

Description	Week Ending 12/22/2018	Week Ending 1/26/2019	% Change from Week Prior to Shutdown to Week Ending 1/26/2019	Week Ending 2/2/2019	% Change from Week Prior to Shutdown to Week Ending 2/2/2019
Level of Service for the Accts. Mgmt. <sup>a</sup>	75.4%	36.8%	-51.2%	48.3%	-35.9%
Average Speed of Answer (AM) <sup>b</sup>	12.8	31.9	149.2%	17.0	32.8%
Level of Service for ACS <sup>c</sup>	69.1%	30.9%	-55.3%	38.3%	-44.6%
Average Speed of Answer (ACS) <sup>d</sup>	15.7	51.9	230.6%	48.3	207.6%
Level of Service for the Installment Agreement/Bal. Due Line <sup>e</sup>	54.6%	12.8%	-76.6%	6.70%	-87.7%
Average Speed of Answer for the Installment Agreement/Bal. Due Line <sup>f</sup>	23.2	93.00	300.9%	80.6	247.4%

- a IRS, Joint Operations Center (JOC), *Snapshot Reports: Enterprise Snapshot* (Dec. 23, 2017, Jan. 27, 2018, Feb. 3, 2018, Dec. 22, 2018, Jan. 26, 2019, and Feb. 2, 2019).
- b *Id.*
- c IRS, JOC, *Snapshot Reports: Product Line Detail* (Dec. 23, 2017, Jan. 27, 2018, Feb. 3, 2018, Dec. 22, 2018, Jan. 26, 2019, and Feb. 2, 2019).
- d *Id.*
- e *Id.*
- f *Id.*

Figure 3 shows where the IRS was in terms of several key work measures and the percentage change for all these activities when compared to the same period for the prior year. Immediately before the shutdown, the IRS’s main phone line was significantly improved over the same period the year before (75.4 percent LOS for FY 2019 compared to 56.8 percent LOS in FY 2018).<sup>31</sup> But the difference between FY 2018 and FY 2019 for levels of service and wait times for *all phone lines* at the end of the shutdown and the first week all employees returned is ... shocking. For example, the LOS for both the Accounts Management and ACS phone lines experienced at least a 56 percent decrease in FY 2019 from FY 2018 levels.<sup>32</sup> For the week ending February 2, 2019, which was the first week of the filing season, these same lines continued to show a decrease of over 40 percent from FY 2018 levels. Specifically, the Accounts Management lines had 48 percent LOS and a 17 minute wait time, compared to 86 percent LOS and a 4 minute wait time in FY 2018; the ACS lines had a 38 percent LOS and 48 minute wait time, compared to a 65 percent LOS and a 19 minute wait time in FY 2018.<sup>33</sup>

Make no mistake about it, these numbers translate into real harm to real taxpayers. And they represent increased rework for the IRS downstream, at a time when the IRS is already resource challenged. The IRS will be facing tough decisions as it revises its workplans for FY 2019 in light of the shutdown’s impact.

31 IRS, Joint Operations Center (JOC), *Snapshot Reports: Enterprise Snapshot* (Dec. 22, 2018).  
 32 IRS, Joint Operations Center (JOC), *Snapshot Reports: Enterprise Snapshot* (Jan. 26, 2018); IRS, Joint Operations Center (JOC), *Snapshot Reports: Product Line Detail* (Jan. 26, 2018).  
 33 IRS, Joint Operations Center (JOC), *Snapshot Reports: Enterprise Snapshot* (Feb. 2 2018); IRS, Joint Operations Center (JOC), *Snapshot Reports: Product Line Detail* (Feb. 2, 2018).

**FIGURE 3, Selected IRS Inventories and Levels of Service Pre-Comparison to Last Year for Week Ending Prior to Shutdown, Week Ending at Conclusion of Shutdown, and Week after Operations Resumed**

Description	Week Ending 12/23/2017	Week Ending 12/22/2018	Percent Change from Corresponding Week of Prior Year	Week Ending 1/27/2018	Week Ending 1/26/2019	Percent Change from Corresponding Week of Prior Year	Week Ending 2/3/2018	Week Ending 2/2/2019	Percent Change from Corresponding Week of Prior Year
Level of Service for the Accts. Mgmt. Lines	56.8%	75.4%	32.7%	84.2%	36.8%	-56.3%	86.2%	48.3%	-44.0%
Average Speed of Answer (AM) Minutes	16.4	12.8	-22.0%	4.6	31.9	593.5%	4.4	17.0	286.4%
Level of Service for ACS	63.7%	69.1%	8.5%	72.7%	30.9%	-57.5%	64.5%	38.3%	-40.6%
Average Speed of Answer (ACS) Minutes	18.9	15.7	-16.9%	11.4	51.9	355.3%	19.2	48.3	151.6%
Level of Service for the Bal. Due Line	59.8%	54.6%	-8.7%	70.2%	12.8%	-81.8%	57.8%	6.70%	-88.4%
Average Speed of Answer (Bal. Due) Minutes	26.8	23.2	-13.4%	16.3	93.0	470.6%	30.1	80.6	167.8%
total Individual Returns Received (cum.)							18,302,000	16,035,000	-12.4%
Total Individual Returns Processed (cum.)							17,931,000	13,306,000	-25.8%
Individual Master File (IMF) Pipeline (weekly)							229,470	437,183	90.5%
IMF Error Resolution (weekly)							211,868	621,385	193.3%

### Impact of the Shutdown on Taxpayers and Taxpayer Rights

As described above and in the Purple Book legislative recommendation, *Authorize the Office of the Taxpayer Advocate to Assist Certain Taxpayers During a Lapse in Appropriations*, neither the 2018 Non-Filing Season nor the 2019 Filing Season Lapse plans excepted TAS employees for the purpose of fulfilling their statutory mission of helping taxpayers resolve their problems with the IRS.<sup>34</sup> Moreover, no IRS employee was excepted for the purpose of releasing or withdrawing liens, releasing levies, or returning levy proceeds.

Because of Chief Counsel’s interpretation of “protecting property” to mean protecting only government property, TAS’s work advocating on behalf of taxpayers experiencing refund delays, identity theft, or inappropriate or even unlawful liens and levies was not excepted. Even under the 2019 Filing Season Lapse Plan, in which the IRS would issue refunds—an act that protects *taxpayers’* as opposed to *government* property—TAS was singled out as not being excepted to work with taxpayers experiencing refund delays. This decision was made despite our providing clear evidence of the scope and importance of TAS activity in this area. Below is a list of the highest volume FY 2018 TAS cases that relate to returns processing. These returns show up almost immediately once the filing season opens:

**FIGURE 4, FY 2018 TAS Case Receipts<sup>35</sup>**

FY 2018 TAS Case Receipts Relating to Return Processing	
Pre-refund Wage Verification	66,048
Identity Theft Victim Assistance	13,787
Processing Amended Returns (1040Xs)	8,767
Unpostable/Rejected Returns (Error Resolution or ERS)	8,673
Taxpayer Protection Program (suspected identity theft returns) Unpostables	7,947
Other Refund Inquiries/Issues	7,628
Processing Original Return Issues	5,312
Returned/Stopped Refunds	3,398
Injured Spouse Claims	3,231
IRS Refund Offset (economic hardship)	2,739
Math Error Issues	1,994

The IRS’s authority to collect revenue is not unconditional. It is conditioned on statutory protections, and a lapse in appropriations does not eliminate those protections. It is unconscionable for the government to allow its employees to *enforce* collection of taxes without the concomitant taxpayer rights protections enacted by Congress. Chief among those protections is the Taxpayer Advocate Service, along with statutorily mandated releases of levies where a taxpayer is experiencing economic hardship<sup>36</sup> and withdrawals of notices of federal tax liens which were premature or otherwise not in accordance with administrative procedures, or in the “best interests of the taxpayer (as determined by the National

34 IRC § 7803(c)(2)(A)(i).

35 Taxpayer Advocate Management Information System (TAMIS).

36 IRC § 6343(a)(1)(D).

Taxpayer Advocate) and the United States” or where it furthers the collection of tax or the taxpayer has entered into an installment agreement.<sup>37</sup>

None of these protections is considered an excepted activity, leading to bizarre results. For example, a taxpayer with a levy issued against his or her bank account can normally call ACS and have the levy released by entering into an IA. *Under the 2019 Filing Season Lapse Plan, however, ACS employees can put the taxpayer into an installment agreement, but they cannot release the levy.* Further, if a taxpayer called to say he or she could not afford to pay, the employee might be able to put the taxpayer into Currently Not Collectible status, but still could not release the levy, thereby violating IRC § 6343(a).<sup>38</sup> This is, of course, absurd. And harmful to the taxpayer. And to trust in the tax system and long term voluntary compliance.

Additional evidence of taxpayer harm is shown in Figure 5, which lists the number of IRS notices issued immediately before and during the shutdown, all of which have significant consequences if deadlines are missed. In fact, for a period of time after the United States Tax Court closed on December 25, 2018, the U.S. mail and private delivery services returned petitions to the original sender. Thus, the IRS will not know that the taxpayer timely filed a Tax Court petition protesting the proposed deficiency or the Collection Due Process hearing determination. In the former case, IRS systems will assess the tax and, in both cases, collection will commence, even though under the law all that activity is stayed. Both the Court and the IRS will have to spend extra resources to unwind all this.

And none of this takes into account taxpayer anxiety. Figure 5 shows the volume of certain notices that were issued both before and during the shutdown. These notices – Notice of Levy, Statutory Notice of Deficiency, and Notice of Right to Collection Due Process Hearing, bear statutory deadlines that have serious consequences for the taxpayer if he or she does not take action during that period. When the IRS is shut down, it is impossible for the taxpayer to get the information and assistance needed to move forward. With respect to notices of levy, if the taxpayer cannot contact the IRS and make other payment arrangements within 21 days of the issuance of the levy, the employer or financial institution must pay over the funds to the IRS. The 21-day period for over 18,000 levies expired during the shutdown.<sup>39</sup>

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37 IRC § 6323(j)(1)(A)-(D).

38 See *Vinatieri v. Comm’r*, 133 T.C. 392, 400 (Dec. 21, 2009), in which the Tax Court held: “When a taxpayer establishes in a pre-levy collection hearing under section 6330 that the proposed levy would create an economic hardship, it is unreasonable for the settlement officer to determine to proceed with the levy which section 6343(a)(1)(D) would require the IRS to immediately release. Rather than proceed with the levy, the settlement officer should consider alternatives to the levy.”

39 Office of Taxpayer Correspondence (Feb. 2019).

**FIGURE 5, Selected IRS Correspondence Volumes Where Part of Response Period Occurred During Shutdown and Correspondence Volumes of IRS Correspondence Mailed During Shutdown<sup>40</sup>**

Description	Volume of Notices/Letters Issued Prior to Shutdown Where Shutdown Interfered with Response Deadline	Volume of Notices/Letters Issued During Shutdown Period
Statutory Notices of Deficiency (90 Days to Respond) <sup>a</sup>	527,957	9,267
Notice With CDP Rights (30 Days to Respond) <sup>b</sup>	40,657	13,161
Notice to Provide Information Requested by IRS Exam (30 Days to Respond) <sup>c</sup>	18,492	78
Notice of Levy (21 Days to Respond) – Including Copy Mailed to Taxpayer <sup>d</sup>	18,406	0

- a CP3219A and Letter 3219.
- b ACS Letter LT11.
- c CP75, CP75A, and CP75D.
- d Forms 668A, 668W, 8519.

### The Way Forward: Digging the IRS Out of this Mess

As officials and pundits are fond of saying, the IRS is the federal agency that touches everyone. While it is true that the IRS is the accounts receivable function of the federal government, this description doesn't quite capture its awesome power to audit and assess taxes, and to seize income and assets, without the need to obtain a judgment. It is also a major disburser of federal benefits and payments. Nearly 112 million individual taxpayers received a refund in 2018, averaging about \$2,900.<sup>41</sup> The refundable Earned Income Tax Credit is among the largest federal antipoverty programs, delivering \$63 billion for about 25 million taxpayers in 2018.<sup>42</sup> Similarly, nearly \$28 billion in Premium Tax Credits helped defray the cost of health insurance for over six million taxpayers.<sup>43</sup>

It is irresponsible for an agency that touches all aspects of people's lives to be underfunded, understaffed, and at the mercy of shutdowns. As we document in these pages, the IRS is wrestling with its workload. With the best of intentions—namely, trying to do its job—it is making strategic decisions that ultimately burden taxpayers, increase its own rework, and create distance and distrust between taxpayers and the tax agency, thereby undermining voluntary compliance. And it is experiencing a “cycle of frustration” as it tries to soldier on with its important work in the midst of shutdowns and funding stops and starts.

There are steps we can take to change this trajectory:

First, the ADA should be amended to provide that where the government takes enforcement action against a taxpayer during a shutdown (or has taken enforcement action just prior to a shutdown), personnel must be excepted to ensure the taxpayer protections and rights enacted by Congress are

40 Office of Taxpayer Correspondence (Feb. 2019). The IRS also mailed 8,807 copies of the Notice of Levy to taxpayers.

41 IRS, Filing Season Statistics (Nov. 2018).

42 IRS, W&I Earned Income Tax Credit (EITC) Fast Facts (last accessed Feb. 2019). Calendar Half Year Report, June 2018. Historically, half year data represents over 95 percent of EITC returns.

43 Information Returns Master File (IRMF) Compliance Data Warehouse (CDW) TY 2017 returns processed in 2018.

available.<sup>44</sup> The ADA was enacted in 1981. At that time, the EITC was only 6 years old, and provided a maximum refundable credit of \$500, as opposed to \$6,431 for TY 2018.<sup>45</sup> There were no Premium Tax Credits, no American Opportunity Tax Credit, no refundable Child Tax Credit. There are no regulations promulgated under the ADA, and the only legal guidance was issued in 1981 and 1990. Neither of these opinions addresses the role of the IRS in terms of public welfare in the 21st century. We offer a recommendation in the 2019 Purple Book that would address part of this problem.<sup>46</sup>

Second, as discussed above and in more detail later in this report, the IRS should be given additional dedicated, multi-year funding to replace its antiquated core information technology systems, so it can deliver the service and compliance activities that are expected of a 21st century tax administration.<sup>47</sup>

Third, the IRS should invest heavily in improving its communications with taxpayers, especially those notices and letters that have legal significance, such as Notices of Deficiency and Collection Due Process hearing notices. By designing a rights-based notice rather than an enforcement-based notice, the IRS will educate taxpayers and encourage greater engagement, which in turn is likely to improve voluntary compliance.<sup>48</sup>

Fourth, Congress should require the IRS to seriously study and report on the possibility of expanding its withholding system to move closer to a hybrid pay-as-you-earn (PAYE) system. We estimate that in TY 2016, 45 percent of nonitemizing filings reported wage earnings subject to withholding as the sole source of income. Thus, even simple PAYE allows for complete withholding of tax at the source for these approximately 59 million filings. With a variety of withholding adjustments, some involving a greater or lesser degree of difficulty, PAYE tax collection could be extended to seven of the primary income sources, covering 62 percent (91 million) of tax returns.<sup>49</sup> This approach will ease taxpayer and IRS burden alike.

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44 See National Taxpayer Advocate 2019 Purple Book (Legislative Recommendation: *Authorize the Office of the Taxpayer Advocate to Assist Certain Taxpayers During a Lapse in Appropriations*) (Dec. 31, 2018).

45 Dennis J. Ventry, Jr., *The Collision of Tax and Welfare Politics: The Political History of the Earned Income Tax Credit, 1969–99*, NAT'L TAX J. (Dec. 2000).

46 See National Taxpayer Advocate 2019 Purple Book (Legislative Recommendation: *Authorize the Office of the Taxpayer Advocate to Assist Certain Taxpayers During A Lapse in Appropriations*) (Dec. 31, 2018).

47 See Legislative Recommendation: *IT Modernization: Provide the IRS with Additional Dedicated, Multi-Year Funding to Modernize Its Core IT Systems Pursuant to a Plan that Sets Forth Specific Goals and Metrics and Is Evaluated Annually by an Independent Third Party*, *infra*.

48 See Introduction to Notices: *Notices Are Necessary to Inform Taxpayers of Their Rights and Obligations, Yet Many IRS Notices Fail to Adequately Inform Taxpayers, Leading to the Loss of Taxpayer Rights*, *infra*; Most Serious Problem: *Math Error Notices: Although the IRS Has Made Some Improvements, Math Error Notices Continue to Be Unclear and Confusing, Thereby Undermining Taxpayer Rights and Increasing Taxpayer Burden*, *infra*; Most Serious Problem: *Statutory Notices of Deficiency: The IRS Fails to Clearly Convey Critical Information in Statutory Notices of Deficiency, Making it Difficult for Taxpayers to Understand and Exercise Their Rights, Thereby Diminishing Customer Service Quality, Eroding Voluntary Compliance, and Impeding Case Resolution*, *infra*; Most Serious Problem: *Collection Due Process Notices: Despite Recent Changes to Collection Due Process Notices, Taxpayers Are Still at Risk for Not Understanding Important Procedures and Deadlines, Thereby Missing Their Right to an Independent Hearing and Tax Court Review*, *infra*; and Literature Review: *Improving Notices Using Psychological, Cognitive, and Behavioral Science Insights*, *infra*.

49 These seven income types are wages, interest, pensions, dividends, capital gains, Individual Retirement Account (IRA) income, and unemployment. Study: *A Conceptual Analysis of Pay-As-You-Earn (PAYE) Withholding Systems as a Mechanism for Simplifying and Improving U.S. Tax Administration*, *infra*.

Fifth, the IRS should re-examine how it measures its performance in all its activities—outreach and education, audits, collection—and regularly assess whether its initiatives increase future voluntary compliance or undermine it.<sup>50</sup>

With these five steps, the IRS will have the tools to deliver a robust and useful online accounts while providing meaningful person-to-person assistance to taxpayers via phone, virtual conferences, or in-person. It will have the research to allow it to select appropriate returns for a repertoire of compliance touches and will not waste significant resources on no change audits. It will be able to approach all its compliance touches as an opportunity to educate and gain trust with the taxpayer, because it will be utilizing data and research to understand the causes of noncompliance. And where enforcement action is required, taxpayers will have confidence that IRS employees understand and respect the significant protections afforded by the IRC, including the Taxpayer Bill of Rights.<sup>51</sup>

It is true that taxes are the “lifeblood of government,” but as I’ve written elsewhere, it is the taxpayers of the United States who pay that lifeblood.<sup>52</sup> We need to honor our taxpayers by providing them the best tax administration possible. The report that follows includes our recommendations to improve the taxpayer’s journey through the tax system as well as improve the effectiveness and efficiency of the IRS.

Respectfully Submitted,



Nina E. Olson  
National Taxpayer Advocate  
12 February 2019

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50 See Taxpayer Rights Assessment: *IRS Performance Measures and Data Relating to Taxpayer Rights*, *infra*; Most Serious Problem: *Tax Law Questions: The IRS’s Failure to Answer the Right Tax Law Questions at the Right Time Harms Taxpayers, Erodes Taxpayer Rights, and Undermines Confidence in the IRS*, *infra*; Most Serious Problem: *Navigating The IRS: Taxpayers Have Difficulty Navigating the IRS, Reaching the Right Personnel to Resolve Their Tax Issues, and Holding IRS Employees Accountable*, *infra*; Most Serious Problem: *Correspondence Examination: The IRS’s Correspondence Examination Procedures Burden Taxpayers and are not Effective in Educating the Taxpayer and Promoting Future Voluntary Compliance*, *infra*; Most Serious Problem: *Field Examination: The IRS’s Field Examination Program Burdens Taxpayers and Yields High No-Change Rates, Which Waste IRS Resources and May Discourage Voluntary Compliance*, *infra*; Most Serious Problem: *Field Collection: The IRS Field Collection Function Is Not Appropriately Staffed or Trained to Minimize Taxpayer Burden and Ensure Taxpayer Rights Are Protected*, *infra*.

51 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR that was adopted by the IRS are now codified in the IRC.

52 Nina E. Olson, *Taking the Bull by its Horns: Some Thoughts on Constitutional Due Process in Tax Collection*, 2010 Erwin N. Griswold Lecture Before the American College of Tax Counsel, 63 Tax Law. 227, 234 (2010).

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## TAXPAYER RIGHTS ASSESSMENT: IRS Performance Measures and Data Relating to Taxpayer Rights

In the 2013 Annual Report to Congress, the National Taxpayer Advocate proposed a “report card” of measures that “...provide a good indication whether the IRS is treating U.S. taxpayers well and furthering voluntary compliance.”<sup>1</sup>

In 2014, the IRS officially adopted the Taxpayer Bill of Rights (TBOR) which is a list of ten rights that the National Taxpayer Advocate recommended to help taxpayers and IRS employees alike gain a better understanding of the dozens of discrete taxpayer rights scattered throughout the multi-million word Internal Revenue Code (IRC).<sup>2</sup> In late 2015, Congress followed suit by adding the list of fundamental rights to the IRC.<sup>3</sup> While listing these rights in IRC § 7803(a)(3) is a significant achievement for increasing taxpayers’ awareness of their rights, the process of integrating taxpayer rights into all aspects of tax administration continues. The *Taxpayer Rights Assessment* contains selected performance measures and data organized by the ten taxpayer rights and is one step toward integrating taxpayer rights into tax administration.

This *Taxpayer Rights Assessment* is a work in progress. The following data provide insights into IRS performance; however, they are by no means comprehensive. In some instances, data is not readily available. In other instances we may not yet have sufficient measures in place to address specific taxpayer rights. And, despite what the numbers may show, we must be concerned for those taxpayers who still lack access to services and quality service even when performance metrics are increasing. This *Taxpayer Rights Assessment* will grow and evolve over time as data becomes available and new concerns emerge.

**1. THE RIGHT TO BE INFORMED** – Taxpayers have the right to know what they need to do to comply with the tax laws. They are entitled to clear explanations of the laws and IRS procedures in all tax forms, instructions, publications, notices, and correspondence. They have the right to be informed of IRS decisions about their tax accounts and to receive clear explanations of the outcomes.

Measure/Indicator	Fiscal Year (FY) 2016	FY 2017	FY 2018
Individual Correspondence Volume (adjustments) <sup>a</sup>	4,817,708	4,598,654	4,485,906
Average cycle time to work Individual Master File (IMF) Correspondence <sup>b</sup>	84 days	69 days	66 days
Inventory Overage <sup>c</sup>	49.1%	39.5%	37.9%
Business Correspondence Volume (adjustments) <sup>d</sup>	2,940,925	2,736,451	2,595,131
Average cycle time to work Business Master File (BMF) Correspondence <sup>e</sup>	47 days	45 days	51 days
Inventory Overage <sup>f</sup>	8.6%	11.7%	23.5%
Total Correspondence (all types)	TBD	TBD	TBD
Quality of IRS Forms & Publications	TBD	TBD	TBD
IRS.gov Web Page Ease of Use	TBD	TBD	TBD
IRS Outreach	TBD	TBD	TBD

<sup>a</sup> IRS, Joint Operations Center (JOC), *Adjustments Inventory Reports: July-September Fiscal Year (FY) Comparison (FY 2017 and FY 2018)*. This correspondence data is also repeated under Right 4 – *The Right to Challenge the IRS’s Position and Be Heard*.

<sup>b</sup> IRS, Research Analysis and Data (RAD), *Accounts Management Reports: Collection Information System (CIS) Closed Case Cycle Time (FY 2017 and FY 2018)*.

<sup>c</sup> IRS, *Weekly Enterprise Adjustments Inventory Report, FY 2017 and FY 2018* (weeks ending Sept. 30, 2017 and Sept. 29, 2018).

<sup>d</sup> IRS, JOC, *Adjustments Inventory Reports: July-September Fiscal Year Comparison (FY 2017 and FY 2018)*.

<sup>e</sup> IRS, RAD, *Accounts Management Reports: CIS Closed Case Cycle Time (FY 2017 and FY 2018)*.

<sup>f</sup> IRS, *Weekly Enterprise Adjustments Inventory Report, FY 2017 and FY 2018* (weeks ending Sept. 30, 2017 and Sept. 29, 2018).

- 1 See National Taxpayer Advocate 2013 Annual Report to Congress xvii-xviii (Preface: *Taxpayer Service Is Not an Isolated Function but Must Be Incorporated throughout All IRS Activities, Including Enforcement*).
- 2 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).
- 3 See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 401(a) (2015) (codified at IRC § 7803(a)(3)).

**2. THE RIGHT TO QUALITY SERVICE** – Taxpayers have the right to receive prompt, courteous, and professional assistance in their dealings with the IRS, to be spoken to in a way they can easily understand, to receive clear and easily understandable communications from the IRS, and to speak to a supervisor about inadequate service.

Measure/Indicator	FY 2016	FY 2017	FY 2018
Number of Returns Filed (projected, all types) <sup>a</sup>	246,945,921	247,807,099	250,470,800
Total Individual Income Tax Returns <sup>b</sup>	150,711,378	150,786,286	152,106,500
E-file Receipts, calendar year (Received by 12/02/16, 12/01/17, 11/23/18) <sup>c</sup>	131,851,000	132,319,000	135,459,000
E-file Receipts: Tax Professional (calendar year) <sup>d</sup>	60%	60%	59%
E-file Receipts: Self Prepared (calendar year) <sup>e</sup>	40%	40%	41%
Returns Prepared by:			
VITA / TCE / AARP (tax year) <sup>f</sup>	3,542,336	3,402,019	3,270,848
Free File Consortium (tax year) <sup>g</sup>	2,356,167	2,352,555	2,486,120
Fillable Forms (tax year) <sup>h</sup>	346,098	325,482	317,527
Number of Taxpayer Assistance (“Walk-In”) Centers (TAC) <sup>i</sup>	376	371	359
Number of TAC Contacts <sup>j</sup>	4.5 million	3.3 million	2.9 million
Total Calls to IRS <sup>k</sup>	117,479,981	95,618,714	98,532,231
Number of Attempted Calls to IRS Customer Service Lines <sup>l</sup>	104,275,387	74,471,676	77,715,282
Toll Free: Percentage of calls answered [Level of Service (LOS)] <sup>m</sup>	53.4%	77.1%	75.9%
Toll Free: Average Speed of Answer <sup>n</sup>	17.8 minutes	8.4 minutes	7.5 minutes
NTA Toll Free: Percentage of calls answered (LOS) <sup>o</sup>	58.1%	76.7%	78.4%
NTA Toll Free: Average Speed of Answer <sup>p</sup>	8.9 minutes	2.9 minutes	3.2 minutes
Practitioner Priority: Percentage of calls answered (LOS) <sup>q</sup>	71.0%	81.9%	84.9%
Practitioner Priority: Average Speed of Answer <sup>r</sup>	10.5 minutes	8.9 minutes	7.5 minutes
Tax Exempt/Government Entities: Percentage of calls answered (LOS) <sup>s</sup>	56.8%	69.5%	69.2%
Tax Exempt/Government Entities: Average Speed of Answer <sup>t</sup>	15.9 minutes	9.2 minutes	8.8 minutes
Toll Free Customer Satisfaction <sup>u</sup>	88.0%	90.0%	90.0%
Awareness of Service (or utilization)	TBD	TBD	TBD
IRS Issue Resolution – Percentage of taxpayers who had their issue resolved as a result of the service they received	TBD	TBD	TBD
Taxpayer Issue Resolution – Percentage of taxpayers who reported their issue was resolved after receiving service	TBD	TBD	TBD

<sup>a</sup> IRS Pub. 6292, *Fiscal Year Return Projections for the United States 2017-2024* 3 (Sept. 2017); IRS Pub. 6292, *Fiscal Year Return Projections for the United States: 2018-2025* 3 (June 2018). The FY 2017 figure has been updated from what we reported in the 2017 Annual Report to Congress to report actual return counts. The FY 2018 figures are projected numbers. The number of returns and related metrics are proxies for IRS workload and provide context for the environment in which taxpayers seek Quality Service and other rights.

<sup>b</sup> IRS Pub. 6292, *Fiscal Year Return Projections for the United States: 2017-2024* 3 (Sept. 2017); IRS Pub. 6292, *Fiscal Year Return Projections for the United States: 2018-2025* 3 (June 2018). The FY 2017 figure has been updated from what we reported in the 2017 Annual Report to Congress to report actual return counts. The FY 2018 figures are projected numbers.

<sup>c</sup> IRS, *E-File Reports*, <http://efile.enterprise.irs.gov/Progress.asp> (last visited Dec. 7, 2018). Rounded to the nearest thousand.

<sup>d</sup> *Id.* (Dec. 9, 2018).

<sup>e</sup> *Id.*

<sup>f</sup> Free, in-person return preparation is offered to low income and older taxpayers by non-IRS organizations through the Volunteer Income Tax Assistance (VITA), Tax Counseling for the Elderly (TCE), and American Association of Retired Persons (AARP) Tax-Aide programs. IRS, Compliance Data Warehouse (CDW), Individual Returns Transaction File. The FY 2016 figures have been updated from what we reported in the 2016 Annual Report to Congress. The FY 2016 figures represent tax year 2015 tax returns. The FY 2017 figures represent tax year 2016 tax returns. The FY 2018 figures represent tax year 2017 tax returns.

<sup>g</sup> IRS, CDW, Electronic Tax Administration Marketing Database. The FY 2016 figures represent tax year 2015 tax returns. The FY 2017 figures represent tax year 2016 tax returns. The FY 2018 figures represent tax year 2017 tax returns.

<sup>h</sup> *Id.* The FY 2016 figures have been updated from what we reported in the 2016 Annual Report to Congress. The FY 2016 figures represent tax year 2015 returns. The FY 2017 figures represent tax year 2016 tax returns. The FY 2018 figures represent tax year 2017 tax returns.

<sup>i</sup> FY 2016 figures from IRS response to TAS fact check (Dec. 20, 2016). FY 2017 figures from IRS response to TAS information request (Nov. 3, 2017). FY 2018 figures from IRS response to TAS information request (Oct. 24, 2018). The FY 2018 figure was calculated as of August 2018, and does not include 38 face-to-face Virtual Service Delivery sites located at community partner facilities.

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- j Wage and Investment Division (W&I), Business Performance Review (BPR), 4th Quarter, FY 2018 12 (Nov. 8, 2018).
- k IRS, JOC, *Snapshot Reports: Enterprise Snapshot* (weeks ending Sept. 30, 2017 and Sept. 30, 2018; reports generated Oct. 19, 2018).
- l *Id.* Number of calls to Accounts Management (formerly Customer Services) is the sum of 29 lines (0217, 1040, 4933, 1954, 0115, 8374, 0922, 0582, 5227, 9887, 9982, 4184, 7388, 0452, 0352, 7451, 9946, 5215, 3536, 2050, 4017, 2060, 4778, 4259, 8482, 8775, 5500, 4490, and 5640). The FY 2018 figure includes the sum of a 30th line (5245).
- m IRS, JOC, *Snapshot Reports: Enterprise Snapshot* (weeks ending Sept. 30, 2016 and Sept. 30, 2017; reports generated Oct. 19, 2018). Accounts Management calls answered include reaching live assistant or selecting options to hear automated information messages.
- n IRS, JOC, *Snapshot Reports: Enterprise Snapshot* (weeks ending Sept. 30, 2017 and Sept. 30, 2018; reports generated Oct. 19, 2018).
- o IRS, JOC, *Snapshot Reports: Product Line Detail* (weeks ending Sept. 30, 2017 and Sept. 30, 2018; reports generated Oct. 19, 2018).
- p *Id.*
- q *Id.*
- r *Id.*
- s *Id.*
- t *Id.*
- u W&I, *FY 2018 W&I Customer Satisfaction – Dissatisfaction Report* (2018).

### 3. THE RIGHT TO PAY NO MORE THAN THE CORRECT AMOUNT OF TAX – Taxpayers have the right to pay only the amount of tax legally due, including interest and penalties, and to have the IRS apply all tax payments properly.

Measure/Indicator	FY 2016	FY 2017	FY 2018
Toll-Free Tax Law Accuracy <sup>a</sup>	96.4%	96.7%	95.5%
Toll-Free Accounts Accuracy <sup>b</sup>	96.1%	96.0%	96.1%
Scope of Tax Law Questions Answered	TBD	TBD	TBD
Correspondence Examinations – Individual Tax Returns			
No change rate <sup>c</sup>	16.2%	14.7%	12.6%
Agreed rate <sup>d</sup>	20.6%	22.4%	23.4%
Non-response rate <sup>e</sup>	42.1%	40.6%	41.2%
Percentage of cases appealed	TBD	TBD	TBD
Field Examinations – Individual Tax Returns			
No change rate <sup>f</sup>	14.6%	14.3%	13.3%
Agreed rate <sup>g</sup>	45.4%	46.1%	48.4%
Non-response rate <sup>h</sup>	0.3%	0.3%	0.7%
Percentage of cases appealed	TBD	TBD	TBD
Office Examinations – Individual Tax Returns			
No change rate <sup>i</sup>	12.2%	14.4%	12.2%
Agreed rate <sup>j</sup>	43.4%	42.8%	44.1%
Non-response rate <sup>k</sup>	20.6%	19.0%	18.3%
Percentage of cases appealed	TBD	TBD	TBD
Math Error Adjustments	TBD	TBD	TBD
Math Error Abatements	TBD	TBD	TBD
Number of Statutory Notices of Deficiency Issued	TBD	TBD	TBD
Number of Statutory Notices of Deficiency Appealed	TBD	TBD	TBD
Number of Collection Appeals Program Conferences	TBD	TBD	TBD
Number of Collection Appeals Program Conferences Reversing IRS position	TBD	TBD	TBD
Number of Collection Due Process Conferences	TBD	TBD	TBD
Number of Collection Due Process Conferences Reversing IRS position	TBD	TBD	TBD

a W&I, BPR, 4th Quarter, FY 2018 10 (Nov. 8, 2018).

b *Id.*

c IRS, CDW, Audit Information Management System (AIMS), Closed Case Database. Internal Revenue Manual (IRM) 4.4.12.5.49.1 (June 1, 2002) defines a no change as case closed by the examiner with no additional tax due (disposal code 1 and 2).

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- d IRS, CDW, Audit Information Management System, Closed Case Database. IRM 4.4.12.5.22.2 (June 1, 2002) defines an agreed case as disposal code 3, 4, 8, or 9.
- e IRS, CDW, AIMS, Closed Case Database.
- f *Id.*
- g *Id.*
- h *Id.*
- i *Id.*
- j *Id.*
- k *Id.*

**4. THE RIGHT TO CHALLENGE THE IRS'S POSITION AND BE HEARD** – Taxpayers have the right to raise objections and provide additional documentation in response to formal IRS actions or proposed actions, to expect that the IRS will consider their timely objections and documentation promptly and fairly, and to receive a response if the IRS does not agree with their position.

Measure/Indicator	FY 2016	FY 2017	FY 2018
Individual Correspondence Volume (adjustments) <sup>a</sup>	4,817,708	4,598,654	4,485,906
Average cycle time to work IMF Correspondence <sup>b</sup>	84 days	69 days	66 days
Inventory Overage <sup>c</sup>	49.1%	39.5%	37.9%
Business Correspondence Volume <sup>d</sup>	2,940,925	2,736,451	2,595,131
Average cycle time to work BMF Correspondence <sup>e</sup>	47 days	45 days	51 days
Inventory Overage <sup>f</sup>	8.6%	11.7%	23.5%
Percentage of Math Error Adjustments Abated	TBD	TBD	TBD
Percentage of Statutory Notices of Deficiency Appealed to Tax Court	TBD	TBD	TBD
Number of Collection Appeal Program Conferences Requested by Taxpayers <sup>g</sup>	TBD	TBD	TBD
Percentage of CAP Conferences that Reversed the IRS Position	TBD	TBD	TBD
Number of Collection Due Process Hearings Requested by Taxpayers <sup>h</sup>	TBD	TBD	TBD
Percentage of Collection Due Process Hearings that Reversed the IRS Position	TBD	TBD	TBD

a IRS, JOC, *Adjustments Inventory Reports: July-September Fiscal Year Comparison* (FY 2017 and FY 2018).

b IRS, RAD, *Accounts Management Reports: CIS Closed Case Cycle Time* (FY 2017 and FY 2018).

c IRS, *Weekly Enterprise Adjustments Inventory Report*, FY 2017 and FY 2018 (weeks ending Sept. 30, 2017 and Sept. 29, 2018).

d IRS, JOC, *Adjustments Inventory Reports: July-September Fiscal Year Comparison* (FY 2017 and FY 2018).

e IRS, RAD, *Accounts Management Reports: CIS Closed Case Cycle Time* (FY 2017 and FY 2018).

f IRS, *Weekly Enterprise Adjustments Inventory Report*, FY 2017 and FY 2018 (weeks ending Sept. 30, 2017 and Sept. 29, 2018).

g Taxpayers may request a Collection Appeals Process review as the result of IRS actions such as filing a Notice of Federal Tax Lien, an IRS levy or seizure of property, and termination, rejection, or modification of an installment agreement. See IRS Pub. 1660, *Collection Appeal Rights*.

h Taxpayers may request a Collection Due Process review when the IRS plans to take actions such as filing a federal tax lien or levy. See IRS Pub. 1660, *Collection Appeal Rights*.

**5. THE RIGHT TO APPEAL AN IRS DECISION IN AN INDEPENDENT FORUM** – Taxpayers are entitled to a fair and impartial administrative appeal of most IRS decisions, including many penalties, and have the right to receive a written response regarding the Office of Appeals' decision. Taxpayers generally have the right to take their cases to court.

Measure/Indicator	FY 2016	FY 2017	FY 2018
Number of Cases Appealed <sup>a</sup>	114,362	103,574	103,359
Appeals Staffing (On-rolls) <sup>b</sup>	1,449	1,345	1,207
Number of States without an Appeals or Settlement Officer <sup>c</sup>	11	11	11
Customer Satisfaction of Service in Appeals <sup>d</sup>	67%	68%	N/A
Average Days in Appeals to Resolution	TBD	TBD	TBD
Percentage of Statutory Notices of Deficiency Appealed to Tax Court	TBD	TBD	TBD

a Office of Appeals, BPR, 3rd Quarter, FY 2018 9 (Aug. 23, 2018). The FY 2018 number is a projected figure. The Appeals FY 2018 4th Quarter BPR was not available at time of print.

b For FY 2016 and FY 2017, Office of Appeals, BPR, 3rd Quarter, FY 2018 12 (Aug. 23, 2018). The Appeals FY 2018 4th Quarter BPR was not available at time of print. For FY 2018, IRS, Human Resources Reporting Center, <https://persinfo.web.irs.gov/track/workorg.asp>, IRS Staffing by Business Unit for week ending Sep. 29, 2018.

c For FY 2016 and FY 2017, IRS, Human Resources Reporting Center, <https://persinfo.web.irs.gov/posrpt.htm>. For FY 2016 and FY 2017, Employee Position (OF8) Listing for weeks ending Oct. 1, 2016 and Sept. 30, 2017. For FY 2018, IRS response to TAS fact check (Nov. 21, 2018). The FY 2016 figure has been updated from what we reported in the 2016 Annual Report to Congress. The IRS also has Appeals and Settlement Officers in the District of Columbia which are not included in this figure.

d Office of Appeals, BPR, 3rd Quarter, FY 2018 9 (Aug. 23, 2018). The Appeals FY 2018 4th Quarter BPR was not available at time of print.

## 6. THE RIGHT TO FINALITY – Taxpayers have the right to know the maximum amount of time they have to challenge the IRS’s position as well as the maximum amount of time the IRS has to audit a particular tax year or collect a tax debt. Taxpayers have the right to know when the IRS has finished an audit.

Measure/Indicator	FY 2016	FY 2017	FY 2018
Average Days to Complete Correspondence Examination (non-EITC) <sup>a</sup>	199 days	207 days	236 days
Average Days to Complete Correspondence Examination (EITC) <sup>b</sup>	219 days	222 days	240 days
Average Days to Reach Determination on Applications for Exempt Status <sup>c</sup>	54 days	54 days	69 days
Average Days for Exempt Organization Function to Respond to Correspondence <sup>d</sup>	45 days	27 days	46 days

a W&I, BPR, 4th Quarter, FY 2018 14 (Nov. 8, 2018). The FY 2016 and FY 2017 figures have been updated from what we reported in the 2017 Annual Report to Congress.

b *Id.*

c For FY 2016 and FY 2017, Tax Exempt & Government Entities (TE/GE), BPR, 4th Quarter, FY 2017 9 (Nov. 30, 2017). For FY 2018, TE/GE, Compliance, Planning & Classification email to TAS (Dec. 13, 2018).

d *Id.*

## 7. THE RIGHT TO PRIVACY – The right to privacy goes to the right to be free from unreasonable searches and seizures and that IRS actions would be no more intrusive than necessary. Taxpayers have the right to expect that any IRS inquiry, examination, or enforcement action will comply with the law and be no more intrusive than necessary, and will respect all due process rights, including search and seizure protections and will provide, where applicable, a collection due process hearing.

Measure/Indicator	FY 2016	FY 2017	FY 2018
Number (or percentage) of Collection Due Process cases where IRS cited for Abuse of Discretion	TBD	TBD	TBD
Number of Offers in Compromise Submitted using ‘Effective Tax Administration’ as Basis	TBD	TBD	TBD
Percentage of Offers in Compromise Accepted that used ‘Effective Tax Administration’ as Basis	TBD	TBD	TBD
Number of cases where taxpayer received repayment of attorney fees as result of final judgment	TBD	TBD	TBD

- 8. THE RIGHT TO CONFIDENTIALITY** – Taxpayers have the right to expect that any information they provide to the IRS will not be disclosed unless authorized by the taxpayer or by law. Taxpayers have the right to expect appropriate action will be taken against employees, return preparers, and others who wrongfully use or disclose taxpayer return information.

Measure/Indicator	FY 2016	FY 2017	FY 2018
Number of Closed Unauthorized Access of Taxpayer Account (UNAX) Investigations <sup>a</sup>	147	151	198
UNAX Investigations Resulting in Prosecution, Removal, Resignation or Suspension of Employee <sup>b</sup>	38	64	78
UNAX Investigations Resulting in other Administrative Dispositions <sup>c</sup>	81	74	105
UNAX Investigations Where Employee Cleared of Wrongdoing <sup>d</sup>	28	13	15

a IRS, Automated Labor and Employee Relations Tracking System (ALERTS). The number of IRS employees averaged 85,002 in FY 2016, 83,775 in FY 2017, and 80,836 in FY 2018. IRS, Human Resources Reporting Center, *Fiscal Year Population Report*.

b IRS, ALERTS.

c *Id.* Administrative dispositions includes alternative discipline in lieu of suspension; case cancelled or merged with another case; caution letter; last chance agreement; oral counseling; reprimand; written counseling; etc.

d *Id.*

- 9. THE RIGHT TO RETAIN REPRESENTATION** – Taxpayers have the right to retain an authorized representative of their choice to represent them in their dealings with the IRS. Taxpayers have the right to seek assistance from a Low Income Taxpayer Clinic if they cannot afford representation.

Measure/Indicator	FY 2016	FY 2017	FY 2018
Percentage of Power of Attorney Requests Overage (as of 10/1/16, 9/30/17, 9/29/2018) <sup>a</sup>	0%	18.2%	0%
Number of Low Income Taxpayer Clinics Funded (calendar year) <sup>b</sup>	138	138	134
Funds Appropriated for Low Income Taxpayer Clinics <sup>c</sup>	\$12.0 million	\$12.0 million	\$12.0 million
Number of States with a Low Income Taxpayer Clinic (calendar year) <sup>d</sup>	49	49	48
Number of Low Income Taxpayer Clinic Volunteer Hours (calendar year) <sup>e</sup>	60,669	47,480	57,914

a IRS, JOC, *Customer Account Services, Accounts Management Paper Inventory Reports* (weeks ending Oct. 1, 2016, Sept. 30, 2017, and Sept. 29, 2018).

b IRS Pub. 5066, *Low Income Tax Clinics Program Report* (Jan. 2017, Feb. 2018, and Dec. 2018).

c Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, enacted Dec. 18, 2015. Consolidated Appropriations Act, 2017, Pub. L. No. 115-31, enacted May 5, 2017. Consolidated Appropriations Act, 2018, Pub. L. No. 115-141, enacted March 23, 2018. The amounts actually awarded to Low Income Taxpayer Clinics (LITCs) differed from the appropriated amounts. The amount awarded to clinics in FY 2016 was over \$11.4 million based on the number of available grantees who met the requirements and were selected for funding. The amount awarded to clinics in FY 2017 was approximately \$11.8 million based on the number of available grantees who met the requirements and were selected for funding. The amount awarded to clinics in FY 2018 was over \$11.8 million based on the number of available grantees who met the requirements and were selected for funding. The FY 2016 figures have been updated from what we reported in the 2016 Annual Report to Congress.

d IRS Pub. 5066, *Low Income Tax Clinics Program Report* (Jan. 2017, Feb. 2018, and Dec. 2018). For calendar year (CY) 2018, forty-eight states and the District of Columbia had at least one LITC. As of the start of the 2018 CY there was no LITC in Hawaii or North Dakota.

e *Id.* The FY 2016 number (60,669) was confirmed by the LITC Program Director (Oct. 28, 2016). The FY 2016 Pub. 5066 reported a rounded number (60,000). The FY 2016 figure reflects volunteer hours from CY 2015. The FY 2017 figure reflects volunteer hours from CY 2016. The FY 2018 figure reflects volunteer hours from CY 2017.

**10. THE RIGHT TO A FAIR AND JUST TAX SYSTEM** – Taxpayers have the right to expect the tax system to consider facts and circumstances that might affect their underlying liabilities, ability to pay, or ability to provide information timely. Taxpayers have the right to receive assistance from TAS if they are experiencing financial difficulty or if the IRS has not resolved their tax issues properly and timely through its normal channels.

Measure/Indicator	FY 2016	FY 2017	FY 2018
Offer in Compromise (OIC): Number of Offers Submitted <sup>a</sup>	64,479	62,243	59,127
OIC: Percentage of Offers Accepted <sup>b</sup>	42.5%	38.1%	37.8%
Installment Agreements (IA): Number of Individual & Business IAs <sup>c</sup>	3,115,404	2,924,780	2,883,035
Streamlined Installment Agreements Number of Individual & Business IAs <sup>d</sup>	2,630,811	2,236,434	2,079,743
Installment Agreements Collection Field Function (Cff): Number of Individual & Business IAs <sup>e</sup>	42,978	35,449	39,178
Streamlined Installment Agreements (Cff): Number of Individual & Business IAs <sup>f</sup>	8,477	6,936	5,224
Number of OICs Accepted per Revenue Officer <sup>g</sup>	7.7	7.6	9.1
Number of IAs Accepted per Revenue Officer <sup>h</sup>	12.0	10.6	14.8
Percentage of Cases in the Queue (Taxpayers) <sup>i</sup>	15.5%	13.9%	16.6%
Percentage of Cases in the Queue (Modules) <sup>j</sup>	23.9%	21.8%	24.6%
Percentage of Taxpayer Delinquent Accounts (TDAs) reported Currently Not Collectible – Surveyed (shelved) <sup>k</sup>	16.9%	32.3%	75.6%
Age of Delinquencies in the Queue <sup>l</sup>	4.5 years	4.5 years	4.8 years
Percentage of Modules in Queue prior to three tax years ago <sup>m</sup>	78.7%	78.2%	79.6%
Percentage of cases where the taxpayer is fully compliant after five years <sup>n</sup>	48%	47%	51%

a IRS, Collection Activity Report No. 5000-108, FY 2016 (Oct. 7, 2016), FY 2017 (Oct. 2, 2017), and FY 2018 (Oct. 1, 2018).

b *Id.*

c IRS, Collection Activity Report No. 5000-6, FY 2016 (Oct. 3, 2016), FY 2017 (Oct. 1, 2017), and FY 2018 (Sep. 30, 2018).

d *Id.*

e *Id.*

f *Id.*

g *Id.* See also IRS Human Resources Reporting Center – number of revenue officers in Small Business/Self-Employed as of the end of FY 2016, FY 2017, and FY 2018 (pay period 19).

h *Id.*

i IRS, Collection Activity Report No. 5000-2, FY 2016 (Oct. 3, 2016), FY 2017 (Oct. 1, 2017), and FY 2018 (Sep. 30, 2018).

j *Id.*

k *Id.* Beginning in FY 2017, the IRS shelves cases prior to potential transfer for the Private Collection Initiative. Row title has been updated to clarify the data points.

l Accounts Receivable Dollar Inventory. Age of cases in the collection queue as of cycle 37 of 2016, and 2017, and 2018.

m IRS, Collection Activity Report No. 5000-2, FY 2016 (Oct. 3, 2016), FY 2017 (Oct. 1, 2017), and FY 2018 (Sep. 30, 2018).

n Calculation by TAS Research. Percentage of taxpayers with tax delinquent accounts in 2011, 2012, and 2013, respectively, and who have no new delinquencies five years later. The FY 2017 figure has been updated from what we reported in the 2017 Annual Report Congress. IRS, CDW, Individual Master File (IMF).

## INTRODUCTION: The Most Serious Problems Encountered by Taxpayers: The Taxpayer's Journey

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Internal Revenue Code (IRC) § 7803(c)(2)(B)(ii)(III) requires the National Taxpayer Advocate to prepare an Annual Report to Congress that contains a summary of at least 20 of the most serious problems (MSPs) encountered by taxpayers each year. For 2018, the National Taxpayer Advocate has identified, analyzed, and offered recommendations to assist the IRS and Congress in resolving 20 such problems.

As in earlier years, this report discusses at least 20 of the most serious problems encountered by taxpayers—but not necessarily *the top 20* most serious problems. That is by design. Since there is no objective way to select the 20 MSPs, we consider a variety of factors when making this determination. Moreover, while we carefully rank each year's problems under the same methodology (described below), the list remains inherently subjective in many respects.

To simply report on the top 20 problems would limit our effectiveness in focusing congressional, IRS, and public attention on critical issues. It would require us to repeat much of the same data and propose many of the same solutions year to year. Thus, the statute gives the National Taxpayer Advocate flexibility in selecting both the subject matter and the number of topics discussed and to use the report to put forth actionable and specific solutions instead of mere criticism and complaints.

### Methodology of the Most Serious Problem List

The National Taxpayer Advocate considers a number of factors in identifying, evaluating, and ranking the MSPs encountered by taxpayers. In many years, the National Taxpayer Advocate identifies a theme or groupings of issues for the Annual Report that is reflected in the selection of issues. For example, this year the MSPs illustrate the taxpayer's journey. The MSPs are grouped by the stages of the journey as follows:

- The Prefiling Stage: Taxpayer Access to Information;
- The Return Filing Process: Balancing Ease and Efficiency with Revenue Protection;
- The Examination Process: Minimizing Taxpayer Burden in the Selection and Conduct of Audits;
- The Notice Function: IRS Written Communication with Taxpayers;
- The IRS Collection Function: Minimizing Taxpayer Burden and Addressing Taxpayers' Ability to Pay; and
- The Litigation Stage: Access to Representation.

The 20 issues in this year's report are ranked according to the following criteria:

- Impact on taxpayer rights;
- Number of taxpayers affected;
- Interest, sensitivity, and visibility to the National Taxpayer Advocate, Congress, and other external stakeholders;
- Barriers these problems present to tax law compliance, including cost, time, and burden;
- The revenue impact of noncompliance; and
- Taxpayer Advocate Management Information System (TAMIS) and Systemic Advocacy Management System (SAMS) data.

Finally, the National Taxpayer Advocate and the Office of Systemic Advocacy examine the results of the ranking on the remaining issues and adjust it where editorial or numerical considerations warrant a particular placement or grouping.

### **Taxpayer Advocate Management Information System (TAMIS) List**

The identification of the MSPs reflects not only the mandates of Congress and the IRC, but TAS's integrated approach to advocacy—using individual cases as a means for detecting trends and identifying systemic problems in IRS policy and procedures or the Code. TAS tracks individual taxpayer cases on TAMIS. The top 25 case issues, listed in Appendix 1, reflect TAMIS receipts based on taxpayer contacts in Fiscal Year 2018, a period spanning October 1, 2017, through September 30, 2018.

### **Use of Examples**

The examples presented in this report illustrate issues raised in cases handled by TAS. To comply with IRC § 6103, which generally requires the IRS to keep taxpayer returns and return information confidential, the details of the fact patterns have been changed. In some instances, the taxpayer has provided written consent for the National Taxpayer Advocate to use facts specific to that taxpayer's case. These exceptions are noted in footnotes to the examples.

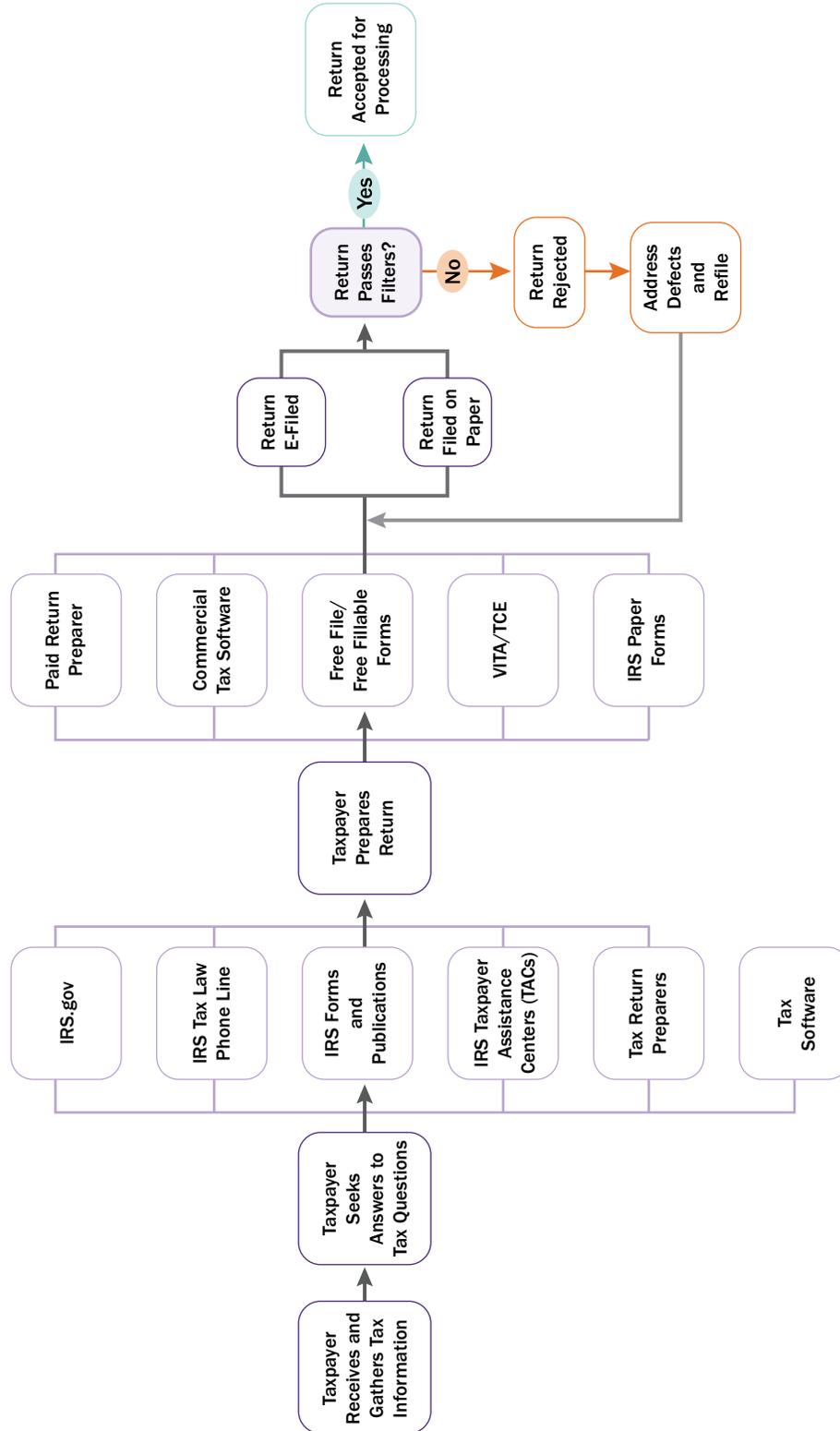
### **Data Compilation and Validation**

The data cited in the National Taxpayer Advocate's annual reports generally come from one of three sources: (i) publicly available data such as the IRS Data Book, Government Accountability Office reports, and Treasury Inspector General for Tax Administration reports; (ii) IRS databases to which TAS has access; and (iii) IRS data that is provided by the Operating Divisions pursuant to TAS information requests. Once data has been compiled, TAS's Office of Research and Analysis double checks it. Then TAS sends all data included in the "most serious problems" section of the report to the IRS for final verification prior to publication.

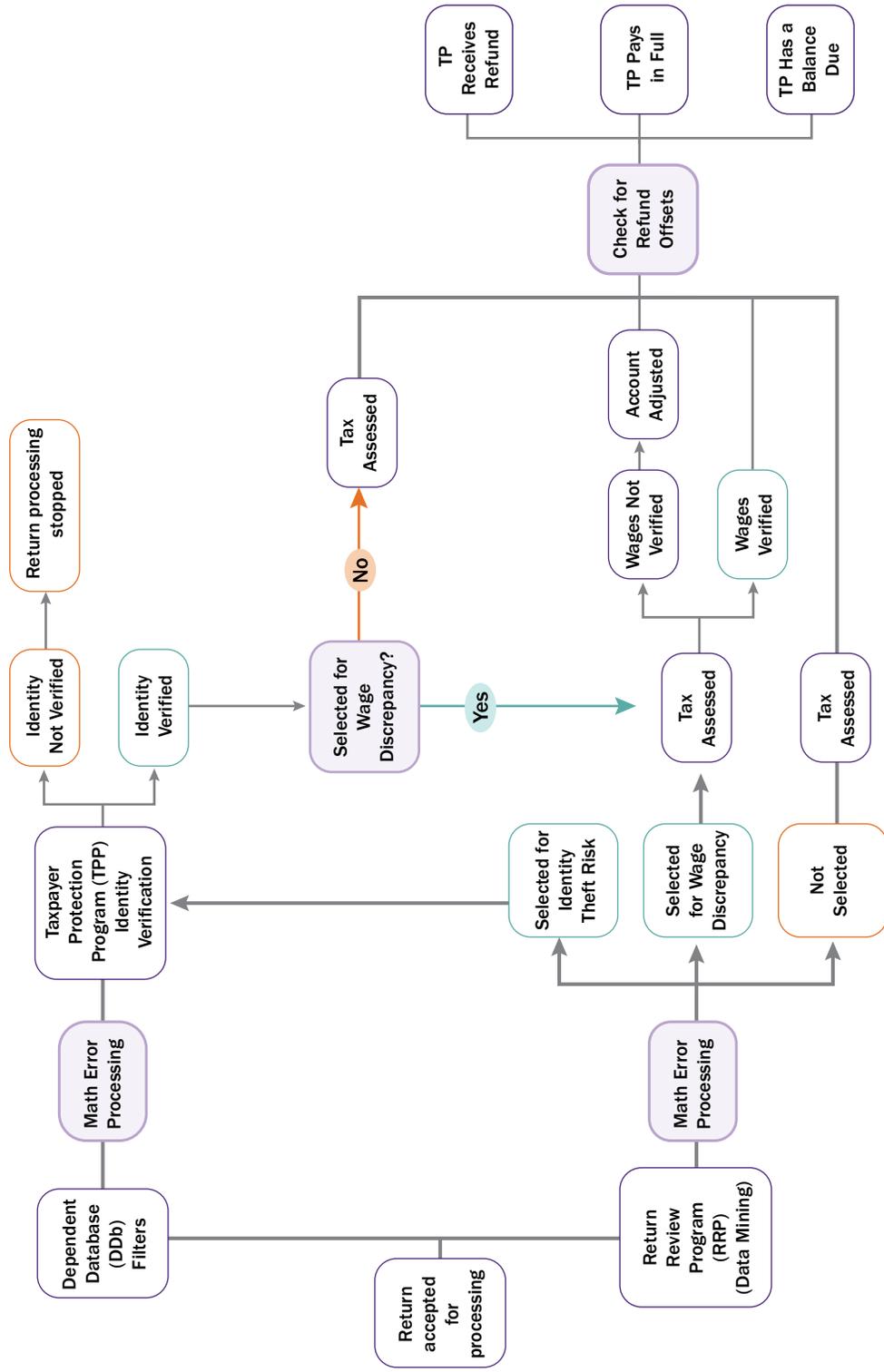
On the rare occasion where TAS and the IRS have a disagreement about data, we generally meet to discuss it, and if a disagreement persists, we note it in the report. This process ensures data integrity and full transparency regarding data sources and reliability.

# THE TAXPAYER'S JOURNEY: Roadmaps of the Taxpayer's Path Through the Tax System

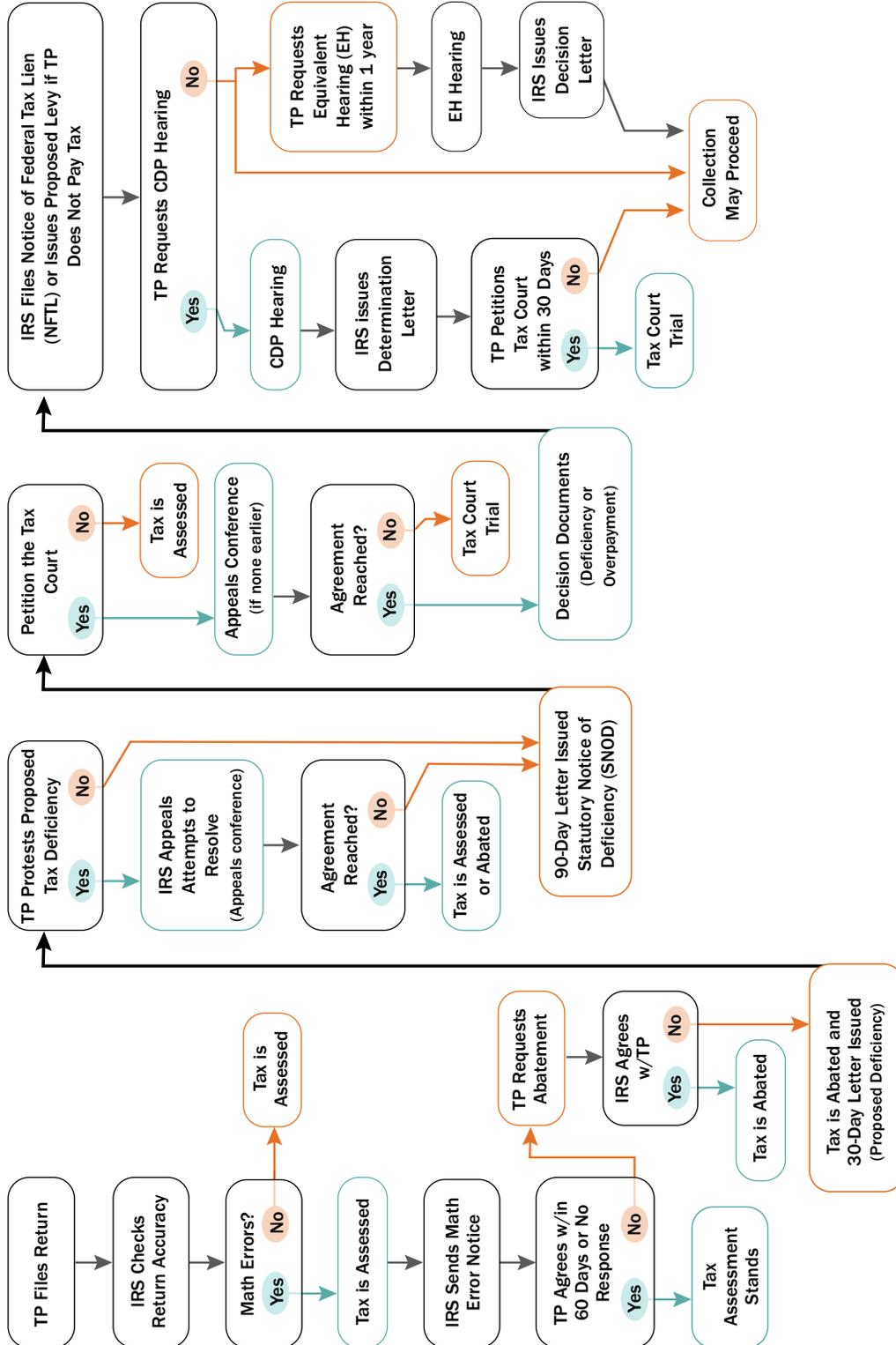
## Tax Return Preparation Roadmap



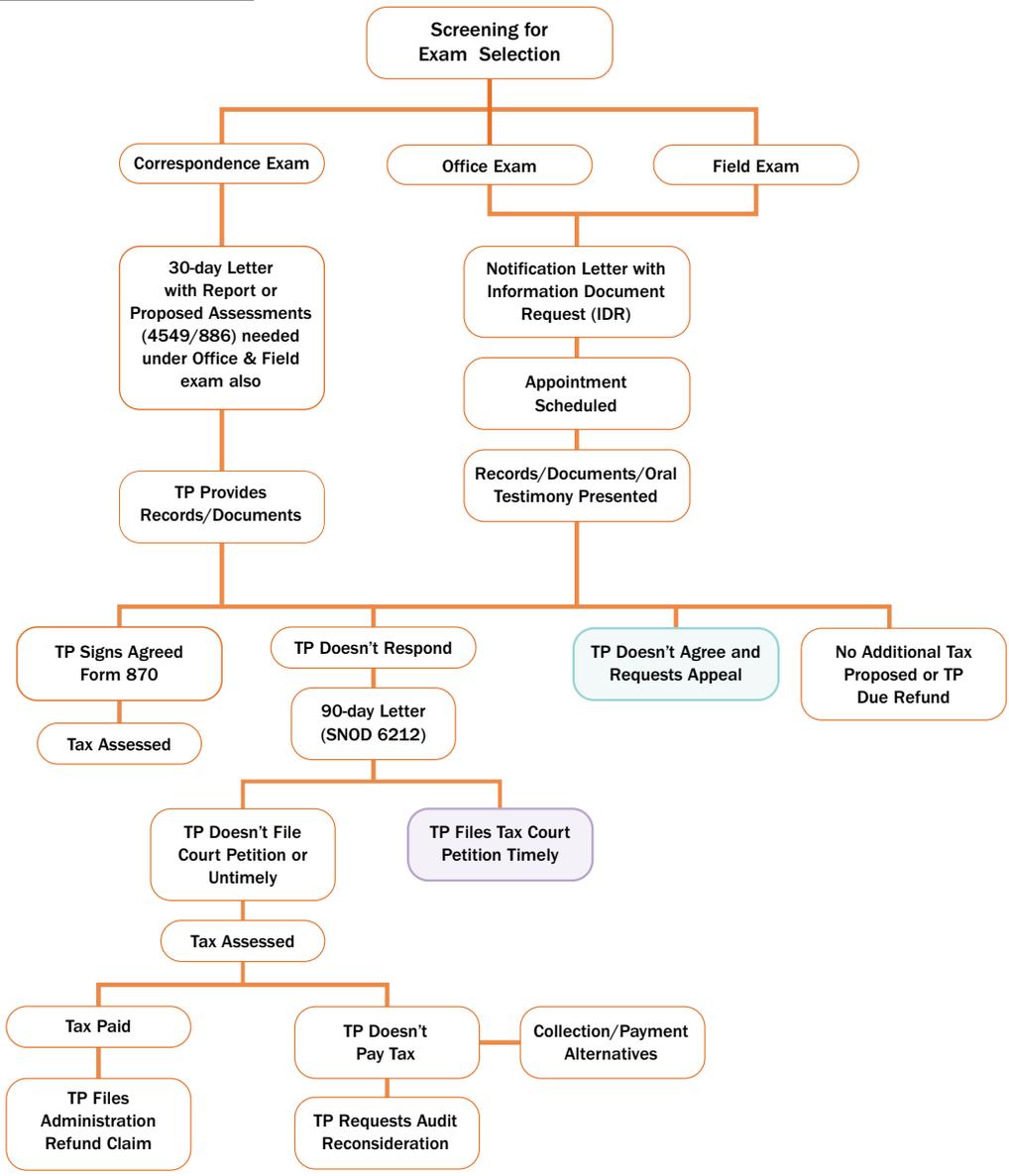
Tax Return Processing Roadmap



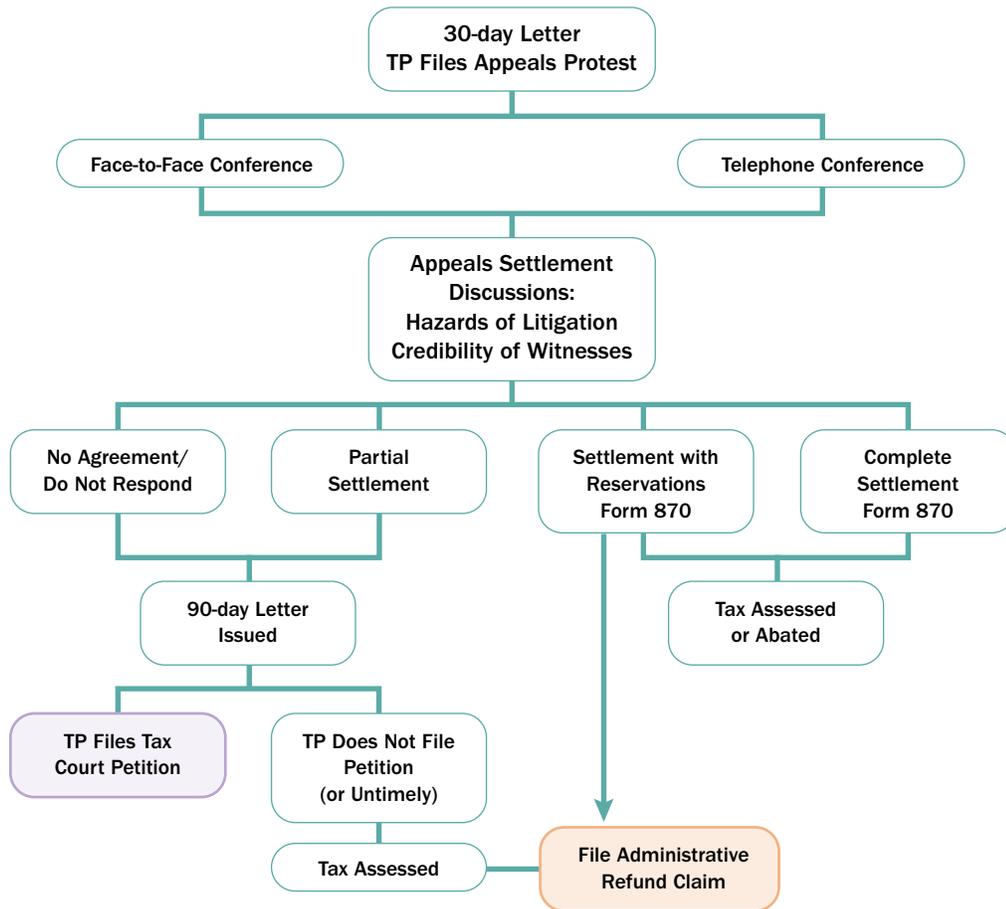
Notices Roadmap



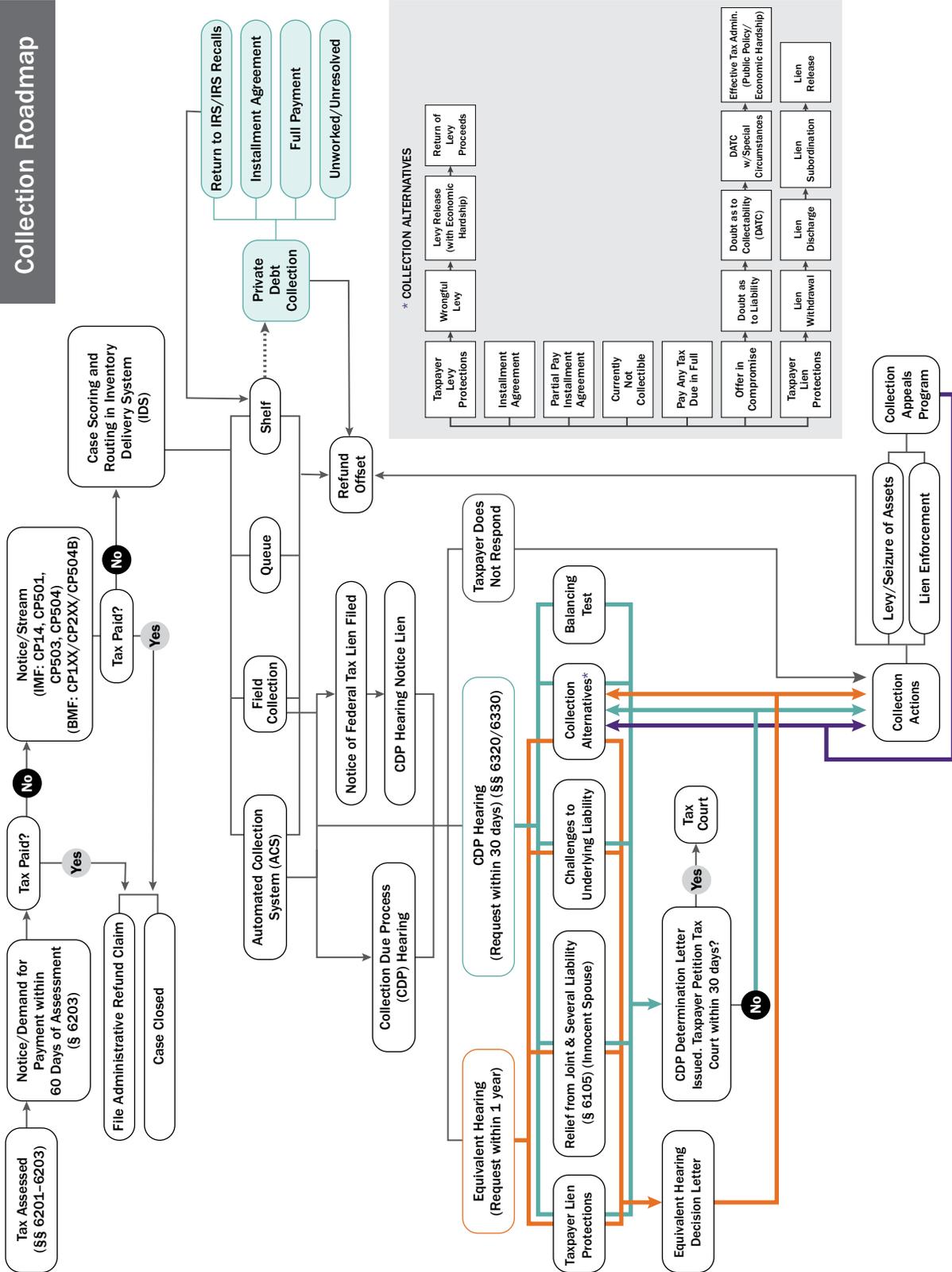
**Exam Roadmap**



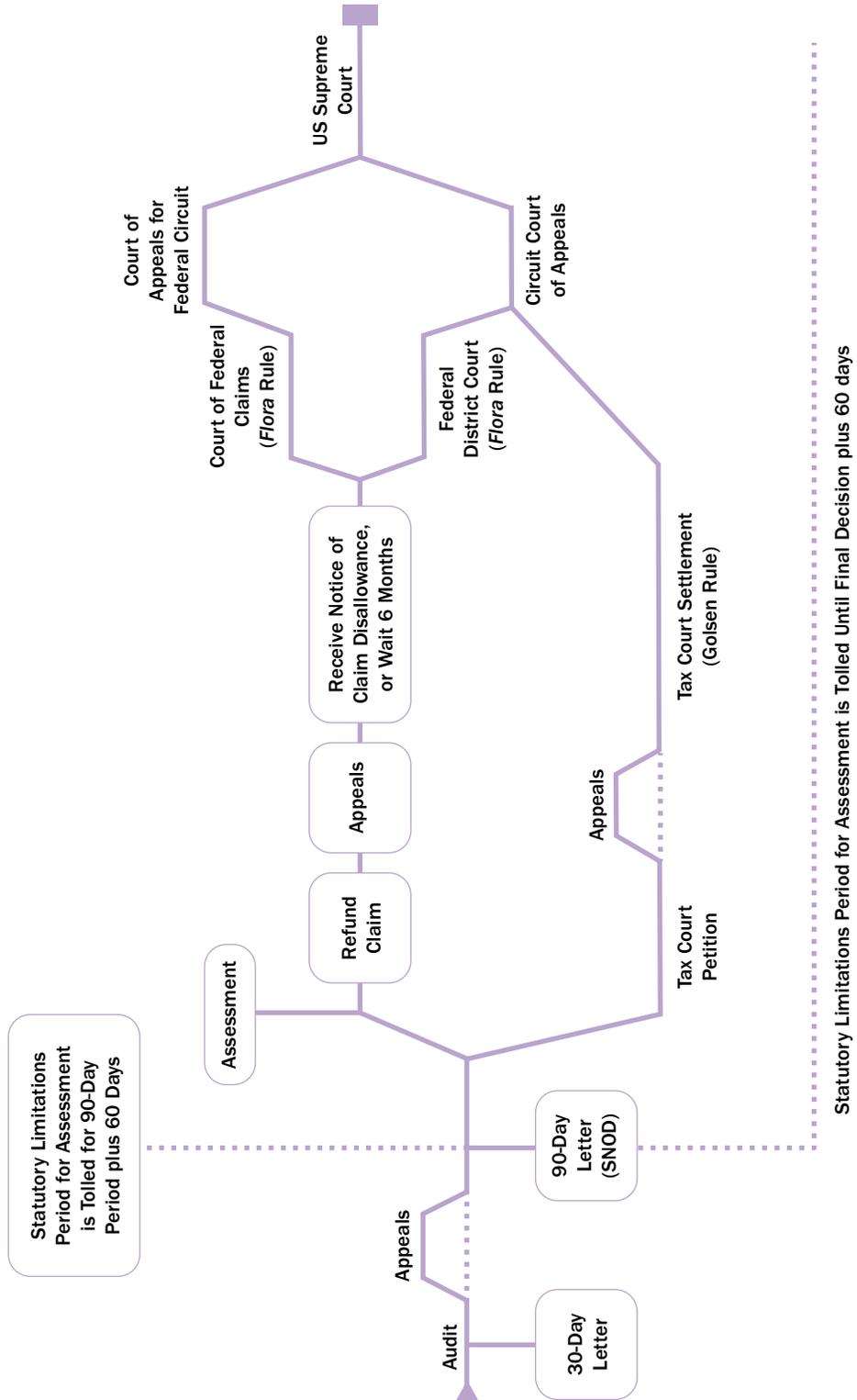
## Appeals Roadmap



# Collection Roadmap



Litigation Roadmap



**MSP  
#1****TAX LAW QUESTIONS: The IRS's Failure to Answer the Right Tax Law Questions at the Right Time Harms Taxpayers, Erodes Taxpayer Rights, and Undermines Confidence in the IRS****RESPONSIBLE OFFICIAL**

Ken Corbin, Commissioner, Wage and Investment Division

**TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to a Fair and Just Tax System*

**DEFINITION OF PROBLEM**

The Internal Revenue Code (IRC) is a behemoth document containing nearly four million words, further complicated by the most sweeping tax reform since 1986, the Tax Cuts and Job Act (TCJA), passed in December 2017.<sup>2</sup> Taxpayers need answers to tax law questions, both basic and complicated, and they need those answers quickly and accurately to meet their obligations for the upcoming year. The *right to be informed* is fundamental to exercising all other taxpayer rights and serves as a cornerstone for taxpayers to understand their tax rights and responsibilities. This is why it is the first right in the Taxpayer Bill of Rights.<sup>3</sup> If the IRS fails to meet the *right to be informed*, it undermines all other taxpayer rights, including the *rights to quality service* and *to a fair and just tax system*.

Calling the tax agency, charged with implementing and administering the nation's tax law, and being told your question is out-of-scope (*i.e.*, the IRS does not answer that question, during filing season or otherwise), that the employee can only answer your question during filing season, or that the employee who answers your call is not trained to answer your question violates taxpayer rights. Expecting taxpayers to fit all tax law questions into a 3.5-month window during filing season results in frustration for taxpayers, lowers confidence in the service the IRS provides, and may force taxpayers to use costly third-party options to accurately answer their questions. Further, the downstream consequences of not answering taxpayer questions at all or not answering questions accurately creates rework for the IRS and burden for the taxpayer to seek a correct answer elsewhere.

The National Taxpayer Advocate has identified the following problems associated with the IRS's approach to answering tax law questions:

- Failure to collect information about calls regarding out-of-scope issues prevents the IRS from educating taxpayers about those issues via alternative methods;

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 A search of the IRC conducted using the "word count" feature in Microsoft Word turned up nearly four million words. National Taxpayer Advocate 2012 Annual Report to Congress 6. See also Pub. L. No. 115-97, 131 Stat. 2054 (Dec. 22, 2017).

3 See TBOR, [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights).

- Test calls to the IRS reveal inconsistent service for taxpayers; and
- The IRS has not adopted best practices to address tax law questions.

## ANALYSIS OF PROBLEM

### Background

In 2014, the IRS implemented a policy to only answer tax law questions during filing season,<sup>4</sup> roughly from January through mid-April of any year. It justified this abrupt change in policy as a cost-savings effort in a time of budget constraints. This change does not comport with an agency charged with administering the tax law and focused on the customer experience.

For tax returns due in 2015, 2016, and 2017, over 13 million individual taxpayers per tax year filed returns with extensions of time to file.<sup>5</sup> An average of 9.5 million taxpayers per year filed quarterly estimated taxes.<sup>6</sup> All of these taxpayers have legitimate needs for IRS tax law assistance year-round. Further, taxpayers have ever-changing tax situations. People move, open a business, close a business, get married, get divorced, have children, and many other life changes that affect their tax obligations. Forcing taxpayers into a 3.5-month window to ask questions or making it necessary for them to seek advice from a third-party source can be frustrating and costly to the taxpayer and result in eroded trust and confidence in the IRS.

### Failing to Track Out-of-Scope Topics Taxpayers Ask About Is a Missed Opportunity

The IRS designates certain tax law topics as out-of-scope, meaning it does not provide answers to taxpayers who call or visit the IRS inquiring about those issues.<sup>7</sup> In the past, taxpayers could electronically submit questions on out-of-scope topics via the R-mail system, but the IRS discontinued the program in 2015.<sup>8</sup> The IRS does not track what taxpayers ask about if the topic is out-of-scope.<sup>9</sup> Failing to do so limits the ability of the IRS to determine if there is sufficient demand for information about a topic to consider declaring the topic in-scope. If the IRS tracked the out-of-scope topics taxpayers called or visited a Taxpayer Assistance Center (TAC) about, it could use the information to refine its services.

Particularly in TACs, the IRS could use this information to determine if there are topics specific to a certain location and add services on topics that would be useful in that area. Further, tracking the scope of all taxpayer contacts provides a better picture to the IRS of the types of contacts taxpayers make and the scope of work received by the IRS. If many taxpayers are calling about similar issues, the IRS can use such information to better refine its outreach strategy or to develop more robust information on its website, in press releases, or publications. TAS has recently begun tracking all taxpayer contacts to

4 Internal Revenue Manual (IRM) 21.3.4.9.1(2) (Oct. 1, 2018). See also IRM 21.3.4.9.1(3) (Oct. 1, 2018) (providing topics that will be answered all year and allowing for a manager discretion for answering post-filing season individual tax law questions).

5 IRS, Compliance Data Warehouse (CDW) (data retrieved Nov. 13, 2018).

6 IRS, CDW (data retrieved Nov. 13, 2018). This number includes taxpayers who elected to have their current year tax refund applied to the following year's estimated tax liability, however, these taxpayers may also need assistance during the year regarding the application of their pre-payment.

7 IRM 21.1.1.3.1, *Out of Scope and Limited Service* (Oct. 1, 2018); IRM 21.1.1-1, *Out-of-Scope Topics and Forms* (Oct. 1, 2017).

8 IRM 21.3.8.6, *R-Mail and Out of Scope Procedures* (Oct. 1, 2015).

9 IRS response to TAS information request (Oct. 24, 2018).

inform our resource allocation and better understand the types of issues taxpayers bring to TAS, which in turn will inform our outreach strategy.<sup>10</sup>

The IRS offers the Interactive Tax Assistant (ITA) to taxpayers seeking assistance via the internet.<sup>11</sup> Taxpayers can look for popular topics or search to find out if a particular topic is available. If a topic is available, the taxpayer can answer a series of questions to determine an answer based on his or her situation. If the IRS tracked search terms entered into ITA, it could develop additional materials or interactive tools to answer commonly asked questions. The IRS could also use artificial intelligence and pattern-recognition technology to develop answers or help direct taxpayers to the correct information.

### Results of TAS Test Calls Show Inconsistent Service and Answers

In order to test the customer experience with respect to tax law questions, TAS developed and tested a series of questions relating to areas of the law that are deemed in-scope and had not changed under the TCJA, issues that are deemed out-of-scope, and topics impacted by the TCJA.<sup>12</sup> Between April and October 2018, TAS conducted test calls to the IRS to discover what might happen when a taxpayer calls the IRS.

TAS conducted two rounds of test calls in 2018, in April and May, and again in September and October.<sup>13</sup> In both rounds of test calls, TAS callers experienced inconsistent service, even when asking questions about changes under the TCJA, which the IRS previously indicated it would now answer year-round. Several callers reported the same script being read over the phone, telling the callers:

There is no tax law personnel at this time due to budgetary cuts. This tax topic cannot be answered at this time. The employees that will be able to answer this question will be available beginning January 2, 2019 through April 15, 2019.

This is particularly concerning given the IRS is supposed to be answering TCJA calls year-round. In one instance, a caller was told she needed to hire a paid professional to answer her question. On many calls, the employee told the caller the call would be transferred, and the transfer ended in a pre-recorded message telling the caller the question was out-of-scope and then disconnecting the call.

On a test call made in April 2018, a TAS representative asked a question regarding the home office deduction under the TCJA. The answer is simple: the home office deduction (IRC § 280A) did not change under the TCJA. However, the customer service representative who answered the phone after the TAS caller pushed the selection to ask a question about tax reform apologized and explained that he had not yet received training on the TCJA and did not expect to receive training until the end of calendar year. Later calls in September and October featured additional employees relating that they had little training in the new tax law and also apologizing for being unable to help.

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10 The Contact Record screen captures specific data on all customer contacts and provides TAS with additional quantifiable information on what drives taxpayers to contact TAS.

11 IRS, *Interactive Tax Assistant*, <https://www.irs.gov/help/ita>.

12 TAS employees called the main IRS 1040 phone line in two rounds of tests between April 2018 and October 2018. Callers were assigned specific questions about various topics, some impacted by the TCJA, some topics that are considered year-round tax law topics, and some that are answered only during filing season. The calls were limited in number and do not represent a statistically valid sample. We relate our findings here solely as qualitative and anecdotal evidence of the taxpayer's experience. A record of the test calls made to the IRS is contained in Appendix A.

13 For further discussion of the test tax law calls, see National Taxpayer Advocate Fiscal Year 2019 Objectives Report 36-40.

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Taxpayers have legitimate needs for IRS tax law assistance year-round. Further, taxpayers have ever-changing tax situations. People move, open a business, close a business, get married, get divorced, have children, and many other life changes that affect their tax obligations.

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While it is understandable that the specific details of the application of tax law changes may not be determined in the early months following enactment, it is unacceptable that employees answering a telephone line designated for tax reform did not have a basic outline of the law and what high level provisions had or had not changed. The failure to provide its employees with this information, so they provide even rudimentary service to taxpayers, is demoralizing for the workforce and frustrating for taxpayers.

### Assistance With the Tax Cuts and Jobs Act May Not Meet Taxpayer Needs

While the decision to answer TCJA questions year-round is the right thing to do, it is unclear how long the IRS will continue to answer TCJA questions outside of filing season.<sup>14</sup> Further, the IRS did not begin answering questions about the TCJA until after the beginning of 2019.<sup>15</sup> Taxpayers who have called (as demonstrated by the results of the TAS test calls) to date seeking assistance with meeting their tax year 2018 obligations were told to call back in January 2019, to seek assistance from third parties, or to research the question on the IRS website. However, information has been slow to roll out to the IRS website, and taxpayers may have needed to make adjustments to their withholding at the beginning of tax year 2018 to avoid penalties and interest when they file their returns in 2019.

In an attempt to fill the void of information, TAS developed a Tax Changes website in August that includes line-by-line explanations of the tax changes for individuals under the TCJA.<sup>16</sup> The topics compare the law in 2017 to the new law and provide scenarios that may impact the taxpayer based on the changes and links to other resources that may be useful in determining how the new law applies to the taxpayer's situation. TAS continues to add materials to the Tax Changes tool as they become available. The website is now available in Spanish.

While the IRS is currently working on training its employees on the TCJA, as of late October, much of the training was not yet finalized.<sup>17</sup> Several annual trainings were updated to reflect the TCJA changes; however, the updated forms for taxpayers were not yet available at the time, so the trainings could not reflect the new forms and thus could only reference the new forms rather than demonstrating them for employees.<sup>18</sup> Finally, the IRS has designated some topics related to the TCJA out-of-scope, even though the law has changed in those areas, such as treatment of student loans discharged on account of death or disability or limitation on losses for taxpayers other than corporations.<sup>19</sup>

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14 IRS response to TAS information Request (Oct. 24, 2018); IRS response to TAS information request (Mar. 2, 2018).

15 *Id.*

16 TAS, *Tax Changes by Topic*, <https://taxchanges.us/?source=ttk>.

17 IRS response to TAS information request (Oct. 24, 2018).

18 *Id.*

19 *Id.*

### The IRS Is Not Providing World-Class Service in Relation to Tax Law Questions

While countries around the world differ in how they provide advice or answer taxpayer questions, several countries have much more robust and diversified channels to answer questions than the IRS provides. An approach that meets taxpayers where they are, whether that is online, in-person, on the phone, or another method provides more opportunities for taxpayers to receive information and would support the *right to be informed*. The IRS could adopt these methods and use emerging techniques such as artificial intelligence and pattern recognition technology to identify uncommon or complex topics.

Her Majesty's Revenue and Customs (HMRC), the United Kingdom's taxation authority, has dozens of dedicated phone lines, email addresses, and mail addresses available to taxpayers depending on topic.<sup>20</sup> HMRC also offers live chat for specific topics, including self-assessment and pay-as-you-earn income tax.<sup>21</sup> Further, taxpayers can use Twitter to ask general questions to HMRC.<sup>22</sup>

Taxpayers in Norway also have multiple ways to receive tax law assistance from The Norwegian Tax Administration. Taxpayers can call for assistance, but they can also chat live online from 9 a.m. to 3:30 p.m. on weekdays.<sup>23</sup> Taxpayers may also ask questions on the Administration's Facebook page with assistants standing by to answer, email, or book an appointment in-person.<sup>24</sup>

Helping taxpayers get the right answer should be a focus of any tax administration. By getting the correct answer up front, taxpayers will be able to more easily comply correctly with their tax obligations and prevent rework on the part of the taxpayer or the IRS.

## CONCLUSION

Providing taxpayers timely and accurate answers to their tax law questions is crucial to helping taxpayers understand and meet their tax obligations and is fundamental to the *right to be informed*. If a taxpayer cannot find answers from the IRS, it undermines all taxpayer rights. The IRS has many tools available to meet the needs of taxpayers and ensure that taxpayers can find the assistance they need promptly. By meeting taxpayers where they are, whether on the phone or online, more taxpayers will be able to get answers to their tax law questions. The IRS can and should track what topics taxpayers seek assistance with that it does not currently answer and use that data to better inform and refine its strategy for answering tax law questions, particularly in light of the recent changes to the tax code, which impact all taxpayers.

20 Her Majesty's Revenue and Customs (HMRC), *Contact HM Revenue & Customs* <https://www.gov.uk/government/organisations/hm-revenue-customs/contact> (last visited Nov. 14, 2018).

21 HMRC, *Self Assessment: general enquiries* <https://www.gov.uk/government/organisations/hm-revenue-customs/contact/self-assessment> (last visited Nov. 14, 2018).

22 *Id.*

23 The Norwegian Tax administration, *Contact us* <https://www.skatteetaten.no/en/contact/> (last visited Nov. 14, 2018).

24 *Id.*

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Answer in-scope tax law questions year-round.
2. Deem all questions related to the new tax law as in-scope for a reasonable period of at least two years and evaluate taxpayer demand prior to declaring topics out of scope.
3. Track calls and contacts about out-of-scope topics and develop Interactive Tax Law Assistant (ITLA) scripts for frequently asked questions or consider declaring topics in-scope.
4. Develop a method to respond to uncommon or complex questions (*i.e.*, those that are out-of-scope for the phones and TACs) via email or call back to the taxpayer, such as utilizing artificial intelligence and pattern recognition.

## Appendix A

Question 1: For tax year 2018, can I still use the "Simplified Method" for claiming the home office deduction?						
Date of Call	Start Time	End Time	Question Call Summary	Question Answer	Question Selection	Question Answer Comments
May 2018	10:14	10:40	Asked if self-employed or employee, did research, nothing that lists home office on his info, may be qualified business income deduction, transfer me to SE assistant, SE CSR said they have no specifics on this subject right now, provided irs.gov to link to Tax Reform, IRS has not implemented new guidance.	No Answer Given	CSR read me some information, but the information did not respond to question; #CSR's answer did not leave me with any sense how to proceed; #Although listed as in-scope, the CSR did not answer the question.; #Other	Told me there were some new changes for sole proprietorships but had no specifics of home office in her information and if it had changed under the tax reform. Provided Pub 535 for additional information on home office. (Note home office specific information is in Pub 587)
May 2018	17:08	17:16	Don't know if it had changed or not. We have not received any updated information about tax reform issues. Suggested I keep checking irs.gov for latest updates. Asked what Pub I would find home office information, they did not know, referred me to irs.gov and then search self-employment issues.	No	Although listed as in-scope, the CSR did not answer the question.; #CSR's answer did not leave me with any sense how to proceed; #Other	Did not try to find correct answer for question. Did not try to find publication number for home office deduction, kept referring me to irs.gov to check status for tax reform updates.
Sept. 2018	14:23	14:37	He attempted to research for me but said he could not locate any information on my question and that probably meant it did not change. Explained how to get to tax reform provisions on irs.gov, then business deductions/depreciation, should be in that section. Stated they do not have a lot of information on the new tax reform provisions. Expect to learn more when they go to training later in the year.	No Answer Given	CSR's answer did not leave me with any sense how to proceed; #Although listed as in-scope, the CSR did not answer the question.	Was sorry he could not help me.
Sept. 2018	14:44	14:52	First off initial assistant answering refused to repeat her ID number, told me she already gave it to me not going to give in again, then transfer me to next assistant. Next assistant told me he was not trained for home office deduction questions. Told me they don't have any live assistants on that topic this time of year. Told me to check the website, didn't give any additional information. Told me due to budgetary concerns and staffing shortfall IRS has no one can answer tax reform questions. Told me that I needed to seek paid assistance if I could not find answer on IRS website.	No Answer Given	CSR said question was not in-scope; #CSR's answer did not leave me with any sense how to proceed; #Although listed as in-scope, the CSR did not answer the question.	

Question 2: Has the additional standard deduction for the blind or elderly changed for tax year 2018?

Date of Call	Start Time	End Time	Question Call Summary	Question Answer	Question Selection	Question Answer Comments
May 2018	14:23	14:33	<p>First assistor stated she would need to transfer me to the correct area of Tax Reform that would be able to answer my question. She stated she would be placing me on hold for probably five to seven minutes. She came back on in a minute and said she was transferring me.</p> <p>The second assistor stated that all of the standard deductions have changed but let me look it up. The Form 1040ES has all of the information regarding standard deductions listed on the form. She stated that I would be able to view the information online on page 2 of the Form 1040ES. She stated for single, unmarried for the tax year of 2018, I would be entitled to an additional \$1,600 for each checkbox checked for over 65 and blind. If MFJ or MFS, I would be entitled to an additional \$1,300 for each checkbox checked.</p>	Yes	Other	CSR provided the correct information and advised me where I could locate the information online.
May 2018	14:34	14:41	<p>Ok so your question is in regard to Tax Reform Act. The best way for you to get the information is to review the Form 1040ES. Even though the Form 1040ES is for making estimated tax payments and you may not be required to make estimated tax payments, the form has information regarding standard deduction. He asked my filing status, I said single. He stated the standard deduction would be \$12,000 plus an additional \$1,600 for over 65 and an additional \$1,600 if blind for an additional total of \$3,200 if both over 65 and blind. He stated that the IRS will have additional information regarding the changes later this year.</p>	Yes	Other	He referred me to the Form 1040ES to review the information. He did state that even though I may not be required to make estimated payments that the Form 1040ES contains information regarding the standard deduction amounts for 2018.
Sept. 2018	12:41	12:52	<p>I need to review Congress overview that has recently been disseminated. We may also get information closer to filing season. Placed on hold while he reviewed for the information. The information from Congress does not have this information on it. Let me check the standard deduction. Asked my filing status, I stated single. He stated that the standard deduction was \$6,350 now being increased to \$12,000 no information is available for the blind and elderly at this time. He suggested I research irs.gov using 2018 standard deduction info when it got closer to filing season.</p>	No	CSR read me some information, but the information did not respond to question	
Sept. 2018	13:00	13:07	<p>The assistor tried to find the answer but came back on the line and stated that he needed to send my call to the Basic Tax Law line.</p>	No	Other	The assistor stated he did not have the information that he needed to send me to the Basic Tax Law line. A message came on the line and stated that the line was only answered during the filing season. If calling after filing season, advised to access irs.gov for additional information.

**Question 3: Has the taxation of social security changed for tax year 2018?**

Date of Call	Start Time	End Time	Question Call Summary	Question Answer	Question Selection	Question Answer Comments
May 2018	09:14	09:20	No answer given	No Answer Given	Other	"There is no Tax Law personnel at this time due to budgetary cuts. This tax topic cannot be answered at this time. The employees that will be able to answer this question will be available beginning January 2, 2019 through April 15, 2019."
May 2018	09:22	09:42		No Answer Given	Other	Both CSR's stated that they did not know the answer and would transfer to someone that can answer tax law questions. I was on hold for 20 minutes and then disconnected.
Sept. 2018	09:05	09:17	"There is no Tax Law personnel at this time due to budgetary cuts. This tax topic cannot be answered at this time. The employees that will be able to answer this question will be available beginning January 2, 2019 through April 15, 2019."	No	CSR's answer did not leave me with any sense how to proceed	"There is no Tax Law personnel at this time due to budgetary cuts. This tax topic cannot be answered at this time. The employees that will be able to answer this question will be available beginning January 2, 2019 through April 15, 2019."
Sept. 2018	10:15	10:41	Stated they do not have a lot of information on the new tax reform. "There is no Tax Law personnel at this time due to budgetary cuts. This tax topic cannot be answered at this time. The employees that will be able to answer this question will be available beginning January 2, 2019 through April 15, 2019."	No	CSR's answer did not leave me with any sense how to proceed; #Other	Stated they do not have a lot of information on the new tax reform. "There is no Tax Law personnel at this time due to budgetary cuts. This tax topic cannot be answered at this time. The employees that will be able to answer this question will be available beginning January 2, 2019 through April 15, 2019."

**Question 4:** I heard there are new limits on how much I can deduct for state and local income and property taxes in tax year 2018. Is that right? If so, what is the limit?

**Question 4b:** I heard that New York recently passed a law to set up charitable funds. Donors can make the contributions to these charitable funds instead of paying local taxes. They also get a state income tax credit for a portion of the prior year contribution. If I make a contribution to these funds, can I claim a charitable deduction on my federal return (in 2018)?

Date of Call	Start Time	End Time	Question Call Summary	Question Answer	Question Selection	Question Answer Comments
May 2018	16:55	17:01	CSR apologized, stated they currently do not have reps handling tax law questions. Those reps were laid off due to budget issues. Tax law reps are only available from January 2nd to April 15th. CSR stated I could call back next year around January 2 and April 15th for assistance. CSR also suggested irs.gov site and offered to transfer me to automated tax topic line for information about my related tax topic. I agreed to listening to the Tax Topic automated line response. I was directed to the IRS site.	No Answer Given	Other	CSR did not answer my question and stated tax law questions are only handled between January 2nd and April 15th. Per CSR I can go to the IRS website for immediate assistance or I can call back between January 2 and April 15, 2019.
May 2018	08:16	08:20	As soon as I asked my question, the CSR advised me she was transferring to an area where I could type my question. I was transferred to the Tax Topic line where I received an automated response indicating questions are only answered during tax filing season and call got disconnected.	No Answer Given	Other	

Date of Call	Question 4b Summary	Question 4b Comment
May 2018	N/A	N/A
May 2018	N/A	No Answer Given

**Question 5: I have a child who lives in Canada. Can I claim a dependency exemption for my child on a 2018 tax return?**

**Question 5b: Can I claim the child tax credit or additional child tax credit (CTC/ACTC) for my child this year (Tax Year 2018)?**

**Question 5c: Can I claim a tax credit for my child as a qualifying relative?**

Date of Call	Start Time	End Time	Question Call Summary	Question Answer	Question Selection	Question Answer Comments
May 2018	16:55	17:01	CRS insisted she was not allowed to answer my question.	No Answer Given	Other; #CSR said question was not in-scope	CSR refused to answer my questions because she was "only allowed to answer those types of questions during the filing season." I tried to see if she maybe knew whether the dependency exemption had changed for next year and she said she was not sure about the requirements and pointed me to the website. She was very nice and apologized for the frustration of not being able to ask a person my question. When I asked her if the information about the changes as a result of the new tax law were on the website, she checked the website and said yes, it did explain what the differences were for 2018.
May 2018	08:16	08:20	The assistant said she couldn't answer my question because it was out of scope, there were budget cuts, and it could only be answered during the filing season. She referred me to the ITA. I asked if the ITA was updated to reflect the tax reform law because I wanted to make sure the tax reform law didn't change whether I could claim a dependent. She said she didn't know, it may not be updated, and I may want to get help from a private practitioner. I asked her if there was someone I could talk to ask if the tax reform law changed the dependency exemption. She was very rude and told me it was out of scope. She practically hung up on me as I thanked her and said goodbye.	No	CSR said question was not in-scope	

Date of Call	Question 5b Summary	Question 5b Answer	Question 5b Comments	Question 5c Summary	Question 5c Answer	Question 5c Comments
May 2018	She had the same response—she was not allowed to answer that kind of question and was not sure about the requirements for the credit. She advised to check the website.	No Answer Given		I didn't ask the third question since it was clear the answer would be the same as the first two and I didn't want to bully the CSR at this point.	No Answer Given	
May 2018	I couldn't ask this because she wouldn't answer my first question.	No	Assistant said she couldn't answer personal tax questions		No	Same as prior questions

**Question 6: I Live in Virginia and have a child who lives in Mexico. Can I claim a dependency exemption for my child on my 2018 tax return?**

**Question 6b: Can I claim the CTC/ACTC for my child on my 2018 tax return?**

**Question 6c: Can I claim a credit for my child as a qualifying relative?**

Date of Call	Start Time	End Time	Question Call Summary	Question Answer	Question Selection	Question Answer Comments
May 2018	14:24	14:40	CSR first mentioned looking to irs.gov for guidance and after referencing his "job aid," he stated that changes to the tax law included elimination of the personal and dependency exemptions.	Yes	CSR read me some information, but missed key issues that should have been raised	The CSR stated incorrectly that the new laws regarding the specific provisions of child tax credit and dependent credit had not yet been determined but would be contained in upcoming IRS publication later this year.
May 2018	15:16	15:20	N/A			
Oct. 2018	09:41	09:45	Assistor told me questions about dependents can only be answered by an assistor during the filing season. Assistor transferred me to an automated message that instructed me to visit irs.gov for answers.	No Answer Given	CSR said question was not in-scope	

Date of Call	Question 6b Summary	Question 6b Answer	Question 6b Comments	Question 6c Summary	Question 6c Answer	Question 6c Comments
May 2018	The CSR indicated that under the new tax law, the CTC was still available. I asked him if it was available to me, and he was unable to tell me at all. He said the specific rules had not yet been issued. I said: "I pay all the support for my 10-year-old son, but he doesn't live with me." CSR told me he was totally reliant on his job aid and read me a couple sentences indicating the credit would be available, but he didn't know any of the requirements to claim the credit and told me to check the IRS website later in the year for upcoming new publications.	No		After about 8 minutes of talking, the CSR was clearly trying to end the call, but I asked him to repeat the last thing he had read about the \$500 dependency exemption because I think that might apply to me. He reread from the job aid but was unable to tell me if the credit was available to me. He said the specific provisions had not yet been released and would be released in and IRS publication later in the year.	No	
Oct. 2018		No Answer Given			No Answer Given	

**Question 7: I understand there is a new 20% deduction for pass-through entities. Can I claim the new 20% pass-through deduction on income from my law practice in 2018?**

Date of Call	Start Time	End Time	Question Call Summary	Question Answer	Question Selection	Question Answer Comments
May 2018	10:14	10:40	The CSR read me a short script about the new deduction and then told me to go to IRS.gov and search for tax reform. She read the script very quickly, so I had a hard time absorbing the information. The script said sole proprietors can deduct qualified business income. Said, what is qualified business income, but she said she could not answer that question because she didn't have any guidance. I asked if the new deduction applied to lawyers and she said to check the website.	Partially	CSR read me some information, but the information did not respond to question	The CSR did not tailor her the response to the facts or ask about key facts that could change the answer. She said she did not know that lawyers are not permitted to take the 20% deduction for self-employed and pass-through entities if their income exceeds a threshold. She was unwilling to address whether any limits applied to the deduction.
May 2018	17:08	17:16	N/A	No Answer Given	Other	I reached the CSR and asked my question. He said he would transfer me to a department that could answer it. I tried to ask what department he was transferring me to, but he didn't answer. He transferred me to a recording that said the question would no longer be answered by an IRS representative and said I could find my answer on IRS.gov.
May 2018	14:23	14:37	The CSR, who was the tax law specialist, read me a paragraph that she found on IRS.gov, but it did not answer my question. She just confirmed that a 20% deduction existed for qualified business income and that it applied to sole proprietors. She could not tell me how to compute qualified business income or whether the deduction applied to lawyers. She spent a few minutes telling me how to navigate IRS.gov. She said they had until Dec. 31 to provide guidance and that I should check the website. She also said I could check the instructions to the 1040ES worksheet or Publication 525.	No	CSR read me some information, but the information did not respond to question	I reached a CSR before reaching the CSR, who was the tax law specialist, and I had to repeat my question twice to the first CSR because she didn't understand at first. Then she said she had to transfer me to the tax law department where I had to repeat the question a third time.
Sept. 2018	14:44	14:52	The CSR answered. I asked my question. She transferred me to an expert in the tax law area. The transfer was picked up quickly. I repeated my question to the second CSR and she said she was not aware of any 20% deduction for pass-through entities. She asked if my business was a corporation. I said no. It is a passthrough entity. Then she put me on hold and transferred me to another CSR who answered. I repeated my question a third time. She asked if I had checked the web. I said I hadn't found the answer on the web. She said the question was out of scope. I asked what I should do. She said to check the web.	Don't Know	CSR said question was not in-scope	

**Question 8: I need to compute my estimated tax payments (due April 15, June 15, September 15 and January 15) I heard that passthrough entities can deduct 20% of their income. Assuming I can claim the new 20% deduction, do I deduct 20% from my income before I calculate my self-employment tax or after?**

Date of Call	Start Time	End Time	Question Call Summary	Question Answer	Question Selection	Question Answer Comments
May 2018	13:29	13:52	After my call was first answered, I was informed my call had to be transferred to an individual in the business section. I was then placed on hold and received an automated message that my call would be answered in 15-30 minutes. My call was then answered at 13:49 a CSR, after an 18-minute hold time at which time I asked my question, after I asked my question, the CSR informed me that my question was a tax law question and that there are certain areas that the we [IRS] can't answer and then directed me to irs.gov and to research the issue through the Q&A. He informed me to input key words to refine my search and if I wasn't able to find the answer I was looking for, then I may need to consult with a tax practitioner. He then continued to explain that they [IRS] used to answer tax law questions but now they are directing taxpayers to the website and other online information such as publications to get answers to tax questions. He apologized for any inconvenience and the call ended. Total time on the call was 23 mins. . 35 sec.	No Answer Given	Although listed as in-scope, the CSR did not answer the question.	Assistor directed me to irs.gov specifically the Q&As on the topic using a key word search and if that didn't answer my question, to consult a tax practitioner.
May 2018	09:00	09:02	No response was given. Automated message directing me to IRS.gov. See comments	No Answer Given		Called business line at 800-829-4933 and followed the prompts to SE tax questions. After 2 minutes of following the prompts, I received an automated message that this type of question is only answered during filing season and for questions after filing season, to go to irs.gov for more information. Afterwards, the call automatically ended. This was the first time I had heard this type of automated message.
Oct. 2018	16:09	16:12	The CSR mentioned that her system was down and was unable to pull up any specific account info but may be able to assist me if my question was general in nature. I posed the scenario in Q8 and was informed that she would have to look up my individual account in order to answer that question and since her system was down, she was not able to assist me and to call back later.	No Answer Given	Although listed as in-scope, the CSR did not answer the question.	
Oct. 2018	16:18	16:58	Called and spoke to a CSR who mentioned she only dealt with payroll issues (F940/941s) and transferred me to Tax Law line. Waited on hold until 16:55 and spoke to another CSR who mentioned that the IRS is not currently answering tax law questions due to budget cuts but referred me to the Interactive Tax Assistant (ITA) online and walked me through the process to get my question answered. She also mentioned IRS Pubs 505 and 334. She apologized she could not offer further assistance. I thanked her and mentioned I would try the ITA.	Partially	Other	

**Question 9: I am married but considering filing using the married filing separate status. What are the key differences?**  
**Question 9b: Both my spouse and I own stocks separately. We might have losses on these stocks. Does filing separately make a difference in the treatment of these losses?**  
**Question 9c: We both receive social security benefits, does filing separately affect the tax treatment of those benefits?**  
**Question 9d: If I file jointly with my spouse, and he doesn't tell me or the IRS about all of his income, could I be liable?**  
**Question 9e: Can I claim the Earned Income Tax Credit (EITC) if I file separately from my spouse?**  
**Question 9f: Can I itemize if I file separately from my spouse and she takes the standard deduction?**  
**Question 9g: If my spouse itemizes, can I take the standard deduction?**

Date of Call	Start Time	End Time	Question Call Summary	Question Answer	Question Selection	Question Answer Comments
May 2018	23:10	23:13		No Answer Given		I was transferred automatically to a recording because my question was about filing status and the recording indicated that these questions would only be answered during filing season and rattled off a list of online self-help options.
May 2018	15:19	15:26	I was transferred again to the same recording that said this question can only be answered during the filing season.	No Answer Given		
Oct. 2018	08:47	08:58	Rep gave me the basic key differences of filing married vs married filing separate. Rep also advised me 1040A, 1040EZ etc. will no longer be available. Schedules will be available and referred me to irs.gov to view form and schedule if needed (draft view). Rep suggested assistance of tax preparer if not able to follow instructions.	Yes		
Sept. 2018	15:47	15:51	N/A - I got a recording	No Answer Given		

Date of Call	Question 9b Summary	Question 9b Answer	Question 9b Comments	Question 9c Summary	Question 9c Answer	Question 9c Comments	Question 9d Summary	Question 9d Answer
Oct. 2018	Provided limits of FS2 vs FS3	Yes	Rep referred me to irs.gov for additional info.	No % provided, refer me to irs.gov and worksheets for computation.	Partially	Rep referred me to irs.gov for additional info.	Rep did not go in details but referred me to irs.gov site	Partially

Date of Call	Question 9d Comments	Question 9e Summary	Question 9e Answer	Question 9e Comments	Question 9f Summary	Question 9f Answer	Question 9f Comments
Oct. 2018	No mention of Innocent Spouse	No EIC if FS3	Yes	Rep referred me to irs.gov for additional info.	For FS3 both need to itemize (if applicable or take the standard deduction.	Yes	Rep referred me to irs.gov for additional info.

**Question 10:** We are a military family. We will be moving to our next duty station soon. In order to deduct our unreimbursed moving expenses, what distance and time tests apply to our move?

**Question 10b:** Where on Form 1040 will we need to take the moving expense deduction?

Date of Call	Start Time	End Time	Question Call Summary	Question Answer	Question Selection	Question Answer Comments
May 2018	14:54	1525	Initiated phone call at 14:54. The first time I called, I was ultimately transferred to a recording where I was directed to online resources before the call ended. The second time I called, I correctly selected prompts for a tax reform question 5 times. I reached an IRS rep. I asked my question, and she transferred me to "Special Service" to assist with a military tax question. The next person picked up at 15:07 hours. She responded that she had not been trained on my topic and told me to go on IRS.gov and search ITA for an answer.	Yes	Other	I responded that it was a tax reform question. She became frustrated with me and asked whether I now had a different question. She explained that the only questions they are answering under the tax reform line is about disaster related issues. At 15:15, she put me on hold and then I was transferred to another CSR. He was very nice, and although he had to put me on hold once while he looked for an answer, he returned and read general information about my topic. The information he read contained the answer to my question. The call ended at 15:25 hours.
Sept. 2018	14:16	14:32		No	CSR read me some information, but the information did not respond to question	A CSR answered call and transferred to a special military unit. Another CSR answered the phone. I asked the first question. She responded, "That's a tax law question and there is nobody here at this time that can answer that question. However, it falls under Tax Reform, so I'd like to read a blurb to you." Two minutes later, she came back and read a blurb about Qualified Moving Expenses, and an exception for active duty service members. However, the blurb still did not answer what time and distance tests apply. When I asked my question again, she responded, "The IRS has no information on this at this time. They will provide information as it becomes available."

Date of Call	Question 10b Summary	Question 10b Answer	Question 10b Comments
May 2018	I asked the second CSR my question, to which he replied that I would report the deduction on the front page, similar to how it's been done in the past, towards the bottom of the Form 1040.	Yes	As opposed to the first IRS rep with whom I spoke, the second CSR was very cordial. He ended the phone call with, "Thank you. Have a great day and thank you for your service."
	I very clearly asked the second part of my question—where on the Form 1040 do I report the moving expense deduction? The CSR immediately became irritated and said, "I told you already that we have no additional information to give you! If you have other questions on technicalities, you'll have to call back on January 2nd to ask them." I politely and calmly explained that this was a different question than the first question and that I just needed to know where to report this moving expense deduction on the Form 1040. "She was very aggravated and responded, "I have nothing to add. You'll have to call back in January. Good-bye!" And she promptly hung up on me. No kidding.	No	

**Question 11: I heard the new tax law got rid of the penalty for not having health insurance. Does that mean that if I don't have health insurance this year (2018), I won't have to pay the penalty?**

Date of Call	Start Time	End Time	Question Call Summary	Question Answer	Question Selection	Question Answer Comments
May 2018	11:57	12:12	The CSR was very polite. She clarified which tax year I was asking about and put me on hold for two mins. She came back and read a statement saying shared responsibility payment eliminated after 2018. I asked for clarification that it is still in place in 2018 and she agreed.	Yes		Assistor read the statement which used the official term (SRP) requiring me to seek clarification, but she was polite and answered accurately.
Oct. 2018	16:28	16:33	If I selected health care law rather than new tax law option, it directs you to automated answer system. The answer was technically correct—you have to pay the ISRP but it assumes the listener is sophisticated and has basic knowledge of the ISRP.	Yes		If you select health care law option in phone tree, it directs you to the automated answer line.
Oct. 2018	16:38	17:07	Once I reached the CSR in individual accounts (after being transferred and waiting 25 minutes), she knew off the top of her head that I would still need to pay the ISRP when I filed my TY 2018 return	Yes		The CSR knew the correct answer off the top of her head.
Oct. 2018	08:03	08:47	The penalty of \$695 applies for TY 2018 but \$0 will be charged after.	Yes		Rep referred to irs.gov for additional information.

## MSP #2 **TRANSPARENCY OF THE OFFICE OF CHIEF COUNSEL: Counsel Is Keeping More of Its Analysis Secret, Just When Taxpayers Need Guidance More than Ever**

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### RESPONSIBLE OFFICIAL

William M. Paul, Acting Chief Counsel

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to a Fair and Just Tax System*

### DEFINITION OF PROBLEM

The IRS Office of Chief Counsel (OCC) provides advice to headquarters employees, which is called Program Manager Technical Advice (PMTA). PMTA must be disclosed to the public pursuant to a settlement with Tax Analysts.<sup>2</sup> Moreover, taxpayers need prompt guidance now more than ever, due to the recently enacted Tax Cuts and Jobs Act (TCJA).<sup>3</sup> Thus, the National Taxpayer Advocate is concerned that the OCC:

- (1) Has been disclosing fewer PMTAs (as shown on Figure 1.2.1);
- (2) Allows its attorneys to avoid disclosure by issuing advice as an email, rather than a memo;
- (3) Has not issued written guidance to its attorneys describing what must be disclosed as PMTA; and
- (4) Has no systems to ensure all PMTAs are timely identified, processed as PMTAs, and disclosed.

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1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 *Tax Analysts v. IRS*, Stipulation of Decision, CA No. 1:96-2285-CKK (July 23, 2007).

3 Pub. L. No. 115-97, 131 Stat. 2054 (Dec. 22, 2017). We are referencing the short title of the bill, H.R. 1, rather than the law.

## ANALYSIS OF PROBLEM

### Background

The *right to be informed* is the first right listed in the Taxpayer Bill of Rights for good reason. If taxpayers do not know the rules and why the IRS has adopted them, they cannot determine if they should exercise their other rights (e.g., the *right to challenge the IRS's position and be heard* or the *right to appeal an IRS decision in an independent forum*).<sup>4</sup>

However, the OCC does not acknowledge that a function of its advice is “to inform taxpayers or practitioners about how it interprets the law,” and says its failure to do so “is not a problem that taxpayers have” and “is not a serious problem encountered by taxpayers.”<sup>5</sup> Consistent with this view, the OCC has sometimes adopted strained legal interpretations to avoid transparency. For example, in addition to PMTA, the IRS is required to disclose certain advice issued to employees in field offices under IRC § 6110 (called Chief Counsel Advice (CCA)).<sup>6</sup> In 2004, the OCC declined to disclose CCA rendered in less than two hours (generally emails).<sup>7</sup> A court found there was no legal basis for this “two-hour rule.”<sup>8</sup>

IRC § 6110 does not apply to the advice the OCC provides to headquarters employees, such as PMTA issued to program managers, but such advice may still have to be disclosed under the Freedom of Information Act (FOIA).<sup>9</sup> In 2006, to investigate the IRS's compliance with the disclosure rules, TAS requested a sample of nonpublic legal memos. The OCC initially refused to provide any memos to TAS, citing pending litigation with Tax Analysts in which it had argued the memos could be withheld under the “deliberative process” privilege. It received considerable criticism for its refusal, and ultimately gave TAS the memos.<sup>10</sup> Tax Analysts subsequently reopened its stalled litigation.<sup>11</sup>

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- 4 For prior discussions of transparency, see, e.g., National Taxpayer Advocate Fiscal Year 2019 Objectives Report to Congress 43-50 (Area of Focus: *The Offshore Voluntary Disclosure (OVD) Programs Still Lack Focus Transparency, Violating the Right to Be Informed*); National Taxpayer Advocate 2011 Annual Report to Congress 380-403 (Most Serious Problem: *The IRS's Failure to Consistently Vet and Disclose its Procedures Harms Taxpayers, Deprives It of Valuable Comments, and Violates the Law*); National Taxpayer Advocate 2010 Annual Report to Congress 71-84 (Most Serious Problem: *IRS Policy Implementation Through Systems Programming Lacks Transparency and Precludes Adequate Review*); National Taxpayer Advocate 2007 Annual Report to Congress 124-139 (Most Serious Problem: *Transparency of the Office of Professional Responsibility*); National Taxpayer Advocate Fiscal Year 2008 Objectives Report to Congress xxi-xxvii (Area of Emphasis: *Update on Transparency of the IRS*); National Taxpayer Advocate 2006 Annual Report to Congress 10-30 (Most Serious Problem: *Transparency of the IRS*).
- 5 Office of Chief Counsel (OCC) response to TAS information request (Sept. 11, 2018) (hereinafter, “OCC response,” reprinted in the Appendix).
- 6 See also Treas. Reg. § 301.6110-1 et seq. IRC § 6110 was expanded by the IRS Restructuring and Reform Act of 1998 (RRA 98), Pub. L. No. 105-206, § 3509, 112 Stat. 685 (1998) to ensure “all taxpayers can be assured of access to the ‘considered view of the Chief Counsel’s national office on significant tax issues.’” Joint Committee on Taxation (JCT), JCS-6-98, General Explanation of Tax Legislation Enacted in 1998, 120 (Nov. 24, 1998) (quoting *Tax Analysts v. IRS*, 117 F.3d 607, 617 (D.C. Cir. 1997)).
- 7 Chief Counsel Notice 2004-012 (Feb. 19, 2004).
- 8 See *Tax Analysts v. IRS*, 495 F.3d 676 (D.C. Cir. 2007), *aff’g* 416 F. Supp. 2d 119 (D.D.C. 2006). See, e.g., Sheryl Stratton, *Court Rejects Two-Hour Rule for Withholding Chief Counsel Advice*, 110 TAX NOTES 1015 (Mar. 6, 2006); Jeremiah Coder, *Something for Everyone in Initial Batch of Two-Hour Rule Advice* 119 TAX NOTES 30 (Apr. 7, 2008).
- 9 5 U.S.C. § 552 et. seq.
- 10 National Taxpayer Advocate Fiscal Year 2007 Objectives Report to Congress xxi-xxvii; Allen Kenney, *Uncooperative Counsel Irks Olson, Confuses Crowd*, 114 TAX NOTES 278 (Jan. 22, 2007) (reporting that former Senator Bob Kerrey recommended that former IRS Commissioner Everson “intercede” on the advocate’s behalf and that Congress “back the advocate up for fear that Olson’s position would lose its ‘teeth.’”).
- 11 See Sheryl Stratton and Lisa M. Nadal, *ABA Tax Section Meeting: Olson Discusses Chief Counsel’s Undisclosed Legal Advice*, 114 TAX NOTES 401 (Jan. 29, 2007).

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The *right to be informed* is the first right listed in the Taxpayer Bill of Rights for good reason. If taxpayers do not know the rules and why the IRS has adopted them, they cannot determine if they should exercise their other rights (e.g., the *right to challenge the IRS's position and be heard* or the *right to appeal an IRS decision in an independent forum*).

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The IRS settled with Tax Analysts in July 2007, agreeing to disclose PMTA dated or prepared after 1994 “on the basis of the standards announced by” the U.S. Court of Appeals for the District of Columbia Circuit in its June 14, 2002 opinion in *Tax Analysts v. IRS*, “as applied by the district court” in its February 7, 2007 opinion.<sup>12</sup>

These cases generally permit the OCC to withhold deliberative and pre-decisional communications, but not OCC’s final legal positions. The Circuit Court explained “[i]t is not necessary that the TAS [advice] reflect the final *programmatic* decisions of the program officers who request them. It is enough that they represent OCC’s final *legal* position....”<sup>13</sup> Only legal conclusions issued to other attorneys within the OCC or to the Commissioner of Internal Revenue (*i.e.*, the Chief Counsel’s supervisor under IRC § 7803(b)(3)(A)) could be withheld.

Advice to other decision makers with words like “we suggest” could be withheld as pre-decisional, whereas those indicating “we conclude” generally could not.<sup>14</sup> Documents with both deliberative and non-deliberative material were released with redactions so that the OCC’s final legal positions and underlying analyses could be disclosed.<sup>15</sup> Notably, neither court decision authorized the OCC to withhold advice simply because it contained the analysis underlying the OCC’s final legal conclusions, even if those conclusions would be released in another form.

### The OCC Is Disclosing Fewer PMTAs

Although one might expect the TCJA to increase the need for PMTA, the number posted on IRS.gov is substantially below its historical average, as shown in Figure 1.2.1.

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12 *Tax Analysts v. IRS*, 294 F.3d 71 (D.C. Cir. 2002), *remanded*, 483 F. Supp. 2d 8 (D.D.C. 2007).

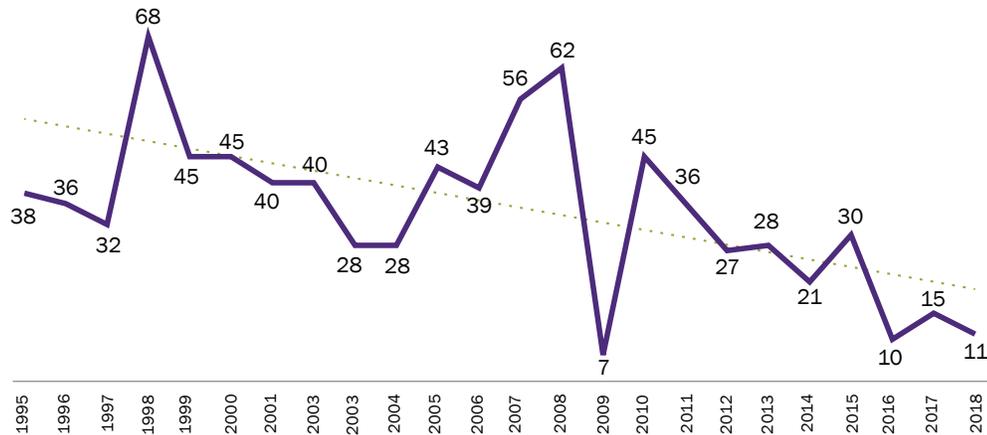
13 *Tax Analysts v. IRS*, 294 F.3d at 81.

14 *Id.*

15 See *Tax Analysts v. IRS*, 294 F.3d at 75 (citing *Tax Analysts v. IRS*, 97 F. Supp. 2d 13, 17-18 (D.C. Cir. 2000) (approving the practice of redacting only the “portions of LMs that reflect the opinions and analysis of the author and did not ultimately form the basis of the final revenue ruling.”).

FIGURE 1.2.1<sup>16</sup>

**Program Manager Technical Advice Posted Items on IRS.gov  
by Calendar Year of Issuance**



Following tax legislation enacted in 1998, the IRS issued 68 PMTAs, but there has been no similar uptick in PMTAs following the TCJA. As of this writing, only 11 PMTAs were issued and released in 2018 (*i.e.*, PMTA 2018-11 to -20), and only one of these related to the TCJA (*i.e.*, PMTA 2018-16, as discussed below).<sup>17</sup> Moreover, the OCC has suggested that it was not even required to release the TCJA-related PMTA.<sup>18</sup>

### The OCC Does Not Disclose Email as PMTAs

PMTAs may be declining because, according to the OCC, it is not required to disclose advice as PMTA unless it is in “*memorandum form*.”<sup>19</sup> In other words, any OCC attorney can avoid disclosing PMTA by copying the memo’s analysis into an email.

The OCC says that it “does not encourage its attorneys to provide legal advice in a manner that circumvents” the disclosure rules.<sup>20</sup> Most attorneys, however, are not going to want to disclose their advice lest the public spot an error. The OCC has historically opposed transparency (as illustrated by the Tax Analysts litigation), and this “form over substance” loophole gives OCC attorneys an easy way to avoid disclosure. Unlike the two-hour rule, which was based on the reasonable assumption that quick

16 TAS analysis of Program Manager Technical Advice (PMTA) posted on IRS.gov. The number of a PMTA reflects the date it was released, rather than the date it was issued. For example, ten PMTAs have numbers beginning with “2017-”, suggesting that they were *released* in 2017, but 15 were *issued* in 2017, as shown on the chart. Nine of the PMTA issued in 2017 have numbers beginning with “2018-”, suggesting they were not released until 2018. The figures in the chart reflect the number issued each year, provided they were later released. For a few PMTAs that did not have an issue date, TAS either omitted them or estimated the year they were issued based when the casefile was closed and the date of memos the OCC posted before and after them. Some PMTAs that were issued in 2018 may not have been released.

17 See IRS, *Legal Advice Issued to Program Managers*, <https://www.irs.gov/privacy-disclosure/legal-advice-issued-to-program-managers> (last updated Nov. 16, 2018).

18 OCC response to TAS information request (Sept. 11, 2018) (reprinted in the Appendix) (Q12: “Does the Tax Analysts settlement require the OCC to release the memo underlying the IRS’s position in section 965 FAQ 14?” A12: “The Office of Chief Counsel published this memorandum at the request of the Division Commissioner, LBI.”).

19 OCC response (A5). Emails have been released as PMTA, which suggests the OCC has changed its position. See, e.g., PMTA 2008-01567 (Sept. 28, 2007); PMTA 2007-01190 (Aug. 14, 2007); PMTA 2007-01186 (June 11, 2007).

20 OCC response (A21).

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Following tax legislation enacted in 1998, the IRS issued 68 Program Manager Technical Advice (PMTAs), but there has been no similar uptick in PMTAs following the Tax Cuts and Job Act.

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responses are not as well thought out as those that take longer, this email loophole has no basis in law. Nor is it a rational policy. The form of the advice has no bearing on how much thought went into the analysis or how it will be used.

*The OCC Has Not Provided Its Attorneys With Written Guidance Describing What Must Be Disclosed as PMTA, and Its Oral Guidance Is Inadequate*

**OCC: TRANSPARENCY IS NOT OUR JOB, WE AVOID WRITING THINGS DOWN, AND THAT'S NOT A PROBLEM**

The OCC does not acknowledge that a function of its advice is “to inform taxpayers or practitioners about how it interprets the law,” and says its failure to do so “is not a problem that taxpayers have” and “is not a serious problem encountered by taxpayers.”<sup>21</sup> Consistent with this view, the OCC has no written training materials to explain what needs to be disclosed as PMTA,<sup>22</sup> and the Chief Counsel Directives Manual (CCDM) provides no specific guidance on how its attorneys should determine whether advice to program managers needs to be disclosed.<sup>23</sup>

**ORAL EXPLANATION AND TRAINING: CLEAR AS MUD?**

OCC attorneys orally explained to TAS that if advice is not adopted by the IRS, then it does not need to be disclosed, and if it is adopted and incorporated into another document, it also does not need to be disclosed.<sup>24</sup> Because positions the IRS adopts are incorporated into public documents, this logic seems to suggest the OCC does not believe *any* PMTA must be disclosed. The OCC attorneys also said advice to some headquarters employees, including the National Taxpayer Advocate, does not need to be disclosed because the employees are not program managers.<sup>25</sup> They did not identify any category of advice that would have to be disclosed as PMTA.

The OCC says it has provided oral training to about 207 attorneys since 2015 (*i.e.*, less than 40 percent of those employed in Washington DC).<sup>26</sup> However, the attorneys were not given written materials, and there is no way to know if their oral training was any more illuminating than these statements.

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21 OCC response (preamble).

22 OCC response (A24) (no written training).

23 OCC response (A22 and A23).

24 TAS meeting with OCC concerning disclosure issues (July 9, 2018).

25 TAS received conflicting information in subsequent meetings with OCC management, but the OCC declined to clarify its position in its formal response, which referred to this meeting. See OCC response (A6). As noted below, the OCC has often provided advice to the National Taxpayer Advocate that was disclosed as PMTA.

26 OCC response (A24). There were an average of about 566 OCC attorneys in Washington, DC during this period. IRS Human Resources Reporting Center, *POD and Building Reports, Counts by State, City and Building* (Nov. 2, 2018) (showing 580, 558, 538, and 587 at the end of FYs 2015-2018, respectively).

### OCC: WE WON'T VERIFY OUR ORAL EXPLANATION, EXCEPT FOR THE HUGE LOOPHOLE

The OCC declined to verify its oral explanation of the PMTA rules in writing. In its formal response (reprinted in the Appendix), the OCC described what must be disclosed as “advice [that] is in *memorandum form* and otherwise meets the standards announced by the circuit court in *Tax Analysts v. IRS*, 294 F.3d 71 (D.C. Cir. 2002), and as applied by the district court in *Tax Analysts v. IRS*, 483 F. Supp. 2d 8 (D.D.C. 2007).” [Emphasis added.]<sup>27</sup> It described what can be withheld as anything that “is properly determined to be privileged under the standard described” by the circuit court’s decision.<sup>28</sup> The only specific item that this written response verified was that the OCC can avoid disclosure by issuing the advice as an email, rather than in “memorandum form.”<sup>29</sup>

### *The OCC Has No Systems to Ensure All PMTA Are Timely Identified, Processed as PMTA, and Disclosed*

The OCC’s written response also revealed that it has no system to determine whether the attorneys who issue PMTAs have provided them to the function responsible for making disclosure determinations (*e.g.*, OCC attorneys assigned to Procedure & Administration (P&A)).<sup>30</sup> Further, the OCC has no guidelines for how quickly PMTA must be sent to this function and posted, saying only that they are generally processed quarterly.<sup>31</sup> As a result, PMTAs may be posted long after the IRS has implemented the advice—and long after it could benefit taxpayers and their representatives (*e.g.*, by avoiding positions that would incur penalties or ensnare them in audits or litigation). Moreover, the lack of any timeliness goals makes it difficult to determine whether a particular PMTA was withheld or whether its disclosure was merely delayed.

### *OCC Seems to Release PMTAs Because the Program Managers Want It To, Rather Than Because of the Settlement*

Although the settlement seems to require the OCC to release some PMTAs that the program manager would probably not want to release, it is not clear that the IRS has released any such documents in recent years. Moreover, the effort that TAS has expended in trying get a few memos released—memos that the National Taxpayer Advocate believes should have been released under the settlement without any advocacy by TAS—confirms what OCC’s oral explanation and written response suggest—that OCC believes almost nothing needs to be disclosed as PMTA under the settlement. In these recent cases, the OCC agreed to release advice only upon request of the program manager (*e.g.*, by asking that the advice be issued as a memo, rather than as an email). The proposition that advice is released only when an agency affirmatively wants to release it makes a mockery of the Tax Analysts settlement and the FOIA.

### EXAMPLE 1: “CALLS” NEEDED TO COMPLY WITH THE TAX CUTS AND JOBS ACT

Following enactment of the TCJA, IRS program managers and other headquarters employees asked the OCC to make “calls” about what the new law required so that they could update hundreds of tax forms, instructions, and publications, and issue “soft guidance,” such as FAQs and Fact Sheets.<sup>32</sup> It would have been helpful for the public—including tax advisors and companies that write tax software—to see OCC’s final legal calls, which were made long before they were incorporated into items that would be

27 OCC response (A5).

28 OCC response (A6, A13, A14).

29 OCC response (A5).

30 OCC response (A27).

31 OCC response (A28).

32 IRS, *Tax Reform Implementation Office (Q&As), Frequently Asked Questions: Implementing the New Tax Law* (Feb. 8, 2018).

released to the public. Even when the OCC's conclusions were incorporated into other guidance, the reasons for the conclusions generally remained undisclosed. TAS urged the IRS and the OCC to post more of the OCC's legal calls as PMTA, but they declined.<sup>33</sup>

The District Court in *Tax Analysts* said that “[e]ven if the document is pre-decisional at the time it is prepared, it can lose that status if it is adopted, formally or informally, as the agency position on an issue or is used by the agency in its dealings with the public.”<sup>34</sup> This raises questions about why the OCC seemed to believe it could withhold the OCC's calls once they were adopted or incorporated into other documents, such as instructions, publications, and FAQs, particularly if the calls explained why the agency adopted the positions and the documents the IRS disclosed did not.

Along the same lines, the Circuit Court in *Tax Analysts* allowed the IRS to redact *only* the portions of Legal Memoranda (LM) (the successor to General Counsel Memoranda) that reflected the opinions and analysis of the author and that did not ultimately form the basis for the final revenue ruling.<sup>35</sup> There was no suggestion in the *Tax Analysts* decisions that the IRS could publish conclusions and withhold the underlying analysis in its entirety.

#### EXAMPLE 2: ADVICE CONCERNING POST-PROCESSING MATH ERROR ADJUSTMENTS

In early 2018, TAS asked the OCC about the legality of plans by the Wage & Investment Division (W&I) to use math error authority (MEA) to disallow tax credits long after the IRS had processed the returns (*i.e.*, post-processing) and issued refunds.<sup>36</sup> The OCC responded by issuing a memo on April 10, 2018, approving the practice. The OCC released the memo during the week of September 10, 2018, only because “[t]here was an agreement between the W&I Commissioner and the National Taxpayer Advocate to release this memorandum,” and not because of the settlement.<sup>37</sup> It is unclear why the OCC thought it needed *IRS permission to release* this memorandum as opposed to being *required to disclose* it under the settlement. Moreover, it is unclear why its release was delayed for five months.

#### EXAMPLE 3: ADVICE CONCERNING THE TRANSITION TAX UNDER IRC § 965<sup>38</sup>

The TCJA imposed a new transition tax under IRC § 965, which had to be reported on 2017 returns but that could be paid over an eight-year period without interest under IRC § 965(h). The IRS issued an FAQ in March 2018 that directed taxpayers to separately designate estimated tax payments to cover

33 In separate internal meetings, employees from the Tax Reform Implementation Office (TRIO) and the OCC discussed a legend that would be affixed to any advice OCC provided to the TRIO so that the advice would not have to be disclosed, but the OCC denied it was using any such legend in its formal response to TAS. See OCC response (A28).

34 *Tax Analysts v. IRS*, 483 F. Supp. 2d at 13.

35 *Tax Analysts v. IRS*, 294 F.3d at 75.

36 National Taxpayer Advocate Fiscal Year 2019 Objectives Report to Congress 114-118 (Area of Focus: *The IRS Has Expanded Its Math Error Authority, Reducing Due Process for Vulnerable Taxpayers, Without Legislation and Without Seeking Public Comments*).

37 See OCC response (responding to question 11, “Does the Tax Analysts settlement require the OCC to release as PMTA the memo about post-processing math error, which was issued to the W&I Commissioner and the NTA on April 10, 2018? If the answer is no, please explain.”); Christine Speidel, *Retroactive Math Error Notices May Be on the Horizon*, PROCEDURALLY TAXING BLOG (Sept. 13, 2018), <http://procedurallytaxing.com/retroactive-math-error-notices-may-be-on-the-horizon/> (noting PMTA 2018-17 was released “earlier this week”).

38 For a more detailed discussion of this issue, see National Taxpayer Advocate, *IRS Administration of the Section 965 Transition Tax Contravenes Congressional Intent and Imposes Unintended Burden on Taxpayers*, NTA BLOG (Aug. 16, 2018), [https://taxpayeradvocate.irs.gov/news/nta-blog-irs-administration-of-the-section-965-transition-tax-contravenes-congressional-intent-and-imposes-unintended-burden-on-taxpayers?category=Tax News](https://taxpayeradvocate.irs.gov/news/nta-blog-irs-administration-of-the-section-965-transition-tax-contravenes-congressional-intent-and-imposes-unintended-burden-on-taxpayers?category=Tax%20News) (hereinafter “NTA 965 Blog”).

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The District Court in *Tax Analysts* said that “[e]ven if the document is pre-decisional at the time it is prepared, it can lose that status if it is adopted, formally or informally, as the agency position on an issue or is used by the agency in its dealings with the public.”

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section 965 liabilities (e.g., by writing “Section 965 payment” on a check).<sup>39</sup> That led some taxpayers who had already paid sufficient estimated tax to make another payment. On Friday, April 13, 2018—a few business days before the filing and payment due date—the IRS issued FAQ 14, which said any excess estimated tax payments could not be refunded or credited to other liabilities unless they exceeded the entire 2017 liability, including transition taxes payable in subsequent years.<sup>40</sup>

Perhaps due to its narrow view of what needs to be disclosed as PMTA and when, the IRS did not timely release the legal analysis underlying FAQ 14. Had its legal analysis been released before the extra transition tax payments were made, it would have been clear that the OCC did not believe the IRS had the legal authority to refund or credit these excess amounts. The IRS’s lack of transparency, thus, encouraged taxpayers to make unnecessary payments.

After the IRS issued FAQ 14, some corporate taxpayers scrambled to file Form 4466, *Corporation Application for Quick Refund of Overpayment of Estimated Tax*, so that they could recover excess estimated tax payments before their returns were due and the tax was assessed—a situation not addressed by the FAQs.<sup>41</sup> Stakeholders, including the American Institute of Certified Public Accountants (AICPA) and the U.S. Chamber of Commerce, argued that FAQ 14 was inconsistent with the purpose of IRC § 965(h).<sup>42</sup> Others suggested the IRS had no authority to deny pre-assessment refund requests on Form 4466.<sup>43</sup> TAS immediately elevated these concerns to the Tax Reform Implementation Office (TRIO). The TRIO explained that the OCC had written a detailed memo,

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39 IRS, *Questions and Answers about Reporting Related to Section 965 on 2017 Tax Returns*, <https://www.irs.gov/newsroom/questions-and-answers-about-reporting-related-to-section-965-on-2017-tax-returns> (FAQ 10, issued on Mar. 13 and amended on Apr. 13, 2018).

40 IRS, *Questions and Answers about Reporting Related to Section 965 on 2017 Tax Returns*, <https://www.irs.gov/newsroom/questions-and-answers-about-reporting-related-to-section-965-on-2017-tax-returns> (FAQs 13 and 14, posted Apr. 13, 2018). Due to computer problems, the due date was extended to April 18. IR-2018-100 (Apr. 17, 2018).

41 KPMG, *IRS updates FAQs, “transition tax” under Code section 965* (Apr. 14, 2018), <https://home.kpmg.com/us/en/home/insights/2018/04/tnf-irs-updates-faqs-transition-tax-section-965.html>.

42 Letter from American Institute of Certified Public Accountants (AICPA) to Acting IRS Commissioner and Large Business and International (LB&I) Commissioner, *Questions and Answers about Reporting Related to Section 965 on 2017 Tax Returns - IRS Update of April 13, 2018* (Apr. 29, 2018), <https://www.aicpa.org/advocacy/cpaadvocate/2018/aicpa-urges-irs-action-on-section-965.html>; Letter from U.S. Chamber of Commerce to Commissioner of Internal Revenue (Oct. 9, 2018), [https://www.uschamber.com/sites/default/files/u.s.\\_chamber.\\_s.\\_corp\\_coalition\\_965\\_letter\\_mnuchinrettigkautter.pdf](https://www.uschamber.com/sites/default/files/u.s._chamber._s._corp_coalition_965_letter_mnuchinrettigkautter.pdf). In some cases, the IRS stretches the plain language of the law to harm taxpayers. See, e.g., *Summa Holdings, Inc. v. Comm’r*, 848 F.3d 779, 785 (6th Cir. 2017) (rejecting the IRS’s argument that it should be permitted “to recharacterize the meaning of statutes—to ignore their form, their words, in favor of [its] perception of their substance” in order to deny tax benefits that Congress may have intended). In others, it does so when a technical reading would be difficult to administer. See, e.g., Alice G. Abreu and Richard K. Greenstein, *Defining Income*, 11 FLA. TAX REV. 295 (2011) (discussing how IRS has avoided technical applications of the law to frequent flier miles, home run balls and other situations where doing so would be controversial or difficult to administer). Thus, stakeholders may have been surprised at the OCC’s inability to reach the result seemingly intended by Congress in connection with IRC § 965(h).

43 Tom Greenaway and Mike Zima, *Unlucky Friday the 13th: No Refunds this Year for Taxpayers Who Defer Paying Mandatory Repatriation Tax?*, PROCEDURALLY TAXING BLOG (Jul. 19, 2018), <http://procedurallytaxing.com/unlucky-friday-the-13th-no-refunds-this-year-for-taxpayers-who-defer-paying-mandatory-repatriation-tax/>.

which said the IRS was legally required to retain the payments—a document (probably an email) that has never been disclosed to TAS or the public.

When TAS requested the transition tax memo, the TRIO referred us to the OCC. The OCC initially said the memo was pre-decisional and would not be released to the public *or to TAS*. The OCC eventually released a new memo (digitally signed on August 1) to TAS on the same day it was released to the public.<sup>44</sup> As with the PMTAs discussed above, it only released this memo because of a “request” by the Large Business and International Division (LB&I), and not because of the settlement or TAS’s request.<sup>45</sup>

However, neither this memo nor any of the IRS’s FAQs addressed whether the IRS could grant applications on Form 4466 for refunds of excess estimated tax payments pursuant to IRC § 6425, before any tax had been assessed for 2017. Accordingly, TAS asked the OCC for legal advice about whether the IRS was authorized to pay these refunds.<sup>46</sup> The OCC said it would only answer this question if the business owner (LB&I) requested it.<sup>47</sup> LB&I said it did not want the OCC to issue the advice, and OCC did not provide the advice to TAS.<sup>48</sup>

Lacking access to the legal support necessary to help taxpayers, TAS issued several Taxpayer Assistance Orders (TAOs) and a proposed Taxpayer Advocate Directive (TAD) to prevent W&I from processing and rejecting Forms 4466 before TAS could elevate these decisions to the IRS Commissioner.<sup>49</sup> The OCC and the IRS’s active efforts to avoid disclosing its legal analysis to TAS and the public undermined taxpayer rights, including the *right to pay no more than the correct amount of tax*. They also undermined TAS’s ability to assist taxpayers as well as to identify the problem and propose administrative or legislative changes to address it, as required by IRC § 7803.<sup>50</sup>

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44 See PMTA 2018-16 (Aug. 2, 2018), [https://www.irs.gov/pub/lanoa/pmta\\_2018\\_16.pdf](https://www.irs.gov/pub/lanoa/pmta_2018_16.pdf).

45 OCC response (A12).

46 See, e.g., IRC § 7803(c)(2)(A) (requiring TAS to assist taxpayers in resolving problems with the IRS, identify areas in which taxpayers have such problems, and to propose legislative and administrative changes to mitigate the problems). Stakeholders raised the same questions. See, e.g., Letter from AICPA to Secretary of the Treasury and Assistant Secretary for Tax Policy, *Application of 2017 Estimated Tax Payments to Section 965(h) Installment Obligations* (Sept. 17, 2018), <https://www.aicpa.org/content/dam/aicpa/advocacy/tax/downloadabledocuments/20180917-aicpa-comments-on-965-overpayments.pdf>.

47 For an example of the types of questions TAS asked OCC to answer, see *NTA 965 Blog*.

48 On August 8, TAS formally asked the OCC for the advice by August 31, 2018. On August 20, 2018, the Commissioner of Large Business and International Division informed TAS that he did not want the OCC to issue the advice.

49 See IRC § 7811 (Taxpayer Assistance Order authority); Internal Revenue Manual (IRM) 1.2.50.4, Delegation Order 13-3 (formerly DO-250, Rev. 1) (Jan. 17, 2001) (Taxpayer Advocate Directive authority). Although OCC has still not issued the formal opinion TAS requested, those at the highest levels of the IRS, the OCC, and Treasury considered the matter and informed TAS that, in their view, the IRS was not authorized to pay the refunds. In that way, the IRS complied with the TAOs.

50 The IRS Commissioner subsequently clarified that the National Taxpayer Advocate has the right to request and receive legal advice analysis from the OCC and to review the legal analysis that the OCC issues to other business units, unless the IRS Commissioner determines that she should not have access to the analysis. IRS response to TAS (Dec. 18, 2018). On November 26, 2018, Congress proposed IRC § 965(h) to fix the problem, but the legislation could have been proposed sooner if the IRS had been more transparent about the reason for the problem. See House Amendment to the Senate Amendment to H.R. 88, Division A, *The Retirement, Savings, and Other Tax Relief Act of 2018* § 501 (Nov. 26, 2018).

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The Office of Chief Counsel does not acknowledge that a function of its advice is “to inform taxpayers or practitioners about how it interprets the law.” This view explains why it has interpreted the settlement narrowly, created a huge loophole for emailed advice, avoided writing down what needs to be disclosed under the settlement, and avoided establishing systems to ensure Program Manager Technical Advice (PMTA) are identified and timely disclosed.

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## CONCLUSION

The taxpayers’ *right to be informed* includes the right to “clear explanations of the laws and IRS procedures.”<sup>51</sup> However, the OCC does not acknowledge that a function of its advice is “to inform taxpayers or practitioners about how it interprets the law.” This view explains why it has interpreted the settlement narrowly, created a huge loophole for emailed advice, avoided writing down what needs to be disclosed under the settlement, and avoided establishing systems to ensure PMTA are identified and timely disclosed. The National Taxpayer Advocate respectfully disagrees with OCC’s cramped interpretation of the disclosure requirements.

## RECOMMENDATIONS

The National Taxpayer Advocate recommends the OCC:

1. Develop clear written guidance that defines when advice constitutes PMTA that must be disclosed.
2. Require disclosure of any advice that is, in substance, PMTA. For example, the OCC’s guidance should not permit attorneys to withhold advice because of its form or mode of transmission (*e.g.*, email), because of the title of the recipient, or because a business unit does not want the advice to be disclosed.
3. Establish a written process to monitor whether advice that should be disclosed as PMTA is being identified and disclosed to the public in a timely manner. For example, consider aiming to disclose PMTAs no later than when the IRS issues guidance (*e.g.*, FAQs, Publications, News Releases, IRMs, etc.) that reveals the agency’s position.
4. Incorporate the new PMTA guidance and monitoring procedures into the Chief Council Directives Manual, distribute it at PMTA training classes, and release it to the public.

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51 IRS, Pub. 1, *Your Rights as a Taxpayer* (2016).

## Appendix: OCC response to TAS information request (Sept. 11, 2018)<sup>52</sup>

### Basic Description of Project:

While the OCC has an interest in protecting documents from disclosure under the deliberative process privilege, taxpayers and practitioners also need timely details about how the OCC interprets the law, such as recent changes made to the Internal Revenue Code by the Tax Cuts and Jobs Act (TCJA) that are not purely deliberative. As an advocate for taxpayers, the National Taxpayer Advocate has been urging the IRS to release to the public more of the guidance it receives from the OCC (*e.g.*, guidance referred to as OCC “calls” that the IRS has immediately adopted and used to create forms, instructions, publications, news releases, fact sheets, and FAQs (called “soft guidance”)).

TAS discussed the parameters under which the National Taxpayer Advocate and TAS can receive legal advice from the OCC with CC:P&A on July 9, and again on July 30, and on August 2, 2018. In addition, TAS discussed at those meetings what constitutes Program Manager Technical Advice (PMTA), who is a Program Manager (PM), and what procedures OCC attorneys follow to ensure adherence to the terms of the settlement with Tax Analysts. Most of the questions below are intended to confirm information discussed at these three meetings, and some require only a Yes/No answer.

### Information Requested:

[**Preamble to OCC response**] Section 7803(b) established in the Department of the Treasury the Chief Counsel for the Internal Revenue to serve as an independent legal advisor to the Commissioner and to his officers and employees. The Chief Counsel reports both to the General Counsel and to the Commissioner with respect to legal advice and interpretation of the tax law not relating solely to tax policy. The Chief Counsel reports solely to the General Counsel with respect to legal advice and interpretation of the tax law relating solely to tax policy. As an independent legal advisor, the Office of Chief Counsel is not subject to the direction of or oversight by the National Taxpayer Advocate. The function of the legal advice provided by the Office of Chief Counsel is not to inform taxpayers or practitioners about how it interprets the law, but to assist the Commissioner and his officers and employees in administering the Internal Revenue Code. The Office of Chief Counsel releases certain legal advice because decisions of the courts have interpreted the Freedom of Information Act to require the release of certain types of legal advice it provides. The Office of Chief Counsel takes seriously its responsibility to comply with the FOIA and the decisions of the courts interpreting that law. The issue of whether the Office of Chief Counsel is releasing advice in compliance with court decisions interpreting the FOIA and the process for performing that function is not a problem that taxpayers have with the Internal Revenue Service and it is not a serious problem encountered by taxpayers. We are nonetheless responding to these questions in the spirit of transparency and cooperation.

[**TAS comment:** IRC § 7803(c)(2)(B)(ii) says the National Taxpayer Advocate’s annual report must “contain recommendations for such administrative and legislative action as may be appropriate to resolve problems encountered by taxpayers,” as well as “such other information as the National Taxpayer Advocate may deem advisable.” The statute does not empower the OCC to determine whether an issue

<sup>52</sup> TAS’s questions are in black, OCC’s answers and comments are in green boxes, and TAS’s comments to OCC’s answers are in [brackets]. TAS has generally removed the portions of this document that discuss the National Taxpayer Advocate’s access to legal advice for the reasons described in footnote 50.

is a problem for taxpayers. The first provision in the Taxpayer Bill of Rights is the *Right to Be Informed*, and the *Right to Be Informed* encompasses the right to understand the IRS's legal reasoning. One cannot accept or challenge an agency's legal position without understanding what it is and the basis for it. Therefore, we believe OCC's policy of keeping legal advice secret from the taxpaying public to the maximum extent possible does, indeed, constitute a serious problem for taxpayers. In addition, we note that the authorizing statute charges the National Taxpayer Advocate with identifying the most serious problems encountered by taxpayers. The statute does not empower the OCC to determine which issues to designate as problems, nor does it limit what other information the National Taxpayer Advocate may include in her report.]

- (5) Would advice the OCC drafted for the National Taxpayer Advocate concerning a program that the National Taxpayer Advocate does not directly administer be released under the Tax Analysts settlement as PMTA, assuming it is not pre-decisional or subject to another privilege?

[A5] Yes, if the advice is in memorandum form and otherwise meets the standards announced by the circuit court in *Tax Analysts v. IRS*, 294 F.3d 71 (D.C. Cir. 2002), and as applied by the district court in *Tax Analysts v. IRS*, 483 F. Supp. 2d 8 (D.D.C. 2007).

[TAS Comment: A5 suggests the OCC does not disclose advice unless it is in “memorandum form.”]

#### Questions Concerning the Public's Access to OCC's Advice

- (6) Can the OCC withhold advice (that would otherwise be characterized as PMTA and posted) on the basis that it is issued to a headquarters employee who is not a PM?

[A6] The Office of Chief Counsel will withhold advice when it is properly determined to be privileged under the standard described by the D.C. Circuit Court of Appeals in *Tax Analysts v. IRS*, 294 F.3d 71 (D.C. Cir. 2002).

- (7) Are all the individuals listed in this chart under the “HQ” heading, including the Operating Division Commissioners and the National Taxpayer Advocate, considered PMs for purposes of the disclosure rules? <http://ccintranet.prod.irsounsel.treas.gov/OrgStrat/Offices/PA/CCA%20Check/FIELD%20VS%20HQ.htm>. If not, please identify those who are not.

[A7] Yes.

- (8) Does the Tax Analysts settlement require the OCC to release advice to PMs concerning options not taken because they are not permissible as a legal matter (e.g., advice that the IRS does not have legal authorization to use math error authority under a specific set of circumstances)?

[A8] The Office of Chief Counsel releases advice in accordance with *Tax Analysts v. IRS*, 294 F.3d 71 (D.C. Cir. 2002), *Tax Analysts v. IRS*, 483 F. Supp. 2d 8 (D.D.C. 2007), and the settlement reached subsequent to those decisions. As noted by the D.C. Circuit Court of Appeals, the distinction between deliberative technical assistance memoranda (TAs) and TAs that represent Counsel's considered legal

conclusions is not amenable to a categorical formula. It can turn on the subject matter of the TA, on its recipient, on its place in the decision-making process, and even on its tone. This question suggests the resolution of this issue is susceptible to a categorical approach, an approach that the D.C. Circuit specifically rejected.

**[TAS Comment:** The OCC attorneys who administer the PMTA program informed TAS that advice concerning options that the IRS did not adopt would always be withheld. Questions 8 and 9 were aimed at identifying OCC’s reasons for withholding such advice.]

- (9) Does the Tax Analysts settlement require the OCC to release advice to PMs concerning options not taken because it concludes they are policy calls (*e.g.*, advice that the IRS is legally authorized to use math error authority under a specific set of circumstances, but the IRS decides not to use this authority)?

**[A9]** Counsel releases advice in accordance with *Tax Analysts v. IRS*, 294 F.3d 71 (D.C. Cir. 2002), *Tax Analysts v. IRS*, 483 F. Supp. 2d 8 (D.D.C. 2007), and the settlement reached subsequent to those decisions. As noted by the D.C. Circuit Court of Appeals, the distinction between deliberative technical assistance memoranda (TAs) and TAs that represent Counsel’s considered legal conclusions is not amenable to a categorical formula. It can turn on the subject matter of the TA, on its recipient, on its place in the decision-making process, and even on its tone. This question suggests the resolution of this issue is susceptible to a categorical approach, an approach that the D.C. Circuit specifically rejected.

- (10) If the answer to either of the prior two questions is no, please reconcile the OCC’s position with the statement by the Circuit Court in *Tax Analysts* (on p. 81) that “[i]t is not necessary that the TAs [advice] reflect the final *programmatic* decisions of the program officers who request them. It is enough that they represent OCC’s final legal position ....”

**[A10]** N/A.

- (11) Does the Tax Analysts settlement require the OCC to release as PMTA the memo about post-processing math error, which was issued to the W&I Commissioner and the National Taxpayer Advocate on April 10, 2018? If the answer is no, please explain.

**[A11]** There was an agreement between the W&I Commissioner and the National Taxpayer Advocate to release this memorandum, and it was released in accordance with that agreement.

- (12) Does the Tax Analysts settlement require the OCC to release the memo underlying the IRS’s position in section 965 FAQ 14? If the answer is no, please explain.

**[A12]** The Office of Chief Counsel published this memorandum at the request of the Division Commissioner, LBI.

- (13) Will the OCC withhold advice as pre-decisional solely because its legal conclusions will be disclosed later by the IRS as soft guidance?
- a. If yes, please reconcile the OCC's position with the rationale of the Circuit Court in *Tax Analysts* (see p. 75), which suggests that memoranda (not just the conclusions) which form the basis for the agency's conclusions should be disclosed (*i.e.*, the court cited *Tax Analysts v. IRS*, 97 F. Supp. 2d 13, 17-18 (D.C. Cir. 2000), which approved the practice of redacting only the portions of memos "that reflect the opinions and analysis of the author and did not ultimately form the basis" for the conclusions adopted by the agency).

[A13] The Office of Chief Counsel will withhold advice when it is properly determined to be privileged under the standard described by the D.C. Circuit Court of Appeals in *Tax Analysts v. IRS*, 294 F.3d 71 (D.C. Cir. 2002).

[TAS Comment: The OCC attorneys who administer the PMTA program informed TAS that advice the IRS adopted and incorporated into any kind of guidance or published product (*e.g.*, soft guidance, a form, or the IRM) would always be withheld. They reasoned that although the IRS's conclusion had to be disclosed, if those conclusions would be incorporated into a product that would be disclosed, then the OCC's underlying legal analysis could be withheld. A13 says that the OCC will withhold advice "when it is properly determined to be privileged" under the *Tax Analysts* decision. The response states the obvious and provides no useful information. The purpose of our question—which the response avoids answering—was to elicit information regarding which factors go into determining how that decision is made, so the public is not effectively told "trust us."]

- (14) If the OCC's advice is pre-decisional when issued, does the *Tax Analysts* settlement require the OCC to disclose it as PMTA later if the IRS ultimately adopts the positions taken in the advice (*e.g.*, the IRS adopts the positions in soft guidance)?
- a. If not, please reconcile OCC's position with the statement of the District Court in the *Tax Analysts* case (on p. 13) that "[E]ven if the document is pre-decisional at the time it is prepared, it can lose that status if it is adopted, formally or informally, as the agency position on an issue or is used by the agency in its dealings with the public." (Quotation omitted.)

[A14] The Office of Chief Counsel will withhold advice when it is properly determined to be privileged under the standard described by the D.C. Circuit Court of Appeals in *Tax Analysts v. IRS*, 294 F.3d 71 (D.C. Cir. 2002).

[TAS Comment: The OCC attorneys who administer the PMTA program informed TAS that once advice was withheld as pre-decisional, it would never be disclosed.]

- (15) Will the OCC withhold advice to a PM in its entirety (rather than disclosing a redacted version) if the advice is "primarily" pre-decisional?
- a. If so, please reconcile the OCC's position with the Circuit Court's approval in *Tax Analysts* of the District Court's decision to allow the IRS to withhold documents covered by the attorney work product privilege, but to require it to disclose redacted documents that were primarily pre-decisional.

[A15] The Office of Chief Counsel will release legal advice under the standard described by the D.C. Circuit Court of Appeals in *Tax Analysts v. IRS*, 294 F.3d 71 (D.C. Cir. 2002), as well as any other relevant court opinions requiring the release of agency working law that is not otherwise privileged.

[TAS Comment: The OCC attorneys who administer the PMTA program told TAS that OCC could withhold in its entirety, any advice that was “primarily” pre-decisional.]

- (16) What legend does the OCC put on tax reform advice issued to the TRIO and why?

[A16] The Office of Chief Counsel does not put a legend on legal advice to TRIO, because legends are not determinative of whether or not advice is privileged.

[TAS Comment: TAS representatives attended meetings with both the IRS and OCC where such a legend was discussed. On July 9, 2018, we were even told the legend had been approved by the Chief Counsel.]

- (17) Who determines whether OCC advice to PMs is pre-decisional or otherwise privileged?

[A17] The Office of Chief Counsel.

[TAS Comment: A17 does not indicate whether the person who determines whether OCC’s advice is privileged is the OCC attorney(s) issuing the advice or the OCC attorneys who administer the PMTA program.]

- (18) Our understanding is that a document released as PMTA is generally considered to be “agency working law” that is not “pre-decisional.” Is that accurate?
- a. If yes, please describe what “agency working law” is. If not, please define PMTA.

[A18] The Office of Chief Counsel releases as PMTA non-privileged legal advice according to the standards announced by *Tax Analysts v. IRS*, 294 F.3d 71 (D.C. Cir. 2002), *Tax Analysts v. IRS*, 483 F. Supp. 2d 8 (D.D.C. 2007), and the settlement reached subsequent to those decisions.

- (19) If advice is PMTA does that mean it must be released?

[A19] The Office of Chief Counsel releases as PMTA non-privileged legal advice according to the standards announced by *Tax Analysts v. IRS*, 294 F.3d 71 (D.C. Cir. 2002), *Tax Analysts v. IRS*, 483 F. Supp. 2d 8 (D.D.C. 2007), the settlement reached subsequent to those decisions, and any other court opinions requiring the release of legal advice.

[TAS Comment: A18 and A19 do not define PMTA or acknowledge that when something constitutes PMTA, then it must be released.]

- (20) How many documents that constitute PMTA have been withheld in full in each of the last 5 years?

[A20] We do not keep this statistic, but we have reviewed the information we have, which covers nearly four years (October 2014 - August 2018). During that time, one PMTA document was withheld in full, and it was withheld as tax convention information under section 6105.

[TAS Comment: Because the OCC response does not define PMTA or indicate whether something classified as PMTA must be released, A20 is impossible to interpret.]

- (21) Is email advice subject to disclosure as PMTA?

[A21] The Office of Chief Counsel releases as PMTA non-privileged legal advice according to the standards announced by *Tax Analysts v. IRS*, 294 F.3d 71 (D.C. Cir. 2002), *Tax Analysts v. IRS*, 483 F. Supp. 2d 8 (D.D.C. 2007), and the settlement reached subsequent to those decisions.

- a. Can legal analysis that must be disclosed as PMTA if it is transmitted by memo be shielded from disclosure by transmitting the same analysis in the body of an email?

[A21a] Legal advice that is sent by email is released under the provisions of section 6110. Contrary to what is implied by this question, the Office of Chief Counsel does not encourage its attorneys to provide legal advice in a manner that circumvents our obligations under the Code and case law to release legal advice. In fact, our recent training sessions have begun by emphasizing that employees should treat compliance with the disclosure of legal advice requirements as seriously as they take compliance with the tax laws, noting that the obligation to release CCA is a part of Title 26.

[TAS Comment: A5 acknowledges the OCC does not disclose advice unless it is in “memorandum form.” Our concern is that OCC attorneys can defeat the PMTA disclosure requirements entirely if, once PMTA has been written, an attorney transmits it by email rather than by memo. A21a says the OCC does not encourage its attorneys to provide legal advice in a manner that circumvents the disclosure requirements of IRC § 6110. A21a is unresponsive to Q21a because IRC § 6110 does not apply to PMTA. The disclosure of PMTA is governed by the FOIA and the settlement with Tax Analysts, rather than Title 26. A21a does not address whether the OCC encourages its attorneys to circumvent the rules that apply to PMTA.]

- (22) Is there a definition of PM or PMTA anywhere in the CCDM?

[A22] No. Technical Assistance Memoranda are described in historical parts of the IRM (Part 39.8).

- (23) Please identify the sections of the CCDM that provide the standards that OCC attorneys are supposed to apply when determining whether to forward memos to the PMTA mailbox for posting to the FOIA library at <https://www.irs.gov/privacy-disclosure/legal-advice-issued-to-program-managers>?

[A23] Legal Advice is covered in Part 33 of the CCDM.

[**TAS Comment:** Although CCDM 33.1.2.2.4 references PMTA, it does not provide any specific guidance about when PMTA should be disclosed. Thus, A22 and A23 confirm that the CCDM contains no specific guidance that OCC attorneys can use to determine whether advice should be disclosed as PMTA.]

- (24) Please provide the dates of any training conducted within the last 5 years addressing the disclosure of PMTA and identify the group of attorneys who were invited.
- a. For each of these training sessions, approximately how many attorneys attended?
  - b. Please provide any written training materials distributed to attendees at each of the training sessions identified in response to this question.

[**A24**] We do not keep this data in one location but have reviewed our recent records and found the following training discussing the disclosure of PMTA (and there may be others):

- Training was held in October 2015 for about 20 ACCI attorneys and managers.
- Training was held in December 2015 for about 15 new national office hires as part of New Attorney Orientation.
- Training for FIP was held in 2015 for approximately 20-30 attorneys and managers.
- Training was held in October 2015 for about 5 new attorneys.
- Training was held in February 2016 for about 5 new attorneys.
- Training for ACCI was held in FY 2017 for about 20 attorneys and managers.
- Training was held in December 2016 for about 15 new national office hires as part of New Attorney Orientation.
- Training was held for P&A in FY 2017 for about 25 attorneys and managers.
- Training was held for Corporate in FY 2017 for about 20 attorneys and managers.
- Training for ACCI was held in August 2017 for about 20 attorneys and managers.
- Training was held in September 2017 for about 7 new attorneys.
- Training was held in November 2017 for about 25 new national office hires as part of New Attorney Orientation.

No written training materials were distributed.

- (25) Is it accurate that CC:P&A is responsible for developing, teaching, and administering the disclosure standards and OCC managers generally are responsible for ensuring compliance with those standards?
- a. If yes, have written standards been provided to all OCC managers? Please provide copies of any standards they are given.

[**A25**] P&A has subject matter responsibility for interpreting the requirements imposed by FOIA and section 6110, and administers the release of legal advice identified as subject to release under the procedures in the CCDM. P&A regularly provides training as outlined above.

- (26) Are all items that are forwarded to the PMTA mailbox posted as PMTA?
- a. If the answer is no, please explain what criteria is used to decide whether to post the advice.

[A26] The Office of Chief Counsel releases as PMTA non-privileged legal advice according to the standards announced by *Tax Analysts v. IRS*, 294 F.3d 71 (D.C. Cir. 2002), *Tax Analysts v. IRS*, 483 F. Supp. 2d 8 (D.D.C. 2007), and the settlement reached subsequent to those decisions.

- (27) How does the OCC know if all PMTA that are required to have been disclosed have been identified and timely posted to the FOIA library at <https://www.irs.gov/privacy-disclosure/legal-advice-issued-to-program-managers>?

[A27] P&A emails the redacted PMTAs to F&M for posting on the website. Once the F&M employee has posted the documents to the Electronic Reading Room, she lets P&A know. We are not aware of any failure in the posting of documents identified and processed as PMTA.

[TAS Comment: A27 does not address how the OCC knows whether its attorneys are timely and properly forwarding PMTA to P&A or whether P&A attorneys are timely and properly forwarding them to F&M to be posted.]

- (28) How quickly after PMTA is issued do OCC guidelines require it be made public?
- a. In practice, how quickly after PMTA is issued is it made public?

[A28a] PMTA is generally processed quarterly and posted in groups. If an office had a need to have publication of a particular document expedited, the offices would accommodate that request.

[TAS Comment: A28a suggests the OCC has no guidelines regarding how quickly a PMTA must be made public.]

MSP  
#3**NAVIGATING THE IRS: Taxpayers Have Difficulty Navigating the IRS, Reaching the Right Personnel to Resolve Their Tax Issues, and Holding IRS Employees Accountable****RESPONSIBLE OFFICIALS**

Ken Corbin, Commissioner, Wage and Investment Division  
 Mary Beth Murphy, Commissioner, Small Business/Self-Employed Division  
 Douglas O'Donnell, Commissioner, Large Business and International Division  
 David Horton, Acting Commissioner, Tax Exempt and Government Entities Division  
 Donna Hansberry, Chief, Office of Appeals  
 John D. Fort, Chief, Criminal Investigation

**TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*

**DEFINITION OF PROBLEM**

A key factor in the success of any public-facing enterprise is the ability to provide an effective and efficient mechanism for addressing customer inquiries.<sup>2</sup> The IRS administers the government's constitutional authority to assess and collect federal taxes. Although taxpayers are required by law to pay their duly owed taxes, they are also the agency's "customers." Unlike the private sector, the agency's failure to adequately engage these customers cannot cause taxpayers to take their business elsewhere, but it will jeopardize the voluntary compliance on which the U.S. tax system depends.<sup>3</sup> As a result, the challenges faced by taxpayers when attempting to contact IRS personnel knowledgeable about their accounts pose substantial risks to all parties.<sup>4</sup>

- 
- 1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code. See Internal Revenue Code (IRC) § 7803(a)(3).
  - 2 Bobby Cameron and Tim Harmon, Forrester Research, *Elevate Omnichannel Customer Experience With Continuous Business Services* 3 (May 4, 2015); Deanna Laufer, Forrester Research, *How to Build the Right CX Strategy* 4 (Jan. 10, 2017).
  - 3 Nina E. Olson, *Telephone Service in an Omnichannel Environment (Part 2 of 2)*, NTA BLOG, (Feb. 8, 2018), [https://taxpayeradvocate.irs.gov/news/nta-blog-telephone-service-in-an-omnichannel-environment-part-2?category=Tax News](https://taxpayeradvocate.irs.gov/news/nta-blog-telephone-service-in-an-omnichannel-environment-part-2?category=Tax%20News); National Taxpayer Advocate 2016 Annual Report to Congress vol. 3, 44-45.
  - 4 Additionally, as discussed in Most Serious Problem: *Tax Law Questions: The IRS's Failure to Answer the Right Tax Law Questions at the Right Time Harms Taxpayers, Erodes Taxpayer Rights, and Undermines Confidence in the IRS*, *supra*, taxpayers wishing to accurately prepare their tax returns have been receiving decreases levels of individual support from the IRS.

Although these difficulties have been discussed by the National Taxpayer Advocate in earlier reports, they continue to beset taxpayers.<sup>5</sup> For example, the IRS was recently ranked last in quality communication in a survey of 15 federal agencies undertaken by Forrester Research.<sup>6</sup> All too often, taxpayers wishing to obtain information must embark on a voyage that requires them to interpret obscure IRS acronyms and function names, navigate a complex and multifaceted phone tree, and identify unnamed and often-changing responsible IRS officials. This journey is by no means a seamless one, and in many cases, taxpayers are left floundering on the rocks of confusion, frustration, and misinformation.

As a result, the National Taxpayer Advocate remains concerned that:

- Taxpayers often have difficulty locating IRS personnel who can provide accurate and responsive information regarding their cases;
- Even if taxpayers are tenacious enough to reach a helpful IRS employee, they may not be able to work with that person again; and
- Taxpayers have trouble holding IRS personnel accountable, as managers can be hard to find and no mechanism for tracking complaints generally exists.

## ANALYSIS OF PROBLEM

### Taxpayers Often Have Difficulty Locating IRS Personnel Who Can Provide Accurate and Responsive Information Regarding Their Cases

For many taxpayers, navigating their way through the IRS to obtain the answers and the support they desire can be a challenging and frustrating undertaking. In part, this situation is attributable to the reality that taxpayers prefer different methodologies of assistance for different issues and tasks. These preferences are illustrated in Figure 1.3.1:

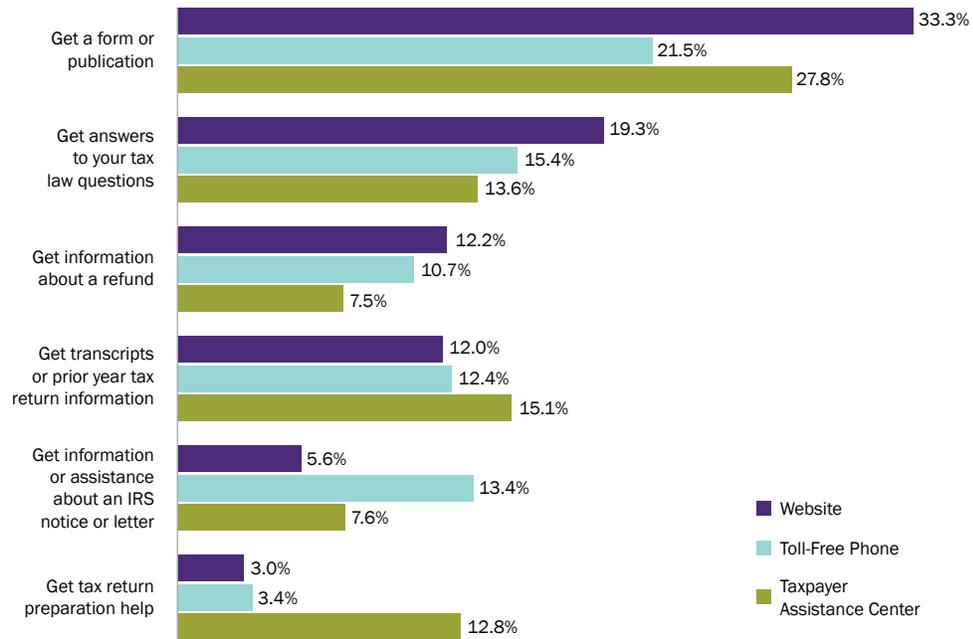
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5 National Taxpayer Advocate 2017 Annual Report to Congress 22-35; National Taxpayer Advocate 2017 Annual Report to Congress vol. 2, 229-244; National Taxpayer Advocate 2014 Annual Report to Congress 123-133; National Taxpayer Advocate 2008 Annual Report to Congress 114-125.

6 Faith Adams and Rick Parrish, *Clear Communication is Vital for Government CX Success*, Forrester Research 4 (Feb. 14, 2018).

FIGURE 1.3.17

Top Needs for Those Using Only One Service by Delivery Channel



Nevertheless, the IRS does its best to push everyone into a “one size fits all” virtual environment. This effort, typically justified by the desire to preserve resources, has resulted in the ongoing closure of Taxpayer Assistance Centers (TACs) and substantial limitations placed on when taxpayers can receive answers to tax law questions.<sup>8</sup> Further, the IRS has attempted to design letters that artificially suppress the number of follow-up calls, even when the outcome is bad for the IRS and worse for taxpayers.<sup>9</sup>

This effort is nothing new, as the IRS has long resisted publishing the names of key offices or otherwise facilitating communication. For example, the IRS has historically refused to make any telephone directories for practitioners or similar directories available to the general public.<sup>10</sup> Moreover, some practice units, including Individual Taxpayer Identification Number (ITIN) processing and the

7 National Taxpayer Advocate 2017 Annual Report to Congress 27. This information, which was compiled by TAS Research, highlights the most used services for each delivery channel. We focus on the top three services for each channel, but the graph includes more than three services since not every channel had high demand for the same preferred services. The percentages shown represent the portion of taxpayers who used that particular delivery channel and only needed help with one IRS service. National Taxpayer Advocate 2017 Annual Report to Congress vol. 2, 82.

8 See Most Serious Problem: *Tax Law Questions: The IRS’s Failure to Answer the Right Tax Law Questions at the Right Time Harms Taxpayers, Erodes Taxpayer Rights, and Undermines Confidence in the IRS*, *supra*; National Taxpayer Advocate 2017 Annual Report to Congress 117; National Taxpayer Advocate 2017 Annual Report to Congress 34.

9 IRS, Automated Collection System (ACS) Optimization/Research, Applied Analytics, and Statistics (RAAS), ACS LT16 Notice Test Pilot Report, 3 (Sept. 27, 2017); National Taxpayer Advocate Fiscal Year (FY) 2019 Objectives Report to Congress 42.

10 National Taxpayer Advocate Fiscal Year (FY) 2016 Objectives Report to Congress vol. 2, 45. The Integrity and Verification Operation (IVO) seeks to identify potentially false returns, usually through income documents reported by third parties. National Taxpayer Advocate 2017 Annual Report to Congress 221.

Integrity and Verification Operation (IVO), lack taxpayer-facing phone numbers altogether.<sup>11</sup> The IRS continues to limit the ability of taxpayers to contact IRS personnel directly, even though this transparency and accessibility would be helpful to taxpayers, and in spite of prior recommendations by the National Taxpayer Advocate.<sup>12</sup>

In the IRS Restructuring and Reform Act of 1998 (RRA 98), Congress required the IRS to make itself accessible to taxpayers, specifically by placing the addresses and telephone numbers for local offices in local phone directories across the country.<sup>13</sup> Although the IRS technically complies with these requirements, live telephone contact with a local office is impossible as a practical matter. Rather than reaching a person, taxpayers in search of local assistance from a TAC receive a recorded message accompanied by a menu that transfers them to the national IRS telephone line where they can speak with telephone assistors.<sup>14</sup> Only if the assistors cannot resolve the issues are taxpayers able to schedule in-person appointments with IRS local offices. This attempt to satisfy the congressional mandate with general numbers, which can be difficult and frustrating to navigate when seeking to obtain direct account information or negotiate account-related agreements, is in keeping neither with the spirit of RRA 98, nor the prior recommendations of the National Taxpayer Advocate.<sup>15</sup>

The IRS should seek to exceed minimum Congressional requirements and make contact information of local offices and particular practice units available online. The general public should have readily available access to an easily searchable, accessible IRS directory that incorporates metadata and common-speech terminology. If the IRS would then supplement this enhanced online access by having local- and unit-specific personnel answer phone calls, taxpayers could deal directly with issues and IRS personnel would find it easier to think of taxpayers as more than work objects in need of processing.

No such progress has yet been achieved, however. In the National Taxpayer Advocate's 2014 Annual Report to Congress, TAS diagrammed the journey of a hypothetical taxpayer calling to ask questions about filing a request for an offer in compromise.<sup>16</sup> In that example, a taxpayer navigated a maze of menus and options, and ended up waiting on hold until they were cut off after approximately six minutes on the phone. In another simulated taxpayer phone call placed at 3:00 p.m. Eastern time on July 18, 2018, TAS sought to reproduce the same journey in an effort to evaluate how IRS telephone accessibility has evolved over the last four years. This time, the call was not cut off; instead, the taxpayer waited on hold for approximately one hour before giving up and terminating the call.<sup>17</sup> This telephonic odyssey is shown below:

11 National Taxpayer Advocate 2017 Annual Report to Congress 225-226. Only after taxpayers are issued Individual Taxpayer Identification Number (ITIN) notices are they provided with a phone number through which to pursue inquiries. IRS response to TAS fact check request (Oct. 25, 2018).

12 National Taxpayer Advocate 2014 Annual Report to Congress 123-133.

13 Section 3709 of the IRS Restructuring and Reform Act of 1998 (RRA 98), 105 Pub. L. No. 206, 112 Stat. 779 provides: "The Secretary of the Treasury or the Secretary's delegate shall, as soon as practicable, provide that the local telephone numbers and addresses of Internal Revenue Service offices located in any particular area be listed in a telephone book for that area."

14 National Taxpayer Advocate Fiscal Year (FY) 2019 Objectives Report to Congress vol. 2, 24.

15 RRA 98 § 3705(d), 105 Pub. L. No. 206, 112 Stat. 777; RRA 98 § 3709, 105 Pub. L. No. 206, 112 Stat. 779. See, e.g., National Taxpayer Advocate 2014 Annual Report to Congress 123-133.

16 National Taxpayer Advocate 2014 Annual Report to Congress 128-129.

17 If taxpayers call on cell phone plans with limited minutes, this extended hold time would cause not only substantial irritation, but also significant economic hardship for those already having difficulty paying their taxes.

FIGURE 1.3.2, Part 1 of 4

## AN IRS TELEPHONE JOURNEY

- WHO** TAS, calling as a taxpayer with questions about filing a request for an offer in compromise
- WHAT** Length of time to reach a customer service representative and be transferred to the centralized offer in compromise unit for help
- WHEN** 07/18/18 at 3 p.m. ET

TAS

Taxpayer dials 1-800-829-1040.

IRS

Welcome to the Internal Revenue Service. You can also visit us at [www.IRS.gov](http://www.IRS.gov).

- 1 To continue in English, press 1.
- 2 Para continuar en Español, oprima 2.

TAS

Taxpayer presses 1.

IRS

We currently are experiencing high call volumes. IRS.gov allows you to check your refund, get a tax form, or find answers to tax law questions. You can also access your account online to view the amount you owe, make a payment, view your payment history, or get a transcript of your tax records. In addition, you can obtain your prior year AGI. If you are filing your return electronically, go to [IRS.gov/account](http://IRS.gov/account) for more details. If you choose to wait, your call will be processed in the order it was received.

- 1 For questions about your refund, or to check the status of your Form 1040X, Amended Tax Return, press 1.
- 2 For answers about your personal income taxes, the tax reform law, or calculating your income tax withholding, or to order a tax form or publication or a tax transcript, press 2.
- 3 For answers about your business taxes, press 3.
- 4 To hear general information about the health care law, including how it may affect individuals, families, and employers, press 4.
- 5 For questions about your personal or business taxes as it relates to healthcare, press 5.
- 9 To repeat this menu, press 9.

1 of 4

FIGURE 1.3.2, Part 2 of 4

## AN IRS TELEPHONE JOURNEY

TAS

Taxpayer presses 2.

IRS

- 7 If you are filing your return electronically and need to order a transcript to obtain your prior year AGI, press 7.
- 1 For questions about a form you have already submitted, or a payment, or to order a tax transcript, press 1.
- 2 For questions about the tax reform law, calculating your income tax withholding, or tax rules or help filing a form, or if you need to order a tax form or publication, press 2.
- 9 To repeat this menu, press 9.
- 6 To return to the previous menu, press 6.

At this point, the taxpayer may be confused as none of the prompts address his issue. He has questions about filing a request for an offer in compromise, but none of these prompts address his need.

TAS

Taxpayer presses 1.

IRS

- 1 For questions about your refund, or to check the status of your Form 1040X, Amended Tax Return, press 1.
- 2 If you need an account or tax return transcript, press 2.
- 3 For all other questions about your tax history or payment, press 3.
- 9 To repeat this menu, press 9.
- 6 To return to the previous menu, press 6.

The taxpayer is further confused by prompt one because the earlier announcement already asked the taxpayer if he had questions about his refund and amended tax return, and he did not select that option.

TAS

Taxpayer presses 3.

IRS

- 1 To find out how to correct a form you already filed, press 1.
- 2 For all other questions about your tax history or payment, press 2.
- 9 To repeat this menu, press 9.
- 6 To return to the previous menu, press 6.

2 of 4

FIGURE 1.3.2, Part 3 of 4

## AN IRS TELEPHONE JOURNEY

TAS  
Taxpayer presses 2.

IRS  
Please wait. To access your account information, please enter the Social Security number or employer identification number for which you are calling.

TAS  
Taxpayer enters Social Security number.

IRS  

- 1 If you enter a Social Security number, press 1.
- 2 If you enter an employer identification number, press 2 now.

TAS  
Taxpayer presses 1.

IRS  
 The Social Security number you entered was XXX-XX-XXXX.  

- 1 If this is correct, press 1 now.
- 2 If this is not correct, press 2 now.

TAS  
Taxpayer presses 1.

IRS  
 The Social Security number you entered was XXX-XX-XXXX.  

- 1 If this is correct, press 1 now.
- 2 If this is not correct, press 2 now.

TAS  
Taxpayer presses 1 to confirm again.

IRS  
 Please listen to the following seven topics. Press the number given when you hear your topic.
 

- 1 If you have your notice, letter, or bill, and want to set up a payment plan, press 1.
- 2 If you want to know the amount needed to pay your bill in full, press 2.
- 3 To request a transcript of your tax return or a transcript of your account, press 3.
- 4 To verify we received a payment you made, press 4.
- 5 For a detailed review of your account information, press 5.
- 6 If your question is about your personal identification number, or PIN, that was established to use our automated system, or you have a question about the account you established to access your account information on the internet, press 6.
- 7 If you received a notice, letter, or bill, and want to know if the innocent spouse rule applies to you, press 7.
- 9 To hear the topics again, press 9.

 If you have not heard your topic, please hold.

3 of 4

FIGURE 1.3.2, Part 4 of 4

## AN IRS TELEPHONE JOURNEY

Even though the taxpayer has misplaced his notice, he just wants to speak with someone so he presses a number.

TAS

Taxpayer presses 1.

IRS

Your call may be monitored or recorded to quality purposes. Please hold while we transfer your call. Please wait. *[hold music]*

After the taxpayer presses 1 to set up a payment plan, he waits on hold for an assistor for an hour. For a taxpayer using a phone with pay-as-you-go minutes, this would be an expensive call indeed, especially for someone who is already having problems paying his or her taxes.

During the hold, recorded messages repeatedly and with increasing urgency encourage the taxpayer to hang up and go online to set up a payment plan. One example states:

IRS

*Calling to arrange payment? Did you know the IRS charges a user fee to set up a monthly payment agreement? You can save money on the setup fee by setting it up online yourself. Monthly payment agreement fees can be as much as \$225 if established over the phone while speaking to one of our representatives, or as low as \$31 if you go online and set up a direct debit installment agreement from your bank account. Please visit [www.IRS.gov/opa](http://www.IRS.gov/opa) for more information.*

After being on the phone for over an hour, the taxpayer, who had a strong desire to speak directly with an IRS employee, hangs up, perhaps to call again, perhaps to go online, or perhaps to abandon the payment plan process altogether.

4 of 4

Even in the virtual realm, into which the IRS has been attempting to push taxpayers, substantial progress remains to be made. Another recent study by Forrester Research shows that most taxpayers found their digital experience with the IRS to be unsatisfactory in some important respects.<sup>18</sup> *These results were found to exist across all generations: Millennials, Generation X, and Baby Boomers.* Figure 1.3.3 summarizes the results of this survey:

**FIGURE 1.3.3, Poorly Rated Features of the IRS Website<sup>19</sup>**

The IRS website is...	Millennials	Generation X	Baby Boomers+
An ideal government website	13%	14%	11%
Easily searchable	12%	17%	11%
Well organized	10%	15%	10%
User-friendly	10%	16%	12%

The IRS must seek to improve the quality of communications with taxpayers. This attentiveness is crucial because communication is one of the top five drivers of customer experience. Clear and effective communication makes taxpayers more likely to trust the agency, do what is asked of them, skip expensive customer service channels, view the agency more positively, and forgive the agency when it makes a mistake.<sup>20</sup> Given that the IRS is currently the lowest-ranked federal agency in this category, it is missing a significant opportunity to enhance customer satisfaction and improve tax compliance.<sup>21</sup>

One way of addressing sometimes differing taxpayer communication preferences, remedying occasionally frustrating IRS computer interactions, and helping taxpayers better navigate the IRS would be to establish a 311 type system. Generally speaking, such systems promptly connect callers to operators who research their questions to provide quick answers, or transfer callers to an appropriate office that can assist them. This 311 system can fit within a more comprehensive omnichannel environment that utilizes customer experience mapping and customer journey analytics now employed in private industry.<sup>22</sup> Such a channel would facilitate increased efficiencies, diminished wait times, and improved interactions between taxpayers and appropriate IRS personnel. This approach, which has previously been recommended by the National Taxpayer Advocate, has been effectively adopted by several state and local governments, including large cities such as New York, Chicago, Minneapolis, and Jacksonville.<sup>23</sup> An omnichannel or similar type of mechanism should be embraced by the IRS as a centerpiece of its effort to improve communication and overall customer experience.

18 Consumer Technographics, *Digital Experience and Engagement with Government Agencies*, Forrester Research 7 (June 2018).

19 *Id.*

20 Faith Adams and Rick Parrish, *Clear Communication is Vital for Government CX Success*, Forrester Research 4-5 (Feb. 14, 2018).

21 *Id.*

22 National Taxpayer Advocate 2017 Annual Report to Congress 22-35; National Taxpayer Advocate Fiscal Year (FY) 2019 Objectives Report to Congress (Area of Focus: *Omnichannel*); Maxie Schmidt-Subramanian and Andrew Hogan, Forrester Research, *How to Measure Digital Customer Experience*, 3 (Jun 21, 2016).

23 Tod Newcombe, *Is the Price of 311 Systems Worth Knowing?* GOVERNING THE STATES AND LOCALITIES (Mar. 2014), <http://www.governing.com/topics/urban/gov-311-systems-cost.html> (last visited Nov. 2, 2018).

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## The IRS must seek to improve the quality of communications with taxpayers.

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### Even If Taxpayers Are Tenacious Enough to Reach a Helpful IRS Employee, They May Not Be Able to Work With That Person Again

Some of the obstacles to quality communication within the IRS are attributable to a diffusion of responsibility and a lack of continuity with respect to various categories of cases. Several IRS functions do not assign specific employees throughout the lifetime of a case. These functions include Correspondence Examination, Return Integrity Compliance Services (RICS), Automated Collection System (ACS), and math error.<sup>24</sup> Instead, taxpayers simply are assigned to the next available examiner when they call in. This lack of identification with a particular case substantially limits case familiarity and personal accountability on the part of IRS personnel working in these programs. Moreover, impacted taxpayers typically are forced to go through the arduous process of navigating the IRS to reach a responsive employee, only to find that they need to start all over again the next time they have a question or require a given action regarding their case.

Approximately 20 years ago, as part of RRA 98, Congress sought to address and remedy this specific problem. Among other things, RRA 98 required the IRS to develop a procedure “to the extent practicable and if advantageous to the taxpayer” to assign one IRS employee to handle a taxpayer’s matter throughout the life of the case.<sup>25</sup> Some IRS functions provide one employee for each case, such as Field Collection, while other IRS units, such as Correspondence Examination and others discussed above, circumvent the spirit, if not the letter, of this directive.<sup>26</sup> The IRS justifies this latter policy and supports the use of group phone numbers by asserting that, in these cases, assigning a single employee is not practicable.<sup>27</sup> The IRS also defends its “first available employee” approach as beneficial to taxpayers because it decreases wait times.<sup>28</sup> Nevertheless, the same problems facing taxpayers in 1998 continue to burden taxpayers today. These issues persist despite concerns registered by the National Taxpayer Advocate, the Treasury Inspector General for Tax Administration (TIGTA), and the Government Accountability Office (GAO) regarding the difficulties experienced by taxpayers in contacting the appropriate IRS personnel to answer their questions and resolve their cases.<sup>29</sup>

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24 National Taxpayer Advocate 2014 Annual Report to Congress 134-144.

25 RRA 98, Pub. L. No. 105-206 § 3705(b), 112 Stat. 685, 777 (1998).

26 National Taxpayer Advocate 2014 Annual Report to Congress 134.

27 National Taxpayer Advocate Fiscal Year (FY) 2016 Objectives Report to Congress vol. 2, 48-50.

28 *Id.*

29 Government Accountability Office (GAO), Report to the Committee on Finance, U.S. Senate, IRS Correspondence Audits: Better Management Could Improve Tax Compliance and Reduce Taxpayer Burden 18-20 (June 2014); Treasury Inspector General for Tax Administration (TIGTA) Ref. No. 2012-30-093, Improved Toll-Free Telephone Services Should Make It Easier for Taxpayers to Obtain Assistance During a Correspondence Audit 7 (Aug. 17, 2012); National Taxpayer Advocate 2014 Annual Report to Congress 134; National Taxpayer Advocate 2012 Annual Report to Congress vol. 2, 78.

The following example illustrates some of these commonly occurring problems:<sup>30</sup>

Assume that a married couple filing a joint return became the subject of a correspondence examination, during which a \$10,000 casualty loss claim was questioned. Taxpayers responded to the inquiry and mailed in additional evidence to support the claimed loss. They were therefore dismayed to receive an initial examination report that disallowed the casualty loss and that gave no indication that the additional evidence was ever considered.

Taxpayers attempted to speak directly to someone working the examination in the service center to which the case was assigned. However, they were provided with no phone number to contact the examiner directly and were not even able to leave a voicemail message. The best that Taxpayers could manage was to leave a general message with the service center asking that someone return their call. Taxpayers received the requested callback, but they were out at the time and, because they did not know to authorize that a message be left, they had no knowledge that the call was ever returned.

At this point, they engaged the services of a tax practitioner, who began the contact process via mail and telephone all over again to resubmit the evidence and find out what occurred. After several mailings and exchanged messages, Compliance issued a 30-day letter (examination report) denying the loss.

Eventually, the adjustment was protested to the IRS Office of Appeals and a settlement mutually acceptable to the IRS and the Taxpayers was negotiated. Tax Practitioner, however, walked away feeling that the same result could have been arrived at in the early stages of the examination if Taxpayers simply had been able to contact an assigned examiner accountable for analyzing the evidence. Instead, Taxpayers ended up incurring unnecessary representational expenses and suffering frustration and disillusionment because of the barriers they faced in attempting to *challenge the IRS's position and be heard*.<sup>31</sup>

As a means of decreasing these types of problems and enhancing continuity, the IRS should assign a single point of contact throughout the lifetime of a taxpayer's case or at least allow taxpayers the ability to communicate with such a person on a repeat basis.<sup>32</sup> While this single point of contact is impracticable and generally unnecessary for isolated account issues or tax law questions, it is important and valuable for both taxpayers and the IRS in areas typically involving ongoing dialogue, such as compliance cases or offers in compromise.<sup>33</sup> This step, which has previously been recommended by the National Taxpayer Advocate, would itself make navigating the IRS a much easier process and lessen the

30 This example is developed based on testimony provided by practitioners and related in the National Taxpayer Advocate 2014 Annual Report to Congress 138-139. Although the testimony was furnished as far back as 2012, the problems described continue today.

31 IRC § 7803(a)(3)(d).

32 Improving taxpayer service in this area should present only minimal resource issues. To begin with, a single point of contact would only potentially be assigned once taxpayers affirmatively contact the IRS. Further, such an option could be presented in a way that taxpayers could exercise choice regarding whether to work with the next available examiner or with a single point of contact. Likewise, the IRS could manage possible staffing issues arising from the latter alternative by establishing a "buddy system" to provide coverage during extended personnel absences. Short-term unavailability could be addressed through the implementation of a callback system that allowed for appointment scheduling and the use of technology ranging from telephone calls to virtual conferencing.

33 Substantial progress remains to be made in addressing isolated account issues and related service requests. For example, the National Taxpayer Advocate has recently heard from a number of practitioners expressing concerns and frustrations regarding tax preparer authentication and the acquisition of client transcripts.

frequency with which it was necessary.<sup>34</sup> It would have the additional benefit of increasing the quality of interactions between taxpayers and IRS personnel.

### **Taxpayers Have Trouble Holding IRS Personnel Accountable, As Managers Can Be Hard to Find and No Mechanism for Tracking Complaints Generally Exists**

Once taxpayers are successful in having their calls routed to the appropriate place, they all too often experience problems having those calls returned and receiving responsive information.<sup>35</sup> Further, managers of unresponsive employees can sometimes be equally difficult to locate and contact. Currently, there is no universal complaint mechanism within the IRS that allows taxpayers to address these issues and have the results monitored.<sup>36</sup>

The IRS receives customer complaints through a variety of channels, including the IRS Commissioner's office, Treasury, Congress, and the Office of Presidential Correspondence.<sup>37</sup> Complaints are routed to the responsible office, where a manager completes a report that is logged in the e-Trak system.<sup>38</sup> That system, however, is neither searchable nor designed for easy analysis of systemic customer service or personnel issues.<sup>39</sup>

A number of practice units within the Wage & Investment (W&I) and the Small Business/Self-Employed (SB/SE) Operating Divisions also allow taxpayers to seek direct contact with a manager to discuss questions or raise complaints and such inquiries are sometimes monitored to help ensure that they are answered by managers within 24 hours.<sup>40</sup> This access to managers by taxpayers is a step in the right direction. However, these complaints, the reasons they are made, and the quality of responses they generate are not tracked in such a way that they can be systematically analyzed to facilitate accountability and improved performance. Further, this lack of a tracking mechanism may cause taxpayers to be reluctant to lodge complaints with managers out of fear of retaliation.

In order to facilitate accountability, the IRS should create a comprehensive system through which taxpayers can ask to speak with managers and that tracks whether the manager contacts the taxpayer, how quickly this contact is made, what the issue is, and how the issue is addressed. This monitoring can be facilitated by a robust 311 system that not only helps taxpayers navigate, but that can be used as a tool to analyze the content of inquiries and track the resolution of complaints.<sup>41</sup> Effective complaint monitoring also presupposes meaningful quality measures that provide an accurate picture of taxpayers' overall experiences and the resolutions they obtain.<sup>42</sup> The IRS must commit to improving the overall customer experience by putting these mechanisms in place and holding employees and their managers accountable for their treatment of taxpayers.

34 National Taxpayer Advocate 2014 Annual Report to Congress 134-144.

35 *Id.* at 124-127.

36 IRS response to TAS information request (Jul. 10, 2018).

37 IRS response to TAS fact check (Oct. 25, 2018).

38 IRS response to TAS information request (Jul. 10, 2018).

39 *Id.*

40 IRS response to TAS fact check (Oct. 25, 2018); IRS response to TAS information request (Jul. 25, 2018).

41 Tod Newcombe, *Is the Price of 311 Systems Worth Knowing?* GOVERNING THE STATES AND LOCALITIES (Mar. 2014), <http://www.governing.com/topics/urban/gov-311-systems-cost.html> (last visited Nov. 2, 2018).

42 National Taxpayer Advocate 2017 Annual Report to Congress 28-30; National Taxpayer Advocate 2017 Annual Report to Congress vol. 2, 229-244; Nina E. Olson, *Telephone Service in an Omnichannel Environment (Part 2 of 2)*, NTA BLOG, (Feb. 8, 2018) [https://taxpayeradvocate.irs.gov/news/nta-blog-telephone-service-in-an-omnichannel-environment-part-2?category=Tax News](https://taxpayeradvocate.irs.gov/news/nta-blog-telephone-service-in-an-omnichannel-environment-part-2?category=Tax%20News).

## CONCLUSION

Taxpayers often have difficulty locating IRS personnel who can provide accurate and responsive information regarding their cases. All too often, their only way of speaking with an actual person is by means of the IRS's main toll-free phone line, which includes difficult-to-interpret options and can lead to extended and potentially expensive hold times. Additionally, the IRS tries hard to channel sometimes-unwilling taxpayers into online self-service venues, which the majority of users deem to be substandard in many respects. Accordingly, it is not surprising that the IRS has been recently ranked last in quality communication in a survey of 15 federal agencies undertaken by Forrester Research.<sup>43</sup>

Even when taxpayers are provided with a specific phone number, most often it is for a group, rather than for an individual employee. These group numbers make it difficult for taxpayers to have a sense of continuity and rapport with the personnel working their cases. Moreover, a lack of ownership on the part of IRS personnel who work these cases can decrease the efficiency and effectiveness of case resolutions and worsen the customer experience. Compounding these circumstances, the IRS has no overarching mechanism for allowing taxpayers to raise questions and complaints to managers directly and to hold both employees and managers accountable for addressing such complaints in a timely and responsive manner.

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Provide all members of the general public with an accessible and easily searchable IRS directory that incorporates metadata and common-speech terminology to assist taxpayers in contacting particular offices within the IRS.
2. Institute a 311-type system where taxpayers can be transferred by an operator to the specific office within the IRS that is responsible for their cases.
3. Adopt a model for correspondence examinations and similar cases, such as those worked in ACS, in which a single employee is assigned to the case while it is open within the IRS function.
4. Establish a complaint and inquiry tracker that monitors and records requests to speak with supervisors, subsequent follow-up, and the results of that contact.

<sup>43</sup> Faith Adams and Rick Parrish, *Clear Communication is Vital for Government CX Success*, Forrester Research (Feb. 14, 2018).

**MSP  
#4****FREE FILE: The IRS's Free File Offerings Are Underutilized, and the IRS Has Failed to Set Standards for Improvement****RESPONSIBLE OFFICIAL**

Ken Corbin, Commissioner, Wage and Investment Division

**TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*

**DEFINITION OF PROBLEM**

To fulfill its statutory duty to increase electronic filing (e-filing), the IRS partners with Free File, Inc. (FFI), a group of private-sector tax return preparation software providers.<sup>2</sup> The 12 members of FFI offer free federal tax preparation software products, accessible at IRS.gov, to eligible taxpayers. The participants in the program must ensure that their products in the aggregate are available to 70 percent of all taxpayers, or about 105 million taxpayers, particularly focusing on economically disadvantaged and underserved communities.<sup>3</sup> Currently, taxpayers that have adjusted gross incomes (AGIs) of less than \$66,000 are eligible to use Free File software, while taxpayers with AGIs greater than that amount can use Free File Fillable Forms, the electronic version of IRS paper forms.<sup>4</sup>

Since 2002, the year the Free File program began, the number of individual tax returns increased by 15 percent and e-filing has increased by 180 percent.<sup>5</sup> While electronic filing has increased greatly since 2002, the goals of the Free File program have stagnated and use of the program has steadily declined.<sup>6</sup> Only about 2.5 million people filed returns using FFI software in fiscal year (FY) 2017 compared to over three million in FY 2014, and the peak of about 5 million taxpayers in tax year (TY) 2004.<sup>7</sup> The IRS has not committed funding to advertise FFI and raise awareness of the services offered. It no longer produces a demographics report or satisfaction survey to help identify why the number of Free File users is decreasing or what other types of services would best attract new users.<sup>8</sup>

- 1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).
- 2 See IRS Restructuring and Reform Act of 1998 (RRA 98), Pub. L. No. 105–206, 112 Stat. 685.
- 3 Eighth Memorandum of Understanding on Service Standards and Disputes Between the Internal Revenue Service and Free File, Inc. (effective as of Oct. 31, 2018), <https://www.irs.gov/pub/irs-utl/Eight%20Free%20File%20MOU.pdf> (Hereinafter 2018 Free File MOU).
- 4 See *Free File Software Offers*, <https://apps.irs.gov/app/freeFile/jsp/index.jsp> (last visited on Oct. 10, 2018).
- 5 In fiscal year (FY) 2002, the IRS received 130,905,000 individual income tax returns, and received 150,690,787 in FY 2017. In FY 2002, the IRS received 46,890,813 e-filed individual income tax returns, and 131,641,943 in FY 2017. See IRS Data Book (FY 2002, 2017).
- 6 See IRS Data Book (FY 2017, FY 2016, FY 2015, FY 2014) (showing Free File software usage has declined from 3,261,248 returns filed in FY 2014 to 2,536,183 returns in FY 2017).
- 7 See IRS Data Book (FY 2017, FY 2016, FY 2015, FY 2014); Michelle S. Chu and Melissa M. Kovalick, IRS, *An Analysis of the Free File Program*, presented at 99th Annual Conference on Taxation at 117 (Nov. 16-18, 2006).
- 8 IRS response to TAS information request (Sept. 7, 2018). Due to the lapse in appropriations, IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

While some taxpayers may be unaware of FFI services, others are unable to use the program due to its eligibility restrictions and language limitations. Taxpayers that do use the program have little guidance about the strengths and weaknesses of each software package's offering prior to selection, and may begin a return only to find the program lacks the capability to prepare the return or to fully capture the deductions and credits available to the taxpayer. As a result of these shortcomings, the services provided by FFI do not meet the needs and preferences of eligible taxpayers, particularly within underserved populations, undermining taxpayers' rights *to quality service* and *to pay no more than the correct amount of tax*. Specifically, the National Taxpayer Advocate is concerned that:

- In TY 2016, 2.3 percent of eligible taxpayers used Free File software, and only 0.2 percent of eligible taxpayers used Free File Fillable Forms;<sup>9</sup>
- Age restrictions sharply curtail the number of FFI options available to elderly taxpayers, as only three of the 12 FFI providers offer services to taxpayers of all ages and five have age limitations that start before the age of 60;<sup>10</sup>
- No Free File options were available for English as a Second Language (ESL) taxpayers in filing season 2018; and
- Testing by TAS shows several software providers have limitations in their navigational features and ability to help taxpayers correctly complete their returns, resulting in poor service quality.<sup>11</sup>

## ANALYSIS OF PROBLEM

### Background

The IRS Restructuring and Reform Act of 1998 (RRA 98) required the IRS to work with the private industry to increase e-filing, and set the goal of having 80 percent of all federal tax returns filed online by 2008.<sup>12</sup> Similarly, the George W. Bush administration's EZ Tax Filing Initiative directed the IRS to create "a single point of access to free on-line preparation and electronic tax filing services provided by Industry Partners to reduce burden and costs to taxpayers."<sup>13</sup> Initially, the Administration wanted the IRS to develop its own digital Form 1040, *U.S. Individual Income Tax Return*, accessed through WhiteHouse.gov, but IRS leadership determined the IRS did not have the capacity or resources to develop that product. Instead, the IRS partnered with a consortium of private tax preparation software companies, then known as the Free File Alliance, after the Office of Chief Counsel determined this consortium did not violate anti-trust provisions.<sup>14</sup>

In an agreement signed on October 30, 2002, members of the consortium agreed to provide free online return preparation services on an IRS.gov webpage to 60 percent of taxpayers during the tax filing

9 IRS response to TAS information request (Sept. 7, 2018).

10 See *Free File Software Offers*, <https://apps.irs.gov/app/freeFile/jsp/index.jsp> (last visited Oct. 10, 2018).

11 Note: the information included in this report reflects observations from the Free File offerings available for the 2018 filing season.

12 RRA 98, Pub. L. No. 105–206, 112 Stat. 685.

13 Presidential Initiatives: *IRS Free File*, <https://georgewbush-whitehouse.archives.gov/omb/egov/c-1-3-IRS.html>.

14 Treasury Department, *Treasury, IRS Announce New Efforts to Expand E-Filing* (Jan. 30, 2002), <https://www.treasury.gov/press-center/press-releases/Pages/po964.aspx>; see Letter from Charles James, Assistant Attorney General, Antitrust Division, Department of Justice, to Stephen Ryan, Manatt, Phelps, & Phillips, LLP (representing Free File Consortium) (Oct. 7, 2002) (Hereinafter DOJ Antitrust Letter 1).

season.<sup>15</sup> The agreement allowed the software providers to determine the scope of their offerings, but obligated the IRS to take oversight action, such as implementing usability performance measures and notifying the consortium if services are not being properly performed.<sup>16</sup> The IRS also had authority to terminate the agreement if the consortium failed to provide appropriate coverage, taking into account “the extent to which actual usage of Free Services has increased.”<sup>17</sup>

The IRS intended the Free File partnership to be the “best method” to “promote higher quality Free Services by utilizing the existing expertise of the private sector, maximize consumer choice, promote competition for such Free Services, and thereby meet the objectives in the least costly manner.”<sup>18</sup> In the Free File Memorandum of Understanding, the IRS “pledged to not enter the tax preparation software and e-filing services marketplace.”<sup>19</sup> As a result, the IRS has not followed other countries’ tax administrations in developing its own innovative offerings, such as pre-populated returns, to reduce taxpayer burden.<sup>20</sup> While the complexity and structure of the U.S. tax system make it difficult to compare to other countries, the National Taxpayer Advocate does believe that following some innovations, such as an expanded “Pay-As-You-Earn (PAYE)” system, would allow for more accurate and efficient collection of tax liabilities.<sup>21</sup>

While the initial agreement required the Free File Alliance to provide free software services to only 60 percent of taxpayers, several members made their offerings available to all taxpayers without restrictions.<sup>22</sup> Members were ranked in “tiers” on the IRS webpage, with the highest-tier members listed first.<sup>23</sup> As a result, use of Free File expanded greatly, as 5.1 million taxpayers filed Free File returns in tax year 2004, a 46 percent increase from the previous year.<sup>24</sup> In reviewing the Free File program for anticompetitive effects, the Department of Justice found that the providers’ expansion of services,

15 Free On-Line Electronic Tax Filing Agreement entered into between the IRS and the Free File Alliance, LLC (effective as of Oct. 30, 2002), <https://www.irs.gov/pub/irs-utl/2002-free-online-electronic-tax-filing-agreement.pdf> (Hereinafter 2002 Free File Agreement).

16 *Id.* at 3-4.

17 *Id.* at 2.

18 *Id.* at 1. Describing this decision, Treasury Secretary Paul O’Neil stated, “I don’t intend for the IRS to get into the software business, but rather to open a constructive dialogue with those who already have established expertise in this field.” Department of the Treasury, *Treasury, IRS Announce New Efforts to Expand E-Filing* (Jan. 30, 2002), <https://www.treasury.gov/press-center/press-releases/Pages/po964.aspx>.

19 2018 Free File MOU.

20 See Brookings Institute, Tax Policy Center, *Briefing Book*, 447, [https://www.taxpolicycenter.org/sites/default/files/briefing-book/tpc-briefing-book\\_0.pdf](https://www.taxpolicycenter.org/sites/default/files/briefing-book/tpc-briefing-book_0.pdf) (“At last count, 36 countries, including Germany, Japan, and the United Kingdom, permit return-free filing for some taxpayers.”). The National Taxpayer Advocate notes that many of these countries don’t deliver refundable credits through the tax code, and tax by the individual unit, rather than by the family, making for a more simplified tax system.

21 The IRS should analyze and report on the feasibility of and steps necessary for furnishing information return (e.g., Form W-2, 1099) data to taxpayers electronically for direct importation into Free Fillable Forms and software or for provision to authorized tax return preparers. See also Legislative Recommendation: *Tax Withholding And Reporting: Improve the Processes and Tools for Determining the Proper Amount of Withholding and Reporting of Tax Liabilities*, *infra*; Research Study: *A Conceptual Analysis of Pay-As-You-Earn (PAYE) Withholding Systems As a Mechanism for Simplifying and Improving U.S. Tax Administration*, vol. 2, *infra*.

22 Michelle S. Chu and Melissa M. Kovalick, IRS, *An Analysis of the Free File Program*, presented at 99th Annual Conference on Taxation at 117 (Nov. 16-18, 2006), <https://www.irs.gov/pub/irs-soi/06rpppchu.pdf>.

23 Letter from Renata Hesse, Chief, Networks and Technology section, Department of Justice Antitrust Division, to Lori Larson, Chief, Public Contracts and Technology Branch, General Legal Services (May 9, 2005) at 2 (Hereinafter DOJ Antitrust Letter 2).

24 Michelle S. Chu and Melissa M. Kovalick, IRS, *An Analysis of the Free File Program*, presented at 99th Annual Conference on Taxation at 117 (Nov. 16-18, 2006), <https://www.irs.gov/pub/irs-soi/06rpppchu.pdf>; see also Treasury Inspector General for Tax Administration (TIGTA), *Use of the Free File Program Declined After Income Restrictions Were Applied*, Report 2006-40-171 (Sept. 29, 2006).

even as a method of cross-selling their paid goods and services, was “precisely the sort of activit[y] the antitrust laws were designed to protect” and “should be encouraged” by the IRS.<sup>25</sup> However, the next Free File agreement ended the tiered structure and significantly curtailed the scope of free services that could be offered by each provider, specifying that no provider could cover over 50 percent of taxpayers.<sup>26</sup>

The National Taxpayer Advocate continued to criticize the limitations of the Free File program, and advocated that the IRS provide all taxpayers, regardless of income, with a bare-bones digital version of the paper Form 1040 complete with fillable fields, links to instructions, and math and numeric transfer capacity, along with free electronic filing.<sup>27</sup> To meet this need, the 2009 Free Memorandum of Understanding (MOU) created “Free File Fillable Forms,” a forms-based product designed by the members to make electronic versions of IRS forms and schedules available to all taxpayers.<sup>28</sup>

The IRS has renewed its agreement with the Free File Alliance, now called Free File, Inc. (FFI), multiple times, including the most recent agreement signed on October 31, 2018.<sup>29</sup> Amendments to the agreement have included broadening the scope of eligibility for the Free File program to 70 percent of all taxpayers, heightening security and privacy requirements, and requiring for members to provide an electronic Free File indicator.<sup>30</sup> However, the Free File program still falls short in addressing key areas in need of reform to better serve taxpayers, as discussed below.

### The Goals for Free File, Inc., Have Not Evolved Since Its Creation and Its IRS Budget Has Decreased to Zero

Despite surpassing the e-filing goal of 80 percent set by RRA 98, the goals of the Free File program remain stagnant.<sup>31</sup> The 2018 Free File MOU lists four objectives:

1. “Make tax return preparation and filing easier and reduce the burden on individual taxpayers, particularly the economically disadvantaged and underserved populations;
2. Support the IRS’s statutory goals of increased electronic filing, pursuant to the IRS Restructuring and Reform Act of 1998;
3. Provide greater service and access to the Services to taxpayers; and

25 DOJ Antitrust Letter 2 at 3-4.

26 Free On-Line Electronic Tax Filing Agreement entered into between the IRS and the Free File Alliance, LLC (effective as of Oct. 30, 2005), <https://www.irs.gov/pub/irs-utl/2005-free-online-electronic-tax-filing-agreement.pdf> (hereinafter 2005 Free File Agreement).

27 See, *IRS National Taxpayer Advocate Annual Report and IRS Oversight Board Annual Report: Hearing Before the H. Subcomm. on Oversight of the H. Comm. on Ways and Means*, 107th Cong. 23 (2002) (transcript of testimony); *Tax Return Preparation Options for Taxpayers: Hearing Before the S. Finance Comm.*, 109th Cong. (2006) (transcript of testimony); *Tax Return Filing Season, Internal Revenue Service Operations, Fiscal Year 2009 Budget Proposals*, and the *IRS National Taxpayer Advocates Annual Report: Hearing Before the H. Subcomm. on Oversight of the H. Comm. on Ways and Means*, 110th Cong. 82 (Mar. 13, 2008) (transcript of testimony); see also, National Taxpayer Advocate 2004 Annual Report to Congress 89-102 (Most Serious Problem: *Electronic Return Preparation and Filing*); National Taxpayer Advocate 2004 Annual Report to Congress 471-477 (Legislative Recommendation: *Free Electronic Filing For All Taxpayers*); S. 1321, 109th Cong. § 310 (2005).

28 Fifth Memorandum of Understanding on Service Standards and Disputes Between the Internal Revenue Service and Free File Alliance, LLC (effective as of Oct. 20, 2009), <https://www.irs.gov/pub/irs-utl/2009-fourth-ff-mou.pdf> (hereinafter 2009 Free File MOU).

29 2018 Free File MOU.

30 *Id.*

31 Nearly 130 million tax returns or about 88 percent of all individual income tax returns were e-filed in FY 2018. IRS, *Filing Season Statistics for Week Ending August 31, 2018*. Only about 40 million, or approximately 31 percent, were e-filed in FY 2001, prior to the creation of Free File. IRS Data Book (FY 2001).

4. Implement one of the proposals in the President's Fiscal Year 2003 budget, specifically to encourage further growth in electronic filing by providing taxpayers the option to file their tax return online without charge using cooperation with, and encouraging competition within, the private sector."<sup>32</sup>

The objectives have remained substantively unchanged since the program's inception. They continue to reference statutory e-filing goals from 1998 and the President's 2003 budget, rather than identifying new areas for focus and ways to expand the program.

Furthermore, the program formerly had a minimal budget of about \$6 million, but that budget was reduced and ultimately eliminated over the years.<sup>33</sup> The current IRS marketing budget for the Free File program is zero.<sup>34</sup> Failing to set new goals for the Free File program or allocate sufficient money towards it reveals how the IRS prioritizes the Free File program and hinders the program from improving the e-filing services the IRS endorses for taxpayers.

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The objectives have remained substantively unchanged since the Free File program's inception. They continue to reference statutory e-filing goals from 1998 and the President's 2003 budget, rather than identifying new areas for focus and ways to expand the program.

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### The IRS Has Not Provided Effective Oversight and Evaluation of the Free File Program

The IRS has not taken steps to evaluate whether the Free File program is even meeting the existing goals described above. To ensure program standards are being met, the 2018 Free File MOU emphasizes the "in-place review process" for the program rather than adding any new initiatives.<sup>35</sup> The current "in-place review process" occurs once prior to filing season and once during filing season. This review is mainly to ensure the software providers' technical compliance with the Free File MOU, and does not evaluate the quality of the offerings from Free File software providers.<sup>36</sup> Thus, the National Taxpayer Advocate is concerned that merely reemphasizing the limited reviews currently in place, without adding resources or creating new measures, will not adequately evaluate the experiences of taxpayers using the program.

32 2018 Free File MOU.

33 Max Cherney, *100 Million Americans Can File Their Taxes for Free, Yet Only 3 Million People Do It*, MARKET WATCH, (Apr. 17, 2018), <https://www.marketwatch.com/story/how-to-file-your-taxes-for-free-online-if-you-make-less-than-66000-a-year-2018-03-28>.

34 IRS response to TAS information request (Sept. 7, 2018).

35 IRS News Release IR-2018-213, IRS, *Free File Alliance Announce Changes to Improve Program; Improved Taxpayer Options Available for 2019 Free File Program* (Nov. 2, 2018), <https://www.irs.gov/newsroom/irs-free-file-alliance-announce-changes-to-improve-program-improved-taxpayer-options-available-for-2019-free-file-program>.

36 These reviews: validate that the software has acquired the appropriate security and privacy certifications; test that a filer can easily prepare, file, print, download and save a tax return using the Free File software; ensure ancillary services/products, Refund Anticipation Checks and Refund Anticipation Loans are not being offered; ensure third party security and privacy certifications have been acquired to assure industry security and privacy standards and practices are being used; and validate a guarantee of calculations is provided by each company. IRS response to TAS information request (Sept. 7, 2018).

In another example of the IRS's limited evaluation of its partnership, even though FFI members are required to provide a use indicator to identify returns filed using Free File, the IRS has not prepared a Free File demographics report since 2015.<sup>37</sup> Without conducting a demographics report, the IRS has no way to know which taxpayers are using Free File services. The IRS also no longer conducts Free File satisfaction surveys, which it claims is due to budget constraints.<sup>38</sup> However, the most recent Free File MOU from 2018 specifically assigns the members of FFI the responsibility to “provide the necessary support to accomplish a customer satisfaction survey.”<sup>39</sup> Thus, the IRS failure to avail itself of that support shows the IRS's failure to exercise oversight to enforce the standards set for the program.

Conducting robust demographics analysis and satisfaction surveys, along with testing of taxpayer scenarios, would help the IRS determine why particular groups use or do not use the Free File offerings, which providers are offering inadequate services, and how it can improve its agreement with FFI to better meet the needs of taxpayers.<sup>40</sup> There is an old adage that “you get what you measure.” By neglecting to measure and evaluate the Free File program, the IRS is missing a valuable opportunity to fulfill its promises in the 2018 Free File MOU to make the program more taxpayer friendly. The IRS should work with TAS to develop meaningful measures and better oversight, including routine testing, to better ensure the offerings provided on Free File fulfill the *right to quality service*.

### Only About 2.5 Million People Filed Returns Using Free File, Inc. in Tax Year 2017, and Use of the Program Continues to Decline

The number of taxpayers filing online has greatly increased since the early 2000s, with almost 130 million or 88 percent of all tax returns being filed electronically in FY 2017. However, less than two percent, or only about 2.5 million of those returns, were filed using Free File.<sup>41</sup> In comparison, paid preparers filed almost 78.6 million tax returns electronically in tax year 2017.<sup>42</sup> Over 3.5 million returns were prepared through Volunteer Income Tax Assistance and Tax Counseling for the Elderly programs, a higher number than prepared by FFI despite the fact that taxpayers must expend more time and resources to go to one of these sites.<sup>43</sup>

37 IRS response to TAS information request (Sept. 7, 2018). Due to the lapse in appropriations, IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

38 IRS response to TAS information request (Sept. 7, 2018).

39 2018 Free File MOU at 17.

40 For example, the most recent Free File demographics report from 2015 does not show how many Spanish speaking taxpayers used its services. See *Demographics of TY 2015 Traditional Free Filers, Free File Fillable Form Users, True Paper Filers, V-code Filers, and Form 1040 Series Filers*, included in IRS response to TAS information request (Sept. 7, 2018).

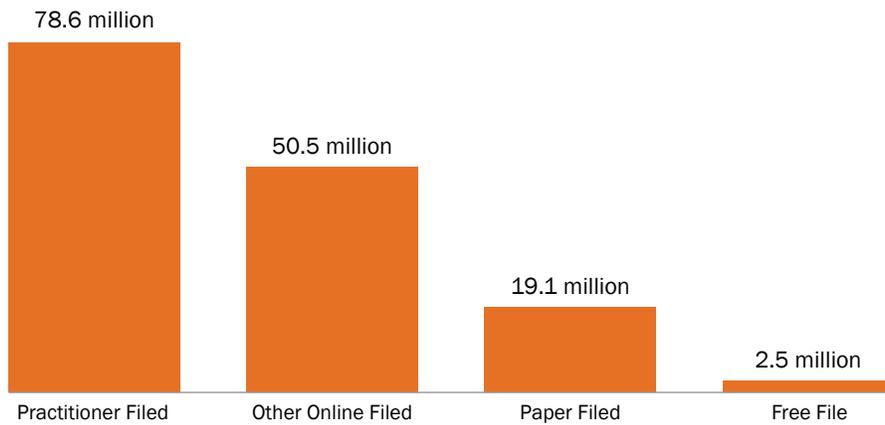
41 IRS Data Book (FY 2017) and IRS, *2017 Filing Season Statistics* (Dec. 29, 2017). In tax year 2016, just under 2.3 percent of all eligible taxpayers submitted returns using the Free File software, and just 0.2 percent of taxpayers used Free File Fillable Forms to submit their returns. IRS response to TAS information request (Sept. 7, 2018).

42 IRS Data Book at 9 (FY 2017).

43 *Id.* at 47 (showing numbers of returns).

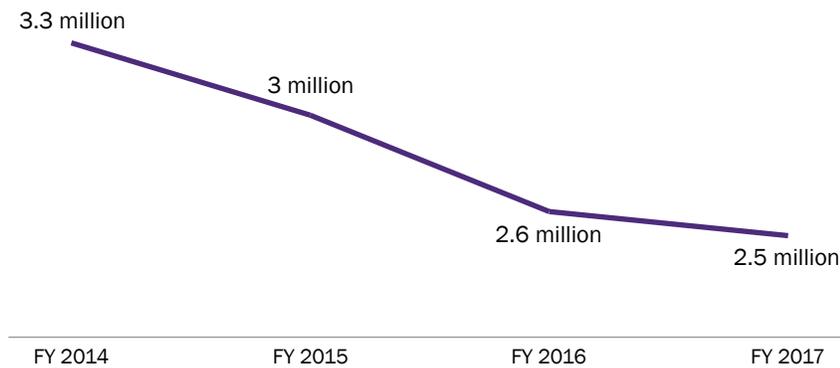
**FIGURE 1.4.1**<sup>44</sup>

**Individual Return Filings by Filing Type, FY 2017**



**FIGURE 1.4.2**<sup>45</sup>

**Free File Returns by Fiscal Year**



44 IRS Data Book at 9 (FY 2017).

45 IRS Data Book (FY 2017, FY 2016, FY 2015, FY 2014).

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**Conducting robust demographics analysis and satisfaction surveys, along with testing of taxpayer scenarios, would help the IRS determine why particular groups use or do not use the Free File offerings, which providers are offering inadequate services, and how it can improve its agreement with Free File, Inc. (FFI) to better meet the needs of taxpayers.**

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As Figure 1.4.2 illustrates, use of Free File software has continued to decrease since 2014. This declining usage also shows the program's low retention rate, as only 44 percent of taxpayers that used Free File in FY 2014 and were eligible to use the program again in FY 2015 did so.<sup>46</sup> FFI usage was at its greatest when software providers could offer unrestricted services to more than 50 percent of taxpayers, as over 5 million taxpayers used FFI software in TY 2004.<sup>47</sup> While the 2005 restriction preventing each software provider from covering more than 50 percent of individual taxpayers was intended to make it easier for software providers to enter the Free File program, the number of participating providers has decreased from 20 providers in the program's early years to just 12 in FY 2018.<sup>48</sup> Thus, this restriction has failed to achieve its goal and, instead, has limited the options available to taxpayers.

The elimination of any marketing budget for the Free File program has made it difficult for the IRS to make taxpayers aware of the services available, as advertising for the program is limited to a few filing season press releases. There is virtually no marketing or promotion of Free File Fillable Forms on the IRS.gov homepage, even though this service is available for everyone. The IRS has mainly focused its efforts to increase awareness of the Free File program on making it easy to locate Free File on IRS.gov and IRS2Go, but these efforts do not show taxpayers the value of Free File or why they should use FFI instead of a paid return preparer. As stated above, because the IRS no longer conducts FFI customer satisfaction surveys, it does not have a way to know why the number of Free File users is decreasing or what other types of services would best attract new users. These questions must be answered to determine whether the program is worth continuing.

### **The Services Provided by Free File, Inc. Fail to Meet the Needs of Taxpayers, Particularly Within Underserved Populations**

#### *Free File Does Not Effectively Serve Its Targeted Demographics*

The latest FFI operating agreement specifically highlights economically disadvantaged and underserved populations as the targeted groups for Free File services.<sup>49</sup> Taxpayers in vulnerable groups typically have limited disposable income and free time to spend on tax return preparation. However, FFI is failing to serve taxpayers within these populations, particularly low income taxpayers, elderly taxpayers, and ESL taxpayers.<sup>50</sup>

46 Jacob Goldin, *Participation in the IRS Free File Program*, TAX NOTES (Oct. 23, 2017).

47 Michelle S. Chu and Melissa M. Kovalick, IRS, *An Analysis of the Free File Program*, presented at 99th Annual Conference on Taxation at 117 (Nov. 16-18, 2006).

48 See *Free File Software Offers*, <https://apps.irs.gov/app/freeFile/jsp/index.jsp> (last visited on Oct. 10, 2018).

49 2018 Free File MOU.

50 Stakeholders raised concerns that the Free File program would not serve its target audience adequately in comments to the Federal Register Notice on Free Internet Filing Agreement. Specifically, these comments noted that the program would not protect the interests of low income taxpayers and risked excluding English as a Second Language taxpayers. See IRS Electronic Tax Administration, *Responses to Federal Register Notice on Free Internet Filing Agreement* (Sept. 17, 2002).

First, while a high percentage of taxpayers using FFI software are low income, this number still constitutes a small proportion of low income taxpayers as a whole. Figure 1.4.3 illustrates the breakdown of income levels of Free File users in 2015, the last year the IRS prepared a demographics analysis report.

**FIGURE 1.4.3, Percentage of Free File Users by Income Demographics (TY 2015)<sup>51</sup>**

Adjusted Gross Income	Traditional Free File	Free File Fillable Forms
Negative AGI	1.00%	0.30%
\$0 to \$17,000	47.75%	13.10%
\$17,001 to \$25,000	15.91%	4.77%
\$25,001 to \$35,000	15.35%	5.58%
\$35,001 to \$50,000	14.13%	7.95%
\$50,001 to \$75,000	5.79%	20.56%
\$75,001 to \$100,000	0.03%	20.98%
\$100,001 or More	0.04%	26.75%
<b>Total</b>	<b>100.00%</b>	<b>100.00%</b>

Figure 1.4.3 shows the majority of all Free File software users had adjusted gross income of \$25,000 or less.<sup>52</sup> However, this represents only about 1.5 million taxpayers, or just under 3 percent of all taxpayers in this demographic.<sup>53</sup> This shows that a substantial number of low income taxpayers are using other methods to file their returns or are not filing at all. If low income taxpayers pay for tax return preparation services instead of using the free ones offered by FFI, they would have less resources available to cover other basic living expenses. Although there may be legitimate reasons for using for-fee services—lack of tax knowledge, fear of making mistakes, desire for refund anticipation loans—the IRS has not conducted research to determine why low income taxpayer prefer for-fee services over free filing.

Second, elderly taxpayers are limited in the Free File software options available to them. While the IRS does offer the Tax Counseling for the Elderly program to assist taxpayers age 60 or older with return preparation, this program is only available during the filing season and is not designed to serve every taxpayer in this age range. Free on-demand electronic tax preparation service is still a valuable resource for taxpayers in this demographic. However, only three of the 12 FFI providers offer services to taxpayers of all ages, and even these have use restrictions based on the taxpayer's state of residence, income, or eligibility for the Earned Income Tax Credit.<sup>54</sup> Five of the 12 FFI providers have age limitations that start before the age of 60, with some even excluding taxpayers over the age of 50.<sup>55</sup> Age

51 See *Demographics of TY 2015 Traditional Free Filers, Free File Fillable Form Users, True Paper Filers, V-code Filers, and Form 1040 Series Filers*, included in IRS response to TAS information request (Sept. 7, 2018).

52 *Id.* Due to the lapse in appropriations, IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

53 Only 1,513,295 taxpayers out of 56.9 million total taxpayers with income \$25,000 or less used Free File software. *Id.*

54 For example, one Free File, Inc. (FFI) software provider makes its services available to all ages, but the taxpayer must have adjusted gross income of less than \$33,000 or be eligible for the Earned Income Tax Credit. See *Free File Software Offers*, <https://apps.irs.gov/app/freeFile/jsp/index.jsp> (last visited on Oct. 10, 2018).

55 *Id.*

restrictions like these sharply curtail the number of FFI options available to taxpayers, making it more difficult for them to choose a return package suited to their needs and preferences.

Third, ESL taxpayers face extreme difficulty navigating and using the Free File software, as no options were available in languages other than English in filing season 2018. The Hispanic community in the United States typically has a lower rate of electronic filing than other demographic groups.<sup>56</sup> A recent TAS study showed that because of language barriers and less education, Spanish-speaking taxpayers may be especially vulnerable to unscrupulous return preparers who promote high-interest loans and charge high fees.<sup>57</sup> Thus, there is a great need for free tax return preparation assistance, vetted by the IRS, to be made available to Spanish-speaking taxpayers. However, this need is not being met by FFI. While the IRS does provide some guidance to Spanish-speaking taxpayers on IRS.gov, the description and display for using Free File is only available in English.

FIGURE 1.4.4

#### IRS Free File Guidance in Spanish



Even if an ESL taxpayer can navigate through this screen, none of the return preparation software options available have a Spanish language option.<sup>58</sup> In its most recent Free File Memorandums of Understanding, the IRS made making tax filing easier for underserved populations a key objective, and even required members to provide a Spanish Free File indicator to show how many taxpayers took advantage of such services.<sup>59</sup> However, in another example of the IRS's lack of oversight and evaluation of the Free File program, there were zero providers offering such a Spanish-language version in filing season 2018. Because the IRS itself has not translated the Form 1040 into Spanish, Free File Fillable Forms are also only available in English.<sup>60</sup> These limitations in service can drive Spanish-speaking taxpayers to costly paid preparer options.

56 Sonja Pippin and Mehmet Tosun, *Electronic Tax Filing in the United States: An Analysis of Possible Success Factors* 12 ELECTRONIC JOURNAL OF E-GOVERNMENT, ISSUE 1, 22-38 (2014).

57 National Taxpayer Advocate 2015 Annual Report to Congress vol. 2, 102 (Research Study: *Understanding the Underserved Hispanic Population*) ("Hispanics who use unregulated preparers run the risk of having their returns prepared incorrectly, either as a result of incompetency or willful misconduct."). TAS research has shown that only six percent of Hispanic taxpayers used a free tax preparation service by a trained volunteer, while 60 percent used a paid tax return preparer other than an attorney, CPA, or enrolled agent. *Id.*

58 Due to the lapse in appropriations, IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

59 2018 Free File MOU at 16; 2015 Free File MOU at 16.

60 In tax year 2017, TAS translated Form 1040 into Spanish, the first time ever this form has been available in a language other than English. TAS will update this form with changes for the 2018 Form 1040. The form is available at TAS's tax reform website, <https://taxchanges.us/es/>.

*Testing by TAS Shows That Content Quality Is Not Consistent Among All Free File Software Providers, As Several Have Limitations in Their Navigation and Capabilities*

The National Taxpayer Advocate continues to be concerned that the IRS does not sufficiently exercise its authority to set standards for what must be included in each Free File software provider's service offerings. The 2018 Free File MOU sets standards for core forms and schedules that must be offered by Free File software providers, but does not ensure that each offering covers specific deductions, credits, and exemptions.<sup>61</sup> To evaluate each Free File software provider's ability to support items a taxpayer may include on a return, TAS tested several return preparation scenarios including Schedule C deductions, the tuition and fees credit, the Earned Income Tax Credit, casualty loss/disaster relief provisions, and the mortgage insurance premium deduction. Our testers had varying success completing their simulated return, depending on the provider they chose and the complexity of the scenario.<sup>62</sup>

The perceived benefit of Free File software, as opposed to just Free File Fillable Forms, is that it gives guidance to help taxpayers navigate through the return filing process and alert them of all deductions and credits for which they may be eligible. However, testers noted that the quality of guidance provided during the process varied greatly among the software providers. Some sites had helpful tools like video tutorials, live chat features, explanations of deductions, and review features to help ensure taxpayers hadn't missed any credits or deductions. On others, however, the testers noted confusion in finding a help center, being overwhelmed by lists of unexplained deductions, and difficulty in correcting errors.

Testers of the casualty loss/disaster relief scenario noted that some providers failed to have prompts for how to claim this deduction, and they were left searching for the proper forms on their own. Testers of the Schedule C scenario noted that while all providers supported filing a Schedule C, some did not allow adding in depreciable assets or offer additional guidance on depreciation. Some sites also failed to explain how particular deductions or credits were calculated and selected, making it difficult for taxpayers to ensure they had selected the appropriate ones.<sup>63</sup> As a result of these limitations, taxpayers with limited knowledge of tax law depending on the Free File program for guidance may not realize they are eligible for some deductions and credits or claim them improperly, leading them to file incorrect returns.<sup>64</sup> If the service quality provided by Free File software fails to meet taxpayers' expectations, it can erode trust in the agency given the IRS's seeming endorsement of the Free File software offerings.

61 See 2018 Free File MOU. When TAS has conducted testing on Free File software in the past, our office found significant limitations in the coverage of some software providers. For example, testing by TAS in 2006 showed that a majority of providers did not include tax law benefits provided after Hurricane Katrina. See *Tax Return Preparation Options for Taxpayers: Hearing Before the S. Finance Comm.*, 109th Cong. (2006) (transcript of testimony). Similarly, testing in 2015 showed several Free File packages did not include info about exemptions from the Individual Shared Responsibility Payment of the Affordable Care Act, meaning some taxpayers paid a penalty they didn't owe. See National Taxpayer Advocate 2015 Annual Report to Congress 167-179, fn. 20 (Most Serious Problem: *Affordable Care Act (ACA) – Individuals: The IRS Is Compromising Taxpayer Rights As It Continues to Administer the Premium Tax Credit and Individual Shared Responsibility Payment Provisions*).

62 Please note: TAS's objective was to determine the existence and extent of limitations and problems that a typical user of the Free File sites would encounter. In some instances, the testers found the sites very difficult to navigate and were unable to locate forms or answers that later testers could locate. Therefore, the results described below reflect simply what our testers experienced and not necessarily what a site was capable of accomplishing.

63 For example, when testing the tuition and fees deduction scenario, one tester noted that some of the software providers did not explain the difference between the American Opportunity Credit, Lifetime Learning Credit, and the tuition and fees deduction. These providers would merely provide the credit or deduction determined to be most beneficial, without providing the bottom line value for all three.

64 Some software tested seemed overly focused on refund maximization, which could tempt taxpayers to provide incorrect information in hopes of getting a larger refund.

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If the IRS continues to show no appetite for monitoring and overseeing, including testing, the products it gives the appearance of endorsing, the IRS should end its Free File offerings and, instead, focus on improving and promoting free fillable forms, which is the 21st century version of the Form 1040.

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### Cross-Marketing and Advertising of Other Services on Free File Software Platforms Can Confuse Taxpayers, and Gives the Impression of IRS Endorsement of For-Fee Services

All Free File sites are accessed through the official IRS.gov website, yet cross-marketing of ancillary products and services is common on many of the sites. In the past, the National Taxpayer Advocate has raised concerns that cross-marketing and advertising on Free File software platforms can distract and confuse taxpayers as they complete their returns and undercut the value of the free services provided.<sup>65</sup>

TAS commends the IRS for including important amendments to strengthen taxpayer protections and limit the marketing of paid services by FFI members in the 2018 Free File MOU.<sup>66</sup> The new MOU includes language requiring software providers to automatically return taxpayers to the IRS Free File page if they don't qualify for an offer, preventing software providers from upselling their other products through "value-add" buttons on landing pages.<sup>67</sup> The MOU also contains provisions for limiting email solicitations of taxpayers in subsequent years, and requiring Free File software providers to offer returning taxpayers Free File products as a first option in subsequent years.<sup>68</sup>

While these amendments are important, the National Taxpayer Advocate continues to be concerned over the marketing of paid state tax filing services on Free File platforms. Our testing showed some providers required taxpayers to enter in state tax return information, even if the taxpayer did not intend to file a state return, and then advertised the price of the state return at the end of the process. While some states offer free filing independent of FFI, the 2018 Free File MOU prohibits the IRS from making

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65 See *Tax Return Preparation Options for Taxpayers: Hearing Before the S. Finance Comm.*, 109th Cong. (2006) (transcript of testimony).

66 For a description of our prior testing, see *Tax Return Preparation Options for Taxpayers: Hearing Before the S. Finance Comm.*, 109th Cong. (2006) (transcript of testimony).

67 IRS News Release IR-2018-213, *IRS, Free File Alliance Announce Changes to Improve Program; Improved Taxpayer Options Available for 2019 Free File Program* (Nov. 2, 2018), <https://www.irs.gov/newsroom/irs-free-file-alliance-announce-changes-to-improve-program-improved-taxpayer-options-available-for-2019-free-file-program>. See also 2018 Free File MOU § 4.32.2 (Requiring Members to "provide, as a first option, a prominent hyperlink for the taxpayer to return to the IRS Free File Landing Page" if the taxpayer "enters a Member's Free File Landing Page and begins to complete a return but ultimately cannot qualify for the Member's free offer."); § 4.32.6 ("Members shall not include a "value-added" button (*i.e.*, an icon, link or any functionality that provides a taxpayer with access to a Member's commercial products or services) on the Member's Free File Landing Page.").

68 See also 2018 Free File MOU § 4.14 (A returning taxpayer must "be given a first option to return to the Member's Free File offer before receiving any other alternative choices for the Member's publicly available commercial tax preparation products or services."); § 4.32.4 ("Free File Members shall communicate not less than once annually via email with their taxpayer customers who used Free File services and completed their returns through Free File in the immediately preceding tax year prior to the opening of the following tax season. The content of this email(s) shall only remind the taxpayer about the availability of the Member's Free File offer and invite them to return to the Member's Free File Landing Page. Free File Members shall not use these communications to communicate with the taxpayer about any non-Free File commercial products or services. No marketing, soliciting, sale or selling activity, or electronic links to such activity, will be permitted in these email(s).").

taxpayers aware of these services.<sup>69</sup> By providing links to software providers marketing paid state-return options and not advertising the other free state options available, the IRS is in effect endorsing these for-fee products. Thus, rather than providing a service that meets taxpayers' needs, Free File software has the potential to mislead taxpayers and ensnare them in for-fee product offerings.

## CONCLUSION

With no effective goals, measures, or budget, the IRS's Free File program in its current format has become an ineffective relic of early efforts to increase e-filing. Rather than being a beneficial program providing free return preparation services to all, it is an inadequate program that provides limited services and is used by only a small percentage of eligible taxpayers. The IRS is devoting zero resources to oversight and testing of this program to understand why taxpayers aren't using it and how the services offered could be improved. When the services provided by FFI fail to meet the needs and preferences of taxpayers, particularly in underserved communities, it reflects poorly on the IRS and can erode taxpayers' trust in fair tax administration.

If the IRS is going to promote the product, then it needs a dedicated budget and staff to set standards for the program, including what provisions products must incorporate in order to participate, to prevent taxpayers from being harmed. This starts with setting actionable goals that address issues currently faced by taxpayers and establishing measures to assess whether those goals are being met. The IRS must monitor and test with scenarios what the products do and present taxpayers with more information so they can make an informed choice about whether to use each product. Focusing on the taxpayer's experience using the Free File program will allow the IRS to identify how to best alter and develop the program to make free tax return preparation a more convenient and viable option for taxpayers.

If the IRS continues to show no appetite for monitoring and overseeing, including testing, the products it gives the appearance of endorsing, the IRS should end its Free File offerings and, instead, focus on improving and promoting free fillable forms, which is the 21<sup>st</sup> century version of the Form 1040.<sup>70</sup> This fillable electronic version of the Form 1040 should build on what is offered by Free File Fillable Forms, including linking from IRS form instructions to IRS publications, increased guidance for common areas of taxpayer confusion, creating versions available in other languages like Spanish, and providing a dedicated email where taxpayers can get help when experiencing technology glitches.

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69 See 2018 Free File MOU § 4.22. The 2018 Free File MOU specifies that providing links from “the IRS Free File Website to Non-Free File State Department of Revenue websites is grounds for FFI to immediately dissolve its obligations in this MOU.” 2018 Free File MOU § 4.22.

70 For additional description of this recommendation, see Legislative Recommendation: *Tax Withholding And Reporting: Improve the Processes and Tools for Determining the Proper Amount of Withholding and Reporting of Tax Liabilities*, *infra*.

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Develop actionable goals for the Free File program, including targeted-use percentages, prior to entering into a new agreement with Free File, Inc.
2. Work with TAS to create measures evaluating taxpayer satisfaction with the Free File program and test each return preparation software's ability to complete various forms, schedules, and deductions.
3. Provide Free File Fillable Forms and Software options for English as a Second Language taxpayers.
4. Prepare an advertising and outreach plan to make taxpayers, particularly in underserved communities, aware of the services available through the Free File program.
5. Allow Free File members to provide services to all taxpayers as a part of its next operating agreement instead of capping the percentage of eligible taxpayers each software provider can cover.
6. Redesign the Free File Software Lookup Tool to better direct taxpayers to software providers that best meet their circumstances.
7. Improve the capabilities offered to taxpayers through Free File Fillable Forms, including:
  - a. Linking from IRS form instructions to related IRS publications;
  - b. Providing increased guidance for common areas of taxpayer confusion;
  - c. Ensuring taxpayer's abilities to download, save, and print all forms with troubleshooting assistance; and
  - d. Creating a dedicated email where taxpayers can get help when experiencing technology glitches.
8. If the above recommendations are not substantially adopted, discontinue the Free File Program and create an improved electronic free fillable forms program including the features described in Recommendation 7.

## **MSP #5 FALSE POSITIVE RATES: The IRS's Fraud Detection Systems Are Marred by High False Positive Rates, Long Processing Times, and Unwieldy Processes Which Continue to Plague the IRS and Harm Legitimate Taxpayers**

### **RESPONSIBLE OFFICIAL**

Ken Corbin, Commissioner, Wage and Investment Division

### **TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to a Fair and Just Tax System*

### **DEFINITION OF PROBLEM**

In calendar year (CY) 2016, tax refund fraud cost the government approximately \$1.6 billion.<sup>2</sup> The IRS's Return Integrity Operations office (RIO), which is housed in the Wage and Investment Division (W&I), is tasked with reducing this cost by detecting and preventing both identity theft (IDT) in the Taxpayer Protection Program (TPP) and non-IDT refund fraud in the Pre-Refund Wage Verification Program (WVP).<sup>3</sup> The IRS primarily does this using two systems: the Dependent Database (DDb) and the Return Review Program (RRP).<sup>4</sup> Although the fraud detection systems protected about \$7.6 billion in revenue between January 1 and September 30, 2018, they also delayed the processing of almost \$20 billion in legitimate refunds.<sup>5</sup> Between January 1 and October 3, 2018, the False Positive Rate (FPR) for non-IDT refund fraud filters was 81 percent, while the FPR for IDT refund fraud filters was 63 percent.<sup>6</sup>

Further, according to the IRS, 64 percent of returns selected into the non-IDT refund fraud program in 2018 were legitimate even though more than two weeks elapsed from the time of selection until the IRS

- 1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).
- 2 Government Accountability Office (GAO), GAO-18-224, Tax Fraud and Noncompliance: *IRS Can Strengthen Pre-Refund Verification and Explore More Uses 1* (Jan. 30, 2018).
- 3 Although not all tax refund fraud involves identity theft (IDT), and not all IDT involves tax refund fraud (e.g., employment-related IDT does not involve the theft of tax refunds), there are enough similarities between the two that it is appropriate to discuss them together.
- 4 The Dependent Database (DDb) and the Return Review Program (RRP) systems use filters, comprised of many rules or models, to score each return. If the return receives a certain score and is flagged as potentially fraudulent, the return goes to the Taxpayer Protection Program (TPP) or the Income Wage Verification (IWV) Program for further scrutiny. Internal Revenue Manual (IRM) 25.25.2.1, *Program Scope and Objectives* (May 7, 2018); IRM 25.25.6.1.7, *Taxpayer Protection Program Overview* (Aug. 28, 2018).
- 5 IRS response to TAS information request (Nov. 1, 2018).
- 6 A false positive occurs when a system selects a legitimate return and delays the refund past the prescribed review period. See IDT and IVO Performance Report, 19, 32 (Oct. 10, 2018).

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Although the fraud detection systems protected about \$7.6 billion in revenue between January 1 and September 30, 2018, they also delayed the processing of almost \$20 billion in legitimate refunds.

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released the refund—in addition to a two-week screening time prior to selection—for a total of about four weeks. The IRS refers to this 64 percent figure as the “operational performance rate” (OPR).<sup>7</sup>

While the National Taxpayer Advocate is very supportive of the IRS’s goal of detecting and mitigating refund fraud, she remains concerned about the fraud detection systems’ high FPR, long processing times, and unwieldy processes that are aggravated by outdated systems.<sup>8</sup> More specifically, we have identified the following issues pertaining to the IRS’s fraud detection systems:

- The IRS does not capture all the information necessary to evaluate the accuracy and efficiency of its non-IDT and IDT refund fraud programs, and the information that it does track reveals significant delays in refunds due a large number of legitimate taxpayers.
- Factors contributing to high FPRs and refund processing delays include the fraud detection systems’ weekly check for third-party information, the IRS’s failure to consider if revenue lost is truly at risk for a selected return, and the barriers taxpayers face in authenticating their identity.
- The Electronic Fraud Detection System (EFDS) contributes to long processing times because it lacks systemic verification capabilities.
- The high FPR and long delays resulted in a 287 percent increase in TAS Pre-Refund Wage Verification cases between January 1 and September 30, 2018, when compared to the same time period in the prior year. Further, in nearly half of the cases closed between January 15 and June 30, 2018, taxpayers ultimately received the refunds originally claimed on their returns.<sup>9</sup>

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7 The IRS defines the Operational Performance Rate (OPR) as returns that are selected and not released by the pre-wage verification program within two weeks of selection. As discussed below, the National Taxpayer Advocate believes the OPR is not an accurate measure of the post-screening/selection False Positive Rate (FPR).

8 See, e.g., National Taxpayer Advocate 2016 Annual Report to Congress 151-160; National Taxpayer Advocate 2015 Annual Report to Congress 45-55, 180-187; National Taxpayer Advocate 2014 Annual Report to Congress, vol. 2, 44-90; National Taxpayer Advocate 2013 Annual Report to Congress 75-83; National Taxpayer Advocate 2012 Annual Report to Congress 42-67, 95-110; National Taxpayer Advocate 2011 Annual Report to Congress 48-73; National Taxpayer Advocate 2009 Annual Report to Congress 307-317; National Taxpayer Advocate 2008 Annual Report to Congress 79-94; National Taxpayer Advocate 2007 Annual Report to Congress 96-115; National Taxpayer Advocate 2005 Annual Report to Congress 25-54, 180-191; National Taxpayer Advocate 2004 Annual Report to Congress 133-136; National Taxpayer Advocate 2003 Annual Report to Congress 175-181.

9 Data obtained from Taxpayer Advocate Management Information System (TAMIS) (Feb. 1, 2018, Mar. 1, 2018, Apr. 1, 2018, May 1, 2018, Jun. 1, 2018, and Jul. 1, 2018).

## ANALYSIS OF PROBLEM

### Background

The IRS's efforts to detect and prevent refund fraud is managed by the RIO of the W&I, which oversees both the TPP (IDT refund program) and the WVP (non-IDT refund program).<sup>10</sup>

In the early days of its fraud detection program, the IRS relied solely on EFDS for detecting and preventing fraud detection.<sup>11</sup> However, EFDS's numerous inefficiencies impeded its ability to keep pace with the rapidly changing world of fraud.<sup>12</sup> In 2017, the IRS retired EFDS for fraud detection purposes; however, EFDS still remains a critical part of the IRS's fraud detection program.<sup>13</sup> Two of the most significant EFDS components still in use are the final case selection function and the case management function. The outdated EFDS case management function poses significant problems for taxpayers and is further discussed below.

The IRS relies primarily on two systems to detect and prevent fraud: the DDb to detect IDT, and the RRP to detect IDT *and* non-IDT.<sup>14</sup> The DDb contains filters which are comprised of rules that are binary in nature, (*i.e.*, if the rule is broken, the return will be selected for further analysis; if the rule is not broken, the return will continue through normal processing).

The RRP, on the other hand, contains filters which are comprised of both rules and models.<sup>15</sup> The IRS uses the RRP rules and models in a variety of ways:

- **Predictive models.** The IRS develops many different models that help detect emerging fraud, outliers, and inconsistent, or suspicious behavior of taxpayers filing refund claims. These models also mine data and help IRS seek out patterns predictive of IDT and other refund fraud. For example, a model may use a combination of existing variables from the 1040 individual tax return, such as tax credits or income claimed.<sup>16</sup>
- **Business rules.** RRP contains over 1,000 rules (a “yes” or “no” outcome) developed by the IRS to flag returns for evidence of anomalous behavior. For example, RRP uses a business rule to distinguish between returns for which it has received an associated Form W-2, *Wage and Tax Statement (W-2)*, from those which it has not.<sup>17</sup>

10 See IRM 25.25.6.1.1, *Background* (Apr. 11, 2018); IRM 25.25.6.1 (1) and (3), *Program Scope and Objectives* (Apr. 11, 2018); and IRM 25.25.3.1(1), *Program Scope and Objectives* (May 10, 2018). For purposes of this Most Serious Problem, we have used “TPP” and “IDT refund fraud program” interchangeably, as well as the terms, “pre-refund wage verification program” and “non-IDT refund program.”

11 In 1994, the IRS installed the Electronic Fraud Detection System (EFDS) system to identify questionable and potentially fraudulent returns. See Treasury Inspector General for Tax Administration (TIGTA) Report Ref. No. 2017-20-080, *The Return Review Program Increases Fraud Detection; However, Full Retirement of the Electronic Fraud Detection System Will Be Delayed* 7 (Sept. 25, 2017).

12 *Id.*

13 There are 11 EFDS components that remain in effect and will likely not be retired in the near future. See TIGTA Report Ref. No. 2017-20-080, *The Return Review Program Increases Fraud Detection; However, Full Retirement of the Electronic Fraud Detection System Will Be Delayed* 7 (Sept. 25, 2017).

14 IRM 25.25.6.1.7(1), *Taxpayer Protection Program Overview* (Aug. 28, 2018); IRM 25.25.3.1(1), *Program Scope and Objectives* (May 10, 2018).

15 IRS response to TAS information request (Aug. 3, 2018). RRP models were activated in 2016 for IDT fraud, and in 2017 for non-IDT fraud. RRP models had to be built from the ground up because EFDS and RRP run on two separate, incompatible platforms. Beginning in Filing Season 2019, nearly all of the models that were in EFDS will now be in RRP.

16 GAO Report, Ref. No. GAO-18-544, *Tax Fraud and Noncompliance: IRS Could Further Leverage the Return Review Program to Strengthen Tax Enforcement* 12 (July 2018).

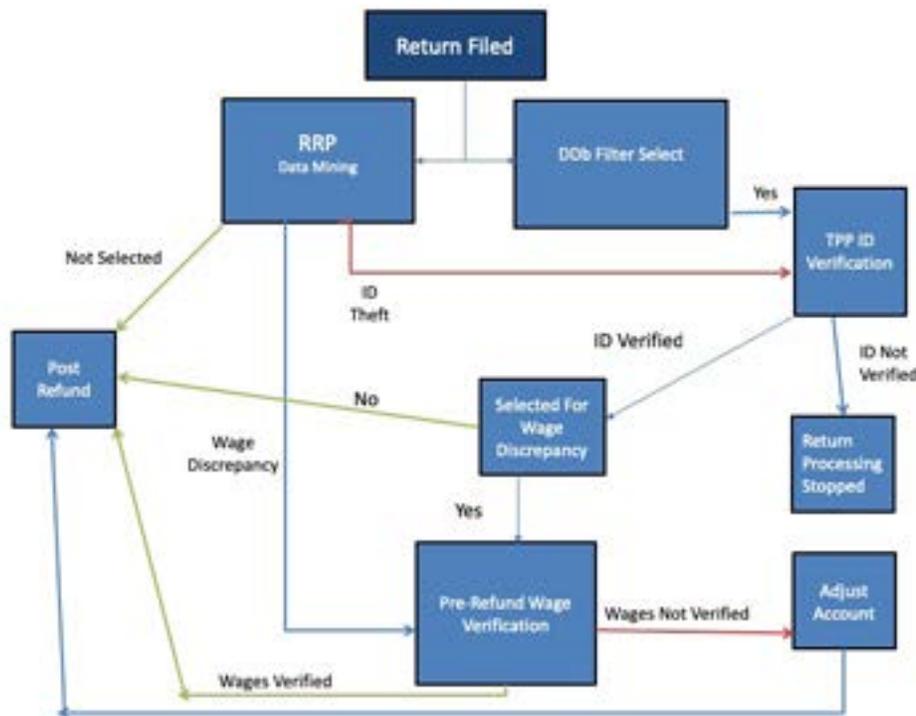
17 *Id.*

- Clustering.** RRP uses a tool that reveals patterns and relationships in masses of data, which allows the system to identify clusters of returns that share traits predictive of deceitful schemes and refund fraud. For example, the IRS could potentially use clustering to identify groups of returns that share the same geographic location, among other traits.<sup>18</sup>

Once the models complete their analysis using the techniques listed above, each return is given a score. The risk score is then fed into RRP filters, which will select returns based on whether the score exceeds a specified threshold, while considering other information in the system. If the score exceeds the threshold and other conditions are met, the return will be routed to either the TPP or WVP, whichever is most appropriate.

Figure 1.5.1 provides a simplified flow chart of the complicated processes the IRS uses to screen returns where a refund has been claimed and IDT or non-IDT refund fraud is suspected.

**FIGURE 1.5.1, Flow Chart of Refund Return Screening for Identity Theft and Non-Identity Theft Refund Fraud**



When a taxpayer’s return is sent to the TPP process, the IRS will ask the taxpayer to authenticate his or her identity either over the phone, online, or by visiting a Taxpayer Assistance Center (TAC).<sup>19</sup> When taxpayers are sent to the pre-refund wage verification process, the information on their returns will be matched with third-party information provided by their employer(s) and payer(s). Beginning in Filing Season (FS) 2017, employers and most other payers were required to submit third-party reporting

18 GAO Report, Ref. No. GAO-18-544, *Tax Fraud and Noncompliance: IRS Could Further Leverage the Return Review Program to Strengthen Tax Enforcement* 12 (July 2018).

19 IRM 25.25.6.1.7, *Taxpayer Protection Program Overview* (Aug. 28, 2018). International taxpayers can mail in documentation to authenticate their identity. Letter 5447C, *Potential Identity Theft during Original Processing; Foreign Address* (Sept. 2018).

information (*Forms W-2 and Forms 1099-MISC-Nonemployee Compensation*) before or on January 31, thus providing the IRS more time to match the wage and tax information reported on the taxpayer's return against information submitted by third parties.<sup>20</sup>

### Selecting Returns as Potentially Fraudulent Significantly Delays Refunds for Many Legitimate Taxpayers, Increasing Taxpayer Anxiety and Causing Financial Hardship

If a return is assigned to TPP, it will generally take about 40 days from the filing of the return for the refund to be issued.<sup>21</sup> From January 1 through June 30, 2018, more than 1.7 million returns were selected into TPP.<sup>22</sup> The timeframe for returns selected into TPP is as follows:

- Submission to selection: 2 days
- Notification to Resolution: 24 days  
(includes selection to notification: 5 days)
- Resolution to Refund: 14 days
  - **Total days = 40**<sup>23</sup>

If a return is assigned to the pre-refund wage verification process, it also takes about 38 days for a refund to be issued from the time the return was submitted.<sup>24</sup> From January 1 through June 30, 2018, approximately 1.2 million returns were selected into the pre-refund wage verification program.<sup>25</sup> The timeframe for returns selected into the pre-refund wage verification program is as follows:

- Submission to Refund Fraud Start: 14 days
- Notification to Resolution: 17 days  
(includes selection to notification: 7 days)
- Resolution to Refund: 7 days
  - **Total Days = 38**<sup>26</sup>

Returns can also be subject to both the TPP and the pre-refund wage verification processes. When returns display characteristics of both IDT and non-IDT fraud, a return will be processed through TPP first. Then, if the taxpayer authenticates his or her identity, the return will then be processed through the pre-refund wage verification process. From January 1 through June 30, 2018, 211,076 returns were selected into both the TPP and the WVPs.<sup>27</sup> On average, taxpayers' refunds were issued 46 days after

20 Section 201 of the Protecting Americans From Tax Hikes (PATH) Act of 2015 amended IRC § 6071 to require that certain information returns be filed by January 31, generally the same date as the due date for employee and payee statements and are no longer eligible for the extended filing date for electronically filed returns under IRC § 6071(b). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 201 (2015).

21 IRS response to TAS information request (Aug. 3, 2018).

22 *Id.*

23 *Id.*

24 *Id.*

25 *Id.*

26 *Id.*

27 Compliance Data Warehouse (CDW) Individual Master File (IMF) Transaction Code 150 History file and CDW IMF Transaction History file (Nov. 20, 2018). About 10 percent of these accounts were manually selected into the TPP and may never have gone to the pre-refund wage program.

the return was submitted.<sup>28</sup> The timeframe for returns selected into both the TPP and pre-refund wage verification programs is as follows:

- Submission to IDT Selection: 2 days
- Notification to IDT Resolution: 24 days  
(includes selection to notification: 5 days)
- IDT Resolution to Refund Fraud Start: 7 days
- Start to Refund Fraud Resolution: 6 days
- Resolution to Refund: 7 days
  - **Total Days = 46**<sup>29</sup>

### The IRS Does Not Capture All the Information Necessary to Evaluate the Accuracy and Efficiency of Its Non-IDT and IDT Refund Fraud Programs, and the Information That It Does Track Reveals Significant Delays in Refunds Due a Large Number of Legitimate Taxpayers

To evaluate the accuracy and efficiency of the non-IDT refund fraud program, the IRS tracks two data points to evaluate how accurate its filters are working in selecting fraudulent returns, and whether legitimate returns selected by the filters are being quickly resolved. These data points are the FPR and the operational performance rate.

**False Positive Rate:** This data point is the percentage of legitimate returns selected by the IRS as potentially fraudulent, divided by the total number of returns selected by the IRS as potentially fraudulent.

**Example:** The IRS selected 100 returns as potentially fraudulent. Eighty of these returns turned out to be legitimate. Therefore, to determine the false positive rate, divide 80 by 100, which equals 80 percent.

**Operational Performance Rate:** The IRS's current formula for this rate is the false positive rate discounting those returns the IRS confirmed as legitimate within two weeks of selection (*i.e.*, no more than four weeks from filing, including the two weeks the IRS has to decide if the return should be selected as potentially fraudulent). Specifically, the OPR retains the same denominator as the FPR (the total number of returns selected by the IRS), but the numerator is decreased by the number of returns that the IRS clears as legitimate within two weeks of selection.

**Example:** The IRS selected one hundred returns, with 80 returns determined to be legitimate (FPR). Twenty of these 80 legitimate returns were resolved within two weeks of selection (four weeks total). Thus, the OPR is 60 percent [(80 minus 20)/100 = 60 percent].

These data points are very useful in determining how this program impacts taxpayers but in order to fully capture that impact, one other data point should be added. This is a variation on the OPR. For purposes of this discussion, it will be referred to as the "Operational FPR".

28 CDW IMF Transaction Code 150 History file and CDW IMF Transaction History file (Nov. 20, 2018).

29 *Id.*

**Operational FPR:** This data point is the ratio of the legitimate returns resolved after the four-week period (the numerator) and *the number of returns left after the four-week period* (the denominator).

**Example:** The IRS selected 100 returns, and it determined 80 were legitimate. Twenty of the 80 legitimate returns were resolved within two weeks of selection. That means the “Operational FPR” would be 75 percent [(80 minus 20)/(100 minus 20) = 75 percent].

This formula is a more accurate depiction of the number of legitimate returns that took more than two weeks to be resolved from the time of selection than the OPR, because the numerator and denominator mirror one another. Specifically, both numbers exclude the number of returns resolved within two weeks of selection. On the other hand, the OPR does not exclude the number of returns resolved within two weeks of selection from the formula’s denominator, which distorts the percentage and gives an inaccurate appearance of improved performance. In fact, when TAS Research applied the above-discussed formula for Operational FPR and excluded the number of returns resolved within two weeks of selection from both the numerator and the denominator, it found that the Operational FPR is 77 percent.<sup>30</sup>

These three data points (FPR, OPR, and Operational FPR) will assist the IRS in identifying problems and finding solutions (*i.e.*, do the fraud detection filters need to be refined, or is there a need for additional staffing to resolve the selected cases faster?). More specifically, it will tell the IRS the following:

- (1) Whether the IRS is quickly resolving the legitimate returns on the front end; or
- (2) Whether the IRS is *not* quickly resolving the legitimate returns on the front end but rather has a very high number of legitimate returns that have slipped through the four-week period and thus are creating both taxpayer and IRS burden.

Therefore, these data points will assist the IRS in determining whether it is quickly resolving these issues so they don’t create taxpayer burden, generate phone calls to the IRS, or create TAS cases. When analyzing the FPR and OPR for the non-IDT refund fraud program during FY 2018, it is clear that the program affected a large number of taxpayers who filed legitimate returns and whose refunds were delayed more than four weeks beyond the date of filing. As mentioned earlier, the FPR for non-IDT refund fraud was 81 percent from January 1 through October 3, 2018.<sup>31</sup> For the same time period, the non-IDT refund fraud program had an OPR of 64 percent of returns selected into the program that were legitimate even though more than two weeks elapsed from the time of selection until the refund was released. As discussed, this figure understates the number of legitimate returns that were delayed beyond two weeks from the time of selection.<sup>32</sup> In 2018, many more taxpayers were impacted by these delays than in past years as non-IDT refund fraud filters selected in excess of one million returns from January 1 through October 3, 2018, a roughly 400 percent increase when compared to the same time period last year.<sup>33</sup>

30 TAS used the following formula to reach the 77 percent figure: Selections: 1,312,439. FPR = 63 percent (calculated (826,837/1,312,439)). Fraud Detection rate (refile rate): 81 percent (calculated (1,063,076/1,312,439)). The numerator of the “Operational FPR” would be 826,837. The denominator of the “Operational FPR” calculation = 1,312,439 minus 236,239 (the number of returns cleared within two weeks) = 1,076,200. Therefore, the “Operational FPR” then equals 826,837/1,076,200 = 77 percent.

31 IDT & IVO Selections Performance Report 32 (Oct. 10, 2018).

32 *Id.*

33 *Id.*

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When TAS Research excluded the number of returns resolved within two weeks of selection from both the numerator and the denominator, it found that the “Operational False Positive Rate” is 77 percent.

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The IDT refund fraud program’s FPR was lower than that of the non-IDT refund fraud program but was still well above 50 percent at 63 percent.<sup>34</sup> Unlike the non-IDT refund fraud program, the IDT refund fraud program does not track an OPR. This is because IDT processing is quite different than non-IDT processing. When the return is selected for possible IDT, processing is suspended, and a letter is sent to the taxpayer asking him or her to authenticate his or her identity. Thus, time must be allowed for the letter to be received by the taxpayer, and the taxpayer must take action to authenticate his or her identity for return processing to continue so that the refund can be released.

Conversely, the release of selected non-IDT refunds does not rely on the taxpayer to take any action. Despite these differences, it is imperative that the IDT refund fraud program track the number of cases that take more than a specified period of time to be resolved. It is reasonable that the IDT program would use different criteria to establish this data point. Although the criteria might vary from that of the non-IDT refund fraud program, the formula applied should be similar to the Operational FPR described above. Further, the IRS should consider conducting a study to identify why taxpayers do not authenticate more quickly.

These figures, the non-IDT and IDT refund fraud FPRs, and the OPR for non-IDT refund fraud, albeit limited in the information they provide, illustrate that these programs select too many legitimate returns, and take too long to release the refunds. A false positive rate of around 50 percent is generally accepted among those in the private sector.<sup>35</sup> With current FPRs of 81 and 63 percent, there is plenty of opportunity for the IRS to improve its refund fraud filters, without jeopardizing revenue protection.<sup>36</sup>

### **Factors Contributing to High False Positive Rates and Refund Processing Delays Include the Fraud Detection Systems’ Weekly Check for Third-Party Information, the IRS’s Failure to Consider If Revenue Lost Is Truly at Risk for a Selected Return, and the Barriers Taxpayers Face in Authenticating Their Identity**

For non-IDT refund fraud, refunds associated with returns selected by a filter are generally frozen until the taxpayer’s employer or payer provides third-party data to the IRS or Social Security Administration (SSA), which forwards the information to the IRS. Once the taxpayer’s third-party information is posted, it can be matched with information on the taxpayer’s return, and the refund will be released. However, this process is dependent upon employers’ timely submission of the required information to the SSA or payers’ timely submission to the IRS. For FY 2018, the IRS received 42 percent of expected employer/employee documentation on or by February 5, representing 43 percent of employee information documents.<sup>37</sup>

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34 IDT & IVO Selections Performance Report 32 (Oct. 10, 2018).

35 *Fraud and False Declines: Fighting the Downward Spiral with Collaboration*, (April 28, 2017), <https://www.thepayers.com/expert-opinion/fraud-and-false-declines-fighting-the-downward-spiral-with-collaboration/768755>.

36 *Id.*

37 *Id.* at 40.

Although employers' late submissions of employee information delay the process, the IRS can take additional steps to verify returns even without an employer's submission. For example, the IRS could review the employer's history and determine if there is a pattern of submitting employee information late. If so, and the information on the return is largely consistent with prior year returns, the IRS could presume the return is legitimate and release the refund.

Another issue regarding missing wage information is the frequency at which IRS systems check for the posting of this information, which was checked weekly during FS 2018, instead of daily. Thus, a fraud detection filter may select the return because there is no third-party information available to verify the return. However, the IRS may receive the employer information within a day or two of selecting the return, but the IRS would not be aware that it received that third-party information for at least a week due to IRS systems weekly check for third-party information. For the 2019 filing season, the IRS has made adjustments to several of its filters to systemically check for the posting of third-party information daily instead of weekly.

Other examples where enhancements can be made include releasing returns, particularly if the third-party information is either inconsequential to the refund or would result in a larger refund to the taxpayer. For instance, TAS has handled cases where the return was held because third-party information did not match the information on the return, yet the third-party information would only have served to increase the refund amount.<sup>38</sup> When the return is being selected due to a mismatch between the information on the return and the third-party information, refund fraud systems should be developed to conduct a refund analysis and, if the third-party information would either have no impact on the amount of the refund or would increase the amount of the refund, the refund should be released immediately. Simple adjustments to the selection process such as these could very well prevent taxpayers from being selected into the pre-refund wage verification process, or could expedite the release of the return if they are selected. This would allow the IRS to better utilize its resources to verify returns where there is a substantial potential for fraud.

For IDT, the taxpayer is required to authenticate his or her identity either over the phone, online, or in person at a TAC.<sup>39</sup> Since taxpayers' refunds are being delayed, the expectation is that taxpayers would authenticate their identity as quickly as possible. However, the process on average still takes about 40 days.<sup>40</sup> The IRS would be well-advised to follow up with taxpayers who take longer than average to authenticate by inquiring into their reasons for delaying their identity authentication. This information is critical to determine if taxpayers experienced any difficulties authenticating that may be alleviated through changes to IRS procedures. Some possible barriers taxpayers may face when trying to authenticate include difficulty in reaching a customer service representative (CSR) to authenticate their identity over the phone.

Additionally, taxpayers may have difficulty obtaining assistance at a TAC, since generally, TACs will only see taxpayers by appointment.<sup>41</sup> During FS 2018, TACs were overwhelmed with appointments. TAS received complaints that taxpayers were waiting for up to three months to obtain an appointment

38 TAS Systemic Advocacy Management System (SAMS) issues 37230 and 37347.

39 IRM 25.25.6.1.7, *Taxpayer Protection Program Overview* (Aug. 28, 2018).

40 IRS response to TAS information request (Aug. 3, 2018).

41 IRS News Release IR-2016-172, *Tax Preparedness Series: IRS Face-To-Face Help Now by Appointment* (Dec. 20, 2016). IRS response to TAS fact check (Dec. 20, 2016); IRS, *Fact Sheet: Internal Revenue Service Appointment Service Test* (Feb. 26, 2015). The IRS began a pilot during filing season (FS) 2015 whereby taxpayers needed to call for an appointment at 44 sites. The IRS expanded the pilot to more locations during FS 2016, and in November 2016, it completed a transition to appointment-only service at all Taxpayer Assistance Centers (TACs).

in some TACs.<sup>42</sup> Initially, taxpayers selected for possible IDT, who were trying to authenticate their identities at a TAC, could not get appointments until May, after the filing season had concluded.<sup>43</sup> To address this issue, the IRS solicited volunteers from other IRS business units to work at TACs so taxpayers could get appointments to authenticate their identities before the conclusion of the filing season.<sup>44</sup>

### The IRS's Outdated Electronic Fraud Detection System (EFDS) Contributes to Long Processing Times Because It Lacks Systemic Verification Capabilities

One of the new non-IDT filters for FS 2018 selected about 303,000 Earned Income Tax Credit (EITC) and Additional Child Tax Credit (ACTC) returns as potentially fraudulent because no third-party income information had been posted as of February 15, 2018, about two weeks after the January 31 deadline established by law.<sup>45</sup> Once these accounts were selected as potentially fraudulent, the IRS anticipated that the EFDS would be able to release refunds in bulk when income on the return could be verified with third-party information. However, because EFDS does not interact with the IRS system that maintains third-party income information, employees must enter the third-party information into EFDS one document at a time, and then manually release the refunds. What makes this so exasperating is that the IRS has been claiming for more than a decade that it will retire its EFDS in favor of a more modern, sophisticated system.<sup>46</sup> This is just the latest example of how old systems harm taxpayers and create more work for the IRS.<sup>47</sup> The frustration of this delay is compounded by the fact that taxpayers cannot receive information about their refunds that are being held when they call the IRS because IRS

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**Because Electronic Fraud Detection System (EFDS) does not interact with the IRS system that maintains third-party income information, employees must enter the third-party information into EFDS one document at a time, and then manually release the refunds.**

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42 TAS Systemic Advocacy Management System Issue 37305.

43 Memorandum from Director of IRS Field Assistance (Apr. 2, 2018).

44 *Id.* See also Wage & Investment, Business Performance Review 3 (Aug. 2018).

45 IDT and IVO Selection Performance Report (Feb. 28, 2018); *Continued Oversight Over the Internal Revenue Service: Joint Hearing Before the H. Subcomm. on Health Care, Benefits, and Administrative Rules and H. Subcomm. on Government Operations*, 115th Cong. (2018) (statement of Nina E. Olson, National Taxpayer Advocate).

46 See TIGTA Report Ref. No. 2017-20-080, *The Return Review Program Increases Fraud Detection; However, Full Retirement of the Electronic Fraud Detection System Will Be Delayed* 7 (Sept. 25, 2017); see also National Taxpayer Advocate 2016 Annual Report to Congress 109-120 (Most Serious Problem: *Enterprise Case Management (ECM): The IRS's ECM Project Lacks Strategic Planning and Has Overlooked the Largely Completed Taxpayer Advocate Service Integrated System (TASIS) As a Quick Deliverable and Building Block for the Larger ECM Project*).

47 See Legislative Recommendation: *IT Modernization: Provide the IRS with Additional Dedicated, Multi-Year Funding to Replace Its Antiquated Core IT Systems Pursuant to a Plan that Sets Forth Specific Goals and Metrics and Is Evaluated Annually by an Independent Third Party*, *infra*; National Taxpayer Advocate 2016 Annual Report to Congress 109-120 (Most Serious Problem: *Enterprise Case Management (ECM): The IRS's ECM Project Lacks Strategic Planning and Has Overlooked the Largely Completed Taxpayer Advocate Service Integrated System (TASIS) As a Quick Deliverable and Building Block for the Larger ECM Project*).

CSRs do not have access to the EFDS case management system for the WVP.<sup>48</sup> The IRS could give CSRs the ability to view information about why the return was flagged, which in turn, would help taxpayers resolve issues more quickly.<sup>49</sup>

**The High FPR and Long Delays Resulted in a 287 Percent Increase in Taxpayer Advocate Service Pre-Refund Wage Verification Cases From January 1 through September 30, 2018, When Compared to the Same Time Period in the Prior Year, and in Nearly Half of the TAS Cases Closed Between January 15 and June 30, 2018, Taxpayers Ultimately Received the Refunds Originally Claimed on Their Returns**

The increase in returns being selected as potentially fraudulent, the high FPRs, and the large number of selected returns being delayed beyond two weeks, have all contributed to a significant increase in TAS's case receipts.

**FIGURE 1.5.2, TAS Pre-Refund Wage Verification Hold Receipts**

TAS Pre-Refund Wage Verification Hold Monthly Receipts for 2017 and 2018 (January through September)										
Year	January	February	March	April	May	June	July	August	September	Total
2017	692	1,989	4,169	2,070	2,017	1,768	1,487	1,358	882	16,432
2018	712	3,628	13,361	10,056	9,223	5,811	7,797	7,786	5,263	63,637

As shown in Figure 1.5.5, TAS pre-refund wage verification refund hold case receipts from January 1 through September 30, 2018, increased from 16,432 to 63,637 cases, or 287 percent, when compared to the same period last year.<sup>50</sup> To evaluate this significant increase, TAS research analyzed all the non-IDT refund fraud cases that were closed in TAS inventory between January 15 and June 30, 2018, that were related to issues arising out of taxpayer's tax year 2017 returns. During this time period, TAS closed 42,120 cases, and out of this number, 18,816 or 45 percent of the taxpayers received the refund that was originally shown on their return.<sup>51</sup> Fifty-five percent of the 18,816 cases that were identified by the RRP system were selected solely by one filter.<sup>52</sup> These findings are consistent with the high 81 percent FPR and the 77 percent for Operational FPR for non-IDT refund fraud. It further illustrates how a problem with one single filter can affect thousands of taxpayers who file legitimate returns. The National Taxpayer Advocate urges the IRS to work with her and her staff to review the findings of TAS's research to prevent a similar situation from occurring in future filing seasons.

48 IRM 21.5.6.4.35.3.1, -R Freeze Phone Procedures for Accounts with Integrity and Verification Operations (IVO) Involvement (Jun. 15, 2018); *Continued Oversight Over the Internal Revenue Service: Joint Hearing Before the H. Subcomm. on Health Care, Benefits, and Administrative Rules and H. Subcomm. on Government Operations*, 115th Cong. (2018) (statement of Nina E. Olson, National Taxpayer Advocate).

49 Notes from National Taxpayer Advocate Meeting with SAS (Apr. 25, 2018).

50 Data obtained from TAMIS (Feb. 1, 2017; Oct. 1, 2017; Feb. 1, 2018; Oct. 1, 2018).

51 CDW IMF Transaction Code 150 History file and CDW IMF Transaction History file (Nov. 20, 2018). The 18,816 included cases where the refund issued was the same amount as the refund shown on the return, less a math error adjustment.

52 Match of TAMIS data to RRP selection file, 2018 IWW Selection, provided by the IRS.

## CONCLUSION

The National Taxpayer Advocate acknowledges the importance of reducing tax fraud and recognizes that robust fraud detection systems are required to meet this objective. However, when these systems routinely have FPRs above 60 percent, they harm legitimate taxpayers and create unnecessary work for the IRS. Equally important is the IRS's efforts in designing a process that can quickly analyze returns and release refunds to legitimate taxpayers.

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Calculate an "Operational FPR" in addition to the FPR and OPR for non-IDT accounts.
2. Develop criteria to be used in measuring OPR for IDT accounts.
3. Conduct a study to determine why it takes some taxpayers longer to authenticate their identities and what barriers they may encounter when attempting to do so.
4. Design the refund fraud system to consider if applying the third-party information to the return would actually result in a larger refund when there is a mismatch between third-party information and the information on a taxpayer's return.
5. Request from outside vendors information on ways to improve the FPR, along with proposals to determine the factors that are contributing to high FPRs.
6. Establish a maximum acceptable FPR goal within industry accepted standards and an actionable timeline to achieve that goal, based on the information and proposals received from outside vendors.

**MSP #6**      **IMPROPER EARNED INCOME TAX CREDIT PAYMENTS: Measures the IRS Takes to Reduce Improper Earned Income Tax Credit Payments Are Not Sufficiently Proactive and May Unnecessarily Burden Taxpayers**

### RESPONSIBLE OFFICIALS

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### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Privacy*
- *The Right to a Fair and Just Tax System*

### DEFINITION OF PROBLEM

When the IRS allows a taxpayer's erroneous claim of the earned income tax credit (EITC), it makes an "improper payment."<sup>2</sup> The IRS estimates that 25 percent of the claimed EITC credits it allowed in fiscal year (FY) 2018 were improper payments.<sup>3</sup> The IRS's attempts to reduce the EITC improper payment rate have met with limited success.<sup>4</sup> While she recognizes the importance of tracking and minimizing improper payments, the National Taxpayer Advocate is concerned that the focus on "a number" masks both the successes and challenges in improving EITC compliance. Specifically:

- The effect of any statutory measures intended to reduce the EITC improper payment rate are not reflected in the IRS's estimate for years;<sup>5</sup>
- The IRS lost an exemption that allowed it to reduce the improper payment estimate by improper payments it recovered;<sup>6</sup>

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 See Improper Payments Information Act of 2002 (IPIA), Pub. L. No. 107-300 § 2(d)(A), 116 Stat. 2350, 2351 (2002), defining an improper payment as "any payment that should not have been made or that was made in an incorrect amount (including overpayments and underpayments)."

3 Department of Treasury, Agency Financial Report (AFR) Fiscal Year (FY) 2018 194 (Nov. 2018), estimating an earned income tax credit (EITC) improper payment rate of 25.06 percent.

4 As discussed below, since FY 2010 the improper payment rate has fluctuated but has never been estimated as less than 22.8 percent.

5 See, e.g., Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title II, § 201 (a) and (b), 129 Stat. 2242, 3076 (2015) (hereinafter PATH Act), codified at IRC §§ 6071(c) and 6402 (m), discussed below.

6 See Government Accountability Office (GAO), GAO 18-377, *Improper Payments, Actions and Guidance Could Help Address Issues and Inconsistencies in Estimation Processes*, App'x IV, Comments from the Internal Revenue Service (May 2018). When recovered payments are taken into account, the FY 2018 improper payment rate is 23.41 percent rather than 25.06 percent. AFR, FY 2018, 194 n. 4 (Nov. 2018).

- The improper payment rate does not take into account that for every dollar of EITC improper payments, 40 cents of EITC went unclaimed by taxpayers who appear to be eligible for the credit;<sup>7</sup>
- A principal cause of the EITC improper payment rate is the complexity of the rules for claiming EITC, yet the IRS does not provide a dedicated telephone help line available year-round for taxpayers to call with questions about EITC;<sup>8</sup>
- EITC improper payments are a relatively small portion of the tax gap;<sup>9</sup> and
- The EITC program costs less to administer than other non-tax benefit programs and has higher participation rates.<sup>10</sup>

In attempting to address improper payments, the IRS may unnecessarily burden taxpayers.<sup>11</sup> The IRS could gain insight from TAS research study results and the proactive approaches other tax administrations have adopted in their interactions with taxpayers.<sup>12</sup>

## ANALYSIS OF PROBLEM

### Background

The current statutory framework pertaining to improper payments originated in 2002, when Congress required the heads of executive agencies, pursuant to guidance from the Office of Management and Budget (OMB), to identify programs and activities susceptible to significant improper payments and report to Congress the estimated amount of improper payments.<sup>13</sup>

7 Treasury Inspector for Tax Administration (TIGTA), Ref. No. 2018-IE-R004, *The Internal Revenue Service Should Consider Modifying the Form 1040 to Increase Earned Income Tax Credit Participation by Eligible Tax Filers* at 2 (Apr. 2, 2018).

8 The rules for claiming the child tax credit (CTC) are similarly complex. See IRC § 24. The importance of the CTC was magnified by legislation that increased the amount of the credit from \$1,000 to \$2,000, for tax years 2018-2025. See Pub. L. No. 115-97, § 1022(a), 131 Stat. 2054, 2073 (2017). The National Taxpayer Advocate has recommended that Congress consolidate numerous family status provisions into a new Family Credit and require the IRS to establish a dedicated, year-round toll-free help line staffed by IRS personnel to respond to questions about the credit. National Taxpayer Advocate 2016 Annual Report to Congress 329 (Legislative Recommendation: *Restructure the Earned Income Tax Credit and Related Family Status Provisions to Improve Compliance and Minimize Taxpayer Burden*).

9 As discussed below, EITC misreporting constitutes six percent of the gross tax gap and ten percent of the tax gap attributable to income misreporting by individuals.

10 As discussed below, the cost of administering the EITC program is around one percent of benefits delivered, with a participation rate of 79 percent.

11 See below for a discussion of the IRS's pursuit of extended math error authority and its imposition of two-year bans on claiming EITC.

12 See, e.g., Organisation for Economic Co-operation and Development (OECD), *The Changing Tax Compliance Environment and the Role of Audit* 19, 23-26 (2017), [https://www.oecd-ilibrary.org/taxation/the-changing-tax-compliance-environment-and-the-role-of-audit\\_9789264282186-en](https://www.oecd-ilibrary.org/taxation/the-changing-tax-compliance-environment-and-the-role-of-audit_9789264282186-en) (last visited Nov. 26, 2018).

13 IPIA, Pub. L. No. 107-300, 116 Stat. 2350 (2002), as amended. Current Office of Management and Budget (OMB) guidance consists of OMB M-15-02, Appendix C to Circular No. A-123, *Requirements for Effective Estimation and Remediation of Improper Payments* (2014), as modified by OMB M-18-20 Transmittal of Appendix C to OMB Circular A-123, *Requirements for Payment Integrity Improvement* 25 (June 26, 2018). This guidance implements requirements from the following: (1) IPIA; (2) the Improper Payments Elimination and Recovery Act of 2010 (IPERA), Pub. L. No. 111-204, 116 Stat. 2350 (2010); (3) the Improper Payments Elimination and Recovery Improvement Act of 2012 (IPERIA), Pub. L. No. 112-248, 126 Stat. 2390 (2012); and (4) Executive Order 13520 *Reducing Improper Payments* (Nov. 20, 2009). The 2014 OMB guidance defined "significant improper payments" as gross annual improper payments (*i.e.*, the total amount of overpayments and underpayments) in the program exceeding (1) both 1.5 percent of program outlays and \$10,000,000 of all program or activity payments made during the fiscal year reported or (2) \$100 million (regardless of the improper payment percentage of total program outlays). EITC underpayments are defined as the amount of EITC disallowed by the IRS in processing that should have been allowed, as determined by the National Research Program (NRP) examination. AFR, FY 2013 at 206. Thus, unclaimed EITC amounts are not underpayments and are not included in the calculation of improper payments.

A 2009 Executive Order and 2012 legislation required OMB, among other things, to designate and exercise additional oversight with respect to “high priority” programs.<sup>14</sup> Because EITC has been so designated, the IRS must provide, for inclusion in the Department of the Treasury’s annual Agency Financial Report (AFR), not only the rate and amount of improper EITC payments, but additional information such as the root causes of the improper payments. Pursuant to OMB guidance issued in June 2018, the IRS will be required, among other things, to estimate improper payments attributable to other refundable tax credit programs, such as the Affordable Care Act Premium Tax Credit, the Child Tax Credit, and, potentially, the American Opportunity Tax Credit.<sup>15</sup>

In addition to reporting EITC improper payment rates over the years, the IRS has conducted an array of studies relating to erroneous EITC claims, particularly when funds were appropriated for such research.<sup>16</sup> Recent IRS initiatives include studies on the effectiveness of “soft” notices, discussed below.

### EITC Improper Payments Estimates, Based on Audits of Tax Years Four Years in the Past, Do Not Reflect the Most Recent Remedial Measures or Take Into Account Unclaimed EITC

As part of its National Research Program (NRP), each year the IRS audits a sample of EITC returns and uses data from the audits to estimate the rate of improper EITC payments for that audit year.<sup>17</sup> The *rate* derived from the NRP data is then used to estimate the *amount* of improper payments for the current year. The most recent year for which NRP data is available is 2014. The total amount of EITC claimed on 2014 returns was divided into the amount which, according to NRP audits, were improper payments to arrive at an improper payment *rate* of 25.06 percent.<sup>18</sup> The FY 2018 EITC improper payment *amount* was estimated by multiplying the NRP *rate* (25.06 percent, based on audits of a tax year four years in the past) times the amount of EITC claimed in 2018 (\$73.6 billion) to arrive at \$18.4 billion.<sup>19</sup> This four-year lag between audit outcomes for the tax year that generated the estimated *rate* and the estimated *amount* of improper payments for a given year is a feature of the improper payment estimating process.

14 Executive Order 13520, *Reducing Improper Payments* § 2 (Nov. 20, 2009); IPERIA, § 3. OMB M-18-20 *Transmittal of Appendix C to OMB Circular A-123, Requirements for Payment Integrity Improvement 25* (June 26, 2018) defines high priority programs as those with more than \$2 billion in improper payments in a given year, an increase from the prior threshold of \$750 million.

15 OMB M-18-20 *Transmittal of Appendix C to OMB Circular A-123, Requirements for Payment Integrity Improvement 25* (June 26, 2018). The guidance institutes this requirement with respect to all programs with outlays in excess of \$5 billion, starting in fiscal year 2020. Thus, programs that meet that threshold will also qualify as “high priority” programs. Affordable Care Act (ACA), Premium Tax Credit, and CTC outlays already exceed that threshold, and the American Opportunity Tax Credit outlays, while currently below the threshold, may grow to the threshold amount in the future. IRS response to TAS information request (Aug. 30, 2018).

16 For example, in 1997, Congress authorized a \$716 million appropriation over five years (from FY 1998 to 2002) “for improved application” of the EITC. Balanced Budget Act of 1997, Pub. L. No. 105–33, § 5702, 111 Stat. 251, 648 (1997). Among the studies the IRS conducted was *Compliance Estimates for Earned Income Tax Credit Claimed on 1999 Returns* 13 (Feb. 28, 2002), reporting, e.g., that among known errors, the largest *amount of overclaims* was caused by taxpayers claiming children who were not their qualifying children, most commonly because the residency requirement was not met. The most *frequent* known error was income misreporting.

17 IRS, *Improper Payments Estimates for the Earned Income Tax Credit: Methodology for the Fiscal Years 2010-2013 Update 2* (May 2010) (on file with TAS). EITC overclaims, defined as the difference between the amount of EITC claimed by the taxpayer on his or her return and the amount the taxpayer should have claimed, as determined by the NRP audit, are reported in the Treasury’s AFR as “actual monetary loss to the government.” See, e.g., AFR, FY 2017 at 176 (Nov. 2017).

18 See AFR, FY 2017 at 174 (Nov. 2017), for a description of this methodology (which does not appear in the FY 2018 AFR).

19 AFR, FY 2018 at 194 (Nov. 2018).

Thus, the estimated EITC improper payment rate does not reflect the most recent measures taken by Congress and the IRS to reduce EITC improper payments.<sup>20</sup>

*The IRS Lost Its Exemption From a Reporting Requirement That Allowed It to Reduce Improper Payment Estimates by Recovered Amounts*

In the past, the IRS estimated the improper payment rate by first estimating the gross amount of improper payments, and reducing that amount by the amount of erroneous EITC payments “prevented or recovered.”<sup>21</sup>

This method of computing the EITC improper payment rate was permitted because the IRS had obtained an exemption from the statutory requirement, introduced in 2012, that agencies “include all identified improper payments in the reported estimate, regardless of whether the improper payment in question has been or is being recovered.”<sup>22</sup> The IRS’s temporary exemption was allowed “because the tax system differs from spending programs in that much of the verification and compliance activity for potentially erroneous tax returns takes place after refunds have been issued.”<sup>23</sup> In other words, unlike other benefit programs, EITC does not have a separate application process—the tax return is the application. By design, significant compliance activity occurs after issuance of refunds.

However, the IRS’s exemption was not permanent, and the inconsistency was never resolved by the IRS and OMB.<sup>24</sup> In 2018, the IRS acquiesced to the Government Accountability Office’s recommendation that it change its method of computing improper payments to disregard recovered amounts.<sup>25</sup>

Thus, the improper payment rate used to estimate the amount of improper payments in FY 2018, 25.06 percent, was not reduced by recovered improper payments.<sup>26</sup> The change in the calculation does not reflect a change in taxpayer compliance, but yields a higher improper payment estimate. When recovered improper payments are taken into account, the *rate* used to calculate the amount of improper payments for FY 2018 becomes 23.41 percent.<sup>27</sup> The estimated *amount* of improper payments would thus be 23.41 percent times the amount of EITC claimed on 2018 returns (\$73.6 billion) to arrive at \$17.2 billion (rather than \$18.4 billion).

20 For example, beginning with 2017, the PATH Act imposed a Jan. 31 due date for filing Forms W-2, *Wage and Tax Statement*, Forms W-3, *Transmittal of Wage and Tax Statements*, and any returns or statements required to report nonemployee compensation (such as Forms 1099-MISC, *Miscellaneous Income*), with the Social Security Administration, and required the IRS to delay payment of any refund that includes the EITC or the refundable portion of the CTC until Feb. 15 of each filing year.

21 “Prevented” EITC improper payments are EITC claims that are determined to be erroneous before a refund is paid (these amounts are sometimes referred to as the amount of revenue protected), while “recovered” improper payments are erroneous EITC claims that are paid but later recuperated.

22 IPERIA § 3(b)(2)(D), implemented with OMB M-15-02, Appendix C to Circular No. A-123, *Requirements for Effective Estimation and Remediation of Improper Payments* 18 (2014).

23 GAO, GAO 18-377, *Improper Payments, Actions and Guidance Could Help Address Issues and Inconsistencies in Estimation Processes*, App’x IV, Comments from the Internal Revenue Service (May 2018).

24 *Id.*, noting that “[t]he exemption was intended to be temporary until the IRS and OMB could address outstanding questions related to the appropriate representation of EITC and other refundable tax credit overclaims. However, since none of the discussions with OMB have resulted in any decisions to date, the IRS will update its reporting so that recoveries are no longer included in our estimates.”

25 *Id.*

26 The IRS will continue to take into account “prevented” erroneous payments and will also provide a computation of the EITC improper payments that takes into account recovered erroneous payments for comparison purposes. IRS response to TAS information request (Aug. 30, 2018).

27 AFR, FY 2018 at 194 n. 4 (Nov. 2018).

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The estimated amount of improper payments also does not take into account that many taxpayers who appear to be eligible do not claim Earned Income Tax Credit (EITC). The Treasury Inspector General for Tax Administration estimated that ... for every dollar of EITC improper payments, there were 40 cents of unclaimed EITC.

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*For Every Dollar of EITC Improper Payments, There Were 40 Cents of Unclaimed EITC*

The estimated amount of improper payments also does not take into account that many taxpayers who appear to be eligible do not claim EITC. The Treasury Inspector General for Tax Administration (TIGTA) estimated that in 2014, when the EITC improper payments were estimated to be \$17.7 billion, \$7.3 billion in EITC refunds went unclaimed.<sup>28</sup> In other words, TIGTA estimated that for every dollar of EITC improper payments, there were 40 cents of unclaimed EITC.

Additionally, the improper payment rate does not take into account that EITC, although claimed by the “wrong” taxpayer, may have reached the intended beneficiary, a qualifying child. For example, suppose a taxpayer claims EITC with respect to a qualifying child, A, who is not the taxpayer’s qualifying child. However, the taxpayer’s former spouse could have claimed EITC with respect to A but did not. Thus, allowing EITC claimed by a parent who turns out to be the “wrong” taxpayer could be an improper payment, even though the benefit was only paid once, and was paid with respect to a qualifying child.<sup>29</sup>

Since 2010, EITC estimated improper payment rates have fluctuated between a low of 22.8 percent in 2012 and a high of 27.2 percent in 2014, as shown in Figure 1.6.1.<sup>30</sup>

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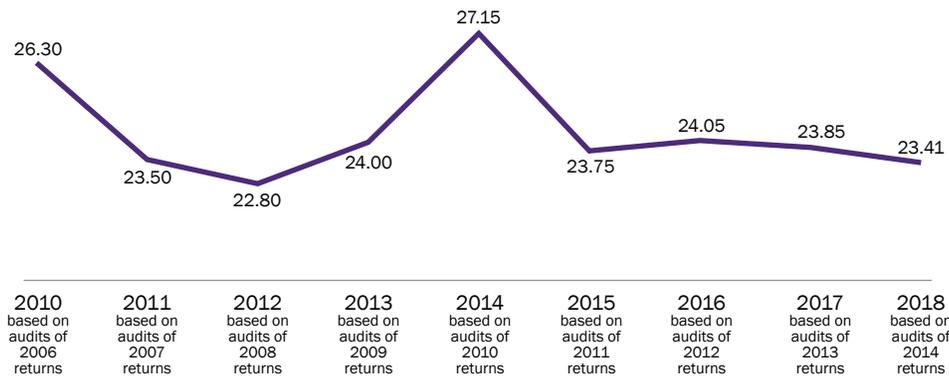
28 AFR, FY 2014 at 201 (Nov. 2014), estimating improper EITC payments of \$17.7 billion; TIGTA, Ref. No. 2018-IE-R004, *The Internal Revenue Service Should Consider Modifying the Form 1040 to Increase Earned Income Tax Credit Participation by Eligible Tax Filers* at 2 (Apr. 2, 2018), estimating that five million potentially eligible taxpayers did not claim approximately \$7.3 billion in EITC refunds on their 2014 returns.

29 The extent to which improper payments occur under these circumstances is not known, but could be developed from NRP data. IRS response to TAS information request (Aug. 31, 2018).

30 See U.S. Dept. of the Treas., AFRs, FYs 2010-2018, <https://home.treasury.gov/about/budget-financial-reporting-planning-and-performance/agency-financial-report>. Until FY 2010, the improper payment rate was expressed as a midpoint between upper and lower bounds. The upper and lower bounds reflected assumptions about whether taxpayers who did not participate in the NRP audits were actually entitled to EITC. Beginning with FY 2010, the rate was expressed as a single rate with confidence intervals, with nonparticipating taxpayers treated as being entitled to EITC at the same rate as those who participated in the NRP audit. However, the AFR continued to report upper and lower bounds through 2014. Figure 1.6.1 depicts the midpoint value for the 2010-2014 and the single point estimate thereafter. For purposes of consistency the FY 2018 value, 23.41 percent, is the one that takes into account recovered amounts.

FIGURE 1.6.1

## Estimated EITC Improper Payment Rates, 2010-2018



### EITC Improper Payments Arise From Complexity of the Rules and Are Not Usually Due to Fraud

The IRS is required to categorize improper payments using one or more of the following root causes: Program Design or Structural Issues; Inability to Authenticate Eligibility; Failure to Verify; Administrative or Process Errors; Medical Necessity; Insufficient Documentation to Determine; and Other.<sup>31</sup> According to the IRS, almost all EITC improper payments (94 percent) are caused by Inability to Authenticate Eligibility: Data Needed Does Not Exist.<sup>32</sup> This category includes cases in which the taxpayer could not substantiate, and the IRS could not confirm:

- That a claimed “qualifying child” met the requirements for that status (49.5 percent of the payments);<sup>33</sup>
- That the taxpayer correctly reported income, mainly self-employment income, not reported to the IRS by third parties (26 percent of the payments);
- That the taxpayer’s return reflected the correct filing status (15 percent of the payments);<sup>34</sup> or

31 See OMB M-15-02 Appendix C to Circular No. A-123, *Requirements for Effective Estimation and Remediation of Improper Payments* 25 (2014). The “inability to authenticate eligibility” root cause is further divided into two sub-categories: (1) inability to access data; and (2) data needed does not exist.

32 AFR, FY 2018 at 196 (Nov. 2017). NRP auditors record the nature of the errors taxpayers made when they erroneously claimed EITC, and the IRS then groups the error according to the “root cause” classification required by OMB. IRS response to TAS information request (Aug. 30, 2018). OMB provides as examples of this type of “root cause:” “the inability to establish that a child lived with a family for a certain amount of time-for the purpose of determining that a family is eligible for a tax credit-because no database exists to do so” and “failing to provide an agency with information on earnings, and the agency does not have access to databases containing the earnings information.” OMB M-15-02, Appendix C to Circular No. A-123, *Requirements for Effective Estimation and Remediation of Improper Payments* 26-27 (2014).

33 Specifically, they do not exist, or the IRS does not have access to, third-party databases that would confirm, at the time of filing: residency; relationship (when a non-parent claims the qualifying child); age (where the claimed child is a full-time student or is disabled); marital status of children claimed; or whether a valid Social Security number (SSN) is also valid for EITC and not issued solely to receive federal benefits. IRS, *Derivation of Improper Payment Root Cause Percentages* 3 (Aug. 2015).

34 Specifically, the IRS cannot confirm when taxpayers who file as heads of household are actually married. IRS, *Derivation of Improper Payment Root Cause Percentages* 3 (Aug. 2015).

- That the taxpayer met other EITC eligibility requirements (three percent of the payments).<sup>35</sup>

However, as Treasury and the IRS acknowledge, a central cause of EITC improper payments is the complexity of the rules and the errors, a cause not captured by the OMB categories.<sup>36</sup> Experience has shown that simplifying the rules can reduce noncompliance.<sup>37</sup>

Moreover, TAS studies demonstrate that taxpayers may not be able to document the claim to the examiner's satisfaction, but the taxpayer may actually be entitled to the claimed EITC (*i.e.*, denial of EITC proves only that the IRS did not accept the claim, not necessarily that the taxpayer was not eligible for the EITC).<sup>38</sup> In addition, taxpayers may be able to demonstrate eligibility for the credit once they receive adequate explanations of what substantiation the IRS requires.<sup>39</sup> To its credit, the IRS has worked with TAS to foster auditors' acceptance of a broader range of substantiating documentation.<sup>40</sup>

As noted above, according to IRS data, when taxpayers erroneously claim EITC with respect to children who were not their qualifying children, the most common error is that the residency requirement was not met.<sup>41</sup> At the urging of the National Taxpayer Advocate, the IRS agreed to allow some audited taxpayers to use affidavits to establish that they met the residency requirement.<sup>42</sup> Tax Year (TY) 2018 returns will be selected for the initiative in 2019, with the audit results known in 2020.<sup>43</sup>

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- 35 Specifically, the IRS cannot independently verify when a valid SSN is not valid for EITC and not issued solely to receive federal benefits. IRS, *Derivation of Improper Payment Root Cause Percentages* 3 (Aug. 2015). Additionally, the IRS attributes 0.5 percent of improper payments to cases in which a taxpayer without qualifying children claimed EITC and the taxpayer could have been claimed as the dependent of another taxpayer, or the taxpayer lived outside the U.S. (the IRS cannot verify whether a taxpayer could have been claimed as a dependent by another taxpayer or the length of time a taxpayer lived abroad).
- 36 AFR, FY 2014 at 140, noting that "Treasury and IRS analyses, as well as audits by the GAO and TIGTA, have consistently found that payment errors for EITC and other tax credit programs are largely attributable to the statutory design and complexity of the credits within the tax system, and not rooted in internal control weaknesses, financial management or financial reporting deficiencies." See also Robert Greenstein, John Wancheck, and Chuck Marr, Center on Budget and Policy Priorities, *Reducing Overpayments in the Earned Income Tax Credit*, updated Feb. 20, 2018, noting that "What the Internal Revenue Service (IRS) refers to as the EITC's 'improper payment rate' is not a 'fraud' rate and shouldn't be characterized as such."
- 37 See, e.g., Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), Pub. L. 107-16, § 303, 115 Stat. 38 (2001), modifying and clarifying tiebreaker rules (*i.e.*, rules for determining, when an individual is the qualifying child of more than one taxpayer, which taxpayer is entitled to the credit), and IRS, *Compliance Estimates for the Earned Income Tax Credit Claimed on 2006-2008 Returns* 20 (Aug. 2014) comparing the "negligible" incidence of tie-breaker errors, comprising one to two percent of all overclaims, and the 17 percent rate found in the 1999 Compliance Study, and noting "this difference reflects the change in tiebreaker rules that were part of EGTRRA and took effect in 2002."
- 38 See, e.g., National Taxpayer Advocate 2004 Annual Report to Congress, vol. 2 i, *EITC Audit Reconsideration Study*, demonstrating that 43 percent of taxpayers who sought reconsideration of audits that disallowed the EITC in whole or in part received additional EITC as a result of the audit reconsideration.
- 39 See National Taxpayer Advocate 2012 Annual Report to Congress, vol. 2 74, (Research Study: *Study of Tax Court Cases In Which the IRS Conceded the Taxpayer was Entitled to Earned Income Tax Credit (EITC)*), discussing a TAS study of a random sample of cases in which the IRS denied a claim for EITC but conceded the issue after the taxpayer petitioned the Tax Court for review. In most cases, taxpayers repeatedly seek information from the IRS before they file their Tax Court petitions. They evidently do not receive from examiners adequate explanations of what documents are needed, but they do receive adequate explanations once they have exited the examination phase of the case.
- 40 See Internal Revenue Manual (IRM) 4.19.14-1, *Examples of Acceptable Documentation for EITC claims (not all-inclusive)* (July 29, 2016) listing various "new" documents for auditors to consider, such as paternity test results, eviction notices, and statements from homeless shelters. However, anecdotal evidence, such as comments from low income taxpayer clinicians, indicates that some auditors still request unreasonable amounts of documents from taxpayers in support of their EITC claims.
- 41 IRS, *Compliance Estimates for Earned Income Tax Credit Claimed on 2006-2008 Returns* 22 (2014).
- 42 National Taxpayer Advocate 2017 Annual Report to Congress 141, 149 (Most Serious Problem: *The IRS Continues to Make Progress to Improve Its Administration of the EITC, But It Has Not Adequately Incorporated Research Findings that Show Positive Impacts of Taxpayer Education on Compliance*).
- 43 IRS response to TAS information request (Sept. 26, 2018), noting that the IRS will compare prior audit results to audits of taxpayers who received the affidavits.

### EITC Improper Payments Are a Relatively Small Portion of the Tax Gap, While the EITC Program Costs Less to Administer Than Other Non-Tax Benefit Programs and Has Higher Participation Rates

The overall amount of true tax liability that is not paid voluntarily and timely is referred to as the gross tax gap.<sup>44</sup> The most recent estimate of the gross tax gap, based on data for tax years 2008-2010, is \$458 billion. A portion of the gross tax gap, \$264 billion, or 58 percent, is attributable to income misreporting by individual taxpayers.<sup>45</sup> The three largest components of this \$264 billion consist of:

- \$125 billion, or 47 percent, attributable to business income misreporting;<sup>46</sup>
- \$64 billion, or 24 percent, attributable to misreporting of non-business income;<sup>47</sup> and
- \$40 billion, or 15 percent, attributable to misreporting of credits.<sup>48</sup>

Of the \$40 billion in misreported credits, \$26 billion is attributable to EITC misreporting.<sup>49</sup>

Thus, EITC misreporting is a relatively small portion of the tax gap—six percent of the gross tax gap and ten percent of the tax gap attributable to income misreporting by individuals—as shown in Figure 1.6.2.

44 IRS, Research, Analysis & Statistics, *Federal Tax Compliance Research: Tax Gap Estimates for Tax Years 2008-2010*, Publication 1415, 1 (May 2016), noting that “the word ‘tax’ in the phrase ‘tax gap’ is used broadly to encompass both tax and refundable and non-refundable tax credits.”

45 *Id.* at 9, reporting annual average estimates for 2008-2010.

46 Business income includes income reported on Schedules C, E, and F, *i.e.*, nonfarm proprietor income (29 percent), flow-through income (from partnerships, S corporations, and estates and trusts) (eight percent), rent and royalty income (eight percent), and farm income (two percent). *Id.* at 19.

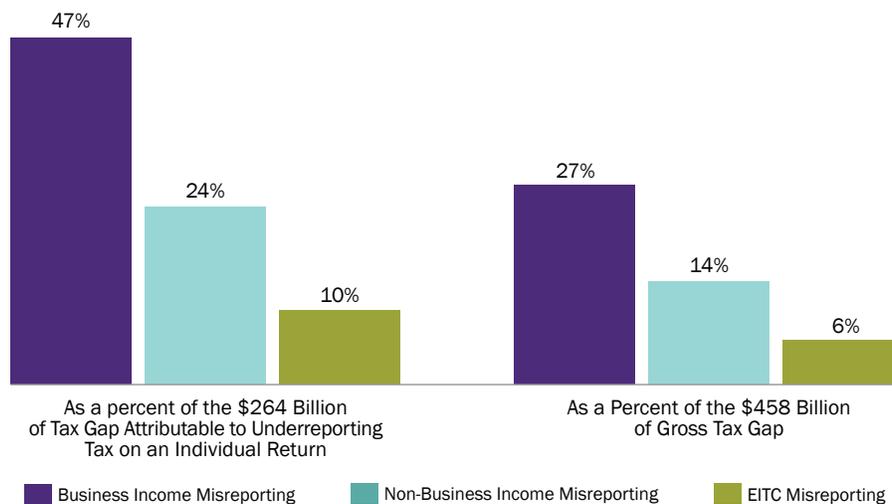
47 Non-business income includes all other individual taxpayer income that is not business income (e.g., wages, salaries, tips, unemployment compensation, pensions and annuities, alimony, interest, dividends, and capital gains). *Id.* at 18.

48 *Id.* at 10.

49 *Id.* at 19, noting that EITC accounts for ten percent of the individual income tax underreporting tax gap; ten percent of \$264 billion is \$26 billion. There are some differences in the methodology for calculating tax gap estimates and calculating improper EITC payments. For example, as noted above, the EITC improper payment rate is expressed as a single rate with confidence intervals, with taxpayers who did not participate in the audit being treated as entitled to EITC at the same rate as those who participated in the NRP audit. For purposes of estimating the tax gap, the EITC audit outcome is used; in most cases, EITC claimed by taxpayers who do not participate in the audit is disallowed. Because of this and other differences in methodology, the amount of estimated EITC misreporting (\$26 billion) for purposes of estimating the tax gap exceeds the estimated improper payment amount (\$18 billion for FY 2013, based on audits of 2010 returns).

FIGURE 1.6.2

## Three Largest Components of the Tax Gap, Tax Years 2008-2010



Unlike other anti-poverty programs, taxpayers are not required to meet with caseworkers or submit documentation to establish their eligibility before claiming EITC. Thus, the cost of administering the EITC program (around one percent of benefits delivered) is significantly lower than non-tax payment or benefit programs, and the EITC participation rate (79 percent) is relatively high.<sup>50</sup> IRS auditors, including NRP auditors, who disallow EITC claimed with respect to a qualifying child are reminded that the taxpayer may still be eligible for the childless worker credit.<sup>51</sup> However, as discussed above, a significant amount of EITC goes unclaimed by taxpayers who appear to be eligible for the credit. IRS notices reminding taxpayers of EITC have not been particularly effective in increasing participation rates.<sup>52</sup> The IRS could explore the possibility of increasing the EITC participation rate by automatically

50 For a comparison of the costs and benefits of federal payment programs (e.g., Supplemental Nutrition Assistance Program (SNAP), Women, Infants, and Children (WIC), Supplemental Security Income (SSI), Temporary Assistance to Needy Families (TANF), Department of Housing and Urban Development (HUD), Children's Health Insurance Program (CHIP), Medicaid, and school lunch programs), see National Taxpayer Advocate 2016 Annual Report to Congress 341 (Legislative Recommendation: *Restructure the Earned Income Tax Credit and Related Family Status Provisions to Improve Compliance and Minimize Taxpayer Burden*). See also IRS, *EITC Participation Rate by States*, n.1, <https://www.eitc.irs.gov/eitc-central/participation-rate/eitc-participation-rate-by-states> (last visited Nov. 26, 2018), for tax year 2014.

51 See, e.g., IRM 4.19.14.5.5, *EITC - No Qualifying Children* (Nov. 2, 2017); IRM 4.22.8.6.3.3, *Completing the EIC Eligibility Rules Section of the EIC Lead Sheet Tab* (Jan. 10, 2014).

52 See Office of Evaluation Service, *Tax Filing and EITC Take-up: Reminders promote tax filing compliance and increase EITC payments*, <https://oes.gsa.gov/projects/eitc-filing/> (last visited Nov. 26, 2018), evaluating the effect of sending "combinations of behaviorally informed postcards and brochures, highlighting the recipient's potential eligibility for the EITC" and finding that while the notices increased the number of returns filed, the notices did not increase the rates at which individuals claimed the EITC, although they did increase the amount of EITC dollars paid to treatment individuals by about \$25 on average.

allowing the credit to taxpayers who do not claim EITC but file returns showing they are eligible for it, particularly those eligible for the “childless worker” EITC.<sup>53</sup>

### IRS Measures to Reduce EITC Improper Payments May Unnecessarily Burden Taxpayers

Despite the acknowledged complexity of the rules for claiming EITC as a cause of improper EITC claims, IRS and Treasury legislative proposals to address EITC improper payments have centered on enforcement measures rather than on simplification.<sup>54</sup> For example, the IRS and Treasury consistently recommend expanding the IRS’s math error authority by conferring “correctible error authority.”<sup>55</sup> The National Taxpayer Advocate has for many years voiced her concerns about expansions of the IRS’s math error authority and how the IRS exercises that authority and thus does not support this proposal in its current sweeping form.<sup>56</sup>

The IRS also exercises its authority under IRC § 32(k) to impose two-year bans on claiming EITC on taxpayers who claim EITC with “reckless or intentional disregard of rules and regulations.” TAS found that according to IRS data, the IRS improperly imposed the ban 49 percent of the time in 2009, 44 percent of the time in 2010, and 39 percent in 2011.<sup>57</sup> The IRS imposed 3,442 two-year bans on taxpayers who claimed EITC on their 2017 returns.<sup>58</sup>

53 IRC § 32(c)(1)(A)(ii) defines “eligible individual” to include taxpayers who do not have a “qualifying child.” The maximum amount of EITC for a single worker with no children was \$510 for 2017. IRS, Publication 596, *Earned Income Credit (EIC)* 32 (Jan. 16, 2018). Form 1040 does not capture information about residency, a requirement for claiming childless-worker EITC, but the IRS, through automation and data mining, could use the databases it has access to in order to determine whether the residency requirement was met. See TIGTA, Ref. No. 2018-IE-R004, *The Internal Revenue Service Should Consider Modifying the Form 1040 to Increase Earned Income Tax Credit Participation by Eligible Tax Filers* (Apr. 2, 2018) for a similar recommendation, that the IRS, instead of sending reminder notices, consider revising Form 1040 to capture information about taxpayers’ eligibility for EITC, such as ages of children and duration of residency with the taxpayer, and then automatically refund the EITC to eligible taxpayers even if they did not claim it.

54 In contrast, other tax administrations recognize their responsibility to actively seek tax simplification. See, e.g., Australian Tax Office (ATO), Second Commissioner Andrew Mills, *Tax Administration Continuum - ‘The Law was Made for Man, not Man for the Law’* (2017), <https://www.ato.gov.au/Media-centre/Speeches/Other/Tax-Administration-Continuum---The-Law-was-Made-for-Man,-not-Man-for-the-Law/> (last visited Nov. 26, 2018), noting “[t]he final aspect of the Tax Continuum in the ATO’s role as the tax administrator is legislative change. It is an understatement to say that tax law is extremely complex and labyrinthine...the ATO has a duty to advocate when the law is not operating as intended and when there are unintended consequences for the taxpayer.”

55 See, e.g., *General Explanations of the Administration’s Fiscal Year Revenue Proposals* (Treasury Greenbook) FY 2017 at 225, <https://www.treasury.gov/resource-center/tax-policy/Documents/General-Explanations-FY2017.pdf>, proposing to give the Treasury regulatory authority to permit the IRS to “correct errors in cases where (1) the information provided by the taxpayer does not match the information contained in government databases, (2) the taxpayer has exceeded the lifetime limit for claiming a deduction or credit, or (3) the taxpayer has failed to include with his or her return documentation that is required by statute.”

56 See, e.g., National Taxpayer Advocate 2002 Annual Report to Congress 25, 185 (Most Serious Problem: *Math Error Authority*; Key Legislative Recommendation: *Math Error Authority*). See also Most Serious Problem: *Math Error Notices: Although the IRS Has Made Some Improvements, Math Error Notices Continue to be Unclear and Confusing, Thereby Undermining Taxpayer Rights*, *infra*; Most Serious Problem: *The IRS Has Failed to Exercise Self-Restraint in Its Use of Math Error Authority, Thereby Harming Taxpayers*, *infra*.

57 National Taxpayer Advocate 2013 Annual Report to Congress 103, 105 (Most Serious Problem: *The IRS Inappropriately Bans Many Taxpayers from Claiming EITC*).

58 The IRS imposed 9,431; 6,445; 6,296; and 6,106 two-year bans claimed on returns for tax year 2013–2016, respectively. IRS Compliance Data Warehouse (CDW), Individual Returns Transaction File, Aug. 2018.

### Tax Administrations Benefit From Shifting to Proactive Compliance Activities

As the Organisation for Economic Co-operation and Development (OECD) notes, tax administrations are benefiting from a shift from reactive compliance activities (*e.g.*, audits) to proactive activities (*e.g.*, outreach and education, behavioral nudges) and upstream activities (*e.g.*, early interventions when a potential tax debt arises and pay-as-you-earn systems).<sup>59</sup>

For example, the Australian Taxation Office (ATO) distinguishes between reviews (conducted to assess whether or not there is a risk of noncompliance and to collect information about particular industries and activities) and audits (conducted where there appears to be noncompliance or where a review would be or has been insufficient).<sup>60</sup> In either situation, the ATO may correct the return and assess additional tax, but this “escalation” approach typically begins with a review, described as “an opportunity to quickly and cooperatively resolve matters in a transparent way” rather than a full-blown audit.<sup>61</sup>

ATO also effectively uses behavioral insights by taking measures such as:<sup>62</sup>

- Sending text message payment reminders to taxpayers who are likely to pay late or not at all. In 2015-2016, sending 540,000 SMS debt prompts resulted in more than \$949 million in debt being paid on time;
- Sending thank-you messages to taxpayers who had paid on time after receiving an SMS reminder in a previous payment quarter;
- Using “nearest neighbor” analysis to advise taxpayers when a claimed deduction is significantly higher than that claimed by their peers, which prompted many to reduce their claimed deductions; and
- Considering sending text messages advising taxpayers of tax benefits they may have overlooked (*e.g.*, taxpayers could be advised that the deductions they had claimed were below the amounts claimed by their peers, and that they should recheck whether they had claimed all the deductions to which they were entitled).

As discussed below, similar proactive approaches to interacting with taxpayers who claim or appear to be eligible to claim EITC may help reduce the EITC improper payment rate.

59 OECD, *The Changing Tax Compliance Environment and the Role of Audit* 19, 23-26 (2017), [https://www.oecd-ilibrary.org/taxation/the-changing-tax-compliance-environment-and-the-role-of-audit\\_9789264282186-en](https://www.oecd-ilibrary.org/taxation/the-changing-tax-compliance-environment-and-the-role-of-audit_9789264282186-en). For a discussion of various pay-as-you-earn (PAYE) systems in other countries and an analysis of the benefits, burdens, and limitations of a broader PAYE system as it might be applied in the U.S., see Research Study: *A Conceptual Analysis of Pay-As-You-Earn (PAYE) Withholding Systems as a Mechanism for Simplifying and Improving U.S. Tax Administration*, vol. 2, *infra*.

60 ATO, *Taxpayers' charter: If you're subject to review or audit* 3 (2013), <https://www.ato.gov.au/assets/0/104/300/362/2cd37d1a-1184-4568-8dd1-98ecbeb1e503.pdf>.

61 ATO, *Reviews*, <https://www.ato.gov.au/business/private-owned-and-wealthy-groups/what-you-should-know/tailored-engagement/reviews/> (last visited Nov. 26, 2018).

62 ATO, Second Commissioner Andrew Mills, *Tax Administration Continuum - 'The Law was Made for Man, not Man for the Law'* (2017), <https://www.ato.gov.au/Media-centre/Speeches/Other/Tax-Administration-Continuum---The-Law-was-Made-for-Man,-not-Man-for-the-Law/> (last visited Nov. 26, 2018).

### IRS EITC Notices Should Be More Tailored and Include Additional Telephone Support

The IRS issues “soft” notices to taxpayers who appear to have claimed EITC in error, advising them to check their returns to verify that the information is correct.<sup>63</sup> However, IRS studies of the effectiveness of the soft notices indicate that receiving a soft notice had minimal effect on taxpayer behavior.<sup>64</sup>

In contrast to the general instructions provided in the soft notices, the National Taxpayer Advocate in 2016 sent *salient* letters to representative samples of taxpayers who appeared to have claimed EITC in error on their 2014 returns.<sup>65</sup> The letters were mailed at a time when taxpayers were likely to be thinking about taxes, *i.e.*, in the two weeks before the filing season began. Taxpayers were beginning to receive tax documents, such as W-2s, in the mail, and the envelope with the TAS letter bore the notation, in red letters, that it contained “Important Tax Information.” Thus, taxpayers were more likely to open the mail. The message was tailored to identify the specific error the taxpayer appeared to have made, and educated the taxpayer about the requirements for claiming EITC. TAS Research studied the effect of the letters on taxpayer compliance, and on the basis of those findings, the National Taxpayer Advocate revised the letters and sent them to taxpayers in representative samples the following year.<sup>66</sup>

One revision to the 2017 letter that was sent to a separate sample of 967 taxpayers who appeared to not have met the residency requirements on their 2015 returns offered a dedicated “Extra Help” telephone line.<sup>67</sup> The help line was staffed by TAS employees trained to answer taxpayer questions about the letter and the EITC eligibility rules. Only 35 taxpayers called the additional phone number and spoke with a TAS employee. Nevertheless, according to TAS projections, sending the TAS letter with the extra help telephone line to all taxpayers whose 2015 returns appeared to be erroneous because the residency requirement was not met would have averted over \$44 million in erroneous EITC claims.<sup>68</sup> TAS will repeat the study in a future filing season, offering the extra help line for all notices. The study will also

63 See IRM 4.19.14.2, *EITC Soft Notices* (Dec. 7, 2017), describing Letter 5621, *Help Us Confirm Your Relationship to the EIC Qualifying Children* and Letter 5621-A, *Confirm Your Schedule C Income Used to Claim Earned Income Tax Credit*. These letters give taxpayers the general instruction to “make sure your children meet the criteria for claiming the Earned Income Tax Credit (EITC)” or “make sure the income and expenses you reported on your Schedule C or Schedule C-EZ are correct.”

64 IRS Wage & Investment, *FY 2016 DDb Soft Notice Phase III: Notice Effectiveness 3* (Jan. 2017), reporting that the soft notices issued in December of 2015 averted only about \$40 per taxpayer in erroneous EITC claims. Additional analysis conducted with respect to 2016 yielded similar results. IRS response to TAS information request (Sept. 25, 2018).

65 National Taxpayer Advocate 2016 Annual Report to Congress vol. 2 32 (Research Study: *Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits (EITC) Apparently in Error and Were Sent an Educational Letter From the National Taxpayer Advocate*), showing that the TAS letter averted noncompliance on tax year (TY) 2015 returns where the TY 2014 return appeared erroneous because the relationship test was not met. Sending the TAS letter to all taxpayers whose TY 2014 returns appeared to be erroneous because the relationship test was not met would have averted about \$47 million of erroneous EITC claims.

66 National Taxpayer Advocate 2017 Annual Report to Congress vol. 2 13 (Research Study: *Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits (EITC) Apparently In Error and Were Not Audited But Were Sent an Educational Letter From the Taxpayer Advocate Service, Part 2: Validation of Prior Findings and the Effect of an Extra Help Phone Number and a Reminder of Childless-Worker EITC Income Tax Credits (EITC) Apparently in Error and Were Sent an Educational Letter From the National Taxpayer Advocate*), showing that sending the TAS letter to all taxpayers whose 2015 returns appeared to be erroneous because the relationship test was not met would have averted over \$53 million in erroneous EITC claims.

67 For a recommendation to Congress that the IRS be required to provide year-round telephone support, see National Taxpayer Advocate 2016 Annual Report to Congress 329 (Legislative Recommendation: *Restructure the Earned Income Tax Credit and Related Family Status Provisions to Improve Compliance and Minimize Taxpayer Burden*).

68 National Taxpayer Advocate 2017 Annual Report to Congress vol. 2 13 (Research Study: *Study of Subsequent Filing Behavior of Taxpayers Who Claimed Earned Income Tax Credits (EITC) Apparently In Error and Were Not Audited But Were Sent an Educational Letter From the Taxpayer Advocate Service, Part 2: Validation of Prior Findings and the Effect of an Extra Help Phone Number and a Reminder of Childless-Worker EITC Income Tax Credits (EITC) Apparently in Error and Were Sent an Educational Letter From the National Taxpayer Advocate*).

include focus groups to capture qualitative information on the effectiveness of the content and layout of the messages.

The IRS is planning to send soft notices to taxpayers who appear to have claimed EITC in error on their 2017 returns because they misreported the amount of their earned incomes, and to study the effect of the soft notices on taxpayers' 2018 returns.<sup>69</sup> The National Taxpayer Advocate encourages the IRS to provide specificity in these soft notices and direct taxpayers to a dedicated telephone help line available year-round they can call with questions about EITC.<sup>70</sup>

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**A principal cause of the Earned Income Tax Credit (EITC) improper payment rate is the complexity of the rules for claiming EITC, yet the IRS does not provide a dedicated telephone help line available year-round for taxpayers to call with questions about EITC.**

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## CONCLUSION

A principal cause of the EITC improper payment rate is the complexity of the rules for claiming EITC, and taxpayers encounter difficulty in documenting their eligibility to claim the credit. At the same time, many taxpayers who appear to be eligible to claim EITC do not claim it, a phenomenon not reflected in the improper payment rate. Automatically allowing EITC in some cases, sending tailored communications to those who appear to have claimed the credit in error, and providing dedicated telephone support available year-round may increase participation rates and avert future erroneous claims.

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<sup>69</sup> IRS response to TAS information request (Sept. 25, 2018).

<sup>70</sup> See Literature Review: *Improving Notices Using Psychological, Cognitive, and Behavioral Science Insights*, *infra*.

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Seek a permanent exemption from the requirement that the IRS include recovered EITC payments in the EITC improper payment estimate.
2. Collaborate with TAS to identify a method of identifying taxpayers who do not claim EITC but are eligible for the childless worker EITC, and automatically award the childless worker credit to those taxpayers.
3. Collaborate with TAS to identify the changes to Form 1040 that would be needed, and the data gathering techniques that could be employed, to award EITC to taxpayers who are eligible for EITC with respect to a qualifying child but do not claim it on their returns.
4. Collaborate with TAS Research in designing and conducting the planned study to compare prior EITC audit results to audit results of taxpayers who used affidavits to establish that they met the residency requirement.
5. Revise soft notices that are sent to taxpayers advising them they may have claimed EITC in error to explain the error the taxpayer appears to have made (*e.g.*, not meeting the residency requirement or the relationship requirement, misreporting income or deductions).
6. Establish a dedicated, year-round toll-free “help line” staffed by IRS personnel trained to respond to EITC and Child Tax Credit questions.
7. In soft notices to taxpayers advising them that they may have claimed EITC in error, include the dedicated telephone “help line.”

**MSP  
#7****RETURN PREPARER OVERSIGHT: The IRS Lacks a Coordinated Approach to Its Oversight of Return Preparers and Does Not Analyze the Impact of Penalties Imposed on Preparers****RESPONSIBLE OFFICIALS**

Ken Corbin, Commissioner, Wage and Investment Division  
 Mary Beth Murphy, Commissioner, Small Business/Self-Employed Division  
 Carol Campbell, Director, Return Preparer Office  
 Stephen A. Whitlock, Director, Office of Professional Responsibility

**TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Quality Service*
- *The Right to a Fair and Just Tax System*

**DEFINITION OF PROBLEM**

The IRS is tasked with collecting taxes and administering the Internal Revenue Code (IRC). In calendar year 2018, the IRS processed over 150 million individual tax returns, with almost 80 million taxpayers relying on paid preparers.<sup>2</sup> More than half of these returns were submitted by return preparers who are unregulated by the IRS.<sup>3</sup> Unenrolled preparers—those generally not subject to IRS regulation—account for over half of all preparers.<sup>4</sup>

It is a necessary part of the IRS's duties to ensure that preparers are competent and accountable, since return preparers play such a critical role in tax administration and ensuring tax compliance. The public needs a way to differentiate between professional, competent, and experienced preparers, and their incompetent or unscrupulous counterparts. The National Taxpayer Advocate has written extensively on the need to protect taxpayers from non-compliant return preparers.<sup>5</sup>

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- 1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).
  - 2 Compliance Data Warehouse (CDW), *Return Preparers and Providers database Preparer Tax Identification Number (PTIN) table and the Individual Return Transaction File (IRTF) Entity file* (data updated Sept. 30, 2018 for both databases).
  - 3 *Id.*
  - 4 *Id.*
  - 5 See National Taxpayer Advocate 2015 Annual Report to Congress 261-283 (Most Serious Problem: *The IRS's EITC Return Preparer Strategy Does Not Adequately Address the Role of Preparers in EITC Noncompliance*); National Taxpayer Advocate 2013 Annual Report to Congress 61-74 (Most Serious Problem: *Taxpayers and Tax Administration Remains Vulnerable to Incompetent and Unscrupulous Return Preparers While the IRS Is Enjoined From Continuing Its Efforts to Effectively Regulate Unenrolled Preparers*); National Taxpayer Advocate 2009 Annual Report to Congress 41-69 (Most Serious Problem: *The IRS Lacks a Servicewide Return Preparer Strategy*); National Taxpayer Advocate 2006 Annual Report to Congress 197-221 (Most Serious Problem: *Oversight of Unenrolled Return Preparers*); National Taxpayer Advocate 2005 Annual Report to Congress 223-237 (Most Serious Problem: *Regulation of Electronic Return Originators*); National Taxpayer Advocate 2004 Annual Report to Congress 67-88 (Most Serious Problem: *Oversight of Unenrolled Return Preparers*); National Taxpayer Advocate 2003 Annual Report to Congress 270-301 (Legislative Recommendation: *Federal Tax Return Preparers: Oversight and Compliance*); National Taxpayer Advocate 2002 Annual Report to Congress 216-230 (Legislative Recommendation: *Regulation of Federal Tax Return Preparers*).

The case for IRS oversight of the return preparation industry is clear. When an attorney is hired, there is some level of confidence that the attorney is competent. One could verify that the attorney has passed a bar exam and meets the continuing legal education and professional responsibility requirements of his or her state's bar association. When one visits a hair salon, the hair stylist will have a certificate displayed, which attests to the fact that the stylist has undergone the training necessary to obtain the license. In contrast, there is no such guarantee that an unenrolled tax return preparer has passed any exam, continues to engage in ongoing education, or meets any other minimum standard of competency to prepare federal tax returns.

If anyone can hang out a shingle as a “tax return preparer” with no minimum competency requirements or oversight, problems with return accuracy will abound. The Government Accountability Office (GAO) confirmed this by having its auditors pose as taxpayers visiting tax return preparation chains (which had a minimum of ten locations). Only two out of the 19 randomly selected preparers calculated the correct amount of refund in a GAO study.<sup>6</sup> The National Consumer Law Center has conducted similar “mystery shopper visits” with similar results.<sup>7</sup>

The IRS had started to implement a program to impose minimum competency requirements on the unenrolled tax preparation profession. However, in 2013, the District Court for the District of Columbia enjoined the IRS from regulating tax return preparers via testing and continuing education requirements.<sup>8</sup> In 2014, the U.S. Court of Appeals for the District of Columbia upheld the decision, meaning that the IRS will need to fulfill its oversight responsibility within the confines of the current law.

Even with the courts enjoining the IRS from testing and certifying tax return preparers, the National Taxpayer Advocate believes that the IRS still has a vital role to play in protecting taxpayers' *rights to quality service* and *to a fair and just tax system*. The court decision does not absolve the IRS of the responsibility to protect taxpayers.

Specifically, the IRS should:

- Establish a truly cross-functional team to develop and communicate a coordinated strategy to effectively provide oversight of return preparers;
- Conduct in-depth analysis of the impact of penalty assessments on preparers' behavior in subsequent years, and publish the findings;
- Assert a more active role in the voluntary certification process, including designing an examination and developing training materials; and
- Ensure that any references to the directory of Federal Tax Return Preparers are not misleading.

6 Government Accountability Office (GAO), GAO-14-467T, *PAID TAX RETURN PREPARERS: In a Limited Study, Preparers Made Significant Errors* (Apr. 8, 2014).

7 See National Consumer Law Center (NCLC), *Riddled Returns: How Errors and Fraud by Paid Tax Preparers Put Consumers at Risk and What States Can Do* (Mar. 2014), [www.nclc.org/images/pdf/pr-reports/report-riddled-returns.pdf](http://www.nclc.org/images/pdf/pr-reports/report-riddled-returns.pdf).

8 *Loving v. Internal Revenue Service*, 917 F. Supp. 2d 67 (D.D.C. 2018), *aff'd*, 742 F.3d 1013 (D.C. Cir. 2014).

## ANALYSIS OF PROBLEM

### Background

There are several types of tax return preparers. Attorneys, Certified Public Accountants (CPAs), and Enrolled Agents (EAs) have passed examinations to demonstrate their knowledge and proficiency. Furthermore, they must comply with applicable continuing education requirements for their jurisdiction. These tax professionals have unlimited representation rights before the IRS and may represent their clients on any matters including examinations, collection issues, and appeals.

Unenrolled preparers are individuals other than an attorney, CPA, EA, enrolled retirement plan agent, or enrolled actuary who prepares and signs a taxpayer's return as the paid preparer (or who prepares a return but is not required to sign the return). For tax returns filed after December 31, 2015, unenrolled preparers who have completed the IRS's Annual Filing Season Program (AFSP)<sup>9</sup> for both the year the tax return was filed *and* for the year(s) in which the representation occurs, have limited representation rights.<sup>10</sup> They may represent clients whose returns they have prepared, but only before Revenue Agents, Customer Service Representatives, and similar IRS employees; they may not represent clients before Appeals or Collections officers.<sup>11</sup>

Unenrolled preparers who have not received the AFSP Record of Completion do not have the right to represent taxpayers. If the unenrolled preparer checked the box as a third party designee on the Form 1040, the preparer may speak to the IRS to provide more information about an item on the tax return, but may not execute closing agreements, extend the statutory period for tax assessments or collection of tax, execute waivers, or sign any document on behalf of a taxpayer.<sup>12</sup>

Anyone who prepares federal tax returns for compensation is required to have a valid preparer tax identification number (PTIN).<sup>13</sup> Tax preparers are required to include their PTIN on and sign any returns they prepare. However, some "ghost" tax preparers file tax returns on their clients' behalf without any indication that the taxpayer used a paid tax preparer to complete the return.

Figure 1.7.1 shows the number of individual tax returns prepared for tax year (TY) 2017 by type of preparer. Unenrolled preparers (including those who completed the voluntary AFSP) account for more than half of the nearly 77 million individual tax returns prepared by a preparer.

9 The Annual Filing Season Program is a voluntary program designed to encourage non-credentialed tax return preparers to participate in continuing education courses. To obtain an Annual Filing Season Program Record of Completion, a return preparer must obtain 18 hours of continuing education (including a six-credit hour Annual Federal Tax Refresher course that covers filing season issues and tax law updates) from an IRS-approved continuing education provider. In addition to completing the appropriate continuing education courses, the return preparer must also renew his or her preparer tax identification number (PTIN) for the upcoming year. IRS, *Frequently Asked Questions: Annual Filing Season Program*, <https://www.irs.gov/tax-professionals/frequently-asked-questions-annual-filing-season-program> (last visited Dec. 6, 2018).

10 Rev. Proc. 2014-42, *Annual Filing Season Program* § 6, 2014-29 I.R.B. 192 (2014).

11 See Internal Revenue Manual (IRM) 21.3.7.5.6(3), *Unenrolled Return Preparer (Level H) Representative Research, Rejections and Processing* (Sept. 13, 2017).

12 See Instructions to 2018 Form 1040 (Dec. 10, 2018); IRS Pub. 947, *Practice Before the IRS and Power of Attorney* 4 (Rev. Feb. 2018).

13 See Treas. Reg. § 1.6109-2.

**FIGURE 1.7.1, Volume of Tax Year 2017 Individual Tax Returns by Preparer Type<sup>14</sup>**

	Number of Returns								
	Form 1040	Form 1040 with Schedule C	Form 1040A	Form 1040EZ	Form 1040 A/EZ with Schedule EIC	Form 1040 with Schedules C & EIC	Form 1040 with Schedule F	Form 1040 with Schedules F & EIC	Total
Unenrolled Preparer (Unenrolled Prep)	16,634,128	4,456,328	4,480,376	3,260,274	6,949,731	3,035,224	391,237	45,492	39,252,790
Attorney (ATTY)	589,182	180,644	44,916	27,869	31,529	20,109	32,312	2,401	928,962
Certified Acceptance Agent (CAA)	202,595	70,389	67,025	45,944	79,889	44,393	1,868	207	512,310
Certified Public Accountant (CPA)	14,784,869	5,010,256	698,486	486,295	671,680	549,718	601,204	35,088	22,837,596
Enrolled Agent (EA)	5,273,359	1,546,780	863,847	547,327	733,998	382,294	149,137	13,257	9,509,999
Enrolled Actuary	5,688	2,210	1,203	1,063	2,320	2,003	82	8	14,577
Enrolled Retirement Plan Agent (ERPA)	357	104	87	31	167	30	-	1	777
State Regulated Tax Preparer (SRTP)	1,736,864	500,310	404,694	244,619	506,970	255,470	9,080	964	3,658,971
<b>Total</b>	<b>39,227,042</b>	<b>11,767,021</b>	<b>6,560,634</b>	<b>4,613,422</b>	<b>8,976,284</b>	<b>4,289,241</b>	<b>1,184,920</b>	<b>97,418</b>	<b>76,715,982</b>

A recent poll conducted by the Consumer Federation of America indicates strong support for reform of the tax preparer industry. Eighty-six percent of respondents support the requirement that paid tax preparers pass a competency test. Sixty-eight percent of respondents believe that either the federal government or their state government should require paid tax preparers to be licensed.<sup>15</sup> Only seven states (California, Connecticut, Illinois, Maryland, Nevada, New York, and Oregon) currently impose minimum competency standards for unenrolled preparers.<sup>16</sup>

### Legal Framework

On January 18, 2013, the U.S. District Court for D.C. enjoined the IRS from enforcing regulatory requirements for registered tax return preparers.<sup>17</sup> As a result of this decision in *Loving vs. Internal Revenue Service*, the IRS is not able to mandate that unenrolled tax return preparers complete competency testing or secure continuing education. (This holding does not apply to attorneys, CPAs, or EAs, who are already subject to continuing education requirements imposed by their licensing agencies.)

The *Loving* decision was upheld by the U.S. Court of Appeals for the District of Columbia Circuit on February 11, 2014. The IRS has not further appealed the decision to the Supreme Court. Various bills

14 CDW, *Return Preparers and Providers database PTIN table and the IRTF Entity file* (data updated Sept. 30, 2018 for both databases).

15 See Consumer Federation of America, *Second National Poll Indicates Strong Support for Reform of Paid Tax Preparer Industry* (Mar. 22, 2017), <https://www.nclc.org/images/pdf/taxes/pr-paid-tax-preparer-industry.pdf>.

16 Don't Mess with Taxes, *Seven States that Regulate Paid Tax Preparers* (July 11, 2018), <https://www.dontmesswithtaxes.com/2018/07/7-states-that-regulate-paid-tax-preparers.html>.

17 *Loving v. Internal Revenue Service*, 917 F. Supp. 2d 67 (D.D.C. 2018), *aff'd*, 742 F.3d 1013 (D.C. Cir. 2014).

have been proposed that would require tax return preparers to take a competency exam, attend continuing education classes, and submit to a background check.<sup>18</sup> However, Congress has not enacted any.

### The IRS Should Establish a Truly Cross-Functional Team to Develop and Communicate a Coordinated Strategy to Effectively Provide Oversight of Return Preparers

Although the IRS unilaterally cannot mandate return preparers pass competency tests or undergo continuing education, there is still a need for the IRS to provide a certain level of oversight. Taxpayers need to feel confident that they can rely on return preparers. Rather than designating one centralized Commissioner-level office to coordinate oversight of return preparers, the IRS has spread this responsibility over multiple offices across several organizations.

The Return Preparer Office (RPO) oversees preparer registration and renewal programs, is engaged in general outreach and education, and administers the Annual Filing Season Program. The RPO does not engage in disciplinary proceedings related to return preparers.

The Office of Professional Responsibility (OPR) was established as the governing body responsible for interpreting and applying Treasury Department Circular 230, *Regulations Governing Practice before the Internal Revenue Service*. OPR's stated mission is to "interpret and apply the standards of practice for tax professionals in a fair and equitable manner," and its goals include increasing awareness of the Circular 230 standards of practice through outreach activities, as well as investigating cases where practitioners have run afoul of Circular 230. Attorneys, CPAs, and EAs are among the tax professionals subject to Circular 230. OPR lacks the authority to provide oversight of non-Circular 230 practitioners; however, participants in the AFSP must consent to the Circular 230 obligations. The OPR may take disciplinary action (including against unenrolled agents who have obtained limited representation rights by virtue of completing the AFSP) who are involved in "disreputable conduct."<sup>19</sup>

The Wage and Investment (W&I) division's Return Integrity and Compliance Services (RICS) function has developed a Refundable Credits Return Preparer Strategy Guide and Procedures. RICS acknowledges that refundable credit noncompliance among return preparers is problematic for the IRS. For example, more than three-quarters of returns allowed in processing the earned income tax credit (EITC) are prepared by unenrolled preparers.<sup>20</sup> Accordingly, W&I's strategy to prevent and reduce improper payments of refundable credits includes strengthening relationships with return preparers, educating them about the credits, and enforcing the preparer due diligence requirements.<sup>21</sup>

18 See Protecting Taxpayers Act, S. 3278, 115th Cong. (referred to S. Comm. on Finance July 26, 2018); Tax Return Preparer Competency Act, H.R. 4141, 114th Cong. (referred to the H. Comm. on Ways and Means Dec. 1, 2015).

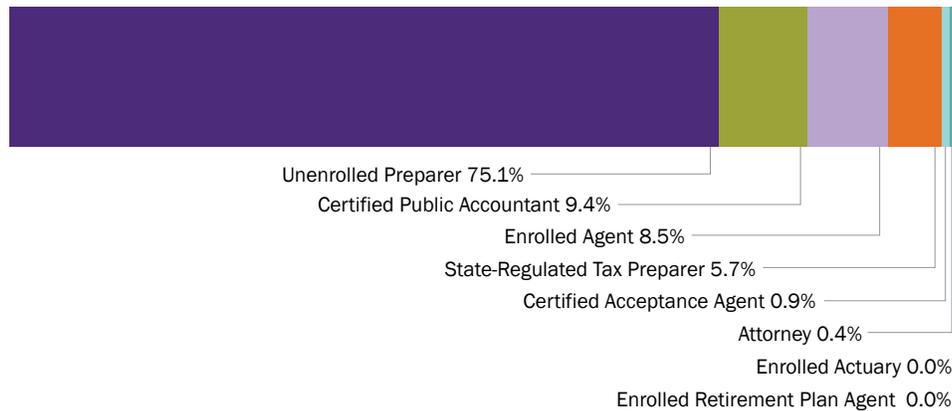
19 IRS Pub. 947, *Practice Before the IRS and Power of Attorney 4*, 7 (Rev. Feb. 2018).

20 CDW, *Return Preparers and Providers database PTIN table and the IRTF Entity file* (data updated Sept. 30, 2018, for both databases).

21 See National Taxpayer Advocate 2015 Annual Report to Congress 261-283 (Most Serious Problem: *The IRS's EITC Return Preparer Strategy Does Not Adequately Address the Role of Preparers in EITC Noncompliance*). The preparer due diligence requirements are set forth in Treas. Reg. 1.6695-2. A preparer must (1) complete and submit Form 8867, (2) use worksheets or other method to compute credits, (3) have no knowledge that any information used by the preparer is incorrect, and (4) retain records. See below for additional discussion about preparer penalties.

FIGURE 1.7.2<sup>22</sup>

## Earned Income Tax Credit Returns Filed by Profession (Tax Year 2018)



Small Business and Self-Employed (SB/SE) oversees the Return Preparer Program (RPP). Under the RPP, the IRS can open program action cases (PACs), which are “preparer investigations where clients of questionable preparers are examined to determine whether preparer penalties and/or injunctive actions against the preparers are warranted.”<sup>23</sup>

The Criminal Investigation (CI) division administers an Abusive Return Preparer Program. Under this program, CI pursues return preparers for criminal offenses related to the preparation and filing of false income tax returns. Corrupt return preparers who claim inflated personal or business expenses, false deductions, excessive exemptions, or unallowable tax credits may be referred to the Department of Justice for injunctions from preparing taxes, or even criminal sanctions.<sup>24</sup>

There is a risk that the IRS is not achieving effective oversight with so many different offices and programs in place to oversee return preparers. The IRS’s internal procedures reference a “National Headquarters Return Preparer Strategy,” but no further information about such a strategy is contained in the Internal Revenue Manual (IRM).<sup>25</sup> The SB/SE Examination Program Letter for fiscal year 2018 contained a goal to develop a servicewide return preparer strategy.<sup>26</sup>

22 CDW, *Return Preparers and Providers database PTIN table and the IRTF Entity file* (data updated Sept. 30, 2018, for both databases).

23 IRM 4.1.10.3, *Program Action Cases Overview (PAC)* (Jan. 14, 2011).

24 IRS, *Criminal Investigation 2018 Annual Report* 9. In fiscal year (FY) 2018, there were 224 investigations initiated from the Abusive Return Preparer Program, with 170 indictments (148 of which received sentencing). IRS, *Criminal Investigation 2018 Annual Report* 124.

25 See IRM 4.1.1.6.20.1, *Return Preparer Coordinator (RPC)* (Oct. 25, 2017) (“The area Return Preparer Coordinator (RPC) will be responsible for planning and coordinating the implementation of area and National Headquarters Return Preparer Strategy.”); IRM 4.1.10.1, *Overview of the Return Preparer Program* (Jan. 14, 2011) (“The Area Return Preparer Coordinator (RPC) will be responsible for planning and coordinating the implementation of the Area and the National Headquarters Return Preparer Strategy.”).

26 Small Business/Self-Employed (SB/SE), *FY 2018 SB/SE Examination Program Letter* 7 (“Exam will lead a collaborative effort involving multiple compliance organizations (e.g., Wage & Investment (W&I), CI, Return Preparer Office (RPO)) to develop a comprehensive, Servicewide strategy incorporating the full range of educational, civil and criminal enforcement and judicial actions to ensure we use our limited resources in the most efficient and effective manner to address preparer non-compliance.”).

In May 2018, the IRS convened a cross-functional team tasked with developing a coordinated servicewide return preparer strategy.<sup>27</sup> The cross-functional team included representatives from SB/SE (Exam and Collection), Communications, Criminal Investigation, Research, Applied Analytics, and Statistics, W&I, Governmental Liaison, Large Business and International, Return Preparer Office, Office of Professional Responsibility, SB/SE Research, Office of Servicewide Penalties, and Chief Counsel. TAS was not invited to participate on this team. To make this a truly cross-functional team, the National Taxpayer Advocate believes that representatives from TAS, the voice of the taxpayer inside the IRS, must be included.

In developing the return preparer strategy, this team should take on a tiered approach. Rather than immediately resorting to penalties and sanctions, the team should consider the impact of education and soft notices on preparers. The IRS has some efforts with respect to soft notices, but the work is not coordinated or strategically planned.<sup>28</sup> If the IRS does not currently have good data on this, the team should work with the Research function to gather the data needed. The team is still conducting analysis; to date, no recommendations have been made.<sup>29</sup>

Once the IRS has developed a coordinated return preparer strategy, the next challenge is to figure out the best way to spread this message. For populations where taxpayers are especially vulnerable to unscrupulous and opportunistic preparers, the IRS needs to ensure its strategy is communicated. The IRS will need to take a multi-faceted approach, working with partners such as the Volunteer Income Tax Assistance sites and the Low Income Taxpayer Clinics, with consumer rights groups, and with local churches and other community groups. IRS employees need to be on the ground in these communities, partnering with the various groups listed above. In addition, the IRS can explore developing creative public service announcements for TV and radio, as well as tapping into non-traditional social media outlets.<sup>30</sup> The Nationwide Tax Forums could be one way to communicate the strategy, but there is much more the IRS may do to reach unenrolled preparers.

### The IRS Should Conduct In-Depth Analysis on the Impact of Penalty Assessments on Preparers' Behavior in Subsequent Years, and Publish the Findings

The tax code provides for several different types of preparer penalties. Section 6694 imposes two types of penalties for understatement of taxpayer's liability by tax return preparer:

- Understatement due to **unreasonable position** (IRC § 6694(a)); penalty is the greater of \$1,000 or 50 percent of the income derived by the preparer with respect to the return or claim for refund.
- Understatement due to **willful or reckless conduct** (IRC § 6694(b)); penalty is the greater of \$5,000 or 50 percent of the income derived by the preparer with respect to the return or claim for refund.

27 IRS response to TAS information request (Nov. 29, 2018).

28 For a more detailed discussion, see National Taxpayer Advocate 2016 Annual Report to Congress 261-283 (Most Serious Problem: *The IRS's EITC Return Preparer Strategy Does Not Adequately Address the Role of Preparers in EITC Noncompliance*).

29 IRS response to TAS information request (Nov. 29, 2018).

30 See National Taxpayer Advocate 2016 Annual Report to Congress 261-283 (Most Serious Problem: *The IRS's EITC Return Preparer Strategy Does Not Adequately Address the Role of Preparers in EITC Noncompliance*) for some specific recommendations on conducting effective outreach for the IRS's EITC return preparer strategy.

Section 6695 imposes a host of other assessable penalties with respect to the preparation of tax returns, including:

- Failure to furnish copy to taxpayer (IRC § 6695(a));
- Failure to sign return (IRC § 6695(b));
- Failure to furnish identification number (IRC § 6695(c));
- Failure to retain copy or list (IRC § 6695(d)); and
- Failure to comply with due diligence requirements with respect to eligibility for the EITC (IRC § 6695(g)).

**FIGURE 1.7.3, IRC §§ 6694 and 6695 Penalties Assessed (FYs 2015–2018)<sup>31</sup>**

	FY 2015	FY 2016	FY 2017	FY 2018
Number of IRC §§ 6694 and 6695 Penalties Assessed	3,624	2,582	2,107	2,292

As Figure 1.7.3 shows, the IRS has assessed penalties for preparer misconduct very sparingly, considering that the GAO found errors in returns filed by 17 of 19 paid preparers in its limited sample, and estimated that tax returns filed by paid preparers had a 60 percent error rate.<sup>32</sup> A recent report issued by the Treasury Inspector General for Tax Administration (TIGTA) found that just 15 percent of referrals to a return preparer coordinator resulted in a PAC investigation, and 41 percent of PAC investigations were closed without penalty assessments.<sup>33</sup> The IRM provides a list of factors that should be considered when determining if a PAC investigation should be opened.<sup>34</sup> Even in situations where the IRS determines that a PAC is not warranted, the IRS should consider whether there is value in sending out a letter. An example of using a soft touch to influence behavior is the issuance of a letter notifying a preparer that a complaint has been received.

The goal of W&I's Refundable Credits Return Preparer Strategy is to reduce overclaims of EITC and other refundable credits through education and compliance treatments. One of the treatment streams consists of auditing paid preparers who claim EITC and other credits for compliance with their IRC § 6695(g) due diligence requirements.<sup>35</sup>

31 CDW, *IMF Transaction History File* (data compiled Dec. 2018). This included assessments from Master File Tax (MFT) 13 and MFT 55.

32 GAO, GAO-14-467T, *Paid Tax Return Preparers: In a Limited Study, Preparers Made Significant Errors* 9 (Apr. 8, 2014).

33 Treasury Inspector General for Tax Administration (TIGTA), Ref. No. 2018-30-042, *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct* 11 (July 25, 2018).

34 Factors for consideration of Program Action Case (PAC) action include, but are not limited to:

- ◆ The egregious nature of the questionable conduct—*i.e.*, does the preparer engage in a widespread practice of making material errors and/or demonstrate intentional misconduct.
- ◆ The number of client taxpayers affected by the preparer's conduct.
- ◆ The available resources of the examination groups receiving the PAC examinations.
- ◆ The type(s) of returns involved (*i.e.*, 1040) and the tax years available.
- ◆ The dollar amounts and materiality of potential adjustments.
- ◆ Prior compliance activities — *i.e.* preparer penalties previously asserted, Earned Income Tax Credit (EITC)/Electronic Return Originator (ERO) visitations, and/or RPO compliance letters.

IRM 4.1.10.3.2, *PAC Development Factors* (Dec. 13, 2016).

35 IRS response to TAS information request (Aug. 13, 2018).

**FIGURE 1.7.4, IRC § 6695(g) Due Diligence Audits<sup>36</sup>**

FY	Audits Assigned	Surveyed	Discontinued	No Change	Penalties Proposed
2014	747	0 (0%)	21 (3%)	130 (17%)	596 (80%)
2015	1,001	0 (0%)	46 (5%)	145 (14%)	810 (81%)
2016	1,180	8 (1%)	47 (4%)	203 (17%)	922 (78%)
2017	787	0 (0%)	24 (3%)	119 (15%)	644 (82%)
2018	803	0 (0%)	27 (3%)	122 (15%)	654 (81%)

SB/SE conducts these due diligence audits (also known as “site visits”) before and during the filing season. During a due diligence audit, the examiner will interview the preparer and review at least 25 returns, looking at the preparer’s due diligence records, checklists, worksheets, copies of client provided documents, etc.<sup>37</sup> Preparers can face a penalty of \$500 (indexed for inflation) for failing to meet the due diligence requirements. Interestingly, the IRS reports that 96 percent of its due diligence audits are conducted on unenrolled agents.<sup>38</sup>

In theory, consistent assessment of such penalties will help encourage accountability and change behavior.<sup>39</sup> After the IRS has assessed penalties against a preparer, it should track the impact on subsequent behavior by reviewing tax returns filed by preparers who have been assessed penalties, and publish the findings. TAS research studies have demonstrated no change audits result in *decreased* compliance in future years; the no change rates of preparer due diligence audits shown above raise similar concerns.<sup>40</sup>

The IRS has not had great success in collecting the penalties assessed. Part of the problem is that these liabilities are processed just like any other taxpayer liability within the Collection function. In the past, the Collection Program Letter prioritized the collection of preparer penalties. However, the collection of these penalties is no longer included as a priority.<sup>41</sup> As a result of limited IRS resources and the low prioritization by Collection in actively working preparer penalty assessments, TIGTA noted that the IRS collected just 15 percent of the penalties assessed against individual return preparers from calendar year (CY) 2012 to CY 2015.<sup>42</sup>

36 EITC Preparer Treatment Delivery Tool (Dec. 12, 2018). The actual audits are conducted by SB/SE.

37 IRS, *Auditing for Due Diligence Compliance*, <https://www.eitc.irs.gov/tax-preparer-toolkit/preparer-compliance-focused-and-tiered/auditing-for-due-diligence-compliance> (last visited Dec. 6, 2018).

38 IRS response to TAS information request (Aug. 2, 2018).

39 Although there is scholarly debate on how much of a deterrent effect penalties actually have on tax compliance. See Michael Doran, *Tax Penalties and Tax Compliance*, 46 HARV. J. ON LEGIS. 111-161 (2009). See also Research Study: *Do Taxpayers Respond to the Substantial Understatement Penalty? Analysis of Bunching Below the Substantial Understatement Penalty Threshold*, *infra*.

40 Erik Hoelzl, Erich Kirchler, and Ingrid Wahl, *Enforced Versus Voluntary Tax Compliance: The “Slippery Slope” Framework*, 29 J. ECON. PSYCHOL. 218-219 (2008).

41 The FY 2013, FY 2014, and FY 2015 Program Letters for Collection included the collection of tax return preparer penalties as a priority. The FY 2016 and FY 2017 Program Letters did not list collection of tax return preparer penalties as a priority.

42 TIGTA, Ref. No. 2018-30-042, *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct* 15 (July 25, 2018).

As a result of limited IRS resources and the low prioritization by Collection in actively working preparer penalty assessments, Treasury Inspector General for Tax Administration (TIGTA) noted that the IRS collected just 15 percent of the penalties assessed against individual return preparers from calendar year (CY) 2012 to CY 2015.

In addition to assessing penalties for preparer misconduct, the IRS may apply sanctions against unscrupulous preparers. The Secretary of the Treasury may (after notice and opportunity for a proceeding) suspend, disbar from practice, or censure representatives who are incompetent, are disreputable, violate regulations, or willfully and knowingly mislead or threaten the person being represented (or a prospective person to be represented).<sup>43</sup> In the first six months of CY 2018, the IRS reported only one disbarment, 34 suspensions, and zero censures.<sup>44</sup>

**FIGURE 1.7.5, OPR Disciplinary Actions, CY 2015 to CY 2018 (through June)<sup>45</sup>**

	CY 2015	CY 2016	CY 2017	CY 2018 (through June)
Disbarment	2	2	1	1
Suspension	61	57	46	34
Censure	0	3	1	0
<b>Total OPR Case Receipts</b>	<b>905</b>	<b>894</b>	<b>2,018</b>	<b>2,018</b>

In extreme cases, return preparers (enrolled or unenrolled) may be enjoined from preparing tax returns. Such a process requires coordination between SB/SE Exam, CI, IRS Office of Chief Counsel, and the Department of Justice.<sup>46</sup> Perhaps because an injunction against a return preparer requires a great deal of coordination, the IRS rarely imposes such sanctions.<sup>47</sup>

### The IRS Should Assert a More Active Role in the Voluntary Certification Process, Including Designing an Examination and Developing Training Materials

While it is true that the courts have enjoined the IRS from requiring testing and certification of tax return preparers, the IRS still has the responsibility to protect taxpayers.

As discussed above, the IRS already administers the AFSP, the voluntary certification program for unenrolled preparers. Currently, the IRS does not administer the knowledge-based comprehension test that participants must pass to obtain the AFSP Record of Completion. Rather, participants are referred

43 31 U.S.C. § 330.

44 Note that the Office of Professional Responsibility has oversight responsibility over Circular 230 tax professionals; it does not have jurisdiction over unenrolled preparers.

45 IRS, *OPR's Case Dispositions*, <https://www.irs.gov/tax-professionals/oprs-case-dispositions> (last visited Dec. 21, 2018).

46 IRM 4.32.2.2, *Overview of Abusive Transactions (AT) Program* (June 4, 2018); IRM 4.32.2.3, *Abusive Transactions Defined* (June 4, 2018).

47 In calendar year 2016, only 70 preparers were enjoined from preparing returns. TIGTA, Ref. No. 2018-30-042, *The Internal Revenue Service Lacks a Coordinated Strategy to Address Unregulated Return Preparer Misconduct* 16 (July 25, 2018).

to a list of continuing education providers who are responsible for the development and administration of the comprehension test. However, the National Taxpayer Advocate believes that because it owns this program, the IRS and the IRS alone should design the test that is administered to program participants.<sup>48</sup> This would ensure that the content covers the issues the IRS finds to be problematic.

One idea the IRS can consider as it develops its overall return preparer strategy is to tie in continuing education training to the abatement of preparer penalties. For example, if an unenrolled preparer is assessed a \$500 penalty at the conclusion of a due diligence audit, the IRS may be able to encourage that preparer to take a voluntary continuing education course by offering to abate all or a portion of the penalty upon passing the test.

### The IRS Should Ensure that Any References to the Directory of Federal Tax Return Preparers Are Not Misleading

The IRS maintains a public directory of federal tax return preparers to help taxpayers find return preparers with certain credentials and qualifications. This searchable and sortable database includes the name, city, state, and ZIP Code of preparers with valid PTINs—including attorneys, CPAs, EAs, enrolled retirement plan agents, and enrolled actuaries. The database also includes a list of participants who have completed the AFSP for that year.

While this database can be helpful to taxpayers, the IRS should be cautious in how it references the Directory of Federal Tax Return Preparers in its communication with taxpayers. For example, in the Appeals Letter 3808, *Docketed Acknowledgment and Conference (to Petitioner)*, taxpayers are referred to the Directory of Federal Tax Return Preparers, although (1) many return preparers listed in the directory may not be authorized to represent taxpayers (if they are not attorneys, CPAs, or EAs), and (2) even a registered return preparer (*i.e.*, one who participates in the AFSP) who prepared and signed the taxpayer's return may only be authorized under Circular 230 to provide limited representation with regard to an examination of that return and are specifically prohibited from otherwise representing the taxpayer.<sup>49</sup> It is misleading and potentially harmful for the IRS to reference the Directory of Federal Tax Return Preparers without adequately explaining the potential limited representation authorities of such preparers.

Although the IRS is prohibited from requiring unregulated preparers to undergo testing, this does not mean that preparers cannot obtain certification voluntarily, as a way of differentiating themselves from their competition. The IRS can lead the effort in the development and review of training material used by third-party certification programs.

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48 Continuing education providers could continue to administer the test, and the IRS can partner with these providers in designing the test, but the IRS alone should direct and design the content.

49 IRS, Circular 230, §10.3(f).

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Invite representatives from TAS to the cross-functional team that was established to develop a coordinated strategy to provide effective oversight of return preparers.
2. Develop a comprehensive plan to communicate the coordinated return preparer strategy to Circular 230 preparers and unenrolled preparers.
3. Develop a community-based, grassroots communication strategy for educating vulnerable taxpayer populations about how to select a competent return preparer and the risk of return preparer fraud.
4. Conduct analysis on the impact of penalty assessments and no change audits on preparers' behavior in subsequent years, and publish the findings.
5. Revise letters and notices (including Appeals Letter 3808) that reference the Directory of Federal Tax Return Preparers to ensure that appropriate caveats are clearly articulated.

## INTRODUCTION TO THE EXAMINATION PROCESS: Promoting Voluntary Compliance and Minimizing Taxpayer Burden In the Selection and Conduct of Audits

### WHY ARE IRS AUDITS IMPORTANT?

The IRS's primary purpose in selecting tax returns for examination or audit is to promote the highest degree of voluntary compliance.<sup>1</sup>

IRS audits are intended to detect and correct noncompliance of audited taxpayers as well as create an environment to encourage non-audited taxpayers to comply voluntarily. The IRS is authorized to examine books, papers, records, or other data and take testimony to determine the correctness of any return and the liability of any person for tax under Internal Revenue Code (IRC) § 7602(a).

The IRS conducts audits either via correspondence, office, or field audits.<sup>2</sup> Generally, correspondence audits are managed by mail for a single tax year and involve no more than a few issues that the IRS believes can be resolved by reviewing simple documents.<sup>3</sup> A field exam deals with more complex issues and involves a face-to-face meeting between the taxpayer and an IRS revenue agent at the taxpayer's home or place of business.<sup>4</sup> Finally, an office audit is conducted at a local IRS office and generally involves issues that are more complex than those found in correspondence exams but less complex than examinations conducted in the field.<sup>5</sup>

Traditional voluntary compliance has focused on deterrence theory. However, social science research indicates that the deterrence theory accounts for only a portion of the actual compliance rates and that social norms, personal values, and attitudes may have a larger impact on taxpayers' compliance decisions.<sup>6</sup> Studies have shown that to ensure a high level of voluntary tax compliance, taxpayers must have faith and trust in the fairness of the tax system.<sup>7</sup>

This year's Annual Report contains a research study in Volume 2 that explores the influence of tax audits on taxpayers' attitudes and perceptions.<sup>8</sup> Overall, taxpayers in the study who experienced audits reported higher levels of fear, anger, threat, and caution when thinking about the IRS and felt less protected by the IRS.<sup>9</sup> Taxpayers who experienced correspondence exams experienced a lower level of perceived justice compared to those who underwent office and field exams.<sup>10</sup>

1 Internal Revenue Manual (IRM) 1.2.13.1.10, *IRS Policy Statement 4-21* (June 1, 1974).

2 IRS Statement of Procedural Rules, Treas. Reg. § 601.105(b).

3 See National Taxpayer Advocate 2011 Annual Report to Congress vol. 2 71 (discussing the differences between field and correspondence audits). Large Business and International (LB&I) Division's correspondence audits, however, may be more complicated because they involve complex international tax issues.

4 See IRM 4.10.3.3.2, *Where to Conduct Interviews* (Feb. 26, 2016); IRM 4.1.5.3.2.6, *Revenue Agent versus Tax Compliance Officer* (Oct. 20, 2017).

5 *Id.*

6 National Taxpayer Advocate 2014 Annual Report to Congress 122.

7 See Erich Kirchler, Erik Hoelzl, and Ingrid Wahl, *Enforced versus Voluntary Tax Compliance: The "Slippery Slope" Framework*, 29 J. ECON. PSYCHOL. 219 (2008); see also Brian Erard, Matthias Kasper, Erich Kirchler, and Jerome Olsen, *Research Study: What Influence do IRS Audits Have on Taxpayer Attitudes and Perceptions? Evidence from a National Survey*, *infra*.

8 See Brian Erard, Matthias Kasper, Erich Kirchler, and Jerome Olsen, *Research Study: What Influence do IRS Audits Have on Taxpayer Attitudes and Perceptions? Evidence from a National Survey*, *infra*.

9 *Id.*

10 *Id.*

The study results suggest that IRS correspondence exams foster more distrust of the IRS compared to field or office exams.<sup>11</sup> The study also found that taxpayers who experienced an audit that resulted in a refund of tax perceived the IRS with less trust after the conclusion of the audit, suggesting that the taxpayers may have been frustrated to be selected for audit when they had overpaid their tax or felt that the IRS was unfair in its selection of their returns.<sup>12</sup> On the basis of these findings, the National Taxpayer Advocate believes that in selecting returns and evaluating audit cases, the IRS should research and consider how the audits build taxpayers' trust and affect future voluntary compliance.

### What is the Difference Between “Real” Versus “Unreal” Audits?

In addition to audits, the IRS conducts “compliance checks,” which should be evaluated along with the IRS’s audit program to determine how they affect taxpayers’ attitudes, perceptions, and future voluntary compliance. The IRS’s compliance checks involve a host of programs and procedures that require taxpayers to provide verification of tax return items via correspondence. Unlike the correspondence audit, however, these communications are not considered audits and do not afford the same protections provided to taxpayers undergoing the audit process.

The National Taxpayer Advocate has previously written about this issue of “real” vs. “unreal” audits.<sup>13</sup> These contacts or “unreal” audits comprise the majority of compliance contacts and eclipse “real” audit figures. In calendar year 2016, the IRS conducted over 8 million of these “unreal audits” while conducting only 1,033,356 “real” audits.<sup>14</sup> Although this introduction will focus on traditional audits, including correspondence, office, and field, many of the same issues and concerns raised in the IRS correspondence audit program apply to these “unreal audits.”

### What is the Impact of Traditional IRS Audits on Voluntary Compliance?

The IRS’s current examination program is not sufficiently building trust and promoting future voluntary compliance. Because the IRS’s traditional audit program has been reduced greatly over the last ten years, the IRS needs to focus on increasing voluntary compliance with the audits that it does conduct. During fiscal year (FY) 2007, the IRS audited 1.55 million returns, or 0.9 percent of all returns filed,<sup>15</sup> compared to FY 2017, where the IRS audited almost 1.1 million returns, or 0.5 percent of all returns filed. In FY 2017, approximately 88 percent of the IRS’s audits involved audits of individual income tax returns. The remaining audits consisted of corporate income tax returns (two percent), nontaxable returns (*e.g.*, partnership income tax returns) (three percent) and specialty tax returns (seven percent) as shown in Figure 1.0.1 below.<sup>16</sup>

11 See Brian Erard, Matthias Kasper, Erich Kirchler, and Jerome Olsen, Research Study: *What Influence do IRS Audits Have on Taxpayer Attitudes and Perceptions? Evidence from a National Survey*, *infra*.

12 *Id.*

13 National Taxpayer Advocate 2017 Annual Report to Congress 49-63 (Most Serious Problem: *Audit Rates: The IRS Is Conducting Significant Types and Amounts of Compliance Activities That It Does Not Deem to Be Traditional Audits, Thereby Underreporting the Extent of Its Compliance Activity and Return on Investment, and Circumventing Taxpayer Protections*); Nina E. Olson, “Real” vs. “Unreal” Audits and Why This Distinction Matters, NATIONAL TAXPAYER ADVOCATE BLOG (July 6, 2018), <https://taxpayeradvocate.irs.gov/news/nta-blog-real-vs-unreal-audits-and-why-this-distinction-matters?category=Tax News>.

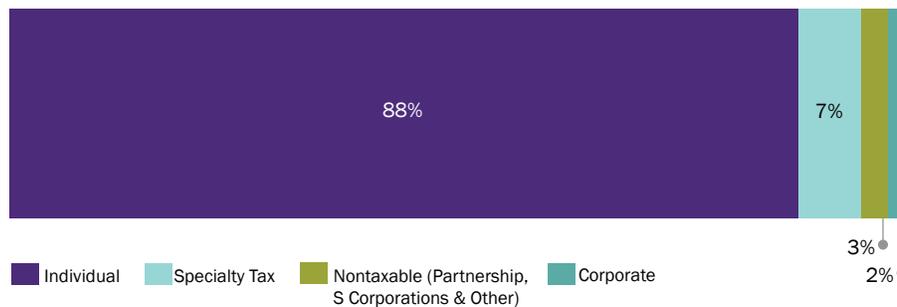
14 *Id.*

15 IRS Data Book, 2007, 23 (Mar. 2008).

16 IRS Data Book, 2017, Publication 55B, 21 (Mar. 2018). Specialty tax returns include employment tax returns, estate returns and gift tax returns. IRM 3.28.2.9 (June 21, 2018).

FIGURE 1.0.1<sup>17</sup>

## Returns Audited in FY 2017 by Return Type



This introduction will discuss examination programs operated by three IRS business operating divisions—Wage & Investment (W&I), Small Business and Self-Employed (SB/SE), and Large Business and International (LB&I). Each operating division is responsible for a specific segment of the taxpayer population and each creates an Examination or Compliance Plan based on coverage objectives and resources.<sup>18</sup> W&I handles taxpayers who pay taxes through withholding. W&I conducts all its audits via correspondence concerning issues such as refundable credits and some returns containing Schedule C, *Profit and Loss from Business*.<sup>19</sup>

SB/SE conducts correspondence audits, office audits, and field examinations of small business taxpayers with assets less than \$10 million, as well as examinations of self-employed and other individuals with income that extends beyond the level of W&I responsibility. LB&I is responsible for the tax compliance of businesses with assets of \$10 million or more, as well as individuals with high wealth or international tax implications. LB&I conducts field, office, and correspondence audits.

As stated above, correspondence exams can be particularly burdensome for many taxpayers, especially low income taxpayers. The IRS makes an already difficult situation, an audit, worse by failing to assign one IRS examiner to each taxpayer case, delaying responses to taxpayers' correspondence by more than 65 days, and frequently closing an exam without any personal contact. The lack of personal contact, in particular, results in a missed opportunity for the IRS to revise its audit selection filters or to update its educational materials to clarify confusing tax issues.<sup>20</sup> During FY 2017, the combined correspondence audits of individuals and of businesses comprised approximately 71 percent of all audits, while office audits and field audits comprised 10 and 19 percent, respectively, as depicted on Figure 1.0.2 below.<sup>21</sup>

17 IRS Data Book, 2017, Publication 55B, 21 (Mar. 2018).

18 IRM 4.1.1.2(1), *Exam Plan* (Oct. 25, 2017); IRM 4.1.21.2.2, *LMSB Compliance Plan* (Aug. 1, 2007); IRM 4.1.26.1.3(1), *Responsibilities* (Dec. 13, 2017).

19 IRM 4.19.11.2.1(10), *Procedures for Screening Individual Returns* (June 22, 2016).

20 See Most Serious Problem: *Correspondence Examination: The IRS's Correspondence Examination Procedures Burden Taxpayers and are Not Effective in Educating the Taxpayer and Promoting Future Voluntary Taxpayer Compliance*, *infra*.

21 IRS, Compliance Data Warehouse (CDW), Automated Information Management System (AIMS) fiscal year (FY) 2017 (Dec. 2018). Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

FIGURE 1.0.2<sup>22</sup>

## FY 2017 Closed Audits by Type of Audit



Although taxpayers who underwent office and field audits reported higher levels of perceived justice compared to correspondence audits, there is still much room for improvement for office and field exams in terms of earning the taxpayers' trust and perceptions of fair treatment, regardless of the result of the audit. The IRS could improve office audits by making several changes, including tracking results of audits that are appealed by the taxpayer, educating taxpayers on future compliance by adding taxpayer education as a quality attribute, and increasing the number of tax compliance officers (TCOs) in more locations throughout the United States, so that taxpayers feel their particular facts and circumstances are understood.<sup>23</sup>

SB/SE's field auditors could improve the taxpayers' audit experience by implementing certain practices, including sharing and discussing the audit plan with taxpayers and affording them the opportunity to propose changes to the plan before it is final, notifying taxpayers during an audit of any consultations with specialists, giving them the opportunity to discuss with the specialist any technical conclusions, and periodically studying taxpayers' filing behavior following field exams to determine the impact of the exam on future compliance.

22 IRS, CDW, AIMS FY 2017 (Dec. 2018). TAS defined Correspondence Audits as audits closed by Tax Examiners in the Wage and Investment Division (W&I) and the Small Business/Self-Employed Division (SB/SE), Office Audits as audits closed by Tax Compliance Officers in SB/SE, and Field Audits as audits closed by Revenue Agents in SB/SE and LB&I. Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

23 See Most Serious Problem: *Office Examination: The IRS Does Not Know Whether Its Office Examination Program Increases Voluntary Compliance or Educates the Audited Taxpayers About How to Comply in the Future*, *infra*.

## How Do the IRS Operating Divisions Select Returns for Audits?

### *SB/SE Audit Selection Processes*<sup>24</sup>

SB/SE selects returns for audit based on referrals, including IRS and external sources and taxpayer-initiated contacts, and selection methods called workstreams. SB/SE uses 33 workstreams to identify and review tax returns that may merit an audit.<sup>25</sup> About one-third of the workstreams use some form of automation to identify the returns that should enter the workstream.<sup>26</sup> All corporate returns with assets less than \$10 million and all individual returns are computer scored under the Discriminant Function (DIF) system.<sup>27</sup>

SB/SE identifies a pool of returns from which it selects a smaller group of returns to audit through the process of classification. SB/SE's Campus Classification function is generally responsible for identifying, selecting, and delivering returns to the various examination functions within the IRS.<sup>28</sup> During classification, an experienced examiner is expected to use his or her skills, technical expertise, local knowledge, and experience to identify hidden, as well as obvious, issues.<sup>29</sup> The classifier further determines whether the return should be examined, identifies the preliminary scope of the audit, and identifies a limited number of items that will be examined.<sup>30</sup> The classifier is also responsible for determining the type of examination to be conducted and the grade of the examiner appropriate for conducting the examination.<sup>31</sup>

Because field and office audits are face-to-face, SB/SE selects returns for field and office audit based on the geographic location of Revenue Agents and TCOs. The IRS does not conduct field or office exams in areas where no examiners or TCOs are located. Currently, there are no TCOs located in Alaska, Delaware, Montana, North Dakota, South Dakota, or Wyoming. Therefore, office exams are not conducted in these states.<sup>32</sup>

### *W&I Audit Selection Processes*<sup>33</sup>

W&I relies substantially on the Dependent Database (DDb), an automated computer application to select returns for audit.<sup>34</sup> Although W&I uses other sources, such as Integrity and Verification Operations (IVO) referrals, manual classification, referrals from other parts of the IRS, and outside

24 Government Accountability Office (GAO), *IRS Return Selection: Certain Internal Controls for Audits in the Small Business and Self-Employed Division Should be Strengthened*, GAO-16-103 (Dec. 2015). The GAO report discusses in detail SB/SE's process for selecting returns for audit.

25 GAO, *IRS Return Selection: Certain Internal Controls for Audits in the Small Business and Self-Employed Division Should be Strengthened*, GAO-16-103 (Dec. 2015).

26 *Id.*

27 IRM 4.1.2.7.2 (1), *Individual Returns* (Oct. 19, 2017); IRM 4.1.2.7.3(1), *Corporation Returns* (Oct. 19, 2017); IRM 4.1.2.7.4(1), *S Corporation Returns* (Oct. 19, 2017).

28 IRM 4.19.11.1.1, *Background* (Oct. 11, 2017).

29 IRM 4.1.5.3.3.1(3), *Standards for Classification* (Oct. 20, 2017).

30 *Id.*

31 IRM 4.1.5.3.3.1(6), *Standards for Classification* (Oct. 20, 2017).

32 IRS response to TAS information request (Oct. 15, 2018).

33 GAO, *IRS Return Selection: Wage and Investment Should Define Audit Objectives and Refine Other Internal Controls*, GAO-16-102 (Dec. 2015). The GAO report discusses in detail how W&I selects individual returns for audit.

34 *Id.* The IRS may not be using the Dependent Database effectively because it concentrates its Earned Income Tax Credit (EITC) audit resources on taxpayers with a noncompliance issue that is relatively minor (the relationship test), compared to an issue associated with 75 percent of all EITC qualifying child errors (the residency test). See also National Taxpayer Advocate 2015 Annual Report to Congress 248-260 (Most Serious Problem: *Earned Income Tax Credit (EITC): The IRS Is Not Adequately Using the EITC Examination Process as an Educational Tool and Is Not Auditing Returns With the Greatest Indirect Potential for Improving EITC Compliance*).

referrals for the selection of cases for correspondence audit, most of W&I's returns are selected from DDb.<sup>35</sup> DDb identifies potential non-compliance using data from various sources, including IRS databases, child custody information from the Department of Health and Human Services, the dependent and child birth information from the Social Security Administration, and prisoner information from the National Prisoner File, to determine the validity of the claims for tax credits and refunds.

### *LB&I Audit Selection Processes*<sup>36</sup>

LB&I is in the process of changing the way it addresses compliance, including how it identifies tax returns for audit, and is moving toward implementing issue-based projects it calls “campaigns.”<sup>37</sup> According to LB&I, a campaign is a compliance project focused on a specific compliance issue, such as partnerships underreporting income, rather than on using characteristics of the whole tax return for audit consideration.<sup>38</sup>

Campaigns could consist of an audit, or a less burdensome treatment, such as letters asking taxpayers to consider changing how they report the issue or providing additional guidance to help taxpayers accurately report the issue on their returns. Although the long-term plan is for the campaigns to constitute a significant part of the LB&I compliance program, currently, campaigns only comprise a small minority, only about six percent, of LB&I's audit work.<sup>39</sup>

LB&I is reportedly working to create metrics for the campaigns, but it is unclear how the IRS currently determines a campaign is not working and should be abandoned, or perhaps should be broadened and expanded. The IRS recently ended some of its campaigns, but has not developed a strategy to communicate the terminations publicly.<sup>40</sup> While LB&I implements campaigns, officials said that the existing selection methods it uses will continue to operate until LB&I decides whether to replace them.<sup>41</sup> LB&I officials also said that existing selection methods may be repurposed to operate within campaigns as well.<sup>42</sup>

Like W&I and SB/SE, LB&I identifies returns to audit using computerized scoring models and filters. Additionally, LB&I picks returns with specific issues for compliance initiative projects (CIP) or returns that are mandated for audit, such as refund returns that are subject to Joint Committee on Taxation review.<sup>43</sup> LB&I also identifies returns with known abusive tax schemes and gives additional scrutiny to individual tax returns with certain international tax issues.

35 Integrity and Verification Operations filters are not accurate resulting in a high rate of false positives. See Most Serious Problem: *False Positive Rates: The IRS's Fraud Detection Systems Are Marred by High False Positive Rates, Long Processing Times, and Unwieldy Processes Which Continue to Plague the IRS and Harm Legitimate Taxpayers*, *supra*.

36 GAO, *IRS Return Selection: Improved Planning, Internal Controls, and Data Would Enhance Large Business Divisions Efforts to Implement New Compliance Approach*, GAO-17-324 (Mar. 2017).

37 *Id.*

38 *Id.*

39 LB&I Business Performance Review, 3rd Quarter (Oct. 2018).

40 Amanda Athanasiou, *IRS Weighing Termination of LB&I Campaigns*, TAX NOTES TODAY (Nov. 8, 2018).

41 GAO, *IRS Return Selection: Improved Planning, Internal Controls, and Data Would Enhance Large Business Divisions Efforts to Implement New Compliance Approach* 9, GAO-17-324 (Mar. 2017).

42 *Id.*

43 The Joint Committee on Taxation, a Congressional committee, is required to review any proposed refund or credit of income or estate and gift taxes or certain other taxes more than \$2 million (\$5 million in the case of a C corporation) under IRC § 6405.

After returns are scored by computers or pulled for special projects and mandatory work, LB&I conducts another review called classification, in which LB&I staff identifies whether the return merits an audit and identifies specific issues for audit consideration. After the identified returns have been classified or otherwise reviewed for specific tax issues, they are listed in a queue for audit managers to assign to auditors. Auditors in the field assess whether the queued returns have large, unusual, or questionable features.

Once selected, LB&I audits fall into specific categories. Among the most common are Coordinated Industry Cases (CIC), Industry Cases (IC), and International Individual Compliance Cases (IIC). The CIC program puts large enterprises under continual audits. LB&I categorizes tax returns as CIC based on factors that include assets, gross receipts, and operating entities. CIC taxpayers are audited by a team, while IIC returns are usually audited by a single auditor. IIC has responsibility for auditing U.S. taxpayers living or working abroad, or in a U.S. Territory. IIC also identifies tax returns for audit for U.S. taxpayers, who hold income-producing assets in a foreign country or claim the foreign earned income exclusion, or foreign tax credit, and non-resident taxpayers who have a U.S. filing requirement.<sup>44</sup>

### What Do the Audit Results Show?

The distribution of audit results by audit type show some of the strengths and weaknesses of the IRS's examination programs in terms of promoting voluntary compliance.

As depicted on Figure 1.0.3<sup>45</sup> below, the IRS office and field audits show high agreed rates of about 45 percent on average. The IRS should be commended for these high agreed rates because agreement suggests that audit was an effective educational tool. That is, the taxpayer was educated about the issue, understands the mistake, and may be less likely to repeat the mistake in the future.

On the other hand, many of the field audits also concluded with “no change” in the tax adjustment.<sup>46</sup> This high no change rate suggests that both SB/SE and LB&I are not identifying the correct tax returns or issues for audit. Thus, both the IRS's and taxpayer's resources are being used ineffectively. Additionally, an audit study showed that the taxpayer may become more non-compliant after a no change audit.<sup>47</sup> The no change rate for corporate returns was 31 percent in FY 2017.<sup>48</sup> For corporations

44 IRM 4.60.4.5 (Feb. 3, 2015).

45 IRS, CDW AIMS, Individual Master File (IMF), Business Master File (BMF) FY 2017 (Nov. 2018). IRM 4.4.12.5.49.1, *No Change Disposal Codes* (June 1, 2002) defines a no change as case closed by the examiner with no additional tax due (disposal code 1 and 2). In the IRS response to TAS fact check (Dec. 20, 2018), SB/SE notes disposal code 1 as an agreed closure. TAS does not agree with SB/SE's definition because these cases do not require agreement from the taxpayer since there is no additional tax liability (see, e.g., IRM 4.10.8.2.2, *No Change with Adjustments Report Not Impacting Other Tax Year(s)* (Sept. 12, 2014)) and the taxpayers agreement, or disagreement, with the adjustment(s) as it pertains to another's year's liability is not known. Treasury Inspector General for Tax Administration (TIGTA) Report 2018-30-069 concurs with TAS's definition. Additionally, SB/SE includes 'partially agreed' cases (in which a taxpayer executes an agreement to some, but not all, of the proposed adjustments) as agreed cases in their reporting. TAS excludes those cases since the final disposition of the case is unknown (see, e.g., IRM 4.4.12.2.6, *Final Disposition After Input of Partial Assessment* (Sept. 17, 2015), which indicates that cases closed as partial agreements must be updated to reflect either a later agreement or the issuance of a notice of deficiency). Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

46 IRM 4.4.12.5.49.1, *No Change Disposal Codes* (June 1, 2002) defines a no change as case closed by the examiner with no additional tax due (disposal code 1 and 2).

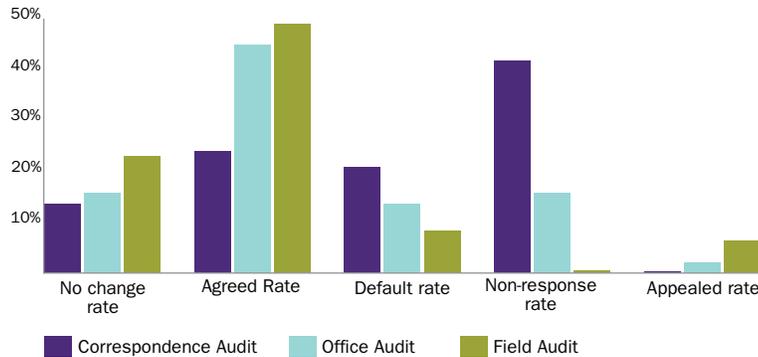
47 National Taxpayer Advocate 2015 Annual Report to Congress vol. 2, 67-100 (Research Study: Brian Erard, Matthias Kasper, Erich Kirchler, and Jerome Olsen, *Audit Impact Study*); see also Most Serious Problem: *Field Examination: The IRS's Field Examination Program Burdens Taxpayers and Yields High No-Change Rates, Which Waste IRS Resources and May Discourage Voluntary Compliance*, *infra*.

48 IRS Data Book, 2017, Publication 55B, 21 (Mar. 2018).

with total assets between 50 and 100 million, the no change rate was as high as 50 percent in FY 2017.<sup>49</sup> Similarly, for partnership returns and S corporation returns, the no change rate in FY 2017 was 43 percent and 29 percent, respectively.<sup>50</sup>

**FIGURE 1.0.3<sup>51</sup>**

**FY 2017 Closed Audit Results by Type of Audit**



49 IRS Data Book, 2017, Publication 55B, 21 (Mar. 2018).

50 *Id.*

51 IRS, CDW AIMS, IMF, BMF FY 2017 (Nov. 2018). IRM 4.4.12.5.49.1, *No Change Disposal Codes* (June 1, 2002) defines a no change as case closed by the examiner with no additional tax due (disposal code 1 and 2). In the IRS response to TAS fact check (Dec. 20, 2018), SB/SE notes disposal code 1 as an agreed closure. TAS does not agree with SB/SE's definition because these cases do not require agreement from the taxpayer since there is no additional tax liability (see, e.g., IRM 4.10.8.2.2, *No Change with Adjustments Report Not Impacting Other Tax Year(s)* (Sept. 12, 2014)) and the taxpayers agreement, or disagreement, with the adjustment(s) as it pertains to another's year's liability is not known. TIGTA Report 2018-30-069 concurs with TAS's definition. Additionally, SB/SE includes 'partially agreed' cases (in which a taxpayer executes an agreement to some, but not all, of the proposed adjustments) as agreed cases in their reporting. TAS excludes those cases since the final disposition of the case is unknown (see, e.g., IRM 4.4.12.2.6, *Final Disposition After Input of Partial Assessment* (Sept. 17, 2015), which indicates that cases closed as partial agreements must be updated to reflect either a later agreement or the issuance of a notice of deficiency). Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

For SB/SE and W&I correspondence exams combined, the audit results show a non-response rate of 40 percent and a default rate of 20 percent in FY 2017 as shown on Figure 1.0.3 above.<sup>52</sup> The 40 percent non-response rate indicates that taxpayers did not respond at all to the IRS's correspondence audit notice. In addition, of those taxpayers who did respond to the correspondence audit notices, 20 percent did not petition the Tax Court or sign an agreement after the issuance of the statutory notice of deficiency.<sup>53</sup>

Most of these correspondence audits involved audits of individual income tax returns of low income taxpayers with incomes of \$25,000 or less who claimed the Earned Income Tax Credit (EITC).<sup>54</sup> Approximately 38.6 percent or 361,360 of all individual income tax audits consisted of this group of taxpayers in FY 2017.<sup>55</sup> The high non-response and default rates suggest that it is especially difficult for taxpayers who claim the EITC to respond to the IRS timely and appropriately for several reasons, including the complexity of EITC eligibility requirements and complicated family living situations.<sup>56</sup>

### Most Serious Problems

In the three Most Serious Problems that follow, the National Taxpayer Advocate expresses concerns that IRS examinations fail to increase future voluntary compliance, do not measure voluntary compliance in terms of taxpayers' positive attitudes towards the IRS and educating taxpayers, and place undue burdens on taxpayers. The Most Serious Problems are:

- **CORRESPONDENCE EXAMINATION:** *The IRS's Correspondence Examination Procedures Burden Taxpayers and are Not Effective in Educating the Taxpayer and Promoting Future Voluntary Compliance;*
- **FIELD EXAMINATION:** *The IRS's Field Examination Program Burdens Taxpayers and Yields High No Change Rates, Which Waste IRS Resources and May Discourage Voluntary Compliance;* and
- **OFFICE EXAMINATION:** *The IRS Does Not Know Whether Its Office Examination Program Increases Voluntary Compliance or Educates the Audited Taxpayers About How to Comply in the Future.*

52 A default assessment is one made by the IRS subject to its authority under IRC §§ 6212 and 7602, where the taxpayer fails to file a petition with the U.S. Tax Court or sign an agreement after the issuance of a statutory notice of deficiency (SNOD). IRC § 7602 authorizes the IRS to conduct audits and assess all taxes imposed by Title 26. If the auditor determines that a deficiency of tax exists, subject to IRC § 6212, he or she may send the taxpayer a notice of deficiency by certified mail or registered mail; however, as restricted by IRC § 6213 the IRS may not make an assessment "until such notice has been mailed to the taxpayer, or until the expiration of such 90-day or 150-day period," or, if taxpayer has filed a timely petition with the Tax Court, until the decision of the Tax Court has become final. See also IRM 4.8.9.26, *Defaulted Notices* (July 9, 2013).

53 For the 20 percent of taxpayers who did not sign an agreement or petition the Tax Court after the issuance of the notice of deficiency, they are giving up crucial rights including their right to the only prepayment judicial forum where the taxpayer can appeal an IRS decision. See Most Serious Problem: *Statutory Notices of Deficiency: The IRS Fails to Clearly Convey Critical Information in Statutory Notices of Deficiency, Making it Difficult for Taxpayers to Understand and Exercise Their Rights, Thereby Diminishing Customer Service Quality, Eroding Voluntary Compliance, and Impeding Case Resolution*, *infra*; see also Most Serious Problem: *Pre-Trial Settlements in the U.S. Tax Court: Insufficient Access to Available Pro Bono Assistance Resources Impedes Unrepresented Taxpayers from Reaching a Pre-Trial Settlement and Achieving a Favorable Outcome*, *infra*.

54 IRS Data Book, 2017, Publication 55B, 21 (Mar. 2018).

55 IRS Data Book, 2017, Publication 55B, 21 (Mar. 2018). This percentage is derived from 361,360 divided by 933,785 which is the business and nonbusiness returns with Earned Income Tax Credit with under \$25,000 of total gross receipts divided by total individual income tax returns audited.

56 See Most Serious Problem: *Correspondence Exam: The IRS's Correspondence Examination Procedures Burden Taxpayers and are Not Effective in Educating the Taxpayer and Promoting Future Voluntary Compliance*, *infra*.

MSP  
#8**CORRESPONDENCE EXAMINATION: The IRS's Correspondence Examination Procedures Burden Taxpayers and Are Not Effective in Educating the Taxpayer and Promoting Future Voluntary Compliance****RESPONSIBLE OFFICIALS**

Mary Beth Murphy, Commissioner, Small Business/Self-Employed Division  
Ken Corbin, Commissioner, Wage and Investment Division

**TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and be Heard*
- *The Right to a Fair and Just Tax System*

**DEFINITION OF PROBLEM**

Internal Revenue Code (IRC) § 7602(a) provides the IRS with the authority to conduct examinations for the purposes of determining whether a tax return is correct, creating a return where the taxpayer has not filed, and determining a taxpayer's tax liability. In fiscal year (FY) 2017, the IRS audited almost 1.1 million tax returns (including business and individual returns), approximately 0.5 percent of all returns received that year.<sup>2</sup> During FY 2017, the IRS conducted approximately 71 percent of all audits (business and individual) by correspondence.<sup>3</sup> Proponents of correspondence examinations argue they are beneficial because they allow the IRS to audit many taxpayers without complex issues and minimize burden for them. However, in many cases, the issues deemed as "not complex" may involve complicated rules and procedures, or complicated fact situations, or both as in the case of the Earned Income Tax Credit (EITC). In addition, taxpayers audited by correspondence may suffer greater burden because of:

- The difficulty of sending and receiving correspondence (including having it considered at the right time);
- The lack of clarity in IRS correspondence; and
- The lack of a single employee assigned to the taxpayer's case.

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 IRS Data Book, 2017, Publication 55B, 21 (Mar. 2018). This number does not include certain returns, such as those of tax exempt and government entities, nor does it include other compliance contacts that can be considered "unreal" audits, and which make the number much higher. See National Taxpayer Advocate 2017 Annual Report to Congress 49-63 (Most Serious Problem: *Audit Rates: The IRS Is Conducting Significant Types and Amounts of Compliance Activities that It Does Not Deem to Be Traditional Audits, Thereby Underreporting the Extent of Its Compliance Activity and Return on Investment, and Circumventing Taxpayer Protections*).

3 IRS Data Book, 2017, Publication 55B, 22 (Mar. 2018).

For FY 2018 correspondence audits, the IRS took more than 65 days to respond to the majority of taxpayer replies in both EITC cases and non-EITC refundable credit cases.<sup>4</sup> During FY 2018, the Small Business/Self-Employed Division (SB/SE) exam employees answered the exam phone line only about 35 percent of the time<sup>5</sup> and, not surprisingly, SB/SE reported receiving only about 0.87 incoming calls per correspondence exam potentially because taxpayers could not get through.<sup>6</sup> These problems are exacerbated when the audited taxpayer is low income, has limited English proficiency, or there are other impediments that hinder communication during the audit.

An examination is primarily an education vehicle, so the taxpayer learns the rules, corrects mistakes, and can comply in the future. The tax assessed from the examination is a byproduct of the exam, but it is not the purpose. In fact, the IRS gains about twice as much from the long-term effects of an audit than it does from the actual audit itself.<sup>7</sup>

The National Taxpayer Advocate is concerned that:

- Audit selection procedures may lead to complex cases being audited by correspondence and a disproportionate burden on low income taxpayers;
- Insufficient training on complex issues for correspondence examiners may prevent them from correctly determining the liability or knowing when to transfer a case to an employee with specific expertise;
- A substantial number of taxpayers audited by correspondence face barriers to understanding and effectively participating in the audit;
- The IRS's correspondence is often confusing and does not provide sufficient time for the taxpayer to respond; and
- The IRS metrics do not consider taxpayer needs and preferences when determining the effectiveness of its correspondence exam program, and the IRS prioritizes measures such as cycle time and closures, which ignore the impact on the taxpayer.

## ANALYSIS OF PROBLEM

### Background

In the past ten years, the percentage of overall audits (including businesses and individuals) conducted by correspondence has remained steady, around 80 percent. However, overall audits have decreased substantially, as shown in Figure 1.8.1.

4 IRS, *W&I RICS Examination PAC 7F Reports* (Sept. 2018), combining correspondence statuses 55 and 57. See Internal Revenue Manual (IRM) 4.19.13.11, *Monitoring Overaged Replies* (Feb. 9, 2018) instruction to give either a 107 or a 150-day follow up expectation to taxpayers. For a discussion of the IRS's practice of mothballing overaged audit responses from taxpayers, see Case Advocacy section, *infra*.

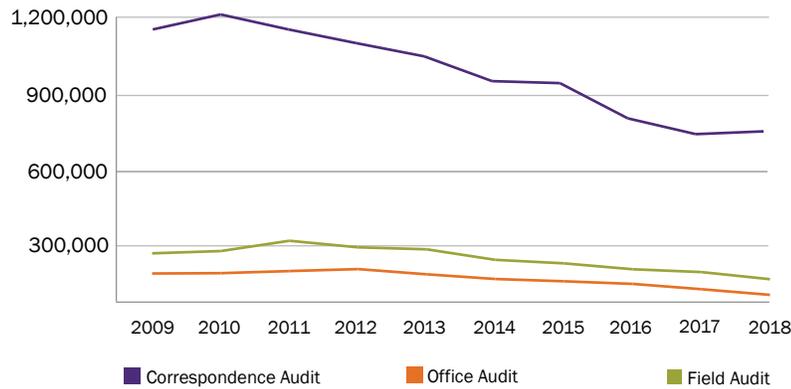
5 IRS, Product Line Detail (Enterprise Performance) Snapshot report (week ending Sept. 30, 2018).

6 IRS response to TAS information request (Oct. 24, 2018).

7 Jason DeBacker, Bradley T. Heim, Anh Tran, and Alexander Yuskavage, *Once Bitten, Twice Shy? The Lasting Impact of IRS Audits on Individual Tax Reporting* (Aug. 25, 2015) (working paper, Indiana University), <https://pdfs.semanticscholar.org/3833/61d62ea27f93deb89bf2c4b926bc5e96e14b.pdf>.

**FIGURE 1.8.1<sup>8</sup>**

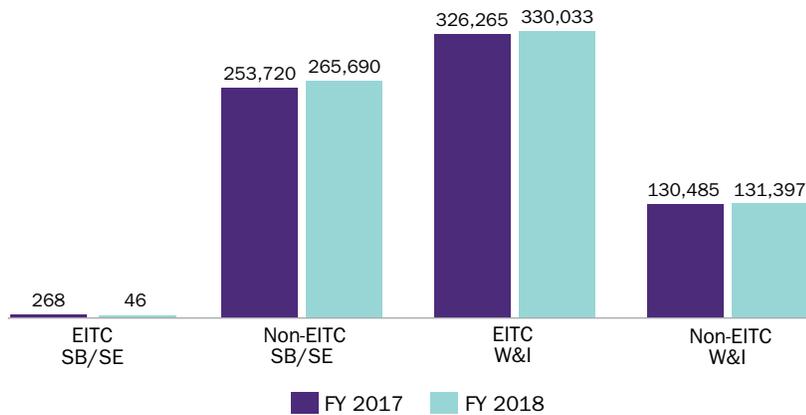
**Number of Correspondence Audits, Office Audits, and Field Audits Closed during Fiscal Years 2009 through 2018**



As shown in Figure 1.8.2, in FY 2018, SB/SE closed about 266,000 correspondence exams,<sup>9</sup> and Wage and Investment Division (W&I) closed about 461,000 correspondence exams, with EITC exams comprising about 72 percent of W&I’s exams.<sup>10</sup>

**FIGURE 1.8.2<sup>11</sup>**

**W&I and SB/SE Correspondence Audits Closed by EITC and Non-EITC for FY 2017 to 2018**



8 IRS response to TAS Fact Check (Dec. 20, 2018). For the purposes of this chart, correspondence audits include audits closed by campus tax examiners in the Wage and Investment Division (W&I) and Small Business/Self-Employed Division (SB/SE). Field audits include audits closed by revenue agents in SB/SE and Large Business and International (LB&I). Office audits include audits closed by tax compliance officers in SB/SE.

9 IRS response to TAS information request (Oct. 24, 2018).

10 *Id.*

11 IRS response to TAS fact check (Dec. 20, 2018). IRS response to TAS information request (Oct. 24, 2018).

SB/SE handles discretionary correspondence audits, including over 30 individual tax issues, such as nonrefundable credits, Schedule A and Schedule C expenses, and unreported income.<sup>12</sup> Of the nearly 447,000 Schedule C exams closed by SB/SE in the last two fiscal years, about 29 percent were conducted by correspondence. Schedule C correspondence exams represented about 38 percent of all correspondence exams conducted by SB/SE.<sup>13</sup> The IRS has indicated that it may conduct correspondence exams for some issues related to the new deduction for qualified business income under IRC § 199A, but has not projected the volume.<sup>14</sup>

SB/SE uses a variety of sources to determine which cases to audit. To determine the exam work plan, SB/SE reports looking at the staffing/hours to work returns, projections for inventory already started or delivered to the various Exam functions, and the Exam Planning Scenario Tool (EPST), which determines the mix of inventory for Discriminant Index Function returns for Correspondence Exam Discretionary as well as Field Revenue Agents (RAs) and Tax Compliance Officers (TCOs).<sup>15</sup> EPST provides scenarios of optimized mix by activity codes for Field (RA & TCO) and by project codes for Campus, based on historical business results.<sup>16</sup> Activity codes describe the financial scope of the return and its complexity, which help determine the appropriate type of examiner.<sup>17</sup> Project Codes identify a specific feature or item on a tax return that the IRS would like to monitor for compliance purposes, for example, Schedule A – Casualty Loss.<sup>18</sup>

Starting in FY 2016, W&I exclusively worked all new EITC correspondence exams.<sup>19</sup> The majority of the inventory in the Refundable Credits Examination Operation (RCEO) is derived from the computer program known as the Dependent Database (DDb).<sup>20</sup> In FY 2014, DDb identified more than 77 percent of the closed EITC audits.<sup>21</sup>

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- 12 See IRM 4.19.15.1 through 4.19.15.43 (Dec. 1, 2017). SB/SE does not specifically audit Earned Income Tax Credit (EITC), but they will make automatic adjustments to EITC, the American Opportunity Tax Credit, and the Child Tax Credit when the Adjusted Gross Income changes due to other audit adjustments, including changes to Schedule C income.
- 13 IRS response to TAS fact check (Dec. 20, 2018).
- 14 The IRS anticipates a low volume of IRC § 199A exams during FY 2019 since most examinations efforts during that fiscal year will be tax year 2017 and earlier returns. IRS response to TAS information request (Oct. 24, 2018).
- 15 Discretionary exams are conducted by choice, as opposed to EITC exams that are driven by the Revenue Protection Strategy or the refundable credits exams identified by risk based scoring criteria. See IRM 4.19.15.1.3, *Roles and Responsibilities* (Dec. 1, 2017); IRM 4.19.14.1.1, *Background* (Dec. 7, 2017); IRM 4.19.14.1.4, *Program Management and Review* (Dec. 7, 2017).
- 16 IRS response to TAS information request (Apr. 27, 2018). The activity code identifies the type of return examined, e.g., Form 1040 in a specified income range and the project code identifies the examination issue(s), e.g., EITC. See Document 6036 (October 2017).
- 17 IRM Exhibit 4.4.1-1, *Reference Guide* (Apr. 15, 2016). An activity code would present a brief description of the return such as: Non-Farm Business with Schedule C or F where Total Gross Receipts are between \$XX and \$XX, and Total Positive Income is less than \$XX. IRS, Document 6036, *Examination Division Reporting System Codes Booklet 18-24* (Oct. 2017). The activity codes include the actual dollar range, which TAS redacted here. “In general, total positive income is the sum of all positive amounts shown for the various sources of income reported on the individual income tax return, and thus excludes losses.” IRS 2017 Databook, October 1, 2016 to September 30, 2017, 33, <https://www.irs.gov/pub/irs-soi/17databk.pdf>.
- 18 IRS, Project Code Listing (Oct. 16, 2018).
- 19 IRS response to TAS information request (Oct. 24, 2018).
- 20 IRS response to TAS information request (June 22, 2018).
- 21 Government Accountability Office (GAO), *Certain Internal Controls for Audits in the Small Business and Self-Employed Division Should Be Strengthened*, 16-103 (Dec. 2015). The IRS may not be using the Dependent Database (DDb) effectively because it concentrates its EITC audit resources on taxpayers with a noncompliance issue that is relatively minor (the relationship test), compared to an issue associated with 75 percent of all EITC qualifying child errors (the residency test). National Taxpayer Advocate 2015 Annual Report to Congress 248-260 (Most Serious Problem: *Earned Income Tax Credit (EITC): The IRS Is Not Adequately Using the EITC Examination Process As an Educational Tool and Is Not Auditing Returns With the Greatest Indirect Potential for Improving EITC Compliance*).

**FIGURE 1.8.3, Top 5 Project Codes Examined by W&I and SB/SE Correspondence Audit Programs in FY 2010 and FY 2018<sup>22</sup>**

Project Description	FY 2010	Project Description	FY 2018
First Time Homebuyer Credit (Pre-Refund case)	281,446	EITC DDb (Pre-Refund)	105,765
EITC DDb (Pre-Refund)	160,647	Employee Business Expense	71,429
Non-Filer Program	113,612	Schedule C Expenses	57,657
Employee Business Expense	69,106	EITC-DDb Post refund	47,903
EITC-DDb Post Refund	67,841	Non-Filer Program	37,791

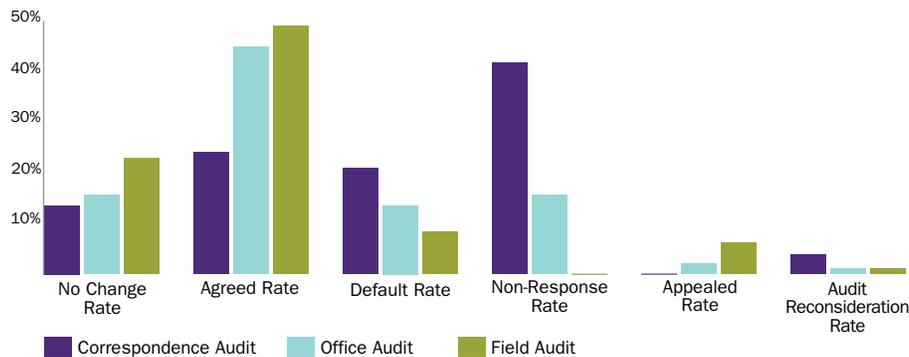
As shown in Figure 1.8.4, correspondence audits generally have lower no change rates, lower agreed rates, and significantly higher non-response rates. Appealed rates are surprisingly low for correspondence audits, given the low agreed rates, and may reflect taxpayers who are not receiving the correspondence or who have simply given up. On the other hand, audit reconsiderations are significantly higher for correspondence exams, which may reflect that taxpayers do not understand their appeal rights or do not realize what has happened until the IRS tries to collect from them.<sup>23</sup>

22 IRS, Compliance Data Warehouse (CDW) Audit Information Management System (AIMS) fiscal year (FY) 2010 and FY 2018 (Dec. 2018), and IRS response to TAS fact check (Dec. 20, 2018). TAS chose project codes because they show why a return was selected and reflect the number of EITC adjustments. Issue codes reflect the adjustment line item on the tax return, e.g., the issue code for exemptions means that the exemptions were in question and the examiner classified that issue. However, issue codes do not include EITC in the top five because the EITC is an automatic adjustment, so the examiner does not classify it. For example, changing the number of dependents would automatically calculate an EITC adjustment, but EITC would not be reflected in the issue code.

23 IRS, CDW AIMS, Individual Master File (IMF), Business Master File (BMF) FY 2017 (Nov. 2018). Correspondence Audit includes SB/SE and W&I closures. IRM 4.4.12.5.49.1, *No Change Disposal Codes* (June 1, 2002) defines a no change as case closed by the examiner with no additional tax due (disposal code 1 and 2). In the IRS response to TAS fact check (Dec. 20, 2018), SB/SE notes disposal code 1 as an agreed closure. TAS does not agree with SB/SE's definition because these cases do not require agreement from the taxpayer since there is no additional tax liability (see, e.g., IRM 4.10.8.2.2, *No Change with Adjustments Report Not Impacting Other Tax Year(s)* (Sept. 12, 2014)) and the taxpayers agreement, or disagreement, with the adjustment(s) as it pertains to another's year's liability is not known. Treasury Inspector General for Tax Administration (TIGTA) Report 2018-30-069 concurs with TAS's definition. Additionally, SB/SE includes 'partially agreed' cases (in which a taxpayer executes an agreement to some, but not all, of the proposed adjustments) as agreed cases in their reporting. TAS excludes those cases since the final disposition of the case is unknown (see, e.g., IRM 4.4.12.2.6, *Final Disposition After Input of Partial Assessment* (Sept. 17, 2015), which indicates that cases closed as partial agreements must be updated to reflect either a later agreement or the issuance of a notice of deficiency). IRS response to TAS fact check (Dec. 20, 2018) did not disagree with TAS's definitions for no change or agreed closures.

FIGURE 1.8.4<sup>24</sup>

### Closing Rates, Appealed Rate, and Audit Reconsideration Rate for Correspondence Audit, Office Audit, and Field Audit Closed in FY 2017



### Audit Selection Procedures May Lead to Complex Cases Being Audited by Correspondence and a Disproportionate Burden on Low Income Taxpayers

The IRS selects taxpayers for correspondence audit who have legally and factually complex issues, such as taxpayers claiming the EITC or Child Tax Credit (CTC) with differing relationships with the child claimed, complicated living situations where a child may not reside in one residence the entire year, and multiple sources of support for the child.<sup>25</sup> Taxpayers claiming the EITC with qualifying children must have a timely issued Social Security number (SSN) for the taxpayer and children; and there are three primary tests for each qualifying child:

- Age test: the child must be younger than the taxpayer and under 19 at the end of the calendar year (or under 24 if a full-time student, or any age if permanently and totally disabled).<sup>26</sup>
- Relationship test: the child must be the taxpayer's son or daughter, stepchild, foster or adopted child, or a descendant of any of them (*e.g.*, a grandchild), or a child who is a sibling, stepsibling, or half-sibling of the taxpayer, or a descendant of any of them (*e.g.*, a nephew or grandnephew).<sup>27</sup>
- Residence test: the child must live with the taxpayer for more than half the calendar year.<sup>28</sup>

Taxpayers entering correspondence exams may be unfamiliar with these rules because they may have had little involvement in filing their returns due to using a paid preparer. For EITC returns filed for tax year 2017, over half were prepared by paid preparers.<sup>29</sup>

24 IRS, CDW AIMS, IMF, BMF FY 2017 (Nov. 2018). FY 2017 will have a low audit reconsideration compared to older years due to the lack of time since the audit closing date. Correspondence Audit includes SB/SE and W&I closures. Field Audit includes SB/SE and LB&I closures.

25 GAO explains: "Verifying eligibility with residency and relationship requirements can be complicated and subject to interpretation," and the IRS itself acknowledges on its website: "EITC is complex and many special rules apply." GAO, *Comprehensive Compliance Strategy and Expanded Use of Data Could Strengthen IRS's Efforts to Address Noncompliance 16-475* (May 2016); IRS, *Do I Qualify for the Earned Income Tax Credit?* (Jan. 2017), <https://www.irs.gov/newsroom/do-i-qualify-for-the-earned-income-tax-credit>.

26 IRC § 152(c)(3).

27 IRC § 152(c)(2).

28 IRC § 152(c)(1)(B).

29 IRS, CDW, IRTF tax year 2017. (Dec. 2018).

In addition to using correspondence exams for complex family status issues, the IRS is increasingly using them to audit Schedule C taxpayers. SB/SE increased its percentage of Schedule C exams conducted by correspondence from 18 percent in FY 2017 to 24 percent in FY 2018.<sup>30</sup> The National Taxpayer Advocate is concerned about the IRS's potential use of correspondence exams for the IRC § 199A qualified business deduction, which involves highly complex issues as evidenced by the almost 47-page proposed regulations.<sup>31</sup>

### Insufficient Training on Complex Issues for Correspondence Examiners May Prevent Examiners From Correctly Determining the Liability or Knowing When to Transfer a Case to an Employee With Specific Expertise

Currently, tax examiners (who conduct correspondence audits for W&I and SB/SE) receive approximately 85 hours of basic income tax law training when they are hired. This training covers primarily items on the Form 1040, *U.S. Individual Income Tax Return*, but may be supplemented by training on additional deductions or specific issues.<sup>32</sup> For example, a correspondence examiner may subsequently complete the six-hour course #17877, *Schedule C Travel, Meals & Entertainment*, the 18-hour course #17874, *Mortgage Interest*, or the 1.5 hour course, #17872, *Schedule C Exams: Legal and Professional Fees*.

However, unlike TCOs and RAs conducting office and field examinations, tax examiners do not receive the full spectrum of training on Form 1040 and related forms and schedules in one comprehensive training session. This presents difficulties for the IRS and the taxpayer if an exam item expands or evolves into an issue for which the correspondence examiner has not yet been trained. For example, a review of a taxpayer's travel, meals, and entertainment expenses may reveal that the claimed deduction is actually a car and truck expense. If the tax examiner has not yet completed the two-hour course #17876, *Car and Truck*, the taxpayer's *right to pay no more than the correct amount of tax* may be impaired.<sup>33</sup>

### A Substantial Number of Taxpayers Audited by Correspondence Face Barriers to Understanding and Effectively Participating in the Audit

#### *Challenges for Low Income Taxpayers*

Almost half of all correspondence exams conducted by W&I and SB/SE for individual taxpayers are EITC exams, which necessarily involve low income taxpayers.<sup>34</sup> Taxpayers with lower incomes and

30 IRS response to TAS fact check (Dec. 20, 2018).

31 Qualified Business Income Deduction, 83 Fed. Reg. 40884 (proposed Aug. 16, 2018) (to be codified at Treas. Reg. §§ 1.199A-1 through 1.199A-6).

32 IRS response to TAS information request (May 21, 2018); IRS response to TAS information request (June 6, 2018); IRS response to TAS fact check (Dec. 20, 2018).

33 IRS response to TAS information request (May 21, 2018). Examiners have the option to transfer a correspondence exam to an area office if the issue is deemed too complex for correspondence and they receive managerial approval. However, without adequate technical training, an examiner might not recognize the issue should be reassigned to an employee with more or different expertise. IRM 4.19.13.15.1, *Transfers to Area Office* (Jan. 1, 2016).

34 Approximately 46 percent of correspondence examinations (excluding partnership audits conducted under the partnership audit rules of the Tax Equity and Fiscal Responsibility Act (TEFRA)) closed by W&I or SB/SE during FYs 2017 and 2018 were EITC exams. IRS response to TAS information request (Oct. 24, 2018). IRS response to TAS information request (Oct. 25, 2018). Almost three quarters of W&I correspondence exams closed during FY 2018 were EITC exams. IRS response to TAS fact check (Dec. 20, 2018).

education levels may have more difficulty understanding the tax laws and may rely on incompetent or unscrupulous return preparers.<sup>35</sup>

**FIGURE 1.8.5, Individual Returns Closed by Correspondence Audit in FY 2010 and FY 2018 by Activity Code.<sup>36</sup>**

	FY 2010	FY 2018
Form 1040PR/1040SS	382	157
Form 1040, EITC present & TPI <\$200,000 and Schedule C/F TGR <\$25,000 or EITC with No Schedule C/F	539,318	350,820
Form 1040, EITC present & TPI <\$200,000 and Schedule C/F TGR >\$24,999	12,495	7,728
Form 1040, No EITC present – TPI <\$200,000 and No Schedule C, E, F, or Form 2106	327,621	119,450
Form 1040, No EITC present – TPI <\$200,000 and Schedule E or Form 2106 but No Schedule C or F	128,243	97,133
Form 1040, No EITC present - Non-farm Business with Schedule C/F TGR <\$25,000 and TPI <\$200,000	84,937	74,485
Form 1040, No EITC present - Non-farm Business with Schedule C/F TGR \$25,000 - \$99,999 and TPI <\$200,000	31,442	17,736
Form 1040, No EITC present - Non-farm Business with Schedule C/F TGR \$100,000 - \$199,999 and TPI <\$200,000	11,999	10,076
Form 1040, No EITC present - Non-farm Business with Schedule C/F TGR >\$199,999 and TPI <\$200,000	1,885	3,333
Form 1040, No EITC present - Farm Business Not Classified Elsewhere and TPI <\$200,000	2,752	2,218
Form 1040, No EITC present - No Schedule C or F and TPI >\$199,999 and <\$1,000,000	53,931	16,783
Form 1040, No EITC present - Schedule C or F present and TPI >\$199,999 and <\$1,000,000	19,079	13,871
Form 1040, No EITC present - TPI >\$999,999	9,369	3,210

Correspondence examinations may be especially challenging for taxpayers with a language barrier, who may benefit from a face-to-face conversation. A 2014 TAS survey found that 70 percent of Hispanic consumers who are representative of the general Hispanic population age 18 and older were below 250 percent of the federal poverty level, making them more likely to claim refundable credits designed for low income taxpayers, which are generally audited by correspondence.<sup>37</sup> Furthermore, despite the high number of low income taxpayers who use paid preparers, low income taxpayers audited by correspondence may not be represented during the actual audit. A 2007 TAS study found the vast majority of EITC taxpayers audited were unrepresented.<sup>38</sup> Unrepresented taxpayers may not understand

35 In 2014, 80 percent of students leaving high school (including those who graduated and those who did not) from families with income in the top quartile enrolled in college, compared with only 45 percent from families in the bottom quartile. The Pell Institute, *Indicators of Higher Education Equity in the United States: 2016 Historical Trend Report* 20, [http://www.pellinstitute.org/downloads/publications-Indicators\\_of\\_Higher\\_Education\\_Equity\\_in\\_the\\_US\\_2016\\_Historical\\_Trend\\_Report.pdf](http://www.pellinstitute.org/downloads/publications-Indicators_of_Higher_Education_Equity_in_the_US_2016_Historical_Trend_Report.pdf).

36 IRS response to TAS fact check (Dec. 20, 2018).

37 Forrester Research, Inc., *The Taxpayer Advocate Service: Hispanic Underserved Analysis*, Q4 2014, 10 (Dec. 2014). See National Taxpayer Advocate 2015 Annual Report to Congress vol. 2, 101-110 (Research Study: *Understanding the Hispanic Underserved Population*).

38 National Taxpayer Advocate 2007 Annual Report to Congress vol. 2 94-116 (Study: *IRS Earned Income Credit Audits — A Challenge to Taxpayers*).

the correspondence or how to respond correctly without being able to ask questions face-to-face.<sup>39</sup> In the 2007 TAS study, TAS found that represented taxpayers were twice as likely to retain EITC after the audit, and they retained almost twice as much EITC, as unrepresented taxpayers.<sup>40</sup>

### *Difficulty in Receiving Mail and Having Correspondence Timely Reviewed*

Compounding other issues is the fact that taxpayers do not always receive correspondence from the IRS. During the last two fiscal years, approximately eight percent of statutory notices of deficiency (SNODs) in EITC correspondence exams and four percent of SNODs in non-EITC exams conducted by W&I were undeliverable.<sup>41</sup> Undeliverable mail rates for the SNODs in SB/SE correspondence exams were higher than W&I correspondence exams during FYs 2017 and 2018, indicating that small businesses and self-employed taxpayers may have more problems with receiving SNODs.<sup>42</sup>

Even when mail is received and responded to, it may not be worked in time. Although SB/SE and W&I report associating exam correspondence to the taxpayer's file within one or two days, examiners may not review the correspondence until much later.<sup>43</sup> As shown in Figures 1.8.6 and 1.8.7, W&I was delinquent in reviewing and responding to responses for the majority of correspondence audits.<sup>44</sup>

**FIGURE 1.8.6, W&I Response Time for FY 2018 EITC Audits<sup>45</sup>**

	Cases	Percentage
Responses 65 days old or greater	55,318	83%
Responses less than 65 days old	11,508	17%

**FIGURE 1.8.7, W&I Response Time for FY 2018 Non-EITC Refundable Credit Audits<sup>46</sup>**

	Cases	Percentage
Responses 65 days old or greater	22,487	79%
Responses less than 65 days old	5,881	21%

39 See Most Serious Problem: *Statutory Notices of Deficiency: The IRS Fails to Clearly Convey Critical Information in Statutory Notices of Deficiency, Making it Difficult for Taxpayers to Understand and Exercise Their Rights, Thereby Diminishing Customer Service Quality, Eroding Voluntary Compliance, and Impeding Case Resolution*, *infra*.

40 National Taxpayer Advocate 2007 Annual Report to Congress vol. 2 94-116 (Study: *IRS Earned Income Credit Audits — A Challenge to Taxpayers*).

41 TAS response to TAS information request (Oct. 25, 2018). See Most Serious Problem: *Statutory Notices of Deficiency: The IRS Fails to Clearly Convey Critical Information in Statutory Notices of Deficiency, Making it Difficult for Taxpayers to Understand and Exercise Their Rights, Thereby Diminishing Customer Service Quality, Eroding Voluntary Compliance, and Impeding Case Resolution*, *infra*.

42 IRS response to TAS fact check (Dec. 20, 2018).

43 IRS response to TAS information request (Oct. 25, 2018). IRS response to TAS information request (Oct. 24, 2018).

44 IRS responses are considered delinquent when the case is in status 55 or 57, which requires at least 65 days to have elapsed since receiving the taxpayer's reply. IRM 4.19.13.11, *Monitoring Overaged Replies* (Feb. 9, 2018); IRS, *W&I RICS Examination PAC 7F Reports* (Sept. 2018) (combining correspondence statuses 55 and 57). For a discussion of the IRS's inadequate handling of overaged audit responses from taxpayers, see Case Advocacy section, *infra*.

45 IRS, *W&I RICS Examination PAC 7F Reports* (Sept. 2018).

46 *Id.*

During 2018, taxpayers received an IRS “Interim Letter” informing them of delays of four, five, or, in many cases, six months just for the IRS to review the taxpayer’s correspondence.<sup>47</sup> Because the IRS only provides taxpayers with 30 days to provide documentation in a correspondence exam, these delays may appear patently unfair to the taxpayer, harming trust in the tax system and negatively affecting voluntary compliance.<sup>48</sup>

Since many correspondence exams are conducted pre-refund, taxpayers may not receive their refunds until the filing season of the next year.<sup>49</sup> TAS elevated the concern to W&I management, who attributed the long wait times to attrition losses and a heavy volume of mail receipts. The IRS waits at least 105 days after issuing the SNOD to allow for a taxpayer response before proceeding to assess the tax by default.<sup>50</sup> However, the SNOD may go out before the IRS considers the taxpayer’s examination response (including substantiating documents) because the system has advanced the case to the next stage and will not permit the employee to stop it.<sup>51</sup>

### *Inability To Reach the Employee Who Evaluates the Taxpayer’s Response*

Even where the IRS receives the taxpayer’s correspondence and reviews it, taxpayers in correspondence exams may not be able to speak to an employee familiar with the case because the IRS does not assign a single employee to each taxpayer’s case, as directed by the IRS Restructuring and Reform Act of 1998 (RRA 98).<sup>52</sup> The IRS will assign the case to a tax examiner if it determines a reply “needs technical assistance or evaluation of records sent by the taxpayer.”<sup>53</sup>

Furthermore, because IRS correspondence does not include the contact information of the employee who reviewed the taxpayer’s reply, the taxpayer cannot ask questions of the person who made the decision.<sup>54</sup> Once a tax examiner reviews a taxpayer’s documentation, makes an evaluation, and creates a letter to the taxpayer explaining why the documentation is not sufficient, such a letter should include the employee’s name and contact information. RRA 98 states: “...any manually generated correspondence received by a taxpayer from the Internal Revenue Service shall include in a prominent manner the name, telephone number, and unique identifying number of an Internal Revenue Service employee the taxpayer may contact with respect to the correspondence.”<sup>55</sup> By not including this information, the IRS may be violating the law and is impairing the taxpayer’s *right to challenge the IRS’s position and be heard*.

47 Letter 3500, *Interim Letter to Correspondence from Taxpayer*. See Systemic Advocacy Management System (SAMS) issues 39961, 39948, 39794, 39786, 39779, 36457, 36121, 35726, and 34740 documenting use of Letter 3500 and chronic delays in responding to taxpayer correspondence.

48 For a discussion of how perceived fairness affects voluntary compliance, see Erich Kirchler, Erik Hoelzl, and Ingrid Wahl, *Enforced versus Voluntary Tax Compliance: The “Slippery Slope” Framework*, 29 J. ECON. PSYCHOL. 218-219 (2008).

49 During 2018 through the end of October, the IRS sent out approximately 176,000 CP 75 *Exam Initial Contact Letter – EIC – Refund Frozen* to taxpayers, indicating that it was holding their refunds pending a correspondence examination. The average cycle time for a correspondence audit in W&I during the last two fiscal years was about 190 days and 229 for SB/SE. IRS response to TAS information request (Oct. 25, 2018); IRS response to TAS information request (Oct. 24, 2018).

50 IRM 4.19.10.1.5.2, *Standard Suspense Periods for Correspondence Examination* (Dec. 8, 2017).

51 See IRM 4.19.13.10.6, *Taxpayer Requests Additional Time to Respond*, 7-8 (Mar. 30, 2018).

52 Pub. L. No. 105-206 § 3705(b), 112 Stat. 685, 777 (1998). See National Taxpayer Advocate 2014 Annual Report to Congress 134-144 (Most Serious Problem: *Correspondence Examination: The IRS Has Overlooked the Congressional Mandate to Assign a Specific Employee to Correspondence Examination Cases, Thereby Harming Taxpayers*).

53 IRM 4.19.13.10, *Taxpayer Replies* (Feb. 20, 2018).

54 See, e.g., Letter 525, *General 30 Day Letter* (Sept. 2014).

55 Pub. L. No. 105-206, § 3705(a) (1998).

The IRS may not know how many taxpayers are trying to reach the IRS about a correspondence exam because taxpayers cannot reach an employee at all. During FY 2018, the SB/SE exam phone line only had a 61 percent level of service, with only 35 percent of calls being answered by an exam employee, and about 17 percent routed to an automated message.<sup>56</sup> W&I reports receiving an average of only about 1.6 incoming calls per correspondence exam during the last two fiscal years, and SB/SE reports only about 0.8 incoming calls per correspondence exam.<sup>57</sup> A 2010 IRS analysis found that 62 percent of correspondence exam callers were repeat callers.<sup>58</sup>

In many cases, there is no personal contact before closing a case. In FY 2018, about 42 percent of W&I and SB/SE correspondence audits were closed with no personal contact.<sup>59</sup> During FYs 2017 and 2018, W&I reported an average of 0.09 outgoing calls per correspondence exam—approximately one call for every 11 cases.<sup>60</sup> The IRM touts: “Because the ACE [Automated Correspondence Exam] system will automatically process the case through creation, statutory notice and closing, tax examiner (TE) involvement is eliminated entirely on no-reply cases. Once a taxpayer reply has been considered, the case can be reintroduced into ACE for automated Aging and Closing in most instances.”<sup>61</sup> Because examinations are an opportunity for the taxpayer to show the IRS that it is wrong (or why the taxpayer believes the IRS is wrong), closing an exam with no personal contact means the IRS misses an opportunity to fix its filters or update its educational materials to clarify confusing issues. Further, TAS has found that outgoing contacts can increase the response rate for taxpayers, reduce the average cycle time of the exam, and increase the taxpayer agreed rate—which not only saves the IRS resources, but may mean the taxpayer better understood the exam and why the return was incorrect.<sup>62</sup>

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**TAS has found that outgoing contacts can increase the response rate for taxpayers, reduce the average cycle time of the exam, and increase the taxpayer agreed rate—which not only saves the IRS resources, but may mean the taxpayer better understood the exam and why the return was incorrect.**

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56 IRS, Product Line Detail (Enterprise Performance) Snapshot report (week ending Sept. 30, 2018).

57 IRS response to TAS information request (Oct. 24, 2018); IRS response to TAS information request (Oct. 25, 2018).

58 Thirteen percent of correspondence exam callers called more than eight times. POP Team Recommendations, Solutions to Improve Taxpayer Satisfaction in Correspondence Examination Briefing Document (June 21, 2010).

59 IRS response to TAS fact check (Dec. 20, 2018).

60 *Id.*

61 IRM 4.19.20.2, *Automated Correspondence Exam Overview (ACE)* (Jan. 8, 2015).

62 The IRS selected 900 correspondence exam cases for a test group in which Exam telephoned the taxpayers ten days after the initial contact letter and again just prior to issuing the statutory notice of deficiency (cases were randomly selected from Project Codes 0261 and 0289 inventory via the DDb starting in cycle 2011-04 and continuing through cycle 2011-18). For those taxpayers successfully contacted, the response rate was 61 percent compared to 43 for the control group, the average cycle time was 21 days less than the control group, and the agreed rate was 30 percent compared to just 20 percent for the control group. TAS, *Earned Income Tax Credit (EITC) Enhanced Communication Test (CEEET)* White Paper (Nov. 2012).

### The IRS's Correspondence Is Often Confusing and Does Not Provide Sufficient Time to Respond

A past TAS survey of taxpayers who were audited on the EITC found that more than 25 percent of them did not understand the IRS audit notice was telling them they were under audit, and about half didn't understand what they needed to do in response to the audit letter.<sup>63</sup> This lack of awareness is not limited to low income taxpayers claiming refundable credits. A study of self-employed taxpayers audited by correspondence between 2010 and 2015 found 39 percent of taxpayers did not recall they had been audited.<sup>64</sup>

In a TAS study of enhanced communication during EITC correspondence audits, Exam forwarded almost 700 cases to TAS that were closed other than as “no change” or “agreed” and TAS was able to contact 37 percent of these taxpayers. In 44 percent of the cases, the taxpayers acknowledged they were ineligible for the EITC, but only two percent of these 44 percent said they understood they were ineligible prior to TAS's contact.<sup>65</sup> Taxpayers who understand what they did wrong may avoid making the same mistakes in the future. Further, this taxpayer education may promote voluntary compliance because multiple studies show that increasing knowledge of tax law results in a higher willingness of those taxpayers to comply.<sup>66</sup> However, when asked about procedures for educating audited taxpayers to avoid repeat mistakes, W&I stated: “The document request and publications included in the notices inform taxpayers of the tax law requirements and examples of documentation that can be provided to support the audit issues.”<sup>67</sup>

The IRS correspondence and forms are clearly inadequate to inform and educate taxpayers. The CP 75, *Exam Initial Contact Letter – EIC – Refund Frozen*, one of the most common initial contact letters in correspondence exams, demonstrates why taxpayers may not understand what documentation is requested.<sup>68</sup> The CP 75 states at the top that the IRS is auditing the taxpayer's return, which may help alleviate confusion over whether the taxpayer is being audited. However, the CP 75 refers the taxpayer to Form 886-H-EIC to understand which documents a taxpayer must send in to prove EITC eligibility. As shown in Figure 1.8.8, this form is particularly confusing because it asks taxpayers to submit information to prove different residency requirements without clearly telling the taxpayer which documents may be submitted and which may fulfill some of or all of the different requirements.

63 National Taxpayer Advocate 2007 Annual Report to Congress vol. 2, 103 (Study: *IRS Earned Income Credit Audits — A Challenge to Taxpayers*).

64 National Taxpayer Advocate 2017 Annual Report to Congress vol. 2, 163 (Matthias Kasper, Sebastian Beer, Erich Kirchler & Brian Erard, Research Study: *Audits, Identity Theft Investigations, and Taxpayer Attitudes: Evidence from a National Survey*).

65 TAS, *Earned Income Tax Credit (EITC) Enhanced Communication Test (CEEET) White Paper* (Nov. 2012).

66 *Id.*

67 IRS response to TAS information request (June 22, 2018).

68 In FY 2018 the volume of CP75 notices were: CP75, 181,342; CP75A, 48,573; CP75C, 107; and CP75D, 17,949. IRS, CDW, *Notice Delivery System (NDS) FY 2018* (Dec. 2018).

FIGURE 1.8.8, Excerpt of Question 1 from Form 886-H-EIC

Form <b>886-H-EIC</b> (October 2018)			Department of the Treasury—Internal Revenue Service <b>Documents You Need to Send to Claim the Earned Income Credit on the Basis of a Qualifying Child or Children for Tax Year 2018</b>		
Taxpayer name		Taxpayer identification number		Tax year	
<p>To get Earned Income Credit (EIC), the child must have lived with you, be related to you and be a certain age. Para recibir el Crédito por Ingreso del Trabajo (EIC, por sus siglas en inglés), el niño tiene que haber convivido con usted, ser su pariente, y tener una edad específica. Visite IRS.gov/eitc para buscar la versión en español del Formulario 886-H-EIC (SP) (May. 18-2018) o llame al 1-800-829-3675. Visit IRS.gov/eitc to find out more about who qualifies for EIC.</p>					
<p><b>1. Each child that you claim must have lived with you for more than half of 2018* in the United States. The United States includes the 50 states and the District of Columbia. It doesn't include Puerto Rico or U.S. possessions such as Guam.</b></p> <p><small>*Certain times that you, or the child, is temporarily away from home due to special circumstances as long as the child lived with you. Examples include illness, college, business, vacation, military service or detention in a juvenile facility.</small></p>					
<p>To prove the child lived with you in the United States, the document(s) must have:</p> <ul style="list-style-type: none"> <li>your U.S. address, your name, and the child's name. If you use a P.O. Box as your mailing address, you must send it registered mail, first-class, or by Air Application stamped by the Post Office.</li> <li>the dates in 2018 the child lived at the same address as you must cover more than half of 2018.</li> <li>if the document has the child's name and your address but not your name, you need to send in another document with your name showing the same address.</li> </ul>		<p>If you can send one or more of the following documents to prove the child lived with you for more than half of 2018:</p> <ul style="list-style-type: none"> <li>school records (you may need to send one or more school records)</li> <li>medical records from doctors, hospital or medical clinic (communication records may not include all the necessary information)</li> <li>adoption or child placement documents</li> <li>court records</li> </ul>		<p>Or, send dated statements on letterhead from:</p> <ul style="list-style-type: none"> <li>the child's school</li> <li>the child's childcare provider (not a relative)</li> <li>the child's health care provider, doctor, nurse or clinic</li> <li>a social service agency</li> <li>a placement agency official</li> <li>your employer</li> <li>an Indian tribal official</li> <li>your landlord or property manager</li> <li>a piece of mailing</li> <li>others.</li> </ul>	

A taxpayer reading this form may wonder: What kind of document is sufficient to prove residency in the United States? Can only the documents in the second column related to proving the child lived with the taxpayer be used to show residency in the United States? Are the documents in the third column alternatives for both the first and the second column? What information must be included on a dated statement? Would a school record issued at the end of the year demonstrate residency for more than half the year, or would two be required? These questions could go on and on but, unfortunately, a taxpayer has only 30 days to seek clarification from the IRS and provide the records. Although taxpayers can request an extension of time to provide information, it appears either not many EITC taxpayers take advantage of this or not many of these requests are granted. During the last two fiscal years, W&I granted approximately 2,100 of these requests for additional time to respond, compared to SB/SE, which granted approximately 27,000.<sup>69</sup>

Furthermore, without an IRS employee being able to view the record a taxpayer is proposing to submit, the examiner may not know that such a record would be inadequate until after the taxpayer already mails it in.<sup>70</sup> Then, assuming the documentation is not accepted, instead of a conversation about how to remedy the problem, the taxpayer would receive a “30-day letter,” indicating how the IRS proposes to adjust the return and providing the taxpayer a 30-day window to provide further documentation before the IRS issues the SNOD.<sup>71</sup> In some cases, the taxpayer may receive the 30-day letter at the initiation of the audit, where the IRS combines the initial contact letter and the preliminary report into

69 Approximately 72 percent of W&I correspondence exams are EITC exams. Starting in 2016, SB/SE started no new EITC correspondence audits. IRS response to TAS information request (Oct. 24, 2018); IRS response to TAS information request (Oct. 25, 2018). Neither operating division could provide the number of denied requests for additional time to provide documentation.

70 Virtual service delivery and other videoconferencing technology could mitigate this problem by allowing a taxpayer to show records to an IRS employee in real time. See National Taxpayer Advocate 2014 Annual Report to Congress 154-162 (Most Serious Problem: *Virtual Service Delivery: Despite a Congressional Directive, the IRS Has Not Maximized the Appropriate Use of Videoconferencing and Similar Technologies to Enhance Taxpayer Services*).

71 IRC § 6213(a). Once a taxpayer receives the Statutory Notice of Deficiency (SNOD), the taxpayer may still provide documentation to the IRS, but the 90-day period for petitioning the U.S. Tax Court to challenge the liability before paying has begun.

a “combo-letter.” This letter confuses the taxpayer and sends a message that the IRS has already made a preliminary decision about the taxpayer’s case without even reviewing the taxpayer’s documentation.

**The IRS Metrics Do Not Consider Taxpayer Needs and Preferences When Determining the Effectiveness of Its Correspondence Exam Program, and the IRS Prioritizes Measures Such as Cycle Time and Closures, Which Ignore the Impact on the Taxpayer**

SB/SE points to the following metrics for measuring its examination program:

1. Full time employees
2. Closures and new starts by types of return
3. Inventory
4. Cycle time
5. Employee engagement index
6. Customer satisfaction
7. Reconsiderations
8. Quality score<sup>72</sup>

W&I provided an even shorter list in response to TAS, highlighting only three metrics included in its FY 2017 final Business Performance Review:

1. Cycle time
2. No change rate
3. Accuracy rate<sup>73</sup>

Although customer satisfaction may affect voluntary compliance, this measure fails to capture taxpayers who did not participate in the audit by not responding.<sup>74</sup> The IRS should measure response rates to determine how many taxpayers participated and use this information to tailor its correspondence or contacts for certain issues that resulted in low participation rates. Further, the metrics overall are inadequate to determine the effectiveness of the correspondence examination program in terms of choosing the best cases to audit, educating the taxpayer, and increasing voluntary compliance. In addition to customer satisfaction surveys, the IRS could use surveys to gauge how well taxpayers understand the audit. As discussed above, a 2007 TAS study found that more than 25 percent of EITC taxpayers audited were not even aware they were being audited.<sup>75</sup> A metric that captured an agreement rate would be more meaningful in determining effectiveness of compliance education than the summary “change” rate by which IRS computes its return on investment because it would suggest the taxpayer understands the error and will avoid making it again.

The IRS could also capture data regarding whether taxpayers understand the information they need to provide by surveying or conducting focus groups with taxpayers and looking at what types of documentation taxpayers frequently sent that were deemed insufficient. This could help the IRS better

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<sup>72</sup> IRS response to TAS information request (Apr. 27, 2018).

<sup>73</sup> IRS response to TAS information request (June 22, 2018).

<sup>74</sup> SB/SE Campus Exam Mail Customer Satisfaction Report, SB/SE Research TM20349 (Aug. 2018).

<sup>75</sup> National Taxpayer Advocate 2007 Annual Report to Congress vol. 2 103 (Study: *IRS Earned Income Credit Audits — A Challenge to Taxpayers*).

inform taxpayers about exactly what documentation is acceptable and may even provide an impetus for the IRS accepting additional forms of documentation as a result of what the surveys show.

Although SB/SE reports audit reconsideration numbers,<sup>76</sup> it does not do so in a meaningful way because it compares only the sheer number of audit reconsiderations for field audits and correspondence audits without looking at the percentage. Further, the IRS should measure how many correspondence audits result in in appeals conferences and the result of those conferences. Additionally, the IRS should track the number of appeals to the U.S. Tax Court, including what percentage resulted in a lower liability or a full concession by the IRS, to understand where greater communication or better employee training is needed.<sup>77</sup>

Finally, neither W&I nor SB/SE measure how taxpayers perceive the IRS and how they feel about paying taxes after a correspondence audit.<sup>78</sup> A recent TAS study found that taxpayers audited by correspondence report a lower sense of fairness in the examination and are more likely to hold negative views towards the IRS than individuals audited in-person.<sup>79</sup>

Analyzing how correspondence audits affect taxpayer attitudes towards the IRS, including filing and paying taxes, would go beyond just looking at whether a taxpayer was satisfied with the customer service received during the audit. The IRS could gather data to analyze filing and payment compliance in the years following an audit to determine the effect on future behavior.

## CONCLUSION

The IRS's correspondence examination program burdens taxpayers and misses opportunities to educate the taxpayer. The IRS is ignoring important measures such as the resulting impact on voluntary compliance and taxpayer attitudes. Focusing on metrics like closures and cycle time has allowed the IRS to ignore the taxpayer perspective. Failing to assign an employee to a taxpayer's case, not allowing the taxpayer to speak with the examiner making decisions about the taxpayer's case, closing cases with little or no personal contact, and asking taxpayers to wait six months or more for the IRS to consider documentation directly undermine the taxpayer's *right to challenge the IRS's position and be heard*, and impair *the rights to be informed, to quality service, to pay no more than the correct amount of tax, and to a fair and just tax system*.

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76 IRS response to TAS information request (Oct. 24, 2018).

77 A 2012 TAS study found taxpayers in EITC cases that were fully conceded by the IRS called the IRS on average five times after petitioning the U.S. Tax Court; yet, only one fifth of the cases were conceded due to the hazards of litigation. National Taxpayer Advocate 2012 Annual Report to Congress vol. 2 87.

78 SB/SE Campus Exam Mail Customer Satisfaction Report, SB/SE Research TM20349 (Aug. 2018). The taxpayer may add open-ended comments to the customer satisfaction survey, but the survey does not measure the taxpayer's perception of fairness.

79 See Brian Erard, Matthias Kasper, Erich Kirchler, and Jerome Olsen, Research Study: *What Influence do IRS Audits Have on Taxpayer Attitudes and Perceptions? Evidence from a National Survey*, *infra*.

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Require at least one personal contact between an IRS employee and the taxpayer (this can be satisfied by an outgoing or incoming phone call) before closing a correspondence examination.
2. Measure taxpayers' filing compliance (including filing a return, making an error on a return, and underreporting taxes on a return) following correspondence examinations and apply this data to guide audit selection based on the resulting impact on compliance.
3. Continue to assign a single employee for a correspondence examination when the IRS receives a response from the taxpayer either by phone or correspondence, and expand on this right by retaining this employee as the single point of contact throughout the remainder of the exam.
4. Per RRA 98 § 3705(a), place on outgoing taxpayer correspondence the name and telephone number of the tax examiner who reviewed the taxpayer's correspondence where a tax examiner has reviewed and made a determination regarding that specific documentation.
5. Conduct surveys of taxpayers following correspondence examinations to gauge their understanding of the examination process and their resulting attitudes towards the IRS and towards filing and paying taxes.
6. Collect data regarding which forms of documentation taxpayers sent in a correspondence examination that were deemed insufficient and revise existing correspondence examination letters to better explain documentation requirements.
7. End the practice of using the combination letter and provide taxpayers with an initial contact prior to issuing the preliminary audit report.

MSP  
#9**FIELD EXAMINATION: The IRS's Field Examination Program Burdens Taxpayers and Yields High No Change Rates, Which Waste IRS Resources and May Discourage Voluntary Compliance****RESPONSIBLE OFFICIALS**

Mary Beth Murphy, Commissioner, Small Business/Self-Employed Division

Douglas O'Donnell, Commissioner, Large Business and International Division

**TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to a Fair and Just Tax System*

**DEFINITION OF PROBLEM**

Internal Revenue Code (IRC) § 7602(a) provides the IRS with the authority to conduct examinations to determine whether a tax return is correct, to create a return where the taxpayer has not filed, and to determine a taxpayer's tax liability. In fiscal year (FY) 2017, the IRS conducted only 29 percent of all audits and 23 percent of individual income tax return audits in the field or in an office, with the remaining conducted by correspondence.<sup>2</sup> Both IRS operating divisions conducting field audits, Small Business/Self-Employed (SB/SE) and Large Business and International (LB&I), have conducted fewer field exams in recent years, with approximately 272,000 field exams in FY 2010 and only about 156,000 field exams in FY 2018.<sup>3</sup>

The primary objective in identifying tax returns for examination is to promote the highest degree of voluntary compliance.<sup>4</sup> However, the IRS may not be driving voluntary compliance and further, may have no way of knowing whether it is doing so as a result of its field exams. Between FY 2010 and FY 2018, an average of about 23 percent of SB/SE field audits and about 32 percent of LB&I field audits

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 IRS Data Book, 2017, Publication 55B, 22-23 (Mar. 2018).

3 IRS, Compliance Data Warehouse (CDW), Automated Information Management System (AIMS) fiscal year (FY) 2010 and 2018 (Dec. 2018). Due to the lapse in appropriations, the Large Business and International Division (LB&I) did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

4 Internal Revenue Manual (IRM) 1.2.13.1.10, *Policy Statement 4-21* (June 1, 1974).

resulted in no change.<sup>5</sup> Research shows that no change audits result in greater future noncompliance.<sup>6</sup> When measuring results, the IRS appears to look primarily at the bottom line from specific audits per resources expended—measuring closures, cycle time, employee satisfaction, and quality scores—and not the indirect effects. Moreover, neither SB/SE nor LB&I have a measure to track whether future filing or payment compliance increases after an audit. Although both divisions track the number of requests for audit reconsideration, they do not track how many of these audit reconsiderations are eventually appealed by the taxpayer.<sup>7</sup>

From a taxpayer's perspective, field audits provide an opportunity to interact with IRS employees face-to-face and work directly with a single employee or team. However, some taxpayers may not have access to all IRS employees making decisions about their issues, such as technical specialists. Others experience difficulty in understanding the scope of the audit due to a lack of transparency or overly broad document requests. The IRS has no formal centralized system to track taxpayer complaints and requests to speak to a manager in field exams. As a result, the IRS reduces the opportunities for two-way communication to learn why a particular issue should not be examined and what taxpayers are doing wrong, intentionally or unintentionally.

The National Taxpayer Advocate is concerned that:

- The IRS may be wasting resources and failing to drive future voluntary compliance due to the high no change rates for its field audits;
- The primary purpose of audits is to improve voluntary compliance, yet the IRS does not measure how field audits affect taxpayers' future filing behavior and attitudes towards tax administration;
- With declining numbers of field audits, the IRS must ensure that it selects the best cases to drive future compliance;
- A lack of transparency during field exams, including SB/SE's declining to share an individual exam plan with the taxpayer, infringes on the taxpayer's *right to be informed*; and
- The IRS does not provide a clear path for taxpayers to elevate issues nor does it track taxpayer complaints about field exams.

These shortcomings in the field examination process impair taxpayers' rights *to be informed, to quality service, to pay no more than the correct amount of tax, to challenge the IRS's position and be heard, and to a fair and just tax system.*

5 IRS, CDW, AIMS FY 2010 to FY 2018 (Dec. 2018). IRM 4.4.12.5.49.1, *No Change Disposal Codes* (June 1, 2002) defines a no change as a case closed by the examiner with no additional tax due (disposal code 1 and 2). In the Small Business/Self-Employed Division (SB/SE) response to TAS fact check (Dec. 20, 2018), SB/SE notes disposal code 1 as an agreed closure. TAS does not agree with the SB/SE definition because these cases do not require agreement from the taxpayer since there is no additional tax liability (see, e.g., IRM 4.10.8.2.2, *No Change with Adjustments Report Not Impacting Other Tax Year(s)* (Sept. 12, 2014)) and the taxpayer's agreement, or disagreement, with the adjustment(s) as it pertains to another's year's liability is not known. Treasury Inspector General for Tax Administration (TIGTA) Report 2018-30-069 concurs with TAS's definition. Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

6 National Taxpayer Advocate 2015 Annual Report to Congress vol. 2 67-100 (Sebastian Beer, Matthias Kasper, Erich Kirchler, Brian Erard, *Audit Impact Study*).

7 IRS responses to TAS information request (Nov. 1, 2018); Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

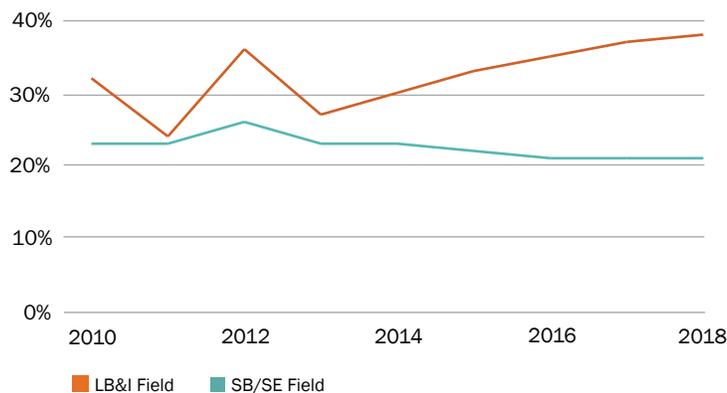
## ANALYSIS OF PROBLEM

### The IRS May Be Wasting Resources and Failing to Drive Voluntary Compliance Due to the High No Change Rates For Its Field Audits

There are direct and indirect effects from audits that propose no additional tax to be assessed (“no change” audits). First, a no change audit means the IRS has expended time and resources without assessing any additional dollars that can be collected from the taxpayer. Second, the IRS may have prompted the taxpayer to choose to report less tax in the future. A 2015 study conducted for TAS found that self-employed taxpayers filing Schedule C who received a no change audit reduced their reported income by 37 percent three years after the audit.<sup>8</sup> This is in contrast to taxpayers with audits recommending an additional tax assessment, who instead increased the amount of tax they reported after the audit by an average of 250 percent.<sup>9</sup> A recent study also found that taxpayers with audits recommending additional tax report a higher perceived risk of future audits, which may explain why they increased the amount of tax they reported in subsequent years.<sup>10</sup> Despite the direct and indirect effects of audits, the IRS maintains a high no change rate for its field exams, as shown in Figure 1.9.1.

FIGURE 1.9.1<sup>11</sup>

#### No Change Rate for Field Exams Closed During FY 2010-2018



8 National Taxpayer Advocate 2015 Annual Report to Congress vol. 2 88 (Research Study: *Audit Impact Study*).

9 *Id.*

10 See Brian Erard, Matthias Kasper, Erich Kirchler, and Jerome Olsen, Research Study: *What Influence do IRS Audits Have on Taxpayer Attitudes and Perceptions? Evidence from a National Survey*, *infra*.

11 IRS, CDW, AIMS FY 2010 to FY 2018 (Dec. 2018). IRM 4.4.12.5.49.1, *No Change Disposal Codes* (June 1, 2002) defines a no change as a case closed by the examiner with no additional tax due (disposal code 1 and 2). In the SB/SE response to TAS fact check (Dec. 20, 2018), SB/SE notes disposal code 1 as an agreed closure. TAS does not agree with the SB/SE definition because these cases do not require agreement from the taxpayer since there is no additional tax liability (see, e.g., IRM 4.10.8.2.2, *No Change with Adjustments Report Not Impacting Other Tax Year(s)* (Sept. 12, 2014)) and the taxpayer’s agreement, or disagreement, with the adjustment(s) as it pertains to another liability is not known. TIGTA Report 2018-30-069 concurs with TAS’s definition. Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

The no change rate for SB/SE field exams has remained steady over recent years at close to a quarter of exams, meaning almost a quarter of the SB/SE field audits may actually be encouraging taxpayers to become less compliant.<sup>12</sup> LB&I, on the other hand, had higher no change rates in its field audits, about 32 percent on average from FY 2010 to FY 2018, demonstrating that LB&I may not be achieving its stated goal of targeting noncompliance.<sup>13</sup> For corporate taxpayers, over 100 of whom are under continuous audit, this no change rate is particularly concerning.<sup>14</sup>

### The Primary Purpose of Audits Is to Improve Voluntary Compliance, yet the IRS Does Not Measure How Field Audits Affect Taxpayers' Future Filing Behavior and Attitudes Towards Tax Administration

Although audits do have a direct effect in terms of recommending additional tax dollars to be assessed, the overarching goal should be improving voluntary compliance. In fact, the IRS gains about twice as much from the long-term effects of an audit than it does from the actual audit itself when one compares additional reported taxable income in years following the audit with the additional dollars assessed as a direct result of the audit.<sup>15</sup> IRS Policy Statement 4-21 identifies promoting voluntary compliance as the primary driver of selecting returns for audits.<sup>16</sup> One scholar explains what it means for the U.S. tax system to be based on voluntary compliance:

It means that the tax authority does not have adequate resources, and never did, to assess taxes against each taxpayer directly or audit every return. Since the IRS cannot execute either of these practices, it instead relies on individual taxpayers to accurately assess their own tax liability on annual returns and timely pay the correct amount due.<sup>17</sup>

Key to increasing voluntary compliance is building trust in taxpayers. To encourage this trust the IRS must focus on perceived fairness, which includes distributive justice, procedural justice, and retributive justice.<sup>18</sup> In terms of procedural justice, “taxpayers consider the treatment by the tax authorities, information provided, costs regarding compliance and administration, and the dynamics of allocation of revenues.”<sup>19</sup> Transparency also plays a role as “increased information related to tax law and explanations

12 When excluding SB/SE field exams conducted as part of the National Research Program (NRP), the no change rate is similar—an average of approximately 22 percent for SB/SE non-NRP exams for FY 2010-2018. IRS, CDW, AIMS FY 2010 through FY 2018 (Dec. 2018). “NRP audits are selected through stratified random sampling and therefore the no change rate would be expected to be higher than returns that are being selected for examination due to indications of a high risk of noncompliance.” IRS response to TAS fact check (Dec. 21, 2018).

13 Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

14 IRS, CDW, AIMS FY 2010 through FY 2017 (Dec. 2018). LB&I is transitioning its former continuous audit program for large corporations, the Coordinated Industry Case program, to the new Large Corporate Compliance program, which aims to develop better risk profiles for large corporations. Nonetheless, the group of high risk taxpayers under continuous audit is currently over 100 taxpayers, down only slightly from 2016. LB&I Business Performance Review, FY 2018 4th Quarter (Nov. 16, 2018).

15 Jason DeBacker, Bradley T. Heim, Anh Tran, and Alexander Yuskavage, *Once Bitten, Twice Shy? The Lasting Impact of IRS Audits on Individual Tax Reporting* (Aug. 25, 2015) (working paper, Indiana University), <https://pdfs.semanticscholar.org/3833/61d62ea27f93deb89bf2c4b926bc5e96e14b.pdf>.

16 IRM 1.2.13.1.10, *Policy Statement 4-21* (June 1, 1974).

17 J.T. Manhire, *What Does Voluntary Tax Compliance Mean?: A Government Perspective*, 164 U. Pa. L. Rev. Online 11 (2015), <http://www.pennlawreview.com/online/164-U-Pa-L-Rev-Online-11.pdf>.

18 Erich Kirchler, Erik Hoelzl, and Ingrid Wahl, *Enforced versus Voluntary Tax Compliance: The “Slippery Slope” Framework*, 29 J. Econ. Psychol. 218-219 (2008).

19 Distributive justice concerns the exchange of resources, both benefits and cost, and retributive justice applies when the sanctions for breaking rules are perceived as appropriate. *Id.*

for changes can increase fairness perceptions.”<sup>20</sup> Also important are a culture of interaction, perceived neutrality regarding the treatment of different groups, and equal and respectful treatment of taxpayers.<sup>21</sup> Finally, metrics used to evaluate examinations should look at three types of indirect effects: (1) induced effects, which are behavior changes due to a change in the enforcement level or audit rate; (2) subsequent period effects, which are changes in an individual taxpayer’s behavior post-audit; and (3) group effects, which are changes in compliance by members of the taxpayer’s social network.<sup>22</sup>

In measuring the effectiveness of the field audit program, the IRS appears to look primarily at the bottom line from specific audits per resources expended, without measuring the indirect effects, including social network effects. SB/SE’s Business Performance Review (BPR) reflects that the IRS measures closures, cycle time, employee satisfaction, and quality scores.<sup>23</sup> LB&I’s BPR includes similar performance measures.<sup>24</sup> In 2014, the National Taxpayer Advocate recommended that the IRS “[a]dopt ‘increasing voluntary compliance’ as the primary measure for evaluating both enforcement and taxpayer service initiatives.”<sup>25</sup> However, neither SB/SE nor LB&I have added a measure to track whether future filing or payment compliance increases after an audit.<sup>26</sup> Further, neither operating division has a system in place to track if audited taxpayers are compliant in future years.

The current measures may not be useful if the IRS does not choose the correct cases for an audit. Cycle time may be quick if the IRS is auditing taxpayers who are relatively compliant. Closing cases may not be a positive outcome if the taxpayer does not feel the issues are resolved. Although both SB/SE and LB&I track audit reconsiderations, neither tracks how many of these reconsiderations go to the IRS Office of Appeals, meaning the IRS does not know when it gets the answer wrong or when there are hazards of litigation, both of which should inform audit selection.<sup>27</sup>

In addition to subsequent compliance, the IRS should also track taxpayers’ attitudes towards the IRS, tax administration, and paying their taxes after an audit. A study commissioned by TAS found that in terms of taxpayers’ attitudes towards the IRS and paying taxes, no change audits resulted in the most positive taxpayer attitudes, greater than taxpayers receiving a refund.<sup>28</sup> Taxpayers with additional taxes proposed had the most negative attitudes after an audit.<sup>29</sup> Likewise, taxpayers with additional taxes proposed reported a weaker sense of procedural and distributive justice, lower levels of trust in the IRS, a greater sense of coercion, and more feelings of anger.<sup>30</sup> Although reducing the number of taxpayers with additional tax proposed is not desirable, the IRS could still use metrics such as these to drive changes to

20 Erich Kirchler, Erik Hoelzl, and Ingrid Wahl, *Enforced versus Voluntary Tax Compliance: The “Slippery Slope” Framework*, 29 J. ECON. PSYCHOL. 219 (2008).

21 *Id.*

22 Kim Bloomquist, *Incorporating Indirect Effects in Audit Case Selection: An Agent-Based Approach*, IRS Research Bulletin 103 (2012), <https://www.irs.gov/pub/irs-soi/12resconincorporating.pdf>.

23 SB/SE FY 2018 1st Quarter Business Performance Review (BPR). BPRs review the operating divisions’ progress on meeting their performance goals and report on new or emerging issues that may affect programs and performance. IRM 1.5.1.15, *Proposing, Reviewing, and Updating Performance Budget Measures* (Sept. 24, 2014).

24 IRS response to TAS information request (May 4, 2018). Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

25 National Taxpayer Advocate 2014 Annual Report to Congress 122.

26 IRS response to TAS information request (Nov. 1, 2018). Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

27 *Id.*

28 See Brian Erard, Matthias Kasper, Erich Kirchler, and Jerome Olsen, *Research Study: What Influence do IRS Audits Have on Taxpayer Attitudes and Perceptions? Evidence from a National Survey*, *infra*.

29 *Id.*

30 *Id.*

the way the IRS conducts audits. For example, the IRS could test whether a greater focus on educating the taxpayer during the audit might reduce feelings of coercion because a taxpayer would understand the mistake made. Greater transparency at the beginning of the exam (discussed below) could reduce feelings of mistrust.

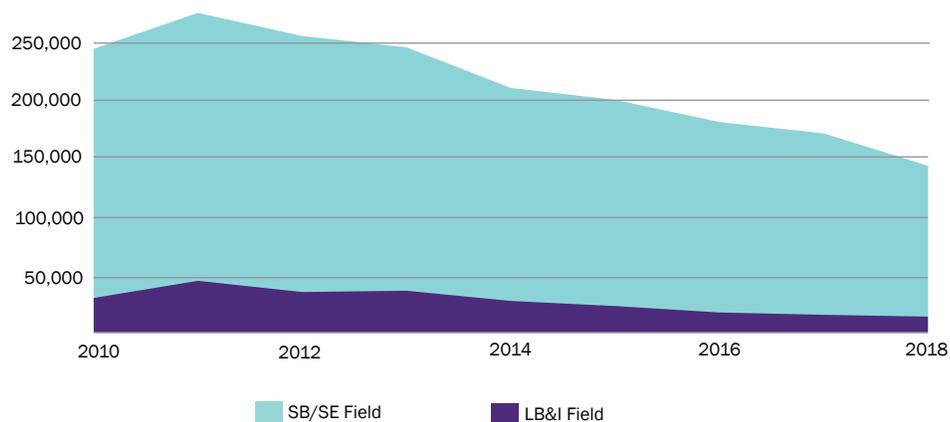
The field exam customer satisfaction surveys do not capture this information because they are more focused on how the taxpayer feels about a specific encounter and not how the taxpayer might alter their behavior in the future. LB&I reports that it has been collaborating with Research, Applied Analytics and Statistics (RAAS) to conduct behavioral research related to the LB&I campaigns to determine their impact on taxpayer behavior.<sup>31</sup> The National Taxpayer Advocate encourages the IRS to continue with this research and conduct behavioral research regarding all audit treatments to better understand how they may affect voluntary compliance.

### With Declining Numbers of Field Exams and Revenue Agents, the IRS Must Ensure That It Selects the Best Cases to Drive Future Compliance

As shown in Figure 1.9.2, both SB/SE and LB&I field audits have been declining in recent years, reflecting that both operating divisions may need to be more discriminating as managers must choose to survey more cases and audit less.

**FIGURE 1.9.2**<sup>32</sup>

#### Volume of Field Audit Closures by Operating Division FY 2010-2018



Both LB&I and SB/SE focus largely on the current compliance risk—choosing returns based primarily on anticipated noncompliance found on that specific return. SB/SE selects over 22 percent of audits

31 IRS response to TAS information request (May 4, 2018). Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

32 IRS, CDW, AIMS FY 2010 to FY 2018 (Nov. 2018) for LB&I. IRS response to TAS fact check (Dec. 20, 2018). Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

based on the computer program Discriminant Function (DIF),<sup>33</sup> and over half of its audits based on a related-year audit, meaning instead of auditing a new taxpayer, it opens an audit on another tax year for a taxpayer already under audit.<sup>34</sup> As a result, there is only a limited number of audits to be selected from other criteria such as information matching and compliance projects. Although the Treasury Inspector General for Tax Administration (TIGTA) recently criticized SB/SE for not auditing enough related-year returns,<sup>35</sup> this criticism considered only the bottom line in terms of direct revenue from the examination. When one considers the indirect effects of an examination, including how the audited taxpayer and the taxpayer's peers in the community or industry might change their behavior, it is clear that audit selection must go beyond just the dollars assessed on a return.

LB&I uses the computerized scoring system, known as the Discriminant Analysis System (DAS), to score returns for corporations with assets over \$10 million to be delivered to the field.<sup>36</sup> Recent Government Accountability Office (GAO) audits of both SB/SE and LB&I show weaknesses for both operating divisions in how they document and justify managers' final decisions about whether to audit or survey a case that is included in the queue of potential cases.<sup>37</sup> Thus, even if computer systems such as the DIF or the DAS are effective in weeding out and not selecting taxpayers who are likely compliant, the IRS may not be making the best decisions in the end regarding which taxpayers in the queue to audit.

To be more nimble in identifying emerging trends and creating an enforcement presence, LB&I initiated the "campaign" program, in which it will conduct issue-based examinations and apply one or multiple treatment streams based on compliance risk.<sup>38</sup> There are currently 45 campaigns, and examples include: Foreign Earned Income Exclusion, Swiss Bank Program, IRC 48C Energy Credit, and Deferral of Cancellation of Indebtedness Income.<sup>39</sup> Although the long-term plan is for the campaigns to constitute a significant part of the LB&I compliance program, currently they only comprise a small minority—only about six percent—of LB&I's audit work.<sup>40</sup> LB&I is reportedly working to create metrics for the campaigns, but it is unclear how the IRS currently determines a campaign is not working and should

33 "The Discriminant Function (DIF) is a risk-based method of scoring tax returns for examination potential. The models are based on the mathematical technique called discriminant analysis and are developed using data from the National Research Program or the prior Taxpayer Compliance Measurement Program (TCMP) data." IRS response to TAS fact check (Dec. 21, 2018). Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

34 These prior or subsequent year returns were mostly related to methods for trying to shelter income and DIF-identified returns. Government Accountability Office (GAO), *IRS Return Selection: Certain Internal Controls for Audits in the Small Business and Self-Employed Division Should Be Strengthened*, GAO 16-103 (Dec. 2015).

35 TIGTA, *Improvements Are Needed to Ensure Adequate Consideration of the Pickup of Prior and/or Subsequent Returns During Field Examinations*, 2018-30-073 (Sept. 17, 2018).

36 IRS response to TAS information request (May 4, 2018). IRS, *2016 Internal Revenue Service Advisory Council (IRSAC) Large Business and International Report* (Sept. 30, 2017), <https://www.irs.gov/tax-professionals/2016-irsac-lbi-report>. Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

37 GAO, *IRS Return Selection: Certain Internal Controls for Audits in the Small Business and Self-Employed Division Should Be Strengthened*, GAO 16-103 (Dec. 2015); GAO, *IRS Return Selection: Improved Planning, Internal Controls, and Data Would Enhance Large Business Division Efforts to Implement New Compliance Approach*, GAO 17-324 (Mar. 2017).

38 IRS, *IRS Announces Initial Rollout of Campaigns* (June 28, 2018), <https://www.irs.gov/businesses/large-business-and-international-launches-compliance-campaigns>.

39 IRS response to TAS information request (Nov. 1, 2018). IRS, *Full List of LB Large Business and International Campaigns* (Oct. 30, 2018), <https://www.irs.gov/businesses/full-list-of-lb-large-business-and-international-campaigns>. Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

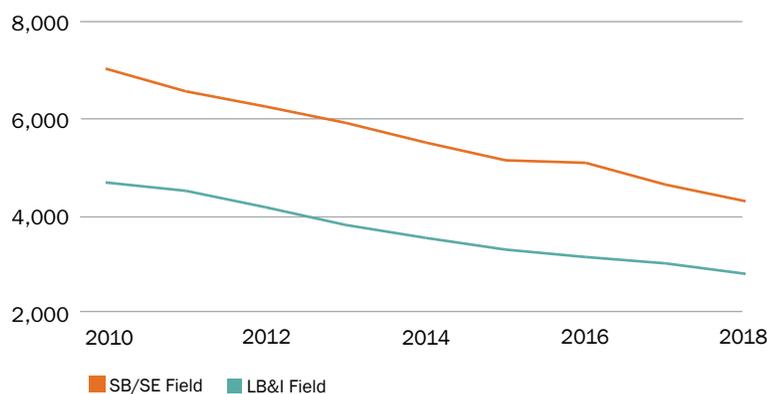
40 LB&I FY 2018 3rd Quarter BPR. Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

be abandoned, or perhaps should be broadened and expanded. The IRS recently ended some of its campaigns, but has not developed a strategy to communicate the terminations publicly.<sup>41</sup> Without a system in place to provide updates on the exams conducted as part of the campaigns in real time—for example, when an issue is closed or an exam is agreed to—the IRS will not be able to adjust its exam strategy at the earliest point in time.

Not surprisingly, a reduction in Revenue Agents corresponds with the reduction in field exams over recent years. Both IRS operating divisions conducting field exams in FY 2018 employed only about 60 percent of the Revenue Agents they had in FY 2010.

**FIGURE 1.9.3**<sup>42</sup>

**Nonsupervisory Revenue Agents Last Pay Period of FY 2010 to FY 2018**



This reduction makes it more critical for the IRS to ensure it has exam employees in the right locations. LB&I states that organizational components generally have discretion to decide at which locations to hire based on workload.<sup>43</sup> However, looking at past or current workload may not allow the IRS to have staffing in place in the right locations as it identifies emerging trends. Similarly, SB/SE may be taking a myopic view in selecting locations to hire examiners. For non-specialty examiners, SB/SE uses workload studies to distribute workload based on the geographic locations with the highest DIF scores.<sup>44</sup> However, only about a fifth of SB/SE field audits are based on DIF scores.<sup>45</sup> SB/SE was planning a new partnership audit selection process known as Flow-through Initiatives, partnering Field Case Selection with RAAS to improve workload selection for flow-through returns with emphasis on using data to

41 Amanda Athanasiou, *IRS Weighing Termination of LB&I Campaigns*, TAX NOTES TODAY (Nov. 8, 2018).

42 IRS Human Resources Reporting Center, *Workforce Information by Organization Report* for the ending pay period FY 2010 to FY 2018 for non-supervisory Revenue Agent jobs series 512. SB/SE counts do not include SB/SE campuses. Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

43 IRS response to TAS information request (Nov. 1, 2018). Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

44 IRS response to TAS information request (Nov. 1, 2018).

45 GAO, *IRS Return Selection: Certain Internal Controls for Audits in the Small Business and Self-Employed Division Should Be Strengthened*, GAO 16-103 (Dec. 2015).

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Both IRS operating divisions conducting field exams in Fiscal Year (FY) 2018 employed only about 60 percent of the Revenue Agents they had in FY 2010.

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create business rules, statistical models, and select returns using an enterprise case approach. However, the IRS abruptly ended this initiative due to “resources.”<sup>46</sup>

### A Lack of Transparency During Field Exams, Including SB/SE’s Declining to Share an Individual Exam Plan With the Taxpayer, Infringes on the Taxpayer’s Right to Be Informed

The IRS misses opportunities by not learning from taxpayers during exams what the taxpayers are doing wrong, either intentionally or unintentionally. Although the focus of examinations can change as the audit unfolds, providing greater transparency at the beginning of an exam would allow the taxpayer to raise concerns that might show why an issue should not be examined or where taxpayers could use additional guidance. This transparency might also allow taxpayers to change their filing behavior for later years or correct errors via amended returns. Instead, taxpayers may not understand the focus of the examination until midway through.

When LB&I initiates an audit, it shares with the taxpayer an examination plan for that particular audit that includes the issues to be examined, timeframes, personnel required, processes to be followed, and respective responsibilities.<sup>47</sup> Both members of the exam team and the taxpayer sign the plan, committing to achieving the timeline set out.<sup>48</sup> When asked why SB/SE does not share a similar audit plan with the taxpayer, it stated: “SB/SE audits are more focused, with smaller scope, less complex and faster cycle time which does not warrant a full in-depth audit plan like LB&I’s process,” and “[g]enerally SB/SE examiners share/discuss the issues that will be audited and provide the taxpayers with an Information Document Request (IDR) prior to the initial appointment.”<sup>49</sup> However, the IDR may not provide the same level of detail as the LB&I exam plan nor is it a substitute for it.<sup>50</sup>

Before the LB&I exam plan is final, it must be shared and discussed with the taxpayer in an interactive way that “contributes to their understanding of the examination plan and also affords them the opportunity to propose changes before the plan is final.”<sup>51</sup> SB/SE’s IDR does not perform the same function as an exam plan. The IDR is a “request” for documents that, if the IRS determines is not responded to fully, can be the precursor to a summons—that is, an adversarial act in which there is no room for discussion. Moreover, the IRM allows SB/SE to use *pro-forma* type IDRs with a list of commonly requested items in exams; however, it warns examiners not to use a “shot-gun” approach by requesting everything on the list.<sup>52</sup> However, practitioners at a 2016 Congressional hearing on small

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46 IRS response to TAS information request (Nov. 1, 2018).

47 IRS, Publication 4837, *Achieving Quality Examinations through Effective Planning, Execution and Resolution* (Oct. 2010).

48 *Id.*

49 IRS responses to TAS information requests (May 4, 2018, Nov. 1, 2018).

50 IRM 4.46.3.8, *Examination Plan* (Mar. 14, 2016). Among other items, the LB&I Exam Plan must include: detailed steps for each issue; case and issue timeline(s) with milestone dates; issue team members, including each team member’s estimated days; established dates and decision points that are used to periodically risk-assess issues being examined; and agreements made during the opening meeting. IRM 4.46.3.8.1, *Elements of an Examination Plan* (Mar. 14, 2016).

51 IRM 4.46.3.8.2, *Taxpayer Review of the Examination Plan* (Mar. 14, 2016).

52 IRM 4.10.2.10.2, *Requesting Information or Documents from the Taxpayer* (Jan. 17, 2017).

business burdens stated “we are finding requests for things outside the scope of the audit”<sup>53</sup> and “while these requests [IDRs] are often customized, they also contain boilerplate items that agents are required to seek regardless of the issues that the agent has identified and regardless of the type of business that the taxpayer is operating.”<sup>54</sup>

This lack of transparency impairs the taxpayer’s *right to be informed*. It not only creates burden for the taxpayer, who does not know what is being audited, but it also prevents the IRS from weeding out issues that do not need to be part of the audit or using information from the taxpayer to better understand why the taxpayer made a mistake and how the IRS can adjust its public guidance in real time to prevent further problems. Sharing the audit plan could allow for earlier resolution of issues. Taxpayers could also adjust prior or later year returns to avoid related audits. Further, with this increased communication with the taxpayer, the IRS may discover that the audit of the particular type of taxpayer or issue is not the best use of its resources and adjust its audit strategy.

### The IRS Does Not Provide a Clear Path For Taxpayers to Elevate Issues Nor Does It Track Taxpayer Complaints About Field Exams

Another item that prevents the IRS from identifying, in real time, problems with its audit selection tools and examination procedures is the lack of a clear path for taxpayers to elevate issues and make complaints. Although the use of a “team” exam approach is necessary for large or complex cases, taxpayers may be cut off from the decision-makers in their cases. One practitioner explained to Congress:

While this [specialist] assistance is necessary, the process is often mysterious and the taxpayer is left in the dark regarding who is making decisions. Our experience includes situations where a revenue agent who lacks expertise may rely on a technical specialist to make the decision in an examination, and due to staffing levels, the specialist may not have adequate time to fully assist, so revenue agents have only consultations with them. In some cases, the taxpayer is not aware that this has occurred or has not had an opportunity to discuss the specialist’s technical conclusions.<sup>55</sup>

Furthermore, when taxpayers have complaints, they may not have a reasonable path to raise them. The Tax Executive Institute notes the IRS’s public statement that there will be no single member of the exam team with a majority vote, and the first point of contact empowered to make the decision about whether to consider an issue resolved or abandoned is the Deputy Commissioner of LB&I.<sup>56</sup> With the number of members of an exam team and their breadth across the IRS, taxpayers at an impasse may have few options other than elevating to the Deputy Commissioner of LB&I.

Neither LB&I nor SB/SE Examination has a formal, centralized system to track taxpayer complaints and requests to speak to a manager.<sup>57</sup> As such, there is no mechanism for the IRS to catalog what it has

53 *IRS Puts Small Businesses Through Audit Wringer: Hearing before the H. Comm. on Small Business*, 114th Cong. (2016) (statement of Warren Hudak, President, Hudak & Company, testifying on behalf of the National Association of Enrolled Agents).

54 *Id.* (statement of Jennifer E. Breen, Partner, Morgan, Lewis & Bockius LLP, testifying on behalf of the American Bar Association Section of Taxation).

55 *Id.* (statement of Kathy Petronchak, Director of IRS Practice and Procedure, Alliantgroup).

56 Tax Executive Institute, *The New LB&I: Recent IRS reorganization raises panoply of significant issues* (Feb. 23, 2016), <http://taxexecutive.org/the-new-lbi/>.

57 IRS response to TAS information request (May 4, 2018). Due to the lapse in appropriations, LB&I did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

learned in terms of what is or is not working from the taxpayer's perspective and use this to adjust its compliance strategy and ensure its case selection is optimal.

## CONCLUSION

The IRS has many opportunities for improving its field examination program. The unacceptably high no change rates across the field exam programs reveal that the IRS is wasting resources by examining taxpayers for whom it will not recommend additional tax assessments. Further, these no change exams may be worse than no exams at all because taxpayers may choose to report less tax in subsequent years as a result of the exam. In order to meet its goal of promoting voluntary compliance, the IRS must reduce the no change rates and create measures that capture how a taxpayer changes his or her filing behavior and attitudes as a result of an audit. Creating better measures may also help the IRS identify areas where it needs to change how it conducts its exams—namely providing greater transparency and a clearer path for taxpayers to raise complaints.

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Periodically survey taxpayers after field exams to determine the impact of the exam on the taxpayers' understanding of the audit process and audit adjustments, and attitudes towards the IRS and filing and paying taxes.
2. Periodically study taxpayers' filing behavior following field exams to determine whether the exams had an impact on whether the taxpayer filed, how much income the taxpayer reported, and whether the taxpayer repeated a mistake made on a previous return.
3. Require SB/SE to provide an examination plan similar to what LB&I requires for all audited taxpayers for all field examinations.
4. Notify taxpayers during an audit of any consultations with specialists and provide an opportunity for taxpayers to discuss with the specialist any technical conclusions that result from these consultations.
5. Track and report on the number of field examinations (including audit reconsiderations) that go to Appeals and the resulting adjustments.

**MSP  
#10****OFFICE EXAMINATION: The IRS Does Not Know Whether Its Office Examination Program Increases Voluntary Compliance or Educates the Audited Taxpayers About How to Comply in the Future****RESPONSIBLE OFFICIAL**

Mary Beth Murphy, Commissioner, Small Business/Self-Employed Division

**TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to a Fair and Just Tax System*

**DEFINITION OF PROBLEM**

Under Internal Revenue Code (IRC) § 7602(a) the IRS may conduct examinations to determine whether a tax return is correct, to create a return where the taxpayer has not filed, and to determine a taxpayer's tax liability. The IRS's Office Examinations Program (Office Exam), administered by the Small Business/Self-Employed Division (SB/SE), performs a small fraction of all IRS audits per year. In fiscal year (FY) 2017, the IRS audit coverage rate for all returns was 0.5 percent.<sup>2</sup> Of those audited, only 102,517 returns were audited through office exams (approximately ten percent).<sup>3</sup> Office exams are generally performed in locations where the IRS has the appropriate examination personnel, Tax Compliance Officers (TCOs).<sup>4</sup> SB/SE currently has 639 TCOs performing office exams, a 49 percent decrease compared with FY 2011, despite office exams having higher agreed-to rates than correspondence exams.<sup>5</sup>

IRS Policy Statement 4-21 states that the primary purpose in selecting tax returns for examination is to promote the highest degree of voluntary compliance.<sup>6</sup> However, the IRS does not know if Office Exam

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 IRS, *Data Book* 23 (2017). The audit coverage rate is computed from the 1,059,934 returns audited in fiscal year (FY) 2017 across its examination programs divided by the 195,614,161 returns filed in calendar year 2016.

3 IRS response to TAS information request (Oct. 15, 2018).

4 Internal Revenue Manual (IRM) 4.10.2.9.2 (2), *Place and Time of Examination* (Feb. 11, 2016).

5 IRS response to TAS information request (Oct. 15, 2018). IRS, Compliance Data Warehouse (CDW), Automated Information Management System (AIMS) FYs 2011 to 2018 (Dec. 2018).

6 IRM 1.2.13.1.10, *Policy Statement 4-21* (June 1, 1974).

achieves this purpose. The National Taxpayer Advocate's concerns about the overall effectiveness of office exams are two-fold:<sup>7</sup>

- The measures the IRS uses to determine the effectiveness of the exam selection process do not capture data needed to determine the program's impact on increasing voluntary compliance; and
- The scope of the office exam program may limit its impact and introduce bias into the selection process, rendering the program available only to taxpayers who are geographically proximate, have specific issues, or where the IRS has appropriate examination personnel.

In-person face-to-face exams have the potential to provide a real opportunity for the IRS to educate taxpayers on filing compliance for the future and to increase voluntary compliance. Limiting office exams to a small portion of the taxpayer pool, closing the exams cursorily, and failing to approach the exam as an educational experience cannot serve to genuinely further the goal of increasing voluntary compliance and fails to capitalize on the opportunity to put a human face on the IRS.

## BACKGROUND

The IRS uses several workstreams to identify returns that may merit additional scrutiny, including assigning all returns a discriminant function (DIF) score, implementing special projects, and receiving referrals.<sup>8</sup> IRS employees review the pool of returns to determine if the return should be audited and the appropriate audit process. Returns may then be assigned to employees for audit.

### Office Exams Offer Advantages to Taxpayers Versus Correspondence Exams

The IRS employee has an opportunity to educate the taxpayer in-person and ensure the taxpayer understands the law going forward. The face-to-face experience benefits both the taxpayer and the IRS—the taxpayer can, in real time, ask questions and explain his or her position to the IRS, and the IRS employee can immediately see if the taxpayer understands the current examination, next steps to be taken, and how to comply in the future. Compare this with the correspondence examination process where a taxpayer with limited understanding of the law may never speak to an IRS employee during the entire process.

When a return is selected for office examination, the TCO may send the taxpayer a letter with the date, time, and location of the exam.<sup>9</sup> Research shows that an opt-out system (where a person is sent a letter with a firm date and time for an appointment) versus an opt-in (where a person is sent a letter requesting he or she call and schedule an appointment) may be more effective in ensuring the person shows up for

7 For an in-depth discussion of the National Taxpayer Advocate's concerns about other types of examinations, see Most Serious Problem: *Correspondence Examination: The IRS's Correspondence Examination Procedures Burden Taxpayers and are Not Effective in Educating the Taxpayer and Promoting Future Voluntary Compliance*, *supra*; Most Serious Problem: *Field Examination: The IRS's Field Examination Program Burdens Taxpayers and Yields High No Change Rates, Which Waste IRS Resources and May Discourage Voluntary Compliance*, *supra*.

8 For a discussion of the exam selection process, see *Introduction to the Examination Process: Promoting Voluntary Compliance and Minimizing Taxpayer Burden in the Selection and Conduct of Audits*, *supra*.

9 IRM 4.10.2.8.1.1 (Nov. 4, 2016). One letter option is IRS, Letter 2202, *Initial Contact Letter – Firm Set Appointment Letter* (Feb. 2017). This letter sets an appointment date and time for the taxpayer. Two other possible letters request that the taxpayer call the IRS to schedule the appointment. IRS Letter 3572 (Dec. 2016); IRS Letter 3572-A (Dec. 2016).

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Office exams offer a unique opportunity to educate a taxpayer in person and to help the taxpayer understand his or her filing obligations going forward. With higher agreed-to rates and lower non-response rates than correspondence exam, the process results in a better outcome for taxpayers and the IRS.

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the appointment.<sup>10</sup> Correspondence exams (and the two office exam letters requesting the taxpayer call the IRS for an appointment) require the taxpayer to proactively respond to a letter, the functional equivalent to an opt-in system, and may be less effective in eliciting a response from the taxpayer, resulting in higher non-response rates. A mixed approach, where the letter sets a date for the exam, but permits the taxpayer to call to reschedule would allow for flexibility for the taxpayer, but also prompt the taxpayer to act due to the scheduled appointment.

Office exams offer a unique opportunity to educate a taxpayer in person and to help the taxpayer understand his or her filing obligations going forward. With higher agreed-to rates and lower non-response rates than correspondence exam, the process results in a better outcome for taxpayers and the IRS.<sup>11</sup> Many of the same benefits may be available from exams conducted in a virtual face-to-face environment, provided the IRS has the appropriate technology; however, virtual audits would not be an entire substitute for in-person audits due to the limitations of internet and technology access among taxpayers.<sup>12</sup>

### The IRS Does Not Know if the Office Exam Program Effectively Promotes Voluntary Compliance

IRS Policy Statement 4-21 clearly articulates the IRS's stated purpose in selecting returns for examination:

The primary objective in selecting returns for examination is *to promote the highest degree of voluntary compliance* on the part of taxpayers. This requires the exercise of professional judgment in selecting sufficient returns of all classes of returns in order to assure all taxpayers of equitable consideration, in utilizing available experience and statistics indicating the probability of substantial error, and in making the most efficient use of examination staffing and other resources.<sup>13</sup>

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10 Studies have shown that an opt-out system for flu vaccinations results in higher rates of vaccination for those who receive a notice with a prescheduled appointment compared to those who receive an opt-in notice requesting they make an appointment. See, e.g., Gretchen Chapman, Meng Li, Howard Leventhal, Elaine Leventhal, *Default Clinic Appointments Promote Influenza Vaccination Uptake Without a Displacement Effect*, BEHAVIORAL SCIENCE & POLICY, Vol. 2 Issue 2 2016, at 41-50.

11 IRS, CDW, AIMS FY 2011 to 2018 (Dec. 2018). Combined, SB/SE and Wage and Investment (W&I) correspondence exams for FY 2018 had a non-response rate of over 40 percent, compared to 14 percent for office exam.

12 National Taxpayer Advocate 2017 Annual Report to Congress, vol. 2 61-146 (Research Study: *A Further Exploration of Taxpayers' Varying Abilities and Attitudes Toward IRS Options for Fulfilling Common Taxpayer Service Needs*) (95 percent confidence level). Taxpayers indicated that about 28 percent did not have broadband, which translates to over 41 million taxpayers without this type of access. This is more prevalent within the vulnerable population groups including low income taxpayers (at or below 250 percent of poverty level based on household size, income, and location), seniors (age 65 and older), and taxpayers with disabilities (long term condition self-reported in the survey).

13 IRM 1.2.13.1.10, *Policy Statement 4-21* (June 1, 1974).

Although this statement is decades old, the concept of promoting voluntary compliance is one that should underlie all IRS programs and procedures, including the selection of returns for examination.

As described in a research study in Volume 2 of this report, the type of audit can be important relative to the attitudes and behavior of taxpayers who have been audited. In the sample of taxpayers in the report, only 64 percent of taxpayers remember being audited, with stark differences from those who underwent correspondence audits versus field or office examinations.<sup>14</sup> Eighty percent of those subject to office audit recall being audited, compared to less than 40 percent of those who experienced correspondence exam.

Overall, taxpayers in the study who experienced audits reported higher levels of fear, anger, threat and caution when thinking about the IRS and feel less protected by the IRS.<sup>15</sup> Taxpayers who experienced field or office exams reported higher levels of perceived justice compared to those who underwent correspondence exam.<sup>16</sup> Further, the study results suggest that taxpayers who undergo correspondence exam have a high erosion of trust of the IRS compared to those who experience field or office exam.<sup>17</sup> Surprisingly, the study found that taxpayers who experienced an audit which resulted in a refund of tax perceived the IRS with less trust after the conclusion of the audit, suggesting that perhaps the taxpayers may have been frustrated to be selected for audit when they had overpaid their tax or felt that the IRS was unfair its selection of their returns.<sup>18</sup>

### *The IRS Gets What It Measures*

If the IRS's goal is to promote voluntary compliance through the examination process, it needs to measure how taxpayers who undergo audits comply in future years. Currently the IRS relies on typical measures of cycle time, closure rates, quality scores, and employee satisfaction in evaluating the examination process.<sup>19</sup> None of these measures address the impact of audits on voluntary compliance, whether the taxpayer understood why his or her tax was adjusted, or whether the examination concluded in the right result for the taxpayer—*i.e.*, what happens when a taxpayer appeals the results of the exam?<sup>20</sup>

While the IRS measures field examination customer satisfaction, it does not separately survey office exam customer satisfaction. Further, while the field examination customer satisfaction survey may also capture taxpayers who underwent office examination, a customer satisfaction survey is not effective in achieving a broad picture of taxpayer satisfaction with the field examination process as the response rate is too low to extrapolate to the entire population.<sup>21</sup> The IRS should not combine field and office exam taxpayer satisfaction into one survey; instead, it should break out taxpayer satisfaction by type of

14 See Brian Erard, Matthias Kasper, Erich Kirchler, and Jerome Olsen, Research Study: *What Influence do IRS Audits Have on Taxpayer Attitudes and Perceptions? Evidence from a National Survey*, *infra*.

15 *Id.*

16 *Id.*

17 *Id.*

18 *Id.*

19 SB/SE, *2nd Quarter 2018 Business Performance Review* 13. IRM Exhibit 4.2.8-1, *Quality Attributes Rated by Field and Office Exam National Quality Reviewers* (Mar. 5, 2018).

20 IRS response to TAS information request (Oct. 15, 2018). TAS understands that SB/SE Research will be working with the Campus Correspondence Audit function determining to what extent it is feasible to assess the impact they have on voluntary compliance. SB/SE intends to look at recent audit projects by industry and geographic region, including the extent to which the addition of outreach or education could magnify any impact of those examinations on voluntary compliance—assuming that outreach or education information is available in a timely manner to meet deliverable timeframes. TAS looks forward to the results of this project. IRS response to TAS fact check (Dec. 13, 2018).

21 IRS, *SB/SE Field Exam Mail Customer Satisfaction Report Survey Year 2017* (Aug. 2018). SB/SE did not receive enough responses to this survey to extrapolate the results to the larger population.

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The IRS gets what it measures. If it does not measure how the exam process impacts future compliance, and it does not measure the quality of an exam to at a minimum include educating the taxpayer, it cannot hope to achieve these outcomes.

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exam to allow the IRS to use the data it obtains to improve and refine the office examination program. However, the IRS also combines office and field exam into one category when it reports on the results of examination in the IRS Data Book.<sup>22</sup>

The IRS could benefit from studying the future compliance of taxpayers subject to audit. Tracking future compliance, with an emphasis on type of audit performed, core issues examined, taxpayer type, and other characteristics, including the number and nature of interactions between the IRS auditor and the taxpayer, would help the IRS refine its audit strategy and use its audit resources more effectively to promote future compliance.

The mission of SB/SE Examination is to “provide Small Business and Self-Employed (SB/SE) taxpayers top quality service by helping them understand and meet tax responsibilities and by applying the tax law with integrity and fairness.”<sup>23</sup> Underlying this mission statement is a key element that states the goal of “educating and informing taxpayers so they understand what they must do to comply with the law.” Educating and informing taxpayers about how to achieve compliance and remain compliant in the future should be a primary goal of face-to-face interactions with taxpayers. However, nowhere in the quality review attributes of office exams does the IRS measure whether the employee educated the taxpayer and provided the taxpayer with information the taxpayer needs to be compliant in the future.<sup>24</sup>

Further, the SB/SE office examination program does not track the results of appealed exams.<sup>25</sup> Failing to do so misses an opportunity to understand if the exam process could be improved so that fewer taxpayers feel the need to appeal the results of the initial exam or to offer training if similar issues are consistently being conceded or settled on appeal.

Again, the IRS gets what it measures.<sup>26</sup> If it does not measure, as discussed above, how the exam process impacts future compliance, and it does not measure the quality of an exam to at least include educating the taxpayer, it cannot hope to achieve these outcomes.

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22 IRS, *2017 Data Book* (Mar. 2018).

23 IRM 1.1.16.3 (Nov. 16, 2018).

24 IRM 4.2.8 Exhibit 4.2.8-1, *Quality Attributes Rated by Field and Office Exam National Quality Reviewers* (Mar. 5, 2018). See also IRM 21.20.1-5, *EQRS/NQRS Attributes* (Oct. 22, 2018).

25 IRS response to TAS information request (Oct. 15, 2018).

26 National Taxpayer Advocate 2017 Annual Report to Congress 93-106.

## The Scope of the Office Exam Program May Limit Its Impact and Introduce Bias Into the Selection Process

### *Office Exams Are Geographically Limited*

Office exams are generally scheduled at the office closest to the taxpayer's residence, if the office has the appropriate examination personnel on site.<sup>27</sup> This constraint immediately limits which taxpayers may ever be selected for office exam. Currently, taxpayers in Alaska, Delaware, Montana, North Dakota, South Dakota, or Wyoming, where there are no TCOs conducting office exams, will never be audited via office exam.<sup>28</sup> Whereas taxpayers who live in Virginia (2 TCOs), North Carolina (7 TCOs), or Michigan (8 TCOs) may have a much lower chance of being audited via office exam versus taxpayers who live in Texas (59 TCOs), New York (62 TCOs), or Florida (50 TCOs).<sup>29</sup> Further, within the states that do have TCOs conducting office exams, the number of office exam locations have decreased from 241 to 175 (a 27 percent decrease) between 2011 and 2018.<sup>30</sup>

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27 IRM 4.10.2.9.2(2) (Feb. 11, 2016).

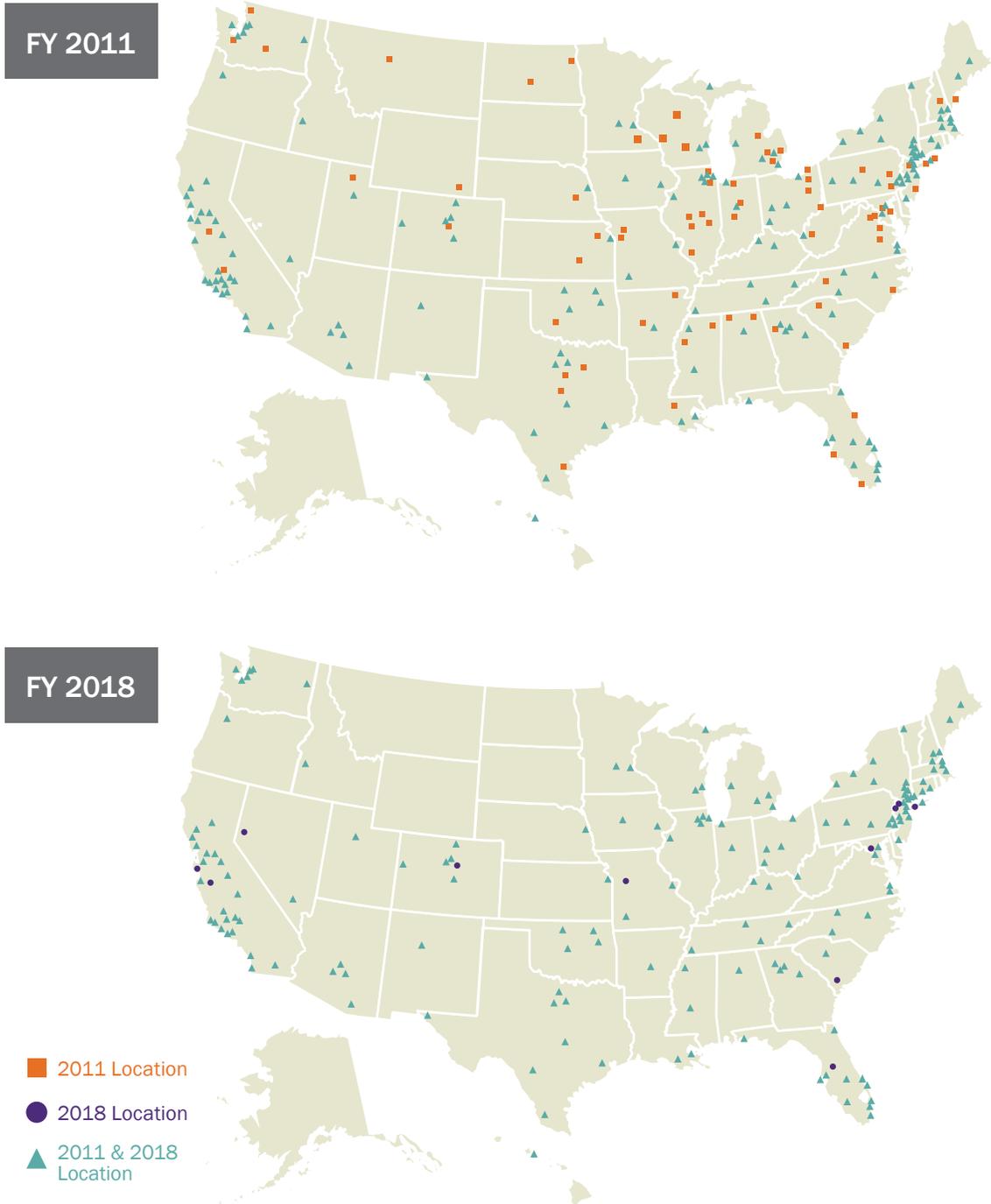
28 IRS response to TAS information request (Oct. 15, 2018).

29 *Id.*

30 *Id.*

**FIGURE 1.10.1**<sup>31</sup>

**Small Business/Self-Employed Tax Compliance Officer Locations  
Fiscal Years 2011 and 2018**



31 IRS response to TAS information request (Oct. 15, 2018).

Selecting taxpayers for office exam based on where TCOs are located introduces selection bias into the office exam process and impacts the *right to quality service* and the *right to a fair and just tax system*. Such a process will also necessarily impact the type of businesses that are selected for office exam due to lack of TCOs in certain areas or make it more likely that businesses located in an area with a concentration of TCOs will be subject to office exam. Selecting in this manner also cuts the other way—an office exam gives the taxpayer an opportunity to interact in person with the IRS, and office exams have generally better outcomes for taxpayers than correspondence exams, such as lower default rates and higher agreed-to rates, so taxpayers selected for other types of exams due to the lack of nearby TCOs may be worse off than other taxpayers.<sup>32</sup>

### *Office Exams Are Limited by Topic*

SB/SE audits business tax returns. Classifiers sort potential returns for audit between Revenue Agents (RAs) (for field exam) and TCOs. The time planned for an audit by TCOs is substantially less than for an RA, so TCOs address less complicated issues.<sup>33</sup> The Internal Revenue Manual lists examples of issues for office exam:

Dependency exemptions; income from tips, pensions, annuities, rents, fellowships, scholarships, royalties, and income not subject to withholding; deductions for business related expenses; deductions for bad debts; determinations of basis of property; deductions for education expenses; capital gain versus ordinary income determinations; complex miscellaneous itemized deductions such as casualty and theft losses where determinations of fair market value are required; Schedule E basis and passive activity issues for flow-through losses; and deductions for employee business expenses such as travel and entertainment.<sup>34</sup>

However, the IRS notes that is only an illustrative list, provides a checklist guide of additional items to consider, and leaves the classification of the exam up to the judgment of the classifier.<sup>35</sup>

Since office exams have a higher agreed-to rate than correspondence exams, they can serve as a more effective means to get to the right answer for the taxpayer, as well as educating him or her about future compliance. The IRS could test-pilot programs for office exams in areas, such as charitable contributions, and track customer satisfaction, exam results, and future compliance of those taxpayers compared to taxpayers audited via correspondence exams to determine if office exam is more effective.

32 IRS, CDW, AIMS FY 2011 to 2018 (Dec. 2018). For a discussion of the National Taxpayer Advocate's concerns regarding other types of exams see Most Serious Problem: *Correspondence Examination: The IRS's Correspondence Examination Procedures Burden Taxpayers and are not Effective in Educating the Taxpayer and Promoting Future Voluntary Compliance*, *supra*; Most Serious Problem: *Field Examination: The IRS's Field Examination Program Burdens Taxpayers and Yields High No-Change Rates, Which Waste IRS Resources and May Discourage Voluntary Compliance*, *supra*.

33 IRM 4.1.5.3.2.6 (Oct. 20, 2017).

34 *Id.*

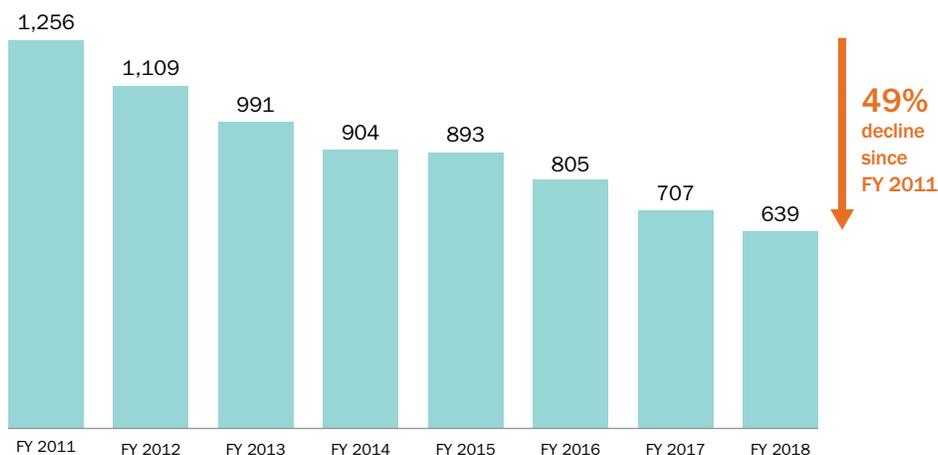
35 *Id.* Further indicated in the provided table for consideration are that Forms 1120s with assets under \$250,000 with no balance sheet issues, no priority issues, no acquisitions, mergers, reorganizations, no recapitalizations, liquidations, no stock redemptions, no IRC 351 stock transfer, and no final returns can be assigned to TCOs; Forms 1040s with Schedule C/F gross receipts and/or costs of goods sold between \$200,000 and \$750,000 if the return has multiple Schedule C/Fs and other indicators or less than \$200,000 if other indicators are not present; individuals receiving wages from closely held C corporations and claiming employee business expenses/Schedule C expenses; gross receipts as a classified issue less than \$200,000; Schedule C/F with only non-gross receipts issues classified and total gross receipts less than \$500,000.

### *Office Exams Are Limited by Number of TCOs*

The employees who conduct office exams have declined precipitously. In FY 2011, the IRS had 1,256 employees conducting office exams and, in FY 2018, only 639, a decrease of 49 percent in only seven years.<sup>36</sup>

**FIGURE 1.10.2, Number of Tax Compliance Auditors Conducting Office Audits, FY 2011 to FY 2018<sup>37</sup>**

**Tax Compliance Auditors Conducting Office Audits, Fiscal Years 2011-2018**



As discussed above, office exams are already limited geographically by employee location, an issue further exacerbated by the staggering decline in IRS employees conducting office exams. Of the remaining 175 locations across the country where TCOs conduct office exams, 32 percent of the offices have only one TCO.<sup>38</sup> In FY 2018, the IRS closed about 79,000 office exams, or 124 exams per examiner.<sup>39</sup>

<sup>36</sup> IRS response to TAS research request (Oct. 15, 2018).

<sup>37</sup> *Id.*

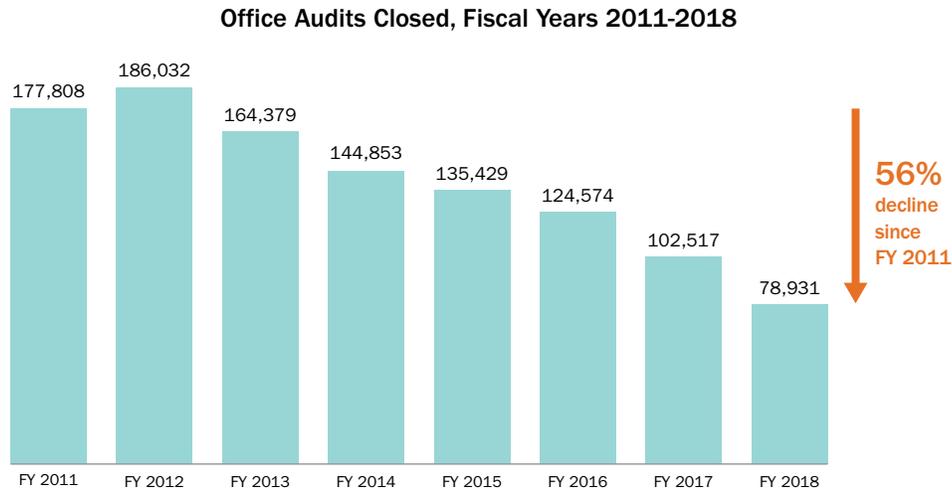
<sup>38</sup> *Id.* IRS response to TAS fact check (Dec. 13, 2018).

<sup>39</sup> *Id.*

### Office Exams Have Significantly Declined

The number of office exams conducted by the IRS has declined since FY 2011 (with the exception of FY 2012). In FY 2011, the IRS closed almost 178,000 office exams, compared to about 79,000 in FY 2018, a nearly 56 percent decrease.<sup>40</sup>

**FIGURE 1.10.3, Number of Office Audits Closed, FY 2011 to FY 2018<sup>41</sup>**



At the same time, dollars assessed from the office exam program have decreased only 28 percent from FY 2011 to FY 2018, suggesting that the IRS is doing a better job selecting returns for office exam.<sup>42</sup> Dollars per return has actually increased, from \$6,666 in FY 2011 to \$10,815 in FY 2018, an increase of approximately 62 percent, further suggesting the IRS is selecting better returns for examination.<sup>43</sup>

The constraints on office exam limit the likelihood of selection for an office exam based on many factors. This may impact the *right to a fair and just tax system*. Taxpayers who are not geographically proximate to an IRS office with office exam personnel are unlikely to ever be selected for an office exam versus those taxpayers who live nearby.

<sup>40</sup> IRS response to TAS information request (Oct. 15, 2018). IRS response to TAS fact check (Dec. 13, 2018).

<sup>41</sup> *Id.*

<sup>42</sup> *Id.*

<sup>43</sup> *Id.*

## CONCLUSION

Promoting voluntary compliance is an important goal. However, the current IRS office exam program cannot show its progress toward this goal because of the way the program is designed and by SB/SE's failure to determine an actual impact on future voluntary compliance. Not only does the IRS not measure future compliance of taxpayers who undergo an audit, it neglects to track the results of its own audits that are appealed. Operating an examination program without significant analysis of the results of the program beyond closure rates and closure results is a missed opportunity for the IRS to improve the process and promote future voluntary compliance.

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Develop measures to track the downstream compliance of audited taxpayers by type of exam.
2. Track results of audits that are appealed by the taxpayer by type of exam.
3. Add educating the taxpayer on future compliance to the quality attributes of an exam for field and office exam.
4. Increase the number of TCOs and put them in more locations throughout the United States.
5. Expand the issues covered by office exam, develop pilot programs for office exams for issues such as charitable contributions, and track the customer satisfaction for these pilots versus taxpayers audited via correspondence exam for the same issues.

## MSP #11 POST-PROCESSING MATH ERROR AUTHORITY: The IRS Has Failed to Exercise Self-Restraint in Its Use of Math Error Authority, Thereby Harming Taxpayers

### RESPONSIBLE OFFICIALS

Ken Corbin, Commissioner, Wage and Investment Division  
William M. Paul, Acting Chief Counsel

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to Privacy*
- *The Right to a Fair and Just Tax System*

### DEFINITION OF PROBLEM

When a return appears to contain one of 17 types of errors (misleadingly called math errors), the IRS can summarily assess additional tax without first giving the taxpayer a notice of deficiency, which triggers the right to petition the Tax Court (*i.e.*, the normal “deficiency procedures”).<sup>2</sup> Because this “math error authority” (MEA) is not limited to clear-cut errors, it can deprive taxpayers of benefits to which they are entitled, and leave them with no realistic opportunity for judicial review, as discussed in prior reports.<sup>3</sup>

The taxpayer is best equipped to receive and understand a math error notice and address any discrepancy immediately after filing. On April 10, 2018, however, the IRS concluded it can use MEA after processing the return, just like an audit.<sup>4</sup> Such delays increase the risk that taxpayers will not be able to respond timely. Yet, the IRS has used this new post-processing MEA to reverse refundable credits for students, children, and the working poor (*i.e.*, the American Opportunity Tax Credit (AOTC), Child

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 See IRC §§ 6213(b), (g)(2) (listing in (A)-(Q), the 17 specific types of errors). If the taxpayer timely responds to a math error notice, then the IRS abates the assessment and must follow deficiency procedures before making another assessment. See IRC §§ 6213(a), (b)(2).

3 See, e.g., National Taxpayer Advocate Fiscal Year (FY) 2019 Objectives Report to Congress 114-118 (Area of Focus: *The IRS Has Expanded Its Math Error Authority, Reducing Due Process for Vulnerable Taxpayers, Without Legislation and Without Seeking Public Comments*); National Taxpayer Advocate 2014 Annual Report to Congress 163; National Taxpayer Advocate 2013 Annual Report to Congress vol. 2, 5, 91-92; National Taxpayer Advocate 2011 Annual Report to Congress 74; National Taxpayer Advocate 2006 Annual Report to Congress 311; National Taxpayer Advocate 2003 Annual Report to Congress 113; National Taxpayer Advocate 2002 Annual Report to Congress 25, 186; National Taxpayer Advocate 2001 Annual Report to Congress 33. For a proposal to expand the opportunity for judicial review, see Legislative Recommendation: *Fix the Flora Rule: Give Taxpayers Who Cannot Pay the Same Access to Judicial Review as Those Who Can*, *infra*.

4 Program Manager Technical Advice (PMTA) 2018-17 (Apr. 10, 2018), [https://www.irs.gov/pub/lanoa/pmta\\_2018\\_17.pdf](https://www.irs.gov/pub/lanoa/pmta_2018_17.pdf).

Tax Credit (CTC), the Additional Child Tax Credit (ACTC), and the Earned Income Tax Credit (EITC), respectively) on 17,691 returns in fiscal year (FY) 2018—often nearly two years after the returns were filed.<sup>5</sup>

The IRS improperly denied credits to 289 of these taxpayers and sent 113 of them the wrong letters to explain why their credits were disallowed, according to the Treasury Inspector General for Tax Administration (TIGTA).<sup>6</sup> TIGTA also said the IRS wasted over \$400,000 doing manual reviews because it did not address the problem systemically and did not reject e-filed returns immediately—a process that would have allowed taxpayers or their preparers to address the problem right away.<sup>7</sup>

The National Taxpayer Advocate is concerned that the IRS may continue to use MEA and its new post-processing MEA in situations where it poses unreasonable risks to the taxpayer's *right to pay no more than the correct amount of tax, to challenge the IRS's position and be heard, to privacy (i.e., that enforcement will "be no more intrusive than necessary")*, and *to a fair and just tax system (i.e., to "expect the tax system to consider [their specific] facts and circumstances")*. She is also concerned it will waste resources when the resulting assessments are incorrect.

## ANALYSIS OF PROBLEM

### Discrepancies in Data Do Not Mean an Assessment Is Needed

Discrepancies can appear on returns even if the taxpayer is entitled to the benefits he or she claimed. For example, the IRS has MEA to assess tax when a taxpayer claims a dependent, but does not include the dependent's correct taxpayer identification number (TIN).<sup>8</sup> Because a TIN is a long string of numbers, it can contain typographical errors.

A TAS study of math errors on dependent TINs found that:<sup>9</sup>

- The IRS subsequently reversed (at least part of) the math errors on 55 percent of the returns with incorrect TINs.
- The IRS could have resolved 56 percent of them using information already in its possession (*e.g.*, the TIN listed on a prior year return).
- In 41 percent of the cases where the IRS could have corrected the TINs (and in another 11 percent where it could have corrected at least one TIN), the taxpayer was denied a tax benefit that he or she was entitled to receive.
- Such taxpayers were denied \$1,274 on average.

5 IRS response to TAS information request (Nov. 9, 2018).

6 Treasury Inspector General for Tax Administration (TIGTA), Ref. No. 2018-40-015, *Employer Noncompliance With Wage Reporting Requirements Significantly Reduces the Ability to Verify Refundable Tax Credit Claims Before Refunds Are Paid* 13 (Feb. 26, 2018).

7 TIGTA, Ref. No. 2018-40-015, *Employer Noncompliance With Wage Reporting Requirements Significantly Reduces the Ability to Verify Refundable Tax Credit Claims Before Refunds Are Paid* 11 (Feb. 26, 2018).

8 IRC § 6213(g)(2)(H). In the case of an individual, a taxpayer identification number (TIN) may include a Social Security number (SSN), an Individual TIN (ITIN), or an Adoption TIN (ATIN). IRS, Pub. 1915 (2018). An ITIN is issued to individuals who are required to have a TIN for tax purposes, but are not eligible for a SSN. An ATIN is a temporary number issued to a child who is being adopted in the U.S. before the child can obtain a SSN.

9 National Taxpayer Advocate 2011 Annual Report to Congress vol. 2, 114, 117-120 (Research Study: *Math Errors Committed on Individual Tax Returns – A Review of Math Errors Issued on Claimed Dependents*).

The IRS's failure to investigate potential errors before assessing tax is inconsistent with general direction from Congress that the IRS should not use MEA to resolve uncertainty against the taxpayer.<sup>10</sup>

As another example, the IRS also has MEA to reverse EITC claimed by a noncustodial parent for a child who is shown on the Federal Case Registry (FCR) of child support orders as being in someone else's custody.<sup>11</sup> An IRS study found that 39 percent of the children reported on the returns selected for audit, based solely on FCR data mismatches were claimed correctly.<sup>12</sup> Because FCR data is not sufficiently reliable, the IRS has adopted the National Taxpayer Advocate's recommendation not to assess math errors based on mismatches between returns and FCR data. However, the IRS may not have undertaken this study without direction from Congress.

### MEA Procedures Raise Concerns When the Assessments Are Erroneous

Any expansion of MEA raises the following concerns when the resulting assessments could be in error:<sup>13</sup>

- The IRS does not always try to resolve apparent discrepancies before burdening taxpayers with summary assessments.
- IRS communication difficulties—confusing letters, fewer letters (*i.e.*, one math error notice as compared to three or more letters in an audit), and shorter deadlines (*i.e.*, 60 days as compared to more than 120 days in an audit)—make it more difficult for taxpayers to respond timely.<sup>14</sup>
- Because it is easier to miss math error deadlines, more taxpayers—particularly low income taxpayers—will have the burden to prove their returns are correct, and lose access to the Tax Court.

10 H.R. REP. No. 94-658, at 290 (1976) (“... care should be taken to be sure that what appears to be an error in addition or subtraction is not in reality an error in transcribing a number from a work sheet, with the final figure being correct even though an intermediate arithmetical step on the return appears to be wrong ... It is expected that the Service will check such possible sources of arithmetical errors before instituting the summary assessment procedures.”). *Id.* at 291 (“... this summary assessment procedure is not to be used where the Service is merely resolving an uncertainty against the taxpayer.”).

11 Economic Growth and Tax Relief Reconciliation Act of 2001, Pub. L. No. 107-16, § 303(g), 115 Stat. 38, 56-57 (2001) (codified at IRC § 6213(g)(2)(M)). The House Conference Report requested a study of the FCR database by the Department of Treasury, in consultation with the National Taxpayer Advocate, of the accuracy and timeliness of the data in the FCR; the efficacy of using math error authority in this instance in reducing costs due to erroneous or fraudulent claims; and the implications of using math error authority in this instance, given the findings on the accuracy and timeliness of the data. H.R. REP. No. 107-84, at 147 (2001) (Conf. Rep.). See also National Taxpayer Advocate 2002 Annual Report to Congress 189 (Legislative Recommendation: *Math Error Authority*).

12 See IRS, *Federal Case Registry Final Report*, Project 5-02-12-3-005 (CR-39) (July 2003) (“almost 39% of the FCR children were allowed per examination ... With the exclusion of no reply cases ... the rate of FCR children that are allowed per examination increases to 53.5%”).

13 For a more detailed discussion of the differences between the audit and math error procedures, see National Taxpayer Advocate Fiscal Year (FY) 2019 Objectives Report to Congress 114-118. For a detailed discussion of the math error process and math error notices, see Most Serious Problem: *Math Error Notices: Although the IRS Has Made Some Improvements, Math Error Notices Continue to Be Unclear and Confusing, Thereby Undermining Taxpayer Rights and Increasing Taxpayer Burden*, *infra*.

14 Although it should be easier for taxpayers to understand and respond to audit notices than math error notices, a TAS study found “almost 40 percent [of those receiving an Earned Income Tax Credit (EITC) audit notice] ... did not understand what the IRS was questioning ... [and] only about half of the respondents felt that they knew what they needed to do in response to the audit letter.” National Taxpayer Advocate 2007 Annual Report to Congress vol. 2, 100, 103-104. For a discussion of continuing problems with math error notices see, Most Serious Problem: *Math Error Notices: Although the IRS Has Made Some Improvements, Math Error Notices Continue to Be Unclear and Confusing, Thereby Undermining Taxpayer Rights and Increasing Taxpayer Burden*, *infra*.

- Internal Revenue Code (IRC) § 7605(b) generally prohibits the IRS from examining a return more than once, but the IRS can examine a return after making a math error adjustment.<sup>15</sup>

For these reasons, the National Taxpayer Advocate has opposed the Treasury Department's repeated requests for Congress to authorize it to use its regulatory authority to expand the types of issues the IRS could address using MEA (called "correctable error" authority).<sup>16</sup> She recommended that Congress limit MEA to the following situations:<sup>17</sup>

1. There is a mismatch between the return and unquestionably reliable data.
2. The IRS's math error notice clearly describes the discrepancy and how taxpayers may contest the assessment.
3. The IRS has researched the information in its possession (*e.g.*, information provided on prior-year returns) that could reconcile the apparent discrepancy.<sup>18</sup>
4. The IRS does not have to analyze facts and circumstances or weigh the adequacy of information submitted by the taxpayer to determine if the return contains an error.
5. The abatement rate for a particular issue or type of inconsistency is below a specified threshold for those taxpayers who respond.
6. For any new data or criteria, the Department of Treasury, in conjunction with the National Taxpayer Advocate, has evaluated and publicly reported to Congress on the reliability of the data or criteria for purposes of assessing tax using math error procedures.

The IRS could adopt these common-sense limits without legislation. Doing so would minimize risks to the taxpayer's *right to pay no more than the correct amount of tax* or *to challenge the IRS's position and be heard*. It would also help prevent the IRS from wasting resources on incorrect assessments.

### Post-Processing Math Error Adjustments Are Even More Burdensome

Post-processing math error adjustments are even more burdensome for taxpayers than regular math error adjustments. If the IRS summarily assesses a liability after processing the return, the taxpayer is less likely to be able to:

- Receive and understand the IRS's communication;
- Discuss the issue with a preparer;
- Access underlying documentation;
- Recall and explain facts relevant to the filing;
- Return any refunds (or endure an offset) without experiencing an economic hardship; and

15 For a detailed discussion of how math errors and other "unreal audits" bypass taxpayer protections, see, *e.g.*, National Taxpayer Advocate 2017 Annual Report to Congress 49-63 (Most Serious Problem: *The IRS Is Conducting Significant Types and Amounts of Compliance Activities That It Does Not Deem to Be Traditional Audits, Thereby Underreporting the Extent of Its Compliance Activity and Return on Investment, and Circumventing Taxpayer Protections*).

16 See, *e.g.*, Department of the Treasury, *General Explanations of the Administration's Fiscal Year 2013 Revenue Proposals* 168-169 (Feb. 2012); Department of the Treasury, *General Explanations of the Administration's Fiscal Year 2017 Revenue Proposals* 225-226 (Feb. 2016). For concerns about the recommendation, see, *e.g.*, National Taxpayer Advocate 2017 Purple Book 44-45; National Taxpayer Advocate 2015 Annual Report to Congress 329-339; Nathan J. Richman, *Expanding Math Error Authority Could Worsen 2 Tax Systems Issues*, 2017 TNT 127-2 (July 5, 2017).

17 See National Taxpayer Advocate 2015 Annual Report to Congress 329-339.

18 It is TAS's understanding that the IRS is legally authorized to correct returns using math error authority so as to benefit the taxpayer (*e.g.*, when it has information sufficient to determine the taxpayer is entitled to a credit).

- Learn how to avoid the problem before the next filing season.

Perhaps for the same reasons, the law limits how long after filing the IRS can make assessments, and the IRS tries to maintain the “currency” of its audits and has a policy statement that generally bars examiners from addressing old delinquencies.<sup>19</sup> Because taxpayers are supposed to have the *right to quality service* and *to privacy* (*i.e.*, the right to expect that enforcement action will be no more intrusive than necessary), the IRS can and should take similar precautions to ensure it detects math errors while processing returns or not at all. If instead, the IRS uses post-processing MEA to recover EITC benefits, it could be sued for violating the taxpayer’s constitutional rights.<sup>20</sup>

### The IRS Is Now Using Post-Processing MEA to Recover Credits

In December 2015, the Protecting Americans From Tax Hikes (PATH) Act barred taxpayers from claiming the AOTC, CTC, ACTC, or EITC using TINs issued after the due date of the return (*e.g.*, using TINs issued in 2015 to file returns for 2014 during 2016, which are called retroactive claims).<sup>21</sup> TIGTA found the IRS had improperly paid these credits to 15,744 taxpayers who filed 2014 returns during the 2016 filing season.<sup>22</sup> TIGTA subsequently found the IRS improperly paid retroactive claims on 2013-2015 returns to 4,509 taxpayers during the 2017 filing season.<sup>23</sup> The IRS used post-processing MEA to recover these credits from 17,691 taxpayers in FY 2018—often nearly two years after they filed the returns.<sup>24</sup>

Like the TAS study of MEA (discussed above), TIGTA’s review of returns processed during the 2017 filing season found that the IRS sometimes got it wrong—improperly denying credits to 289 taxpayers.<sup>25</sup> Moreover, it sent 113 taxpayers the wrong letters to explain why their credits were disallowed, thus giving them the wrong explanations, undermining their ability to correct the IRS’s mistakes or obtain judicial review.<sup>26</sup>

19 IRC § 6501(a) (assessment limitations period); IRS, *Reducing the Federal Tax Gap, A Report on Improving Voluntary Compliance* 36 (Aug. 2, 2007), [https://www.irs.gov/pub/irs-news/tax\\_gap\\_report\\_final\\_080207\\_linked.pdf](https://www.irs.gov/pub/irs-news/tax_gap_report_final_080207_linked.pdf) (discussing audit currency); Policy Statement 5-133 (P-5-133), *reprinted as* IRM 1.2.14.1.18(5) (Aug. 4, 2006) (generally limiting the “enforcement of delinquency procedures for not more than six (6) years”).

20 For a discussion of this argument, see National Taxpayer Advocate, *The IRS Might Recover EITC Using Its Newly Discovered Post-Processing Math Error Authority, but Is It Constitutional?* NTA BLOG (Sept. 13, 2018), <https://taxpayeradvocate.irs.gov/news/nta-blog-the-irs-might-recover-eitc-using-its-newly-discovered-post-processing-math-error-authority-but-is-it-constitutional>.

21 See Sections 204-206 of Division Q of the Consolidated Appropriations Act, Pub. L. No. 114-113, 129 Stat. 2242 (2015) (codified at IRC §§ 32(m), 24(e), and 25A(i)(6)).

22 See TIGTA, Ref. No. 2017-40-042, *Processes Do Not Maximize the Use of Third-Party Income Documents to Identify Potentially Improper Refundable Credit Claims* 5 (July 17, 2017). See also TIGTA, Ref. No. 2018-40-032, *The Internal Revenue Service Is Not in Compliance with Improper Payment Requirements* 11-12 (Apr. 9, 2018); TIGTA, Ref. No. 2018-40-015, *Employer Noncompliance With Wage Reporting Requirements Significantly Reduces the Ability to Verify Refundable Tax Credit Claims Before Refunds Are Paid* 3 (Feb. 26, 2018).

23 TIGTA, Ref. No. 2018-40-015, *Employer Noncompliance With Wage Reporting Requirements Significantly Reduces the Ability to Verify Refundable Tax Credit Claims Before Refunds Are Paid* 9-10 (Feb. 26, 2018).

24 IRS response to TAS information request (Nov. 9, 2018).

25 TIGTA, Ref. No. 2018-40-015, *Employer Noncompliance With Wage Reporting Requirements Significantly Reduces the Ability to Verify Refundable Tax Credit Claims Before Refunds Are Paid* 10 (Feb. 26, 2018).

26 *Id.* at 13 (Feb. 26, 2018).

However, the IRS did not adopt TIGTA's recommendation to substitute a rejection process for e-filed tax returns, citing technical difficulties.<sup>27</sup> Upon receipt of the return, the IRS could reject it and immediately inform the taxpayer that the TIN that was used to claim the credit was not issued before the due date of the return.<sup>28</sup> Such a process would give the taxpayer an opportunity to address the apparent discrepancy proactively, often with the assistance of his or her preparer or tax preparation software, and save the IRS resources (*i.e.*, over \$400,000, according to TIGTA).<sup>29</sup>

## CONCLUSION

Because of the lack of due process afforded to taxpayers when the IRS uses MEA, it should only be used for clear errors. Clear errors can be detected and addressed immediately when the taxpayer is best prepared to understand the IRS's communications and respond timely and appropriately. To reduce the temptation to use MEA in ways that trample taxpayer rights and create costly rework, the IRS should publicly announce a policy that limits its use. Such a policy would help it resist calls to use MEA and post-processing MEA inappropriately.

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS, in collaboration with the National Taxpayer Advocate, adopt a policy statement (or similar guidance) to:

1. Limit the circumstances in which the IRS will use MEA (including post-processing MEA).
2. Voluntarily adopt the limits on the use of MEA recommended to Congress by the National Taxpayer Advocate in her 2015 annual report.<sup>30</sup>
3. Require the IRS to alert taxpayers to any discrepancies as early as possible, for example, by rejecting an e-filed return, where permissible, rather than waiting to use MEA, or waiting even longer to use post-processing MEA.

27 TIGTA, Ref. No. 2018-40-015, *Employer Noncompliance With Wage Reporting Requirements Significantly Reduces the Ability to Verify Refundable Tax Credit Claims Before Refunds Are Paid* 12-13 (Feb. 26, 2018). Any such rejection should obviously be accompanied with a clear and detailed explanation. Before rejecting any return, the IRS's systems should use information in the IRS's possession to help taxpayers correct any apparent discrepancies, such as typos, that might help the taxpayer qualify for the credits they claimed.

28 For the same reasons, the National Taxpayer Advocate recommended the IRS "Reject electronic filed returns when the taxpayer received APTC [the advanced premium tax credit] and did not reconcile on Form 8962, *Premium Tax Credit (PTC)*, as the IRS plans to do for silent returns that do not include Form 8965, *Health Coverage Exemptions*." National Taxpayer Advocate 2017 Annual Report to Congress 266, 276 (Most Serious Problem: *The IRS Has Made Progress in Implementing the Individual and Employer Provisions of the ACA But Challenges Remain*). Of course, the IRS would first have to ensure it is authorized to reject such returns.

29 TIGTA, Ref. No. 2018-40-015, *Employer Noncompliance With Wage Reporting Requirements Significantly Reduces the Ability to Verify Refundable Tax Credit Claims Before Refunds Are Paid* 12-13 (Feb. 26, 2018). If the taxpayer felt they were still entitled to the credit, he or she could file on paper and then explain his or her reasons in any subsequent examination or math error process.

30 See National Taxpayer Advocate 2015 Annual Report to Congress 329-339.

## INTRODUCTION TO NOTICES: Notices Are Necessary to Inform Taxpayers of Their Rights and Obligations, Yet Many IRS Notices Fail to Adequately Inform Taxpayers, Leading to the Loss of Taxpayer Rights

### WHY ARE NOTICES IMPORTANT?

The IRS mailed over 175 million notices in fiscal year (FY) 2018, making notices one of the most frequent interactions between taxpayers and the IRS.<sup>1</sup> In many cases, notices are the primary form of communication from the IRS to taxpayers with respect to matters that have significant impact on taxpayers' lives.

The Taxpayer Bill of Rights lists the *right to be informed* as the first of the ten taxpayer rights because of the importance of taxpayers understanding what they need to do to comply with the tax laws. Taxpayers need clear explanations of the IRS's procedures and actions about their tax liability and the rights they have in response to the IRS's actions. Because notices are often the main communication from the IRS to taxpayers, they are key to ensuring taxpayers are adequately informed. Notices inform taxpayers of important events, such as the IRS's intent to increase the taxpayer's tax liability, the IRS's filing of a Notice of Federal Tax Lien (NFTL) against the taxpayer's property, or of the IRS's intent to levy the taxpayer's wages or bank account. They also inform taxpayers of their right to a hearing to challenge the IRS's actions in the above events—the Collection Due Process (CDP) hearing.<sup>2</sup> Failure to respond to notices can often lead to the loss of core taxpayer rights, such as the *right to pay no more than the correct amount of tax, to appeal the IRS's decision in an independent forum, and to a fair and just tax system*.

If the IRS determines a taxpayer owes more tax, it generally cannot assess the tax until it first provides the taxpayer with notice and an opportunity to challenge the proposed assessment. For example, the IRS has the authority to assess a tax for mathematical errors (*e.g.*,  $2 + 2 = 5$ ), or clerical errors (*e.g.*, writing the number 12 for an entry on the return instead of 21, or leaving an entry blank) if the error led to the taxpayer paying less tax than they owe.<sup>3</sup> This means that, unless taxpayers request an abatement (a reduction or elimination of the deficiency the IRS claims the taxpayer owes) within 60 days from the date on the math error notice, the IRS may proceed with collection of the tax without issuing a Statutory Notice of Deficiency (SNOD) under the normal deficiency procedure as described below.<sup>4</sup> If taxpayers do not request an abatement when they receive a math error notice, they do not receive a SNOD and, therefore, cannot make a prepayment petition to the United States Tax Court (Tax Court) to review the IRS's assessment.

The SNOD,<sup>5</sup> also called a 90-day letter, states the proposed amount of additional income, estate, or gift tax, the taxable year involved, and the basis for the increased tax. It also notifies the taxpayer that he or she has 90 days (or 150 days if the taxpayer resides outside the U.S.) from the date of mailing in which

1 The number of notices was pulled from Computer Paragraph (CP) and Correspondence letters from the IRS Notice Gatekeeper, notices from the Notice Delivery System not included on the Notice Gatekeeper site, and Individual Master File (IMF) and Business Master File (BMF) balance due notices based on cases being in notice status in the Accounts Receivable Dollar Inventory files.

2 See Internal Revenue Code (IRC) §§ 6320 & 6330.

3 IRC §§ 6213(b), (g).

4 IRC § 6213(b)(2)(A).

5 The Statutory Notice of Deficiency (SNOD) is sent to the taxpayer by certified or registered mail. IRC § 6212(a).

to file a petition in the Tax Court if he or she disagrees with the IRS's proposed tax assessment.<sup>6</sup> The notice of deficiency is the taxpayer's "ticket" to the Tax Court, the only prepayment judicial forum where the taxpayer can *appeal an IRS decision*.<sup>7</sup>

After the IRS assesses a liability, the taxpayer may sometimes seek judicial review when the IRS tries to collect. The IRS communicates CDP rights during two critical times. Before the IRS levies property or after it has filed a NFTL, it must send a CDP notice, which gives the taxpayer the right to request an administrative CDP hearing before the IRS Office of Appeals (Appeals).<sup>8</sup> During the CDP hearing, the Appeals Officer must obtain verification that "requirements of any applicable law or administrative procedure have been met."<sup>9</sup> The Appeals Officer also must consider "whether any proposed collection action balances the need for the efficient collection of taxes with the legitimate concern of the person that any collection action be no more intrusive than necessary."<sup>10</sup> Taxpayers are given the opportunity to raise a collection alternative, such as an installment agreement or offer in compromise, and in some instances, they can contest the underlying liability.<sup>11</sup> The CDP hearing also is a prerequisite for challenging the IRS collection action in court. If taxpayers disagree with the IRS's determination after the CDP hearing and wish to appeal, they must file a petition with the Tax Court within 30 days of the Appeals' determination.<sup>12</sup> If taxpayers miss the deadline, the Tax Court does not have jurisdiction to review the IRS's determination and the taxpayers are deprived of their CDP rights.<sup>13</sup>

## SUMMARY

### Background: Prior TAS research and recommendations related to IRS notices

The National Taxpayer Advocate previously recommended that SNODs have the contact information and addresses of Local Taxpayer Advocates printed on them so that taxpayers are aware that there is someone in their state who can assist them with their tax issues.<sup>14</sup> The requirement that this address and contact information be included in SNODs is codified at Internal Revenue Code (IRC) § 6212(a),

6 IRC § 6212(a); Internal Revenue Manual (IRM) 4.8.9.8, *Preparing Notices of Deficiency* (July 9, 2013).

7 For a discussion of the difficulties for taxpayers where they are unable to access the Tax Court, see Legislative Recommendation: *Fix the Flora Rule: Give Taxpayers Who Cannot Pay the Same Access to Judicial Review as Those Who Can*, *infra*.

8 See generally, IRC §§ 6320 (lien), 6330 (levy).

9 IRC § 6330(c)(1).

10 IRC § 6330(c)(3)(C).

11 IRC § 6330(c).

12 IRC § 6330(d)(1). For a discussion of how the current language in several IRS CDP and innocent spouse notices of determination confuses taxpayers, especially *pro se* taxpayers, and causes them to misinterpret the deadline to file a petition with the Tax Court, see National Taxpayer Advocate 2017 Annual Report to Congress 299-306 (Most Serious Problem: *Collection Due Process Notices: Despite Recent Changes to Collection Due Process Notices, Taxpayers Are Still at Risk for Not Understanding Important Procedures and Deadlines, Thereby Missing Their Right to an Independent Hearing and Tax Court Review*); National Taxpayer Advocate 2017 Annual Report to Congress 299-306; (Legislative Recommendation: *Collection Due Process and Innocent Spouse Notices: Amend IRC §§ 6320, 6330, and 6015 to Require That IRS Notices Sent to Taxpayers Include a Specific Date by Which Taxpayers Must File Their Tax Court Petitions and Provide That a Petition Filed by Such Specified Date Will Be Treated As Timely*).

13 For a more thorough discussion of the importance of CDP rights in tax administration, see Nina E. Olson, *Taking the Bull by Its Horns: Some Thoughts on Constitutional Due Process in Tax Collection*, 63 TAX LAWYER 227.

14 National Taxpayer Advocate 2014 Annual Report to Congress 237-244 (Most Serious Problem: *Statutory Notices of Deficiency: Statutory Notices of Deficiency Do Not Include Local Taxpayer Advocate Office Contact Information on the Face of the Notice*).

enacted as part of the Internal Revenue Service Restructuring and Reform Act of 1998.<sup>15</sup> Including this information is especially important given that the IRS lacks a local presence in many areas.<sup>16</sup>

Many IRS notices reference the IRS website to inform taxpayers of their rights or the procedures to respond to notices. However, a TAS research study found that millions of mainly low income taxpayers lack adequate internet access and thus are harmed by the IRS not providing the necessary information on the notices themselves.<sup>17</sup> This situation in and of itself, apart from the issue of unclear or overly complex notices, demonstrates that the IRS is not adequately meeting the needs of taxpayers.<sup>18</sup>

Another problem the National Taxpayer Advocate has expressed concern with is the IRS's expanding use of math error authority to summarily resolve tax issues against taxpayers.<sup>19</sup> This expansion, along with a lack of notice clarity, creates unnecessary burden for taxpayers.<sup>20</sup> In fact, a TAS research study found that 55 percent of math errors involving claimed dependents were abated.<sup>21</sup> Even worse, in over 50 percent of these cases that received no adjustment, the IRS did not issue any refunds that the taxpayers were at least partially entitled to.<sup>22</sup> Due to these problems facing taxpayers, the National Taxpayer Advocate has recommended that the IRS work with TAS to review any proposed expansion of math error authority to ensure taxpayer rights are adequately protected.<sup>23</sup>

In the interest of clearer CDP and Innocent Spouse notices and protecting taxpayer rights, the National Taxpayer Advocate has previously recommended amending IRC §§ 6320, 6330, and 6015 to require that these notices include the specific deadline date by which taxpayers must file a petition and that a petition filed by that date should be treated as timely.<sup>24</sup>

### What are the key elements to making the information understandable?

The language and design of notices can help taxpayers understand what they may owe and how to resolve their tax balance, or it can confuse taxpayers. Confused taxpayers may take wrong actions or no action at all, thus, forfeiting their *rights to pay no more than the correct amount of tax*, to have their

15 Pub. L. No. 105-206, § 1102(b), 112 Stat. 685, 703 (1998).

16 National Taxpayer Advocate 2016 Annual Report to Congress 86-97 (Most Serious Problem: *Geographic Focus: The IRS Lacks an Adequate Local Presence in Communities, Thereby Limiting Its Ability to Meet the Needs of Specific Taxpayer Populations and Improve Voluntary Compliance*).

17 National Taxpayer Advocate 2017 Annual Report to Congress vol. 2 63-64 (Research Study: *A Further Exploration of Taxpayers' Varying Abilities and Attitudes Towards IRS Options for Fulfilling Common Taxpayer Service Needs*).

18 National Taxpayer Advocate 2009 Annual Report to Congress 110 (Most Serious Problem: *Beyond EITC: The Needs of Low Income Taxpayers Are Not Being Adequately Met*).

19 National Taxpayer Advocate Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration* 44-45 (Continue to Limit the IRS's Use of "Math Error Authority" to Clear-cut Categories Specified by Statute) (Dec. 2017); National Taxpayer Advocate 2014 Annual Report to Congress 163-171 (Most Serious Problem: *Math Error Notices: The IRS Does Not Clearly Explain Math Error Adjustments, Making It Difficult for Taxpayers to Understand and Exercise Their Rights*).

20 *Id.*

21 National Taxpayer Advocate 2011 Annual Report to Congress vol. 2 114-144 (Research Study: *Math Errors Committed on Individual Tax Returns: A Review of Math Errors Issued for Claimed Dependents*).

22 *Id.* at 120.

23 National Taxpayer Advocate 2011 Annual Report to Congress 524-530 (Legislative Recommendation: *Mandate That the IRS, in Conjunction with the National Taxpayer Advocate, Review Any Proposed Expanded Math Error Authority to Protect Taxpayer Rights*).

24 National Taxpayer Advocate 2017 Annual Report to Congress 299-306 (Legislative Recommendation: *Collection Due Process and Innocent Spouse Notices: Amend IRC §§ 6320, 6330, and 6015 to Require That IRS Notices Sent to Taxpayers Include a Specific Date by Which Taxpayers Must File Their Tax Court Petitions, and Provide That a Petition Filed by Such Specified Date Will Be Treated As Timely*).

position heard, and to challenge the IRS's actions in Appeals or the Tax Court. All this could result in the IRS wrongfully levying the taxpayers' wages and bank accounts, seizing their home, or prohibiting their freedom to travel internationally.

A literature review in this year's Annual Report to Congress examines the available research on the psychological, cognitive, and behavioral science insights behind effective notice design.<sup>25</sup> The IRS should use these insights, such as writing notices in plain language and designing notices to effectively lay out the steps taxpayers must take to complete necessary actions to protect their rights. The IRS should also prominently include important information, such as deadlines and the rights taxpayers have and can lose by not responding in time. This information needs to be highlighted to draw taxpayers' attention and ensure that taxpayers will timely take appropriate action. However, the IRS must be mindful not to use these insights to the detriment of taxpayers, for example, by using behavioral techniques to influence taxpayers to pay tax bills that they cannot afford to pay and are not required to pay if they are eligible for Currently Not Collectible (CNC-hardship) status.<sup>26</sup>

### Most Serious Problems

In the three Most Serious Problems that follow, the National Taxpayer Advocate expresses concerns about IRS notices that fail to adequately inform taxpayers about their rights, responsibilities, and procedural requirements. The National Taxpayer Advocate also makes suggestions for notice redesign based on how taxpayers best perceive and comprehend written information.<sup>27</sup>

With respect to notice design, the Most Serious Problems described below are detailed in the following pages:

- **MATH ERROR NOTICES:** *Although the IRS Has Made Some Improvements, Math Error Notices Continue to Be Unclear and Confusing, Thereby Undermining Taxpayer Rights and Increasing Taxpayer Burden;*
- **STATUTORY NOTICES OF DEFICIENCY:** *The IRS Fails to Clearly Convey Critical Information in Statutory Notices of Deficiency, Making it Difficult for Taxpayers to Understand and Exercise Their Rights, Thereby Diminishing Customer Service Quality, Eroding Voluntary Compliance, and Impeding Case Resolution;* and
- **COLLECTION DUE PROCESS NOTICES:** *Despite Recent Changes to Collection Due Process Notices, Taxpayers Are Still at Risk for Not Understanding Important Procedures and Deadlines, Thereby Missing Their Right to an Independent Hearing and Tax Court Review.*

25 Literature Review: *Improving Notices Using Psychological, Cognitive, and Behavioral Science Insights*, *infra*.

26 National Taxpayer Advocate 2016 Annual Report to Congress vol. 2 54, 60 (Research Study: *The Importance of Financial Analysis in Installment Agreements (IAs) in Minimizing Defaults and Preventing Future Payment Noncompliance*).

27 See Most Serious Problem: *Statutory Notices of Deficiency: The IRS Fails to Clearly Convey Critical Information in Statutory Notices of Deficiency, Making it Difficult for Taxpayers to Understand and Exercise Their Rights, Thereby Diminishing Customer Service, Eroding Voluntary Compliance, and Impeding Case Resolution*, *infra*; Most Serious Problem: *Collection Due Process Notices: Despite Recent Changes to Collection Due Process Notices, Taxpayers Are Still at Risk for Not Understanding Important Procedures and Deadlines, Thereby Missing Their Right to an Independent Hearing and Tax Court Review*, *infra*; Most Serious Problem: *Math Error Notices: Although the IRS Has Made Some Improvements, Math Error Notices Continue to Be Unclear and Confusing, Thereby Undermining Taxpayer Rights and Increasing Taxpayer Burden*, *infra*.

MSP  
#12**MATH ERROR NOTICES: Although the IRS Has Made Some Improvements, Math Error Notices Continue to Be Unclear and Confusing, Thereby Undermining Taxpayer Rights and Increasing Taxpayer Burden****RESPONSIBLE OFFICIALS**

Ken Corbin, Commissioner, Wage and Investment Division

Mary Beth Murphy, Commissioner, Small Business/Self-Employed Division

**TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to Privacy*
- *The Right to a Fair and Just Tax System*

**DEFINITION OF PROBLEM**

Math error authority was originally intended to give the IRS the ability to summarily correct mistakes that could be fixed just by looking at the face of a taxpayer's return.<sup>2</sup> At the IRS's behest, Congress has since expanded the definition of math error to include a host of other items.<sup>3</sup> Concerned with the consequences to taxpayer rights from the expansion of math error authority, Congress directed that, when the IRS makes an adjustment to a taxpayer's return, it must give an explanation of the adjustment.<sup>4</sup> The explanation of the adjustment in the math error notice is critical to the taxpayer's ability to challenge the adjustment and preserve the right to petition the United States Tax Court (Tax Court), before paying the tax, by timely requesting abatement.<sup>5</sup> In calendar years (CYs) 2015-2017, the IRS issued approximately two million math error notices each year.<sup>6</sup> However, the IRS does not track the abatement rates of math errors.<sup>7</sup>

Despite the congressional directive, math error notices, sent to explain the math error adjustments the IRS made to the taxpayer's return, remain confusing and lack clarity. The National Taxpayer Advocate

<sup>1</sup> See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

<sup>2</sup> The Revenue Act of 1926, Pub. L. 69-20 § 274(f) (1926) (codified at IRC §§ 6213(b), (g)).

<sup>3</sup> See IRC § 6213(g) (lists all current definitions of mathematical or clerical errors).

<sup>4</sup> S. REP. No. 94-938, at 375 (1976); H. REP. No. at 289 (1976).

<sup>5</sup> IRC § 6213(b).

<sup>6</sup> IRS response to TAS information request (Aug. 22, 2018) (number of math error notices issued from 2015-2017 (2015: 1,953,360; 2016: 1,851,621; 2017: 2,318,399)).

<sup>7</sup> IRS response to TAS information request (Aug. 22, 2018).

has expressed concerns about the lack of clarity in math error notices since her 2004 Annual Report to Congress.<sup>8</sup> Although the IRS has improved its explanations on some math error notices, in many cases the notices remain unclear and complex. This makes it difficult for taxpayers to determine what, specifically, the IRS corrected on their return and whether they should accept the adjustment or request a correction, as well as the consequences of inaction. Further, because the IRS does not measure the reversal rates of math error assessments,<sup>9</sup> it has no way of knowing the extent to which it is issuing accurate assessments and forgoes valuable data that could be used to identify which math error notices should be revised for additional clarity.

As a result, the National Taxpayer Advocate remains concerned that:

- The IRS is using its math error authority to summarily resolve increasingly complex issues that go beyond those considered by and allowed by Congress.
- Confusing math error notices affect millions of taxpayers a year and the IRS does not measure math error abatement rates to determine which notices need revisions due to high reversal rates.
- Despite revisions, many math error notices continue to inadequately inform taxpayers of their appeal rights, the consequences of inaction, and the specific nature of the purported error.
- The IRS has failed to use historical data to make simple corrections to taxpayer returns, and instead issues summary assessments and math error notices that are later abated.

## ANALYSIS OF PROBLEM

### Background

The IRS must generally issue a statutory notice of deficiency (SNOD) before assessing tax adjustments on taxpayers who had errors on their tax returns, which led to them paying less tax than they owed.<sup>10</sup> This notice of deficiency gives taxpayers 90 days to petition the Tax Court for a judicial review of an IRS assessment before paying the tax.<sup>11</sup> However, the IRS has the authority to assess a tax for mathematical errors (*e.g.*,  $2 + 2 = 5$ ) or clerical errors (*e.g.*, writing 12 for an entry on the return instead of 21, or leaving an entry blank).<sup>12</sup> This means that, unless taxpayers request an abatement (a reduction or elimination of the deficiency the IRS claims the taxpayer owes) within 60 days from the date on the math error notice, the IRS may proceed with collection of the tax without issuing a SNOD under the normal deficiency procedure.<sup>13</sup> In other words, a SNOD is the ticket to the Tax Court; if taxpayers do not request an abatement when they receive a math error notice, they do not receive that ticket.

### The IRS Is Using its Math Error Authority to Summarily Resolve Increasingly Complex Issues That Go Beyond Those Considered by and Allowed by Congress

In 1976, Congress set new rules around the IRS's math error authority, expanding the errors the IRS could summarily assess to include "clerical errors."<sup>14</sup> Congress sought to improve taxpayer rights around

<sup>8</sup> See National Taxpayer Advocate 2014 Annual Report to Congress 163-171; National Taxpayer Advocate 2011 Annual Report to Congress 74-92; National Taxpayer Advocate 2011 Annual Report to Congress 524-530; National Taxpayer Advocate 2004 Annual Report to Congress 163-179.

<sup>9</sup> IRS response to TAS information request (Aug. 22, 2018).

<sup>10</sup> IRC § 6213(a).

<sup>11</sup> *Id.*

<sup>12</sup> IRC §§ 6213(b), (g).

<sup>13</sup> IRC § 6213(b)(2)(A).

<sup>14</sup> Tax Reform Act of 1976, Pub. L. 94-455.

math errors, providing abatement remedies for taxpayers to contest math errors before paying the tax and that the taxpayer “must be given an explanation of the asserted error.”<sup>15</sup> Congress, concerned with the IRS’s use of math error authority where its use was not authorized by statute, also sought to clarify limits to the IRS’s authority, noting that the summary assessment procedure should not be used to merely resolve an uncertainty against the taxpayer.<sup>16</sup> Congress provided extensive examples describing how it envisioned the IRS’s expanded summary assessment authority to work. For instance:

[L]ine 6b of the Form 1040 requires the taxpayer to list, “First names of your dependent children who lived with you” and then to enter the number of those dependent children in a column for personal exemptions. If a taxpayer lists three names on line 6b but then enters “4” in the column, it is not clear whether the taxpayer miscounted (in which case the taxpayer should have written “3” in the column), or whether the taxpayer erroneously omitted the name of one of the dependent children (in which case the taxpayer’s column-entry of “4” would be correct). In this case, the Service should, of course, take steps to determine which entry is correct, and the taxpayer has the obligation of showing that he or she is entitled to the number of exemptions claimed. However, this summary assessment procedure is not to be used where the Service is merely resolving an uncertainty against the taxpayer.<sup>17</sup>

Despite this congressional direction, the IRS’s use of math error authority to summarily resolve increasingly complex issues goes beyond those considered by and allowed by Congress.<sup>18</sup> If the IRS uses its math error authority to address these more complex issues that may require additional fact-finding, like correctable error and post-processing, the IRS’s assessments are more likely to be erroneous.<sup>19</sup> Notice unclarity and shorter math error deadlines, along with the expansion of math error authority, increases the risk of incorrect assessments and erosion of taxpayer rights, such as *the right to be informed*, *the right to pay no more than the correct amount of tax*, and *the right to appeal an IRS decision in an independent forum*. Despite this, the Department of Treasury has encouraged the expansion of IRS math error authority because it is cost efficient and simpler than regular deficiency procedures.<sup>20</sup>

15 General Explanation of the Tax Reform Act of 1976, 94th Cong., 2d Sess., 372 (1976).

16 *Id.*

17 *Id.*

18 For a discussion on the IRS’s expanded use of math error authority for “correctable errors,” see Nina E. Olson, *Why Correctable Error Authority Raises Significant Taxpayer Rights Concerns – Part 1*, NTA BLOG (Aug. 9, 2017), <https://taxpayeradvocate.irs.gov/news/why-correctable-authority-error-raises-significant-taxpayer-rights-concerns-part-1>; Nina E. Olson, *Correctable Error Authority Part 2: Why Correctable Error Authority Creates More Problems Than It Resolves*, NTA BLOG (Aug. 16, 2017), <https://taxpayeradvocate.irs.gov/news/correctable-error-authority-part-2-why-correctable-error-authority-creates-more-problems-than-it-resolves?category=Tax%20News>. For a discussion on the IRS’s use of post-processing with math errors, see Most Serious Problem: *Post-Processing Math Error Authority: The IRS Has Failed to Exercise Self-Restraint in Its Use of Math Error Authority, Thereby Harming Taxpayers*, *supra*.

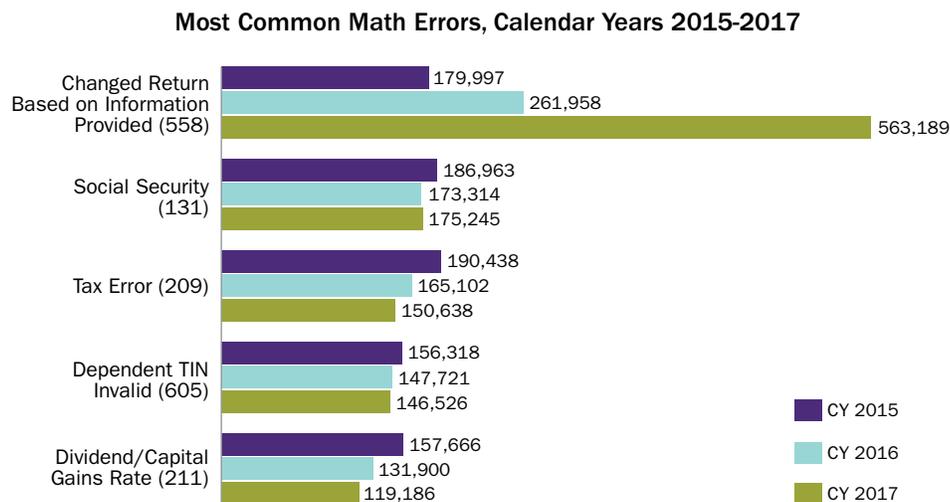
19 See National Taxpayer Advocate Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration 44-45 (Continue to Limit the IRS’s Use of “Math Error Authority” to Clear-cut Categories Specified by Statute)* (Dec. 2017); National Taxpayer Advocate 2014 Annual Report to Congress 163-171 (Most Serious Problem: *Math Error Notices: The IRS Does Not Clearly Explain Math Error Adjustments, Making It Difficult for Taxpayers to Understand and Exercise Their Rights*).

20 Department of the Treasury, *General Explanations of the Administration’s Fiscal Year 2017 Revenue Proposals*, 225-226 (Feb. 2016), <https://www.treasury.gov/resource-center/tax-policy/Documents/General-Explanations-FY2017.pdf>. See also National Taxpayer Advocate Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration 44-45 (Continue to Limit the IRS’s Use of “Math Error Authority” to Clear-cut Categories Specified by Statute)* (Dec. 2017).

### The IRS Use of Math Error Authority Affects Millions of Taxpayers Annually, and Confusing Notices May Disproportionately Affect Low Income Taxpayers

For CYs 2015-2017, the IRS issued approximately two million math error notices each year.<sup>21</sup> Figure 1.12.1 shows the five most common types of math error notices the IRS issued in CYs 2015-2017.<sup>22</sup> In addition to these standard notices, the IRS issued around 20,000 non-standard math error notices annually over the same three-year period.<sup>23</sup>

**FIGURE 1.12.1**<sup>24</sup>



Math error notices lacking in clarity may disproportionately harm low income taxpayers who more often have limited English proficiency, limited computer access, lower literacy rates, lower education levels, and disabilities.<sup>25</sup> Some math error notices may especially affect low income taxpayers. For example, the median income of those with Earned Income Credit (EIC) and Individual Taxpayer Identification Number (ITIN) math errors is lower than for other common math errors.

21 IRS response to TAS information request (Aug. 22, 2018) (number of math error notices issued from 2015-17 (2015: 1,953,360; 2016: 1,851,621; 2017: 2,318,399)).

22 IRS response to TAS information request (Aug. 22, 2018). The five most common math error notices issued from 2015-2017 were, by taxpayer notice code (TPNC): TPNC 558 (We changed the refund amount or the amount you owe on your tax return based on the information you provided in response to our previous correspondence); TPNC 131 (We changed the amount of taxable social security benefits on page 1 of your tax return because there was an error in the computation of the taxable amount); TPNC 209 (We changed the amount of tax shown on your return. The amount entered was incorrect based on your taxable income and filing status); TPNC 605 (Each dependent listed on your tax return must have a valid Social Security number (SSN) or Individual Taxpayer Identification Number (ITIN). For one or more of your dependents the last name doesn't match our records or the records provided by the Social Security Administration...); TPNC 211 (We changed the amount of tax shown on your return. The tax rates on Qualified Dividends and Capital Gains are generally lower than the standard rates. It appears your tax was not computed using these rates or the amount of tax was computed incorrectly).

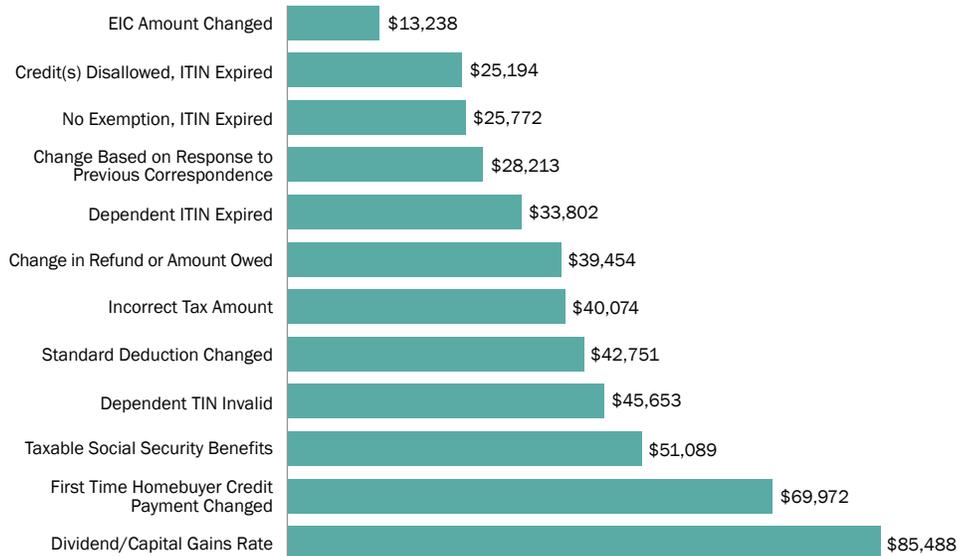
23 IRS response to TAS information request (Aug. 22, 2018) (Nonstandard notices are those errors not assigned a TPNC, and the IRS must write these notices individually depending on the circumstances. From calendar years (CY) 2015-2017, the IRS issued 58,792 nonstandard math error notices; 2015: 16,232; 2016: 23,925; 2017: 18,635).

24 *Id.* We are uncertain of the exact reason for the TPNC 558 spike between CYs 2016 and 2017, but it may have been caused by the IRS using TPNC 558 for a temporary tax issue instead of creating a new code and reprogramming its notices for a short-term issue.

25 National Taxpayer Advocate 2009 Annual Report to Congress 110 (Most Serious Problem: *Beyond EITC: The Needs of Low Income Taxpayers Are Not Being Adequately Met*).

FIGURE 1.12.2<sup>26</sup>

## Median Income by Selected Math Errors, Calendar Year 2017



ME Code	Description	Median TPI	Count
285	EIC Amount Changed	\$13,238	75,957
817	Credit(s) Disallowed, ITIN Expired	\$25,194	75,199
642	No Exemption, ITIN Expired	\$25,772	70,021
558	Change Based on Response to Previous Correspondence	\$28,213	556,113
644	Dependent ITIN Expired	\$33,802	80,426
299	Change in Refund or Amount Owed	\$39,454	87,025
209	Incorrect Tax Amount	\$40,074	153,058
192	Standard Deduction Changed	\$42,751	80,263
605	Dependent TIN Invalid	\$45,653	144,263
131	Taxable Social Security Benefits	\$51,089	181,298
649	First-Time Homebuyer Credit Payment Changed	\$69,972	50,967
211	Dividend/Capital Gains Rate	\$85,488	131,871

However, when TAS asked the IRS directly if it tracks or reports the income demographics for various math error notice recipients, the IRS replied that it, “does not track, report, or collect this data,” which keeps the IRS from making adjustments to its notices based on income demographics.<sup>27</sup> The IRS Office

26 Calculation by TAS Research. Median Total Positive Income and counts for taxpayers with presence of Taxpayer Notice Codes, CY 2017. IRS, Compliance Data Warehouse (CDW), Individual Returns Transaction File (IRTF) (data retrieved Oct. 30, 2018).

27 IRS response to TAS information request (Aug. 22, 2018).

of Chief Counsel is given an opportunity to review each math error notice revision and taxpayer notice code (TPNC) language for legal sufficiency,<sup>28</sup> although legally sufficient notices may still lack clarity and be difficult for taxpayers, especially low income taxpayers, to understand.

### The IRS Conducts Math Error Notice Revisions Piecemeal, and Math Error Notices Continue to Lack Clarity, Despite Revisions

Below are two examples of math error notices that lack clarity and do not ensure that taxpayer rights are being adequately protected. Example 1 discusses a TPNC, a standard math error explanation coded into notices and sent to taxpayers.<sup>29</sup> Example 2 discusses the entirety of a math error notice, the CP11.

**Example 1:** “We changed the refund amount or the amount you owe on your tax return based on the information you provided in response to our previous correspondence.”<sup>30</sup>

A notice with this TPNC is sent to taxpayers after the IRS has already contacted the taxpayer for additional information and the taxpayer has responded. The letter requesting additional information for processing is the 12C letter, on which TPNC 558 is sometimes included.<sup>31</sup> Math error notices have a standard layout and the IRS inserts pre-worded paragraphs into certain parts of the notices that fit the circumstances of the taxpayer. If the IRS made a change to a taxpayer’s return based on information the taxpayer provided previously, the taxpayer is sent a notice with this TPNC explanation. However, this explanation lacks clarity and specificity. It does not explicitly describe the issue. Neither does it detail what correspondence the notice is referring to. This provides little clarity when a taxpayer may have had more than one correspondence with the IRS, especially if the taxpayer had multiple questionable items on their tax return. What if the taxpayer made several calls to the IRS, or sent several letters? What specific piece of information is the IRS referring to? The TPNC does not explain whether the IRS accepted or rejected the information the taxpayer provided.

While some notices do cite the line on the return that the IRS changed,<sup>32</sup> they often provide an inadequate explanation to the taxpayer of the full nature of the issue with his or her return or previous correspondence. As noted earlier, when Congress expanded summary assessment authority for math errors in 1976, it explicitly instructed the IRS that “the taxpayer must be given an explanation of the asserted error.”<sup>33</sup> Congress also provided examples describing how it envisioned the IRS’s expanded summary assessment authority would work.<sup>34</sup> Thus, to be consistent with the examples in the legislative history, the IRS should cite the specific issues and correspondence it is referring to, along with the line numbers and description of what was adjusted, and the amount of increase or decrease in taxable income and tax.

The IRS has recently revised some math error notices (*e.g.*, the CP11). While we commend the IRS for these efforts, the newly revised notices still lack clarity in some areas and can be further improved.

28 IRS response to TAS information request (Aug. 22, 2018).

29 See Internal Revenue Manual (IRM) 3.12.220.1.24 (Jan. 1, 2016).

30 TPNC 558.

31 IRS, Letter 12C, *Individual Return Incomplete for Processing: Forms 1040, 1040A or 1040EZ* (Jan. 2, 2018).

32 For example, IRS, Letter 12C, *Individual Return Incomplete for Processing: Forms 1040, 1040A or 1040EZ* (Jan. 2, 2018).

33 General Explanation of the Tax Reform Act of 1976, 94th Cong., 2d Sess., 372 (1976).

34 See General Explanation of the Tax Reform Act of 1976, 94th Cong., 2d Sess., 372-374 (1976) (for the examples Congress gave on how to handle math error issues for arithmetic errors, use of tables, inconsistent entries, omissions of supporting schedules, and exceeding statutory limits).

FIGURE 1.12.3, Example 2: The 2017 and 2018 CP11 (“Math Error Balance Due of \$5 or More”)



Department of the Treasury  
Internal Revenue Service

Changes to your 2015 Form 1040

**Amount due:** [REDACTED]

We found a miscalculation on your 2015 Form 1040, which affects the following area of your return:

- Tax Computation

We changed your return to correct this error. As a result, you owe [REDACTED]

**What you need to do immediately**

Review this notice, and compare our changes to the information on your tax return.

**If you agree with the changes we made**

- Pay the amount due of [REDACTED] by March 13, 2017, to avoid additional penalty and interest charges.

Continued on back...



**Payment**

- Make your check or money order payable to the United States Treasury.
- Write your Social Security number [REDACTED] the tax year (2015), and the form number (1040) on your payment and any correspondence.

**Amount due by March 13, 2017** [REDACTED]

INTERNAL REVENUE SERVICE

Notice CP11

Tax Year 2015

Notice date February 20, 2017

Social Security number [REDACTED]

To contact us 1-800-829-0922

Page 1 of 5

Included due date for payment, but nothing for 60day appeal deadline.

**Billing Summary**

Tax you owed [REDACTED]

Payments you made [REDACTED]

~~Failure-to-file penalty~~ [REDACTED]

Failure-to-pay penalty [REDACTED]

Interest charges [REDACTED]

**Amount due by March 13, 2017** [REDACTED]

Includes due by date, but not loss of prepayment appeal date.



Notice	CP11
Tax Year	2015
Notice date	February 20, 2017
Social Security number	[REDACTED]
Page 2 of 5	

**What you need to do immediately — continued**

**If you agree with the changes we made — continued**

- Pay online or mail a check or money order with the attached payment stub. **You can pay online now at [www.irs.gov/payments](http://www.irs.gov/payments).**

No information about appeal rights or the 60-day deadline.



**If you disagree with the amount due**

- Call us at 1-800-829-0922 to review your account with a representative. Be sure to have your account information available when you call.

We'll assume you agree with the information in this notice if we don't hear from you.

**Payment options**

**Pay now electronically**

We offer free payment options to securely pay your tax bill directly from your checking or savings account. When you pay online or with your mobile device, you can:

- Receive instant confirmation of your payment
- Schedule payments in advance
- Reschedule or cancel a payment before the due date

You can also pay by debit or credit card for a small fee. To see all of our payment options, visit [www.irs.gov/payments](http://www.irs.gov/payments).

**Payment plans**

If you can't pay the full amount you owe, pay as much as you can now and make arrangements to pay your remaining balance. Visit [www.irs.gov/paymentplan](http://www.irs.gov/paymentplan) for more information on installment agreements and online payment agreements. You can also call us at 1-800-829-0922 to discuss your options.

**Offer in Compromise**

An offer in compromise allows you to settle your tax debt for less than the full amount you owe. If we accept your offer, you can pay with either a lump sum cash payment plan or periodic payment plan. To see if you qualify, use the Offer in Compromise Pre-Qualifier tool on our website. For more information, visit [www.irs.gov/offers](http://www.irs.gov/offers).

The explanation of the error is not provided until page 3, instead of on page 1 as a vital piece of information, which studies show will make it less likely taxpayers will read it.

CP11  
Tax Year 2015  
Notice date February 30, 2017  
Social Security number  
Page 3 of 5

Payment options – continued

Account balance and payment history

For information on how to obtain your current account balance or payment history, go to www.irs.gov/balancedue.

If you already paid your balance in full within the past 21 days or made payment arrangements, please disregard this notice.

If you think we made a mistake, call 1-800-829-0922 to review your account.

If we don't hear from you

- Pay by March 13, 2017, to avoid penalty and interest charges.

Changes to your 2015 tax return

Information was changed because of the following:

- We changed the refund amount or the amount you owe on your tax return because the amount entered on your tax return was computed incorrectly.

Your tax calculations

Description	Amount
Adjusted gross income, line 37	
Taxable income, line 43	
Total tax, line 63	

Your payments and credits

Description	Amount
Income tax withheld, line 64	
Estimated tax payments, line 65	
Other credits, lines 66a, 67-73	
Other payments	
Total payments and credits	

The notice now includes the lines on the return where the errors occurred, which assists with taxpayer understanding.

Penalties

We are required by law to charge any applicable penalties.

Failure-to-file

Description	Amount
Total failure-to-file	

We assess a 5% monthly penalty for filing your return late for each month or part of a month the return is late, for up to 5 months. When a penalty for paying late applies for the same month, the amount of the penalty for filing late for that month is reduced by the amount of the penalty for paying late for that month. The penalty for paying late is 1/2% for each month or part of a month. We base the monthly penalty for filing late on the tax required to be shown on the return that you didn't pay by the original return due date, without regard to extensions. We base the monthly penalty for paying late on the net unpaid tax at the beginning of each penalty month following the payment due date for that tax. When an income tax return is more than 60 days late, the minimum penalty is \$205 or 100% of the tax required to be shown on the return that you didn't pay on time, whichever is less. (Internal Revenue Code section 6651)

Failure-to-pay

Date received	Months late	Unpaid amount	Penalty rate	Amount

Notice CP11  
 Tax Year 2015  
 Notice date February 20, 2017  
 Social Security number [REDACTED]  
 Page 4 of 5

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**Total failure-to-pay**

We assess a 1/2% monthly penalty for not paying the tax you owe by the due date. We base the monthly penalty for paying late on the net unpaid tax at the beginning of each penalty month following the payment due date for that tax. This penalty applies even if you filed the return on time. We charge the penalty for each month or part of a month the payment is late; however, the penalty can't be more than 25% in total.

- The due date for payment of the tax shown on a return generally is the return due date, without regard to extensions.
- The due date for paying increases in tax is within 21 days of the date of our notice demanding payment (10 business days if the amount in the notice is \$100,000 or more).

If we issue a Notice of Intent to Levy and you don't pay the balance due within 10 days of the date of the notice, the penalty for paying late increases to 1% per month. For individuals who filed on time, the penalty decreases to 1/4% per month while an approved installment agreement with the IRS is in effect for payment of that tax. (Internal Revenue Code section 6651)

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**Removal or reduction of penalties**

We understand that circumstances - such as economic hardship, a family member's death, or loss of financial records due to natural disaster - may make it difficult for you to meet your taxpayer responsibility in a timely manner.

If you would like us to consider removing or reducing any of your penalty charges, please do the following:

- Identify which penalty charges you would like us to reconsider (e.g., 2005 late filing penalty).
- For each penalty charge, explain why you believe it should be reconsidered.
- Sign your statement, and mail it to us.

We will review your statement and let you know whether we accept your explanation as reasonable cause to reduce or remove the penalty charge(s).

---

**Removal of penalties due to erroneous written advice from the IRS**

If you were penalized based on written advice from the IRS, we will remove the penalty if you meet the following criteria:

- If you asked the IRS for written advice on a specific issue.
- You gave us complete and accurate information.
- You received written advice from us.
- You relied on our written advice and were penalized based on that advice.

To request removal of penalties based on erroneous written advice from us, submit a completed Claim for Refund and Request for Abatement (Form 843) to the IRS service center where you filed your tax return. For a copy of the form or to find your IRS service center, go to [www.irs.gov](http://www.irs.gov) or call 1-800-829-0922.

  
**Notice** CP11  
**Tax Year** 2015  
**Notice date** February 20, 2017  
**Social Security number**   
 Page 5 of 5

**Interest charges**

We are required by law to charge interest when you do not pay your liability on time. Generally, we calculate interest from the due date of your return (regardless of extensions) until you pay the amount you owe in full, including accrued interest and any penalty charges. Interest on some penalties accrues from the date we notify you of the penalty until it is paid in full. Interest on other penalties, such as failure to file a tax return, starts from the due date or extended due date of the return. Interest rates are variable and may change quarterly. (Internal Revenue Code section 6601)

Period	Days	Interest rate	Interest factor	Amount due	Interest charge
					

We multiply your unpaid tax, penalties, and interest (the amount due) by the interest rate factor to determine the interest due.

**Additional information**

- Visit [www.irs.gov/cp11](http://www.irs.gov/cp11)
- You may find the following publications helpful:
  - Publication 1, Your Rights as a Taxpayer
  - Publication 594, The Collection Process
- For tax forms, instructions, and publications, visit [www.irs.gov](http://www.irs.gov) or call 1-800-TAX-FORM (1-800-829-3676).
- Did you e-file your tax return? Electronically filed returns are less likely to have math errors resulting in notices such as this one. It's free to file your taxes electronically. Go to [www.irs.gov/efile](http://www.irs.gov/efile) for information and instructions.
- Paying online is convenient, secure, and ensures timely receipt of your payment. To pay your taxes online or for more information, go to [www.irs.gov/payments](http://www.irs.gov/payments).
- You can contact us by mail at the address at the top of this notice. Be sure to include your social security number, the tax year, and the form number you are writing about.
- Keep this notice for your records.

Nothing about right to appeal. No mention of TAS or LITCs, unlike 2018 CP11.

If you need assistance, please don't hesitate to contact us.



Department of the Treasury  
Internal Revenue Service  
Atlanta, GA 39901-0010

[Redacted]

Notice	CP11
Tax year	2017
Notice date	February 24, 2018
Social security number	nnn-nn-nnnn
To contact us	Phone 1-NNN-NNN-NNNN
Your caller ID	nnnn

Page 1 of 7

Changes to your 2017 Form 1040

### Amount due: \$362.73

We found miscalculations on your 2017 Form 1040, which affect the following areas of your return:

- Child Tax Credit
- Earned Income Tax Credit

We changed your return to correct these errors. As a result, you owe \$362.73.

#### Billing Summary

Tax you owed	\$1,828.00
Shared responsibility payment	2.00
Payments you made	-1,624.00
Failure-to-file penalty	135.00
Interest charges	21.73
<b>Amount due by March 16, 2018</b>	<b>\$362.73</b>

#### What you need to do immediately

Large, bold font on first page draws attention to need to pay.

Review this notice and compare our changes to the information on your tax return

#### If you agree with the changes we made

- Pay the amount due of \$362.73 by March 16, 2018, to avoid additional penalty and interest charges.
- Pay online or mail a check or money order with the attached payment stub. **You can pay online now at [www.irs.gov/payments](http://www.irs.gov/payments).**

Continued on back...



Actual deadline date for payment is included, but no mention of 60-day deadline to request abatement.

[Redacted]

Notice	CP11
Notice date	February 24, 2018
Social security number	nnn-nn-nnnn

#### Payment

- Make your check or money order payable to the United States Treasury.
- Write your social security number (nnn-nn-nnnn), the tax year (2017), and the form number (1040) on your payment.

Amount due by March 16, 2018

**\$362.73**

INTERNAL REVENUE SERVICE  
AUSTIN, TX 73301-0023  
s018999546711s

0000 0000000 00000000000 0000000 0000

First page is designed like a bill, with amount due and due by date before any mention of appeal rights or deadlines.

Smaller font and non-bold, deemphasizes this section on appeal rights compared to the "if you agree" and payment information above.

Notice CP11  
Tax year 2017  
Notice date February 24, 2018  
Social security number nnn-nn-nnnn  
Page 2 of 7

What you need to do immediately – continued

**If you disagree with the amount due**

Call us at [1-800-xxx-xxxx] to review your account with a representative. Be sure to have your account information available when you call.

Though 60 days mentioned, does not include the actual deadline date like "amount due by" on page 1.

- If you contact us in writing within 60 days of the date of this notice, we will reverse the change we made to your account. However, if you are unable to provide us additional information that justifies the reversal and we believe the reversal is in error, we will forward your case for audit. This step gives you formal appeal rights, including the right to appeal our decision in court before you have to pay the additional tax. After we forward your case, the audit staff will contact you within 5 to 6 weeks to fully explain the audit process and your rights. If you do not contact us within the 60-day period, you will lose your right to appeal our decision before payment of tax.

Improvement from previous math error notices by including the taxpayer's appeal rights and 60-day deadline.

- If you do not contact us within 60 days, the change will not be reversed and you must pay the additional tax. You may then file a claim for refund. You must submit the claim within 3 years of the date you filed the tax return, or within 2 years of the date of your last payment for this tax.

We'll assume you agree with the information in this notice if we don't hear from you.

[Back of payment stub]

Appeal rights are on page 2 of a 7-page notice, and research shows that many people do not even read the second page. Such important information should be on the first page.

Payment options are included and emphasized before the notice explains the specific nature of the math error.



**Notice** CP11  
**Tax year** 2017  
**Notice date** February 24, 2018  
**Social security number** nnn-nn-nnnn  
 Page 3 of 7

**Payment options**

**Pay now electronically**

We offer free payment options to securely pay your tax bill directly from your checking or savings account. When you pay online or with your mobile device, you can:

- Receive instant confirmation of your payment
- Schedule payments in advance
- Reschedule or cancel a payment before the due date

You can also pay by debit or credit card for a small fee. To see all of our payment options, visit [www.irs.gov/payments](http://www.irs.gov/payments).

**Payment plans**

If you can't pay the full amount you owe, pay as much as you can now and make arrangements to pay your remaining balance. Visit [www.irs.gov/paymentplan](http://www.irs.gov/paymentplan) for more information on installment agreements and online payment agreements. You can also call us at 1-800-829-8374 to discuss your options.

**Offer in Compromise**

An offer in compromise allows you to settle your tax debt for less than the full amount you owe. If we accept your offer, you can pay with either a lump sum cash payment plan or periodic payment plan. To see if you qualify, use the Offer in Compromise Pre-Qualifier tool on our website. For more information, visit [www.irs.gov/offers](http://www.irs.gov/offers).

**Account balance and payment history**

For information on how to obtain your current account balance or payment history, go to [www.irs.gov/payments](http://www.irs.gov/payments).

If you already paid your balance in full within the past 21 days or made payment arrangements, please disregard this notice.

If you think we made a mistake, call 1-800-829-8374 to review your account.

**If we don't hear from you**

Pay \$362.73 by March 16, 2018, to avoid additional penalty and interest charges.

Explanation of error does not appear until page 4. Taxpayers must read through many pages to find this critical information. Appeal rights come before, but the error the taxpayer may appeal does not appear until this page. Most people won't even read this far.

**Notice** CP11  
**Tax year** 2017  
**Notice date** February 24, 2018  
**Social security number** nnn-nn-nnnn  
**Page 4 of 7**

**Changes to your 2017 tax return**

Was it one? Was it more than one? What is the age limitation? More specific information should be included so that the taxpayer will know if the adjustment was correct and the nature of the error.

We changed your information because:

- We didn't allow part or all of your child tax credit and/or additional child tax credit on page 2 of your tax return. One or more of your children exceeds the age limitation
- We changed the amount claimed as Earned Income Credit (EIC) on your tax return. The amount claimed as EIC was figured or entered incorrectly on your tax return.

**Your tax calculations**

Including the line number and the differences in calculations is an improvement over previous notices.

Description	Your calculation	IRS calculation
Adjusted gross income, line 37	\$13,829.00	\$13,829.00
Taxable income, line 43	\$0.00	\$0.00
Shared responsibility payment	\$0.00	\$2.00
<b>Total tax, line 63</b>	<b>\$1,828.00</b>	<b>\$1,828.00</b>

**Your payments and credits**

Description	IRS calculations
Income tax withheld, line 64	\$0
Estimated tax payments, line 65	0
Other credits, line 66	1,624.00
Other payments line 74	0
<b>Total payments and credits</b>	<b>\$1,624.00</b>

**Penalties**

We are required by law to charge any applicable penalties

**Failure-to-file**

Description	Amount
<b>Total failure-to-file</b>	<b>\$135.00</b>

We assess a 5% monthly penalty for filing your return late for each month or part of a month the return is late, for up to 5 months.

When a penalty for paying late applies for the same month, the amount of the penalty for filing late for that month is reduced by the amount of the penalty for paying late for that month. The penalty for paying late is ½% for each month or part of a month.

We base the monthly penalty for filing late on the tax required to be shown on the return that you didn't pay by the original return due date, without regard to extensions. We base the monthly penalty for paying late on the net unpaid tax at the beginning of each penalty month following the payment due date for that tax.

When an income tax return is more than 60 days late, the minimum penalty is \$210 or 100% of the tax required to be shown on the return that you didn't pay on time, whichever is less.

(Internal Revenue Code Section 6651)

<b>Notice</b>	<b>CP11</b>
<b>Tax year</b>	<b>2017</b>
<b>Notice date</b>	<b>February 24, 2018</b>
<b>Social security number</b>	<b>nnn-nn-nnnn</b>
<b>Page 5 of 7</b>	

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### **Removal or reduction of penalties**

We understand that circumstances—such as a serious illness or injury, a family member's death, or loss of financial records due to natural disaster—may make it difficult for you to meet your taxpayer responsibility in a timely manner.

We can generally process your request for penalty removal or reduction quicker if you contact us at the number listed above with the following information:

- Identify which penalty charges you would like us to reconsider (e.g., 2016 late filing penalty).
- For each penalty charge, explain why you believe it should be reconsidered.

If you write us, include a signed statement and supporting documentation for penalty abatement request.

We'll review your statement and let you know whether we accept your explanation as reasonable cause to reduce or remove the penalty charge(s).

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### **Removal of penalties due to erroneous written advice from the IRS**

If you were penalized based on written advice from the IRS, we will remove the penalty if you meet the following criteria:

- You wrote us asking for written advice on a specific issue
- You gave us adequate and accurate information
- You received written advice from us
- You reasonably relied on our written advice and were penalized based on that advice

To request removal of penalties based on erroneous written advice from us, submit a completed Claim for Refund and Request for Abatement (Form 843) to the address shown above. For a copy of the form, go to [www.irs.gov](http://www.irs.gov) or call 1-800-TAX-FORM (1-800-843-8374).

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	<b>Notice</b>	CP11
	<b>Tax year</b>	2017
	<b>Notice date</b>	February 24, 2018
	<b>Social security number</b>	nnn-nn-nnnn
	<b>Page 6 of 7</b>	

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**Interest charges** We are required by law to charge interest on unpaid tax from the date the tax return was due to the due date the tax is paid in full. The interest is charged as long as there is an unpaid amount due, including penalties, if applicable. (Internal Revenue Code section 6601)

Description	Amount
<b>Total interest</b>	<b>\$21.73</b>

The table below shows the rates used to calculate the interest on your unpaid amount due. For a detailed calculation of your interest, call 1-800-829-8374.

Period	Interest rate
Beginning October 1, 2017	3%

We multiply your unpaid tax, penalties, and interest (the amount due) by the interest rate factor to determine the interest due.

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**Additional interest charges** If the amount you owe is \$100,000 or more, please make sure that we receive your payment within 10 work days from the date of your notice. If the amount you owe is less than \$100,000, please make sure that we receive your payment within 21 calendar days from the date of your notice. If we don't receive full payment within these time frames, the law requires us to charge interest until you pay the full amount you owe.

**Notice** CP11  
**Tax year** 2017  
**Notice date** February 24, 2018  
**Social security number** nnn-nn-xxxx  
**Page 7 of 7**

**Additional information**

Information about taxpayer rights is included, but it is relegated to the last page of the notice. This shows the importance the IRS places on taxpayer rights. Collection is on the first page, while rights are on the last.

- Visit [www.irs.gov/cp11](http://www.irs.gov/cp11)
- You may find the following publications helpful:
  - Publication 1, Your Rights as a Taxpayer
  - Publication 594, The Collection Process
- For tax forms, instructions, and publications, visit [www.irs.gov/formspubs](http://www.irs.gov/formspubs) or call 1-800-TAX-FORM (1-800-829-3676).
- Did you e-file your tax return? Electronically filed returns are less likely to have math errors resulting in notices such as this one. It's free to file your taxes electronically. Go to [www.irs.gov/efile](http://www.irs.gov/efile) for information and instructions.
- Paying online is convenient, secure, and ensures timely receipt of your payment. To pay your taxes online or for more information, go to [www.irs.gov/payments](http://www.irs.gov/payments).
- You can contact us by mail at the address at the top of the first page of this notice. Be sure to include your social security number and the tax year and form number you are writing about.
- Keep this notice for your records..

The IRS should be commended for including information about TAS and LITCs that can assist taxpayers with understanding the math error notice and their rights. However, this is on page 7. Taxpayers may learn of their right to appeal earlier in the notice, but dismiss it as too costly before reading this information.

The Taxpayer Advocate Service (TAS) is an independent organization within the IRS that can help protect taxpayer rights. TAS can offer you help if your tax problem is causing a hardship, or you've tried but haven't been able to resolve your problem with the IRS. If you qualify for TAS assistance, which is always free, TAS will do everything possible to help you. Visit [www.taxpayeradvocate.irs.gov](http://www.taxpayeradvocate.irs.gov) or call 1-877-777-4778.

Assistance can be obtained from individuals and organizations that are independent from the IRS. The Directory of Federal Tax Return Preparers with credentials recognized by the IRS can be found at <http://irs.treasury.gov/rpo/rpo.jsf>. IRS Publication 4134 provides a listing of Low Income Taxpayer Clinics (LITCs) and is available at [www.irs.gov](http://www.irs.gov). Also, see the LITC page at [www.taxpayeradvocate.irs.gov/litcmap](http://www.taxpayeradvocate.irs.gov/litcmap). Assistance may also be available from a referral system operated by a state bar association, a state or local society of accountants or enrolled agents or another nonprofit tax professional organization. The decision to obtain assistance from any of these individuals and organizations will not result in the IRS giving preferential treatment in the handling of the issue, dispute or problem. You don't need to seek assistance to contact us. We will be pleased to deal with you directly and help you resolve your situation.

We're required to send a copy of this notice to both you and your spouse. Each copy contains the information you are authorized to receive. Please note: Only pay the amount due once.

- If you need assistance, please don't hesitate to contact us.

The new draft 2018 CP11 addresses some past TAS recommendations, such as including the exact tax return line where the math error occurred.<sup>35</sup> It also contains a portion on the taxpayer's rights, and reference to TAS and Low Income Taxpayer Clinics (LITC), including that they could assist the taxpayer, though this is buried on page seven of the notice.

Notwithstanding these somewhat positive changes, there are still several areas that could be improved to ensure clarity. For example, while the notice does include language advising that a taxpayer must contact the IRS to protest the change made within 60 days to retain the right to appeal pre-tax (which the 2017 CP11, currently in use, does not have), it does not include the date of the deadline itself. Including the date of the deadline would ensure that taxpayers are not confused about the date by which they must file to retain their appeal rights. Added clarity with a listed deadline date may be especially beneficial considering that the taxpayers in question may have made mathematical or clerical errors on their tax forms, so adding 60 days to the notice date may lead them to calculate an inaccurate filing date. This language should be on the first page to ensure taxpayers read it.

Another improvement that the IRS should make is with the placement of the proposed errors on the notice. The 2017 CP11 is five pages long and the 2018 CP11 is seven pages long, and neither discuss the specifics of the actual error committed by the taxpayer until the third and fourth page, respectively. Payment options are displayed before an explanation of the math error and the return line the error was committed on, emphasizing payment over the specifics of the proposed error. As discussed below, the way the forms are presented, and choices are displayed, impacts how taxpayers view and interpret the forms, potentially steering them away from exercising their rights to challenge the IRS's decision.<sup>36</sup>

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**The way the forms are presented, and choices are displayed, impacts how taxpayers view and interpret the forms, potentially steering them away from exercising their rights to challenge the IRS's decision .... The structure of these notices actively discourages abatement requests and places obstacles into taxpayers' efforts to learn about and use their rights.**

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Further, with respect to the 2018 CP11, the taxpayer's appeal rights or deadlines are not mentioned on the first page, which is designed like a bill, prioritizing the amount owed and payment due date. The *right to challenge the IRS's position and be heard*, by requesting deficiency procedures, is de-emphasized. On the second page, the "what you need to do immediately" section is continued, in smaller and non-bold font, different than how it is on the first page. This, along with its placement on the second page, de-emphasizes the appeal rights section of the form, which contains a wall of text that taxpayers may merely scan over. The "what you need to do immediately—continued" heading should be similarly as big and bold as it is on the first page, and the appeal information should be broken down into more

35 See, e.g., National Taxpayer Advocate 2011 Annual Report to Congress 74-92 (Most Serious Problem: *Expansion of Math Error Authority and Lack of Notice Clarity Create Unnecessary Burden and Jeopardize Taxpayer Rights*).

36 See, e.g., IRS, *Behavioral Insights Toolkit 21* (2017) (discussing "choice architecture," how the way choices are structured can influence a taxpayer's decision making); see Literature Review: *Improving Notices Using Psychological, Cognitive, and Behavioral Science Insights*, *infra*.

manageable segments<sup>37</sup> to ensure that taxpayers are drawn to the information about their appeal rights and read through it, ideally on the first page itself.

The explanation of the math error the taxpayer committed is on the fourth page, so, though they are informed of their appeal rights in the 2018 CP11, taxpayers don't know what to protest until page four of the notice. Taxpayers are not informed that they have rights or that they could qualify for free assistance until page seven of the notice. Few taxpayers are likely to read through these text-heavy seven pages to reach this important information. The structure of these notices actively discourages abatement requests and places obstacles into taxpayers' efforts to learn about and use their rights.

Compared to the 2017 CP11, the 2018 CP11 is better. However, the CP11 could still be further improved, as discussed below. If taxpayers do not understand that they can challenge the IRS's change to their return (and must do so within 60 days) because a notice is unclear, they may pay more tax than they owe. Unclear notices may also prevent taxpayers from understanding that they will lose the right to prepayment judicial review in Tax Court, before paying the assessment, if they don't respond to the math error notice by the 60-day deadline. Math error notices are not collection notices, they are notices to inform taxpayers that the IRS has made some adjustments to their tax return and assessed a tax against them. These notices must inform taxpayers that they have the right to dispute the assessed tax within 60 days, which will give them an opportunity to petition the Tax Court. They must also inform taxpayers that there are resources available to help them, namely TAS and LITCs. All this important information should be on the first page of the notice. Also on the first page, the IRS can include language that, if the taxpayer agrees with the change, information on how to pay is available on the next page of the notice. This informs taxpayers of their rights and deadlines and directs them through the necessary steps of the math error process.

In its response to the National Taxpayer Advocate's 2014 Math Error Notice Most Serious Problem recommendations, the IRS decided to not take action recommended by the National Taxpayer Advocate to organize a team, which would include TAS, to review all current explanations of math error adjustments, and rewrite, where necessary, to ensure that the congressional directive for clarity is met.<sup>38</sup> The IRS instead cited its own process to create and revise taxpayer correspondence as sufficient. The IRS did take action on creating IRM guidelines for crafting math error explanations that do not have an applicable TPNC (non-standard notices).<sup>39</sup> The IRS postponed action on updating math error notices to clearly disclose that taxpayers may request abatement without providing an explanation or substantiating documentation until "resources will allow."<sup>40</sup>

The IRS has not conducted any studies to explore math error notice clarity in the past five years.<sup>41</sup> TAS requested that the IRS measure the abatement rates for math error assessments by notice number or TPNC in 2011.<sup>42</sup> The IRS has not developed a system to measure math error reversal rates for math

37 See Literature Review: *Improving Notices Using Psychological, Cognitive, and Behavioral Science Insights* (discussing the psychological concept of "chunking," that the human brain can only consciously retain roughly four chunks of different information at one time), *infra*.

38 National Taxpayer Advocate Fiscal Year (FY) 2016 Objectives Report to Congress vol. 2 58-60 (IRS and TAS Responses: Most Serious Problem: *Math Error Notices: The IRS Does Not Clearly Explain Math Error Adjustments, Making it Difficult for Taxpayers to Understand and Exercise Their Rights*).

39 *Id.*

40 *Id.*

41 IRS response to TAS information request (Aug. 22, 2018).

42 See National Taxpayer Advocate 2011 Annual Report to Congress 74-92 (Most Serious Problem: *Expansion of Math Error Authority and Lack of Notice Clarity Create Unnecessary Burden and Jeopardize Taxpayer Rights*).

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The IRS has not developed a system to measure math error reversal rates for math error assessments by notice number or Taxpayer Notice Code (TPNC), which limits the ability of the IRS or TAS to analyze if there are problems with over-selection or clarity of particular math error notices.

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error assessments by notice number or TPNC,<sup>43</sup> which limits the ability of the IRS or TAS to analyze if there are problems with over-selection or clarity of particular math error notices.

### **The IRS's Failure to Use Historical Data to Correct Taxpayer Returns Unnecessarily Burdens Taxpayers and Wastes IRS Resources**

The IRS places the burden on taxpayers for errors that the IRS could solve using internal data, instead of denying credits that taxpayers actually qualify for and using valuable IRS time and resources answering responses to math error notices that the IRS should not have sent.<sup>44</sup> For example, TAS found, in its 2011 study on math error authority and dependent TINs, that 55 percent of these types of errors were abated, and 56 percent of the abatements could have been identified by the IRS with internal data.<sup>45</sup> Additionally, a TAS study found that, in a sample of cases where taxpayers had a missing or incorrect dependent TIN math error and received no refund, 41 percent of the cases that received no adjustment could have been corrected, and all the refunds allowed, by the IRS examining its own records.<sup>46</sup> Another 11 percent of these cases could have been at least partially corrected by historical data.<sup>47</sup> This translates to more than 40,000 taxpayers who may have not received refunds that they were entitled to.<sup>48</sup> These taxpayers lost an average of \$1,274.<sup>49</sup>

There is no legal prohibition against the IRS using historical data and making these types of corrections without burdening taxpayers with math error notices.<sup>50</sup> In fact, the IRS directs employees to perform research and make changes to perfect a taxpayer's return before contacting the taxpayer for additional information.<sup>51</sup> The IRS could similarly direct its employees to search historical return information and make those changes that benefit taxpayers, such as correcting a dependent TIN to allow for a refund. The IRS should also measure abatement rates and review them to identify and correct potential math error problems like those it has had before.

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43 IRS response to TAS information request (Aug. 22, 2018).

44 National Taxpayer Advocate 2011 Annual Report to Congress vol. 2 114-144 (Research Study: *Math Errors Committed on Individual Tax Returns: A Review of Math Errors Issued for Claimed Dependents*).

45 *Id.* at 117.

46 *Id.* at 120.

47 *Id.*

48 *Id.*

49 *Id.*

50 Email from Division Counsel/Associate Chief Counsel (NTA Program) (Nov. 14, 2018) (on file with TAS).

51 See, e.g., IRM 3.12.3.4.3.3 (Jan. 1, 2019) (this IRM section instructs IRS employees to search the taxpayer's return and attachments, as well as perform Integrated Data Retrieval System (IDRS) research, to correct missing or incorrect TINs before contacting the taxpayer for additional information).

The IRS has stated that it reviews TPNC descriptive paragraphs annually.<sup>52</sup> However, in reviewing the top ten most frequent math error notices TPNC descriptive paragraphs from CYs 2015-2017, there were no discernible changes in language.<sup>53</sup> As demonstrated by Example 1, these descriptive paragraphs remain confusing, using language that does not always clearly direct the taxpayer to the problem with their return.

### New Laws and Research-Based TAS-Designed Notices Can Guide the IRS In Making Clearer Notices

Executive Order 13707 and associated guidance recognized that behavioral science insights could benefit the American people and provided instructions to federal agencies how to use and implement the available behavioral science research.<sup>54</sup> Recently introduced legislation in the House of Representatives would require federal agencies to provide greater notice clarity.<sup>55</sup> The legislation would require notices that agencies send to individuals to contain:

- (1) the action item;
- (2) information on whether a response is required, optional, or not required;
- (3) the deadline, if applicable;
- (4) how to complete the action item; and
- (5) the agency's contact information.<sup>56</sup>

All the above items would need to be in a clearly marked section at the top of the first page of the notice.<sup>57</sup> The 2018 CP11, although an improvement over past IRS math error notices, would be inadequate under this legislation because the required items are spread over multiple pages, and the exact date of the deadline to retain appeal rights is not included.

TAS is currently working on new notice designs that would enhance clarity and taxpayer rights. The language of IRS notices should be framed in the language of the Taxpayer Bill of Rights. For example, a sample notice could read:

You have the right to challenge the IRS and be heard. So, if you disagree with the adjustment we've made to your return, you must call or write us and ask us to reverse the change to your return. This is a request to abate the tax and you must do so within 60 days of the date of this notice, by [last day to request abatement]. If you do this, we will then contact you for more information, and if we still believe your tax return is incorrect, we will

52 IRS response to TAS information request (Aug. 22, 2018) ("annually, the Business Operating Division's (BOD) Subject Matter Experts (SME) review existing TPNCs. The SMEs submit requests to the Office of Taxpayer Correspondence (OTC) to revise existing TPNCs or develop new TPNCs, as appropriate. The OTC works with the SMEs to develop language that is compliant with the Plain Language Act, IRS Style Guide, and the Gregg Reference Manual." The OTC then secures business approval for technical accuracy, obtains approval from Counsel for statutory compliance, and sends to TAS for review and feedback); IRS response to TAS fact check (Nov. 26, 2018) ("Each year, the IRS makes numerous changes to the verbiage of existing TPNCs, deletes obsolete TPNCs, and creates new TPNCs.").

53 IRS response to TAS information request (Aug. 22, 2018).

54 Exec. Order No. 13707, 3 C.F.R. § 13707 (Sept. 15, 2015); Executive Office of the President, Memorandum from John P. Holdren, Director, Office of Science and Technology Policy, to the Heads of Executive Departments and Agencies, *Implementation Guidance for Executive Order 13707: Using Behavioral Science Insights to Better Serve the American People* (Sept. 15, 2016).

55 Too Long Didn't Read Act of 2018, H.R. 5321, 115th Cong. (2018).

56 *Id.*

57 *Id.*

keep the change we made. If you disagree with our decision, you will have the chance to challenge our decision by petitioning the United States Tax Court without having to pay the tax first.

TAS is working on suggested updated notices that take current research on how humans best perceive and understand writing and using those principles to design new notices based on researched best practices.<sup>58</sup> One such practice is the concept of framing, a behavioral science concept that, by framing information in a particular way, can influence how people respond to it.<sup>59</sup>

The framing in the IRS math error notices appears to be framing them like a bill, with the amount owed and payment information featured first and prominently. However, framing a notice in the context of taxpayer rights could be beneficial to taxpayers to help them understand their rights and what they can and must do in response to a notice; for a math error notice, either paying what they owe or petitioning the change to their return.

Another concept is the idea that making things even incrementally more difficult will reduce action. For example, in a study on Medicare notices, researchers found that simply making information available (through a web link or telephone number) was much less successful than actually including the information itself on the notice.<sup>60</sup> This means that the IRS should strive to create fewer steps and make each process easier for taxpayers to increase their likelihood to engage and understand. One way the IRS could do this with regards to notices is to include an abatement form within the notice package, so that if a taxpayer would like to request abatement, they do not need to go through as many steps, such as calling the IRS, but can instead simply fill out a mostly pre-populated form and return it. The IRS should work with TAS and follow its researched suggestions to improve notice clarity and prevent the infringement of taxpayer rights.

## CONCLUSION

Math error authority has its place as an effective tool to correct unambiguous errors. While the IRS has improved some explanations on some math error notices, these revisions remain short of providing clear, concise, and visually prominent information for taxpayers to determine what, specifically, the IRS corrected on their return and whether they should accept the adjustment or request a correction, as well as the consequences of inaction. Most importantly, the notices do not clearly frame the steps to be taken in the language of taxpayer rights—specifically, *the right to challenge the IRS and be heard*, and *the right to appeal to an independent forum*. Framing notices in the context of a taxpayer's rights may make taxpayers pay more attention to the notices. Moreover, the IRS does not measure the reversal rates of math error assessments and, as a result, cannot determine the extent to which it is issuing accurate assessments and forgoes valuable data that could be used both in identifying which math error notices should be revised for added clarity and in using historical data to eliminate the need for issuing math error notices that are later abated.

58 See Literature Review: *Improving Notices Using Psychological, Cognitive, and Behavioral Science Insights*, *infra*; see also IRS, *Behavioral Insights Toolkit* (2017).

59 Deloitte Consulting LLP, *Using the Nudge in Tax Compliance: Leveraging Behavioral Insights to Boost Tax Revenue* 9 (2017); see also Literature Review: *Improving Notices Using Psychological, Cognitive, and Behavioral Science Insights*, *infra*.

60 Jeffrey R. Kling et. al., *Comparison Friction: Experimental Evidence from Medicare Drug Plans*, 127 Q. J. Econ. 199, 200-201 (2012); see also Literature Review: *Improving Notices Using Psychological, Cognitive, and Behavioral Science Insights*, *infra*.

## RECOMMENDATIONS

The National Taxpayer recommends that the IRS:

1. Measure the abatement rates of its math errors and use the data to assess which math errors are most problematic and which notices need to be revised for clarity.
2. On all math error notices, cite to the actual line on the return that the IRS is changing, and the reason why the IRS is making the change (*e.g.*, “you claimed 6 dependents on line x, but multiplied the dependency exemption by 7 on line y”).
3. Emphasize the Taxpayer Bill of Rights, and specific taxpayer rights on math error notices by including the taxpayer’s *right to challenge the IRS and be heard*, and the *right to appeal*, the specific deadline date the taxpayer must respond by, and the loss of their right to make a prepayment petition of the IRS’s change to their return to the Tax Court, if the taxpayer does not respond by the date in the notice.
4. Further emphasize the steps that taxpayers may take (pay or file to petition) on the first page of its math error notices, so that taxpayers are clear on what their options are in response to notices. The section heading that discusses appeal options should be similarly as big and bold as the section heading discussing payment.
5. Place the explanation of the math error on the first page of the notice, not the third or fourth, so that taxpayers see and read the explanation before they read about the numerous payment options, which nudges them to pay and not question the purported error or if they should appeal. Page one should also include the deadline date to appeal, and what taxpayers lose if they do not appeal, as well as information about the TBOR, TAS, and LITCs.
6. Work directly with TAS on notice redesign to ensure notice clarity and adequate inclusion of taxpayer rights on math error notices.
7. Use internal data to make corrections to returns that benefit taxpayers, instead of burdening taxpayers with unnecessary math error assessments that are later abated.

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## STATUTORY NOTICES OF DEFICIENCY: The IRS Fails to Clearly Convey Critical Information in Statutory Notices of Deficiency, Making it Difficult for Taxpayers to Understand and Exercise Their Rights, Thereby Diminishing Customer Service Quality, Eroding Voluntary Compliance, and Impeding Case Resolution

### RESPONSIBLE OFFICIALS

Ken Corbin, Commissioner, Wage and Investment Division  
 Mary Beth Murphy, Commissioner, Small Business/Self-Employed Division  
 Douglas O'Donnell, Commissioner, Large Business and International Division  
 David Horton, Acting Commissioner, Tax Exempt and Government Entities Division  
 Donna Hansberry, Chief, Office of Appeals

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to a Fair and Just Tax System*

### DEFINITION OF PROBLEM

The statutory notice of deficiency (SNOD) notifies the taxpayer that there is a proposed additional tax due, identifying the type of tax, and period involved, and that the taxpayer has the right to bring suit in the United States Tax Court before assessment and payment.<sup>2</sup> The taxpayer has 90 days (or 150 days if the taxpayer resides outside the United States) to petition the U.S. Tax Court.<sup>3</sup> If the taxpayer does not petition the Tax Court, after the 90 (or 150) days expire, the IRS will assess the tax, send the taxpayer a tax bill, and start collections.<sup>4</sup> The notice of deficiency is the taxpayer's "ticket" to the Tax Court, the only pre-payment judicial forum where the taxpayer can *appeal an IRS decision*. The SNOD is critical to many low income and middle income taxpayers because generally without it they would be required to pay the tax first and go to refund fora, such as federal district courts or the United States Court of Federal Claims, in order to challenge the tax adjustment in an independent judicial forum. The notice also provides due process, as part of procedural justice, to taxpayers, especially those who cannot afford representation.<sup>5</sup> Approximately 69 percent of cases in Tax Court are brought by unrepresented

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified at Internal Revenue Code (IRC) § 7803(a)(3).

2 IRC §§ 6212(a), 6213(a); Internal Revenue Manual (IRM) 4.8.9.8, *Preparing Notices of Deficiency* (July 9, 2013).

3 IRC § 6213(a).

4 IRC § 6212(a); IRM 4.8.9.8, *Preparing Notices of Deficiency* (July 9, 2013).

5 See Most Serious Problem: *Pre-trial Settlements in the U.S. Tax Court: Insufficient Access to Available Pro Bono Assistance Resources Impedes Unrepresented Taxpayers from Reaching a Pre-trial Settlement and Achieving a Favorable Outcome*, *infra*.

taxpayers, and that percentage increases to 91 percent among cases where the deficiency for a tax year is \$50,000 or less and the taxpayer elects small tax case (S Case) procedures.<sup>6</sup>

In fiscal year (FY) 2017, the IRS issued more than 2.7 million of the four types of SNODs that are separately tracked (called the “3219 SNODs”), as shown on Figure 1.13.1.<sup>7</sup> There were only about 27,000 docketed cases in Tax Court that year, however, suggesting that less than one percent of taxpayers who received a SNOD filed a petition with the Tax Court.<sup>8</sup> The IRS tracks the income level of taxpayers receiving three of the 3219 SNODs, excluding the SNODs issued to those who did not file a return.<sup>9</sup> The majority of these three types of 3219 SNODs (called Non-Automated Substitute for Return or Non-ASFR SNODs) were issued to low income taxpayers. Nearly 59 percent of those receiving a Non-ASFR SNOD make less than \$50,000 per year.<sup>10</sup> Yet low income taxpayers, who may be eligible for representation through Low Income Taxpayer Clinics (LITCs), are less likely to petition the Tax Court.<sup>11</sup> In FY 2018, the median total positive income (TPI) for individuals who did not petition the Tax Court in response to a SNOD issued after an audit was about \$24,000.<sup>12</sup>

The National Taxpayer Advocate is concerned that the lack of taxpayers’ responses to SNODs may be, in part, due to faulty design and poor presentation of information in the notices, making it difficult for taxpayers to understand critical information and exercise their rights. We have identified the following issues pertaining to IRS SNODs:

- SNODs do not alert taxpayers of their rights and the consequences for not exercising them;
- SNODs do not sufficiently apply plain writing principles, nor incorporate behavioral research insights, as directed by the Plain Writing Act and Executive Order 13707; and
- The IRS continues to omit Local Taxpayer Advocate (LTA) information required by law on certain SNODs, thereby violating taxpayer rights.

6 American Bar Association (ABA), Section of Taxation, *Comment Letter on the Tax Court Rules of Practice and Procedure Relating to the Appearance and Representation before the Court 2* (Oct. 3, 2018), <https://www.americanbar.org/content/dam/aba/administrative/taxation/policy/100318comments.pdf>. The small tax case criteria are provided in IRC § 7463.

7 Although there are many versions of the Statutory Notice of Deficiency (SNOD), the four types being referenced are: CP 3219A, LTR 3219, LTR 3219C, and LTR 3219N, as discussed below.

8 IRS Office of Chief Counsel, ABA Report, Tax Section, Court Procedure Committee 12 (Sept. 30, 2017) (providing the sources of cases petitioned to the Tax Court for fiscal year (FY) 2017) (on file). Some of the SNODs issued in FY 2017 would not have resulted in docketed cases before FY 2018. In addition, some cases docketed in FY 2017 could have resulted from SNODs issued in an earlier year.

9 We can also determine the income of other taxpayers who received a SNOD after an audit—even if we do not know which type of SNOD they received — because these cases are tracked on the Compliance Data Warehouse (CDW) Audit Information Management System (AIMS) Closed Case Database, and we can obtain the taxpayer’s income from the Individual Returns Transaction File (IRTF) F1040 table.

10 CDW Notice Delivery System (NDS) Notice Table (Dec. 11, 2018); IRTF Form 1040 Table (Dec. 11, 2018). Due to the lapse in appropriations, the IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

11 See Most Serious Problem: *Pre-trial Settlements in the U.S. Tax Court: Insufficient Access to Available Pro Bono Assistance Resources Impedes Unrepresented Taxpayers from Reaching a Pre-trial Settlement and Achieving a Favorable Outcome*, *infra*. In order to qualify for assistance from an Low Income Tax Clinic (LITC), generally a taxpayer’s income must be below 250 percent of the current year’s federal poverty guidelines, based on family size and with income adjustments for Hawaii and Alaska. IRC § 7526(b)(1)(b)(ii). As of January 2018, 250 percent of the federal poverty level was \$51,950 for a family of three. See IRS Pub. 3319, *Low Income Taxpayer Clinics (LITC) Grant Application Package and Guidelines* 45-46 (May 2018).

12 CDW AIMS Closed Case Database (Dec. 11, 2018); IRTF F1040 table (Dec. 11, 2018). In computing this income level, TAS excluded accounts for which the IRS had no record of the taxpayer’s income in any of the prior three tax years. The IRS had such records for more than 90 percent of these accounts. Total positive income (TPI) is the taxpayer’s income from all sources before adjusting for deductions and exemptions. Due to the lapse in appropriations, the IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

## ANALYSIS OF PROBLEM

### Background

Generally, taxpayers self-assess taxes when filing their income tax returns. However, the IRS may determine that a taxpayer owes additional tax and may request additional information or select the taxpayer's return for an audit.<sup>13</sup> If the taxpayer and the IRS cannot agree on the alleged tax liability in connection with an audit, document matching (*e.g.*, after issuance of a CP 2000), or appeals process, the IRS will issue a notice of deficiency.<sup>14</sup> When the IRS issues a SNOD, the taxpayer has 90 days to file a petition in Tax Court.<sup>15</sup> No assessment of any tax or collection through levy or proceeding in court may begin until after the notice has been mailed and this 90-day period has expired.<sup>16</sup> When a taxpayer timely files a petition with the Tax Court, no assessment or collection is allowed until the Tax Court enters a final decision.<sup>17</sup>

If the taxpayer files a petition with the Tax Court, the Tax Court provides support and special procedures for unrepresented taxpayers. In accordance with IRC § 7463, the Tax Court offers simplified and expedited procedures for tax disputes involving amounts of \$50,000 or less. For example, if a taxpayer elects small tax case status, and the case goes to trial, under Rule 174 of the Tax Court Rules and Procedure, the trial will be conducted as “informally as possible consistent with orderly procedure”<sup>18</sup> and “any evidence deemed by the Court to have probative value shall be admissible.”<sup>19</sup> Neither briefs nor oral arguments will be required unless the court otherwise directs.<sup>20</sup>

The tax assessment is an important administrative act because it sets the stage for the IRS to start collecting unpaid tax balances using methods such as seizure and levy of a taxpayer's property.<sup>21</sup> The Supreme Court explained the significance of the assessment in *Bull v. United States*: “The assessment is given the force of a judgment, and if the amount assessed is not paid when due, administrative officials may seize the debtor's property to satisfy the debt.”<sup>22</sup> If, after the IRS issues a series of notices and the taxpayer does not dispute the IRS collection actions by requesting a hearing or paying the tax, the IRS may file a lien or levy the taxpayer's property, including the taxpayer's bank accounts or wages.<sup>23</sup>

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13 See IRC 7602(a); see also IRS Publication 556, *Examination of Returns, Appeal Rights, and Claims for Refunds* (Rev. Sept. 2013).

14 IRM 11.4.2.7.4, *CP 2000* (Oct. 5, 2006). The CP 2000 notice is issued to taxpayers proposing an adjustment to their tax account based on disparities found between the taxpayers return and information returns.

15 IRC §§ 6212, 6213. If the notice is addressed to a person outside the United States, the taxpayer has 150 days to file a petition in the Tax Court.

16 See IRC § 6213(a). However, if collection of an unassessed liability is in jeopardy, the IRS may make an immediate assessment and pursue collection without the need to follow normal assessment and collection procedures. As soon as a “jeopardy assessment” is made, the tax, penalties, and interest become due and payable. IRC §§ 6851, 6861. See also IRC §§ 6201-6207, 6303(a). If no petition is filed with the Tax Court, upon the expiration of the 90-day period, the IRS will assess the tax liability. Within 60 days of making the assessment, the IRS must provide the taxpayer notice of the assessment and demand for payment.

17 See IRC §§ 6213(a), 7481.

18 Rule 174(b), Tax Court Rules and Procedure.

19 *Id.*

20 Rule 174(c), Tax Court Rules and Procedure.

21 IRC §§ 6320, 6330.

22 *Bull v. United States*, 295 U.S. 247, 259-260 (1935). See also IRC § 6321.

23 The IRS must issue a Notice of Federal Tax Lien after filing a federal tax lien and provide taxpayers with the right to a hearing under IRC § 6320. The IRS must also give notice to the taxpayer before issuing a levy under IRC § 6330. See also IRC § 6331.

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The notice of deficiency is the taxpayer’s “ticket” to the Tax Court, the only pre-payment judicial forum where the taxpayer can *appeal an IRS decision*.

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Thus, it is critical that taxpayers dispute the tax before the 90 days expires if they disagree with the IRS’s proposed assessment. Otherwise, once the tax is assessed, the IRS will start collecting the liability. In most cases, for taxpayers to challenge the tax in an independent judicial forum, they must pay the tax and then request a refund.<sup>24</sup> This option is costly and unfeasible for some taxpayers.

As noted above, available data suggest that less than one percent of the taxpayers, who receive one of the four types of SNODs separately, file a petition with the Tax Court. Other taxpayers are not availing themselves of a fundamental taxpayer right—the *right to appeal an IRS decision in an independent forum*. They may not be availing themselves of their rights because the SNODs do not effectively communicate the information needed for taxpayers to understand their rights, the relevant tax issues, nor how to respond.

The most commonly issued SNODs are the 3219 SNODs.<sup>25</sup> The 3219 SNODs include:

- CP 3219A, *Automated Underreporter* (The IRS issues CP 3219A when the taxpayer’s return information does not match third-party information sent to the IRS.);
- LTR 3219, *Correspondence Exam* (The LTR 3219, which is mailed from the IRS Service Center, is issued after a correspondence exam where there is no agreement between the IRS and the taxpayer.);
- LTR 3219C, *Automated Questionable Credit* (The LTR 3219C is issued to taxpayers who may have false wages or withholding, or who are being denied refundable credits.);<sup>26</sup> and
- LTR 3219N, *Automated Substitute for Return (ASFR)* (The LTR 3219N is issued to assess tax against those who have unfiled returns.).<sup>27</sup>

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24 In order to bring a refund suit, the taxpayer must first file a claim for refund with the IRS and, upon its denial by the IRS or the IRS’s failure to act within six months, the taxpayer must then file a suit for refund in the district courts or the U.S. Court of Federal Claims. See IRC § 7422. In certain cases, audit reconsideration is available to eligible taxpayers who have a tax balance and can provide new documents to the examination division. IRM 4.13.1.2, *Definition of an Audit Reconsideration* (Dec. 16, 2015). Under IRC § 6330 (c)(2)(b), taxpayers may challenge a tax liability at a collection due process hearing. Specifically, the taxpayer may also raise at the hearing challenges to the existence or amount of the underlying tax liability for any tax period if the taxpayer did not receive a statutory notice of deficiency for the tax liability or did not otherwise have an opportunity to dispute the tax liability (e.g., if the SNOD was not sent to the last known address). See also Most Serious Problem: *Collection Due Process Notices: Despite Recent Changes to Collection Due Process Notices, Taxpayers Are Still at Risk for Not Understanding Important Procedures and Deadlines, Thereby Missing Their Right to an Independent Hearing and Tax Court Review*, *infra*. For a proposal that would allow taxpayers to file suit in a United States District Court or in the United States Court of Federal Claims without first paying an assessment in full, see Legislative Recommendation: *Fix the Flora Rule: Give Taxpayers Who Cannot Pay the Same Access to Judicial Review as Those Who Can*, *infra*.

25 IRS response to TAS information request (Dec. 12, 2018).

26 IRM 25.25.7.4, *Taxpayer Responses* (Aug. 23, 2018).

27 IRM 3.10.72-2, *Correspondence C Letters – Routing Guide* (Jan. 1, 2018); Exhibit IRM. 3.10.72-3, *Computer Paragraph (CP) Notices – Routing Guide* (Jan. 1, 2018).

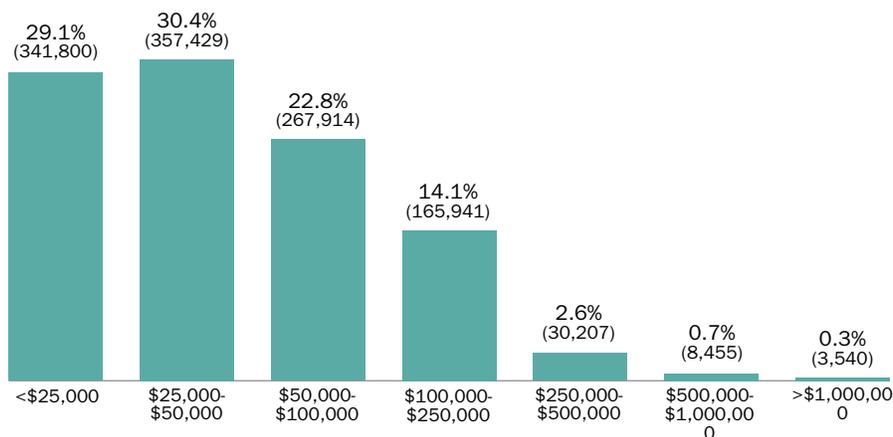
**FIGURE 1.13.1, Number of 3219 SNODs Mailed Over Past Five Years<sup>28</sup>**

	FY 2013	FY 2014	FY 2015	FY 2016	FY 2017
CP 3219A	1,898,982	2,697,153	2,580,817	2,151,790	2,208,720
LTR 3219	1,664,838	523,635	617,170	463,748	463,067
LTR 3219C	31,156	38,891	37,791	34,562	15,186
LTR 3219N	149,901	175,183	192,481	13,570	32,204
<b>Total</b>	<b>3,744,877</b>	<b>3,434,862</b>	<b>3,428,259</b>	<b>2,663,670</b>	<b>2,719,177</b>

As shown in Figure 1.13.2, about 59 percent of all those receiving Non-ASFR SNODs make less than \$50,000 per year, while only 41 percent have incomes between \$50,000 and one million dollars per year. Clearly, the majority are issued to low income taxpayers.

**FIGURE 1.13.2<sup>29</sup>**

**Distribution of Taxpayers with Non-ASFR SNODs by Total Positive Income (TPI) in TY 2017**



The income distribution of taxpayers petitioning or not petitioning the Tax Court after an audit in response to a SNOD also indicates that lower income taxpayers are less likely to petition the Tax Court. The median TPI for those individuals who did *not* petition the Tax Court was nearly \$24,000,<sup>30</sup> whereas, the median TPI for those who *did* petition the Tax Court during that same period was slightly over \$72,000.<sup>31</sup> A more detailed breakdown of these income distributions as reflected on Figures 1.13.3 and 1.13.4, show the same thing.

28 IRS response to TAS information request (Dec. 12, 2018).

29 CDW Notice Delivery System NDS Notice table (Dec. 11, 2018); CDW AIMS Closed Case Database (Dec. 11, 2018); IRTF F1040 table (Dec. 11, 2018). These figures are based on the total number of CP 3219A, LTR 3219, and LTR 3219C. They do not include the LTR 3219N, which is issued in the Automated Substitute for Return (ASFR) Program. Due to the lapse in appropriations, the IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

30 CDW AIMS Closed Case Database and FY 2018 IRTF F1040 table. Due to the lapse in appropriations, the IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

31 *Id.*

**FIGURE 1.13.3, Distribution of Taxpayers Petitioning the Tax Court After an Audit in Response to SNODs in FY 2018<sup>32</sup>**

FY 2018	Percentage
Total Positive Income < \$25k	20.5%
Total Positive Income ≥ \$25k and < \$50k	16.3%
Total Positive Income ≥ \$50k and < \$100k	25.1%
Total Positive Income ≥ \$100k and < \$250k	25.7%
Total Positive Income ≥ \$250k and < \$500k	5.8%
Total Positive Income ≥ \$500k and < \$1M	3.0%
Total Positive Income ≥ \$1M	3.5%
<b>Total</b>	<b>100.0%</b>

Figure 1.13.3 shows that most, or 63 percent, of individual taxpayers who filed petitions in FY 2018 after an audit in response to a SNOD, had incomes *of at least* \$50,000. In contrast, only a minority or 37 percent had incomes *below* \$50,000.

**FIGURE 1.13.4, Distribution of Taxpayers Not Petitioning the Tax Court After an Audit in Response to SNODs in FY 2018<sup>33</sup>**

FY 2018	Percentage
Total Positive Income < \$25k	52.6%
Total Positive Income ≥ \$25k and < \$50k	22.4%
Total Positive Income ≥ \$50k and < \$100k	16.7%
Total Positive Income ≥ \$100k and < \$250k	7.3%
Total Positive Income ≥ \$250k and < \$500k	0.7%
Total Positive Income ≥ \$500k and < \$1M	0.2%
Total Positive Income ≥ \$1M	0.1%
<b>Total</b>	<b>100.0%</b>

Figure 1.13.4 shows that the majority, or 75 percent, of individual taxpayers who did not file petitions in FY 2018 after an audit in response to a SNOD, had TPI of less than \$50,000. These taxpayers may not realize they may be eligible for free representation at the Tax Court by LITCs.<sup>34</sup> Alternatively, they may not understand the SNODs they have received from the IRS.

32 CDW AIMS Closed Case Database, Petitioned Cases, FY 2018 (Dec. 11, 2018). This figure shows the subset of petitions following an audit (and appeal, if any) and case closure. It does not include petitions following more automated procedures (e.g., AUR and ASFR). Due to the lapse in appropriations, the IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

33 *Id.* Due to the lapse in appropriations, the IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

34 See Most Serious Problem: *Pre-Trial Settlements in the U.S. Tax Court: Insufficient Access to Available Pro Bono Assistance Resources Impedes Unrepresented Taxpayers from Reaching a Pre-trial Settlement and Achieving a Favorable Outcome*, *infra*.

## SNODs Do Not Alert Taxpayers of Their Rights and the Consequences for Not Exercising Them

In 2008, the IRS embarked on a major initiative to improve the clarity, accuracy, and effectiveness of its taxpayer correspondence.<sup>35</sup> The Taxpayer Communications Task group (TACT), with the aid of Siegel+Gale (now Siegelvision), conducted a review of taxpayer correspondence. Siegel+Gale concluded that “the differences among many letters reflected internal IRS structure, as opposed to taxpayer needs.”<sup>36</sup> The IRS developed a new framework for IRS letters based on suggestions from both IRS employees and stakeholders. SNODs, however, continue to fail in conveying critical information necessary for taxpayers to understand their obligations and rights, and to take appropriate action.

We have selected the CP 3219A SNOD to examine because it comprises over 80 percent of the 3219 SNODs, as depicted in Figure 1.13.1.<sup>37</sup> The CP 3219A SNOD fails to adequately inform taxpayers of their rights and protections with regard to the IRS’s actions. Notably, while the IRS has a Spanish version of the notice, it does not have SNODs available in other major world languages.<sup>38</sup> Moreover, there is no mechanism whereby a taxpayer can *proactively* request a Spanish-language SNOD. Instead, he or she must contact the IRS upon receiving the English-language SNOD and request a Spanish-language one. This request does not toll the running of the 90-day period to petition the Tax Court.<sup>39</sup>

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- 35 See Siegel+Gale, *2A Report: Analysis of the IRS Correspondence System; Taxpayer Communications Taskgroup (TACT) Charter* (Nov. 2008).
- 36 Siegel+Gale, Case study, Internal Revenue Service, *Making Paperwork Less Taxing*, <https://www.siegelgale.com/wp-content/uploads/2011/05/Case-Study-IRS.pdf> (last visited Jan. 29, 2018). Accord Siegel+Gale, *2A Report: Analysis of the IRS Correspondence System; Taxpayer Communications Taskgroup (TACT) Charter* 8 (Nov. 2008) (noting “some notices do not clearly provide the taxpayers with the information needed to respond.”).
- 37 CDW Notice Delivery System NDS Notice table. See Exhibit IRM 3.10.72-3, *Computer Paragraph (CP) Notices – Routing Guide* (Jan. 1, 2018). As noted above, the CP 3219A, also known as an Automated Under Reporter (AUR) SNOD, is issued when the taxpayer’s return information does not match third party information sent to the IRS, such as wage and income information from employers and financial institutions. Due to the lapse in appropriations, the IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.
- 38 For further discussion on the National Taxpayer Advocate’s efforts to address the IRS’s lack of access to multilingual notices, see National Taxpayer Advocate 2011 Annual Report to Congress 137-150 (Most Serious Problem: *Foreign Taxpayers Face Challenges in Fulfilling U.S. Tax Obligations*). The National Taxpayer Advocate has long highlighted the lack of forms and publications for taxpayers with limited English proficiency. See, e.g., National Taxpayer Advocate 2017 Annual Report to Congress 181-194 (Most Serious Problem: *Individual Taxpayer Identification Numbers (ITINs): The IRS’s Failure to Understand and Effectively Communicate With the ITIN Population Imposes Unnecessary Burden and Hinders Compliance*); National Taxpayer Advocate 2011 Annual Report to Congress 273-283 (Most Serious Problem: *Introduction to Diversity Issues: The IRS Should Do More to Accommodate Changing Taxpayer Demographics*); National Taxpayer Advocate 2008 Annual Report to Congress 141-157 (Most Serious Problem: *Access to the IRS by Individual Taxpayers Located Outside the United States*); and National Taxpayer Advocate 2006 Annual Report to Congress 222-247 (Most Serious Problem: *Correspondence Delays*).
- 39 Although the IRS provides various telephone prompts in several different languages, if a taxpayer calls in a language other than Spanish and the IRS assistor cannot understand the taxpayer’s question, the IRS instructs assistors to tell callers they are attempting to contact interpreters. IRM 3.42.7.14.4, *Over the Phone Interpreter Service (OPI)* (June 1, 2018) discusses the IRS Language Service webpage with resources for limited English proficiency (LEP) taxpayers and provides nine telephone prompts in various foreign languages. When the interpreter service is unable to provide an interpreter, assistors are directed to apprise the interpreter vendor using a “feedback form;” however, the IRM provides no mechanism for IRS assistors to follow up with the non-English speaking taxpayer. Further, IRS assistors are told if a taxpayer is calling in a language other than Spanish and assistors cannot understand the taxpayer, assistors should instruct the caller to call back with an interpreter. See IRM 21.3.10.5(7), *Transfers and/or Referrals* (Oct. 1, 2018).

FIGURE 1.13.5, Excerpt of Statutory Notice of Deficiency CP 3219A



Department of the Treasury  
Internal Revenue Service

[Redacted]

[Redacted]

[Redacted]

Notice CP3219A

Tax year [Redacted]

Notice date [Redacted]

Social security number [Redacted]

AUR control number [Redacted]

To contact us [Redacted]

Last date to petition Tax Court [Redacted]

Page 1 of 9

**1 Notice of Deficiency**  
**Proposed increase in tax and notice of your right to challenge**

**2** We have determined there is a deficiency (increase) in your [Redacted] income tax based on information we received from third parties (such as employers or financial institutions) that doesn't match the information you reported on your tax return. See below for an explanation of how this increase was calculated. This letter is your NOTICE OF DEFICIENCY, as required by law.

**3a If you disagree**  
You have the right to challenge this determination in U.S. Tax Court. If you choose to do so, you must file your petition with the Tax Court by March 5, 2018. This date can't be extended. See below for details about how and where to file a petition.

**3c If you agree**  
You can pay now or receive a bill. See the section below titled "If you agree with the proposed changes, you can pay now or receive a bill."

**Summary of proposed changes**

[Redacted]

**3b If you want to resolve this matter with the IRS**  
You may be able to resolve this matter without going to the U.S. Tax Court if you contact us directly. See the "You may be able to resolve your dispute with the IRS" section below.

**3d If you want assistance**  
You may be able to receive assistance from a Low Income Taxpayer Clinic or from the Taxpayer Advocate Service. See the "Additional information" section below.

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**You have the right to petition the Tax Court**

You have the right to challenge our deficiency determination, including penalties, before making any payment by filing a petition with the U.S. Tax Court. You must file your petition within 90 days (or 150 days if the notice is addressed to a person outside of the United States) from the date of this letter, which is [Redacted]. The Tax Court can't consider your case if the petition is filed late. If you decide to file a petition, send that petition to the following address:

United States Tax Court  
400 Second Street, NW  
Washington, DC 20217

Continued on back...

The 3219A SNOD<sup>40</sup> suffers from the following issues:

1. **Title of Notice:** “Notice of Deficiency, Proposed Increase in Tax.” This title should clearly and simply explain the purpose of the notice in plain language. However, the IRS uses technical terms, such as deficiency.<sup>41</sup> A better title could be: “The IRS Will Increase Your Tax After 90 Days Unless You Disagree and Use Your Right to Petition the Tax Court. This is Your Legal Notice, a Notice of Deficiency.” This title still references the legal concept of “deficiency” but clearly explains to the taxpayer why they need to read the content of the notice.
2. **Purpose of Notice:** This section should explain, in plain language, the purpose of the SNOD. For example, this section could state: “We have determined you owe more tax based on information we received from your employer or financial institution. The attached summary shows in detail, the basis for the tax increase. You have the right to challenge the IRS determination, without paying the tax first, by petitioning the U.S. Tax Court by [fill in date]. If you miss this deadline or fail to pay the tax, the IRS will then assess the tax and begin collection, including garnishing your wages or placing a lien on your property. If you need help in preparing a petition, you may be eligible for assistance from Low Income Taxpayer Clinics (LITC), which represent low income taxpayers who need help in resolving a tax dispute and are unable to afford to hire representatives to advocate on their behalf before the IRS or the courts.”
3. **Actions Required:** Here, the IRS structures its options without regard to taxpayer rights and protections.<sup>42</sup> The choices are not only confusing to taxpayers, but also undermine critical taxpayer rights, including the *right to be informed*, the *right to pay no more than the correct amount of tax*, and the *right to a hearing in an independent forum*. Based on the number of “ifs,” there appear to be four options: [a], [b], [c], and [d]. In reality, the taxpayer has two choices—either to agree or to disagree with the proposed increased tax. Instead, the SNOD should present options for taxpayers, such as:
 

If you disagree, you can petition the Tax Court by [fill in deadline]. If you agree, you can sign the waiver and pay now, or wait for an IRS bill.
4. **Help:** This section should explain the assistance available to taxpayers. Although the notice includes information about LITCs and TAS, it could state: “If you need help, including understanding this notice, you can contact a Low Income Taxpayer Clinic, a Local Taxpayer Advocate, the United States Tax Court website, or the IRS.” More detailed information concerning each of these resources could go on page two of the SNOD.
5. **Consequences for Failing to Act:** The consequences for a taxpayer failing to respond is provided on the third page and should instead be clearly spelled out on the first page. This section could instead state: “If you do not petition the Tax Court by [fill-in deadline], you will lose your chance

40 The complete AUR SNOD is located at IRS website, [https://www.irs.gov/pub/notices/cp3219a\\_english.pdf](https://www.irs.gov/pub/notices/cp3219a_english.pdf) (last visited Feb. 2, 2019).

41 IRC § 6211(a). See also Iva W. Cheung, *Plain Language to Minimize Cognitive Load: A Social Justice Perspective*, 60 IEEE TRANSACTIONS ON PROF. COMM. 448, 454 (2017) (“Applying plain-language principles is an evidence based way to reduce cognitive load. Minimizing cognitive load increases the likelihood that people with heavy mental burdens will read and understand the communication.”). See also Literature Review: *Improving Notices Using Psychological, Cognitive, and Behavioral Science Insights*, *infra*.

42 MDRC, News from the BIAS Project, BEHAVIORAL BUZZ, Sept. 2015, at 1. “Research has shown that simplifying forms and providing information can increase take-up of government programs. Making messages clearer and easier to understand and streamlining choices can reduce procrastination and make it easier for clients to complete complex paperwork. Clear instructions, few required fields, and visual prompts that draw the eye to key information are examples of techniques that can improve applications and make it less likely that these forms are barriers to service receipt.” See also Literature Review: *Improving Notices Using Psychological, Cognitive, and Behavioral Science Insights*, *infra*.

to dispute the tax in court without paying the tax first. If the tax is not paid, the IRS will assess the tax and begin collection, including garnishing your wages or placing a lien on your property.”

6. **Organization and Design:** The SNOD’s content should be structured to guide taxpayers in understanding the IRS’s proposed action, the taxpayer’s rights and obligations, and the assistance available to them. The IRS should use the following principles:
- Organize the content so that it flows logically;
  - Break content into short sections that reflect natural stopping points; and
  - Write headings that help readers anticipate what will follow.<sup>43</sup>

Moreover, the CP 3219A SNOD refers taxpayers to the IRS website’s web page, “Understanding Your CP 3219A Notice,” which also presents confusing information. For example, the web page states the following:

If you **don’t agree** with the changes and have additional information for us to consider, mail or fax the information with the **Form 5564** to the address or fax number on the notice.  
(*Emphasis added.*)

The IRS confuses taxpayers by advising taxpayers to use the same form, Form 5564, *Notice of Deficiency-Waiver*, both when they agree with the tax changes and when they disagree with the tax changes. In addition, if taxpayers disagree with the tax changes and submit the Form 5564 with additional information, and the IRS does not resolve their tax issue, they risk missing the Tax Court filing deadline.<sup>44</sup>

In redesigning the SNOD, the IRS should include the Tax Court website and telephone number, as well as a copy of IRS Publication 4134, *Low Income Taxpayer Clinic List*. Furthermore, the IRS should develop and train its employees to educate taxpayers who call the IRS telephone number listed in the SNOD about the Tax Court petition process. IRS employees should emphasize the importance and necessity of filing a petition with the Tax Court, as well as guide taxpayers through the Tax Court petition filing process when taxpayers express that they do not agree with the tax adjustments. Most importantly, IRS employees should make referrals to TAS and LITCs because of the urgency of pending Tax Court petition filing deadlines.

43 Center for Plain Language, *Five Steps to Plain Language*, <https://centerforplainlanguage.org/learning-training/five-steps-plain-language/> (last visited Oct. 2, 2018).

44 See IRS website at <https://www.irs.gov/individuals/understanding-your-cp3219a-notice> (last visited Dec. 13, 2018).

### SNODs Do Not Sufficiently Apply Plain Writing Principles nor Incorporate Behavioral Research Insights as Directed by the Plain Writing Act and Executive Order 13707

To improve the IRS notice clarity, the National Taxpayer Advocate has included a literature review in this year's report that discusses plain language principles and behavioral science research methods. The literature review explores what influences people's decision making, including small changes in language, choice architecture, as well as the salience and framing of information.<sup>45</sup>

Under the Plain Writing Act of 2010, federal agencies are required to use clear, concise, and well-organized government communication the public can understand.<sup>46</sup>

Additionally, federal agencies are required to consider employing behavioral science research to improve how its information is presented.<sup>47</sup> Specifically, federal agencies are to consider how the content, format, timing, and medium by which information is conveyed to the public affects comprehension and action by individuals.<sup>48</sup>

The National Taxpayer Advocate believes the IRS should redesign notices of deficiency, using plain language principles and behavioral science methods, to clearly convey the proposed tax increase to taxpayer's account, to emphasize the taxpayer's right to challenge the IRS's determination before the Tax Court, and to obtain assistance from LITCs and TAS.

In addition, the IRS should collaborate with TAS and stakeholders, especially the Taxpayer Advisory Panel (TAP) and LITCs, in designing the SNOD. The redesign process should consist of the IRS conducting a pilot of several SNODs, including its current notices and rights-based prototypes, and measuring such attributes as: (1) the petition rate of each notice; (2) the TAS contact rate for each notice; (3) the IRS contact rate for each notice; and (4) the downstream consequences of each notice (*e.g.*, disposition of cases, such as whether the taxpayer settled, conceded, or prevailed in Tax Court and whether the taxpayer's deficiency decreased or the taxpayer requested an audit reconsideration).

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45 See Literature Review: *Improving Notices Using Psychological, Cognitive, and Behavioral Science Insights*, *infra*.

46 5 U.S.C. § 301; 3 C.F.R. 13707.

47 3 C.F.R. 13707; see Memorandum from Executive Office of the President, Office of Science and Technology Policy to the Heads of Executive Departments and Agencies, *RE: Implementation Guidance for Executive Order 13707: Using Behavioral Science Insights to Better Serve the American People* (Sept. 15, 2016).

48 *Id.* See also Literature Review: *Improving Notices Using Psychological, Cognitive, and Behavioral Science Insights*, *infra*.

### The IRS Continues to Omit LTA Information Required By Law on Certain SNODs, Thereby Violating Taxpayer Rights

The Internal Revenue Service Restructuring and Reform Act of 1998 (RRA 98),<sup>49</sup> codified at 26 U.S.C. § 6212(a), requires the IRS to provide notice of the taxpayer's right to contact the local office of the taxpayer advocate and the location and phone number of the appropriate office.<sup>50</sup> TAS offices are now aligned with the taxpayer population by ZIP code, so the IRS can easily identify the correct office for inclusion in the notices.

If the taxpayer contacts the LTA before the 90 days expires, some examples of how an LTA could assist these taxpayer include:

- TAS may be able to have the SNOD rescinded on the grounds that the IRS has not responded to the taxpayer's documents or addressed documentation sent in by the taxpayer;
- TAS may be able to have the IRS review the taxpayer's documents quickly in order to resolve the case within 90 days;
- TAS may be able to explain to the taxpayer the IRS's proposed action and if they disagree with the IRS, provide guidance in filing a petition with the Tax Court;
- TAS may also explain to the taxpayer the basis for the IRS action and if the taxpayer agrees, TAS will have educated the taxpayer and enhanced future compliance; and
- TAS may provide contact information for LITCs and encourage taxpayers to seek assistance.

In the twenty years since Congress enacted this requirement, the National Taxpayer Advocate has raised this issue in several congressional reports, and TAS has worked extensively with the IRS to ensure the service is complying with the law.<sup>51</sup> Since 2015, TAS has partnered with the Office of Taxpayer Correspondence to update notices with the required LTA information.

Several notices, however, still do not include the required information.<sup>52</sup> The IRS has informed TAS that because its notice-producing systems are old and inflexible, adding the LTA information to these notices is impossible.<sup>53</sup> Instead, the IRS has included reference to the Taxpayer Bill of Rights (TBOR), TAS, the TAS website, and the TAS toll-free phone number in notices. While this is important information, it does not meet the statutory requirement, which was established at the same time

49 Pub. L. No. 105-206, 112 Stat. 703 (1998).

50 26 U.S.C. § 6212(b). See also Most Serious Problem: *Collection Due Process Notices: Despite Recent Changes to Collection Due Process Notices, Taxpayers Are Still at Risk for Not Understanding Important Procedures and Deadlines, Thereby Missing Their Right to an Independent Hearing and Tax Court Review*, *infra*. Although there is no legislative history available to explain why Congress felt that notices of deficiency should include a mention of TAS, the Joint Committee on Taxation's explanation of the IRS Restructuring and Reform Act of 1998 sections that created the position of the National Taxpayer Advocate, indicate that Congress envisioned the newly created National Taxpayer Advocate playing an important role in "preserving taxpayer rights and solving problems that taxpayers encounter in their dealings with the IRS."

51 See National Taxpayer Advocate 2016 Annual Report to Congress 36 (Special Focus: *IRS Future State: The National Taxpayer Advocate's Vision for a Taxpayer-Centric 21st Century Tax Administration*); National Taxpayer Advocate 2014 Annual Report to Congress 237-244 (Most Serious Problem: *Statutory Notices of Deficiency: Statutory Notices of Deficiency Do Not Include Local Taxpayer Advocate Office Contact Information on the Face of the Notice*).

52 For example, the following letters still lack LTA information: Letter 3219-C, *Notice of Deficiency*; Letter 1753, *Notice of Excise Tax Change*; Letter 531-A, *90-Day Letter Form 1040*; Letter 1120, *Discrepancy Adjustments*; and Letter 531-B, *90-Day Letter; Form 5330, Return of Excise Taxes Related to Employee Benefit Plans*; and Form 990-T, *Exempt Organization Business Income Tax Return*.

53 Email from Wage and Investment Division (W&I) (Oct. 24, 2018) (on file with TAS).

Congress required the National Taxpayer Advocate to maintain at least one local office in each state.<sup>54</sup> Without knowing that *local* assistance is available, a taxpayer may not call a national toll-free number or visit an internet site. In addition, the TAS website may not be easily accessible to the 11 million taxpayers who never use the internet, the 14 million without internet access at home, or the 41 million taxpayers without broadband access.<sup>55</sup> While the TAS national toll-free number is included in notices, that number is not staffed by TAS employees. Moreover, taxpayers need to know that they can talk with someone who is located in the same locale or community, and has knowledge of the underlying economic conditions that may affect their cases.<sup>56</sup>

The failure of the IRS to include LTA information on its notices of deficiency harms taxpayers and violates taxpayers' *right to be informed* and *right to a fair and just tax system*.<sup>57</sup>

## CONCLUSION

Despite the IRS's efforts over the past ten years, the IRS has not designed its SNODs from a taxpayer rights perspective. SNODs fail to alert taxpayers of the IRS's proposed action and its consequences, such as levying the taxpayer's property. Moreover, current SNODs fail to clearly convey taxpayers' obligations and rights and the free resources available to help them understand the SNOD and respond to the IRS. To be most effective, SNODs need to emphasize the taxpayer's right to obtain assistance through TAS and LITCs, right to object to the IRS's decision before an independent forum, and right to representation, if eligible. As described in the literature review compiled by TAS, the IRS should use plain language principles and behavioral insights to redesign SNODs in collaboration with TAS and stakeholders. Because of the sheer number of SNODs being sent to low income taxpayers and the number of taxpayers who do not petition the Tax Court in response to a SNOD, it is critical that the IRS make the SNOD redesign a priority.

54 See IRC 7803(c). The National Taxpayer Advocate has the responsibility of appointing Local Taxpayer Advocates and making available at least one such advocate for each state.

55 See National Taxpayer Advocate 2017 Annual Report to Congress vol. 2 63 (Research Study: *A Further Exploration of Taxpayers' Varying Abilities and Attitudes Towards IRS Options for Fulfilling Common Taxpayer Service Needs*).

56 See National Taxpayer Advocate 2016 Annual Report to Congress 86-97 (Most Serious Problem: *Geographic Focus: The IRS Lacks an Adequate Local Presence in Communities, Thereby Limiting Its Ability to Meet the Needs of Specific Taxpayer Populations and Improve Voluntary Compliance*); National Taxpayer Advocate 2016 Annual Report to Congress vol. 2 102-122 (Literature Review: *Geographic Considerations for Tax Administration*).

57 See TBOR, [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in IRC § 7803(a)(3).

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Redesign the notices of deficiency, using plain language principles and behavioral science methods, to clearly convey the taxpayer's proposed tax increase, his or her right to challenge the IRS's determination before the Tax Court, and his or her ability to obtain TAS or LITC assistance.
  - a. Collaborate with the TAS and stakeholders, especially the TAP and LITCs, in designing the SNOD.
  - b. Conduct a pilot of several SNODs, including current notices and rights-based prototypes, to measure: (1) the petition rate of each notice; (2) the TAS contact rate for each notice; (3) the IRS contact rate for each notice; and (4) the downstream consequences of each notice (*e.g.*, disposition of cases, such as whether the taxpayer settled, conceded, or prevailed in Tax Court and whether the taxpayer's deficiency decreased or the taxpayer requested an audit reconsideration).
2. Develop and train IRS employees in best practices for assisting taxpayers who call the IRS in response to a SNOD, to include having IRS employees remind and guide taxpayers in filing Tax Court petitions.
3. Facilitate the process for petitioning the Tax Court by including with the notice of deficiency the Tax Court website and telephone number, as well as a copy of IRS Publication 4134, *Low Income Taxpayer Clinic List*.
4. Include the Local Taxpayer Advocate's contact information on the face of the notices, specifically on Letters 3219-C, 1753, 531-A, and 531-B.
  - a. If the IRS is unable to update computer programming to provide the telephone number and address information of LTAs pursuant to IRC § 6212(a) during the current year, include Notice 1214,<sup>58</sup> listing all LTA office contact information, when mailing letters 3219-C, 1753, 531-A, and 531-B.
  - b. Develop a timeline to secure and allocate funding to implement the necessary IRS system upgrades to allow for the programming of LTA addresses and contact information on the face of letters 3219-C, 1753, 531-A, and 531-B, as required by law.

<sup>58</sup> Notice 1214, *Helpful Contacts for your "Notice of Deficiency"* (Jan. 2018).

**MSP  
#14****COLLECTION DUE PROCESS NOTICES: Despite Recent Changes to Collection Due Process Notices, Taxpayers Are Still at Risk for Not Understanding Important Procedures and Deadlines, Thereby Missing Their Right to an Independent Hearing and Tax Court Review****RESPONSIBLE OFFICIALS**

Mary Beth Murphy, Small Business/Self-Employed Division  
Ken Corbin, Commissioner, Wage and Investment Division  
Donna Hansberry, Chief, Office of Appeals

**TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to a Fair and Just Tax System*

**DEFINITION OF THE PROBLEM**

Collection Due Process (CDP) hearings are one of the most important taxpayer protections created by the IRS Restructuring and Reform Act of 1998 (RRA 98).<sup>2</sup> CDP hearings provide taxpayers with an independent review by the IRS Office of Appeals of the decision to file a Notice of Federal Tax Lien (NFTL) or the IRS's proposal to undertake a levy action. If the taxpayer disagrees with the outcome of the CDP hearing, he or she can seek review by the U.S. Tax Court.

Collection due process rights further the *right to privacy*, the *right to a fair and just tax system*, and the *right to challenge the IRS's position and be heard*.<sup>3</sup> For instance, during the CDP hearing, the Appeals Officer (AO) must obtain verification that “requirements of any applicable law or administrative procedure have been met.”<sup>4</sup> The AO also must consider “whether any proposed collection action balances the need for the efficient collection of taxes with the legitimate concern of the person that any collection action be no more intrusive than necessary.”<sup>5</sup> Taxpayers are given the opportunity to raise a collection alternative, such as an installment agreement or offer in compromise, and in some instances they can contest the underlying liability.<sup>6</sup>

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 IRS Restructuring and Reform Act of 1998 (RRA 98), Pub. L. No. 105-206, § 3401, 112 Stat. 685, 746 (1998).

3 For a more thorough discussion of the importance of CDP rights in tax administration, see Nina E. Olson, *Taking the Bull by Its Horns: Some Thoughts on Constitutional Due Process in Tax Collection*, 63 TAX LAWYER 227.

4 IRC § 6330(c)(1).

5 IRC § 6330(c)(3)(C).

6 IRC § 6330(c).

However, as discussed below, the response rate for CDP notices is quite low, between less than one percent and ten percent, depending on the taxpayer's income level and notice type. Many and diverse stakeholders have expressed concerns that CDP rights are communicated poorly to taxpayers.<sup>7</sup> The Treasury Inspector General for Tax Administration (TIGTA) reports that some taxpayers were denied a CDP hearing because they sent their request for a CDP hearing to the wrong office.<sup>8</sup> The Tax Court has also noted confusion surrounding the notice of determination.<sup>9</sup>

Given what is at stake in CDP cases, any confusing or inadequate correspondence can have grave consequences for a taxpayer's rights. The National Taxpayer Advocate has the following concerns about the current CDP notices:

- The design and wording in CDP administrative notices underemphasize the importance of CDP rights;
- Important information for exercising CDP administrative rights are not clearly communicated to taxpayers; and
- The defects in the notice of determination may prevent some taxpayers from appealing their cases to Tax Court.

## ANALYSIS OF THE PROBLEM

### Background

During hearings leading to the enactment of RRA 98, Senator Roth, Chairman of the Senate Finance Committee, explained in 1998:

There is no doubt that the powers of the Internal Revenue Service are extraordinary. The IRS can seize property, paychecks, and even the residences of the people it serves. Businesses can be padlocked, sometimes causing hundreds of employees who are also taxpayers to be put out of work ... This is an awesome amount of power to place in the hands of any government agency. Is it appropriate? Perhaps. But with such power there must be an effective counterbalance of responsibility. Why? Because the greater the power, the more extensive the damage that can be done if that power is abused.<sup>10</sup>

Senator Roth's concerns were not far-fetched. To draft RRA 98, legislators heard testimony from taxpayers. Thomas Savage, owner of a construction management company, testified about his experience where a subcontractor he worked with accrued a tax debt. The IRS determined the

<sup>7</sup> National Taxpayer Advocate 2017 Annual Report to Congress 299-306 (Legislative Recommendation: *Collection Due Process and Innocent Spouse Notices: Amend IRC §§ 6320, 6330, and 6015 to Require That IRS Notices Sent to Taxpayers Include a Specific Date by Which Taxpayers Must File Their Tax Court Petitions, and Provide That a Petition Filed by Such Specified Date Will Be Treated As Timely*); Carlton Smith, PROCEDURALLY TAXING, *CDP Notice of Determination Sentence Causing Late Pro Se Petitions*, <http://procedurallytaxing.com/cdp-notice-of-determination-sentence-causing-late-pro-se-petitions/> (Mar. 24, 2016); TAX NOTES TODAY, *Harvard Federal Tax Clinic Provides IRS Reform Recommendations*, 2018 TNT 70-19 (Apr. 17, 2018).

<sup>8</sup> Treasury Inspector for Tax Administration (TIGTA), Ref. No. 2018-10-054, *Review of the Office of Appeals Collection Due Process Program* 6 (Sept. 5, 2018).

<sup>9</sup> In *Houk v. Commissioner*, the court noted that "people of ordinary intelligence who do not have tax training and who have previously received both a lien notice and a levy notice and have requested CDP hearings for both ... must find [the title of the notice of determination] confusing." *Houk v. Comm'r.*, Order for Supplement to Motion for Entry of Decision, Tax Ct. No. 22140-15L (June 2, 2018).

<sup>10</sup> *Practices and Procedures of the Internal Revenue Service: Hearing Before the S. Comm. on Finance*, 105th Cong. 2 (1998) (opening statement of Senator William V. Roth, Jr.).

subcontractor to be currently not collectible and turned its attention to Mr. Savage. The IRS incorrectly argued there was a partnership between Mr. Savage and the subcontractor. Mr. Savage testified that:

Undaunted by the challenge to provide the authority in support of this fictitious partnership, the revenue officer caused the IRS to issue a 30-day letter which proposed an assessment against the fictitious partnership. We immediately filed a written protest with the IRS appeals officer and eagerly awaited an appeals conference to put the case behind us. As things turned out, we were never given an opportunity to present our case to the appeals office.”<sup>11</sup>

CDP hearings were designed not to limit the IRS’s awesome collection powers but to serve as a check on abuses of that power. Moreover, CDP hearings ensure taxpayers have an opportunity to raise their concerns to an independent official prior to the IRS taking its first potentially devastating collection action.

### *CDP Processes and Procedures*

The IRS communicates CDP rights during two critical times. First, the IRS communicates the right to request a CDP administrative hearing with notices such as Letter 1058, *Final Notice of Intent to Levy and Notice of Your Right to a Hearing* (notice of intent to levy), or Letter 3172, *Notice of Federal Tax Lien and Your Rights to a Hearing Under IRC 6320* (NFTL).<sup>12</sup> Following the CDP hearing, the IRS communicates its determination to the taxpayer via a notice of determination, such as Letter 3193, *Notice of Determination: Concerning Collection Action(s) Under Section 6320 and/or 6330 of the Internal Revenue Code* (notice of determination), which includes the right to appeal the determination to Tax Court.<sup>13</sup>

The IRS provides the taxpayer with 30 days in which to request an administrative CDP hearing.<sup>14</sup> Taxpayers who miss the 30-day deadline to request a CDP hearing may still receive an equivalent hearing within one year from the day after the date of the intent to levy notice or within one year from the day after the end of the five business day period following the filing of the NFTL.<sup>15</sup> It is unclear if missing the deadline to request an administrative CDP hearing in the first place is a matter of jurisdiction for the Tax Court and can be subject to equitable tolling if later litigated.<sup>16</sup>

11 *Practices and Procedures of the Internal Revenue Service: Hearing Before the S. Comm. on Finance*, 105th Cong. 83 (1998) (statement of Thomas Savage, business owner).

12 IRS, Letter 1058, *Final Notice Notice of Intent to Levy and Notice of Your Right to a Hearing* (Jan. 2017); IRS, Letter 3172, *Notice of Federal Tax Lien and Your Rights to a Hearing Under IRC 6320* (Mar. 2017). Notice LT11, *Notice of Intent to Levy and Notice of Your Right to a Hearing*, is sent to taxpayers whose cases are in Automated Collection Services (ACS) and Letter 1058 is sent to taxpayers whose cases are assigned to Revenue Officers. This discussion will focus on Letter 1058 for the conversation regarding intent to levy notices.

13 IRS Letter L3193, *Notice of Determination: Concerning Collection Action(s) Under Section 6320 and/or 6330 of The Internal Revenue Code* (July 2018).

14 IRC §§ 6320(a)(3)(B) and 6330(a)(3)(B).

15 Treas. Reg. § 301.6330-1(h)(2)(iv)(Q&A17). The equivalent hearing will be held by Appeals and generally will follow Appeals’ procedures for a CDP hearing. Appeals will not, however, issue a notice of determination, it will issue a decision letter. Also, unlike with a CDP hearing, the IRS may continue collection action while the equivalent hearing is pending, and the taxpayer cannot appeal the decision letter to Tax Court. Treas. Reg. § 301.6320-1(h)(2); Treas. Reg. § 301.6330-1(h)(2).

16 *Kim v. Comm’r.*, T.C. Memo. 2005-96. For a discussion about how the time period for filing a CDP hearing request is not an issue of jurisdiction, see Keith Fogg, *The Jurisdictional Ramifications of Where You Send a CDP Request*, TAX NOTES (Nov. 12, 2018).

However, if the taxpayer disagrees with the IRS's determination after the CDP hearing and wishes to appeal, he or she must file a petition with the U.S. Tax Court within 30 days of the IRS's determination.<sup>17</sup> The Tax Court has held that the 30-day filing deadline to seek judicial review under IRC § 6330(d)(1) is an issue of jurisdiction.<sup>18</sup> Without jurisdiction, the Tax Court cannot hear a case. Furthermore, the deadline is not subject to equitable tolling, meaning the court cannot extend the deadline for any reason.<sup>19</sup>

### *CDP Notices Have a Low Response Rate*

Figure 1.14.1 shows the number and response rate (percentage) for CDP notices issued in fiscal year (FY) 2017 by the taxpayer's income.<sup>20</sup> Regardless of income, all the notices had a very low response rate. For instance, 162,887 taxpayers who live in poverty received the intent to levy CDP notice during FY 2017. Of the 162,887 such taxpayers who received a levy notice, only 1,733 (approximately one percent) requested a CDP hearing. An additional 267 of those taxpayers requested an equivalent hearing. This is roughly 13 percent of the taxpayers who responded.<sup>21</sup>

There is a small increase in the response rate as the taxpayer's income increases but differs depending on which notice is being considered. The largest response rate is the group of taxpayers who received both a notice of intent to levy and an NFTL, and whose income was above 250 percent of the federal poverty level. In this group, the IRS issued 40,338 notices and the IRS received 4,194 CDP hearing requests, creating a response rate of around ten percent. An additional 797 taxpayers (two percent of the taxpayers) requested an equivalent hearing, which represents nearly 16 percent of the responses.<sup>22</sup>

17 IRC § 6330(d)(1).

18 *Weber v. Commissioner*, 122 T.C. 258 (Mar. 22, 2004).

19 *Duggan v. Commissioner*, Tax Ct. Docket No. 4100-15L (order dated June 26, 2015). The Ninth circuit affirmed the 30-day deadline is a matter of jurisdiction. *Duggan v. Commissioner*, 2018 U.S. App. LEXIS 886 (9th Cir. Jan. 12, 2018).

20 The analysis broke down income according to the guidelines found in IRC § 7526(b)(1)(B), which considers eligibility for low income tax clinic (LITC) representation based on a financial breakdown where 90 percent of the clients do not exceed 250 percent of the federal poverty level. However, the IRS will process taxpayers through a low income filter for the purposes of the Federal Payment Levy Program (FPLP) if the taxpayer's income falls below 250 percent of the federal poverty level. IRM 5.19.9.3.2.3, *Low Income Filter Exclusion* (Oct. 20, 2016).

21 The 267 equivalent hearing requests constitute 13 percent of the 2,000 responses to the intent to levy CDP notice (1,733 timely requests and 267 equivalent hearing requests).

22 The 797 equivalent hearing requests constitute 16 percent of the 4,991 responses to both the lien and levy CDP notice (4,194 timely requests and 797 equivalent hearing requests).

FIGURE 1.14.1, CDP Notices Issued in FY 2017 and Hearing Requests by Income Level<sup>23</sup>

Income Group	CDP Notice Type	TPs mailed Notices	Appeal Requested	Equivalent Hearing Requested	Notice of Determination Issued
In Poverty	Levy only	162,887 (75%)	1,733 (1%)	267 (<1%)	1,361 (1%)
	Lien only	41,058 (19%)	1,413 (3%)	226 (1%)	1,096 (3%)
	Both Levy and Lien	14,041 (6%)	1,064 (8%)	197 (2%)	802 (6%)
	Subtotal	217,986	4,210 (2%)	690 (<1%)	3,259 (1%)
Above Poverty to 250% Federal Poverty Level	Levy only	261,658 (88%)	2,767 (1%)	396 (<1%)	2,228 (1%)
	Lien only	25,207 (8%)	1,128 (4%)	168 (1%)	908 (4%)
	Both Levy and Lien	10,647 (4%)	867 (8%)	155 (2%)	643 (6%)
	Subtotal	297,512	4,762 (2%)	719 (<1%)	3,779 (1%)
Above 250% of Federal Poverty Level	Levy only	641,469 (83%)	9,144 (1%)	1,472 (<1%)	7,393 (1%)
	Lien only	94,046 (12%)	5,789 (6%)	794 (1%)	4,721 (5%)
	Both Levy and Lien	40,338 (5%)	4,194 (10%)	797 (2%)	3,225 (8%)
	Subtotal	775,853	19,127 (2%)	3,063 (<1%)	15,339 (2%)
Overall Total TPs	<b>Total</b>	<b>1,291,351</b>	<b>28,099 (2%)</b>	<b>4,472 (&lt;1%)</b>	<b>22,377 (2%)</b>

Additionally, many taxpayers navigate the CDP process (including litigation in Tax Court) without representation. In fact, for the period between June 1, 2016 and May 31, 2017, there were 568 Tax Court petitions filed in CDP cases.<sup>24</sup> Of those, 335 petitions were filed by *pro se* taxpayers, meaning that approximately 59 percent of taxpayers who appealed a CDP determination were unrepresented.<sup>25</sup>

23 Compliance Data Warehouse, Individual Returns Transaction File, Information Returns Master File. A single taxpayer could have received CDP notices for more than one module. A tax module is a combination of a type of tax and the tax period when it was originally due. A total of 72,215 taxpayers were categorized into the “in poverty” group because for tax year 2017 they did not file a return and there were no third-party reports of income for them. It is possible that some of these taxpayers may have had unreported income. This data does not include information from businesses.

24 Data pulled from Tax Litigation Counsel Automated Tracking System (TLCATS) and Counsel Automated Systems Environment – Management Information System (CASE-MIS) (July 26, 2018).

25 *Id.*

### *To Address Practitioners' Criticisms, TAS Reviewed CDP Notices*

TAS started an ongoing review of CDP-related notices in FY 2018. As part of this review, TAS first reviewed the legal requirements for each notice. According to IRC § 6330, the notice of intent to levy must:

- Include notice of the taxpayer's right to a CDP hearing before a levy is made;<sup>26</sup>
- Include the following information in "simple and nontechnical terms":
  - a) The amount of unpaid taxes;<sup>27</sup>
  - b) The right to request a CDP hearing during the 30-day period;<sup>28</sup>
  - c) The proposed IRS action and the rights of the taxpayer with respect to such action, including a brief statement setting forth:
    - i. The Code provisions relating to levy and sale of property;
    - ii. Levy and sale of property procedures;
    - iii. Available administrative appeals and associated procedures;
    - iv. Available alternatives that could prevent the levy (including installment agreements); and
    - v. Provisions of this title and procedures relating to redemption of property and release of liens on property.<sup>29</sup>

The NFTL notice has similar legal requirements under IRC § 6320(a)(3).

An NFTL notice must include:

- The amount of unpaid tax;
- The right of the person to request a hearing during the 30-day timeframe beginning five days after the lien is filed;
- The administrative appeals available to the taxpayer with respect to such lien and the procedures relating to such appeals;
- The provisions relating to the release of liens on property; and
- The provisions of IRC § 7345 relating to the certification of seriously delinquent tax debts and the denial, revocation, or limitation of passports of individuals with such debts pursuant to § 32101 of the Fixing America's Surface Transportation (FAST) Act.<sup>30</sup>

There are requirements for the notice of determination, but most apply to the results of the specific CDP hearing. For instance, the notice of determination must address whether the proposed collection action represents a balance between the need for the efficient collection of taxes and the legitimate concern of

26 This notice requirement does not apply to levies on state tax refunds, jeopardy levies, federal contractor levies, or disqualified employment tax levies. IRC § 6330(a)(1).

27 IRC § 6330(a)(3)(A).

28 IRC § 6330(a)(3)(B).

29 IRC § 6330(a)(3)(C).

30 IRC § 6320(a)(3)(E). Comparable language is not required for intent to levy CDP notices, however, the IRS currently does include it. Such language is required in the levy notice following notice and demand for payment under IRC § 6331(d). IRC § 6331(d)(4)(G).

the taxpayer that any collection action be no more intrusive than necessary.<sup>31</sup> Most pertinent to this discussion is the requirement that the notice will advise the taxpayer of his or her right to seek judicial review within 30 days of the date of the Notice of Determination.<sup>32</sup>

### The Design and Wording in CDP Notices Underemphasize the Importance of CDP Rights

The current CDP administrative notices do not inform taxpayers about *why* CDP rights are important to taxpayers. For instance, the intent to levy notice says, “This is your notice of our intent to levy ... and your right to request a Collection Due Process hearing ...” It does not explain what a CDP hearing is, why a taxpayer would want to request one, and does not adequately explain equivalent hearings. Telling a taxpayer why CDP rights are important furthers the *right to be informed*.<sup>33</sup> And from a behavioral science perspective, including an explanation would provide a “nudge” that could increase a taxpayer’s decision to exercise his or her rights. A “nudge” steers people in a particular direction while allowing them to maintain their choice.<sup>34</sup>

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The current Collection Due Process (CDP) administrative notices do not inform taxpayers about *why* CDP rights are important to taxpayers .... It does not explain what a CDP hearing is, why a taxpayer would want to request one, and does not adequately explain equivalent hearings.

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### Important information for Exercising CDP Rights Is Not Clearly Communicated to Taxpayers

#### *The Deadline to Request a CDP Hearing May Be Missed By Taxpayers*

The intent to levy notice mentions the deadline to request the CDP hearing in the fourth paragraph of the first page. It is not in bold font or otherwise set apart from the rest of the text. Based on behavioral research, we know that plain language helps a reader understand material. However, plain language does not just consist of simple wording. Plain language also means structuring the material so that it flows easily for the reader as well as incorporating typography (bold font, etc.) and white space to guide the reader.<sup>35</sup> The current intent to levy notice does not effectively communicate the file-by date by burying it in text and not putting it in bold font to guide the reader’s attention.

The National Taxpayer Advocate is also concerned with how the response due date is communicated to taxpayers who receive an NFTL. According to IRC § 6320(a)(2), the IRS must provide notice to the taxpayer of the NFTL “not more than 5 business days after the day of the *filing* of the notice of lien.” [Emphasis added.] The taxpayer’s 30-day timeframe to request a CDP hearing starts “on the day after

31 Treas. Reg. § 301.6330-1(e)(3)(Q&A E-8).

32 *Id.*

33 IRC § 7803(a)(3)(A).

34 Deloitte Consulting LLP, *Using the Nudge in Tax Compliance: Leveraging Behavioral Insights to Boost Tax Revenue* 9 (2017). See also Literature Review: *Improving Notices Using Psychological, Cognitive, and Behavioral Science Insights*, *infra*.

35 Center for Plain Language, *Five Steps to Plain Language*, <https://centerforplainlanguage.org/learning-training/five-steps-plain-language/>. For more information on how plain language can help taxpayers, see Literature Review: *Improving Notices Using Psychological, Cognitive, and Behavioral Science Insights*, *infra*.

the 5-day period” mentioned in IRC § 6320(a)(2).<sup>36</sup> However, the IRS considers the NFTL to be filed on the date it *should* be received by the recording office and to determine this date, the IRS adds three days to the NFTL mailing date.<sup>37</sup>

Here is an example:

1. IRS mails NFTL to the recording office on September 6, 2017.
2. Estimated Filing Date: (+ 3 business days) = September 11.
3. Required notification to the taxpayer: (+ 5 business days) = September 18 (IRS mails NFTL letter to TP, with date on it).
4. File By Date: (30 days from required notification) = October 18.

However, in reality the recording office does not receive the NFTL until September 20, 2017. Based on this date, the IRS would have been required to mail notification to the taxpayer within five business days of September 20, or by September 27. The taxpayer’s 30-day deadline to request a CDP hearing would expire 30 days later, on October 27. The lag time in receiving the notice should have allowed the taxpayer an additional nine days to request a CDP hearing.

While including an exact date to request a CDP hearing based on a projected filing date may allow the IRS to issue large amounts of NFTLs and CDP notices, untold circumstances could prevent the delay of the filing of an NFTL. Since the filing date is critical to the timeframe for requesting a CDP hearing, the taxpayer could have a longer period of time to request a CDP hearing than the NFTL letter indicates, but he or she would not know it.<sup>38</sup>

### *CDP Administrative Notices Do Not Clearly Instruct Taxpayers Where to Send Their CDP Hearing Requests*

The intent to levy notice instructs the taxpayer to send his or her CDP hearing request to “the above address.” Again, this information is buried in text. Multiple addresses may also appear on the notice, one for a response and one for payment. The harm caused by this confusion is evident in the order issued by the Tax Court in *Zonies v. Commissioner*, where Mr. Zonies sent his CDP request to the wrong office and by the time it arrived at the right office, his 30-day time frame had expired.<sup>39</sup> A recent TIGTA report reviewed 70 CDP cases and found that approximately 11 percent of the taxpayers sent their CDP hearing requests to the wrong office.<sup>40</sup> As mentioned earlier, to help taxpayers read and understand the notice, the IRS needs to place the address early in the notice and set apart by bold font. Moreover, since the CDP notice provides significant, one-time due process rights, the address to make a CDP hearing request should be more prominent than the address for making payments. The CDP notice should prioritize taxpayer rights.

36 IRC § 6320(a)(3)(B).

37 IRM 5.12.6.3.6(3), *CDP Notice Time Frames* (Jan. 19, 2018).

38 TAS is reviewing the data for taxpayers filing lien and levy CDP hearing requests to determine whether a longer time period would mitigate some of the low hearing rates and late filing issues. We may make a legislative recommendation regarding these deadlines in later reports.

39 *Zonies v. Comm’r.*, Docket No. 18711-15L, Order (Feb. 22, 2016). See also Keith Fogg, *Sending Your Collection Due Process Hearing Request to the Correct Address*, *PROCEDURALLY TAXING* (Apr. 26, 2016), <http://procedurallytaxing.com/sending-your-collection-due-process-hearing-request-to-the-correct-address/>; Keith Fogg, *The Jurisdictional Ramifications of Where You Send a CDP Request*, *TAX NOTES* (Nov. 12, 2018).

40 TIGTA, *Review of the Office of Appeals Collection Due Process Program*, Report No. 2018-10-054 6 (Sept. 5, 2018). TIGTA reviewed 70 CDP cases and identified 8 taxpayers who mailed or faxed their CDP hearing request to the wrong office.

### *Notices Should Include References to TAS and Low Income Taxpayer Clinics*

IRC § 6212(a) requires that the notice of deficiency, which is sent to a taxpayer prior to assessment of a liability, include “a notice to the taxpayer of the taxpayer’s right to contact a local office of the taxpayer advocate and the location and phone number of the appropriate office.” However, no such requirement exists for CDP notices. The IRS includes a reference to TAS and Low Income Taxpayer Clinics (LITC) in publications 594, *The IRS Collection Process*, and 1660, *Collection Appeal Rights*. However, the taxpayer may not read to the end of the notice or to read the enclosed publications if he or she does not find the notice easy to read or salient to them.

There is no legislative history available to explain why Congress felt that notices of deficiency should include a mention of TAS but CDP notices should not. However, we can glean some understanding from the Joint Committee on Taxation’s explanation of the RRA 98 sections that created the position of the National Taxpayer Advocate. Congress envisioned the newly created National Taxpayer Advocate playing an important role in “preserving taxpayer rights and solving problems that taxpayers encounter in their dealings with the IRS.”<sup>41</sup> Additionally, the Local Taxpayer Advocates were set up to report directly to the National Taxpayer Advocate and not another IRS function.<sup>42</sup> Including a reference to TAS in the CDP notices will further the National Taxpayer Advocate’s ability to fulfill her duties to taxpayers and Congress. It will also fulfill the taxpayer’s *right to be informed* during a critical juncture of his or her case. Including a reference to the LITC program will also further the taxpayer’s *right to be informed* and the *right to retain representation* during a crucial time in their case.<sup>43</sup>

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Because Collection Due Process (CDP) hearings offer the taxpayer an opportunity to raise alternatives to IRS collection actions, require balancing the government’s interest in the efficient collection of tax with the taxpayer’s interest that such action be no more intrusive than necessary, and in some instances provide taxpayers with an opportunity to challenge the underlying liability, CDP notices should be models of clarity and educate the taxpayer about the importance of the hearing process itself.

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### **Defects in the Notice of Determination May Prevent Some Taxpayers From Appealing Their Cases to Tax Court**

Following the CDP hearing with Appeals, the IRS will issue a notice of determination to the taxpayer. Taxpayers have 30 days in which to request Tax Court review of a notice of determination.<sup>44</sup> Unlike a notice of deficiency, which legally requires a specific date by which the taxpayer must file his or her petition in Tax Court, the IRS is not required to include a specific date in a notice of determination.<sup>45</sup>

41 J. Comm. on Tax’n, *General Explanation of Tax Legislation Enacted in 1998* 32 (Nov. 24, 1998).

42 *Id.*

43 The LITC program provides free representation to low income taxpayers and outreach to taxpayers who speak English as a second language. IRC § 7526.

44 IRC § 6330(d)(1). Treasury regulations stipulate that the “30-day period within which the taxpayer is permitted to seek judicial review of Appeals’ determination commences the day after the date of the Notice of Determination.” Treas. Reg. 301.6330-1(e)(3)(Q&A E-10).

45 IRC § 6213(a).

The IRS chose not to include a date on the notice because Appeals employees date and mail the notice of determination manually. The IRS is concerned that manually calculating a specific date by which the taxpayers must respond would “add complexity and additional time to the processing of letters and any erroneous calculations could result in taxpayers missing the petition deadline through no fault of their own.”<sup>46</sup> The process for including a date on the notice of deficiency is included in IRM 8.20.6.8.4, which Appeals employees follow. It is unclear why this process could not apply to the notice of determination.<sup>47</sup>

A review of court cases illustrates why the filing deadline needs to be plainly communicated to taxpayers.<sup>48</sup> The current notice of determination reads, “If you want to dispute this determination in court, you must file a petition with the United States Tax Court within 30 days from the date of this letter.”<sup>49</sup> This language may confuse taxpayers. For instance, what does the term “within” mean to the non-expert taxpayer? Is the date of the letter day one or day zero? The best way to protect taxpayer rights is to include a specific date by which taxpayers must file their petition in Tax Court. The National Taxpayer Advocate made a legislative recommendation in her 2017 Annual Report to Congress to require a specific response date in CDP notices; others in the tax field have called for similar reform.<sup>50</sup>

This date should be provided in bold and in a prominent place, such as in the upper righthand corner of the notice. Including this information up front and in bold font is not just a matter of convenience. The IRS acknowledges that “much behavior is driven by what we pay attention to. Saliency is the ability to command attention to something by giving it more weight or putting it in a position that will capture attention and influence choices.”<sup>51</sup> The current notice of determination lacks saliency as taxpayers cannot ascertain easily when they need to file their petition. In fact, simply changing the location and presentation of choices in a notice can decrease “cognitive burden.”<sup>52</sup> With an easier understanding, taxpayers may be more inclined to exercise their CDP rights.

Similar to the CDP administrative notices, the notice of determination also does not explain the significance of the right to go to Tax Court and why a taxpayer should file a petition. The right to go to Tax Court is at the heart of the taxpayers’ *right to appeal an IRS decision in an independent forum*; it gives the taxpayer the opportunity to present his or her concerns about the IRS’s proposed action before a fully independent tribunal, and provides important oversight to the IRS’s collection powers. As discussed with the CDP administrative notices, language added to explain why a taxpayer would want to file a petition in Tax Court could “nudge” taxpayers.

46 IRS response to TAS information request (Dec. 6, 2018).

47 *Id.*

48 For instance, see *Duggan v. Commissioner*, Tax Ct. Docket No. 4100-15L 2 (order dated June 26, 2015); *Swanson v. Commissioner*, Tax Ct. Docket No. 14406-15S (order dated Jan. 14, 2016); *Pottgen v. Commissioner*, Tax Ct. Docket No. 1410-15L (order dated Mar. 4, 2016); *Integrated Management, Inc., v. Commissioner*, Tax Ct. Docket No. 27674-16SL (order dated May 31, 2017); *Protter v. Commissioner*, Tax Ct. Docket No. 22975-15SL (order dated Sept. 26, 2017). These cases are not cited for precedent, rather only for the fact patterns showing taxpayers miscalculated the deadline to file.

49 The previous language reads “If you want to dispute this determination in court, you must file a petition with the United States Tax Court within a 30-day period beginning the day after the date of this letter.” IRS, Letter 3193, *Notice of Determination Concerning Collection Actions Under Sections 6320 and 6330* (Dec. 2016).

50 National Taxpayer Advocate 2017 Annual Report to Congress 299-306 (Legislative Recommendation: *Collection Due Process and Innocent Spouse Notices: Amend IRC §§ 6320, 6330, and 6015 to Require That IRS Notices Sent to Taxpayers Include a Specific Date by Which Taxpayers Must File Their Tax Court Petitions, and Provide That a Petition Filed by Such Specified Date Will Be Treated As Timely*); Carlton Smith, *CDP Notice of Determination Sentence Causing Late Pro Se Petitions*, PROCEDURALLY TAXING (Mar. 24, 2016), <http://procedurallytaxing.com/cdp-notice-of-determination-sentence-causing-late-pro-se-petitions>.

51 IRS, *Behavioral Insights Toolkit 24* (2017).

52 *Id.*

## CONCLUSION

Correspondence issued by the IRS plays a crucial role in tax administration. If drafted appropriately, it can educate and empower taxpayers. For CDP notices in particular, this may be the first time taxpayers have run into a situation where they need to exercise their due process rights. Because CDP hearings offer the taxpayer an opportunity to raise alternatives to IRS collection actions, require balancing the government's interest in the efficient collection of tax with the taxpayer's interest that such action be no more intrusive than necessary, and in some instances provide taxpayers with an opportunity to challenge the underlying liability, CDP notices should be models of clarity and educate the taxpayer about the importance of the hearing process itself. This education includes filing instructions and deadlines as well as additional resources the taxpayer can use if they have questions.

The IRS's current approach with communications that relate to CDP rights often overlooks some valuable opportunities to maximize the benefits of informing, educating, and interacting with taxpayers. For example, behavioral science shows us that location of text and typography can make a notice easier to read. The important aspects of the notice, such as the deadline to file and address to respond, should be early in the notice and easy to discern from the rest of the text. On a larger scale, taxpayers need to understand why these notices are salient to them and how CDP rights can impact their lives. They need to understand what the IRS proposes to do, what they will experience if they do not respond, and how to exercise their rights.

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Include the exact date on the Notices of Determination by which the taxpayer must file a petition in Tax Court.
2. Work with TAS to redesign the CDP notices so that they reflect the principles of visual cognition and processing of complex information. This will include changes such as:
  - (a) Putting clear explanations about the importance of these hearings in terms relating to taxpayer rights and protections;
  - (b) Highlighting deadlines early in the notices and in bold font; and
  - (c) Including references to TAS and the LITC program.
3. Work with TAS to explore methods of more accurate notification of the due date for CDP hearing requests with respect to lien filings.

## INTRODUCTION TO COLLECTION: A Roadmap to the IRS Collection Process

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One of the most obvious and important roles of the IRS is the collection of taxes. In 2014, the IRS restructured its Collection organization, which is housed within the Small Business/Self-Employed (SB/SE) Division.<sup>1</sup> The stated mission for this organization is:

To collect delinquent taxes and secure delinquent tax returns through the fair and equitable application of the tax laws, including the use of enforcement tools when appropriate, provide education to customers to enable future compliance, and thereby protect and promote public confidence in the American tax system.

In 2015, Congress codified the Taxpayer Bill of Rights (TBOR) into the tax code; these ten rights are enumerated in Internal Revenue Code (IRC) § 7803(a)(3) and include *the right to pay no more than the correct amount of tax, the right to privacy, and the right to a fair and just tax system*. One of the challenges for the IRS is to fulfill its obligation to collect taxes while comporting with its stated mission of educating taxpayers and with the TBOR.

In fiscal year (FY) 2017, the IRS brought in \$3.4 trillion in revenue.<sup>2</sup> The vast majority of those payments were made voluntarily by taxpayers.<sup>3</sup> There are generally three ways in which taxpayers may voluntarily submit tax payments to the IRS: (1) through withholding by third parties (*e.g.*, employers); (2) making estimated payments (typically on a quarterly basis); or (3) submitting payments with their tax return.

The Taxpayer's Journey: Roadmaps of the Taxpayer's Path Through the Tax System section, following the Preface, includes a graphical overview of how the Collection process works and how taxpayers may progress through it, along with the applicable deadlines taxpayers must be aware of to retain their rights.

### The Collection Notice Stream

If taxpayers do not voluntarily pay taxes assessed, the IRS may initiate collection action. IRS collection actions brought in nearly \$40 billion in FY 2017 (1.2 percent of total revenue collected).<sup>4</sup> The majority (\$30.6 billion in FY 2017) of the amount collected is from the “notice stream,” a series of letters issued early in the life of the debt, notifying the taxpayer of the balance due and requesting payment of the full amount.<sup>5</sup>

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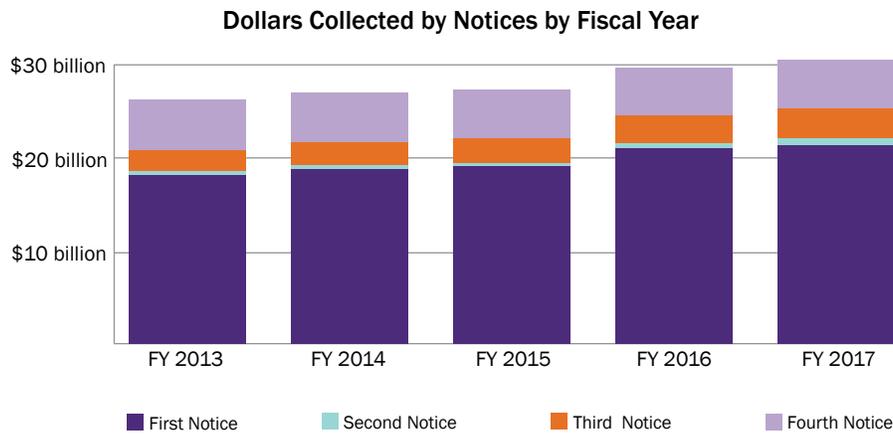
1 IRS, Small Business/Self-Employed (SB/SE) Executive Organizational Chart (Mar. 2018).

2 IRS, *2017 Data Book* iii.

3 Less than one percent of revenue came from cases that were generally in a collection status where enforced collection could occur.

4 IRS, *2017 Data Book* 17, 41. This figure includes dollars collected from all collection activity.

5 Treasury Inspector General for Tax Administration (TIGTA), Ref. No. 2018-30-069, *Trends in Compliance Activities Through Fiscal Year 2017* 6 (Sept. 13, 2018).

FIGURE 1.0.1<sup>6</sup>

If the taxpayer does not pay in full or otherwise respond to the notice stream, the IRS issues a notice of intent to levy via certified mail.<sup>7</sup> If the taxpayer does not pay within 30 days of that notice, the IRS sends a collection due process (CDP) notice that provides a taxpayer the opportunity to appeal the filing or issuance of liens or levies.<sup>8</sup>

### Right to CDP Hearings

CDP hearings are one of the most important taxpayer protections created by the IRS Restructuring and Reform Act of 1998 (RRA 98).<sup>9</sup> CDP hearings provide taxpayers with an independent review by the IRS Office of Appeals of the decision to file a Notice of Federal Tax Lien (NFTL) or the IRS's proposal to undertake a levy action. If the taxpayer disagrees with the outcome of the CDP hearing, he or she can seek review by the U.S. Tax Court.

CDP rights further *the right to privacy, the right to a fair and just tax system, and the right to challenge the IRS's position and be heard.*<sup>10</sup> For instance, during the CDP hearing, the Appeals Officer (AO) must obtain verification that "requirements of any applicable law or administrative procedure have been met."<sup>11</sup> The AO also must consider "whether any proposed collection action balances the need for the efficient collection of taxes with the legitimate concern of the person that any collection action be no more intrusive than necessary."<sup>12</sup> Taxpayers are given the opportunity to raise a collection alternative,

6 Enforcement Revenue Information System (July 2018).

7 See Internal Revenue Code (IRC) § 6331(d).

8 See IRC §§ 6320 and 6330. For an in-depth discussion of the Collection Due Process (CDP) process, please see Most Serious Problem: *Collection Due Process Notices: Despite Recent Changes to Collection Due Process Notices, Taxpayers Are Still at Risk for Not Understanding Important Procedures and Deadlines, Thereby Missing Their Right to an Independent Hearing and Tax Court Review, infra.*

9 IRS Restructuring and Reform Act of 1998 (RRA 98), Pub. L. No. 105-206, § 3401, 112 Stat. 685, 746 (1998).

10 For a more thorough discussion of the importance of CDP rights in tax administration, see Nina E. Olson, *Taking the Bull by Its Horns: Some Thoughts on Constitutional Due Process in Tax Collection*, 63 TAX LAWYER 227 (2010).

11 IRC § 6330(c)(1).

12 IRC § 6330(c)(3)(C).

such as an installment agreement or offer in compromise, and in some instances they can contest the underlying liability.<sup>13</sup>

CDP hearings were designed not to limit the IRS's awesome collection powers but to serve as a check on abuses of that power. Moreover, CDP hearings ensure taxpayers have an opportunity to raise their concerns to an independent official prior to the IRS taking its first potentially devastating collection action.

### CDP Processes and Procedures

The IRS communicates CDP rights during two critical times. First, the IRS communicates the right to request a CDP administrative hearing with notices such as Letter 1058, *Final Notice of Intent to Levy and Notice of Your Right to a Hearing* (Notice of Intent to Levy), or Letter 3172, *Notice of Federal Tax Lien and Your Rights to a Hearing Under IRC 6320* (NFTL).<sup>14</sup> Following the CDP hearing, the IRS communicates its determination to the taxpayer via a notice of determination, such as Letter 3193, *Notice of Determination: Concerning Collection Action(s) Under Section 6320 and/or 6330 of the Internal Revenue Code* (notice of determination), which includes the right to appeal the determination to Tax Court.<sup>15</sup>

The IRS provides the taxpayer with 30 days in which to request an administrative CDP hearing.<sup>16</sup> Taxpayers who miss the 30-day deadline to request a CDP hearing may still receive an equivalent hearing within one year from the day after the date of the intent to levy notice or within one year from the day after the end of the five-business-day period following the filing of the NFTL.<sup>17</sup> It is unclear if missing the deadline to request an administrative CDP hearing in the first place is a matter of jurisdiction for the Tax Court and can be subject to equitable tolling if later litigated.<sup>18</sup>

However, if the taxpayer disagrees with the IRS's determination after the CDP hearing and wishes to appeal, he or she must file a petition with the U.S. Tax Court within 30 days of the IRS's determination.<sup>19</sup> The Tax Court has held that the 30-day filing deadline to seek judicial review under IRC § 6330(d)(1) is an issue of jurisdiction.<sup>20</sup> Without jurisdiction, the Tax Court cannot hear a case.

13 IRC § 6330(c).

14 IRS, Letter 1058, *Final Notice of Intent to Levy and Notice of Your Right to a Hearing* (Jan. 2017); IRS, Letter 3172, *Notice of Federal Tax Lien and Your Rights to a Hearing Under IRC 6320* (Mar. 2017). Notice LT11, *Notice of Intent to Levy and Notice of Your Right to a Hearing*, is sent to taxpayers whose cases are in Automated Collection System (ACS) and Letter 1058 is sent to taxpayers whose cases are assigned to Revenue Officers. This discussion will focus on Letter 1058 for the conversation regarding intent to levy notices.

15 IRS Letter L3193, *Notice of Determination: Concerning Collection Action(s) Under Section 6320 and/or 6330 of The Internal Revenue Code* (July 2018).

16 IRC §§ 6320(a)(3)(B) and 6330(a)(3)(B).

17 Treas. Reg. 301.6330-1(i)(1)(iv)(Q&A 17). The equivalent hearing will be held by Appeals and generally will follow Appeals' procedures for a CDP hearing. Appeals will not, however, issue a notice of determination, it will issue a decision letter. Also, unlike with a CDP hearing, the IRS may continue collection action while the equivalent hearing is pending, and the taxpayer cannot appeal the decision letter to Tax Court. Treas. Reg. 301.6320-1(i); Treas. Reg. 301.6330-1(i).

18 *Kim v. Comm'r.*, T.C. Memo. 2005-96. For a discussion about how the time period for filing a CDP hearing request is not an issue of jurisdiction, see Keith Fogg, *The Jurisdictional Ramifications of Where You Send a CDP Request*, TAX NOTES (Nov. 12, 2018).

19 IRC § 6330(d)(1).

20 *Weber v. Comm'r.*, 122 T.C. 258 (2004).

Furthermore, courts have held the deadline is not subject to equitable tolling, meaning the court cannot extend the deadline for any reason.<sup>21</sup>

### Scoring and Routing of Collection Cases

If a taxpayer continues to have a tax liability after being sent a series of notices from the IRS, the IRS generally assigns the liability to Taxpayer Delinquent Accounts (TDA) status.<sup>22</sup> The case is scored and routed through the IRS's Inventory Delivery System (IDS), which uses analytical scoring models and business rules to manage unresolved cases.<sup>23</sup> IDS is designed to (1) identify and filter out cases that should not be pursued further (*i.e.*, those that should be “shelved”), (2) categorize some cases as high risk (*e.g.*, those in which the period of limitations on collection will expire soon), and (3) determine whether cases should be routed to either the IRS's Automated Collection System (ACS) or Field Collection to be worked.<sup>24</sup> In FY 2018, the IDS routed 87 percent of TDA taxpayers to ACS, which is mainly responsible for responding to taxpayers' calls and sending notices, while about one percent of TDA taxpayers were sent to Field Collection, where a case can be assigned to a specific Revenue Officer.<sup>25</sup>

Shelved cases are those that the IRS sets aside without pursuing enforced collection action (such as levies).<sup>26</sup> They may continue in that status until the period of limitations on collection expires.<sup>27</sup> The liabilities of over 950,000 taxpayers were routed to the Shelf in FY 2018.<sup>28</sup> Shelved cases are still subject to systemic collection action, such as a refund offset, and the IRS is required to assign some shelved cases to a private collection agency.<sup>29</sup> Shelved cases are closed with a generic closing code, Currently

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- 21 *Duggan v. Comm'r*, Tax Ct. Docket No. 4100-15L (order dated June 26, 2015). The Court of Appeals for the Ninth Circuit affirmed the 30-day deadline is a matter of jurisdiction. *Duggan v. Comm'r*, 2018 U.S. App. LEXIS 886 (9th Cir. 2018). See National Taxpayer Advocate 2017 Annual Report to Congress 283-292 (Legislative Recommendation: *Make the Time Limits for Bringing Tax Litigation Subject to the Judicial Doctrines of Forfeiture, Waiver, Estoppel, and Equitable Tolling, and Clarify That Dismissal of an Untimely Petition Filed in Response to a Statutory Notice of Deficiency Is Not a Decision on the Merits of a Case*); The National Taxpayer Advocate reiterates her recommendation this year. See National Taxpayer Advocate 2019 Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration* (Dec. 31, 2018).
- 22 Taxpayer Delinquent Account (TDA) status applies to balance due accounts when “the taxpayer has an outstanding liability for taxes, penalties and/or interest.” Internal Revenue Manual (IRM) 19.16.4 (Oct. 10, 2012).
- 23 See IRM 5.1.20.2 (Nov. 2, 2016).
- 24 Government Accountability Office (GAO), GAO-15-647, *Collection Process Is Largely Automated, but Lacks Adequate Internal Controls* 11 (2015). For a description of ACS, see Most Serious Problem: *IRS'S Automated Collection System (ACS): ACS Lacks a Taxpayer-Centered Approach, Resulting in a Challenging Taxpayer Experience and Generating Less Than Optimal Collection Outcomes for the IRS*, *infra*. For a description of the Field, see Most Serious Problem: *Field Collection: The IRS Has Not Appropriately Staffed and Trained Its Field Collection Function to Minimize Taxpayer Burden and Ensure Taxpayer Rights Are Protected*, *infra*.
- 25 IRS, Collection Activity Report NO-5000-2 (Oct. 1, 2018) (showing the cases of 3,048,419 TDA taxpayers were sent to ACS, while the cases of 34,511 TDA taxpayers were sent to the Field).
- 26 Cases can be shelved by the Inventory Delivery System (IDS) or later on in the collection stream by ACS or Field Collection if it remains unworked.
- 27 Under IRC § 6502, the IRS must generally collect tax within ten years after assessment. Shelved cases may be reactivated in certain situations, such as when a taxpayer owes a liability in future years. IRS response to TAS information request (Oct. 17, 2018).
- 28 IRS Compliance Data Warehouse, Individual Accounts Receivable Dollar Inventory Module File (current through cycle 2018-37) (data drawn Nov. 8, 2018). The IRS maintains records of individual taxpayers' accounts on the Individual Master File (IMF). Each module on the IMF represents a specific tax liability. Taxpayers may have unpaid liabilities with respect to more than one tax year, or module.
- 29 IRC § 6306(c) generally requires the IRS to assign to private collection agencies all “inactive tax receivables,” defined as any “tax receivable” that meets any one of three criteria, including if 365 days have passed without taxpayer or third-party interaction to further collection of the account. A “tax receivable” for purposes of the statute is an account the IRS includes in “potentially collectible inventory,” a term not defined in the statute or in Treasury regulations. See Most Serious Problem: *Private Debt Collection: The IRS's Expanding Private Debt Collection Program Continues to Burden Taxpayers Who Are Likely Experiencing Economic Hardship While Inactive PCA Inventory Accumulates*, *infra*.

Not Collectible (CNC) Unproductive.<sup>30</sup> The IRS may assign a specific reason for designating a case as CNC, such as the taxpayer's economic hardship, only later in the collection process.<sup>31</sup>

### Most Serious Problems

With respect to collection, we include Most Serious Problems providing an in-depth look at concerns with the IRS's Field Collection and ACS functions, and a Most Serious Problem discussing the risks of the IRS not proactively identifying economic hardship throughout the collection process.

- **ECONOMIC HARDSHIP:** *The IRS Does Not Proactively Use Internal Data to Identify Taxpayers at Risk of Economic Hardship Throughout the Collection Process;*
- **FIELD COLLECTION:** *The IRS Has Not Appropriately Staffed and Trained Its Field Collection Function to Minimize Taxpayer Burden and Ensure Taxpayer Rights Are Protected;* and
- **IRS'S AUTOMATED COLLECTION SYSTEM (ACS):** *ACS Lacks a Taxpayer-Centered Approach, Resulting in a Challenging Taxpayer Experience and Generating Less Than Optimal Collection Outcomes for the IRS.*

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<sup>30</sup> IRS response to TAS information request (Oct. 17, 2018).

<sup>31</sup> See IRM 5.16.1.2, *Currently Not Collectible Procedures* (Sept. 18, 2018); IRM 5.16.1.2.9, *Hardship* (Sept. 18, 2018); IRM 5.15.1.17, *Making the Collection Decision* (Aug. 29, 2018).

## MSP #15 **ECONOMIC HARDSHIP: The IRS Does Not Proactively Use Internal Data to Identify Taxpayers at Risk of Economic Hardship Throughout the Collection Process**

### RESPONSIBLE OFFICIAL

Mary Beth Murphy, Commissioner, Small Business/Self-Employed Division

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to a Fair and Just Tax System*

### DEFINITION OF PROBLEM

Economic hardship, as defined in Treasury regulations and the Internal Revenue Manual, occurs when an individual is “unable to pay his or her reasonable basic living expenses.”<sup>2</sup> Congress has repeatedly emphasized the importance of protecting taxpayers experiencing economic hardship from collection actions that would exceed their ability to pay. For example, in the collection arena:

- Since 1988, Internal Revenue Code (IRC) § 6343 has required the IRS to release a levy if the IRS determines that “such levy is creating an economic hardship due to the financial condition of the taxpayer;”<sup>3</sup>
- Since 1998, IRC § 6330 has permitted a taxpayer, in a collection due process hearing, to raise the inability to pay due to hardship as a “challenge to the appropriateness of collection action;”<sup>4</sup> and
- Since 1998, IRC § 7122 has required the IRS to develop allowable living expense (ALE) guidelines to determine when an offer in compromise (OIC) is adequate and should be accepted to resolve a dispute.<sup>5</sup>

The IRS has internal data that it can use to identify taxpayers at risk of economic hardship. For example, when a taxpayer calls the IRS stating that he or she cannot pay the tax due, the IRS collection employee is able to verify some or all of the financial information provided by the taxpayer. If the employee determines the taxpayer’s ALEs exceed his income, the employee will place the taxpayer’s

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 See IRC § 6343, Treas. Reg. § 301.6343-1, and Internal Revenue Manual (IRM) 5.8.11.2.1 (Aug. 5, 2015).

3 IRC § 6343(a)(1)(D).

4 IRC §§ 6320(c), 6330(c)(2)(A)(ii).

5 IRC § 7122(d). If the allowable living expense (ALE) standards exceed the taxpayer’s income, the taxpayer is unable to pay his or her necessary living expenses. Statutory protections of taxpayers who are likely in economic hardship are available in other contexts. See, e.g., IRC § 7526, authorizing funding for the Low Income Taxpayer Clinic (LITC) grant program for taxpayers who cannot afford representation in IRS disputes (generally, those with incomes below 250 percent of the federal poverty level) and are therefore vulnerable to overreaching, and IRC § 6159(f), excusing taxpayers whose incomes do not exceed 250 percent of the federal poverty level from paying user fees to enter into installment agreements (IAs).

account into “currently not collectible (CNC) - hardship” status.<sup>6</sup> As a result, the taxpayer is protected from IRS collection action to ensure he is left with an adequate means to provide for basic living expenses.

However, despite the availability of this information and Congressional guidance to shield these taxpayers from harmful collection activity, the IRS does not *proactively* identify taxpayers likely in economic hardship throughout the collection process.<sup>7</sup> The IRS does not consider ALE guidelines in deciding which collection cases to work, although research by TAS shows that about 93 percent of payments received by the IRS in a sample group came from taxpayers with income exceeding their calculated ALEs or who have assets that can be detected through systemic means.<sup>8</sup> In fact, the IRS does not use internal data at any stage of the collection process to automatically place an indicator that the taxpayer is at risk of economic hardship.<sup>9</sup> This means that the IRS does not have a method to alert collection employees that a taxpayer may be at risk of economic hardship and, when responding to taxpayer inquiries, to ask questions about the taxpayer’s finances to determine an appropriate collection action or alternative.

The IRS’s failure to use information in its databases to consider facts and circumstances that might affect taxpayers’ ability to pay, and respond to them appropriately, violates taxpayers’ *rights to a fair and just tax system* and *to finality*. Many if not most taxpayers who cannot afford to pay their tax liabilities are likely unaware the IRS is required to halt collection action if they are in economic hardship. Thus, they may enter into payment agreements they cannot afford, including streamlined installment agreements (IAs) that do not require financial information from the taxpayer.<sup>10</sup> Furthermore, this approach causes IRS to expend resources attempting to collect from taxpayers who cannot afford to pay, and creates unnecessary rework when those taxpayers default on IAs. TAS’s research shows:

- In fiscal year (FY) 2018, about 40 percent of taxpayers who entered into streamlined IAs within the Automated Collection System (ACS) had incomes at or below their ALEs;<sup>11</sup>

6 IRM 5.16.1.2.9 (Sep. 18, 2018).

7 The IRS has internal data available to provide an initial indicator of whether a taxpayer may be at risk of economic hardship, but uses this information in very limited circumstances, such as the Low Income Indicator (LII) used to determine whether taxpayers entering into an IA are eligible for a reduced waived user fee. The LII is placed on the IRS’s internal Masterfile system, and is determined by reviewing the taxpayer’s income and exemptions on the taxpayer’s most recent tax return and comparing them with the poverty level charts created by the Department of Health and Human Services (HHS). IRM 5.14.1.2 (July 16, 2018); see also IRS response to TAS information request (Sept. 14, 2018).

8 See Research Study: *Further Analyses of “Federal Tax Liens and Letters: Effectiveness of the Notice of Federal Tax Liens (NFTL) and Alternative IRS Letters on Individual Tax Debt Resolution,”* *infra*. The National Taxpayer Advocate persuaded the IRS to conduct a study to determine if the NFTL or one of three alternative collection letters were more effective in reducing the balances owed by taxpayers. The IRS selected a random sample of about 13,000 taxpayers within ACS who generally owed between \$10,000 and \$25,000 whose liabilities were being transferred to the collection queue. TAS Research’s analysis of these cases showed that taxpayers with income exceeding their calculated ALE or who have systemically detected assets account for about 93 percent of the payments made over two years regardless of the treatment type.

9 An exception to this approach is the IRS’s automatic Federal Payment Levy Program (FPLP). At the urging of the National Taxpayer Advocate, the IRS adopted 250 percent of the federal poverty level as a proxy for identifying taxpayers likely in economic hardship for purposes of FPLP. Recipients of Social Security Administration (SSA) retirement benefits with incomes below that level are generally excluded from the FPLP program. See IRM 5.19.9.3.2.3, *Low Income Filter (LIF) Exclusion* (Oct. 20, 2016).

10 See National Taxpayer Advocate 2016 Annual Report to Congress 230-238 (Most Serious Problem: *Installment Agreements: The IRS Is Failing to Properly Evaluate Taxpayers’ Living Expenses and Is Placing Taxpayers in IAs They Cannot Afford*).

11 Due to the lapse in appropriations, Due to the lapse in appropriations, the IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process. See also Most Serious Problem: *IRS’s Automated Collection System (ACS): ACS Lacks a Taxpayer-Centered Approach, Resulting in a Challenging Taxpayer Experience and Generating Less Than Optimal Collection Outcomes for the IRS,* *infra*.

- About 39 percent of streamlined IAs within ACS involving taxpayers with income at or below their ALES defaulted in FY 2018;<sup>12</sup>
- Forty percent of taxpayers who entered into IAs while their debts were assigned to private collection agencies (PCAs) had incomes at or below their ALES;<sup>13</sup> and
- In FY 2018, the IRS placed 155,186 taxpayers in CNC-Hardship status.<sup>14</sup>

## ANALYSIS OF PROBLEM

### For Decades Congress Recognized the Need to Protect Taxpayers Who Are in Economic Hardship

Prior to 1988, IRC § 6343 authorized the release of a levy only if the IRS determined that release would facilitate collection of the tax.<sup>15</sup> Amendments to IRC § 6343 in 1988 set out conditions under which the IRS is *required* to release a levy, including when “the Secretary has determined that such levy is creating an economic hardship due to the financial condition of the taxpayer.”<sup>16</sup> Economic hardship is present “if satisfaction of the levy in whole or in part will cause an individual taxpayer to be unable to pay his or her reasonable basic living expenses.”<sup>17</sup>

Prior to 1998, there was no statutory procedure for any independent review of the IRS’s collection decision.<sup>18</sup> In 1998, Congress enacted IRC §§ 6320 and 6330 to provide for a collection due process (CDP) hearing at the administrative level and for Tax Court review of the IRS’s resulting determination—both to take place after the Notice of Federal Tax Lien (NFTL) is filed but before the IRS takes enforced collection action, such as a levy.<sup>19</sup> At the CDP hearing, taxpayers may challenge the appropriateness of the proposed collection action.<sup>20</sup> If they demonstrate they are in economic hardship, the IRS is obliged to consider alternatives, such as CNC Hardship status.<sup>21</sup>

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- 12 TAS Research analysis of the Individual Master File and Individual Returns Transaction File on IAs established in fiscal year (FY) 2018. This figure assumes taxpayers have one IRS-allowed vehicle ownership and operating expense, and a second if they were married filing jointly. As discussed below, if we assume the taxpayers did not have vehicle ownership expenses, the default rate would be about 32 percent.
- 13 See Most Serious Problem: *Private Debt Collection: The IRS’s Expanding Private Debt Collection Program Continues to Burden Taxpayers Who Are Likely Experiencing Economic Hardship While Inactive PCA Inventory Accumulates*, *infra*.
- 14 Custom analysis by TAS Research. IRS, IMF, Collection Activity Report NO-5000-149 (Oct. 11, 2018).
- 15 See Internal Revenue Code of 1954, Pub. L. No. 83-591, 68A Stat. 3 (1954). Section 6334 provided in its entirety: “It shall be lawful for the Secretary or his delegate, under regulations prescribed by the Secretary or his delegate, to release the levy upon all or part of the property or rights to property levied upon where the Secretary or his delegate determines that such action will facilitate the collection of the liability, but such release shall not operate to prevent any subsequent levy.”
- 16 See Omnibus Taxpayer Bill of Rights, Pub. L. No. 100-647, § 6236(f), 102 Stat. 3342, 3740 (1988), also known as Taxpayer Bill of Rights 1 (TBOR 1), enacting IRC § 6343(a)(1)(D).
- 17 Treas. Reg. § 301.6343-1(b)(4).
- 18 See *IRS Restructuring: Hearings on H.R. 2676 Before the S. Finance Comm.*, 105th Cong. 376, 377 (1998) (testimony of Michael Saltzman, tax attorney, White and Case).
- 19 IRS Restructuring and Reform Act of 1998 (RRA 98), Pub. L. No. 105-206, § 3401, enacting IRC §§ 6320 and 6330.
- 20 IRC §§ 6320(c), 6330(c)(2)(A)(ii).
- 21 See *Vinatieri v. Comm’r*, 133 T.C. 392, 400 (Dec. 21, 2009), in which the Tax Court held: “When a taxpayer establishes in a pre-levy collection hearing under section 6330 that the proposed levy would create an economic hardship, it is unreasonable for the settlement officer to determine to proceed with the levy which section 6343(a)(1)(D) would require the IRS to immediately release. Rather than proceed with the levy, the settlement officer should consider alternatives to the levy.”

Prior to 1998, the IRS evaluated taxpayers' abilities to pay their tax liabilities by comparing their incomes to their ALEs.<sup>22</sup> In 1998, Congress codified this practice by amending IRC § 7122 to *require* the IRS to develop ALEs "designed to provide that taxpayers entering into a compromise have an adequate means to provide for basic living expenses."<sup>23</sup> The ALE standards, also known as the Collection Financial Standards, include national and local standards, which are guidelines established by the IRS to provide consistency in certain expense allowances.<sup>24</sup> These standards determine how much money taxpayers need for basic living expenses such as housing and utilities, food, transportation, and health care, based on family size and where they live.<sup>25</sup> The National Taxpayer Advocate continues to have concerns that ALE standards fail to reflect what it truly costs to meet necessary living expenses, but ALEs can nevertheless be an important starting point to detect taxpayers at risk of economic hardship.<sup>26</sup>

### The IRS Scores and Routes Collection Cases Using Internal Data About Taxpayers

If a taxpayer continues to have a tax liability after being sent a series of notices from the IRS, the IRS generally assigns the liability to Taxpayer Delinquent Accounts (TDA) status.<sup>27</sup> The case is scored and routed through the IRS's Inventory Delivery System (IDS), which uses analytical scoring models and business rules to manage unresolved cases.<sup>28</sup> IDS is designed to (1) identify and filter out cases that should not be pursued further (*i.e.*, those that should be shelved), (2) categorize some cases as high risk (*e.g.*, those in which the period of limitations on collection will expire soon), and (3) determine whether cases should be routed to either the IRS's ACS or the Collection Field function (the Field) to be worked.<sup>29</sup> In FY 2018, the IDS routed 87 percent of TDA taxpayers to ACS, which is mainly responsible for responding to taxpayers' calls and sending notices, while about one percent of TDA taxpayers were sent to the Field, where a case can be assigned to a specific Revenue Officer.<sup>30</sup>

22 See, e.g., IRM 105.1.3 (Sept. 25, 1996), <http://core.publish.no.irs.gov/irm/p05/pdf/30353i96.pdf>; IRM 57(10)(10).1(4), *Determination of Adequate Offer* (Sept. 22, 1994), cross referencing IRM 5323 on IAs, <http://core.publish.no.irs.gov/irm/p05/pdf/35490e98.pdf>.

23 IRS Restructuring and Reform Act of 1998 (RRA 98), Pub. L. No. 105-206, § 3462, 112 Stat. 685, 764 (Jul. 22, 1998), adding subsection (c) (which is now subsection (d)) to IRC § 7122.

24 IRM 5.15.1.8 (Aug. 29, 2018).

25 See IRS, *Collection Financial Standards*, <https://www.irs.gov/businesses/small-businesses-self-employed/collection-financial-standards>. The ALEs are guidelines that "establish the minimum a taxpayer and family needs to live." The IRS may allow additional amounts for basic living expenses if the taxpayer substantiates the need to deviate from the standards. IRM 5.15.1.8 (6), *Financial Analysis Handbook: Allowable Expense Overview* (Aug. 29, 2018). Allowable expenses include transportation expenses, which may consist of ownership expenses (loan or lease payments) and operating expenses (maintenance, repairs, insurance, fuel, registrations, licenses, inspections, parking, and tolls). Unless otherwise indicated, in calculating taxpayers' ALEs, we allowed operating expenses (two allowances in the case of joint filers and one allowance for all other taxpayers), and all taxpayers were allowed one vehicle ownership expense.

26 See Research Study: *A Study of the IRS's Use of the Allowable Living Expense Standards*, *infra*.

27 Taxpayer Delinquent Account (TDA) status applies to balance due accounts when "the taxpayer has an outstanding liability for taxes, penalties and/or interest." IRM 19.16.4 (Oct. 10, 2012).

28 See IRM 5.1.20.2 (Nov. 2, 2016).

29 Government Accountability Office (GAO) GAO-15-647, *Collection Process Is Largely Automated, but Lacks Adequate Internal Controls* 11 (Jul. 2015). For a description of the ACS, see Most Serious Problem: *IRS'S Automated Collection System (ACS): ACS Lacks a Taxpayer-Centered Approach, Resulting in a Challenging Taxpayer Experience and Generating Less Than Optimal Collection Outcomes for the IRS*, *infra*. For a description of field collection, see Most Serious Problem: *Field Collection: The IRS Has Not Appropriately Staffed and Trained Its Field Collection Function to Minimize Taxpayer Burden and Ensure Taxpayer Rights Are Protected*, *infra*.

30 IRS, *Collection Activity Report NO-5000-2* (Oct. 1, 2018), (showing the cases of 3,048,419 TDA taxpayers were sent to ACS, while the cases of 34,511 TDA taxpayers were sent to the Field).

Shelved cases are those that the IRS sets aside without pursuing enforced collection action (such as levies).<sup>31</sup> They may continue in that status until the period of limitations on collection expires.<sup>32</sup> The liabilities of over 950,000 taxpayers were routed to the Shelf in FY 2018.<sup>33</sup> Shelved cases are still subject to systemic collection action, such as a refund offset, and the IRS is required to assign some shelved cases to a PCA.<sup>34</sup> Shelved cases are closed with a generic closing code, CNC-Unproductive.<sup>35</sup> The IRS may assign a specific reason for designating a case as CNC, such as the taxpayer's economic hardship, only later in the collection process.<sup>36</sup>

### The Models Used by the IRS to Score and Route Cases Do Not Adequately Identify Taxpayers Experiencing Economic Hardship

As discussed above, Congress has repeatedly directed the IRS to protect taxpayers who experience economic hardship or who cannot pay their basic living expenses. This concept is also embedded in the Taxpayer Bill of Rights.<sup>37</sup> In 2014, the Treasury Inspector General for Tax Administration found that IRS case selection criteria did not consider the financial condition of delinquent taxpayers.<sup>38</sup> Similarly, in 2015, the Government Accountability Office reviewed the IRS's case categorizing and routing process and found effectiveness was not routinely monitored.<sup>39</sup> As a result of these reports and a study by the IRS assessing the collection impact of working different types of cases, the IRS redeveloped the models used within IDS to better predict and filter unproductive cases, or cases where no payments are expected.<sup>40</sup>

While the models used in the case scoring process are designed to identify and shelve unproductive cases, they are not designed to specifically identify if a taxpayer is at risk of economic hardship.<sup>41</sup> The models do not incorporate ALEs, developed by the IRS to identify the amount of expenses "necessary to

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- 31 Cases can be shelved by the Inventory Delivery System (IDS) or later on in the collection stream by ACS or the Field if it remains unworked.
- 32 Under IRC § 6502, the IRS must generally collect tax within ten years after assessment. Shelved cases may be reactivated in certain situations, such as when a taxpayer owes a liability in future years. IRS response to TAS information request (Oct. 17, 2018).
- 33 IRS Compliance Data Warehouse, Individual Accounts Receivable Dollar Inventory Module File (current through cycle 2018-37) (data drawn Nov. 8, 2018). The IRS maintains records of individual taxpayers' accounts on the Individual Master File (IMF). Each module on the IMF represents a specific tax liability. Taxpayers may have unpaid liabilities with respect to more than one tax year, or module.
- 34 IRC § 6306(c) generally requires the IRS to assign to Private Collection Agencies (PCAs) all "inactive tax receivables," defined as any "tax receivable" that meets any one of three criteria, including if 365 days have passed without taxpayer or third-party interaction to further collection of the account. A "tax receivable" for purposes of the statute is an account the IRS includes in "potentially collectible inventory" (PCI), a term not defined in the statute or in Treasury regulations. See also Most Serious Problem: *Private Debt Collection: The IRS's Expanding Private Debt Collection Program Continues to Burden Taxpayers Who Are Likely Experiencing Economic Hardship While Inactive PCA Inventory Accumulates*, *infra*.
- 35 IRS response to TAS information request (Oct. 17, 2018).
- 36 See IRM 5.16.1.2, *Currently Not Collectible Procedures* (Sept. 18, 2018); IRM 5.16.1.2.9, *Hardship* (Sept. 18, 2018); IRM 5.15.1.17, *Making the Collection Decision* (Aug. 29, 2018).
- 37 Taxpayers' *right to a fair and just tax system* includes the right to expect the IRS consider facts and circumstances that might affect their ability to pay.
- 38 See Treasury Inspector General for Tax Administration (TIGTA), Ref. No. 2014-30-068, *Field Collection Could Work Cases With Better Collection Potential*, (Sept. 12, 2014).
- 39 See GAO, GAO-15-647, *IRS Case Selection: Collection Process Is Largely Automated, but Lacks Adequate Internal Controls* (July 2015).
- 40 Erik Miller, Stacy Orlett, and Alex Turk, IRS, *Uncollectible Versus Unproductive: Compliance Impact of Working Collection Cases That Are Ultimately Not Fully Collectible*, (2014). See also IRS response to TAS information request (Oct. 17, 2018).
- 41 IRS response to TAS information request (Oct. 17, 2018).

provide for a taxpayer's and his or her family's health and welfare and/or production of income."<sup>42</sup> Thus, taxpayers meeting the IRS's own definition of economic hardship may go undetected at the scoring phase.

### **Failing to Identify Taxpayers at Risk of Economic Hardship and Appropriately Manage Their Liabilities Throughout the Collection Process May Exacerbate Their Financial Struggles and Jeopardize Their Ability to Become Compliant**

#### *Taxpayers Experiencing Economic Hardship May Enter Into Payment Agreements They Cannot Afford*

Because economic hardship cases are not flagged at the onset of the collection process, there is no indicator to alert IRS employees that a taxpayer may be unable to pay and to consider collection alternatives. For example, if a taxpayer calls ACS in response to a threatening collection notice, a telephone assistor may not be alerted to consider collection alternatives or take a full look at the taxpayer's financial situation.<sup>43</sup> Thus, many anxious or intimidated taxpayers may enter into payment agreements they cannot afford, even though additional financial analysis would show that other collection alternatives, such as an OIC, a Partial Pay IA, or CNC-Hardship status, would be more appropriate.<sup>44</sup>

The IRS routinely undertakes collection treatments that do not require any financial analysis, including entering taxpayers into streamlined IAs. Over the last six years, nearly 4.3 million IAs have been arranged for cases assigned to ACS and about 84 percent of those IAs were streamlined—that is, entered into with no financial analysis.<sup>45</sup> Figure 1.15.1 shows a breakdown of alternative collection arrangements entered into by taxpayers in FY 2018 by all collection units, showing OICs were the least used collection alternative.

42 IRM 5.15.1.7(1) (Oct. 2, 2012). The National Taxpayer Advocate continues to have concerns over how the IRS applies ALEs in other collection activities, and believe that ALE standards should be based on costs rather than expenditures, and cover a wider range of expenses. See Research Study: *Further Analyses of "Federal Tax Liens and Letters: Effectiveness of the Notice of Federal Tax Liens and Alternative IRS Letters on Individual Tax Debt Resolution,"* *infra*; National Taxpayer Advocate 2016 Annual Report to Congress 192-202 (Most Serious Problem: *Allowable Living Expense (ALE) Standard: The IRS's Development and Use of ALEs Does Not Adequately Ensure Taxpayers Can Maintain a Basic Standard of Living for the Health and Welfare of Their Households While Complying With Their Tax Obligations*). Still, ALEs can be an important starting point to detect taxpayers that may be experiencing economic hardship.

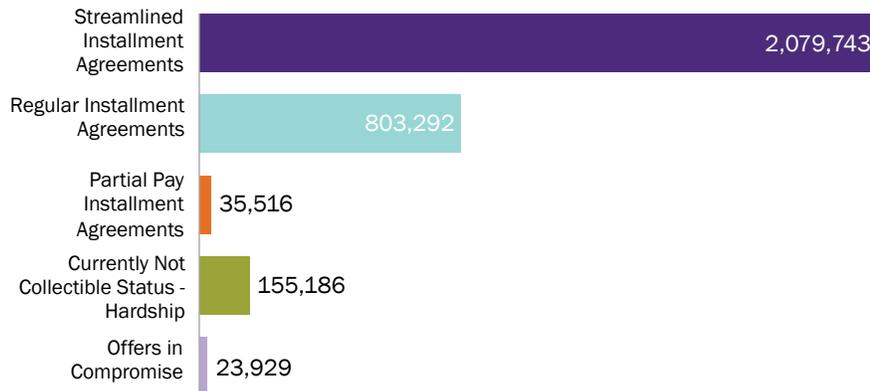
43 Failing to identify economic hardship cases is particularly a problem for cases with delinquencies assigned to ACS. See Most Serious Problem: *IRS'S Automated Collection System (ACS): ACS Lacks a Taxpayer-Centered Approach, Resulting in a Challenging Taxpayer Experience and Generating Less Than Optimal Collection Outcomes for the IRS,* *infra* ("Taxpayers are further frustrated when talking to ACS because they may be talking to an employee who is unfamiliar with their geographic circumstances, and because they may have to explain the conditions in their region over and over since ACS provides no single point of contact.").

44 A Partial Pay IA is a type of IA in which the taxpayer makes payments over the length of time remaining on the collection statute, even though these payments will not fully pay the liability. For additional discussion of concerns regarding the types of collection arrangements taxpayers enter into in ACS, see Most Serious Problem: *IRS'S Automated Collection System (ACS): ACS Lacks a Taxpayer-Centered Approach, Resulting in a Challenging Taxpayer Experience and Generating Less Than Optimal Collection Outcomes for the IRS,* *infra*.

45 There are instances where IAs maybe arranged by other Collection units than ACS. In FY 2018, streamlined IAs made up about 72 percent of total installment agreements. IRS, Collection Activity Report NO-5000-6 (Oct. 1, 2018).

FIGURE 1.15.1<sup>46</sup>

## Alternative Collection Arrangements in FY 2018



Forty percent of taxpayers who entered into a streamlined IA in ACS in FY 2018 had incomes at or below their ALEs.<sup>47</sup> These taxpayers agreed to pay their tax debts while, even by the IRS's own standards, they could not pay for their basic living expenses. These taxpayers may default on their IAs, or continue to make payments but be unable to meet what the IRS has determined are basic living expenses.<sup>48</sup> TAS research shows the default rate for streamlined IAs of taxpayers whose income was at or below their ALEs within ACS in FY 2018 was about 39 percent.<sup>49</sup>

As discussed above, shelved cases that are not designated as CNC-Hardship may be eligible for assignment to a PCA.<sup>50</sup> PCAs do not have the authority to assist taxpayers in resolving their accounts, *e.g.*, by designating the account as CNC-Hardship. PCAs may only request full payment of the liability or, if the taxpayer cannot immediately pay in full, the PCA may propose a streamlined IA.<sup>51</sup> Forty percent of taxpayers who entered into IAs while their debts were assigned to PCAs had incomes at or below their ALEs.<sup>52</sup> This result shows the grave consequences faced by taxpayers when economic hardship cases are not detected and flagged in the case scoring stage, or later as part of the process of determining which cases are sent to the PCAs.

46 IRS, Collection Activity Report NO-5000-6 (Oct. 1, 2018) (showing number of IAs); IRS, Collection Activity Report NO-5000-108 (Oct. 2, 2018) (showing number of OICs); IRS, Collection Activity Report NO-5000-149 (Oct. 11, 2018) (showing number of cases closed as CNC-Hardship).

47 See Most Serious Problem: *IRS'S Automated Collection System (ACS): ACS Lacks a Taxpayer-Centered Approach, Resulting in a Challenging Taxpayer Experience and Generating Less Than Optimal Collection Outcomes for the IRS*, *infra*.

48 The IRS does not track why IAs default, so it has no way to know how many taxpayers in streamlined IAs could no longer afford to pay.

49 TAS Research analysis of the IMF and Individual Returns Transaction File on IAs established in FY 2018. This figure assumes taxpayers have one IRS-allowed vehicle ownership and operating expenses, and only a second one if the taxpayer filed jointly with his or her spouse. As discussed below, if we assume the taxpayers did not have vehicle ownership expenses, the default rate would be about 32 percent.

50 IRC § 6306(c). Liabilities in Currently Not Collectible (CNC)-Hardship status are not selected for assignment to PCAs. An account that is assigned to a PCA and then placed in CNC-Hardship status is recalled from PCA inventory. IRS response to TAS information request (Dec. 19, 2017).

51 See IRC § 6306(b).

52 See Most Serious Problem: *Private Debt Collection: The IRS's Expanding Private Debt Collection Program Continues to Burden Taxpayers Who Are Likely Experiencing Economic Hardship While Inactive PCA Inventory Accumulates*, *infra*.

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Over the last six years, about 4.3 million Installment Agreements (IAs) have been arranged for cases assigned to Automated Collection System (ACS) and about 84 percent of those IAs were streamlined—that is, entered into with no financial analysis.

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### *Shelving Economic Hardship Cases Does Not Help Taxpayers Resolve Their Liabilities and Can Harm Future Compliance*

Taxpayers with cases shelved by the IRS receive no further communications from the IRS to resolve the liability other than an annual balance due reminder.<sup>53</sup> This means that penalties and interest will continue to accrue on the taxpayer's liability unless the taxpayer reaches out on his or her own to make a payment. Yet without any nudges from the IRS, many taxpayers may not understand the significance of their balance due and not prioritize paying it off.<sup>54</sup> This can lead to the accumulation of interest and penalties, which make the balance more difficult to pay off down the road.

Furthermore, working a case, even when it is not likely to produce full payment, produces downstream benefits by helping taxpayers become more compliant in the future. The IRS currently does not have any established measures to identify a change in compliance behavior after contact with ACS, although it intends to include behavioral tracking of how taxpayers respond to notices in its notice redesign process.<sup>55</sup> However, the 2014 “Uncollectible Versus Unproductive” study relied on by the IRS to update IDS scoring found that while working CNC cases would produce smaller payments than other types of cases, “the estimated subsequent compliance impact of working CNC cases is relatively large compared to cases without a CNC determination.”<sup>56</sup> While the National Taxpayer Advocate does not believe the IRS should pursue collection enforcement activity against taxpayers with a CNC determination, engaging these taxpayers through additional correspondence could be effective at bringing them back into compliance and should be studied in greater detail by the IRS.<sup>57</sup>

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53 IRS response to TAS information Request (Oct. 17, 2018). See also CP 71A, *Annual Reminder of Balance Due Taxes*. TAS has previously recommended that the IRS send notices at least quarterly to taxpayers with delinquent tax liabilities to collect more revenue and remind taxpayers of the accumulation of interest and penalties. See National Taxpayer Advocate Purple Book 46 (*Amend IRC § 7524 to Require the IRS to Mail Notices at Least Quarterly to Taxpayers With Delinquent Tax Liabilities*) (Dec. 31, 2017). This recommendation was adopted in the Protecting Taxpayers Act introduced by Senators Portman and Cardin. S. 3278, 115th Cong. § 201 (2018).

54 See Literature Review: *Improving Notices Using Psychological, Cognitive, and Behavioral Science Insights*, *infra*.

55 IRS response to TAS information Request (Oct. 17, 2018).

56 Erik Miller, Stacy Orlett, and Alex Turk, IRS, *Uncollectible Versus Unproductive: Compliance Impact of Working Collection Cases That Are Ultimately Not Fully Collectible*, (2014) (“Overall, 12 percent of the individual taxpayers in our study acquired an additional module with an average unpaid assessment of \$804. Cases routed to ACS with a subsequent CNC determination had the lowest percentage of subsequent modules at 8 percent.”).

57 For a discussion of the impact of additional correspondence, see Research Study: *Further Analyses of “Federal Tax Liens and Letters: Effectiveness of the Notice of Federal Tax Liens and Alternative IRS Letters on Individual Tax Debt Resolution,”* *infra*.

## The IRS Should Better Identify Taxpayers at Risk of Economic Hardship and Develop a Communications Strategy to Work With These Taxpayers Rather Than Taking Automated Collection Action

### *The IRS Should Use Internal Data to Identify Taxpayers at Risk of Economic Hardship Prior to Undertaking Collection Action*

TAS's research shows that an algorithm using internal data about a taxpayer's income and assets, and comparing that information to ALEs, can be a reliable way to predict taxpayers at risk of economic hardship. TAS evaluated a sample of 278 cases in which a taxpayer's account was closed by ACS or the Field with an IA in FY 2018—all cases in which the IRS obtained financial information from the taxpayer which showed ability to pay—and analyzed whether filtering those cases based on systemic information about a taxpayer's income and ALEs would arrive at the same result.<sup>58</sup> Only 14 cases, or five percent of the sample group, showed no ability to pay by the algorithm—meaning that TAS's algorithm arrived at the same result as the IRS employee in 95 percent of the cases. In five of the 14 cases where TAS's algorithm indicated the taxpayer had no ability to pay, the IRS employee initiated a back-up CNC determination in case the IA defaulted. This suggests that even in cases where TAS's algorithm arrived at a different result than on the financial information statement, it didn't miss by much and the IRS recognized these taxpayers could still be at risk of economic hardship.<sup>59</sup> Thus, these results indicate that the IRS could use internal data as an effective starting point in financial analysis of a taxpayer's ability to pay.<sup>60</sup>

Using an automated algorithm to proactively identify taxpayers at risk of economic hardship would allow the IRS to address these cases more appropriately, and could be used in several scenarios:

- **Case Scoring:** The algorithm could apply a marker during case scoring to show the case is at risk of economic hardship and route it a new specific group within ACS, or the “Economic Hardship Shelter.”
- **Telephone Correspondence:** The algorithm could be used to create a template for telephone assistors to view a comparison of the taxpayer's income to ALEs upon inputting the taxpayer's Social Security number. This way, if a taxpayer calls in about his or her tax liability, the assistor would be automatically alerted to ask more questions about the taxpayer's finances prior to setting the taxpayer up on an IA.<sup>61</sup>

58 TAS excluded two cases from the sample because we could not find additional information on the two cases because of an error in the data collection instrument. TAS Research estimated the income for taxpayers in these cases using the Total Positive Income (TPI) reported on the taxpayer's FY 2017 tax return. To evaluate taxpayers that may not have filed a prior-year return, TAS also considered information from third party Information Reporting Program (IRP) documents, including Forms 1099 interest, 1099 dividends, 1099 R (retirement income), 1099 B (stocks and bonds), 1099 MISC, 1099 SSA, and W-2. To incorporate assets, TAS Research looked at Form 1098 (Mortgage Interest), and real estate tax or mortgage interest paid on Schedule A. TAS calculated the amount of ALEs for each case by using the National Standards (with household size determined based on the number of exemptions claimed on the return), Local Standards (determined by the zip code on the return), Vehicle Ownership Expense, and Out of Pocket Healthcare Expenses (determined by the taxpayer's age). If the taxpayer did not file a return in a previous year, TAS allocated the lower amount.

59 The filter's computed ALE amount did not exceed the IRS's computed amount in 82 percent of the cases in our sample.

60 The IRS has expressed concern regarding the ALE determination methodology and how to address income when no income tax return is found. However, the results of TAS's research highlight the need for the IRS to study the feasibility of using internal data further and in which situations the algorithm could be beneficial.

61 While the National Taxpayer Advocate believes the flag indicating a case is at risk of economic hardship should trigger this discussion, using this template would update the information and help ensure the taxpayer's financial situation has not changed since initial case scoring.

- **Online Installment Agreements:** The algorithm could provide a warning for taxpayers entering into streamlined IAs online that they have been flagged as at risk of economic hardship, and could provide the contact number to call if they believe they cannot pay the tax debt without incurring economic hardship.
- **Automated Collection Treatments:** The algorithm could screen out taxpayers with income below their ALEs from automated collection treatments such as the Federal Payment Levy Program, selection for referral to PCAs, or for passport certification unless and until the IRS makes a direct personal contact with the taxpayer to verify the information.<sup>62</sup>
- **CNC-Hardship Review:** The algorithm could be incorporated into the IRS's systemic follow-up review of hardship cases to determine whether the taxpayer's current financial situation has positively changed and the taxpayer's case can be put back into the active inventory.<sup>63</sup>

Systemically flagging cases as at risk of economic hardship would not automatically place these taxpayers in CNC-Hardship status, but it would protect these taxpayers from further collection action until the IRS gathers sufficient financial information to make a determination.<sup>64</sup>

*The IRS Should Contact Taxpayers Likely at Risk of Economic Hardship by Letter and Create a Dedicated Phonenumber to Discuss Potential Collection Alternatives With Those Taxpayers*

Rather than leaving the case neglected while penalties and interest continue to accrue as on the shelf, the IRS should take steps to facilitate communication with taxpayers identified as at risk of economic hardship. Identified cases should be routed to a specific group within ACS, or the “Economic Hardship Shelter.” From that group, the IRS could provide:

- **Hardship Help Line:** A dedicated help line would help the IRS work with taxpayers at risk of economic hardship and collect any other information needed to make the determination that the taxpayer should be placed in CNC-Hardship status.
- **Hardship Notice:** TAS's research shows that additional, targeted contact with taxpayers can help them understand their obligations and avoid future mistakes.<sup>65</sup> The IRS should send a specific notice to educate flagged taxpayers on potential collection alternatives and resources available,

62 The House of Representatives included a provision to exclude taxpayers whose incomes are less than 250 percent of the federal poverty level from referral to a PCA in the bipartisan Taxpayer First Act, H.R. 5444, which passed the House with a recorded vote of 414-0 on April 18, 2018. A recent proposal in Congress would exclude taxpayers whose incomes are at or below 200 percent of the federal poverty level from having their debts assigned to a PCA. See House Amendment to the Senate Amendment to H.R. 88, Division B, § 1205 *Taxpayer First Act of 2018* (Nov. 26, 2018). The IRS should also continue to take steps to incorporate using TAS's retirement income calculator for FPLP. See National Taxpayer Advocate 2018 Objectives Report to Congress 80-87 (Area of Focus: *The IRS Has Improved Its Internal Guidance for Retirement Levies But More Can Be Done*).

63 IRM 5.16.1.6 (Dec. 8, 2014) (describing the two-year review process for CNC cases).

64 In FY 2018, the IRS placed 155,186 taxpayers in CNC-Hardship status in FY 2018. Custom analysis by TAS Research, IRS, IMF, Collection Activity Report NO-5000-149 (Oct. 11, 2018). About 60 percent of these cases involved taxpayers with income less than ALEs and no indication of an asset, which could have been flagged by the economic hardship algorithm at the outset of case scoring. TAS Research analysis of the IMF and Individual Returns Transaction File on IAs established in FY 2018. While taxpayers can be placed in CNC-Hardship even with income above ALEs, this data indicates that using ALEs as a filter can be an effective baseline indication of taxpayers likely to experience economic hardship.

65 See Literature Review: *Improving Notices Using Psychological, Cognitive, and Behavioral Science Insights*, *infra*; see also IRS, *Behavioral Insights Toolkit* 13, 27 (2017) (“Feedback and reminders highlight a specific piece of information to increase the chances that recipients will act on or respond to the information in a desired way.”).

including TAS and the Low Income Taxpayer Clinic (LITC).<sup>66</sup> The letter should encourage taxpayers to call the Hardship Help Line, and clearly list the number to do so.

This type of communication would show a willingness by the IRS to work with the taxpayers to meet their needs and circumstances, fulfilling taxpayer *rights to be informed* and *to quality service*, and could improve taxpayer trust in the agency.<sup>67</sup>

These communications should be *resolution-oriented*, explaining to taxpayers the risks of neglecting a tax liability and how penalties and interest can continue to accrue. To better serve taxpayers at risk of economic hardship, the IRS should partner with TAS and the LITCs to develop regular, annual training focusing exclusively on economic hardship to prepare collection employees for how to work with these taxpayers. The training should cover how to help taxpayers develop a plan to resolve the liability through collection alternatives, and highlight the appropriate use of OICs. In drafting IRC § 7211, Congress directed the IRS to make OICs more available to taxpayers to “enhance taxpayer compliance.”<sup>68</sup> The Committee Report reflects the belief that the IRS should be “flexible in finding ways to work with taxpayers who are sincerely trying to meet their obligations and remain in the tax system” and “make it easier for taxpayers to enter into offer in compromise agreements, and should do more to educate the taxpaying public about the availability of such agreements.”<sup>69</sup> Pursuing collection alternatives with taxpayers suffering economic hardship would benefit those taxpayers by helping them to resolve their liability in a way that meets their financial situation and fulfills the taxpayer *right to finality*.

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**TAS’s research shows that an algorithm using internal data about a taxpayer’s income and assets, and comparing that information to Allowable Living Expenses (ALEs), can be a reliable way to predict taxpayers at risk of economic hardship.**

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### *Flagging Economic Hardship During Case Scoring Will Allow the IRS to Avoid Rework Caused by Defaulting Installment Agreements*

TAS’s economic hardship algorithm can be an important indicator that a taxpayer *is* able to pay: in a research study by TAS, 93 percent of the payments received by the IRS in our sample group came from taxpayers with income in excess of their ALE or with an indication of an asset.<sup>70</sup> In a time of limited resources, focusing on more productive cases rather than IAs likely to default or to produce no payment

66 For additional discussion on the impact of sending collection alternative notices, see Research Study: *Further Analyses of “Federal Tax Liens and Letters: Effectiveness of the Notice of Federal Tax Liens and Alternative IRS Letters on Individual Tax Debt Resolution,”* *infra*. See also Most Serious Problem: *Pre-Trial Settlements in the U.S. Tax Court: Insufficient Access to Available Pro Bono Assistance Resources Impedes Unrepresented Taxpayers from Reaching a Pre-trial Settlement and Achieving a Favorable Outcome.,* *infra*.

67 The National Taxpayer Advocate believes the IRS should assign one ACS employee to a taxpayer’s case who is located in the same geographic region as the taxpayer so that the employee can better understand and relate to the taxpayer’s facts and circumstances. See Most Serious Problem, *IRS’s Automated Collection System (ACS): ACS Lacks a Taxpayer-Centered Approach, Resulting in a Challenging Taxpayer Experience and Generating Less Than Optimal Collection Outcomes for the IRS,* *infra*.

68 S. REP. No. 105-174, at 88 (1998).

69 *Id.* at 88-89.

70 See Research Study: *Further Analyses of “Federal Tax Liens and Letters: Effectiveness of the Notice of Federal Tax Liens and Alternative IRS Letters on Individual Tax Debt Resolution,”* *infra*.

could help the IRS avoid unnecessary rework, including time and resources to obtain an updated financial statement, reroute the case, or even issue a Notice of Federal Tax Lien determination with additional periods. Thus, proactively flagging taxpayers at risk of economic hardship would benefit taxpayers and the IRS alike. When coupled with the offer of a dedicated phone line to those taxpayers, the resulting future voluntary compliance will increase those benefits.

## CONCLUSION

The IRS must have a different approach to address taxpayers who are *unable*, as opposed to *unwilling*, to pay their tax liabilities and bring them back into compliance. The Congressional mandates for the IRS to consider whether taxpayers can meet basic living expenses in CDP hearings and OICs show a recognition of the need to protect taxpayers who are experiencing economic hardship to prevent collection actions from exacerbating that hardship further. When taxpayers enter into payment agreements they cannot afford, it violates their *right to a fair and just tax system*. Similarly, neglecting taxpayers experiencing economic hardship by simply shelving their case or potentially routing them to a PCA violates the *rights to quality service* and *to finality*.

Using internal data to compare a taxpayer's financial status to their ALEs would allow the IRS to identify taxpayers at risk of economic hardship and shield those taxpayers from potentially harmful collection actions without further financial analysis. The IRS could use this algorithm to identify cases with higher collection potential and identify taxpayers that may be suited for collection alternatives. A notice detailing the options available to the taxpayer would help make the tax liability seem less of an insurmountable obstacle, and could prompt the taxpayer to reach out to the IRS to resolve their liability. In addition, a dedicated phone line for taxpayers at risk of economic hardship would help a taxpayer determine which option is most appropriate and answer any questions. Proactively working to identify and engage taxpayers experiencing economic hardship would be an important step in developing a taxpayer-focused approach to tax administration.

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Develop and utilize an algorithm to compare a taxpayer's financial information to ALEs during IDS case scoring and as a template made available to Revenue Officers and telephone assistants responding to taxpayer inquiries.
2. Apply this algorithm before sending any cases to PCAs, and exclude any case involving a taxpayer at risk of economic hardship from potentially collectible inventory.
3. Route cases identified as at risk of economic hardship to a specific group within ACS and send those taxpayers a specific written notification to educate them on collection alternatives and additional assistance available, including TAS and LITCs.
4. Create a new help line dedicated to responding to taxpayers at risk of economic hardship and helping them determine the most appropriate collection alternative, including OICs.
5. Partner with TAS and LITCs to develop issue-focused training for IRS employees who interact with taxpayers at risk of economic hardship.

MSP  
#16**FIELD COLLECTION: The IRS Has Not Appropriately Staffed and Trained Its Field Collection Function to Minimize Taxpayer Burden and Ensure Taxpayer Rights Are Protected****RESPONSIBLE OFFICIAL**

Mary Beth Murphy, Commissioner, Small Business/Self-Employed Division

**TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Privacy*
- *The Right to a Fair and Just Tax System*

**DEFINITION OF PROBLEM**

Field Collection works cases<sup>2</sup> that have not been resolved through the notice stream or through the Automated Collection System (ACS).<sup>3</sup> In general, to resolve cases Revenue Officers can file a lien, issue a levy, seize assets, recommend suits to foreclose on a federal tax lien or reduce the tax debt to judgment. Often these cases are aged and generally involve resolution of tax debts with complex financial circumstances, the investigation and assertion of trust fund liabilities related to employment taxes, finding collection alternatives that cannot be resolved by mere levy or seizure of assets, and ensuring taxpayers are in full compliance with filing tax returns and paying taxes. In fiscal year (FY) 2018, the average age of cases with at least one unpaid assessment assigned to Field Collection was 1,203 days.<sup>4</sup> Revenue Officers are supposed to make field visits to taxpayer locations to gain a better understanding of taxpayers' financial circumstances and the economic conditions in their geographic area.<sup>5</sup> They meet with taxpayers face-to-face and assess their ability to pay the tax.

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 In Field Collection, Revenue Officers work cases, which consist of various delinquent and balance due modules. See Internal Revenue Manual (IRM) 5.1.20, *Field Collecting Procedures, Collection Inventory* (Nov. 2, 2016).

3 For an overview of the IRS collection process and information about each Collection function, see the Introduction to Collection, *infra*.

4 IRS, Compliance Data Warehouse (CDW), Individual and Business Module Accounts Receivable Dollar Inventory. Small Business/Self-Employed (SB/SE) could not confirm the reported average age of a case due to limited information provided regarding the methodology. However, the Strategic Analysis & Modeling (SAM) team came up with a similar average age of 1,353 days by conducting a series of queries for the same time frame of Individual Master File (IMF) and Business Master File (BMF) cases assigned to Status 26 during fiscal year (FY) 2018 using data from CDW's Masterfile Status History and Accounts Receivable Dollar Inventory tables.

5 See IRM 5.1.10.3, *Initial Contact* (Dec. 11, 2018); Field Compliance Embedded Quality FC Job Aid (Sept. 2017), Attribute 401, Field Visitation.

Notwithstanding their responsibility to collect tax, Revenue Officers must adhere to taxpayers' right to privacy and right to a fair and just tax system, which means, respectively, the Revenue Officer must balance the government's interest in collecting the tax with the taxpayer's interest that the collection action be "no more intrusive than necessary," and the Revenue Officer must consider the taxpayer's specific "facts and circumstances that might affect their underlying liabilities, ability to pay, or ability to provide information timely."<sup>6</sup> The current state of Field Collection has impaired the ability of Revenue Officers to fulfill their mission in accord with the TBOR.

The National Taxpayer Advocate has the following concerns:

- Revenue Officer staffing has declined by 45 percent since 2011<sup>7</sup> and therefore is not as accessible to taxpayers, and is less able to assess economic conditions on the ground;
- IRS procedures do not provide for early intervention by Revenue Officers;
- Revenue Officers are not given the appropriate tools (*e.g.*, ability to enter into offers in compromise (OICs); reduced training) to effectively collect revenue; and
- IRS metrics for evaluating the effectiveness of Field Collection are incomplete; they do not properly measure the value of first contact resolution, future voluntary compliance, prevention of economic hardship, or the education of taxpayers.

## ANALYSIS OF PROBLEM

### Background

If taxpayers do not voluntarily pay taxes assessed, the IRS may initiate collection action. The IRS will send a series of letters issued early in the life of the debt, notifying the taxpayer of the balance due and requesting payment of the full amount (this is called the "notice stream"). If the taxpayer does not pay in full or otherwise respond to the notice stream, the IRS issues a final notice of intent to levy via certified mail.<sup>8</sup> If the taxpayer does not pay within 30 days of that notice, the IRS sends a collection due process (CDP) notice that provides a taxpayer the opportunity to appeal the filing or issuance of liens or levies.<sup>9</sup>

<sup>6</sup> See IRS Pub. 1, *Your Rights as a Taxpayer* (rev. Sept. 2017).

<sup>7</sup> The number of Revenue Officers declined from 4,817 at the end of FY 2011 to 2,639 at the end of FY 2018. IRS Human Resources Reporting Center (Sept. 24, 2011 and Sept. 29, 2018). Due to the lapse in appropriations, the IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

<sup>8</sup> See IRC § 6331(d).

<sup>9</sup> See IRC §§ 6320 and 6330. For an in-depth discussion of the Collection Due Process (CDP) process, see Most Serious Problem: *Collection Due Process Notices: Despite Recent Changes to Collection Due Process Notices, Taxpayers Are Still at Risk for Not Understanding Important Procedures and Deadlines, Thereby Missing Their Right to an Independent Hearing and Tax Court Review*, *supra*.

FIGURE 1.16.1<sup>10</sup>

### Dollars Collected (including Offset) by Field Collection by Fiscal Year



The chart above shows the amounts collected by Field Collection (including via offsets from taxpayer refunds) for the five-year period from FY 2013 to FY 2017. The dollars collected by Field Collection has been relatively steady, despite the significant reduction in Revenue Officer staffing that we had mentioned. The IRS brought in over \$3 billion in FY 2018 from Taxpayer Delinquent Accounts (TDAs) assigned to Field Collection.<sup>11</sup> Additionally, nearly \$1.3 billion was collected from installment agreements attributable to Field Collection.<sup>12</sup>

Field Collection issued 439,001 levies in FY 2018.<sup>13</sup> This is a 47 percent decrease when compared to FY 2011. In FY 2018, Field Collection completed 275 seizures, down 65 percent from 776 in FY 2011.<sup>14</sup> Field Collection filed 225,852 liens in FY 2018, down 60 percent from 566,889 liens filed in FY 2011.<sup>15</sup>

10 See FY 2018: IRS, Collection Activity Report 5000-2, Taxpayer Delinquent Accounts (TDAs) (Sept. 30, 2018); FY 2017: IRS, Collection Activity Report 5000-2, TDA Report (Oct. 1, 2017); FY 2016: IRS, Collection Activity Report 5000-2, TDA Report (Oct. 2, 2016); FY 2015: IRS, Collection Activity Report 5000-2, TDA Report (Oct. 4, 2015); FY 2014: IRS, Collection Activity Report 5000-2, TDA Report (Sept. 28, 2014); FY 2013: IRS, Collection Activity Report 5000-2, TDA Report (Sept. 29, 2013).

11 The exact amount collected by Field Collection in FY 2018 was \$3,073,180,944. IRS, Collection Activity Report 5000-2 (Sept. 30, 2018); IRS, Collection Activity Report 5000-6 (Sept. 30, 2018).

12 \$1,294,794,616 was collected from installment agreements (IAs) in FY 2018. IRS, Collection Activity Report 5000-2 (Sept. 30, 2018); IRS, Collection Activity Report 5000-6 (Sept. 30, 2018).

13 IRS, Collection Activity Report 5000-24 (Oct. 9, 2018). In FY 2011, Field Collection issued 882,751 levies; IRS, Collection Activity Report 5000-C23 (Oct. 11, 2011).

14 IRS, Collection Activity Report 5000-24 (Oct. 9, 2018); IRS, Collection Activity Report 5000-C23 (Oct. 11, 2011).

15 This includes liens filed by Advisory and lien refiles. IRS, Collection Activity Report 5000-25 (Oct. 1, 2018).

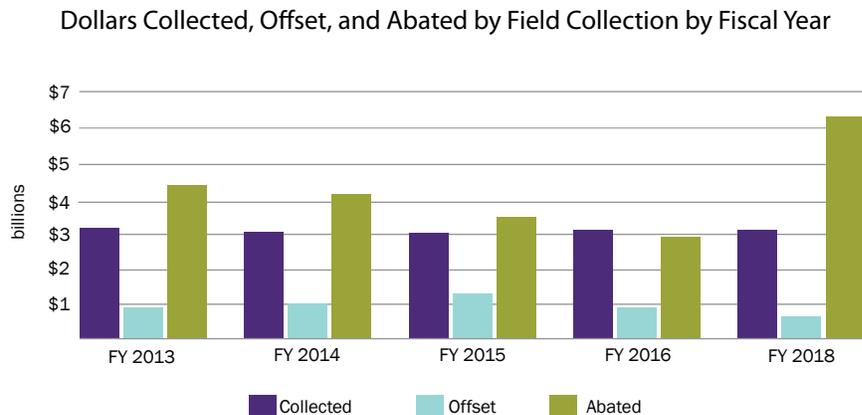
**FIGURE 1.16.2**<sup>16</sup>

Figure 1.16.2 shows the amounts abated by Field Collection from FY 2013 to FY 2018.<sup>17</sup> An abatement is a decrease in the amount of penalties or tax that is imposed upon a person.<sup>18</sup> The figure above includes partial and full abatements. Examples of abatements include abatement of the failure to file penalty, abatement of estimated tax penalty, abatement of the failure to deposit penalty, or abatement of the failure to pay penalty, and abatement of the IRS's substitute for return assessment under IRC § 6020(b). Interestingly enough, Field Collection abated more than it collected in many years.

### The Role of Field Collection

The Field Collection function is the final depot in the collection roadmap. The function relies on Revenue Officers to work all tax accounts that were not resolved in the notice stream and the ACS. Revenue Officers are charged with collecting delinquent taxes and securing unfiled tax returns from individual and business taxpayers. Aspects of a Revenue Officer's responsibilities include education, research and investigation, and, when necessary, appropriate enforcement.

One of the important roles Revenue Officers play is to educate taxpayers on their tax filing and paying obligations. Taxpayers have the right to be informed and the right to know what they need to do to comply with tax laws. They are entitled to clear explanations of the law and IRS procedures and IRS decisions about their tax accounts and to receive clear explanations of the outcomes. During their interaction with taxpayers, Revenue Officers have an opportunity to provide guidance on a wide range

16 See FY 2018: IRS, Collection Activity Report 5000-2, TDA Report (Sept. 30, 2018); FY 2016: IRS, Collection Activity Report 5000-2, TDA Report (Oct. 2, 2016); FY 2015: IRS, Collection Activity Report 5000-2, TDA Report (Oct. 4, 2015); FY 2014: IRS, Collection Activity Report 5000-2, TDA Report (Sept. 28, 2014); FY 2013: IRS, Collection Activity Report 5000-2, TDA Report (Sept. 29, 2013).

17 The National Taxpayer Advocate discusses abatements of tax in the 2016 Annual Report to Congress, recommending that the IRS determine and mitigate the factors causing such a large percent of the tax to be abated, so that resources are not wasted on assessments not due. See National Taxpayer Advocate 2016 Annual Report to Congress vol. 2, 81-102 (Research Study: *Collecting Business Debts: Issues for the IRS and Taxpayers*). The "dollars collected" only includes dollars collected from TDAs assigned to Field Collection it does not include revenue from IAs or secured returns. FY 2017 data is omitted from the graph because of a few large outliers. In FY 2017, Field Collection abated more than six times the amount it collected. IRS, Collection Activity Report 5000-2 (Oct. 1, 2017).

18 BLACK'S LAW DICTIONARY (Free Online Legal Dictionary 2nd Ed.).

of financial matters and help taxpayers take actions to resolve their tax issues. That interaction should include public outreach to provide information about the Revenue Officers' role in the collection of taxes and the policy, process, and procedures of field collection. Yet, there is no outreach function for Field Collection, or even within the SB/SE division. As of April 1, 2017, the IRS moved the Stakeholder Liaison function out of SB/SE and into headquarters Communications & Liaison.

As part of the investigative process, Revenue Officers in Field Collection are expected to meet with taxpayers (individual taxpayers and business taxpayers, or their representatives) in person to discuss and establish collection alternatives.<sup>19</sup> Such meetings may be held at the taxpayer's place of business, the taxpayer's residence, or at the representative's office.<sup>20</sup> Revenue Officers will also obtain and analyze financial information to determine the taxpayer's ability to pay the tax bill.

The majority of Field Collection cases are related to business taxpayers. At the end of FY 2018, business taxpayers comprised 53 percent of Field Collection cases.<sup>21</sup> Business cases are often more complicated, requiring time and resources to properly assess and address the business's unique compliance circumstances. This includes investigation and assertion of the trust fund recovery penalty (TFRP) on persons involved in the activities to collect, account for, and pay over taxes held in trust of employment tax.<sup>22</sup> Active businesses with employees are called in-business-trust-fund (IBTF) taxpayers. IBTF taxpayers require personal contact and, in most circumstances, a field visit.<sup>23</sup> These accounts cannot be simply resolved in the notice stream or the ACS when the issues involve more than one tax period, unfiled employment tax returns, or late federal tax deposits.

### The IRS Has Been Entrusted With Powerful Collection Powers

Congress has given the IRS some very powerful tools to bolster its collection efforts. For example, if a taxpayer has outstanding tax liabilities and has not responded to the notices to pay, the IRS may file a Notice of Federal Tax Lien or levy assets or income without first going to court and obtaining a judgment.<sup>24</sup> These are awesome collection powers granted to the IRS. For a private creditor to garnish a paycheck or attach a lien to assets, generally it would need to first go to court and obtain a judgment, while the IRS may take these actions administratively.

Using its lien and levy authorities are drastic measures that can have significant negative impact on taxpayers. Thus, before taking these measures, Revenue Officers are to check whether taxpayers are not suffering economic hardship from circumstances that would make their account "currently not collectible."<sup>25</sup>

19 See IRM 5.1.10.3.2, *Effective Initial Contact* (Nov. 20, 2017); IRM 5.1.10.3(3), *Initial Contact* (Dec. 11, 2018) ("In most cases, you should try to make initial contact with taxpayers in the field.")

20 IRM 5.15.1.2(4), *Overview and Expectations* (Aug. 29, 2018).

21 IRS, Collection Activity Report 5000-2 (Dec. 3, 2018).

22 IRC § 6672. See IRM 5.7.3, *Establishing Responsibility and Willfulness for the Trust Fund Recovery Penalty* (Aug. 6, 2015); IRM 1.2.14.1.3, *Policy Statement 5-14 (Formerly P-5-60)* (June 9, 2003); IRM 5.17.7, *Legal Reference Guide for Revenue Officers, Liability of Third Parties for Unpaid Employment Taxes* (July 18, 2012).

23 See IRM 5.1.10.3, *Initial Contact* (Dec. 11, 2018); Field Compliance Embedded Quality Field Collection (FC) Job Aid (Sept. 2017), Attribute 401, Field Visitation.

24 See IRC § 6321; IRC § 6331.

25 See IRM 5.11.1.3.1, *Pre-Levy Considerations* (Nov. 9, 2017). "Revenue Officers must exercise good judgment in making the determination to levy... If the revenue officer has sufficient information and verified that the levy would cause an economic hardship, the levy should not be issued." See also Most Serious Problem: *Economic Hardship: The IRS Does Not Proactively Use Internal Data to Identify Taxpayers at Risk of Economic Hardship Throughout the Collection Process*, *supra*.

If a Revenue Officer determines that a taxpayer is unable to pay the tax bill in full, the Revenue Officer may consider alternative means of resolving the tax debt. Such collection alternatives may include:

- Setting up an installment agreement that would allow the taxpayer to pay the bill over time;
- Recommending relief from penalties imposed when the tax bill is overdue (*e.g.*, if there is reasonable cause) or recommending adjustment or abatement if the tax debt is in doubt;
- Evaluating whether the taxpayer is a good candidate for an offer in compromise, where the IRS would accept less than the full amount of the tax liability; or
- Suspending collection due to currently not collectible accounts, which could include IBTF taxpayers.<sup>26</sup>

Because Revenue Officers are expected to engage in personal contact with taxpayers, it is important for Revenue Officers to maintain a geographic presence in the communities in which they serve.<sup>27</sup> For example, there may be circumstances unique to that community that should be taken into consideration. Having IRS employees with a geographic presence in the local community can pay dividends by making the IRS seem more relatable. TAS research studies have shown that personal contacts produce better response, resolution, and agreement rates, and result in better-educated taxpayers.<sup>28</sup>

As of December 6, 2018, there were 2,639 Revenue Officers nationwide.<sup>29</sup> Figures 1.16.3 and 1.16.4 reflect the number of Revenue Officers by state in FY 2011 and, again, in FY 2018.<sup>30</sup>

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26 Accounts may be reported currently not collectible (CNC) using closing code 13 when an operating corporation, exempt organization, or limited liability partnership can pay current taxes but cannot pay its back taxes and enforcement cannot be taken because the business has no distrainable accounts receivable or other receipts or equity in assets. See IRM 5.16.1.2(1), *Currently Not Collectible Procedures, Closing Code 13* (Sept. 18, 2018); IRM 5.16.1.2.7, *In-Business Corporations, Exempt Organizations, Limited Liability Partnerships, or Limited Liability Corporations* (Aug. 25, 2014).

27 See National Taxpayer Advocate 2017 Annual Report to Congress vol. 2, 245 (Literature Review: *Fostering Taxpayer Engagement Through Geographic Presence*).

28 See, *e.g.*, National Taxpayer Advocate 2013 Annual Report to Congress vol. 2, 15 (Research Study: *A Comparison of Revenue Officers and Automated Collection System in Addressing Similar Employment Tax Delinquencies*).

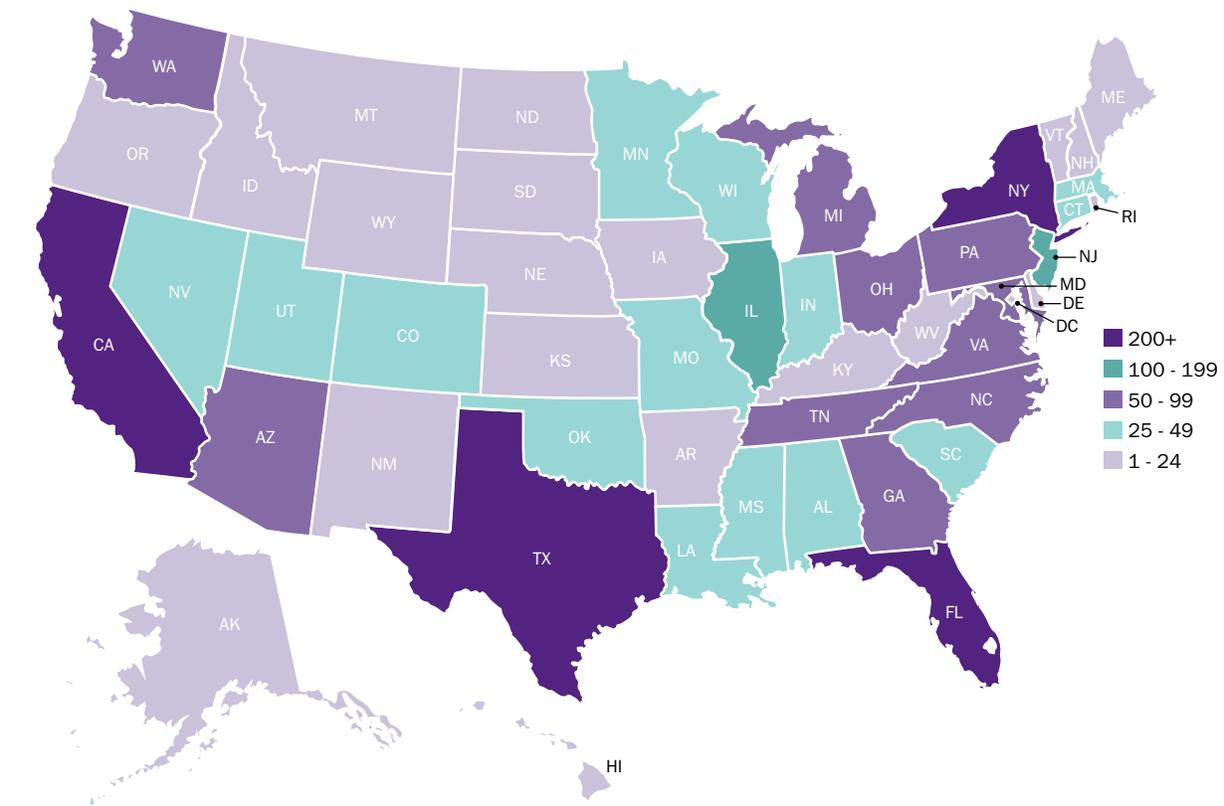
29 IRS Human Resources Reporting Center (Sept. 29, 2018). Due to the lapse in appropriations, the IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

30 Due to the lapse in appropriations, the IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.



FIGURE 1.16.4<sup>32</sup>

## Revenue Officer (RO) by State and US Possession, 2018



Field Collection has plans to hire up to an additional 750 Revenue Officers (budget permitting) in FY 2019,<sup>33</sup> but note that nearly a quarter of the current Revenue Officer cadre is eligible to retire.<sup>34</sup>

### Revenue Officers Need to Be More Accessible to Taxpayers

As Figure 1.16.5 reflects, there has been a significant reduction in the staffing of Revenue Officers over the past several years. As of the end of FY 2018, there were 2,639 Revenue Officers, down 45 percent from 4,817 Revenue Officers in FY 2011. One negative consequence of this decline in staffing is that it makes it more difficult for taxpayers to have face-to-face interaction with Revenue Officers. In less populated states, a taxpayer may be required to drive hundreds of miles to meet with the nearest Revenue Officer. Moreover, the decrease in IRS offices staffed with Revenue Officers makes it more

<sup>32</sup> U.S. Possessions with no Revenue Officers include AP, AS, GU, MH, MP, PW and Virgin Islands, U.S.

<sup>33</sup> IRS response to TAS information request (Oct. 5, 2018). Due to the lapse in appropriations, the IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

<sup>34</sup> As of January 5, 2019, 606 Revenue Officers will be eligible for retirement. Data obtained from the IRS Human Resources Reporting Center (Dec. 11, 2018). Due to the lapse in appropriations, the IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

difficult for individual Revenue Officers to understand the economic conditions in the taxpayer’s geographic area or industry—conditions that influence the taxpayer’s ability to pay the tax debt.<sup>35</sup>

In recent conversations TAS held with stakeholder groups, practitioners expressed a common frustration with the lack of responsiveness of the Revenue Officers.<sup>36</sup> Practitioners voiced concern about the difficulty in not only arranging face-to-face meetings, but even in reaching Revenue Officers via phone or having them return calls.

According to the 2019 National Agreement between the IRS and the National Treasury Employees Union (NTEU), Revenue Officers are among the positions eligible for “frequent telework”—meaning that they have regular and recurring duties that may be performed at an approved site other than the official post of duty for more than 80 hours each month.<sup>37</sup> Frequent teleworkers are still required to report to their assigned post of duty at least two days each pay period for their full tour of duty.<sup>38</sup> However, since Revenue Officers are considered “mobile workers,” they can meet that reporting requirement by performing field work in their assigned post of duty at least twice during each pay period, in lieu of coming into the office. In other words, there is no minimum amount of time required for a Revenue Officer to spend in his or her office.

With the trend of frequent teleworking and “hoteling” (a hoteling arrangement is one where teleworking employees share a single workstation on a rotating basis, rather than have a dedicated office, allowing the government to save resources), taxpayers and practitioners may continue to have difficulty reaching their assigned Revenue Officer by phone, or receiving a callback.

**FIGURE 1.16.5, “Hoteling” by Revenue Officer Groups, Calendar Year (CY) 2014 to CY 2018<sup>39</sup>**

	CY 2014	CY 2015	CY 2016	CY 2017	CY 2018 (thru June)
Revenue Officer Groups Allowing “Hoteling”	3	9	13	22	37

Field Collection has not conducted formal analysis on the impact of hoteling on Revenue Officers’ performance of duties and their interaction with taxpayers.<sup>40</sup> The trend toward more frequent hoteling of Revenue Officers may lead to reduced face-to-face office meetings, a reduced ability to accommodate walk-in or last-minute appointments, more difficulty in scheduling appointments (because of the need to adjust to the Revenue Officer’s hoteling schedule), delays in posting payments made by taxpayers,

35 Some IRS offices offer Virtual Service Delivery (VSD), where a taxpayer may interact with IRS employees via webcam. This VSD option seems like a good idea in theory, particularly for taxpayers in rural areas that may be hours away from the nearest IRS office. However, the only IRS business units that currently offer VSD capability are Field Assistance, TAS, and Appeals—and uptake has been disappointing. The technology is also challenging. With decreased Revenue Officer staffing, expanding some form of user-friendly virtual face-to-face technology to Field Collection would make it easier for taxpayers to get face-to-face contact with Revenue Officers. However, even if there is a demonstrated demand for VSD or alternative digital solutions, Field Collection should not diminish the option for traditional face-to-face interaction—there is no need for the IRS to make taxpayers choose one over the other.

36 TAS telephone calls with practitioners (Oct. 3, 2018; Oct. 10, 2018).

37 *2019 National Agreement Between IRS and NTEU*, Article 50, § 1.B.1, § 2.F.3.

38 *2019 National Agreement Between IRS and NTEU*, Article 50, § 1.A.4.

39 IRS response to TAS information request (Oct. 5, 2018).

40 *Id.*

and delays in posting tax returns. (The IRS did indicate that many offices have an “Revenue Officer of the Day” assigned to ensure that a Revenue Officer is available for unscheduled visits and to accept payments and tax returns, but such a designation would not be feasible in offices where there is just one Revenue Officer.)<sup>41</sup> The IRS recognizes that there could be issues arising from teleworking Revenue Officers and lag time in accepting payments and financial information from taxpayers. For example, IRM 5.1.2, *Field Collection Procedures, Remittances, Form 809, and Designated Payments* (Nov. 26, 2014), discusses how teleworking employees should safeguard and timely post payments and OIC receipts from taxpayers. Offices that share secretaries will face additional hurdles in ensuring there is not a significant lag time in processing such that it burdens taxpayers and infringes on their right to quality service.

While there may be a resource savings to the government for increased hoteling of its Field Collection employees, we do not know the true cost—whether there is a negative impact on taxpayer service. The IRS may offer reduced customer service by delaying some administrative duties (such as posting payments, posting returns, inputting pending installment agreements, inputting bankruptcy indicators, etc.) because Revenue Officers spend less time in the office or because support staff is shared.

### Assignment of Field Collection Cases Should Allow for Early Intervention

By the time a Revenue Officer makes contact, taxpayers may be unable to pay the debt in full because the debt has grown so large as a result of accrued penalties and interest, or because the taxpayer’s financial condition has deteriorated over time. This risk of “pyramiding” taxes and interest is especially high in IBTF cases, which account for 15 percent of Field Collection’s modules in inventory as of the end of FY 2018.<sup>42</sup> Thus, it is imperative that a Revenue Officer quickly assess the taxpayer’s situation and take early intervention measures, as appropriate

Recognizing the importance of early intervention, in June 2015, the IRS formed a Field Inventory Process Improvement Team (FIPIT) that looked at the impact of how inventory was assigned to Revenue Officers.<sup>43</sup> The “Fresh Inventory” pilot limited the assignment of inventory to Collection cases that had recent liabilities on tax periods less than three years old. The pilot applied to all individual and business tax liabilities. The goal was to have in-person contact with taxpayers as early as possible to educate them regarding compliance requirements and reduce the risk of pyramiding further, which is costly to the taxpayer.

For this Fresh Inventory pilot, cases were compared to control groups and the pilot groups generally had a higher number of full pay cases and a lower number of currently not collectible closures. The pilot groups also closed substantially more cases per Revenue Officer. This suggests that early intervention is a benefit to the taxpayer and makes it easier for the IRS to collect or otherwise resolve the case.

There are no plans to immediately implement any of the FIPIT pilots.<sup>44</sup> The results from the Fresh Inventory pilot suggest that the IRS could modify its case selection and assignment methodologies for Revenue Officers to encourage early intervention. This, in turn, would reduce taxpayer burden and increase the likelihood of the taxpayer becoming compliant in the future. The IRS should implement the approach utilized in the Fresh Inventory pilot, and explore other approaches to older inventory.

41 IRS response to TAS information request (Oct. 5, 2018).

42 IRS, Collection Activity Report 5000-2, TDA Report (Sept. 30, 2018).

43 IRS response to TAS information request (Oct. 5, 2018).

44 *Id.*

In 2014, Employment Tax engaged the Office of Research, Analysis, and Applied Statistics (RAAS) to examine the effectiveness of several potential expansions of the Federal Tax Deposit (FTD) Alert program, as part of the Early Interaction Initiative Pilot. The purpose of this initiative was “to determine the right treatment, at the right time, for the right taxpayer.”<sup>45</sup> The pilot studied the effectiveness of earlier interaction with taxpayers by first sending “soft letter notices” earlier in the quarter, to remind businesses of their obligation to make timely FTDs. The overall outcome of the FTD Early Interaction Initiative was an increase in the number and frequency of Alerts issued per quarter, and an expansion of the FTD Alert treatments into new taxpayer segments. The new taxpayer segments were businesses who needed early interaction, education, and Revenue Officer intervention.

The Early Interaction Initiative Pilot concluded in September 2016, showing some positive results. They indicated Revenue Officer field visits on IBTF taxpayers and early interaction were effective in ensuring businesses complied with FTD depository requirements. Based on the results of the pilot, Revenue Officer visits are estimated to have generated additional payments compared to a control group with no early interaction in 2017.<sup>46</sup> RAAS’s analysis is currently under review.

### Properly Evaluating the Effectiveness of Field Collection Is Difficult But Achievable

As a general rule, the IRS assigns the “easier” collection cases to Campus Collection—high volume, “fresh” cases that the IRS thinks will not involve much personal contact—while it reserves the more problematic collection cases for Field Collection. Thus, it is not possible to make an apples-to-apples comparison of the effectiveness of Campus Collection versus Field Collection by looking strictly at the revenue collected.<sup>47</sup>

The IRS measures quality through two systems—the Embedded Quality Review System (EQRS) and the National Quality Review System (NQRS).<sup>48</sup> EQRS is used to evaluate employee performance on cases and rate case actions against quality attributes.<sup>49</sup> NQRS provides independent case review information that is used to determine organizational performance. Many of the same quality attributes are used to review employee performance and assess organizational quality. The quality measurement systems evaluate Field Collection performance relative to the actions taken by Revenue Officers specific to the IRM, Collection policy, and statute, but it does *not* measure the outcome or impact of those actions to taxpayers, including if those actions resulted in undue harm or burden to taxpayers.<sup>50</sup>

Although Field Collection measures quality, it does not include such results in its Monthly Assessment of Performance (MAP) and Business Performance Review (BPR). Only the metrics shown on the MAP and BPR are used to evaluate the effectiveness of the Field Collection program.<sup>51</sup>

45 IRS response to TAS information request (Oct. 5, 2018).

46 *Id.*

47 For an in-depth look at the Automated Collection System (ACS) function, see Most Serious Problem: *IRS’s Automated Collection System (ACS): ACS Lacks a Taxpayer-Centered Approach, Resulting in a Challenging Taxpayer Experience and Generating Less Than Optimal Collection Outcomes for the IRS*, *infra*.

48 IRM 5.13.1, *Embedded Quality Field Organizations Administrative Guidelines* (Oct. 4, 2018).

49 See Field Compliance Embedded Quality FC Job Aid (Sept. 2017).

50 See IRM 21.10.1.7.12, *EQRS/NQRS Standard Reports* (Oct. 1, 2013); IRM 21.10.1.7.12.1, *Standard EQRS Reports* (May 17, 2018); IRM 21.10.1.7.12.2, *Standard NQRS Reports* (Sept. 11, 2018).

51 IRS response to the TAS information request (Apr. 26, 2018).

The Collection managers' manual has a very cursory section on taxpayer rights.<sup>52</sup> This is the section of the IRM that lists the ten rights and instructs managers to ensure rights are “always observed.” Yet there is nothing in the managers' manual discussing specific ways to uphold these rights, such as meeting with taxpayers to hear any objections that they may have.

Revenue Officers have a number of important responsibilities as they interact with taxpayers, including:

- **Identifying economic hardship.** When a taxpayer states he or she is suffering from economic hardship, has the Revenue Officer taken all the appropriate steps to protect the taxpayer from further collection action? Has the Revenue Officer been proactive about identifying economic hardship and responded promptly to taxpayers' claims of experiencing economic hardship?<sup>53</sup>
- **Preserving taxpayer rights.** Has the Revenue Officer advised the taxpayer of the Taxpayer Bill of Rights or merely handed (or mailed) the taxpayer Publication 1? The IRS should track whether these rights are being communicated from the outset of any collection case.<sup>54</sup>
- **Evaluating collection alternatives.** After the Revenue Officer obtains the taxpayer's financial information and analyzed the situation, has the Revenue Officer seriously explored all of the collection alternatives?<sup>55</sup> Has the Revenue Officer explained each of the applicable options to the taxpayer in terms the taxpayer can understand? Has the Revenue Officer seriously considered the taxpayer's objections to the proposed collection action?<sup>56</sup>
- **Taking timely actions.** While cycle time is one measurement, Revenue Officers also should be evaluated on whether they took timely actions. While timely actions are part of case quality review process, overall program metrics do not track the average timeliness of Revenue Officer actions.<sup>57</sup>
- **Impacting taxpayers' future compliance behavior.** Revenue Officers have an opportunity to make a real impact on the future compliance behavior of taxpayers with whom they interact. If the IRS tracked this behavior, even by pulling nationally representative samples annually, Revenue Officers may be more invested in making an effort to ensure that taxpayers understand the process and are aware of what is expected of them.<sup>58</sup> Taxpayers have the right to be informed of IRS decisions about their tax accounts and are entitled to clear explanations of the laws and IRS procedures. One way to fulfill this right is for Revenue Officers to conduct and participate in outreach events to inform and educate taxpayers and practitioners about the collection process.
- **Receiving proper training.** Revenue Officers should regularly receive training, not only on the technical aspects of the job but on how to effectively interact with taxpayers. Courses on financial analysis should be required of all Revenue Officers. In addition, Revenue Officers should be offered communications and psychology workshops, enhancing Revenue Officers' skills in having conversations with taxpayers when collection action is imminent. Field Collection

52 IRM 1.4.50.3.2, *Protecting Taxpayer Rights* (Aug. 21, 2018).

53 See IRM 5.11.1.3.1, *Pre-Levy Considerations* (Nov. 9, 2017).

54 See Field Compliance Embedded Quality FC Job Aid, Attribute 607 Taxpayer Rights (page 21). Also, the Integrated Collection System (ICS) contact history screen allows you to select 'Taxpayer Rights Publications.' A pick list allows for verification of Pub 1, Pub 594 and Pub 1660; at least one publication must be selected to verify this selection.

55 See Field Compliance Embedded Quality FC Job Aid, Attribute 203 Requested/Secured Financial Information 5; Attribute 432 Verify/Analyze Ability to Pay 11; Attribute 434 Research & Technical Analysis 12.

56 See IRC § 7803(a)(3)(D).

57 Field Collection has Embedded Quality metrics which cases are reviewed. See Field Compliance Embedded Quality FC Job Aid 2; Attribute 200 Timely Initial Contact 4; Timely Follow-up Actions 16; Attribute 505 Timely Employee Actions.

58 See Field Compliance Embedded Quality FC Job Aid, Attribute 437 Compliance 14; Attribute 800 Customer Impact (National Review Only) 27.

should require a course that teaches ways to balance collection with taxpayer education regarding their rights as taxpayers and their responsibilities in tax compliance and awareness of other collection alternatives—and bring in external presenters from Low Income Taxpayer Clinics or private practitioners, as well as TAS, to give Revenue Officers a sense of the taxpayer perspective.

Organizational goals can drive behavior, but only when performance metrics are aligned with those goals. By emphasizing measures such as cycle time and percent of time spent in the field,<sup>59</sup> Collection sends a message to Revenue Officers that case closures and rates of performance are more important than balancing their role in the collection of taxes and tax returns and informing taxpayers of their rights, the IRS collection process and procedures, and the importance of voluntary compliance.

### Virtual Training of Revenue Officers Is No Substitute for In-Person Training

In the National Taxpayer Advocate’s 2017 Annual Report to Congress, we reported that the IRS cut its training budget from a high of \$170 million in FY 2010 to just under \$40 million in FY 2017.<sup>60</sup> Not only has it slashed three-quarters of its training budget, but the IRS is moving away from face-to-face training and focusing its training efforts on virtual learning.

The IRS provided data on the number of training sessions it delivered over the past five fiscal years.<sup>61</sup> We reviewed what was provided and found that much of Field Collection’s training is completed virtually. In the past, Field Collection regularly delivered face-to-face training, especially for new hires. However, this is no longer the case.<sup>62</sup> In FY 2018, there were 14 times as many virtual training sessions as there were in-person training sessions.<sup>63</sup>

**FIGURE 1.16.6, Field Collection Training Sessions, FY 2014 to FY 2018<sup>64</sup>**

Fiscal Year	In-Person Sessions	Attendees	Total Hours	Virtual Sessions	Attendees	Total Hours
2014	105	2,151	15,579	1,464	78,627	201,991
2015	110	19,108	102,880	1,127	59,547	94,822
2016	10	461	16,199	137	704	1,390
2017	73	1,355	13,310	952	63,450	95,920
2018	74	20,897	58,685	1,058	47,158	45,926

59 SB/SE Business Performance Report (4th Qtr FY 2018); SB/SE Business Performance Report (3rd Qtr FY 2018).

60 National Taxpayer Advocate 2017 Annual Report to Congress 86.

61 IRS response to TAS information request (Oct. 5, 2018); IRS response to TAS information request (Nov. 7, 2017).

62 In-person attendees: FY 2014 43 new hires; FY 2015 280 hires; FY 2016 0 new hires; FY 2017 6 new hires; FY 2018 184 new hires. Virtual attendees: FY 2014 226 new hires; FY 2015 58 new hires; FY 2016 0 new hires; FY 2017 91 new hires; FY 2018 135 new hires. IRS response to TAS information request (Oct. 5, 2018); IRS response to TAS information request (Nov. 7, 2017); IRS response to TAS fact check (Jan. 30, 2019).

63 SB/SE disagreed. In its January 30, 2019, response, SB/SE asserted that there were eight times as many virtual training sessions as there were in-person training sessions. In FY 2018, there were 74 in-person person training sessions and 1,058 virtual sessions reported. Upon review of the virtual classes, 452 are Skillsoft online developmental courses. These courses are voluntary in nature and have inappropriately skewed these results. Excluding the voluntary Skillsoft developmental courses and utilizing a virtual class count of 606 (1,058 – 452).

64 IRS response to TAS information request (Oct. 5, 2018); IRS Human Capital Office response to TAS information request (Nov. 7, 2017). Due to the lapse in appropriations, the IRS did not provide a timely response to our request to verify these figures during the TAS Fact Check process.

We appreciate that there are substantial cost savings that the IRS may achieve by driving its employees to undergo virtual learning. However, the work of Revenue Officers requires the exercise of judgment and discretion. Discussions of case studies, partaking in role playing, practicing interviewing and negotiating techniques—these are skills that are vital for Field Collection employees and do not lend themselves to the virtual learning environment.

For example, TAS recommends the Financial Analysis series become a core competency course taught face-to-face.<sup>65</sup> This core competency will strengthen Revenue Officers' ability to more effectively work complex business cases<sup>66</sup> and provide them the tools to better identify and work their own OIC case versus shipping the case to an OIC Specialist who would not be familiar with the taxpayer's economic situation or geographic location.<sup>67</sup> Also, TAS recommends a new course be created, using the case study technique, on how to make an economic hardship determination including pre- and post-levy situations<sup>68</sup> and incorporating training on placing businesses into CNC status.<sup>69</sup>

## CONCLUSION

Revenue Officers have a difficult task. They are assigned collection cases that are aged and often require a great deal of legwork. Yet the trend is for Revenue Officers to receive less in-person training. Field Collection can help Revenue Officers become more effective by assigning them more recent cases (so Revenue Officers can make more of an impact via early intervention measures, as demonstrated by several recent pilot programs), by making them available to meet taxpayers face-to-face or respond timely to taxpayer calls, by encouraging Revenue Officers to conduct educational programs in their communities, and by changing how it evaluates Revenue Officers.

65 Financial Analysis series would include the following courses: (1) Basic Financial Analysis for Wage Earners; (2) Basic Financial Analysis for the Self-Employed (schedule C filer; emphasis on understanding bank statement info, P&L statement with comparison to Schedule C); (3) Financial Analysis for Flow-through Entities (emphasis on understanding the income statement and balance sheet); and (4) Financial Analysis of C-corporations and consolidated entities.

66 Field Collection reported that only 37 Revenue Officers in FY 2018 attended a financial analysis course. See IRS response to the TAS information request (Oct. 5, 2018).

67 IRM 5.8.5, *Offer in Compromise, Financial Analysis* (Mar. 23, 2018); IRM 5.1.2.5.6.2, *Processing Offer in Compromise Receipts* (Sept. 26, 2014).

68 IRM 5.1.12.20.1.1, *Make an Economic Hardship Determination* (Aug. 5, 2014); IRM 5.11.1.3.1, *Pre-Levy Considerations* (Nov. 9, 2017); IRM 5.11.2.3.1.4, *Economic Hardship* (Apr. 15, 2014). See also IRM 5.16.1.2.9, *Hardship* (Sept. 18, 2018).

69 IRM 5.16.1.2.7, *In-Business Corporations, Exempt Organizations, Limited Liability Partnerships, or Limited Liability Companies* (Aug. 25, 2014), specifically that accounts can be reported CNC using closing code 13 if such organizations can pay current taxes but cannot pay back its back taxes and enforcement cannot be taken because the business has no distrainable accounts receivable or other receipts or equity in assets. Only 3,273 cases were closed as CNC using closing code 13 (hardship for businesses) in FY 2018. IRS, CDW, Business Master File.

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Formally evaluate the impact on taxpayers of hoteling Revenue Officers—for example, is there any quantifiable harm to taxpayers due to the lag time in responding to taxpayer or practitioner calls or appointments, or in posting payments and tax returns, installment agreements, and OICs?
2. Implement lessons from the “Fresh Inventory” pilot to modify its case selection and assignment methodologies for Revenue Officers to focus on early intervention that educate taxpayers on compliance, resolve cases timely, and promote future voluntary compliance.
3. Implement the Early Interaction Initiative to ensure business taxpayers are in compliance with and educated on the federal tax deposit requirements for employment taxes.
4. Issue a policy for a “Revenue Officer of the day” in all field offices, except offices with only one Revenue Officer, so every taxpayer, wherever they are located in the country, receives the same quality service. Such a policy would help ensure that payments and tax returns are posted timely, correspondence and questions are responded to timely, and face-to-face meetings are available.
5. Promote taxpayers’ future compliance by Revenue Officers conducting and participating in outreach events that provide information on policy and procedures of Field Collection and the role of Revenue Officers in the collection of taxes and voluntary tax compliance.
6. Establish a quality measurement system that measures (using a statistically valid sample) the future voluntary compliance impact of Field Collection actions, including if those actions resulted in undue harm or burden to taxpayers.
7. Grant Revenue Officers the authority to work Offer in Compromise cases.

**MSP  
#17****IRS'S AUTOMATED COLLECTION SYSTEM (ACS): ACS Lacks a Taxpayer-Centered Approach, Resulting in a Challenging Taxpayer Experience and Generating Less Than Optimal Collection Outcomes for the IRS****RESPONSIBLE OFFICIAL**

Mary Beth Murphy, Commissioner, Small Business/Self-Employed Division

**TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Finality*
- *The Right to Privacy*
- *The Right to Confidentiality*
- *The Right to Retain Representation*
- *The Right to a Fair and Just Tax System*

**DEFINITION OF PROBLEM**

The Automated Collection System (ACS) is a major IRS computerized collection inventory system used to send notices demanding payment, and to issue notices of federal tax liens (NFTLs) and levies. ACS employees also answer taxpayer telephone calls to resolve balance due accounts and delinquencies. ACS relies on mailed notices to generate taxpayer contact. In fiscal year (FY) 2018, this approach resulted in ACS only collecting about seven percent (\$3.4 billion) of the \$47 billion placed in its inventory.<sup>2</sup>

Just as important as the dollars collected is the process followed by the IRS collection function, including ACS. The dollars collected are the byproduct of the compliance work that ACS employees *should* be doing—namely, understanding the cause of the current tax debt, curing the current tax debt by looking at appropriate collection alternatives, and ensuring that these collection alternatives enable the taxpayer to be compliant going forward.

However, ACS is drifting from this philosophy by suppressing the systemic issuance of ACS taxpayer notices and by considering redesigned notices that place a heavy emphasis on self-service channels and, in some circumstances, enforcement action as well. This undermines four cardinal taxpayer rights: *the*

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 IRS, Small Business/Self-Employed (SB/SE), Collection Activity Report (CAR) NO-5000-2, Taxpayer Delinquent Account (TDA) Cumulative Report, Part 1 - TDA's, Automated Collection System (ACS)/CS, Receipts (line 11.19), Credits (Line 13.0) (Sept. 2018). The amount collected in fiscal year (FY) 2018 is from TDAs received in FY 2018 as well as from the dollars remaining in ACS inventory at the end of FY 2017.

*right to be informed, the right to privacy* (IRS action be no more intrusive than necessary); *the right to a fair and just tax system* (considering the specific facts and circumstances); and *the right to challenge the IRS's position and be heard* (which means to talk with and listen to taxpayers).

As a result, the National Taxpayer Advocate continues to have a number of concerns regarding ACS operations, including:

- Despite a recent study that shows monthly notices are productive in generating contact with the taxpayer, ACS has suppressed the issuance of taxpayer notices to prevent a poor level of service (LOS) on its phone lines and is considering redesigned notices that push taxpayers towards self-service channels.
- ACS routinely enters taxpayers into streamlined installment agreements (IAs) which do not require any financial analysis, thereby missing opportunities to have discussions with taxpayers about their financial situations and assist them in finding the best collection alternatives for their particular facts and circumstances. This is evident by the 22 percent overall default rate for streamlined IAs in FY 2018,<sup>3</sup> and the 42 percent default rate for streamlined IAs of taxpayers whose income was at or below 250 percent of the federal poverty level (FPL) for the same time period.<sup>4</sup>
- ACS employees still do not properly observe the holding in *Vinatieri v. Commissioner*,<sup>5</sup> even though it is nearly ten years old.
- When taxpayers raise economic hardship, these discussions may be unfruitful because taxpayers do not have one single point of contact in ACS, and taxpayers may be speaking to ACS employees who are not familiar with the geographic region in which they reside.
- ACS may not be identifying the most productive cases to work but, instead, may be addressing cases that are better suited for field collection.

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3 IRS CAR, *Installment Agreement (IA) Default Report*, FY 2018.

4 TAS Research used the following source to analyze ACS and installment agreement accounts for FY 2018: IRS CAR, *Installment Agreement (IA) Default Report*, FY 2018.

5 *Vinatieri v. Comm'r*, 133 T.C. 392 (2009).

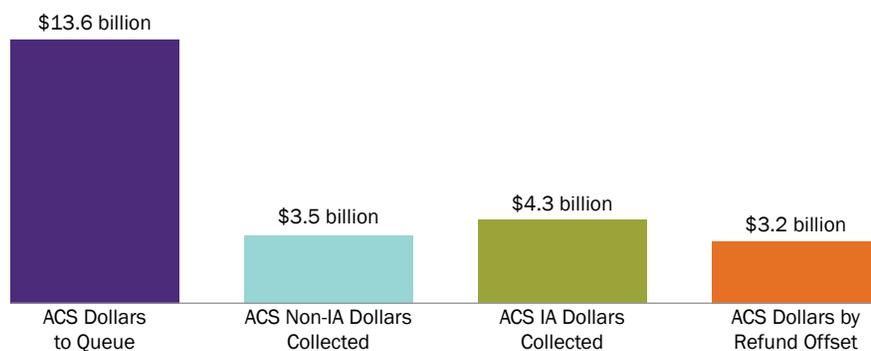
## ANALYSIS

### Background

At the end of FY 2018, ACS had about \$47 billion placed in its inventory and it collected about \$3.4 billion of that amount during the same time period, or about seven percent.<sup>6</sup> About \$4.3 billion was collected through IAs.<sup>7</sup> In FY 2018, ACS transferred \$13.6 billion, or 29 percent of inventory placed with ACS in FY 2018, in unresolved cases to the Queue.<sup>8</sup> Figure 1.17.1 shows dollars collected through full payment, IA, refund offset, and dollars transferred to the Queue for FY 2018.

**FIGURE 1.17.1<sup>9</sup>**

**Automated Collection System (ACS) Dollars Collected by Source and Dollars Transferred to the Queue for FY 2018**



As Figure 1.17.1 shows, ACS transfers about twice as many dollars to the Queue as it collects, and collects about half as many dollars through refund offsets as it does through IAs or other payments.

One possible response to ACS's performance may be to increase the use of its collection authority, namely, the issuance of liens and levies. However, Figure 1.17.2 shows there is little correlation between total revenue collected by the IRS and an increase in notices of federal tax liens and levies issued.

6 CAR 5000-2 (Oct. 1, 2018).

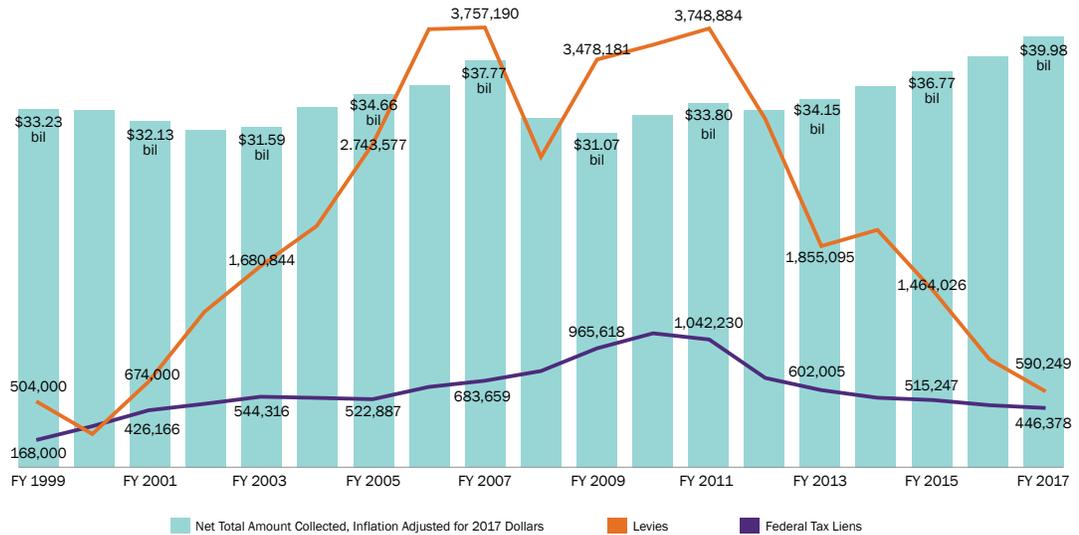
7 CAR 5000-6 (Oct. 1, 2018). IRS response to TAS fact check (Dec. 13, 2018). This amount is limited to accounts in taxpayer delinquent account (TDA) status and that are placed in ACS inventory.

8 CAR 5000-2 (Oct. 1, 2018). The Queue is an electronic holding area for accounts that will not be worked immediately. See Internal Revenue Manual (IRM) 1.4.50.8.3 (Sept. 12, 2014).

9 CAR 5000-2 (Sep. 30, 2018); CAR 5000-6 (Sep. 30, 2018).

FIGURE 1.17.2<sup>10</sup>

ACS Liens and Levies and IRS Dollars Collected From Fiscal Years 1999-2017



What Figure 1.17.2 demonstrates is that taxpayers tend to pay their tax debts, irrespective of the level of enforced collection actions. Thus, rather than focusing solely on increasing enforcement actions, ACS should focus on how to best reach taxpayers, how to get taxpayers into the most appropriate collection alternatives, and what are the best cases to focus these efforts on. However, as the discussion below shows, ACS appears to be moving in the opposite direction.

### Despite a Recent Study That Shows Monthly Notices Are Productive, ACS Has Suppressed the Issuance of Taxpayer Notices to Prevent a Poor Level of Service on Its Phone Lines and Is Considering Redesigned Notices That Push Taxpayers Towards Self-Service Channels

Despite a recent study that shows monthly notices are productive in generating contact with the taxpayer, ACS has suppressed the issuance of taxpayer notices to prevent a poor LOS on its phone lines and is considering redesigned notices that push taxpayers towards self-service channels.

An IRS study regarding NFTLs found that regular monthly notices to taxpayers regarding their liabilities were generally more effective than any other reminder notices included in the study as an effective collection mechanism.<sup>11</sup> Specifically, a monthly notice brought in more money than any

10 IRS Data Book, Table 16, *Delinquent Collection Activities FYs 1999-2017*. Note that the dollars collected in this figure are IRS-wide dollars collected, and not just dollars collected by ACS. This does not include FY 2018 dollars because the FY 2018 IRS data book with this data is not yet published.

11 See Research Study: *Further Analyses of "Federal Tax Liens and Letters: Effectiveness of the Notice of Federal Tax Liens and Alternative IRS Letters on Individual Tax Debt Resolution"*, *infra*. This study compares the monthly notice to other reminder notices sent but does not compare the monthly notice to the Notice of Federal Tax Lien. See also Consumer Financial Protection Bureau, *Quarterly Consumer Credit Trends, Public Records* (Feb. 2018). Recently, the three major credit reporting agencies—Equifax, TransUnion, and Experian—announced they would no longer report tax liens on a taxpayer's credit report.

other reminder notice included in the study. Sending a monthly notice that shows tax due plus accrued penalties and interest would be more reflective of a private company's collection practices and more in line with tax collection approaches in other countries.<sup>12</sup> However, rather than adding additional notices, ACS has recently suppressed the systemic issuance of the LT16, *Request for Taxpayer to Contact ACS*. This suppression was done to decrease the number of taxpayers calling ACS, to prevent a projected LOS of 31 percent for FY 2018<sup>13</sup> (although better than projected, the LOS on ACS phone lines was still a dismal 63 percent during filing season (FS) 2018).<sup>14</sup> Nevertheless, improvements to LOS should not be achieved by taking steps that discourage taxpayers from contacting the IRS.

Two recent IRS studies considered whether redesigned notices would be more effective than notices either currently or previously used by ACS.<sup>15</sup> These studies, however, were largely focused on how notices can push taxpayers to use self-service channels such as the Online Payment Agreement (OPA) or Voice Balance Due (VBD).<sup>16</sup> In fact, the redesigned notices emphasized the availability of self-service channels while reducing the visual prominence of the telephone contact number. Not surprisingly, these notices resulted in a reduction in the number of taxpayers calling that number when compared to the LT16, which was the Control notice. However, taxpayers who received the redesigned notices were more likely to call an IRS number that they found through other means, such as using a phone book or the Internet. Specifically, even though the Control group notice resulted in the greatest number of total inbound calls, the redesigned notices all resulted in a greater number of inbound calls using phone numbers found through other means, when compared with the Control notice.<sup>17</sup>

Similar to the LT16 study, a study conducted on the CP14 Notice, *Balance Due of \$5 or More, No Math Error*, placed a high emphasis on pushing taxpayers towards self-service channels and limiting the cost to the IRS by reducing the number of inbound calls the notices generate. However, the study correctly acknowledges that different types of notices may be appropriate for different types of taxpayers. The study further points out that when taxpayer responses to notices are markedly different depending on the size of their balance or the age of their debt, the IRS could use this information to treat different taxpayer groups with specific notices. Tailoring notices to unique taxpayer characteristics could increase

12 *Introduction to Behavioral Economics for CDM Applications and Best Practices for Bill Design*, BEWorks (2016), [beworks.com/assets/pdfs/BEworks\\_Energy\\_Sector\\_Report.pdf](http://beworks.com/assets/pdfs/BEworks_Energy_Sector_Report.pdf); OECD, Tax Administration, *Insights from Innovations In Tax Debt Management* 158 (2017), [http://dx.doi.org/10.1787/tax\\_admin-2017-en](http://dx.doi.org/10.1787/tax_admin-2017-en); FORBES, *A Better Way to Collect Bills From Customers Without Alienating Them* (Mar. 31, 2017), <https://www.forbes.com/sites/elizabethharris/2017/03/31/a-better-way-to-collect-bills-from-customers-without-alienating-them/#21aca8162c2f>.

13 IRS response to TAS fact check (Dec. 13, 2018).

14 ACS CFO Financial Management, *Office of Cost Accounting, Cost-Based Performance Measures FY 2012-2017*, 2. This level of service was due in part to the eight million telephone calls that ACS assumed from Accounts Management in 2016.

15 However, the Urgent notice still resulted in fewer calls than the Control notice. IRS, *ACS Optimization/Research, Applied Analytics, and Statistics (RAAS) ACS LT16 Notice Redesign Test Pilot Report 23-24* (Sept. 27, 2017).

16 IRS, *ACS/RAAS ACS LT16 Notice Redesign Test Pilot Report 20* (Sept. 27, 2017). Online Payment Agreement (OPA) is a portal on the IRS.gov website where taxpayers can login and establish an IA. Voice Balance Due (VBD) is an interactive telephone system that allows taxpayers to use a touchtone keypad to take action. Both OPA and VBD are self-service channels that taxpayers can use independently without the assistance of an IRS employee.

17 IRS, *ACS Optimization/RAAS ACS LT16 Notice Redesign Test Pilot Report 22-23* (Sept. 27, 2017). For example, taxpayers who received the Control notice made 980 calls to the phone number printed on the notice (Kansas City ACS site) and 934 calls to other IRS telephone numbers—yielding a total of 1,914 phone calls, the most of any notice. While all of the redesigned notices resulted in fewer total phone calls, with reductions of 12 percent to 33 percent relative to the Control Group, they all resulted in more telephone calls to numbers not printed on the notice compared to the Control Group.

compliance and dollars collected.<sup>18</sup> Going forward, IRS should further explore what types of notices generate the best result for particular taxpayers.<sup>19</sup>

Both of the redesign studies discussed above omitted two significant characteristics that should be included in IRS collection notices. First, notices should include the name and phone number of an individual ACS employee. Taxpayers are more likely to respond to notices when they feel like the notice is coming from an actual person whom they can contact regarding their tax problem.<sup>20</sup>

A second element that should be present is a focus on taxpayer rights. Notices should be designed within a taxpayer rights framework and identify the taxpayer rights relevant to the particular notice. For example, a monthly reminder notice about a taxpayer's outstanding liability could start out by saying, "Under the Taxpayer Bill of Rights, you have the *right to quality service* and *the right to be informed*. In an effort to observe these rights, we want to keep you informed of the amount you currently owe the IRS. You also have the *right to a fair and just tax system*, where all the facts and circumstances of your situation are considered, so if you are unable to pay the amount due because of a financial hardship, please contact us at ...." Designing notices within a taxpayer rights framework will educate taxpayers as to what rights are relevant to their current situation and will ensure taxpayers are informed about what rights they can exercise during this particular IRS interaction.

### **ACS Routinely Enters Taxpayers Into Streamlined Installment Agreements Which Do Not Require Any Financial Analysis, Thereby Missing Opportunities to Have Discussions With Taxpayers About Their Financial Situations and Assist Them in Finding the Best Collection Alternatives for Their Particular Facts and Circumstances**

Beginning in 2012, the IRS expanded the availability of streamlined IAs,<sup>21</sup> which do not require financial analysis. More specifically, these IAs are based purely on mathematical equations. For instance, the liability is divided by as many as 84 months (seven years), which establishes the taxpayer's monthly payment.<sup>22</sup> Over the last six years, 4,285,773 IAs has been arranged for cases assigned to ACS and about 84 percent of those IAs were streamlined.<sup>23</sup> In FY 2018, 40 percent of ACS taxpayers who entered into streamlined IAs had income that fell below the allowable living expenses (ALE) threshold, meaning they agreed to pay on their tax liability while likely jeopardizing their ability to pay their basic

18 IRS, *Small Business/Self-Employed SB/SE Collection & RAAS CP14 Notice Redesign Test Pilot Report 15-20* (April 12, 2018).

19 *Id.* at 29 (April 12, 2018). Future research should attempt to isolate the impact of specific behavioral elements by designing notices that test a smaller number of discrete changes.

20 See American Bar Association, *Nudging and Educating Taxpayers to Comply: Reevaluating Traditional Approaches to Taxpayer Compliance 20, 22, 29-40* (May 2018), [https://www.americanbar.org/content/dam/aba/events/taxation/meetingmaterials/18may\\_materials/18may-ift-nudgingandeducationg-villalobos-slides.authcheckdam.pdf](https://www.americanbar.org/content/dam/aba/events/taxation/meetingmaterials/18may_materials/18may-ift-nudgingandeducationg-villalobos-slides.authcheckdam.pdf).

21 IRS, IR-2012-31, *IRS Offers New Penalty Relief and Expanded Installment Agreements to Taxpayers under Expanded Fresh Start Initiative* (Mar. 7, 2012). See also National Taxpayer Advocate 2012 Annual Report to Congress 358-357 (*Introduction to Collection Issues: The IRS "Fresh Start" Initiative Has Produced Significant Improvements in Some Collection Policies; However, Significantly More Emphasis on Service Delivery Is Necessary to Realize the Full Benefits of These Important Changes*).

22 IRS, *Streamlined Processing of Installment Agreements*, <https://www.irs.gov/businesses/small-businesses-self-employed/streamlined-processing-of-installment-agreements> (last visited Nov 15, 2018).

23 There are instances where installment agreements may be arranged by other collection units than ACS.

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## Improvements to the level of service should not be achieved by taking steps that discourage taxpayers from contacting the IRS.

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living expenses.<sup>24</sup> Thirty-two percent of these also had income at or below 250 percent of the FPL for FY 2018.<sup>25</sup>

Unsurprisingly, while the overall default rate for streamlined IAs in FY 2018 was 19 percent,<sup>26</sup> the default rate for streamlined IAs of taxpayers whose income did not exceed their ALEs, was 39 percent.<sup>27</sup>

Despite having various pieces of information indicating that a taxpayer is low income, and having a low income indicator that is placed on accounts with gross income at or below 250 percent of the FPL,<sup>28</sup> the IRS generally does not initiate a discussion about economic hardship with the taxpayer.<sup>29</sup> The IRS should create a template that ACS employees can use which would fill in the Information Return Program (IRP) income, and utilize the family size from the last tax return, and then compare the information to the ALE standard. If there is no recent return on file, the ACS employee could complete the template by asking the taxpayer for their income and family size, then based on this information, could determine how to proceed. If the taxpayer is in fact experiencing economic hardship as determined by completing the template, the ACS employee should open up a discussion regarding

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- 24 See IRS, *Collection Financial Standards*, <https://www.irs.gov/businesses/small-businesses-self-employed/collection-financial-standards> (last visited Dec. 19, 2018). The allowable living expenses (ALEs) are guidelines that “establish the minimum a taxpayer and family needs to live.” The IRS may allow additional amounts for basic living expenses if the taxpayer substantiates the need to deviate from the standards. IRM 5.15.1.8 (6), *Allowable Expense Overview* (Aug. 29, 2018). Allowable expenses include transportation expenses, which may consist of ownership expenses (loan or lease payments) and operating expenses (maintenance, repairs, insurance, fuel, registrations, licenses, inspections, parking, and tolls). Unless otherwise indicated, in calculating taxpayers’ ALEs, we allowed operating expenses (two allowances in the case of joint filers and one allowance for all other taxpayers), and all taxpayers were allowed one vehicle ownership expense.
- 25 CAR, *IA Default Report, FY 2018*. See also Most Serious Problem: *Private Debt Collection: The IRS’s Expanding Private Debt Collection Program Continues to Burden Taxpayers Who Are Likely Experiencing Economic Hardship While Inactive PCA [Private Collection Agency] Inventory Accumulates*, *supra*. Forty-four percent of taxpayers who made payments while their debts were assigned to PCAs had incomes below 250 percent of the federal poverty level. One possible explanation as to why this figure is higher than the 29 percent ACS figure is that ACS is making the decision to not work cases where the taxpayer has low income but rather places them in the Queue where they will later be shelved and sent to the PCAs.
- 26 CAR, *IA Default Report, FY 2018*.
- 27 IRS CAR, *IA Default Report, FY 2018* for the default rate information for streamlined IAs, and TAS Research analysis of the ACS and IA accounts, FY 2018, for results on percentage of streamlined IAs whose income did not exceed their ALEs who defaulted.
- 28 According to IRM 5.14.1.2, *Installment Agreements and Taxpayer Rights* (July 16, 2018), taxpayers entering into IAs are eligible for a reduced or waived user fee if they meet a certain income level. Eligibility is based on the Low-Income Indicator (LII) and Reduced User Fee Indicator (RUF). The LII is placed on the IRS’s internal Masterfile system, and is determined by reviewing the taxpayer’s income and exemptions on the taxpayer’s most recent tax return and comparing them with the poverty level charts created by the Department of Health and Human Services (HHS). If the taxpayer is low income according to HHS standards, a LII will be placed on Masterfile showing that they are eligible for a reduced user fee. A LII can also be placed on the taxpayer’s account if a review of Form 13844, *Application for Reduced User Fee*, reports such a designation. See also IRS response to TAS information request (Sept. 14, 2018). An income-based LII is placed on accounts that are at or below 250 percent of the federal poverty level depending on household size and state of residence.
- 29 IRM 5.19.13.2, *Securing Financial Information* (June 23, 2017). ACS employees will only take financial information if the taxpayer raises one of the following issues: Payment amount requested is insufficient based on current Streamlined Installment Agreement (SIA) criteria and the balance is over a certain amount; Follow paragraph (17) below if the amount is over a certain amount; Aggregate Assessed Balance (AAB) (Command Code (CC) SUMRY) is over \$25,000 (and taxpayer does not meet SIA Over \$25,000 criteria); Partial Payment Installment Agreement (PPIA) is being considered, or Cannot Pay Any Amount Currently Not Collectible (CNC).

offers in compromise or Currently Not Collectible (CNC)/hardship status. If the ACS employee and the taxpayer cannot agree on a resolution, the ACS employee should refer the taxpayer to TAS.

Further, if the completion of the template shows that the taxpayer's income is at or below 250 percent of the FPL, the ACS employee should refer the taxpayer to a Low Income Taxpayer Clinic (LITC).<sup>30</sup> Currently, the Internal Revenue Manual (IRM) instructs employees to advise taxpayers that they might be eligible for LITC assistance in completing a financial statement.<sup>31</sup> This guidance should be expanded to advise customer service representatives (CSRs) to inform all low income taxpayers of the existence of LITCs in their state (or nearby if there is not one in their state).<sup>32</sup>

### ACS Employees Still Do Not Properly Observe the Holding in *Vinatieri v. Commissioner*, Even Though It Is Nearly Ten Years Old

Not only does ACS fail to start conversations about taxpayers' financial situations, or specifically refer them to an LITC, but TAS has learned that, in some instances, ACS does not even properly observe the spirit of the Tax Court holding in *Vinatieri v. Commissioner*, which held that when the IRS sustains even a *proposed* levy on a taxpayer it knows is in economic hardship, it abuses its discretion.<sup>33</sup> For example, TAS was recently made aware of a situation where the ACS CSR refused to place a welfare recipient into CNC hardship status because the taxpayer had an unfiled return from a previous year.<sup>34</sup> The *Vinatieri* case, in which the Tax Court held that it was an abuse of discretion for the IRS to proceed with a levy against a taxpayer who has unfiled returns if the taxpayer has demonstrated economic hardship, is now nearly ten years old. Thus, there is no reasonable explanation for why any ACS employee should be unwilling to place a taxpayer in CNC hardship because of unfiled returns. The IRS has had nearly a decade to develop adequate, regular training that clearly educates its employees on this vital Tax Court holding.

### When Taxpayers Raise Economic Hardship, These Discussions May Be Unfruitful Because Taxpayers Do Not Have One Single Point of Contact in ACS, and Taxpayers May Be Speaking to ACS Employees Who Are Not Familiar With the Geographic Region in Which They Reside

Taxpayers are not assigned one ACS employee to their case, and will likely speak to a different person each time they call in. This can waste taxpayers' valuable time and needlessly tie up IRS phone lines. Furthermore, miscommunication can cause even more problems down the road, yet again forcing both the IRS and the taxpayer to commit more time to resolving this particular issue. In 1998, Congress directed that the IRS develop a procedure "to the extent practicable and if advantageous to the taxpayer"

30 See Most Serious Problem: *Economic Hardship: The IRS Does Not Proactively Use Internal Data to Identify Taxpayers at Risk of Economic Hardship Throughout the Collection Process*, *supra*.

31 IRM 5.19.17.1.7(4), *Campus Procedures for Currently Not Collectible and Offers in Compromise* (Sept. 18, 2018).

32 These bills grant IRS employees the authority to refer taxpayers' information regarding low income taxpayer clinics. H.R. 5438, 115th Cong. § 1 (2017-2018); S. 3278, 115th Cong. § 503 (2017-2018).

33 *Vinatieri v. Comm'r*, 133 T.C. 392 (2009). IRC § 6343(a)(1)(D) requires the IRS to release a levy when it would create an economic hardship due to the financial condition of the taxpayer. Treas. Reg. § 301.6343-1(b)(4) specifies that an economic hardship exists if a taxpayer cannot pay his or her basic living expenses. See also Most Serious Problem: *Economic Hardship: The IRS Does Not Proactively Use Internal Data to Identify Taxpayers at Risk of Economic Hardship Throughout the Collection Process*, *supra*.

34 On June 7, 2018, the Low Income Taxpayer Clinic Listserv had a post regarding ACS employees being unaware of the holding in *Vinatieri*.

to assign one IRS employee to handle a taxpayer's matter until it is closed.<sup>35</sup> One concern surrounding the adoption of a single-point-of-contact approach for ACS may be that is not feasible because the employee may be unavailable. However, if the IRS provided effective "first contact resolution", which would include using the auto-populated economic hardship template discussed above, the number of repeat callers needing to speak to the same ACS employee would be reduced. Further, if the taxpayer calls back and the employee isn't available, the taxpayer can be given a choice: would you like to receive a callback from your assigned ACS CSR, or wait for the next available CSR? Implementing Congress' guidance in IRS Restructuring and Reform Act of 1998 (RRA 98) would enhance taxpayer's communication with ACS by improving continuity, quality taxpayer service, and effective tax administration.

Another significant problem with the design of how ACS manages its cases is that there is no coordination between where the taxpayer resides and the location of the ACS site to which the taxpayer's account is assigned. For instance, a taxpayer who resides in the mid-Atlantic may have his or her case assigned to the ACS site in Des Moines, Iowa. This is problematic because the ACS employee is likely unaware of the particulars of that region, such as cost of living, local industry, and the effect of local natural disasters. For example, ACS employees located in Des Moines, Iowa, may be unfamiliar with and unaware of the long-lasting effects of a natural disaster such as Hurricane Sandy.

### **ACS May Not Be Identifying the Most Productive Cases to Work but Instead May Be Addressing Cases That Are Better Suited for Field Collection**

ACS cases are prioritized by categories high, medium, and low based on modeling scores and a collection potential calculation that calculate the probability of case resolution and compliance. High-priority cases are pushed to the top of the rankings to be worked first by ACS customer service representatives in the "next case" process. However, previous studies have shown that flaws in ACS case prioritization models may exist, and cases it deems low priority may actually yield a higher return on investment (ROI) than cases deemed high priority.<sup>36</sup> During the 2006-2009 IRS private debt collection program, the IRS repeatedly stated that it would not choose to work the private collection agency (PCA) inventory if it had additional resources because the "next best case" criteria it used prioritized other cases, such as older cases with higher balances due.

However, a TAS study that compared the two years that PCAs worked cases to the subsequent two years that ACS worked the same cases showed that the IRS was significantly more effective than the PCAs in collecting tax liabilities in all but the first six months after case receipt.<sup>37</sup> Specifically, the IRS collected about 62 percent more than the PCAs (\$139.4 million compared to \$86.2 million).<sup>38</sup> In addition to

35 IRS Restructuring and Reform Act of 1998 (RRA 98), Pub. L. No. 105-206 § 3705(b), 112 Stat. 685, 777 (1998). Additionally, Congress has recently endorsed a single-point-of-contact customer service approach by requiring that one IRS employee be assigned to each identity theft case. H.R. 5439, 115th Cong. § 1 (2018).

36 IRS response to TAS information request (Sept. 14, 2018). Since the time of these studies, the IRS has implemented a different prioritization system. It ranks cases by high-medium-low in a prioritization process. Defaulted IAs are not a prioritized inventory.

37 We compared PCA and IRS collections during four consecutive six-month intervals following case receipt. See National Taxpayer Advocate 2013 Annual Report to Congress vol. 2, *A Comparison of Revenue Officers and the Automated Collection System in Addressing Similar Employment Tax Delinquencies* 97-107.

38 National Taxpayer Advocate 2013 Annual Report to Congress vol. 2 97-107 (Study: *A Comparison of Revenue Officers and the Automated Collection System in Addressing Similar Employment Tax Delinquencies*). Since the time of this study, ACS has changed its method for prioritizing cases. Thus, the IRS should conduct a study similar to that cited here, applying its new case prioritization method.

demonstrating that hiring PCAs is an ineffective way to collect outstanding tax liabilities,<sup>39</sup> this study also shows that the IRS's assumptions as to what cases are more or less productive was flawed. Another TAS study showed that the cases that are in ACS might yield better results if placed elsewhere in the IRS's collection function. For example, a TAS research study pertaining to employment tax liabilities showed that the Collection Field Function (Cff) collected more dollars and resolved delinquencies more quickly than ACS, regardless of the size of the delinquency. Further, ACS transferred more tax modules, particularly medium- and high-dollar modules (over \$1,500), to the queue and Cff, reducing the IRS's speed and effectiveness in addressing them,<sup>40</sup> thus indicating these employment tax cases may be best suited for initial placement in Cff rather than in ACS.

As mentioned above, ACS prioritizes its cases using modeling scores and a collection potential calculator that calculates the probability of the case resolution and compliance. Surprisingly, however, these modeling scores do not prioritize cases where the taxpayer has previously entered into an IA but have since defaulted on the installment payment.<sup>41</sup> Logically, the IRS should rank cases where there is a defaulted IA as high priority since the taxpayer has previously engaged with the IRS to make arrangements to settle his or her outstanding tax liability. The IRS could categorize these cases as high priority and quickly contact the taxpayer after he or she has defaulted on the IA, stating something to the effect of, "We noticed you recently stopped making payments on your installment agreement and the agreement has been defaulted. We wanted to see if your financial circumstances have changed and if your prior installment agreement could be modified to bring you back into compliance." Since the IRS knows that such taxpayers have the desire to resolve the outstanding liability, it only makes sense that their cases should be moved to the top of the heap.<sup>42</sup> Accordingly, ACS likely can collect more revenue by taking a closer look at how it prioritizes cases and the assumptions on which this prioritization is based.

## CONCLUSION

ACS's emphasis on pushing taxpayers towards self-service channels in its redesigned notices risks alienating taxpayers who either do not have access to such channels, or do not feel comfortable using such channels. When a taxpayer contacts ACS, it should use all the information at its fingertips to consider the taxpayer's unique situation and to suggest resolution options that may best suit that individual taxpayer. Taxpayers are further frustrated when talking to ACS because they may be talking to an employee who is unfamiliar with their geographic circumstances, and because they may have to explain the conditions in their region over and over since ACS provides no single point of contact. Finally, it is critical that ACS use its resources effectively by ensuring it is working the most productive cases. These changes would result in better experiences for taxpayers and better collection outcomes for the IRS.

39 For a more in-depth discussion of the problems facing the IRS's current PDC program, see Most Serious Problem: *Private Debt Collection: The IRS's Expanding Private Debt Collection Program Continues to Burden Taxpayers Who Are Likely Experiencing Economic Hardship While Inactive PCA Inventory Accumulates*, *infra*.

40 National Taxpayer Advocate 2013 Annual Report to Congress vol. 2 16-31.

41 IRS response to TAS information request (Sept. 14, 2018).

42 See OECD, *Working Smarter in Tax Debt Management* 42 (2014), [http://www.keepeek.com/Digital-Asset-Management/oecd/taxation/working-smarter-in-tax-debt-management\\_9789264223257-en#page1](http://www.keepeek.com/Digital-Asset-Management/oecd/taxation/working-smarter-in-tax-debt-management_9789264223257-en#page1).

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Assign one ACS employee to a taxpayer's case, provide this employee's contact information on each notice that is sent to the taxpayer, and assign the case to an ACS employee who is located in the same geographic region as the taxpayer.
2. Send out monthly notice reminders to taxpayers regarding their tax liabilities and accrued penalties and interest.
3. Revise ACS notices using a Taxpayer Bill of Rights framework that conspicuously informs taxpayers of the rights impacted by a given notice.
4. Apply an indicator to cases in which the taxpayer is likely experiencing economic hardship and route these cases to a separate Economic Hardship Shelter excluded from assignment to private collection agencies.
5. Revise ACS's Internal Revenue Manual and scripts to instruct employees when a taxpayer has an economic hardship indicator placed on their account, to consider all possible avenues for resolution, including Partial Payment Installment Agreements, offers in compromise, or placement into Currently Not Collectible hardship status.
6. Conduct a research study to determine if IRS's modeling scores and collection potential calculator are truly identifying the cases that are most likely to be resolved.
7. Reorder ACS protocols to give high priority to cases where a taxpayer has defaulted on a prior installment agreement.

**MSP  
#18****OFFER IN COMPROMISE: Policy Changes Made by the IRS to the Offer in Compromise Program Make It More Difficult for Taxpayers to Submit Acceptable Offers****RESPONSIBLE OFFICIALS**

Mary Beth Murphy, Commissioner, Small Business/Self-Employed Division  
Donna Hansberry, Chief, Office of Appeals

**TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Quality Service*
- *The Right to Finality*
- *The Right to Privacy*
- *The Right to a Fair and Just Tax System*

**DEFINITION OF PROBLEM**

An offer in compromise (OIC) is an agreement between a taxpayer and the government that settles a tax liability for payment of less than the full amount owed. Congress grants the IRS the authority to accept offers pursuant to Internal Revenue Code (IRC) § 7122.<sup>2</sup> To its credit, the IRS has engaged in an outreach campaign to make the OIC a more visible collection tool. For instance, it has worked to develop electronic newsletters, IRS Tax Tips, and social media for both taxpayers and tax professionals to use.<sup>3</sup>

With a robust and flexible OIC program, the IRS receives money that it might not have collected through other means and achieves voluntary tax compliance from the taxpayer (at least for the next five years, which is long enough to create a long-term change in noncompliant behavior).<sup>4</sup> If the taxpayer does not follow the terms of the agreement, the OIC defaults and the debt is reinstated.<sup>5</sup> The taxpayer benefits by reaching finality with his or her tax debt sooner in the collection process and paying what he or she can afford to pay, while the IRS benefits by creating a segment of noncompliant taxpayers who become more compliant.

A 2017 study by TAS Research found that individual taxpayers (Individual Master File (IMF)) with accepted OICs were significantly more likely (58 percent compared to 42 percent) to timely file their subsequent income tax returns for the next five years when compared to taxpayers whose OICs the IRS did not accept. For the first five years after the OIC, IMF taxpayers with accepted OICs were also much

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 Treas. Reg. § 301.7122-1(b).

3 IRS response to TAS information request (Aug. 20, 2018).

4 IRS, Form 656-B, *Offer in Compromise* 6 (Jun. 2018).

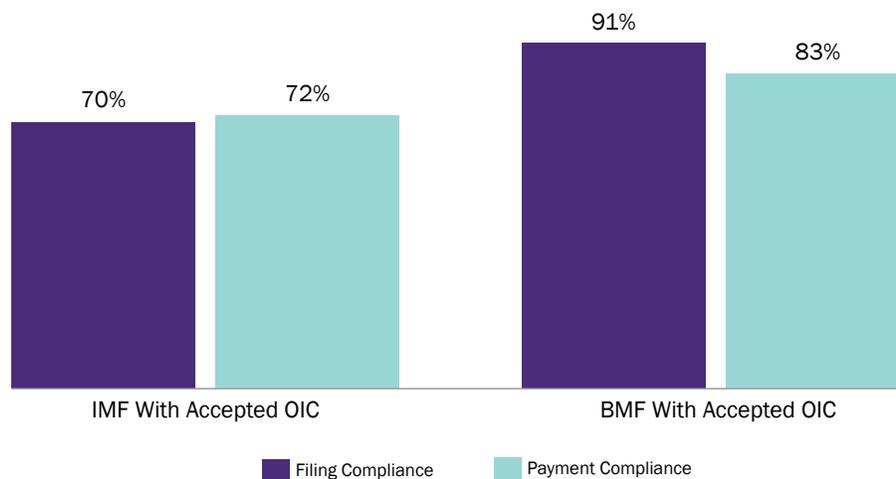
5 Internal Revenue Manual (IRM) 5.8.9.4, *Potential Default Cases*, (Jan. 12, 2017).

more likely to pay their subsequent income taxes than taxpayers whose OICs the IRS did not accept (72 percent compared to 52 percent).<sup>6</sup>

In 2018, TAS Research studied business taxpayers (Business Master File (BMF)) with OICs. It found that BMF taxpayers with accepted OICs have a better filing rate than IMF taxpayers five years out. Figure 1.18.1 shows that while 70 percent of IMF taxpayers with an accepted OIC file their returns five years after an accepted OIC, 91 percent of BMF taxpayers with an accepted OIC do so five years out.<sup>7</sup> BMF taxpayers also have better future payment compliance. Approximately 72 percent of IMF taxpayers with accepted OICs had no balance due five years after an accepted OIC compared to 52 percent of IMF taxpayers without an accepted OIC.<sup>8</sup> Approximately 83 percent of BMF taxpayers had no balance due five years after an accepted OIC compared to 75 percent of BMF taxpayers with no accepted OIC.<sup>9</sup>

**FIGURE 1.18.1**

**IMF and BMF Filing and Payment Compliance for Five Years  
After an Offer in Compromise Is Accepted**



6 National Taxpayer Advocate 2017 Annual Report to Congress vol. 2, 43 (Research Study: *A Study of the IRS Offer in Compromise Program*).

7 *Id.*; Research Study: *A Study of the IRS Offer in Compromise Program for Business Taxpayers* vol. 2, *infra*. For the purposes of the Business Master File (BMF) study, TAS Research focused on partnerships, corporations, or sole proprietors.

8 National Taxpayer Advocate 2017 Annual Report to Congress vol. 2, 55; See Research Study: *A Study of the IRS Offer in Compromise Program for Business Taxpayers*, *infra*.

9 Research Study: *A Study of the IRS Offer in Compromise Program for Business Taxpayers* vol 2, *infra*.

The IRS is also losing revenue collection opportunities because it uses inflated projections of reasonable collection potential (RCP). In about 40 percent of the BMF OICs that were not accepted, the OIC amounts offered are much higher than the amounts ultimately collected through other means.

Notwithstanding the clear benefits of entering into OICs, the National Taxpayer Advocate is concerned that the IRS is not doing enough to help BMF taxpayers file successful OICs. Additionally, the IRS has made changes that create barriers to all taxpayers from submitting successful OICs:

- The IRS moved away from having revenue officers (ROs) available to work OICs in each state;
- OICs submitted by taxpayers who had not filed all necessary tax returns are returned to the taxpayers as not processable, rather than holding them for a period to allow for return filing;
- The IRS will keep the payments sent with OICs it returns for lack of filing compliance;
- OICs returned to the taxpayer in error are not subject to the 24-month deemed acceptance period in IRC § 7122(f); and
- The time it takes to process OICs, including any appeals, may lead to multiple years of refund offsets.

## ANALYSIS OF PROBLEM

### Background

Treasury Regulations provide three grounds for an OIC:

- Doubt as to liability;<sup>10</sup>
- Doubt as to collectibility;<sup>11</sup> and
- Effective tax administration.<sup>12</sup>

The law requires two things before the IRS can deem an OIC processable. First, an OIC submission must include a partial payment (referred to as a Tax Increase Prevention and Reconciliation Act or “TIPRA” payment).<sup>13</sup> Second, the taxpayer must pay any applicable user fee.<sup>14</sup> Additionally, Treasury Regulations require taxpayers to make the OIC in writing, sign the OIC under penalty of perjury, and include all of the information “prescribed or requested by the Secretary.”<sup>15</sup> If an OIC meets the

10 Treas. Reg. 301.7122-1(b)(1). Doubt as to liability exists where there is a genuine dispute as to the existence or amount of the correct tax liability under the law. Doubt as to liability does not exist where the liability has been established by a final court decision or judgment concerning the existence or amount of the liability.

11 Treas. Reg. 301.7122-1(b)(2). Doubt as to collectibility exists in any case where the taxpayer’s assets and income are less than the full amount of the liability.

12 Treas. Reg. 301.7122-1(b)(3). There are two grounds for effective tax administration offers: 1) If the Secretary determines that, although collection in full could be achieved, collection of the full liability would cause the taxpayer economic hardship within the meaning of Treas. Reg. § 301.6343-1 and; 2) If there are no grounds for an offer under the other offer in compromise (OIC) criteria, the IRS may compromise to promote effective tax administration where compelling public policy or equity considerations identified by the taxpayer provide a sufficient basis for compromising the liability. Compromise will be justified only where, due to exceptional circumstances, collection of the full liability would undermine public confidence that the tax laws are being administered in a fair and equitable manner.

13 IRC §§ 7122(c)(1), 7122(d)(3)(C). For lump sum offers, the partial payment must be 20 percent of the OIC amount. For a periodic payment OIC, the partial payment must consist of the first installment payment. IRC § 7122(c)(1)(A)–(B).

14 IRC § 7122(c)(2)(B). The application fee is currently \$186. If an individual taxpayer qualifies for the low income waiver, he or she will not be required to send any payment with the OIC. IRS, Form 656-B, *Offer in Compromise* (Jun. 2018).

15 Treas. Reg. § 301.7122-1(d)(1).

minimum criteria for consideration, the IRS deems it processable.<sup>16</sup> Prior to April 13, 2016, IRS procedures dictated that if any of the following criteria were present, the IRS would determine an OIC as not processable:

- The taxpayer is in bankruptcy;
- The taxpayer did not submit the application fee with the OIC;<sup>17</sup>
- The taxpayer failed to submit the initial payment with the OIC;<sup>18</sup>
- All liabilities have been referred to the Department of Justice;<sup>19</sup>
- The OIC is filed for an unassessed liability and internal information does not indicate that a return has been filed;
- The OIC is filed solely with respect to liabilities for which the statutory period for collection has expired; and
- The taxpayer marks the total amount of the payment as a deposit.<sup>20</sup>

When the IRS determines that an OIC is not processable, it returns the OIC to the taxpayer with a letter explaining the reason for the IRS's determination.<sup>21</sup> With a not-processable returned OIC, the IRS *may* return the application fee and initial payment to the taxpayer.<sup>22</sup> A rejected OIC differs from a returned OIC in that the IRS has reviewed the facts of the case prior to rejection, and the taxpayer receives appeal rights when the OIC is rejected.<sup>23</sup> The IRS will keep payments made on rejected OICs.<sup>24</sup>

### Every Revenue Officer Should Be Able to Process an OIC

Taxpayers submitting an OIC today can expect that the IRS will work their OIC at one of two Centralized OIC sites or in one of two OIC field territories. The revenue officers (ROs) in the field groups are spread across 22 states.<sup>25</sup> ROs who work OICs are referred to as OIC Specialists.<sup>26</sup> Previously, the Special Procedures Function investigated all OICs. As OIC receipts increased, Field ROs worked OICs for a short period time prior to the establishment of specialized Field OIC groups in fiscal year (FY) 1996.<sup>27</sup>

OICs have gone from being something worked by all ROs to something worked in two territories. This consolidation of work is not beneficial to the analysis of OICs, which often must take particular facts and circumstances into account, much of which can be affected by the taxpayer's geography. The IRS

16 IRM 5.8.2.4.1 (May 25, 2018). Centralized OIC employees make the initial determination of processability. *Id.*

17 In lieu of the application fee, a taxpayer may check the low income waiver box on Form 656, which would allow him or her to submit the offer without payment.

18 If the OIC includes part of the initial payment, the OIC may be perfected during the case building process. IRM 5.8.2.4.1 (May 25, 2018).

19 The IRS does not have authority to accept an OIC that is controlled by the Department of Justice. IRM 5.8.1.6.1 (Nov. 8, 2018).

20 This does not include instances where the taxpayer checks the low income waiver box. IRM 5.8.2.3.1(1) (July 28, 2015).

21 IRM 5.8.2.5, *Not Processable* (May 25, 2018).

22 *Id.*; IRM 5.8.7.2, *Returns* (Oct. 07, 2016).

23 IRM 5.8.7.7, *Rejection* (Oct. 7, 2016).

24 IRS, Form 656, *Offer in Compromise 5* (Mar. 2018).

25 Territory 1 has OC Specialists in 10 states and Territory 2 has OC Specialists in 12 states that are not covered in the ten by Territory 1. IRS, *Human Resources Reporting Center*, <https://persinfo.web.irs.gov/> (last visited Oct. 17, 2018).

26 IRS response to TAS information request (Apr. 26, 2018).

27 IRS response to TAS information request (Aug. 20, 2018). In 2005 the Field OIC groups were consolidated into three Areas. *Id.*

should revert back to having a greater geographic presence for OIC Specialists and have at least one OIC Specialist (if not more) in each state. One benefit of having a Field RO work an OIC is that the RO is knowledgeable and familiar with the particular community, its economy, and related issues in which he or she works. However, between FYs 2013 and 2018 there was a ten percent decrease in OIC Specialists (there were 145 OIC Specialists in FY 2013 and 131 as of FY 2018.)<sup>28</sup> The National Taxpayer Advocate previously discussed the issue of decreasing numbers and lack of geographic dispersion of OIC Specialists.<sup>29</sup>

### The IRS Is Not Doing Enough to Help Business Taxpayers File Successful OICs

The National Taxpayer Advocate is concerned that the IRS is not doing enough to accept OICs from BMF taxpayers.<sup>30</sup> In 2018, TAS Research built on a previous study of IMF OICs by focusing on BMF OICs. Overall, the acceptance rate for BMF OICs (24 percent) is lower than the rate for individual OICs (44 percent).<sup>31</sup>

While the IRS may be concerned that IMF and BMF taxpayers use the OIC process to delay collection action, data from TAS research indicates that BMF taxpayers generally want to submit a successful OIC. Of the BMF taxpayers who submitted an OIC, approximately 11 percent churned (churning occurs when a taxpayer submits another OIC within 180 days after the IRS rejects the prior OIC or returns it as not processable).<sup>32</sup> Of the BMF taxpayers that churned, approximately 33 percent ultimately had an OIC accepted.<sup>33</sup> Figure 1.18.2 shows the churning rate based on business type.

**FIGURE 1.18.2, Average Churning and Accepted OICs for BMF Taxpayers by Business Type Between 2007 and 2017**<sup>34</sup>

BMF Type	Total OICs	Percent Churning	Percent Churning With Accepted OIC
Corporation	20,963	11%	23%
Sole proprietor	12,009	12%	44%
Partnerships	4,283	11%	28%

28 IRS response to TAS information request (May 25, 2018).

29 See National Taxpayer Advocate 2014 Annual Report to Congress 211; National Taxpayer Advocate 2002 Annual Report to Congress 15.

30 See, e.g., 2014 National Taxpayer Advocate Annual Report to Congress 206-217.

31 Research Study: *A Study of the IRS Offer in Compromise Program for Business Taxpayers* vol. 2, *infra*.

32 *Id.* Additionally, the National Taxpayer Advocate believes the word “churn” has negative connotations for taxpayers trying to perfect their OICs. Instead, such taxpayers should be viewed as “curing” a defect in the OIC.

33 *Id.*

34 *Id.* The entity type of 7,965 businesses is unknown. Corporations filed 20,963 OICs between 2007 and 2017 with 2,386 churned OICs. Of those churned OICs, the IRS ultimately accepted 548 OICs. Sole proprietors filed 12,009 OICs between 2007 and 2017 with 1,482 OICs churning. Of those churned OICs, the IRS ultimately accepted 640 OICs. Partnerships filed 4,283 OICs between 2007 and 2017 with 501 churned OICs. Of those churned OICs, the IRS ultimately accepted 138 OICs. Because sufficient time has not elapsed to determine if all 2017 OICs churned, churning percentages do not include OICs submitted in 2017.

In the 2017 OIC study, TAS Research looked at rejected OICs by individual taxpayers between 2009 and 2013 and determined that the IRS frequently overestimated RCP.<sup>35</sup> The RCP is calculated by the IRS after reviewing the taxpayer’s financial information and in many instances will serve as the basis for an acceptable OIC amount.<sup>36</sup>

In 2018, TAS Research looked at BMF OICs and again determined that the IRS is losing some revenue collection opportunities because of inflated RCPs connected to rejected OICs and OICs that were returned due to an imperfection. Overall, the OIC amount offered for returned or rejected BMF OICs was often less than what was ultimately collected. However, in about 40 percent of the BMF OICs that were not accepted, the OIC amounts offered are much higher on average than the amounts ultimately collected through other means. For instance as seen in Figure 1.18.3, for the 4,347 returned or rejected corporation OICs, the average amount offered was \$34,695, but the IRS ultimately collected an average of \$53,990.<sup>37</sup> However, 1,766 (over 40 percent) of those returned or rejected corporation OICs offered *more* than what the IRS ultimately collected. In those 1,766 OICs, the average amount offered was \$49,920 and the average amount ultimately collected was just \$16,189.<sup>38</sup> This trend is consistent across all business types.

**FIGURE 1.18.3, Amounts Offered and Collected for All Returned or Rejected Offers From Corporations Compared to Returned or Rejected Offers From Corporations Where the Offer Amount Was Greater Than Payment<sup>39</sup>**

All Returned/Rejected Corp. Offers				
	Count	Mean	Median	Total
Offered	4,347	\$34,695	\$48,000	\$150,818,185
Collected		\$53,990	\$11,084	\$206,024,907
Returned/Rejected Corp. Offers with Offer > Payment				
	Count	Mean	Median	Total
Offered	1,766	\$49,920	\$12,000	\$88,159,029
Collected		\$16,189	\$1,766	\$28,589,014

Furthermore, Figure 1.18.4 focuses on businesses that submitted OICs greater than the amount collected. The table shows that the RCP for each of the entities is overestimated. In fact, depending on business entity type, the RCP is overestimated about seven to ten times greater than the amount that is offered and about 20 to 30 times what has been collected.

35 National Taxpayer Advocate 2017 Annual Report to Congress vol. 2, 59.

36 IRM 5.8.1.2.3, *Policy* (May 5, 2017).

37 Research Study: *A Study of the IRS Offer in Compromise Program for Business Taxpayers* vol. 2, *infra*.

38 *Id.*

39 *Id.* The value for amount collected is calculated through August 2018.

**FIGURE 1.18.4, Business Rejected OICs Which Exceeded Payments by Business Type<sup>40</sup>**

Business Type	Count	Average Amount Offered	Average Amount Collected	Percentage of Amount Offered	Average RCP	Percentage of Amount Collected
Partnership	107	\$28,882	\$7,787	27%	\$210,744	2,706%
Corporation	617	\$53,911	\$21,066	39%	\$414,590	1,968%
Sole Proprietor	178	\$16,345	\$5,794	35%	\$171,005	2,951%

The IRS should study what occurred in the financial analyses of these cases to determine how it can improve the RCP calculation. Since the RCP plays such a large role in OIC analysis, having an accurate RCP will improve the taxpayers' ability to submit successful OICs.

### The IRS Has Made Recent Policy Changes That Discourage All Taxpayers From Submitting Successful Offers

#### *OICs Submitted by a Taxpayer Who Has Not Filed All Necessary Tax Returns Are Returned to the Taxpayer As Not Processable*

In 2016, the IRS announced that it would return OICs submitted by a taxpayer who had not filed all necessary tax returns (based on internal research) to the taxpayer as not processable.<sup>41</sup> Prior to this change, if the IRS determined that a taxpayer was not in filing compliance, the IRS would process the OIC and contact the taxpayer to discuss any late tax returns and allow the taxpayer time to file them within a specified period of time.<sup>42</sup>

The IRS decided to return OICs as not processable due to lack of filing compliance as part of an OIC Future State Initiative, explaining “[the new policy] changes the current COIC practice to sign in offers from non-compliant taxpayers and attempts to bring them current.”<sup>43</sup> With this initiative, the IRS will return such OICs to the taxpayer with instructions to become compliant and then resubmit his or her OIC. A TAS review of the data relied on by the IRS indicates that the IRS considered the time saved by not working these OICs any further; however, it did not consider the time to work a resubmitted OIC or conduct any analysis to compare the time saved by returning these OICs versus keeping them open and achieving filing compliance in the future and resolving outstanding tax liabilities.

40 Research Study: *A Study of the IRS Offer in Compromise Program for Business Taxpayers* vol. 2, *infra*. The value for amount collected is calculated through August 2018.

41 Memorandum from Director, Collection Policy to Director, Specialty Collection Offers, Liens & Advisory (Apr. 13, 2016) (on file with the author).

42 IRM 5.8.3.6(1), *Perfecting Field Cases* (July 28, 2015); IRM 5.8.3.7(1), *Perfecting COIC Cases* (Dec. 7, 2015).

43 IRS response to TAS information request (Sept. 20, 2017). For an in-depth discussion of the IRS's Future State, see National Taxpayer Advocate 2015 Annual Report to Congress 3-13.

During FY 2017 and the first three quarters of FY 2018, the IRS returned 2,767 IMF OICs because of unfiled returns. Of those returned OICs, 947 taxpayers (approximately 34 percent) resubmitted an OIC.<sup>44</sup> The IRS returned 561 OICs to BMF taxpayers because of unfiled returns in FY 2017. Of those returned OICs, 266 taxpayers (approximately 47 percent) resubmitted OICs.<sup>45</sup>

### *The IRS Will Keep the Payments Sent With OICs That Are Returned for Lack of Filing Compliance*

In February 2017, the IRS announced a change in practice in which the IRS will keep the payments sent with OICs that are returned for lack of filing compliance.<sup>46</sup> The payments are applied to the liability; however, the taxpayer cannot have these funds applied to subsequent OICs. In many instances, the OIC funds may be borrowed or are from sources not generally available to the taxpayer. By not processing these OICs (see above) *and* keeping the payments, the IRS creates a major obstacle to submitting a successful OIC.

Prior to 2006, sums submitted with an OIC were considered deposits and were not applied to the liability until the IRS accepted the OIC, unless the taxpayer provided written authorization for application of the payments.<sup>47</sup> Subsequently, the Tax Increase Prevention and Reconciliation Act of 2005 (TIPRA) required taxpayers to submit a partial payment with the OIC package (hence, the “TIPRA payment”).<sup>48</sup> In lieu of updated regulations, the IRS issued Notice 2006-68 in July 2006. Under Notice 2006-68, the IRS treats the TIPRA payment as a payment of tax rather than a refundable deposit, as the regulations do. Of all the IMF OICs that the IRS returned for lack of filing compliance during FY 2018, 554 taxpayers made a TIPRA payment with their original OIC. Of those 554 taxpayers, IRS kept the TIPRA payment in approximately 18 percent of the cases and did not reopen the original OIC, causing the taxpayer to come up with another TIPRA payment for any subsequent OIC.<sup>49</sup> Likewise, 190 BMF taxpayers made a TIPRA payment with their original OIC. Of those taxpayers, 64 percent had their TIPRA payment retained without the OIC being reopened by the IRS. Since the IRS has taken the legal position in Notice 2006-68 that the IRS must keep TIPRA payments because they are viewed as payments and not deposits, the IRS should provide taxpayers with an opportunity to cure any defect prior to considering the OIC not processable. The IRS impedes compliance by keeping OIC payments without first offering an opportunity to cure OICs it would otherwise deem not processable.

44 For the purposes of this analysis, TAS Research considered the OIC to be a resubmission if it was more than four weeks after the date indicated by the Small Business/Self-Employed (SB/SE) division as the return date. IRS response to TAS information request (Aug. 20, 2018); Individual Master File for the Taxpayer Identification Numbers (TINs) provided by SB/SE where an OIC was returned in FY 2017 as unprocessable because of unfiled returns.

45 IRS response to TAS information request (Aug. 20, 2018); Individual Master File for the TINs provided by SB/SE where an OIC was returned in FY 2017 as unprocessable because of unfiled returns.

46 Memorandum from Director, Collection Policy to Director, Specialty Collection, Liens & Advisory (Feb. 23, 2017) (on file with the author).

47 Treas. Reg. § 301.7122-1(h).

48 Tax Increase Prevention and Reconciliation Act of 2005 (TIPRA), Pub. L. No. 109-22, §509, 120 Stat. 362 (2006).

49 IRS response to TAS information request (Aug. 31, 2018). The IRS may reconsider a returned OIC if doing so would be in the best interest of the IRS and the taxpayer. Generally, in these instances the IRS will not require another application fee or TIPRA payment. IRM 5.8.7.3, *Return Reconsideration* (Oct. 7, 2016).

### *OICs Returned in Error Are Not Subject to the 24-Month Deemed Acceptance Period in IRC § 7122(f)*

Under IRC § 7122(f), which Congress added as part of TIPRA, if an OIC has not been rejected within 24 months of submission, the IRS must deem it accepted.<sup>50</sup> This legislation occurred as a result of problems first identified with OIC processing during Congressional hearings for the IRS Restructuring and Reform Act of 1998 (RRA 98).<sup>51</sup> The president of the National Society of Accountants (NSA) reported NSA members experienced “inordinate delays” with the processing of OICs.<sup>52</sup> One woman described her experience getting an OIC in connection with an innocent spouse claim. She reported in part:

I have offered to pay the original assessed amount of \$9,000, but that was flatly rejected. This process of offer in compromise has taken nearly two years to negotiate. At almost every turn, I have hit a wall in terms of requesting information or filing information. It appears to me that the right hand doesn't know what the left hand is doing. I have noticed that in requesting certain information, letters are signed by one person, but questions should be directed to another. This slows the process. An agent in Idaho returned my original offer in compromise because it was submitted on a photocopied form rather than a carbon-copy original. This slows the process.<sup>53</sup>

In an email dated April 27, 2018, IRS Counsel stated that OICs returned in error are not subject to the 24-month deemed acceptance period in IRC § 7122(f).<sup>54</sup> Since an OIC will not be deemed acceptable once it is rejected, the 24-month period under IRC § 7122(f) is extinguished once the OIC is rejected. IRC § 7122(f) does not distinguish between a rejection with merit and a rejection made in error by the IRS.<sup>55</sup> As a result, the IRS will no longer apply the protections of IRC § 7122(f) to OICs returned to taxpayers after an erroneous rejection by the IRS.

Congress created the protections found in IRC § 7122(f) after listening to taxpayers and practitioners describe the situations in which they found themselves. By exempting the time associated with an OIC returned erroneously to the taxpayer, the IRS is going against the Congressional intent in IRC § 7122(f) as well as violating the taxpayer's *right to a fair and just tax system*. This change will also lead to confusion for taxpayers, particularly for those who do not understand the difference between a returned and a rejected OIC. And in totality, all of the changes described above will make it more difficult for taxpayers to get the IRS to accept an OIC.

50 Pub. L. No. 109-222, §509(b)(2), 120 Stat. 363.

51 *Taxpayer Rights Proposals And Recommendations of the National Commission on Restructuring the Internal Revenue Service on Taxpayer Protections and Rights: Hearing Before the H. Subcomm. on Oversight*, 105th Cong. 17 (1997) (statement of Rep. William J. Coyne).

52 *IRS Restructuring: Hearing Before the S. Comm. on Finance*, 105th Cong. 240 (1997) (statement of Douglas C. Burnette, president, National Society of Accountants).

53 *Internal Revenue Service's Methods: Hearing Before the S. Comm. on Appropriations*, 105th Cong. 17 (1998) (statement of Amy Powers).

54 In some instances this will harm taxpayers twice. The IRS believes the 24-month period under IRC § 7122(f) stops to run when an OIC is closed, even if the IRS erroneously returns or withdraws an OIC to a taxpayer and later reopens it. However, the IRS tolls the collection statute expiration date timeframe in such reopened offers, which allows the IRS a longer time to collect the taxpayer's debt if the OIC is not accepted. Treas. Reg. § 301.7122-1(i). So the taxpayer is inconvenienced with an erroneously returned OIC that no longer is protected by a two-year timeframe for processing but is also subjected to a longer collection period.

55 See also IRS, Notice 2006-68, *Downpayments for Offers in Compromise* (July 31, 2006).

### *The Time It Takes for Appeals to Process OIC Appeals May Lead to Multiple Years of Refund Offsets*

As a term of acceptance for the OIC, the taxpayer agrees that the IRS will keep any refund, including interest, that might be due for tax periods extending through the calendar year in which the IRS accepts the offer.<sup>56</sup> This policy may make sense when the OIC can be processed (including any Appeals action) within a year. However, practitioners report this practice harms their clients because processing OICs takes so long that the IRS takes multiple refunds.<sup>57</sup> It can be especially difficult for low income taxpayers who rely on their tax refunds to meet their basic living expenses. Figure 1.18.5 shows the cycle time for OICs worked in Appeals from receipt of the case until closure.

**FIGURE 1.18.5, Appeals Offer in Compromise Case Closed Cycle Time FY 2016-FY 2018**<sup>58</sup>

FY 2016	FY 2017	FY 2018
174.8 days (5.8 months)	193.6 days (6.5 months)	194.7 days (6.5 months)

While Appeals is not the only cause of delayed processing, the average amount of time that Appeals keeps a case has gone from 5.8 months in FY 2016 to 6.5 months in FY 2018. This means if a taxpayer appeals a rejected OIC to Appeals after August of a given year, there is a likelihood that the OIC will be worked into the next calendar year, and the taxpayer will lose an additional refund. The IRS accepted 24,958 IMF OICs in FY 2017 and in 1.5 percent (378 OICs) of those, the taxpayer lost two refunds.<sup>59</sup> The lost refunds total \$ 945,953.<sup>60</sup> For BMF OICs, the IRS accepted 1,599 OICs in FY 2017. Of that amount, less than one percent (seven OICs) lost two refunds. The lost refunds total \$20,383.54.<sup>61</sup> This impacts the taxpayer's *right to a fair and just tax system*.

The role of Appeals is not to develop the case. Appeals employees are instructed to “ask the taxpayer for clarifying information if the taxpayer (particularly a *pro se* taxpayer) is unsure of what to provide to clarify a position that is being advanced by the taxpayer. You will primarily rely on the case development that is in the case file at the time of appeal.”<sup>62</sup> Additionally, Appeals employees are instructed to consider only the items in dispute at the time of the OIC rejection or issues raised by the taxpayer.<sup>63</sup> Since OIC analysis is now centralized, Appeals should review its employees’ training and technical experience to ensure it has a sufficient number of employees to work these OIC cases timely.

56 IRS, Form 656, *Offer in Compromise* 5 (Mar. 2018).

57 TAX ANALYSTS, *Offer in Compromise Participation Can Mean Lost Refunds for Some* (June 12, 2018).

58 IRS response to TAS information request (Aug. 6, 2018).

59 Analysis of OIC submission dates and offset refunds from IMF.

60 *Id.*

61 Analysis of OIC submission dates and offset refunds from BMF.

62 IRM 8.23.1.3(2), *Conference and Settlement Practices* (Apr. 18, 2016).

63 IRM 8.23.1.3(3), *Conference and Settlement Practices* (Apr. 18, 2016).

## CONCLUSION

As demonstrated by TAS Research, the OIC is a valuable collection tool for both the IRS and taxpayers. It is a cost-effective way to encourage long-term tax compliance. It provides finality to taxpayers who are struggling with a tax liability. It saves money for the IRS by collecting as much as possible early in the process, without expensive enforcement action.

However, the IRS has made several changes to the OIC program which threaten to leave the OIC out of reach for some taxpayers. Instead of returning OICs for lack of filing compliance, the IRS should retain the OIC for a period of time during which the taxpayer can “cure” the defect of missing tax returns. By adopting this approach, the IRS would only retain a TIPRA payment in situations where an OIC defect cannot be cured. The IRS should rethink its analysis of when the 24-month processing limitation applies in cases where it rejects an OIC, especially in cases where the rejection was an IRS error. Refusing to apply this protection to taxpayers compounds the IRS errors to the detriment of taxpayers. Last, the IRS should review its policy of offsetting multiple years of refunds where there are long processing times for OIC appeals. The recent IRS changes to the OIC program could harm taxpayers and may impact the OIC’s viability as a collection tool in the future.

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Have at least one OIC Specialist in each state to ensure a more even geographic presence for OIC analysis.
2. Change its policy for deeming OICs not processable if the taxpayer is not current with his or her filing requirement and reinstate the requirement to retain the OIC and contact taxpayers to obtain missing returns within a specified period of time.
3. Reconsider its determination that OICs returned or withdrawn in error are not subject to the 24-month deemed acceptance period in IRC § 7122(f).
4. Limit the number of refunds that can be offset while an OIC is pending to one refund only.
5. Conduct a study to analyze the OIC amount offered and collected amounts to understand why the IRS is rejecting OICs that have an offered amount greater than the dollars collected. For instance, the IRS should look at how it is applying the Allowable Living Expense standards and where the taxpayer is obtaining the payment for the OIC.

**MSP  
#19****PRIVATE DEBT COLLECTION: The IRS's Expanding Private Debt Collection Program Continues to Burden Taxpayers Who Are Likely Experiencing Economic Hardship While Inactive Private Collection Agency Inventory Accumulates****RESPONSIBLE OFFICIAL**

Mary Beth Murphy, Commissioner, Small Business/Self-Employed Division

**TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Finality*
- *The Right to Privacy*
- *The Right to Confidentiality*
- *The Right to a Fair and Just Tax System*

**DEFINITION OF PROBLEM**

The IRS implemented its current Private Debt Collection (PDC) initiative in April 2017.<sup>2</sup> As of September 13, 2018, about \$5.7 billion in debts of more than 600,000 taxpayers were in the hands of private collection agencies (PCAs).<sup>3</sup> The IRS initially assigned cases in which the taxpayer did not dispute liability for the debt. However, 2018 assignments included tax assessments, such as those based on substitutes for return, which have high tax abatement rates.

- 1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).
- 2 IRS News Release IR-2017-74, *Private Collection of Some Overdue Federal Taxes Starts in April; Those Affected Will Hear First From IRS; IRS Will Still Handle Most Tax Debts* (Apr. 4, 2017), <https://www.irs.gov/newsroom/private-collection-of-some-overdue-federal-taxes-starts-in-april-those-affected-will-hear-first-from-irs-irs-will-still-handle-most-tax-debts>.
- 3 Private Debt Collection (PDC) Program Scorecard for fiscal year (FY) 2018 showing that 621,321 taxpayers' accounts with a dollar value of \$5,115,996,181 were in Private Collection Agency (PCA) open inventory.

PDC program revenues have surpassed program costs, but this surplus has been achieved, to a significant extent, by collecting from financially vulnerable taxpayers. According to IRS databases that contain information from tax returns filed by taxpayers and reports of income filed by third parties:

- 40 percent of taxpayers who entered into installment agreements (IAs) while their debts were assigned to PCAs had incomes at or below their allowable living expenses (ALEs), meaning they agreed to pay tax arrears while they could not pay for their basic living expenses;<sup>4</sup>
- 44 percent of taxpayers who made commissionable payments while their debts were assigned to PCAs had incomes at or below 250 percent of the federal poverty level (FPL);<sup>5</sup>
- 37 percent of taxpayers who entered into IAs while their debts were assigned to PCAs defaulted, a frequency that rises to 44 percent when defaulted IAs that PCAs do not report to the IRS as required are taken into account;<sup>6</sup> and
- 34 percent of the amount paid that was attributable to PCA activity was made by taxpayers whose incomes were at or below their ALEs.<sup>7</sup>

The PDC program is not generating the revenues Congress expected, and only about a third of revenues attributable to PCA activity in FY 2018 made their way to, and remained in, the government's General Fund.<sup>8</sup> Moreover, IRS collection activity with respect to taxpayers whose debts were assigned to PCAs actually generated more dollars for the public fisc in FY 2018 than did PCA activity.<sup>9</sup>

At the end of FY 2018, PCAs' inventories included over 400,000 cases in which there was no payment by the taxpayer and no agreement to pay, even though the case had been assigned for at least 90 days.<sup>10</sup> In fact, these cases had been in PCA inventory for 244 days on average.<sup>11</sup> Retaining cases without resolving taxpayers' liabilities allows PCAs to receive commissions on any payments taxpayers happen to make in the future in the absence of any recent PCA collection activity. Had these cases remained

4 This figure reflects allowance of vehicle ownership and operating expenses in calculating allowable living expenses (ALEs). As discussed below, if vehicle ownership expenses are not allowed, 33 percent of taxpayers who entered into installment agreements (IAs) while their debts were assigned to PCAs had incomes at or below their ALEs. For a further discussion of ALEs, see vol. 2, *A Study of the IRS's Use of the Allowable Living Expense Standards*, *infra*.

5 The measure of 250 percent of the federal poverty level is used in tax administration in several contexts. Congress adopted the measure to identify taxpayers who qualify for assistance from low income taxpayer clinics (LITCs) because they cannot afford representation in IRS disputes and are therefore vulnerable to overreaching. See IRC § 7526. The Bipartisan Budget Act of 2018 adopts the measure to determine whether to excuse taxpayers from paying user fees to enter into installment agreements. See Bipartisan Budget Act of 2018, Pub. L. No. 115-123, § 41105, 132 Stat. 64, 157 (Feb. 9, 2018). The IRS uses the measure as a proxy to identify certain retirement income recipients who are likely to be in economic hardship in order to exclude them from its automatic levy program, the Federal Payment Levy Program. See IRM 5.19.9.3.2.3, *Low Income Filter (LIF) Exclusion* (Oct. 20, 2016).

6 Accounts Receivable Dollar Inventory (ARDI), Individual Returns Transaction File (IRTF), Information Returns Master File (IRMF), Compliance Data Warehouse (CDW), reflecting data from inception of the PDC program through FY 2018, discussed below.

7 ARDI, IRTF, IRMF, CDW, reflecting activity on tax modules (the IRS's record of a specific tax liability for a specific tax period), from program inception through FY 2018, discussed below.

8 Congressional Budget Office (CBO) projections; IRS Quarterly Update to Congress, *Private Debt Collection (PDC) Program 1*, for FY 2018, discussed below. According to the Bureau of the Fiscal Service (BFS), "[a]s 'America's Checkbook,' the General Fund of the Government consists of assets and liabilities used to finance the daily and long-term operations of the U.S. Government as a whole. It also includes accounts used in management of the budget of the U.S. Government." BFS, *The General Fund*, <https://fiscal.treasury.gov/general-fund/> (last visited Dec. 18, 2018). Of the \$75.3 million in revenues attributable to PCA activity, a net amount of \$25.8 million, or 34 percent, was generated for the General Fund.

9 As discussed below, in FY 2018 the IRS collected \$37.4 million from taxpayers whose debts were assigned to PCAs, while PCA activity generated a net amount of \$25.8 million for the General Fund.

10 ARDI, IRTF, IRMF, CDW data, showing 408,087 of these cases as of Sept. 30, 2018.

11 *Id.*, reflecting activity since the inception of the PDC program in April 2017 through FY 2018.

in the IRS queue and not assigned to PCAs, the public fisc would be credited with the full amount of collected funds.

## ANALYSIS OF PROBLEM

### Background

IRC § 6306 was amended in 2015 to require the IRS to enter into “qualified tax collection contracts” for the collection of “inactive tax receivables.”<sup>12</sup> The Congressional Budget Office (CBO) estimated that from FYs 2016-2025, the new PDC program would raise \$4.8 billion in revenues and require \$2.4 billion in spending.<sup>13</sup> CBO projected that for FY 2017, the PDC program would generate \$374 million in revenues, and for FY 2018 would generate \$470 million in revenues.<sup>14</sup>

Prior to the launch of the PDC initiative, the National Taxpayer Advocate voiced her concern that the program as implemented would create or exacerbate taxpayers’ economic hardship.<sup>15</sup> By the IRS’s own estimate, under the proposed legislation that required the IRS to outsource certain tax debts to PCAs, about 79 percent of the taxpayers whose debts would be eligible for assignment to PCAs had incomes below 250 percent of the federal poverty level.<sup>16</sup>

On April 23, 2018, about a year after the IRS began assigning tax debts to PCAs, the National Taxpayer Advocate issued a Taxpayer Advocate Directive (TAD) ordering the IRS to exclude from assignment to PCAs the debts of taxpayers whose incomes are below 250 percent of the FPL. The IRS appealed the TAD on May 14, 2018, and the Deputy Commissioner for Services and Enforcement rescinded the TAD on June 20, 2018.<sup>17</sup>

In the meantime, the IRS continued to assign tax debts to PCAs. By September 13, 2018, over \$5.7 billion in debts owed by over 730,000 taxpayers had been assigned to PCAs.<sup>18</sup> About \$5 billion in debts owed by more than 600,000 taxpayers was still in PCA inventory on that date.<sup>19</sup> For FY 2018,

12 See Fixing America’s Surface Transportation Act (FAST Act), Pub. L. No. 114-94, Div. C, Title XXXII, § 32102, 129 Stat. 1312, 1733-36 (2015) (adding subsections (c) and (h) to IRC § 6306).

13 Letter from Keith Hall, CBO Director, to Rep. Bill Shuster, Chairman, Comm. on Transportation and Infrastructure, Table 2 (Dec. 2, 2015).

14 *Id.*, projecting that the PDC program would generate \$374 million in revenues and \$187 million in outlays for FY 2017 and \$470 million in revenues and \$235 million in outlays for FY 2018. The projected outlays appear to include amounts retained under IRC § 6306(e), discussed below, equal to 50 percent of revenues attributable to PCA activity.

15 See National Taxpayer Advocate 2016 Annual Report to Congress 172 (Most Serious Problem: Private Debt Collection (PDC): *The IRS Is Implementing a PDC Program in a Manner That Is Arguably Inconsistent With the Law and That Unnecessarily Burdens Taxpayers, Especially Those Experiencing Economic Hardship*).

16 See Letter from Nina Olson, National Taxpayer Advocate, to Sen. Ron Wyden, Chairman, Comm. on Finance; Sen. Orrin G. Hatch, Ranking Member, Comm. on Finance; Rep. Dave Camp, Chairman, Comm. on Ways and Means; Rep. Sander Levin, Ranking Member, Comm. on Ways and Means; Rep. Charles W. Boustany, Jr., Chairman, Subcomm. on Oversight, Comm. on Ways and Means; Rep. John Lewis, Ranking Member, Subcomm. on Oversight, Comm. on Ways and Means (May 13, 2014).

17 The Taxpayer Advocate Directive (TAD), the IRS’s appeal, and the memorandum rescinding the TAD were published in the National Taxpayer Advocate Fiscal Year (FY) 2019 Objectives Report to Congress 68-79.

18 PDC Program Scorecard for FY 2018, showing that since the program’s inception, \$5,707,490,970 of debt of 730,015 taxpayers were assigned to PCAs.

19 *Id.*, showing that 621,321 taxpayers’ accounts with a dollar value of \$5,115,996,181 were in PCA open inventory.

PCA activity generated \$75.3 million of revenue, which is about 16 percent of the \$470 million CBO projection for FY 2018.<sup>20</sup>

### IRS Activity Generated More For the Public Fisc Than PCA Activity Did

As noted, in FY 2018, taxpayers made \$75.3 million in payments as a result of PCA activity.<sup>21</sup> However, of this \$75.3 million:

- The IRS retained 25 percent, \$18.8 million, as authorized by IRC § 6306(e)(1), to pay for the costs of services performed by PCAs, including commissions;<sup>22</sup> and
- The IRS retained an additional 25 percent, \$18.8 million, as authorized by IRC § 6306(e)(2) “to fund the special compliance personnel program account under section 6307.”<sup>23</sup>

After subtracting the amounts retained pursuant to IRC § 6306(e), \$37.7 million was paid to the General Fund.<sup>24</sup> From the General Fund, an additional \$11.9 million of PDC program costs were paid.<sup>25</sup> Thus, of the \$75.3 million attributable to PCA activity in FY 2018, a net amount of \$25.8 million — or 34 percent — was generated for the General Fund.<sup>26</sup> Figure 1.19.1 shows the disposition of funds collected from taxpayers as a result of PCA activity.

20 IRS Quarterly Update to Congress, *Private Debt Collection (PDC) Program 1*, for FY 2018, discussed below. Because the PDC program was not launched until April of 2017, it may be appropriate to compare the FY 2018 program performance with CBO’s FY 2017 projections. The \$75.3 million in revenues for FY 2018 generated by PCA activity is 20 percent of the \$374 million CBO revenue projection for FY 2017. In its Quarterly Update to Congress, the IRS reported PDC program revenues of \$82.1 million, which includes, in addition to \$75.3 million in revenues attributable to PCA activity, \$6.8 million of payments received within ten days of assignment of the account to a PCA. These payments are not subject to commissions because they are deemed not attributable to PCA activity. Even including the \$6.8 million in program revenues, the program appears to have fallen short of expectations: \$82.1 million is 17 percent of CBO’s projected FY 2018 revenues and 22 percent of projected FY 2017 revenues.

21 *Id.*, showing taxpayers made \$75,372,679 in commissionable payments (*i.e.*, amounts received more than ten days after the IRS notified taxpayers their debts had been assigned to PCAs. These payments are deemed attributable to PCA activity and are thus subject to commissions).

22 IRC § 6306(e)(1) authorizes the IRS to retain and use “an amount not in excess of 25 percent of the amount collected under any qualified tax collection contract for the costs of services performed under such contract.” Pursuant to this provision, the IRS retained \$18,843,170 for its Cost of Services Fund. The IRS paid commissions to PCAs from this fund. IRS Quarterly Update to Congress, *Private Debt Collection (PDC) Program 7*, for FY 2018.

23 Pursuant to IRC § 6306(e)(2), the IRS retained \$18,843,170 for a Special Compliance Personnel Program (SCPP) fund. IRS Quarterly Update to Congress, *Private Debt Collection (PDC) Program 7*, for FY 2018. IRC § 6307(a) requires the IRS to use amounts retained under IRC § 6306(e)(2) to hire, train, and employ special compliance personnel, defined in IRC § 6307(d)(1) as “field function collection officers or in a similar position, or employed to collect taxes using the automated collection system or an equivalent replacement system.”

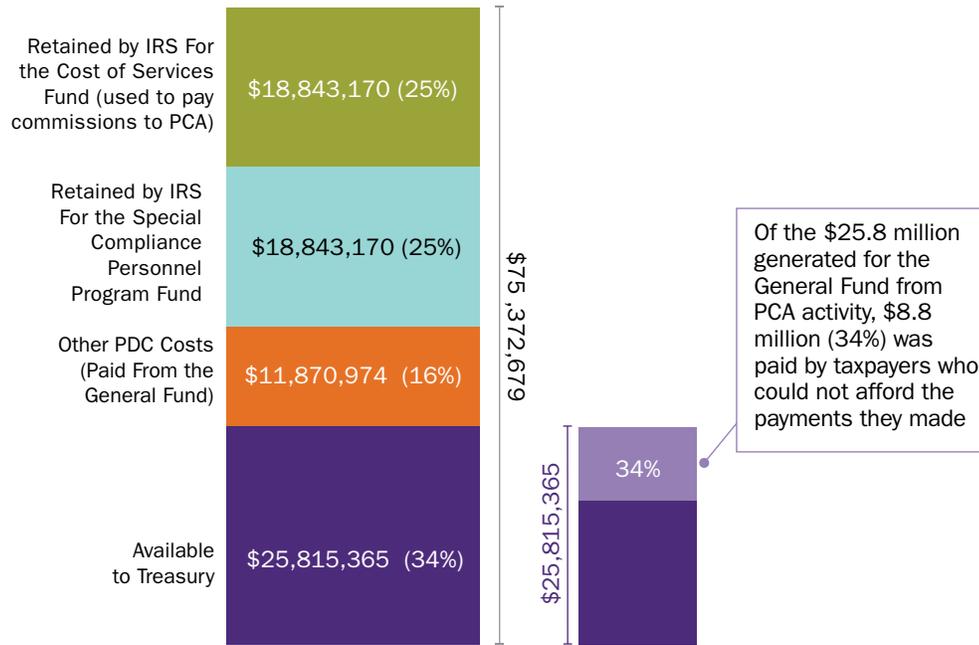
24 IRS response to fact check (Dec. 17, 2018), noting that “[c]ommissionable payments are distributed as follows: 25% (\$19 million) is retained in the Cost of Services fund to pay commissions, 25% (\$19 million) is retained in the SCPP fund to pay for contract administration and SCP [this acronym is undefined] program costs, and 50% goes to the General Fund (\$37 million).” Without rounding, commissionable payments of \$75,372,679 less \$18,843,170 for each special fund authorized by IRC § 6306(e) is \$37,686,339.

25 PDC program costs paid from the General Fund were \$11,870,974. IRS response to TAS fact check (Dec. 17, 2018); IRS Quarterly Update to Congress, *Private Debt Collection (PDC) Program 1*, for FY 2018.

26 Without rounding, \$37,686,339 less \$11,870,974 is \$25,815,365.

**FIGURE 1.19.1**

**Disposition of \$75 Million of Commissionable Payments Made in FY 2018 by Taxpayers Whose Debts Were Assigned to Private Collection Agencies**



As discussed in greater detail below, 34 percent of total payments attributable to PCA activity are made by taxpayers whose incomes are at or below their ALEs. Thus, of the \$25.8 million that was ultimately available to the Treasury as a result of PCA activity, \$8.8 million was paid by taxpayers who could not afford the payments they made.<sup>27</sup>

Moreover, some taxpayers whose debts were assigned to PCAs made payments that were attributable to IRS, rather than PCA, activity:

- The IRS’s initial contact letter advising taxpayers their debt was being assigned to a PCA generated \$6.8 million;<sup>28</sup>
- Through levies on payments these taxpayers were entitled to receive from federal, state, or local governments, the IRS collected an additional \$16.4 million;<sup>29</sup>

27 Without rounding, 34 percent of \$25,815,365 is \$8,777,224. As discussed below, if vehicle ownership expenses are not allowed in calculating ALEs, 30 percent of total payments attributable to PCA activity are made by taxpayers whose incomes are at or below their ALEs.

28 IRS Quarterly Update to Congress, *Private Debt Collection (PDC) Program 1*, for FY 2018, showing non-commissionable payments (i.e., those received within ten days after the IRS notifies taxpayers their debts have been assigned to a PCA) of \$6,820,047.

29 ARDI, IRTF, IRMF, CDW data, reflecting activity for FY 2018, showing the IRS collected \$16,400,771 through levies, including pursuant to the State Income Tax Levy Program (SITLP); Municipal Tax Levy Program (MTLP); Alaska Permanent Fund Dividend Levy Program (AKPFD); and the Federal Payment Levy Program (FPLP). These cases were recalled by the IRS from PCA inventory; IRC § 6306(d)(4) provides that a tax receivable may not be assigned to a PCA if it is “currently under examination, litigation, criminal investigation, or levy.”

- The IRS collected \$14.2 million by offsetting these taxpayers' federal tax refunds against their outstanding tax liabilities.<sup>30</sup>

This total of \$37.4 million is not subject to commissions or retention by the IRS under IRC § 6306(e).<sup>31</sup> Thus, IRS activity actually generated 1.4 times more dollars for the public fisc than PCA activity did.<sup>32</sup>

PCAs do not appear to be particularly effective in generating payments, especially in view of the burden the PDC program places on taxpayers, discussed below. Only a little more than one percent of the dollar value of the debt assigned to PCAs since inception of the program has been collected.<sup>33</sup> By comparison, the Automated Collection System (ACS), the IRS function that issues collection notices and receives calls from taxpayers with delinquent tax liabilities, collects seven percent of the dollar value of tax liabilities assigned to it.<sup>34</sup> Taxpayers whose cases are assigned to PCAs enter into IAs six percent of the time.<sup>35</sup> In contrast, the ACS function places taxpayers into IAs about ten percent of the time.<sup>36</sup>

### Congress Required the IRS to Develop Allowable Living Expense Standards to Prevent Taxpayers From Being Required to Make Payments They Cannot Afford

The IRS evaluates taxpayers' abilities to pay their tax liabilities by comparing their incomes to their ALEs, a practice that has been in place for decades.<sup>37</sup> The ALE standards determine how much money taxpayers need for basic living expenses such as housing and utilities, food, transportation, and health care, based on family size and where they live.<sup>38</sup> The amount by which a taxpayer's income exceeds his or her ALEs is the starting point for determining the extent to which a taxpayer can afford to pay the debt immediately in full, or over time in installments. If the ALE standards exceed the taxpayer's income, the taxpayer is unable to pay his or her necessary living expenses. Thus, the taxpayer may

30 Refund offsets do not cause a recall of a case from PCA inventory. In FY 2018, the IRS offset \$14,197,449 of refunds claimed by taxpayers whose debts were assigned to PCAs. ARDI, IRTF, IRMF, CDW.

31 The sum of the non-commissionable payments of \$6,820,047, levied amounts of \$16,400,771, and refund offsets of \$14,197,449 is \$37,418,267.

32 Without rounding, \$37,418,267 million in collections that resulted from IRS activity is 1.4 times greater than the \$25,815,365 generated for the General Fund by PCA activity.

33 PDC Program Scorecard for FY 2018. Since inception of the program, the amount of commissionable payments was \$80,736,597, which is 1.4 percent of the dollar value of the amounts assigned, \$5,707,490,970.

34 IRS, Collection Activity Report NO-5000-2, *Taxpayer Delinquent Account Cumulative Report* (Sept. 30, 2018) (showing \$47,125,583,881 assigned for collection and \$3,455,267,613 collected, a rate of 7.33 percent).

35 As discussed below, 43,579 of the 730,015 taxpayers whose debts were assigned to PCAs entered into IAs, a rate of six percent.

36 IRS, Collection Activity Report NO-5000-2, *Taxpayer Delinquent Account Cumulative Report* (Sept. 30, 2018); IRS, Collection Activity Report NO-5000-6, *Installment Agreement Cumulative Report* (Sept. 30, 2018) (showing 4,670,873 individual taxpayers' accounts in Automated Collection Systems (ACS) inventory at the beginning of FY 2018, and an additional 3,197,173 individual taxpayers' accounts assigned to ACS during FY 2018, for total available inventory of 7,868,046 individual taxpayer accounts. Of these, 780,809 taxpayers entered into IAs, a rate of 9.9 percent).

37 See, e.g., IRM 105.1.3, *Collecting Contact Handbook* (Sept. 25, 1996), <http://core.publish.no.irs.gov/irm/p05/pdf/30353i96.pdf>; IRM 57(10)(10).1(4), *Determination of Adequate Offer* (Sept. 22, 1994), cross referencing IRM 5323 on IAs, <http://core.publish.no.irs.gov/irm/p05/pdf/35490e98.pdf>.

38 See IRS, Collection Financial Standards, <https://www.irs.gov/businesses/small-businesses-self-employed/collection-financial-standards>. The ALEs are guidelines that "establish the minimum a taxpayer and family needs to live." The IRS may allow additional amounts for basic living expenses if the taxpayer substantiates the need to deviate from the standards. IRM 5.15.1.8 (6), *Financial Analysis Handbook, Allowable Expense Overview* (Aug. 29, 2018). Allowable expenses include transportation expenses, which may consist of vehicle ownership expenses (loan or lease payments) and operating expenses (maintenance, repairs, insurance, fuel, registrations, licenses, inspections, parking, and tolls). Unless otherwise indicated, in calculating taxpayers' ALEs, we allowed vehicle operating expenses (two allowances in the case of joint filers and one allowance for all other taxpayers), and all taxpayers were allowed one vehicle ownership expense.

qualify for collection alternatives such as an offer in compromise (OIC)<sup>39</sup> or to have the account designated as Currently Not Collectible (CNC) - Hardship.<sup>40</sup>

In 1998, Congress amended IRC § 7122, *requiring* the IRS to develop guidelines to determine when an OIC is adequate and should be accepted to resolve a dispute.<sup>41</sup> Specifically, the IRS was required to develop ALEs “designed to provide that taxpayers entering into a compromise have an adequate means to provide for basic living expenses.”<sup>42</sup> Essentially, Congress codified in IRC § 7122 the existing IRS practice of taking into account taxpayers’ ALEs in determining the extent to which they can pay, and in considering collection alternatives.

The IRS is not required to consider taxpayers’ ALEs, however, in evaluating proposed “streamlined” IAs (*i.e.*, IAs to repay a tax liability of a specified maximum amount within a specified number of months).<sup>43</sup> Taxpayers need not submit financial analysis to qualify for streamlined IAs, and may enter into streamlined IAs online, without interacting with an IRS employee. Nonetheless, taxpayers who seek to resolve their tax liabilities with the IRS have the option of providing financial information that can serve as the basis for collection alternatives, an option particularly relevant to taxpayers whose incomes are exceeded by their ALEs.

#### *In the PDC Initiative as Implemented, the Allowable Living Expenses Guidelines Are Ignored*

In contrast, PCAs can *only* propose that the taxpayer fully pay the liability within 120 days, or, alternatively, enter into a streamlined IA, which currently refers to an IA to repay a tax liability of up

39 See IRC § 7122, described below.

40 See IRM 5.16.1.2, *Currently Not Collectible* (Sept. 18, 2018); IRM 5.16.1.2.9, *Hardship* (Sept. 18, 2018), noting that “hardship exists if a taxpayer is unable to pay reasonable basic living expenses.”

41 IRS Restructuring and Reform Act of 1998 (RRA 98), Pub. L. No. 105-206, § 3462, 112 Stat. 685, 764 (July 22, 1998), adding subsection (c) (which is now subsection (d)) to IRC § 7122.

42 IRC § 7122(d)(2)(A). However, the ALE standards are not to be used “to the extent such use would result in the taxpayer not having adequate means to provide for basic living expenses.” IRC § 7122(d)(2)(B).

43 Streamlined IAs have been available for many years. See, e.g., 1999 TNT 111-26, *Memo on Streamlined Installment Agreements Released* (June 10, 1999) publishing a Mar. 31, 1998, memorandum from the Assistant Commissioner (Collection) that provided for streamlined IAs where the liability did not exceed \$15,000 (an increase over the previous amount of \$10,000); and 1999 TNT 111-24, *Memo on Streamlined Installment Agreements Released* (June 10, 1999) publishing a Mar. 29, 1999 memorandum from the Director, Office of Collection, Service Center and Appraisal Services that increased the maximum amount of liability for streamlined IAs to \$25,000 and increased the maximum duration of streamlined IAs from 36 months to 60 months.

to \$100,000 within six or seven years (and within the period of limitations on collection).<sup>44</sup> PCAs do not have the statutory authority to offer any collection alternatives, and in the PDC program as implemented, they do not gather financial information from taxpayers that the IRS could analyze, despite their statutory authorization to gather financial information.<sup>45</sup> Thus, while a taxpayer's debt is assigned to a PCA, the guidelines that Congress required the IRS to develop for analyzing taxpayers' ability to pay and evaluating collection alternatives will never apply. The National Taxpayer Advocate does not believe this outcome is necessary or appropriate, especially in view of the effect the current PDC initiative has on taxpayers, discussed below. The IRS should ensure that taxpayers whose incomes are at or below their ALEs have direct, unimpeded access to IRS collection alternatives by not assigning their debts to PCAs.<sup>46</sup>

### *Taxpayers Are Often Entitled to Relief That PCAs Cannot Provide*

In the prior iteration of the IRS's PDC initiative, PCAs could refer cases to a Referral Unit consisting of IRS employees.<sup>47</sup> The current PDC initiative does not include a Referral Unit, but some taxpayers whose debts were assigned to PCAs sought assistance from TAS. The disposition of TAS cases provides useful perspective. In FY 2018, TAS closed 157 cases involving taxpayers whose debts had been assigned to PCAs. Some taxpayers became unresponsive after their cases were opened. However, TAS succeeded in reducing or completely eliminating the balance due through penalty abatements, identity theft procedures, credit transfers, amended returns, or other adjustments 22 percent of the time. The taxpayers' accounts were placed in CNC Hardship status another 24 percent of the time.<sup>48</sup> Figure 1.19.2 shows the disposition of the 157 TAS cases.

44 Under IRC § 6502, the IRS must generally collect tax within ten years after assessment. See IRM 5.14.5.2, *Streamlined Installment Agreements* (Dec. 23, 2015), providing that streamlined IAs may be approved for taxpayers where the aggregate unpaid balance of assessments is \$50,000 or less and can be paid within 72 months and within the period of limitations on collection. Taxpayers who owe between \$50,000 and \$100,000 may qualify for a streamlined IA payable over 84 months. See IRS, *Streamlined Processing of Installment Agreements*, <https://www.irs.gov/businesses/small-businesses-self-employed/streamlined-processing-of-installment-agreements>. It appears that the duration of IAs offered by PCAs do not always conform to these IRS guidelines. As the Treasury Inspector General for Tax Administration (TIGTA) has noted, “[w]hile it is true that 84 months is the maximum payment arrangement for both IRS and PCA payment plans, the qualifications for obtaining such an agreement are different in that taxpayers who owe less than \$50,000 may not obtain an 84-month installment agreement from the IRS. However, there is no such restriction for PCA payment arrangements.” See TIGTA, Ref. No. 2019-30-018, *Fiscal Year 2019 Biannual Independent Assessment of Private Collection Agency Performance* 26 (Dec. 31, 2019). IRC § 6306(b) authorizes PCAs to offer IAs of a duration not to exceed five years. As discussed below, the PDC program as implemented authorizes PCAs to offer taxpayers IAs of six or seven years if the IRS approves the IA, an outcome the National Taxpayer Advocate views as an “end run” around the statute. See National Taxpayer Advocate 2016 Annual Report to Congress 172 (Most Serious Problem: *Private Debt Collection (PDC): The IRS Is Implementing a PDC Program in a Manner That Is Arguably Inconsistent With the Law and That Unnecessarily Burdens Taxpayers, Especially Those Experiencing Economic Hardship*). TIGTA shares that concern and other concerns expressed by the National Taxpayer Advocate. See TIGTA, Ref. No. 2018-30-052, *Private Debt Collection Was Implemented Despite Resource Challenges; However, Internal Support and Taxpayer Protections Are Limited* (Sept. 10, 2018).

45 IRC § 6303(b) defines a “qualified tax collection contract” as a contract pursuant to which PCAs “obtain financial information specified by the Secretary with respect to such taxpayer,” among other things. PCAs conduct operations according to provisions in the PCA Policies and Procedures Guide (PPG), which does not contemplate the collection of financial information from taxpayers. (References to the PPG are to the Sept. 30, 2018 version unless otherwise noted.)

46 For a legislative recommendation that the debts of taxpayers whose incomes are less than their ALEs should not be assigned to PCAs, see National Taxpayer Advocate 2019 Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration: Amend IRC § 6306(d) to Exclude the Debts of Taxpayers Whose Incomes Are Less Than Their Allowable Living Expenses From Assignment to Private Collection Agencies or, If That Is Not Feasible, Exclude the Debts of Taxpayers Whose Incomes Are Less Than 250 Percent of the Federal Poverty Level*, *infra*.

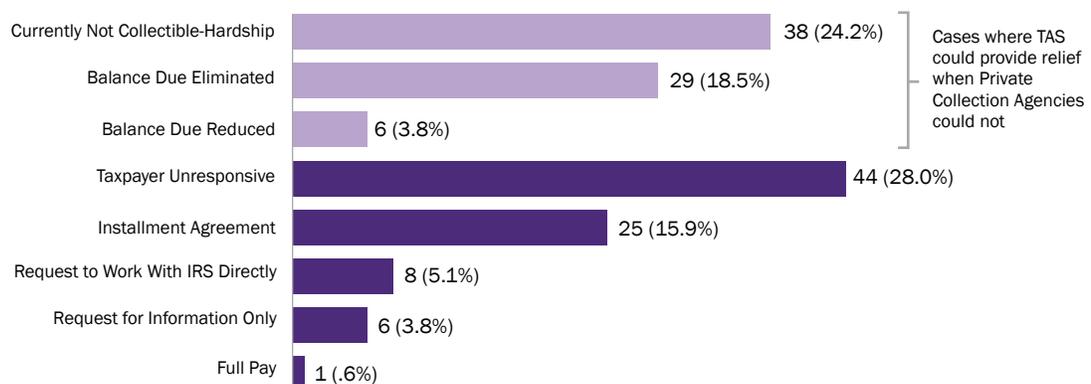
47 See PPG (July 1, 2008 version). The previous PDC initiative was in place from Sept. of 2006 until Mar. of 2009, when the IRS discontinued the program. See *IRS Conducts Extensive Review, Decides Not to Renew Private Debt Collection Contracts, IRS Employees More Flexible, More Cost Efficient* (Mar. 5, 2009), <https://www.irs.gov/newsroom/irs-conducts-extensive-review-decides-not-to-renew-private-debt-collection-contracts>.

48 Data obtained from Taxpayer Advocate Management Information System (TAMIS).

Of taxpayers who entered into installment agreements while their debts were assigned to private collection agencies, 40 percent had incomes at or below their allowable living expenses, meaning they agreed to pay the IRS when they were unable to pay their basic living expenses.

**FIGURE 1.19.2**

**Disposition of TAS Private Debt Collection Cases, FY 2018**



**PCA Installment Agreements, Often With Taxpayers Whose Allowable Living Expenses Exceed Their Incomes, Have High Default Rates**

Taxpayers who enter into IAs outside the PDC program default on their IAs, streamlined or not, at an overall rate of around 14 percent.<sup>49</sup> Overall, taxpayers who enter into *streamlined* IAs while their accounts are assigned to the IRS’s ACS function default around 19 percent of the time.<sup>50</sup> Figure 1.19.3 shows the relationship of income to ALEs of taxpayers who entered into IAs while their debts were

49 IRS, Collection Activity Report, *IA Default Report FY 2018 For 12 Month Period Ending Cycle: 201839*, showing a 14.09 percent overall IA default rate and a 14.32 overall default rate for streamlined IAs.

50 *Id.* According to the IRS, “PCAs offer payment arrangements to taxpayers in a manner consistent with IRS installment agreement procedures for similarly situated taxpayers who call the IRS.”

assigned to PCAs and the rate at which they defaulted on their IAs.<sup>51</sup> For purposes of the comparison, income was the amount shown on the taxpayers' 2017 return, or, if no return was filed, the sum of third-party reports of the taxpayer's income for 2017. If no return was filed and there were no third-party reports of income, the taxpayer's income was assumed to be zero. In some cases, taxpayers made no payments on their IAs, yet remain in PCA inventory, a phenomenon discussed below.

**FIGURE 1.19.3, Relationship of Income to Allowable Living Expenses of 43,579 Taxpayers Who Entered Into Streamlined Installment Agreements While Their Debts Were Assigned to PCAs and Default Rates<sup>52</sup>**

Income Compared to ALEs	Number of Taxpayers	Percent of Taxpayers	Number of Taxpayers Who Defaulted	Percent of Taxpayers Who Defaulted
Taxpayers With Income At or Below Their ALEs	17,596	40%	6,440	37%
Taxpayers With Income Above Their ALEs	25,983	60%	9,613	37%
<b>Total</b>	<b>43,579</b>	<b>100%</b>	<b>16,053</b>	<b>37%</b>

As Figure 1.19.3 shows, of taxpayers who entered into IAs while their debts were assigned to PCAs, 40 percent had incomes at or below their ALEs, meaning they agreed to pay the IRS when they were unable to pay their basic living expenses.<sup>53</sup> Whether or not taxpayers' ALEs exceeded their incomes, the default rate was the same. The difference between these two groups is that according to IRS standards, taxpayers in the former category (those whose ALEs exceed their incomes) agreed to make payments they could not afford.

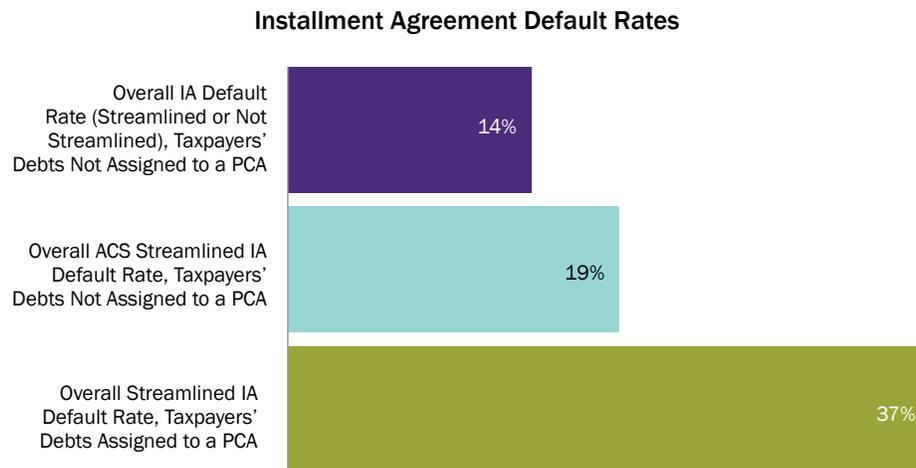
51 ARDI, IRTF, IRMF, CDW data, reflecting activity since the inception of the PDC program in April of 2017 through FY 2018. We identified IAs by searching for modules with a Transaction Code (TC) 971 and Action Code (AC) 63. We identified defaults as IA taxpayers posting a TC 971 AC 163 on any module that entered IA status and that was not fully resolved. The IRS recommended identifying IAs by further restricting the search to taxpayers whose accounts not only bear the TC 971 AC 63, but also have a value in the "Miscellaneous" field of 1, 2, 3, or 4 (corresponding to one of the PCAs). IRS response to fact check (Dec. 17, 2018). When we adopt the IRS's methodology for identifying IAs, we find 7,961 fewer taxpayers who entered into IAs while their debts were assigned to PCAs, 41 percent of whom had incomes at or below their ALEs, and an overall default rate of 23 percent. The difference of 7,961 IAs could represent taxpayers whose debts were assigned to a PCA, but who then entered into an IA with the IRS instead. Because removing these 7,961 IAs reduces the default rate from 37 percent to 23 percent, the question arises whether PCAs always treat IAs as defaulted when appropriate, a concern supported by other data in this report such as the length of time cases remain in PCA inventory with no payment, discussed below. Moreover, when a taxpayer enters into an IA with the IRS, IRS procedures require it to recall the case from the PCA, and the IRS only recalled 4,801 cases due to "Active IA" (leaving 3,160 of the 7,961 cases unaccounted for). The IRS appears to record at least some of these recalled cases as defaulted IAs, while at the same time recording the status of the case as the taxpayer having an IA with the IRS. However, we cannot definitively explain the discrepancy the different methods create. We note that the IRS and TIGTA have encountered similar difficulties in determining the default rate of PCA IAs, but TIGTA found that the overall default rate was 53 percent, which is even higher than the default rate we report here. See TIGTA, Ref. No. 2019-30-018, *Fiscal Year 2019 Biannual Independent Assessment of Private Collection Agency Performance* 4 (Dec. 31, 2018).

52 The values in Figure 1.19.3 reflect the calculation of allowable transportation expenses, described above, in which taxpayers are allowed vehicle ownership and operating expenses. If vehicle ownership expenses are not allowed, and two allowances for vehicle operating expenses are included where the taxpayers filed a joint return and one operating allowance is included for all other taxpayers, then 14,582 taxpayers (33 percent) had incomes at or below their ALEs and 28,997 taxpayers (67 percent) had incomes above their ALEs.

53 Of the 17,596 taxpayers with incomes at or below their ALEs, 3,552 were assumed to have no income because for tax year 2017 they did not file a return and there were no third-party reports of income for them. It is possible that some of these taxpayers may have had unreported income.

Figure 1.19.4 shows overall IA default rates of taxpayers whose debts were not assigned to PCAs, the overall ACS IA default rate for streamlined IAs, and the overall default rate for taxpayers who entered into streamlined IAs while their debts were assigned to PCAs.

**FIGURE 1.19.4**



### Taxpayers, Including Disabled Taxpayers, Make Commissionable Payments They Cannot Afford

Not only do taxpayers whose debts are assigned to PCAs agree to make payments they cannot afford, some taxpayers actually make payments even though their ALEs exceed their incomes. Figure 1.19.5 shows the proportion of commissionable payments overall made by taxpayers according to the relationship between their incomes and their ALEs.

**FIGURE 1.19.5, Commissionable Payments Taxpayers Made While Their Debts Were Assigned to PCAs<sup>54</sup>**

Income Compared to ALEs	Commissionable Payments	Percent
Taxpayers With Income At or Below Their Allowable Living Expenses	\$29,196,941	34%
Taxpayers With Income Above Their Allowable Living Expenses	\$56,019,574	66%
<b>Total</b>	<b>\$85,216,515</b>	<b>100%</b>

54 ARDI, IRTF, IRMF, CDW, reflecting activity on tax modules with an unreversed TC 971 with an AC 054 from program inception through FY 2018. The total amount of commissionable payments (\$85,216,515) shown on these IRS databases differs from the amount reported in the IRS Quarterly Update to Congress, *Private Debt Collection (PDC) Program 1*, for FY 2018 (\$80,736,597), which was prepared using the Custodial Detail Database (CDDb), part of the Financial Management Information System (FMIS). When vehicle ownership expenses are not allowed, then \$25,503,439, or 30 percent was paid by taxpayers whose incomes were at or below their ALEs and \$59,713,076, or 70 percent, was paid by taxpayers whose incomes were above their ALEs.

Thus, a third of the dollars that were collected as a result of PCA activity were collected from taxpayers who could not afford the payments they made.

As discussed above, the National Taxpayer Advocate ordered the IRS to exclude from assignment to PCAs the debts of taxpayers whose incomes are below 250 percent of the FPL.<sup>55</sup> As Figure 1.19.6 demonstrates, of taxpayers who *made commissionable payments* while their debts were assigned to PCAs, 24 percent had incomes *at or below the federal poverty level*. An additional 20 percent had incomes above the federal poverty level to 250 percent of the FPL.<sup>56</sup>

**FIGURE 1.19.6, Relationship of Income to the Federal Poverty Level of 45,371 Taxpayers Who Made Payments While Their Debts Were Assigned to PCAs and Median Amount Paid<sup>57</sup>**

Income Compared to Poverty Level	Number Of Taxpayers	Percent of Taxpayers	Median Amount Paid	Average Income	Median Income
Income At or Below Federal Poverty Level	10,891	24%	\$671	\$3,619	\$890
Income Above Federal Poverty Level up to 250% of Federal Poverty Level	9,119	20%	\$515	\$24,465	\$23,104
Income Above 250% of Federal Poverty Level	25,361	56%	\$780	\$118,640	\$66,351
<b>Total</b>	<b>45,371</b>	<b>100%</b>			

The failure to exclude these low income taxpayers inflicts real harm on vulnerable people.

The 45,371 taxpayers who made payments while their debts were assigned to PCAs shown in Figure 1.19.6 includes 1,031 taxpayers who were Social Security Disability Insurance (SSDI) recipients in 2017.<sup>58</sup> According to the Social Security Administration (SSA):

- SSDI recipients generally could not earn over \$1,180 per month in 2018 without losing their benefits;<sup>59</sup> and
- In 2018, the average monthly amount of disability paid was \$1,197.<sup>60</sup>

55 The federal poverty level is based on family size and varies from year to year. The federal poverty level for a single person was \$12,060 in 2017. U.S. Dept. of Health and Human Resources, Poverty Guidelines (2017), <https://aspe.hhs.gov/2017-poverty-guidelines>. 250 percent of \$12,060 is \$30,150.

56 ARDI, IRTF, IRMF, CDW, reflecting activity since the inception of the PDC program in April 2017 through FY 2018.

57 Of the 10,891 taxpayers with incomes at or below the federal poverty level 4,057 were assumed to have no income because for tax year 2017 they did not file a return and there were no third-party reports of income for them. It is possible that some of these taxpayers may have had unreported income.

58 The IRS agreed to exclude from assignment to PCAs the debts of Social Security Disability Insurance (SSDI) and Supplemental Security Income (SSI) recipients. National Taxpayer Advocate 2017 Annual Report to Congress 10, 17 (Most Serious Problem: *The IRS's Private Debt Collection Program Is Not Generating Net Revenues, Appears to Have Been Implemented Inconsistently with the Law, and Burdens Taxpayers Experiencing Economic Hardship*). The IRS has not honored that commitment. If a taxpayer discloses to a PCA that he or she receives SSDI or SSI benefits, the PCA is required to return the case to the IRS. Payments of SSDI benefits (but not SSI benefits) are reported to the IRS on Form SSA-1099.

59 SSA, *Working While Disabled: How We Can Help* 3 (2018), noting "After your trial work period, you have 36 months during which you can work and still receive benefits for any month your earnings aren't 'substantial.' In 2018, we consider earnings over \$1,180 (\$1,970 if you're blind) to be substantial."

60 SSA, *The Facts about Social Security's Disability Program* 1 (2018).

Thus, a taxpayer receiving income of \$1,180 per month (the maximum amount allowed) and the average amount of disability paid in 2018 would earn \$28,524. IRS records show that for the 1,031 taxpayers who received SSDI:

- Median income was \$20,312;
- Average income was \$35,290;<sup>61</sup>
- The average amount they paid was \$1,556; and
- The median amount they paid was \$453.<sup>62</sup>

As discussed above, the IRS has refused to exclude from assignment to PCAs the debts of taxpayers whose incomes are below 250 percent of the federal poverty level, citing lack of statutory authority to do so.<sup>63</sup> The National Taxpayer Advocate continues to believe the IRS has the discretion, under IRC § 6306, to exclude these taxpayers' accounts from referral to PCAs.<sup>64</sup> In addition, the National Taxpayer Advocate believes that in light of Congress's direction that the IRS develop ALE standards, the IRS is authorized to exclude from assignment to PCAs the debts of taxpayers whose incomes are at or below their ALEs.

### PCAs May be Improperly Retaining Some Cases, and Procedures Should be Modified to Expand the Types of Cases PCAs Must Return to the IRS to Prevent PCAs From Creating Queues of Inactive Cases

PCAs are required to return cases to the IRS in a variety of situations and to compile reports that categorize the reason for the returns.<sup>65</sup> In FY 2018, through September 13, 2018, PCAs returned 15,796 cases.<sup>66</sup> Currently, the IRS does not appear to know the number of returns in each category, except for cases returned because the taxpayer stated he or she received Supplemental Security Income (SSI) *or* SSDI benefits (5,046 cases); or the taxpayer submitted a written request that the PCA cease contacting the taxpayer (2,845 cases).<sup>67</sup>

61 Income includes the spouse's income, where the taxpayer filed a joint return, although the spouse may not have been an SSDI recipient.

62 ARDI, IRTF, IRMF, CDW, reflecting activity since the inception of the PDC program in April 2017 through FY 2018.

63 See June 20, 2018, Memorandum from Deputy Director for Services and Enforcement, rescinding the National Taxpayer Advocate's April 23, 2018 Taxpayer Advocate Directive, published in the National Taxpayer Advocate Fiscal Year 2019 Objectives Report to Congress 75. As discussed above, the IRS has not felt similarly constrained by the temporal limit of IRC § 6303(b), which allows PCAs to offer IAs "for a period not to exceed 5 years," or by the definition in IRC § 6303(b) which defines a "qualified tax collection contract" as a contract pursuant to which PCAs "obtain financial information specified by the Secretary with respect to such taxpayer," among other things.

64 A recent proposal in Congress would exclude taxpayers having "substantially all" of their incomes comprised of SSDI or SSI from having their debts assigned to a PCA. The proposal would also exclude taxpayers whose incomes are at or below 200 percent of the federal poverty level from having their debts assigned to a PCA. See Taxpayer First Act of 2018, H.R. 7227, 115th Cong. § 1205 (2018).

65 Included among the categories of reasons for returning a case are: the taxpayer indicated he or she would send a one-time voluntary payment; the taxpayer indicated he or she is unable to pay; and the taxpayer informs the PCA that he or she is a recipient of SSI/SSDI benefits. PPG § 17.1.3, *Return Tracking Report*. Where the only liability is for the individual shared responsibility (ISRP) and the taxpayer disagrees with the assessment, PCAs are directed to return the case to the IRS, but there is not a separate return category for this type of case. IRS response to TAS information request (Aug. 14, 2018). None of the 3,243 taxpayers whose ISRP debts were assigned to PCAs by FY 2018 were liable solely for the ISRP. Defaulted IA are returned to the IRS but not separately identified or tracked. IRS response to TAS information request (Apr. 10, 2018).

66 PDC Program Scorecard from program for FY 2018 through Sept. 13, 2018.

67 In response to TAS's request for reports from the PCAs that show a breakdown of the reasons the PCAs returned accounts to the IRS, the IRS responded that "RAAS [IRS Research, Applied Analytics, and Statistics] is in the process of analyzing the returned accounts data and it will be another few months before we can provide any accurate and meaningful report on this data." IRS response to TAS information request (Oct. 31, 2018).

### *PCAs May Be Impermissibly Retaining Cases After Soliciting More Than One Voluntary Payment*

One area that raises the concern that PCAs may be improperly retaining accounts is where there appear to be “voluntary payments.” Voluntary payments are payments that do not fully pay the liability and are not made pursuant to an IA. PCAs are permitted to solicit only *one* voluntary payment, and only from a taxpayer who “can make payments, but will not full pay within the Collection Statute Expiration Date (CSED) or seven years, whichever is less.”<sup>68</sup> After soliciting a voluntary payment, PCAs must return the case to the IRS.<sup>69</sup>

In response to TAS’s inquiry about its oversight in this area, the IRS responded:

Although it is not uncommon for taxpayers to make payments on their accounts without a formal agreement, we asked the PCAs to review these accounts and provide their findings. The PCAs on a regular basis will identify these accounts and include them in their dialing campaigns to attempt to establish payment arrangements.<sup>70</sup>

Thus, it remains unclear from the IRS’s response whether the IRS has developed an adequate mechanism for distinguishing cases in which PCAs solicited more than one voluntary payment from cases in which taxpayers make these payments without any solicitation from the PCAs. Allowing PCAs to secure “voluntary” payments that do not resolve the liability (while interest continues to accrue on the unpaid liability) circumvents the statutory protections of an IA (such as protection against levy) and violates taxpayers’ *right to finality*.

At the end of FY 2018, PCA inventory included the debts of 4,753 taxpayers who had made two or more commissionable payments, yet had not entered into an IA and had not paid their debts in full.<sup>71</sup> This suggests that even if they can afford to make payments, the limited payment alternatives PCAs can offer do not meet their needs. These taxpayers’ debts had been in PCA inventory for 204 days on average.<sup>72</sup>

### *PCAs Appear to be Retaining Cases With Defaulted Installment Agreements Without Informing the IRS as Required*

An area that raises concern about the IRS’s policy of allowing PCAs to retain inventory involves defaulted IAs. When a taxpayer misses three IA payments within a rolling 12-month period, the PCA is required to terminate the IA and inform the IRS that the IA has been terminated.<sup>73</sup> The PCA is not required to return the account to the IRS, however, unless it contacts the taxpayer and the taxpayer states that he or she is unable to restructure the IA to pay the total liability in full within the seven years (or the period of limitations on collection, if earlier).<sup>74</sup>

At the end of FY 2018, PCA inventory included the debts of 3,222 taxpayers who had entered into IAs while their debts were assigned to PCAs and had made *no* payment for more than 120 days after

68 PPG § 10, *Payment Options*.

69 PPG § 10.2.1, *Voluntary Payments*.

70 IRS response to TAS information request (Aug. 14, 2018).

71 ARDI, IRTF, IRMF, CDW, reflecting activity since the inception of the PDC program in April 2017 through FY 2018.

72 *Id.*

73 PPG § 11.5.2, *Missed Payments & Restructuring or Terminating Payment Arrangements*.

74 For example, the PPG § 11.5.2, *Missed Payments & Restructuring or Terminating Payment Arrangements* notes: “Reminder: When unable to contact, three missed payments does not require the PCA to return the account to the IRS. All attempts to contact the taxpayer or representative must be documented.”

entering into the IA, yet IRS records did not reflect termination of the IA. These 3,222 cases had been in PCA inventory for 272 days on average.<sup>75</sup> Thus, the PCAs do not appear to be providing the required notification to the IRS that these taxpayers missed more than three IA payments in a 12-month period. Moreover, this fact pattern suggests that the taxpayers are interested in resolving their liabilities, but the payment terms they agreed to, or the PCAs can offer, are inadequate to permit them to do so.

As discussed above and shown in Figure 1.19.3, at the end of FY 2018, there were 43,579 taxpayers who had entered into IAs while their debts were assigned to PCAs, of whom 16,053 are shown on IRS records as having defaulted. If the 3,222 taxpayers who entered into IAs and made no payments for more than 120 days are treated as defaulted IAs, the total number of defaulted would be 19,275, which is 44 percent of 43,579. Thus, the 37 percent overall default rate for IA that taxpayers entered into while their debts were assigned to PCAs rises to 44 percent when defaulted IAs that PCAs do not report to the IRS as required are taken into account.

PCAs also appear to be retaining inventory when there is no payment and no IA, even though the cases had been assigned for at least 90 days.<sup>76</sup> At the end of FY 2018, there were 402,387 of these cases, and they had been in PCA inventory for 244 days on average.<sup>77</sup>

Figure 1.19.7 shows the number of taxpayers whose debts remain in PCA inventory without being resolved.

**FIGURE 1.19.7, Number of Taxpayers Whose Debts Are in PCA Inventory And Are Not Being Resolved**

	Number of Taxpayers	Average Number of Days Elapsed After Assignment	Median Number of Days Elapsed After Assignment
Two or More Commissionable Payments and No IA or Full Payment	4,753	204	146
IA and No Payment For More Than 120 Days (Excluding Defaults, Recalled Cases, and Returned Cases)	3,222	272	279
No IA or Payment For More Than Three Months After Assignment (Excluding Recalled Cases and Returned Cases)	402,387	244	195
<b>Total</b>	<b>410,362</b>	<b>244</b>	<b>195</b>

75 CDW data, reflecting activity since the inception of the PDC program in April 2017 through FY 2018.

76 The IRS does not require PCAs to return these cases to the IRS, directing only that “The PCA must return an account to the IRS anytime the PCA is unable to collect and has exhausted all reasonable collection efforts.” PPG § 12.3, *Unable to Collect*.

77 CDW data, reflecting activity since the inception of the PDC program in April 2017 through FY 2018.

Allowing PCAs to retain inactive cases defeats the purpose of the PDC program because even where the PCA succeeds in contacting the taxpayer, the liability is not being resolved. Moreover, assignments that effectively become permanent allow PCAs to collect commissions, no matter how much time elapses:

- Between the date the debt was assigned to the PCA and the date the taxpayer makes a payment; and
- Between the date of any PCA activity and the date a taxpayer makes a payment.

### The IRS Now Assigns to PCAs More Complex Cases and Those With Increased Risk That the Liability May Not Be Owed

The IRS has assigned to PCAs the liabilities of about 400,000 taxpayers who did not dispute their liability for any year assigned to a PCA.<sup>78</sup> In FY 2018, this category of cases included, for the first time, liability for the individual shared responsibility payment (ISRP).<sup>79</sup>

As part of “Release 2” of the program, the IRS also assigned cases in which the only tax liability was assessed:

- Based on substitutes for returns;<sup>80</sup>
- Pursuant to the Automated Underreporter (AUR) computer matching system; or
- When the taxpayer did not respond, or stopped responding, to IRS inquiries pursuant to an audit.

By the end of FY 2018, over 150,000 of these cases had been assigned.<sup>81</sup> These cases implicate significant taxpayer rights, particularly the *right to pay no more than the correct amount of tax*, and are subject to additional protections and procedures. For example, taxpayers may seek audit reconsideration with respect to these assessments.<sup>82</sup> If the IRS refuses, after reconsideration, to abate an assessment, taxpayers are entitled to an appeals conference with the IRS Office of Appeals.<sup>83</sup> Moreover, these types of cases have an increased risk that all or part of the liability may not be owed, so that abatement would be appropriate, including penalty abatement.<sup>84</sup> The IRS instructs PCA employees to refer taxpayers who

78 ARDI, IRTF, IRMF, CDW data, reflecting activity since the inception of the PDC program in April 2017 through FY 2018, showing assignment of 412,535 of these cases. See PPG § 12.22, *Compliance Assessments*, noting that “[i]n the first release of inventory, the IRS provided PCAs with tax accounts where the taxpayer reported and calculated the assessable tax.”

79 As noted above, all the taxpayers who were assessed liability for ISRP also had assessments from another source.

80 If the taxpayer failed to file a timely return, the IRS may make a return, referred to as a substitute for return (SFR), as authorized by IRC § 6020(b), based on information reported to the IRS. The SFR may reflect income reported by third parties, but allows only the standard deduction, one exemption (for returns filed prior to tax year 2018), and a filing status of single or married filing separately. See IRM 4.12.1.25.3, *Itemized Personal Deductions* (Oct. 5, 2010); IRM 4.12.1.24.12, *Married Filing Joint Election for Nonfiler cases* (Oct. 5, 2010). See also *Allowable Expenses in an SFR*, <http://mysbse.web.irs.gov/reflibrary/kts/supparticles/14979.aspx>.

81 ARDI, IRTF, IRMF, CDW data, reflecting activity since the inception of the PDC program in April 2017 through FY 2018, showing assignment of 38,352 SFR-only assessments; 63,989 Automated Underreporter-only assessments; and 51,701 audit default-only assessments, for a total of 154,042 cases.

82 See, e.g., IRM 4.13.1.2, *Definition of an Audit Reconsideration* (Dec. 16, 2015).

83 See IRM 5.1.15.4.6.4, *Appeal Rights on Reconsiderations* (Apr. 16, 2010).

84 See, e.g., National Taxpayer Advocate 2004 Annual Report to Congress, vol. 2 1, (Research Study: *EITC Audit Reconsideration Study*), demonstrating that 43 percent of taxpayers who sought reconsideration of audits that disallowed the EITC in whole or in part received additional EITC as a result of the audit reconsideration. See also National Taxpayer Advocate 2012 Annual Report to Congress, vol. 2 74, (Research Study: *Study of Tax Court Cases In Which the IRS Conceded the Taxpayer was Entitled to Earned Income Tax Credit (EITC)*) discussing a TAS study of a random sample of cases in which the IRS denied a claim for EITC but conceded the issue after the taxpayer petitioned the Tax Court for review.

dispute these assessments to the IRS, but the PCAs are not required to return the cases to the IRS.<sup>85</sup> In contrast, the prior iteration of the IRS's PDC initiative required PCAs to refer cases in which taxpayers disputed their liability to the Referral Unit, which would attempt to resolve the dispute within 30 days.<sup>86</sup>

Release 2 cases also include those in which the taxpayer did not file a return which, according to IRS records, was required to be filed (referred to as a delinquent return). PCAs are instructed that taxpayers must file delinquent returns with the IRS as a condition to entering into an IA. However, IRS records indicating a return was required are not always accurate. For example, in FY 2014, 21 percent of the accounts the IRS identified as delinquent were not actually those of nonfilers (*i.e.*, a return had actually been filed) or there was little or no tax due.<sup>87</sup> If a taxpayer states the return was filed, the PCA is to monitor the case for 30 days to give a recently-filed return time to post, or, if the return hasn't appeared in IRS records after ten weeks, the PCA is to advise the taxpayer to re-submit the return.<sup>88</sup> There are no procedures directing PCAs how to handle cases in which the taxpayer asserts he or she was not required to file a return. In any event, once an IA has been created, the failure to file a required return does not cause the IA to terminate.<sup>89</sup>

The IRS held a PDC Engagement Conference on February 14-15, 2018, to train PCA employees how to handle Release 2 cases.<sup>90</sup> By then, TAS had published data showing that a significant portion of taxpayers whose debts were assigned to PCAs could not afford the payments they made.<sup>91</sup> The training provided to PCAs did not include information about ALEs, even though that instruction might have lessened the impact the PDC program has on taxpayers who appear to be experiencing economic hardship.<sup>92</sup> This omission demonstrates the IRS does not take seriously the harm imposed on vulnerable taxpayers.

## CONCLUSION

With unacceptable frequency, the IRS PDC initiative as implemented continues to burden taxpayers who, according to IRS standards, cannot afford to pay for their basic living expenses. There are insufficient safeguards to prevent taxpayers' debts from remaining with PCAs indefinitely, even where PCA activity does not result in payments by taxpayers. Increasingly, the PCA inventory is simply substituting for the IRS inventory queue, with PCAs receiving commissions on payments that are not attributable to PCA activity.

85 PPG § 12.22, *Compliance Assessments*.

86 PPG § 12.15, *Taxpayer Disputes* (July 1, 2008 version).

87 See National Taxpayer Advocate 2014 Annual Report to Congress 197, 202 (Most Serious Problem: *Federal Payment Levy Program: Despite Some Planned Improvements, Taxpayers Experiencing Economic Hardship Continue to Be Harmed by the Federal Payment Levy Program*).

88 PPG § 11.1, *Delinquent Returns*.

89 *Id.*, noting that “[a] delinquent return indicator received after the account is in a payment arrangement status, as indicated by TRCAT 080, does not create a default or termination of the arrangement.”

90 IRS responses to TAS information request (Aug. 14 and Oct. 10, 2018).

91 National Taxpayer Advocate 2017 Annual Report to Congress 10, 11 (Most Serious Problem: *The IRS's Private Debt Collection Program Is Not Generating Net Revenues, Appears to Have Been Implemented Inconsistently with the Law, and Burdens Taxpayers Experiencing Economic Hardship*, reporting that 44 percent of taxpayers who made payments while their debts were assigned to PCAs had incomes below 250 percent of the federal poverty level, and vol. 2 Research Study: *Study of Financial Circumstances of Taxpayers Who Entered Into Installment Agreements and Made Payments While Their Debts Were Assigned to Private Collection Agencies*, reporting that of taxpayers who entered into an IA and made commissionable payments while their debts were assigned to a PCA, 46 percent had incomes less than their ALEs.).

92 IRS response to TAS information request, providing the training materials (Oct. 10, 2018).

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Exclude from assignment to PCAs the debts of taxpayers whose incomes are at or below their allowable living expenses.
2. Work with the Social Security Administration to identify recipients of Social Security Disability Insurance and Supplemental Security Income and exclude those taxpayers' debts from assignment to PCAs.
3. Revise PDC procedures to require IRS review of all PCA cases in which the taxpayer made more than one payment that did not fully pay the liability and was not made pursuant to an IA, to determine whether the PCA requested more than one payment from a taxpayer who can make payments, but cannot fully pay the liability within the Collection Statute Expiration Date (CSED) and if so:
  - a. Recall the case from the PCA;
  - b. Impose a penalty on the PCA for requesting more than one such payment without returning the case to the IRS; and
  - c. Assign an IRS employee to work the case.
4. Revise PDC procedures to:
  - a. Require PCAs to return to the IRS cases in which the taxpayer entered into an installment agreement but made no payments for 120 days thereafter; and
  - b. Assign an IRS employee to work the case.
5. Revise PDC procedures to require PCAs to return to the IRS cases in which the taxpayer did not enter into an IA and did not make any payments within six months of assignment to the PCA.

**MSP  
#20****PRE-TRIAL SETTLEMENTS IN THE U.S. TAX COURT: Insufficient Access to Available Pro Bono Assistance Resources Impedes Unrepresented Taxpayers From Reaching a Pre-Trial Settlement and Achieving a Favorable Outcome****RESPONSIBLE OFFICIALS**

William M. Paul, Acting Chief Counsel  
 Mary Beth Murphy, Commissioner, Small Business/Self-Employed Division  
 Donna Hansberry, Chief, IRS Office of Appeals

**TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Be Informed*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Retain Representation*
- *The Right to a Fair and Just Tax System*

**DEFINITION OF PROBLEM**

Taxpayers unable to afford representation to defend against a potential IRS assessment or collection action may believe there are only two courses of action: do nothing, or proceed unrepresented.<sup>2</sup> When it comes to civil justice problems involving money or housing, poor households are twice as likely to do nothing than moderate-income households, according to legal scholars.<sup>3</sup>

The U.S. Tax Court is the only prepayment judicial forum for taxpayers to resolve their disputes with the IRS. More than 80 percent of cases in Tax Court are brought by unrepresented taxpayers, and that percentage increases to almost 94 percent among cases where the deficiency for a tax year is \$50,000 or

1 See Taxpayer Bill of Rights (TBOR), [www.taxpayerAdvocate.irs.gov/taxpayer-rights](http://www.taxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 Unlike in the context of criminal cases, litigants in civil cases with limited means have no right to counsel. See *Gideon v. Wainwright*, 372 U.S. 335 (1963). However, Congress has codified the TBOR, including the *right to retain representation* in dealings with the IRS, which includes the right to seek assistance from a Low Income Taxpayer Clinic (LITC) if the taxpayer cannot afford to hire a representative. See IRC § 7803(a)(3) and TBOR, [www.taxpayerAdvocate.irs.gov/taxpayer-rights](http://www.taxpayerAdvocate.irs.gov/taxpayer-rights).

3 Rebecca L. Sandefur, *The Fulcrum Point of Equal Access to Justice: Legal and Non-Legal Institutions of Remedy*, 42 *Lox. L.A. L. Rev.* 949, 972-973 (2009); see also Marc Galanter, *Why The "Haves" Come Out Ahead: Speculations on the Limits of Legal Change* (1974) 9 *LAW & Soc'y REV.* 95, 99-100, fn. 11 (suggesting modest income claimants less familiar with litigation will be risk averse and consequently less attracted by uncertain gains and more apprehensive about the potential losses of litigation).

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When it comes to civil justice problems involving money or housing, poor households are twice as likely to do nothing than moderate-income households, according to legal scholars.

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less and the taxpayer elects small tax case (S Case) procedures.<sup>4</sup> The portion of self-represented litigants in Tax Court is consistent with litigants in civil cases in other state and federal courts.<sup>5</sup>

For over 20 years, Tax Court judges have steadfastly supported programs such as the Clinical, Student Practice & Bar Sponsored Calendar Call Program to bring together unrepresented litigants and representatives offering *pro bono* assistance.<sup>6</sup> More recently, programs such as *Pro Bono Days* seek to encourage resolution of litigation 30 days or more before the scheduled trial date. Despite broad-based institutional support for programs, and high rates of same-day resolution for attendees, taxpayer participation rates remain inconsistent. The National Taxpayer Advocate is concerned efforts to provide unrepresented petitioners access to free, competent advice are being undercut and underused because of ineffective outreach and lack of consistent guidance between the IRS Chief Counsel and *pro bono* representatives which undermine the taxpayers' *rights to be informed, to retain representation, and to a fair and just tax system*, and increases the burden on the Tax Court.

## ANALYSIS OF PROBLEM

### Background

#### *Litigating a Controversy in Tax Court*

A taxpayer can obtain judicial review of an IRS liability determination by the Tax Court, a district court, the U.S. Court of Federal Claims, or the Bankruptcy Court.<sup>7</sup> For a taxpayer unable to afford to hire someone for representation, the Tax Court is particularly accessible because it is the only pre-payment forum for judicial review (other than the Bankruptcy Court).<sup>8</sup> To accommodate the

4 American Bar Association (ABA), Tax Section Court Procedure Committee, Office of Chief Counsel, IRS, fiscal year (FY) 2017 PowerPoint presentation, slides 18, 13. A taxpayer may elect the “small tax case” procedure, known as S case procedures, for cases involving up to \$50,000 in deficiency per year (including penalties and other additions to tax, but excluding interest). S cases have advantages; they are less formal, and can be heard in about 15 more cities than regular cases, [https://www.ustaxcourt.gov/taxpayer\\_info\\_start.htm](https://www.ustaxcourt.gov/taxpayer_info_start.htm).

5 According to *The Justice Index*, a project of the National Center for Access to Justice at the Fordham Law School, as many as two-thirds of litigants appear without lawyers in matters as important as evictions, mortgage foreclosures, child custody and child support proceedings, and debt collection cases in state courts. *The Justice Index 2016*, <http://www.justiceindex.org/> (last visited Sept. 20, 2018). See also Memorandum from Lisa Wood, Chair, ABA Standing Comm. on Legal Aid and Indigent Defendants, to Fin. Comm., Bd. of Dirs., Legal Serv. Corp. 2 (June 2, 2014) (reporting a “trend toward involuntary self-representation”).

6 Keith Fogg, *History of Low-Income Taxpayer Clinics*, 67 *TAX LAW.* 1, 77 (2014).

7 With limited exceptions, taxpayers have an automatic right of appeal from the decisions of any of these courts. See IRC § 7482, which provides that the United States Courts of Appeals (other than the United States Court of Appeals for the Federal Circuit) have jurisdiction to review the decisions of the Tax Court. See also 28 U.S.C. § 1294 (appeals from a United States District Court are to the appropriate United States Court of Appeals); 28 U.S.C. § 1295 (appeals from the United States Court of Federal Claims are heard in the United States Court of Appeals for the Federal Circuit); 28 U.S.C. § 1254 (appeals from the United States Courts of Appeals may be reviewed by the United States Supreme Court).

8 IRC §§ 6212, 6213. The 90-day period becomes 150 days if the notice is mailed to a foreign address. *Id.* The IRS may also assess tax without first sending a notice of deficiency if it determines that collection is in jeopardy. See IRC §§ 6851, 6861, 6862, 6871. The IRS can assess certain “assessable” penalties without sending a notice of deficiency or otherwise triggering the Tax Court’s jurisdiction. For example, the penalties in Subchapter B (i.e., IRC §§ 6671-6725) are expressly excluded from the deficiency process. See IRC § 6671(a); *Smith v. Comm’r*, 133 T.C. 424, 428 n.3 (2009).

numerous unrepresented taxpayers who nonetheless want to exercise their rights, the Tax Court uses rather informal procedures, which are even more relaxed if the disputed issue does not exceed \$50,000.<sup>9</sup> As a result, the Tax Court hears over 90 percent of all federal civil tax cases.<sup>10</sup>

To bring a matter before the United States Tax Court, a taxpayer must act by timely filing a petition with the court. If the IRS proposes a deficiency or seeks to enforce a collection action on a taxpayer and the taxpayer does nothing, the Tax Court will not have jurisdiction over the matter.<sup>11</sup> Approximately five months before each calendar call, the Tax Court sends a notice of trial to each petitioner granted a hearing and to the Commissioner of Internal Revenue, indicating the location and time scheduled for the hearing. Generally, Tax Court calendar calls are held one to two times per year in each city where the Tax Court hears cases, although they can occur more frequently, depending on local need.<sup>12</sup>

To efficiently handle cases, the Tax Court typically schedules many hearings on the first day of a calendar call session. Each party is “called” before the judge to set hearings and trials and schedule the court’s “calendar” for the week. Thus, it is known as a “calendar call.” Some Tax Court hearings are resolved in a matter of minutes, while others take longer.

### *Tax Court Encourages Pro Bono Representation of Pro Se Litigants*

To help bring together *pro bono* counsel and unrepresented taxpayers, the Tax Court established the Clinical, Student Practice & Bar Sponsored Calendar Call Program. Since before 1998, judges have allowed approved representatives offering *pro bono* assistance into their court and announced to petitioners that *pro bono* tax lawyers are available to help them.<sup>13</sup> Under the terms of the program, the Court invites academic and nonacademic tax clinics and state bar sponsored organizations to attend calendar calls, and the presiding judge typically announces the availability of no cost assistance, introduces the group or groups of volunteers, and encourages unrepresented litigants to consult with them. The program has grown and now covers a considerable number of calendar call locations.<sup>14</sup> The majority of organizations participating in the program are Low Income Taxpayer Clinics (LITCs), although other organizations that meet the Court’s eligibility requirements also provide assistance.<sup>15</sup> Students and law graduates working at an LITC may be authorized to represent taxpayers before the IRS.<sup>16</sup>

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- 9 IRC § 7463 provides special procedures for small Tax Court cases (where the amount of deficiency or claimed overpayment totals \$50,000 or less) for which appellate review is not available.
- 10 *The Future State of Tax Court Practice and Litigation: An Exploration of Current and Future Issues that Could Affect the Way the Court Does Business*, United States Tax Court Judicial Conference 2 (Chicago, IL Mar. 26–28, 2018) (conference outline).
- 11 The taxpayer must file a timely petition, within 90 days of the deficiency notice’s date (150 days, if the deficiency notice is addressed to a taxpayer outside the U.S.), giving some indication that he contests the deficiency. The taxpayer must attach the deficiency notice to the petition. IRC § 6213(a) and TC Rules 20 – 34. The deficiency notice specifies the deadline for filing the petition. If the deadline is later than 90 days, the later deadline is binding. IRC § 6213(a).
- 12 All 19 Tax Court judges have offices at the court’s Washington, D.C. location. The judges travel to conduct trials in 74 cities nationwide; the Tax Court holds trials only for S cases in 15 of the 74 cities.
- 13 Keith Fogg, *History of Low-Income Taxpayer Clinics*, 67 *TAX LAW.* 1, 77 (2014).
- 14 *Id.*
- 15 See *Requirements for Participation in the United States Tax Court Clinical, Student Practice & Calendar Call Program by Academic Clinics (Law School)*, [https://www.ustaxcourt.gov/clinics\\_academic.htm#SECTION1](https://www.ustaxcourt.gov/clinics_academic.htm#SECTION1).
- 16 The LITC must obtain a special appearance authorization for those students and law graduates from the LITC Program Office. Practice under a special appearance authorization issued by the Director of the LITC Program Office is limited to students and law graduates at an LITC or Student Tax Clinic Program working under the direct supervision of an individual authorized to practice before the IRS.

The Tax Court's primary outreach method for informing petitioners about obtaining legal assistance from local tax clinics and state bar sponsored organizations is the "Stuffer Program." Taxpayers who indicated in their petition that they did not have representation receive information about legal assistance programs from the Tax Court several times:

- With the letter acknowledging receipt of the petition;
- With the notice of trial; and
- 30 days prior to the trial session.

The Tax Court Clinical Student Practice & Bar Sponsored Calendar Call Program provides an opportunity for an unrepresented taxpayer to interact with a *pro bono* attorney. However, an attorney meeting with a client for the first time on the day the case is scheduled to be heard by a judge is not ideal. Unrepresented taxpayers often show up at the calendar call, or at the trial—which the judge may decide to conduct on the same day—unprepared to try a case, or with documents that the taxpayer is presenting to the IRS for the first time. Furthermore, only 25 of the 74 cities where the Tax Court holds trials have a room reserved for persons admitted to practice before the Court, including attorneys associated with tax clinics and Bar sponsored calendar call programs, to meet privately with petitioners.<sup>17</sup> If the parties establish communication prior to the calendar call, they can avoid a host of logistical issues, such as difficulty finding a space to speak privately, being denied access to a federal building because of missing or unacceptable identification, or lack of interpreters.

Some taxpayers contact an LITC or other organization offering aid prior to the calendar call, but many do not. Most taxpayers eligible to receive assistance from an LITC don't even know they exist. According to a 2014 TAS survey of a random sampling of taxpayers eligible to receive LITC assistance, only about 30 percent were aware of an organization outside the IRS that helps taxpayers with IRS problems and only about ten percent of those aware (or about three percent of all taxpayers surveyed) knew the LITC name.<sup>18</sup>

### Litigation Outcomes Show the Importance of Representation as Represented Taxpayers Consistently Fare Better Than Unrepresented

Nearly 27,000 petitions were filed in the Tax Court in Fiscal Year (FY) 2017, and over 22,000 or 83 percent were from unrepresented litigants. Unrepresented taxpayers are more than 2.5 times more likely to have their petition dismissed. For example, in FY 2017, 6,124 *pro se* petitions or about 28 percent were disposed of by default (dismissal) compared to only 411 petitions or less than nine percent of represented taxpayers. Unrepresented taxpayers may have their case dismissed because of a procedural defect and thus are unable to have the court review the merits of their case.<sup>19</sup>

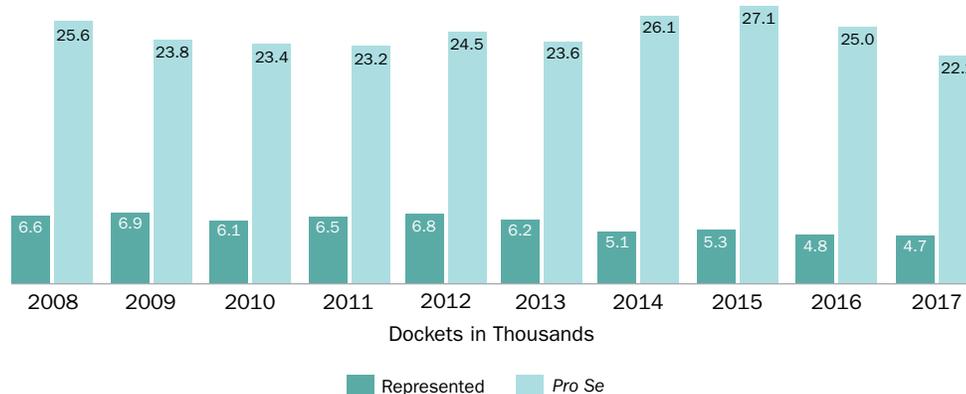
17 See *Requirements for Participation in the United States Tax Court Clinical, Student Practice & Calendar Call Program* by Academic Clinics (Law School), [https://www.ustaxcourt.gov/clinics\\_academic.htm#SECTION1](https://www.ustaxcourt.gov/clinics_academic.htm#SECTION1).

18 See National Taxpayer Advocate 2014 Annual Report to Congress vol. 2 2-26 (Research Study: *Low Income Taxpayer Clinic Program: A Look at Those Eligible to Seek Help From the Clinics*).

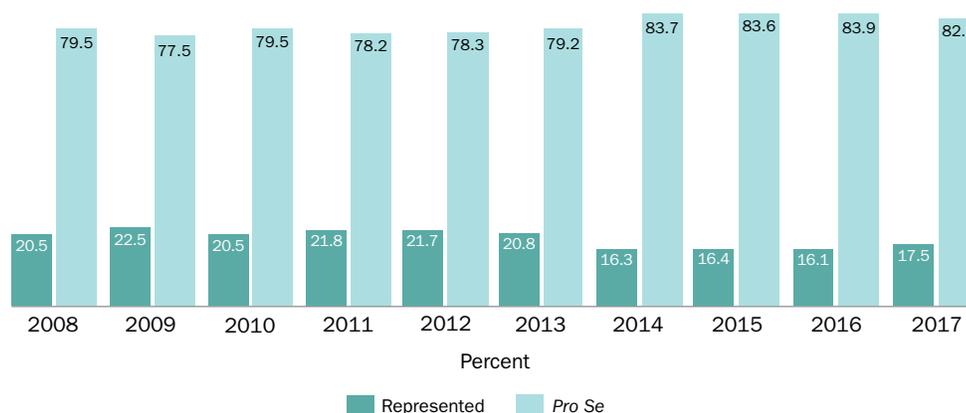
19 ABA, Tax Section Court Procedure Committee, Office of Chief Counsel, IRS, FY 2017 PowerPoint presentation.

FIGURE 1.20.1<sup>20</sup>

## Tax Court Petitions, FYs 2008-2017

FIGURE 1.20.2<sup>21</sup>

## Petitions From Pro Se and Represented Taxpayers, FYs 2008-2017



Many cases that come before the Tax Court involve a proposed deficiency, however even in cases where the IRS was ready to move forward with collection and had mailed a Collection Due Process (CDP) notice, the rates of dismissals and trials are both disproportionately high among unrepresented taxpayers in FY 2017 CDP cases, compared to represented taxpayers, who had disproportionately high rates of reaching a settlement, as shown on Figure 1.20.3. In FY 2017, more than 53 percent of CDP cases with unrepresented taxpayers were dismissed, and about 39 percent settled; compared to 37 percent dismissed and almost 58 percent settled, for represented taxpayers.<sup>22</sup>

20 ABA, Tax Section Court Procedure Committee, Office of Chief Counsel, IRS, FY 2017 PowerPoint presentation, slide 18.

21 *Id.*

22 *Id.*, slide 25.

**FIGURE 1.20.3, Collection Due Process Disposals by Category<sup>23</sup>**

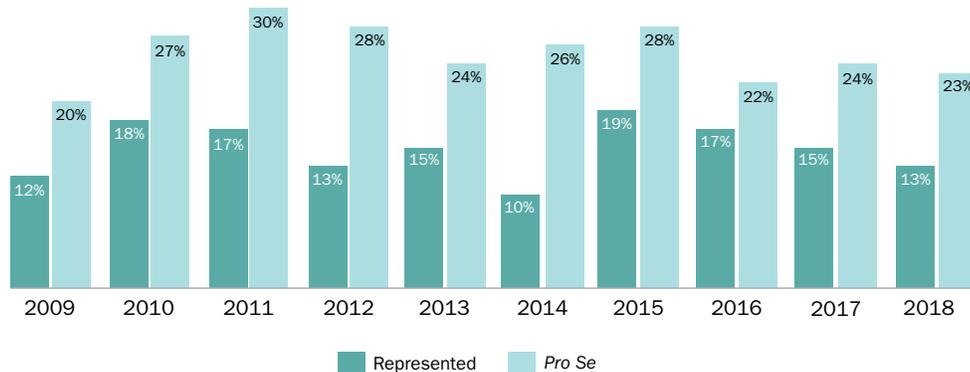
Category	FY08	FY09	FY10	FY11	FY12	FY13	FY14	FY15	FY16	FY17
<b>Settled</b>										
Pro Se	338	451	523	618	617	633	524	483	480	434
Represented	255	353	344	352	455	443	403	338	299	325
<b>Tried-Decided</b>										
Pro Se	111	145	117	137	160	149	87	77	73	83
Represented	33	53	38	37	51	53	38	21	24	28
<b>Dismissed</b>										
Pro Se	454	486	548	615	594	601	611	537	576	595
Represented	108	134	128	132	169	225	213	206	217	211

Even for unrepresented taxpayers that avoid having their petition dismissed, their chances of achieving a favorable outcome aren't as good as taxpayers that are represented. TAS "most litigated issues" analysis shows that unrepresented taxpayers have significantly lesser chances of winning in litigation as shown in Figure 1.20.4.<sup>24</sup>

**FIGURE 1.20.4<sup>25</sup>**

**Litigation Outcomes for Pro Se vs. Represented Taxpayers, 2009-2018**

Cases in Which the Taxpayer Prevailed or There Was a Split Decision



For example, during the 2018 reporting period only 13 percent of unrepresented taxpayers prevailed in full or in part compared to 23 percent of represented taxpayers.<sup>26</sup>

23 ABA, Tax Section Court Procedure Committee, Office of Chief Counsel, IRS, FY 2017 PowerPoint presentation, slide 25.

24 This is a sample of cases that involve the top ten categories of issues litigated each year in which the court issued an opinion. See Most Litigated Issues: *Introduction, infra*. Many cases are resolved before the court issues an opinion. Some taxpayers reach a settlement with the IRS before trial, while the courts dismiss other taxpayers' cases for a variety of reasons, including lack of jurisdiction and lack of prosecution. Courts can issue less formal "bench opinions," which are not published or precedential.

25 National Taxpayer Advocate 2005-2017 Annual Reports to Congress, Most Litigated Issues. The annual reporting period is from June 1 of the year preceding the publication to May 31 of the year of the publication.

26 See Most Litigated Issues: *Introduction, infra*.

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In FY 2017, more than 53% of Collection Due Process (CDP) cases with unrepresented taxpayers were dismissed, and about 39% settled; compared to 37% CDP cases with represented taxpayers were dismissed and almost 58% settled.

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### Using *Pro Bono* Days to Facilitate Representation in Tax Court Cases

To ease the pressure of matters that must be resolved at the calendar call, the IRS Office of Chief Counsel (OCC) in collaboration with the Tax Court and LITCs across the country have launched a variety of one-day events, generally known as “*Pro Bono* Days,” that take place 30 days or more before scheduled calendar calls. A *Pro Bono* Day program generally seeks to help unrepresented taxpayers:

- To understand the law applicable to their case;
- Determine the likelihood of prevailing; ease the taxpayer’s reluctance to turn over information the IRS needs in discovery;
- Reach a pre-trial settlement, when possible; and
- Understand the rules of evidence and procedures if a trial is necessary.

A *Pro Bono* Day is a chance for unrepresented petitioners to meet with *pro bono* representatives (such as attorneys, students, and other authorized representatives) in a less chaotic environment than the courthouse at the calendar call. It is also an opportunity for unrepresented taxpayers with a pending petition in Tax Court to meet face-to-face with representatives from IRS Chief Counsel, and sometimes IRS Appeals and IRS Collections.<sup>27</sup> Similarly, *Pro Bono* Day events provide an opportunity for unrepresented petitioners to consult with *pro bono* attorneys, and attorneys and paralegals in IRS Counsel’s office to resolve procedural matters, such as preparing and filing motions for matters agreed upon and stipulations of factual matters.<sup>28</sup>

For IRS attorneys, resolving cases at *Pro Bono* Day events means they do not need to spend time drafting pre-trial memoranda and motions to dismiss for lack of prosecution which they would otherwise have to prepare when they haven’t been able to communicate with the petitioner prior to the scheduled hearing. Attorney involvement on both sides lessens the burden on Tax Court judges, and serves the interests of justice. Even for cases that aren’t resolved at a *Pro Bono* Day that go to trial, the *pro se* petitioners can benefit from a *Pro Bono* Day. For example, in a substantiation case, the volunteers can tell the taxpayer which documents to bring, questions the judge is likely to ask, and facts to get on the record.<sup>29</sup>

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27 The National Taxpayer Advocate requested that TAS participate in *Pro Bono* Days to help resolve issues with years not before the court or collection matters following settlement.

28 Stipulations are facts, opinions, and legal positions on which the parties agree in writing, and thus do not need to be proven at trial.

29 Nathan J. Richman, *Pro Bono Clinic Days Offer New Option to Help Pro Se Petitioners*, TAX ANALYSTS, 2016 TNT 63-2 (Apr. 1, 2016).

*Pro Bono* Day efforts are heavily dependent upon the support of volunteers, from both the IRS and the local tax practitioner community. Out of 74 cities where the Tax Court holds trials,<sup>30</sup> IRS Counsel has helped *Pro Bono* Day efforts with varying success rates in:

- Baltimore, Maryland;
- Chicago, Illinois;
- Los Angeles, California;
- Thousand Oaks, California;
- Miami, Florida;
- Dallas, Texas;
- Charleston, West Virginia; and
- Seattle, Washington.

In one recent *Pro Bono* Day in Thousand Oaks, California, all the taxpayers who attended resolved their cases on the day of the event.<sup>31</sup>

No matter how well the events work for those taxpayers who take advantage of *Pro Bono* Day events, true success cannot be achieved without sufficient taxpayer participation. However, despite broad-based institutional support for *Pro Bono* Day events, and high rates of same-day resolution for attendees, participation rates among the events are inconsistent. One of the greatest challenges to the success of *Pro Bono* Day events is informing unrepresented taxpayers about them while maintaining the confidentiality of each taxpayer's personal information.

Rules to protect the confidentiality of taxpayers' personal information limit the ways in which taxpayers can be contacted.<sup>32</sup> The IRS and the court may communicate with unrepresented taxpayers to make them aware of available assistance, however, the independent organizations offering assistance do not have ready access to contact information for the petitioners, and thus cannot contact taxpayers directly. Low income taxpayers tend to be a transient population and change addresses more frequently than other taxpayers, which increases the challenge of establishing communication. Some taxpayers are reluctant to communicate with the IRS, and remain unaware that assistance may be available to help them with their pending case.<sup>33</sup>

IRS Counsel attempts to reach unrepresented petitioners by sending out letters informing them about LITC and TAS assistance and by following up with phone calls. The *Pro Bono* Day's sponsors jointly craft a letter for the IRS to send out to *pro se* petitioners, usually four or five weeks before the *Pro Bono* Day.<sup>34</sup> Although the letters are not standardized, the format is generally the same. The letter, accompanied by an IRS cover letter, describes the opportunity for free help from volunteer attorneys or law students to review documents and discuss the issues, including the chance to communicate with the IRS about resolving the issues, and directs interested petitioners to contact an LITC to schedule

30 See *United States Tax Court Places of Trial*, [https://www.ustaxcourt.gov/dpt\\_cities.htm](https://www.ustaxcourt.gov/dpt_cities.htm).

31 Email from Julie Payne, Assistant Division Counsel, IRS (Sept. 7, 2018) (on file with TAS).

32 See IRC § 6103.

33 See National Taxpayer Advocate 2010 Annual Report to Congress 221 (Most Serious Problem: *The IRS Has Not Studied or Addressed the Impact of the Large Volume of Undelivered Mail on Taxpayers*).

34 Nathan J. Richman, *Pro Bono Clinic Days Offer New Option to Help Pro Se Petitioners*, TAX ANALYSTS, 2016 TNT 63-2 (Apr. 1, 2016).

appointments.<sup>35</sup> The IRS must mail the letter because it cannot provide the petitioners' addresses to the clinics and volunteer programs under IRC § 6103 disclosure rules. The letter is distinct from the stuffer notices the court sends out informing petitioners about the Tax Court Clinical Program.<sup>36</sup>

We identified the following challenges affecting *pro se*<sup>37</sup> taxpayers' ability to consult with *pro bono* counsel and resolve cases pre-trial:

- Confidentiality restrictions that limit communication with unrepresented taxpayers about *Pro Bono* Day and other pre-trial resolution events by local LITCs and TAS;
- Limited availability of easily accessible but private meeting spaces for taxpayers experiencing difficulties with security and building access and *pro bono* resolution events scheduled outside of regular business hours;
- Insufficient staffing and unavailability of interpreter services at *Pro Bono* Days and other pre-trial resolution events; and
- Inadequate coordination of events reducing opportunities to offer one-stop resolution options for unrepresented petitioners.

## Addressing *Pro Bono* Day Challenges

### *Increasing Awareness*

*Pro Bono* Day programs could be improved to reach more eligible taxpayers and increase attendance rates. Effective communication with unrepresented petitioners is essential to ensuring they achieve quick and fair resolution of their tax issues. IRS counsel traditionally uses phone calls and mailed letters as the primary methods of communicating with taxpayers that have an upcoming hearing scheduled in the Tax Court. The IRS has attempted several different strategies to improve response rates from attempts to reach unrepresented taxpayers, such as using distinct types of envelopes and sending correspondence at various times between the time the taxpayer files a Tax Court petition and the date of the hearing. However, a taxpayer that has made the decision to take his case to the Tax Court may not be receptive to additional correspondence from the IRS, and may not believe that the IRS is attempting to put the taxpayer in contact with independent counsel. The National Taxpayer Advocate may conduct a study to determine the effectiveness of mailing letters to a representative sample of low income taxpayers who have filed petitions with the Tax Court and who appear to be unrepresented. Such letters would inform the taxpayers about LITCs, and TAS and the assistance they can provide.

Other methods to communicate with Tax Court petitioners might be more effective, but would require the Tax Court to modify its petition form. The Tax Court petition package (available on the Tax Court website)<sup>38</sup> contains several check-the-box selections for the petitioner to indicate the choice for small or regular case classification, requested location of the trial, and other critical information. If the Tax Court added a question for petitioners to indicate their consent to being contacted by an LITC, it would allow organizations offering *pro bono* assistance additional opportunities to reach taxpayers without

35 Nathan J. Richman, *Pro Bono Clinic Days Offer New Option to Help Pro Se Petitioners*, TAX ANALYSTS, 2016 TNT 63-2 (Apr. 1, 2016).

36 *Id.*

37 “*Pro se*” means “for oneself; on one’s own behalf; without a lawyer.” BLACK’S LAW DICTIONARY (10th ed. 2014).

38 U.S. Tax Court Petition Kit, [https://www.ustaxcourt.gov/forms/Petition\\_Kit.pdf](https://www.ustaxcourt.gov/forms/Petition_Kit.pdf).

needing to use the IRS as the messenger. Unrepresented taxpayers could indicate their preferred method of communication: phone calls, letters, or email.<sup>39</sup>

### *Making Assistance Accessible*

Increasing awareness of *Pro Bono* Day events is not the only challenge to their success. Most importantly, the IRS needs to hold the events at locations that offer accessibility and privacy. Taxpayers must be able to get to the event, and once a taxpayer is ready to meet with *pro bono* counsel and the IRS, the locations should provide space for private discussions. In some locales where the Tax Court holds trials there is an LITC nearby that can accommodate hosting the event, however in some parts of the country the nearest LITC might be several hours drive so other locations must be considered. The IRS can and should collaborate with partners to secure such locations. For example, holding the event at a local community center, as opposed to an IRS office in a federally operated building reduces the risk that someone might feel intimidated or be turned away by building security.<sup>40</sup>

Given that many low income taxpayers are not fluent in English, many localities would require the availability of interpreting services to be able to fully assist these taxpayers. The IRS should provide interpreting services to taxpayers unable to communicate in English through over-the-phone interpreters<sup>41</sup> or by partnering with local organizations offering interpretation services.<sup>42</sup>

Proper scheduling of *Pro Bono* Day events may also maximize attendance. Holding the events during evenings and on weekends can make it easier for petitioners to attend, however the IRS must depend on some employees to agree to work outside of their tour of duty which in turn requires permission from their supervisors. The IRS should adopt a national policy that authorizes employees willing to work at night or on weekends for a *Pro Bono* Day, instead of relying on individual managers to decide. The IRS has a dedicated workforce and may recruit employees for *Pro Bono* events after hours. TAS is offering its assistance to coordinate such events with different IRS functions, such as Collection, Appeals, and Office of Chief Counsel. In a move towards future collaboration, the National Taxpayer Advocate is collaborating with the Chief, Appeals and Deputy Chief Counsel (Operations) to organize a new liaison group with members from TAS, Appeals, OCC, and LITCs to identify and resolve issues that stand in the way of eligible taxpayers being able to receive assistance and other taxpayer rights issues.<sup>43</sup>

### *Offering One-Stop Resolution Options for Unrepresented Petitioners*

*Pro Bono* Day events should be organized to provide one-stop resolution of all IRS issues and tax periods. To be most effective, representatives from local IRS Counsel, Appeals, Collection, and TAS should

39 See also Most Serious Problem: *Statutory Notices of Deficiency: The IRS Fails to Clearly Convey Critical Information in Statutory Notices of Deficiency, Making it Difficult for Taxpayers to Understand and Exercise Their Rights, Thereby Diminishing Customer Service Quality, Eroding Voluntary Compliance, and Impeding Case Resolution*, *supra*.

40 See National Taxpayer Advocate 2012 Annual Report to Congress 176. Representatives of LITCs raised concerns about the requirement of many Taxpayer Assistance Centers (TACs) or federal buildings in which some TACs are located to produce a valid, U.S.-issued ID to enter the building. 2013 Annual LITC Grantee Conference, *Recent Developments in IRS Policies and Procedures Related to ITIN Applications*, panel discussion (Dec. 6, 2012).

41 Over the Phone Interpreter (OPI) service is a telephone interpreter-assisted service provided through the IRS by a contractor. OPI affords IRS employees the ability to communicate with taxpayers through interpreters who speak more than 350 languages. OPI Service is available 24 hours per day/7 days per week. It supports the IRS's mission to provide top-quality service for all taxpayers, specifically for those whose native language is not English. This is in compliance with Executive Order 13166, as well as Department of Justice LEP Guidance 67 FR 41455-41472, Department of Treasury LEP Guidance 70 FR 6067, and the TBOR.

42 See IRM 22.31.1, *IRS Language Services* (Oct. 19, 2018).

43 The liaison group held its first meeting on December 4, 2018 at the LITC Annual Conference in Washington, D.C.

attend each *Pro Bono* Day event to resolve disputes pre-trial. Bringing together a broad spectrum of IRS functions allows for resolution of more types of issues, even the many cases where the taxpayer will be unable to pay anything to the IRS, regardless of the outcome of the case. Moreover, many taxpayers with issues before the court also have issues relating to tax years not before the court. By having TAS and other functions available, *Pro Bono* Days can address all the taxpayer's issues, in a face-to-face environment.<sup>44</sup>

We commend the IRS OCC for attempting a variety of formats for helping unrepresented taxpayers resolve cases pre-trial, such as post-petition rolling clinics,<sup>45</sup> invitations to one-on-one meetings, in-person events in IRS space and in LITC space, and virtual clinics where LITCs equipped with video conferencing allow petitioners to meet virtually with TAS, Collection, and Exam employees using WebEx or other virtual service delivery models. Using technology like WebEx allows a taxpayer to have a virtual face to face interaction from a computer or even a smartphone and eliminates difficulties associated with traveling to the court building or difficulties accessing federal buildings because of missing or unacceptable identification.<sup>46</sup> Expanding virtual face-to-face digital communication options for taxpayers may improve participation and protect *the right to a fair and just tax system* and to *appeal an IRS decision in an independent forum*.

If implemented holistically, all these measures would tailor services to meet the needs of this discrete group of taxpayers, systemically improving access to representation and future tax compliance.<sup>47</sup>

## CONCLUSION

Increasing awareness of available resources for unrepresented taxpayers, such as LITCs and TAS, benefits taxpayers by achieving better case outcomes, and allows the IRS and the Tax Court to resolve cases more efficiently, and pre-trial, whenever possible. Holding *Pro Bono* Days allows the Chief Counsel and IRS to provide a unique opportunity for petitioners to resolve their cases via a face-to-face interaction with the Chief Counsel and IRS employees with the benefit of independent counsel looking out for the taxpayers' interests and ensuring taxpayer rights are protected. Doing that successfully requires cross-functional collaboration across IRS functions and careful planning that meets taxpayer needs for accessibility and privacy.

44 Using a similar model, TAS conducts Problem Solving Day events in communities throughout the country where TAS employees from a local office are available to assist taxpayers in person with tax problems they have not been able to resolve with the IRS. During calendar year 2018, TAS assisted 5,959 taxpayers at 427 Problem Solving Day events.

45 "If the calendar is not filled with cases when scheduled six months before trial, the Tax Court could continue to add cases until five months prior to the start of the trial session or until the calendar is full. A rolling calendar would in many cases give the parties additional time to prepare for trial, while not requiring taxpayers who reside in trial locations that are visited less often to wait the additional time to have their cases heard." ABA, Section of Taxation, *Comments on Tax Court Rules of Practice and Procedure* (Nov. 10, 2015).

46 See Nathan J. Richman, *Pro Bono Clinic Days Offer New Option to Help Pro Se Petitioners*, TAX ANALYSTS, 2016 TNT 63-2 (Apr. 1, 2016); Meeting Minutes, LITC/CC/SBSE Working Group (June 13, 2017).

47 See Thomas Dohrmann & Gary Pinshaw, McKinsey & Company, *The Road to Improved Compliance: A McKinsey Benchmarking Study of Tax Administrations – 2008 -2009* (Sept. 2009).

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Adopt alternative methods for communicating with unrepresented Tax Court petitioners, including working with the Tax Court to modify the petition form to allow taxpayers to consent to direct contacts from local LITCs and TAS.
2. Hold more events to encourage pre-trial resolution in easily accessible but private locations and schedule the events outside of regular business hours as necessary.
3. Provide staffing at *Pro Bono* Days and other pre-trial resolution events that can provide interpreting services.
4. Develop one-stop resolution options for *pro se* petitioners at *Pro Bono* Days and other pre-trial resolution events to include representatives from Appeals, Collection, and TAS, along with inviting local LITC or Bar Association volunteers or staff and assigning counsel attorneys from the same locality.

**STATUS  
UPDATE****APPEALS: Appeals Has Taken Important Steps Toward Increasing Campus Taxpayers' Access to In-Person, Quality Appeals, But Additional Progress is Required****RESPONSIBLE OFFICIAL**

Donna Hansberry, Chief, Office of Appeals

**TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to a Fair and Just Tax System*

**DEFINITION OF PROBLEM**

In several Annual Reports to Congress, the National Taxpayer Advocate has discussed the importance of in-person conferences to both taxpayers and the IRS Office of Appeals (Appeals).<sup>2</sup> An in-person conference is sometimes essential to properly explaining and settling a controversy. Such is particularly true for cases involving factual or legal complexity, credibility of witnesses, or hazards of litigation settlements.<sup>3</sup> Taxpayers whose cases are assigned to Appeals field offices have historically had access to in-person conferences.<sup>4</sup> By contrast, Appeals campus cases, which typically involve low and middle income taxpayers, were made ineligible for such conferences in October 2016.<sup>5</sup> This disparity in rights broke down along income lines, as, for example, for fiscal year (FY) 2018 the median adjusted gross income (AGI) of field taxpayers was 33 percent higher than that of campus taxpayers, while the average AGI of field taxpayers was 156 percent higher than that of campus taxpayers.<sup>6</sup>

To its credit, Appeals, taking to heart the urgings of the National Taxpayer Advocate and other stakeholders, has recently changed its policy and reinstated the right of campus taxpayers to transfer their cases to field offices in order to accommodate an in-person conference.<sup>7</sup> Appeals has also indicated that it will continue to pursue additional strategies aimed at ensuring that taxpayers' requests

1 See Taxpayer Bill of Rights (TBOR), <http://www.taxpayeradvocate.irs.gov/taxpayer-rights>. The rights contained in the TBOR are also codified in the Internal Revenue Code. See IRC § 7803(a)(3).

2 National Taxpayer Advocate 2017 Annual Report to Congress 195-202; National Taxpayer Advocate 2016 Annual Report to Congress 206-210; National Taxpayer Advocate 2014 Annual Report to Congress 46-54; National Taxpayer Advocate 2014 Annual Report to Congress 311-314.

3 Letter from American College of Tax Counsel to Kirsten Wielobob, Chief, Appeals (Oct. 10, 2016), 2016 TNT 197-16. See also Letter from Texas Soc'y of Cert. Pub. Accts. to John Koskinen, Comm'r of IRS (Jan. 24, 2017), 2017 TNT 16-16; *ABA Members Comment on Recent Appeals Division Practice Changes*, 2017 TNT 89-10 (May 10, 2017).

4 IRS, Interim Guidance Memorandum (IGM) AP-08-1017-0017, Appeals Conference Procedures, (Oct. 13, 2017).

5 Effective October 1, 2016, Internal Revenue Manual (IRM) 8.6.1.2.2, *Transfers for the Convenience of Taxpayers*, was deleted, eliminating the right of taxpayers to transfer cases out of campuses.

6 Appeals response to TAS information request (Oct. 26, 2018). As used here, the term "average" is synonymous with the term "mean."

7 IRS, IRM AP-08-1118-0013, *Appeals Conference Procedures* (Nov. 30, 2018).

for in-person conferences are accommodated, regardless of whether the assigned Appeals Technical Employee (ATE) is located in a campus or in the field.<sup>8</sup>

The National Taxpayer Advocate applauds Appeals for undertaking this significant step with respect to in-person conferences. This progress, however, does not fully address the larger systemic problems attributable to the reality that the cases of low and middle income taxpayers are disproportionately channeled to campus locations. Although somewhat mitigated by Appeals' new transfer policy, this approach continues to limit geographic access to in-person conferences and causes cases to be assigned to less experienced, lower-graded ATEs, who generally lack firsthand familiarity with the local issues and community circumstances that often are at the heart of taxpayers' cases.<sup>9</sup> Likely unintentionally, Appeals is still systematically perpetuating disproportionate hardships for low and middle income taxpayers.

Accordingly, the National Taxpayer Advocate remains concerned that:

- Appeals has consolidated cases involving smaller dollars and low and middle income taxpayers in campuses;
- Appeals' reliance on campuses presents physical barriers to in-person conferences and makes it difficult for campus taxpayers to have their cases heard by higher-graded, locally based ATEs; and
- Due process issues arise from the disproportionate channeling of low and middle income taxpayers to Appeals campus locations.

## ANALYSIS OF PROBLEM

### Appeals Has Consolidated Cases Involving Smaller Dollars and Low and Middle Income Taxpayers in Campuses

Beginning in the mid-1990s and then more actively in FY 2004, Appeals reallocated some ATEs out of field offices and into campuses.<sup>10</sup> This incremental shift cannot be precisely tracked, as Appeals did not maintain separate staffing data prior to FY 2012, by which time 29 percent of Appeals personnel had been assigned to campuses.<sup>11</sup> This proportion has remained consistent ever since, with campuses containing 30 percent of Appeals personnel in FY 2018.<sup>12</sup> The shift to campuses can be more clearly glimpsed by looking to field offices, which shrank from 93 in FY 2003 to 67 in FY 2018.<sup>13</sup> The end result is that, as of FY 2017, 53 percent of Appeals cases are assigned to only six campus locations.<sup>14</sup>

8 IRS, IGM AP-08-1118-0013, *Appeals Conference Procedures* (Nov. 30, 2018).

9 In this context, "experienced" refers to familiarity with the broad range of issues potentially faced by taxpayers and the contexts in which these cases are resolved.

10 IRS response to TAS information request (May 7, 2018).

11 *Id.*

12 IRS response to TAS information request (Oct. 26, 2018).

13 *Id.*

14 *Id.*

In conversations with TAS, Appeals' primary justification for this shift and the reluctance to transfer cases out of campuses has been the need to accommodate decreased funding.<sup>15</sup> Nevertheless, Appeals' funding rose steadily until FY 2011, when it peaked at \$250 million.<sup>16</sup> By FY 2012, however, when budget decreases began, Appeals had already largely implemented its personnel shift to the campuses.<sup>17</sup>

The criteria utilized by Appeals for case assignment cause most small dollar cases, along with low and middle income taxpayers, to be allocated to the campuses. Although the criteria for assigning cases to campus or field locations are treated by the IRS as "official use only," and are therefore not publishable, the data make clear that higher-dollar cases are channeled out of the campuses and to the field.<sup>18</sup> This approach likewise has the impact of providing wealthier taxpayers with direct access to field offices, but initially assigning less affluent taxpayers to campuses. This relationship is illustrated in Figure 1.S1.1:

**FIGURE 1.S1.1, Average and Median Adjusted Gross Income Among Appeals Field and Campus Individual Taxpayers, FY 2018<sup>19</sup>**

Measure	Field	Campus	Percentage Difference – Field Versus Campus
Average	\$294,000	\$115,000	+156%
Median	\$84,000	\$63,000	+33%

### Appeals' Reliance on Campuses Presents Physical Barriers to In-Person Conferences and Makes It Difficult for Campus Taxpayers to Have Their Cases Heard by Higher-Graded, Locally Based Appeals Technical Employees

Currently, Appeals has only six campus locations spread throughout the United States: Philadelphia, Pennsylvania; Brookhaven, New York; Fresno, California; Ogden, Utah; Memphis, Tennessee; and Florence, Kentucky.<sup>20</sup> Fifty-three percent of Appeals cases are assigned to these campuses.<sup>21</sup> By contrast, the remaining 47 percent are spread among Appeals' 67 field offices.<sup>22</sup> The geographic dispersal of the campuses and field offices is shown in Figure 1.S1.2:

15 Conference call between TAS and Appeals (May 31, 2016). In its response to TAS's information request dated May 7, 2018, Appeals elaborates, "Following passage of the IRS Restructuring and Reform Act of 1998 and the creation of the Collection Due Process workstream, Appeals expanded campus operations to effectively and efficiently manage the workload generated by Compliance campuses." Appeals also explains that there are many reasons for consolidating cases in the campuses, including case complexity, ease case routing, and reduced cycle time. Appeals response to TAS fact check (Nov. 21, 2018).

16 IRS response to TAS information request (May 7, 2018).

17 *Id.*

18 IRS response to TAS information request (Oct. 9, 2018). Appeals clarifies that it does not intentionally assign cases based on taxpayers' adjusted gross incomes (AGI), and instead routes cases based on prior assignments by Compliance or based on the type of case (e.g., Innocent Spouse, Penalty, or Collection Due Process cases). IRS response to TAS fact check (Nov. 21, 2018).

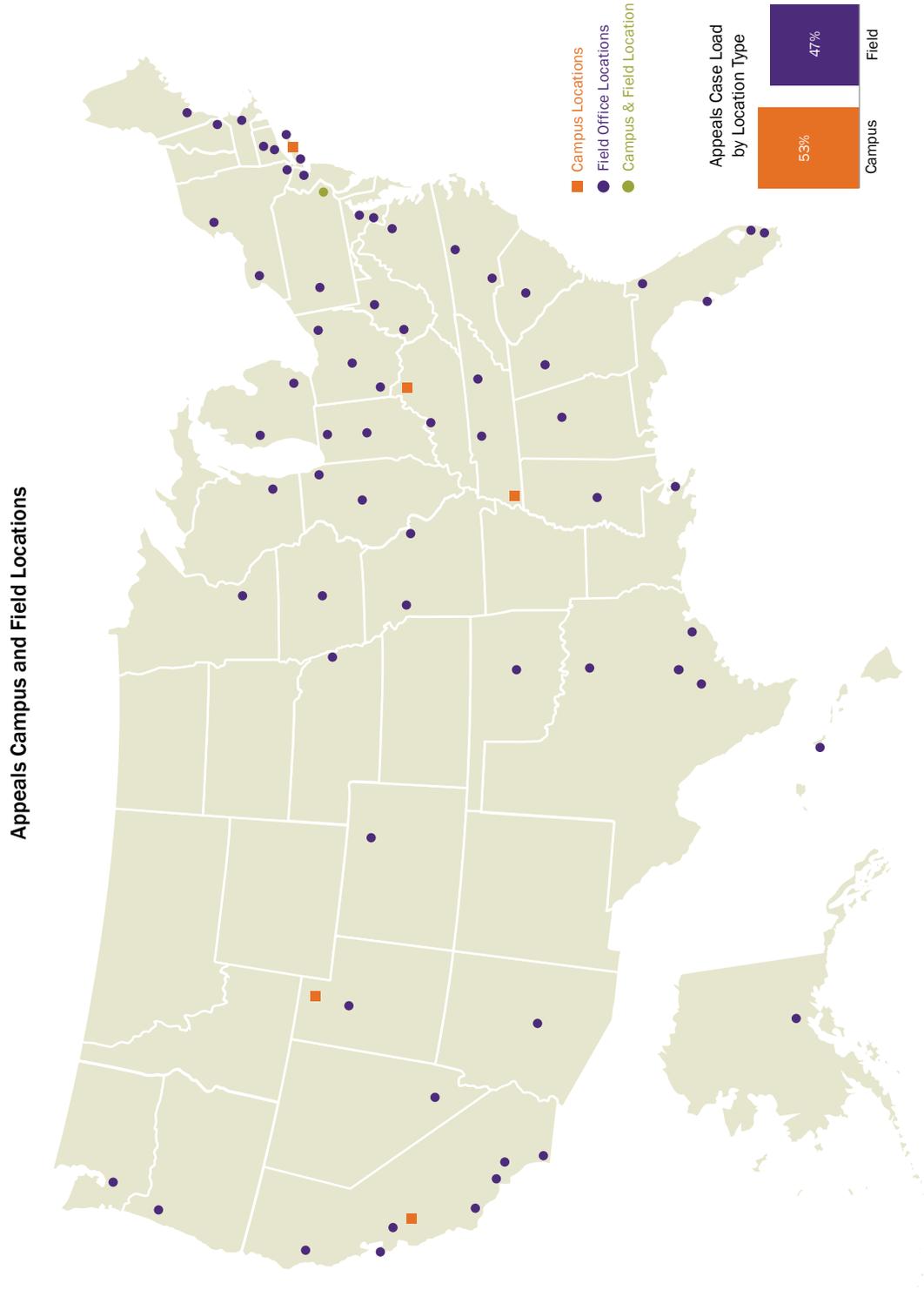
19 IRS response to TAS information request (Oct. 26, 2018). The percentage difference from average campus AGI to average field AGI is calculated by subtracting average campus AGI from average field AGI, then dividing the difference by the average campus AGI. Note that the median AGI calculation helps to adjust for outliers in the dataset. According to Appeals, this data was provided by IRS Research, Applied Analytics & Statistics (RAAS), which drew the information from the Compliance Data Warehouse (CDW). IRS response to TAS fact check (Nov. 21, 2018).

20 IRS response to TAS information request (May 7, 2018).

21 IRS response to TAS information request (Oct. 26, 2018).

22 *Id.*

FIGURE 1.S1.2, Appeals Campus and Field Locations<sup>23</sup>



<sup>23</sup> This map is developed based on information provided in the IRS response to TAS information request (May 7, 2018).

Thanks to Appeals' reinstatement of campus taxpayers' right to seek a case transfer to facilitate an in-person conference, taxpayers are no longer inextricably bound to campuses. Nevertheless, Appeals' campus-centric approach can make this right difficult to exercise. Appeals states that it will use its best efforts to schedule an in-person conference at a location that is reasonably convenient for taxpayers and Appeals. However, given the geographic scarcity of field offices, which are the primary venues for in-person conferences, and the fact that twelve states and Puerto Rico lack a field office altogether, taxpayers wishing for an in-person conference may well be required to travel substantial distances and incur significant cost in order to attend an in-person conference.<sup>24</sup>

The circumstance that 53 percent of all Appeals cases are decided out of only six widely scattered offices is problematic because Appeals best serves taxpayers when it has a broad and diverse geographic footprint.<sup>25</sup> This presence allows ATEs to negotiate case resolutions based on an understanding of the local economic circumstances and prevailing community issues faced by taxpayers. Similarly, taxpayers are more likely to develop a rapport with, and respect the decisions of, ATEs with whom they share common experiences.<sup>26</sup> An Appeals function that is embedded within communities provides a more effective environment for establishing trust and achieving case resolutions.<sup>27</sup> This optimal environment, however, is systematically denied to campus taxpayers unless they opt for an in-person conference, which they may or may not need to resolve their cases. Additionally, given Appeals' current staffing model, Appeals may lack any personnel whatsoever located within a taxpayer's vicinity.

Appeals could expand its geographic footprint and minimize its reliance on campuses by using attrition from the campuses to increase staffing in local field offices with ATEs of various grades and designations such that the office could cover cases ranging from the Earned Income Tax Credit (EITC) to itemized deductions to Schedule C controversies.<sup>28</sup> Likewise, Appeals could enhance its case assignment flexibility by re-designating technically or factually complex case categories, such as those involving EITC claims, such that they could be assigned to higher-graded ATEs where appropriate.<sup>29</sup> These steps would not only expand Appeals' geographic footprint and facilitate the accessibility of in-person conferences, but would lay the foundation for a structure that more effectively and equitably serves both campus and field taxpayers.

24 IRS response to TAS fact check (Nov. 21, 2018).

25 Although 67 field offices would appear ample in comparison with only six campus locations, that number is insufficient to cover the entirety of the U.S., its territories, and the District of Columbia. Currently, 12 states and Puerto Rico lack any Appeals presence offering in-person conferences. IRS response to TAS fact check (Nov. 21, 2018).

26 National Taxpayer Advocate Fiscal Year (FY) 2019 Objectives Report to Congress 138.

27 *Id.*

28 Appeals explains its reluctance to allow case transfers out of the campuses because Appeals concentrates specialized knowledge in particular campuses and because Appeals Technical Employees (ATEs) in campuses are typically lower graded than those in the field and therefore handle less complex cases. Andrew Velarde, *IRS Appeals Confident That In-Person Campus Conferences Will Return*, 2018 TXN 21-63 (May 21, 2018).

29 This step was recommended by the National Taxpayer Advocate to the Chief of Appeals as part of a May 31, 2016, meeting. In that meeting, the then-Chief of Appeals expressed the view that Earned Income Tax Credit (EITC) cases were less complex and therefore best suited for lower-graded ATEs. Given the often challenging factual scenarios and legal issues involved in these cases, however, this perspective should be reevaluated.

### Due Process Issues Arise From the Disproportionate Channeling of Low and Middle Income Taxpayers to Appeals Campus Locations

The way in which cases are assigned to campus locations, combined with Appeals' current staffing model, limits the practical ability of low and middle income taxpayers to avail themselves of an in-person conference, while making that right more easily available to most corporations and wealthy taxpayers. Similarly, low and middle income taxpayers face disproportionate difficulty in obtaining review from an ATE who is familiar with the taxpayers' local issues and economic circumstances. Further, because large and complex cases generally are assigned to the field, senior ATEs have remained in field offices. Ninety-four percent of ATEs in field offices are Grade 13 or above, whereas all ATEs in campuses are Grade 12 or below.<sup>30</sup> Thus, taxpayers whose cases are channeled to the campuses are initially denied access to the most experienced and highly graded ATEs.<sup>31</sup>

Appeals' reinstatement of the right to transfer cases from campuses to the field provides a path for mitigating the most extreme aspects of differential treatment between low and middle income taxpayers and wealthier taxpayers. Appeals deserves substantial credit for taking steps to partially address this disparity. However, the campus-centric model itself obligates taxpayers initially assigned to campuses to take the additional step of seeking case transfers and, in many cases, requires them to incur travel costs and delays, to which wealthier taxpayers are not subject or are better situated to address. Given the importance of in-person conferences, geographic familiarity, and quality case reviews, Appeals' current design and policy continues to disadvantage the group of taxpayers who can least afford litigation as an alternative to an undesirable Appeals outcome. This situation is problematic because, as explained by the Supreme Court in *Goldberg v. Kelly*, "The opportunity to be heard must be tailored to the capacities and circumstances of those who are to be heard."<sup>32</sup>

Regardless of resource constraints or administrative efficiency, such a disparity, albeit unintentionally, presents due process issues that undermine the trust on which the voluntary tax system is based. Appeals has taken a commendable first step toward addressing deeply embedded inequities affecting taxpayers' *right to appeal an IRS decision in an independent forum*.<sup>33</sup> Appeals should continue this progress by expanding its geographic footprint and removing the systemic barriers that make it difficult for low and middle income taxpayers to have the same access to a quality appeal as wealthier taxpayers.

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30 IRS response to TAS information request (Oct. 26, 2018).

31 This differential matters for practical as well as philosophical reasons because the relatively smaller cases typically assigned to campus locations are not necessarily simpler or easier to resolve than cases involving larger amounts in controversy. For example, TAS experience indicates that earned income tax credit (EITC) cases and those relating to innocent spouse relief, while often not monetarily large, can be extremely factually and legally complex. See, e.g., National Taxpayer Advocate 2015 Annual Report to Congress 240-247.

32 *Goldberg v. Kelly*, 397 U.S. 254, 268-269.

33 IRC § 7803(a)(3)(E).

## CONCLUSION

Appeals' reinstatement of the right to transfer campus cases to the field in order to accommodate an in-person conference is a very positive step and removes the worst of the disparity between low and middle income taxpayers on the one hand and wealthier taxpayers on the other hand. Nevertheless, taxpayers whose cases are channeled to the campuses still must apply for a case transfer and, because of Appeals' current staffing model, often will find themselves needing to incur significant cost and other travel-related hardships in order to obtain the same quality appeal to which wealthier taxpayers have more ready access. Appeals has taken an important first step in remedying this disparity but progress remains to be made toward ensuring that all taxpayers have access to a quality appeal.<sup>34</sup>

As a result, the National Taxpayer Advocate continues to encourage Appeals to utilize attrition and other strategies as a means of staffing local Appeals offices so as to have at least one permanent Appeals office in every state, the District of Columbia, and Puerto Rico. Additionally, in conjunction with TAS, Appeals should continue exploring ways of adapting facilities or implementing other approaches to accommodate in-person conferences for taxpayers who prefer to have their cases remain in a campus location.

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34 One aspect of a quality appeal is that a taxpayer's appeals conference should be attended by IRS Counsel or Compliance only with the taxpayer's consent. TAS recently learned, however, that some Appeals managers are seeking out cases that lend themselves to Compliance participation as a means of actively contributing to Appeals' future vision. IRS Appeals, *FY19 Frontline Manager Commitments – Exam Appeals* (on file with TAS). As previously pointed out by the National Taxpayer Advocate, inclusion of either Counsel or Compliance against taxpayers' wishes jeopardizes Appeals' independence and may lead to increased litigation and decreased tax compliance. Accordingly, such performance goals on the part of team managers, which presumably are encouraged by Appeals' leadership, can do significant harm to both Appeals and taxpayers. These goals are also precipitous, as the related pilot program designed to evaluate this initiative has not yet been completed. Nina E. Olson, *When Evaluating its Pilot Program on the Participation of Counsel and Compliance in Conferences, Appeals Should be Transparent and Should Consider Both Objective and Subjective Data*, NTA BLOG (Nov. 7, 2018) [https://taxpayeradvocate.irs.gov/news/nta-blog-appeals-should-be-transparent?category=Tax News](https://taxpayeradvocate.irs.gov/news/nta-blog-appeals-should-be-transparent?category=Tax%20News); National Taxpayer Advocate 2017 Annual Report to Congress 203-210.

## INTRODUCTION: Legislative Recommendations

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Section 7803(c)(2)(B)(ii)(VIII) of the Internal Revenue Code (IRC) requires the National Taxpayer Advocate to include in her Annual Report to Congress, among other things, legislative recommendations to resolve problems encountered by taxpayers.

The table that follows this introduction summarizes congressional action on recommendations that the National Taxpayer Advocate proposed in her 2001 through 2017 Annual Reports.<sup>1</sup> The National Taxpayer Advocate places a high priority on working with the tax-writing committees and other interested parties to try to resolve problems encountered by taxpayers. In addition to submitting legislative proposals in each Annual Report, the National Taxpayer Advocate meets regularly with members of Congress and their staffs and testifies at hearings on the problems faced by taxpayers to ensure that Congress has an opportunity to receive and consider a taxpayer perspective. Last year, for the first time, the National Taxpayer Advocate included with her Annual Report a separate volume, *The National Taxpayer Advocate Purple Book*, which proposed 50 legislative recommendations intended to strengthen taxpayer rights and improve tax administration. The National Taxpayer Advocate has decided to make the Purple Book a recurring addition to her Annual Report. This year's Purple Book contains a concise summary of 58 legislative recommendations, most of which have been made in detail in our prior reports, but others are presented for the first time.<sup>2</sup> Each recommendation is presented in a format similar to the one used for congressional committee reports, with "Present Law," "Reasons for Change," and "Recommendation(s)" sections. We hope for this to be a user-friendly resource for members of Congress and their staffs.

The following discussion highlights legislative activity during the second session of the 115th Congress relating to the National Taxpayer Advocate's proposals.

### Bipartisan Budget Act of 2018

On April 4, 2017, Representative Larson and sixteen other Representatives introduced this legislation, which became Public Law No. 115-123 on February 9, 2018, that enacted one of the National Taxpayer Advocate's prior proposals.<sup>3</sup>

- **Hold Taxpayers Harmless When the IRS Returns Funds Levied From a Retirement Plan or Account.**<sup>4</sup> This provision would hold individuals harmless on improper levies on individual retirement accounts.

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1 An electronic version of the chart is available on the TAS website at [www.TaxpayerAdvocate.irs.gov/Reports](http://www.TaxpayerAdvocate.irs.gov/Reports). The chart lists all legislative recommendations the National Taxpayer Advocate has made since 2001 and identifies each section of the Internal Revenue Code (IRC) affected by the recommendations.

2 See National Taxpayer Advocate 2019 Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration* (Dec. 2018).

3 Bipartisan Budget Act, Pub. L. No. 115-123, § 41104, 132 Stat 64, 155-156 (2018).

4 National Taxpayer Advocate Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration* 41-42 (*Hold Taxpayers Harmless When the IRS Returns Funds Levied From a Retirement Plan or Account*) (Dec. 2018).

## Taxpayer First Act

On April 10, 2018, Representative Jenkins and four other Representatives introduced this legislation, which passed the House by a unanimous vote of 414-0.<sup>5</sup> The Taxpayer First Act would enact many of the National Taxpayer Advocate's prior proposals.

- **Matching Grants Program for Return Preparation.**<sup>6</sup> This provision would establish a Volunteer Income Tax Assistance (VITA) matching grant program.
- **Referrals to LITCs.**<sup>7</sup> This provision would allow officers and employees of the Department of Treasury to advise taxpayers of the availability of and the eligibility requirements for receiving assistance from Low Income Taxpayer Clinics (LITCs). It would also allow such officers and employees to provide to taxpayers the addresses and contact information for these clinics.
- **Waiver of Installment Agreement Fees for Low Income Taxpayers.**<sup>8</sup> This provision would waive any fee otherwise required with the submission of an offer in compromise (OIC) for low income taxpayers. While this provision does not mention installment agreement fees as the title of this recommendation suggests, our past Most Serious Problems (MSPs) and Legislative Recommendations (LRs) that discussed this recommendation extend the recommendation to the OIC and user fees that this provision waives.
- **Restrict Tax Return Disclosures to Necessary Content.**<sup>9</sup> This provision would limit the redisclosures and uses of tax return information to only the express purpose for which consent to use that information was granted. The tax return information shall not be disclosed to any other person without the express permission or request of the taxpayer.
- **Taxpayer Advocate Directive.**<sup>10</sup> This provision would amend IRC § 7803(c) by adding a segment on the power of the National Taxpayer Advocate to issue Taxpayer Advocate Directives (TADs), and that the Administrator of the IRS<sup>11</sup> must modify, rescind, or ensure compliance with a TAD within 90 days of its issuance. The National Taxpayer Advocate may appeal a modification or rescission, to which the Administrator must ensure compliance or provide the National Taxpayer Advocate with a detailed description of the reasons behind making the modification or rescission.

5 Taxpayer First Act, H.R. 5444, 115th Cong. (2018).

6 National Taxpayer Advocate 2014 Annual Report to Congress 55-66 (Most Serious Problem: *VTA/TCE Funding: Volunteer Tax Assistance Programs Are Too Restrictive and the Design Grant Structure Is Not Adequately Based on Specific Needs of Served Taxpayer Populations*); National Taxpayer Advocate 2002 Annual Report to Congress vii-viii.

7 National Taxpayer Advocate 2007 Annual Report to Congress 551-553 (Legislative Recommendation: *Referral to Low Income Taxpayer Clinics*).

8 National Taxpayer Advocate 2017 Annual Report to Congress 307-313 (Legislative Recommendation: *User Fees: Prohibit User Fees That Reduce Revenue, Increase Costs, or Erode Taxpayer Rights*); National Taxpayer Advocate 2015 Annual Report to Congress 14-35 (Most Serious Problem: *IRS User Fees: The IRS May Adopt User Fees to Fill Funding Gaps Without Fully Considering Taxpayer Burden and the Impact on Voluntary Compliance*); National Taxpayer Advocate 2007 Annual Report to Congress 66-82 (Most Serious Problem: *User Fees: Taxpayer Service For Sale*); National Taxpayer Advocate 2006 Annual Report to Congress 141-156 (Most Serious Problem: *Collection Issues of Low Income Taxpayers*).

9 National Taxpayer Advocate 2007 Annual Report to Congress 554-555 (Legislative Recommendation: *Consent-Based Disclosures of Tax Return Information Under Internal Revenue Code Section 6103(c)*).

10 National Taxpayer Advocate 2016 Annual Report to Congress 39-40 (Special Focus: *IRS Future State: The National Taxpayer Advocate's Vision for a Taxpayer-Centric 21st Century Tax Administration*); National Taxpayer Advocate 2011 Annual Report to Congress 573-581 (Legislative Recommendation: *Codify the Authority of the National Taxpayer Advocate to File Amicus Briefs, Comment on Regulations, and Issue Taxpayer Advocate Directives*); National Taxpayer Advocate 2002 Annual Report to Congress 198-215 (Legislative Recommendation: *The Office of the Taxpayer Advocate*).

11 The bill modifies the title of the "Commissioner of Internal Revenue" and replaces it with the "Administrator of the Internal Revenue Service". See Taxpayer First Act, H.R. 5444, 115th Cong. § 11401 (2018).

- **Single Point of Contact.**<sup>12</sup> This provision would require the Secretary of the Treasury to establish and implement procedures to create a single point of contact at the IRS for taxpayers whose tax return has been delayed or adversely affected by tax-related identity theft.
- **Strengthen the Independence of the IRS Office of Appeals.**<sup>13</sup> This provision would establish within the IRS a new office, the IRS Independent Office of Appeals.
- **Tax Court Review of Request for Equitable Innocent Spouse Relief.**<sup>14</sup> This provision clarifies the standards and scope of Tax Court review for equitable innocent spouse relief.
- **Clarify that the Scope and Standard of Tax Court Determinations Under IRC § 6015(f) is *De Novo*.**<sup>15</sup> This provision clarifies that any review of a determination made under IRC § 6015(f) (equitable relief for innocent spouses from joint and several liability on a joint return) will be reviewed *de novo* by the Tax Court.

### Taxpayer First Act of 2018

On July 19, 2018, Senator Hatch and thirteen other Senators introduced this legislation.<sup>16</sup> This Act includes several changes and additions from the House version of the bill. While this Senate version would remove some of the prior National Taxpayer Advocate's recommendations that were included in the House bill, this legislation would still enact a number of the National Taxpayer Advocate's prior proposals.

- **Matching Grants Program for Return Preparation.**<sup>17</sup> This provision would establish a VITA matching grant program.
- **Single Point of Contact.**<sup>18</sup> This provision would require the Secretary of the Treasury to establish and implement procedures to create a single point of contact at the IRS for taxpayers whose tax return has been delayed or adversely affected by tax-related identity theft.
- **Notification of Suspected Identity Theft.**<sup>19</sup> This provision would require the Secretary to notify an individual as soon as practicable if there has been or may have been an unauthorized use of their identity, and it can be disclosed without jeopardizing an investigation relating to tax administration. Such notice must include instructions on further steps, including the necessary forms to complete and how to file a report with law enforcement.

12 National Taxpayer Advocate 2013 Annual Report to Congress 61 (Most Serious Problem: *Regulation of Return Preparers: Taxpayers and Tax Administration Remain Vulnerable to Incompetent and Unscrupulous Return Preparers While the IRS is Enjoined From Continuing its Efforts to Effectively Regulate Unenrolled Preparers*).

13 National Taxpayer Advocate 2009 Annual Report to Congress 346-350 (Legislative Recommendation: *Strengthen the Independence of the IRS Office of Appeals and Require at Least One Appeals Officer and Settlement Officer in Each State*).

14 National Taxpayer Advocate 2001 Annual Report to Congress 128-165 (Legislative Recommendation: *Joint and Several Liability*).

15 National Taxpayer Advocate 2011 Annual Report to Congress 531-536 (Legislative Recommendation: *Clarify that the Scope and Standard of Tax Court Determinizations Under Internal Revenue Code Section 6015(f) is De Novo*).

16 Taxpayer First Act of 2018, S. 3246, 115th Cong. (2018).

17 National Taxpayer Advocate 2014 Annual Report to Congress 55-66 (Most Serious Problem: *VTA/TCE Funding: Volunteer Tax Assistance Programs Are Too Restrictive and the Design Grant Structure Is Not Adequately Based on Specific Needs of Served Taxpayer Populations*); National Taxpayer Advocate 2002 Annual Report to Congress vii-viii.

18 National Taxpayer Advocate 2013 Annual Report to Congress 61 (Most Serious Problem: *Regulation of Return Preparers: Taxpayers and Tax Administration Remain Vulnerable to Incompetent and Unscrupulous Return Preparers While the IRS is Enjoined From Continuing its Efforts to Effectively Regulate Unenrolled Preparers*).

19 National Taxpayer Advocate 2011 Annual Report to Congress 48-74 (Most Serious Problem: *Tax-Related Identity Theft Continues to Impose Significant Burdens on Taxpayers and the IRS*).

- **Increase Preparer Penalties.**<sup>20</sup> This provision would increase penalties for improper disclosure or use of information by preparers of tax returns.
- **Tax Court Review of Request for Equitable Innocent Spouse Relief.**<sup>21</sup> This provision clarifies the standards and scope of Tax Court review for equitable innocent spouse relief.
- **Clarify that the Scope and Standard of Tax Court Determinations Under IRC § 6015(f) is *De Novo*.**<sup>22</sup> This provision clarifies that any review of a determination made under IRC § 6015(f) (equitable relief for innocent spouses from joint and several liability on a joint return) will be reviewed *de novo* by the Tax Court.
- **Scannable Returns.**<sup>23</sup> This provision would require that electronically prepared tax returns that are printed and filed on paper include scannable code, which can convert such a tax return to electronic format.
- **Notification to Exempt Organizations.**<sup>24</sup> This provision would require the IRS to provide notice to tax exempt organizations before the revocation of their tax-exempt status for failure to file their tax return for two consecutive years. The notification shall include information about how to comply to avoid loss of tax-exempt status.
- **Restrict Tax Return Disclosures to Necessary Content.**<sup>25</sup> This provision would limit the redisclosures and uses of tax return information to only the express purpose for which consent to use that information was granted. The tax return information shall not be disclosed to any other person without the express permission or request of the taxpayer.
- **Whistleblower.**<sup>26</sup> This provision amends IRC § 7623 to add civil action protections for whistleblowers against retaliation.
- **Referrals to LITCs.**<sup>27</sup> This provision would allow officers and employees of the Department of Treasury to advise taxpayers of the availability of and the eligibility requirements for receiving assistance from LITCs. It would also allow such officers and employees to provide to taxpayers the addresses and contact information for these clinics.

20 National Taxpayer Advocate 2003 Annual Report to Congress 270-301 (Legislative Recommendations: *Federal Tax Return Preparers: Oversight and Compliance*).

21 National Taxpayer Advocate 2001 Annual Report to Congress 128-165 (Legislative Recommendation: *Joint and Several Liability*).

22 National Taxpayer Advocate 2011 Annual Report to Congress 531-536 (Legislative Recommendation: *Clarify that the Scope and Standard of Tax Court Determinations Under Internal Revenue Code Section 6015(f) is De Novo*).

23 National Taxpayer Advocate 2013 Annual Report to Congress vol. 2 70, 91, 96 (Research Study: *Fundamental Changes to Return Filing and Processing Will Assist Taxpayers in Return Preparation and Decrease Improper Payments*).

24 National Taxpayer Advocate 2011 Annual Report to Congress 444 (Most Serious Problem: *The IRS Makes Reinstatement on an Organization's Exempt Status Following Revocation Unnecessarily Burdensome*).

25 National Taxpayer Advocate 2007 Annual Report to Congress 554-555 (Legislative Recommendation: *Consent-Based Disclosures of Tax Return Information Under Internal Revenue Code Section 6103(c)*).

26 National Taxpayer Advocate 2015 Annual Report to Congress 409-412 (Legislative Recommendation: *Whistleblower Program: Enact Anti-Retaliation Legislation to Protect Tax Whistleblowers*).

27 National Taxpayer Advocate 2007 Annual Report to Congress 551-553 (Legislative Recommendation: *Referral to Low Income Taxpayer Clinics*).

### Taxpayer First Act of 2018

On December 10, 2018, Representatives Jenkins and Lewis introduced this legislation.<sup>28</sup> It passed in the House on December 20, 2018. This Act includes several changes and additions from the first House version and the Senate version of the bill, discussed above.<sup>29</sup> It also is nearly identical to Division B of H.R. 88 which was introduced by Representative Brady on December 17, 2018, and passed in the House on December 20, 2018.<sup>30</sup> This legislation would enact many of the National Taxpayer Advocate's prior proposals.

- **Waiver of Installment Agreement Fees for Low Income Taxpayers.**<sup>31</sup> This provision would waive any fee otherwise required with the submission of an OIC for low income taxpayers. While this provision does not mention installment agreement fees as the title of this recommendation suggests, our past MSPs and LRs that discussed this recommendation extend the recommendation to the OIC and user fees that this provision waives.
- **Tax Court Review of Request for Equitable Innocent Spouse Relief.**<sup>32</sup> This provision clarifies the standards and scope of Tax Court review for equitable innocent spouse relief.
- **Clarify that the Scope and Standard of Tax Court Determinations Under IRC § 6015(f) is *De Novo*.**<sup>33</sup> This provision clarifies that any review of a determination made under IRC § 6015(f) (equitable relief for innocent spouses from joint and several liability on a joint return) will be reviewed *de novo* by the Tax Court.
- **Repeal PDC Provisions.**<sup>34</sup> While the National Taxpayer Advocate's legislative recommendation has been to repeal private debt collection (PDC) provisions, she has made additional recent recommendations to establish an income threshold for referral to PDC for taxpayers whose incomes are less than their allowable living expenses or if their adjusted gross income does not

28 Taxpayer First Act of 2018, H.R. 7227, 115th Cong. (2018).

29 Taxpayer First Act, H.R. 5444, 115th Cong. (2018); Taxpayer First Act of 2018, S. 3246, 115th Cong. (2018).

30 Taxpayer First Act of 2018, H.R. 88, 115th Cong. (2018). This legislation included a provision not present in the Taxpayer First Act which would enact one of the National Taxpayer Advocate's proposals regarding the development of online accounts to provide services to taxpayers and their preparers, including obtaining taxpayer information, making payment of taxes, sharing documents, and addressing and correcting issues. See Taxpayer First Act of 2018, H.R. 88, 115th Cong. § 2102 (2018). See also National Taxpayer Advocate 2004 Annual Report to Congress 471-477 (Legislative Recommendation: *Free Electronic Filing for All Taxpayers*).

31 National Taxpayer Advocate 2017 Annual Report to Congress 307-313 (Legislative Recommendation: *User Fees: Prohibit User Fees That Reduce Revenue, Increase Costs, or Erode Taxpayer Rights*); National Taxpayer Advocate 2015 Annual Report to Congress 14-35 (Most Serious Problem: *IRS User Fees: The IRS May Adopt User Fees to Fill Funding Gaps Without Fully Considering Taxpayer Burden and the Impact on Voluntary Compliance*); National Taxpayer Advocate 2007 Annual Report to Congress 66-82 (Most Serious Problem: *User Fees: Taxpayer Service For Sale*); National Taxpayer Advocate 2006 Annual Report to Congress 141-156 (Most Serious Problem: *Collection Issues of Low Income Taxpayers*).

32 National Taxpayer Advocate 2001 Annual Report to Congress 128-165 (Legislative Recommendation: *Joint and Several Liability*).

33 National Taxpayer Advocate 2011 Annual Report to Congress 531-536 (Legislative Recommendation: *Clarify that the Scope and Standard of Tax Court Determinations Under Internal Revenue Code Section 6015(f) is De Novo*).

34 National Taxpayer Advocate 2006 Annual Report to Congress 458-462 (Legislative Recommendation: *Repeal Private Debt Collection Provisions*).

exceed 250 percent of the applicable poverty level.<sup>35</sup> The provision in this bill would establish an income threshold for referral to PDC for taxpayers whose adjusted gross income does not exceed 200 percent of the applicable poverty level.

- **Taxpayer Advocate Directive.**<sup>36</sup> This provision would amend IRC § 7803(c) by adding a segment on the power of the National Taxpayer Advocate to issue TADs, and that the Commissioner of the Internal Revenue Service must modify, rescind, or ensure compliance with a TAD within 90 days of its issuance. The National Taxpayer Advocate may appeal a modification or rescission, to which the Commissioner must ensure compliance or provide the National Taxpayer Advocate with a detailed description of the reasons behind making the modification or rescission.
- **Matching Grants Program for Return Preparation.**<sup>37</sup> This provision would establish a VITA matching grant program.
- **Referrals to LITCs.**<sup>38</sup> This provision would allow officers and employees of the Department of Treasury to advise taxpayers of the availability of and the eligibility requirements for receiving assistance from LITCs. It would also allow such officers and employees to provide to taxpayers the addresses and contact information for these clinics.
- **Whistleblower.**<sup>39</sup> This provision amends IRC § 7623 to add civil action protections for whistleblowers against retaliation.
- **Single Point of Contact.**<sup>40</sup> This provision would require the Secretary of the Treasury to establish and implement procedures to create a single point of contact at the IRS for taxpayers whose tax return has been delayed or adversely affected by tax-related identity theft.
- **Notification of Suspected Identity Theft.**<sup>41</sup> This provision would require the Secretary to notify an individual as soon as practicable if there has been or may have been an unauthorized use of their identity, and it can be disclosed without jeopardizing an investigation relating to tax

35 Most Serious Problem: *Private Debt Collection: The IRS's Expanding Private Debt Collection Program Continues to Burden Taxpayers Who Are Likely Experiencing Economic Hardship While Inactive PCA Inventory Accumulates*, supra; National Taxpayer Advocate 2019 Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration (Amend IRC § 6306(d) to Exclude the Debts of Taxpayers Whose Incomes are Less Than Their Allowable Living Expenses From Assignment to Private Collection Agencies or, if That Is Not Feasible, Exclude the Debts of Taxpayers Whose Incomes Are Less Than 250 Percent of the Federal Poverty Level)* (Dec. 2018); National Taxpayer Advocate 2017 Annual Report to Congress 10-21 (Most Serious Problem: *Private Debt Collection: The IRS's Private Debt Collection Program Is Not Generating Net Revenues, Appears to Have Been Implemented Inconsistently with the Law, and Burdens Taxpayers Experiencing Economic Hardship*).

36 National Taxpayer Advocate 2016 Annual Report to Congress 39-40 (Special Focus: *IRS Future State: The National Taxpayer Advocate's Vision for a Taxpayer-Centric 21st Century Tax Administration*); National Taxpayer Advocate 2011 Annual Report to Congress 573-581 (Legislative Recommendation: *Codify the Authority of the National Taxpayer Advocate to File Amicus Briefs, Comment on Regulations, and Issue Taxpayer Advocate Directives*); National Taxpayer Advocate 2002 Annual Report to Congress 198-215 (Legislative Recommendation: *The Office of the Taxpayer Advocate*).

37 National Taxpayer Advocate 2014 Annual Report to Congress 55-66 (Most Serious Problem: *VTA/TCE Funding: Volunteer Tax Assistance Programs Are Too Restrictive and the Design Grant Structure Is Not Adequately Based on Specific Needs of Served Taxpayer Populations*); National Taxpayer Advocate 2002 Annual Report to Congress vii-viii.

38 National Taxpayer Advocate 2007 Annual Report to Congress 551-553 (Legislative Recommendation: *Referral to Low Income Taxpayer Clinics*).

39 National Taxpayer Advocate 2015 Annual Report to Congress 409-412 (Legislative Recommendation: *Whistleblower Program: Enact Anti-Retaliation Legislation to Protect Tax Whistleblowers*).

40 National Taxpayer Advocate 2013 Annual Report to Congress 61 (Most Serious Problem: *Regulation of Return Preparers: Taxpayers and Tax Administration Remain Vulnerable to Incompetent and Unscrupulous Return Preparers While the IRS is Enjoined From Continuing its Efforts to Effectively Regulate Unenrolled Preparers*).

41 National Taxpayer Advocate 2011 Annual Report to Congress 48-74 (Most Serious Problem: *Tax-Related Identity Theft Continues to Impose Significant Burdens on Taxpayers and the IRS*).

administration. Such notice must include instructions on further steps, including the necessary forms to complete and how to file a report with law enforcement.

- **Increase Preparer Penalties.**<sup>42</sup> This provision would increase penalties for improper disclosure or use of information by preparers of tax returns.
- **Scannable Returns.**<sup>43</sup> This provision would require that electronically prepared tax returns that are printed and filed on paper include scannable code, which can convert such a tax return to electronic format.
- **Require the IRS to Provide Annual Taxpayer Rights Training to Employees.**<sup>44</sup> This provision would require the Commissioner of Internal Revenue to provide Congress with a written report on a comprehensive training strategy, including a plan to develop annual training regarding taxpayer rights, including the role of the Office of the Taxpayer Advocate, for employees that interface with taxpayers and their managers.
- **Notification to Exempt Organizations.**<sup>45</sup> This provision would require the IRS to provide notice to tax exempt organizations before the revocation of their tax-exempt status for failure to file their tax return for two consecutive years. The notification shall include information about how to comply to avoid loss of tax-exempt status.

### Protecting Taxpayers Act

On April 11, 2018, co-sponsors Senators Portman and Cardin introduced this legislation that would enact several of the National Taxpayer Advocate's proposals.<sup>46</sup>

- **Regulation of Income Tax Return Preparers.**<sup>47</sup> This provision would allow the Department of the Treasury to regulate the practice of tax return preparers and give it the authority to sanction regulated tax return preparers. This provision would also provide minimum competency standards for tax return preparers.
- **Permit the IRS to Release Levies on Small Business Taxpayers.**<sup>48</sup> This provision would allow for the release of federal tax levies which cause business hardship.

42 National Taxpayer Advocate 2003 Annual Report to Congress 270-301 (Legislative Recommendations: *Federal Tax Return Preparers: Oversight and Compliance*).

43 National Taxpayer Advocate 2013 Annual Report to Congress vol. 2 70, 91, 96 (Research Study: *Fundamental Changes to Return Filing and Processing Will Assist Taxpayers in Return Preparation and Decrease Improper Payments*).

44 National Taxpayer Advocate 2019 Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration (Codify the Taxpayer Bill of Rights, a Taxpayer Rights Training Requirement, and the IRS Mission Statement As Section 1 of the Internal Revenue Code)* (Dec. 2018); National Taxpayer Advocate Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration 7 (Require the IRS to Provide Annual Taxpayer Rights Training to Employees)* (Dec. 2017).

45 National Taxpayer Advocate 2011 Annual Report to Congress 444 (Most Serious Problem: *The IRS Makes Reinstatement on an Organization's Exempt Status Following Revocation Unnecessarily Burdensome*).

46 Protecting Taxpayers Act, S. 3278, 115th Cong. (2018).

47 National Taxpayer Advocate 2009 Annual Report to Congress 41-69 (Most Serious Problem: *The IRS Lacks a Servicewide Return Preparer Strategy*); National Taxpayer Advocate 2008 Annual Report to Congress 423-426 (Legislative Recommendation: *The Time Has Come to Regulate Federal Tax Return Preparers*); National Taxpayer Advocate 2007 Annual Report to Congress 140-155 (Most Serious Problem: *Preparer Penalties and Bypass of Taxpayers' Representatives*); National Taxpayer Advocate 2007 Annual Report to Congress 83-95 (Most Serious Problem: *The Use and Disclosure of Tax Return Information by Preparers to Facilitate the Marketing of Refund Anticipation Loans and Other Products with High Abuse Potential*); National Taxpayer Advocate 2003 Annual Report to Congress 270-301 (Legislative Recommendation: *Federal Tax Return Preparers: Oversight and Compliance*); National Taxpayer Advocate 2002 Annual Report to Congress 216-230 (Legislative Recommendation: *Regulation of Federal Tax Return Preparers*).

48 National Taxpayer Advocate 2011 Annual Report to Congress 537-543 (Legislative Recommendation: *Amend IRC § 6343(a) to Permit the IRS to Release Levies on Business Taxpayers that Impose Economic Hardship*).

- **Election to Be Treated as an S Corporation.**<sup>49</sup> This provision would give an extension of time for a small business corporation to elect to be treated as an S corporation. Small businesses could make the election no later than the due date for filing the tax return of the S corporation for the taxable year.
- **Repeal PDC Provisions.**<sup>50</sup> While the National Taxpayer Advocate's legislative recommendation has been to repeal PDC provisions, she has made additional recent recommendations to establish an income threshold for referral to PDC for taxpayers whose incomes are less than their allowable living expenses or if their adjusted gross income does not exceed 250 percent of the applicable poverty level.<sup>51</sup> The provision in this bill would establish an income threshold for referral to PDC for taxpayers whose adjusted gross income does not exceed 250 percent of the applicable poverty level.
- **Matching Grants Program for Return Preparation.**<sup>52</sup> This provision would establish a VITA matching grant program.
- **Referrals to LITCs.**<sup>53</sup> This provision would allow the Secretary to refer taxpayers to LITCs, and to promote the benefits and encourage the use of LITCs in mass communications and referrals. It would also allow the VITA grantee programs to advise taxpayers on the availability and eligibility requirements to use LITCs and to provide to taxpayers the addresses and contact information for these clinics.
- **Waiver of Installment Agreement Fees for Low Income Taxpayers.**<sup>54</sup> This provision would waive any fee otherwise required with the submission of an OIC for low income taxpayers. While this provision does not mention installment agreement fees as the title of this recommendation suggests, the past MSPs and LR that discussed this recommendation extend the recommendation to the OIC and user fees that this provision waives.

49 National Taxpayer Advocate 2010 Annual Report to Congress 410-411 (Legislative Recommendation: *Extend the Due Date for S Corporation Elections to Reduce the High Rate of Untimely Elections*); National Taxpayer Advocate 2004 Annual Report to Congress 390-393 (Legislative Recommendation: *Election To Be Treated As An S Corporation*); National Taxpayer Advocate 2002 Annual Report to Congress 246 (Legislative Recommendation: *Election To Be Treated As An S Corporation*).

50 National Taxpayer Advocate 2006 Annual Report to Congress 458-462 (Legislative Recommendation: *Repeal Private Debt Collection Provisions*).

51 Most Serious Problem: *Private Debt Collection: The IRS's Expanding Private Debt Collection Program Continues to Burden Taxpayers Who Are Likely Experiencing Economic Hardship While Inactive PCA Inventory Accumulates*, *supra*; National Taxpayer Advocate 2019 Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration (Amend IRC § 6306(d) to Exclude the Debts of Taxpayers Whose Incomes are Less Than Their Allowable Living Expenses From Assignment to Private Collection Agencies or, if That Is Not Feasible, Exclude the Debts of Taxpayers Whose Incomes Are Less Than 250 Percent of the Federal Poverty Level)* (Dec. 2018); National Taxpayer Advocate 2017 Annual Report to Congress 10-21 (Most Serious Problem: *Private Debt Collection: The IRS's Private Debt Collection Program Is Not Generating Net Revenues, Appears to Have Been Implemented Inconsistently with the Law, and Burdens Taxpayers Experiencing Economic Hardship*).

52 National Taxpayer Advocate 2014 Annual Report to Congress 55-66 (Most Serious Problem: *VTA/TCE Funding: Volunteer Tax Assistance Programs Are Too Restrictive and the Design Grant Structure Is Not Adequately Based on Specific Needs of Served Taxpayer Populations*); National Taxpayer Advocate 2002 Annual Report to Congress vii-viii.

53 National Taxpayer Advocate 2007 Annual Report to Congress 551-553 (Legislative Recommendation: *Referral to Low Income Taxpayer Clinics*).

54 National Taxpayer Advocate 2017 Annual Report to Congress 307-313 (Legislative Recommendation: *User Fees: Prohibit User Fees That Reduce Revenue, Increase Costs, or Erode Taxpayer Rights*); National Taxpayer Advocate 2015 Annual Report to Congress 14-35 (Most Serious Problem: *IRS User Fees: The IRS May Adopt User Fees to Fill Funding Gaps Without Fully Considering Taxpayer Burden and the Impact on Voluntary Compliance*); National Taxpayer Advocate 2007 Annual Report to Congress 66-82 (Most Serious Problem: *User Fees: Taxpayer Service For Sale*); National Taxpayer Advocate 2006 Annual Report to Congress 141-156 (Most Serious Problem: *Collection Issues of Low Income Taxpayers*).

- **Strengthen the Independence of the IRS Office of Appeals.**<sup>55</sup> This provision would give taxpayers the right to a conference with the IRS Office of Appeals that does not include personnel from the IRS Office of Chief Counsel or IRS compliance functions. Such personnel would not be allowed to participate in the conference without the specific consent of the taxpayer to include them.
- **Restrict Tax Return Disclosures to Necessary Content.**<sup>56</sup> This provision would limit the access of non-IRS employees to tax returns and tax return information.
- **Require the IRS to Provide Annual Taxpayer Rights Training to Employees.**<sup>57</sup> This provision would require the Commissioner of the IRS to provide Congress with a written report on a comprehensive training strategy for employees, including a plan to develop annual training regarding taxpayer rights, including the role of the Office of the Taxpayer Advocate.

### 21st Century IRS Act

On April 10, 2018, Representative Bishop and six other Representatives introduced this legislation that would enact two of the National Taxpayer Advocate's recommendations.<sup>58</sup>

- **Restrict Tax Return Disclosures to Necessary Content.**<sup>59</sup> This provision would limit redisclosures and uses of consent-based disclosures of tax return information.
- **Increase Preparer Penalties.**<sup>60</sup> This provision would require the Secretary to publish guidance to establish uniform standards and procedures for accepting electronic signatures with respect to any request for disclosure of a taxpayer's tax return or tax return information to any practitioner or power of attorney. This relates to our recommendation to strengthen oversight of all preparers by enhancing due diligence and signature requirements.

55 National Taxpayer Advocate 2009 Annual Report to Congress 346-350 (Legislative Recommendation: *Strengthen the Independence of the IRS Office of Appeals and Require at Least One Appeals Officer and Settlement Officer in Each State*).

56 National Taxpayer Advocate 2007 Annual Report to Congress 554-555 (Legislative Recommendation: *Consent-Based Disclosures of Tax Return Information Under Internal Revenue Code Section 6103(c)*).

57 National Taxpayer Advocate 2019 Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration (Codify the Taxpayer Bill of Rights, a Taxpayer Rights Training Requirement, and the IRS Mission Statement As Section 1 of the Internal Revenue Code)* (Dec. 2018); National Taxpayer Advocate Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration 7 (Require the IRS to Provide Annual Taxpayer Rights Training to Employees)* (Dec. 2017).

58 21st Century IRS Act, H.R. 5445, 115th Cong. (2018).

59 National Taxpayer Advocate 2007 Annual Report to Congress 554-555 (Legislative Recommendation: *Consent-Based Disclosures of Tax Return Information Under Internal Revenue Code Section 6103(c)*).

60 National Taxpayer Advocate 2003 Annual Report to Congress 270-301 (Legislative Recommendation: *Federal Tax Return Preparers: Oversight and Compliance*).

### Military Taxpayer Assistance Act

In her 2017 Annual Report, the National Taxpayer Advocate discussed problems with the customer service the IRS provided to the military and made both administrative and legislative recommendations to improve it.<sup>61</sup> On April 11, 2018, Representatives Walz and Kind introduced legislation that would enact four of the National Taxpayer Advocate's proposals.<sup>62</sup>

- Provide a year-round dedicated toll-free telephone line for members of the Uniformed Services and their families to answer tax law and filing questions, and to resolve their tax account and compliance issues.
- Create a special unit of Stakeholder Partnerships, Education & Communication (SPEC) staffed, to the extent possible, with veterans whose responsibilities are to develop and conduct outreach, education, and assistance to current military taxpayers, including National Guard and Reservists, and to those organizations that provide tax assistance to these taxpayers.
- Support the authorization of the VITA program and support ample funding for SPEC to provide face-to-face training for military VITA volunteers in overseas locations.
- Assign a dedicated IRS employee to routinely update the military information on the irs.gov website.

In addition to the legislation discussed above, there were a handful of smaller bills introduced during the second session of the 115th Congress relating to the National Taxpayer Advocate's past recommendations that are not highlighted here but are recorded in the table following this introduction.

61 National Taxpayer Advocate 2017 Annual Report to Congress 151-164 (Most Serious Problem: *Military Assistance: The IRS's Customer Service and Information Provided to Military Taxpayers Falls Short of Meeting Their Needs and Preferences*).

62 Military Taxpayer Assistance Act, H.R. 5479, 115th Cong. (2018).

## National Taxpayer Advocate Legislative Recommendations With Congressional Action

Alternative Minimum Tax (AMT)				
<b>Repeal the Individual AMT</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 82–100; National Taxpayer Advocate 2004 Annual Report to Congress 383–385; National Taxpayer Advocate 2008 Annual Report to Congress 356–362.	Repeal the AMT outright.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 1	Brady	11/2/2017	Passed House, Placed on Senate Calendar 11/28/2017
Legislative Activity 113th Congress	S 1616	Lee	10/30/2013	Referred to the Finance Committee
	HR 243	Ross	1/14/2013	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	HR 86	Bachmann	1/5/2011	Referred to the Ways & Means Committee
	HR 99	Dreler	1/5/2011	Referred to the Ways & Means Committee
	HR 547	Garrett	2/8/2011	Referred to the Ways & Means Committee
	HR 3400	Garrett	11/10/2011	Referred to the Ways & Means Committee
	S 727	Wyden	4/5/2011	Referred to the Finance Committee
	S 820	Shelby	4/14/2011	Referred to the Finance Committee
Legislative Activity 111th Congress	HR 3804	Huelskamp	1/23/2012	Referred to the Ways & Means Committee
	S 3018	Wyden	2/23/2010	Referred to the Finance Committee
	HR 240	Garrett	1/7/2009	Referred to the Ways & Means Committee
	HR 782	Paul	1/28/2009	Referred to the Ways & Means Committee
Legislative Activity 110th Congress	S 932	Shelby	4/30/2009	Referred to the Finance Committee
	S 55	Baucus	1/4/2007	Referred to the Finance Committee
	S 14	Kyl	4/17/2007	Referred to the Finance Committee
	S 1040	Shelby	3/29/2007	Referred to the Finance Committee
	HR 1366	English	3/7/2007	Referred to the Ways & Means Committee
	HR 1942	Garrett	4/19/2007	Referred to the Ways & Means Committee
	HR 3970	Rangel	10/25/2007	Referred to the Ways & Means Committee
Legislative Activity 109th Congress	S 2293	Lott	11/1/2007	Placed on the Senate Legislative Calendar under General Orders. Calendar No. 464
	HR 1186	English	3/9/2005	Referred to the Ways & Means Committee
	S 1103	Baucus	5/23/2005	Referred to the Finance Committee
	HR 2950	Neal	6/16/2005	Referred to the Ways & Means Committee
Legislative Activity 108th Congress	HR 3841	Manzullo	9/2/2005	Referred to the Ways & Means Committee
	HR 43	Collins	1/7/2003	Referred to the Ways & Means Committee
	HR 1233	English	3/12/2003	Referred to the Ways & Means Committee
	S 1040	Shelby	5/12/2003	Referred to the Finance Committee
	HR 3060	N. Smith	9/10/2003	Referred to the Ways & Means Committee
	HR 4131	Houghton	4/2/2004	Referred to the Ways & Means Committee
	HR 4164	Shuster	4/2/2004	Referred to the Ways & Means Committee

	Bill Number	Sponsor	Date	Status
Legislative Activity 107th Congress	HR 437	English	2/6/2001	Referred to the Ways & Means Committee
	S 616	Hutchison	3/26/2002	Referred to the Finance Committee
	HR 5166	Portman	7/18/2002	Referred to the Ways & Means Committee
<b>Index Alternative Minimum Tax (AMT) for Inflation</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 82–100.	If full repeal of the individual AMT is not possible, it should be indexed for inflation.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 111th Congress	S 3223	McConnell	9/13/2010	Placed on the Senate Calendar
	HR 5077	Hall	4/20/2010	Referred to the Ways & Means Committee
	HR 719	Lee	1/27/2009	Referred to the Ways & Means Committee
	S 722	Baucus	3/26/2009	Referred to the Finance Committee
Legislative Activity 110th Congress	HR 1942	Garrett	4/19/2007	Referred to the Ways & Means Committee
Legislative Activity 109th Congress	HR 703	Garrett	2/9/2005	Referred to the Ways & Means Committee
	HR 4096	Reynolds	10/20/2005	12/7/2005 Passed the House; 12/13/2005 Placed on the Senate Legislative Calendar
Legislative Activity 108th Congress	HR 22	Houghton	1/7/2003	Referred to the Ways & Means Committee
Legislative Activity 107th Congress	HR 5505	Houghton	10/1/2002	Referred to the Ways & Means Committee
<b>Eliminate Several Adjustments for Individual AMT</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 82–100.	Eliminate personal exemptions, the standard deduction, deductible state and local taxes, and miscellaneous itemized deductions as adjustment items for individual AMT purposes.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 112th Congress	S 336	DeMint	2/14/2011	Referred to the Finance Committee
Legislative Activity 110th Congress	S 102	Kerry	1/4/2007	Referred to the Finance Committee
Legislative Activity 109th Congress	S 1861	Harkin	10/7/2005	Referred to the Finance Committee
Legislative Activity 108th Congress	HR 1939	Neal	5/12/2003	Referred to the Ways & Means Committee
<b>Private Debt Collection (PDC)</b>				
<b>Repeal PDC Provisions</b>				
National Taxpayer Advocate 2006 Annual Report to Congress 458–462.	Repeal IRC § 6306, thereby terminating the PDC initiative.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	S 2425	Cardin	2/14/2018	Referred to the Finance Committee
	HR 2171	Lewis	4/26/2017	Referred to the Ways & Means Committee
Legislative Activity 114th Congress	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee
Legislative Activity 111th Congress	HR 796	Lewis	2/3/2009	Referred to the Ways & Means Committee
Legislative Activity 110th Congress	HR 5719	Rangel	4/16/2008	Referred to the Finance Committee
	S 335	Dorgan	1/18/2007	Referred to the Finance Committee
	HR 695	Van Hollen	1/24/2007	Referred to the Ways & Means Committee
	HR 3056	Rangel	7/17/2007	10/10/2007 Passed the House; 10/15/2007 Referred to the Finance Committee

<b>Establish Income Threshold</b>				
National Taxpayer Advocate 2016 Annual Report to Congress 172-186. National Taxpayer Advocate 2017 Annual Report to Congress 21.	Exclude the debts of taxpayers whose incomes are less than their allowable living expenses from assignment to private collection agencies or, if that is not feasible, exclude the debts of taxpayers whose incomes are less than 250 percent of the federal poverty level).			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 7227	Jenkins	12/10/2018	Passed the House on 12/20/2018, received in the Senate 12/20/2018
	S 3278	Portman/ Cardin	7/26/2018	Referred to Finance Committee
<b>Tax Preparation and Low Income Taxpayer Clinics (LITC)</b>				
<b>Matching Grants Program for Return Preparation</b>				
National Taxpayer Advocate 2002 Annual Report to Congress vii–viii.	Create a grant program for return preparation similar to the LITC grant program. The program should be designed to avoid competition with VITA and should support the IRS's goal (and need) to have returns electronically filed.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 7227	Jenkins	12/10/2018	Passed the House on 12/20/2018, received in the Senate 12/20/2018
	S 3278	Portman/ Cardin	7/26/2018	Referred to Finance Committee
	S 3246	Hatch	7/19/2018	Referred to Finance Committee
	HR 5444	Jenkins	4/10/2018	Passed in the House, received in the Senate 4/19/2018 and referred to the Finance Committee
	HR 2901	Curbelo	6/15/2017	Referred to the Ways & Means Committee
	S 797	Brown	3/30/2017	Referred to Finance Committee
	HR 605	Davis	1/23/2017	Referred to the Ways & Means Committee
	S 193	Brown	1/23/2017	Referred to Finance Committee
Legislative Activity 114th Congress	Pub. L. No. 114-113, Division E (2015).			
	S 3156	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders
	HR 4835	Honda	3/22/2016	Referred to the Ways & Means Committee
	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
Legislative Activity 113th Congress	Pub. L. No. 113-235, Division E, 128 Stat. 2130, 2336 (2014).			
Legislative Activity 111th Congress	Pub. L. No. 111-117, Div. C, Title I, 123 Stat. 3034, 3163 (2009).			
Legislative Activity 110th Congress	Pub. L. No. 110-161, Div. D, Title I, 121 Stat. 1975, 1976 (2007).			
	HR 5716	Becerra	4/8/2008	Referred to the Ways & Means Committee
	S 1219	Bingaman	4/25/2007	Referred to the Finance Committee
	S 1967	Clinton	8/2/2007	Referred to the Finance Committee

	Bill Number	Sponsor	Date	Status
Legislative Activity 109th Congress	HR 894	Becerra	2/17/2005	Referred to the Financial Institutions and Consumer Credit Subcommittee
	S 832	Bingaman	4/18/2005	Referred to the Finance Committee
	S 1321	Santorum	6/28/2005	9/15/2006 Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with S. Rep. No. 109-336 9/15/2006 Placed on the Senate Legislative Calendar under General Orders. Calendar No. 614
Legislative Activity 108th Congress	S 476	Grassley	2/27/2003	Referred to the Finance Committee
	S 685	Bingaman	3/21/2003	Referred to the Finance Committee
	S 882	Baucus	4/10/2003	5/19/2004 S 882 was incorporated into HR 1528 as an amendment and HR 1528 passed in lieu of S 882
	HR 1661	Rangel	4/8/2003	Referred to the Ways & Means Committee
	HR 3983	Becerra	3/17/2004	Referred to the Ways & Means Committee
Legislative Activity 107th Congress	HR 586	Lewis	2/13/2001	4/18/2002 Passed the House with an amendment; referred to the Senate
	HR 3991	Houghton	3/19/2001	Referred to the Ways & Means Committee
	HR 7	Baucus	7/16/2002	Reported by Chairman Baucus with an amendment; referred to the Finance Committee
<b>Referrals to LITCs</b>				
National Taxpayer Advocate 2007 Annual Report to Congress 551–553.	Amend IRC § 7526(c) to add a special rule stating that notwithstanding any other provision of law, IRS employees may refer taxpayers to LITCs receiving funding under this section. This change will allow IRS employees to refer a taxpayer to a specific clinic for assistance.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 7227	Jenkins	12/10/2018	Passed the House on 12/20/2018, received in the Senate 12/20/2018
	S 3278	Portman/ Cardin	7/26/2018	Referred to the Finance Committee
	S 3246	Hatch	7/19/2018	Referred to the Finance Committee
	HR 5444	Jenkins	4/10/2018	Passed in the House, received in the Senate 4/19/2018 and referred to the Finance Committee
	HR 5438	Holding	4/19/2018	Passed the House
	HR 2171	Lewis	4/26/2017	Referred to the Ways & Means Committee
Legislative Activity 114th Congress	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee
	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	S 1573	Durbin	9/15/2011	Placed on the Senate Legislative Calendar under General Orders; Calendar No. 171
	S 3355	Bingaman	6/28/2012	Referred to the Finance Committee
	HR 6050	Becerra	6/28/2012	Referred to the Ways & Means Committee

	Bill Number	Sponsor	Date	Status
Legislative Activity 111th Congress	HR 4994	Lewis	4/13/2010	Referred to the Ways & Means Committee
	S 3215	Bingaman	4/15/2010	Referred to the Finance Committee
	HR 5047	Becerra	4/15/2010	Referred to the Ways & Means Committee
Legislative Activity 110th Congress	HR 5719	Rangel	4/16/2008	Referred to the Finance Committee
<b>Regulation of Income Tax Return Preparers</b>				
National Taxpayer Advocate 2002 Annual Report to Congress 216–230; National Taxpayer Advocate 2003 Annual Report to Congress 270–301; National Taxpayer Advocate 2007 Annual Report to Congress 83–95 & 140–155; National Taxpayer Advocate 2008 Annual Report to Congress 423–426; National Taxpayer Advocate 2009 Annual Report to Congress 41–69; National Taxpayer Advocate 2009 Annual Report to Congress 60–74.	Create an effective oversight and penalty regime for return preparers by taking the following steps: <ul style="list-style-type: none"> <li>◆ Enact a registration, examination, certification, and enforcement program for federal tax return preparers;</li> <li>◆ Direct the Secretary of the Treasury to establish a joint task force to obtain accurate data about the composition of the return preparer community and make recommendations about the most effective means to ensure accurate and professional return preparation and oversight;</li> <li>◆ Require the Secretary of the Treasury to study the impact cross-marketing tax preparation services with other consumer products and services has on the accuracy of returns and tax compliance; and</li> <li>◆ Require the IRS to take steps within its existing administrative authority, including requiring a checkbox on all returns in which preparers would enter their category of return preparer (i.e., attorney, CPA, enrolled agent, or unenrolled preparer) and developing a simple, easy-to-read pamphlet for taxpayers that explains their protections.</li> </ul>			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	S 3278	Portman/ Cardin	7/26/2018	Referred to the Finance Committee
	HR 2171	Lewis	4/26/2017	Referred to the Ways & Means Committee
	HR 1996	Bonamici	4/6/2017	Referred to House Financial Services
	S 606	Nelson	3/9/2017	Referred to the Finance Committee
Legislative Activity 114th Congress	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee
	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	S 3355	Bingaman	6/28/2012	Referred to the Finance Committee
	HR 6050	Becerra	6/28/2012	Referred to the Ways & Means Committee
Legislative Activity 111th Congress	S 3215	Bingaman	4/15/2010	Referred to the Finance Committee
	HR 5047	Becerra	4/15/2010	Referred to the Ways & Means Committee
Legislative Activity 110th Congress	HR 5716	Becerra	4/8/2008	Referred to the Ways & Means Committee
	S 1219	Bingaman	4/25/2007	Referred to the Finance Committee
Legislative Activity 109th Congress	HR 894	Becerra	2/17/2005	Referred to the Financial Institutions and Consumer Credit Subcommittee
	S 832	Bingaman	4/18/2005	Referred to the Finance Committee
	S 1321	Santorum	6/28/2005	9/15/2006 Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with written report No. 109-336 9/15/2006 Placed on Senate Legislative Calendar under General Orders; Calendar No. 614
Legislative Activity 108th Congress	S 685	Bingaman	3/21/2003	Referred to the Finance Committee
	S 882	Baucus	4/10/2003	5/19/2004 S 882 was incorporated into HR 1528 as an amendment and HR 1528 passed in lieu of S 882
	HR 3983	Becerra	3/17/2004	Referred to the Ways & Means Committee

**Identity Theft****Single Point of Contact**

National Taxpayer Advocate 2013 Annual Report to Congress 61.

Designate a single point of contact for identity theft victims to work with the identity theft victim until all related issues are resolved.

	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 7227	Jenkins	12/10/2018	Passed the House on 12/20/2018, received in the Senate 12/20/2018
	S 3246	Hatch	7/19/2018	Referred to Finance Committee
	HR 5444	Jenkins	4/10/2018	Passed in the House, received in the Senate 4/19/2018 and referred to the Finance Committee
	HR 5439	Renacci	4/9/2018	Passed the House on 4/17/2018; 4/18/2018 Pursuant to the provisions in H. Res. 831, H.R. 5439 is laid on the table
	HR 2171	Lewis	4/26/2017	Referred to the Ways & Means Committee
	HR 439	Renacci	1/11/2017	Referred to the Ways & Means Committee
Legislative Activity 114th Congress	S 3157	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders
	S 3156	Hatch	7/12/2016	Referred to Finance Committee
	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee
	S 767	Nelson	3/9/2015	Referred to Finance Committee
Legislative Activity 113th Congress	S 2736	Hatch	7/31/2014	Referred to Finance Committee

**Notification of Suspected Identity Theft**

National Taxpayer Advocate 2011 Annual Report to Congress 75-83.

Require the IRS to notify taxpayers of suspected identity theft, including employment-related identity theft.

	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 7227	Jenkins	12/10/2018	Passed the House on 12/20/2018, received in the Senate 12/20/2018
	S 3246	Hatch	7/19/2018	Referred to Finance Committee
	HR 2171	Lewis	4/26/2017	Referred to the Ways & Means Committee
	HR 439	Renacci	1/11/2017	Referred to the Ways & Means Committee
	S 606	Nelson	3/9/2017	Referred to Finance Committee
Legislative Activity 114th Congress	S 3157	Hatch	7/12/2016	Referred to Finance Committee
	S 3156	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders
	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee

**Public Awareness Campaign for Low Income Taxpayer Clinics**

National Taxpayer Advocate 2014 Annual Report to Congress 411-416;  
National Taxpayer Advocate 2014 Annual Report to Congress, vol. 2 1-26;  
National Taxpayer Advocate 2007 Annual Report to Congress 551-553.

Authorize the Secretary to promote the benefits of and encourage the use of qualified LITCs through the use of mass communications, referrals, and other means.

	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 5438	Holding	4/9/2018	Referred to the Ways & Means Committee
Legislative Activity 114th Congress	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee

<b>Public Awareness Campaign on Registration Requirements</b>				
National Taxpayer Advocate 2002 Annual Report to Congress 216–230.	Authorize the IRS to conduct a public information and consumer education campaign, utilizing paid advertising, to inform the public of the requirements that paid preparers must sign the return prepared for a fee and display registration cards.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 111th Congress	S 3215	Bingaman	4/15/2010	Referred to the Finance Committee
	HR 5047	Becerra	4/15/2010	Referred to the Ways & Means Committee
Legislative Activity 110th Congress	HR 5716	Becerra	4/8/2008	Referred to the Ways & Means Committee
	S 1219	Bingaman	4/25/2007	Referred to the Finance Committee
Legislative Activity 109th Congress	HR 894	Becerra	2/17/2005	Referred to the Financial Institutions and Consumer Credit Subcommittee
	S 832	Bingaman	4/18/2005	Referred to the Finance Committee
	S 1321	Santorum	6/28/2005	9/15/2006 Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with S. Rep. No. 109-336 9/15/2006 Placed on the Senate Legislative Calendar under General Orders; Calendar No. 614
Legislative Activity 108th Congress	S 685	Bingaman	3/21/2003	Referred to the Finance Committee
	S 882	Baucus	4/10/2003	5/19/2004 S 882 was incorporated into HR 1528 as an amendment and HR 1528 passed in lieu of S 882
	HR 3983	Becerra	3/17/2004	Referred to the Ways & Means Committee
<b>Increase Preparer Penalties</b>				
National Taxpayer Advocate 2003 Annual Report to Congress 270–301.	Strengthen oversight of all preparers by enhancing due diligence and signature requirements, increasing the dollar amount of preparer penalties, and assessing and collecting those penalties, as appropriate.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	S 3246	Hatch	7/19/2018	Referred to the Finance Committee
	HR 5445	Bishop	4/10/2018	Passed in the House
	HR 7227	Jenkins	12/17/2018	Passed the House on 12/20/2018, received in the Senate 12/20/2018
Legislative Activity 112th Congress	Pub. L. No. 112-41 § 501, 125 Stat. 428, 459 (2011).			
Legislative Activity 111th Congress	S 3215	Bingaman	4/15/2010	Referred to the Finance Committee
	HR 5047	Becerra	4/15/2010	Referred to the Ways & Means Committee
Legislative Activity 110th Congress	HR 5719	Rangel	4/16/2008	Referred to the Finance Committee
	HR 4318	Crowley/ Ramstad	12/6/2007	Referred to the Ways & Means Committee
	S 2851	Bunning	4/14/2008	Referred to the Finance Committee
	S 1219	Bingaman	4/25/2007	Referred to the Finance Committee
Legislative Activity 109th Congress	HR 894	Becerra	2/17/2005	Referred to the Financial Institutions and Consumer Credit Subcommittee
	S 832	Bingaman	4/18/2005	Referred to the Finance Committee
	S 1321	Santorum	6/28/2005	9/15/2006 Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with written report No. 109-336 9/15/2006 Placed on Senate Legislative Calendar under General Orders; Calendar No. 614

	Bill Number	Sponsor	Date	Status
Legislative Activity 108th Congress	S 685	Bingaman	3/21/2003	Referred to the Finance Committee
	S 882	Baucus	4/10/2003	5/19/2004 S 882 was incorporated into HR 1528 as an amendment and HR 1528 passed in lieu of S 882
	HR 3983	Becerra	3/17/2004	Referred to the Ways & Means Committee
<b>Refund Delivery Options</b>				
National Taxpayer Advocate 2008 Annual Report to Congress 427–441.	Direct the Department of the Treasury and the IRS to (1) minimize refund turnaround times; (2) implement a Revenue Protection Indicator; (3) develop a program to enable unbanked taxpayers to receive refunds on stored value cards (SVCs); and (4) conduct a public awareness campaign to disseminate accurate information about refund delivery options.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 112th Congress	S 3355	Bingaman	6/28/2012	Referred to the Finance Committee
	HR 6050	Becerra	6/28/2012	Referred to the Ways & Means Committee
Legislative Activity 111th Congress	S 3215	Bingaman	4/15/2010	Referred to the Finance Committee
	HR 5047	Becerra	4/15/2010	Referred to the Ways & Means Committee
	HR 4994	Lewis	4/13/2010	Referred to the Ways & Means Committee
<b>Small Business Issues</b>				
<b>Health Insurance Deduction/Self-Employed Individuals</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 223; National Taxpayer Advocate 2008 Annual Report to Congress 388–389.	Allow self-employed taxpayers to deduct the costs of health insurance premiums for purposes of self-employment taxes.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 111th Congress	Pub. L. No. 111-240, § 2504 Stat 2560 (2010).			
	S 725	Bingaman	3/26/2009	Referred to the Finance Committee
	HR 1470	Kind	3/12/2009	Referred to the Ways & Means Committee
Legislative Activity 110th Congress	S 2239	Bingaman	10/25/2007	Referred to the Finance Committee
Legislative Activity 109th Congress	S 663	Bingaman	3/17/2005	Referred to the Finance Committee
	S 3857	Smith	9/16/2006	Referred to the Finance Committee
Legislative Activity 108th Congress	HR 741	Sanchez	2/12/2003	Referred to the Ways & Means Committee
	HR 1873	Manzullo Velazquez	4/30/2003	Referred to the Ways & Means Committee
Legislative Activity 107th Congress	S 2130	Bingaman	4/15/2002	Referred to the Finance Committee
<b>Married Couples as Business Co-owners</b>				
National Taxpayer Advocate 2002 Annual Report to Congress 172–184.	Amend IRC § 761(a) to allow a married couple operating a business as co-owners to elect out of subchapter K of the IRC and file one Schedule C (or Schedule F in the case of a farming business) and two Schedules SE if certain conditions apply.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 110th Congress	Pub.L. No. 110-28, Title VIII, § 8215, 121 Stat. 193, 194 (2007).			
Legislative Activity 109th Congress	HR 3629	Doggett	7/29/2005	Referred to the Ways & Means Committee
	HR 3841	Manzullo	9/2/2005	Referred to the Ways & Means Committee
Legislative Activity 108th Congress	HR 1528	Portman	6/20/2003	5/19/2004 Passed/agreed to in Senate, with an amendment
	S 842	Kerry	4/9/2003	Referred to the Finance Committee
	HR 1640	Udall	4/3/2003	Referred to the Ways & Means Committee
	HR 1558	Doggett	4/2/2003	Referred to the Ways & Means Committee

<b>Income Averaging for Commercial Fishermen</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 226.	Amend IRC § 1301(a) to provide commercial fishermen the benefit of income averaging currently available to farmers.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 108th Congress	Pub. L. No. 108-357, § 314, 118 Stat. 1468, 1469 (2004).			
<b>Election to Be Treated As an S Corporation</b>				
National Taxpayer Advocate 2004 Annual Report to Congress 390–393.	Amend IRC § 1362(a) to allow a small business corporation to elect to be treated as an S corporation no later than the date it timely files (including extensions) its first Form 1120S, <i>U.S. Income Tax Return for an S Corporation</i> .			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	S 3278	Portman/ Cardin	7/26/2018	Referred to the Finance Committee
Legislative Activity 112th Congress	S 2271	Franken	3/29/2012	Referred to the Finance Committee
Legislative Activity 109th Congress	HR 3629	Doggett	7/29/2005	Referred to the Ways & Means Committee
	HR 3841	Manzullo	9/2/2005	Referred to the Ways & Means Committee
<b>Regulation of Payroll Tax Deposits Agents</b>				
National Taxpayer Advocate 2004 Annual Report to Congress 394–399.	<ul style="list-style-type: none"> <li>◆ Amend the IRC to require any person who enters into an agreement with an employer to collect, report, and pay any employment taxes to furnish a performance bond that specifically guarantees payment of federal payroll taxes collected, deducted, or withheld by such person from an employer and from wages or compensation paid to employees;</li> <li>◆ Amend IRC § 3504 to require agents with an approved Form 2678, <i>Employer/Payer Appointment of Agent</i>, to allocate reported and paid employment taxes among their clients using a form prescribed by the IRS and impose a penalty for the failure to file absent reasonable cause; and</li> <li>◆ Amend the U.S. Bankruptcy Code to clarify that IRC § 6672 penalties survive bankruptcy in the case of non-individual debtors.</li> </ul>			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	Pub. L. No. 114-113, Division E, § 106 (2015).			
Legislative Activity 113th Congress	S 900	Mikulski	05/08/2013	Referred to the Finance Committee
Legislative Activity 110th Congress	S 1773	Snowe	7/12/2007	Referred to the Finance Committee
Legislative Activity 109th Congress	S 3583	Snowe	6/27/2006	Referred to the Finance Committee
	S 1321	Santorum	6/28/2005	9/15/2006 The Finance Committee. Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with written report No. 109-336 9/15/2006 Placed on the Senate Legislative Calendar under General Orders; Calendar No. 614
<b>Issue Dual Address Change Notice</b>				
National Taxpayer Advocate 2004 Annual Report to Congress 394–399.	Issue dual address change notices related to an employer making employment tax payments (with one notice sent to both the employer's former and new address).			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	Pub. L. No. 114-113, Division E, § 106 (2015).			
Legislative Activity 113th Congress	Pub. L. No. 113-76, Division E, Title I, § 106, 128 Stat. 5, 190 (2014) and Pub. L. No. 113-235, Division E, Title I, § 106, 128 Stat. 2130, 2338 (2014).			

<b>Special Consideration for Offer in Compromise</b>				
National Taxpayer Advocate 2004 Annual Report to Congress 394–399.		Give special consideration to an offer in compromise (OIC) request from a victim of fraud or bankruptcy by a third-party payroll tax preparer.		
	Bill Number	Sponsor	Date	Status
Legislative Activity 113th Congress	Pub. L. No. 113-76, Division E, Title I, § 106, 128 Stat. 5, 190 (2014) and Pub. L. No. 113-235, Division E, Title I, § 106, 128 Stat. 2130, 2338 (2014).			
<b>Simplification</b>				
<b>Reduce the Number of Tax Preferences</b>				
National Taxpayer Advocate 2010 Annual Report to Congress 365–372.		Simplify the complexity of the tax code generally by reducing the number of tax preferences.		
	Bill Number	Sponsor	Date	Status
Legislative Activity 112th Congress	S 727	Wyden	4/5/2011	Referred to the Finance Committee
<b>Simplify and Streamline Education Tax Incentives</b>				
National Taxpayer Advocate 2008 Annual Report to Congress 370–372; National Taxpayer Advocate 2004 Annual Report to Congress 403–422.		Enact reforms to simplify and streamline the education tax incentives by consolidating, creating uniformity among, or adding permanency to the various education tax incentives. Specifically, (1) incentives under § 25A should be consolidated with § 222 and possibly § 221; (2) the education provisions should be made more consistent regarding the relationship of the student to the taxpayer; (3) the definitions for “Qualified Higher Education Expenses” and “Eligible Education Institution” should be simplified; (4) the income level and phase-out calculations should be more consistent under the various provisions; (5) all dollar amounts should be indexed for inflation; and (6) after initial use of sunset provisions and simplification amendments, the incentives should be made permanent.		
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 823	Doggett	2/2/2017	Referred to the Ways & Means Committee
	HR 1	Brady	11/2/2017	Passed House, placed on Senate Calendar 11/28/2017
Legislative Activity 114th Congress	S 699	Schumer	3/10/2015	Referred to the Finance Committee
	HR 1260	Doggett	3/4/2015	Referred to the Ways & Means Committee
Legislative Activity 113th Congress	S 835	Schumer	4/25/2013	Referred to the Finance Committee
	HR 1738	Doggett	4/25/2013	Referred to the Ways & Means Committee
	HR 3476	Israel	11/13/2013	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	S 727	Wyden	4/5/2011	Referred to the Finance Committee
	S 3267	Schumer	6/6/2012	Referred to the Finance Committee
	HR 6522	Israel	9/21/2012	Referred to the Ways & Means Committee
<b>Simplify and Streamline Retirement Savings Tax Incentives</b>				
National Taxpayer Advocate 2008 Annual Report to Congress 373–374; National Taxpayer Advocate 2004 Annual Report to Congress 423–432.		Consolidate existing retirement incentives, particularly where the differences in plan attributes are minor. For instance, Congress should consider establishing one retirement plan for individual taxpayers, one for plans offered by small businesses, and one suitable for large businesses and governmental entities (eliminating plans that are limited to governmental entities). At a minimum, Congress should establish uniform rules regarding hardship withdrawals, plan loans, and portability.		
	Bill Number	Sponsor	Date	Status
Legislative Activity 112th Congress	S 727	Wyden	4/5/2011	Referred to the Finance Committee

<b>Children Income</b>				
National Taxpayer Advocate 2002 Annual Report to Congress 231-234	Repeal the rules under Internal Revenue Code section 1(g) that govern the taxation of investment income of children under age 14 and thereby sever the link between the computation of the child's tax liability and the parent's tax return.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 1	Brady	11/2/2017	Pub. L. No. 115-97, § 11001 (2017)
<b>Tax Gap Provisions</b>				
<b>Corporate Information Reporting</b>				
National Taxpayer Advocate 2008 Annual Report to Congress 388.	Require businesses that pay \$600 or more during the year to non-corporate and corporate service providers to file an information report with each provider and with the IRS. Information reporting already is required on payments for services to non-corporate providers. This applies to payments made after December 31, 2011.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 111th Congress	S 1796	Baucus	10/19/2009	10/19/2009 Placed on Senate Legislative Calendar under General Orders; Calendar No. 184
<b>Reporting on Customer's Basis in Security Transaction</b>				
National Taxpayer Advocate 2005 Annual Report to Congress 433-441.	Require brokers to keep track of an investor's basis, transfer basis information to a successor broker if the investor transfers the stock or mutual fund holding, and report basis information to the taxpayer and the IRS (along with the proceeds generated by a sale) on Form 1099-B.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 110th Congress	Pub. L. No. 110-343, § 403, 121 Stat. 3854, 3855 (2008).			
	HR 878	Emanuel	2/7/2007	Referred to the Ways & Means Committee
	S 601	Bayh	2/14/2007	Referred to the Finance Committee
	S 1111	Wyden	4/16/2007	Referred to the Finance Committee
	HR 2147	Emanuel	5/3/2007	Referred to the Ways & Means Committee
	HR 3996 PCS	Rangel	10/30/2007	11/14/2007 Placed on the Senate Calendar; became Pub. L. No. 110-166 (2007) without this provision
Legislative Activity 109th Congress	S 2414	Bayh	3/14/2006	Referred to the Finance Committee
	HR 5176	Emanuel	4/25/2006	Referred to the Ways & Means Committee
	HR 5367	Emanuel	5/11/2006	Referred to the Ways & Means Committee
<b>IRS Forms Revisions</b>				
National Taxpayer Advocate 2004 Annual Report to Congress 480; National Taxpayer Advocate 2010 Annual Report to Congress 40.	Revise Form 1040, Schedule C, to include a line item showing the amount of self-employment income that was reported on Forms 1099-MISC.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 112th Congress	S 1289	Carper	6/28/2011	Referred to the Finance Committee

<p><b>IRS to Promote Estimated Tax Payments Through the Electronic Federal Tax Payment System (EFTPS)</b></p> <p>National Taxpayer Advocate 2005 Annual Report to Congress 381–396.</p>	<p>Amend IRC § 6302(h) to require the IRS to promote estimated tax payments through EFTPS and establish a goal of collecting at least 75 percent of all estimated tax payment dollars through EFTPS by FY 2012.</p>			
	Bill Number	Sponsor	Date	Status
<p>Legislative Activity 109th Congress</p>	S 1321RS	Santorum	6/28/2005	<p>9/15/2006 The Finance Committee. Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with written report No. 109-336</p> <p>9/15/2006 Placed on the Senate Legislative Calendar under General Orders; Calendar No. 614</p>
<p><b>Study of Use of Voluntary Withholding Agreements</b></p> <p>National Taxpayer Advocate 2004 Annual Report to Congress 478–489; National Taxpayer Advocate 2005 Annual Report to Congress 381–396.</p>	<p>Amend IRC § 3402(p)(3) to specifically authorize voluntary withholdings agreements between independent contractors and service-recipients as defined in IRC § 6041A(a)(1).</p>			
	Bill Number	Sponsor	Date	Status
<p>Legislative Activity 109th Congress</p>	S 1321RS	Santorum	6/28/2005	<p>9/15/2006 The Finance Committee. Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with written report No. 109-336.</p> <p>9/15/2006 Placed on the Senate Legislative Calendar under General Orders; Calendar No. 614</p>
<p><b>Require Form 1099 Reporting for Incorporated Service Providers</b></p> <p>National Taxpayer Advocate 2007 Annual Report to Congress 494–496.</p>	<p>Require service recipients to issue Forms 1099-MISC to incorporated service providers and increase the penalties for failure to comply with the information reporting requirements.</p>			
	Bill Number	Sponsor	Date	Status
<p>Legislative Activity 111th Congress</p>	<p>Pub. L No. 111-148 § 9006 (2010).</p> <p>However, this Act also contains a reporting requirement for goods sold, which the National Taxpayer Advocate opposes because of the enormous burden it places on businesses. See Legislative Recommendation: Repeal the Information Reporting Requirement for Purchases of Goods over \$600, but Require Reporting on Corporate and Certain Other Payments.</p>			
<p><b>Require Financial Institutions to Report All Accounts to the IRS by Eliminating the \$10 Threshold on Interest Reporting</b></p> <p>National Taxpayer Advocate 2007 Annual Report to Congress 501–502.</p>	<p>Eliminate the \$10 interest threshold beneath which financial institutions are not required to file Form 1099-INT reports with the IRS.</p>			
	Bill Number	Sponsor	Date	Status
<p>Legislative Activity 112th Congress</p>	S 1289	Carper	6/28/2011	Referred to the Finance Committee
<p>Legislative Activity 111th Congress</p>	S 3795	Carper	9/16/2010	Referred to the Finance Committee

<p><b>Revise Form 1040, Schedule C to Break Out Gross Receipts Reported on Payee Statements Such as Form 1099</b></p> <p>National Taxpayer Advocate 2007 Annual Report to Congress 40.</p>	<p>Administrative recommendation that the IRS add a line to Schedule C, so that taxpayers would separately report the amount of income reported to them on Forms 1099 and other income not reported on Forms 1099. If enacted by statute, the IRS would be required to implement this recommendation.</p>			
	Bill Number	Sponsor	Date	Status
Legislative Activity 111th Congress	S 3795	Carper	9/16/2010	Referred to the Finance Committee
<p><b>Include a Checkbox on Business Returns Requiring Taxpayers to Verify That They Filed All Required Forms 1099</b></p> <p>National Taxpayer Advocate 2007 Annual Report to Congress 40.</p>	<p>Administrative recommendation that the IRS require all businesses to answer two questions on their income tax returns: “Did you make any payments over \$600 in the aggregate during the year to any unincorporated trade or business?” and “If yes, did you file all required Forms 1099?” S 3795 would require the IRS to study whether placing a checkbox or similar indicator on business tax returns would affect voluntary compliance.</p>			
	Bill Number	Sponsor	Date	Status
Legislative Activity 111th Congress	S 3795	Carper	9/16/2010	Referred to the Finance Committee
<p><b>Authorize Voluntary Withholding Upon Request</b></p> <p>National Taxpayer Advocate 2007 Annual Report to Congress 493–494.</p>	<p>Authorize voluntary withholding agreements between independent contractors and service recipients.</p>			
	Bill Number	Sponsor	Date	Status
Legislative Activity 111th Congress	S 3795	Carper	9/16/2010	Referred to the Finance Committee
<p><b>Require Backup Withholding on Certain Payments When TINs Cannot Be Validated</b></p> <p>National Taxpayer Advocate 2005 Annual Report to Congress 238–248.</p>	<p>Administrative recommendation that the IRS require payors to commence backup withholding if they do not receive verification of a payee’s TIN. (S 3795 would require voluntary withholding on certain payments.)</p>			
	Bill Number	Sponsor	Date	Status
Legislative Activity 111th Congress	S 3795	Carper	9/16/2010	Referred to the Finance Committee
<p><b>Worker Classification</b></p> <p>National Taxpayer Advocate 2008 Annual Report to Congress 375–390.</p>	<p>Direct Treasury and the Joint Committee on Taxation to report on the operation of the revised worker classification rules and provide recommendations to increase compliance.</p>			
	Bill Number	Sponsor	Date	Status
Legislative Activity 112th Congress	S 1289	Carper	6/28/2011	Referred to the Finance Committee

### Taxpayer Bill of Rights and *De Minimis* “Apology” Payments

#### Taxpayer Bill of Rights

National Taxpayer Advocate 2014 Annual Report to Congress;  
National Taxpayer Advocate 2013 Annual Report to Congress;  
National Taxpayer Advocate 2011 Annual Report to Congress 493–518;  
National Taxpayer Advocate 2007 Annual Report to Congress 478–448.

Enact a Taxpayer Bill of Rights setting forth the fundamental rights and obligations of U.S. taxpayers.

	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	Pub. L. No. 114-113, Division Q § 401 (2015).			
	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
	S 1578	Grassley	6/16/2015	Referred to the Finance Committee
	S 943	Portman	4/15/2015	Referred to the Finance Committee
	S 951	Ayotte	4/15/2015	Referred to the Finance Committee
	HR 1058	Roskam	2/25/2015	Passed the House of Representatives, and was referred to the Finance Committee on 4/16/2015
Legislative Activity 113th Congress	HR 2768	Roskam	6/22/2013	Passed the House of Representatives, and was referred to the Finance Committee on 8/31/2013
Legislative Activity 112th Congress	S 3355	Bingaman	6/28/2012	Referred to the Finance Committee
	HR 6050	Becerra	6/28/2012	Referred to the Ways & Means Committee
Legislative Activity 111th Congress	S 3215	Bingaman	4/15/2010	Referred to the Ways & Means Committee
	HR 5047	Becerra	4/15/2010	Referred to the Finance Committee
Legislative Activity 110th Congress	HR 5716	Becerra	4/8/2008	Referred to the Ways & Means Committee

#### *De Minimis* “Apology” Payments

National Taxpayer Advocate 2007 Annual Report to Congress 490.

Grant the National Taxpayer Advocate the discretionary, nondelegable authority to provide *de minimis* compensation to taxpayers where the action or inaction of the IRS has caused excessive expense or undue burden to the taxpayer and the taxpayer meets the IRC § 7811 definition of significant hardship.

	Bill Number	Sponsor	Date	Status
Legislative Activity 112th Congress	S 1289	Carper	6/28/2011	Referred to the Finance Committee
Legislative Activity 111th Congress	S 3795	Carper	9/16/2010	Referred to the Finance Committee

#### Toll the Time Period for Financially Disabled Taxpayers to Request Return of Levy Proceeds to Better Protect Their Right to a Fair and Just Tax System

National Taxpayer Advocate 2015 Annual Report to Congress 368–375

Requiring tolling for claims of financially disabled taxpayers.

	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 2171	Lewis	4/26/2017	Referred to the Ways & Means Committee
Legislative Activity 114th Congress	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee

<b>Simplify the Tax Treatment of Cancellation of Debt Income</b>				
National Taxpayer Advocate 2008 Annual Report to Congress 391–396.	Enact one of several proposed alternatives to remove taxpayers with modest amounts of debt cancellation from the cancellation of debt income regime.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 3340	Doggett	7/20/2017	Referred to the Ways & Means Committee, and the Financial Services Committee
Legislative Activity 111th Congress	HR 4561	Lewis	2/2/2010	Referred to the Ways & Means Committee
<b>Joint and Several Liability</b>				
<b>Tax Court Review of Request for Equitable Innocent Spouse Relief</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 128–165.	Amend IRC § 6015(e) to clarify that taxpayers have the right to petition the Tax Court to challenge determinations in cases seeking relief under IRC § 6015(f) alone.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 5444	Jenkins	4/10/2018	Passed in the House, Received in the Senate 4/19/2018 and referred to the Finance Committee
	S 3246	Hatch	7/19/2018	Referred to the Finance Committee
Legislative Activity 109th Congress	Pub. L. No. 109-432, § 408, 120 Stat. 3061, 3062 (2006).			
<b>Effect of Automatic Stay Imposed in Bankruptcy Cases Upon Innocent Spouse and CDP Petitions in Tax Court</b>				
National Taxpayer Advocate 2004 Annual Report to Congress 490–492.	Allow a taxpayer seeking review of an innocent spouse claim or a collection case in U.S. Tax Court a 60-day suspension of the period for filing a petition for review, when the U.S. Bankruptcy Court has issued an automatic stay in a bankruptcy case involving the taxpayer's claim.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 949	Cornyn	4/15/2015	Referred to the Finance Committee
	HR 1828	Thornberry	4/15/2015	Referred to the Ways & Means Committee
Legislative Activity 113th Congress	S 725	Cornyn	4/15/2013	Referred to the Finance Committee
	HR 3479	Thornberry	11/13/2013	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	HR 4375	Johnson	4/17/2012	Referred to the Ways & Means Committee
	S 2291	Cornyn	4/17/2012	Referred to the Ways & Means Committee
<b>Clarify That the Scope and Standard of Tax Court Determinations Under IRC § 6015(f) Is De Novo.</b>				
National Taxpayer Advocate 2011 Annual Report to Congress 531–536.	Amend IRC § 6015 to specify that the scope and standard of review in Tax Court determinations under IRC § 6015(f) is <i>de novo</i> .			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 5444	Jenkins	4/10/2018	Passed in the House, received in the Senate 4/19/2018 and referred to the Finance Committee
	S 3246	Hatch	7/19/2018	Referred to the Finance Committee
	HR 3340	Doggett	7/20/2017	Referred to the Ways & Means Committee, and the Financial Services Committee

	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 3156	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders
	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
	S 949	Cornyn	4/15/2015	Referred to the Finance Committee
	HR 1828	Thornberry	4/15/2015	Referred to the Ways & Means Committee
Legislative Activity 113th Congress	S 725	Cornyn	4/15/2013	Referred to the Finance Committee
	HR 3479	Thornberry	11/13/2013	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	S 2291	Cornyn	4/17/2012	Referred to the Finance Committee
	S 3355	Bingaman	6/28/2012	Referred to the Finance Committee
	HR 60550	Becerra	6/28/2012	Referred to the Ways & Means Committee

### Collection Issues

#### Improve Offer In Compromise Program Accessibility

National Taxpayer Advocate 2006 Annual Report to Congress 507–519.

Repeal the partial payment requirement, or if repeal is not possible, (1) provide taxpayers with the right to appeal to the IRS Appeals function the IRS's decision to return an offer without considering it on the merits; (2) reduce the partial payment to 20 percent of current income and liquid assets that could be disposed of immediately without significant cost; and (3) create an economic hardship exception to the requirement.

	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 7227	Jenkins	12/10/2018	Passed the House on 12/20/2018, received in the Senate 12/20/2018
	S 3278	Portman/ Cardin	7/26/2018	Referred to the Finance Committee
	S 2689	Cornyn	4/17/2018	Referred to the Finance Committee
	HR 2171	Lewis	4/26/2017	Referred to the Ways & Means Committee
Legislative Activity 114th Congress	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	S 3355	Bingaman	6/28/2012	Referred to the Finance Committee
	HR 6050	Becerra	6/28/2012	Referred to the Ways & Means Committee
	S 1289	Carper	6/28/2011	Referred to the Finance Committee
Legislative Activity 111th Congress	HR 4994	Lewis	4/13/2010	Referred to the Ways & Means Committee
	HR 2342	Lewis	5/12/2009	Referred to the Ways & Means Committee

#### Strengthen Taxpayer Protections in the Filing and Reporting of Federal Tax Liens

National Taxpayer Advocate 2009 Annual Report to Congress 357–364.

Provide clear and specific guidance about the factors the IRS must consider when filing a Notice of Federal Tax Lien (NFTL) and amend the Fair Credit Reporting Act to set specific timeframes for reporting derogatory tax lien information on credit reports.

	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	S 3355	Bingaman	6/28/2012	Referred to the Finance Committee
	HR 6050	Becerra	6/28/2012	Referred to the Ways & Means Committee
Legislative Activity 111th Congress	S 3215	Bingaman	4/15/2010	Referred to the Finance Committee
	HR 5047	Becerra	4/15/2010	Referred to the Ways & Means Committee
	HR 6439	Hastings	11/18/2010	Referred to the Ways & Means Committee

<b>Permit the IRS to Release Levies on Small Business Taxpayers</b>				
National Taxpayer Advocate 2011 Annual Report to Congress 537-543.		Amend IRC § 6343(a)(1)(d) to: permit the IRS, in its discretion, to release a levy against the taxpayer's property or rights to property if the IRS determines that the satisfaction of the levy is creating an economic hardship due to the financial condition of the taxpayer's business.		
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	S 3278	Portman/ Cardin	7/26/2018	Referred to Finance Committee
	S 2689	Cornyn	4/17/2018	Referred to Finance Committee
Legislative Activity 112th Congress	HR 4368	McDermott	4/17/2012	Referred to the Ways & Means Committee
<b>Return of Levy or Sale Proceeds</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 202–214.		Amend IRC § 6343(b) to extend the period of time within which a third party can request a return of levied funds or the proceeds from the sale of levied property from nine months to two years from the date of levy. This amendment would also extend the period of time available to taxpayers under IRC § 6343(d) within which to request a return of levied funds or sale proceeds.		
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 1	Brady	11/2/2017	Pub. L. No. 115-97, § 11001 (2017)
	S 1793	Grassley	9/12/2017	Referred to Finance Committee
Legislative Activity 114th Congress	S 3156	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders
	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
	S 1578	Grassley	6/16/2015	Referred to the Finance Committee
	S 949	Cornyn	4/15/2015	Referred to the Finance Committee
	HR 1828	Thornberry	4/15/2015	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	HR 4375	Johnson	4/17/2012	Referred to the Ways & Means Committee
	S 2291	Cornyn	4/17/2012	Referred to the Finance Committee
Legislative Activity 110th Congress	HR 5719	Rangel	4/16/2008	Referred to the Finance Committee
	HR 1677	Rangel	3/26/2007	Referred to the Finance Committee
Legislative Activity 109th Congress	S 1321 RS	Santorum	6/28/2005	9/15/2006 The Finance Committee. Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with written report No. 109-336 9/15/2006 Placed on the Senate Legislative Calendar under General Orders; Calendar No. 614
Legislative Activity 108th Congress	HR 1528	Portman	6/20/2003	5/19/2004 Passed/agreed to in the Senate, with an amendment
	HR 1661	Rangel	4/8/2003	Referred to the Ways & Means Committee
Legislative Activity 107th Congress	HR 3991	Houghton	3/19/2002	Defeated in House
	HR 586	Lewis	2/13/2001	4/18/02 Passed the House with an amendment; referred to the Senate

<b>Reinstatement of Retirement Accounts</b>	
National Taxpayer Advocate 2001 Annual Report to Congress 202–214; National Taxpayer Advocate 2017 Annual Report to Congress Purple Book 41–42; National Taxpayer Advocate 2015 Annual Report to Congress 340–345; National Taxpayer Advocate 2015 Annual Report to Congress 100–111.	Amend the following IRC sections to allow contributions to individual retirement accounts and other qualified plans from the funds returned to the taxpayer or to third parties under IRC § 6343: <ul style="list-style-type: none"> <li>◆ § 401 – Qualified Pension, Profit Sharing, Keogh, and Stock Bonus Plans</li> <li>◆ § 408 – Individual Retirement Account, and SEP-Individual Retirement Account</li> <li>◆ § 408A – Roth Individual Retirement Account</li> </ul>
Legislative Activity	Bill Number   Sponsor   Date   Status
Legislative Activity 115th Congress	HR 1892   Larson   4/4/2017   Pub. L. 115-123
Legislative Activity 114th Congress	S 1578   Grassley   6/16/2015   Finance Committee
Legislative Activity 110th Congress	HR 5719   Rangel   4/16/2008   Referred to the Finance Committee
	HR 1677   Rangel   3/26/2007   Referred to the Finance Committee
Legislative Activity 109th Congress	S 1321RS   Santorum   6/28/2005   9/15/2006 The Finance Committee. Reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title with written report No. 109-336 9/15/2006 Placed on the Senate Legislative Calendar under General Orders; Calendar No. 614
Legislative Activity 108th Congress	HR 1528   Portman   6/20/2003   5/19/2004 Passed/agreed to in the Senate, with an amendment
	HR 1661   Rangel   4/8/2003   Referred to the Ways & Means Committee
	S 882   Baucus   4/10/2003   5/19/2004 S 882 was incorporated in HR 1528 through an amendment and HR 1528 passed in lieu of S 882
Legislative Activity 107th Congress	HR 586   Lewis   2/13/2001   4/18/2002 Passed the House with an amendment; referred to Senate
	HR 3991   Houghton   3/19/2002   Defeated in the House
<b>Levies on Retirement Accounts</b>	
National Taxpayer Advocate 2015 Annual Report to Congress 340–345.	Require the IRS to issue regulations describing a full financial analysis of the taxpayer's projected basic living expenses at retirement prior to allowing a determination to levy on a retirement account.
Legislative Activity	Bill Number   Sponsor   Date   Status
Legislative Activity 115th Congress	HR 2171   Lewis   4/26/2017   Referred to the Ways & Means Committee
Legislative Activity 114th Congress	S 3156   Hatch   7/12/2016   Placed on Senate Legislative Calendar under General Orders
	HR 4912   Lewis   4/12/2016   Referred to the Ways & Means Committee
<b>Consolidation of Appeals of Collection Due Process (CDP) Determinations</b>	
National Taxpayer Advocate 2005 Annual Report to Congress 451–470.	Consolidate judicial review of CDP hearings in the United States Tax Court, clarify the role and scope of Tax Court oversight of Appeals' continuing jurisdiction over CDP cases, and address the Tax Court's standard of review for the underlying liability in CDP cases.
Legislative Activity 109th Congress	Pub. L. No. 109-280, § 855, 120 Stat. 1019 (2006).

<b>Partial Payment Installment Agreements</b> National Taxpayer Advocate 2001 Annual Report to Congress 210–214.	Amend IRC § 6159 to allow the IRS to enter into installment agreements that do not provide for full payment of the tax liability over the statutory limitations period for collection of tax where it appears to be in the best interests of the taxpayer and the IRS.			
Legislative Activity 108th Congress	Pub. L. No. 108-357, § 833, 118 Stat. 1418, 1600 (2004).			
<b>Waiver of Installment Agreement Fees for Low Income Taxpayers</b> National Taxpayer Advocate 2006 Annual Report to Congress 141–156.	Implement an installment agreement (IA) user fee waiver for low income taxpayers and adopt a graduated scale for other IA user fees based on the amount of work required.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 3278	Portman/ Cardin	7/26/2018	Referred to the Finance Committee
	HR 5444	Jenkins	4/10/2018	Passed in the House, received in the Senate 4/19/2018 and referred to the Finance Committee
Legislative Activity 114th Congress	S 3156	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders
	S 949	Cornyn	4/15/2015	Referred to the Finance Committee
	HR 1828	Thornberry	4/15/2015	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	HR 4375	Johnson	4/17/2012	Referred to the Ways & Means Committee
	S 2291	Cornyn	4/17/2012	Referred to the Finance Committee
<b>Strengthen the Independence of the IRS Office of Appeals</b> National Taxpayer Advocate 2009 Annual Report to Congress 346–350.	Strengthen the independence of the IRS Office of Appeals and require at least one appeals officer and settlement officer in each state. In addition the Office of Appeals should be independent from the IRS, should eliminate prohibited <i>ex parte</i> communications with the IRS.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 7227	Jenkins	12/10/2018	Passed the House on 12/20/2018, received in the Senate 12/20/2018
	S 3278	Portman/ Cardin	7/26/2018	Referred to Finance Committee
	HR 5444	Jenkins	4/10/2018	Passed in the House, received in the Senate 4/19/2018 and referred to the Finance Committee
	S 1793	Grassley	9/12/2017	Referred to Finance Committee
Legislative Activity 114th Congress	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
	S 1578	Grassley	6/16/2015	Referred to the Finance Committee
	S 949	Cornyn	4/15/2015	Referred to the Finance Committee
	HR 1828	Thornberry	4/15/2015	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	HR 4375	Johnson	4/17/2012	Referred to the Ways & Means Committee
	S 2291	Cornyn	4/17/2012	Referred to the Finance Committee

**Penalties and Interest****Erroneous Refund Penalty**

National Taxpayer Advocate 2014 Annual Report to Congress 351;  
National Taxpayer Advocate 2011 Annual Report to Congress 544.

Amend IRC § 6676 to clarify that the penalty does not apply to individual taxpayers who acted with reasonable cause and in good faith in erroneously claiming a credit or refund. Taking into account all of taxpayers' facts and circumstances in determining whether they had such reasonable cause would bring this statutory penalty into conformity with the TBOR *right to a fair and just tax system*.

Legislative Activity 114th Congress

Pub. L. No. 114-113, Division Q § 209 (2015).

**Protect Good Faith Taxpayers by Expanding the Availability of Penalty Reductions, Establishing Specific Penalty Abatement Procedures, and Providing Appeal Rights**

National Taxpayer Advocate 2015 Annual Report to Congress 376–382.

Expand the notice period allowing taxpayers to correct their returns and avoid application of the frivolous return penalty from 30 days to 60 days and establish the same mechanism for correcting returns.

Bill Number	Sponsor	Date	Status
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Legislative Activity 115th Congress

HR 2171

Lewis

4/26/2017

Referred to the Ways & Means Committee

Legislative Activity 114th Congress

HR 4912

Lewis

4/12/2016

Referred to the Ways & Means Committee

**Interest Rate and Failure to Pay Penalty**

National Taxpayer Advocate 2001 Annual Report to Congress 179–182.

Repeal the failure to pay penalty provisions of IRC § 6651 while revising IRC § 6621 to allow for a higher underpayment interest rate.

Bill Number	Sponsor	Date	Status
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Legislative Activity 108th Congress

HR 1528

Portman

6/20/2003

5/19/2004 Passed/agreed to in the Senate, with an amendment

HR 1661

Rangel

4/8/2003

Referred to the Ways & Means Committee

**Interest Abatement on Erroneous Refunds**

National Taxpayer Advocate 2001 Annual Report to Congress 183–187.

Amend IRC § 6404(e)(2) to require the Secretary to abate the assessment of all interest on any erroneous refund under IRC § 6602 until the date the demand for repayment is made, unless the taxpayer (or a related party) has in any way caused such an erroneous refund. Further, the Secretary should have discretion not to abate any or all such interest where the Secretary can establish that the taxpayer had notice of the erroneous refund before the date of demand and the taxpayer did not attempt to resolve the issue with the IRS within 30 days of such notice.

Bill Number	Sponsor	Date	Status
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Legislative Activity 109th Congress

HR 726

Sanchez

2/9/2005

Referred to the Ways & Means Committee

Legislative Activity 108th Congress

HR 1528

Portman

6/20/2003

5/19/2004 Passed/agreed to in the Senate, with an amendment

HR 1661

Rangel

4/8/2003

Referred to the Ways & Means Committee

**First Time Penalty Waiver**

National Taxpayer Advocate 2001 Annual Report to Congress 188–192.

Authorize the IRS to provide penalty relief for first-time filers and taxpayers with excellent compliance histories who make reasonable attempts to comply with the tax rules.

Bill Number	Sponsor	Date	Status
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Legislative Activity 108th Congress

HR 1528

Portman

6/20/2003

5/19/2004 Passed/agreed to in the Senate, with an amendment

HR 1661

Rangel

4/8/2003

Referred to the Ways & Means Committee

Legislative Activity 107th Congress

HR 3991

Houghton

3/19/2002

Defeated in the House

<b>Federal Tax Deposit (FTD) Avoidance Penalty</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 222.	Reduce the maximum FTD penalty rate from ten to two percent for taxpayers who make deposits on time but not in the manner prescribed in the IRC.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	S 1793	Grassley	9/12/2017	Referred to Finance Committee
Legislative Activity 109th Congress	HR 3629	Doggett	7/29/2005	Referred to the Ways & Means Committee
	HR 3841	Manzullo	9/2/2005	Referred to the Ways & Means Committee
	S 1321RS	Santorum	6/28/2005	9/15/2006 The Finance Committee, reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with written report No. 109-336 9/15/2006 Placed on the Senate Legislative Calendar under General Orders; Calendar No. 614
Legislative Activity 108th Congress	HR 1528	Portman	6/20/2003	5/19/2004 Passed/agreed to in the Senate with an amendment
	HR 1661	Rangel	4/8/2003	Referred to the Ways & Means Committee
Legislative Activity 107th Congress	HR 586	Lewis	2/13/2001	4/18/2002 Passed the House with an amendment; referred to the Senate
	HR 3991	Houghton	3/19/2002	Defeated in the House
<b>Family Issues</b>				
<b>Uniform Definition of a Qualifying Child</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 78–100.	Create a uniform definition of “qualifying child” applicable to tax provisions relating to children and family status.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 108th Congress	Pub. L. No. 108-311, § 201, 118 Stat. 1169-1175 (2004).			
<b>Means-Tested Public Assistance Benefits</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 76–127.	Amend the IRC §§ 152, 2(b) and 7703(b) to provide that means-tested public benefits are excluded from the computation of support in determining whether a taxpayer is entitled to claim the dependency exemption and from the cost of maintenance test for the purpose of head-of-household filing status or “not married” status.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 108th Congress	HR 22	Houghton	1/3/2003	Referred to the Ways & Means Committee
Legislative Activity 107th Congress	HR 5505	Houghton	10/01/2002	Referred to the Ways & Means Committee
<b>Credits for the Elderly or the Permanently Disabled</b>				
National Taxpayer Advocate 2001 Annual Report to Congress 218–219.	Amend IRC § 22 to adjust the income threshold amount for past inflation and provide for future indexing for inflation.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 107th Congress	S 2131	Bingaman	4/15/2002	Referred to the Finance Committee

**Electronic Filing Issues****Scannable Returns**

National Taxpayer Advocate 2013 Annual Report to Congress vol. 2, § 5, 70, 91, 96.

Require electronically prepared paper returns to include scannable 2-D code.

	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 7227	Jenkins	12/10/2018	Passed the House on 12/20/2018, received in the Senate 12/20/2018
	S 3246	Hatch	7/19/2018	Referred to Finance Committee
	HR 2171	Lewis	4/26/2017	Referred to the Ways & Means Committee
	S 606	Nelson	3/9/2017	Referred to Finance Committee
Legislative Activity 113th Congress	S 2736	Hatch	7/14/2014	Referred to the Finance Committee

**Return Filing and Processing**

National Taxpayer Advocate 2013 Annual Report to Congress, vol. 2 68-96.

Eliminate the March 31st deadline for e-filed information reports. All information reports, whether e-filed or filed on paper, would be due at the end of February.

Legislative Activity 114th Congress  
Pub. L. No. 114-113, Division Q § 201 (2015).

**Safe Harbor for De Minimis Errors Returns and Payee Statements**

National Taxpayer Advocate 2013 Annual Report to Congress vol. 2, § 5, 70, 91, 96.

Safe harbor for *de minimis* errors on information

	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	Pub. L. No. 114-113, Division Q § 202 (2015).			
Legislative Activity 113th Congress	S 2736	Hatch	7/14/2014	Referred to the Finance Committee

**Direct Filing Portal**

National Taxpayer Advocate 2004 Annual Report to Congress 471-477.

Amend IRC § 6011(f) to require the IRS to post fill-in forms on its website and make electronic filing free to all individual taxpayers.

	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 5445	Bishop	4/10/2018	Passed in the House
Legislative Activity 112th Congress	S 1289	Carper	6/28/2011	Referred to the Finance Committee
Legislative Activity 110th Congress	S 1074	Akaka	3/29/2007	Referred to the Finance Committee
	HR 5801	Lampson	4/15/2008	Referred to the Ways & Means Committee
Legislative Activity 109th Congress	S 1321RS	Santorum	6/28/2005	9/15/2006 Referred to the Finance Committee; reported by Senator Grassley with an amendment in the nature of a substitute and an amendment to the title; with written report No. 109-336 9/15/2006 Placed on the Senate Legislative Calendar under General Orders; Calendar No. 614

**Free Electronic Filing For All Taxpayers**

National Taxpayer Advocate 2013 Annual Report to Congress vol. 2, § 5, 70, 91, 96

Revise IRC § 6011(f) to provide that the Secretary shall make electronic return preparation and electronic filing available without charge to all individual taxpayers.

	Bill Number	Sponsor	Date	Status
Legislative Activity 110th Congress	S 2736	Hatch	7/14/2014	Referred to the Finance Committee

Office of the Taxpayer Advocate				
<b>Repeal or Fix Statute Suspension Under IRC § 7811(d)</b>				
National Taxpayer Advocate 2015 Annual Report to Congress 316–328.	Repeal suspension of statute of limitations during pending application for Taxpayer Assistance Order or clarify.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 2171	Lewis	4/26/2017	Referred to the Ways & Means Committee
Legislative Activity 114th Congress	HR 4912	Lewis	4/12/2016	Referred to the Ways & Means Committee
<b>Confidentiality of Taxpayer Communications</b>				
National Taxpayer Advocate 2002 Annual Report to Congress 198–215.	Strengthen the independence of the National Taxpayer Advocate and the Office of the Taxpayer Advocate by amending IRC §§ 7803(c)(3) and 7811. Amend IRC § 7803(c)(4)(A)(iv) to clarify that, notwithstanding any other provision of the IRC, Local Taxpayer Advocates have the discretion to withhold from the IRS the fact that a taxpayer contacted the Taxpayer Advocate Service or any information provided by a taxpayer to TAS.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 108th Congress	HR 1528	Portman	6/20/2003	5/19/2004 Passed/agreed to in the Senate, with an amendment
	HR 1661	Rangel	4/8/2003	Referred to the Ways & Means Committee
<b>Access to Independent Legal Counsel</b>				
National Taxpayer Advocate 2002 Annual Report to Congress 198–215.	Amend IRC § 7803(c)(3) to provide for the position of Counsel to the National Taxpayer Advocate, who shall advise the National Taxpayer Advocate on matters pertaining to taxpayer rights, tax administration, and the Office of Taxpayer Advocate, including commenting on rules, regulations, and significant procedures, and the preparation of <i>amicus</i> briefs.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 108th Congress	HR 1528	Portman	6/20/2003	Referred to the Senate
	HR 1661	Rangel	4/8/2003	Referred to the Ways & Means Committee
<b>Taxpayer Advocate Directive</b>				
National Taxpayer Advocate 2012 Annual Report to Congress 573–602; National Taxpayer Advocate 2002 Annual Report to Congress 419–422.	Amended IRC § 7811 to provide the National Taxpayer Advocate with the non-delegable authority to issue a Taxpayer Advocate Directive to the Internal Revenue Service with respect to any program, proposed program, action, or failure to act that may create a significant hardship for a taxpayer segment or taxpayers at large.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 114th Congress	S 2333	Cardin	11/30/2015	Referred to the Finance Committee
	HR 4128	Becerra	11/30/2015	Referred to the Ways & Means Committee
	S 949	Cornyn	4/15/2015	Referred to the Finance Committee
	HR 1828	Thornberry	4/15/2015	Referred to the Ways & Means Committee
Legislative Activity 112th Congress	S 3355	Bingaman	6/28/2012	Referred to the Finance Committee
	HR 6050	Becerra	6/28/2012	Referred to the Ways & Means Committee
Legislative Activity 111th Congress	S 3215	Bingaman	4/15/2010	Referred to the Finance Committee
	HR 5047	Becerra	4/15/2010	Referred to the Ways & Means Committee

<b>Codify the Authority to Issue a Taxpayer Advocate Directive</b>				
National Taxpayer Advocate 2016 Annual Report 39-40	Grant to the National Taxpayer Advocate non-delegable authority to issue a TAD with respect to any IRS program, proposed program, action, or failure to act that may create a significant hardship for a segment of the taxpayer population or for taxpayers at large, and require that, to object to a directive, the IRS would have to respond timely in writing.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 5342	LaHood	3/20/2018	Referred to the Ways & Means Committee
	HR 5444	Jenkins	4/10/2018	Passed in the House, received in the Senate 4/19/2018 and referred to the Finance Committee.
<b>Exempt Organizations (EO)</b>				
<b>EO Judicial and Administrative Review</b>				
National Taxpayer Advocate 2014 Annual Report to Congress 573–602, 371–379.	Amend IRC § 7428 to allow taxpayers seeking exemption as IRC § 501(c)(4), (c)(5), or (c)(6) organizations to seek a declaratory judgment on the same footing as those seeking exempt status as IRC § 501(c)(3) organizations.			
Legislative Activity 114th Congress	Pub. L. No. 114-113, Division Q § 406 (2015).			
<b>Notification to Exempt Organizations</b>				
National Taxpayer Advocate 2011 Annual Report to Congress 444.	Require the IRS to notify exempt organizations that have not filed an annual notice or return for two consecutive years that the IRS has no record of receiving a return or notice and that the organization's exemption will be revoked if it does not file by the next filing deadline.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 7227	Jenkins	12/10/2018	Passed the House on 12/20/2018, received in the Senate 12/20/2018
	S 3246	Hatch	7/19/2018	Referred to the Finance Committee
Legislative Activity 114th Congress	S 3156	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders
<b>Training</b>				
<b>Comprehensive Training Strategy</b>				
National Taxpayer Advocate 2017 Annual Report to Congress 84-92.	Increase “train the trainer” in-person trainings to allow for more effective delivery of training to field offices; increase training hours per employee, particularly in mission critical job series; encourage employees to identify outside training relevant to their jobs and allow the employees to attend such trainings; and include outside experts in training to leverage knowledge gained from working with taxpayers who are impacted by IRS actions.			
	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	S 3278	Portman/ Cardin	7/26/2018	Referred to the Finance Committee
	HR 7227	Jenkins	12/10/2018	Passed the House on 12/20/2018, received in the Senate 12/10/2018

## Other Issues

**Modify Internal Revenue Code Section 6707A to Ameliorate Unconscionable Impact**

National Taxpayer Advocate 2008 Annual Report to Congress 419–422.

Modify IRC § 6707A to ameliorate unconscionable impact. Section 6707A of the IRC imposes a penalty of \$100,000 per individual per year and \$200,000 per entity per year for failure to make special disclosures of a “listed transaction.”

Bill Number	Sponsor	Date	Status
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Legislative Activity 111th Congress

Pub. L. No. 111-124, § 2041 Stat. 2560 (2010).

S 2771	Baucus	11/16/2009	Referred to the Finance Committee
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HR 4068	Lewis	11/16/2009	Referred to the Ways & Means Committee
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S 2917	Baucus	12/18/2009	Referred to the Finance Committee
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**Eliminate Tax Strategy Patents**

National Taxpayer Advocate 2007 Annual Report to Congress 512–524.

Bar tax strategy patents, which increase compliance costs and undermine respect for congressionally-created incentives, or require the PTO to send any tax strategy patent applications to the IRS so that abuse can be mitigated.

Legislative Activity 112th Congress

Pub. L. No. 112-29 § 14(a), 125 Stat. 284, 327 (2011).

**Restrict Tax Return Disclosures to Necessary Content**

National Taxpayer Advocate 2007 Annual Report to Congress 554–555.

Limit the disclosure of tax returns and tax return information requested through taxpayer consent solely to the extent necessary to achieve the purpose for which consent was requested.

Bill Number	Sponsor	Date	Status
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Legislative Activity 115th Congress

S 3278	Portman/ Cardin	7/26/2018	Referred to the Finance Committee
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S 3246	Hatch	7/19/2018	Referred to the Finance Committee
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HR 5444	Jenkins	4/10/2018	Passed in the House, received in the Senate 4/19/2018 and referred to the Finance Committee
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HR 5445	Bishop	4/10/2018	Passed in the House
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HR 3340	Doggett	7/20/2017	Referred to the Ways & Means Committee
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**Disclosure Regarding Suicide Threats**

National Taxpayer Advocate 2001 Annual Report to Congress 227.

Amend IRC § 6103(i)(3)(B) to allow the IRS to contact and provide necessary return information to specified local law enforcement agencies and local suicide prevention authorities, in addition to federal and state law enforcement agencies in situations involving danger of death or physical injury.

Bill Number	Sponsor	Date	Status
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Legislative Activity 112th Congress

HR 1528	Portman	6/20/2003	5/19/2004 Passed/agreed to in the Senate, with an amendment
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S 882	Baucus	4/10/2003	5/19/2004 S 882 was incorporated in HR 1528 through an amendment and HR 1528 passed in lieu of S 882
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HR 1661	Rangel	4/8/2003	Referred to the Ways & Means Committee
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Legislative Activity 107th Congress

HR 586	Lewis	2/13/2001	4/18/2002 Passed the House with an amendment; referred to the Senate
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**Attorney Fees**

National Taxpayer Advocate 2002 Annual Report to Congress 161–171.

Allow successful plaintiffs in nonphysical personal injury cases who must include legal fees in gross income to deduct the fees “above the line.” Thus, the net tax effect would not vary depending on the state in which a plaintiff resides.

Legislative Activity 108th Congress

Pub. L. No. 108-357, § 703, 118 Stat. 1418, 1546-48 (2004).

<b>Attainment of Age Definition</b>	National Taxpayer Advocate 2003 Annual Report to Congress 308–311.				Amend IRC § 7701 by adding a new subsection as follows: “Attainment of Age. An individual attains the next age on the anniversary of his date of birth.”
	Bill Number	Sponsor	Date	Status	
Legislative Activity 108th Congress	HR 4841	Burns	7/15/2004	7/21/2004 Passed the House; 7/22/2004 Received in the Senate	
<b>Home-Based Service Workers (HBSW)</b>	National Taxpayer Advocate 2001 Annual Report to Congress 193–201.				Amend IRC § 3121(d) to clarify that HBSWs are employees rather than independent contractors.
	Bill Number	Sponsor	Date	Status	
Legislative Activity 110th Congress	HR 5719	Rangel	4/16/2008	Referred to the Finance Committee	
Legislative Activity 107th Congress	S 2129	Bingaman	4/15/2002	Referred to the Finance Committee	
<b>Restrict Access to the Death Master File (DMF)</b>	National Taxpayer Advocate 2011 Annual Report to Congress 519–523.				Restrict access to certain personally identifiable information in the DMF. The National Taxpayer Advocate is not recommending a specific approach at this time, but outlines several available options.
	Bill Number	Sponsor	Date	Status	
Legislative Activity 113th Congress	H.J. Res. 59, 113th Cong. § 203 (2013).				
Legislative Activity 112th Congress	S 3432	Nelson	7/25/2012	Referred to the Finance Committee	
	HR 6205	Nugent	7/26/2012	Referred to the Ways & Means Committee	
<b>Amend the Adoption Credit to Acknowledge Jurisdiction of Native American Tribes</b>	National Taxpayer Advocate 2012 Annual Report to Congress 521.				Amend IRC § 7871(a) to include the adoption credit (IRC § 23) in the list of Code sections for which a Native American tribal government is treated as a “State”.
	Bill Number	Sponsor	Date	Status	
Legislative Activity 114th Congress	S 835	Heitkamp	3/23/2015	Referred to the Finance Committee	
	HR 1542	Kilmer	3/23/2015	Referred to the Ways & Means Committee	
Legislative Activity 113th Congress	S 835	Johnson	7/09/2014	Referred to the Finance Committee	
	HR 1738	Kilmer	6/12/2013	Referred to the Ways & Means Committee	
<b>Filing Due Dates of Partnerships and Certain Trusts</b>	National Taxpayer Advocate 2003 Annual Report to Congress 302.				Amend Internal Revenue Code section 6072(a) to change the regular filing deadline for partnerships described in Section 6031 and trusts described in Section 6012(a)(4) as follows: <ul style="list-style-type: none"> <li>◆ For partnerships and trusts making returns on the basis of a calendar year: Change the regular filing deadline from the 15th day of April following the close of the calendar year to the 15th day of March following the close of the calendar year.</li> <li>◆ For partnerships and trusts making returns on the basis of a fiscal year: Change the regular filing deadline from the 15th day of the fourth month following the close of the fiscal year to the 15th day of the third month following the close of the fiscal year.</li> </ul>
Legislative Activity 114th Congress	Pub. L. No. 114-41 § 2006, 129 Stat. 443, 457 (2015).				
<b>Foreign Account Reporting</b>	National Taxpayer Advocate 2014 Annual Report to Congress 331.				Align the FBAR filing deadline and threshold(s) with the Form 8938 filing deadline and threshold(s). Change the FBAR filing due date to coincide with the due date applicable to a taxpayer’s federal income tax return and Form 8938 (including extensions).
Legislative Activity 114th Congress (July 31, 2015)	Pub. L. No. 114-41 § 2006, 129 Stat. 443, 458-459 (2015).				

## Individual Taxpayer Identification Numbers (ITINs)

**Requirements for the Issuance of ITINs**

National Taxpayer Advocate 2008 Annual Report to Congress 126;  
National Taxpayer Advocate 2010 Annual Report to Congress 319.

Administrative recommendation that the IRS should promote the Certified Acceptance Agent program and use other federal agencies to perform acceptance agent duties as contemplated in the Treasury Regulation (e.g., the Postal Service performs a similar service in processing passport applications).

	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 5361	Paulsen	3/21/2018	Referred to the Ways & Means Committee

Legislative Activity 114th Congress (July 31, 2015)

Pub. L. No. 114-113, Division Q § 203 (2015).

**Develop a Process To Verify That Previously Issued ITINs Have Been Used for Tax Administration Purposes**

National Taxpayer Advocate 2008 Annual Report to Congress 126;  
National Taxpayer Advocate 2010 Annual Report to Congress 319.

Administrative recommendation the IRS should develop a process to verify that previously issued ITINs have been used for tax administration purposes and revoke unused ITINs on a regular basis after notifying ITIN holders.

Legislative Activity 114th Congress

Pub. L. No. 114-113, Division Q § 203 (2015).

**Whistleblower**

National Taxpayer Advocate 2015 Annual Report to Congress 409–412.

Amend IRC § 7623 to include anti-retaliation protection for tax whistleblowers and impose a penalty on whistleblowers for unauthorized disclosure of tax information.

	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 7227	Jenkins	12/10/2018	Passed the House on 12/20/2018, received in the Senate 12/20/2018
	S 3246	Hatch	7/19/2018	Referred to Finance Committee
	S 762	Grassley	3/29/2017	Referred to Finance Committee
Legislative Activity 114th Congress	S 3156	Hatch	7/12/2016	Placed on Senate Legislative Calendar under General Orders

## Military Issues

**Funding for Stakeholder Partnerships, Education & Communication (SPEC)**

National Taxpayer Advocate 2017 Annual Report 151–164

Create a special unit of SPEC staffed with veterans whose responsibilities are to develop and conduct outreach, education, and assistance to current military taxpayers, including National Guard and Reservists, and to those organizations that provide tax assistance to these taxpayers.

- ◆ Allocate ample funding for SPEC to provide face-to-face training for military VITA volunteers in overseas locations,
- ◆ Assign a dedicated IRS employee to routinely update the military information on irs.gov website,
- ◆ Provide a year-round dedicated toll-free telephone line for service members and their families to answer tax law and filing questions, and to resolve their tax account and compliance issues.

	Bill Number	Sponsor	Date	Status
Legislative Activity 115th Congress	HR 5479	Walz	4/11/2018	Referred to the Ways & Means Committee

## LR #1 **IT MODERNIZATION: Provide the IRS with Additional Dedicated, Multi-Year Funding to Replace Its Antiquated Core IT Systems Pursuant to a Plan that Sets Forth Specific Goals and Metrics and Is Evaluated Annually by an Independent Third Party**

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the Position of the Internal Revenue Service and Be Heard*
- *The Right to Appeal a Decision of the Internal Revenue Service in an Independent Forum*
- *The Right to Finality*
- *The Right to Privacy*
- *The Right to Confidentiality*
- *The Right to Retain Representation*
- *The Right to a Fair and Just Tax System*

### PROBLEM

The IRS is the Accounts Receivable Department of the Federal government. In fiscal year (FY) 2018, the IRS collected nearly \$3.5 trillion on a budget of \$11.43 billion.<sup>2</sup> Put differently, for every dollar the IRS received in appropriated funds, it collected about \$300 in federal revenue. Both because the fiscal health of the Federal government depends on the IRS's collection capability and because the taxpayers who pay our nation's bills deserve fair treatment, it is critical that the IRS has the resources to do its job effectively and efficiently.

The IRS does not have adequate information technology (IT) systems to do its job effectively and efficiently. The IRS's core IT systems are among the oldest in the Federal government, limiting the agency's capabilities in significant ways. Partly due to historic poor planning and execution and partly due to lack of funding, the IRS has been unable to replace its antiquated systems. Every year, instead, it layers more and more smaller systems and applications onto its core systems. By analogy, the IRS has erected a 50-story office building on top of a creaky, 60-year-old foundation, and it is adding a few more floors every year. There are inherent limitations on the functionality of a 60-year-old infrastructure, and at some point, the entire edifice is likely to collapse.

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code. See IRC § 7803(a)(3).

2 See Government Accountability Office (GAO), GAO 19-150, Financial Audit: IRS's Fiscal Year (FY) 2018 and 2017 Financial Audits 23 (Nov. 2018) (showing revenue collections); H.R. Rep. No. 115-792, at 14 (2018) (showing appropriation levels).

According to the Government Accountability Office (GAO), the IRS's Individual Master File (IMF) and Business Master File (BMF) systems date to about 1960 and are the two oldest IT systems in the federal government among the major IT systems it surveyed.<sup>3</sup>

The GAO describes the IMF as follows:

[The IMF] is the authoritative data source of individual taxpayer accounts. Within IMF, accounts are updated, taxes are assessed, and refunds are generated as required during each tax filing period. Virtually all IRS information system applications and processes depend on output, directly or indirectly, from this data source.

IMF was written in an outdated assembly language code and operates on a 2010 IBM z196/2817-m32 mainframe. This has resulted in difficulty delivering technical capabilities addressing identity theft and refund fraud, among other things. In addition, there is a risk of inaccuracies and system failures due to complexity of managing dozens of systems synchronizing individual taxpayer data across multiple data files and databases, limitations in meeting normal financial requirements and security controls, and keeping pace with modern financial institutions.<sup>4</sup>

It bears emphasis that “[v]irtually all IRS information system applications and processes depend on output, directly or indirectly, from [the IMF].” IRS IT leaders regularly point out that there is an important distinction between modernizing IT capabilities and modernizing IT core systems. To extend the above analogy, hundreds of IRS systems and applications are resting on the foundation of a 60-year-old office building. Because the building has not yet collapsed, there is an implicit assumption that more floors can be added indefinitely. They cannot.

On April 17, 2018, the filing deadline for 2017 federal income tax returns, an IRS systems crash prevented taxpayers from electronically submitting their tax returns and payments. The crash was attributed to a malfunction in an 18-month-old piece of hardware supporting the IMF—a system that requires more and more support every year.<sup>5</sup> The GAO's director of IT management warned in congressional testimony shortly before the 2018 filing season began that “relying on these antiquated systems for our nation's primary source of revenue is highly risky, meaning the chance of having a failure during the filing season is continually increasing.”<sup>6</sup> The damage from the crash was limited because the IRS gave taxpayers an extra day to file and pay. However, the crash had the effect of creating significant confusion and anxiety among taxpayers and their preparers, and it served as an important wake-up call and a warning of future problems if the IRS is unable to replace its legacy systems soon.

Since 2009, the IRS has been taking steps to replace the IMF with a system known as the Customer Account Data Engine 2 (CADE 2). Its goal is to transition the IMF's functionality and data to CADE 2 and to retire the IMF. To date, however, the IRS has not been able to complete this transition.

3 GAO, GAO-16-468, *Information Technology: Federal Agencies Need to Address Aging Legacy Systems* 28-30 (May 2016).

4 *Id.* at 53.

5 See Aaron Boyd & Frank Konkel, *IRS' 60-Year-Old IT System Failed on Tax Day Due to New Hardware*, Nextgov (Apr. 19, 2018) (citing an IRS official), <https://www.nextgov.com/it-modernization/2018/04/irs-60-year-old-it-system-failed-tax-day-due-new-hardware/147598>.

6 See Frank Konkel, *The IRS System Processing Your Taxes is Almost 60 Years Old*, Nextgov (Mar. 19, 2018) (quoting David Powner, GAO's director of Information Technology Management Issues), <https://www.nextgov.com/it-modernization/2018/03/irs-system-processing-your-taxes-almost-60-years-old/146770>.

Moreover, it has not been able to make comparable progress in retiring the BMF system (which is the authoritative source of individual *business* taxpayer accounts) or several other key legacy systems.

Apart from the risk of catastrophic collapse, the absence of modern IT systems prevents the IRS from doing its job as effectively as it could on a daily basis. The result is that taxpayers are harmed, practitioners are inconvenienced, and the IRS is hampered in delivering on its mission to provide U.S. taxpayers top quality service and apply the tax law with integrity and fairness to all.

## EXAMPLES

**Customer Callback.** Over the past decade, the IRS has received an average of more than 100 million telephone calls each year.<sup>7</sup> We report regularly on IRS telephone performance, including the percentage of calls the IRS answers and the average time taxpayers spend waiting on hold. Performance has varied widely, with the IRS reporting an annual “Level of Service” on its Accounts Management lines from as low as 38 percent in FY 2015 to as high as 77 percent in FY 2017. The average length of time taxpayers spend waiting on hold has also varied considerably, from as few as seven minutes in FY 2018 to as many as 30 minutes in FY 2015.<sup>8</sup>

Most telephone call centers maintained by large businesses and federal agencies, including the Social Security Administration and the Department of Veterans Affairs, offer a “customer callback” feature. That is, in lieu of waiting on hold for long periods of time, callers may elect to receive a call back when the next customer service representative is available. Despite the large volume of calls it receives, the IRS still does not have this technology.<sup>9</sup>

In the President’s FY 2015 and FY 2016 budgets, the IRS proposed adding customer callback and estimated it would cost about \$3.3 million to acquire the technology.<sup>10</sup> In November 2015, however, Commissioner Koskinen said that although the customer callback technology itself would cost only about \$3.5 million, *the IRS had determined its phone system would need to be upgraded to be able to run the customer callback technology—and the upgrade would cost about \$45 million.*<sup>11</sup> We understand the IRS has finally decided to absorb the cost of implementing a customer callback feature. This is a very positive development for taxpayers and practitioners. However, the time, effort, and cost it has required to implement this feature illustrates the challenges the IRS consistently faces as it tries to modernize its capabilities based on antiquated technology platforms.

**Case Management Systems.** The IRS currently maintains approximately 60 major case management systems. The systems are distinct, often requiring an IRS employee seeking information about a taxpayer to conduct searches on multiple systems. This results in poor customer service, because when a taxpayer or practitioner calls the IRS with an account question, the customer service representative who answers the phone often does not have access to the system on which the relevant taxpayer information

7 IRS, Joint Operations Center, *Snapshot Reports: Enterprise Snapshot* (final week of each fiscal year for FY 2009 through FY 2018).

8 *Id.* For additional discussion regarding IRS telephone service, see National Taxpayer Advocate 2017 Annual Report to Congress 22-35 (Most Serious Problem: Telephones: *The IRS Needs to Modernize the Way It Serves Taxpayers Over the Telephone, Which Should Become an Essential Part of an Omnichannel Customer Experience*).

9 *Id.* at 31-32.

10 See IRS, Congressional Justification for Appropriations accompanying the President’s FY 2015 Budget at IRS-20 (2014); IRS, Congressional Justification for Appropriations accompanying the President’s FY 2016 Budget at IRS-22 (2015).

11 See Lisa Rein, *IRS Customer Service Will Get Even Worse This Tax Filing Season, Tax Chief Warns*, Washington Post.com, Nov. 3, 2015.

is stored. This imposes limits on IRS compliance activities for similar reasons. The IRS has been making plans to develop an integrated enterprise-wide case management system, so that IRS employees can see information from all 60 systems in a single search (with varying levels of “permissions” so that, for example, only employees with a need to know would be able to view certain information). However, the IRS has not yet had sufficient personnel or financial resources to develop and implement an integrated system. As a result, the inefficiencies of maintaining 60 separate systems continue to plague the agency.<sup>12</sup>

**Online Taxpayer Accounts.** In the IRS’s Future State plan and, more recently, in its FY 2018-2022 Strategic Plan, the IRS is placing significant emphasis on the development and use of online taxpayer accounts.<sup>13</sup> Robust online accounts would, indeed, be very helpful to many taxpayers, who could view all of their account information online and, in many cases, submit account inquiries through their online accounts, much as they can do with online bank accounts. However, the technology limitations described above—most significantly, the absence of an integrated case management system—limit the IRS in making complete account information available to taxpayers. As a result, taxpayers accustomed to using online accounts with financial institutions and other vendors experience frustration, and more IRS employees are needed to answer phone calls and respond to correspondence about matters that many taxpayers would handle quickly and efficiently online if the functionality were available.

**Online Practitioner Accounts.** Taxpayer representatives, even more than taxpayers, would benefit enormously from online account access. While a typical taxpayer can go many years without having to contact the IRS with account questions, practitioners often have to contact IRS personnel multiple times a day. Hold times on the Practitioner Priority Service telephone line can be long,<sup>14</sup> and hold times when practitioners must call the IRS’s compliance telephone lines can be even longer. Practitioners often charge their taxpayer-clients for the time they spend waiting on hold, increasing tax compliance costs, and for some inquiries—such as balance inquiries, requests for transcripts, or obtaining copies of correspondence—telephone calls are not nearly as effective as a robust online account.

**Provision of Information About TAS to Taxpayers.** Old technology prevents the IRS from doing things big and small. One specific example involves compliance with a requirement imposed by the IRS Restructuring and Reform Act of 1998 that the IRS include information about a taxpayer’s local TAS office in statutory notices of deficiency.<sup>15</sup> TAS offices are aligned with taxpayer populations by ZIP code. It would seem like a relatively easy task for the IRS to program its systems to generate the address and telephone number of the local TAS office on statutory notices of deficiency based on the ZIP code of the taxpayer. The IRS currently uses approximately 20 versions of a statutory notice of deficiency, which vary based on which IRS function issues the notice and certain other factors, and the IRS is, indeed, able to include information about the local TAS office on most versions. However, it lacks the IT capability to include information about the local TAS office on other versions. As a result, IRS personnel must either manually place “stuffer” notices listing all TAS offices in the envelopes with certain statutory notices of deficiency or provide a single website address, thereby failing to identify

12 For additional discussion on IT challenges relating to the IRS’s case management systems, see National Taxpayer Advocate FY 2019 Objectives Report to Congress 47-51 (Area of Focus: *The IRS’s Enterprise Case Management Project Shows Promise, But to Achieve 21st Century Tax Administration, the IRS Needs an Overarching Information Technology Strategy with Proper Multi-Year Funding*).

13 See IRS Pub. 3744, Internal Revenue Service Strategic Plan FY 2018-2022, at 10-12 (rev. 4/2018).

14 Practitioner Priority Service (PPS) is a nationwide toll-free, account-related service for all types of tax practitioners. PPS serves tax practitioners as the first point of contact for assistance regarding account-related issues. For more information about PPS, see IRM 21.3.10, *Taxpayer Contacts Practitioner Priority Service (PPS)* (Sept. 17, 2018).

15 Pub. L. No. 105-206, § 1102(b), 112 Stat. 685, 703 (1998) (codified at IRC § 6212(a)).

which specific TAS office is aligned with the taxpayer's location and requiring IRS employees to perform work that should be fully automated.<sup>16</sup>

**Identification of SSDI Recipients.** In 2016, the Commissioner decided not to assign collection cases involving taxpayers who receive Social Security Disability Insurance (SSDI) to private collection agencies (PCAs) because SSDI recipients are, almost by definition, taxpayers who are in economic hardship and would be placed into “currently not collectible – hardship” status if the IRS were to perform a financial analysis. The IRS still has not implemented this decision. Although the IRS receives and processes Forms SSA-1099 with respect to SSDI recipients, the IRS system used to assign cases to PCAs cannot currently be programmed to pull information from the IRS system that houses Form 1099 information. Therefore, the IRS reports there is no practical way for it to exclude these cases.

## RECOMMENDATION

Provide the IRS with additional dedicated, multi-year funding to replace its core legacy IT systems pursuant to a plan that sets forth specific goals and metrics and is evaluated annually by an independent third party.<sup>17</sup>

## PRESENT LAW

The IRS receives its funding through annual appropriations acts.<sup>18</sup> The IRS budget is divided into four accounts: Taxpayer Services, Enforcement, Operations Support, and Business Systems Modernization (BSM). The BSM account is the principal source of funding for replacing the IRS's core IT systems.

Funding for the BSM account has fluctuated considerably in recent years with Congress reducing BSM funding by 62 percent from FY 2017 (\$290 million) to FY 2018 (\$110 million). Even at the higher level, BSM funding constitutes just a small fraction of the IRS's overall budget, as shown in Figure 2.1.1:

16 For additional discussion of this issue, see *Statutory Notices of Deficiency: The IRS Fails to Clearly Convey Critical Information in Statutory Notices of Deficiency, Making It Difficult for Taxpayers to Understand and Exercise Their Rights, Thereby Diminishing Customer Service Quality, Eroding Voluntary Compliance, and Impeding Case Resolution*, *supra*.

17 The GAO has also recommended that the IRS modernize and replace legacy systems. See GAO-18-153T, *Information Technology: Management Attention Is Needed to Successfully Modernize Tax Processing Systems* 10 (Oct. 2017).

18 The IRS receives a relatively small amount of additional funds from charging user fees for certain services.

**FIGURE 2.1.1, IRS Appropriations – FYs 2017–2019<sup>19</sup>**

Fiscal Year	BSM Funding	Total IRS Funding	BSM as % of Total IRS Funding
2017	\$290 M	\$11.24 B	2.6%
2018	\$110 M	\$11.43 B	1.0%
2019 (House Bill)	\$200 M	\$11.62 B	1.7%
2019 (Senate Bill)	\$110 M	\$11.26 B	1.0%

Most IRS funding is required to be spent within the fiscal year for which it is appropriated, but the IRS is generally given up to three years to spend its BSM funding.

## REASONS FOR CHANGE

IRS IT leaders regularly point out that there is an important distinction between modernizing IT capabilities and modernizing IT core systems. New applications generally can be added to existing systems, and in the short term, those applications are generally sufficient to accomplish their intended goal. But as the IRS’s former chief technology officer has emphasized in congressional testimony, the programming language and data structures of the IMF, BMF and other legacy systems “were built decades ago when computer infrastructure, such as computer memory and storage media, were tape-based, and computational machinery was extremely expensive.”<sup>20</sup>

As a result, the former IRS chief technology officer said:

[W]e have upgraded the underlying hardware and operating systems of these legacy systems, while the application programming language and data structures have essentially remained static .... The situation is analogous to operating a 1960’s automobile with the original chassis, suspension and drive train, but with a more modern engine, satellite radio, and a GPS navigation system. It runs better than the original model but not nearly as efficiently as a system bought today.”<sup>21</sup>

As discussed above, the pervasive technology limitations the IRS faces stem from the age of its core systems. It is always cheaper and easier in the short run to apply a patch than to replace a core system, but patch upon patch is simply not sustainable for several reasons.

First, there are inherent limitations in using nearly 60-year-old information technology. The examples above identify some of them. Although the IRS is constantly developing new systems and applications to meet new needs, the static data structures and programming language impede their effectiveness. The former IRS chief technology officer put it this way: “The main challenge posed by our legacy

19 For FY 2017 IRS funding levels, see Consolidated Appropriations Act, 2017, Pub. L. No. 115-31, Division E, 131 Stat. 135, 331-334 (2017). For FY 2018 IRS funding levels, see Consolidated Appropriations Act, 2018, Pub. L. No. 115-141, Division E, 132 Stat. 348, 540-543 (2018). At this writing, the FY 2019 appropriations act that funds the Treasury Department has not been finalized. For House-proposed funding levels, see H.R. REP. No. 115-792, at 14 (2018) (accompanying H.R. 6258, which was subsequently incorporated into and passed by the House as H.R. 6147, Division B, at 168-176, 115th Cong. (2018)). For Senate-proposed funding levels, see S. REP. No. 115-281, at 25 (2018) (accompanying S. 3107, at 12-19, 115th Cong. (2018)).

20 IRS Legacy Information Technology Systems: Hearing Before the House Comm. on Oversight and Government Reform, 114th Cong. (2016) (statement of Terence Milholland, Chief Technology Officer, Internal Revenue Service).

21 *Id.*

systems is that their data structures do not allow us to easily use the data in our downstream service and compliance systems to best serve taxpayers.”<sup>22</sup>

Second, the older a system becomes, the more difficult it is to maintain. Fewer and fewer computer programmers are conversant with assembly language code and other old programming languages. Because significant programming of legacy systems is still required to prepare for each filing season and for other purposes, the shrinking pool of qualified programmers poses a significant and growing concern.

Third, the older a system becomes, the more expensive it is to maintain. Warranties on IRS legacy systems have long since expired, and some parts are no longer manufactured. Over time, the costs of maintaining legacy systems will continue to increase. For that reason, replacing these systems sooner rather than later is likely to reduce maintenance costs substantially.

Fourth, systems upgrades become more challenging when they are implemented over extended periods of time. Technology that is current at the time a new system is conceived may be obsolete five years later. Therefore, managers of long-term projects are more likely to confront difficult decisions about whether to hew to original plans or to modify them to incorporate newer technology. Newer technology often is more robust and effective, but changing plans mid-stream can create complications and increase costs. If the IRS were given the resources to modernize its systems at a pace comparable to the private sector, some of these challenges could be avoided.

## EXPLANATION OF RECOMMENDATION

We believe the IRS requires significant additional funding to replace its core legacy systems with new IT systems. Given the central role technology and automation play in virtually every aspect of IRS operations, the IRS budget should reflect their importance. It is hard to imagine a large corporation as dependent on technology as the IRS would spend only one percent or two percent of its budget on IT systems upgrades.

Rather than making overall progress in modernizing its legacy systems, some indicators suggest the IRS is still losing ground. According to the Treasury Inspector General for Tax Administration, the percentage of the IRS’s IT hardware classified as “aged” increased from 40 percent at the beginning of FY 2013 to 64 percent at the beginning of FY 2017.<sup>23</sup> The IRS requires sufficient resources to reverse that trend.

We also believe the IRS requires a more predictable flow of funds. Fluctuations in BSM funding from \$290 million in FY 2017, to \$110 million in FY 2018, to somewhere between \$110 and \$200 million in FY 2019 preclude the agency from defining the scope of its upgrades and delivering its projects on time and on budget. If the agency developed an IT plan in FY 2017 on the assumption that it would continue to receive \$290 million a year, it necessarily would fail to meet its goals when the FY 2018 BSM funding level was cut by 62 percent.

22 IRS Legacy Information Technology Systems: Hearing Before the House Comm. on Oversight and Government Reform, 114th Cong. (2016) (statement of Terence Milholland, Chief Technology Officer, Internal Revenue Service).

23 Treasury Inspector General for Tax Administration, Ref. No. 2017-20-051, *Sixty-Four Percent of the Internal Revenue Service’s Information Technology Hardware Infrastructure Is Beyond Its Useful Life* (Sept. 2017).

*We are not advocating that Congress provide the IRS with a blank check.* Significant IT projects are challenging, and historically, the IRS has often failed to produce projected results timely and at budgeted levels. While a portion of its IT failures are likely attributable to insufficient funding or uneven funding streams, another portion is attributable to poor planning and execution. Therefore, we believe that before Congress provides additional funding, it should (i) require the IRS to present a comprehensive IT modernization plan with time frames and cost projections; (ii) directly or through the IRS request an independent assessment of the plan's effectiveness and feasibility from a third-party entity with technology expertise; and (iii) require annual reports on the IRS's progress in meeting its targets from an independent third party with technology expertise.

On balance, we believe the IRS has done a better job of developing and executing its IT modernization plans in recent years. We note that the GAO had included the BSM program on its "High Risk List" for 18 years beginning in 1995, but removed it in 2013 based on agency progress.<sup>24</sup> Similarly, a recent Senate Appropriations subcommittee report said that "the IRS has, in recent years, satisfied the majority of developmental milestones planned for competition early, under budget, or within ten percent of cost and schedule estimates."<sup>25</sup> These are positive signs. With additional funding and proper oversight, we are optimistic the IRS can continue to modernize its IT systems, produce better taxpayer service and compliance results, and ultimately reduce its IT systems maintenance costs as well.

24 IRS Legacy Information Technology Systems: Hearing Before the House Comm. on Oversight and Government Reform, 114th Cong. (2016) (statement of Terence Milholland, Chief Technology Officer, Internal Revenue Service).

25 S. REP. No. 115-281, at 34 (2018).

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## ADMINISTRATIVE APPEAL RIGHTS: Amend Internal Revenue Code Section 7803(a) to Provide Taxpayers With a Legally Enforceable Administrative Appeal Right Within the IRS Unless Specifically Barred by Regulations

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to a Fair and Just Tax System*

### PROBLEM

Congress has long understood the importance of an independent Appeals function within the IRS as a means of facilitating case resolutions and minimizing litigation, which is burdensome to both taxpayers and the government. Accordingly, Congress mandated the creation of the IRS Office of Appeals (Appeals) as an independent function within the IRS as part of the IRS Restructuring and Reform Act of 1998 (RRA 98).<sup>2</sup> As explained by Senator William Roth:

One of the major concerns we've listened to throughout our oversight initiative—a theme that repeated itself over and over again—was that the taxpayers who get caught in the IRS hall of mirrors have no place to turn that is truly independent and structured to represent their concerns. With this legislation, we require the agency to establish an independent Office of Appeals—one that may not be influenced by tax collection employees or auditors.<sup>3</sup>

Appeals subsequently adopted this charge as its guiding principle: “The Appeals Mission is to resolve tax controversies, without litigation, on a basis which is fair and impartial to both the Government and the taxpayer and in a manner that will enhance voluntary compliance and public confidence in the integrity and efficiency of the Service.”<sup>4</sup> Appeals, however, is unable to perform its intended role when its jurisdiction is curtailed by various means, such as precipitous issuance of statutory notices of deficiency (SNOD) or the use of the “sound tax administration” rationale as a reason for bypassing Appeals.<sup>5</sup> The National Taxpayer Advocate has repeatedly warned against depriving taxpayers of their *right to appeal an IRS decision in an independent forum*, a right that was adopted by the IRS in 2014 and reaffirmed by Congress in 2015.<sup>6</sup> Circumventing Appeals causes the IRS to waste resources and taxpayers to incur needless expense, delay, and uncertainty, all of which undermine sound tax administration.

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 Pub. L. No. 105-206, § 1001(a)(4), 112 Stat. 685, 689 (1998).

3 144 CONG. REC. S7622 (July 8, 1998) (Statement of Sen. Roth).

4 Internal Revenue Manual (IRM) 8.1.1.1(1), *Accomplishing the Appeals Mission* (Oct. 1, 2016).

5 National Taxpayer Advocate Fiscal Year (FY) 2016 Objectives Report to Congress 66-69. Certain IRS officials have the power to determine “that a docketed case or issue will not be referred to Appeals.” Rev. Proc. 2016-22, § 3.03, 2016-15 I.R.B. 577, 578.

6 IRS News Release IR-2014-72 (June 10, 2014); IRC § 7803(a)(3)(E). See National Taxpayer Advocate FY 2019 Objectives Report to Congress 140-141; National Taxpayer Advocate FY 2016 Objectives Report to Congress 66-69; National Taxpayer Advocate 2015 Annual Report to Congress 376-382.

## EXAMPLE

Taxpayer, a diversified business, enters into a transaction that the IRS believes to be suspiciously similar to a type of transaction it has previously identified as a tax shelter. As a result, the IRS asserts large deficiencies and penalties against Taxpayer. Thereafter, Taxpayer files a protest with Appeals, arguing that the transaction in question is fundamentally different from the tax shelter transaction with which the IRS is attempting to equate it. Further, Taxpayer contends that, in addition to being distinguishable from a tax shelter, the transaction in question has a legitimate business purpose, and should not generate either tax deficiencies or penalties.

The Office of Chief Counsel, however, unilaterally decides that Taxpayer should not have the opportunity to raise these arguments at Appeals. Instead, Counsel determines that the case should proceed directly to litigation on the basis of “sound tax administration.” As a result, Taxpayer is unable to present its arguments to an independent third party within the IRS and is prevented from seeking the administrative case resolution it believes could have been achieved. Instead, Taxpayer is forced to pursue its case in court, as a matter of public record, incurring substantial cost, delay, and ill-will for the IRS along the way.

## RECOMMENDATIONS

The National Taxpayer Advocate recommends that Congress amend § 7803(a) to establish an independent Office of Appeals and grant taxpayers the right to a prompt administrative appeal within the IRS that provides an impartial review of all compliance actions and an explanation of the Appeals decision, except where the Secretary has determined, pursuant to regulations, that an appeal is not available, including on the basis of designation for litigation or adoption of a frivolous position. Where an appeal is not available, the Secretary shall furnish taxpayers with the procedures for protesting to the Commissioner the decision to bar an appeal in these circumstances.

## PRESENT LAW

Since 1955, the IRS’s Statement of Procedural Rules has provided that taxpayers have the right to an administrative appeal.<sup>7</sup> However, courts have held that the IRS is not bound by its own procedural rules.<sup>8</sup> In addition, Rev. Proc. 87-24 clarified that certain IRS officials could “determine that a case, or an issue or issues in a case, should not be considered by Appeals.”<sup>9</sup> Specifically, cases or issues can be designated for litigation if they “present recurring, significant legal issues affecting large numbers of taxpayers. When there is a critical need for enforcement activity with respect to such issues, cases are designated for litigation in the interest of sound tax administration to establish judicial precedent,

7 20 Fed. Reg. 4621, 4626 (June 30, 1955) (codified at 26 C.F.R. § 601.106(b), which provided that if the IRS “has issued a preliminary or ‘30-day letter’” and the taxpayer has filed a timely protest, “the taxpayer has the right (and will be so advised by the district director) of administrative appeal.”). The situations in which a taxpayer may request an appeal are now at 26 C.F.R. § 601.106(b)(3).

8 See *Ward v. Comm’r*, 784 F.2d 1424, 1430-31 (9th Cir. 1986); *Estate of Weiss v. Comm’r*, T.C. Memo. 2005-284. *But see*, *Richardson v. Joslin*, 501 F.3d 415, 418 (5th Cir. 2007) (“[A]n agency must abide by its own regulations.”) (citing *Accardi v. Shaughnessy*, 347 U.S. 260 (1954)); *United States v. Heffner*, 420 F.2d 809 (4th Cir. 1969) (IRS bound by instructions given to Special Agents); *Rauenhorst v. Comm’r*, 119 T.C. 157 (2002) (IRS bound by revenue rulings).

9 Rev. Proc. 87-24, 1987-1 C.B. 720, *superseded by* Rev. Proc. 2016-22, 2016-15 I.R.B. 577. The superseding Revenue Procedure clarifies and elaborates on Rev. Proc. 87-24, stating, among other things, that Division Counsel or a higher level Counsel can determine that referral to Appeals is not in the interest of sound tax administration.

conserve resources, or reduce litigation costs for the Service and taxpayers.”<sup>10</sup> Typically, the decision of whether or not to designate a given case or issue for litigation requires consultation and approval of a range of parties.<sup>11</sup> Depending upon the procedural posture of the case or issue, these parties can include the operating division with jurisdiction, Chief Counsel, and the Chief of Appeals.<sup>12</sup>

Subsequently, RRA 98 granted taxpayers the statutory right to an administrative appeal in certain circumstances.<sup>13</sup> In particular, these circumstances involve Collection Due Process cases and offers-in-compromise.<sup>14</sup> Even in these instances, however, no right to appeal exists in the case of a frivolous position adopted by a taxpayer.<sup>15</sup>

In late 2015, the IRS requested public comments on procedures that would deny taxpayers the right to go to Appeals if the “referral is not in the interest of sound tax administration,” even in cases not designated for litigation.<sup>16</sup> The American Bar Association Section of Taxation suggested that the IRS “elaborate and clarify the limited circumstances in which docketed cases will be ineligible to be returned to Appeals due to ‘sound tax administration.’”<sup>17</sup> However, the IRS finalized these procedures as Rev. Proc. 2016-22 without addressing this comment. The IRS did not explain why it declined to elaborate on or clarify this standard, which, at least at this point, appears to be both vague and open-ended.<sup>18</sup>

At the National Taxpayer Advocate’s urging, the IRS adopted the Taxpayer Bill of Rights (TBOR) in 2014 and incorporated it into Publication 1, *Your Rights as a Taxpayer*.<sup>19</sup> The TBOR was subsequently enacted by Congress in 2015 and was codified as IRC § 7803(a)(3), which states that the “Commissioner shall ensure that employees of the Internal Revenue Service are familiar with and act in accord with taxpayer rights as afforded by other provisions of this title, including— ... the right to appeal a decision of the Internal Revenue Service in an independent forum.”<sup>20</sup> As further elaborated

10 Chief Counsel Directives Manual (CCDM) 33.3.6.1(1), *Purpose and Effect of Designating a Case for Litigation* (Aug. 11, 2004).

11 CCDM 33.3.6.1(3), *Purpose and Effect of Designating a Case for Litigation* (Aug. 11, 2004).

12 *Id.*

13 Pub. L. No. 105-206, §§ 1001(a)(4), 3401, 112 Stat. 685, 689, 746 (1998) (establishing Appeals as an independent function within the IRS, and granting taxpayers a statutory right to a hearing before Appeals in connection with liens and levies, codified at IRC §§ 6320(b)(1) (lien), 6330(b)(1) (levy)). RRA 98 § 3462 also directed the IRS to establish procedures for administrative appeals of IRS rejections of proposed installment agreements or offers-in-compromise under IRC §§ 6159 and 7122, respectively. In addition, other provisions assume that taxpayers have access to Appeals. See, e.g., IRC §§ 6015(c)(4)(B)(ii)(I), 7430(c)(2), 6621(c)(2)(A)(i).

14 Internal Revenue Service Restructuring and Reform Act of 1998 (RRA 98), Pub. L. No. 105-206, § 3462(c), 112 Stat. 685, 766 (1998). See IRC §§ 6330, 6159(e), and (f); 7122(e).

15 IRC § 6702(b)(2)(A); IRC § 7122(g); IRM 8.22.5.5.3, *Frivolous Issues* (Nov. 8, 2013).

16 Notice 2015-72, 2015-44 I.R.B. 613.

17 Letter from American Bar Association (ABA) Section of Taxation to Comm’r, IRS, Comments on Notice 2015-72 (Nov. 16, 2015), [https://www.americanbar.org/groups/taxation/policy/policy\\_2015.html](https://www.americanbar.org/groups/taxation/policy/policy_2015.html).

18 The IRS’s request for comments may suggest the IRS was seeking to increase the deference given to the final rule. However, the revenue procedure did not purport to establish “legislative” rules. If it had, the IRS would have been required to consider comments and provide a concise statement explaining the basis and purpose for a final rule under 5 U.S.C. § 553(c). The rule could have been challenged on the basis that the IRS did not address the comment and provide a reasoned explanation and that it was arbitrary and capricious under 5 U.S.C. § 706(2)(A). See, e.g., *Altera Corp. & Subs. v. Comm’r*, 145 T.C. 91, 130 (2015) (holding that a regulation was invalid because, in promulgating the regulation, the Treasury did not “adequately respond to commentators,” citing *Motor Vehicle Mfrs. Ass’n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29 (1983) (requiring rules to be the product of reasoned decision-making)).

19 National Taxpayer Advocate 2013 Annual Report to Congress 5-19; National Taxpayer Advocate 2007 Annual Report to Congress 478-489; IRS News Release IR-2014-72 (June 10, 2014).

20 IRC §§ 7803(a)(3), (a)(3)(E).

in IRS Publication 1, which is a statutorily mandated publication, “Taxpayers are entitled to a fair and impartial administrative appeal of most IRS decisions, including many penalties...”<sup>21</sup>

The U.S. District Court for the Northern District of California recently weighed in on the scope of taxpayers’ right to an administrative appeal in *Facebook, Inc. v. IRS*.<sup>22</sup> That case arose out of a five-year audit of Facebook by the IRS, in which the IRS interviewed Facebook employees, issued more than 200 requests for documents, and asked it to agree to five extensions of the statutory period of limitations. When Facebook declined to extend the period for a sixth time, the IRS issued a SNOD. Facebook filed a petition to the Tax Court and asked the IRS to transfer the case to Appeals. The IRS refused based on its view that doing so was “not in the interest of sound tax administration.”<sup>23</sup> Facebook responded by filing suit in District Court and arguing, among other things, that the IRS violated its “right to appeal a decision of the Internal Revenue Service in an independent forum,” under IRC § 7803(a)(3)(E).

The U.S. District Court for the Northern District of California granted the IRS’s motion to dismiss, holding that Facebook did not have an enforceable right to take its case to Appeals. The District Court reasoned that the IRS’s Statement of Procedural Rules did not create enforceable rights and neither did IRC § 7803(a)(3)(E). By its terms, IRC § 7803(a)(3) required the Commissioner to train employees and ensure they act in accord with rights granted under “other provisions.” Moreover, the District Court stated that even if IRC § 7803(a)(3) had created enforceable rights, it was not clear that the “right to appeal in an independent forum” refers to a right to take a case to IRS Appeals, as opposed to a federal court.<sup>24</sup>

## REASONS FOR CHANGE

The right to appeal a decision within the IRS is an indispensable element of fair and equitable tax administration. Such is the case because an appeal represents the final administrative opportunity to resolve a case without resort to litigation. Further, the Office of Appeals is the only IRS decision-making function that attempts to act independently of other agency determinations and to provide taxpayers with an unbiased forum for negotiating case settlements.<sup>25</sup>

Access to Appeals is important for a variety of reasons, including Appeals’ ability to:

- Accept affidavits and weigh oral testimony;
- Consider hazards of litigation; and
- Apply the *Cohan* rule as a means of negotiating a case resolution.<sup>26</sup>

21 IRS, Pub. 1, *Your Rights as a Taxpayer* (Sept. 2017); Pub. L. No. 100-647, § 6227(a), 102 Stat. 3342, 3731 (1988).

22 *Facebook, Inc. & Subs. v. IRS*, 2018-1 U.S.T.C. (CCH) ¶50,248 (N.D. Cal. 2018). For a more in-depth discussion of the *Facebook* decision, see the applicable analysis presented in the Significant Cases Summary, *infra*.

23 Rev. Proc. 2016-22, 2016-15 I.R.B. 577.

24 *But see* IRS, Pub. 1, *Your Rights as a Taxpayer* (Sept. 2017). “Taxpayers are entitled to a fair and impartial administrative appeal of most IRS decisions, including many penalties...” This language, which was the subject of in-depth discussion between the National Taxpayer Advocate and the IRS when Pub. 1 was revised to incorporate the TBOR, explicitly contemplates that the appeal right in question is intended to exist within the IRS, not just in the judicial realm. By law, Publication 1 is required to be sent to taxpayers at various stages of an ongoing dispute.

25 TAS also acts independently, but in keeping with its origins as an ombuds function, TAS does not make substantive case decisions.

26 The *Cohan* rule was developed under federal case law as a means of allowing the fact finder to estimate deductible expenses where the fact of those expenses, although not their amount, can be substantiated. See *Cohan v. Comm’r*, 39 F.2d 540 (2d Cir. 1930).

Currently, however, the IRS has the unilateral ability to deny this forum to any taxpayer on an *ad hoc* basis. Because taxpayers lack a legally enforceable right to an appeal, they are powerless to prevent the IRS from bypassing Appeals if it wishes to punish uncooperative behavior or to avoid settlement negotiations involving a particular taxpayer or issue. This unchecked and unreviewable power raises the specter of unfair and inequitable treatment of individual taxpayers or broader taxpayer groups.

In some very limited circumstances, curtailing taxpayer access to Appeals may indeed prove warranted. However, these situations should not be left to the IRS to determine on an *ad hoc* basis. Rather, they should be clearly laid out by statute so as to protect both taxpayers and the IRS.<sup>27</sup>

Indeed, the IRS already has the ability to bypass Appeals in a number of situations, including when a taxpayer adopts a frivolous position or when the filing of a Collection Due Process hearing request reflects a desire to delay or impede the administration of the federal tax laws.<sup>28</sup> Likewise, Chief Counsel, subject to appropriate consultations and approvals, can designate broad categories of issues or cases for litigation. Accordingly, another such mechanism that is less well-defined and more open to individual discretion is not only unnecessary, but heightens risk of government overreach and jeopardizes taxpayer rights.

## EXPLANATION OF RECOMMENDATIONS

The National Taxpayer Advocate recommends that Congress amend section 7803(a) to establish an independent Office of Appeals and grant taxpayers the right to a prompt administrative appeal within the IRS that provides an impartial review of all compliance actions and an explanation of the Appeals decision, except where the Secretary has determined, pursuant to regulations, that an appeal is not available, including on the basis of designation for litigation or adoption of a frivolous position. Where an appeal is not available, the Secretary shall furnish taxpayers with the procedures for protesting to the Commissioner the decision to bar an appeal in these circumstances.

This legislation would establish the presumption that taxpayers have the right to an appeal, subject only to narrowly defined and clearly articulated regulatory exceptions. Only where these exceptions exist would the IRS have the right to deny an appeal. However, the basis for such a denial must be explained to taxpayers and they would have the right to challenge this determination.

By adopting these recommendations, Congress would protect the viability of the Appeals process within the IRS. At long last, taxpayers would have a legally enforceable right to an administrative appeal, which is their last, and often best, opportunity to resolve a case within the IRS. By permitting this right to be circumscribed only when the Secretary has specified by regulations that an appeal is unavailable, Congress would ensure that any such limitations would be imposed solely when warranted and applied fairly across the overall taxpayer population.

<sup>27</sup> For example, a reasonable case can be made in support of a statutory provision barring appeals of positions determined to be frivolous within the meaning of IRC § 6702(c). Section 11101(a) of the Taxpayer First Act, H.R. 5444, (115th Cong.) (2018) proposes a similar but less sweeping recommendation than the one put forward by the National Taxpayer Advocate. That proposed legislation would amend IRC § 7803 to provide a more generalized right of administrative appeal that could be curtailed only with appropriate notice and explanation from the IRS Commissioner. Among other things, it also would specify that the rights created by the legislation did not extend to appeals of frivolous positions.

<sup>28</sup> IRM 8.11.8.2(1), *IRC 6702 – Frivolous Tax Submissions* (Oct. 28, 2013); IRM 8.22.5.5.3, *Frivolous Issues* (Nov. 8, 2013).

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#3**FIX THE FLORA RULE: Give Taxpayers Who Cannot Pay the Same Access to Judicial Review as Those Who Can****TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to Privacy*
- *The Right to a Fair and Just Tax System*

**PROBLEM**

In 1958 in *Flora I* and again in 1960 in *Flora II*, the U.S. Supreme Court held that taxpayers must fully pay a tax liability before filing a refund suit in a district court or the U.S. Court of Federal Claims (as summarized in the Appendix).<sup>2</sup> The Court reasoned that this full payment rule (a.k.a. the *Flora* rule) would protect the “public purse” and cited its decision in *Cheatham* that justified the rule as necessary to protect the very “existence of government.”<sup>3</sup> In 1875 when *Cheatham* was decided, the rule may have been necessary to prevent local courts from starving the young federal government of the revenue it needed to exist. Today, the full payment rule is no longer needed to protect the existence of the government and may not even protect the public purse.

It is clear, however, that the full payment rule gives the poor who cannot pay a disputed liability less access to judicial review than wealthier taxpayers who can. Because the IRS may assess certain penalties (called “assessable penalties”) before giving the taxpayer an opportunity to petition the Tax Court to review them, the rule also closes the courthouse door to those facing assessable penalties that are too large to pay—precisely the penalties that are most damaging if they are wrongly assessed.<sup>4</sup> Even if the IRS’s liability determination is correct, a lack of due process seems unfair and may erode voluntary

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 See *Flora v. United States (Flora I)*, 357 U.S. 63 (1958), *reaff'd*, *Flora v. United States (Flora II)*, 362 U.S. 145 (1960). *Flora II* was a 5-4 decision with the majority acknowledging that “as we recognized in the prior opinion, the statutory language is not absolutely controlling.” *Flora II*, 362 U.S. at 151.

3 See *Flora I*, 357 U.S. at 67-69 (citing *Cheatham v. United States*, 92 U.S. 85, 89 (1875), which said the very “existence of government” was at stake); *Flora II*, 362 U.S. at 175 (“the Government has a substantial interest in protecting the public purse, an interest which would be substantially impaired if a taxpayer could sue in a District Court without paying his tax in full”). For a discussion of how Congress has increasingly provided taxpayers with procedural protections, overriding the sovereign’s ancient power to require immediate payment of taxes, see Nina E. Olson, 2010 Erwin N. Griswold Lecture Before the American College of Tax Counsel, *Taking the Bull by Its Horns: Some Thoughts on Constitutional Due Process in Tax Collection*, 63 *TAX LAW.* 227 (2010).

4 See IRC §§ 6671(a), 6212, and 6213.

compliance—a consequence which may pose a greater risk to the public purse than providing a pre-payment forum for judicial review.<sup>5</sup>

Moreover, the problems posed by assessable penalties have grown. When *Flora I* was decided, there were only four assessable penalties, but today there are over 50.<sup>6</sup> This erosion of judicial oversight is particularly inconsistent with the taxpayer's *right to appeal an IRS decision in an independent forum* and *right to a fair and just tax system*.

## EXAMPLES

### Example 1: The District Court and the Court of Federal Claims Cannot Review Claims from Those Who Cannot Fully Pay

In 2010, the IRS audited Ms. Jane Doe's 2007 income tax return and issued a notice of deficiency, proposing to disallow her Earned Income Tax Credit (EITC) because she had no bank account or accounting system to substantiate her earned income.<sup>7</sup> If given an opportunity, Ms. Doe could substantiate her income in court using the testimony of customers. Because she did not understand the notice of deficiency, Ms. Doe missed the deadline for filing a petition with the Tax Court.<sup>8</sup> Under the full payment rule, she cannot file suit in a district court or in the Court of Federal Claims before paying in full. Because she cannot afford to pay in full, she cannot get her case reviewed, and the IRS will attempt to collect the inaccurate deficiency.

### Example 2: By the Time a Person Has Fully Paid in Installments, It May Be Too Late to Recover the Early Payments

The facts are the same as in Example 1, except that Ms. Doe entered into an installment agreement (IA) to pay the liability over a six-year period (*i.e.*, between 2010 and 2016).<sup>9</sup> Neither the applicable U.S. District Court nor the U.S. Court of Federal Claims had jurisdiction to review her case before she completed the IA and fully paid. After completing the IA and fully paying the liability in 2016, Ms. Doe filed a claim for refund. By 2016, she could only recover the portions she paid in the last two

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- 5 See, e.g., National Taxpayer Advocate 2012 Annual Report to Congress vol. 2, 1-28 (finding that trust and norms correlate with estimated tax compliance among Schedule C filers). Indeed, *Flora II* suggested that the full payment rule would promote voluntary compliance, in part, because enforced collection of a disputed liability while a case was before a district court or the Court of Federal Claims would adversely affect voluntary compliance. *Flora II* at 176 n. 43. This suggestion by *Flora II* seems to assume that the full payment rule simply shifts litigation from proceedings that do not suspend collection to the Tax Court where enforced collection is suspended. Today, however, the rule empowers the IRS to collect liabilities that are not subject to judicial review.
  - 6 Compare Internal Revenue Code of 1954, Pub. L. No. 83-591, 68 Stat. 730 (1954) (reflecting three assessable penalties, codified at IRC §§ 6672-6674), as amended by Pub. L. No. 84-466, § 3, 70 Stat. 90 (1956) (enacting a fourth, codified at IRC § 6675), with IRC §§ 6671-6725 (more than 50 present-day assessable penalties).
  - 7 This hypothetical example was inspired by a recent case. See *Lopez v. Comm'r*, T.C. Summ. Op. 2017-16 (holding an unbanked taxpayer who timely petitioned the Tax Court was entitled to EITC because she substantiated her earned income in court based on the testimony of customers).
  - 8 Low income taxpayers can easily miss filing deadlines. See, e.g., *Mullins v. IRS*, 120 A.F.T.R.2d (RIA) 5028 (S.D. Ohio 2017) (considering an EITC claim in district court after the taxpayer missed the deadline for filing a petition with the Tax Court and paid the assessment). For example, the notice could be sent to an old address or taken by a roommate. Some taxpayers may be afraid to open a letter from the IRS. Some may not understand the IRS's letters (e.g., due to literacy or language barriers). Others may mistakenly write to the IRS instead of filing a petition with the Tax Court.
  - 9 This hypothetical example was inspired by the dissent in *Flora II*. See *Flora II*, 362 U.S. at 195-96 (J. Whittaker, dissenting) (warning that early installment payments would not be reviewable under the full payment rule). The same result could occur if instead of entering an installment agreement (IA), the IRS simply offset the taxpayer's refunds each year for six years.

years (*i.e.*, 2015 and 2016).<sup>10</sup> Because the full payment rule delayed her suit, it was too late to recover the payments she made during 2010-2014.<sup>11</sup>

### Example 3: Collection Due Process Appeals Jurisdiction Does Not Solve the Problem

The facts are the same as in Example 1, except that after the IRS assessed the deficiency it filed a notice of federal tax lien (NFTL) and sent Ms. Doe a Collection Due Process (CDP) notice.<sup>12</sup> Ms. Doe requested a CDP hearing with the IRS's Appeals function. Appeals could not consider Ms. Doe's underlying liability at the hearing because she had received a statutory notice of deficiency.<sup>13</sup> Although the Tax Court has jurisdiction to review the results of a CDP hearing, it does not have jurisdiction to consider issues not properly raised and considered in the hearing.<sup>14</sup> Thus, it could not review the disputed liability. In addition, Ms. Doe cannot file suit in a district court or in the Court of Federal Claims because she has not fully paid the liability.

### Example 4: Assessable Penalties That Are Too Large to Pay Are Not Subject to Judicial Review

An examiner erroneously proposed over \$160 million in penalties against Mr. John Doe under IRC § 6707 for failure to timely register a tax shelter.<sup>15</sup> The IRS Office of Appeals reduced the penalty to about \$65 million, which Mr. Doe still could not pay. Because IRC § 6707 is an assessable penalty, the IRS properly assessed it without sending him a notice of deficiency. A notice of deficiency would have given him the right to petition the Tax Court.<sup>16</sup> Because Mr. Doe cannot pay the assessment, neither a district court nor the Court of Federal Claims has jurisdiction to review it under the full payment rule. Because he was given the opportunity for an administrative appeal, the Tax Court would not have jurisdiction to review the liability in connection with a CDP hearing.<sup>17</sup>

10 A taxpayer must make an administrative claim for refund before filing suit. IRC § 7422(a). In general, any administrative claim must be made within the later of three years after the filing of the original tax return or two years of payment of the tax. IRC § 6511(a). If the claim is filed in the two-year period, the amount that can be refunded is generally limited to taxes paid within the two-year period before the claim is made. IRC § 6511(b)(2)(B).

11 We do not propose to extend the limitations period because there are good reasons for them. It makes more sense to allow a court to determine how much a person owes as quickly as possible. By the time a taxpayer has paid, witnesses are less likely to be available, memories are more likely to have faded, and relevant documentation is more likely to have been lost. For further discussion of the benefits of limitations periods, see, e.g., National Taxpayer Advocate 2009 Annual Report to Congress 391-399 (Legislative Recommendation: *Provide a Fixed Statute of Limitations for U.S. Virgin Islands Taxpayers*).

12 The IRS must send a collection due process (CDP) notice after filing a Notice of Federal Tax Lien (NFTL) and before issuing a levy. See generally, IRC §§ 6320 (lien), 6330 (levy).

13 IRC § 6330(c)(2)(B); IRC § 6320(c). See also IRM 8.22.8.3 (Aug. 9, 2017).

14 See IRC § 6330(d)(1); Treas. Reg. §§ 301.6320-1(f)(2) Q&A F3, 301.6330-1(f)(2) Q&A F3.

15 This hypothetical example was loosely inspired by *Larson v. United States*, 888 F.3d 578 (2d Cir. 2018), *aff'g* 118 A.F.T.R.2d (RIA) 7004 (S.D.N.Y. 2016) (district court had no jurisdiction to review of assessable penalties under IRC § 6707). However, the example assumes the penalties were erroneously assessed.

16 IRC §§ 6212, 6213.

17 IRC § 6330(c)(2)(B); IRC § 6320(c); Treas. Reg. §§ 301.6320-1(e)(3)A-E2 and 301.6330-1(e)(3)A-E2. These regulations are controversial, as discussed in footnote 32, below.

## RECOMMENDATIONS

A simple solution would be to repeal the full payment rule.<sup>18</sup> If Congress prefers a more tailored approach to improve access to judicial review, the National Taxpayer Advocate recommends Congress:

1. Amend 28 U.S.C. § 1346(a)(1) to clarify that full payment of a disputed amount is only a prerequisite for jurisdiction by district courts and the U.S. Court of Federal Claims if the taxpayer has received a notice of deficiency. If enacted, taxpayers who are subject to assessable penalties would not need to pay them in full before filing suit in a district court or the Court of Federal Claims.
2. Amend 28 U.S.C. § 1346(a)(1) to clarify that a taxpayer is treated as having fully paid a disputed amount for purposes of the full payment rule at the earlier of when the taxpayer has paid some of it (including by offset) and either (a) the IRS has classified the account as currently not collectible due to economic hardship,<sup>19</sup> or (b) the taxpayer has entered into an agreement to pay the liability in installments.<sup>20</sup> If enacted, taxpayers who cannot afford to pay would have the same access to judicial review as those who can (*i.e.*, the option to file suit in a district court or the U.S. Court of Federal Claims).
3. Amend IRC § 6214 to authorize the U.S. Tax Court to review liabilities where the taxpayer has not received a notice of deficiency (*e.g.*, assessable penalties) in a manner that parallels the deficiency process. In addition, allow the IRS to assess and collect liabilities only after any such review is complete or the period for filing a Tax Court petition has expired. Alternatively, Congress could expand the Tax Court's jurisdiction to review liabilities in connection with CDP appeals when the taxpayer has not received a notice of deficiency. These changes would authorize review of assessable penalties by the Tax Court even if the taxpayer had an opportunity for an administrative appeal.<sup>21</sup>

## PRESENT LAW

A taxpayer may seek judicial review of an IRS liability determination in various federal courts. However, judicial review is sometimes unavailable.

### Deficiency Litigation Before the Tax Court

Upon receipt of a statutory notice of deficiency from the IRS, a taxpayer generally has 90 days to file a petition with the Tax Court—the only court (other than the Bankruptcy Court) that can review

<sup>18</sup> A repeal of the full payment rule would increase access to the district courts and the Court of Federal Claims. These courts have no jurisdiction if the taxpayer has petitioned the Tax Court. See IRC § 7422(e). Therefore, a repeal of the full payment rule would not erode judicial economy by allowing taxpayers to litigate the same issue in more than one court. Even if the full payment rule is repealed, however, Congress should consider the third recommendation—to expand the Tax Court's jurisdiction—because its informal rules make it more accessible to unsophisticated taxpayers.

<sup>19</sup> See IRC § 6343(a)(1)(D) (authority to release levies that create an economic hardship); Policy Statement 5-71, IRM 1.2.14.1.14 (Nov. 19, 1980) (establishing a policy to report accounts as currently not collectible when the taxpayer has no assets or income which are, by law, subject to levy).

<sup>20</sup> For a similar proposal, see Carlton M. Smith, *Let the Poor Sue For Refund Without Full Payment*, 125 TAX NOTES 131 (Oct. 5, 2009).

<sup>21</sup> For a similar proposal, see Letter from Keith Fogg, Dir. Fed. Tax Clinic, Legal Svc. Ctr., Harvard L. Sch. to Hon. Lynn Jenkins, Chair, Subcomm. on Oversight of the Comm. on Ways & Means (Apr. 6, 2018) (comments on the Taxpayer First Act, proposal 2), <http://procedurallytaxing.com/wp-content/uploads/2018/04/LetterandProposalsonTaxpayerFirstLegislation.pdf>.

a tax deficiency before it is paid.<sup>22</sup> The Tax Court is particularly accessible to unsophisticated and unrepresented taxpayers because it uses informal procedures, which are even more informal if the dispute does not exceed \$50,000.<sup>23</sup> However, confusing IRS correspondence, illiteracy, language barriers, and unequal access to competent tax professionals can cause taxpayers—particularly low income taxpayers—to miss the deadline for filing a petition with the Tax Court.<sup>24</sup>

The IRS can also assess certain penalties (called “assessable” penalties) without sending a notice of deficiency or otherwise triggering the Tax Court’s jurisdiction.<sup>25</sup> The penalties in Subchapter B (*i.e.*, IRC §§ 6671-6725) are expressly excluded from the deficiency process.<sup>26</sup> Other penalties are implicitly excluded because they do not depend on a tax deficiency.<sup>27</sup> Thus, the Tax Court has no jurisdiction to review them before they are assessed.

### Collection Due Process Litigation Before the Tax Court

After the IRS assesses a liability, the taxpayer may sometimes seek judicial review when the IRS tries to collect. Before the IRS levies property or after it has filed a notice of federal tax lien (NFTL), it must send a CDP notice, which gives the taxpayer the right to request a CDP hearing before the IRS’s Appeals function.<sup>28</sup> Within 30 days of Appeals’ determination, the taxpayer may petition the Tax Court for review.<sup>29</sup>

22 IRC §§ 6212, 6213. The 90-day period becomes 150 days if the notice is addressed to a person who is outside the United States. *Id.* The IRS may also assess tax without first sending a notice of deficiency if it determines that collection is in jeopardy. See IRC §§ 6851, 6861, 6862, 6871. This proposal would not change the existing jeopardy assessment procedures.

23 IRC § 7463.

24 See, e.g., Carlton M. Smith, *Let the Poor Sue For Refund Without Full Payment*, 125 TAX NOTES 131 (Oct. 5, 2009). The IRS is not required to send a notice of deficiency before summarily assessing a math or clerical error. IRC §§ 6213(b), (g). Although taxpayers who timely respond to math error notices can get the IRS to send them notices of deficiency and then file a petition with the Tax Court, low income taxpayers have difficulty understanding math error notices and timely navigating these procedures. See, e.g., National Taxpayer Advocate 2014 Annual Report to Congress 163.

25 Items such as self-assessed taxes and erroneous tax pre-payment credit claims may be assessed without the opportunity for review by the Tax Court because they are not “deficiencies.” See IRC § 6201.

26 See IRC § 6671(a) (“The penalties and liabilities provided by this subchapter [IRC §§ 6671-6725] shall be paid upon notice and demand by the Secretary...”); *Smith v. Comm’r*, 133 T.C. 424, 428 n.3 (2009) (indicating the following penalties are expressly excluded from deficiency procedures: IRC §§ 6677(e) (failure to file information with respect to foreign trust), 6679(b) (failure to file returns, etc., with respect to foreign corporations or foreign partnerships), 6682(c) (false information with respect to withholding), 6693(d) (failure to provide reports on certain tax-favored accounts or annuities), 6696(b) (rules applicable with respect to IRC §§ 6694, 6695, and 6695A), 6697(c) (assessable penalties with respect to liability for tax of regulated investment companies), 6706(c) (original issue discount information requirements), 6713(c) (disclosure or use of information by preparers of returns), 6716(e) (failure to file information with respect to certain transfers at death and gifts)).

27 See *Smith v. Comm’r*, 133 T.C. at 429 n.4 (indicating the following penalties are implicitly excluded from the deficiency process: IRC §§ 6651 (failure to file a tax return or to pay a tax; the deficiency procedures apply only to the portion of the penalty attributable to the deficiency in taxes), 6677 (failure to file information returns with respect to certain foreign trusts), 6679 (failure to file returns, etc., with respect to foreign corporations or foreign partnerships), 6686 (failure to file returns or supply information by domestic international sales corporation or foreign sales corporation), 6688 (assessable penalties with respect to information required to be furnished under sec. 7654), 6690 (fraudulent statement or failure to furnish statement to plan participant), 6692 (failure to file actuarial report), 6707 (failure to furnish information regarding reportable transactions), 6708 (failure to maintain lists of advisees with respect to reportable transactions), 6710 (failure to disclose that contributions are nondeductible), 6711 (failure by tax-exempt organization to disclose that certain information or services are available from the Federal Government), 6712 (failure to disclose treaty-based return positions), and 6707A (failure to include reportable transaction information with return)).

28 See generally, IRC §§ 6320 (lien), 6330 (levy).

29 IRC § 6330(d)(1).

Although the Tax Court has jurisdiction to consider certain challenges to the underlying liability that were properly raised during the CDP hearing,<sup>30</sup> it generally does not have jurisdiction to review assessable penalties or to determine that a taxpayer has an overpayment.<sup>31</sup> A taxpayer cannot challenge the underlying liability if he or she (1) received a statutory notice of deficiency, or (2) otherwise had an opportunity to dispute the liability, which the IRS interprets by regulation to include “a prior opportunity for a conference with Appeals that was offered either before or after the assessment of the liability.”<sup>32</sup> Thus, CDP does not provide an avenue for judicial review of assessments against taxpayers who are subject to assessable penalties that they could have elevated to Appeals.<sup>33</sup>

### Refund Litigation Before a District Court or the Court of Federal Claims

After the taxpayer pays a liability, a district court or the Court of Federal Claims may have jurisdiction to review the taxpayer’s claim for refund.<sup>34</sup> However, these suits are subject to limitations.

#### *Complicated Rules Limit the Timing of Claims and the Amounts That Can Be Refunded*

Before filing a refund suit, the taxpayer must make a timely administrative claim.<sup>35</sup> To be timely, the administrative claim generally must be within the later of (i) three years from when the original return was filed or (ii) two years from when the tax was paid.<sup>36</sup> If the taxpayer can make a claim, the amount he or she can recover is limited based on when the claim is filed. If the claim is filed within the three-year period (*i.e.*, (i) above), the taxpayer can only recover amounts paid within three years, plus any

30 See Treas. Reg. §§ 301.6320-1(f)(2)A-F3; 301.6330-1(f)(2)A-F3.

31 See, e.g., *Greene-Thapedi v. Comm’r*, 126 T.C. 1 (2006) (holding the Tax Court lacked jurisdiction to consider overpayment); *McLane v. Commissioner*, T.C. Memo. 2018-149 (same). For a legislative recommendation to address this problem, see National Taxpayer Advocate 2017 Annual Report to Congress 293-298 (Legislative Recommendation: *Amend IRC § 6330 to Allow the Tax Court Jurisdiction to Determine Overpayments*). For a long history of proposals to expand the Tax Court’s refund jurisdiction, see Harold Dubroff & Brant J. Hellwig, *THE UNITED STATES TAX COURT, AN HISTORICAL ANALYSIS* 315-322 (2d Ed. 2014), [https://www.ustaxcourt.gov/book/Dubroff\\_Hellwig.pdf](https://www.ustaxcourt.gov/book/Dubroff_Hellwig.pdf).

32 IRC § 6330(c)(2)(B); § 6330(c)(4)(A); Treas. Reg. §§ 301.6320-1(e)(3)A-E2 and 301.6330-1(e)(3)A-E2; IRM 8.22.8.3 (Aug. 9, 2017). See also *Our Country Home Enterprises, Inc. v. Comm’r*, 855 F.3d 773 (7th Cir. 2017); *Keller Tank Services II, Inc. v. Comm’r*, 854 F.3d 1178 (10th Cir. 2017); *James v. Comm’r*, 850 F.3d 160 (4th Cir. 2017), and *Lewis v. Comm’r*, 128 T.C. 48 (2007). Some have argued that these cases, which uphold the regulations, misinterpret the statute. See, e.g., Chaim Gordon, *The Disjunctive Test for Challenging a Liability in a CDP Hearing*, 159 TAX NOTES 1615 (Jun. 11, 2018). In CDP cases involving assessable penalties where the IRS has denied access to Appeals, however, the Tax Court may have jurisdiction. See, e.g., *Yari v. Comm’r*, 143 T.C. 157 (2014), *aff’d*, 669 Fed. Appx. 489 (9th Cir. 2016) (claiming jurisdiction to review an assessable penalty under IRC § 6707A). Because the IRS does not view the receipt of a math error notice as a “prior opportunity” to dispute a liability, taxpayers may also obtain judicial review of math or clerical errors in the context of a CDP appeal. See IRM 8.22.8.3(9)(f) (Aug. 9, 2017).

33 IRC § 6330(c)(4)(A)(ii). Notably, if taxpayers were entitled to a pre-deprivation hearing under the Due Process Clause, commentators have suggested that CDP hearings do not provide sufficient protections. See, e.g., Diane Fahey, *The Tax Court’s Jurisdiction over Due Process Collection Appeals: Is It Constitutional*, 55 BAYLOR L. REV. 453, 457 (2003) (pointing out that the taxpayer does not have the right to subpoena witnesses or records, the CDP hearing is not conducted by an independent adjudicator, and the only record of what transpired is the determination letter prepared by the appeals officer afterwards). Others have suggested that Appeals could be more independent. See, e.g., American Bar Association, *Section of Taxation, Comments on Recent Practice Changes at Appeals* (May 9, 2017), <https://www.americanbar.org/content/dam/aba/administrative/taxation/policy/050917comments.pdf>.

34 See 28 U.S.C. §§ 1346(a)(1), 1491.

35 IRC § 7422(a). The IRS must use deficiency procedures to disallow all or part of the EITC on original returns, but may use math error procedures in the case of errors on returns that are mathematical or clerical within the meaning of IRC § 6213(g)(2). The IRS also generally uses deficiency or math error procedures (rather than a notice of claim disallowance) to disallow other refundable credits on original returns. See, e.g., PMTA 2007-0791 (May 2, 2016), and CCA 200202069 (Nov. 30, 2001).

36 IRC § 6511(a). If no return was filed, the limitations period is two years from when the tax was paid.

extension to file, before the date of the claim.<sup>37</sup> Otherwise, the taxpayer can only recover amounts paid within two years before the date of the claim.<sup>38</sup>

Following the administrative claim, the taxpayer can only file suit within a specific period and under certain conditions. The taxpayer cannot file suit before the earlier of when (1) the IRS disallows the claim, or (2) six months have lapsed and the IRS has not responded.<sup>39</sup> The taxpayer also generally cannot file suit later than two years after the IRS mails the notice of claims disallowance.<sup>40</sup>

### *The Full Payment Rule Bars Access by Those Who Cannot Pay*

The full payment rule was established by the Supreme Court in *Flora I* and *II*, as described in the Appendix. It requires a taxpayer to pay an assessment in full before it can be challenged in a refund suit filed in a district court or the Court of Federal Claims. It may also require taxpayers to fully pay the penalties and interest if any dispute about these items would not be determined by the court's resolution of the underlying tax claim.<sup>41</sup>

#### EXCEPTIONS TO THE FULL PAYMENT RULE

There are limited exceptions to the full payment rule. For “divisible” taxes, where the assessment may be divisible into a tax on each transaction or event (*e.g.*, excise taxes), the taxpayer need only pay enough to cover a single transaction or event.<sup>42</sup> For example, the trust fund recovery penalty under IRC § 6672(a)—a collection device that makes all “responsible persons” jointly and severally liable for a business’s trust fund taxes—is a divisible tax. After the IRS assesses the penalty, the responsible person need only pay the amount due with respect to a single employee for a single quarter before filing a suit that will determine his or her overall liability for the trust fund recovery penalty.<sup>43</sup> In such cases, the government may, but is generally not required, to file a counterclaim for the unpaid amounts that involve the same or similar issue (*e.g.*, taxes for other employees), even if they relate to different periods.<sup>44</sup>

There are also several statutory exceptions to the full payment rule. For example, in 1998 Congress clarified that suits by estates would not be barred solely because the executor had elected to pay the

37 IRC § 6511(b)(2)(A).

38 IRC § 6511(b)(2)(B).

39 IRC § 6532(a)(1); 28 U.S.C. § 1346(a)(1) (granting jurisdiction).

40 IRC § 6532(a)(1).

41 See *Shore v. United States*, 9 F.3d 1524 (Fed. Cir. 1993), *rev'g* 26 Cl. Ct. 829, 830 (1992). Immediately after *Flora II*, however, this point was unsettled. See, *e.g.*, Erika L. Robinson, *Refund Suits in Claims Court: Jurisdiction and the Flora Full-Payment Rule After Shore v. United States*, 46 TAX LAW. 827, 831-34 (1993) (describing four different views of the issue announced within a two-year period by the Claims Court); Martin M. Lore & L. Paige Marvel, *Claims Court Does About Face on Flora Full-Payment Rule*, 78 J. TAX'N 81, 81 (1993) (same).

42 *Flora II*, 362 U.S. at 175 n.38 (1960).

43 See, *e.g.*, *Steele v. United States*, 280 F.2d 89 (8th Cir. 1960) (penalties under IRC § 6672 for failure to remit amounts withheld from employees' wages are divisible employee by employee). Similarly, the tax return preparer penalty under IRC § 6695 is divisible. See *Nordbrock v. United States*, 173 F.Supp.2d 959 (D. Ariz. 2000), *aff'd*, 248 F.3d 1172. (9th Cir. 2001).

44 See Fed. R. Civ. P. 13(a) (generally requiring any counterclaim that arises from “transaction or occurrence that is the subject matter of the opposing party’s claim” provided the counterclaim(s) “do not require adding another party over whom the court cannot acquire jurisdiction”); Ct. Fed. Cl. R. 13(a) (same); *Flora II*, 362 U.S. at 166 (“the Government may but seemingly is not required to bring a counterclaim”). The government generally makes permissive counterclaims for unpaid portions of divisible taxes. See Chief Counsel Directives Manual (CCDM) 34.5.1.1.2.5 (Aug. 11, 2004). Counterclaims by the government for unpaid taxes help ensure the collections period under IRC § 6502(a) does not expire with respect to the unpaid amounts while refund litigation is pending with respect to the amounts that have been paid. *Id.*

estate tax in installments under IRC § 6166, and thus, had not fully paid.<sup>45</sup> In addition, in 1976 when Congress established assessable preparer penalties under IRC § 6694, it specifically provided that the preparer could contest them in district court after paying just 15 percent.<sup>46</sup> Congress took the same approach in 1982 when it established assessable penalties under IRC § 6700 (promoting abusive tax shelters) and § 6701 (aiding and abetting understatements).<sup>47</sup> As discussed below, however, no exception currently applies to most other assessable penalties—penalties assessed without providing the taxpayer a statutory notice of deficiency.<sup>48</sup>

### *The IRS May Sometimes Continue Collecting Disputed Amounts*

Although the IRS is not authorized to assess or collect amounts in dispute before the Tax Court, the filing of a suit in a district court or the Court of Federal Claims does not automatically stop IRS assessment or collection activity.<sup>49</sup> Because the filing of a suit to recover a divisible portion of a liability did not prevent the IRS from collecting the remainder, in 1978, Congress provided that taxpayers could avoid collection of the remainder (*e.g.*, through the filing of a NFTL) by posting a bond.<sup>50</sup> Similarly, in 1998, Congress provided that the IRS can not levy to collect unpaid portions of divisible taxes while the taxpayer is contesting a divisible portion, provided the proceeding will determine his or her liability for the unpaid portion by reason of *res judicata* or *collateral estoppel*.<sup>51</sup> For matters not covered by this exception, even if a taxpayer manages to get an unpaid dispute before the court (*e.g.*, if the IRS sues to collect), the IRS may continue collection activity while the dispute is pending.<sup>52</sup>

45 Internal Revenue Service Restructuring and Reform Act (RRA 98), Pub. L. No. 105-206, § 3104(a), 112 Stat. 685, 731-32 (1998) (codified at IRC § 7422(j)).

46 Tax Reform Act, Pub. L. No. 94-455, § 1203(b)(1), 90 Stat. 1520, 1689 (1976) (codified at IRC § 6694(c)). This provision also prevents the IRS from collecting the unpaid portion of the penalty while a suit to determine the penalty is pending. IRC § 6694(c)(1).

47 Tax Equity and Fiscal Responsibility Act, Pub. L. No. 97-248, § 322(a), 96 Stat. 324, 612 (1982) (codified at IRC § 6703(c)).

48 Indeed, a court recently used the statutory exceptions to the full payment rule as a reason to hold that the full payment rule applied to penalties under IRC § 6707 for which Congress had not enacted an exception. See *Larson v. United States*, 888 F.3d 578 (2d Cir. 2018), *aff'g* 118 A.F.T.R.2d (RIA) 7004 (S.D.N.Y. 2016). See also *Diversified Grp., Inc. v. United States*, 841 F.3d 975 (Fed. Cir. 2016).

49 Compare IRC § 7421 (Anti-Injunction Act, prohibiting suits to restrain assessment or collection), with IRC § 6213(a) (providing an exception to the anti-injunction act for the Tax Court). Indeed, the petitioner in *Flora* had argued that Congress established the Tax Court to enable taxpayers to prevent the Government from collecting taxes while disputing a liability. *Flora II*, 362 U.S. at 638.

50 Pub. L. No. 95-628, § 9(a), 92 Stat. 3627, 3633 (1978) (codified at IRC § 6672(c)); Joint Committee on Taxation (JCT), JCS-22-77, *Description of H.R. 7320; Miscellaneous Revisions Relating to Various Timing Requirements Under the Internal Revenue Code 9-10* (May 23, 1977) (explaining “[t]hese collection proceedings and the imposition of a lien against that person’s property may seriously endanger the business or credit of the person against whom the penalty was assessed.”).

51 RRA 98, Pub. L. No. 105-206 § 3433, 112 Stat. 685, 759 (1998) (codified at IRC § 6331(i)).

52 In some cases, the IRS may initiate a collection suit that may give the taxpayer an opportunity to dispute the assessment. See, *e.g.*, IRC § 7403(c) (granting jurisdiction for district courts to “finally determine the merits of all claims to and liens upon the property” subject to a lien in a suit to foreclose); *United States v. Maris, et al.*, 2015-1 U.S. Tax Cas. (CCH) 50,183 (D. Nev. 2015) (denying the government’s motion to reduce an income tax assessment to a judgement because of questions about the validity of the assessment). However, the taxpayer does not control the timing of these suits and has no right to them. Moreover, the IRS generally does not need to file suit to levy or seize property. See, *e.g.*, IRC § 6331.

### Bankruptcy Proceedings Before a Bankruptcy Court

A bankruptcy court “may” review certain tax liabilities, including unpaid assessable penalties that have not been contested and adjudicated in another tribunal.<sup>53</sup> However, the court’s authority to determine a refund is limited, and the court may abstain from determining tax issues for various reasons.<sup>54</sup> For example, it is likely to abstain where the debtor is the only party who would benefit from the review (*i.e.*, the creditors would not benefit).<sup>55</sup> Ironically, the taxpayer is most likely to want judicial review of the assessment in these types of situations. Thus, a taxpayer may not be able to obtain judicial review of tax liabilities and penalties by a bankruptcy court. Moreover, if the tax assessment prompted the bankruptcy, then any such review might be conducted after the liabilities are assessed.

## REASONS FOR CHANGE

### The Full Payment Rule May Force Taxpayers into Bankruptcy

Congress established the Board of Tax Appeals (a predecessor of the Tax Court) in 1924, in part, because it determined that taxpayers who are faced with incorrect assessments should not have to declare bankruptcy to obtain judicial review. The House report explained that “[t]he right of appeal after payment of the tax is an incomplete remedy, and does little to remove the hardship occasioned by an incorrect assessment... [which] sometimes forces taxpayers into bankruptcy...”<sup>56</sup> Because the same concerns exist today, taxpayers who cannot pay should be able to obtain judicial review without declaring bankruptcy.<sup>57</sup>

### The Full Payment Rule Discriminates Against Those Who Cannot Pay

Supreme Court Justice Whittaker’s dissent in *Flora II* explained how the full payment rule discriminates against taxpayers who cannot pay, as follows:

Where a taxpayer has paid ... a part only of an illegal assessment and is unable to pay the balance within the two-year period of limitations, he would be deprived of any means of establishing the invalidity of the assessment and of recovering the amount illegally collected from him, unless it be held, ... that full payment is not a condition upon the jurisdiction of District Courts to entertain suits for refund. Likewise, taxpayers who pay assessments in

53 See 11 U.S.C. § 505(a)(1) (bankruptcy courts “may” review the “amount or legality of any tax, any fine or penalty relating to a tax, or any addition to tax, whether or not previously assessed, whether or not paid...”); 11 U.S.C. § 505(a)(2)(A) (barring review “if such amount or legality was contested before and adjudicated by a judicial or administrative tribunal of competent jurisdiction before the commencement of the case under this title”); *In re Wyly*, 552 B.R. 338 (N.D. Tex. 2016) (reviewing unpaid assessable penalties under IRC §§ 6038(c)(4)(B) and 6677(d)).

54 See, e.g., *In re Luongo*, 259 F.3d 323, 330 (5th Cir. 2001).

55 See, e.g., *In re New Haven Projects Ltd. Liab. Co.*, 225 F.3d 283, 289 (2d Cir. 2000) (affirming abstention in Title 11 because “the amount of unsecured debt was *de minimis*...[and review of the tax issue] would only benefit the Debtor and [its] affiliates...”); *In re Hinsley*, 69 F. App’x 658 (5th Cir. 2003) (unpublished) (reversing the district court’s decision not to abstain because “the only parties likely to benefit from the resolution of a debtor’s dispute with the taxing authority are the debtor and his lienholder on property that is not a part of the estate”); *In re Perry*, 113 A.F.T.R.2d (RIA) 1370 (M.D. Ala. 2014) (abstaining because “the remaining issues concerning the extent of the liability of the debtor to the IRS and the determination of the extent of the tax lien do not affect the unsecured creditors...”); *In re Dees*, 369 B.R. 676, 680 (N.D. Fla. 2007) (“many courts have concluded that abstention is generally appropriate in no-asset Chapter 7 cases since the distribution to creditors is not affected.”).

56 H.R. REP. NO. 68-179, 7 (1924) (quoted by *Flora II*, 362 U.S. at 159); Revenue Act of 1924, 43 Stat. 253, 297-336 (1924) (establishing the Board of Tax Appeals).

57 As noted above, however, even bankruptcy may not provide an opportunity for judicial review of a tax dispute because a bankruptcy court is likely to abstain if the outcome would not affect the taxpayer’s other creditors.

installments would be without remedy to recover early installments that were wrongfully collected should the period of limitations run before the last installment is paid.<sup>58</sup>

This policy concern is as true today as it was in 1960. Taxpayers should not be left without a remedy just because they cannot afford to fully pay an illegal assessment quickly.

Even when taxpayers who cannot afford to pay receive notices of deficiency, which grant access to the Tax Court, the full payment rule discriminates against them by limiting their choice of forum. The choice of forum can be a tactical decision. For example, a person filing in district court may be entitled to a trial by jury, whereas no jury trial is available in the Tax Court or the Court of Federal Claims.<sup>59</sup> Decisions by the Court of Federal Claims are appealable to the Court of Appeals for the Federal Circuit, whereas decisions by the Tax Court and the district courts are appealable to other circuit courts.<sup>60</sup> Considerations about whether to pay the disputed liability and claim overpayment interest or risk liability for underpayment interest may also come into play.<sup>61</sup> Although low income taxpayers may not be able to afford representation in more formal proceedings, *pro bono* representation may be available.<sup>62</sup> Moreover, there does not appear to be a good reason to give a choice of forum only to wealthy taxpayers and those with small assessments that they can pay.

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58 *Flora II*, 362 U.S. at 195-96 (J. Whittaker, dissenting).

59 See, e.g., 28 U.S.C. § 2402 (jury trials in district courts); *Statland v. United States*, 178 F.3d 465 (7th Cir.1999) (no right to jury trial in Tax Court or Court of Federal Claims).

60 IRC § 7482; 28 U.S.C. §§ 1291-1295.

61 See, e.g., IRC § 6621(a) (underpayment and overpayment interest). In general, the government charges interest on underpayments and pays interest on overpayments at the same rate, however, it pays less interest on corporate overpayments than it charges on corporate underpayments. *Id.* Taxpayers who are able to pay can choose whether they would prefer to pay first and potentially earn overpayment interest, or litigate first and potentially owe underpayment interest.

62 See IRC § 7526 (authorizing grants to low income taxpayer clinics (LITCs)). In 2017, LITCs and their volunteers represented low income taxpayers (and appeared) in 1,013 cases before the Tax Court and in 41 cases in other Federal courts. TAS analysis of Form 13424K for grant year 2017 (Sept. 6, 2018); National Taxpayer Advocate, *Low Income Taxpayer Clinic Program Celebrates 20th Anniversary*, NTA BLOG (Aug. 1, 2018), <https://taxpayeradvocate.irs.gov/news/nta-blog-low-income-taxpayer-clinic-program-celebrates-20th-anniversary>.

### Pre-payment Review Poses No Risk to the Existence of Government

In *Flora I*, the Supreme Court justified the harsh results of the full payment rule by citing *Cheatham* and other cases from the 1800s.<sup>63</sup> Decided in 1875, *Cheatham* explained:

If there existed in the courts, State or National, any general power of impeding or controlling the collection of taxes, or relieving the hardship incident to taxation, the very **existence of the government** might be placed in the power of a hostile judiciary. (Emphasis added.)<sup>64</sup>

These may have been legitimate concerns in the 1800s. In the 1700s, the perception that sympathetic local juries in America were refusing to be impartial in customs disputes led the British Parliament to shift all types of revenue litigation to courts sitting without juries.<sup>65</sup> In the absence of a full payment rule, taxpayers could have used the same tactic of filing suits in district courts before sympathetic local juries against the federal government. This threat was exacerbated by the economic state of the federal and state governments at the time. Indeed, in 1790, the federal government had defaulted on its debt obligations, and between 1873 and 1884, ten states had too.<sup>66</sup> In 1880, a taxpayer tried to use this very tactic—the taxpayer waited for the government to sue to collect, then asked the district court judge to instruct the jury to decide if the tax was constitutional. Afterward, the taxpayer appealed the decision to the Supreme Court.<sup>67</sup> This was not a frivolous argument because a few years later, in 1895, the Supreme Court held that portions of the income tax were unconstitutional.<sup>68</sup> Thus, there was at least a possibility that local courts could be used to choke off federal revenue.

This risk was higher in the 1800s because the tax base was narrow, with most revenues coming from high income individuals and businesses. Before 1942, the government collected more in excise taxes

63 *Flora I*, 357 U.S. at 68 (“It is essential to the honor and orderly conduct of the government that its taxes should be promptly paid,” quoting *Cheatham v. United States*, 92 U.S. 85 (1875)). Although *Flora* did not repeat the “existence of government” rationale, *Cheatham* is mentioned seven times in *Flora I* and 20 times in *Flora II*. For a discussion of how Congress has increasingly provided taxpayers with procedural protections, overriding the sovereign’s ancient power to require immediate payment of taxes, see Nina E. Olson, 2010 Erwin N. Griswold Lecture Before the American College of Tax Counsel, *Taking the Bull by Its Horns: Some Thoughts on Constitutional Due Process in Tax Collection*, 63 TAX LAW. 227 (2010).

64 *Cheatham v. United States*, 92 U.S. 85, 89 (1875). See also, *Springer v. United States*, 102 U.S. 586, 594 (1880) (“The prompt payment of taxes is always important to the public welfare. It may be vital to the existence of a government.”). Once the “government existence” rationale had been expressed in *Cheatham*, similar reasons were recited in other cases without further examination. See, e.g., *Phillips v. Comm’r*, 283 U.S. 589, 595 (1931) (“Property rights must yield provisionally to governmental need.” Citing *Cheatham*); *Bull v. United States*, 295 U.S. 247, 259-60 (1935) (“taxes are the life-blood of government, and their prompt and certain availability an imperious need. Time out of mind, therefore, the sovereign has resorted to more drastic means of collection...”). For a discussion of Congress’s decision to expand procedural protections notwithstanding these ancient cases, see Nina E. Olson, 2010 Erwin N. Griswold Lecture Before the American College of Tax Counsel, *Taking the Bull by Its Horns: Some Thoughts on Constitutional Due Process in Tax Collection*, 63 TAX LAW. 227 (2010). For a discussion of the historical basis for similar concerns which lead to the Anti-Injunction Act and how they have abated, see Kristin E. Hickman & Gerald Kerska, *Restoring the Lost Anti-Injunction Act*, 103 VA. L. REV. 1683, 1719-1725 (2017).

65 See *United States v. Stein*, 881 F.3d 853, 859-860 (2018) (J. Pryor concurring).

66 See Carmen M. Reinhart, *This Time Is Different Chartbook: Country Histories on Debt, Default, and Financial Crises* 116 Nat’l Bureau Econ. Res. (NBER), Working Paper No. 15815 (Mar. 2010), <http://www.nber.org/papers/w15815> (figure 66a). The federal government had another technical default after 1933 when Congress passed a resolution indicating it would not honor the “gold clause” in its bonds, which provided for repayment in gold. *Id.*; House Joint Resolution 192 (June 5, 1933). Although the Supreme Court held the government’s actions were unlawful, it did not provide a remedy because it could not quantify the damages. See *Perry v. United States*, 294 U.S. 330 (1935).

67 See *Springer v. United States*, 102 U.S. 586 (1880).

68 See *Pollock v. Farmers’ Loan & Trust Co.*, 157 U.S. 429 (1895) (holding that income taxes on rent, interest and dividends were unconstitutional direct taxes because they were not apportioned among the states in accordance with the population).

than in either individual or corporate income taxes,<sup>69</sup> and in 1895, only the rich paid income taxes, as those with less than \$4,000 (over \$103,000 in today's dollars) in income were exempt.<sup>70</sup> Moreover, there was no broad-based wage withholding or similar pre-payment requirement.<sup>71</sup> Because there were fewer taxpayers, if a significant number filed suit before paying in local courts with local juries, they might have been able to threaten the federal government's very existence.

These historical concerns have subsided because: (1) the 16th Amendment was ratified in 1913, settling questions about the constitutionality of the income tax; (2) Congress increasingly delegated authority to Treasury to issue debt without specific authorization between 1917 and 1939, easing liquidity concerns;<sup>72</sup> (3) the federal government abandoned the gold standard in 1933 so that it could devalue the currency and pay its debts by printing money;<sup>73</sup> and (4) Congress substantially broadened the tax base in 1942, as shown in Figure 2.3.1, and adopted pre-payment mechanisms reducing its dependence on a relatively small number of taxpayers who might sue instead of paying.<sup>74</sup>

69 See Office of Management and Budget (OMB), *Historical Tables* (Table 2.2 - Percentage Composition of Receipts by Source: 1934-2023), <https://www.whitehouse.gov/omb/historical-tables/>.

70 See *Pollock v. Farmers' Loan & Trust Co.*, 157 U.S. 429, 444 (1895) ("The rate of taxation upon corporations and associations is in excess of the rate imposed upon individuals and associations. Persons having incomes of \$4,000 or under pay nothing; corporations having like incomes pay two per cent. Persons having incomes of over \$4,000 pay on the excess."). According to the inflation calculator at the Bureau of Labor Statistics (BLS) \$4,000 in 1913 (the earliest period available) would be worth \$103,036 as of September 2018. BLS, *CPI Inflation Calculator*, <https://data.bls.gov/cgi-bin/cpicalc.pl>. For a detailed discussion of the transformation of the income tax from a class tax to a mass tax and the automation that went along with it, see National Taxpayer Advocate 2011 Annual Report to Congress vol. 2, 1-62 (Study: *From Tax Collector to Fiscal Automaton: Demographic History of Federal Income Tax Administration, 1913-2011*).

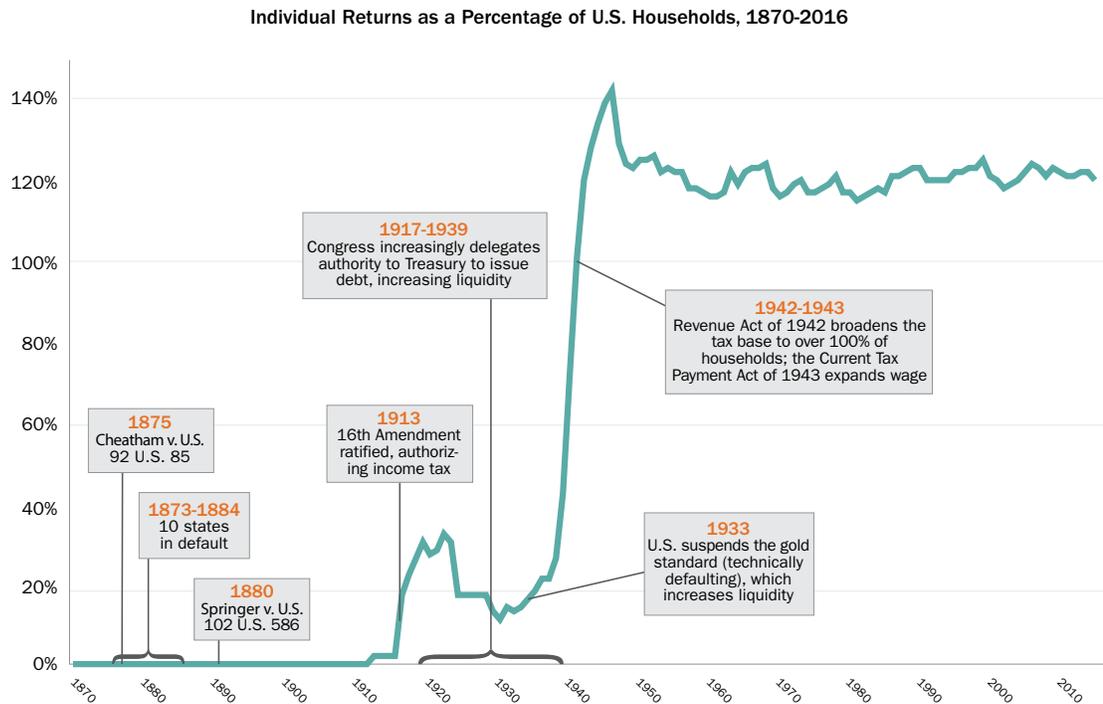
71 Revenue Act of 1942, ch 619, § 172, 56 Stat. 798, 887-92 (1942) (adopting wage withholding for a "Victory" tax); Current Tax Payment Act of 1943, ch. 120, § 2, 57 Stat. 126, 128 (1943) (expanding wage withholding to the income tax). For a detailed discussion of this evolution see, e.g., Anuj C. Desai, *What a History of Tax Withholding Tells Us About the Relationship Between Statutes and Constitutional Law*, 108 Nw. U. L. Rev. 859, 896-902 (2014); Carolyn C. Jones, *Class Tax to Mass Tax: The Role of Propaganda in the Expansion of the Income Tax During World War II*, 37 BUFF. L. REV. 685, 695-699 (1989); Kristin E. Hickman & Gerald Kerska, *Restoring the Lost Anti-Injunction Act*, 103 Va. L. Rev. 1683 (2017).

72 See, e.g., George Hall & Thomas Sargent, *Brief History of US Debt Limits Before 1939*, 115 PNAS 2942-45 (Mar. 20, 2018), <http://www.pnas.org/content/115/12/2942>. Before 1917, each bond issuance had to be approved by Congress.

73 House Joint Resolution 192 (June 5, 1933).

74 Revenue Act of 1942, ch. 619, 56 Stat. 798 (1942). IRS, *Historical Fact Book, A Chronology 1646-1992*, 136 (1997) (noting the Revenue Act of 1942 "broadened the tax base by over 100%"); IRS, Pub. 447, *A History of the Internal Revenue Service, Income Taxes, 1862-1962*, 23 (1962) ("Taxpayers with income under \$5,000 accounted for only 10 percent of the revenue collected in 1939. By 1948, these taxpayers accounted for over 50 percent of revenue collected. In 1939, 700,000 returns accounted for 90 percent of the total tax liability. By 1948, this number had climbed to 25 million returns."). See also National Taxpayer Advocate 2011 Annual Report to Congress vol. 2, 45 (Study: *From Tax Collector to Fiscal Automaton: Demographic History of Federal Income Tax Administration, 1913-2011*) (concluding "[I]n the first quarter-century, income tax was a concern largely to wealthy, white businessmen, doctors, and lawyers, who dealt with their Collectors, who in turn were locally prominent political appointees. All this changed during the second phase, when the exigency of World War II transformed the income tax into a mass revenue generator...").

**FIGURE 2.3.1, The Risks to the Existence of Government Declined as It Broadened the Tax Base<sup>75</sup>**



Congress must have deemed the risk of pre-payment review (at least in the absence of a local jury) to be minimal by 1924 when it established the Board of Tax Appeals (BTA) (*i.e.*, the predecessor of the Tax Court) as a pre-payment forum to hear most tax disputes—or at the latest by 1969 when it established the Tax Court as an Article I court, independent from the executive branch.<sup>76</sup> In 1998, when Congress established the right to a CDP hearing, it increased access to pre-payment judicial review by the Tax Court.<sup>77</sup> Thus, Congress must not have been concerned that increasing pre-payment review by the Tax Court could threaten the existence of government.

<sup>75</sup> TAS analysis of data from the IRS Statistics of Income Division, the U.S. Bureau of the Census, and the Federal Reserve Bank of St. Louis (June 2018) (on file with TAS). The number of tax returns exceeds the number of households because more than one return can be filed by people living in a single Census-defined household. U.S. Census, Glossary, <https://www.census.gov/glossary/#term> (last visited, Oct. 31, 2018) (defining a household). For example, adult children and extended family may file separate returns but live in the same Census-defined household.

<sup>76</sup> Revenue Act of 1924, 43 Stat. 253, 297-336 (1924) (establishing the BTA). Before 1969, the Tax Court was an executive branch agency. Tax Reform Act of 1969, Pub. L. No. 91-172, § 951, 83 Stat. 487, 730 (codified as IRC § 7441). While reciting concerns about dollars at stake in various courts, the *Flora* decisions were primarily based on decisions by prior courts and the assumptions of prior Congresses that full payment was required. See *Flora I*, 357 U.S. at 69 (“there does not appear to be a single case before 1940 in which a taxpayer attempted a suit for refund of income taxes without paying the full amount the Government alleged to be due”); *Flora II*, 362 U.S. at 167 (acknowledging that such cases existed, but stating “[i]f we were to overturn the assumption upon which Congress has acted, we would generate upon a broad scale the very problems Congress believed it had solved” and citing legislative history that characterized the full payment rule as present law).

<sup>77</sup> RRA 98, Pub. L. No. 105-206 § 3401, 112 Stat. 685, 747 (1998) (codified at IRC §§ 6320 and 6330).

Similarly, legislation to eliminate any remaining gaps in this broad access to pre-payment judicial review would not pose a threat to the existence of the government. Moreover, the existence of the government has never depended on the swift collection of penalties.

In *Flora II*, the Supreme Court acknowledged that judicial precedent for the full payment rule was mixed, but its main policy justification for the rule was that allowing taxpayers to litigate in a pre-payment forum would pose risks to the “public purse.”<sup>78</sup> The Court also worried about Tax Court cases flooding the district courts with frivolous claims by those hoping to settle for pennies on the dollar.<sup>79</sup> Judicial review of frivolous claims can help taxpayers to feel they have been heard and give a court the opportunity to clarify both substantive and procedural issues. However, the Court’s concerns about them are now addressed by the penalties for frivolous submissions and refund claims.<sup>80</sup>

In addition, the Court assumed that the full payment rule would not result in hardship because taxpayers could “appeal the deficiency to the Tax Court without paying a cent.”<sup>81</sup> To the extent it could result in a hardship, the Court suggested it was “a matter for Congress,” inviting legislation to fill in those gaps.<sup>82</sup>

### The Full Payment Rule Applies to More Penalties Today

The gaps in pre-payment judicial review have grown. When *Flora II* was decided in 1960, there were only four assessable penalties, two of which were divisible: (1) the trust fund recovery penalty (IRC § 6672), which is divisible (as noted above), (2) the penalty for delaying Tax Court proceedings (IRC § 6673), (3) the penalty for furnishing a fraudulent statement to employees (IRC § 6674), and (4) the penalty for excessive fuel tax refund claims (IRC § 6675), which is also divisible.<sup>83</sup> Today, by contrast, Subchapter B of Chapter 68 contains over 50 different assessable penalties (*i.e.*, the penalties

78 *Flora II*, 362 U.S. at 175 (“the Government has a substantial interest in protecting the public purse, an interest which would be substantially impaired if a taxpayer could sue in a District Court without paying his tax in full”).

79 *Flora II*, 362 U.S. at 646-47 n.41. Indeed, after the Tax Court was granted jurisdiction in CDP appeals, the IRS reported that a small percentage of CDP litigants brought frivolous cases that drained a disproportionate amount of resources. See Joint Committee on Taxation (JCT), JCX-53-03, *Report of the JCT Relating to the Internal Revenue Service as Required by the IRS Reform and Restructuring Act of 1998* Appendix at 22 (May 20, 2003) (IRS letter to JCT) (“About 5% or 906 cases involve frivolous issue taxpayers. However ... [f]rivolous claims occupy a disproportionate share of time over claims from taxpayers having substantive issues.”). However, even some frivolous CDP cases have shed light on substantive and procedural issues. See, e.g., *Ryskamp v. Comm’r*, 797 F.3d 1142 (D.C. Cir. 2015).

80 See, e.g., IRC §§ 6702 (\$5,000 penalty for frivolous submissions to the IRS, including requests for a CDP hearing); 6673 (authorizing sanctions and costs for frivolous submissions to a court); 7482 (same); Rule 5(c), Federal Rules of Civil Procedure (same); IRC § 6676 (penalty for excessive refund claims).

81 *Flora II*, 362 U.S. at 175. Indeed, the Supreme Court observed that “[t]he Board of Tax Appeals [the predecessor of the Tax Court] ... was created by Congress to provide taxpayers an opportunity to secure an independent review of the Commissioner of Internal Revenue’s determination of additional income and estate taxes by the Board in advance of their paying the tax found by the Commissioner to be due. Before the act of 1924 the taxpayer could only contest the Commissioner’s determination of the amount of the tax after its payment.” *Flora I*, 357 U.S. at 74 n. 20.

82 *Flora I*, 357 U.S. at 76.

83 Internal Revenue Code of 1954, Pub. L. No. 83-591, 68 Stat. 730, 828 (1954). The assessable penalty for excessive claims with respect to gasoline was enacted in 1956. Pub. L. No. 84-466, § 3, 70 Stat. 87, 90 (1956) (codified at IRC § 6675). The penalty for excessive fuel tax refund claims is divisible because it applies to each refund claim. Although there is no direct authority for this conclusion, it seems consistent with *Flora II* and the methodology employed by attorneys at the IRS for identifying divisible penalties. See, e.g., *Flora II*, 362 U.S. 171, n.37 (“excise tax deficiencies may be divisible into a tax on each transaction or event.”). See also CCA 201315017 (2013) (concluding that the penalty for failure to file certain information returns or payee statement was divisible).

between IRC §§ 6671 and 6725).<sup>84</sup> As the number of assessable penalties has risen, the fact that they cannot be contested in court before they are assessed and fully paid has become increasingly problematic.<sup>85</sup>

### Procedural Barriers Can Cause Low Income Taxpayers to Miss the Opportunity to Petition the Tax Court

Before making an audit assessment, the IRS is generally required to send the taxpayer a notice of deficiency, which gives the taxpayer 90 days to petition the Tax Court.<sup>86</sup> It would be easier for low income taxpayers to understand these notices and how best to respond if someone explained them in person or by phone. However, the IRS generally audits low income and middle income taxpayers by correspondence or by using even more automated procedures that the IRS does not regard as audits (called “unreal audits”).<sup>87</sup> Confusing IRS correspondence, illiteracy, language barriers, and unequal access to competent tax professionals can cause taxpayers—particularly low income taxpayers—to miss the deadline for filing a petition.<sup>88</sup> Indeed, a 2007 TAS study found more than one-quarter of taxpayers receiving an EITC audit notice did not understand that the IRS was auditing their return, almost 40 percent did not understand what the IRS was questioning, and only about half of the respondents felt that they knew what they needed to do.<sup>89</sup> In other words, there are circumstances in which deficiency procedures do not give taxpayers a realistic opportunity to petition the Tax Court.

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- 84 Assessable penalties now include among other things, the penalties for: failure to file timely and accurate information returns (e.g., IRC §§ 6677, 6679, 6682, 6693, 6698, 6699, 6707, 6707A, 6710, 6723), erroneous claims for refund (IRC § 6676), failure to disclose various things to various people or disclosing too much (e.g., IRC §§ 6685, 6705, 6706, 6709, 6711, 6712, 6713, 6714, 6720C, 6721, 6722, 6725), aiding and abetting understatements (IRC § 6701), promoting tax shelters (IRC § 6700), making frivolous tax submissions (IRC § 6702), and the failure to keep certain records (e.g., IRC §§ 6704, 6708).
- 85 Although some assessable penalties adopted after 1960 are divisible, many are not. Compare CCA 201150029 (2011) (IRC § 6677 not divisible); *Christian Laymen in Partnership, Ltd. v. United States*, 1989 U.S. Dist. LEXIS 15932 (W.D. Okla. Dec. 29, 1989) (IRC § 6698 not divisible); *Larson v. United States*, 888 F.3d 578 (2d Cir. 2018) (IRC § 6707 not divisible) with CCA 201315017 (2013) (IRC §§ 6721 and 6722 divisible) and CCA 200646016 (2006) (IRC § 6708 divisible). For many others, the divisibility issue has not been addressed. As one treatise explained, “[I]t is not always easy to determine whether a tax is divisible.” Michael I. Saltzman, *IRS Practice and Procedure* ¶11.11[1][c] (Revised 2d ed. July 2017).
- 86 IRC § 6213. The 90-day period becomes 150 days if the notice is addressed to a person outside the U.S. *Id.*
- 87 For fiscal year (FY) 2017, 71 percent of the IRS’s audits were conducted by correspondence — a figure that rises to 81 percent for individual returns with total positive income (TPI) of less than \$200,000 and falls to 53 percent for individual returns with TPI of more than \$200,000. IRS Data Book, 2017, Pub. 55B, 22 (Mar. 2018) (Table 9a). “Unreal audit” procedures include Automated Underreporter (AUR), Automated Substitute for Return (ASFR), math and clerical errors, and other automated programs. See, e.g., National Taxpayer Advocate 2017 Annual Report to Congress 49-63 (Most Serious Problem: *Audit Rates*); National Taxpayer Advocate 2016 Annual Report to Congress 27-29 (Special Focus: *IRS Future State: The National Taxpayer Advocate’s Vision for a Taxpayer-Centric 21st Century Tax Administration*); National Taxpayer Advocate 2011 Annual Report to Congress 24 (Introduction to Revenue Protection Issues: *As the IRS Relies More Heavily on Automation to Strengthen Enforcement, There is Increased Risk It Will Assume Taxpayers Are Cheating, Confuse Taxpayers About Their Rights, and Sidestep Longstanding Taxpayer Protections*); Nina E. Olson, *What’s an Audit, Anyway?*, NTA BLOG (Jan. 25, 2012), <https://taxpayeradvocate.irs.gov/news/what's-an-audit-anyway?category=Tax News>.
- 88 National Taxpayer Advocate 2007 Annual Report to Congress vol. 2, 100, 103-104. By comparison, when the IRS audited EITC claimants for its National Research Program, which utilized face-to-face and telephonic communications, 85 percent participated in the audit. See IRS, Pub. 5162, *Compliance Estimates for the Earned Income Tax Credit Claimed on 2006-2008 Returns* iii, 6, 8 (Aug. 2014). For a detailed description about why low income taxpayers miss these deadlines along with a similar proposal for reform, see Carlton M. Smith, *Let the Poor Sue For Refund Without Full Payment*, 125 TAX NOTES 131 (Oct. 5, 2009).
- 89 National Taxpayer Advocate 2007 Annual Report to Congress vol. 2, 100, 103-104. Similarly, a more recent survey of Schedule C taxpayers who had been audited found that only 38.8 percent for those audited by mail knew that they had been audited. National Taxpayer Advocate 2017 Annual Report to Congress vol. 2 148, 163-64 (Matthias Kasper, Sebastian Beer, Erich Kirchler & Brian Erard, *Audits, Identity Theft Investigations, and Taxpayer Attitudes: Evidence from a National Survey*).

Moreover, low income taxpayers did not have the same involvement in tax return filing and administration in 1960 when *Flora II* was decided. It was not until 1975 that Congress enacted the EITC as a means-tested tax credit to assist the working poor, and the EITC remained the only refundable tax credit until the Child Tax Credit was enacted in 1997.<sup>90</sup> After 1997, Congress increasingly began using the tax system to distribute benefits to low and middle income taxpayers, such as Economic Stimulus Payments, the Making Work Pay Credit, the Health Coverage Tax Credit, the First-Time Homebuyer Credit, the COBRA Premium Assistance Credit, the American Opportunity Tax Credit, the Adoption Credit, the Small Business Health Care Tax Credit, and the Premium Assistance Tax Credit.<sup>91</sup> In 2017, the maximum EITC was \$6,318 and 27 million eligible workers and families received about \$65 billion in EITC.<sup>92</sup> Moreover, in 2017 Congress doubled the maximum Child Tax Credit to \$2,000, further increasing interactions between low and middle income taxpayers and the tax system.<sup>93</sup>

In addition, in 1960 the automation required for “unreal” audits did not exist. For example, it was not until 1989 that the IRS developed the first prototype of the “automated underreporter” matching system.<sup>94</sup> Thus, while the government’s interest in keeping taxpayers out of court to protect the public purse has declined, the need for judicial review by low income taxpayers has increased.

## EXPLANATION OF RECOMMENDATIONS

### Clarify That the Full Payment Rule Does Not Apply to Liabilities Unless They Were Subject to Review by the Tax Court

Members of the Supreme Court and others have operated under the assumption that the full payment rule only applied where the taxpayer had an opportunity to petition the Tax Court to review them.<sup>95</sup> However, Congress has sometimes carved out exceptions to the full payment rule based on the assumption that it applied to assessable penalties that could not have been appealed to the Tax Court before payment.<sup>96</sup> Based in part on Congress’s assumptions, the U.S. Court of Appeals for the Second

90 See Pub. L. No. 94-12, § 204, 89 Stat. 26, 30 (1975) (codifying the earned income tax credit (EITC) at IRC § 32); Pub. L. No. 105-34, § 101, 111 Stat. 788, 796 (1997) (codifying the child tax credit at IRC § 24).

91 See, e.g., Congressional Budget Office, *Refundable Tax Credits* (2013), [http://www.cbo.gov/sites/default/files/cbofiles/attachments/RefundableTaxCredits\\_One-Col.pdf](http://www.cbo.gov/sites/default/files/cbofiles/attachments/RefundableTaxCredits_One-Col.pdf); National Taxpayer Advocate 2011 Annual Report to Congress vol. 2, 43-44.

92 IRS, *EITC Fast Facts* (Jan. 29, 2018), <https://www.eitc.irs.gov/partner-toolkit/basic-marketing-communication-materials/eitc-fast-facts/eitc-fast-facts>.

93 See Pub. L. No. 115-97, § 11022, 131 Stat. 2054, 2073 (2017) (codified at IRC § 24). If the IRS offsets these benefits over a number of years, then by the time these offsets fully pay the liability so that the taxpayer can challenge the underlying assessment, he or she may not be able to recover the offsets from the early years, as discussed above.

94 IRS, *Historical Fact Book, A Chronology 1646-1992*, 232 (1997).

95 *Flora II*, 362 U.S. at 175 (“This contention [requiring taxpayers to pay the full assessments before bringing suits will subject some of them to great hardship] seems to ignore entirely the right of the taxpayer to appeal the deficiency to the Tax Court without paying a cent.”); *Laing v. United States*, 423 U.S. 161, 208-09 (1976) (Blackmun, J., dissenting) (“the full-payment rule applies only where... the taxpayer has access to the Tax Court for redetermination prior to payment.”). Indeed, critics of the *Larson* decision (discussed above), which applied the full payment rule to assessable penalties, have pointed out that the majority of the Supreme Court in *Laing* did not disagree with J. Blackmun’s interpretation of *Flora II*, which would have limited the full payment rule to liabilities that could have been appealed to the Tax Court. See, e.g., Andrew Velarde, *Taxpayer Asks Circuit for Do-Over on Full Payment Rule Holding*, 2018 TNT 113-5 (June 12, 2018) (quoting Carlton Smith). Similarly, Mr. Larson pointed out that the Solicitor General agreed with J. Blackmun. See *Larson v. United States*, Docket No. 17-502 (2d Cir. 2018) (petition for rehearing), *reprinted as, Individual Seeks Rehearing In Second Circuit Full Payment Rule Case*, 2018 TNT 113-11 (June 12, 2018).

96 See IRC §§ 6694(c), 6703(c).

Circuit recently confirmed that the full payment rule applies to assessable penalties.<sup>97</sup> If Congress decides to retain the full payment rule, it should clarify that the rule only applies where the taxpayer has received a notice of deficiency and had an opportunity to participate in a pre-payment review of the dispute by the Tax Court. If this or any similar recommendation is adopted, Congress should also provide that the IRS cannot collect the unpaid portion of a liability while refund litigation is pending concerning the same or similar issues, even if attributable to different periods.<sup>98</sup> The doctrines of *res judicata* and *collateral estoppel* should help to ensure that IRS does not re-litigate the same issues with respect to unpaid liabilities.<sup>99</sup>

By itself, this recommendation would not give the Tax Court jurisdiction to review assessable penalties. As noted below, we recommend that Congress authorize the Tax Court to review them. Expanding the Tax Court's jurisdiction would reduce litigation before the district courts and the Court of Federal Claims because a taxpayer could not litigate the same issue in both fora.<sup>100</sup>

### Expand the Definition of Full Payment

The dissenters in *Flora II* worried that the refund limitations period could lapse while a taxpayer was trying to fully pay a liability that he or she wanted to dispute.<sup>101</sup> If Congress decides to retain the full payment rule, it should address this concern. It could do so by treating a liability as fully paid (for purposes of this rule) at the earlier of when the taxpayer has paid something and (a) the IRS classifies the account as currently not collectible due to hardship,<sup>102</sup> or (b) the taxpayer enters into an installment agreement.<sup>103</sup>

### Expand the Tax Court's Jurisdiction to Hear Non-Deficiency Cases

If this recommendation is adopted, the Tax Court would have jurisdiction to review liabilities proposed by the IRS, where the taxpayer did not receive a notice of deficiency (*e.g.*, both the explicitly and implicitly assessable penalties). Before assessing assessable penalties, the IRS would be required to send the taxpayer a non-deficiency notice, which would be similar to a notice of deficiency, and give

97 See *Larson v. United States*, 888 F.3d 578 (2d Cir. 2018), *aff'g* 118 A.F.T.R.2d (RIA) 7004 (S.D.N.Y., 2016), *petition for rehearing filed*, Docket No. 16-CV-00245 (June 8, 2018). For a discussion of this case, see Significant Cases, *infra*. Practitioners have called for legislation in response to this decision. See, *e.g.*, Lawrence Hill & Richard Nessler, *IRS Penalty Assessments Without Due Process?*, 159 TAX NOTES 1763 (June 18, 2018).

98 A full repeal of the full payment rule and similar proposals are not necessarily inconsistent with the Anti-Injunction Act (IRC § 7421), or the tax exception to the Declaratory Judgment Act (28 U.S.C. § 2201) if the taxpayer has paid some amount of the liability before filing suit and if the suit does not prevent the government from collecting unpaid amounts. If the full payment rule is repealed or limited, however, Congress should make clear that the suits it intends to authorize do not violate IRC § 7421 or 28 U.S.C. § 2201 with respect to unpaid amounts that will be decided in connection with the taxpayer's suit. For example, Congress could expand the scope of IRC § 6331(i) which prevents the IRS from levying while a taxpayer is litigating a divisible tax and IRC § 6331(i)(4)(B) which allows a court to enforce this rule by enjoining collection, notwithstanding IRC § 7421. See, *e.g.*, *Beard v. United States*, 99 Fed. Cl. 147 (Fed. Cl. 2011) (enjoining the government's collection action).

99 See, *e.g.*, CCDM 34.5.1.1.2.2.4 (Aug. 11, 2004). The IRS authorizes its lawyers to make permissive counterclaims for the unpaid portions of divisible taxes where the counterclaim either relates to the periods in suit or involves the same or similar issues. CCDM 34.5.1.1.2.5 (Aug. 11, 2004).

100 See IRC § 7422(e).

101 *Flora II*, 362 U.S. at 195-96 (J. Whittaker, dissenting).

102 IRC § 6343(a)(1)(D) and Treas. Reg. § 301.6343-1(b)(4) require the IRS to release a levy that is creating an economic hardship. Rather than pursuing collection actions that would be unproductive, the IRS reports accounts as currently not collectible when the taxpayer has no assets or income which are, by law, subject to levy. See Policy Statement 5-71, IRM 1.2.14.1.14 (Nov. 19, 1980).

103 For a similar proposal, see Carlton M. Smith, *Let the Poor Sue For Refund Without Full Payment*, 125 TAX NOTES 131 (Oct. 5, 2009). A similar rule applies to unpaid installments of estate tax under IRC § 7422(j).

the taxpayer a similarly reasonable period to file a petition with the Tax Court. As with a notice of deficiency, the IRS would be allowed to assess and collect the liabilities only after the Tax Court's review is complete or the period for filing suit has expired.

This proposal would give taxpayers access to a specialized and convenient judicial form. The Tax Court is less formal than a district court or the Court of Federal Claims. Since its inception, the Tax Court has been particularly accessible to *pro se* taxpayers and those wishing to be represented by non-attorneys.<sup>104</sup> Moreover, adjustments to the Tax Court's rules, jurisdiction, and Low Income Taxpayer Clinics and state and local bar association referral practices (*e.g.*, calendar call programs) have made it even more informal and accessible.<sup>105</sup> Over 70 percent of all Tax Court petitions were filed by self-represented taxpayers in 2015.<sup>106</sup>

### Alternatively, Expand the Tax Court's Jurisdiction Under CDP

In lieu of expanding the Tax Court's jurisdiction to cover non-deficiency cases as recommended above, Congress could consider expanding its CDP jurisdiction to cover liabilities not subject to deficiency procedures, even if the taxpayer had an opportunity for an *administrative* review by Appeals. While this alternative would provide an opportunity for judicial review of assessable penalties, judicial review would only occur after they are assessed by the IRS.

Once a liability is assessed, the IRS may begin collection (*e.g.*, by offsetting refunds and issuing a lien notice), and the taxpayer's access to credit may be constrained. It is not clear why a taxpayer should not have the opportunity to appeal an IRS-asserted liability in court before the IRS assesses it, damages the taxpayer's credit, and begins the collection process. Nonetheless, an expansion of CDP could help to ensure that accessible penalties could be reviewed by a court before they are fully paid.

If Congress expands CDP, it should address several of its limitations. First, because the right to a CDP hearing is triggered by a lien or levy, a CDP appeal is not necessarily available to taxpayers whose liabilities are collected by offset (*e.g.*, refundable credits the taxpayer would otherwise have received in a subsequent year). Thus, Congress might want to require the IRS to send CDP notices before offsetting refundable tax credits and allow taxpayers to appeal the resulting determinations to the Tax Court.

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104 Deborah A. Geier, *The Tax Court, Article III, and the Proposal Advanced by the Federal Courts Study Committee: A Study in Applied Constitutional Theory*, CORNELL L. REV., n. 23 (July 1991).

105 See IRC § 7463; Tax Court Rule 174(b). See also Harold Dubroff & Brant J. Hellwig, *THE UNITED STATES TAX COURT, AN HISTORICAL ANALYSIS* 883-901 (2d Ed. 2014), [https://www.ustaxcourt.gov/book/Dubroff\\_Hellwig.pdf](https://www.ustaxcourt.gov/book/Dubroff_Hellwig.pdf); The Federal Courts Study Committee, *Report of The Federal Courts Study Committee* 70 (Apr. 2, 1990). For a summary of LITC activities to assist taxpayers before the Tax Court, see IRS Pub. 5066, *Assisting Taxpayers Face-to-Face with An Increasingly Automated Tax System*, LITC PROGRAM REPORT (Feb. 2018), <https://www.irs.gov/pub/irs-pdf/p5066.pdf>. For a discussion of Tax Court calendar call programs, see U.S. Tax Court, *Clinical, Student Practice & Bar Sponsored Calendar Call Program*, <https://www.ustaxcourt.gov/clinics.htm> (Aug. 6, 2018).

106 Hon. Peter J. Panuthos, *The United States Tax Court and Calendar Call Programs*, 68 TAX LAW. 439, 440 (2015).

Second, the Tax Court does not have jurisdiction to order refunds in CDP appeals (*e.g.*, to order refunds of amounts that had been paid or offset).<sup>107</sup> Accordingly, Congress might also want to expand its jurisdiction to clarify that it could determine overpayments in connection with these appeals.<sup>108</sup>

In addition, both the time for requesting a CDP hearing, and the time for filing a Tax Court petition after receipt of an unfavorable CDP determination from Appeals is relatively short—only 30 days, as compared to 90 days (or 150 days if addressed to a taxpayer overseas) after the IRS sends a notice of deficiency.<sup>109</sup> Moreover, unlike the notice of deficiency, the CDP notice and the CDP determination do not list the last day for the taxpayer to file the request for a hearing or to petition the Tax Court.<sup>110</sup> Congress should also address these problems in connection with any expansion of CDP (*e.g.*, by giving taxpayers as long to respond to a CDP notice as they have in responding to a notice of deficiency and listing that deadline on the notice).

Expanding the Tax Court’s jurisdiction will not open the floodgates to litigation. Between 2004 and 2017 only 1.41 percent of the taxpayers who received a CDP notice requested an administrative hearing (*i.e.*, 365,686 out of 25,991,970) and only 0.08 percent filed a petition with the Tax Court (*i.e.*, 20,248 out of 25,991,970).<sup>111</sup> Moreover, because these percentages include taxpayers with disputes about both collection alternatives and the underlying liability, we might expect this more limited expansion to increase the number of petitions by an even smaller fraction.

107 See, *e.g.*, *Greene-Thapedi v. Comm’r*, 126 T.C. 1 (2006) (holding the Tax Court lacked jurisdiction to consider overpayment in CDP appeal); *McLane v. Comm’r*, T.C. Memo. 2018-149 (same, even though the taxpayer had not received a notice of deficiency). For further discussion of these issues and the need for legislation, see, *e.g.*, Keith Fogg, *Tax Court Reiterates That It Lacks Refund Jurisdiction in Collection Due Process Cases*, PROCEDURALLY TAXING BLOG (Oct. 4, 2018), <http://procedurallytaxing.com/tax-court-reiterates-that-it-lacks-refund-jurisdiction-in-collection-due-process-cases/>.

108 For a legislative recommendation to address this problem, see National Taxpayer Advocate 2017 Annual Report to Congress 293-298 (Legislative Recommendation: *Amend IRC § 6330 to Allow the Tax Court Jurisdiction to Determine Overpayments*).

109 Compare IRC §§ 6330(a)(2)(C), (3)(B), and 6330(d)(1) with IRC §§ 6212, 6213. For an example of the problems this short period creates, see, *e.g.*, Carlton Smith, *Atuke v. Comm’r: A Clearly Unfair Dismissal for Lack of Jurisdiction Where the Taxpayer Had No Time to Timely File*, PROCEDURALLY TAXING BLOG (Apr. 19, 2016), <https://procedurallytaxing.com/atuke-v-commr-a-clearly-unfair-dismissal-for-lack-of-jurisdiction-where-the-taxpayer-had-no-time-to-timely-file-2/>. By the time the IRS mailed CDP notices to individuals in FY 2017, the average delinquency was about 751 days old, and a median of about 441 days old. TAS analysis of Individual Master File, Individual Accounts Receivable Dollar Inventory (Sept. 23, 2018). Observing that CDP cases take longer for the government to resolve than deficiency cases once they reach the Tax Court, some have argued that taxpayers should not have to respond more quickly in CDP cases than in deficiency cases. See Carlton Smith & Keith Fogg, *Tax Court Collection Due Process Cases Take Too Long*, 130 TAX NOTES 403 (Jan. 24, 2011); Carlton Smith & Keith Fogg, *Collection Due Process Hearings Should Be Expedited*, 125 TAX NOTES 919 (Nov. 23, 2009).

110 For a recommendation to address this problem, see National Taxpayer Advocate 2017 Annual Report to Congress 299-306 (Legislative Recommendation: *Amend IRC §§ 6320, 6330, and 6015 to Require That IRS Notices Sent to Taxpayers Include a Specific Date by Which Taxpayers Must File Their Tax Court Petitions, and Provide That a Petition Filed by Such Specified Date Will Be Treated As Timely*).

111 TAS analysis of CDP data (Sept. 5, 2018).

## Appendix: Summary of The Flora Decisions

After the IRS recharacterized a loss that Mr. Flora had incurred in 1950 as a capital loss (rather than an ordinary loss) and sent him a notice of deficiency, he did not timely petition the Tax Court. The IRS then assessed a \$28,908.60 deficiency. The taxpayer made payments totaling \$5,058.54, and then submitted a claim for refund, which the IRS disallowed. In 1956, he filed suit in the U.S. District Court for the District of Wyoming requesting a refund under the Tucker Act, 28 U.S.C. § 1346(a)(1). The Tucker Act authorized the court to hear suits for the recovery of:

*“any internal-revenue tax alleged to have been erroneously or illegally assessed or collected, or any penalty claimed to have been collected without authority or any sum alleged to have been excessive or in any manner wrongfully collected...”* [Emphasis added.]<sup>112</sup>

The District Court held that because the deficiency was not fully paid the court “should not maintain” the action, but it nonetheless entered a judgement for the government on the merits due to a conflict among the circuits about whether full payment was required.<sup>113</sup> On appeal, the Court of Appeals for the Tenth Circuit remanded the case with instructions to dismiss for lack of subject matter jurisdiction. It reasoned the legislative history of the Revenue Act of 1924, which established the Board of Tax Appeals (BTA, the predecessor of the Tax Court) suggested that the BTA was established as a pre-payment forum to mitigate the “hardship imposed on taxpayers by an inflexible ‘pay first, litigate later’ rule” and said “the Supreme Court has consistently indicated that full payment of a tax deficiency is a prerequisite to a judicial claim for refund.”<sup>114</sup> It also suggested that allowing taxpayers to pay a small portion of a deficiency and sue for a refund of that portion would undermine the requirement of IRC § 7422 that a taxpayer must make an administrative claim for refund before filing suit.

In 1958, in *Flora I* the Supreme Court affirmed with only one dissent. While acknowledging that the Tucker Act authorized the court to determine “any sum,” which could be construed as a clear grant of authority, it cited a “sharp division of opinion among the lower courts” as evidence that the language was ambiguous and said that because the Tucker Act is a waiver of sovereign immunity it had to be construed narrowly.<sup>115</sup> It agreed with the Tenth Circuit that the hardship Congress was attempting to alleviate when it subsequently created the BTA as a pre-payment forum was the hardship of having to fully pay a deficiency before filing suit under the Tucker Act. It discounted the taxpayer’s argument that BTA addressed another hardship faced by taxpayers who filed suit in a district court before fully paying—that the IRS could continue to collect the disputed liability during the litigation.<sup>116</sup>

The Court also relied on its decision in *Cheatham*, which was decided in 1875 before the Tucker Act was amended in 1921, and involved the limitations period for filing refund claims.<sup>117</sup> In *Cheatham*, the taxpayer argued that her filing was not late, in part, because she had no right of action until the tax

<sup>112</sup> 28 U.S.C. § 1346(a)(1).

<sup>113</sup> *Flora v. United States*, 142 F. Supp. 602, 604-05 (D. Wyo. 1956), remanded by 246 F.2d 929 (10th Cir. 1957), *aff’d*, *Flora I*, 357 U.S. 63 (1958), *aff’d*, *Flora II*, 362 U.S. 145 (1960).

<sup>114</sup> *Flora*, 246 F.2d 929, 930-31 (10th Cir. 1957) (quoting from *Old Colony Trust Co. v. Comm’r*, 279 U.S. 716 (1929) where the Court said “Before the act of 1924 [establishing the Board of Tax Appeals] the taxpayer could only contest the Commissioner’s determination of the amount of the tax after its payment”).

<sup>115</sup> *Flora I* at 65.

<sup>116</sup> *Id.* at 74. It also cited a statement in a House report for a bill that removed a dollar limitation from the Tucker Act that suggested that Congress assumed that full payment was required. *Id.* at 74-75.

<sup>117</sup> *Cheatham v. United States*, 92 U.S. 85, 89 (1875).

was fully paid. Although the Court accepted the taxpayer's assertion that she had no right of action until the tax was fully paid, it found reasons for why her filing was nonetheless late.<sup>118</sup> In *dicta*, the *Cheatham* Court discussed its understanding about the full payment rule and the policy reasons for the rule. After quoting this discussion from *Cheatham*, the Court said in *Flora I* that “[c]onsistent with that understanding, there does not appear to be a single case before 1940 in which a taxpayer attempted a suit for refund of income taxes without paying the full amount the Government alleged to be due.”<sup>119</sup> This statement was wrong. After a handful of cases were discovered,<sup>120</sup> the Court granted a petition for rehearing and issued *Flora II*, which provides a broader justification for its decision.

In *Flora II*, the Court discounted the argument that the Tucker Act's reference to the recovery of “any sum” plainly authorized a taxpayer to pay a fraction of the liability and then sue to recover it. It said that “any internal-revenue tax” could be interpreted as the entire tax assessment, and that “any sum” could be interpreted as amounts that were neither taxes nor penalties, such as interest. However, it concluded that it faced a “vexing situation—statutory language which is inconclusive and legislative history which is irrelevant.”<sup>121</sup>

Next, the Court acknowledged that before the Tucker Act a taxpayer could sue a tax collector (personally) to recover a partial payment of tax and that there was no indication that the Tucker Act intended to change that result, but discounted the implication that there was no full payment rule.<sup>122</sup> The Court reasoned that its “carefully considered *dictum*” in *Cheatham* (discussed above) prevented it from accepting the analogy between an action under the Tucker Act and a common law action against a collector, especially since the *Cheatham* Court was construing a claim-for-refund statute from which, it said, the relevant language of the Tucker Act was presumably taken.<sup>123</sup>

Next, the Court discussed post-Tucker-Act legislation that suggested Congress assumed there was a full payment rule, including (1) legislation in 1924, which established the Board of Tax Appeals, (2) the Declaratory Judgment Act of 1934, as amended in 1935 (DJA, 28 U.S.C. § 2201 *et seq.*), and (3) IRC § 7422(e). It reiterated the argument expressed in *Flora I* that the BTA was established to provide a pre-payment forum based on the assumption that none existed. Then the Court observed that the DJA granted jurisdiction to “declare the rights and other legal relations of any interested party seeking such declaration,” but specifically carved out tax cases.<sup>124</sup> The Court cited legislative history of the DJA, which said that applying it to taxes would work a “radical departure,” and also cited commentators who thought the radical departure being referenced was a departure from the full payment rule, which they apparently assumed to exist.<sup>125</sup>

118 The *Cheatham* court disagreed with the taxpayer's argument that the limitations period “cannot begin to run until the cause of action accrued, which in this case was not until the money was paid.... and that it could not have been intended by Congress that the very short limitation of six months should include any time before the money was paid, during which they had no right of action.” *Cheatham*, 92 U.S. at 87. However, it did not question her assertion that she had no right of action before the money was paid in full.

119 *Flora I*, 357 U.S. at 69. The dissent cited cases from the Eighth, Third, and Second Circuits that had declined to read a full payment rule into the Tucker Act in or after 1940. *Id.* at 76.

120 See *Flora II*, 362 U.S. at 171 n.37 (categorizing the cases) and 181-85 n.3 (J. Whittaker, dissenting, discussing the cases). Justice Frankfurter wrote a separate opinion in *Flora II* to explain that he changed sides because of the majority's mistake and the persuasiveness of the dissent's research in *Flora II*. *Flora II*, 362 U.S. at 177 (J. Frankfurter, concurring with the dissent).

121 *Id.* at 152.

122 *Id.* at 152-53.

123 *Id.* at 155.

124 28 U.S.C. § 2201.

125 *Flora II*, 362 U.S. at 164-65 n.29.

The Court went on to discuss IRC § 7422(e), which specifies what happens if a taxpayer is in tax litigation before a district court or the Court of Claims when the IRS mails the taxpayer a notice of deficiency proposing additional adjustments with respect to tax which is the subject of the taxpayer's suit. It says the suit is stayed to allow the taxpayer to file a petition with the Tax Court, and if the taxpayer does, the original court loses jurisdiction. If the taxpayer decides to remain in the original court, the IRS may bring a counterclaim; and if it does, the taxpayer generally has the burden of proof. The Court suggested that IRC § 7422(e) did not prescribe rules for all the permutations that could occur without a full payment rule. Thus, it said Congress has assumed these problems are nonexistent except in the rare case where the taxpayer sues in a district court and the IRS then notifies him of an additional deficiency.<sup>126</sup>

Finally, the Court said the prevailing view before 1940 was that full payment had to precede suit, overturning the full payment rule would substantially impair the "public purse," and could be expected to shift a "great portion" of the Tax Court's litigation into the district courts.<sup>127</sup>

Four Justices dissented in *Flora II*. The dissenting opinion first discussed a handful of tax cases from before 1940 where taxpayers who had only paid a portion of their liability had petitioned district courts or the Court of Claims in which the government had not objected or if it had, where the court had rejected the full payment rule.<sup>128</sup> Next, it pointed out that the *dictum* in *Cheatham* that was the focus of the majority opinion "did not embrace, and certainly was not directed to, the question whether full payment of an assessment is a condition upon the jurisdiction of a District Court to entertain a suit for refund."<sup>129</sup> Likewise, it said that the majority's reliance on legislative histories other than the Tucker Act, which were "not directed to the question we have here," were "too imprecise for the drawing of such a far-reaching inference, involving, as it does, the interpolation of a drastic qualification into the otherwise plain, clear and unlimited provisions of the statute."<sup>130</sup>

The dissent dismissed any disharmony resulting from concurrent jurisdiction by the Tax Court and district courts because they already had such jurisdiction with respect to refund claims.<sup>131</sup> It dismissed concerns about revenue loss due to the fact that filing in district court did not stay collection, and in any event, taxpayers could stay collection by filing a petition with the Tax Court.<sup>132</sup> Rather, it worried that taxpayers who could only pay a portion of an invalid assessment within the limitations period would be deprived of any means to recover amounts illegally collected.<sup>133</sup>

Turning to the history of the Tucker Act, the dissent observed that in the 1830s tax collectors could be personally liable for monies illegally collected. This potential liability prompted them to withhold disputed collections from the government. In 1839, Congress expressly prohibited collectors from retaining these collections, and in 1845, the Supreme Court held in *Cary v. Curtis* that the 1839 legislation had also terminated the longstanding common law right of action by taxpayers against the collectors.<sup>134</sup> This case prompted Congress to give taxpayers the right to sue the collectors to recover

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126 *Flora II*, 362 U.S. at 166.

127 *Id.* at 166-177.

128 *Id.* at 181-185 (J. Whittaker, dissenting).

129 *Id.* at 185.

130 *Id.* at 192.

131 *Id.* at 194 n.17.

132 *Id.* at 194.

133 *Id.* at 195.

134 *Id.* (citing *Cary v. Curtis*, 44 U.S. 236, 239 (1845)).

amounts which were not lawfully “payable in part or in whole.”<sup>135</sup> Thus, there was no historic basis for the full payment rule.

The Tucker Act was subsequently enacted in 1887, without making specific reference to taxes or any full payment requirement. It only covered small claims. Taxpayers could still sue collectors for large tax claims. In 1921, the Court held that claims against collectors were personal in nature, and thus, taxpayers could not recover if the collector died. The 1921 amendment to the Tucker Act was designed to allow taxpayers with large tax claims to sue the government in district court.

When Congress amended the Tucker Act in 1921 it went looking for language it could use to refer to taxes. According to the dissent, the language it selected “was chosen because, in another statute, it referred to all of the actions which could be brought for refund of internal revenue taxes” (*i.e.*, what is now IRC § 7422(a), a provision that requires taxpayers to file administrative claims with the IRS before suing in court) and thus should be interpreted broadly.<sup>136</sup> Moreover, the clear language that permitted taxpayers to sue for “any sum,” persuaded the dissent that there was no full payment rule.

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<sup>135</sup> *Flora II*, 362 U.S. at 187 (J. Whittaker, dissenting). The dissent noted that although the statute referred to Customs Collectors, the Court ruled that the legislation also authorized suits to recover illegally collected internal revenue taxes. *Id.* at 188.

<sup>136</sup> *Id.* at 195. It also pointed out that the statute at issue in *Cheatham* did not even include the “any sum” language, which makes it even broader. *Id.* at 190 n.15.

## LR #4 INNOCENT SPOUSE RELIEF: Clarify That Taxpayers May Raise Innocent Spouse Relief In Refund Suits

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*

### PROBLEM

Under Internal Revenue Code (IRC) § 6015(e), the United States Tax Court (the Tax Court) has jurisdiction to review the IRS's denials of requests for innocent spouse relief. Even though taxpayers' right to petition the Tax Court under IRC § 6015(e) is "in addition to any other remedy provided by law," a federal district court refused to consider a taxpayer's innocent spouse claim in a refund suit arising under IRC § 7422. The court's refusal to allow a taxpayer to request innocent spouse relief in a refund suit may create hardship by forcing a taxpayer to seek relief in Tax Court, thus:

- Depriving the taxpayer of his or her right to a jury trial; and
- Depriving a successful taxpayer who makes a deposit to suspend the accrual of interest of the overpayment interest he or she would otherwise receive.

### EXAMPLE

In *Chandler v. U.S.*,<sup>2</sup> the IRS denied Ms. Chandler's request for innocent spouse relief from liability for taxes shown on a joint return. Ms. Chandler paid the tax and requested a refund from the IRS, which was denied. As authorized by IRC § 7422, Ms. Chandler brought a refund suit in a United States District Court, claiming that she was entitled to innocent spouse relief, and requesting a jury trial. The government sought dismissal of Ms. Chandler's complaint for lack of subject-matter jurisdiction, contending that the Tax Court has exclusive jurisdiction to review denials of innocent spouse relief. The district court agreed with the government and dismissed the case.

Following the dismissal of her case in district court, Ms. Chandler could have appealed the decision to a United States Court of Appeals.<sup>3</sup> She could not have obtained Tax Court review of the IRS's denial of her request for innocent spouse relief. The deadline for petitioning the Tax Court expired, and the Tax Court does not have jurisdiction to decide refund suits arising under IRC § 7422.<sup>4</sup>

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 2018 U.S. Dist. LEXIS 173880 (N.D. Tex. 2018), *adopting* 2018 U.S. Dist. LEXIS 174482 (N.D. Tex. 2018).

3 Notice of appeal is required within 60 days after the entry of judgment by the district court. Fed. R. App. P. 4(a)(1)(B). The district court in *Chandler* entered its judgment on Oct. 9, 2018. As of Dec. 13, 2018, it does not appear that an appeal had been filed.

4 Under IRC § 6015(e)(1)(A)(iii), the deadline for petitioning the Tax Court is 90 days after the IRS mails the taxpayer its final notice of determination.

## RECOMMENDATION

Amend IRC §§ 6015 and 66 to clarify that taxpayers are entitled to raise innocent spouse relief in refund suits arising under IRC § 7422.<sup>5</sup>

## PRESENT LAW

### The Internal Revenue Code Provides Taxpayers With Access to Various Judicial Fora

In general, the Tax Court is the only judicial forum in which a taxpayer can challenge the IRS's assertion that he or she is liable for a deficiency in tax before paying the asserted liability in full.<sup>6</sup> There is no right to a jury trial in Tax Court.<sup>7</sup> Until the Tax Court's decision in a deficiency case becomes final, interest and penalties continue to accrue with respect to the entire unpaid liability, if any, ultimately determined to be owed.<sup>8</sup> A taxpayer who obtains innocent spouse relief in Tax Court may be entitled to a refund to the extent permitted by IRC § 6015(g).<sup>9</sup> Interest on any refund would be payable at the rate of three percentage points above the Federal short-term rate.<sup>10</sup> A taxpayer may, without waiting for the outcome in Tax Court, make a deposit that will suspend the accrual of interest and penalties pending the outcome of the case.<sup>11</sup> If the taxpayer ultimately prevails in the Tax Court litigation, the deposit will be returned with interest at the Federal short-term rate.<sup>12</sup>

Rather than petitioning the Tax Court, a taxpayer may pay the asserted tax, which also suspends the accrual of interest and penalties, and then request a refund from the IRS.<sup>13</sup> Taxpayers who pay a proposed deficiency and whose claims for tax refunds have been denied by the IRS cannot bring refund suits in the Tax Court, but they may seek refunds in the United States district courts or in the United States Court of

5 For legislative recommendations relating to innocent spouse claims in collection proceedings, see National Taxpayer Advocate 2010 Annual Report to Congress 377 (Legislative Recommendation: *Allow Taxpayers to Request Equitable Relief Under Internal Revenue Code Section 6015(f) or 66(c) at Any Time Before Expiration of the Period of Limitations on Collection and to Raise Innocent Spouse Relief as a Defense in Collection Actions*); National Taxpayer Advocate 2009 Annual Report to Congress 378 (Legislative Recommendation: *Allow Taxpayers to Raise Relief Under Internal Revenue Code Sections 6015 and 66 as a Defense in Collection Actions*); National Taxpayer Advocate 2007 Annual Report to Congress 549 (Legislative Recommendation: *Allow Taxpayers to Raise Relief Under Internal Revenue Code Sections 6015 and 66 as a Defense in Collection Actions*). The National Taxpayer Advocate reiterates her recommendations this year. See National Taxpayer Advocate 2019 Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration* (Dec. 2018).

6 IRC § 6213(a). IRC § 6211(a) defines “deficiency” as the amount by which the correct tax exceeds the excess of: (1) the sum of the amount reported on the taxpayer's return for such tax if a return was filed and an amount of tax was reported on the return plus amounts previously assessed (or collected without assessment) as a deficiency, over (2) the amount of any rebates.

7 See, e.g., *Statland v. U.S.*, 178 F.3d 465, 472-473 (7th Cir. 1999).

8 See IRC § 6601, imposing interest on underpayments, generally running from the due date of return to the date the liability is paid. See also, e.g., IRC § 6662(b), imposing a 20 percent accuracy-related penalty on certain underpayments; under IRC § 6601(e)(2)(B), interest accrues on this penalty beginning on the date on which the return was required to be filed.

9 IRC § 6015(g) provides that “Except as provided in paragraphs (2) and (3), notwithstanding any other law or rule of law (other than section 6511, 6512(b), 7121, or 7122), credit or refund shall be allowed or made to the extent attributable to the application of this section.”

10 IRC § 6621(a).

11 IRC § 6603(b).

12 IRC § 6603(d)(4); IRC § 6621(b). *Minihan v. Comm'r*, 138 T.C. 1 (2012). Interest on the refund would be payable at the rate of three percentage points above the Federal short-term rate. IRC § 6621(a).

13 IRC § 6511.

Federal Claims.<sup>14</sup> A jury trial is available if the refund suit is brought in a United States District Court.<sup>15</sup> If an individual taxpayer ultimately prevails in the refund suit, his or her payment will be refunded together with interest at the rate of three percentage points above the Federal short-term rate.<sup>16</sup>

### The Innocent Spouse Rules Evolved Over Decades, but Access to More Than One Judicial Forum Remained Intact

IRC § 6013(e), enacted in 1971, provided relief from tax liability arising from filing a joint return with a spouse.<sup>17</sup> Relief was available to a requesting spouse where there had been an omission of income attributable to the other spouse of over 25 percent of the gross income shown on the return. The spouse seeking relief also had to show that he or she did not know or have reason to know of the omission, did not significantly benefit from it, and that it would be inequitable to hold the requesting spouse liable for the deficiency attributable to the omitted income.<sup>18</sup>

Taxpayers sought Tax Court review of the IRS's denial of their innocent spouse claims under the 1971 legislation by commencing deficiency proceedings in the Tax Court.<sup>19</sup> Taxpayers also sought innocent spouse relief in refund suits brought in other federal courts.<sup>20</sup>

With the Tax Reform Act of 1984, Congress expanded the relief available under IRC § 6013(e) to include any substantial understatement (*i.e.*, over \$500) attributable to a spouse's grossly erroneous items (including omissions of gross income and improperly claimed deductions) of which the taxpayer did not know or have reason to know.<sup>21</sup> At the same time, IRC § 66 was also amended to provide for relief from the liability that arises by operation of community property laws.<sup>22</sup>

Taxpayers continued to seek innocent spouse relief pursuant to amended IRC § 6013(e), not only in Tax Court deficiency proceedings, but also in refund suits they brought in other federal courts.<sup>23</sup>

The Internal Revenue Service Restructuring and Reform Act of 1998 (RRA 98) again revised the innocent spouse provisions.<sup>24</sup> IRC § 6013(e) was repealed, and the innocent spouse rules are now found in IRC § 6015. IRC § 6015 provides three avenues for obtaining innocent spouse relief. Section 6015(b) provides "traditional" relief from deficiencies and is available to all joint filers regardless of marital status. Section 6015(c) provides relief from deficiencies for certain spouses who are divorced, separated, widowed, or not living together, by allocating the liability between each spouse. Section 6015(f)

14 IRC § 7422; 28 U.S.C. §§ 1346(a)(1) and 1491. Unlike in Tax Court, to receive judicial review of a tax liability in one of the refund fora, a taxpayer generally must first pay the disputed income tax in full and then file a claim for refund with the IRS. See *Flora v. U.S.*, 362 U.S. 145 (1960).

15 28 U.S.C. § 2402. There is no right to a jury trial in the United States Court of Federal Claims, *U.S. v. Sherwood*, 312 U.S. 584, 587 (1941); *Webster v. U.S.*, 74 Fed. Cl. 439, 444 (2006).

16 IRC § 6621(a).

17 See Pub. L. No. 91-679, 84 Stat. 2063-64 (1971) (adding IRC § 6013(e)).

18 IRC § 6013(e)(1)(A)-(C), as enacted by Pub. L. No. 91-679.

19 IRC § 6213. See, e.g., *Sonnenborn v. Comm'r*, 57 T.C. 373 (1971). The new law applied retroactively to all tax years subject to the Internal Revenue Codes of 1939 and 1954. Pub. L. No. 91-679, § 3.

20 See, e.g., *Sanders v. U.S.*, 509 F.2d 162 (5th Cir. 1975) *aff'g* 369 F. Supp. 160 (N.D. Ala. 1973).

21 Pub. L. No. 98-369, Div. A, § 424(a), 98 Stat. 801 (1984). To qualify for relief, the substantial understatement had to exceed 25 percent of the spouse's adjusted gross income (ten percent if the adjusted gross income was \$20,000 or less).

22 Pub. L. No. 98-369, Div. A, § 424(b), 98 Stat. 801 (1984). Spouses who live in community property states and file separate returns are generally required to report one-half of the community income on their separate returns. *Poe v. Seaborn*, 282 U.S. 101 (1930).

23 See, e.g., *Farmer v. U.S.*, 794 F.2d 1163 (6th Cir. 1986); *Mlay v. IRS*, 168 F. Supp. 2d 781 (S.D. Ohio 2001).

24 Pub. L. 105-206, § 3201(a), (b), 112 Stat. 685 at 734, 739.

provides “equitable” relief from both deficiencies and underpayments, but only applies if a taxpayer is not eligible for relief under IRC § 6015(b) or (c). RRA 98 also amended IRC § 66(c) to provide for equitable relief to taxpayers in community property states.

RRA 98 also enacted IRC § 6015(e), which specified that Tax Court review was available with respect to denials of innocent spouse relief under IRC § 6015 (b) or (c), or where the IRS failed to make a determination within six months after relief was requested.<sup>25</sup> In addition, IRC § 6015(e)(3)(C) provided that if either joint filer brought a timely refund suit while an innocent spouse claim was pending in Tax Court, then the Tax Court was deprived of jurisdiction and “the court acquiring jurisdiction shall have jurisdiction over the petition filed under this subsection.”<sup>26</sup>

Further amendments to IRC § 6015(e)(1)(A) in 2001 clarified that Tax Court review of innocent spouse determinations is “in addition to any other remedy provided by law.”<sup>27</sup> As the Conference Report on the 2001 legislation noted:

*Non-exclusivity of judicial remedy.*—Some have suggested that the IRS Restructuring Act administrative and judicial process for innocent spouse relief was intended to be the exclusive avenue by which relief could be sought. The bill clarifies Congressional intent that the procedures of section 6015(e) were intended to be additional, non-exclusive avenues by which innocent spouse relief could be considered.<sup>28</sup>

Following the 1998 and 2001 legislation, at least one federal court considered a taxpayer’s claim for innocent spouse relief in a refund suit, consistently with IRC § 6015(e)(1)(A).<sup>29</sup> The Tax Relief and Health Care Act of 2006 amended IRC § 6015(e) to expressly provide that the Tax Court has jurisdiction in “stand alone” cases to review IRC § 6015(f) determinations, even where no deficiency has been asserted, but did not affect the provisions of IRC § 6015(e)(1)(A).<sup>30</sup>

### A District Court Recently Held It Did Not Have Jurisdiction to Decide an Innocent Spouse Claim in a Refund Suit

In *Chandler v. U.S.*, the district court refused to consider a taxpayer’s claim for innocent spouse relief in a refund suit, holding that the Tax Court has exclusive jurisdiction to review the IRS’s denial of requests

25 Pub. L.105-206, § 3201(a), 112 Stat. 685 at 734.

26 *Id.* In hearings that preceded the enactment of RRA 98, at least one witness expressed reservations about this provision, noting that requiring removal of an innocent spouse case from the Tax Court simply because of an act by the other spouse “is to perpetuate the situation that brought her to the Tax Court in the first place.” *IRS Restructuring Hearings: Hearing Before the Sen. Comm. on Finance, 105th Cong., 2nd Sess. 126* (Feb. 5, 1998) (statement of Nina E. Olson, Executive Director, The Community Tax Law Project). IRC § 6015(e)(3)(C) now appears as IRC § 6015(e)(3).

27 Community Renewal Tax Relief Act of 2000, Pub. L. 106-544, App’x G, § 313(a), 114 Stat. 2673, 2763A–641 (2001), amending IRC § 6015(e)(1) to read as follows: “(A) IN GENERAL.—In addition to any other remedy provided by law, the individual may petition the Tax Court (and the Tax Court shall have jurisdiction) to determine the appropriate relief available to the individual under this section if such petition is filed—  
(i) at any time after the earlier of—  
(I) the date the Secretary mails, by certified or registered mail to the taxpayer’s last known address, notice of the Secretary’s final determination of relief available to the individual, or  
(II) the date which is 6 months after the date such election is filed with the Secretary, and  
(ii) not later than the close of the 90th day after the date described in clause (i)(I).”

28 H.R. REP. NO. 106-1033, at 1023 (2000) (Conf. Rep.).

29 See, e.g., *Flores v. U.S.*, 51 Fed. Cl. 49 (2001).

30 Pub. L. No. 109-432, Div. C, § 408(a), (c), 120 Stat. 2922, 3061-62 (2006), amending IRC § 6015(e)(1) to provide: “In the case of an individual against whom a deficiency has been asserted and who elects to have subsection (b) or (c) apply, or in the case of an individual who requests equitable relief under subsection (f)—” (emphasis added).

for innocent spouse relief.<sup>31</sup> The court relied on decisions by other courts that refused to allow taxpayers to seek innocent spouse relief in collection proceedings brought in federal courts.<sup>32</sup> The National Taxpayer Advocate believes the line of cases the *Chandler* court relied on were incorrectly decided. For over ten years she has recommended legislation to clarify that the Tax Court does not have exclusive jurisdiction to decide innocent spouse cases and that taxpayers may seek innocent spouse relief in suits brought in other federal courts.<sup>33</sup>

## REASONS FOR CHANGE

Notwithstanding IRC § 6015(e)(1)(A), which provides that an individual who seeks relief from joint liability may petition the Tax Court “in addition to any other remedy provided by law,” in 2018 a district court held that taxpayers cannot seek relief under IRC § 6015 in a refund suit. Other district courts have for decades allowed the claim in refund suits. The *Chandler* case adds to existing confusion about the extent to which taxpayers may seek innocent spouse relief in a judicial forum other than the Tax Court.

The decision in *Chandler*, by foreclosing district court review of innocent spouse claims, leaves taxpayers with only one forum—the Tax Court—in which to seek review of the IRS’s decision to deny their claims. Because there is no right to a jury trial in Tax Court, the *Chandler* decision also forecloses taxpayers’ right to have their cases decided by a jury.

The *Chandler* decision also forces taxpayers who make deposits to suspend the accrual of interest and penalties while their claims are decided in the Tax Court to forego three percentage points of interest if they prevail in Tax Court and are entitled to the return of their deposit.

Even if a different taxpayer in the same situation were to appeal the outcome in the *Chandler* case to a United States Court of Appeal and prevail, the appellate court’s decision would be binding precedent only with respect to district courts within the jurisdiction of that Court of Appeals. Taxpayers need clarification that the defense may be raised in collection suits in any district court.

## EXPLANATION OF RECOMMENDATION

The National Taxpayer Advocate’s recommendation will clarify that, consistent with the statutory language of IRC § 6015 and with judicial precedent, taxpayers may seek innocent spouse relief under IRC §§ 66 and 6015 in refund suits. Clarification will avert further confusion as to whether seeking innocent spouse relief is allowable in federal courts and will provide uniformity among district courts.

31 *Chandler v. U.S.*, 2018 U.S. Dist. LEXIS 173880 (N.D. Tex. 2018) adopting 2018 U.S. Dist. LEXIS 174482 (N.D. Tex. 2018).

32 Cases the court relied on include *U.S. v. Boynton*, 99 A.F.T.R.2d (RIA) 920 (S.D. Cal. 2007); *U.S. v. LeBeau*, 109 A.F.T.R.2d (RIA) 1369 (S.D. Cal. 2012); and *U.S. v. Elman*, 110 A.F.T.R.2d (RIA) 6993 (N.D. Ill. 2012).

33 National Taxpayer Advocate 2010 Annual Report to Congress 377 (Legislative Recommendation: *Allow Taxpayers to Request Equitable Relief Under Internal Revenue Code Section 6015(f) or 66(c) at Any Time Before Expiration of the Period of Limitations on Collection and to Raise Innocent Spouse Relief as a Defense in Collection Actions*); National Taxpayer Advocate 2009 Annual Report to Congress 378 (Legislative Recommendation: *Allow Taxpayers to Raise Relief Under Internal Revenue Code Sections 6015 and 66 as a Defense in Collection Actions*); National Taxpayer Advocate 2007 Annual Report to Congress 549 (Legislative Recommendation: *Allow Taxpayers to Raise Relief Under Internal Revenue Code Sections 6015 and 66 as a Defense in Collection Actions*). The National Taxpayer Advocate reiterates her recommendations this year. See National Taxpayer Advocate 2019 Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration* (Dec. 2018).

LR  
#5**TAX COURT JURISDICTION: Fix the Donut Hole in the Tax Court's Jurisdiction to Determine Overpayments by Non-Filers with Filing Extensions****TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to Finality*
- *The Right to Privacy*
- *The Right to a Fair and Just Tax System*

**PROBLEM**

A non-filer who has overpaid his or her taxes by the original filing deadline generally has two years from that date to file a claim for refund.<sup>2</sup> Under a special rule, however, if the IRS mails the non-filer a notice of deficiency during the first six months of the third year after the original filing deadline and he or she timely petitions the Tax Court, then the Tax Court generally has jurisdiction to refund or credit the overpayment.<sup>3</sup> It would have no such jurisdiction though, if the taxpayer had obtained a six-month filing extension.<sup>4</sup> Congress may have believed it authorized the Tax Court to credit or refund overpayments in this situation in 1997, but a recent decision by the Tax Court in *Borenstein* reveals that the legislative fix was incomplete.<sup>5</sup>

**EXAMPLE<sup>6</sup>**

Ms. B and Ms. C each overpay their taxes for 2012 on April 15, 2013.<sup>7</sup> Ms. B timely requests an extension to file, but Ms. C does not. Neither files a return before the IRS sends a notice of deficiency, which it does on June 19, 2015. Each contests the notice and seeks a refund, filing a petition with the Tax Court. The Tax Court has jurisdiction under Internal Revenue Code (IRC) § 6512(b)(3) to determine Ms. C's overpayment because the IRS sent the notice of deficiency during the third year after Ms. C's tax return due date (*i.e.*, June 19, 2015 is between April 15, 2015 and April 15, 2016). But the Tax Court has no similar jurisdiction to determine Ms. B's overpayment because the IRS sent

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 See IRC §§ 6511(a), (b)(2).

3 See IRC §§ 6513(b) (pre-payments deemed paid on due date), 6512(b)(3)(flush) (Tax Court jurisdiction extended for non-filers), 6511(a) (limitations period), (b)(2) (lookback period).

4 *Borenstein v. Comm'r*, 149 T.C. No. 10 (2017), *appeal docketed*, No. 17-390 (2d Cir. Dec. 4, 2017) (hereinafter *Borenstein*) (interpreting IRC § 6512(b)(3)(flush)).

5 Taxpayer Relief Act of 1997, Pub. L. No. 105-34, § 1282(a) and (b), 111 Stat. 788, 1037-38 (1997) (codified at IRC § 6512(b)(3)(flush)). For a summary of *Borenstein*, see *Significant Cases*, *infra*.

6 This hypothetical example is loosely based on the facts presented in the *Borenstein* case.

7 For purposes of IRC §§ 6511 and 6522, income tax withheld is deemed paid on April 15. See IRC § 6513(b)(1). Similarly, estimated tax is deemed paid on April 15. See IRC § 6513(b)(2).

the notice of deficiency during the *second* year after Ms. B's *extended* due date (*i.e.*, June 19, 2015 is between October 15, 2014 and October 15, 2015). The court lacks jurisdiction to determine Ms. B's overpayment because the IRS mailed the notice of deficiency at just the wrong time—more than two years after she paid the tax but before the third year after her *extended* filing date.

## RECOMMENDATION

Amend IRC § 6512(b)(3) to clarify that when the IRS mails a notice of deficiency after the second year following the due date of the return (without regard to extensions) and before the taxpayer files a return, the limitations and lookback periods for filing a claim for refund or credit (under IRC § 6511(a) and (b)(2)) are at least three years from the due date of the return (*without regard to extensions*).

## PRESENT LAW

Withholding and other pre-payments are generally deemed paid on the due date of the return without regard to extensions.<sup>8</sup> In general, a taxpayer must file a claim for refund of an overpayment within two years of paying the tax or within three years of filing the return, whichever is later (*i.e.*, the limitations period).<sup>9</sup> The amount that can be credited or refunded is limited to amounts paid within the applicable lookback period.<sup>10</sup> If the taxpayer files a return and the claim for refund is filed within the three-year limitations period, then the lookback period is three years, plus any period of any filing extension (*i.e.*, the three-year lookback period).<sup>11</sup> Otherwise, the lookback period is the two-year period preceding the claim (*i.e.*, the two-year lookback period).<sup>12</sup>

If a taxpayer who has not filed a claim for refund receives a notice of deficiency and petitions the Tax Court, then the Tax Court generally has jurisdiction to determine whether the taxpayer is due a refund to the same extent the IRS could have considered a claim filed on the date the IRS mailed the notice of deficiency.<sup>13</sup> However, a special rule applies to extend the limitations and lookback periods (under the final sentence of IRC § 6512(b)(3) when the IRS mails a notice of deficiency *before* the taxpayer files a return. In that case, if the IRS mails the notice of deficiency “during the third year after the due date (with extensions) for filing the return,” then the limitations and lookback periods are three years (not two years), even though the taxpayer has not filed a return.

The special rule in IRC § 6512(b)(3) is supposed to put non-filers who receive notices of deficiency after the two-year lookback period on the same footing as those who file returns on the same day as the IRS mails the notice of deficiency.<sup>14</sup> In *Borenstein*, however, the Tax Court concluded that it has no jurisdiction if the IRS mails the notice of deficiency *after* the second year following the due date (without extensions) and *before* the third year following the due date (with extensions). Thus, the Tax Court determined that there is a donut hole in its jurisdiction.

8 See IRC § 6513(b).

9 See IRC § 6511(a).

10 See IRC § 6511(b)(2).

11 See IRC § 6511(a), (b)(2)(A).

12 See IRC § 6511(a), (b)(2)(B).

13 See IRC § 6512(b)(1), (3)(B).

14 H.R. Rep. No. 105-220, at 701 (1997) (Conf. Rep.).

## REASONS FOR CHANGE

The final sentence of IRC § 6512(b)(3) was enacted in 1997 in response to a decision by the Supreme Court, which held that the two-year lookback period applied to a non-filer because the person had not filed a return before the IRS mailed the notice of deficiency.<sup>15</sup> The Conference Committee report explained that:

[i]f the same taxpayer had filed a return on the date the notice of deficiency was issued, and then claimed a refund, the 3-year ‘look back’ rule would apply, and the taxpayer could have obtained a refund of the overwithheld amounts....<sup>16</sup>

The Committee apparently believed it was appropriate to eliminate this disparate treatment. The report also described the law as permitting taxpayers “who initially fail to file a return, but who receive a notice of deficiency and file suit to contest it in Tax Court during the third year after the return due date, to obtain a refund of excessive amounts paid within the three-year period prior to the date of the deficiency notice.”<sup>17</sup> However, this description may not have been accurate. The final sentence of IRC § 6512(b)(3) states:

... where the date of the mailing of the notice of deficiency is during the third year after the **due date (with extensions)** for filing the return of tax and no return was filed before such date, the applicable [lookback] period under subsections (a) and (b)(2) of section 6511 shall be 3 years. [Emphasis added.]

For non-filers who filed timely extensions of the filing deadline, the Tax Court in *Borenstein* interpreted the parenthetical “with extensions” in a way that undercuts Congress’s intention to put a non-filer on the same footing as a taxpayer who filed a return on the day the IRS mailed the notice of deficiency. Although the *Borenstein* case is being appealed to the U.S. Court of Appeals for the Second Circuit, the Tax Court would not have to follow a taxpayer-favorable Second Circuit decision in cases arising in other circuits.<sup>18</sup> Thus, unless the Tax Court revisits its decision, a legislative fix is needed.

## EXPLANATION OF RECOMMENDATION

The recommendation would put all non-filers who receive notices of deficiency after the two-year lookback period on the same footing as those who file returns on the same day as the IRS mails the notice of deficiency, as intended by Congress in 1997.<sup>19</sup> Specifically, it would permit those who contest the deficiency in the Tax Court during the third year after the return due date (without extension) to obtain credits and refunds of amounts overwithheld and paid or deemed paid on the due date, even if they timely requested a filing extension.

15 *Comm’r v. Lundy*, 516 U.S. 235 (1996).

16 H.R. Rep. No. 105-220, at 701 (1997) (Conf. Rep).

17 *Id.*

18 See *Golsen v. Comm’r*, 54 T.C. 742, 757 (1970), *aff’d*, 445 F.2d 985 (10th Cir. 1971). See also *Glaze v. United States*, 641 F.2d 339 (5th Cir. 1981), *action on dec.*, 1981-140 (June 2, 1981); Chief Counsel Notice CC-2006-010 (Mar. 2, 2006).

19 H.R. Rep. No. 105-220, at 701 (1997) (Conf. Rep).

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#6

## INTERGOVERNMENTAL AGREEMENTS (IGAS): Amend Internal Revenue Code § 1474 to Allow a Period of Notice and Comment on New Intergovernmental Agreements (IGAs) and to Require That the IRS Notify Taxpayers Before Their Data Is Transferred to a Foreign Jurisdiction Pursuant to These IGAs, Unless Unique and Compelling Circumstances Exist

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Be Informed*
- *The Right to Privacy*
- *The Right to Confidentiality*

### PROBLEM

The Foreign Account Tax Compliance Act (FATCA) generally requires foreign financial institutions (FFIs) to provide the U.S. with information regarding foreign accounts held by U.S. taxpayers.<sup>2</sup> Typically, this information exchange occurs via intergovernmental agreements (IGAs), under which FFIs furnish the information to their local tax authority, which in turn transfers it to the U.S.<sup>3</sup> These IGAs also generally incorporate reciprocity, pursuant to which the U.S. agrees to provide the foreign jurisdiction with information regarding its citizens or residents maintaining accounts in the U.S.<sup>4</sup>

As previously cautioned by the National Taxpayer Advocate, the information sharing contemplated by FATCA and similar programs can be extremely helpful in identifying and preventing tax evasion through the use of offshore accounts, but it also presents enormous risks to taxpayer rights.<sup>5</sup> Recognizing the importance of taxpayers' *right to privacy* and *right to confidentiality*, Congress has enacted significant taxpayer protections relating to disclosure and use of taxpayer information.<sup>6</sup> Moreover, the National Institute of Standards and Technology (NIST) has developed detailed

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 Hiring Incentives to Restore Employment Act, Pub. L. No. 111-147, Title V, Subtitle A, 124 Stat. 71, 97 (2010) (adding IRC §§ 1471-1474; 6038D). "U.S. taxpayer" is not a specifically defined term within the IRC. But, for purposes of this analysis, it roughly equates to the term "specified United States person" as defined in IRC § 1473(3).

3 U.S. Department of Treasury, *Foreign Account Tax Compliance Act (FATCA)* (Apr. 11, 2018), <https://www.treasury.gov/resource-center/tax-policy/treaties/Pages/FATCA.aspx>.

4 *Id.*

5 National Taxpayer Advocate 2013 Annual Report to Congress 244; Nina E. Olson, *An Analysis of Tax Settlement Programs as Amnesties - When Should the Government Offer Them and How Should They Be Structured? (Part 1 of 3)*, NTA Blog, (Mar. 14, 2018), <https://taxpayeradvocate.irs.gov/news/nta-blog-analysis-of-tax-settlement-programs-as-amnesties-part-1>; Nina E. Olson, *An Analysis of Tax Settlement Programs as Amnesties - Why IRS's Offshore Voluntary Disclosure Settlement Programs Posed Risks to Voluntary Compliance (Part 2 of 3)*, NTA Blog, (Mar. 21, 2018), <https://taxpayeradvocate.irs.gov/news/nta-blog-an-analysis-of-tax-settlement-programs-as-amnesties-why-irs-s-offshore-voluntary-disclosure-settlement-programs-posed-risks-to-voluntary-compliance-part-2-of-3>; Nina E. Olson, *An Analysis of Tax Settlement Programs as Amnesties: A Discussion of Belated Alternatives to the Offshore Voluntary Disclosure Program and Recommendations for Further Improvements (Part 3 of 3)*, NTA Blog, (Mar. 30, 2018), <https://taxpayeradvocate.irs.gov/news/an-analysis-of-tax-settlement-programs-as-amnesties-a-discussion-of-belated-alternatives-to-the-offshore-voluntary-disclosure-program-and-recommendations-for-further-improvements-part-3-of-3>.

6 See, e.g., IRC § 7213, 6103. See also IRC §§ 7803(a)(3)(G), (H).

cybersecurity guidelines, to which all federal agencies, including the IRS, must conform.<sup>7</sup> Nevertheless, the IRS is exchanging U.S. taxpayer information under circumstances where the data transfers to foreign recipients do not conform to NIST guidelines, and where the IRS cannot ensure that the data is used properly by IGA partners.<sup>8</sup>

The IRS has identified the risks inherent in this approach, but has determined that these risks are acceptable.<sup>9</sup> The data being disclosed and potentially breached, however, relates to taxpayers, not to the IRS. Taxpayers, rather than the IRS, are exposed to the consequences of data theft or misuse potentially arising during or after information transfers to foreign partners pursuant to IGAs. Currently, however, taxpayers have no voice in these IGAs and receive no notification that their personal information is being transferred outside of U.S. jurisdiction.<sup>10</sup>

### EXAMPLE

Taxpayer is a citizen of the U.S. but is currently a resident of a foreign country. The U.S. and the foreign country enter into an IGA, which contemplates the reciprocal sharing of taxpayer information. Once the IGA is in force and the U.S. has done as much as it can to confirm that the cybersecurity measures of the foreign country are satisfactory, the reciprocal exchange of information begins. As part of that exchange, Taxpayer's personal information is provided to the foreign country without Taxpayer's specific knowledge. Once the information arrives in the foreign country and is beyond the continuing oversight of the IRS, a data breach occurs. As a result, Taxpayer's personal information is exposed and Taxpayer becomes the victim of identity theft. Unlike in the U.S., the foreign country does not follow the practice of alerting taxpayers when data breaches occur. Thus, the identity theft results in substantial economic damage to Taxpayer in part because Taxpayer remains unaware of the data breach until unauthorized account activity begins to appear. Moreover, Taxpayer's risk for subsequent damage has effectively been doubled by the circumstance that Taxpayer's personal information now is maintained in two different jurisdictions, thereby increasing exposure to unauthorized disclosure or improper use of that information.

### RECOMMENDATION

The National Taxpayer Advocate recommends that Congress amend Internal Revenue Code (IRC) § 1474 to add:

- IRC § 1474(g)(1), requiring the public announcement of IGAs for notice and comment by taxpayers;
- IRC § 1474(g)(2), requiring that, as part of this announcement, the IRS specify the extent to which the proposed IGA partner jurisdiction complies with the cybersecurity standards to which U.S. federal agencies are held and the taxpayer privacy standards which govern the IRS; and

7 National Institute of Standards and Technology (NIST) Special Publication (SP) 800-63-2 (Aug. 2013), superseded by NIST SP 800-63-3 (June 2017), <https://doi.org/10.6028/NIST.SP.800-63-3>.

8 IRS, Form 14675, *Risk Assessment Tool and Form, Foreign Account Tax Compliance Act (FATCA) International Data Exchange System (IDES) Identity Proofing Requirements* (Jul. 18, 2017) (on file with TAS).

9 *Id.*

10 Most jurisdictions have yet to adopt transparent procedures for notifying taxpayers regarding international information exchanges; however, France and Kazakhstan do routinely notify affected taxpayers. Further, Australia has made significant strides toward the adoption of procedures to ensure transparency under most circumstances. See Ali Noroozi, *Taxpayer Rights: Privacy and Transparency*, 87 *TAX NOTES INT'L* 2 141-145 (July 10, 2017). See also Inspector-General for Taxation, *Review into the Taxpayers' Charter and Taxpayer Protections* 117-128 (Dec. 2016).

- IRC § 1474(g)(3), requiring that, barring unique and compelling circumstances, taxpayers be informed prior to the transfer of their individual information pursuant to the terms of an IGA.

## PRESENT LAW

In 2010, Congress enacted FATCA to address concerns that U.S. taxpayers were not fully disclosing the extent of financial assets held abroad.<sup>11</sup> Subject to various thresholds and exceptions, FATCA requires FFIs to report to the IRS information about financial accounts held by U.S. taxpayers, or by certain foreign entities in which U.S. taxpayers hold a substantial ownership interest.<sup>12</sup> Failure to do so can result in a 30 percent U.S. withholding tax on a broad range of payments.<sup>13</sup> In order to avoid this withholding, an FFI must report directly to the IRS on accountholders, or undertake reporting pursuant to IGAs that have been negotiated between the U.S. and the FFI's country of residence or organization.

Under a Model 1 IGA, FFIs provide accountholder information to their country's tax authority, which in turn transfers it to the IRS.<sup>14</sup> By contrast, under a Model 2 IGA, FFIs report directly to the IRS based on protocols negotiated between the U.S. and the FFI's country of residence.<sup>15</sup> To date, the U.S. has negotiated over 100 IGAs with foreign jurisdictions.<sup>16</sup>

Many Model 1 IGAs, specifically those that are "in force," also include reciprocity, in which the IRS provides information to a given foreign jurisdiction regarding accounts held in the U.S. by residents or citizens of the foreign country. When negotiating reciprocal IGAs with a reciprocal partner, the U.S. includes certain provisions specifically addressing data security.<sup>17</sup> These protections include safeguards aimed at ensuring that the data remains confidential and is used solely for tax purposes.<sup>18</sup> Further, reciprocal IGAs typically require the existence of an infrastructure facilitating timely, accurate, and confidential information exchanges.<sup>19</sup> Only after the U.S. is satisfied that the reciprocal partner has appropriate protections in place does the data transfer take place.<sup>20</sup>

Further, the IRS has taken several steps to mitigate the risk of data breaches resulting from reciprocal agreements, including:

- Establishing long-term relationships with partner countries' points-of-contact;

11 Hiring Incentives to Restore Employment Act, Pub. L. No. 111-147, Title V, Subtitle A, 124 Stat. 71, 97 (2010) (adding IRC §§ 1471-1474; 6038D).

12 U.S. Department of Treasury, *Foreign Account Tax Compliance Act (FATCA)* (Apr. 11, 2018), <https://www.treasury.gov/resource-center/tax-policy/treaties/Pages/FATCA.aspx>.

13 IRC § 1471(a).

14 IRS, *FATCA Information for Governments* (Feb. 17, 2018), <https://www.irs.gov/businesses/corporations/fatca-governments>.

15 *Id.*

16 U.S. Department of Treasury, *Foreign Account Tax Compliance Act (FATCA)* (Apr. 11, 2018), <https://www.treasury.gov/resource-center/tax-policy/treaties/Pages/FATCA.aspx>. Specifically, there are over 100 intergovernmental agreements (IGAs) that are either "in force" or "treated as in effect." An IGA is "in force" when the jurisdiction has enacted implementing legislation for its foreign financial institutions (FFIs) to document and report under the IGA.

17 Department of Treasury, *Model 1A IGA Reciprocal, Preexisting TIEA or DTC* (Nov. 30, 2014), Article 3.7-9.

18 *Id.* See, for example, paragraph 8, which in relevant part, states, "Following entry into force of this Agreement, each Competent Authority shall provide written notification to the other Competent Authority when it is satisfied that the jurisdiction of the other Competent Authority has in place (i) appropriate safeguards to ensure that the information received pursuant to this Agreement shall remain confidential and be used solely for tax purposes, and (ii) the infrastructure for an effective exchange relationship..."

19 Department of Treasury, *Model 1A IGA Reciprocal, Preexisting TIEA or DTC* (Nov. 30, 2014), Article 3.7-9.

20 *Id.*

- Encrypting outbound data files using encryption standards common across all sensitive government uses;<sup>21</sup>
- Providing partner countries with unique private keys to open data transmissions; and
- Undertaking on-site reviews of partner countries to ensure that their safeguards are sufficient and will be in place to protect the incoming data.<sup>22</sup>

Within the U.S., federal agencies, including the IRS, are required to conform to cybersecurity guidelines set forth by NIST.<sup>23</sup> Likewise, Congress enacted a variety of statutes protecting the confidentiality and use of taxpayer data, both inside and outside of the IRS.<sup>24</sup>

## REASONS FOR CHANGE

Notwithstanding significant efforts to ensure the confidentiality and appropriate use of taxpayer data in implementing IGAs, the IRS is unable to comply with NIST standards when transferring that information to reciprocal partners. Likewise, it cannot control what a country does with taxpayer data once the information transfer is complete. These exposures, particularly noncompliance with NIST guidelines, prompted the IRS to undertake an assessment regarding identity proofing and e-authentication with respect to foreign users.<sup>25</sup> Where outbound data transfers to partner countries are concerned, the IRS concluded that the impact of a data breach would be “high,” but that the likelihood of such a breach actually occurring was “very low.”<sup>26</sup> Therefore, the IRS assessed the overall risk stemming from this deficiency as “low.”<sup>27</sup>

That being said, the exposure to the IRS in the event of data theft or misuse occurring either in transfer or after receipt by the foreign jurisdiction is primarily reputational. On the other hand, the true impact of such a data breach would be experienced by the taxpayers whose information is compromised. They could, among other things, be the victims of identity theft or the targets of persecution within foreign jurisdictions. The consequences could range from substantial inconvenience to serious economic damage to harassment and even physical danger.

Nevertheless, taxpayers who are citizens or residents of a foreign jurisdiction have no voice in the U.S.’s decision to pursue an IGA with a foreign jurisdiction, or in the terms that are ultimately negotiated. Likewise, once such an IGA is put into place, these taxpayers may not even know that their account

21 Specifically, the IRS uses Advanced Encryption Standard (AES) encryption, which is the standard recommended by National Institute of Standards and Technology (NIST) for use by all government agencies, including for the protection of top-secret data by the National Security Agency. See NIST, *Cryptographic Standards and Guidelines* (Oct. 10, 2018), <https://csrc.nist.gov/projects/cryptographic-standards-and-guidelines/archived-crypto-projects/aes-development>.

22 IRS, Form 14675, *Risk Assessment Tool and Form, Foreign Account Tax Compliance Act (FATCA) International Data Exchange System (IDES) Identity Proofing Requirements* (July 18, 2017) (on file with TAS).

23 NIST SP 800-63-2 (Aug. 2013), superseded by NIST SP 800-63-3 (June 2017), <https://doi.org/10.6028/NIST.SP.800-63-3>.

24 See, e.g., IRC § 7213, 6103.

25 IRS, Form 14675, *Risk Assessment Tool and Form, Foreign Account Tax Compliance Act (FATCA) Qualified Intermediaries (QI) and Financial Institution Registration* (July 18, 2017) (on file with TAS); IRS, Form 14675, *Risk Assessment Tool and Form, Foreign Account Tax Compliance Act (FATCA) International Data Exchange System (IDES) Identity Proofing Requirements* (July 18, 2017) (on file with TAS).

26 IRS, Form 14675, *Risk Assessment Tool and Form, Foreign Account Tax Compliance Act (FATCA) International Data Exchange System (IDES) Identity Proofing Requirements* (July 18, 2017) (on file with TAS).

27 *Id.*

information is the subject of a data transfer.<sup>28</sup> If impacted taxpayers were allowed to comment on potential IGAs, they could make the U.S. aware of circumstances that perhaps were unknown or undervalued by those participating in the negotiations. Moreover, once informed that data transfers to a foreign jurisdiction were under consideration, taxpayers would have an opportunity to minimize risks to their property and physical safety. This public notice would also give affected taxpayers the chance to address any erroneous information or noncompliance that should be remedied. Further, it would provide them with the opportunity to mitigate the potential impact flowing from misinterpretation or improper re-disclosure of the information by the foreign jurisdiction.

The public notice should explain the safety measures that have been taken to ensure that taxpayer data will be transferred securely and used properly. This explanation will likely provide taxpayers with some reassurance. Nevertheless, the negative consequences of a data breach ultimately fall on the taxpayer, and the risk of damage increases exponentially with every additional country receiving the taxpayer's information.

Of course, unique circumstances may occasionally arise in which individual notification could jeopardize ongoing criminal investigations in either the U.S. or the foreign jurisdiction. In order to address such situations, procedures should be developed to govern the evaluation of this risk and the determination of when nondisclosure to specific individuals is warranted.

## EXPLANATION OF RECOMMENDATION

Congress should amend IRC § 1474 to require announcement of IGAs for notice and comment by taxpayers; specification of the extent to which the proposed IGA partner jurisdiction conforms with the cybersecurity standards to which U.S. federal agencies are held and the taxpayer privacy standards which govern the IRS; and, barring unique and compelling circumstances, notification to taxpayers prior to the transfer of their individual information pursuant to the terms of an IGA. By doing so, Congress would give taxpayers the opportunity to voice specific concerns to be considered prior to implementation of an IGA and would allow taxpayers to undertake steps to mitigate the potential risk flowing from the theft or misuse of data during or after electronic transfer of that data to foreign jurisdictions.

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28 The possibility that data may be provided under a Model 1 IGA is disclosed in various places, including on the face of the current Form W-8BEN, *Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding and Reporting (Individuals)*, and in the current instructions to Form W-8BEN-E, *Certificate of Status of Beneficial Owner for United States Tax Withholding and Reporting (Entities)*. Nevertheless, these generalized statements function more as broad caveats than as targeted notifications.

LR  
#7**FOREIGN ACCOUNT REPORTING: Authorize the IRS to Compromise Assessed FBAR Penalties It Administers****TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Finality*
- *The Right to a Fair and Just Tax System*

**PROBLEM**

In addition to the administration and enforcement of the penalties contained in the Internal Revenue Code (IRC), the IRS has been delegated the authority to enforce Foreign Bank and Financial Accounts (FBAR)<sup>2</sup> reporting requirements and assess FBAR penalties under Title 31 of the United States Code (U.S.C.).<sup>3</sup> FBAR penalties fall under Title 31 and not under any provisions of the IRC (also referred to as Title 26), which the IRS typically would have the authority to administer.

For Title 26 liabilities, IRC § 7122 authorizes the IRS to compromise any civil or criminal case arising under the Internal Revenue laws (prior to referral of the case to the Department of Justice (DOJ)).<sup>4</sup> Although, the IRS has the authority to compromise assessed tax liabilities under IRC § 7122, the IRS does not have the authority to compromise assessed Title 31 FBAR penalties.<sup>5</sup> Assessed FBAR penalties which exceed \$100,000 can only be compromised by the Department of Justice, while those under that amount can be compromised by the Bureau of Fiscal Service (BFS).<sup>6</sup> In situations when the IRS assesses both tax liabilities, including penalties under the IRC and the FBAR penalties stemming from

- 1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).
- 2 See Currency and Foreign Transactions Reporting Act, Pub. L. No. 91-508, Title II, 84 Stat. 1114, 1118 (1970) (codified as amended at 31 U.S.C. §§ 321, 5311–5314, and 5316–5322). Prior to 2003, the Foreign Bank and Financial Accounts (FBAR) reporting requirements were enforced by the Financial Crimes Enforcement Network (FinCEN). In 2003, to increase compliance, FinCEN delegated its FBAR enforcement authority to the IRS. The Director of FinCEN delegated the authority to the IRS to assess FBAR liabilities under Title 31. Specially, the IRS was delegated with assessment of 31 U.S.C. § 5314, 31 C.F.R. § 1010.350, 31 C.F.R. § 1010.306, and 31 C.F.R. § 1010.420, including, with respect to these provisions, the authority to assess and collect civil penalties under 31 U.S.C. § 5321 and 31 C.F.R. § 1010.820 and to take any other action reasonably necessary for the enforcement of these and related provisions. See Memorandum of Agreement Between FinCEN and the IRS (Apr. 10, 2003). See also 31 C.F.R. § 1010.810(g); *Memorandum of Agreement and Delegation of Authority for Enforcement of FBAR Requirements*, Internal Revenue Manual (IRM) Exhibit 4.26.1-3, *FBAR Delegation to IRS* (Apr. 5, 2011).
- 3 31 U.S.C. § 5318(a) provides the Secretary of the Treasury with authority to administer provisions of the Bank Secrecy Act (BSA).
- 4 IRC § 7122. IRS Form 656, *Offer in Compromise* (Rev. Mar. 2018), is the required form for an offer in compromise (OIC).
- 5 There is a *de minimus* exception which allows the head of an executive, judicial, or legislative agency to compromise assessed FBAR penalties up to \$100,000. 31 U.S.C. § 3711(a)(2). However, this authority to compromise falls under the authority of the Bureau of Fiscal Service (BFS). See 31 C.F.R. § 902.1. See also IRM Exhibit 4.26.1-3, *FBAR Delegation to IRS* (Apr. 5, 2011). Prior to assessment, the IRS may compromise the FBAR penalty. For pre-assessment procedures, see IRM 4.26.16, *Report of Foreign Bank and Financial Accounts (FBAR)* (Nov. 6, 2015).
- 6 31 U.S.C. § 3711(a)(2). See also 31 C.F.R. § 902.1.

the same conduct, and it considers an offer in compromise (OIC) for tax liabilities, it cannot consider compromising FBAR penalties to achieve a final, one-stop, complete resolution for the taxpayer.<sup>7</sup>

After the IRS makes assessments under both Title 26 and Title 31, if a taxpayer seeks to compromise his or her Title 26 and Title 31 assessments, the following steps would have to occur:

1. The taxpayer would submit an OIC to the IRS. This OIC would be limited to the Title 26 taxes and penalties. Any amounts owed for the Title 31 FBAR penalty cannot be considered by the IRS.
2. While the IRS is considering the OIC, all debt-collection activity on the Title 26 assessment would be held in abeyance.<sup>8</sup> However, the government, through BFS, can continue collecting the Title 31 FBAR penalty.<sup>9</sup>
3. BFS may eventually refer the Title 31 FBAR penalty to DOJ.<sup>10</sup>
4. The Attorney General or delegate may compromise both the Title 26 and Title 31 case after referral to DOJ for prosecution or defense.<sup>11</sup> However, if in the meantime, the IRS has accepted the OIC, DOJ would only be able to consider a compromise for the FBAR assessments.<sup>12</sup>

Affected taxpayers need to complete multiple steps to compromise all liabilities (FBAR and tax), which increases taxpayer burden not limited to costs of representation and undermines the taxpayer's *right to finality* and the *right to a fair and just tax system*. This process is also inefficient for the government as it may create rework at different stages for several government agencies—the IRS, BFS, and DOJ.

## EXAMPLE

In 2015, Taxpayer A, a citizen of the Republic of India, co-inherited an offshore account in India from his parents, along with his two brothers. Taxpayer A currently is a U.S. legal permanent resident (green card holder) residing in the U.S. but his two brothers, citizens of the Republic of India, live and work in New Delhi, India. Taxpayer A's parents owned a Swiss bank account in the amount of \$1,000,000 and named all three children as beneficiary owners. When the parents passed away all three brothers made withdrawals from the account, which earned six percent in interest per annum. In 2015, Taxpayer A made several withdrawals totaling \$200,000 while his brothers withdrew the remaining balance and closed the account. In 2015, the account accrued \$60,000 in interest.

Taxpayer A failed to report the foreign financial account on the FinCEN Form 114, *Report of Foreign Bank and Financial Accounts* (FBAR), and Form 8938, *Statement of Specified Foreign Financial Assets*. He also failed to indicate he had a beneficial interest in a foreign account on Schedule B of his U.S. federal income tax return for tax year (TY) 2015.

After an audit in 2018, the IRS determined that Taxpayer A acted willfully and assessed a willful FBAR penalty of \$500,000 for TY 2015, 50 percent of the maximum account value during that year. It also attributed the interest of \$60,000 to Taxpayer A's income for TY 2015 which resulted in an additional

7 IRM 5.21.6.7, *Collection of FBAR Penalties* (Feb. 18, 2016).

8 See IRC § 7122; 26 C.F.R. § 301.7122-1.

9 See IRM 5.21.6.7, *Collection of FBAR Penalties* (Feb. 18, 2016).

10 See 31 C.F.R. §§ 285.1-8, 285.11-13.

11 IRC § 7122(a); 31 U.S.C. § 3711(a)(2).

12 See 31 U.S.C. § 3711.

tax, interest and accuracy-related penalties of about \$9,500. The IRS also assessed the penalty for the failure to file the Form 8938, *Statement of Specified Foreign Financial Assets*, of \$10,000 under IRC § 6038D(d)(1).<sup>13</sup>

Taxpayer A experienced economic hardship along with significant medical expenses. Taxpayer A has approached the IRS, seeking to compromise both his tax liabilities and the assessed FBAR penalty. The IRS does not have a statutory authority to compromise the Title 31 assessment. Therefore, Taxpayer A submits a doubt as to collectibility OIC to the IRS to compromise the Title 26 tax debt (\$19,500 for TY 2015). After taking into consideration his allowable living expenses, the IRS accepts Taxpayer A's monthly payments, under the terms of the OIC, consisting of \$125.00 per month for three years. Meanwhile, because Taxpayer A has not been able to afford any payments on his FBAR penalty of \$500,000 (the Title 31 FBAR penalty), the IRS referred that debt to BFS. Taxpayer A approaches BFS to compromise the debt and BFS refers him to DOJ as it does not have authority to compromise an amount above \$100,000. Taxpayer A gives up on finding a settlement with DOJ because he is afraid it would jeopardize his OIC with the IRS.

When BFS starts to garnish his wages and offsets a portion of his social security benefits<sup>14</sup> in payment of the FBAR penalty (*i.e.*, \$500,000 for TY 2015), Taxpayer A defaults on his OIC and the total tax liability (*i.e.*, \$19,500 for TY 2015) plus interest and penalties is reinstated.

## RECOMMENDATION

To promote the taxpayers' *right to finality* and *the right to a fair and just tax system*, and to improve efficiency of IRS's administration of the FBAR penalty, the National Taxpayer Advocate recommends that Congress amend IRC § 7122(a) to allow the IRS to compromise the FBAR penalties assessed by the IRS under U.S.C. Title 31.

## PRESENT LAW

IRC § 7122 authorizes the Secretary to enter into an agreement with a taxpayer that settles the taxpayer's tax liabilities for less than the full amount owed, as long as the liabilities have not been referred to DOJ.<sup>15</sup> Such an agreement is known as an "offer in compromise" (OIC). Treasury regulations provide that the IRS may compromise liabilities to the extent there is doubt as to liability, doubt as to collectibility, or to promote effective tax administration.<sup>16</sup> The regulations further define these terms and provide instances when compromise is appropriate. The IRS has statutory authority to compromise any civil or criminal case arising under the Internal Revenue laws prior to referral to DOJ for prosecution or defense. The Internal Revenue laws are those laws contained in Title 26 of the United States Code.<sup>17</sup>

13 The Foreign Account Tax Compliance Act (FATCA) added IRC § 6038D, which requires U.S. citizens, resident aliens, and certain non-resident aliens to file Form 8938, *Statement of Specified Foreign Financial Assets*, with their federal income tax returns to report foreign assets exceeding specified thresholds. See Pub. L. No. 111-147, Title V, Subtitle A, 124 Stat. 71, 97 (2010).

14 See 31 C.F.R. §§ 285.4(e) and 285.11(d).

15 IRC § 7122(a).

16 Treas. Reg. § 301.7122-1(b).

17 See generally IRC §§ 1-9834.

The requirement to report foreign bank and financial accounts was added to the United States Code in 1970 as part of the “Currency and Foreign Transactions Reporting Act of 1970,” which came to be known as the “Bank Secrecy Act” or “BSA.”<sup>18</sup> Each United States person having a financial interest in, or signature or other authority over, a bank, securities, or other financial account in a foreign country shall report such relationship to the Department of the Treasury each year.<sup>19</sup> Individuals required to file FinCEN Form 114, *Report of Foreign Bank and Financial Accounts* (FBAR), who fail to properly file this form, may be subject to civil monetary penalties under 31 U.S.C. § 5321.

The BSA was codified in Title 31.<sup>20</sup> 31 U.S.C. § 5318(a) provides the Secretary of the Treasury with authority to administer provisions of the BSA. The Secretary of the Treasury delegated the authority to administer civil compliance with Title II of the BSA to the Director, FinCEN.<sup>21</sup> While FinCEN retains its rule-making authority for FBAR, it re-delegated civil FBAR enforcement authority to the IRS.<sup>22</sup> The civil FBAR enforcement authority includes the assessment and collection of civil FBAR penalties.<sup>23</sup> Title 31 FBAR liabilities are not tax debts, which would fall under Title 26.<sup>24</sup>

## REASONS FOR CHANGE

In situations when the IRS assesses both tax liabilities, including penalties under the IRC, and the FBAR penalties stemming from the same conduct, and it considers an OIC for tax liabilities, it cannot consider compromising FBAR penalties to achieve global resolution.<sup>25</sup>

After the IRS makes assessments under both Title 26 and Title 31, if a taxpayer seeks to compromise both assessments, as noted earlier, the taxpayer will need to deal with two or sometimes three different government agencies.<sup>26</sup> First, the taxpayer would submit an OIC to the IRS to compromise his or her tax liabilities, which, however, would not preclude BFS from collecting the Title 31 FBAR penalty during the pendency of the OIC. Then the taxpayer would need to separately request BFS to consider a compromise of the FBAR penalties if the assessment does not exceed the \$100,000 threshold,<sup>27</sup> or to request both BFS and the IRS to refer their respective assessments to DOJ if the FBAR assessment

18 A civil penalty not to exceed \$10,000 may be imposed against anyone who violates or causes a violation of 31 U.S.C. § 5314 and its regulations, including the failure to file an FBAR. 31 U.S.C. § 5321(a)(5)(A)-(B). For willful violations, the maximum penalty is the greater of \$100,000 or 50 percent of the amount of the transaction or the balance in such account at the time of the violation. 31 U.S.C. § 5321(a)(5)(C). See also IRM 4.26.16, *Report of Foreign Bank and Financial Accounts (FBAR)* (Nov. 6, 2015).

19 31 C.F.R. § 1010.350.

20 31 U.S.C. §§ 5311–5314, 5316–5332.

21 See Memorandum of Agreement Between FinCEN and the IRS (Apr. 10, 2003). See also 31 C.F.R. § 1010.810(g). IRS Criminal Investigation (CI) has authority to enforce the criminal provisions of the BSA.

22 See Memorandum of Agreement and Delegation of Authority for Enforcement of FBAR Requirements, available in IRM Exhibit 4.26.1-3, *FBAR Delegation to IRS* (Apr. 5, 2011).

23 *Id.*

24 The FBAR requirements under 31 U.S.C. § 5311 et seq. are separate from the requirements to report income from accounts on the relevant tax returns under Title 26. For more information distinguishing these two requirements, see IRS, *Comparison of Form 8938 and FBAR Requirements* (July 17, 2018), <http://www.irs.gov/Businesses/Comparison-of-Form-8938-and-FBAR-Requirements>.

25 IRM 5.21.6.7, *Collection of FBAR Penalties* (Feb. 18, 2016).

26 If the FBAR assessment is under \$100,000, then the taxpayer will have to deal with two agencies—IRS and BFS. If the FBAR assessment is \$100,000 or more, then it is possible that three agencies will be involved—IRS, BFS, and Department of Justice (DOJ). BFS is involved if the debt is referred to the agency and BFS is taking collection action. BFS, however, will not be involved in the compromise process, though, since only DOJ will have authority at that point. See 31 C.F.R. §§ 285.1-8, 285.11-13. See also IRC § 7122(a); 31 U.S.C. § 3711(a)(2).

27 This amount is excluding interest. See 31 U.S.C. § 3711(a)(2).

exceeds the threshold. Eventually once the taxpayer's case reaches DOJ, the Attorney General or delegate may compromise both tax and FBAR assessments. However, if, in the meantime, the IRS has accepted the OIC, DOJ would be able only to consider a compromise for the FBAR liability.<sup>28</sup> This process involves multiple steps which may duplicate efforts by the government and cause additional burden for taxpayers, including representation costs, extensive delays, and uncertainty.

Granting the IRS the authority to compromise Title 26 and Title 31 assessments would benefit both the government, as a whole, and taxpayers seeking to compromise their debts. The government benefits because one agency has jurisdiction over the whole process and a taxpayer's individual circumstances will be considered in their entirety when an OIC is submitted to the IRS.

## EXPLANATION OF RECOMMENDATION

The recommendation would allow the IRS to compromise FBAR debt it assessed against a taxpayer along with tax liabilities under the IRC. Adding language in IRC § 7122(a) to allow the IRS to compromise FBAR penalties it has assessed would be a cost-effective fix for the government and taxpayers alike.

This legislative change would not create a conflict with the statutory framework for compromise of nontax debts under 31 U.S.C. § 3711.<sup>29</sup> Instead, it would be in line with the IRS's existing authority to compromise any civil or criminal penalties assessed arising under the Internal Revenue laws, prior to referral of the case to DOJ. For Title 26 tax liabilities, IRC § 7122 currently authorizes the IRS to compromise any civil or criminal penalties assessed in cases arising under the Internal Revenue laws *prior* to referral of the case to DOJ. Similarly, if adopted, this legislative change would authorize the IRS to compromise Title 31 FBAR penalties it has assessed but *only prior* to referral of the case to DOJ. DOJ would retain jurisdiction to compromise both tax and nontax (FBAR penalty) liabilities after a case is referred to it by the IRS. This legislative change would allow the IRS to evaluate the taxpayer's financial situation and compromise all tax liabilities and the assessed FBAR penalties stemming from the same conduct, under the principles set forth in IRC § 7122, in one setting. The FBAR compromise authority would allow the IRS to provide taxpayers with a consistent, comprehensive resolution for all liabilities assessed by the IRS, the agency most familiar with the taxpayer's circumstances; thereby also conserving government resources.

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<sup>28</sup> See 31 U.S.C. § 3711.

<sup>29</sup> *Id.*

LR  
#8**TAX WITHHOLDING AND REPORTING: Improve the Processes and Tools for Determining the Proper Amount of Withholding and Reporting of Tax Liabilities****TAXPAYER RIGHTS IMPACTED<sup>1</sup>**

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*

**PROBLEM**

Passage of the Tax Cuts and Jobs Act resulted in a variety of changes that caused many taxpayers to adjust the information furnished to employers so that relatively accurate withholding at source could be undertaken.<sup>2</sup> To assist in this process, the IRS is developing a redesigned Form W-4, *Employee's Withholding Allowance Certificate*, that will likely be available in 2020.<sup>3</sup> Efforts to achieve accurate withholding have generated a range of concerns, including complexity, taxpayer burden, and employee privacy.<sup>4</sup> These issues arise because, unlike in many other countries, such as New Zealand, the U.S. tax system requires employees to navigate an often-confusing and difficult process to provide employers with their personal information, including other sources of income and marital status, so that the correct amount of tax can be withheld.<sup>5</sup>

An additional challenge arises from the circumstance that, in the U.S., withholding is primarily applied against wage income.<sup>6</sup> Thus, taxpayers earning other income, such as interest, dividends, and payments collected as an independent contractor, must factor in those earnings when determining how much should be withheld from their wages in order to meet their overall tax obligations. Such an effort can be both complex and frustrating, and inevitably leads to the disclosure of all such information to employers. Other countries have implemented solutions to these problems, however, that not only preserve employee privacy, but that, in the case of the U.K., allow approximately two-thirds of all taxpayers to end each year having already fully and accurately satisfied their tax liabilities.<sup>7</sup>

- 1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).
- 2 H.R. 1, Tax Cuts and Jobs Act, Pub. L. No. 115-97, 131 Stat. 2054 (2017).
- 3 See IRS, *IRS Statement on Form W-4* (Nov. 5, 2018), <https://www.irs.gov/newsroom/irs-statement-on-form-w-4>.
- 4 Nina E. Olson, *As the IRS Redesigns Form W-4, Employee's Withholding Allowance Certificate, Stakeholders Raise Important Questions*, NTA BLOG (Nov. 29, 2018), [https://taxpayeradvocate.irs.gov/news/nta-blog-as-the-irs-redesigns-form-w-4-employee-s-withholding-allowance-certificate-stakeholders-raise-important-questions?category=Tax News](https://taxpayeradvocate.irs.gov/news/nta-blog-as-the-irs-redesigns-form-w-4-employee-s-withholding-allowance-certificate-stakeholders-raise-important-questions?category=Tax%20News).
- 5 See Research Study: *A Conceptual Analysis of Pay-As-You-Earn (PAYE) Withholding Systems as a Mechanism for Simplifying and Improving U.S. Tax Administration*, *infra*.
- 6 For an in-depth discussion of this issue and for the basis underlying the National Taxpayer Advocate's first two recommendations herein, see Research Study: *A Conceptual Analysis of Pay-As-You-Earn (PAYE) Withholding Systems as a Mechanism for Simplifying and Improving U.S. Tax Administration*, *infra*.
- 7 Louise Eccles, *Millions are Unnecessarily Filing in Tax Returns: Quarter of Those Filing Forms Owe Less than £50 or Nothing at All*, DAILY MAIL (Jun. 15, 2015), <http://www.dailymail.co.uk/news/article-3125675/Millions-needlessly-filing-tax-returns-Quarter-completing-forms-owe-50-all.html>. See also William J. Turnier, *PAYE as an Alternative to an Alternative Tax System*, 23 VA. TAX REV. 205, 212 (Summer 2003).

Another problem currently, though unnecessarily, confronting taxpayers, is their inability to easily access and utilize their own data existing within IRS systems. Related difficulties include the restrictions surrounding free electronic filing (e-filing) of tax returns and the limited usefulness of the Free File Fillable Forms (Fillable Forms) available for preparation of electronic returns.<sup>8</sup> Even though the IRS already receives year-end information reports, such as Forms W-2, *Wage and Tax Statement*, and 1099-MISC-NEC, *Miscellaneous Income (Nonemployee Compensation)*, taxpayers and their authorized tax return preparers are unable to access their data directly from the IRS by means of an online account.<sup>9</sup> As a result of this inability, taxpayers are prevented from importing the data on these forms into tax return preparation software, or into Fillable Forms that themselves could perform the math necessary to calculate tax liabilities or refunds.<sup>10</sup> Accordingly, U.S. taxpayers are provided with suboptimal processes and tools for determining not only the withholding, but also the reporting of tax liabilities, shortcomings that prevent taxpayers from receiving the simplicity, privacy, and accuracy they have a right to expect.

### EXAMPLE

Jane works full-time for Retailer and earned \$25,000 from her employer during the 2018 tax year. Retailer has a policy that strongly discourages other types of outside employment. Nevertheless, Jane, who has a family to support, drives for a rideshare company in her off-hours, earning an additional \$10,000 during the year.

Jane does not want Retailer to find out about her outside employment, so she does not report it as an additional source of income on the Form W-4 she submits to Retailer. Confused by the IRS withholding calculator and afraid of indirectly indicating an additional income source, she does nothing at all with respect to the ridesharing income.<sup>11</sup> As a result, by the end of 2018, Jane is substantially under-withheld. In early 2019, Jane attempts to prepare her 2018 tax return using software that is part of Free File, Inc., which she learned about through IRS.gov. Although she intends to comply with her tax obligations, Jane is misled by the software's emphasis on obtaining the "maximum refund" and omits her rideshare income reflected on her Form 1099. Ultimately, the IRS identifies the omission from income and Jane is not only subjected to an additional income tax liability, but to the failure to pay penalty because the IRS did not accept her explanation that her omission was made in good faith and that she should receive reasonable cause relief.<sup>12</sup>

8 For a more in-depth discussion of the IRS Free File Program, see Most Serious Problem: *Free File: The IRS's Free File Offerings Are Underutilized, and the IRS Has Failed to Set Standards for Improvement*, *supra*.

9 See Legislative Recommendations: *It Modernization: Provide the IRS with Additional Dedicated, Multi-Year Funding to Replace Its Antiquated Core IT Systems Pursuant to a Plan that Sets Forth Specific Goals and Metrics and Is Evaluated Annually by an Independent Third Party*, *supra*; National Taxpayer Advocate 2017 Annual Report to Congress 36-48.

10 See Most Serious Problem: *Free File: The IRS's Free File Offerings Are Underutilized, and the IRS Has Failed to Set Standards for Improvement*, *supra*.

11 See IRS, *IRS Withholding Calculator* (Dec. 11, 2018) <https://www.irs.gov/individuals/irs-withholding-calculator>.

12 See IRC § 6651(a)(3).

## RECOMMENDATION

The National Taxpayer Advocate recommends that Congress enact legislation directing the Treasury Department, in consultation with the IRS and the National Taxpayer Advocate, to analyze and report on the feasibility of and steps necessary for:

1. Adopting an IRS-determined withholding code as an alternative to the Form W-4 approach currently utilized in U.S. tax administration;
2. Expanding withholding at source to encompass not only wages, but taxable interest, pensions, dividends, capital gains, Individual Retirement Arrangement (IRA) income, unemployment, and eventually certain earnings as an independent contractor; and
3. Furnishing information return data to taxpayers electronically for direct importation into tax return preparation software or for provision to authorized tax return preparers.

## PRESENT LAW

### Simple Withholding Is Workable, but Limited

The most basic form of Pay-As-You-Earn (PAYE) tax collection is simple withholding, which is the approach applied in the U.S. Under that system, employers paying wages for services performed by employees are required to deduct and withhold Social Security, Medicare, and income taxes from those wages.<sup>13</sup> Thereafter, employers are obligated to remit these taxes to the IRS.<sup>14</sup> PAYE was implemented as a revenue collection mechanism during World War II, and has operated in roughly the same form ever since.<sup>15</sup> Although this system has proven effective and durable insofar as it goes, it is also overly-complex, insufficiently private, and unduly imprecise for 21st century tax administration.

Under the U.S.'s simple withholding system, taxpayers provide their employers with a Form W-4 detailing, among other things, their marital status, elected allowances, and any additional amounts they would like withheld. Withholding is then undertaken from wage income on a paycheck-by-paycheck basis. Percentage adjustments are automatically made to account for the amount of earnings within each pay period, but these adjustments are too generalized to result in accurate withholding for many taxpayers.<sup>16</sup> Moreover, earnings from other sources, such as interest, dividends, capital gains, and self-employment income, are not subject to withholding.

As a result, a year-end tax reconciliation is required to compare the amounts collected via withholding against the taxpayer's aggregate annual tax liability. This reconciliation, which in the U.S. is implemented through a post-year-end tax return filing requirement imposed on taxpayers, then generates a tax refund, a tax liability, or no payment from either the government or the taxpayer depending on the outcome.<sup>17</sup>

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<sup>13</sup> See IRC §§ 3101, 3102(a) and 3402(a).

<sup>14</sup> IRC § 3403.

<sup>15</sup> Pub. L. No. 68, Ch. 120, 57 Stat. 126 (1943). For a discussion of the historical evolution of the U.S. system of tax administration, see National Taxpayer Advocate 2011 Annual Report to Congress 1-150 (Study: *From Tax Collector to Fiscal Automaton: Demographic History of Federal Income Tax Administration, 1913-2011*).

<sup>16</sup> IRS Notice 1036 (Dec. 2018).

<sup>17</sup> IRC § 6012.

### Other Countries Have Adopted an Expanded PAYE in Beneficial Ways

Taxpayers and policymakers in other countries have similar concerns regarding privacy and complexity as those expressed with respect to the U.S. withholding system. One antidote to some of these ills has been to route taxpayer information and withholding determinations through the tax authority, rather than through the employer.

For example, in New Zealand, withholding codes are obtained from the tax authority by employees and then forwarded by employees to their employers.<sup>18</sup> These withholding codes determine the amount of tax to be deducted from gross wages and salaries and remitted by employers to the tax authority.<sup>19</sup> The withholding codes take into account the type of employment, the number of jobs held, and the employee's entitlement to various rebates and deductions.<sup>20</sup> Among other things, the withholding codes factor in taxpayers' eligibility for various benefits, such as a credit for people earning between \$24,000 and \$48,000, families with minor dependents, and those possessing student loans.<sup>21</sup> Further, employees can apply to the tax authority for a special withholding code certificate reflecting unique situations, such as previously accruing losses eligible for deduction.<sup>22</sup>

Taxpayers obtain a withholding code by answering an anonymous questionnaire available on the tax authority's website.<sup>23</sup> The result of these questions generates a code corresponding to a series of potential circumstances (*e.g.*, one employer, income of \$75,000, one minor dependent). Thereafter, taxpayers furnish the applicable withholding code to their employers.<sup>24</sup> If taxpayers fail to do so, withholding is instead applied at a higher-than-normal default rate of 45 percent.<sup>25</sup> Anytime taxpayers' circumstances change, they can return to the tax authority's website and obtain a revised withholding code, which in turn they forward to their employer. Likewise, if the tax authority determines that taxpayers are using an incorrect withholding code, it will send them a letter asking them to return to the website and update the applicable withholding code.<sup>26</sup>

The use of withholding codes protects taxpayer privacy in that employers have no transparency into underlying taxpayer information. Employers simply receive a code that tells them how much to withhold and remit each pay period. They have no knowledge regarding the circumstances of employees that cause a given code to be generated or revised. Further, employers are spared the burden of processing multiple Forms W-4 and protecting the private tax information with which they are entrusted. Rather, they can undertake withholding based on a specific, government-issued code on which they can rely and that minimizes the possibility of harmful data breaches.

18 New Zealand Inland Revenue, *What is my tax code?* (Mar. 31, 2017) <http://www.ird.govt.nz/contact-us/topfive/four/tax-code-index.html?id=201711MegaMenu>.

19 *Id.*

20 *Id.*

21 New Zealand Inland Revenue, *Work Out Your Tax Code* (Dec. 4, 2015) <http://www.ird.govt.nz/how-to/taxrates-codes/workout/>; New Zealand Inland Revenue, *Independent Earner Tax Credit* (July 20, 2017) <http://www.ird.govt.nz/income-tax-individual/tax-credits/ietc/?id=201512TaxRateCalculator>.

22 International Bureau of Fiscal Documentation (IBFD), *New Zealand – Country Analysis 1. Individual Income Tax* (Oct. 1, 2017) 1.10.3, *Withholding taxes*.

23 New Zealand Inland Revenue, *What is my tax code?* (Mar. 31, 2017) <http://www.ird.govt.nz/contact-us/topfive/four/tax-code-index.html?id=201711MegaMenu>.

24 *Id.*

25 IBFD, *New Zealand – Country Analysis 1. Individual Income Tax* (Oct. 1, 2017) 1.10.3.1, *Employment Income*.

26 New Zealand Inland Revenue, *What is my tax code?* (Mar. 31, 2017) <http://www.ird.govt.nz/contact-us/topfive/four/tax-code-index.html?id=201711MegaMenu>. For a more in-depth discussion of the New Zealand tax system and the use of withholding codes, see Research Study: *A Conceptual Analysis of Pay-As-You-Earn (PAYE) Withholding Systems as a Mechanism for Simplifying and Improving U.S. Tax Administration*, *infra*.

Another approach aimed at increasing the simplicity and accuracy of withholding at source is to expand the scope of PAYE itself. In the U.K., for instance, PAYE is not only applied to a broader range of income, but is more nimble than in the U.S. As technology improved, the U.K. sought to accommodate changing work patterns and increase the precision and efficiency of tax collection by updating PAYE. In 2009, the U.K. created the National Insurance and PAYE Service (NPS) to compile and maintain in a single location records relating to earnings, tax, and National Insurance.<sup>27</sup> Then, in 2013, the U.K. began requiring most employers to report PAYE income tax information to the tax authority in real time.<sup>28</sup> The ability to maintain and access a single taxpayer record in real time allows for more accurate and efficient tax determinations and collections throughout the year, while also facilitating a new benefits payment system, the Universal Credit.<sup>29</sup>

In order to cover the maximum number of taxpayers as comprehensively as possible under its PAYE system, the U.K. takes some different approaches than those adopted by the U.S. In particular, U.K. taxpayers file and are taxed individually regardless of their family status.<sup>30</sup> By contrast, the U.S.'s retrospective approach to administering tax benefits, such as the Earned Income Tax Credit, with reference to the ongoing existence of the family unit, places significant limitations on the number of tax returns to which a PAYE system could be applied.<sup>31</sup>

In the U.K., withholding at source occurs on a range of income beyond wage earnings, including royalties, pensions, and annuities.<sup>32</sup> Additionally, certain other categories of income, such as capital gains under an £11,700 threshold and dividends under a £5,000 threshold, that do not easily lend themselves to a PAYE system of tax collection, are exempted from taxation.<sup>33</sup> Moreover, beginning with a 2013 phase-in, the U.K. has generally administered benefits and support programs on a direct payment basis, rather than through the tax system.<sup>34</sup> These adjustments make it easier for PAYE to operate very broadly and to collect the full annual tax liability from the majority of U.K. taxpayers during the course of the year.

27 David Gauke, *PAYE Story*, *Tax'n* (Sept. 21, 2011), <http://www.taxation.co.uk/taxation/Articles/2011/09/21/29571/payee-story>. Note, National Insurance in the U.K. is similar in concept to Social Security in the U.S.

28 Jessica Winch, Q&A: *Why Your PAYE is Switching to 'Real Time'*, *TELEGRAPH*, (Apr. 5, 2013), <http://www.telegraph.co.uk/finance/personalfinance/tax/9973700/QandA-Why-your-PAYE-tax-is-changing-to-real-time.html>. As used herein, the term "real time" means contemporaneously or instantaneously, as the case may be.

29 *Id.*

30 William G. Gale and Janet Holtzblatt, *On the Possibility of a No-Return Tax System*, *L NAT'L LAW TAX J.* no. 3, 1997, 475, 477-479.

31 National Taxpayer Advocate 2016 Annual Report to Congress 325-357. For a more in-depth discussion of this issue, see Research Study: *A Conceptual Analysis of Pay-As-You-Earn (PAYE) Withholding Systems As a Mechanism for Simplifying and Improving U.S. Tax Administration*, *infra*.

32 IBFD, United Kingdom - Country Analysis 1. Individual Income Tax (Jan. 1, 2017) 1.3.3, *Pension income*; 1.10.3, *Withholding taxes*.

33 Her Majesty's Revenue and Customs (HMRC), *Capital Gains Tax*, <https://www.gov.uk/capital-gains-tax/print> (last visited Nov. 19, 2018); HMRC, *Dividends Allowance Factsheet* (Aug. 17, 2015). <https://www.gov.uk/government/publications/dividend-allowance-factsheet/dividend-allowance-factsheet>. See also IBFD, United Kingdom - Country Analysis 1. Individual Income Tax (Jan. 1, 2017) 1.3.3, *Pension Income*; 1.10.3, *Withholding taxes*.

34 Department for Work and Pensions, *Universal Credit Announced* (Oct. 5, 2010) <https://www.gov.uk/government/news/universal-credit-introduced>; Department of Work and Pensions, *Universal Credit and You* (Jul. 25, 2018) Sec. 4, <https://www.gov.uk/government/publications/universal-credit-and-you/universal-credit-and-you-a#payments---how-when-and-where>. For a more in-depth discussion of the U.K. PAYE system and similar systems applied in other countries, see Research Study: *A Conceptual Analysis of Pay-As-You-Earn (PAYE) Withholding Systems as a Mechanism for Simplifying and Improving U.S. Tax Administration*, *infra*.

### Free File Fillable Forms Are Available to U.S. Taxpayers, but Do Not Live Up to Their Potential

The IRS Restructuring and Reform Act of 1998 (RRA 98) required the IRS to work with private industry to increase e-filing, and set the goal of having 80 percent of all federal tax returns filed online by the year 2007.<sup>35</sup> Subsequently, the Bush Administration's EZ Tax Filing Initiative directed the IRS to create "a single point of access to free on-line preparation and electronic tax filing services provided by Industry Partners to reduce burden and costs to taxpayers."<sup>36</sup> The Bush Administration's original concept was that the IRS would develop its own digital Form 1040, *U.S. Individual Income Tax Return*, to be accessed through WhiteHouse.gov. IRS leadership, however, determined that the IRS did not have the capacity or resources to develop such a product.<sup>37</sup>

Instead, the IRS partnered with a consortium of private tax return preparation software companies now known as Free File, Inc (FFI).<sup>38</sup> In 2002, FFI agreed to provide low and middle income taxpayers free online return preparation services via an IRS.gov webpage.<sup>39</sup> The agreement allowed the software providers to determine the scope of their offerings, but obligated the IRS to assume oversight responsibilities.<sup>40</sup>

Beyond free tax return preparation services for low and middle income taxpayers, the National Taxpayer Advocate has long contended that the IRS should also provide all taxpayers, regardless of income, with a bare-bones digital version of the paper Form 1040, complete with fillable fields, links to instructions, and math and numeric transfer capacity, along with free e-filing.<sup>41</sup> In response to this advocacy, the 2009 Free File Memorandum of Understanding created Fillable Forms, a forms-based product designed by FFI to make electronic versions of IRS forms and schedules available to all taxpayers.<sup>42</sup>

Currently, the 12 members of FFI offer free federal tax return preparation software products to eligible taxpayers. For the 2018 tax year, taxpayers that have adjusted gross incomes (AGIs) of \$66,000 or less are eligible to use Free File software, while taxpayers with AGIs greater than that amount can use Fillable

35 IRS Restructuring and Reform Act of 1998 (RRA 98), Pub. L. No. 105–206, § 2001(a)(2), 112 Stat. 685, 723 (1998). For a more in-depth discussion of the Free File Program that came about as a result of this legislation, see Most Serious Problem: *Free File: The IRS's Free File Offerings Are Underutilized, and the IRS Has Failed to Set Standards for Improvement*, *supra*. This Most Serious Problem also discusses Free File Fillable Forms, which are the subject of this Legislative Recommendation.

36 Presidential Initiatives: IRS Free File, <https://georgewbush-whitehouse.archives.gov/omb/egov/c-1-3-IRS.html> (last visited Dec. 12, 2018).

37 See Most Serious Problem: *Free File: The IRS's Free File Offerings Are Underutilized, and the IRS Has Failed to Set Standards for Improvement*, *supra*.

38 Treasury Department, *Treasury, IRS Announce New Efforts to Expand E-Filing* (Jan. 30, 2002), <https://www.treasury.gov/press-center/press-releases/Pages/po964.aspx>.

39 Free On-Line Electronic Tax Filing Agreement entered into between the IRS and the Free File Alliance, LLC (effective as of Oct. 30, 2002), <https://www.irs.gov/pub/irs-utl/2002-free-online-electronic-tax-filing-agreement.pdf> (hereinafter 2002 Free File Agreement).

40 2002 Free File Agreement at 3-4.

41 National Taxpayer Advocate 2012 Annual Report to Congress 232-250; National Taxpayer Advocate 2004 Annual Report to Congress 471-477 (Key Legislative Recommendation: *Free Electronic Filing for All Taxpayers*).

42 Fifth Memorandum of Understanding on Service Standards and Disputes Between the Internal Revenue Service and Free File Alliance, LLC (effective as of Oct. 20, 2009), <https://www.irs.gov/pub/irs-utl/2009-fourth-ff-mou.pdf> (hereinafter 2009 Free File MOU).

Forms.<sup>43</sup> These Fillable Forms, however, continue to fall short of the functionality and convenience envisioned by both the Bush Administration and the National Taxpayer Advocate.<sup>44</sup>

## REASONS FOR CHANGE

### Taxpayers and Employers Would Benefit From the Use of a Withholding Code

As explained above in the “Present Law” section, a number of countries, including New Zealand, have adopted a withholding code as a central aspect of their withholding system. The primary benefit of such an approach is that all of a taxpayer’s tax information is protected from disclosure to the employer, while requiring no new disclosures to the tax authority. Basic personal information, such as marital status and other sources of income, will not be made available to the employer, at least not via operation of the income tax system. This wall of separation between employees’ tax information and employers not only protects employees’ privacy, but minimizes the risk of data breaches and charges that employers have misused personal information.

Further, the use of a withholding code, assuming the application of appropriate advances in technology embraced by other countries, can allow for real-time adjustments to the amount of periodic withholding undertaken by employers.<sup>45</sup> The ability to make such adjustments and the increased ease with which taxpayers can report changes in their circumstances allows for an easier and more precise collection of tax liabilities at source.

Additionally, although the provision of taxpayer information to the IRS for purposes of a withholding code determination would not necessarily guarantee simplicity, if properly implemented, such a process would be less cumbersome than redesign and subsequent use of the Form W-4. Moreover, the IRS could and should prioritize accessibility and ease of use by taxpayers when designing a withholding code interface through the use of a mobile-friendly version of the webpage and an automated telephone questionnaire. Further, the IRS could establish safeguards to help ensure that items which should be included in the withholding determination are actually reported and become part of the withholding code. Thus, the adoption of a withholding code, such as that used by New Zealand, would not only preserve privacy, but would be more straightforward for both taxpayers and employers.

### An Expanded PAYE System Would Allow for More Accurate and Efficient Collection of Tax Liabilities at Source

Another mechanism for improving PAYE is to increase its coverage so that it can collect tax liabilities on income items other than wage earnings. Of the 147 million tax returns filed for tax year (TY) 2016, 62 percent reported only income fully captured by seven line items on IRS Form 1040.<sup>46</sup> Accordingly, a relatively large portion of the U.S. taxpayer population earns the vast majority of its income from a limited number of income sources, thus making expanded tax collection via withholding at source

43 See *Free File Software Offers*, <https://apps.irs.gov/app/freeFile/jsp/index.jsp> (last visited Oct. 10, 2018).

44 For example, truly effective Fillable Forms would, among other things, allow users to download tax forms to their personal computers as PDF files, print hard copies of any form or schedule, easily reference IRS publications, instructions, and tax tables via hyperlink, and contact a helpline to obtain troubleshooting assistance.

45 See Legislative Recommendations: *IT Modernization: Provide the IRS with Additional Dedicated, Multi-Year Funding to Replace Its Antiquated Core IT Systems Pursuant to a Plan that Sets Forth Specific Goals and Metrics and Is Evaluated Annually by an Independent Third Party*, *supra*.

46 TAS Research analysis of IRS Compliance Data Warehouse (CDW), Individual Returns Master File (IRTF), Tax Year (TY) 2016 returns. This percentage is based on all filers, not just nonitemizers.

potentially feasible. Figure 2.8.1 shows the incremental tax collection increases that could result from a PAYE regime expanded to cover the top seven sources of income for U.S. individual taxpayers.

**FIGURE 2.8.1, Cumulative Buildup of PAYE TY 2016 Income Items<sup>47</sup>**

Income type(s)	Number of nonitemizing tax returns	Incremental addition	Percentage of nonitemizing returns	Percentage of all tax returns
Wage only	59,300,000	59,300,000	45%	40%
Wage and/or interest	65,600,000	+6,300,000	50%	45%
Wage, interest, and/or pension	71,000,000	+5,300,000	54%	48%
Wage, interest, pension, and/or dividends	73,400,000	+2,500,000	56%	50%
Wage, interest, pension, dividends, and/or capital gains	78,900,000	+5,500,000	60%	54%
Wage, interest, pension, dividends, capital gains, and/or IRA	87,100,000	+8,200,000	66%	59%
Wage, interest, pension, dividends, capital gains, IRA, and/or unemployment	90,700,000	+3,600,000	69%	62%

As the IRS already imposes reporting obligations on payors in each one of these seven income categories, implementing a parallel withholding regime would be straightforward, albeit not simple. Likewise, if various adjustments were made to the tax system such that certain frequently claimed deductions and credits could be included in PAYE, the system could accurately collect tax liabilities during the year for over half of all U.S. taxpayers.<sup>48</sup> Even more coverage could be obtained by devising a mechanism for voluntary withholding by certain independent contractors, such as those participating in the sharing economy.<sup>49</sup> This withholding, however, would only be feasible in the context of payors that exceeded a specified size threshold.

An initial expansion of PAYE should focus on increasing the income sources with respect to which withholding could be applied. Thereafter, if desirable, deductions and credits could be incorporated into the PAYE system, a step that would facilitate the exact withholding of tax liability for substantial numbers of U.S. taxpayers.

Ultimately, an increase in PAYE coverage, be it of modest or more ambitious scope, would yield benefits to both taxpayers and the government. The more income items included in a PAYE regime, the more taxpayers would have their tax liabilities fully collected at source. This circumstance would free

47 IRS, IRTF, CDW, individual returns for TY 2016, data accessed Oct. 1, 2018. The buildup of PAYE income items relies solely on nonitemizing returns, as this the potential PAYE system considered here is designed to cover only those taxpayers claiming the standard deduction. For a more in-depth discussion of the possible limitations on a U.S. PAYE system, see Research Study: *A Conceptual Analysis of Pay-As-You-Earn (PAYE) Withholding Systems as a Mechanism for Simplifying and Improving U.S. Tax Administration*, *infra*.

48 For an in-depth discussion of ways to expand PAYE coverage, see Research Study: *A Conceptual Analysis of Pay-As-You-Earn (PAYE) Withholding Systems as a Mechanism for Simplifying and Improving U.S. Tax Administration*, *infra*.

49 *Improving Tax Administration Today: Hearing Before the S. Subcomm. on Taxation and IRS Oversight of the S. Comm. on Finance*, 115th Cong. (Jul. 26, 2018) (statement of Nina E. Olson, National Taxpayer Advocate); National Taxpayer Advocate 2017 Annual Report to Congress 329-331; National Taxpayer Advocate Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration* 81-82 (Dec. 2017); National Taxpayer Advocate 2017 Annual Report to Congress 165-171.

taxpayers from the potential of paying large year-end tax liabilities and would free the IRS from having to seek payment of those liabilities from taxpayers, some of whom may have already spent the money on living and other expenses. Moreover, an expanded PAYE system would substantially minimize the number and impact of reporting errors made by good-faith taxpayers, as many of the calculation and remittance duties would be undertaken by employers or other third parties.

### Requisite Year-End Tax Reconciliations Could Be Simplified and Streamlined by Robust Fillable Forms

FFI has created a range of electronic tax returns, schedules, and forms, which comprises its Fillable Forms product. According to the IRS, “Taxpayers can download, save and print their tax return/tax return information as .PDF document(s) using their own computer.”<sup>50</sup> Nevertheless, TAS has received complaints that taxpayers are unable to print the Form 1040 from Fillable Forms, and that taxpayers cannot save the Form 1040 and attachments to their own computers upon completion.

Additionally, many of these Fillable Forms have limitations that restrict their usefulness to taxpayers. For example, line 11 of Schedule A will only allow one individual’s personal information to be entered.<sup>51</sup> Similarly, taxpayers are unable to add explanatory statements and still retain eligibility for e-filing.<sup>52</sup> While such caveats will only affect relatively few taxpayers, most Fillable Forms have similarly small limitations, which, taken together, stand as a substantial deterrent to broad use of the program.

Further, the IRS currently does not make available online accounts that would allow taxpayers to access their individual documents and import the data directly into a return. Even if that ability existed, Fillable Forms lack the capacity to perform the required mathematical steps involved in completing the tax return. Although Fillable Forms do exist, taxpayers must populate those forms themselves, perform the needed mathematical operations, and accurately transcribe the results of their computations. Given the multiple steps to be undertaken and the relatively minimal value derived by taxpayers from use of Fillable Forms, it is not surprising that only 0.2 percent of U.S. taxpayers used Fillable Forms in 2017.<sup>53</sup>

As a potential means of increasing this level of usage and enhancing the accuracy of filed returns, the IRS itself should be charged with analyzing and reporting on the feasibility of developing a robust and effective suite of interactive tax returns, schedules, and forms. The starting point of this initiative would be the establishment of individual accounts that taxpayers could access to obtain their real-time tax information and related forms, such as Forms W-2 and 1099. Thereafter, taxpayers should be able to import the data on these forms into their tax returns, which then would automatically perform the necessary calculations to determine tax refunds or liabilities. Further, all of this tax return information should be downloadable, such that it can be used by taxpayers themselves, forwarded to authorized tax return preparers, or imported into tax return preparation software. Such upgraded functionality would significantly expand the use of Fillable Forms and substantially increase the ease and accuracy of tax return preparation.

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50 IRS response to TAS information request (Sept. 7, 2018).

51 IRS, *Available Forms and Limitations* (Nov. 21, 2018) <https://www.irs.gov/e-file-providers/list-of-available-free-file-fillable-forms>.

52 *Id.*

53 IRS response to TAS information request (Sept. 7, 2018).

## EXPLANATION OF RECOMMENDATION

The National Taxpayer Advocate recommends that Congress enact legislation directing the Treasury Department, in consultation with the IRS and the National Taxpayer Advocate, to analyze and report on the feasibility of and steps necessary for: adopting an IRS-determined withholding code as an alternative to the Form W-4 approach currently utilized in U.S. tax administration; expanding withholding at source to encompass not only wages, but taxable interest, pensions, dividends, capital gains, IRA income, unemployment, and eventually certain earnings as an independent contractor; and furnishing information return data to taxpayers electronically for direct importation into tax return preparation software or to authorized tax return preparers.<sup>54</sup>

By doing so, Congress would facilitate important research and thought regarding specific changes that could bring the U.S. tax system into the 21st century and meaningfully enhance the ease with which taxpayers can comply with their tax obligations. Among other things, taxpayers' privacy could be increased through the use of a withholding code issued to employers. Further, by expanding the scope of the U.S. PAYE system, additional withholding at source could be undertaken such that taxpayers would have their tax liabilities collected more accurately throughout the year, and fewer adjustments would be needed during the year-end tax reconciliation process. Finally, the implementation of a truly robust Fillable Forms regime would allow taxpayers to more easily and precisely undertake preparation and filing of their income tax returns.

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<sup>54</sup> If the study indicates that progress toward PAYE is feasible, Congress should consider specifying a target date by which implementation should be completed. Such a deadline had a salutary impact in the case of e-filing goals and likely would have similar benefits in the instant case. See Pub. L. No. 105-206, § 2001(a)(2), 112 Stat. 685, 723 (1998).

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## INDIAN EMPLOYMENT CREDIT: Amend IRC § 45A to Make the Indian Employment Credit an Elective Credit for Employers Who Hire Native Americans

### TAXPAYER RIGHTS IMPACTED<sup>1</sup>

- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to a Fair and Just Tax System*

### PROBLEM

Occasionally, the original intent of Congress in enacting legislation may be frustrated when the law interacts with other, existing provisions. Such is the case for the Indian Employment Credit (IEC), codified in Internal Revenue Code (IRC) § 45A. In 1993, Congress introduced IRC § 45A,<sup>2</sup> a provision that provides a monetary incentive in the form of a tax credit to employers who hire Native Americans who meet all the requirements of the provision.<sup>3</sup> IRC § 45A works by providing a *mandatory* tax credit based on the wages and employee health insurance costs paid by the employer to qualified employees in the taxable year.<sup>4</sup>

The Indian Employment Credit was created to encourage employers to hire more Native American workers in economically distressed communities, since many Native American reservations throughout the United States suffered “from staggering unemployment, nagging poverty, and huge infrastructure deficiencies.”<sup>5</sup> The credit is available only if the Native American employee of the employer claiming the credit lives and works on or near a recognized Indian reservation.<sup>6</sup> Furthermore, only the first \$20,000 of wages of the employee are eligible for this credit and wages paid by the employer to any employee who makes more than \$30,000 per year (adjusted for inflation) are not eligible for this credit.<sup>7</sup>

IRC § 45A is affected by two other provisions within the IRC. First, § 280C prohibits a deduction for the portion of wages and salaries paid in the taxable year which is equal to the sum of credits *determined* under § 45A.<sup>8</sup> This provision effectively prevents a taxpayer from benefitting both from the Indian

- 1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).
- 2 IRC § 45A, Omnibus Budget Reconciliation Act of 1993, Pub. L. No. 103-66 (1993) (as amended by the Bipartisan Budget Act of 2018, Pub. L. No. 115-123, § 40301(a), 132 Stat. 64, 145) (2018)). IRC § 45A does not apply to taxable years beginning after December 31, 2017. See IRC § 45A(f). We are making this recommendation because it is likely that the Indian Employment Credit (IEC) may be extended again by Congress. The Indian Employment Credit has been repeatedly extended by Congress continuously since it was introduced in 1993. The Indian Employment Credit is claimed on IRS Form 8445, *Indian Employment Credit* (2017), <https://www.irs.gov/pub/irs-pdf/f8845.pdf>.
- 3 See IRC § 45A. This credit is often referred to as the “Indian Employment Credit.”
- 4 See IRC § 45A. This provision covers *any* employer, engaged in a trade or business, who pays wages to or health insurance costs for qualified Native American employees. The plain language of the statute indicates that the credit is not elective but rather mandatory. As discussed below, the Tax Court has interpreted the statute in the same way. See *Uniband, Inc. v. Comm’r*, 140 T.C. 230 (2013).
- 5 139 CONG. REC. S7815, 199-200 (daily ed. June 24, 1993) (statement of Senator John McCain) (during floor debate on H.R. 2264, the Senate adopted the provision with the Amendment 537).
- 6 IRC § 45A(c)(1)(C).
- 7 IRC § 45A(c)(2)–(3).
- 8 IRC § 280C.

Employment Credit and another deduction on the same costs. Second, IRC § 38(c) sets a cap on business credits generally, which includes IRC § 45A.<sup>9</sup>

The mandatory nature of IRC § 280C can sometimes result in an employer's tax liability *increasing* because it could result in a *mandatory* reduction of the employer's IRC § 162 deduction by the amount allowed under IRC § 45A while the allowable amount of credit is limited under the IRC § 38(c) general business credit limitation.<sup>10</sup> As mentioned earlier, the mandatory nature of IRC § 45A also contributes to this problem. This outcome, resulting in a disadvantage for the employer that would have been better off not having hired Native American employees, frustrates the original purpose of the credit.

### EXAMPLE

Company X is a small sand, gravel, and stone company which produces materials to be used for construction. Company X has been located on an Indian reservation in Pierre, South Dakota since 1990. It hires Native American members of the Sioux Nation reservation, located near the Cheyenne River, to work as construction equipment operators and warehouse technicians.

In Tax Year (TY) 1993 (*i.e.*, the base year for the credit), Company X's qualified wages paid for its qualified Native American employees were \$10,000 per year for each employee. Company X had two qualified Native American employees in TY 1993 with qualified wages of \$20,000 (\$10,000 each). In TY 2016, Company X had qualified wages of \$60,000 and two qualified employees (\$30,000 each).<sup>11</sup> Company X had no qualified employee health insurance costs in either tax year. The IRC § 280C limitation is applied separately to the TY 2016 for which the credit is being computed and to the base year—TY 1993. Thus, Company X's wages of \$60,000 for TY 2016 is limited to \$40,000 (*i.e.*, due to the \$20,000 cap for each employee). The \$20,000 for TY 1993 is then subtracted from the TY 2016 amount (\$40,000), leaving \$20,000, and the correct credit is 20 percent of that, or \$4,000. However, Company X has reached the cap of all allowable IRC § 38(c) business credits, and the Indian Employment Credit cannot reduce Company X's tax liability any further.

As a result, the company has a low Indian Employment Credit which cannot be claimed; however, to Company X's disadvantage, the IRS reduced Company X's total deductible wages that it could have claimed under the IRC § 162 business expenses by the Indian Employment credit amount of \$4,000 determined under IRC § 45A. The net result of the IRS's adjustments (*i.e.*, the disallowance of the Indian employment credit and the reduction of total wage deductions) resulted in a greater amount of tax for Company X.

Upon finding out about this disadvantage in the reduction of its total deductible wages, Company X tried to file an amended tax return arguing that IRC § 45A is elective, so that it can elect not to take the credit and not allow the IRS determination to stand. The IRS rejected the correction, however, arguing that the credit is mandatory, citing to the Tax Court's plain language interpretation of IRC § 45A in *Uniband*.<sup>12</sup>

<sup>9</sup> IRC § 38(c)(1).

<sup>10</sup> IRC § 38(c)(1); IRC § 280C(a). IRC § 280C(a) disallows a deduction for an amount of the wages equal to the credit for employment credits, including for IRC § 45A. The Indian Employment Credit is also subject to the limitations and carryover rules in IRC §§ 38 and 39. See IRC §§ 38 and 39.

<sup>11</sup> These figures are adjusted for inflation under IRC § 415(d). Beginning in 2009, the original § 45A(c)(2) limit of \$30,000 to be considered a qualified employee was adjusted for inflation to be \$45,000. See IRS Notice 2008-102, 2008-2 C.B. 1106.

<sup>12</sup> *Uniband, Inc. v. Comm'r*, 140 T.C. 230, 271 (2013) (internal citations omitted).

## RECOMMENDATION

In the event that Congress extends IRC § 45A, as it has in the past, and to promote the taxpayers' *rights to pay no more than the correct amount of tax and to a fair and just tax system*, the National Taxpayer Advocate recommends Congress amend the statute to make the Indian Employment Credit elective instead of a mandatory credit for employers who hire eligible Native American employees.<sup>13</sup>

## PRESENT LAW

In 1993, Congress created the Indian Employment Credit, to provide an incentive in the form of a tax credit to employers who hire eligible Native Americans who meet all the requirements of the provision.<sup>14</sup> For tax years beginning before 2018,<sup>15</sup> an employer may claim the Indian Employment Credit equal to 20 percent of the excess of the sum of qualified wages and the qualified employee health insurance costs paid or incurred during a tax year, over the amount paid or incurred by the employer during TY 1993 (the base year).<sup>16</sup> This credit must be claimed on the IRS Form 8445, *Indian Employment Credit*.<sup>17</sup> For the purposes of the Indian Employment Credit, the aggregate amount of the qualified wages and employee health insurance costs for any employee allowed for any given year is \$20,000 per tax year.<sup>18</sup> Furthermore, employees of the employer receiving wages or health insurance benefits above \$30,000 are not eligible to be included by the employer for this credit.<sup>19</sup> To qualify for this credit:

- 1) The employee or his or her spouse must be an enrolled member of an Indian tribe;<sup>20</sup>
- 2) The services performed by the employee for the employer must be performed within an Indian reservation;<sup>21</sup>
- 3) The employee's principal place of abode while performing the services must be on or near the Indian reservation where the services are performed;<sup>22</sup>
- 4) Over 50 percent of the wages paid or incurred by the employer to the employee during the tax year must be for services performed in the employer's trade or business,<sup>23</sup> and

13 On January 16, 2019, Senate Committee on Finance Chairman Charles Grassley stated that it is "too late" to renew extenders (such as IRC § 45A) for the 2018 filing season but that the Committee aims to renew extenders later in the year. See *Grassley: Time Up for Tax Extenders*, CONGRESSIONAL QUARTERLY NEWS (Jan. 16, 2019) (statement of Senate Committee on Finance Chairman Charles Grassley).

14 IRC § 45A, Omnibus Budget Reconciliation Act of 1993, Pub. L. No. 103-66 (1993) (as amended by the Bipartisan Budget Act of 2018, Pub. L. No. 115-123, § 40301(a), 132 Stat. 64, 145) (2018)). IRC § 45A does not apply to taxable years beginning after December 31, 2017. See IRC § 45A(f). We are making this recommendation because it is likely that the Indian Employment Credit may be extended again by Congress. The Indian Employment Credit has been repeatedly extended by Congress continuously since it was introduced in 1993. Most recently, in February 9, 2018, it was extended to apply to all tax years before December 31, 2017. See Pub. L. No. 115-123, § 40301(a), 132 Stat. 64, 145 (2018).

15 See IRC § 45A(f).

16 IRC § 45A(a)–(c).

17 IRS Form 8445, *Indian Employment Credit* (2017), <https://www.irs.gov/pub/irs-pdf/f8845.pdf>.

18 IRC § 45A(b)(3).

19 IRC § 45A(c)(2).

20 IRC § 45A(c)(1)(A).

21 IRC § 45A(c)(1)(B). For the purposes of this credit, an Indian reservation means a reservation as defined in § 3(d) of the Indian Financing Act of 1974 or § 4(10) of the Indian Child Welfare Act of 1978. See also *Instructions for Form 8845, Indian Employment Credit* (Feb. 27, 2018), <https://www.irs.gov/pub/irs-pdf/i8845.pdf>.

22 IRC § 45A(c)(1)(C). The statute restricts the employee's place of employment to on or near an Indian reservation in which the employment services are performed. The term "Indian reservation" is defined by IRC § 168(j)(6).

23 IRC § 45A(c)(4).

5) the employees cannot be a five percent or more owner of the company,<sup>24</sup> or a person employed in the gambling and gaming industry.<sup>25</sup>

Furthermore, under IRC § 38(c)(1), business credits, such as the Indian Employment Credit, may not exceed the excess (if any) of the taxpayer's net income tax over the greater of either the tentative minimum tax for the taxable year or 25 percent of so much of the taxpayer's net regular tax liability that exceeds \$25,000.<sup>26</sup> This further places a limitation in the form of a cap on the Indian Employment Credit and was aimed at preventing business taxpayers from using credits to reduce their tentative minimum tax.<sup>27</sup>

## REASONS FOR CHANGE

This potential disincentive that exists with using the Indian Employment Credit in certain situations can be avoided by making the credit an *elective* credit instead of a *mandatory* credit.<sup>28</sup> As explained above, the Indian Employment Credit was introduced to create an incentive to hire Native Americans on Indian reservations.<sup>29</sup> The credit was intended to “in some way attempt to address endemic and severe problems that exist on Indian country,” which exist because of “the failure of [the United States] to live up to treaty obligations.”<sup>30</sup>

A 2013 United States Tax Court case, *Uniband, Inc. v. Commissioner*, provides useful insight into how the credit is calculated and whether it is mandatory.<sup>31</sup> In *Uniband*, the taxpayer took its entire IRC §162 business deduction<sup>32</sup> instead of reducing the deduction and claiming the Indian Employment Credit, which the taxpayer was entitled to take.<sup>33</sup> The taxpayer in *Uniband* did this because the amount of the credit the company was eligible for was limited under the general business credit in IRC §38(c)(1).<sup>34</sup> IRC § 45A only provides an amount *determined* that becomes a component of what is *allowed* as a credit by IRC § 38(a).<sup>35</sup> The IRS adjusted the taxpayer's return by applying the limited credit and reducing

24 IRC § 45A(c)(5)(B).

25 IRC § 45A(c)(5)(C).

26 IRC § 38(c)(1). The statute defines “net income tax” as the sum of the regular tax liability and the tax imposed by IRC § 55 reduced by the credits allowable under subparts A and B of this part (*i.e.*, §§ 21 - 30D). IRC § 38(c)(1). The statute defines “net regular tax liability” as the regular tax liability reduced by the sum of the credits allowable under subparts A and B of this part (*i.e.*, §§ 21 - 30D). IRC § 38(c)(1). The term “tentative minimum tax” means the amount determined under IRC § 55(b)(1) (defining the term “qualified wages”).

27 See H.R. REP. No. 103-213, at 720-723 (1993) (Conf. Rep.). See also *Uniband, Inc. v. Comm’r*, 140 T.C. 230, 271 (2013) (internal citations omitted). The Tax Cuts and Jobs Act of 2017 repealed the corporate alternative minimum tax. See Pub. L. No. 115-97, § 12001, 131 Stat. 2054, 2092 (2017).

28 The Indian Employment Credit has been repeatedly extended by Congress since it was introduced in 1993. Most recently, in February 9, 2018, it was extended to apply to all tax years before December 31, 2017. See Pub. L. No. 115-123, § 40301(a), 132 Stat. 64, 145 (2018) (amending the provision to make it applicable to taxable years beginning after Dec. 31, 2016, as provided by § 40301(b) of Pub. Law. No. 115-123, which appears as a note to this section) amended subsection (f) by substituting “December 31, 2017” for “December 31, 2016”).

29 139 CONG. REC. S7815, 199-200 (daily ed. June 24, 1993).

30 *Id.* (statement of Senator John McCain) (during floor debate on H.R. 2264, the Senate adopted the provision with the Amendment 537).

31 *Uniband, Inc. v. Comm’r*, 140 T.C. 230 (2013).

32 IRC § 162(a) allows a deduction for all the ordinary and necessary expenses paid or incurred during the taxable year in carrying on any trade or business. IRC § 262, however, provides that no deduction is allowed for personal, living, or family expenses. IRC § 162(a); IRC § 262.

33 *Uniband, Inc. v. Comm’r*, 140 T.C. 230, 241 (2013).

34 *Id.* at 270.

35 *Id.* at 271.

the taxpayer's IRC §162 deduction by the full amount determined (but not allowed) under IRC § 45A.<sup>36</sup> This resulted in a net disadvantage to the taxpayer.<sup>37</sup>

The taxpayer in *Uniband* presented two arguments against the IRS's interpretation.<sup>38</sup> First, the taxpayer argued that the Indian Employment Credit is not mandatory, and therefore if a taxpayer chooses not to claim it then the taxpayer's IRC §162 deduction should similarly not be reduced.<sup>39</sup> Second, the taxpayer argued that IRC § 280C should be read as only limiting the deduction to the extent that the Indian Employment Credit is limited under IRC § 38(c)(1) to avoid frustrating the purpose of the Indian Employment Credit, which is to encourage businesses to hire more Native Americans.<sup>40</sup>

The Tax Court disagreed with both of the taxpayer's assertions in *Uniband*.<sup>41</sup> The court interpreted IRC § 280C as not contemplating the amount of credit that is "allowed," but rather requiring a deduction of the amount of credit that is "determined."<sup>42</sup> Therefore, the Tax Court reasoned that IRC § 280C is independent of whether the general business credit, and by extension the Indian Employment Credit, is fully allowed under IRC § 38(a) or limited by IRC § 38(c)(1).<sup>43</sup> The Tax Court declined to accept the taxpayer's policy argument, which it determined departed from the "plain language" reading of the statute as currently written.<sup>44</sup> Additionally, the Court pointed out that Congress can fix this issue by making it an elective credit.<sup>45</sup> The Tax Court's plain meaning interpretation of IRC § 45A and its reference to the legislative history of the research credit provision in IRC § 51(g), a different tax credit, with the same drawbacks as IRC § 45A, indicates that the Tax Court believes that the sole remedy is legislative, not judicial.<sup>46</sup>

Figure 2.9.1 is a table that shows the total number of taxpayers who have claimed the Indian Employment Credit for the past three tax years. As shown, the greatest amount of Indian Employment Credit claimed in the past three tax years was through IRS Form 1040, by individual taxpayers. In TY 2017, a total of 6,544 individual taxpayers claimed it on Form 1040, compared to 170 estates and trusts, and 455 corporations. As shown, in TY 2016, a total of 8,399 individual taxpayers claimed it on Form 1040, compared to 225 estates and trusts, and 948 corporations. Furthermore, in TY 2015, a total of 8,269 individual taxpayers claimed it on Form 1040, compared to 264 estates and trusts, and 978 corporations.

36 *Uniband, Inc. v. Comm'r*, 140 T.C. 230, 241 (2013).

37 *Id.*

38 *Id.* at 270.

39 *Id.*

40 *Id.* at 270-72.

41 *Id.*

42 *Id.*

43 *Id.* at 271.

44 *Id.* at 272.

45 *Id.*

46 *Id.*

**FIGURE 2.9.1, Indian Employment Credit Statistics for TY 2015–2017<sup>47</sup>**

Type of IRS Form Used by Taxpayers	Form 1040 (Individual Taxpayers)			Form 1041 (Estates and Trusts)			Corporations		
	TY2015	TY2016	TY2017	TY2015	TY2016	TY2017	TY2015	TY2016	TY2017
Total No. of Taxpayers Claiming I.E.C.	8,269	8,399	6,544	264	225	170	978	948	455
Total I.E.C. Claimed in U.S. Dollars	\$657,714,356	\$1,952,242,529	\$765,705,903	\$1,013,260	\$819,882	\$351,413	\$73,281,571	\$65,757,183	\$14,614,049

## EXPLANATION OF RECOMMENDATION

Congress can model IRC § 45A after the language in the work opportunity credit in IRC § 51(j), which states that “[a] taxpayer may elect to have this section not apply for any taxable year.”<sup>48</sup> The Tax Court in *Uniband* also pointed to other examples in the IRC where similar credits were elective.<sup>49</sup>

Considering the legislative purpose of IRC § 45A, described above, it would make sense to prevent a disincentive for employers by making the credit elective rather than mandatory. As the Tax Court observed, “Congress has shown that it is aware of the conundrum of the sort” and “it knows how to fix it when it wants to—*i.e.*, by allowing a credit determination to be optional in certain cases.”<sup>50</sup>

The Indian Employment Credit can be made elective or optional for employers by adding language such as in IRC § 51(j)(1) to the section 45A that would allow taxpayers to opt out in any taxable year.<sup>51</sup> That way, in situations in which employers are disadvantaged by taking the credit, they may avoid the disadvantage by electing not to claim the credit. Otherwise, the legislative intent to create an economic incentive to benefit Native American communities is frustrated because businesses would think twice about hiring Native American employees.

47 This data was obtained on Jan. 31, 2019, from the Business Returns Transaction File on the IRS Compliance Data Warehouse (CDW) (returns processed as of cycle 43) (data through Oct. 2018) and from the Individual Returns Transaction File on the IRS CDW (returns processed as of cycle 43) (data through Oct. 2018). The calculations for corporations in the figure combined data from IRS Forms 1120F, 1120L, 1120, 1120C, 1120PC, and 1120REIT for each tax year (TY) (TY 2015, TY 2016, and TY 2017).

48 IRC § 51(j)(1).

49 See *Uniband, Inc. v. Comm’r*, 140 T.C. 230, 271 n.33 (2013) (citing to elective language in IRC § 51(j)(1) (“A taxpayer may elect to have this section [work opportunity credit] not apply for any taxable year”); IRC § 40(f)(1) (“A taxpayer may elect to have this section [alcohol fuel credit] not apply for any taxable year”); IRC § 43(e)(1) (“A taxpayer may elect to have this section [enhanced oil recovery credit] not apply for any taxable year”); IRC § 45B(d)(1) (“This section [credit for portion of employer Social Security taxes paid with respect to employee cash tips] shall not apply to a taxpayer for any taxable year if such taxpayer elects to have this section not apply for such taxable year”); IRC § 45E(e)(3) (“This section [small employer pension plan startup cost credit] shall not apply to a taxpayer for any taxable year if such taxpayer elects to have this section not apply for such taxable year”); IRC § 45H(g) (“No credit [for production of low sulfur diesel fuel] shall be determined under subsection (a) for the taxable year if the taxpayer elects not to have subsection (a) apply to such taxable year”).

50 See *Uniband, Inc. v. Comm’r*, 140 T.C. 230, 270 (2013).

51 See IRC § 51(j)(1).

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## CHILD TAX CREDIT: Amend Internal Revenue Code § 24(c)(1) to Conform With § 152(c)(3)(B) for Permanently and Totally Disabled Individuals Age 17 and Older

### PROBLEM

In general, Internal Revenue Code (IRC) § 24 entitles a taxpayer to claim a Child Tax Credit (CTC) of up to \$2,000 (for tax years (TYs) 2018-2025) for each qualifying child, as defined in IRC § 152(c), who is under age 17 at the end of the TY (with an exception for certain noncitizens).<sup>1</sup> The amount of the credit is applied to any taxes due and, in some instances, is refundable (the refundable portion is known as the Additional Child Tax Credit, or ACTC).<sup>2</sup>

Under IRC § 24(c)(1), a qualifying child for the child tax credit must generally meet the definition of a qualifying child as defined in IRC § 152(c) with an exception for certain noncitizens and with a different age requirement: the child must not have attained the age of 17. However, IRC § 152(c)(3)(B) provides an exception to the general age requirement within the definition of a qualifying child under IRC § 152(c), if the individual is permanently and totally disabled<sup>3</sup> at any time during the calendar year, permitting a guardian to claim as a qualifying child an individual who is totally and permanently disabled, regardless of age.<sup>4</sup>

The result is that a guardian may have a permanently and totally disabled dependent older than the general age limit who meets the definition of a qualifying child for purposes of other sections of the IRC,<sup>5</sup> but not for purposes of the CTC.<sup>6</sup> This difference undermines the *right to a fair and just tax system*.<sup>7</sup>

Changes to the tax law under the Tax Cuts and Jobs Act (TCJA) render this issue more pressing.<sup>8</sup> While the TCJA added a new credit of \$500 for other dependents under IRC § 24 and expanded the CTC, it also suspended dependency exemptions, leaving taxpayers with a permanently and totally disabled child who has attained the age of 17 potentially worse off than under the previous tax law.<sup>9</sup>

- 1 Internal Revenue Code (IRC) § 24(a) and (c), as modified by the Tax Cuts and Jobs Act (TCJA), P.L. No. 115-97, § 11022. The amendment to section 24 by the TCJA is in effect for tax years 2018 through 2025. The amount of the Child Tax Credit (CTC) is reduced (but not below zero) by \$50 for each \$1,000 (or fraction thereof) by which the taxpayer's modified adjusted gross income exceeds the threshold amount (\$400,000 in the case of a joint return, \$200,000 for any other filing status). IRC § 24(b)(1) and (2) as modified by the TCJA, P.L. No. 115-97, § 11022.
- 2 IRC § 24(d). For a further discussion of the National Taxpayer Advocate's concerns about various family status provisions of the IRC, see National Taxpayer Advocate 2017 Annual Report to Congress 453-461; National Taxpayer Advocate 2016 Annual Report to Congress 325-357.
- 3 The definition of permanently and totally disabled for this purpose is contained in IRC § 22(e)(3).
- 4 IRC § 152(c)(3).
- 5 See, e.g., IRC § 32.
- 6 IRC § 24(c)(1).
- 7 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).
- 8 Pub. L. No. 115-97 (2017).
- 9 TCJA, Pub. L. No. 115-97, §§ 11022 and 11041 (2017). These provisions are effective for tax years 2018 through 2025.

## EXAMPLE

Taxpayers Jane and John Doe are parents of a permanently and totally disabled 27-year-old son, Will. On their 2017 tax return, the taxpayers claimed a dependency exemption of \$4,050 and a CTC of \$1,000 for their son. The IRS allowed the dependency exemption but disallowed the CTC, because their son was over age 17.

Congress passed tax reform legislation at the end of 2017 that effective for TYs 2018-2025, suspended dependency exemptions, but added a \$500 credit for a dependent who is not a qualifying child for the CTC. As a result, Jane and John Doe may not now claim a dependency exemption or a CTC for Will, and are only eligible for a \$500 credit.

## RECOMMENDATION

To assist taxpayers with a permanently and totally disabled child age 17 or older, the National Taxpayer Advocate recommends that Congress amend IRC § 24(c)(1) to provide that, in general, the term “qualifying child” means a qualifying child (as defined in section 152(c)) of the taxpayer who has not attained age 17 or who meets the exception under IRC § 152(c)(3)(B), which provides a special rule for an individual who is permanently and totally disabled.

## PRESENT LAW

For TYs 2018 through 2025, IRC § 24 entitles a taxpayer to claim a CTC of up to \$2,000 for each qualifying child, as defined in IRC § 152(c), who is under age 17 at the end of the tax year (with an exception for certain noncitizens).<sup>10</sup> The amount of the credit is applied to any taxes due and, in some instances, is refundable (the refundable portion is known as the ACTC).<sup>11</sup>

IRC § 24(c)(1) provides that, a qualifying child for the CTC must meet the definition of a qualifying child as defined in IRC § 152(c) with an exception for certain noncitizens and with a different age requirement: the child must not have attained the age of 17. IRC § 152(c)(3)(B) provides an exception to the general age requirement for a qualifying child in IRC § 152(c), if the individual is permanently and totally disabled<sup>12</sup> at any time during the calendar year, permitting a guardian to claim as a qualifying child an individual who is totally and permanently disabled, regardless of age.<sup>13</sup> A similar exception does not apply for purposes of the age requirement under IRC § 24(c).

The TCJA added a new credit for other dependents under IRC § 24 for a dependent who is not a qualifying child for purposes of the CTC, it significantly increased the CTC, and it suspended dependency exemptions.<sup>14</sup>

10 IRC § 24(a) and (c), as modified by the TCJA, P.L. No. 115-97, § 11022. See § 24(h). The amount of the CTC is reduced (but not below zero) by \$50 for each \$1,000 (or fraction thereof) by which the taxpayer’s modified adjusted gross income exceeds the threshold amount (\$400,000 in the case of a joint return, \$200,000 for any other filing status). IRC § 24(b)(1) and (2) as modified by the TCJA, P.L. No. 115-97, § 11022.

11 IRC § 24(d). For a further discussion of the National Taxpayer Advocate’s concerns about various family status provisions in the IRC, see National Taxpayer Advocate 2017 Annual Report to Congress 453-461; National Taxpayer Advocate 2016 Annual Report to Congress 325-357.

12 The definition of permanently and totally disabled for this purpose is contained in IRC § 22(e)(3).

13 IRC § 152(c)(3).

14 TCJA, Pub. L. No. 115-97, §§ 11022 and 11041 (2017). These changes to the tax law are effective for tax years 2018-2025.

## REASONS FOR CHANGE

A recent court case illustrates the impact this disparity has on families with permanently and totally disabled adult children, particularly under the current law due to the suspension of dependency exemptions. In *Polsky v. United States*, the court found that the taxpayers were not entitled to the CTC for their daughter.<sup>15</sup> The Polskys are parents of a permanently and totally disabled adult. On their 2010 and 2011 tax returns, the taxpayers claimed their daughter as a qualifying child for the CTC, and the IRS disallowed the credit as the child was over age 17 and did not meet the age requirement to be a qualifying child for the CTC. On appeal, the taxpayers argued that IRC § 152(c)(3)(B) controls, not the general age requirement in IRC § 24. IRC § 24(c)(1) states generally that a qualifying child must meet the requirements of IRC § 152(c) and be under the age of 17. IRC § 152(c)(3)(B) provides that an individual meets the age requirements for purposes of IRC § 152(c)(3)(A) if at any time during the year the individual was permanently and totally disabled. The Polskys argued that as their daughter was permanently and totally disabled in the years at issue and, therefore, was a qualifying child under IRC § 152(c), she was also a qualifying child for purposes of IRC § 24. The court agreed with the rationale of the lower court's decision that IRC § 24 incorporates the basic requirements of IRC § 152(c) and adds the additional age limitation of not having attained age 17 for purposes of the CTC. The exception under IRC § 152(c)(3)(B) for permanently and totally disabled individuals is intended to allow taxpayers, such as the Polskys, to continue to claim the individual as a dependent, so long as their daughter remains permanently and totally disabled and meets the other requirements under IRC § 152(c). Thus, the court held that the taxpayers were not entitled to claim the CTC for the years at issue.<sup>16</sup>

As the Court noted in the case of *Polsky v. United States*, while IRC § 24(c)(1) incorporates the basic requirements of IRC § 152(c), it adds the additional requirement that the child must not have attained the age of 17.<sup>17</sup> The Court postulated that § 152(c)(3)(B) was crafted to allow taxpayers to extend the dependency exemption, regardless of the age of the permanently and totally disabled child, and IRC § 24(c)(1) was crafted to end the CTC once a child attains the age of 17. However, under the TCJA, the dependency exemption under IRC § 151 has been suspended through 2025.<sup>18</sup> While taxpayers who have a dependent who does not meet the definition of a qualifying child for purposes of the CTC may now claim a \$500 credit for other dependents, the changes to the law by TCJA may leave taxpayers with a permanently and totally disabled child in a worse position than before the enactment of the TCJA and undermine the *right to a fair and just tax system*.<sup>19</sup>

## EXPLANATION OF RECOMMENDATION

TAS reviewed tax returns filed for TY 2017 and found that approximately 380,000 returns were filed claiming a dependent who was also receiving Social Security Disability Income and was at least 15 years younger than the primary or secondary taxpayer on the tax return.<sup>20</sup> While this information is not a perfect proxy for the number of taxpayers claiming a permanently and totally disabled child age 17 or older as a dependent (due to the limitations of data the IRS has available), it provides a picture of the number of families who may be impacted by the age limitation of the CTC and the suspension

15 844 F.3d 170 (3d Cir. 2016).

16 *Polsky v. United States*, 844 F.3d 170 (3d Cir. 2016).

17 *Id.*

18 TCJA, Pub. L. No. 115-97, § 11041 (2017).

19 *Id.*

20 IRS, Compliance Data Warehouse (CDW), data retrieved by TAS (Dec. 6, 2018).

of the dependency exemption for TYs 2018-2025. Compared to a family without a permanently and totally disabled child age 17 or older, these families may face higher costs associated with child care, exacerbating the impact of not being able to claim the CTC. In the most recent National Survey of Children with Special Health Care Needs, nearly 22 percent of all respondents indicated that the condition their child has creates financial problems for their family, while nearly 39 percent of families who indicated their children have conditions that usually, always, or a great deal affect the child's abilities report financial problems.<sup>21</sup> Amending IRC § 24(c)(1) to conform with the requirements of IRC § 152(c)(3)(B) will assist these families and support the *right to a fair and just tax system*.

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21 Department of Health and Human Services, *The National Survey of Children with Special Health Care Needs* 53 (2010).

## MOST LITIGATED ISSUES: Introduction

Internal Revenue Code (IRC) § 7803(c)(2)(B)(ii)(X) requires the National Taxpayer Advocate to identify in her Annual Report to Congress the ten tax issues most litigated in federal courts (Most Litigated Issues).<sup>1</sup> The National Taxpayer Advocate may analyze these issues to develop legislative recommendations to mitigate the disputes resulting in litigation.

TAS identified the Most Litigated Issues from June 1, 2017, through May 31, 2018, by using commercial legal research databases. For purposes of this section of the Annual Report, the term “litigated” means cases in which the court issued an opinion.<sup>2</sup> This year’s Most Litigated Issues are, in order from most to least cases:

- Accuracy-Related Penalty (IRC §§ 6662(b)(1) and (2));<sup>3</sup>
- Trade or Business Expenses (IRC § 162(a) and related Code sections);
- Summons Enforcement (IRC §§ 7602(a), 7604(a), and 7609(a));
- Gross Income (IRC § 61 and related Code sections);
- Collection Due Process (CDP) hearings (IRC §§ 6320 and 6330);
- Failure to File Penalty (IRC § 6651(a)(1)), Failure to Pay Penalty (IRC § 6651(a)(2)), and Failure to Pay Estimated Tax Penalty (IRC § 6654);
- Civil Actions to Enforce Federal Tax Liens or to Subject Property to Payment of Tax (IRC § 7403);
- Charitable Contribution Deductions (IRC § 170);
- Schedule A Deductions Under IRC §§ 211-224; and
- Frivolous issues penalty (IRC § 6673 and related appellate-level sanctions).

Two topics, Schedule A deductions and the frivolous issues penalty were not identified as Most Litigated Issues last year. These issues replaced the family status issues and relief from joint and several liability as Most Litigated Issues.<sup>4</sup> Frivolous issues last appeared in the Most Litigated Issues section in 2016<sup>5</sup> while itemized deductions reported on Schedule A of IRS Form 1040 did not appear in the National Taxpayer Advocate’s Annual Report to Congress since 2002.<sup>6</sup> Accuracy-related penalties remained the top litigated issue this year, and we identified 120 cases, 18 less than the 138 cases we identified last year

1 Federal tax cases are tried in the United States Tax Court, United States District Courts, the United States Court of Federal Claims, United States Bankruptcy Courts, United States Courts of Appeals, and the United States Supreme Court.

2 Many cases are resolved before the court issues an opinion. Some taxpayers reach a settlement with the IRS before trial, while the courts dismiss other taxpayers’ cases for a variety of reasons, including lack of jurisdiction and lack of prosecution. Courts can issue less formal “bench opinions,” which are not published or precedential.

3 Internal Revenue Code (IRC) § 6662 also includes (b)(3), (b)(4), (5), (6), (7), and (8), but because those types of accuracy-related penalties were not heavily litigated, we have only analyzed (b)(1), and (2).

4 See National Taxpayer Advocate 2017 Annual Report to Congress 345.

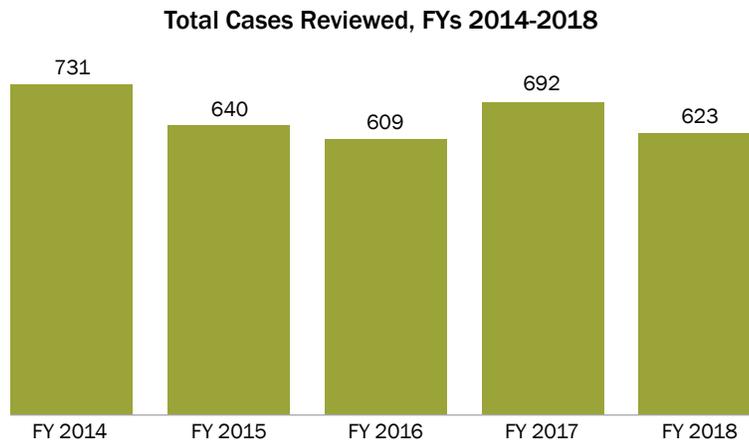
5 *Id.* at 410.

6 See National Taxpayer Advocate 2002 Annual Report to Congress 344-349. The Tax Cuts and Jobs Act (TCJA) suspended the overall limit on itemized deductions based on Adjusted Gross Income (AGI) for tax years 2018 through 2025. See Pub. L. No. 115-97, § 11046, 131 Stat. 2054, 2088 (2017). It remains to be seen how litigation in this area will change in the coming years due to the changes to itemized deductions under the TCJA.

(a 13 percent decrease).<sup>7</sup> Most case categories decreased in number of cases litigated this year except for trade or business expenses, which experienced an increase of seven percent.<sup>8</sup>

Overall, the total number of cases identified in the Most Litigated Issues section decreased from 692 in 2017 to 623 this year, a 10 percent decrease from last year.<sup>9</sup>

**FIGURE 3.0.1**



We also noticed a slight dip from last year in the percentage of cases involving *pro se* taxpayers who prevailed, as 13 percent of *pro se* taxpayers prevailed as compared to 15 percent in 2017.<sup>10</sup>

<sup>7</sup> See National Taxpayer Advocate 2017 Annual Report to Congress 348.

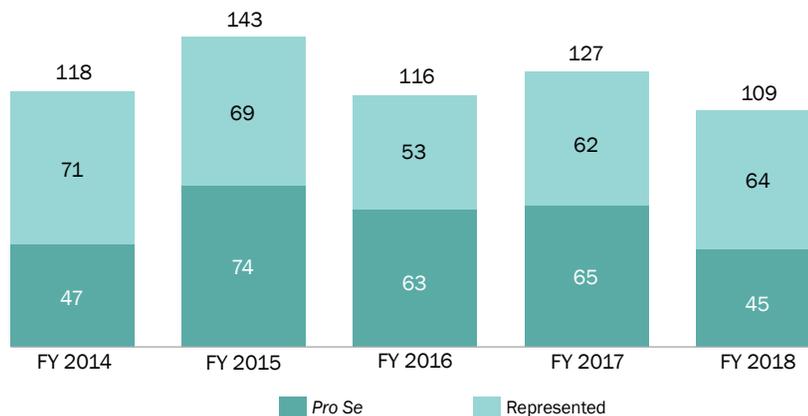
<sup>8</sup> *Id.*

<sup>9</sup> See National Taxpayer Advocate 2017 Annual Report to Congress 348. This decline may be attributed to the general decline in tax litigation in recent years. See, e.g., David McAfee, Tax Court: *Tax Court Caseload Drops as Enforcement Lags: Former Chief Judge 142 DTR 8* (Jul. 24, 2018) (former Chief Judge L. Paige Marvel noted that the Tax Court's inventory is dropping, due in part to lax enforcement).

<sup>10</sup> See National Taxpayer Advocate 2017 Annual Report to Congress 349.

FIGURE 3.0.2

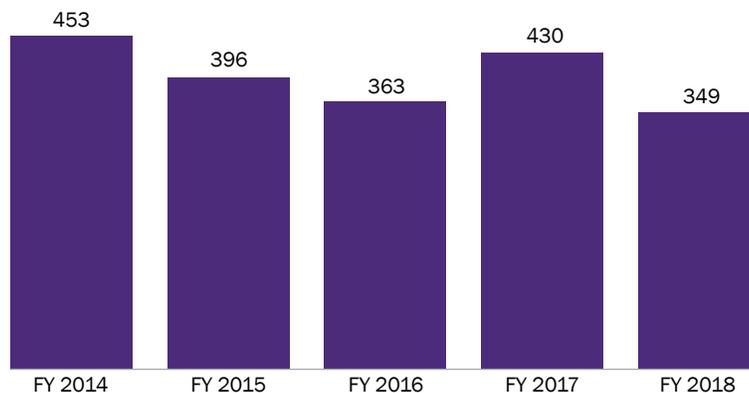
## Taxpayers Prevailing in Full or Part, FYs 2014-2018



Overall, the percentage of *pro se* litigation decreased from 62 percent of cases to 56 percent.

FIGURE 3.0.3

## Pro Se Litigants, FYs 2014-2018



Once TAS identified the Most Litigated Issues, we analyzed each one in five sections: summary of findings, taxpayer rights impacted, description of present law, analysis of the litigated cases, and conclusion.<sup>11</sup> Each case is listed in Appendix 3, which categorizes the cases by type of taxpayer (*i.e.*, individual or business).<sup>12</sup> Appendix 3 also provides the citation for each case, indicates whether the

11 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

12 Individuals filing Schedules C, E, or F are deemed business taxpayers for purposes of this discussion even if items reported on such schedules were not the subject of litigation.

taxpayer was represented at trial or argued the case *pro se* (*i.e.*, without representation), and lists the court's decision.<sup>13</sup>

We have also included a “Significant Cases” section summarizing decisions that are not among the top ten issues but are relevant to tax administration. In this section, we used the same reporting period, beginning on June 1, 2017, and ending on May 31, 2018, that we used for the ten Most Litigated Issues.

For the second year, we reviewed Tax Court summary judgments and bench orders, which are unpublished, which we discuss separately below, but did not include in the final counts for the Most Litigated Issues.<sup>14</sup> Unpublished litigation from the Tax Court has become available to the public in recent years through the court's website, but remains unavailable through electronic legal commercial databases.

## AN OVERVIEW OF HOW TAX ISSUES ARE LITIGATED

Taxpayers can generally litigate a tax matter in four different types of courts:

- The United States Tax Court;
- United States District Courts;
- The United States Court of Federal Claims; and
- United States Bankruptcy Courts.

With limited exceptions, taxpayers have an automatic right of appeal from the decisions of any of these courts.<sup>15</sup>

The Tax Court is a “prepayment” forum. In other words, taxpayers can access the Tax Court without having to pay the disputed tax in advance. The Tax Court has jurisdiction over a variety of issues, including deficiencies, certain declaratory judgment actions, appeals from CDP hearings, relief from joint and several liability, and determination of employment status.<sup>16</sup>

13 “*Pro se*” means “for oneself; on one’s own behalf; without a lawyer.” BLACK’S LAW DICTIONARY (10th ed. 2014). For purposes of this analysis, we considered the court’s decision with respect to the issue analyzed only. A “split” decision is defined as a partial allowance on the specific issue analyzed. The citations also indicate whether decisions were on appeal at the time this report went to print.

14 In prior years our review of litigation in federal courts was generally limited to discussing Tax Court opinions published in commercial databases. Each division or memorandum opinion goes through a legislatively mandated pre-issuance review by the Chief Judge. IRC §§ 7459(b); 7460(a). While division opinions are precedential, orders are not, being issued “in the exercise of discretion” by a single judge. See § 7463(b); Rule 50(f), Tax Court Rules of Practice and Procedure (denying precedential status to orders) and § 152(c) (denying precedential status to bench opinions).

15 See IRC § 7482, which provides that the United States Courts of Appeals (other than the United States Court of Appeals for the Federal Circuit) have jurisdiction to review the decisions of the Tax Court. There are exceptions to this general rule. For example, IRC § 7463 provides special procedures for small Tax Court cases (where the amount of deficiency or claimed overpayment totals \$50,000 or less) for which appellate review is not available. See also 28 U.S.C. § 1294 (appeals from a United States District Court are to the appropriate United States Court of Appeals); 28 U.S.C. § 1295 (appeals from the United States Court of Federal Claims are heard in the United States Court of Appeals for the Federal Circuit); 28 U.S.C. § 1254 (appeals from the United States Courts of Appeals may be reviewed by the United States Supreme Court).

16 IRC §§ 6214; 7476-7479; 6330(d); 6015(e); 7436.

The United States District Courts and the United States Court of Federal Claims have concurrent jurisdiction over tax matters in which (1) the tax has been assessed and paid in full<sup>17</sup> and (2) the taxpayer has filed an administrative claim for refund.<sup>18</sup> The United States District Courts, along with the bankruptcy courts in very limited circumstances, provide the only fora in which a taxpayer can receive a jury trial.<sup>19</sup> Bankruptcy courts can adjudicate tax matters that were not adjudicated prior to the initiation of a bankruptcy case.<sup>20</sup>

### ANALYSIS OF PRO SE LITIGATION

As in previous years, many taxpayers appeared before the courts *pro se*. Figure 3.0.4 lists the Most Litigated Issues for the review period June 1, 2017, through May 31, 2018, and identifies the number of cases, categorized by issue, in which taxpayers appeared without representation. As the figure illustrates, the issues with the highest rates of *pro se* appearance are frivolous issues and civil actions to enforce tax liens or subject property to tax.

**FIGURE 3.0.4, Pro Se Cases by Issue**

Most Litigated Issue	Litigated Cases Reviewed	Pro Se Litigation	Percentage of Pro Se Cases
Accuracy-Related Penalty	120	60	50%
Trade or Business Expenses	106	60	57%
Summons Enforcement	85	51	60%
Gross Income	79	42	53%
Collection Due Process	74	46	62%
Failure to File, Failure to Pay, and Estimated Tax Penalties	47	19	40%
Civil Actions to Enforce Federal Tax Liens or to Subject Property to Payment of Tax	39	26	67%
Charitable Deductions	29	10	34%
Schedule A Deductions	23	15	65%
Frivolous Issues	21	20	95%
<b>Total</b>	<b>623</b>	<b>349</b>	<b>56%</b>

Figure 3.0.5 affirms our contention that taxpayers are more likely to prevail if they are represented. *Pro se* taxpayers prevailed in 13 percent of cases this year as compared to 15 percent last year. Thus, for this year, the success rate for represented taxpayers was ten percentage points greater than that of *pro se* taxpayers.

17 28 U.S.C. § 1346(a)(1). See *Flora v. United States*, 362 U.S. 145 (1960), *reh'g denied*, 362 U.S. 972 (1960). For the National Taxpayer Advocate's Legislative Recommendation regarding the *Flora* rule, see Legislative Recommendation: *Fix the Flora Rule: Give Taxpayers Who Cannot Pay the Same Access to Judicial Review as Those Who Can*, *supra*.

18 IRC § 7422(a).

19 The bankruptcy court may only conduct a jury trial if the right to a trial by jury applies, all parties expressly consent, and the district court specifically designates the bankruptcy judge to exercise such jurisdiction. 28 U.S.C. § 157(e).

20 See 11 U.S.C. §§ 505(a)(1) and (a)(2)(A).

FIGURE 3.0.5, Outcomes for Pro Se and Represented Taxpayers

Most Litigated Issue	Pro Se Taxpayers			Represented Taxpayers		
	Total Cases	Taxpayer Prevailed In Whole or In Part	Percent	Total Cases	Taxpayer Prevailed In Whole or In Part	Percent
Accuracy-Related Penalty	60	13	22%	60	21	35%
Trade or Business Expenses	60	10	17%	46	15	33%
Summons Enforcement	51	0	0%	34	7	21%
Gross Income	42	7	17%	37	9	24%
Collection Due Process	46	4	9%	28	5	18%
Failure to File, Failure to Pay, and Estimated Tax Penalties	19	2	11%	28	4	14%
Civil Actions to Enforce Federal Tax Liens or to Subject Property to Payment of Tax	26	0	0%	13	2	15%
Charitable Deductions	10	0	0%	19	5	26%
Schedule A Deductions	15	6	40%	8	1	13%
Frivolous Issues	20	3	15%	1	0	0%
<b>Total</b>	<b>349</b>	<b>45</b>	<b>13%</b>	<b>274</b>	<b>69</b>	<b>25%</b>

## ANALYSIS OF UNPUBLISHED OPINIONS

We identified 107 bench orders and 203 summary judgments<sup>21</sup> by searching the Tax Court orders on its website.<sup>22</sup> We listed the selected cases in Appendix 3. We selected cases in which either a decision was entered on the merits of a substantive issue, or there was a substantive discussion of a distinct tax law matter.<sup>23</sup> The most prevalent issues discussed in the bench opinions reviewed (which also appear in this year's Most Litigated Issues) were accuracy-related penalty (43 cases or about 40 percent), trade or business expenses (39 cases or about 36 percent), and gross income (22 cases or 21 percent).<sup>24</sup>

Eighty-two percent of the 1,120 summary judgment orders we reviewed were procedural and did not discuss a substantive tax law issue, leaving 203 substantive decisions. In contrast to bench opinions, CDP matters dominated this category of unpublished litigation, with 81 percent (165 cases) of the

21 Unlike bench orders, summary judgments are decisions without trial. U.S. Tax Court Rules of Practice and Procedure, Title XII. Denying summary judgment in full or in part leaves issues in play for litigation and is not a final disposition on the merits of the litigated issue, which is a prerequisite for including a case in the counts for the Most Litigated Issues.

22 We utilized the orders search tab applying the reporting period date restriction and key search phrases: "summary judgment" and "7459(b)." We did not analyze summary judgments and bench orders in other federal courts. See Public Access to Court Electronic Records (PACER) User Manual for ECF Courts, Sept. 2014, <https://www.pacer.gov/documents/pacermanual.pdf> (explaining PACER search functions). We limited our search to the Tax Court as most tax litigation occurs in Tax Court.

23 Under Rule 121(d), if the adverse party does not respond to the motion for summary judgment, then the Tax Court may enter a decision against that party, when appropriate, and in light of the evidence contained within the administrative record. See Rule 121(d), Tax Court Rules of Practice and Procedure. We included summary judgments entered upon default in situations where the order discussed the merits.

24 Cases often discuss more than one substantive issue and as a result these reported percentages do not total 100. In 2017, the same issues were in the top three, with different frequency. Gross income was the most frequent, followed by trade and business expenses, then the accuracy related penalty. National Taxpayer Advocate 2017 Annual Report to Congress 349.

substantive, non-procedural summary judgments. The next largest category consisted of gross income issues which made up about six percent (13 cases).

Overall the IRS prevailed in 91 percent of motions for summary judgment in the substantive, non-procedural cases (184 cases) and in about 68 percent of bench opinions (73 cases). Split decisions resulted in four percent (nine of 203) of summary judgment orders and in 21 percent (22 of 107) of bench opinions. Overall, 85 percent (262 cases) of taxpayers appeared pro se in the unpublished opinions reviewed.<sup>25</sup>

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<sup>25</sup> See Appendix 3, *infra*.

## Significant Cases

This section describes cases that generally do not involve any of the ten most litigated issues, but nonetheless highlight important issues relevant to tax administration.<sup>1</sup> These decisions are summarized below.

**In *Larson v. United States*, the U.S. Court of Appeals for the Second Circuit held that it lacked jurisdiction to review assessable penalties under 28 U.S.C. § 1346(a) because the taxpayer had not fully paid them, as required under the *Flora* rule, and also lacked jurisdiction under the Administrative Procedure Act (APA).<sup>2</sup>**

Following Mr. Larson's conviction for promoting tax shelters, the IRS proposed over \$160 million in civil penalties under IRC § 6707 for failure to timely register the shelters. The IRS's Appeals function reduced the penalty by the amounts paid by alleged co-promoters who were jointly and severally liable, leaving an assessment of over \$65 million. Mr. Larson could not pay the full assessment, so he only paid about \$1.4 million. He then filed a refund claim, which the IRS rejected.

Mr. Larson petitioned the U.S. District Court for the Southern District of New York. The court granted the IRS's motion to dismiss because Mr. Larson had not fully paid the assessment, as required by the *Flora* rule (also called the "full payment" rule).<sup>3</sup> In 1960, the Supreme Court held in *Flora* that because the government had waived its sovereign immunity under 28 U.S.C. § 1346(a)(1) only with respect to refund claims that were fully paid, it lacked jurisdiction to review unpaid or partially paid claims.<sup>4</sup>

Mr. Larson appealed, arguing that: (1) the full payment rule only applies in deficiency cases, such as *Flora*, that could have been brought in the U.S. Tax Court before being paid; (2) the full payment rule violates his Fifth Amendment right to due process because he cannot fully pay and seek review; (3) the Administrative Procedure Act (APA) grants jurisdiction because there are no other avenues for judicial review; and (4) the penalty violates the excessive fines clause of the Eighth Amendment.

The U.S. Court of Appeals for the Second Circuit said that because 28 U.S.C. § 1346(a)(1) does not distinguish between deficiencies and assessable penalties, both are subject to the full payment rule. It observed that following the enactment of 28 U.S.C. § 1346(a), Congress provided limited exceptions to the rule for some penalties (*e.g.*, IRC §§ 6694(c) and 6703(c)), but not for the penalties at issue.

While acknowledging that the *Flora* decision had assumed the full payment rule would not result in hardship because taxpayers could "appeal the deficiency to the Tax Court without paying a cent,"<sup>5</sup> the Second Circuit said the availability of Tax Court review was not essential to the *Flora* court's

1 When identifying the ten most litigated issues, TAS analyzed federal decisions issued during the period beginning on June 1, 2017, and ending on May 31, 2018. For purposes of this section, we used the same period.

2 *Larson v. United States*, 888 F.3d 578 (2d Cir. 2018), *aff'g* 118 A.F.T.R.2d (RIA) 7004 (S.D.N.Y. 2016), *petition for rehearing and rehearing en banc filed*, Docket No. 16-CV-00245 (June 8, 2018).

3 *Flora v. United States (Flora)*, 362 U.S. 145 (1960), *reaff'g* *Flora v. United States*, 357 U.S. 63 (1958). Mr. Larson may have paid \$1.4 million because he thought he was fully paying a "divisible" portion of the penalty, which could trigger jurisdiction under *Flora*, 362 U.S. at 175, n. 37-38. A penalty is divisible if portions can be allocated to separate transactions or violations. After he filed suit, however, the Federal Circuit held in *Diversified Group Inc. v. United States*, 841 F.3d 975 (Fed. Cir. 2016), that the penalty under IRC § 6707 is not divisible.

4 28 U.S.C. § 1346(a)(1) grants jurisdiction "for the recovery of any internal-revenue tax alleged to have been erroneously or illegally assessed or collected, or any penalty claimed to have been collected without authority or any sum alleged to have been excessive or in any manner wrongfully collected under the internal-revenue laws."

5 *Flora*, 362 U.S. at 175.

conclusion.<sup>6</sup> Rather, *Flora* was based on Congress's understanding that full payment was required, as evidenced by the statutory scheme that Congress fashioned around 28 U.S.C. § 1346(a).<sup>7</sup> *Flora* did not rewrite the statute to engraft the requirement that an alternate forum be available, according to the court.<sup>8</sup>

Next, the Second Circuit evaluated Larson's due process claims. In evaluating such claims, courts consider three factors: (1) the private interest that will be affected by the official action; (2) the risk of an erroneous deprivation of such interest through the procedures used, and the probable value, if any, of additional or substitute procedural safeguards; and (3) the government's interest, including the function involved and the fiscal and administrative burdens that the additional or substitute procedural requirement would entail.<sup>9</sup> After weighing these factors, the court concluded that the full payment rule did not violate Mr. Larson's right to due process because of his opportunity to be heard by the IRS Office of Appeals, which had reduced the assessment, and the government's interest in protecting the public purse.<sup>10</sup>

Finally, the Second Circuit concluded it had no jurisdiction under the APA. By providing an exception to the full payment rule for some penalties but not others, Congress had implicitly precluded prepayment review. Even if it had not implicitly precluded prepayment review, it provided specific and adequate review procedures by providing for post-payment review, according to the court.<sup>11</sup> Although Mr. Larson cited cases in which other courts found post-payment review inadequate, the court distinguished them as involving challenges to regulations or claims of bad faith. Moreover, the court observed that Mr. Larson's case was reviewed by Appeals.<sup>12</sup>

6 *Larson*, 888 F.3d at 582. Supreme Court Justice Blackmun had interpreted *Flora* as indicating that “the full-payment rule applies only where... the taxpayer has access to the Tax Court for redetermination prior to payment,” but the Second Circuit explained that Justice Blackmun's view did not garner majority support. *Larson*, 888 F.3d at 582, n.8 (citing *Laing v. United States*, 423 U.S. 161, 208-209 (1976) (Blackmun, J., dissenting)). Critics have pointed out that the Second Circuit brushed off the fact that the majority did not disagree with J. Blackmun on this point and that the Solicitor General made the same argument. See, e.g., Andrew Velarde, *Taxpayer Asks Circuit for Do-Over on Full Payment Rule Holding*, 2018 TNT 113-5 (June 12, 2018) (quoting Carlton Smith).

7 *Larson*, 888 F.3d at 582.

8 *Id.* The Supreme Court had remarked in *Flora* that it was vexed by “statutory language [of § 1346(a)] which is inconclusive and legislative history which is irrelevant.” *Flora*, 362 U.S. at 152. This may suggest that the Supreme Court felt it was, in fact, rewriting an inconclusive statute.

9 *Mathews v. Eldridge*, 424 U.S. 319, 335 (1976).

10 The court mentioned the “public purse,” “efficient administration,” and the “government need ... [to promptly] secure its revenues” as justifications for the lack of a pre-payment forum for judicial review of an assessable tax penalty, quoting an old case that cited older decisions that expressed concerns, which carried more force before 1913. See *Larson*, 888 F.3d at 583-584 (quoting *Phillips v. Comm’r*, 283 U.S. 589, 595-96 (1931) (citing *Cheatham v. United States*, 92 U.S. 85, 89 (1876) (worrying the “very existence of the government might be placed in the power of a hostile judiciary” if taxpayers could dispute liabilities before paying))). Before 1913 when the 16th Amendment was ratified, there were legitimate concerns that a “hostile judiciary” would block the federal government from collecting various taxes, such as the income tax, which the Supreme Court had held was largely unconstitutional. See *Pollock v. Farmers' Loan & Trust Co.*, 157 U.S. 429 (1895). By 1924 such concerns must have subsided because Congress authorized pre-payment review of most tax deficiencies by a predecessor of the Tax Court. Revenue Act of 1924, 43 Stat. 253, 297-336 (1924). However, the court did not revisit the underlying analysis. For a discussion of how Congress has increasingly provided taxpayers with procedural protections, overriding the sovereign's ancient power to require immediate payment of taxes, see Nina E. Olson, 2010 Erwin N. Griswold Lecture Before the American College of Tax Counsel, *Taking the Bull by Its Horns: Some Thoughts on Constitutional Due Process in Tax Collection*, 63 TAX LAW. 227 (2010).

11 The court also noted that the Anti-Injunction Act (AIA) bars APA claims unless there is no alternative avenue for judicial review. *Larson*, 888 F.3d at 585, n.11.

12 Critics have argued that the opportunity to present a case to the IRS's Appeals function does not provide sufficient due process. See, e.g., Lawrence Hill & Richard Nessler, *IRS Penalty Assessments Without Due Process?*, 159 TAX NOTES 1763 (June 18, 2018).

Because the court had no jurisdiction, it did not evaluate whether the penalty violated the excessive fines clause of the Eighth Amendment. The court acknowledged that a \$61 million penalty assessment that is not subject to judicial review unless the taxpayer fully pays it “seems troubling,” particularly where the taxpayer cannot pay.<sup>13</sup> But, the court remarked that “it is Congress’ responsibility to amend the law.”<sup>14</sup>

This case is significant because it highlights that taxpayers do not have the unabridged right to judicial review, especially when the IRS’s penalty determination is so severe or the taxpayer is so poor that the assessment cannot be paid.<sup>15</sup> This report includes a specific legislative recommendation to address the problems highlighted by this case.<sup>16</sup>

**In *United States v. Stein*, the U.S. Court of Appeals for the Eleventh Circuit held a taxpayer’s affidavit may create an issue of material fact sufficient to preclude summary judgment in a collection case even if it is self-serving and uncorroborated, notwithstanding the presumption of correctness afforded to IRS assessments.<sup>17</sup>**

In 2015, the government sued Ms. Stein in district court to collect approximately \$220,000 in unpaid tax assessments, late penalties, and interest owed for tax years 1996, 1999, 2000, 2001, and 2002.<sup>18</sup> The government introduced her tax returns and account transcripts, but had not deposed Ms. Stein.

In response, Ms. Stein offered a sworn affidavit which listed the amounts she owed and paid for a number of years, including specific amounts the IRS acknowledged that it had misapplied, and declared “[I]t is my unwavering contention that I paid the taxes due, including late filing penalties, at such time as I filed the returns for each of the tax years in question.”<sup>19</sup> The district court granted the IRS’s motion for summary judgment because it said that self-serving assertions cannot rebut the presumption of correctness given to tax assessments under *Mays v. United States*.<sup>20</sup>

A panel of the U.S. Court of Appeals for the Eleventh Circuit affirmed,<sup>21</sup> but after reconsidering the case *en banc*, the court vacated the panel’s decision and overruled *Mays*. It reasoned that Federal Rule of Civil Procedure (FRCP) 56(a) authorizes summary judgment only when “there is no genuine dispute as to any material fact” and the moving party is “entitled to judgment as a matter of law,” rather than a trial by jury. Because the nonmoving party can dispute a material fact using an affidavit under FRCP 56(c), an affidavit can be enough to permit the case to survive summary judgment.

Although an affidavit cannot be conclusory, it can be self-serving and based solely on personal knowledge or observation. Such affidavits are routinely used to defeat summary judgment. The court reasoned there is no basis to treat affidavits in tax cases any differently under FRCP 56. Thus, it held

13 *Larson*, 888 F.3d at 587.

14 *Id.* (internal quotation omitted).

15 The court did not discuss the “right to appeal a decision of the Internal Revenue Service in an independent forum” under IRC § 7803(a)(3)(D).

16 See Legislative Recommendation: Fix the *Flora* Rule: Give Taxpayers Who Cannot Pay the Same Access to Judicial Review as Those Who Can, *supra*.

17 *United States v. Stein*, 881 F.3d 853 (11th Cir. 2018).

18 District courts have jurisdiction under IRC § 7402(a) to “render such judgments and decrees as may be necessary or appropriate for the enforcement of the internal revenue laws.”

19 *Stein*, 881 F.3d at 856.

20 763 F.2d 1295, 1297 (11th Cir. 1985).

21 *United States v. Stein*, 840 F.3d 1355 (11th Cir. 2016), *aff’g* 117 A.F.T.R.2d (RIA) 800 (S.D. Fla. 2016).

that a non-conclusory affidavit which complies with FRCP 56 can create a genuine dispute concerning an issue of material fact, even if it is self-serving and uncorroborated.<sup>22</sup>

The Eleventh Circuit cautioned, however, that a self-serving and uncorroborated affidavit would not always preclude summary judgment. Although *Mays* was a refund case, the court also cautioned that it was not expressing a view as to whether something other than uncorroborated oral testimony would be necessary to withstand summary judgment in a tax refund case.<sup>23</sup>

This case is significant because it may prompt the IRS to solicit and consider the taxpayer's position before filing a collection suit, even if the taxpayer's position includes statements that are self-serving and uncorroborated. Such an outcome would be consistent with several taxpayer rights, including the rights *to pay no more than the correct amount of tax* and *to challenge the IRS position and be heard*.<sup>24</sup> Indeed, this case has already prompted other courts to reject the IRS's motion for summary judgment where the IRS has declined to consider the taxpayer's position.<sup>25</sup>

**In *Chamber of Commerce v. IRS*, the U.S. District Court for the Western District of Texas held that the Anti-Injunction Act (AIA) did not bar a pre-enforcement challenge to a temporary regulation, and the temporary regulation was invalid because the IRS did not comply with the APA's notice and comment requirements.**<sup>26</sup>

In April 2016, the IRS issued both temporary and proposed regulations to inhibit inversions.<sup>27</sup> The plaintiffs argued the regulations exceeded the IRS's statutory authority, were arbitrary and capricious, and were issued without notice and opportunity for comment in violation of the APA.<sup>28</sup> The IRS argued the plaintiffs lacked standing and that the suit was barred by the AIA.<sup>29</sup>

First, the court held that the plaintiff associations had standing because Allergan, which was one of their members, had standing. Allergan had standing because it was injured by the regulations. Allergan had agreed to merge with Pfizer under the assumption that the combined company would not be subject to tax in the U.S. (*i.e.*, it was an inversion). The court found that the regulations were promulgated, in part, to prevent the Pfizer-Allergan inversion, which they did, and Allergan was facing continuing injury because it would have pursued other inversions but for the regulations. It did not need to engage in negotiations for deals that were economically impracticable just so that it could establish standing.

22 A thoughtful concurrence by Justice Pryor framed the historical context of the decision. See *Stein*, 881 F.3d at 859-860 (Pryor, J., concurring). He noted that after hearing that local juries in America were rendering biased decisions in customs litigation, the British Parliament shifted revenue litigation to courts sitting without juries. This led the colonists to adopt the Seventh Amendment right to a jury trial in civil cases. Therefore, he noted that *Mays* had "ousted the jury from its historical role in the exact context—the enforcement of tax laws—that prompted the founding generation to adopt the Seventh Amendment in the first place." *Id.* at 860.

23 *Stein*, 881 F.3d at 858, n.2.

24 See IRC § 7803(a)(3).

25 See, e.g., *McClendon v. United States*, No. 17-20174, 2018 U.S. App. LEXIS 16030 (5th Cir. June 14, 2018); *United States v. Wilkins*, No. 8:14-CV-993-EAK-JSS, 2018 WL 1988872 (M.D. Fla. Mar. 2, 2018).

26 *Chamber of Commerce v. IRS*, No. 1:16-cv-944-LY, 2017 WL 4682050 (W.D. Tex. Oct. 6, 2017).

27 Treas. Reg. § 1.7874-8T; Prop. Treas. Reg. § 1.7874-8; *Inversions and Related Transactions*, 81 Fed. Reg. 20,588-591 (Apr. 8, 2016).

28 See 5 U.S.C. § 706.

29 See IRC § 7421.

Next, the court held the AIA did not bar the suit. The AIA precludes taxpayers from filing “suit for the purpose of restraining the assessment or collection of any tax.”<sup>30</sup> The court concluded that the plaintiffs were challenging the validity of a temporary regulation governing who is subject to taxation under the IRC. It reasoned that the AIA does not insulate from challenge every rule that might eventually assist the government in assessing or collecting a tax. Enforcement of the regulation would precede any assessment or collection of tax.

The court quoted from the Supreme Court’s analysis in *Direct Marketing*, which held that the Tax Injunction Act (TIA), a state analogue to the AIA, did not bar a pre-enforcement challenge to a Colorado law, which required out-of-state retailers to report purchases by Colorado customers.<sup>31</sup> *Direct Marketing* analyzed whether enforcement of the reporting requirements was an act of assessment or collection as those terms are used in the IRC. Because it was not, the TIA did not apply. By analogy, because enforcement of the anti-inversion regulations was not an act of assessment or collection, the court concluded that the AIA did not bar a pre-assessment challenge to them.

In addition, the court held that the temporary regulations were invalid because the IRS failed to comply with the notice and comment requirements of the APA. The APA generally requires agencies to publish a notice of proposed rulemaking in the Federal Register and give interested persons an opportunity to comment at least 30 days before the effective date.<sup>32</sup> However, the temporary regulations were effective immediately.

First, the IRS argued that the temporary regulations were exempt from the notice and comment requirement under IRC § 7805(e) and its legislative history. According to the IRS, Congress’s intention was to codify the practice of allowing temporary regulations to be effective immediately (*i.e.*, before notice and comment). However, IRC § 7805(e) merely states that “[a]ny temporary regulation issued by the Secretary shall also be issued as a proposed regulation.” Further, the APA provides that a “[s]ubsequent statute may not be held to supersede or modify [the notice-and-comment procedure] ... except to the extent that it does so expressly.”<sup>33</sup>

The court reasoned that IRC § 7805(e) does not expressly provide an exception to the notice and comment procedure, and legislative history cannot override the explicit directives of the APA. Moreover, IRC § 7805(b) places limits on when tax regulations can be effective and does not carve out a special rule for temporary regulations.<sup>34</sup> Thus, the court concluded that IRC § 7805 did not authorize the IRS to modify the notice and comment procedure for temporary regulations.

The IRS also argued that the temporary regulations were exempt (under 5 U.S.C. § 553(b)(3)(A)) from the notice and comment requirement because they were merely “interpretive” and not “legislative,” but the court was not convinced. According to the court, legislative rules create law and affect individual rights and obligations, whereas interpretative rules are statements as to what the agency thinks the statute or regulation means. The statute authorized regulations to provide a computation that would trigger the anti-inversion rules, and the temporary regulations provided the substantive adjustments

30 IRC § 7421(a). As the Declaratory Judgment Act (28 U.S.C. § 2201) is generally interpreted as barring the same suits as the AIA (*i.e.*, the statutes are “coterminous”), it is common practice not to analyze them separately.

31 *Direct Mktg. Ass’n v. Brohl*, 135 S. Ct. 1124 (2015).

32 5 U.S.C. § 553.

33 5 U.S.C. § 559.

34 IRC § 7805(b) (“[N]o temporary, proposed, or final regulation relating to the internal revenue laws shall apply to any taxable period ending before the earliest of the following dates: ... In the case of any final regulation, the date on which any proposed or temporary regulation to which such final regulation relates was filed with the Federal Register....”).

needed to implement the statute.<sup>35</sup> Thus, the court determined they were legislative and not exempt from the notice and comment requirement.<sup>36</sup>

This case is significant because it suggests that rules that are effective immediately (before the agency has proposed the rule and considered public comments) are at greater risk of being challenged and held invalid on the basis that they did not comply with the APA.<sup>37</sup> It is also significant because it interprets the AIA more narrowly than the U.S. Court of Appeals for the District of Columbia Circuit, potentially making it easier to obtain pre-enforcement judicial review of regulations.<sup>38</sup>

**In *Facebook, Inc. v. IRS*, the U.S. District Court for the Northern District of California held that Facebook had no enforceable right to take its case to the IRS Office of Appeals and the court had no authority to review the IRS's unexplained decision.**<sup>39</sup>

The IRS audited Facebook over a five-year period, interviewing employees, issuing more than 200 requests for documents, and asking it to agree to five extensions of the statutory period of limitations. When Facebook declined to extend the period for a sixth time, the IRS issued a statutory notice of deficiency. Facebook petitioned the Tax Court and asked the IRS to transfer the case to the IRS's independent Appeals function. The IRS refused. It determined that doing so was “not in the interest of sound tax administration,” as it was permitted to do by Rev. Proc. 2016-22.<sup>40</sup> It did not explain why.

By way of background, since 1955, the IRS's statement of procedural rules have provided that a taxpayer has the right to an administrative appeal.<sup>41</sup> However, courts have held that the IRS is not bound by its statement of procedural rules.<sup>42</sup> In addition, Rev. Proc. 87-24 clarified that certain IRS officials could “determine that a case, or an issue or issues in a case, should not be considered by Appeals.”<sup>43</sup> Subsequently, the Internal Revenue Service Restructuring and Reform Act of 1998 granted taxpayers

35 Compare IRC § 7874(c)(6) (authorizing “regulations to treat stock as not stock.”) and IRC § 7874(a)(2)(B)(ii) (providing a computation) with Treas. Reg. § 1.7874-8T(b) (providing a somewhat different computation).

36 The court did not cite the Supreme Court's decision in *Mayo Foundation for Medical Education and Research v. United States*, 562 U.S. 44, 55 (2011), which implied that both interpretive and legislative regulations are entitled to so-called *Chevron* deference if (and maybe only if) they are issued after notice and comment. For a discussion of this issue, see, e.g., Elizabeth Chorvat, *Anti-Inversion Regulation Invalidated in Federal Court*, 157 TAX NOTES 401 (Oct. 16, 2017).

37 For helpful analysis, see Andrew Velarde, *Chamber of Commerce Throws Door Open for More Reg Challenges*, 2017 TNT 190-1 (Oct. 3, 2017). The IRS should have been on notice in 2010 that its arguments might not be accepted because a concurring opinion in the Tax Court would have come out the same way. See National Taxpayer Advocate 2010 Annual Report to Congress 418, 423 (discussing the concurring opinion in *Intermountain Ins. Serv. of Vail, LLC v. Comm'r*, 134 T.C. 211 (2010), *rev'd* by 2011-1 U.S.T.C. (CCH) ¶50,468 (D.C. Cir. 2011)). Moreover, the IRS could have avoided the effective date problem by merely expressing a “good cause” to make the regulations effective immediately, as permitted under the APA, particularly if the good cause is to “prevent abuse.” IRC § 7805(b)(3) expressly states that “[T]he Secretary may provide that any regulation may take effect or apply retroactively to prevent abuse.”

38 See *Florida Bankers Assoc. v. U.S. Dep't of Treasury*, 799 F.3d 1065 (D.C. Cir. 2015) (holding the AIA barred a challenge to information reporting regulations). For further discussion of this case, see National Taxpayer Advocate 2016 Annual Report to Congress 415, 418-20 (Most Litigated Issue: *Significant Cases*). For comprehensive analysis that lends support to a narrow interpretation of the AIA, see Kristin E. Hickman & Gerald Kerska, *Restoring the Lost Anti-Injunction Act*, 103 Va. L. Rev. 1683 (2017).

39 *Facebook, Inc. & Subsidiaries v. IRS*, 2018-1 U.S.T.C. (CCH) ¶50,248 (N.D. Cal. 2018).

40 Rev. Proc. 2016-22, 2016-15 I.R.B. 577, *superseding* Rev. Proc. 87-24, 1987-1 C.B. 720.

41 20 Fed. Reg. 4621, 4626 (June 30, 1955) (codified at 26 C.F.R. § 601.106(b), which provided that if the IRS “has issued a preliminary or ‘30-day letter’” and the taxpayer has filed a timely protest, “the taxpayer has the right (and will be so advised by the district director) of administrative appeal.”).

42 See *Ward v. Comm'r*, 784 F.2d 1424, 1431 (9th Cir. 1986); *Estate of Weiss v. Comm'r*, T.C. Memo. 2005-284 (2005). *But see, Richardson v. Joslin*, 501 F.3d 415, 418 (5th Cir. 2007) (“[A]n agency must abide by its own regulations.”) (citing *Accardi v. Shaughnessy*, 347 U.S. 260 (1954)); *United States v. Heffner*, 420 F.2d 809 (4th Cir. 1969) (IRS bound by instructions given to Special Agents); *Rauenhorst v. Comm'r*, 119 T.C. 157 (2002) (IRS bound by revenue rulings).

43 Rev. Proc. 87-24, 1987-1 C.B. 720, *superseded* by Rev. Proc. 2016-22, 2016-15 I.R.B. 577.

the statutory right to an administrative appeal in specific circumstances, but did not address whether taxpayers always have the right to an administrative appeal.<sup>44</sup>

In her 2007 Annual Report to Congress and in subsequent reports, the National Taxpayer Advocate recommended that the IRS adopt or that Congress codify a taxpayer bill of rights (TBOR) that included, among other things, the right to an appeal in an independent forum.<sup>45</sup> On June 10, 2014, the IRS adopted the TBOR and incorporated it into Publication 1.<sup>46</sup> On December 18, 2015, the Protecting Americans from Tax Hikes (PATH) Act codified the TBOR.<sup>47</sup> IRC § 7803(a)(3) now provides that the “Commissioner shall ensure that employees of the Internal Revenue Service are familiar with and act in accord with taxpayer rights as afforded by *other provisions* of this title, including—... the right to appeal a decision of the Internal Revenue Service in an independent forum.” (Emphasis added.)<sup>48</sup>

In late 2015, the IRS requested public comments on procedures that would deny taxpayers the right to go to Appeals if the “referral is not in the interest of sound tax administration,” even in cases not designated for litigation.<sup>49</sup> The American Bar Association Section of Taxation suggested the IRS “elaborate and clarify the limited circumstances in which docketed cases will be ineligible to be returned to Appeals due to ‘sound tax administration.’”<sup>50</sup> However, the IRS finalized these procedures as Rev. Proc. 2016-22 without addressing this comment. The IRS did not explain why it declined to elaborate on or clarify this standard.<sup>51</sup>

In this case, Facebook responded to the IRS’s refusal to refer its case to Appeals by filing suit in district court, alleging the IRS (1) violated its “right to appeal a decision of the Internal Revenue Service in an independent forum,” under IRC § 7803(a)(3)(E), and (2) violated the APA when it promulgated Rev. Proc. 2016-22, and when it denied Facebook access to Appeals. It requested *mandamus*-like relief.

44 Pub. L. No. 105-206, §§ 1001(a)(4), 3401, 112 Stat. 685, 689, 746 (1998) (establishing Appeals, and granting taxpayers a statutory right to a hearing before Appeals in connection with liens and levies, codified at IRC §§ 6320(b) (lien), 6330(b) (levy)). Section 3462 also directed the IRS to establish procedures for administrative appeals of IRS rejections of proposed installment agreements or offers-in-compromise under IRC §§ 6159 and 7122, respectively. In addition, other provisions assume that taxpayers have access to Appeals. See, e.g., IRC §§ 6015(c)(4), 7430(c)(2), 6621(c)(2)(A).

45 See, e.g., National Taxpayer Advocate 2007 Annual Report to Congress 478-489 (Legislative Recommendation: *Taxpayer Bill of Rights and De Minimis “Apology” Payments*) (recommending, in relevant part, that the right to appeal include the right “to be advised of and avail themselves of a prompt administrative appeal that provides an impartial review of *all* compliance actions (unless expressly barred by statute) and an explanation of the appeals decision”); National Taxpayer Advocate, *Toward a More Perfect Tax System: A Taxpayer Bill of Rights as a Framework for Effective Tax Administration* (2013); National Taxpayer Advocate 2013 Annual Report to Congress 5-19 (Most Serious Problem: *The IRS Should Adopt a Taxpayer Bill of Rights as a Framework for Effective Tax Administration*).

46 IRS News Release IR-2014-72 (June 10, 2014).

47 Pub. L. No. 114-113, 129 Stat. 2242 (2015). For a discussion of the effect of the TBOR, see, e.g., Alice Abreu & Richard Greenstein, *Embracing the TBOR*, 157 TAX NOTES 1281 (Nov. 27, 2017).

48 IRC § 7803(a)(3), (a)(3)(E).

49 Notice 2015-72, 2015-44 I.R.B. 613.

50 Letter from Am. Bar Ass’n Section of Taxation to Comm’r, IRS, *Comments on Notice 2015-72* (Nov. 16, 2015), [https://www.americanbar.org/groups/taxation/policy/policy\\_2015.html](https://www.americanbar.org/groups/taxation/policy/policy_2015.html).

51 The IRS’s request for comments may suggest it was seeking to increase the deference given to the final rule. However, the revenue procedure did not purport to establish “legislative” rules. If it had, the IRS would have been required to consider comments and provide a concise statement explaining the basis and purpose for a final rule under 5 U.S.C. § 553(c). The rule could have been challenged on the basis that the IRS did not address the comment and provide a reasoned explanation and that it was arbitrary and capricious under 5 U.S.C. § 706(2)(A). The Tax Court held in *Altera Corp. & Subs. v. Comm’r*, 145 T.C. 91 (2015) that a regulation was invalid because, in promulgating the regulation, the Treasury did not “adequately respond to commentators,” citing *Motor Vehicle Mfrs. Ass’n v. State Farm Mut. Auto. Ins. Co.*, 463 U.S. 29 (1983) (requiring rules to be the product of reasoned decision-making). The Tax Court’s decision was recently reversed, but the reversal was withdrawn. See *Altera Corp. & Subs. v. Comm’r*, No. 16-70496, 2018 WL 3542989 (9th Cir. July 24, 2018), *rev’g*, 145 T.C. 91 (2015), *withdrawn by*, 2018 WL 3734216 (9th Cir. Aug. 7, 2018).

The IRS moved to dismiss, countering that Facebook lacked standing and that its determination to deny Facebook access to Appeals was not reviewable under the APA because it was not a final agency action. The U.S. District Court for the Northern District of California granted the IRS's motion to dismiss. First, it reasoned that Facebook did not have an enforceable right to take its case to Appeals. The IRS's Statement of Procedural rules did not create enforceable rights and neither did the PATH Act. By its terms, the PATH Act required the Commissioner to train employees and ensure they act in accord with rights granted under "other provisions." Because of this training requirement, the TBOR was not a nullity. Even if the PATH Act had created enforceable rights, it was not clear that the "right to appeal in an independent forum" refers to a right to take a case to IRS Appeals, as opposed to the Tax Court.<sup>52</sup> Because deprivation of a nonexistent right does not constitute an injury, the court concluded that Facebook lacked standing.

The court also concluded that the IRS decision not to refer Facebook's case to Appeals was not reviewable under the APA. Unless another statute provides for review, only "final agency action for which there is no other adequate remedy in a court" is reviewable under the APA.<sup>53</sup> To be final, an action must (1) consummate the agency's decision-making process, and (2) establish rights and obligations or create binding legal consequences. The court concluded that neither the IRS's promulgation of Rev. Proc. 2016-22, nor its denial of Facebook's request to take its case to Appeals were final agency actions. The court reasoned that Rev. Proc. 2016-22 was not a final action because it did not create or determine any rights, obligations, or legal consequences.<sup>54</sup> Similarly, the IRS's decision not to refer the case to Appeals was not reviewable because Facebook's rights, obligations, and legal consequences will flow from judicial review, rather than from the IRS's decision not to refer its case to Appeals, according to the court.<sup>55</sup>

This case is significant because it suggests that the TBOR did not abrogate pre-existing limits on a taxpayer's right to an appeal. Perhaps more significantly, however, it suggests that when the IRS promulgates a revenue procedure that ignores stakeholder comments, ignores its own longstanding procedural rules, and then singles out one taxpayer for special treatment by withholding procedural protections afforded to other taxpayers without explanation, courts are helpless to review its actions.<sup>56</sup>

52 However, IRS Pub. 1, *Your Rights as a Taxpayer*, suggests the right encompasses both administrative and judicial appeal rights. It provides that "[T]axpayers are entitled to a fair and impartial administrative appeal of most IRS decisions... [and] Taxpayers generally have the right to take their cases to court." This language was heavily negotiated with the IRS by the National Taxpayer Advocate.

53 5 U.S.C. § 704. Facebook did not allege that the IRS's action was reviewable under another statute.

54 The court apparently did not consider the potential for the IRS to deny an administrative appeal to be a legal consequence. Nor did it discuss *Cohen v. United States*, 650 F.3d 717 (D.C. Cir. 2011), which held that a procedural notice that established excise tax refund procedures was reviewable under the APA as a final agency action.

55 A final decision by Appeals would seem to be a final agency action, but a decision to deny access to Appeals is not a final agency action, according to the court. As noted above, the IRS did not explain the basis for its decision to deny access to Appeals. However, the court did not discuss other cases where the IRS's determinations have been deemed arbitrary and capricious on the basis that they were inadequately explained. See, e.g., *Fisher v. Comm'r*, 45 F.3d 396, 397 (10th Cir. 1995), *non acq.* 1996-2 C.B. 2 (holding a supplemental notice of deficiency that did not provide reasons for declining to waive a penalty was invalid because "[i]t is an elementary principle of administrative law that an administrative agency must provide reasons for its decisions," quoting *Harberson v. NLRB*, 810 F.2d 977, 984 (10th Cir. 1987) and citing *SEC v. Chenery Corp.*, 318 U.S. 80, 94 (1943)).

56 This case illustrates how the IRS can issue and apply some procedural rules (*i.e.*, Rev. Proc. 2016-22, which provides a limited right to go to Appeals) in a way that burdens taxpayers and taxpayer rights, while at the same time ignoring other procedural rules (*e.g.*, 26 C.F.R. § 601.106(b)(3), which provides an unlimited right to go to Appeals) that would lessen this burden and be consistent with taxpayer rights.

**In *United States v. Colliot*, the U.S. District Court for the Western District of Texas held that the IRS could not impose the maximum penalty provided by law for a willful failure to file a Report of Foreign Bank and Financial Accounts (FBAR) because it had not updated regulations which provided a lower maximum penalty.<sup>57</sup>**

The IRS filed suit against Mr. Colliot to collect civil penalties assessed for the willful failure to report foreign accounts on a Report of Foreign Bank and Financial Accounts (FBAR) for years 2007-2010. The IRS's penalty assessments included \$548,773 for four FBAR violations in 2007, and another \$196,082 for four violations in 2008.

Mr. Colliot argued that the IRS's penalty assessments were arbitrary and capricious and an abuse of discretion because they exceeded the \$100,000 limit set forth in a regulation that was validly issued in 1987 after public notice and comment and that was still in force.<sup>58</sup> The IRS countered that the maximum penalty provided by the 1987 regulation was superseded by a change to 31 U.S.C. § 5321(a)(5) in the American Jobs Creation Act (AJCA) of 2004.<sup>59</sup> The ACJA increased the maximum FBAR penalty from \$100,000 to 50 percent of the amount in the unreported account (with no fixed cap).<sup>60</sup>

The court agreed with Mr. Colliot. When the statute sets a ceiling (but not a floor) for a penalty, it vests the Secretary with discretion to determine the penalty amount so long as it does not exceed the ceiling. By leaving the 1987 regulations in place, the Secretary used this discretion to limit the penalties the IRS would impose to amounts below the maximum provided by the statute (both before and after the AJCA). Thus, the 1987 regulation was consistent with the statute, as amended by the AJCA. Moreover, an agency can only repeal a regulation issued via notice-and-comment rulemaking by using the notice-and-comment rulemaking process.<sup>61</sup> Consequently, the IRS acted arbitrarily and capriciously when it failed to apply the regulation in assessing penalties against Mr. Colliot.<sup>62</sup>

This case is significant because it suggests that until the 1987 regulation is updated or repealed, it may limit the maximum penalty the IRS can impose for FBAR violations.<sup>63</sup> At the very least, this case

<sup>57</sup> *United States v. Colliot*, 2018-1 U.S.T.C. (CCH) ¶150,259 (W.D. Tex. May 16, 2018).

<sup>58</sup> *Amendments to Implementing Regulations Under the Bank Secrecy Act*, 52 Fed. Reg. 11436, 11445-46 (1987) (codified as 31 C.F.R. § 103.57(g)(2), and later re-codified as 31 C.F.R. § 1010.820(g)(2)) (authorizing Report of Foreign Bank and Financial Accounts (FBAR) penalties “not to exceed the greater of the amount (not to exceed \$100,000) equal to the balance in the account at the time of the violation, or \$25,000,” an upper limit that reiterated what was then provided by 31 U.S.C. § 5321(a)(5)(C)).

<sup>59</sup> American Jobs Creation Act of 2004 (AJCA), Pub. L. No. 108-357, § 821, 118 Stat. 1418, 1586 (2004) (codified at 31 U.S.C. § 5321(a)(5)(C)).

<sup>60</sup> Before the American Jobs Creation Act (ACJA) of 2004 the maximum FBAR penalty under was the greater of (1) \$25,000 or (2) 100 percent of the unreported account at the time of the violation, but not to exceed \$100,000. 31 U.S.C. § 5321(a)(5)(C) (2003). The ACJA increased the maximum penalty to the greater of (1) \$100,000, or (2) 50 percent of the amount in the account at the time of the violation (with no upper limit). 31 U.S.C. § 5321(a)(5)(C) (2018).

<sup>61</sup> See *Perez v. Mortgage Bankers Ass'n*, 135 S. Ct. 1199, 1206 (2015) (requiring agencies to “use the same procedures when they amend or repeal a rule as they used to issue the rule in the first instance”).

<sup>62</sup> See 5 U.S.C. § 706(2) (requiring agency action to be “in accordance with law”). See also *Richardson v. Joslin*, 501 F.3d 415, 418 (5th Cir. 2007) (“[A]n agency must abide by its own regulations.”) (citing *Accardi v. Shaughnessy*, 347 U.S. 260 (1954)). In lieu of dismissing the case with prejudice, on August 16, 2018 the court reformed (reduced) the amount of the FBAR penalty assessments to conform to the threshold set by 31 C.F.R. § 1010.820. *United States v. Colliot*, Order 1:16-cv-01281-SS (W.D. Tex. Aug. 16, 2018).

<sup>63</sup> Compare *United States v. Urayb Wadhan et al.*, No. 17-CV-1287-MSK, 2018 WL 3454973 (D. Colo. July 18, 2018) (citing *Colliot* and limiting the penalty to \$100,000), with *Norman v. United States*, No. 15-872T, 2018 U.S. Claims LEXIS 888 (Fed. Cl. July 31, 2018) (disagreeing with *Colliot* and allowing a penalty of more than \$100,000 on the basis that the statute said the maximum penalty “shall be increased”). For additional discussion, see, e.g., Robert Goulder, *Hurling F-Bombs at FBAR*, 91 TAX NOTES INT'L 1083 (Sept. 3, 2018).

suggests the IRS faces litigating hazards if it continues to ignore the limits provided by the regulation. The government may also expect to receive claims for refund from taxpayers who have paid FBAR penalties of more than the maximums set forth in the 1987 regulation.

**In *Estate of Stauffer v. IRS*, the United States District Court for the District of Massachusetts held that a taxpayer’s “financial disability” suspended the period for filing a claim for refund because the IRS’s refusal to consider a psychologist’s diagnosis was unreasonable.<sup>64</sup>**

Mr. Stauffer died at the age of 90. In 2013, his estate discovered that he had overpaid his taxes in 2006 when he was being treated by Dr. Schneider, Ed.D., a psychologist. The Estate sought a refund beyond the normal limitations period for filing refund claims under IRC § 6511(a).<sup>65</sup> It argued that the claim was timely because the period was suspended while Mr. Stauffer was “financially disabled.” The Estate submitted a statement by Mr. Schneider as proof of Mr. Stauffer’s disability.

With certain exceptions, IRC § 6511(h)(2) provides that a person is “financially disabled” when he or she “is unable to manage his [or her] financial affairs by reason of a medically determinable physical or mental impairment...” To establish a “financial disability,” IRC § 6511(h)(2) requires the claimant to provide proof “in such form and manner as the Secretary may require.” Pursuant to Rev. Proc. 99-21 the Secretary requires that the proof include a statement from a “physician,” which it defines by reference to section “1861(r)(1) of the Social Security Act, 42 U.S.C. § 1395x(r).”<sup>66</sup> This definition excludes psychologists. Thus, the IRS denied the claim without determining whether Mr. Stauffer was financially disabled during the relevant period.

The Estate argued that the IRS unreasonably limited the proof it would consider. The IRS filed a motion to dismiss for lack of jurisdiction because the Estate had not filed a timely administrative claim with the IRS.<sup>67</sup> According to the court, IRC § 6511(h) authorized the IRS to establish a procedural rule as to the “form and manner” of offering proof of financial disability. Although 5 U.S.C. § 553 generally requires agencies to adopt rules only after providing the public with an opportunity for notice and comment, this requirement does not apply to “procedural” rules. The Estate did not argue that the IRS had exceeded its authority by using Rev. Proc. 99-21 to adopt a substantive rule without notice and comment. Thus, the court reviewed the “reasonableness” of the rule established by Rev. Proc. 99-21 according to the deferential “arbitrary and capricious” standard provided by 5 U.S.C. § 706(2)(A).<sup>68</sup>

Even under this deferential standard, however, the agency must provide a “reasoned explanation” for rejecting the “reasonably obvious alternatives” available to it.<sup>69</sup> The court said that it was not obvious

64 *Estate of Stauffer v. IRS*, 285 F. Supp. 3d 474 (D. Mass. 2017). A subsequent decision found the taxpayer was not financially disabled because a power of attorney was in effect. See *Stauffer v. IRS*, 2018 U.S. Dist. LEXIS 180954 (D. Mass. 2018).

65 IRC § 6511(a) (explaining the limitations period generally expires “within 3 years from the time the return was filed or 2 years from the time the tax was paid, whichever of such periods expires the later.”).

66 Rev. Proc. 99-21, § 4, 1999-1 C.B. 960.

67 See IRC § 7422(a) (“no suit or proceeding shall be maintained in any court for the recovery of any internal revenue tax ... until a claim for refund or credit has been duly filed with the Secretary...”).

68 In other words, the court essentially gave *Chevron* deference to Rev. Proc. 99-21, even though the government had announced it would no longer take the position that its revenue procedures were entitled to such deference. See Marie Sapirie, *DOJ Won’t Argue for Chevron Deference for Revenue Rulings and Procedures*, Official Says, 131 TAX NOTES 674 (2011). By contrast, a Magistrate Judge who had reviewed the case recommended giving mere *Skidmore* deference to Rev. Proc. 99-21 (*i.e.*, upholding it only to the extent it has the power to persuade) and concluded it was an unpersuasive interpretation of the law.

69 *Estate of Stauffer*, 285 F. Supp. 3d at 484.

why the IRS would refuse to consider the statement of a psychologist who contemporaneously diagnosed and treated the individual. Even in Social Security cases (*i.e.*, cases governed by the statute from which Rev. Proc. 99-21 borrowed its definition) a psychologist's opinion is entitled to great weight. The government offered no evidence that the IRS had any reason that was not arbitrary for adopting a definition of "physician" that excluded psychologists from the category of professionals qualified to support a claimant's financial disability. Thus, the court denied the government's motion to dismiss.<sup>70</sup>

This case is significant because it suggests that, notwithstanding Rev. Proc. 99-21, some courts may require the IRS to consider statements by psychologists when determining a person's financial disability. Accordingly, it could lead the IRS to address longstanding concerns expressed by the National Taxpayer Advocate and others that IRC § 6511(h), as implemented by Rev. Proc. 99-21, is too narrow to protect many taxpayers who are unable to make timely claims because of a physical or mental impairment.<sup>71</sup>

**In *Borenstein v. Commissioner*, the Tax Court held it had no jurisdiction to review an overpayment claim by a non-filer who had obtained a filing extension because the IRS mailed the notice of deficiency at just the wrong time—after the second year following the original due date and before the third year following the extended due date.**<sup>72</sup>

By April 15, 2013, Ms. Borenstein had paid more tax than she owed for 2012, but timely requested a six-month extension to file. Her prepayments were deemed to have been made on the due date of the return (*i.e.*, April 15, 2013, in the case of her prepayments for 2012).<sup>73</sup> Ms. Borenstein did not file a return by the extended due date of October 15, 2013. On June 19, 2015, the IRS sent her a notice of deficiency. She filed her delinquent 2012 return claiming a refund on August 29, 2015, and timely petitioned the Tax Court a few weeks later. The IRS argued the Tax Court lacked jurisdiction with respect to the overpayment.

The Tax Court has jurisdiction to determine if the taxpayer has made an overpayment with respect to a disputed year,<sup>74</sup> but only with respect to amounts paid during the applicable lookback period.<sup>75</sup> The lookback period ends on the date a taxpayer files an administrative claim for refund, unless the taxpayer

<sup>70</sup> The court said that "a decision committed by statute to an agency's discretion may be subject to more limited review than the standard established in 5 U.S.C. § 706(2)(A)" and offered the IRS an opportunity to brief that issue. *Estate of Stauffer*, 285 F. Supp. 3d at 483, n. 2 (citations omitted). See 5 U.S.C. § 701(a)(2) ("This chapter applies, according to the provisions thereof, except to the extent that—... (2) "agency action" is committed to agency discretion by law."). The court also discounted the IRS's argument that the psychologist's statement was submitted with the appeal and not with the initial claim. It cited various authorities for the proposition that imperfect claims, including those that lack a doctor's note, can be perfected later.

<sup>71</sup> See National Taxpayer Advocate 2013 Annual Report to Congress 302-310 (Legislative Recommendation: *Broaden Relief from Timeframes for Filing a Claim for Refund for Taxpayers with Physical or Mental Impairments*). See also Bruce A. McGovern, *The New Provision for Tolling the Limitations Period for Seeking Tax Refund: Its History, Operation and Policy, and Suggestions for Reform*, 65 Mo. L. Rev. 797, 873 (2000); Keith Fogg & Rachel Zuraw, *Financial Disability for All*, 62 Cath. U. L. Rev. 965 (2013); American Bar Association, Section of Taxation, *Comments on Revenue Procedure 99-21* (Feb. 1, 2018), <https://www.americanbar.org/content/dam/aba/administrative/taxation/policy/020118comments.authcheckdam.pdf>. After this case was decided, the IRS requested comments on Rev. Proc. 99-21, but the request only concerned the burden associated with the paperwork requirements. See IRS, *Notice and request for Comments*, 82 Fed. Reg. 48,314 (Oct. 17, 2017).

<sup>72</sup> *Borenstein v. Comm'r*, 149 T.C. No. 10 (2017), *appeal docketed*, No. 17-3900 (2d Cir. Dec. 4, 2017).

<sup>73</sup> IRC § 6513(b).

<sup>74</sup> IRC § 6512(b)(1).

<sup>75</sup> IRC § 6512(b)(3).

did not file one, in which case, the period ends on the date the IRS mails the notice of deficiency.<sup>76</sup> The length of the lookback period also depends on when the taxpayer filed an administrative claim for refund.<sup>77</sup> For claims timely filed within the three-year period provided by IRC § 6511(a) (*i.e.*, within three years of filing the return), the lookback period is three years plus the period of any filing extension(s).<sup>78</sup> For other claims, the lookback period is two years.<sup>79</sup>

In *Lundy*, the Supreme Court held that the two-year lookback period applied to a non-filer because the taxpayer had not filed a return before the IRS mailed the notice of deficiency.<sup>80</sup> Like most non-filers, including the taxpayer in *Lundy*, Ms. Borenstein did not file a return before the IRS mailed the notice of deficiency (*i.e.*, June 19, 2015). Thus, the notice of deficiency would have been too late to trigger jurisdiction for amounts she was deemed to have paid on the due date (*i.e.*, April 15, 2013) under the two-year lookback period.

In response to *Lundy*, however, Congress added a final sentence to IRC § 6512(b)(3), which applies a three-year lookback period to certain non-filers.<sup>81</sup> The sentence states:

... where the date of the mailing of the notice of deficiency is during the third year after the **due date (with extensions)** for filing the return of tax and no return was filed before such date, the applicable [lookback] period under subsections (a) and (b)(2) of section 6511 shall be 3 years. [Emphasis added.]

The IRS argued that this sentence did not give the Tax Court jurisdiction with respect to Ms. Borenstein's claim because October 15, 2013, was Ms. Borenstein's "due date (with extensions)" and the IRS did not mail her a notice of deficiency during the third year thereafter (*i.e.*, on or after October 15, 2015). Thus, Ms. Borenstein's notice of deficiency was mailed during the second year after the "due date (with extensions)," not the third.

Ms. Borenstein and *amici curiae* observed that the IRS's interpretation created an anomalous result—a donut hole in the Tax Court's overpayment jurisdiction as applied to non-filers with valid filing extensions.<sup>82</sup> The Tax Court would have had jurisdiction if the IRS had mailed the notice of deficiency on or between October 15, 2015, and April 15, 2016, but had no jurisdiction in this case because it mailed the notice during the donut hole period (*i.e.*, between April 15, 2015, and October 15, 2015). They argued that this anomalous result could be avoided.

The Tax Court agreed with the IRS, however, rejecting Ms. Borenstein's arguments as inconsistent with the plain language of the statute. It also declined to invoke the "anti absurdity" doctrine. While acknowledging that a plain-language interpretation of the law produced an odd result in certain circumstances, the court concluded that it did not render the amendment "absurd" as a whole.

76 Specifically, IRC § 6512(b)(3)(B) authorizes refunds or credits of amounts paid "within the period which would be applicable under section 6511(b)(2)... if on the date of the mailing of the notice of deficiency a claim had been filed (whether or not filed)...."

77 To be timely, IRC § 6511(a) generally requires a taxpayer to make an administrative claim for refund within two years of paying the tax or within three years of filing the return, whichever is later.

78 See IRC § 6511(b)(2)(A).

79 See IRC § 6511(b)(2)(B).

80 *Comm'r v. Lundy*, 516 U.S. 235 (1996).

81 Taxpayer Relief Act of 1997, Pub. L. No. 105-34, § 1282(a) and (b), 111 Stat. 1037-38 (1997).

82 *Borenstein v. Comm'r*, 149 T.C. No. 10, at \*5 (2017).

This case is significant because it suggests that Congress did not fully address the problem highlighted by *Lundy* in the case of non-filers who obtain filing extensions. Depending upon when the IRS issues a notice of deficiency, the Tax Court may not have jurisdiction to grant them refunds to which they would otherwise be entitled.<sup>83</sup>

**In *Hulett v. Commissioner*, the Tax Court held that filing a return with the United States Virgin Islands (USVI) triggered the statute of limitations for U.S. Income Tax purposes, even if the taxpayers were not *bona fide* residents of the USVI, because the USVI forwarded parts of their return to the IRS.<sup>84</sup>**

Taxpayers claiming residency in the USVI are required to file returns with and pay tax to the USVI Bureau of Internal Revenue (BIR), but before 2007 it was unclear what, if anything, they had to file with the IRS.<sup>85</sup> Their tax liability, which is determined under a “mirror code” system, is usually the same as it would be if they were residents of the United States. However, those who receive approval from the USVI Economic Development Commission may claim the Economic Development Program (EDP) credit under IRC § 934, which reduces the effective tax rate on certain income.<sup>86</sup>

Ms. Coffey (aka Ms. Hulett) worked in the USVI during 2003 and 2004 and filed joint returns with the BIR, rather than the IRS, because she claimed to be a *bona fide* resident of the USVI. The BIR sent photocopies of the first two pages of the Forms 1040 for the years at issue, along with their W-2s (both U.S. W-2s and VI W-2s) to the IRS pursuant to the Tax Implementation Agreement (TIA). The IRS processed the forms and created a tax transcript for those years, which showed a U.S. tax liability of zero.

The IRS began to audit the 2003 and 2004 returns in August 2005 and in May 2006, respectively, but did not issue a notice of deficiency until 2009. It contended that Ms. Coffey was not a *bona fide* resident of the USVI and was not entitled to the EDP credit. The Coffeys petitioned the Tax Court, arguing the three-year statute of limitations (SOL) on assessment provided by IRC § 6501(a) had expired. The IRS countered that the SOL was open because, for the year in question, it would only begin to run when the Coffeys filed a return with the IRS, not when they filed a return with the BIR. The Coffeys argued that even if they were not *bona fide* USVI residents and were supposed to file with the IRS, the BIR had forwarded their return information to the IRS, thereby triggering the SOL upon receipt by the IRS.

83 For a recommendation to fix this glitch, see Legislative Recommendation: Tax Court Jurisdiction: *Fix the Donut Hole in the Tax Court's Jurisdiction to Determine Overpayments by Taxpayers with Filing Extensions*, *supra*.

84 *Hulett v. Comm'r*, 150 T.C. No. 4 (2018), *motion for reconsideration filed* (Feb. 28, 2018). By way of background, the National Taxpayer Advocate has recommended legislation to provide a fixed statute of limitations to those claiming United States Virgin Islands (USVI) residency and filing with the Bureau of Internal Revenue (BIR). See National Taxpayer Advocate 2009 Annual Report to Congress 391-399 (Legislative Recommendation: *Provide a Fixed Statute of Limitations for U.S. Virgin Islands Taxpayers*). According to the Eleventh Circuit Court of Appeals: “We agree with the assessment made by the National Taxpayer Advocate in a 2009 report to Congress: [The IRS's statute-of-limitations position] sends the message that the IRS might arbitrarily eliminate the benefit of any SOL by singling out those who take advantage of legitimate tax incentives. Perceptions of arbitrary and unfair tax administration not only undermine the purpose of tax incentives designed to attract business to the USVI, but may also increase controversy and diminish the public's willingness to comply with the law, potentially reducing federal tax receipts.” *Huff v. Comm'r*, 743 F.3d 790, 799 n.12 (11th Cir. 2014).

85 IRS Form 1040, *Instructions* (2004); IRS Pub. 570, *Tax Guide for Individuals with Income from U.S. Possessions* (2004). Although IRC § 7654(e) required the IRS to issue regulations under IRC § 932, the IRS did not provide specific guidance about the filing requirements until 2007. Notice 2007-19, 2007-1 C.B. 689 divided those claiming to be *bona fide* USVI residents into two categories: those who earned \$75,000 or more and those who did not. Those earning more than \$75,000 had to file with the BIR and send a zero return (*i.e.*, return reporting no gross income) to the IRS office in Pennsylvania, with a statement explaining the taxpayer's residency. Shortly thereafter, Notice 2007-31, 2007-1 C.B. 971, eliminated the income distinction and provided that all taxpayers claiming *bona fide* USVI residency should file just with the BIR, a position later adopted by regulation. Treas. Reg. § 1.932-1(c)(2)(ii). However, this was the IRS's position only for tax years ending on or after December 31, 2006.

86 See IRC § 934(b).

To qualify as a return under the *Beard* test, a submission must (1) contain sufficient data to calculate tax liability, (2) purport to be a return, (3) be an honest and reasonable attempt to satisfy the requirements of the tax law, and (4) be executed under penalties of perjury.<sup>87</sup> The IRS argued what it received from the BIR was not a return because it lacked an original signature and also because it did not contain sufficient data to allow the IRS to “verify” the liability, but the Tax Court was not convinced.<sup>88</sup>

The Tax Court observed that for purposes of getting interest on an overpayment, IRC § 6611(g) provides that “a return shall not be treated as filed until it is filed in processible form,” which requires enough information for the IRS to verify the taxpayer’s computations. Thus, IRC § 6611(g) implies that a filing that lacks sufficient information to be “processable” or verifiable can still be a return.<sup>89</sup> Moreover, returns need not be perfect.<sup>90</sup> Those that are fraudulent or missing schedules are still returns for purposes of the SOL.<sup>91</sup> The court explained that the IRS had received enough information to “compute” taxable income (*i.e.*, income, deductions, and credits) without creating special procedures, as evidenced by the tax transcripts it created, even if it had not received all of the information it needed to compute the correct taxable income or to verify it.

As to the other requirements, the Tax Court concluded that the Coffeys’ filing purported to be a return because it was on the Form 1040. The court rejected the IRS’s assertion that the Form 1040 was merely a territorial filing, as the failure to file it would have been prosecuted as a failure to file a Federal Income Tax Return. It also concluded that the filing was a reasonable attempt to satisfy the law, rejecting the IRS’s assertion that the “reasonable attempt” prong of the test was subjective and that a return that reflected all zeros would have been more reasonable than what the IRS received. Further, the subjective intent of the taxpayer is not important because it would be impractical for the IRS to contemplate the taxpayer’s state of mind when processing returns.<sup>92</sup>

Finally, the Tax Court found that the requirement to sign the returns under penalties of perjury was satisfied. Although the IRS objected that the signature was photocopied, the court reasoned that in certain circumstances the IRS accepts returns by fax.<sup>93</sup> Moreover, courts have concluded that even missing signatures can be overlooked in certain circumstances (*e.g.*, where one spouse neglects to sign

87 *Beard v. Comm’r*, 82 T.C. 766 (1984), *aff’d per curiam*, 793 F.2d 139 (6th Cir. 1986).

88 The IRS did not argue that the returns did not start the SOL because they were not “filed” with the IRS.

89 Similarly, the court observed according to the Internal Revenue Manual (IRM), “a return will be valid even though it is missing Form W-2 or Schedule D, but it will not be processable because the calculations are not verifiable.” IRM 25.6.1.6.16(2) (Oct. 1, 2010).

90 *Zellerbach Paper Co. v. Helvering*, 293 U.S. 172, 180 (1934).

91 See *Blount v. Comm’r*, 86 T.C. 383 (1986) (missing Form W-2); *McCaskill v. Comm’r*, 77 T.C. 689 (1981) (missing Schedule C); *Badaracco v. Comm’r*, 464 U.S. 386 (1984) (fraudulent returns).

92 Judge Marvel, writing for the dissent, argues that subjective intent of the taxpayer (or his or her representative) to file a return with the IRS is required to start the statute of limitations (SOL). Professor Camp observes that the majority of the Tax Court took a more functional approach that recognizes that the purpose of IRC § 6501(a) is to provide closure. See Bryan Camp, *Lesson From the Tax Court: Forms Follow Function in Return Filing*, TAXPROF BLOG (Feb. 5, 2018), [http://taxprof.typepad.com/taxprof\\_blog/2018/02/lesson-from-the-tax-court-when-filing-a-return-is-a-matter-of-principle.html](http://taxprof.typepad.com/taxprof_blog/2018/02/lesson-from-the-tax-court-when-filing-a-return-is-a-matter-of-principle.html). He argues that the court’s rationale in *Coffey* is inconsistent with *Allen v. Comm’r*, 128 T.C. 37 (2007) where the Tax Court held that the extended SOL applicable to fraudulent returns applied to a taxpayer’s return, even though a preparer, rather than the taxpayer, committed the fraud. For further discussion of *Allen*, see National Taxpayer Advocate 2007 Annual Report to Congress 562, 565 (*Significant Cases*).

93 See, *e.g.*, Rev. Rul. 68-500, 1968-2 C.B. 575 (fax signatures okay after authorization with original signature); Rev. Proc. 2005-39, 2005-2 C.B. 82 (permitting fax signatures on certain employment tax returns). See also CCA 200518079 (May 6, 2005) (concluding fax signatures are valid on a Form 872, *Consent to Extend the Time to Assess Tax*).

a joint return or where a subsidiary neglects to sign a consolidated return).<sup>94</sup> While the signature requirement helps to authenticate returns, in this case the BIR had already authenticated them.

This case is significant because it shows that the IRS continues to burden taxpayers and waste resources pursuing old cases without sufficient legal authority, even though it does not have clean hands and Congress has reiterated that taxpayers have the right to finality.<sup>95</sup> As the court explained:

[t]he IRS failed to promulgate mandatory regulations under section 932, failed to tell taxpayers that they should file protective zero returns, and failed to send the Coffeys a notice of deficiency within three years of receiving the cover-over documents. And, only a few short years later, the IRS finally did promulgate regulations that adopt precisely the position that the Coffeys took about how to start the statute of limitations. Despite all this, the Commissioner tells us that the Coffeys lose—though one is left to wonder how the current regulation is valid if the Commissioner is correct that filing anything other than a zero return with the IRS would be inadequate under the Code.

Over a decade ago, stakeholders, including stakeholders in Congress, complained to the National Taxpayer Advocate about the IRS's position.<sup>96</sup> TAS warned the IRS that it would end up wasting resources by pursuing old cases based on unconvincing legal theories, as it apparently continues to do.<sup>97</sup> This case highlights the need for Congress to require the IRS to place more emphasis on taxpayer rights.<sup>98</sup> The case also helps to clarify what constitutes a return and when the IRS has received enough information to start the SOL.<sup>99</sup>

94 See, e.g., *Estate of Campbell v. Comm'r*, 56 T.C. 1 (1971) (spouse); *Gen. Mfg. Corp. v. Comm'r*, 44 T.C. 513 (1965) (subsidiary).

95 IRC § 7803(a)(3)(F). See *Coffey v. Comm'r*, 150 T.C. No. 4, at \*58 (2018).

96 See, e.g., Letter from Ranking Member, House Ways and Means Committee, to National Taxpayer Advocate, *reprinted as, Rangel Requests Meeting With Olson on Tax Treatment of U.S.V.I. Residents*, 2007 TNT 64-15 (Sept. 19, 2006).

97 The IRS apparently prioritized revenue considerations. See Letter from IRS to Ranking Member, Senate Finance Committee, *reprinted as, USVI Proposal Would 'Significantly Affect Examinations,' IRS Says*, 2007 TNT 222-245 (Nov. 9, 2007).

98 See National Taxpayer Advocate Purple Book: *Compilation of Legislative Recommendations to Strengthen Taxpayer Rights and Improve Tax Administration 5-6 (Enact the Taxpayer Bill of Rights as a Freestanding Provision in the Internal Revenue Code)* (Dec. 2017). This case is one of many involving USVI SOL issues. See, e.g., *Appleton v. Comm'r*, 140 T.C. 273 (2013).

99 Under the Tax Court's reasoning the SOL began to run when the IRS received two pages of the return from the BIR, however, a taxpayer would not know when the IRS received such information from the BIR. By contrast, Judge Thornton's concurring opinion suggests that the SOL started when the BIR received the returns because the return was a reasonable attempt to satisfy the requirement. More Judges joined this concurring opinion than the opinion of the court.

MLI  
#1**Accuracy-Related Penalty Under IRC § 6662(b)(1) and (2)****SUMMARY**

Internal Revenue Code (IRC) § 6662(b)(1) and (2) authorizes the IRS to impose a penalty if a taxpayer's negligence or disregard of rules or regulations causes an underpayment of tax required to be shown on a return, or if an underpayment exceeds a computational threshold called a substantial understatement, respectively. IRC § 6662(b) also authorizes the IRS to impose the accuracy-related penalty on an underpayment of tax in six other circumstances.<sup>1</sup>

**TAXPAYER RIGHTS IMPACTED<sup>2</sup>**

- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to a Fair and Just Tax System*

**PRESENT LAW**

The amount of an accuracy-related penalty equals 20 percent of the portion of the underpayment attributable to the taxpayer's negligence or disregard of rules or regulations, or to a substantial understatement.<sup>3</sup> An underpayment is the amount by which any tax imposed by the IRC exceeds the excess of:

The sum of (A) the amount shown as the tax by the taxpayer on his return, plus (B) amounts not shown on the return but previously assessed (or collected without assessment), over the amount of rebates made.<sup>4</sup>

In computing the amount of underpayment for accuracy-related penalty purposes, Congress changed the law in 2015 to provide that the excess of refundable credits over the tax is taken into account as a negative amount.<sup>5</sup> Therefore, for returns filed after December 18, 2015, or for returns filed on or before

1 Internal Revenue Code (IRC) § 6662(b)(3) authorizes a penalty for any substantial valuation misstatement under chapter 1 (IRC §§ 1-1400U-3); IRC § 6662(b)(4) authorizes a penalty for any substantial overstatement of pension liabilities; IRC § 6662(b)(5) authorizes a penalty for any substantial estate or gift tax valuation understatement; IRC § 6662(b)(6) authorizes a penalty when the IRS disallows the tax benefits claimed by the taxpayer when the transaction lacks economic substance; IRC § 6662(b)(7) authorizes a penalty for any undisclosed foreign financial asset understatement; and IRC § 6662(b)(8) authorizes a penalty for any inconsistent estate basis. IRC § 6662(b)(8) was added by the Surface Transportation and Veterans Health Care Choice Improvement Act of 2015, Pub. L. No. 114-41, § 2004(c)(1), 129 Stat. 443, 456 (2015). We have chosen not to cover the IRC § 6662(b)(3) - (8) penalties in this report, as these penalties were not litigated nearly as often as IRC § 6662(b)(1) and 6662(b)(2) during the period we reviewed.

2 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the IRC. See IRC § 7803(a)(3).

3 IRC § 6662(b)(1) (negligence/disregard of rules or regulations); IRC § 6662(b)(2) (substantial understatement of income tax).

4 IRC § 6664(a).

5 *Id.* Prior to December 18, 2015, refundable credits could not reduce below zero the amount shown as tax by the taxpayer on a return. See *Rand v. Comm'r*, 141 T.C. 376 (2013). On December 18, 2015, Congress enacted a law that reversed the Tax Court's decision in *Rand* and amended IRC § 6664(a) to be consistent with the rule of IRC § 6211(b)(4). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title II, § 209, 129 Stat. 2242, 3084 (2015).

that date for which the period of limitations on assessment under IRC § 6501 has not expired, a taxpayer can be subject to an IRC § 6662 underpayment penalty based on a refundable credit that reduces tax below zero.

The IRS may assess penalties under IRC § 6662(b)(1) and (2), but the total penalty rate generally cannot exceed 20 percent (*i.e.*, the penalties are not “stackable”).<sup>6</sup> Generally, taxpayers are not subject to the accuracy-related penalty if they establish that they had reasonable cause for the underpayment and acted in good faith.<sup>7</sup>

### Negligence

The IRS may impose the IRC § 6662(b)(1) negligence penalty if it concludes that a taxpayer’s negligence or disregard of the rules or regulations caused the underpayment. A taxpayer will be subject to the negligence component of the penalty only on the portion of the underpayment attributable to negligence. If a taxpayer wrongly reports multiple sources of income, for example, some errors may be justifiable mistakes, while others might be the result of negligence; the penalty applies only to the latter.

Negligence is defined to include “any failure to make a reasonable attempt to comply with the provisions of this title, and the term ‘disregard’ includes any careless, reckless, or intentional disregard.”<sup>8</sup> Negligence includes a failure to keep adequate books and records or to substantiate items that give rise to the underpayment.<sup>9</sup> Strong indicators of negligence include instances where a taxpayer failed to report income on a tax return that a payor reported on an information return,<sup>10</sup> as defined in IRC § 6724(d)(1),<sup>11</sup> or failed to make a reasonable attempt to ascertain the correctness of a deduction, credit, or exclusion.<sup>12</sup> The IRS can also consider various other factors in determining whether the taxpayer’s actions were negligent.<sup>13</sup>

### Substantial Understatement

Generally, an “understatement” is the difference between (1) the correct amount of tax and (2) the tax reported on the return, reduced by any rebate.<sup>14</sup> Understatements are further reduced by the portion attributable to (1) an item for which the taxpayer had substantial authority or (2) any item for which the taxpayer, in the return or an attached statement, adequately disclosed the relevant facts affecting the

6 Treas. Reg. § 1.6662-2(c). The penalty rises to 40 percent if any portion of the underpayment is due to a gross valuation misstatement (IRC § 6662(h)(1)); Treas. Reg. § 1.6662-5(a), a nondisclosed noneconomic substance transaction (IRC § 6662(i)(1)), or an undisclosed foreign financial asset understatement (IRC § 6662(j)(3)).

7 IRC § 6664(c)(1).

8 IRC § 6662(c).

9 Treas. Reg. § 1.6662-3(b)(1).

10 Treas. Reg. § 1.6662-3(b)(1)(i).

11 IRC § 6724(d)(1) defines an information return by cross-referencing various other sections of the IRC that require information returns (e.g., IRC § 6724(d)(1)(A)(ii) cross-references IRC § 6042(a)(1) for reporting of dividend payments).

12 Treas. Reg. § 1.6662-3(b)(1)(ii).

13 These factors include the taxpayer’s history of noncompliance; the taxpayer’s failure to maintain adequate books and records; actions taken by the taxpayer to ensure the tax was correct; and whether the taxpayer had an adequate explanation for underreported income. Internal Revenue Manual (IRM 4.10.6.2.1, *Negligence* (May 14, 1999)). See also IRM 20.1.5.2.2, *Common Features of Accuracy-Related and Civil Fraud Penalties* (Dec. 13, 2016).

14 IRC § 6662(d)(2)(A)(i) - (ii).

item's tax treatment and the taxpayer had a reasonable basis for the tax treatment.<sup>15</sup> For individuals, the understatement of tax is substantial if it exceeds the greater of \$5,000 or ten percent of the tax that must be shown on the return for the taxable year.<sup>16</sup> For corporations (other than S corporations or personal holding companies), an understatement is substantial if it exceeds the lesser of ten percent of the tax required to be shown on the return for the taxable year (or, if greater, \$10,000), or \$10,000,000.<sup>17</sup>

For example, if the correct amount of tax is \$10,000 and an individual taxpayer reported \$6,000, the substantial underpayment penalty under IRC § 6662(b)(2) would not apply because although the \$4,000 shortfall is more than ten percent of the correct tax, it is less than the fixed \$5,000 threshold. Conversely, if the same individual reported a tax of \$4,000, the substantial understatement penalty would apply because the \$6,000 shortfall is more than \$5,000, which is the greater of the two thresholds.

### Reasonable Cause and Good Faith

The accuracy-related penalty does not apply to any portion of an underpayment where the taxpayer acted with reasonable cause and in good faith.<sup>18</sup> A reasonable cause determination considers all the pertinent facts and circumstances.<sup>19</sup> Generally, the most important factor is the extent to which the taxpayer made an effort to determine the proper tax liability.<sup>20</sup> Reliance on a return preparer may constitute reasonable cause and good faith if the reliance was reasonable and the taxpayer acted in good faith.<sup>21</sup> *Neonatology Associates v. Commissioner* establishes the three-part test for reasonable reliance on a tax professional in accuracy-related penalty cases:

- (1) The adviser was a competent professional who had sufficient expertise to justify reliance;
- (2) The taxpayer provided necessary and accurate information to the adviser; and
- (3) The taxpayer actually relied in good faith on the adviser's judgment.<sup>22</sup>

### Reasonable Basis

An understatement of tax may be reduced by any portion of the understatement attributable to an item for which the tax treatment is adequately disclosed and supported by a reasonable basis.<sup>23</sup> This standard is met if the taxpayer's position reasonably relies on one or more authorities listed in Treas. Reg. § 1.6662-4(d)(3)(iii).<sup>24</sup> Applicable authority could include information such as sections of the IRC; proposed, temporary, or final regulations; revenue rulings and revenue procedures; tax treaties

15 IRC § 6662(d)(2)(A)(i) - (ii). No reduction is permitted, however, for any item attributable to a tax shelter. See IRC § 6662(d)(2)(C)(i). If a return position is reasonably based on one or more of the authorities set forth in Treas. Reg. § 1.6662-4(d)(3)(iii), the return position will generally satisfy the reasonable basis standard. This may be true even if the return position does not satisfy the substantial authority standard found in Treas. Reg. § 1.6662-4(d)(2). See Treas. Reg. § 1.6662-3(b)(3).

16 IRC § 6662(d)(1)(A)(i) - (ii).

17 IRC § 6662(d)(1)(B)(i) - (ii). S corporations and personal holding companies are subject to the same thresholds as individuals and all other non-C corporation taxpayers, found in IRC § 6662(d)(1)(A)(i) - (ii).

18 IRC § 6664(c)(1).

19 Treas. Reg. § 1.6664-4(b)(1).

20 *Id.*

21 Treas. Reg. § 1.6664-4(b).

22 115 T.C. 43, 99 (2000) (citations omitted), *aff'd*, 299 F.3d 221 (3d Cir. 2002).

23 IRC § 6662(d)(2)(B)(ii)(I), (II).

24 Treas. Reg. § 1.6662-3(b)(3).

and regulations thereunder, and Treasury Department and other official explanations of such treaties; court cases; and congressional intent as reflected in committee reports.<sup>25</sup>

### Penalty Assessment and the Litigation Process

In general, the IRS proposes the accuracy-related penalty as part of its examination process<sup>26</sup> and through its Automated Underreporter (AUR) computer system.<sup>27</sup> Before a taxpayer receives a notice of deficiency, he or she generally has an opportunity to engage the IRS on the merits of the penalty.<sup>28</sup> Once the IRS concludes an accuracy-related penalty is warranted, it must follow deficiency procedures (*i.e.*, IRC §§ 6211-6213).<sup>29</sup> Thus, the IRS must send a notice of deficiency with the proposed adjustments and inform the taxpayer that he or she has 90 days to petition the United States Tax Court to challenge the assessment.<sup>30</sup> Alternatively, taxpayers may seek judicial review through refund litigation.<sup>31</sup> Under certain circumstances, a taxpayer can request an administrative review of IRS collection procedures (and the underlying liability) through a Collection Due Process hearing.<sup>32</sup>

IRC § 6751(b)(1) provides the general rule that no penalties may be assessed “unless the initial determination of such assessment is personally approved (in writing) by the immediate supervisor of the individual making such determination or such higher-level official as the Secretary may designate.” However, IRC § 6751(b)(2)(B) provides an exception for penalties calculated automatically “through electronic means.” The IRS interprets this exception as allowing it to use its AUR system to propose

25 Treas. Reg. § 1.6662-4(d)(3)(iii).

26 IRM 4.10.6.2(1), *Recognizing Noncompliance* (May 14, 1999) (“assessment of penalties should be considered throughout the audit”). See also IRM 20.1.5.3, *Examination Penalty Assertion* (Dec. 13, 2016).

27 The Automated Underreporter (AUR) is an automated program that identifies discrepancies between the amounts that taxpayers reported on their returns and what payors reported via Form W-2, Form 1099, and other information returns. IRM 4.19.3.2, *Overview of IMF Automated Underreporter* (Dec. 15, 2017); IRM 4.19.3.17.6, *Accuracy-Related Penalty Due to Negligence or Disregard of Rules or Regulations (Negligence Disregard Penalty)* (May 19, 2017).

28 For example, when the IRS proposes to adjust a taxpayer’s liability, including additions to tax such as the accuracy-related penalty, it typically sends a notice (“30-day letter”) of proposed adjustments to the taxpayer. A taxpayer has 30 days to contest the proposed adjustments to the IRS Office of Appeals, during which time he or she may raise issues related to the deficiency, including any reasonable cause defense to a proposed penalty. If the issue is not resolved after the 30-day letter, the IRS sends a statutory notice of deficiency (“90-day letter”) to the taxpayer. See IRS Pub. 5, *Your Appeal Rights and How to Prepare a Protest if You Don’t Agree* (Jan. 1999); IRS Pub. 3498, *The Examination Process* (Nov. 2004). However, for some taxpayers, the IRS sends a “combo” letter that combines the initial contact letter and the 30-day letter, which confuses taxpayers who do not know whether they should continue working with the examination function, file an appeal, or both. See National Taxpayer Advocate 2011 Annual Report to Congress, vol. 2, 85-86.

29 IRC § 6665(a)(1).

30 IRC § 6213(a). A taxpayer has 150 days instead of 90 to petition the Tax Court if the notice of deficiency is addressed to a taxpayer outside of the United States. See Most Serious Problem: *Statutory Notices of Deficiency: The IRS Fails to Clearly Convey Critical Information in Statutory Notices of Deficiency, Making it Difficult for Taxpayers to Understand and Exercise Their Rights, Thereby Diminishing Customer Service Quality, Eroding Voluntary Compliance, and Impeding Case Resolution*, *supra*.

31 Taxpayers may litigate an accuracy-related penalty by paying the tax liability (including the penalty) in full, filing a timely claim for refund, and then timely instituting a refund suit in the appropriate United States District Court or the Court of Federal Claims. 28 U.S.C. § 1346(a)(1); 28 U.S.C. § 1491; IRC §§ 7422(a); 6532(a)(1); *Flora v. United States*, 362 U.S. 145 (1960) (generally requiring full payment of tax liabilities as a prerequisite for jurisdiction over refund litigation). For exceptions to the *Flora* rule, see Legislative Recommendation: *Fix the Flora Rule: Give Taxpayers Who Cannot Pay the Same Access to Judicial Review as Those Who Can*, *supra*.

32 IRC §§ 6320 and 6330 provide for due process hearings in which a taxpayer may raise a variety of issues, including the underlying liability, provided the taxpayer did not actually receive a statutory notice of deficiency or did not otherwise have an opportunity to dispute such liability. IRC §§ 6320(c), 6330(c)(2)(B). See Most Serious Problem: *Collection Due Process Notices: Despite Recent Changes to Collection Due Process Notices, Taxpayers Are Still at Risk for Not Understanding Important Procedures and Deadlines, Thereby Missing Their Right to an Independent Hearing and Tax Court Review*, *supra*.

the substantial understatement and negligence components of the accuracy-related penalty without supervisor review.<sup>33</sup>

### Burden of Proof

In court proceedings involving individual taxpayers, the IRS bears the initial burden of production regarding the accuracy-related penalty.<sup>34</sup> The IRS must first present sufficient evidence to establish that the penalty was warranted.<sup>35</sup> The burden of proof then shifts to the taxpayer to establish any exception to the penalty, such as reasonable cause.<sup>36</sup> Because the reasonable basis standard is a higher standard to meet than reasonable cause, it is possible that a taxpayer may obtain relief from a penalty assessment by successfully arguing a reasonable cause defense, even if that defense does not satisfy the reasonable basis standard.<sup>37</sup>

## ANALYSIS OF LITIGATED CASES

We identified 120 opinions issued between June 1, 2017, and May 31, 2018, where taxpayers litigated the negligence or disregard of rules or regulations, or the substantial understatement components of the accuracy-related penalty. The IRS prevailed in full in 86 cases (72 percent), taxpayers prevailed in full in 29 cases (24 percent), and five cases (four percent) were split decisions. Table 1 in Appendix 3 provides a detailed list of these cases.

Taxpayers appeared *pro se* (without representation) in 60 of the 120 cases (50 percent). *Pro se* taxpayers convinced the court to dismiss or reduce the penalty in 22 percent of those 60 cases, which is slightly below the overall success rate for taxpayers challenging these penalties. In some cases, the court found taxpayers liable for the accuracy-related penalty but failed to clarify whether it was for negligence under IRC § 6662(b)(1) or a substantial understatement of tax under IRC § 6662(b)(2), or both. Regardless of the subsection at issue, the analysis of reasonable cause is generally the same. As such, we have combined our analyses of reasonable cause for the negligence and substantial understatement cases.

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- 33 If a taxpayer responds to an AUR-proposed assessment, the IRS first involves its employees at that point to determine whether the penalty is appropriate. If the taxpayer does not respond timely to the notice, the computers automatically convert the proposed penalty to an assessment without managerial review. See National Taxpayer Advocate 2014 Annual Report to Congress 404-410 (Legislative Recommendation: *Managerial Approval: Amend IRC § 6751(b) to Require IRS Employees to Seek Managerial Approval Before Assessing the Accuracy-Related Penalty Attributable to Negligence under IRC § 6662(b)(1)*); National Taxpayer Advocate 2007 Annual Report to Congress 259 (“Although automation has allowed the IRS to more efficiently identify and determine when such underreporting occurs, the IRS’s over-reliance on automated systems rather than personal contact has led to insufficient levels of customer service for taxpayers subject to AUR. It has also resulted in audit reconsideration and tax abatement rates that are significantly higher than those of all other IRS examination programs.”).
- 34 IRC § 7491(c) provides that “the Secretary shall have the burden of production in any court proceeding with respect to the liability of any individual for any penalty, addition to tax, or additional amount imposed by this title.”
- 35 *Higbee v. Comm’r*, 116 T.C. 438, 446 (2001); IRC § 7491(c). See *Portillo v. Comm’r*, 932 F.2d 1128 (5th Cir. 1991), *rev’g in part, aff’g in part, remanding* T.C. Memo. 1990-68, which involved an assessment based solely on an information return submitted by a third party and held that the presumption of correctness does not apply to the IRS’s deficiency assessment in a case involving unreported income if the IRS cannot present any evidence supporting the determination.
- 36 IRC § 7491(a). See also Tax Ct. R. 142(a).
- 37 Treas. Reg. § 1.6662-3(b)(3).

### Requirement for Managerial Approval Prior to Assessment of Penalties

In last year's Accuracy-Related Penalty Most Litigated Issue, we reported on two significant decisions regarding the IRC § 6751(b)(1) requirement to have a supervisor approve the penalties in writing prior to the initial determination of assessment. In *Chai v. Commissioner*, the Second Circuit held that the supervisory approval requirement is an element of a penalty claim for which the IRS bears the burden of production, and the court allowed the taxpayer to raise the lack of supervisory approval after trial.<sup>38</sup> Following *Chai*, the United States Tax Court vacated its 2016 decision in *Graev v. Commissioner*, where it had held that it was premature to conclude that the IRS had failed to comply with the supervisory approval requirement during trial because the penalty had not yet been assessed and written approval of the initial determination of the assessment could occur any time before the assessment.<sup>39</sup>

#### *Graev v. Commissioner (Graev III)*<sup>40</sup>

In late 2017, the Tax Court overruled in part its 2016 *Graev* decision and held that it was appropriate in the deficiency proceeding to consider the taxpayers' argument that the IRS failed to comply with the IRC § 6751(b)(1) supervisory approval requirement. The Graevs had claimed a charitable deduction for the donation of a facade easement. A revenue agent disallowed the deduction and proposed penalties. The agent's manager approved a 40 percent gross valuation misstatement penalty under IRC § 6662(h). IRS Counsel subsequently recommended the IRS assert, in the alternative, the 20 percent accuracy-related penalty under IRC § 6662(a). The revenue agent revised the notice of deficiency to include both penalties for the alternative noncash contributions, as recommended, but did not resubmit it for written supervisory approval. In litigation, the IRS conceded the 40 percent penalty, but continued to assert the 20 percent penalty. In the amendment to the answer, the IRS also asserted for the first time IRC § 6662(a) penalties at the 20 percent rate for the cash charitable contribution deduction and carryover deduction.

The Tax Court agreed with *Chai* that compliance with the supervisory approval requirement was part of the IRS's burden of production under IRC § 7491(c).<sup>41</sup> However, the court did not adopt *Chai*'s holding that the burden of proof with respect to the penalties also rests with the IRS.<sup>42</sup> The court found the IRS satisfied the IRC § 6751(b) requirement with respect to the alternative noncash contributions included in the notice of deficiency because the IRS Area Counsel docket attorney's memorandum, recommending the IRS assert the 20 percent penalty in the alternative, was approved in writing by his immediate supervisor, an Associate Area Counsel.<sup>43</sup> As to the cash charitable contribution deduction, which was not raised until the amendment to the answer, the court found the IRS had also met its burden because the amendment to the answer was approved in writing by the supervisor of the attorney who made and filed the amendment.<sup>44</sup>

38 *Chai v. Comm'r*, 851 F.3d 190 (2d Cir. 2017).

39 *Graev v. Comm'r*, 147 T.C. No. 16 (2016), vacated, Docket No. 30638-08 (T.C. Mar. 30, 2017).

40 149 T.C. No. 23 (2017) (hereinafter *Graev III*). This decision is the third in a series of Tax Court decisions related to the Graevs' liability for tax years 2004 and 2005.

41 149 T.C. No. 23.

42 149 T.C. No. 23, 2017 U.S. Tax Ct. LEXIS 58 at \*15 n.20 ("Once the Commissioner's burden of production is met, the taxpayer has the burden of proof with respect to defenses, *Higbee v. Commissioner*, 116 T.C. at 446, except that if the Commissioner pleads a new matter, an increase in deficiency, or an affirmative defense in the answer, the burden of proof is on the Commissioner.").

43 149 T.C. No. 23.

44 *Id.*

The taxpayers argued that, although Chief Counsel attorneys can sometimes make the initial determination of penalties, they never have the authority to make the initial penalty determination if the penalties are included in the notice of deficiency. The court rejected this argument and the argument that an initial determination cannot take the form of advice. The court found nothing in the legislative history that would suggest the person considered to make the initial determination is dependent on whether the penalty is included in the notice of deficiency.<sup>45</sup> Further, the court found that an initial determination under IRC § 6751(b), whether made by an examination employee or Chief Counsel attorney, is advice until it receives supervisory approval and is finalized by the Commissioner or one of his agents.<sup>46</sup>

### *Other Decisions Addressing IRC § 6751(b)*

Of the 120 cases we reviewed this year, there were eight decisions where the court found the taxpayers not liable for the accuracy-related penalty under IRC § 6662(b)(1) or (b)(2) because the IRS did not meet its burden of production with respect to the supervisory approval requirement.<sup>47</sup> In two of these eight cases, the court refused to reopen the record to allow additional evidence of compliance with IRC § 6751(b).<sup>48</sup> In addition to *Graev III*, in ten of the cases reviewed, the court specifically noted that the IRS met its burden of production with respect to the IRC § 6751(b) requirement, including two cases where it chose to reopen the record to allow evidence of compliance.<sup>49</sup> In *Dynamo Holdings Limited Partnership v. Commissioner*, an opinion not included in the 120 cases because it was not a final decision on the merits of IRC § 6662, the taxpayers' motion to dismiss the accuracy-related penalties based on lack of supervisory approval was denied.<sup>50</sup> The court concluded that under IRC § 7491(c), the IRS did not have the burden of production with respect to the penalties because it was a partnership-level proceeding, which is not a proceeding with respect to an individual and by its nature inconsistent with IRC § 7491(c), which relates to liability. However, the court noted that the IRS's not bearing the burden of production does not necessarily mean a motion by the IRS to reopen the record should be denied. A taxpayer may raise the lack of supervisory approval as a defense to the penalties. Then the IRS might want to reopen the record to demonstrate compliance if the issue was properly raised as a defense. However, in *Dynamo Holdings*, the partnership did not raise the lack of supervisory approval until after the record was closed and the case was fully submitted, and did not seek to reopen the record to argue there was no written approval.

*Dynamo Holdings* and the other cases where the court either did or did not allow for the record to be reopened demonstrate the confusion and variability following the aftermath of the *Chai* and *Graev* decisions. In June 2018, the IRS Office of Chief Counsel issued a Notice, explaining how to address IRC § 6751(b) issues in litigation.<sup>51</sup> The Notice advises that if an attorney raises the penalty in an answer or amended answer, the attorney's immediate supervisor must provide written approval. If an IRS employee receives a recommendation from a Chief Counsel attorney that a penalty should be asserted, the Notice states that the attorney should advise the IRS employee to document his or her acceptance of that recommendation and have his or her immediate supervisor approve the acceptance in

45 149 T.C. No. 23.

46 *Id.*

47 See, e.g., *Ford v. Comm'r*, T.C. Memo. 2018-8, *aff'd*, 2018 U.S. App. LEXIS 31221 (6th Cir., Nov. 5, 2018); *Azam v. Comm'r*, T.C. Memo. 2018-72.

48 *Rademacher v. Comm'r*, T.C. Memo. 2018-43; *Azam v. Comm'r*, T.C. Memo. 2018-72.

49 *Fiedziuszko v. Comm'r*, T.C. Memo. 2018-75; *Sarvak v. Comm'r*, T.C. Memo. 2018-68.

50 150 T.C. No. 10 (2018). The taxpayers in these consolidated cases were a corporation and the tax matters partner of a partnership. The IRS sought to impose the accuracy-related penalty only against the tax matters partner.

51 IRS Chief Counsel Notice Section 6751(b), Compliance Issues for Penalties in Litigation, CC-2018-006 (June 6, 2018).

writing. In cases where there is no sufficient evidence to meet the burden of production with respect to the supervisory approval requirement, the Notice advises Counsel attorneys to concede the case.

### Reasonable Cause

#### *Grecian Magnesite Mining, Industrial & Shipping Co., SA v. Commissioner*<sup>52</sup>

The taxpayer, a foreign corporation, bought an interest in a U.S. limited liability company that was a partnership for tax purposes. In 2008, the partnership redeemed the taxpayer's interest and made two liquidating payments to the taxpayer. The taxpayer did not report any gain from the redemption. Although the taxpayer conceded that the gain realized that was attributable to U.S. real property interests was taxable income, the taxpayer challenged the remainder of the gain that was not U.S.-source income and not effectively connected to a U.S. trade or business, and the accuracy-related penalty for the conceded liability.

The court found the taxpayer was not liable for the accuracy-related penalty because the taxpayer established reasonable cause and good faith. The court noted that the foreign corporation had no other involvement in U.S. business, outside the investment in the partnership. The taxpayer's central financial officer did not understand the concept of a partnership for tax purposes. The taxpayer relied on advice from a trusted advisor to hire a tax professional, which the court found was reasonable given what little the taxpayer knew of the U.S. tax system. Although the tax professional did not specialize in international tax or have an LL.M. degree, the court found that as a licensed attorney and certified public accountant, the tax professional met the *Neonatology* test requiring "a competent professional who had sufficient expertise to justify reliance."<sup>53</sup>

#### *Petersen v. Commissioner*<sup>54</sup>

The married taxpayers were shareholders of a closely held S corporation, which formed an employee stock ownership plan (ESOP) and transferred stock and cash to the related ESOP trust. As a matter of first impression, the court held that the entity holding the corporation's stock for the benefit of its ESOP participants was a "trust" under the Code. Also as a matter of first impression, the court held the S corporation and employees taking part in the ESOP were "related persons" under IRC § 267(a), which defers deductions for expenses paid by a taxpayer to a related person until those payments are includable in the person's gross income. In determining the taxpayers met the reasonable cause and good faith exception to the accuracy-related penalty, the court relied solely on the fact that the application of IRC § 267(a) to employers and ESOP participants was a question of first impression. The court noted that it had previously decided not to impose a penalty where it was an issue of first impression and the statutory language was not fully clear.<sup>55</sup> Because the taxpayers made a good-faith effort to assess their tax liabilities properly and acted reasonably and in good faith, the court refused to impose any accuracy-related penalty.

<sup>52</sup> 149 T.C. No. 3 (2017).

<sup>53</sup> 149 T.C. No. 3, 2017 U.S. Tax Ct. LEXIS 36 at \*51 (quoting *Neonatology Assocs., P.A. v. Comm'r*, 115 T.C. at 99).

<sup>54</sup> *Petersen v. Comm'r*, 2017 WL 2558852 (T.C. 2017), appeal docketed, No. 17-9003 (10th Cir., Aug. 8, 2017).

<sup>55</sup> *Id.* at \*26 (citing *Hitchens v. Comm'r*, 103 T.C. 711, 719-720 (1994)). See also *Avrahami v. Comm'r*, 2017 WL 3610601 (T.C. Aug. 21, 2017), another case we reviewed this year, in which the court found reasonable cause and good faith based partly on the fact that the issue involving a captive insurance company was one of first impression.

*McGuire v. Commissioner*<sup>56</sup>

The married taxpayers received the advanced premium tax credit (APTC) under the Affordable Care Act, which was paid directly to their health insurance provider to reduce their insurance premiums. During the tax year, Mrs. McGuire, who was not working at the start of the year, received a job that increased their household income above 400 percent of the federal poverty level, disqualifying them for the APTC. The taxpayers made repeated attempts to notify their health insurance provider of this change in income. However, their health insurance provider did not make any changes to account for this change in income, nor did it update the taxpayers' address after the taxpayers notified them of this change. Thus, the taxpayers did not receive correspondence from the provider or Form 1095-A, *Health Insurance Marketplace Statement*.

When the taxpayers filed their annual return, they did not report the APTC of \$7,092 that was paid to the healthcare provider. First, the court noted that in the notice of deficiency, the IRS made "a boilerplate determination of an accuracy-related penalty" by identifying "four possible causes for the underpayment: negligence, a substantial understatement of income tax, a substantial valuation misstatement, and a transaction lacking economic substance." The court immediately disregarded the latter two as having no relevance to the facts of this case. Likewise, the court disregarded the negligence penalty, noting that the IRS had the burden of production with respect to penalties but did not provide any evidence as to why the negligence penalty might apply.<sup>57</sup> Finally, the court determined that even though the amount of understatement met the threshold under IRC § 6662(d)(1)(A), the taxpayers were not liable for the accuracy-related penalty due to reasonable cause and good faith. The court stated that not receiving an information return generally is not enough in and of itself to constitute reasonable cause. However, the court noted that it had recently held in *Frias v. Commissioner* that nonreceipt of an information return could contribute to a reasonable cause finding if the taxpayer did not know or have reason to know about receiving the income.<sup>58</sup> The court noted that the taxpayers did not receive the Form 1095-A, and the APTC was paid directly to the health insurance provider. The taxpayers had relied on a third party (the healthcare provider) to properly determine and adjust their eligibility for the APTC. In addition, the taxpayers relied on a certified public accountant to prepare their return.

**Calculation of the Understatement***Galloway v. Commissioner*<sup>59</sup>

The married taxpayers filed a return claiming the American Opportunity Tax Credit (AOC), which was calculated on Form 8863 as \$7,500 (\$2,500 for each of their children). However, due to what appears to be a clerical error, the taxpayers only reported the refundable portion of the credit (\$3,000) on their Form 1040, and omitted the \$4,500 nonrefundable portion. The taxpayers claimed a refund of \$4,303 on their return, but during processing the IRS adjusted their return to account for the nonrefundable portion of the AOC and issued a refund of \$8,803. Subsequently during examination, the IRS disallowed the AOC in full.

56 *McGuire v. Comm'r*, 2017 WL 3730620 (T.C. Aug. 28, 2017).

57 The National Taxpayer Advocate has previously written about how the IRS's assessment of negligence penalties by automatic means without speaking to the taxpayer infringes on taxpayer rights. National Taxpayer Advocate 2014 Annual Report to Congress 404-410 (Legislative Recommendation: *Managerial Approval: Amend IRC § 6751(b) to Require IRS Employees to Seek Managerial Approval Before Assessing the Accuracy-Related Penalty Attributable to Negligence under IRC § 6662(b)(1)*).

58 In *Frias v. Commissioner*, the taxpayer was on maternity leave from her job and did not know or have reason to know that her loan from her retirement plan was treated as a deemed distribution because her employer did not deduct the loan repayment amounts from her paycheck. T.C. Memo. 2017-139.

59 149 T.C. No. 19 (2017).

Mr. Galloway conceded at trial that they were not entitled to any portion of the AOC, and the opinion suggests the AOC had already been claimed for the children in the prior four taxable years, making the children ineligible. However, the taxpayers argued that the IRS did not meet its burden of production with respect to the accuracy-related penalty under IRC § 6662(b)(2) because the understatement should be limited to \$3,000, which was the amount of the refund they sought on their return. The taxpayers posited that had the IRS not issued them the refund, the amount of the deficiency would be under the statutory \$5,000 threshold. The court disagreed, citing the definition of an understatement in IRC § 6662(d)(2)(A), which states that the amount of tax shown on a taxpayer's return is "reduced by any rebate."<sup>60</sup> The court rejected the argument that the taxpayers were being penalized by the IRS's action and noted that for a refund to meet the definition of "rebate," it must be based on a determination that the tax imposed is less than the tax shown on the taxpayer's return. The court considered the tax shown on the return to include the nonrefundable AOC shown on the Form 8863 and considered its omission on the Form 1040, *U.S. Individual Income Tax Return*, to be a clerical error.

The taxpayers argued that the amount of the understatement should nonetheless be reduced to \$3,000 because there was substantial authority for the taxpayers to not claim the nonrefundable portion of the credit. In the alternative, they argued the form used to calculate the credits served as a disclosure, and there was a reasonable basis for the taxpayers not to claim the \$4,500 on the return. The court dismissed these arguments because:

We do not view petitioners as having claimed only a \$3,000 refundable AOC: Their Form 8863 reported a total AOC of \$7,500. Petitioners are not subject to the accuracy-related penalty for their failure to claim a \$4,500 nonrefundable AOC on their Form 1040 but instead for their claim of such a credit on their Form 8863. Because the refundable portion of the AOC is, by definition, 40% of the total AOC to which a taxpayer is entitled, sec. 25A(i)(6), claiming a \$3,000 refundable AOC and no nonrefundable AOC cannot be supported by substantial authority.<sup>61</sup>

Finally, the taxpayers argued reasonable cause and good faith, stating they attempted to follow the instructions of a return preparation program and the error was due to confusion. The court relied heavily on the unambiguous statutory language that states the credit is only available for the first four years of post-secondary education and the clear instructions on Form 8863 to conclude that the taxpayers' confusion was not reasonable based on the circumstances.

This case demonstrates that an understatement can give rise to an accuracy-related penalty where the taxpayer actually entered a larger refund on part of his or her return, but did not claim it, and the IRS adjusted the return. In a footnote, the court notes that in theory, an understatement could arise from a refund that is based on an erroneous third-party information return, but presumably a taxpayer would be able to show reasonable cause and good faith if he or she did nothing to initiate the refund and bore no responsibility for the erroneous third-party reporting.<sup>62</sup>

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60 *Galloway*, 149 T.C. No. 19.

61 *Galloway*, 149 T.C. No. 19, 2017 U.S. Tax Ct. LEXIS 53 at \*20.

62 *Galloway*, 149 T.C. No. 19, 2017 U.S. Tax Ct. LEXIS 53 at \*19 n.4.

## CONCLUSION

The accuracy-related penalty under IRC § 6662(b)(1) and (2) remains the number one most litigated tax issue, continuing a trend from the last five years. The *Graev III* decision should bring more clarity for future cases by establishing that the Tax Court will follow the *Chai* decision with respect to the requirement for the IRS to show compliance with IRC § 6751(b) as part of its burden of production. However, because of the multiple cases that were initiated before *Graev III* and some even before *Chai*, the Tax Court is likely to continue to grapple with under what circumstances it is appropriate to reopen the record to allow the IRS to demonstrate compliance. This year, we saw courts allow it in some circumstances, but not in others. In addition, because the Tax Court declined to adopt *Chai*'s holding that compliance with IRC § 6751(b) is part of the burden of proof, there may be some uncertainty for taxpayers depending on where their cases may be appealed.

The cases of *Petersen v. Commissioner* and *McGuire v. Commissioner* were positive for taxpayers. In *Petersen*, the court suggested that issues of first impression should generally give rise to a reasonable cause finding. Conversely, in *McGuire*, the court held that nonreceipt of an information return does not generally constitute reasonable cause by itself, but that such nonreceipt could contribute to a reasonable cause finding.

The *Galloway* decision shows that the IRS can find an accuracy-related penalty as a result of an adjustment it makes to a return, based on an attached form. The court mentioned in a footnote the possibility of finding an understatement based on a third-party's information return but noted that such a taxpayer could qualify for the reasonable cause exception. Future cases may show how far the IRS can go in terms of basing an accuracy-related penalty on an adjustment it makes to a return.

## MLI #2 Trade or Business Expenses Under IRC § 162 and Related Sections

### SUMMARY

The deductibility of trade or business expenses has long been among the ten Most Litigated Issues (MLIs) since the first edition of the National Taxpayer Advocate's Annual Report to Congress in 1998.<sup>1</sup> We identified 106 cases involving a trade or business expense issue that were litigated in federal courts between June 1, 2017, and May 31, 2018. The courts affirmed the IRS position in 81 of these cases, or about 76 percent, while taxpayers fully prevailed in only six cases, or about six percent of the cases. The remaining 19 cases, or about 18 percent, resulted in split decisions.

### TAXPAYER RIGHTS IMPACTED<sup>2</sup>

- *The Right to Be Informed*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to a Fair and Just Tax System*

### PRESENT LAW

Internal Revenue Code (IRC) § 162(a) permits a taxpayer to deduct ordinary and necessary trade or business expenses paid or incurred during the taxable year.<sup>3</sup> These expenses include:

- A reasonable allowance for salaries or other compensation for personal services actually rendered;
- Travel expenses while away from home in the pursuit of a trade or business; and
- Rentals or other payments for use of property in a trade or business.<sup>4</sup>

In addition to the general allowable expenses described above, IRC § 162 addresses deductible and nondeductible expenses incurred in carrying on a trade or business, and provides special rules for health insurance costs of self-employed individuals.<sup>5</sup>

The interaction of IRC § 162 with other Code sections that explicitly limit or disallow deductions can be very complex. For example, the year in which the deduction for trade or business expenses can be

1 See National Taxpayer Advocate 1998-2016 Annual Reports to Congress.

2 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

3 The taxable year in which a business expense may be deducted depends on whether the taxpayer uses the cash or accrual method of accounting. IRC § 446.

4 IRC § 162(a)(1), (2), and (3).

5 See, e.g., IRC § 162(c), (f), and (l). For example, nondeductible trade or business expenses include illegal bribes, kickbacks, fines, and penalties.

taken and its amount depend on when the cost was paid or incurred, the useful life of an asset on the date of acquisition, and when it was sold or when the business operation is terminated.<sup>6</sup>

Rules regarding the practical application of IRC § 162 have evolved largely from case law and administrative guidance over the years. The IRS, the Department of Treasury, Congress, and the courts continue to pose questions and provide legal guidance about whether a taxpayer is entitled to certain trade or business deductions. The litigated cases analyzed for this report illustrate both the ongoing nature of this process and the necessary analysis of facts and circumstances unique to each case. When a taxpayer seeks judicial review of the IRS's determination of a tax liability relating to the deductibility of a particular expense, the courts must often address a series of questions, including, but not limited to, the ones discussed below.

### What Is a Trade or Business Expense Under IRC § 162?

Although “trade or business” is a widely used term in the IRC, neither the Code nor the Treasury Regulations provide a definition.<sup>7</sup> The definition of a “trade or business” comes from common law, where the concepts have been developed and refined by the courts.<sup>8</sup> The Supreme Court has interpreted “trade or business” for purposes of IRC § 162 to mean an activity conducted with “continuity and regularity” and with the primary purpose of earning income or making a profit.<sup>9</sup>

### What Is an Ordinary and Necessary Expense?

IRC § 162(a) requires a trade or business expense to be both “ordinary” and “necessary” in relation to the taxpayer's trade or business to be deductible. In *Welch v. Helvering*, the Supreme Court stated that the words “ordinary” and “necessary” have different meanings, both of which must be satisfied for the taxpayer to benefit from the deduction.<sup>10</sup> The Supreme Court describes an “ordinary” expense as customary or usual and of common or frequent occurrence in the taxpayer's trade or business.<sup>11</sup> The Court describes a “necessary” expense as one that is appropriate and helpful for the development of the business.<sup>12</sup>

Common law also requires that in addition to being ordinary and necessary, the amount of the expense must be reasonable for the expense to be deductible. In *Commissioner v. Lincoln Electric Co.*, the Court of Appeals for the Sixth Circuit held “the element of reasonableness is inherent in the phrase ‘ordinary

6 See, e.g., IRC § 165 (deductibility of losses), IRC § 167 (deductibility of depreciation), IRC § 183 (activities not engaged in for profit), and IRC § 1060 (special allocation rules for certain asset acquisitions, including the reporting of business asset sales when closing a business).

7 *Comm'r v. Groetzinger*, 480 U.S. 23, 35 (1987). “The phrase ‘trade or business’ has been in section 162(a) and that section's predecessors for many years. Indeed, the phrase is common in the Code, for it appears in over 50 sections and 800 subsections and in hundreds of places in proposed and final income tax regulations... The concept thus has a well-known and almost constant presence on our tax-law terrain. Despite this, the Code has never contained a definition of the words “trade or business” for general application, and no regulation has been issued expounding its meaning for all purposes. Neither has a broadly applicable authoritative judicial definition emerged.”

8 Carol Duane Olson, *Toward a Neutral Definition of “Trade or Business” in the Internal Revenue Code*, 54 U. CIN. L. REV. 1199 (1986).

9 *Groetzinger*, 480 U.S. at 35.

10 290 U.S. 111, 115 (1933) (suggesting an examination of “life in all its fullness” will provide an answer to the issue of whether an expense is ordinary and necessary).

11 *Deputy v. du Pont*, 308 U.S. 488, 495 (1940) (internal citations omitted).

12 See *Comm'r v. Heining*, 320 U.S. 467, 471 (1943).

and necessary.’ Clearly it was not the intention of Congress to automatically allow as deductions operating expenses incurred or paid by the taxpayer in an unlimited amount.<sup>13</sup>

Further, an employee business expense is not ordinary and necessary if the employee is entitled to reimbursement from the employer.<sup>14</sup> The employee has the burden of establishing the amount of the expense and that the expense is not eligible for reimbursement.

### Is the Expense a Currently Deductible Expense or a Capital Expenditure?

A currently deductible expense is an ordinary and necessary expense paid or incurred during the taxable year in the course of carrying on a trade or business.<sup>15</sup> No current deductions are allowed for the cost of acquisition, construction, improvement, or restoration of an asset expected to last more than one year.<sup>16</sup> Instead, those types of expenses are generally considered capital expenditures, which may be subject to depreciation, amortization, or depletion over the useful life of the property.<sup>17</sup>

Whether an expenditure is deductible under IRC § 162(a) or is a capital expenditure under IRC § 263 is a question of fact. Courts have adopted a case-by-case approach to applying principles of capitalization and deductibility.<sup>18</sup>

### When Is an Expense Paid or Incurred During the Taxable Year, and What Proof Is There That the Expense Was Paid?

IRC § 162(a) requires an expense to be “paid or incurred during the taxable year” to be deductible. The IRC also requires taxpayers to maintain books and records that substantiate income, deductions, and credits, including adequate records to substantiate deductions claimed as trade or business expenses.<sup>19</sup> If a taxpayer cannot substantiate the exact amounts of deductions by documentary evidence (*e.g.*, invoice paid, paid bill, or canceled check) but can establish that he or she had some business expenditures, the courts may employ the *Cohan* rule to grant the taxpayer a reasonable amount of deductions.<sup>20</sup>

#### The Cohan Rule

The *Cohan* rule is one of “indulgence” established in 1930 by the Court of Appeals for the Second Circuit in *Cohan v. Commissioner*.<sup>21</sup> The court held that the taxpayer’s business expense deductions were not adequately substantiated, but stated that “the [Tax Court] should make as close an approximation as it can, bearing heavily if it chooses upon the taxpayer whose inexactitude is of his own making. But

13 176 F.2d 815, 817 (6th Cir. 1949), *cert. denied*, 338 U.S. 949 (1950).

14 *Podems v. Comm’r*, 24 T.C. 21, 22-23 (1955).

15 IRC § 162(a).

16 IRC § 263. See also *INDOPCO, Inc. v. Comm’r*, 503 U.S. 79 (1992).

17 IRC § 167; IRC § 179. Note, the Tax Cuts and Jobs Act increased the maximum deduction under IRC § 179 from \$500,000 to \$1 million and increased the maximum asset-spending phaseout from \$2 million to \$2.5 million. IRC § 179(b)(1), (b)(2).

18 See *PNC Bancorp, Inc. v. Comm’r*, 212 F.3d 822 (3d Cir. 2000); *Norwest Corp. v. Comm’r*, 108 T.C. 265 (1997).

19 IRC § 6001. See also Treas. Reg. §§ 1.6001-1 and 1.446-1(a)(4).

20 See *Cohan v. Comm’r*, 39 F.2d 540 (2d Cir. 1930).

21 *Id.* George M. Cohan was an actor, playwright, and producer who spent large sums travelling and entertaining actors, employees, and critics. Although Cohan did not keep a record of his spending on travel and entertainment, he estimated that he incurred \$55,000 in expenses over several years. The Board of Tax Appeals, now the Tax Court, disallowed these deductions in full based on Cohan’s lack of supporting documentation. Nevertheless, on appeal, the Second Circuit concluded that Cohan’s testimony established that legitimate deductible expenses had been incurred. As a result, the Second Circuit remanded the case back to the Board of Tax Appeals with instructions to estimate the amount of deductible expenses.

to allow nothing at all appears to us inconsistent with saying that something was spent.”<sup>22</sup> In *Estate of Elkins v. Commissioner*, the Fifth Circuit described “the venerable lesson of Judge Learned Hand’s opinion in *Cohan*: In essence, make as close an approximation as you can, but never use a zero.”<sup>23</sup>

The *Cohan* rule cannot be used in situations where IRC § 274(d) applies. IRC § 274(d) provides that unless a taxpayer complies with strict substantiation rules, no deductions are allowable for:

- Travel expenses;
- Gifts; and
- Certain “listed property.”<sup>24</sup>

A taxpayer must substantiate a claimed IRC § 274(d) expense with adequate records or sufficient evidence to establish the amount, time, place, and business purpose.<sup>25</sup> A contemporaneous log is not explicitly required, but a statement not made at or near the time of the expenditure has the same degree of credibility only if the corroborative evidence has “a high degree of probative value.”<sup>26</sup>

### Who Has the Burden of Proof in a Substantiation Case?

Generally, the taxpayer bears the burden of proving that he or she is entitled to the business expense deductions and the IRS’s proposed determination of tax liability is incorrect.<sup>27</sup> IRC § 7491(a) provides that the burden of proof shifts to the IRS when the taxpayer:

- Introduces credible evidence with respect to any factual issue relevant to ascertaining the taxpayer’s liability;
- Complies with the requirements to substantiate deductions;
- Maintains all records required under the Code; and
- Cooperates with reasonable requests by the IRS for witnesses, information, documents, meetings, and interviews.

## ANALYSIS OF LITIGATED CASES

The deductibility of trade or business expenses has been one of the ten MLIs since the first edition of the National Taxpayer Advocate’s Annual Report to Congress in 1998.<sup>28</sup> This year, we reviewed 106 cases involving trade or business expenses that were litigated in federal courts from June 1, 2017, through May 31, 2018. Table 2 listed in Appendix 3. contains a list of the respective issues in these cases.

22 39 F.2d 540 (2d Cir. 1930) at 544, *aff’g and remanding* 11 B.T.A. 743 (1928).

23 767 F.3d 443, 449 n. 7 (5th Cir. 2014) (citing *Cohan*, 39 F.2d at 543-44), *rev’g* 140 T.C. 86 (2013).

24 “Listed property” means any passenger automobile; any other property used as a means of transportation; any property of a type generally used for purposes of entertainment, recreation, or amusement; any computer or peripheral equipment (except when used exclusively at a regular business establishment and owned or leased by the person operating such establishment); and any other property specified by regulations. IRC § 280F(d)(4)(A) and (B).

25 Treas. Reg. § 1.274-5T(b). Ironically, if George M. Cohan brought his case today before the Tax Court, he would be unable to benefit from application of that rule because of the strict substantiation required by IRC § 274(d).

26 Treas. Reg. § 1.274-5T(c)(1); *Reynolds v. Comm’r*, 296 F.3d 607, 615-16 (7th Cir. 2002) (noting that keeping written records is not the only method to substantiate IRC § 274 expenses but “alternative methods are disfavored”).

27 See *Welch v. Helvering*, 290 U.S. 111, 115 (1933) (citations omitted) and U.S. Tax Court Rules of Practice and Procedure, Rule 142(a).

28 See National Taxpayer Advocate 1998-2016 Annual Reports to Congress.

Figure 3.2.1 categorizes the main issues raised by taxpayers. Cases involving more than one issue are included in more than one category.

**FIGURE 3.2.1, Trade or Business Expense Issues Cases Reviewed<sup>29</sup>**

Issue	Type of Taxpayer	
	Individual	Business
Substantiation of Expenses Under IRC § 162, Including Application of the <i>Cohan</i> Rule	3	44
Substantiation of Expenses Under IRC § 274(d)	9	23
Schedule A Unreimbursed Employee Expenses Requiring Proof Employer Did Not Reimburse Taxpayer Under IRC § 162	14	5
Hobby Losses, Nondeductible Under Either IRC §§ 183 or 162	1	12
Home Office Under IRC § 280A	0	3
Net Operating Losses Under IRC § 172	0	7
Personal Expenditures Disallowed Under IRC § 262	2	1
Capitalization and Cost Recovery Under IRC §§ 263, 263A, 195, 179, and 167	3	9
Illegal Activities Under IRC §§ 280E, 162(c), 162(f), and 162(g)	0	1
Economic Substance Doctrine	1	3
Business Bad Debt Deduction Under IRC § 166	0	10
Not Engaged In a Trade or Business Under IRC § 162	2	10
Interest Deduction Under IRC § 163	0	2

Taxpayers represented themselves (*pro se*) in 60 of the 106 cases (about 57 percent). Taxpayers were represented by counsel in 46 out of the 106 cases (about 43 percent). Of the 106 cases, the taxpayers prevailed in six cases in full, and in 19 cases in part. The IRS won in the remaining 81 cases. None of the *pro se* individual taxpayers prevailed in full.

As in previous years, a number of individual taxpayers claimed deductions for Schedule A unreimbursed employee expenses that were either related to personal rather than business activities or the taxpayer did not meet the burden of showing his or her employer would not reimburse these expenses.<sup>30</sup> Additionally, taxpayers claimed travel, meals, and entertainment expenses, but occasionally failed to meet the heightened substantiation requirements of IRC § 274(d).<sup>31</sup> Many *pro se* litigants were unable to meet substantiation requirements.<sup>32</sup>

29 Multiple issues can appear within one case; therefore these figures will not match the total case count.

30 See, e.g., *Farolan v. Comm'r*, T.C. Summ. Op. 2018-28; *Cates v. Comm'r*, T.C. Memo. 2017-178, *appeal dismissed*, (11th Cir. Apr. 30, 2018); *Beckey v. Comm'r*, T.C. Summ. Op. 2017-80.

31 See *Lewis v. Comm'r*, T.C. Memo. 2017-117; *Fehr v. Comm'r*, T.C. Summ. Op. 2018-26.

32 See *Wooten v. Comm'r*, T.C. Summ. Op. 2017-58.

### Individual Taxpayers

Unsurprisingly, relatively few of this year's IRC § 162 trade or business cases involve individual taxpayers (the term "individual" excludes sole proprietorships). All of these cases were issued as either Tax Court memorandum opinions or summary opinions.<sup>33</sup> Two cases illustrating some of the most commonly arising issues in individual trade or business cases are *Baham v. Commissioner* and *Rademacher v. Commissioner*.<sup>34</sup>

Although Tax Court summary opinions have no precedential value, the Tax Court's decision in *Baham v. Commissioner* provides an instructive scenario in which *pro se* Taxpayers (a husband and wife) sought to deduct, as unreimbursed employee business expenses, costs the wife incurred in relation to various animals she brought into the classroom as a teacher.<sup>35</sup> In order for a teacher to deduct expenses for teaching supplies, the supplies must be directly related to the job and a necessary expense of being a teacher, not just helpful to students and appropriate for use in the classroom.<sup>36</sup>

At various points, Mrs. Baham acquired and cared for two bearded dragons, two African gray parrots, several red-eared sliders, two rabbits, koi, a tortoise, and a rainbow boa that she kept in the classroom during the school year. She then would take them home at the end of each school year to look after them over the summer. The Tax Court determined the related expenses generally were not personal expenditures, as testimony indicated that her children disliked having the animals at home because they were required to clean up after them, and the animals were not given names. Moreover, the animals did assist the teacher in her work, as they reduced tardiness and truancy and helped better engage the attention of students.

Nevertheless, the Tax Court denied Taxpayers' claimed deductions on the grounds that the expenses were not "ordinary and necessary," as required by IRC § 162. "We do not doubt that the classroom animals were pedagogically helpful to students and appropriate for classroom use, but this is not sufficient to cause these expenses to be deductible as ordinary and necessary business expenses." The court based its holding on the premise that, although teachers may, at times, provide equipment for classroom use out of their own funds, they do not do so ordinarily, even though the result might be to enhance their reputations as dedicated teachers or to increase the quality of the education they provide.

As discussed in the Present Law section above, taxpayers must substantiate their trade or business expenditures. Additionally, certain categories of expenses are subject to heightened substantiation requirements under IRC § 274(d). One case considering whether these more stringent standards were met is *Rademacher v. Commissioner*, which examined the expenses of a manager of a used car business.<sup>37</sup> Taxpayer, as part of his duties, incurred expenses for vehicle mileage, travel, meals, and entertainment, which he sought to deduct.

33 Tax Court decisions are categorized into three types: regular decisions, memorandum decisions, and small tax case ("S") decisions. The regular decisions of the Tax Court include cases which have some new or novel point of law, or in which there may not be general agreement, and therefore have the most legal significance. In contrast, memorandum decisions generally involve fact patterns within previously settled legal principles and therefore are not as legally significant. Finally, "S" case decisions (for disputes involving \$50,000 or less where the taxpayer has elected Small Case status) are not appealable and thus have no precedential value. See also IRC § 7463(b); U.S. Tax Court Rules of Practice and Procedure, Rules 170-175.

34 *Baham v. Comm'r*, TC Summ. Op. 2017-85; *Rademacher v. Comm'r*, T.C. Memo 2018-43.

35 *Baham v. Comm'r*, T.C. Summ. Op. 2017-85.

36 *Farias v. Comm'r*, T.C. Memo. 2011-248 (citations omitted).

37 *Rademacher v. Comm'r*, T.C. Memo. 2018-43.

The Tax Court disallowed Taxpayer's meals and entertainment expenses attributable to snacks, coffee, and drinks for potential clients, which he estimated at approximately \$60 per day, but could not document.<sup>38</sup> On the other hand, as part of his duties, Taxpayer was required to attend the same four car auctions every week, to which he drove his personal vehicle. As he was not reimbursed for this mileage and could establish that he drove approximately 38,000 miles per year for the years in question, the Tax Court held that Taxpayer had met his substantiation burden, even under the heightened standards of IRC § 274(d). Accordingly, these deductions were sustained.

### Business Taxpayers

TAS reviewed 86 cases involving business taxpayers. In this context, business taxpayers fully prevailed in six cases (approximately seven percent), partially prevailed in 13 cases (approximately 15 percent), and the IRS was completely successful in the remaining cases (approximately 78 percent).

Of cases in which business taxpayers fully or partially prevailed, 47 percent (9 of 19) involved taxpayers represented by counsel. Alternatively, ten *pro se* business taxpayers partially prevailed, but none fully prevailed. Of cases in which the IRS fully prevailed, approximately 49 percent (33 of 67) involved business taxpayers represented by counsel, while approximately 51 percent (34 of 67) involved *pro se* taxpayers.

As was the case for the individual taxpayers, substantiation of deductible expenses was by far the most prevalent issue. In most such cases, courts denied business taxpayers' deductions for failure to substantiate.<sup>39</sup> However, courts did allow deductions for some expenses when business taxpayers were able to provide sufficient evidence in the form of records, receipts, or logs.<sup>40</sup> Courts occasionally applied the *Cohan* rule where the taxpayer presented sufficient documentation to prove an expense was incurred but had limited documentation of the precise amount.<sup>41</sup> As previously mentioned, however, IRC § 274(d) makes the *Cohan* rule unavailable in certain circumstances in which taxpayers are subject to heightened documentation requirements.

Nevertheless, even where IRC § 274(d) requirements are absent, the courts still demand the production of persuasive evidence before they will apply *Cohan*. For example, in *Brookes v. Commissioner*, a husband and wife carried on a business under the auspices of Brookes Financial, an S corporation.<sup>42</sup> Taxpayer wife operated an art business, while Taxpayer husband conducted a financial services and tax return preparation business.

Among other expenditures, Taxpayers sought to deduct miscellaneous expenses through their S corporation, including legal and professional fees, maintenance costs, office expenses, and storage, telephone, and utility charges. The Tax Court determined Taxpayers provided poorly organized evidence but nonetheless looked at the merits of the case and applied the *Cohan* rule. As explained by

38 Under changes made by the Tax Cuts and Jobs Act, Pub. L. No. 115-97, 131 Stat. 2054, 2124 (2017), deductions for entertainment expenses are no longer allowable for amounts incurred or paid after December 31, 2017. IRC § 274(a)(1). Subject to various limitations, meals remain deductible to the extent that they do not constitute entertainment.

39 See, e.g., *RJ Channels, Inc. v. Comm'r*, T.C. Memo. 2018-27; *Justine v. Comm'r*, T.C. Memo. 2017-198.

40 See, e.g., *Cai v. Comm'r*, T.C. Memo. 2018-52.

41 See, e.g., *Pokawa v. Comm'r*, T.C. Memo. 2017-186.

42 *Brookes v. Comm'r*, T.C. Memo. 2017-146.

the Tax Court, however, Taxpayers' level of substantiation was insufficient even to support an estimate of any deductions:

The Court has sustained respondent's determination with regard to these deductions because petitioners have failed to offer any evidence that certain expenses were in fact paid and because petitioners' lack of receipts, confusing and inconsistent accounting techniques, and vague testimony leave the Court with no reasonable means of differentiating or estimating which of the reported expenses Brookes Financial paid as ordinary and necessary business expenses.

By contrast, the Tax Court was willing to apply *Cohan* to allow some deductions for art supply costs and rental expenditures. The Tax Court began its analysis by determining that Taxpayers did not meet their substantiation burden because of illegible or insufficient receipts for the art supplies and a lack of proof of payment for the rent. Nevertheless, the court applied *Cohan* to allow Taxpayers a portion of their claimed deductions, as the court was persuaded that such payments had been made and the minimum amount could be estimated with reasonable accuracy.

Another issue that is the subject of recurring litigation from year to year involves taxpayers' attempts to deduct losses from activities that may or may not be engaged in for profit. To the extent that an activity is carried on as a trade or business, such losses are fully deductible, but to the extent that the activity in question represents a hobby, expenses are only deductible against income generated by the activity. For example, in *Knowles v. Commissioner*, Taxpayer, in addition to other deductions, claimed losses attributable to Big Dog Farms, which was established for the purpose of breeding, selling, and showing horses.<sup>43</sup>

The Tax Court examined Taxpayer's deductions using the nine factor test of Treas. Reg. § 1.183-2(b).<sup>44</sup> Among other things, the Tax Court determined that Big Dog Farm's losses were perpetual and substantial; that the activity was not carried on in a businesslike manner; that Taxpayer could not substantiate that she had ever hired professionals to assist in operating the horse farm; that Taxpayer demonstrated no reasonable expectation that the farm or its assets would appreciate in value; and that Taxpayer was a medical doctor who had significant income during the tax years at issue, and the losses from Big Dog Farms would generate substantial tax benefits. Based on these factual findings, the Tax Court concluded that Big Dog Farms was not a for-profit activity and generated hobby losses that, under IRC § 183, could only be deducted against income generated by the horse farm.<sup>45</sup>

In cases where the existence of a business is not in controversy, the courts are sometimes called upon to determine whether a given transaction had economic substance and therefore produced an expense deductible under IRC § 162 or related Code sections. For example, in *Rutter v. Commissioner*, Taxpayer operated a medical technology company that did business as a C corporation.<sup>46</sup> Taxpayer, a reknowned

<sup>43</sup> *Knowles v. Comm'r*, T.C. Memo. 2017-152.

<sup>44</sup> Those factors are: (1) the manner in which the taxpayer carries on the activity; (2) the expertise of the taxpayer or his advisors; (3) the time and effort expended by the taxpayer in carrying on the activity; (4) the expectation that assets used in the activity may appreciate in value; (5) the success of the taxpayer in carrying on similar or dissimilar activities; (6) the taxpayer's history of income or losses with respect to the activity; (7) the amount of occasional profits, if any, which are earned; (8) the financial status of the taxpayer; and (9) elements of personal pleasure or recreation.

<sup>45</sup> To illustrate the frequency with which this controversy arises with respect to horsebreeding operations, see *Hylton v. Comm'r*, 721 F. App'x 300 (4th Cir. 2018), *aff'g* T.C. Memo. 2016-234, *reh'g* and *reh'g en banc denied*, No. 17-1777 (4th Cir. Aug. 3, 2018), and *McMillan v. Comm'r*, 697 F. App'x 489 (9th Cir. 2017), *aff'g* T.C. Memo. 2013-40, *cert. denied*, 138 S.Ct. 1010 (2018).

<sup>46</sup> *Rutter v. Comm'r*, T.C. Memo. 2017-174, *appeal dismissed*, No. 17-73320 (9th Cir. Jan. 30, 2018).

biotechnologist, previously had played a role in sequencing the HIV genome; discovering the Hepatitis C virus; developing a diagnostic test to detect HIV and the Hepatitis B and C viruses; developing the first vaccine for the Hepatitis B virus using recombinant DNA technology; and co-developing a method to clone human insulin genes to produce vaccines that are used throughout the world. His new company, iMetrikus International (iMetrikus) developed technology systems to improve doctor-patient access to clinical data via a device and an application. Taxpayer was not a shareholder of common stock in iMetrikus; he was its driving force and funded the bulk of its operations through cash advances. Ultimately, the company was unable to form the corporate partnerships it had envisioned, incurred millions of dollars of losses, and eventually ceased business operations. As the company's financial situation became increasingly precarious, Taxpayer and the company entered into negotiations regarding the cash he had previously contributed, as part of which they collectively executed a debt forgiveness certificate for \$8.55 million.

Taxpayer sought to deduct this amount under IRC § 166 as a bad debt incurred in the course of a trade or business. The IRS, however, argued that the \$8.55 million was not debt, but instead represented equity that could not yet be deducted. In analyzing the issue, the Tax Court looked to the economic substance of the transfers in question. “The question of whether the advances...are debt or equity depends on the economic substance of the transactions between them and not upon the form of the advances.”<sup>47</sup>

As a guide to analyzing the cash advances, the Tax Court considered a range of nonexclusive factors traditionally distinguishing debt from equity. For example, Taxpayer acted as a capital investor, rather than a creditor; exercised management control over the company; and provided funds under circumstances and terms that no regular creditor would have found acceptable. Based on these criteria, the Tax Court concluded that, in substance, the cash advances represented equity in the company. Accordingly, Taxpayer's IRC § 166 bad debt deduction was disallowed.

A separate element essential to an IRC § 162 deduction is the taxpayer's ability to prove that it was incurred in the year in which the deduction is claimed. This issue arises in another IRC § 166 case, *Hatcher v. Commissioner*.<sup>48</sup> Taxpayer loaned her boyfriend approximately \$400,000 over a period of years to develop a golf-themed cartoon strip entitled, “In the Rough.” Later, after the boyfriend became an ex-boyfriend, she sought repayment in 2010 and received an email saying, “I HAVE NO MONEY.” Shortly thereafter, Taxpayer and her husband sued the ex-boyfriend in an attempt to recover some or all of the amounts loaned. Ultimately, no money was ever recovered and Taxpayer sought to claim a bad debt deduction for the principal interest in 2010.

The Fifth Circuit, however, affirmed the Tax Court's decision that Taxpayer had failed her burden of proving that the debt actually became worthless in 2010. In particular, the Fifth Circuit noted that Taxpayer's attempts to collect the debt via legal proceedings in 2011 and related negotiations in 2012 were inconsistent with the position that the debt was worthless as of 2010. Consequently, even though the debt may have been worthless in a later year and properly deductible in that year, it could not be claimed as an IRC § 166 bad debt deduction related to the conduct of a trade or business in 2010.

Once expenses otherwise deductible under IRC § 162 are established, the question arises regarding whether those expenditures created assets with a useful life of more than one year, such that the

47 Rutter, T.C. Memo. 2017-174 (quoting *Davis v. Comm'r*, 69 T.C. 814, 835 (1978)).

48 *Hatcher v. Comm'r*, 726 F. App'x (5th Cir. 2018), *aff'g* T.C. Memo. 2016-188.

expenditures must be capitalized and depreciated over the useful life of the assets.<sup>49</sup> In *Wells v. Commissioner*, Taxpayer owned and operated a farm in Colorado, which produced grapes for wine and grape juice, and which also leased part of its land to third parties for the grazing of horses and cattle.<sup>50</sup> The farm experienced a number of nature-related setbacks, including drought, a wildfire, flooding, and bears that consumed much of the grape harvest and damaged vines. Taxpayer incurred a variety of resulting costs, including installation of an improved piping system carrying water throughout the farm, replacement of a road, construction of fencing, and rehabilitation of areas damaged by fire. Taxpayer sought to currently deduct under IRC § 162 the full amount of these expenses.

Although allowing some of the claimed deductions, the IRS contended that the bulk of the expenses should be capitalized and recovered over time. The Tax Court generally agreed with the IRS, ruling that these expenditures did not simply restore the property to its prior condition, but extended the useful life of the property for a period in excess of one year. Most of the expenditures were made as part of a long-term plan of improvement and could not be fully deducted in the year incurred. Accordingly, the Tax Court required that the expenditures be capitalized and recovered over time as depreciation deductions.

## CONCLUSION

The existence and amount of allowable business expenses are highly fact-specific and are often open to interpretation. IRC § 162 deductions are based upon a complex interaction of multiple statutes and regulations, as well as case law. This circumstance perpetuates substantial controversy between the IRS and taxpayers regarding the scope and extent of properly claimed business deductions. As a result, courts rendered decisions in over 106 cases involving IRC § 162 related issues between June 1, 2017, and May 31, 2018.

As in prior years, a variety of cases arose regarding the merits of claimed deductions for home office expenses, hobby losses, and business expenses that were held to be personal in nature. Many of these cases involved taxpayers' often-unsuccessful attempts to meet general substantiation requirements or to comply with the heightened substantiation rules of IRC § 274(d). Moreover, a number of taxpayers in this year's litigated cases evidenced difficulty distinguishing between nondeductible personal expenses or hobby losses on the one hand, and deductible business expenses on the other hand.

As recommended by the National Taxpayer Advocate in the past, ongoing efforts to educate taxpayers and their representatives on these subjects are an essential element of tax compliance and would benefit both taxpayers and the IRS.<sup>51</sup> Also, consistent with observed historical patterns, many *pro se* litigants were unable to meet substantiation requirements. This circumstance presents an opportunity for the IRS to conduct better outreach and education on substantiation issues. However, we note that there are only 105 employees dedicated to outreach for small business/self-employed taxpayers, and 17 states have no such employee within their borders.<sup>52</sup>

49 The capitalization analysis occurs under IRC §§ 263 and 263A, while the period over which the capitalized costs will be recovered is generally determined by IRC § 167.

50 *Wells v. Comm'r*, T.C. Memo. 2018-11, *appeal docketed*, No. 18-9007 (10th Cir. Aug. 27, 2018).

51 National Taxpayer Advocate 2016 Annual Report to Congress 388-389.

52 National Taxpayer Advocate Fiscal Year (FY) 2019 Annual Report to Congress 2.

Additionally, many of the cases that are litigated in this area likely could be resolved at the administrative level if the IRS developed and implemented a more robust alternative dispute resolution program.<sup>53</sup> Such a program would facilitate a dialogue between taxpayers and the IRS that would clarify disputed facts and would help taxpayers better understand the applicable law. This process for clarification and education would enable taxpayers and the IRS to administratively resolve an increased number of cases and generally resort to litigation only where there are true disagreements regarding the facts or law essential to a case decision. It would also further taxpayers' rights *to be informed* and *to challenge the IRS's position and be heard*.

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53 National Taxpayer Advocate 2016 Annual Report to Congress 211-219.

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## Summons Enforcement Under IRC §§ 7602, 7604, and 7609

## SUMMARY

Pursuant to Internal Revenue Code (IRC) § 7602, the IRS may examine any books, records, or other data relevant to an investigation of a civil or criminal tax liability.<sup>1</sup> To obtain this information, the IRS may serve a summons directly on the subject of the investigation or any third party who may possess relevant information.<sup>2</sup> If a person summoned under IRC § 7602 neglects or refuses to obey the summons; to produce books, papers, records, or other data; or to give testimony as required by the summons, the IRS may seek enforcement of the summons in a United States District Court.<sup>3</sup>

A person who has a summons served on him or her may contest its legality if the government petitions to enforce it.<sup>4</sup> Thus, summons enforcement cases are different from many other cases described in other Most Litigated Issues because often the government, rather than the taxpayer, initiates the litigation. If the IRS serves a summons on a third party, any person entitled to notice of the summons may challenge its legality by filing a motion to quash or by intervening in any proceeding regarding the summons.<sup>5</sup> Generally, the burden on the taxpayer to establish the illegality of the summons is heavy.<sup>6</sup> When challenging the summons's validity, the taxpayer generally must provide "some credible evidence" supporting an allegation of bad faith or improper purpose.<sup>7</sup> The taxpayer is entitled to a hearing to examine an IRS agent about his or her purpose for issuing a summons only when the taxpayer can point to specific facts or circumstances that plausibly raise an inference of bad faith.<sup>8</sup> Naked allegations of improper purpose are not enough, but because direct evidence of IRS's bad faith "is rarely if ever available," circumstantial evidence can suffice to meet that burden.<sup>9</sup>

TAS identified 85 federal cases decided between June 1, 2017, and May 31, 2018, involving IRS summons enforcement issues. The government was the initiating party in 61 cases, while the taxpayer was the initiating party in 24 cases. Overall, taxpayers fully prevailed in three cases, while four cases were split. The IRS prevailed in the remaining 78 cases.

1 Internal Revenue Code (IRC) § 7602(a)(1); Treas. Reg. § 301.7602-1.

2 IRC § 7602(a).

3 IRC § 7604(b).

4 *U.S. v. Powell*, 379 U.S. 48, 58 (1964).

5 IRC § 7609(b).

6 *U.S. v. LaSalle Nat'l Bank*, 437 U.S. 298, 316 (1978).

7 *U.S. v. Clarke*, 134 S. Ct. 2361, 2367 (2014), *vacating* 517 F. App'x 689 (11th Cir. 2013), *rev'g* 2012-2 U.S.T.C. (CCH) ¶ 50,732 (S.D. Fla. 2012).

8 *Id.* (stating that "[t]he taxpayer need only make a showing of facts that give rise to a plausible inference of improper motive").

9 *U.S. v. Clarke*, 134 S. Ct. 2361, 2367-68 (2014), *vacating* 517 F. App'x 689 (11th Cir. 2013), *rev'g* 2012-2 U.S.T.C. (CCH) ¶ 50,732 (S.D. Fla. 2012).

## TAXPAYER RIGHTS IMPACTED<sup>10</sup>

- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to Privacy*
- *The Right to a Fair and Just Tax System*

## PRESENT LAW

The IRS has broad authority under IRC § 7602 to issue a summons to examine a taxpayer's books and records or demand testimony under oath.<sup>11</sup> Further, the IRS may obtain information related to an investigation from a third party if, subject to the exceptions of IRC § 7609(c), it provides notice to the taxpayer or other person identified in the summons.<sup>12</sup> In limited circumstances, the IRS can issue a summons even if the name of the taxpayer under investigation is unknown, *i.e.*, a "John Doe" summons.<sup>13</sup> However, the IRS cannot issue a summons after referring the matter to the Department of Justice (DOJ).<sup>14</sup>

If the recipient fails to comply with a summons, the United States may commence an action under IRC § 7604 in the appropriate United States District Court to compel document production or testimony.<sup>15</sup> If the United States files a petition to enforce the summons, the taxpayer may contest the validity of the summons in that proceeding.<sup>16</sup> Also, if the summons is served upon a third party, any person entitled to notice may petition to quash the summons in an appropriate district court, and may intervene in any proceeding regarding the enforceability of the summons.<sup>17</sup>

Generally, a taxpayer or other person named in a third-party summons is entitled to notice.<sup>18</sup> However, the IRS does not have to provide notice in certain situations. For example, the IRS is not required to give notice if the summons is issued to aid in the collection of "an assessment made or judgment rendered against the person with respect to whose liability the summons is issued."<sup>19</sup> Congress created this exception because it recognized a difference between a summons issued to compute the taxpayer's taxable income and a summons issued after the IRS has assessed tax or obtained a judgment.

10 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the IRC. See IRC § 7803(a)(3).

11 IRC § 7602(a). See also *LaMura v. U.S.*, 765 F.2d 974, 979 (11th Cir. 1985) (citing *U.S. v. Bisceglia*, 420 U.S. 141, 145-146 (1975)).

12 IRC § 7602(c). Those entitled to notice of a third-party summons (other than the person summoned) must be given notice of the summons within three days of the day on which the summons is served to the third party but no later than the 23rd day before the day fixed on the summons on which the records will be reviewed. IRC § 7609(a).

13 The court must approve a "John Doe" summons prior to issuance. In order for the court to approve the summons, the United States commences an *ex parte* proceeding. The United States must establish during the proceeding that its investigation relates to an ascertainable class of persons; it has a reasonable basis for the belief that these unknown taxpayers may have failed to comply with the tax laws; and it cannot obtain the information from another readily available source. IRC § 7609(f).

14 IRC § 7602(d). This restriction applies to "any summons, with respect to any person if a [DOJ] referral is in effect with respect to such person." IRC § 7602(d)(1).

15 IRC § 7604.

16 *U.S. v. Powell*, 379 U.S. 48, 58 (1964).

17 IRC § 7609(b). The petition to quash must be filed not later than the 20th day after the date on which the notice was served. IRC § 7609(b)(2)(A).

18 IRC § 7609(a)(1); Treas. Reg. § 301.7609-1(a)(1). See, e.g., *Cephas v. U.S.*, 112 A.F.T.R.2d (RIA) 6483 (D. Md. 2013).

19 IRC § 7609(c)(2)(D)(i). The exception also applies to the collection of a liability of "any transferee or fiduciary of any person referred to in clause (i)." IRC § 7609(c)(2)(D)(ii).

For example, the IRS does not have to give notice to the taxpayer or person named in the summons if it is attempting to determine whether the taxpayer has an account in a certain bank with sufficient funds to pay an assessed tax because such notice might seriously impede the IRS's ability to collect the tax.<sup>20</sup> Courts have interpreted this "aid in collection" exception to apply only if the taxpayer owns a legally identifiable interest in the account or other property for which records are summoned.<sup>21</sup> Additionally, the IRS is not required to give notice when, in connection with a criminal investigation, an IRS criminal investigator serves a summons on any person who is not the third-party record-keeper.<sup>22</sup>

Whether the taxpayer contests the summons in a motion to quash or in response to the United States' petition to enforce, the legal standard is the same.<sup>23</sup> In *United States v. Powell*, the Supreme Court set forth four threshold requirements (referred to as the *Powell* requirements) that must be satisfied to enforce an IRS summons:

1. The investigation must be conducted for a legitimate purpose;
2. The information sought must be relevant to that purpose;
3. The IRS must not already possess the information; and
4. All required administrative steps must have been taken.<sup>24</sup>

The IRS bears the initial burden of establishing that these requirements have been satisfied.<sup>25</sup> The government meets its burden by providing a sworn affidavit of the IRS agent who issued the summons declaring that each of the *Powell* requirements has been satisfied.<sup>26</sup> The burden then shifts to the person contesting the summons to demonstrate that the IRS did not meet the requirements or that enforcement of the summons would be an abuse of process.<sup>27</sup>

The taxpayer can show that enforcement of the summons would be an abuse of process if he or she can prove that the IRS issued the summons in bad faith.<sup>28</sup> In *United States v. Clarke*, the Supreme Court held that during a summons enforcement proceeding, a taxpayer has a right to conduct an examination of the responsible IRS officials about whether a summons was issued for an improper purpose only when the taxpayer "can point to specific facts or circumstances plausibly raising an inference of bad faith."<sup>29</sup> Blanket claims of improper purpose are not sufficient, but circumstantial evidence can be.<sup>30</sup>

20 H.R. REP. NO. 94-658 AT 310, REPRINTED IN 1976 U.S.C.C.A.N. AT 3206. SEE ALSO S. REP. NO. 94-938, PT. 1, AT 371, REPRINTED IN 1976 U.S.C.C.A.N. AT 3800-01 (containing essentially the same language).

21 *Ip v. U.S.*, 205 F.3d 1168, 1172-1176 (9th Cir. 2000).

22 IRC § 7609(c)(2)(E). A third-party record-keeper is broadly defined and includes banks, consumer reporting agencies, persons extending credit by credit cards, brokers, attorneys, accountants, enrolled agents, and owners or developers of computer source code but only when the summons "seeks the production of the source or the program or the data to which the source relates." IRC § 7603(b)(2).

23 *Kamp v. U.S.*, 112 A.F.T.R.2d (RIA) 6630 (E.D. Cal. 2013).

24 *U.S. v. Powell*, 379 U.S. 48, 57-58 (1964).

25 *Fortney v. U.S.*, 59 F.3d 117, 119-120 (9th Cir. 1995).

26 *U.S. v. Dynavac, Inc.*, 6 F.3d 1407, 1414 (9th Cir. 1993).

27 *Id.*

28 *U.S. v. Powell*, 379 U.S. 48, 58 (1964).

29 *U.S. v. Clarke*, 134 S. Ct. 2361, 2367 (2014), *vacating* 517 F. App'x 689 (11th Cir. 2013), *rev'g* 2012-2 U.S.T.C. (CCH) ¶ 50,732 (S.D. Fla. 2012).

30 *U.S. v. Clarke*, 134 S. Ct. 2361, 2367-68 (2014), *vacating* 517 F. App'x 689 (11th Cir. 2013), *rev'g* 2012-2 U.S.T.C. (CCH) ¶ 50,732 (S.D. Fla. 2012).

A taxpayer may also allege that the information requested is protected by a constitutional, statutory, or common-law privilege, such as the:

- Fifth Amendment privilege against self-incrimination;
- Attorney-client privilege;<sup>31</sup>
- Tax practitioner privilege;<sup>32</sup> or
- Work product privilege.<sup>33</sup>

However, these privileges are limited. For example, courts reject blanket assertions of the Fifth Amendment,<sup>34</sup> but note that taxpayers may have valid Fifth Amendment claims regarding specific documents or testimony.<sup>35</sup> However, even if a taxpayer may assert the Fifth Amendment on behalf of him or herself, he or she cannot assert it on behalf of a business entity.<sup>36</sup>

Additionally, taxpayers cannot, on the basis of the Fifth Amendment privilege, withhold self-incriminatory evidence of a testimonial or communicative nature if the summoned documents fall within the “foregone conclusion” exception to the Fifth Amendment. The exception applies if the government establishes its independent knowledge of three elements:

1. The documents’ existence;
2. The documents’ authenticity; and
3. The possession or control of the documents by the person to whom the summons was issued.<sup>37</sup>

The attorney-client privilege protects “tax advice,” but not tax return preparation materials.<sup>38</sup> The “tax shelter” exception limits the tax practitioner privilege and permits discovery of communications between a practitioner and client that promote participation in any tax shelter.<sup>39</sup> Thus, the tax practitioner privilege does not apply to any written communication between a federally authorized tax practitioner and “any person, any director, officer, employee, agent, or representative of the person, or any other person holding a capital or profits interest in the person” which is “in connection with the promotion of the direct or indirect participation of the person in any tax shelter.”<sup>40</sup>

31 The attorney-client privilege provides protection from discovery of information where: (1) legal advice of any kind is sought, (2) from a professional legal advisor in his or her capacity as such, (3) the communication is related to this purpose, (4) made in confidence, (5) by the client, (6) and at the client’s insistence protected, (7) from disclosure by the client or the legal advisor, (8) except where the privilege is waived. *U.S. v. Evans*, 113 F.3d 1457, 1461 (7th Cir. 1997) (citing 8 JOHN HENRY WIGMORE, EVIDENCE IN TRIALS AT COMMON LAW § 2292 (John T. McNaughten rev. 1961)).

32 IRC § 7525 extends the protection of the common law attorney-client privilege to federally authorized tax practitioners in federal tax matters. Criminal tax matters and communications regarding tax shelters are exceptions to the privilege. IRC § 7525(a)(2), (b). The interpretation of the tax practitioner privilege is based on the common law rules of attorney-client privilege. *U.S. v. BDO Seidman, LLP*, 337 F.3d 802, 810-12 (7th Cir. 2003).

33 The work product privilege protects against the discovery of documents and other tangible materials prepared in anticipation of litigation. Fed. R. Civ. P. 26(b)(3); see also *Hickman v. Taylor*, 329 U.S. 495 (1947).

34 See, e.g., *U.S. v. McClintic*, 113 A.F.T.R.2d (RIA) 330 (D. Or. 2013).

35 See, e.g., *U.S. v. Lawrence*, 113 A.F.T.R.2d (RIA) 1933 (S.D. Fla. 2014).

36 *Braswell v. U.S.*, 487 U.S. 99 (1988).

37 *U.S. v. Bright*, 596 F.3d 683, 692 (9th Cir. 2010).

38 *U.S. v. Frederick*, 182 F.3d 496, 500 (7th Cir. 1999).

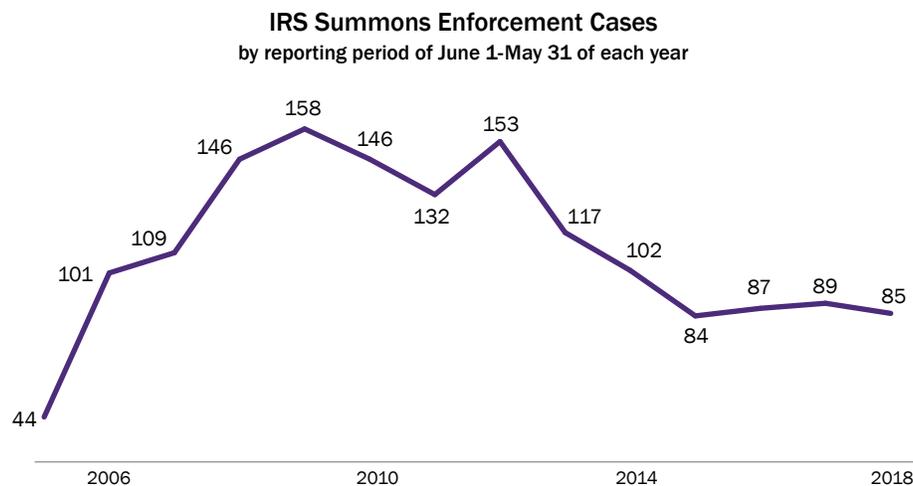
39 IRC § 7525(b). See also *Valero Energy Corp. v. U.S.*, 569 F.3d 626 (7th Cir. 2009).

40 IRC § 7525(b). A tax shelter is defined as “a partnership or other entity, any investment plan or arrangement, or any other plan or arrangement, if a significant purpose of such partnership, entity, plan, or arrangement is the avoidance or evasion of Federal income tax.” IRC § 6662(d)(2)(C)(ii).

## ANALYSIS OF LITIGATED CASES

Summons enforcement has been a Most Litigated Issue in the National Taxpayer Advocate's Annual Report to Congress every year since 2005, when TAS identified only 44 cases but predicted the number would rise as the IRS became more aggressive in its enforcement initiatives. The number of cases peaked at 158 for the reporting period ending on May 31, 2009, but had generally declined, except for a one-year increase for the year ending May 31, 2012, as shown in Figure 3.3.1. This year, the number of summons enforcement cases fell slightly, as TAS identified 85 cases for the reporting period ending on May 31, 2018, a decrease from the 89 cases TAS identified during last year's reporting period. A detailed list of these cases appears in Table 3 of Appendix 3.

**FIGURE 3.3.1**



Of the 85 cases TAS reviewed this year, the IRS prevailed in full in 78, a 92 percent success rate, which is one percent less than the 2017 reporting period.<sup>41</sup> Taxpayers had representation in 34 cases (40 percent) and appeared *pro se* (*i.e.*, on their own behalf) in the remaining 51. This is a notable increase in the percentage of represented taxpayers as 28 percent of taxpayers were represented during the 2017 reporting period.<sup>42</sup> This year's percentage of represented taxpayers (40 percent) is a return close to the percentage we observed during the 2016 reporting period, where 44 percent of taxpayers had representation.<sup>43</sup> Sixty-four cases involved individual taxpayers, while the remaining 21 involved business taxpayers, including sole proprietorships.<sup>44</sup> Cases generally involved one of the following themes.

41 See National Taxpayer Advocate 2017 Annual Report to Congress 395.

42 *Id.*

43 See National Taxpayer Advocate 2016 Annual Report to Congress 459.

44 There were cases in which the IRS issued summons for investigations into both the individual taxpayer and his or her business. For the purposes of this Most Litigated Issue, TAS placed these cases into the business taxpayer category.

### Petitions to Enforce and *Powell* Requirements

The United States petitioned to enforce a summons in 61 cases and successfully met its burden under *Powell* in 58 cases.<sup>45</sup> In two cases, taxpayers partially prevailed with *Powell* challenges. An example of a partially successful *Powell* challenge can be found in *United States v. Lui*.<sup>46</sup> In *Lui*, the taxpayer, an individual with interests in foreign entities and bank accounts, was served with summonses on two occasions related to his alleged tax liabilities. In the first summons, the IRS requested testimony from the taxpayer, and in the second summons, the IRS requested testimony and documents concerning the taxpayer's foreign interests. Pursuant to the first summons, the taxpayer refused to testify on privilege grounds. Following the second summons, the taxpayer refused to testify once more, and provided only a portion of the requested documents. The IRS sought a court order to enforce both summonses. Based on the initial petition and accompanying declaration, the court found that the IRS had established a *prima facie* case under *Powell*. Once the government met its initial burden, the burden shifted to the taxpayer. Consequently, the court ordered the taxpayer to show cause as to why he should not be compelled to testify and to produce all the requested documents.

In showing why he should not be compelled to produce all the requested documents, the taxpayer argued that he did not possess, control, or have custody of the requested documents. The IRS had sought a broad range of documents in connection with the taxpayer's foreign holdings and posited that the taxpayer had not provided credible evidence showing that he no longer possessed the documents. In evaluating the parties' claim, the court adopted a sliding scale test from *United States v. Malhas*,<sup>47</sup> *i.e.*, "the more the IRS's evidence suggests the taxpayer possesses the documents at issue, the heavier the taxpayer's burden to successfully demonstrate that he does not." In *Malhas*, the taxpayer had the burden of showing that he was not in possession of documents requested by the IRS. The court found that the taxpayer failed to provide credible evidence, as he relied only on his own affidavits and testimony. In contrast, the IRS provided a plethora of documents and records illustrating the taxpayer's connection with the requested documents. Based upon those facts, the court in *Malhas* found that the taxpayer failed to satisfy his burden.

In contrast to *Malhas*, in the instant case, the court found that the taxpayer had a substantially more compelling position. The taxpayer presented far more than his own affidavit to support his argument of non-possession. The taxpayer showed that he had transferred his interest in the foreign holdings (upon which the document summonses were directed) to the control and custody of his siblings by the date of the summonses. Since the taxpayer transferred the documents, the documents were effectively out of his control. The IRS offered little evidence to the contrary, but pointed out the "suspicious timing" of the transfers. The court noted that suspicious timing alone was insufficient to overcome the plethora of evidence that the taxpayer presented, finding that the taxpayer succeeded in demonstrating that he did not possess documents directly related to the assets he had transferred. However, the court found that the taxpayer had not met the burden of showing that he had no documents related to the transfer of those assets. Accordingly, the court ordered the taxpayer to turn over all records in his possession regarding the transfers, or to submit a declaration under penalty of perjury that no such documents exist.

45 See, e.g., *U.S. v. Cavins*, 121 A.F.T.R.2d (RIA) 2220 (S.D. Ill. 2018); *U.S. v. Elridge*, 121 A.F.T.R.2d (RIA) 1341 (E.D. Ark. 2018); *U.S. v. Morton*, 2017 U.S. App. LEXIS 20409 (6th Cir. 2017), *reh'g denied*, 2017 U.S. App. LEXIS 22757 (6th Cir. 2017), *aff'g* 119 A.F.T.R.2d (RIA) 362 (W.D. Mich. 2016); *U.S. v. Earth, Wind, and Solar, Inc.*, 120 A.F.T.R.2d (RIA) 5328 (E.D. Cal. 2017), *adopting* 119 A.F.T.R.2d (RIA) 2335 (E.D. Cal. 2017); *U.S. v. Pardue*, 120 A.F.T.R.2d (RIA) 5283 (M.D. Fla. 2017), *adopting* 120 A.F.T.R.2d (RIA) 5281 (M.D. Fla. 2017).

46 *U.S. v. Lui*, 120 A.F.T.R.2d (RIA) 5332 (N.D. Cal. 2017).

47 *U.S. v. Malhas*, 116 A.F.T.R.2d (RIA) 6724 (N.D. Ill. 2015).

In showing why he should not be compelled to testify, the taxpayer invoked his Fifth Amendment privilege. A taxpayer may “invoke his Fifth Amendment rights in response to an IRS summons when there are substantial hazards of self-incrimination that are real and appreciable,” but mere blanket assertions of the Fifth Amendment are disallowed. Since the taxpayer asserted his Fifth Amendment privilege to almost every question asked of him during his testimony, the court found that the taxpayer’s invocation of the Fifth Amendment privilege was overbroad and that he should be required to answer at least some additional questions. More specifically, the court ordered the taxpayer to answer the general background questions. However, the court decided not to compel any follow-up questions about the taxpayer’s interests in foreign accounts or his ownership and reporting of foreign entities, except for one question with respect to which *Lui* waived his Fifth Amendment privilege as this topic was included in his declaration to the court. The court also allowed a series of specific follow up questions regarding the taxpayer’s declaration.

Finally the court addressed the taxpayer’s challenge to the IRS’s *prima facie* case and analyzed the *Powell* factors.<sup>48</sup> It concluded that summonses were properly verified following all required administrative steps, were relevant to the taxpayer’s tax liabilities, would lead to discovery of new information, and were not made in bad faith.

Accordingly, the IRS’s petition to enforce summons against the taxpayer was granted in part and denied in part as to the documents he did not possess.

### Petitions to Quash and Lack of Subject Matter Jurisdiction

Taxpayers petitioned to quash an IRS summons to a third party in 25 instances;<sup>49</sup> however, in many of these cases, courts dismissed the petitions for lack of jurisdiction on procedural or notice grounds. For example, an appellate court affirmed a district court’s dismissal of a taxpayer’s petition to quash a summons issued to the taxpayer’s bank because the summons was issued to aid in the collection of a tax and the taxpayer therefore had no recourse under IRC § 7609.<sup>50</sup> In *Rifle Remedies, LLC v. United States*, the taxpayer, a limited liability corporation, sought to quash a summons issued by the IRS to a third party, the Marijuana Enforcement Division of the Colorado Department of Revenue.<sup>51</sup> The IRS was investigating the taxpayer on the basis of IRC § 280E, which prohibits deductions or credits for amounts acquired through the trade or business of trafficking in controlled substances.<sup>52</sup>

The IRS’s burden to enforce the summons “is a slight one because the statute must be read broadly in order to ensure that the enforcement powers of the IRS are not unduly restricted.”<sup>53</sup> After the IRS shows compliance with the *Powell* factors which is usually established by the affidavits of the IRS employees who issued the summons, the burden then shifts to the taxpayer resisting enforcement of the summons. This burden is a heavy one because the taxpayer should show that enforcement would “constitute an

48 *U.S. v. Powell*, 379 U.S. 48, 57-58 (1964).

49 In some instances, the taxpayer made the motion to quash in its answer to the government’s petition to enforce.

50 *Ngo v. U.S.*, 699 F. App’x 617 (9th Cir. 2017), *aff’g* 118 A.F.T.R.2d (RIA) 5453 (N.D. Cal. 2015). Under IRC § 7609(c)(2)(D)(i), the IRS is not required to provide notice to the taxpayer, and the taxpayer therefore has no right to quash the summons if the summons is issued to aid in the collection of the taxpayer’s liability.

51 *Rifle Remedies, LLC v. U.S.*, 120 A.F.T.R.2d 6385 (D. Colo. 2017).

52 See IRC § 280E (prohibiting a deduction or credit for carrying on any trade or business if such trade or business consists of trafficking in controlled substances (within the meaning of schedule I and II of the Controlled Substances Act)). For more information about IRS enforcement of IRC § 280E, see Leslie Book, *Court Allows IRS to Proceed With Summons Issued to Taxpayer in the Medical Marijuana Business*, Procedurally Taxing Blog, <http://procedurallytaxing.com/court-allows-irs-to-proceed-with-summons-issued-to-taxpayer-in-the-medical-marijuana-business/> (Apr. 20, 2017).

53 *Rifle Remedies, LLC v. U.S.*, 120 A.F.T.R.2d 6385 (D. Colo. 2017) (internal citations omitted).

abuse of the court's process, or that in issuing the summons the IRS lacked institutional good faith."<sup>54</sup> To meet this burden the taxpayer must factually oppose the IRS's allegations by affidavit and refute the government's *prima facie* Powell showing or factually support a proper affirmative defense. Thus, the court started its analysis with an evaluation of the taxpayer's position with respect to the Powell requirements.

First, with respect to the legitimate purpose Powell requirement, the court found that the IRS's summons was issued to verify the taxpayer's financial records and to determine whether information reported in the taxpayer's tax returns could be substantiated. The taxpayer raised several illegitimate purpose arguments rebutting the IRS's position, but the court rejected all of them. The taxpayer's primary argument was that the IRS was essentially conducting a criminal investigation, as the taxpayer was being investigated for trafficking in a controlled substance. The court rejected this argument (alongside the other illegitimate purpose arguments), noting that the primary purpose of the investigation was to determine whether the taxpayer was entitled to a deduction or credit, and the IRS's inquiry into whether IRC § 280E applies to the taxpayer is not a criminal prosecution.

In respect to the second Powell requirement, the taxpayer did not contest that the IRS agent's declaration sufficiently established that the information sought by the summons would be relevant to the purpose of the IRS's investigation.

With respect to the Powell requirement that the information sought by the IRS was not already in its possession, the taxpayer argued that the IRS possessed the information it sought to summon. The taxpayer believed that the IRS obtained '.xls files' which contained private taxpayer information. These files were allegedly large enough to contain all the requested information already. The court rejected this argument, concluding that the IRS did not possess the specific information that it has requested in the summons.

With respect to the last Powell requirement that the material sought by the IRS be relevant to its investigation and that the IRS follow all necessary administrative steps, the court found that the IRS satisfied its burden through its declaration. The taxpayer did not contest this. Accordingly, the court found that IRS satisfied its burden under Powell, and thus the burden shifted to the taxpayer. Construing the taxpayer's arguments challenging the purpose of the IRS' investigation as attempting to satisfy the taxpayer's burden of showing that enforcement of the summons will be an abuse of process or that the IRS lacked institutional good faith, the court rejected those arguments as insufficient. Those arguments were "based upon rank speculation, on a lack of facts, or a combination of both."<sup>55</sup> Accordingly, the Court denied the taxpayer's petition to quash summonses, and granted the IRS's motion to enforce summonses.

### Privileges

As in past years, taxpayers attempted to invoke various privileges, including Fifth Amendment and attorney-client privileges in response to an IRS summons. In one case, the taxpayers successfully invoked the attorney-client privilege for certain requested documents or testimony.<sup>56</sup> In another case,

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54 *Rifle Remedies, LLC v. U.S.*, 120 A.F.T.R.2d 6385 (D. Colo. 2017) (internal citations omitted).

55 *Id.*

56 *See U.S. v. Owensboro Dermatology Associates*, 120 A.F.T.R.2d (RIA) 5119 (W.D. Ky. 2017).

the United States Court of Appeals for the Ninth Circuit vacated and remanded rulings from a district court to review memos *in camera* for privilege concerns.<sup>57</sup>

In *United States v. Servin*, the taxpayer, an attorney, appealed a district court order enforcing two administrative summonses issued by the IRS on the basis of attorney-client privilege.<sup>58</sup> The IRS suspected that the taxpayer owed delinquent taxes and sought to verify the income the taxpayer generated from his law practice. To accomplish this, the IRS requested information concerning the taxpayer's client list, which encompassed the names and addresses of each client. The taxpayer responded to the summons, appearing, but did not disclose the requested information.

In appealing the district court's decision, the taxpayer argued that state attorney-client privilege laws and the duty of confidentiality (drawn from the state rules of professional conduct) prohibited the unconsented disclosure of a client's name and address. The Court of Appeals for the Third Circuit rejected this position on both grounds. First, the Court of Appeals held that federal law concerning attorney-client privilege preempted state law, and that on the federal level, the privilege only shielded against the disclosure of confidential information. Absent rare circumstances, the attorney-client privilege did not shield against disclosing clients' identities. Since the taxpayer did not present any unusual circumstances that would warrant a different approach, the court rejected the argument on privilege grounds. Second, the appellate court rejected the taxpayer's reliance on the state rules of professional conduct. The court reasoned that the duty of confidentiality is extensive under state law, but it is not substantive law because it governs only disciplinary proceedings against attorneys practicing in the state who violate the rules—it does not affect judicial application of the attorney-client privilege. Accordingly, since the taxpayer failed to provide a compelling argument, the Court of Appeals upheld the lower court's decision.

### Civil Contempt

A taxpayer who “neglects or refuses to obey” an IRS summons may be held in civil contempt.<sup>59</sup> In five cases this year, taxpayers were held in civil contempt for failing to comply with a court order enforcing an IRS summons.<sup>60</sup> However, in *United States v. Lui*, discussed earlier, the government's motion for contempt was denied.<sup>61</sup> In another case, *United States v. Ali*, the Court of Appeals for the Fourth Circuit affirmed a district court finding a taxpayer in contempt for failing to produce certain documents subject to an enforcement order.<sup>62</sup> The taxpayer had refused to produce the documents at the contempt stage on grounds of nonpossession and asserted Fifth Amendment privilege.<sup>63</sup> The court rejected the taxpayer's position on the ground that those defenses were to be raised at the enforcement stage, since allowing the taxpayer to rely on these defenses at the contempt stage would lead to a retrial of the original

57 See *U.S. v. Sanmina Co. and Subsidiaries*, 707 F. App'x 865 (9th Cir. 2017), *vacating and remanding* 115 A.F.T.R.2d (RIA) 1882 (N.D. Cal. 2015). We discussed the lower court's decision in our 2015 Annual Report. See National Taxpayer Advocate 2015 Annual Report to Congress 473-474.

58 *U.S. v. Servin*, 721 F. App'x 156 (3d. Cir. 2018), *aff'g* 121 A.F.T.R. 2d (RIA) 646 (E.D. Pa. 2017).

59 IRC § 7604(b).

60 See *U.S. v. Briseno*, 121 A.F.T.R.2d (RIA) 1540 (E.D. Cal. 2018); *U.S. v. Ali*, 874 F.3d 825 (4th Cir. 2017), *aff'g* 119 A.F.T.R.2d (RIA) 1145 (D. Md. 2016); *U.S. v. Barela*, 120 A.F.T.R.2d (RIA) 6494 (E.D. Cal. 2017); *U.S. v. Conner*, 120 A.F.T.R.2d (RIA) 6244 (N.D. Tex. 2017), *appeal docketed*, No. 17-11417 (5th Cir., Dec. 1, 2017), *adopting* 120 A.F.T.R.2d (RIA) 6241 (N.D. Tex. 2017); *U.S. v. Posner*, 120 A.F.T.R.2d (RIA) 5812 (S.D. Cal. 2017).

61 *U.S. v. Lui*, 121 A.F.T.R.2d (RIA) 1537 (N.D. Cal. 2018).

62 *U.S. v. Ali*, 874 F.3d 825 (4th Cir. 2017), *aff'g* 119 A.F.T.R.2d (RIA) 1145 (D. Md. 2016).

63 We discussed the *Ali* case in the privilege section of our 2015 Annual Report summons enforcement most litigated issue narrative. See National Taxpayer Advocate 2015 Report to Congress 473.

controversy. The court relied on the Supreme Court in *United States v. Rylander*<sup>64</sup> that if a taxpayer contests a summons, he or she must raise all applicable defenses at the enforcement stage, not for the first time in a contempt proceeding.<sup>65</sup>

The taxpayer's appeal of the district court's contempt order relied on three arguments. First, Ms. Ali contended that because she asserted her Fifth Amendment privilege against self-incrimination during the enforcement proceeding, she could not also assert a defense of nonpossession at that time. The Court of Appeals refused to allow the taxpayer to invoke the Fifth Amendment to satisfy her burden of production at the contempt stage even if she previously asserted that right at the enforcement stage based on *Rylander*. Then the court addressed the taxpayer's second and third arguments. Ms. Ali contended that once she produced some documents in response to an enforcement order, she could not be held in contempt unless the IRS could prove by clear and convincing evidence that she failed to produce all the responsive documents in her possession or control. She also argued that the district court erroneously switched the burden from the IRS to her by requiring her to affirmatively show that she had produced all responsive documents in her possession or control. The Court rejected these arguments. First of all, a summons enforcement order establishes a presumption that the defendant possesses responsive documents. Thus, the IRS did not need to show that the taxpayer had actual possession of other responsive documents that she failed to produce. Instead, the failure to produce documents presumptively within the taxpayer's possession constitutes an actual or constructive violation of the enforcement order. Therefore, it was enough for the IRS to show, by clear and convincing evidence, that the taxpayer's production was presumptively incomplete, *e.g.*, a production of bank records omitting bank statements is presumptively incomplete. The IRS is not required to identify each missing bank statement and need not prove that the taxpayer has access to that specific statement.

After the IRS establishes that the taxpayer violated the enforcement order, the burden shifts to the taxpayer to show that she made reasonable efforts to comply in good faith.

The Court of Appeals agreed with the district court's finding that the taxpayer had not satisfied this burden, concluding that a bare assertion of nonpossession or the production of some responsive documents do not demonstrate all reasonable efforts to comply with the summons enforcement order. Accordingly, the Court of Appeals for the Fourth Circuit found that the district court did not abuse its discretion in finding the taxpayer in contempt.

Overall, contempt proceedings accounted for approximately seven percent of all summons-related cases. Unless the taxpayer complied with the court order, the taxpayer was subject to arrest.<sup>66</sup>

### Virtual Currency and "John Doe" Summons

The IRS has taken the position that virtual currency, such as Bitcoin, is considered property for tax purposes and therefore general tax principles apply to transactions involving such currency.<sup>67</sup> In *United States v. Coinbase, Inc.*, the IRS served a John Doe summons on a virtual currency exchange seeking

64 460 U.S. 752 (1983).

65 The Supreme Court recognized "present inability to comply" as the only exception, *i.e.*, when an inability to comply arises after the enforcement proceeding and exists at the time of the contempt proceeding. 460 U.S. at 756-757.

66 *U.S. v. Briseno*, 121 A.F.T.R.2d (RIA) 1540 (E.D. Cal. 2018); *U.S. v. Barela*, 120 A.F.T.R.2d (RIA) 6494 (E.D. Cal. 2017); *U.S. v. Posner*, 120 A.F.T.R.2d (RIA) 5812 (S.D. Cal. 2017).

67 See IRS Notice 2014-21, 2014-16 I.R.B. 938; IRS Pub. 525, *Taxable and Nontaxable Income* 4 (Jan. 2017). In her 2013 Annual Report to Congress, the National Taxpayer Advocate recommended that the IRS issue guidance to assist users of digital currency. See National Taxpayer Advocate 2013 Annual Report to Congress 249-255 (Most Serious Problem: *DIGITAL CURRENCY: The IRS Should Issue Guidance to Assist Users of Digital Currency*).

records regarding nearly all of its customers for a two-year period.<sup>68</sup> After the exchange failed to comply with the summons, the IRS filed a petition to enforce the summons. The court heard oral argument on a motion to quash the summons and a motion to intervene, leading the IRS to narrow the scope of its summons.<sup>69</sup> Whereas the initial summons sought information from nearly all the exchange's users, the narrowed summons sought information regarding accounts "with at least the equivalent of \$20,000 in any one transaction type."<sup>70</sup> The currency exchange refused to comply with the narrowed summons, and subsequently, the court granted a motion by a "John Doe" to intervene and challenge the government's attempt to enforce the summons.<sup>71</sup>

### *The Right to Intervene*

An intervenor must satisfy a four-part test to qualify:

- (1) file a timely motion;
- (2) assert an interest relating to the property or transaction which is the subject of the summons enforcement action;
- (3) be so situated that without intervention the disposition of the action may impair or impede the intervenor's ability to protect that interest; and
- (4) have an interest not adequately represented by other parties.<sup>72</sup>

The party seeking to intervene bears the burden of showing the four elements are met, but the requirements are broadly interpreted in favor of intervention.<sup>73</sup> The IRS did not dispute that John Doe had timely applied to intervene. Thus, the Court turned to the remaining three factors. John Doe did not claim privilege in his Coinbase records, but contended that the broad scope of the summons suggests an abuse of process sufficient to support intervention as of right. The IRS did not explain how it can "legitimately use most of these millions of records on hundreds of thousands of users."<sup>74</sup> It claimed that as long as it submitted a declaration from an IRS agent that it is conducting an investigation to determine the identity and correct tax liabilities of taxpayers who had conducted transactions in virtual currencies, the summons does not involve an abuse of process. The Court refused to adopt the IRS argument stating that under this reasoning "the IRS could request bank records for every United States customer from every bank branch in the United States because it is well known that tax liabilities in general are under reported and such records might turn up tax liabilities."<sup>75</sup> The court noted that the IRS could not cite a single case to support such broad discretion. The IRS also argued that because the summons was issued pursuant to 15 U.S.C. § 7609(f), John Doe did not have a protectable interest, claiming that only the direct subject of the summons may challenge the government's good faith. The Court was unpersuaded commenting that nothing in the John Doe summons procedure adopted by Congress suggests that when the John Doe nonetheless learns of a summons from other means the John Doe has no interest in challenging the enforcement of that summons. The court also rejected the

68 *U.S. v. Coinbase, Inc.*, 120 A.F.T.R.2d (RIA) 5239 (N.D. Cal. 2017). For the related case, see also *U.S. v. Coinbase, Inc.*, 120 A.F.T.R.2d (RIA) 6671 (N.D. Cal. 2017). We discussed the Coinbase "John Doe" summons litigation in our 2017 Annual Report. See National Taxpayer Advocate 2017 Annual Report to Congress 400.

69 See *U.S. v. Coinbase, Inc.*, 120 A.F.T.R. 2d (RIA) 5239 (N.D. Cal. 2017).

70 *U.S. v. Coinbase, Inc.*, 120 A.F.T.R. 2d (RIA) 5239, 5241 (N.D. Cal. 2017).

71 See *U.S. v. Coinbase, Inc.*, 120 A.F.T.R. 2d (RIA) 5239 (N.D. Cal. 2017).

72 See *U.S. v. Oregon*, 839 F.2d 635, 637 (9th Cir. 1988).

73 See *Prete v. Bradbury*, 438 F.3d 949, 954 (9th Cir. 2006).

74 *U.S. v. Coinbase, Inc.*, 120 A.F.T.R. 2d (RIA) 5239, 5243 (N.D. Cal. 2017).

75 *Id.*

IRS's argument that John Doe's intervention would place an undue burden on the IRS's legitimate use of John Doe summons. Finally, the court disagreed with the IRS's assertion that John Doe was merely trying to shield his or her identity. The IRS had consented to its proceeding as a John Doe. John Doe had offered to reveal his or her identity provided the IRS would agree not to then withdraw the summons to moot John Doe's interest in the proceeding, but the IRS had rejected John Doe's offer. The Court determined that John Doe has a protectable interest in this enforcement proceeding. Moving to the next prong, the court concluded that if the IRS would obtain John Doe's personal information and other transaction history at Coinbase, it would impair the intervenor's ability to protect his or her protectable interest in the summons proceeding. Lastly, the court concluded that John Doe's interests were not adequately represented by other parties, distinguishing the intervenor's and Coinbase's interests. Coinbase's financial interest as an entity is that the IRS's investigation does not affect its profits or valuation. The intervenor's personal interest, however, is in the very documents the IRS seeks. As a result, Coinbase and John Doe may have differences as to a proper resolution of the summons enforcement action. For these reasons the court concluded that John Doe has a right to intervene.

### *The Narrowed Summons*

Following the oral argument on the intervention motions, the IRS narrowed the scope of its summons seeking information regarding accounts “with at least the equivalent of \$20,000 in any one transaction type (buy, sell, send, or receive) in any one year during the 2013-2015 period.”<sup>76</sup> According to Coinbase the summons would apply to 8.9 million transactions and 14,355 account holders. Coinbase refused to comply with the Narrowed Summons, opposing the summons enforcement by the IRS along with John Doe.<sup>77</sup> Three *amici* briefs in opposition were filed by the Competitive Enterprise Institute; the Coin Center; and the Digital Currency and Ledger Defense Fund. Because the parties did not dispute that the third and fourth *Powell* factors were satisfied, the court only addressed the first and second *Powell* factors: whether the summons serves a legitimate purpose, and whether it seeks relevant information. With respect to the legitimate purpose *Powell* requirement, the court noted that over a two-year period, the exchange had conducted over 6 billion in transactions and had at least 5.9 million customers. Despite this, in the same period, only 800 to 900 taxpayers a year have electronically filed returns with a property description related to bitcoin. This discrepancy led to the inference that more of the exchange's users are trading virtual currencies than reporting gains on their tax returns. Subsequently, the court found that the revised summons had the legitimate purpose of investigating the “reporting gap between the number of virtual currency users [the exchange] claims to have had during the summons period” and “U.S. bitcoin users reporting gains or losses to the IRS during the summoned years.”<sup>78</sup> Although the respondents raised a number of counterarguments, the court rejected them, emphasizing that the IRS's burden is minimal at this stage in the proceeding.

With respect to the relevance *Powell* requirement, the court agreed that while the requested records would permit the IRS to investigate unreported taxable gains, the IRS's demand for information was too broad. In addition to transaction records and information concerning account holder identity, the IRS sought “account opening records, copies of passports or driver's licenses, all wallet addresses, all public keys for all accounts/wallets/vaults, records of Know-Your-Customer diligence, agreements or instructions granting a third-party access, control, or transaction approval authority, and correspondence between Coinbase and the account holder.”<sup>79</sup> The court found that at this stage in the proceeding, these

76 *U.S. v. Coinbase, Inc.*, 120 A.F.T.R. 2d (RIA) 5239, 5241 (N.D. Cal. 2017).

77 120 A.F.T.R.2d (RIA) 6671 (N.D. Cal. 2017).

78 120 A.F.T.R.2d (RIA) 6671, 6674 (N.D. Cal. 2017).

79 120 A.F.T.R.2d (RIA) 6671, 6676 (N.D. Cal. 2017).

requests sought information that was broader than necessary. The court reasoned that the first question the IRS had to resolve was whether an account holder had a taxable gain. If the account holder did not, then correspondence between the exchange and the account holder was irrelevant. Consequently, the court narrowed the type of documents that the IRS may acquire to documents material to identifying the account holder and any unreported gains. For instance, while the court permitted enforcement of records concerning the taxpayer's ID number, name, date of birth, address, and transaction history, the court found that documents concerning Records of Know-Your-Customer diligence, agreements or instructions granting a third-party access, control, or transaction approval authority, and correspondence between Coinbase and the account holder as unnecessary. Accordingly, the outcome resulted in a split decision, with court granting the IRS's petition to enforce in part.<sup>80</sup>

## CONCLUSION

The IRS may issue a summons to obtain information to determine whether a tax return is correct or if a return should have been filed to ascertain a taxpayer's tax liability or to collect a liability.<sup>81</sup> Accordingly, the IRS may request documents and testimony from taxpayers who have failed to provide that information voluntarily.

Summons enforcement continues to be a significant source of litigation and the number of litigated cases rose slightly from last year. The IRS also continues to be successful in the vast majority of summons enforcement litigation. Taxpayers and third parties rarely succeed in contesting IRS summonses due to the significant burden of proof and strict procedural requirements.

The increase in virtual transactions and gig economy seem to attract legitimate IRS attention,<sup>82</sup> but may also lead to overreaching by the government in its summons' demands for information. We anticipate more summons enforcement activity in this area with IRS seeking information from third-party platforms.

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80 120 A.F.T.R.2d (RIA) 6671 (N.D. Cal. 2017).

81 IRC § 7602(a).

82 See National Taxpayer Advocate 2017 Annual Report to Congress 165-171 (Most Serious Problem: *Participants in the Sharing Economy Lack Adequate Guidance From the IRS*).

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## Gross Income Under IRC § 61 and Related Sections

## SUMMARY

When preparing tax returns, taxpayers must complete the crucial calculation of gross income for the taxable year to determine the tax they must pay. Gross income has been among the Most Litigated Issues in each of the National Taxpayer Advocate's Annual Reports to Congress.<sup>1</sup> For this report, we reviewed 79 cases decided between June 1, 2017, and May 31, 2018. The majority of cases involved taxpayers failing to report items of income, including some specifically mentioned in Internal Revenue Code (IRC) § 61 such as wages,<sup>2</sup> interest,<sup>3</sup> dividends,<sup>4</sup> and pensions.<sup>5</sup>

TAXPAYER RIGHTS IMPACTED<sup>6</sup>

- *The Right to Be Informed*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to a Fair and Just Tax System*

## PRESENT LAW

IRC § 61 broadly defines gross income as “all income from whatever source derived.”<sup>7</sup> The U.S. Supreme Court has defined gross income as any accession to wealth.<sup>8</sup> The concept of “gross income” is to be broadly construed, while exclusions from income are to be narrowly construed.<sup>9</sup> However, over time, Congress has carved out numerous exceptions and exclusions from this broad definition of gross income, and has based other elements of tax law on the definition.<sup>10</sup>

The Commissioner may identify particular items of unreported income or reconstruct a taxpayer's gross income using methods such as the bank deposits method.<sup>11</sup> If the Commissioner determines a tax

1 See, e.g., National Taxpayer Advocate 2017 Annual Report to Congress 420-427; National Taxpayer Advocate 2013 Annual Report to Congress 355-361.

2 Internal Revenue Code (IRC) § 61(a)(1). See, e.g., *Fleming v. Comm'r*, T.C. Memo. 2017-120.

3 IRC § 61(a)(4). See, e.g., *Avrahami v. Comm'r*, 149 T.C. No. 7 (2017).

4 IRC § 61(a)(7). See, e.g., *Povolny Group, Inc.*, T.C. Memo. 2018-37.

5 IRC § 61(a)(9). See, e.g., *Azam v. Comm'r*, T.C. Memo. 2018-72.

6 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the IRC. See IRC § 7803(a)(3).

7 IRC § 61(a).

8 *Comm'r v. Glenshaw Glass*, 348 U.S. 426, 431 (1955) (interpreting § 22 of the Internal Revenue Code of 1939, the predecessor to IRC § 61).

9 See *Comm'r v. Schleier*, 515 U.S. 323, 327-328 (citations omitted) (1995); *Taggi v. U.S.*, 35 F.3d 93, 95 (citations omitted) (2d Cir. 1994).

10 See, e.g., IRC §§ 104 (compensation for injuries or sickness); 105 (amounts received under accident and health plans); 108 (income from discharge of indebtedness); 6501 (limits on assessment and collection, determination of “substantial omission” from gross income).

11 IRC § 6001. See, e.g., *DiLeo v. Comm'r*, 96 T.C. 858, 867 (1991).

deficiency, the IRS issues a Statutory Notice of Deficiency.<sup>12</sup> If the taxpayer challenges the deficiency, the Commissioner's notice is entitled to a presumption of correctness; the taxpayer bears the burden of proving that the determination is erroneous or inaccurate.<sup>13</sup>

## ANALYSIS OF LITIGATED CASES

In the 79 opinions involving gross income issued by the federal courts and reviewed for this report, gross income issues most often fell into two categories: (1) what is included in gross income under IRC § 61, and (2) what can be excluded under other statutory provisions. A detailed list of the cases appears in Table 4 of Appendix 3.

In 37 cases (about 47 percent), taxpayers were represented, while the rest were *pro se* (without counsel). Nine of the 37 cases where taxpayers had representation (about 24 percent) prevailed in full or in part in their cases, whereas *pro se* taxpayers prevailed in full or in part in seven cases (about 17 percent). Overall, taxpayers prevailed in full or in part in 16 of 79 cases (about 20 percent).

Drawing on the full list in Table 4 of Appendix 3, we have chosen to discuss cases involving damage awards, income treatment under U.S. tax treaties, and a case of first impression involving the treatment of an excess state tax credit.

### Damage Awards

Taxation of damage awards continues to generate litigation. This year, taxpayers in at least seven cases (about eight percent of those reviewed) challenged the inclusion of damage awards in their gross income, but no taxpayers prevailed in these cases.<sup>14</sup>

IRC § 104(a)(2) specifies that damage awards and settlement proceeds<sup>15</sup> are taxable as gross income unless the award was received “on account of personal physical injuries or physical sickness.”<sup>16</sup> Congress added the “physical injuries or physical sickness” requirement in 1996;<sup>17</sup> until then, the word “physical” did not appear in the statute. The legislative history of the 1996 amendments to IRC § 104(a)(2) provides that “[i]f an action has its origin in a physical injury or physical sickness, then all damages (other than punitive damages) that flow therefrom are treated as payments received on account of physical injury or physical sickness...[but] emotional distress is not considered a physical injury or physical sickness.”<sup>18</sup> Thus, damage awards for emotional distress are not considered as received on account of physical injury or physical sickness, even if the emotional distress results in “insomnia, headaches, [or] stomach disorders.”<sup>19</sup>

12 IRC § 6212. See also Internal Revenue Manual (IRM) 4.8.9.2, *Notice of Deficiency Definition* (Aug. 11, 2016).

13 See IRC § 7491(a) (burden shifts only where the taxpayer produces credible evidence contradicting the Commissioner's determination and satisfies other requirements). See also *Welch v. Helvering*, 290 U.S. 111, 115 (1933) (citations omitted).

14 See, e.g., *Bell v. U.S.*, 290 F. Supp. 3d 166 (D. Conn. 2017).

15 See Treas. Reg. § 1.104-1(c) (damages, for purposes of IRC § 104(a)(2), means amounts received (other than workers' compensation) “through prosecution of a legal suit or action, or through a settlement agreement entered into in lieu of prosecution”).

16 IRC § 104(a)(2).

17 Pub. L. No. 104-188, § 1605(a), 110 Stat. 1755, 1838 (1996).

18 H.R. REP. NO. 104-586, at 143-44 (1996) (Conf. Rep.).

19 H.R. REP. NO. 104-737, at 301 (1996) (Conf. Rep.). Note, however, that IRC § 104(a)(2) excludes from income damages, up to the cost of medical treatment for which a deduction under IRC § 213 was allowed for any prior taxable year, for mental or emotional distress causing physical injury.

To justify exclusion from income under IRC § 104, the taxpayer must show settlement proceeds are in lieu of damages for physical injury or sickness.<sup>20</sup> In *Bell v. U.S.*, the taxpayers (husband and wife) sought a refund of taxes withheld from a settlement payment received by Dr. Bell.<sup>21</sup> The taxpayers attempted to assert that the settlement was payment for a physical injury and thus should be exempt from taxation. The court first looked to the payor's intention to determine the nature of the settlement payment. In this case, the supplemental agreement signed by Dr. Bell and his employer specified release with regard to any claim arising from his employment and termination of employment, not tort-type rights. Second, the court considered whether the damages sought were for physical injuries or physical sickness under IRC § 104(a)(2).<sup>22</sup> While Dr. Bell argued that he intended to bring claims related to the intentional infliction of emotional distress and the negligent infliction of emotional distress, which are both torts under Connecticut state law, and thus the release also covered these, giving rise to tort-type claims, the court disagreed. Further, the court found that even if Dr. Bell had released these tort-type claims, damages for emotional distress are not physical injuries or sickness under IRC § 104(a)(2). Thus, the court held that the payment from the settlement contract is considered wages, and therefore the taxpayers were not entitled to a refund of taxes withheld from the settlement proceeds.<sup>23</sup>

As illustrated by continuing litigation of the characterization of settlement damages, the question of when damage awards can be excluded from gross income continues to confuse taxpayers. The National Taxpayer Advocate notes that taxpayers continue to disagree with the IRS's and courts' interpretation that mental illness equates to emotional distress, as opposed to physical sickness or injury.<sup>24</sup> In the same way that a physical injury or sickness may have mental or emotional side effects, many mental illnesses manifest themselves as physical symptoms. For instance, many people who have severe depression experience the following physical symptoms: stomachaches, indigestion, constant headaches, tightness in the chest, difficulty breathing, and fatigue.<sup>25</sup> Physical symptoms occur in other mental disorders, such as Post-Traumatic Stress Disorder (PTSD), which affects people who have experienced a traumatic event, such as mugging, rape, torture, being kidnapped or held captive, child abuse, car accidents, train wrecks, plane crashes, bombings, natural or human-caused disasters, or military combat.<sup>26</sup> Current research shows the experience of trauma can cause neurochemical changes in the brain that create a vulnerability to hypertension and atherosclerotic heart disease, abnormalities in thyroid and other hormone functions, and increased susceptibility to infections and immunologic disorders that are associated with PTSD.<sup>27</sup> The interpretation that mental illness equates to emotional distress seems particularly outdated when

20 See, e.g., *Green v. Comm'r*, 507 F.3d 857 (5th Cir. 2007), *aff'g* T.C. Memo. 2005-250.

21 290 F. Supp. 3d 166 (D. Conn. 2017).

22 See also *Abrahamsen v. U.S.*, 228 F.3d 1360, 1363 (Fed. Cir. 2000).

23 "Whether a specific settlement agreement falls into one of the exceptions for taxable wages under [the Federal Insurance Contributions Act] calls for the same standard as whether a settlement agreement is excluded from gross income." *Bell*, 290 F. Supp. 3d at 170 (citation omitted).

24 See, e.g., *Collins v. Comm'r*, T.C. Summ. Op. 2017-74; *Devine v. Comm'r*, T.C. Memo. 2017-111.

25 National Institute of Mental Health, *Signs and Symptoms of Depression*, <https://www.nimh.nih.gov/health/topics/depression/index.shtml> (last visited Aug. 30, 2018).

26 National Institute of Mental Health, *Post-Traumatic Stress Disorder*, <http://www.nimh.nih.gov/health/topics/post-traumatic-stress-disorder-ptsd/index.shtml> (last visited Aug. 30, 2018).

27 See U.S. Department of Veterans Affairs, *National Center for PTSD*, <http://www.ptsd.va.gov/professional/co-occurring/ptsd-physical-health.asp> (last visited Aug. 30, 2018).

considering the medical advancements in understanding the physical cause and symptoms of mental illness.<sup>28</sup>

### Income Under Tax Treaties

Taxpayers in at least six cases argued that various items of income were excludable under a variety of tax accords, conventions or treaties.<sup>29</sup> Only one taxpayer prevailed in part in this series of cases.<sup>30</sup> Each case required the courts to interpret the terms of the treaty, convention or accord in relation to the item of income the taxpayer was attempting to exclude.

In *Guo v. Commissioner*, the Tax Court considered, in a matter of first impression, the taxpayer's contention that his unemployment compensation is exempt from income tax under the Convention with Respect to Taxes on Income and Capital between Canada and the United States.<sup>31</sup> In this case, the taxpayer was a Canadian citizen who worked in the U.S. as a post-doctoral fellow. When her employment concluded, she returned to Canada and applied to the state of Ohio for unemployment compensation.

The taxpayer received unemployment compensation from Ohio during 2012 and Ohio issued her a 1099-G, *Certain Government Payments*, reflecting no federal income tax withheld. She timely filed her 1040NR-EZ, *U.S. Income Tax Return for certain Nonresident Aliens with No Dependents*, and took the position that her unemployment compensation was excludable under the treaty. The Commissioner and the taxpayer agreed that she received the unemployment compensation, that it was an item of gross income, and it was "effectively connected" to the conduct of the taxpayer in relation to a U.S. trade or business.<sup>32</sup> However, the Commissioner and the taxpayer disagreed over the exclusion of the income under the treaty.

The court looked first to the written language of the treaty and noted that neither the treaty nor its protocols specify how unemployment compensation should be treated. The taxpayer argued that under article XV of the treaty, unemployment compensation falls into the category of "salaries, wages, and other similar remuneration."<sup>33</sup> The court found that unemployment compensation is neither salary nor wages, and remuneration is not defined in the treaty. It next turned to the IRC for a definition of remuneration, where it is also not defined; however, the court found the location of the term within the IRC and its context to provide guidance and found it closely associated with wages paid for services.<sup>34</sup> Thus, the court found that unemployment compensation is not remuneration as it is not wages or

28 National Taxpayer Advocate 2009 Annual Report to Congress 351-56 (Legislative Recommendation: *Exclude Settlement Payments for Mental Anguish, Emotional Distress, and Pain and Suffering from Gross Income*). The National Taxpayer Advocate recommended that Congress amend IRC §104(a)(2) to exclude from gross income payments received as settlement for mental anguish, emotional distress, and pain and suffering. Such change was recommended because mental anguish, emotional distress, and pain and suffering can be caused by a physical condition in the body and can cause physical symptoms. Over the past few years, doctors and researchers have made significant advances in identifying changes that occur in the brain when a person is plagued with mental illness.

29 See, e.g., *Ye v. Comm'r*, T.C. Memo. 2017-216.

30 See *Kiselev v. Comm'r*, T.C. Summ. Op. 2018-2.

31 *Guo v. Comm'r*, 149 T.C. No. 14 (2017), *appeal dismissed*, 2018 WL 3216499 (D.C. Cir., May 11, 2018).

32 *Id.*

33 *Id.*

34 Two places in the IRC that mention remuneration are IRC § 3401 (definitions for withholding income tax from wages) and IRC § 3121 (definitions for withholding federal insurance contributions act taxes from wages).

benefits paid by an employer to an employee but “other income” under article XXII of the treaty,<sup>35</sup> which is not excludable from U.S. taxation.

### Refundable State Tax Credits

The Court of Federal Claims decided a case of first impression regarding the characterization and taxability of targeted New York State tax credits.<sup>36</sup> New York State offers state income tax credits to businesses or individuals who meet the requirements of the tax credit program. The purpose of the program is to rehabilitate targeted areas of New York. The program applies a percentage of the cost of the project against a corporation’s franchise tax or an individual’s income tax liability and any amount in excess of that owed can be deferred to another tax year or credited as an overpayment. New York does not tax any part of the credit. In *Ginsburg v. Commissioner*, the taxpayers (a husband and wife) received an excess credit of nearly \$2 million from New York State, which they did not include as income on their tax return.<sup>37</sup> The IRS conducted an audit and asserted a tax deficiency. Mr. and Mrs. Ginsburg then paid the deficiency and brought a refund suit. They argued that the excess credit was not income, as it was a classic recovery of capital. Alternatively, they argued the excess credit is excludable from gross income as a nontaxable contribution to capital. The Commissioner asserted the excess credit is a cash subsidy and not excludable from gross income.<sup>38</sup> Both parties moved for summary judgment.

Similar to the case of *Maines v. Commissioner*, which we discussed in a previous report, the court in *Ginsburg* found that while New York treated the credit as a nontaxable refund, federal law ultimately controls how state-created interests are taxed under the federal income tax.<sup>39</sup>

The court found that the excess credit was nothing more than a cash transfer to the taxpayers, and on its face was income, unless an exclusion from income could be applied. The court next considered the theories of capital recovery and nontaxable contribution to capital advanced by the taxpayers. The court determined that the recovery of capital doctrine is limited to the sale of goods, which is not applicable in the instant matter.<sup>40</sup> The court also rejected the taxpayers’ contention that the excess credit was a contribution to capital by New York State and thus not taxable. The court noted that the transfer was not made for an interest in the taxpayers’ partnership and the taxpayers freely chose to participate in the program. As a result, the excess credit was income to the taxpayers and did not qualify for any exception or exclusion from gross income.<sup>41</sup>

35 Article XXII of the treaty was captioned “Other Income” and served as a catchall provision to cover items of income not dealt with elsewhere in the treaty. It expressly provided that the U.S. could tax items of income arising in the U.S.

36 *Ginsburg v. U.S.*, 136 Fed. Cl. 1 (2018), *appeal docketed*, No. 18-1788 (Fed. Cir., Mar. 30, 2018).

37 136 Fed. Cl. 1 (2018), *appeal docketed*, No. 18-1788 (Fed. Cir., Mar. 30, 2018).

38 *Ginsburg v. Comm’r*, 136 Fed. Cl. 1 (2018), *appeal docketed*, No. 18-1788 (Fed. Cir., Mar. 30, 2018).

39 *Maines v. Comm’r*, 144 T.C. 123 (2015). See National Taxpayer Advocate 2015 Annual Report to Congress 479-80.

40 As the District Court for the Eastern District of New York explained in the case of *In re Tax Refund Litigation*, 766 F. Supp. 1248 (E.D.N.Y. 1991), “There can be no return of capital until, as in the case of a manufacturer or merchandiser, that asset is sold or exchanged by the lessor.” In *Ginsburg v. Commissioner*, the taxpayer retained all ownership of the property in question, therefore, there could be no return of capital since the taxpayer had not divested of the asset for which he claimed to be recovering capital.

41 *Ginsburg v. Commissioner*, 136 Fed. Cl. 1 (2018), *appeal docketed*, No. 18-1788 (Fed. Cir., Mar. 30, 2018).

## CONCLUSION

Taxpayers litigate many of the same gross income issues every year due to the complex nature of what constitutes gross income. As the definition is very broad and the courts broadly interpret accession to wealth as gross income, most cases were decided in favor of the IRS and exclusions from gross income continued to be narrowly interpreted.

Overall, litigation of items of gross income decreased this year, from 85 cases in the 2017 reporting cycle to 79 cases this year.<sup>42</sup> The number of cases involving the tax treatment of settlements and awards held steady in this reporting cycle at seven; thus, it clearly remains a perennial area of confusion for taxpayers. The National Taxpayer Advocate has previously recommended a legislative change that would clarify the tax treatment of court awards and settlements by permitting taxpayers to exclude any payments received as a settlement or judgment for mental anguish, emotional distress, or pain and suffering.<sup>43</sup>

One new area appeared in the issues reviewed this year and presented the Tax Court with an issue of first impression involving the treatment of income under various tax treaties. Previous reporting cycles did not identify cases in this area.<sup>44</sup> Taxpayers litigated this issue with only minor success this year, prevailing in part in only one case.

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42 National Taxpayer Advocate 2017 Annual Report to Congress 420-427.

43 National Taxpayer Advocate Annual 2009 Report to Congress 351-356 (Legislative Recommendation: *Exclude Settlement Payments for Mental Anguish, Emotional Distress, and Pain and Suffering from Gross Income*).

44 See, e.g., National Taxpayer Advocate 2017 Annual Report to Congress 544-546 (Appendix 3).

MLI  
#5**Appeals From Collection Due Process (CDP) Hearings Under IRC §§ 6320 and 6330****SUMMARY**

The IRS Restructuring and Reform Act of 1998 (RRA 98)<sup>1</sup> created Collection Due Process (CDP) hearings to provide taxpayers with an independent review by the IRS Office of Appeals (Appeals) of the decision to file a Notice of Federal Tax Lien (NFTL) or the IRS's proposal to undertake a levy action. In other words, a CDP hearing is an opportunity for a taxpayer to have a meaningful hearing prior to the IRS's first levy or immediately after its first NFTL filing to enforce a tax liability. At the hearing, the taxpayer has the right to raise any relevant issues related to the unpaid tax, the lien, or the proposed levy, including the appropriateness of the collection action, collection alternatives, spousal defenses, and, under certain circumstances, the underlying tax liability.<sup>2</sup>

Once Appeals issues a determination, a taxpayer has the right to judicial review of the determination if the taxpayer timely requests a CDP hearing and timely petitions the United States Tax Court.<sup>3</sup> Generally, the IRS suspends levy actions during a levy hearing and any judicial review that may follow.<sup>4</sup>

Only a small fraction of taxpayers exercise their right to an administrative hearing, and far fewer taxpayers petition the Tax Court to review their case. Between 2004 and 2018, only 1.43 percent of the taxpayers who received a CDP notice requested an administrative hearing (*i.e.*, 390,041 out of 27,264,457) and only 0.08 percent filed a petition in Tax Court (*i.e.*, 22,012 out of 27,264,457).

Yet CDP has been one of the federal tax issues most frequently litigated in the federal courts since 2001. Our review of litigated issues found 74 opinions on CDP cases during the review period of June 1, 2017, through May 31, 2018, which is a decrease of about 13 percent since last year's report.<sup>5</sup> Taxpayers prevailed in full in five of these cases (about seven percent) and, in part, in four others (over five percent). The 12 percent success rate for the taxpayers is higher than last year. Of the nine opinions where taxpayers prevailed in whole or in part, four taxpayers appeared without a representative authorized to advocate to the court on their behalf (*pro se*),<sup>6</sup> and five were represented by an attorney or other court-approved professional.

The cases discussed below demonstrate that CDP hearings serve a vital role by providing a venue for taxpayers to raise legitimate issues before the IRS deprives the taxpayer of property. Many of these decisions shed light on substantive and procedural issues.

- 1 IRS Restructuring and Reform Act of 1998 (RRA 98), Pub. L. No. 105-206, § 3401, 112 Stat. 685, 746 (1998).
- 2 Internal Revenue Code (IRC) §§ 6320(c) (lien) and 6330(c)(2) (levy). IRC § 6320(c) generally requires Appeals to follow the levy hearing procedures under IRC § 6330 for the conduct of the lien hearing, the review requirements, and the balancing test.
- 3 IRC § 6330(d) (setting forth the time requirements for obtaining judicial review of Appeals' determination); IRC §§ 6320(a)(3)(B) and 6330(a)(3)(B) (setting forth the time requirements for requesting a Collection Due Process (CDP) hearing for lien and levy matters, respectively).
- 4 IRC § 6330(e)(1) provides that generally, levy actions are suspended during the CDP process (along with a corresponding suspension in the running of the limitations period for collecting the tax). However, IRC § 6330(e)(2) allows the IRS to resume levy actions upon a determination by the Tax Court of "good cause," if the underlying tax liability is not at issue.
- 5 For a list of all cases reviewed, see Table 5 in Appendix 3, *infra*.
- 6 *Pro se* means "[f]or oneself; on one's own behalf; without a lawyer." *Pro Se*, BLACK'S LAW DICTIONARY (10th ed. 2014).

CDP hearings provide taxpayers with a way to exercise several rights articulated in the Taxpayer Bill of Rights, which was adopted by the IRS in 2014 and was subsequently incorporated in the Internal Revenue Code (IRC) in response to the National Taxpayer Advocate's recommendations.<sup>7</sup> For example, by providing an opportunity for a taxpayer to challenge the underlying liability and raise alternatives to the collection action, the CDP hearing empowers the taxpayer *to challenge the IRS's position and be heard*. If the taxpayer disagrees with Appeals' determination, he or she may file a petition in Tax Court, an exercise of the taxpayer's *right to appeal an IRS decision in an independent forum*. Lastly, since the Appeals Officer (AO) must consider whether the IRS's proposed collection action balances the overall need for efficient collection of taxes with the legitimate concern that the IRS's collection actions are no more intrusive than necessary, the CDP hearing protects a taxpayer's *right to privacy* while also ensuring the taxpayer's *right to a fair and just tax system*.

### TAXPAYER RIGHTS IMPACTED<sup>8</sup>

- *The Right to Be Informed*
- *The Right to Quality Service*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to Privacy*
- *The Right to a Fair and Just Tax System*

### PRESENT LAW

Current law provides taxpayers an opportunity for independent review of an NFTL filed by the IRS or of a proposed levy action.<sup>9</sup> As discussed above, CDP rights ensure taxpayers receive adequate notice of IRS collection activity and an opportunity for a meaningful hearing before the IRS deprives the taxpayer of property.<sup>10</sup> The hearing allows taxpayers to raise issues related to collection of the liability, including:

- The appropriateness of collection actions;<sup>11</sup>
- Collection alternatives such as an installment agreement (IA), offer in compromise (OIC), posting a bond, or substitution of other assets;<sup>12</sup>
- Appropriate spousal defenses;<sup>13</sup>

7 See Taxpayer Bill of Rights (TBOR), <http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights>, IRC § 7803(a)(3).

8 See TBOR, <http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights>. The rights contained in the TBOR are also codified in the IRC. See IRC § 7803(a)(3).

9 IRC §§ 6320 and 6330.

10 Prior to RRA 98, the U.S. Supreme Court had held that a post-deprivation hearing was sufficient to satisfy due process concerns in the tax collection arena. See *U.S. v. Nat'l Bank of Commerce*, 472 U.S. 713, 726-731 (1985); *Phillips v. Comm'r*, 283 U.S. 589, 595-601 (1931).

11 IRC § 6330(c)(2)(A)(ii).

12 IRC § 6330(c)(2)(A)(iii).

13 IRC § 6330(c)(2)(A)(i).

- The existence or amount of the underlying tax liability, but only if the taxpayer did not receive a statutory notice of deficiency or have another opportunity to dispute the liability;<sup>14</sup> and
- Any other relevant issue relating to the unpaid tax, the NFTL, or the proposed levy.<sup>15</sup>

A taxpayer cannot raise an issue considered at a prior administrative or judicial hearing if the taxpayer participated meaningfully in that hearing or proceeding.<sup>16</sup>

## PROCEDURAL COLLECTION DUE PROCESS REQUIREMENTS

The IRS must provide a CDP notice to the taxpayer indicating the particular tax and tax period after filing the first NFTL and generally before its first intended levy is issued.<sup>17</sup> The IRS must provide the notice not more than five business days after the day of filing the NFTL, or at least 30 days before the day of the proposed levy.<sup>18</sup>

If the IRS files a lien, the CDP lien notice must inform the taxpayer of the right to request a CDP hearing within a 30-day period, which begins on the day after the end of the five business day period after the filing of the NFTL.<sup>19</sup> In the case of a proposed levy, the CDP levy notice must inform the taxpayer of the right to request a hearing within the 30-day period beginning on the day after the date of the CDP notice.<sup>20</sup>

## REQUESTING A CDP HEARING

Under both lien and levy procedures, the taxpayer must return a signed and dated written request for a CDP hearing within the applicable period.<sup>21</sup> The Code and regulations require taxpayers to provide their reasons for requesting a hearing.<sup>22</sup> Failure to provide the basis may result in denial of a face-to-face hearing.<sup>23</sup> Taxpayers who fail to timely request a CDP hearing will be afforded an “equivalent hearing,”

14 IRC § 6330(c)(2)(B).

15 IRC § 6330(c)(2)(A); Treas. Reg. §§ 301.6320-1(e) and 301.6330-1(e).

16 IRC § 6330(c)(4).

17 IRC § 6330(f) permits the IRS to levy without first giving a taxpayer a CDP notice in the following situations: the collection of tax is in jeopardy, a levy was served on a state to collect a state tax refund, the levy is a disqualified employment tax levy, or the levy was served on a federal contractor. A disqualified employment tax levy is any levy to collect employment taxes for any taxable period if the person subject to the levy (or any predecessor thereof) requested a CDP hearing with respect to unpaid employment taxes arising in the most recent two-year period before the beginning of the taxable period with respect to which the levy is served. IRC § 6330(h)(1). A federal contractor levy is any levy if the person whose property is subject to the levy (or any predecessor thereof) is a federal contractor. IRC § 6330(h)(2). Under IRC § 6330(f), the IRS must still provide the opportunity for a CDP hearing “within a reasonable period of time after the levy.”

18 IRC §§ 6320(a)(2) or 6330(a)(2). The CDP notice can be provided to the taxpayer in person, left at the taxpayer’s dwelling or usual place of business, or sent by certified or registered mail (return receipt requested, for the CDP levy notice) to the taxpayer’s last known address.

19 IRC § 6320(a)(3)(B); Treas. Reg. § 301.6320-1(b)(1).

20 IRC § 6330(a)(3)(B); Treas. Reg. § 301.6330-1(b)(1).

21 IRC §§ 6320(a)(3)(B) and 6330(a)(3)(B); Treas. Reg. §§ 301.6320-1(c)(2), Question and Answer (Q&A) (C1)(ii) and 301.6330-1(c)(2), Q&A (C1)(ii).

22 Treas. Reg. §§ 301.6320-1(c)(2), Q&A (C1)(ii) and 301.6330-1(c)(2), Q&A (C1)(ii).

23 IRC §§ 6320(b)(1) and 6330(b)(1); Treas. Reg. §§ 301.6320-1(c)(2), Q&A (C1); 301.6330-1(c)(2), Q&A (C1); 301.6320-1(d)(2), Q&A (D8); and 301.6330-1(d)(2), Q&A (D8). The regulations require the IRS to provide the taxpayer an opportunity to “cure” any defect in a timely filed hearing request, including providing a reason for the hearing. Form 12153 includes space for the taxpayer to identify collection alternatives that he or she wants Appeals to consider, as well as examples of common reasons for requesting a hearing. See IRS Form 12153, *Requests for Collection Due Process or Equivalent Hearing* (Dec. 2013); Internal Revenue Manual (IRM) 8.6.1.4.1, *Conference Practice* (Oct. 1, 2016).

which is similar to a CDP hearing but lacks judicial review.<sup>24</sup> Taxpayers must request an equivalent hearing within the one-year period beginning the day after the five-business-day period following the filing of the NFTL, or in levy cases, within the one-year period beginning the day after the date of the CDP notice.<sup>25</sup>

The IRS generally is required to suspend the levy action throughout a CDP hearing involving a notice of intent to levy. However, the requirement to suspend a levy action is inapplicable in certain circumstances where the IRS is not required to provide a CDP hearing prior to the levy and is only required to provide the CDP hearing within a reasonable time after the levy.<sup>26</sup> These circumstances occur when the IRS determines that:

- The collection of tax is in jeopardy;
- The collection resulted from a levy on a state tax refund;
- The IRS has served a disqualified employment tax levy; or
- The IRS has served a federal contractor levy.<sup>27</sup>

The IRS also is required to suspend levy action throughout any judicial review of Appeals' determination, unless the IRS obtains an order from the court permitting levy action because the underlying tax liability is not at issue, and the IRS can demonstrate good cause to resume collection activity.<sup>28</sup>

## HOW A CDP HEARING IS CONDUCTED

CDP hearings are informal. When a taxpayer requests a hearing with respect to both a lien and a proposed levy, Appeals will attempt to conduct one hearing.<sup>29</sup> A taxpayer can request that the hearing be in person; however, courts have ruled that a CDP hearing need not be face-to-face but can take place by telephone or correspondence,<sup>30</sup> and Appeals will typically conduct the hearing by telephone

24 Treas. Reg. §§ 301.6320-1(i)(2), Q&A (I6) and 301.6330-1(i)(2), Q&A (I6); *Business Integration Servs., Inc. v. Comm'r*, T.C. Memo. 2012-342 at 6-7; *Moorhouse v. Comm'r*, 116 T.C. 263 (2001). A taxpayer can request an Equivalent Hearing by checking a box on Form 12153, *Requests for Collection Due Process or Equivalent Hearing*, by making a written request, or by confirming that he or she wants the untimely CDP hearing request to be treated as an Equivalent Hearing when notified by Collection of an untimely CDP hearing request. IRM 5.19.8.4.3, *Equivalent Hearing (EH) Requests and Timeliness of EH Requests* (Nov. 1, 2007).

25 Treas. Reg. §§ 301.6320-1(i)(2), Q&A (I7) and 301.6330-1(i)(2), Q&A (I7).

26 See, e.g., *Dorn v. Comm'r*, 119 T.C. 356 (2002); *Zapara v. Comm'r*, 124 T.C. 223 (2005); *Bibby v. Comm'r*, T.C. Memo. 2013-281.

27 IRC § 6330(e)(1) provides the general rule for suspending collection activity. IRC § 6330(f) provides that if collection of the tax is deemed in jeopardy, the collection resulted from a levy on a state tax refund, or the IRS served a disqualified employment tax levy or a federal contractor levy, IRC § 6330 does not apply, except to provide the opportunity for a CDP hearing within a reasonable time after the levy. See *Clark v. Comm'r*, 125 T.C. 108, 110 (2005) (citing *Dorn v. Comm'r*, 119 T.C. 356 (2002)).

28 IRC § 6330(e)(1) and (e)(2).

29 IRC § 6320(b)(4).

30 *Katz v. Comm'r*, 115 T.C. 329, 337-38 (2000) (finding that telephone conversations between the taxpayer and the Appeals Officer (AO) constituted a hearing as provided in IRC § 6320(b)). Treas. Reg. §§ 301.6320-1(d)(2), Q&A (D)(6), Q&A (D)(8) and 301.6330-1(d)(2), Q&A (D)(6), Q&A (D)(8).

unless the taxpayer requests a face-to-face conference.<sup>31</sup> The CDP regulations state that taxpayers who provide non-frivolous reasons for opposing the IRS collection action will generally be offered but not guaranteed face-to-face conferences.<sup>32</sup> Taxpayers making frivolous arguments are not entitled to face-to-face conferences.<sup>33</sup> A taxpayer will not be granted a face-to-face conference concerning a collection alternative, such as an IA or OIC, unless other taxpayers would be eligible for the alternative under similar circumstances.<sup>34</sup> For example, the IRS will not grant a face-to-face conference to a taxpayer who proposes an OIC as the only issue to be addressed but failed to file all required returns and is therefore ineligible for an offer. Appeals may, however, at its discretion, grant a face-to-face conference to explain the eligibility requirements for a collection alternative.<sup>35</sup>

The CDP hearing is to be held by an impartial officer from Appeals, who is barred from engaging in *ex parte*<sup>36</sup> communications with IRS employees about the substance of the case and who has had “no prior involvement.”<sup>37</sup> In addition to addressing the issues raised by the taxpayer, the AO must verify that the IRS has met the requirements of all applicable laws and administrative procedures.<sup>38</sup> An integral component of the CDP analysis is the balancing test, which requires the IRS AO to determine whether the proposed collection action balances the need for efficient collection of taxes with the legitimate concern of the taxpayer that any collection action be “no more intrusive than necessary.”<sup>39</sup> The balancing test is central to a CDP hearing because it instills a notion of fairness into the process from the perspective of the taxpayer.<sup>40</sup>

31 Under the recently adopted IRM 8.6.1.4.1, *Conference Practice* (Oct. 1, 2016), the default rule became telephone conferences, with in-person conferences only being available in cases meeting certain criteria and where the Appeals Team Manager approved. Appeals recently announced that it would issue guidance to employees “informing them that Appeals will return to allowing taxpayers to have in-person Appeals conferences in field cases.” However, the policy change is limited to field offices, which leaves the low income taxpayer and much of the middle class without access to in-person conferences.

32 Treas. Reg. §§ 301.6320-1(d)(2), Q&A (D)(7) and 301.6330-1(d)(2), Q&A (D)(7).

33 Treas. Reg. §§ 301.6320-1(d)(2), Q&A (D)(8) and 301.6330-1(d)(2), Q&A (D)(8).

34 *Id.*

35 *Id.*

36 *Ex parte* means “done or made at the instance and for the benefit of one party only, and without notice to, or argument by, anyone having an adverse interest.” *Ex parte*, BLACK’S LAW DICTIONARY (10th ed. 2014).

37 IRC §§ 6320(b)(1), 6320(b)(3), 6330(b)(1), and 6330(b)(3). See also Rev. Proc. 2012-18, 2012-1 C.B. 455. See, e.g., *Industrial Investors v. Comm’r*, T.C. Memo. 2007-93; *Moore v. Comm’r*, T.C. Memo. 2006-171, *action on dec.*, 2007-2 (Feb. 27, 2007); *Cox v. Comm’r*, 514 F.3d 1119, 1124-28 (10th Cir. 2008), *action on dec.*, 2009-1 (June 1, 2009), 2009-22 I.R.B.1.

38 IRC § 6330(c)(1); *Hoyle v. Comm’r*, 131 T.C. 197 (2008); *Talbot v. Comm’r*, T.C. Memo. 2016-191 (2016).

39 IRC § 6330(c)(3)(C); IRM 8.22.4.2.2, *Summary of CDP Process* (Sept. 25, 2014). See also H.R. REP. No. 105-599, at 263 (1998). For simplicity, we use the term “proposed collection action” referring to both the actions taken and proposed. IRC § 6330 requires the IRS to notify the taxpayer of the right to request a CDP hearing not less than 30 days before issuing the first levy to collect a tax. Pursuant to IRC § 6320, the taxpayer is notified of the right to request a CDP hearing within five business days after the first Notice of Federal Tax Lien (NFTL) for a tax period that is filed. Thus, Treasury Regulations under IRC § 6320 require a Hearing Officer to consider “[w]hether the continued existence of the filed [NFTL] represents a balance between the need for the efficient collection of taxes and the legitimate concern of the taxpayer that any collection action be no more intrusive than necessary.” See Treas. Reg. § 301.6320-1(e)(3), Q&A (E)(1)(vi). Similarly, a levy action can be taken before a hearing in the following situations: collection of the tax was in jeopardy; levy on a state to collect a federal tax liability from a state tax refund; disqualified employment tax levies; or a federal contractor levy. See IRC § 6330(f); IRM 8.22.4.2.2, *Summary of CDP Process* (Sept. 25, 2014).

40 See National Taxpayer Advocate 2014 Annual Report to Congress 185-196 (Most Serious Problem: *Collection Due Process: The IRS Needs Specific Procedures for Performing the Collection Due Process Balancing Test to Enhance Taxpayer Protections*). See also Nina E. Olson, *Taking the Bull by Its Horns: Some Thoughts on Constitutional Due Process in Tax Collection*, 2010 Erwin N. Griswold Lecture Before the American College of Tax Counsel, 63 TAX LAW. 227 (2010).

Special rules apply to the IRS's handling of hearing requests that raise frivolous issues. IRC § 6330(g) provides that the IRS may disregard any portion of a hearing request based on a position the IRS has identified as frivolous or that reflects a desire to delay or impede the administration of tax laws.<sup>41</sup> Similarly, IRC § 6330(c)(4)(B) provides that a taxpayer cannot raise an issue if it is based on a position identified as frivolous or reflects a desire to delay or impede tax administration.

IRC § 6702(b) allows the IRS to impose a penalty for a specified frivolous submission, including a frivolous CDP hearing request.<sup>42</sup> A request is subject to a penalty if any part of it “(i) is based on a position which the Secretary has identified as frivolous ... or (ii) reflects a desire to delay or impede the administration of Federal tax laws.”<sup>43</sup> A taxpayer can timely petition the Tax Court to review an Appeals decision if Appeals determined that a request for an administrative hearing was based entirely on a frivolous position under IRC § 6702(b)(2)(A) and issued a notice stating that Appeals will disregard the request.<sup>44</sup> An Appeals letter disregarding a CDP hearing request is a determination that confers jurisdiction under IRC § 6330(d)(1), because it authorizes the IRS to proceed with the disputed collection action.<sup>45</sup> The IRS Office of Chief Counsel disagreed with the Tax Court precedent in *Thornberry* and is maintaining the position that the Tax Court lacks jurisdiction to review a petition resulting from the denial of a frivolous hearing request under IRC § 6330(g).<sup>46</sup>

In *Ryskamp v. Commissioner*, the D.C. Circuit upheld the Tax Court's precedent in *Thornberry* that the IRS's disregard of a taxpayer's CDP hearing request as frivolous under IRC § 6330(g) is subject to judicial review, and affirmed the Tax Court's holding that the IRS abused its discretion in rejecting a taxpayer's request for a hearing by sending boilerplate rejection letters that do not articulate the grounds of the frivolousness determination.<sup>47</sup> While the IRS Office of Chief Counsel disagrees with *Ryskamp* on both issues, Counsel has modified its litigating guidelines as follows:

- Counsel will no longer contest the Tax Court's threshold jurisdiction to evaluate whether a CDP hearing was properly denied under IRC § 6330(g);
- Counsel will request a remand to Appeals where a hearing was improperly denied;
- Where a hearing was properly denied, instead of filing a motion to remand so Appeals can more fully explain the reasons for rejecting the taxpayer's arguments as frivolous, Counsel will file an appropriate motion with the Court to resolve the case through a dismissal or summary judgment; and

41 IRC § 6330(g). IRC § 6330(g) is effective for submissions made and issues raised after the date on which the IRS first prescribed a list of frivolous positions. Notice 2007-30, 2007-1 C.B. 833, which was published on or about April 2, 2007, provided the first published list of frivolous positions. Notice 2010-33, 2010-17 C.B. 609, contains the current list.

42 The frivolous submission penalty applies to the following submissions: CDP hearing requests under IRC §§ 6320 and 6330, offer in compromise (OIC) under IRC § 7122, installment agreements (IAs) under IRC § 6159, and applications for a Taxpayer Assistance Order under IRC § 7811.

43 IRC § 6702(b)(2)(A). Before asserting the penalty, the IRS must notify the taxpayer that it has determined that the taxpayer filed a frivolous hearing request. The taxpayer has 30 days to withdraw the submission to avoid the penalty. IRC § 6702(b)(3).

44 See *Thornberry v. Comm'r*, 136 T.C. 356, 367 (2011). The D.C. Appeals Court upheld *Thornberry* in *Ryskamp v. Comm'r*, 797 F.3d 1142 (D.C. Cir. 2015) cert. denied, 136 S. Ct. 834 (2016). See also National Taxpayer Advocate 2015 Annual Report to Congress 489 (Most Litigated Issue: Appeals from Collection Due Process Hearings Under IRC §§ 6320 and 6330).

45 *Thornberry v. Comm'r*, 136 T.C. 356, 364 (2011).

46 See IRS Chief Counsel Notice CC-2016-008, *Disregarding Frivolous CDP Hearing Requests Under Section 6330(g)* (Apr. 4, 2016).

47 *Ryskamp v. Comm'r*, 797 F.3d 1142 (D.C. Cir. 2015), cert. denied, 136 S. Ct. 834 (2016).

- Counsel will also consider filing a motion to permit levy so that the Service can immediately levy after the Tax Court's order.<sup>48</sup>

## JUDICIAL REVIEW OF AN IRS DETERMINATION AFTER A CDP HEARING

Within 30 days of Appeals' determination, the taxpayer may petition the Tax Court for judicial review.<sup>49</sup> In several recent court cases,<sup>50</sup> taxpayers filed their petitions one day late because they miscalculated the time period for filing their Tax Court petitions. The Tax Court found it lacked jurisdiction to review the IRS's determination, and several courts of appeal affirmed.<sup>51</sup> The court will only consider issues, including challenges to the underlying liability, that were properly raised during the CDP hearing.<sup>52</sup> An issue is not properly raised if the taxpayer fails to request that Appeals consider the issue, or if the taxpayer fails to present any evidence regarding consideration of that issue after being given a reasonable opportunity.<sup>53</sup> The Tax Court, however, may remand a case back to Appeals for more fact finding when the taxpayer's factual circumstances have materially changed between the hearing date and the trial.<sup>54</sup> When the case is remanded to Appeals, the Tax Court retains jurisdiction.<sup>55</sup> The resulting hearing on remand provides the parties with an opportunity to complete the initial hearing while preserving the taxpayer's right to return to Court and receive judicial review of the ultimate administrative determination.<sup>56</sup>

The standard of review the court will apply depends on the nature of the issue it is reviewing. Where the validity of the underlying tax liability is properly at issue in the hearing, the court will review the amount of the tax liability on a *de novo*<sup>57</sup> basis, and the scope of its review extends to evidence

48 IRS Chief Counsel Notice CC-2016-008, *Disregarding Frivolous CDP Hearing Requests Under Section 6330(g)* (Apr. 4, 2016). In the 2014 Annual Report to Congress, the National Taxpayer Advocate expressed concerns about the Office of Appeals not giving proper attention to the CDP balancing test, especially to legitimate concerns of taxpayers regarding the intrusiveness of the proposed collection action, and often using *pro forma* statements that the balancing test has been conducted. See National Taxpayer Advocate 2014 Annual Report to Congress 185-196 (Most Serious Problem: *Collection Due Process: The IRS Needs Specific Procedures for Performing the Collection Due Process Balancing Test to Enhance Taxpayer Protections*).

49 IRC § 6330(d)(1).

50 See, e.g., *Duggan v. Comm'r*, Order of Dismissal for Lack of Jurisdiction, Tax Ct. No. 4100-15L (2015) (dismissing for lack of jurisdiction where petition was filed "31 days after the mailing of the notices of determination."); *Pottgen v. Comm'r*, Order of Dismissal for Lack of Jurisdiction, Tax Ct. No. 1410-15L (2016) (dismissing for lack of jurisdiction where petition was received by Tax Court one day late); *Integrated Event Management, Inc. v. Comm'r*, Order of Dismissal for Lack of Jurisdiction, Tax Ct. No. 27674-16SL (2017) (dismissing for lack of jurisdiction where petition was filed one day late, disagreeing with taxpayer's calculation putting the day of the letter as day zero rather than as day one); *Protter v. Comm'r*, Order of Dismissal for Lack of Jurisdiction, Tax Ct. No. 22975-15SL (2017) (dismissing for lack of jurisdiction where petition was mailed 31 days after the date on the notice of determination, disagreeing with Taxpayer's construction of the operative language effectively putting the day of the letter as day zero).

51 See, e.g., *Cunningham v. Comm'r*, 716 F. App'x 182 (4th Cir. 2018), *aff'g* No. 16-014090 (T.C. Dec. 7, 2016); *Duggan v. Comm'r*, 879 F.3d 1029 (9th Cir. 2018), *aff'g* No. 15-4100 (T.C. June 26, 2015).

52 *Giamelli v. Comm'r*, 129 T.C. 107 (2007).

53 Treas. Reg. §§ 301.6320-1(f)(2), Q&A (F)(3); 301.6330-1(f)(2), Q&A (F)(3).

54 *Churchill v. Comm'r*, T.C. Memo. 2011-182; see also IRS Chief Counsel Notice CC-2013-002, *Remands to Appeals in CDP Cases When There Is a Post-Determination Change in Circumstances* (Nov. 30, 2012), which provides Counsel attorneys with instructions on when a remand based on changed circumstances might be appropriate; *but see Kehoe v. Comm'r*, T.C. Memo. 2013-63 (taxpayer's eligibility to make withdrawals from his IRA without the threat of penalty does not amount to a material change in circumstances such that remand would be appropriate).

55 See, e.g., *Pomeroy v. Comm'r*, T.C. Memo. 2013-26 at 20; Bob Kamman, *For IRS Appeals Office, An Epidemic of Remands*, PROCEDURALLY TAXING (Oct. 9, 2018), <http://procedurallytaxing.com/for-irs-appeals-office-an-epidemic-of-remands/>.

56 *Wadleigh v. Comm'r*, 134 T.C. 280, 299 (2010).

57 *De novo* means "anew." *De Novo*, BLACK'S LAW DICTIONARY (10th ed. 2014).

introduced at the trial that was not a part of the administrative record.<sup>58</sup> Where the Tax Court is reviewing the appropriateness of the collection action or subsidiary factual and legal findings, the Court will review these determinations under an abuse of discretion standard.<sup>59</sup>

### Court Review of Facts Outside the Administrative Record

When the review is for abuse of discretion, it is the position of the Tax Court that the scope of its review extends beyond the administrative record to include evidence adduced at trial, although in nonliability CDP cases appealable to the U.S. Courts of Appeals for the First, Eighth, and Ninth Circuits, the scope of review is limited to the administrative record.<sup>60</sup> However, in cases appealable to the other U.S. Courts of Appeals, which have yet to address that precise issue in a precedential opinion, the court may consider new evidence not contained in the administrative record.<sup>61</sup>

### Opportunity to Contest an Underlying Liability

The regulations distinguish between liabilities that are subject to deficiency procedures and those that are not. For liabilities subject to deficiency procedures, an opportunity for a post-examination conference with the IRS Office of Appeals does not bar the taxpayer (in appropriate circumstances) from contesting his or her liability in a later CDP proceeding.<sup>62</sup> On the other hand, where a liability is not subject to deficiency procedures, “[a]n opportunity to dispute the underlying liability includes a prior opportunity for a conference with Appeals that was offered either before or after the assessment of the liability.”<sup>63</sup> For example, an IRC § 6707A penalty<sup>64</sup> is an assessable penalty not subject to deficiency procedures.

In March 2017, in *Bitter v. Commissioner*,<sup>65</sup> the Tax Court further reiterated that a taxpayer is entitled to challenge his underlying liability for a § 6707A penalty only if the taxpayer did not have a prior opportunity to dispute it. A “prior opportunity” was found to include a prior opportunity for a conference with Appeals. The *Bitter* determination was a culmination of similar developments in circuit court decisions on the same issue, including the Fourth Circuit decision *James v. Commissioner*,<sup>66</sup> the Tenth Circuit decision in *Keller Tank Serv. II v. Commissioner*,<sup>67</sup> and the Seventh Circuit decision in *Our Country Home Enterprises, Inc. v. Commissioner*.<sup>68</sup>

58 The legislative history of RRA 98 addresses the standard of review courts should apply in reviewing Appeals’ CDP determinations. H.R. REP. NO. 105-599, at 266. See also IRS Chief Counsel Notice CC-2014-002, *Proper Standard of Review for Collection Due Process Determinations* (May 5, 2014).

59 See, e.g., *Murphy v. Comm’r*, 469 F.3d 27 (1st Cir. 2006); *Dalton v. Comm’r*, 682 F.3d 149 (1st Cir. 2012).

60 See *Keller v. Comm’r*, 568 F.3d 710, 718 (9th Cir. 2009), *aff’g* in part as to this issue T.C. Memo. 2006-166; *Murphy v. Comm’r*, 469 F.3d 27; *Robinette v. Comm’r*, 439 F.3d 455 (8th Cir. 2006), *rev’g* 123 T.C. 85 (2004).

61 See IRC § 7482(b)(1)(G)(i), *Rozday v. Comm’r*, 703 F. App’x. 138, 139 (3d Cir. 2017); *Tuka v. Comm’r*, 324 F. App’x 193, 195 n.2 (3d Cir. 2009); *Emery Celli Cuti Brinckerhoff & Abady, P.C. v. Comm’r*, T.C. Memo. 2018-55; and *Robinette v. Comm’r*, 123 T.C. at 103.

62 See Treas. Reg. §§ 301.6320-1(e)(3), Q&A-E2 and 301.6330-1(e)(3), Q&A-E2. Cf. IRC § 6330(c)(2)(B) (receiving the statutory notice of deficiency precludes the taxpayer from contesting the underlying liability).

63 See Treas. Reg. §§ 301.6320-1(e)(3), Q&A-E2 and 301.6330-1(e)(3), Q&A-E2.

64 IRC § 6707A provides a monetary penalty for the failure to include a reportable transaction required to be disclosed under IRC § 6011.

65 *Bitter v. Comm’r*, T.C. Memo. 2017-46.

66 See *James v. Comm’r*, 850 F.3d 160 (4th Cir. 2017).

67 See *Keller Tank Serv. II, Inc. v. Comm’r*, 854 F.3d 1178 (10th Cir. 2017).

68 See *Our Country Home Enterprises, Inc. v. Comm’r*, 855 F.3d 773 (7th Cir. 2017).

## APPELLATE VENUE FROM DECISIONS OF THE TAX COURT

IRC § 7482(b)(1)(G) specifies that CDP cases are appealable to the circuit of the taxpayer's legal residence (if the taxpayer is an individual) or the taxpayer's principal place of business, office, or agency (if the taxpayer is not an individual). This provision applies only to cases filed after December 18, 2015, but it should not be construed to create any inference regarding cases filed before that date.<sup>69</sup>

For cases filed before December 18, 2015, the correct venue for appeals from the Tax Court generally was the D.C. Circuit Court unless one of the rules specified in IRC § 7482(b)(1) or exceptions specified in IRC § 7482(b)(2) or (b)(3) applied. For instance, IRC § 7482(b)(1)(A) provides that in cases where a taxpayer other than a corporation seeks redetermination of a tax liability, venue for review by the United States Court of Appeals lies with the Court of Appeals for the circuit based upon the taxpayer's legal residence.<sup>70</sup> Pursuant to IRC § 7482(b)(2), the taxpayer and the IRS may stipulate the venue for an appeal in writing. In *Byers v. Commissioner*, the D.C. Circuit held that it would not transfer cases in non-liability CDP cases unless both parties stipulate to the transfer.<sup>71</sup> However, the Court acknowledged that in some CDP cases involving both challenges to the tax liability and collection issues, the venue presumably would be in the appropriate regional circuit.<sup>72</sup>

It has been the longstanding practice of taxpayers and the IRS to appeal CDP, innocent spouse, and interest abatement cases to the circuit of the taxpayer's legal residence, principal place of business, or principal office or agency. The Tax Court has also followed this approach. Under the rule established in *Golsen v. Commissioner*,<sup>73</sup> the Tax Court follows the precedent of the circuit court to which the parties have the right to appeal regardless of whether the taxpayer's tax liability was at issue. In 2014, to address the uncertainty and confusion among taxpayers and practitioners caused by the *Byers* decision, the National Taxpayer Advocate recommended that Congress amend IRC § 7482 to provide that the proper

69 Pub. L. No. 114-113, Div. Q, Title IV, § 423(a), (b) (2015). See also IRS Chief Counsel Notice CC-2016-006, *Path [Protecting Americans from Tax Hikes] Act Legislative Amendments: Appellate Venue for CDP and Innocent Spouse Cases, Tax Court Jurisdiction and S-Case Status for Interest Abatement Cases, and Applicability of Federal Rules of Evidence the Tax Court* (Feb. 1, 2016). For cases filed before that date, the guidance in IRS Chief Counsel Notice CC-2015-006, *Venue for Appeals from Decisions of the Tax Court* (June 30, 2015) applies.

70 IRC § 7482(b)(1) also provides that the proper venue lies with the Court of Appeals for the circuit in which the taxpayer is located: in the case of a corporation seeking redetermination of tax liability, the principal place of business or principal office or agency of the corporation, or if it has no principal place of business or principal office or agency in any judicial circuit, then the office to which was made the return of the tax in respect of which the liability arises; in the case of a person seeking a declaratory decision under IRC § 7476, the principal place of business or principal office or agency of the employer; in the case of an organization seeking a declaratory decision under IRC § 7428, the principal office or agency of the organization; in the case of a petition under IRC §§ 6226, 6228(a), 6247, or 6252 (for partnership taxable years beginning on or before Dec. 31, 2017), or in the case of a petition under IRC § 6234 (for partnership taxable years beginning after Dec. 31, 2017), the principal place of business of the partnership; in the case of a taxpayer under section IRC § 6234(c) (for partnership taxable years beginning on or before Dec. 31, 2017), (i) the legal residence of the taxpayer if the taxpayer is not a corporation, and (ii) the place or office applicable under subparagraph (B) if the taxpayer is a corporation; in the case of a petition under IRC § 6015(e) (for partnership taxable years beginning after Dec. 31, 2017), the legal residence of the taxpayer; or in the case of a petition under IRC §§ 6320 or 6330 (for partnership taxable years beginning after Dec. 31, 2017), (i) the legal residence of the taxpayer if the taxpayer is an individual, and (ii) the principal place of business or principal office or agency if the taxpayer is an entity other than an individual.

71 740 F.3d 668 (D.C. Cir. 2014). For a more detailed discussion of the *Byers* case see National Taxpayer Advocate 2014 Annual Report to Congress 477-494 (Most Litigated Issue: *Appeals from Collection Due Process Hearings Under IRC §§ 6320 and 6330*).

72 740 F.3d at 676. The Court noted that it had "no occasion to decide ... whether a taxpayer who is seeking review of a CDP decision on a collection method may file in a court of appeals other than the D.C. Circuit if the parties have not stipulated to venue in another circuit." *Id.* at 677.

73 54 T.C. 742 (1970), *aff'd*, 445 F.2d 985 (10th Cir. 1971).

venue to seek review of a Tax Court decision in all collection due process cases lies with the federal court of appeals for the circuit in which the taxpayer resides.<sup>74</sup> Congress made this precise legislative change in 2015.<sup>75</sup>

## ANALYSIS OF PUBLISHED OPINIONS

We identified and reviewed 74 CDP court opinions, a decrease of about 13 percent from the 85 published opinions in last year's report. From 2003 to 2010, the average number of published opinions was approximately 185. Since 2011, the average number of published opinions has dropped by about half, to 90. We analyzed potential factors that could have affected CDP litigation. First, we looked at the number of CDP notices the IRS issued to taxpayers, either in relation to an NFTL or a levy. The number of CDP notices increased from 2003, peaking in 2012 at just over 2,778,000, and then began to decrease. By 2018, the number of notices had decreased by 47 percent from 2012. Second, we determined the number of CDP hearing requests has generally followed the same trend.<sup>76</sup> In 2011, the number of CDP hearing requests peaked at 36,755, up from 10,889 requests in 2003. However, between 2011 and 2018, the number of hearing requests has declined by 34 percent. Finally, the number of Tax Court petitions also grew from 2003 to 2012, peaking at 1,963, and then started falling in 2012. From 2012 to 2018, petitions dropped by about ten percent. These trends are depicted in Figure 3.5.1, Collection Due Process (CDP) Notices, Hearing Requests, Petitions, and Litigation.

74 National Taxpayer Advocate 2014 Annual Report to Congress 387-391 (Legislative Recommendation: *Appellate Venue in Non-Liability CDP Cases: Amend IRC § 7482 to Provide That the Proper Venue to Seek Review of a Tax Court Decision in All Collection Due Process Cases Lies with the Federal Court of Appeals for the Circuit in Which the Taxpayer Resides*).

75 See Protecting Americans from Tax Hikes (PATH) Act of 2015, Pub. L. No. 114-113, Div. Q, Title IV, § 423(b).

76 IRC §§ 6320 and 6330 provide a taxpayer the right to a hearing if a request is made within a 30-day period.

FIGURE 3.5.1

Collection Due Process (CDP) Notices, Hearing Requests, Petitions, and Litigation

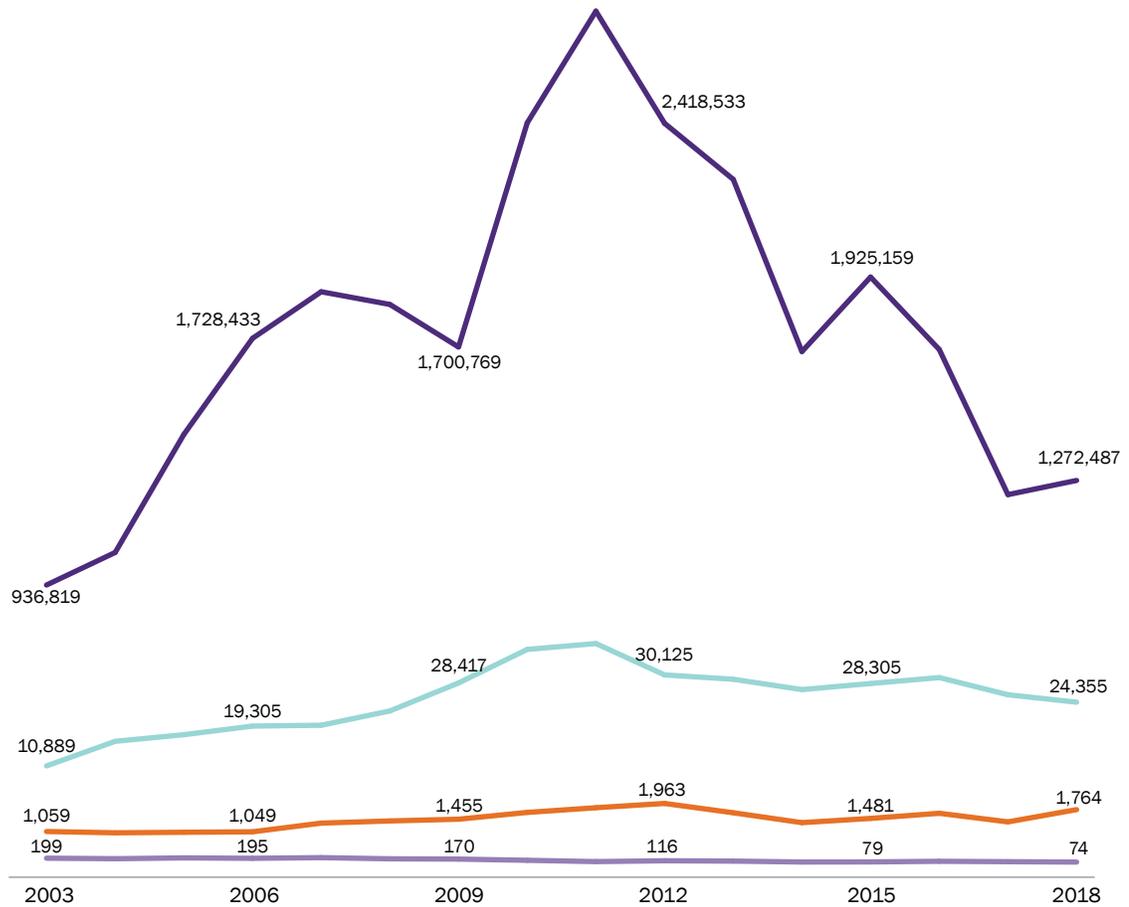
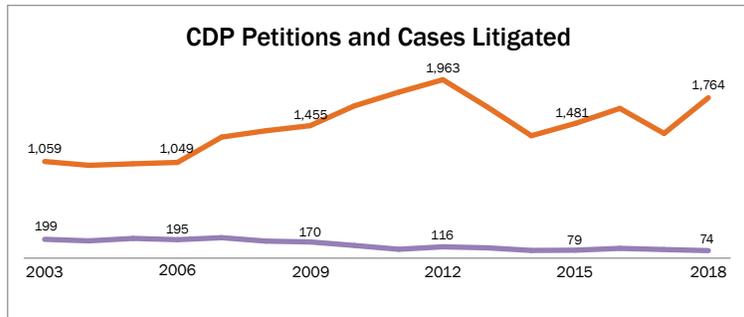


Chart is not to exact scale

- CDP Notices Mailed
- CDP Hearing Requests
- CDP Petitions
- CDP Cases Litigated



The decline in notices, hearing requests, and petitions may be attributed, in part, to a series of operational changes in fiscal years (FYs) 2011 and 2012 that led to fewer NFTL filings during the past few years and a higher number of accepted OICs than in 2011 and 2012.<sup>77</sup> These factors likely had a positive impact on many taxpayers and revenue collection. Fewer NFTL filings directly impacts the number of CDP notices issued to taxpayers, which in turn influence the number of CDP hearing requests and subsequent petitions to review IRS CDP determinations in Tax Court.

We acknowledge that there may be some additional reasons for the general decline in the number of litigated CDP cases. The IRS has experienced significant budget and staff reductions since 2010, which likely had an impact on enforced collection action. Any decline in litigated cases in the years after 2010 may also be due to taxpayers litigating many issues of first impression in the years immediately following the enactment of IRC §§ 6320 and 6330, which have been resolved by the courts.

The 74 opinions identified this year do not reflect the full number of CDP cases because the court does not issue an opinion in all cases.<sup>78</sup> Some are resolved through settlements, and in other cases, taxpayers do not pursue litigation after filing a petition with the court.<sup>79</sup> The Tax Court also disposes of some cases by issuing unpublished orders.<sup>80</sup> Table 5 in Appendix 3 provides a detailed list of the published CDP opinions, including specific information about the issues, the types of taxpayers involved, and the outcomes of the cases.

## LITIGATION SUCCESS RATE

Taxpayers prevailed in full in five of the 74 opinions issued during the year ending May 31, 2018 (about seven percent). Taxpayers prevailed in part in four other cases (over five percent). Of the nine published opinions in which the courts found for the taxpayer, in whole or in part, the taxpayers appeared *pro se* in four cases and were represented in five cases. Cognizant of the distinct disadvantage that *pro se* litigants face, federal courts routinely read their submissions liberally and interpret them to raise the strongest arguments that they suggest.<sup>81</sup> The IRS prevailed fully in 65 cases (about 88 percent) of the published

77 For instance, in fiscal year (FY) 2017, the IRS filed about 57 percent fewer NFTLs than in FY 2011, including a corresponding 62 percent reduction in liens filed by the Automated Collection System (ACS). In FY 2011, the IRS filed 1,042,230 liens. See IRS, Collection Activity Report 5000-23 (Oct. 11, 2011). In FY 2017, the IRS filed 446,378 liens. See IRS, Collection Activity Report 5000-25 (Oct. 4, 2017). We also note that the IRS has accepted 29 percent more OICs than during FY 2011, and that the actual number of accepted offers has almost doubled when compared to FY 2010, with FY 2017 having an acceptance rate of 38.1 percent. See IRS, Collection Activity Report 5000-108 (Oct. 5, 2010); IRS, Collection Activity Report 5000-108 (Oct. 5, 2011); IRS, Collection Activity Report 5000-108 (Oct. 2, 2017).

78 See U.S. Tax Court, Orders Search, <https://www.ustaxcourt.gov/InternetOrders/OrdersSearch.aspx>.

79 Prior to Oct. 17, 2006, the taxpayer could also petition the federal district court if the Tax Court did not have jurisdiction over the underlying tax liability (e.g., if the matter involved an employment tax liability).

80 The statistics analyzing the number of litigated cases excludes Tax Court summary judgments and bench orders, which are unpublished, however Appendix 3, Tables 11 and 12 of the Most Litigated Issues section lists the summary judgments and bench orders. Each division or memorandum opinion goes through a legislatively mandated pre-issuance review by the Chief Judge. IRC §§ 7459(b); 7460(a). While division opinions are precedential, orders are not, being issued “in the exercise of discretion” by a single judge. See 7463(b); Rule 50(f), Tax Court Rules of Practice and Procedure (denying precedential status to orders) and 152(c) (denying precedential status to bench opinions). See also *Introduction: Most Litigated Issues*, *supra*.

81 See *Haines v. Kerner*, 404 U.S. 519, 520 (1972); *Burgos v. Hopkins*, 14 F.3d 787, 790 (2d Cir. 1994); *Buczek v. U.S.*, No. 15-CV-273S, 2018 U.S. Dist. LEXIS 77471, at \*3 (W.D.N.Y. May 8, 2018).

opinions, a decrease from the 92 percent success rate last year.<sup>82</sup> The 12 percent success rate<sup>83</sup> among taxpayers is higher than last year.

## Issues Litigated

### *Cunningham v. Commissioner*

In *Cunningham v. Commissioner*,<sup>84</sup> the taxpayer sought Court of Appeals review of the Tax Court’s dismissal of her petition for review of an IRS CDP determination. The Tax Court concluded that it lacked the necessary jurisdiction to review Ms. Cunningham’s petition, which she filed one day after the 30-day deadline set forth in IRC § 6330(d)(1).

The IRS issued Cunningham a final notice of intent to levy in October 2015 for unpaid income tax she allegedly owed from 2010, 2011, 2013, and 2014.<sup>85</sup> After receiving the notice, Cunningham exercised her right to a CDP hearing before the IRS Office of Appeals.<sup>86</sup> Following the hearing, the IRS sent Cunningham a letter dated May 16, 2016, advising her of its decision. The letter explained the IRS’s determination that the levy notice was properly issued and that the proposed levy was appropriate and no more intrusive than necessary.<sup>87</sup> It also advised Cunningham that if she wished to dispute the determination, she “must file a petition with the United States Tax Court within a 30-day period beginning the day after the date of this letter.” Finally, it cautioned that “[t]he law limits the time for filing your petition to the 30-day period mentioned above. The courts cannot consider your case if you file late.”

On June 16, 2016—31 days after the date of the determination letter—Cunningham mailed a petition to the Tax Court seeking to challenge the IRS’s decision. The IRS moved to dismiss for lack of jurisdiction, and the Tax Court granted the motion since she filed it after the statutory deadline.<sup>88</sup> Cunningham appealed.

In her appeal, Cunningham claimed the letter was misleading and tricked her and other taxpayers into filing late as equitable grounds for why the filing deadline should have been tolled.

The Court of Appeals applied reasoning from a recent Supreme Court decision analyzing a statutorily prescribed deadline for appealing the determination of a government agency to consider whether the 30-day deadline to file a petition with the Tax Court for review of a CDP determination was jurisdictional, distinguishing jurisdictional time limits from claim processing rules.<sup>89</sup> There is a

82 National Taxpayer Advocate 2015 Annual Report to Congress 489 (Most Litigated Issue: *Appeals from Collection Due Process Hearings Under IRC § 6320 and 6330*).

83 The success rate includes decisions for the taxpayer as well as split decisions.

84 *Cunningham v. Comm’r*, 716 F. App’x 182 (4th Cir. 2018), *aff’g* No. 16-014090 (T.C. Dec. 7, 2016).

85 IRC § 6330(a).

86 IRC § 6330(a), (b).

87 IRC § 6330(a), (b), and (c)(3).

88 IRC § 6330(d)(1).

89 716 F. App’x at 183-184. While acknowledging that noncompliance with a jurisdictional time limit can never be excused, the Court of Appeals noted that “mandatory claim-processing rules” are “less stern,” and “may be waived or forfeited.” See *Cunningham*, 716 F. App’x at 184 (citing *Hamer v. Neighborhood Housing Servs. of Chicago*, 138 S. Ct. 13, 17 (2017) (“A provision governing the time to appeal in a civil action qualifies as jurisdictional only if Congress sets the time.”)).

rebuttable presumption that equitable tolling is available to litigants, even in cases where the government is a party.<sup>90</sup>

The Court of Appeals concluded that “even if” the 30-day period specified in the statute to file a petition for Tax Court review of a CDP hearing was subject to equitable tolling, the specific circumstances of Cunningham’s appeal “must warrant the application of equitable tolling in this particular case.”<sup>91</sup> Federal courts employ equitable tolling sparingly, and only in those rare instances where—due to circumstances external to the party’s own conduct—it would be unconscionable to enforce the limitation period against the party and gross injustice would result, when a litigant can establish:

- That he or she has been pursuing his or her rights diligently, and
- That some extraordinary circumstance stood in his or her way and prevented timely filing.<sup>92</sup>

Cunningham did not show that she had been pursuing her rights diligently and that extraordinary circumstances external to her own conduct prevented her from timely filing her appeal. The court noted that Cunningham’s miscalculation of the filing deadline may well have been an innocent mistake—she either misread (or misunderstood) the IRS’s notice, or else simply miscounted the number of days—but posited that granting equitable tolling on those grounds alone would erode the authority of the filing deadline to mere advisory status.

The court stated that the IRS’s letter notifying Cunningham of the filing deadline stated that she had a 30-day period beginning the day after the date of the letter to file an appeal, which was not misleading and could only be construed to require counting the day after the date of the letter as day one. The court went on to say Cunningham’s interpretation of the letter as requiring her to count the day after the date of the letter as day zero was contrary to U.S. Tax Court Rules of Practice and Procedure, Rule 25(a), the plain language of the letter, and common sense. For these reasons, the Court of Appeals for the Fourth Circuit affirmed the Tax Court’s dismissal of Cunningham’s petition, as the facts did not warrant equitable tolling of the petition filing deadline.

### *Duggan v. Commissioner*

The Court of Appeals for the Ninth Circuit in *Duggan v. Commissioner*<sup>93</sup> analyzed whether the 30-day period to file a Tax Court petition was jurisdictional and whether an untimely petition strips the Tax Court of jurisdiction to hear the case. In a manner similar to Ms. Cunningham, Mr. Duggan erroneously calculated the deadline for mailing a petition for review to the Tax Court, mistakenly counting the first day after the date of the IRS determination letter as day zero and mailing his petition 31 days after the date of the IRS determination.

90 *Irwin v. Dep’t of Veterans Affairs*, 498 U.S. 89, 95-96, 111 S. Ct. 453, 112 L. Ed. 2d 435 (1990). The court noted that it is uncertain whether the presumption applies at all outside the context of Article III courts. See *Sebelius v. Auburn Regional Med. Ctr.*, 568 U.S. 145, 158-159, (2013) (“We have never applied the *Irwin* presumption to an agency’s internal appeal deadline....”).

91 716 F. App’x at 183-184. While acknowledging that noncompliance with a jurisdictional time limit can never be excused, the Court of Appeals noted that “mandatory claim-processing rules” are “less stern,” and “may be waived or forfeited.” See *Cunningham*, 716 F. App’x at 184 (citing *Hamer v. Neighborhood Housing Servs. of Chicago*, 138 S. Ct. 13, 17 (2017) (internal quotation marks omitted)).

92 *Menominee Indian Tribe of Wis. v. U.S.*, 136 S. Ct. 750, 755 (2016), and *Whiteside v. U.S.*, 775 F.3d 180, 184 (4th Cir. 2014) (*en banc*).

93 *Duggan*, 879 F.3d 1029 (9th Cir. 2018), *aff’g* T.C. No. 15-4100 (T.C. June 26, 2015).

The IRS moved the Tax Court to dismiss the petition for lack of jurisdiction. Mr. Duggan, proceeding *pro se*, opposed the IRS's motion, arguing that the IRS's notices were "incomplete, misleading, or ambiguous," and that his attempts to comply with the filing deadline were reasonable. The Tax Court granted the IRS's motion and dismissed Duggan's petition on jurisdictional grounds. Duggan moved for reconsideration, contending, among other things, that he should not be faulted for his reasonable interpretation of the filing deadline. The Tax Court denied Duggan's motion to reconsider, and Duggan timely appealed his case to the Court of Appeals for the Ninth Circuit.

Unlike the Fourth Circuit in *Cunningham*, the Court of Appeals for the Ninth Circuit first analyzed whether the 30-day deadline to file a CDP petition in Tax Court was jurisdictional before considering equitable tolling, "because a party's failure to satisfy a deadline that is jurisdictional places the case beyond the powers of the court."<sup>94</sup> If the 30-day period is jurisdictional, the court concluded that it would not have authority to entertain "such a suit even if the timeliness objection were waived by the other party, or if a compelling argument for equitable tolling could otherwise be made."<sup>95</sup> After reviewing cases holding that the IRC § 6015(e)(1)(A) 90-day deadline to file an innocent spouse petition in the Tax Court is jurisdictional, the court applied similar reasoning to IRC § 6330(d)(1).<sup>96</sup>

An amicus brief filed in the case discussing the import of recent Supreme Court decisions on the jurisdiction of IRC § 6330(d)(1)<sup>97</sup> cited a prior version of § 6330(d)(1) that allowed a person who brought an appeal in an incorrect court 30 days to refile in the correct court as evidence of Congressional intent that the filing deadline was not jurisdictional. The court disagreed, stating that the plain language of the current version of IRC § 6330(d)(1) confers jurisdiction on the Tax Court only if a CDP petition is filed in that court within 30 days of the IRS's determination, and noting that "[t]he starting point in discerning congressional intent ... is the existing statutory text and not predecessor statutes."<sup>98</sup> Addressing the amicus brief arguments, the court pointed out that Congress might have intended the 30-day deadline to file an appeal in the Tax Court to be non-jurisdictional while including a clause explicitly granting a second 30-day deadline for misdirected appeals out of an abundance of caution or to sweep in cases not comprehended by the doctrine of equitable tolling. Alternatively, the court speculated that Congress might have intended the second 30-day deadline to act as an exception that mitigates the harshness of an otherwise jurisdictional rule. Regardless, the court concluded that "such speculation must yield to the text of the statute."<sup>99</sup>

Accordingly, the court held that because the text of IRC § 6330(d)(1) conditions the Tax Court's jurisdiction on the timely filing of a petition for review, the 30-day deadline in IRC § 6330(d)(1) is jurisdictional. Duggan's failure to meet this deadline divested the Tax Court of the power to hear his case and foreclosed any argument for equitable tolling.

94 *Duggan*, 879 F.3d 1029, 1031 (citing *U.S. v. Kwai Fun Wong*, 135 S. Ct. 1625, 1631 (2015)).

95 *Duggan*, 879 F.3d 1029, 1031.

96 Several courts of appeal have held that the 90-day deadline in § 6015(e)(1)(A) is a jurisdictional requirement and the Tax Court lacks jurisdiction to hear untimely petitions for innocent spouse relief, regardless of whether equitable considerations supporting the extension of the prescribed time period exist. See *Matuszak v. Comm'r*, 862 F.3d 192 (2d Cir. 2017); *Rubel v. Comm'r*, 856 F.3d 301 (3d Cir. 2017), *aff'g* No. 16-9183 (T.C. July 11, 2016); *Calvo v. Comm'r*, 117 A.F.T.R.2d (RIA) 2246 (D.C. Cir. 2016). See also National Taxpayer Advocate 2017 Annual Report to Congress 462-72; 299-306. See also *Maier v. Comm'r*, 360 F.3d 361 (2d Cir. 2004).

97 *Duggan*, 879 F.3d at 1034, n. 2. The court granted leave to file an amicus brief "discussing the import of recent Supreme Court decisions on the jurisdictionality of § 6330(d)(1)" to another taxpayer, because the decision in this case could potentially have affected the outcome of her appeal.

98 *Duggan*, 879 F.3d at 1034 (citing *Lamie v. U.S.*, 540 U.S. 526, 534, (2004)) (internal citations omitted).

99 *Duggan*, 879 F.3d 1029, 1034 (citing *United Food & Commercial Workers Union Local 751 v. Brown Grp., Inc.*, 517 U.S. 544, 550 (1996)) (internal quotations omitted).

### *McCree v. Commissioner*

In *McCree v. Commissioner*,<sup>100</sup> the IRS Integrity & Verification Operation (IVO) screened the taxpayer's timely filed 2010 return for possible fraudulent inflated withholdings, after she reported a zero taxable amount on an IRA distribution, claiming a refund of more than \$8,000.<sup>101</sup> She reported the distribution as a rollover, but failed to deposit the distribution in a qualified account. IVO determined that the withholdings reported on her tax return were correct, but it did not evaluate or determine whether she had reported her income correctly. IVO sent Ms. McCree Letter 4464C, *Questionable Refund 3rd Party Notification*, informing her that her refund was being held for review and verification, and that she was "not required to do anything at this time" and that if she did not receive her refund within 45 days, she could call the telephone number provided. She received her refund 39 days later.

Sixteen months later, the IRS mailed her a statutory notice of deficiency determining a deficiency in her 2010 federal income tax of \$5,637 and an accuracy-related penalty under IRC § 6662(a) of \$1,127.40; however, Ms. McCree did not receive the notice.

Ms. McCree made several attempts to contest the liability, but IRS incorrectly told her she could not, because she had already had an opportunity to contest the underlying liability. Before the initial CDP hearing, Ms. McCree submitted documents that supported reducing her underlying liability and eliminating the accuracy-related penalty. During the CDP hearing, Appeals abated some of the tax liability and the entire accuracy-related penalty based on the documentation she provided, despite erroneously informing Ms. McCree that she would be unable to contest the 2010 tax liability.

Ms. McCree, who represented herself at all stages of the controversy, claimed Letter 4464C was an audit letter, and she was improperly audited twice.<sup>102</sup> She argued that IRS should not be able to issue a refund after reviewing a return and later audit that return and determine a deficiency.

The issuance of a refund to the taxpayer after acceptance of the taxpayer's return and verification of withholding did not preclude the IRS from subsequently determining a deficiency in the taxpayer's income tax and seeking to recover the refund. A letter from the IRS informing the taxpayer that the refund was being withheld to verify withholdings did not constitute an unnecessary examination since the letter did not request documents or information and was only a limited informational contact by the IRS. The Court noted that the IRS IVO does not conduct audits of taxpayers' tax returns but does screen tax returns to detect false wages or withholding.

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<sup>100</sup> T.C. Memo. 2017-145.

<sup>101</sup> For concerns about the IRS's fraud detection and wage verification programs, see National Taxpayer Advocate 2016 Annual Report to Congress 151-160 (Most Serious Problem: *Fraud Detection: The IRS's Failure to Establish Goals to Reduce High False Positive Rates for Its Fraud Detection Programs Increases Taxpayer Burden and Compromises Taxpayer Rights*) and National Taxpayer Advocate 2017 Annual Report to Congress 219-226 (Most Serious Problem: *Fraud Detection: The IRS Has Made Improvements to Its Fraud Detection Systems, But a Significant Number of Legitimate Taxpayers Are Still Being Improperly Selected by These Systems, Resulting in Refund Delays*).

<sup>102</sup> See National Taxpayer Advocate 2017 Annual Report to Congress 49-63 (Most Serious Problem: *Audit Rates: The IRS Is Conducting Significant Types and Amounts of Compliance Activities That It Does Not Deem to Be Traditional Audits, Thereby Underreporting the Extent of Its Compliance Activity and Return on Investment, and Circumventing Taxpayer Protections*) and Nina Olson, "Real" vs. "Unreal" Audits and Why This Distinction Matters, NTA BLOG (July 6, 2018), <https://taxpayeradvocate.irs.gov/news/nta-blog-real-vs-unreal-audits-and-why-this-distinction-matters>.

Research of records in IRS possession to verify withholdings does not constitute an examination in violation of IRC § 7605(b).<sup>103</sup> Letter 4464C was not an indication of an audit or an examination, but one of the “narrow, limited contacts or communications between the Service and a taxpayer that do not involve the Service inspecting the taxpayer’s books of account.”<sup>104</sup>

Because Ms. McCree properly challenged her underlying liability, the proper standard of review for the court with respect to this issue is *de novo*.<sup>105</sup> Since Ms. McCree made the necessary showing that there was a genuine issue of material fact for trial, the court awarded her a partial victory and agreed that she could contest her underlying liability at a future trial setting.

### *Seminole Nursing Home, Inc. v. Commissioner*

In *Seminole Nursing Home, Inc. v. Commissioner*,<sup>106</sup> the corporate taxpayer did not contest the underlying tax liability, but contended that the business would suffer economic hardship if the proposed levy were sustained. At the CDP hearing, the corporate taxpayer proposed a monthly payment that would allow it to stay current on its federal tax deposit payments as a collection alternative, and argued that it was less intrusive than enforced levy action. The IRS Settlement Officer (SO) rejected the installment agreement because the taxpayer was not in compliance with its federal employment tax deposit obligations. Rejecting a collection alternative because of noncompliance with estimated tax payment requirements does not violate the proper balancing requirement, but noncompliance is not the only factor involved in the balancing requirement. The taxpayer claimed the SO either did not conduct the required CDP balancing test<sup>107</sup> or did not explain her reason for concluding that its requirements were met.

The Tax Court noted that economic hardship relief is only available to individual taxpayers,<sup>108</sup> pursuant to Treas. Reg. § 301.6343-1(b)(4)(i).<sup>109</sup> The court held the SO was not required to consider the taxpayer’s economic hardship argument in the light of IRC § 6343(a)(1)(D) and thus, it was not an abuse of discretion. Although a corporation may not claim economic hardship as a defense,

103 See Rev. Proc. 2005-32, § 4.03; see also *Grossman v. Comm’r*, 74 T.C. 1147, 1156 (1980) (holding that mere examination of a taxpayer’s income tax return and accompanying schedules does not constitute a second inspection of that taxpayer’s books within the meaning of section 7605(b)); *Rice v. Comm’r*, T.C. Memo. 1994-204.

104 See Rev. Proc. 2005-32, § 4.03.

105 See *Giamelli v. Comm’r*, 129 T.C. at 111.

106 *Seminole Nursing Home, Inc. v. Comm’r*, T.C. Memo. 2017-102.

107 See National Taxpayer Advocate 2014 Annual Report to Congress 185-196 (Most Serious Problem: *Collection Due Process: The IRS Needs Specific Procedures for Performing the Collection Due Process Balancing Test to Enhance Taxpayer Protections*); see also Nina E. Olson, *Taking the Bull by Its Horns: Some Thoughts on Constitutional Due Process in Tax Collection*, 2010 Erwin N. Griswold Lecture Before the American College of Tax Counsel, 63 TAX LAW. 227 (2010).

108 See National Taxpayer Advocate 2017 Annual Report to Congress, Purple Book 34 (*Authorize the IRS to Release Levies That Cause Economic Hardship for Business Taxpayers*).

109 See *Lindsay Manor Nursing Home, Inc. v. Comm’r*, 148 T.C. 9 (2017). The court found that the discretion provided to the Secretary by IRC § 6343(a) and the existence of other avenues for nonindividuals in similar circumstances to obtain the relief (e.g., such as offers in compromise based on doubt as to collectability or public policy considerations) intended by Congress indicate that the limiting of “economic hardship” to individuals by Treas. Reg. § 301.6343-1(b)(4)(i) is not inconsistent with the provisions of IRC § 6343(a). Moreover, the regulations note that applying an economic hardship standard to nonindividuals would not necessarily promote effective tax administration because it might result in the Government’s determining whether and when to forgo the collection of taxes to support a nonviable business; but see National Taxpayer Advocate 2011 Annual Report to Congress 537-543 (Legislative Recommendation: *Amend IRC § 6343(a) to Permit the IRS to Release Levies on Business Taxpayers that Impose Economic Hardship*); and Protecting Taxpayers Act, S. 3278, 115th Cong. § 303 (2018).

the balancing test should consider a taxpayer's specific economic realities and the consequences of a proposed collection action.<sup>110</sup>

Prior to the CDP hearing, the taxpayer submitted a Form 433-B, *Collection Information Statement for Businesses*, showing that its monthly income exceeded its monthly expenses, and it had adequate net monthly income for monthly payments. However, the SO made a substantial mathematical error, reflected both in her case activity report and on the Form 433-B. The error made it appear that the taxpayer's monthly expenses far exceed its income. This factual error, while harmless to the SO's denial of the taxpayer's proposed installment agreement request, was consistently repeated.<sup>111</sup>

The Court remands a CDP case to the IRS Appeals Office when the Court determines that a further hearing would be "helpful," "necessary," or "productive."<sup>112</sup> The additional hearing is not intended as a new hearing or a "do over" for a taxpayer whose missteps during the CDP process resulted in its collection alternative's being rejected, but rather a supplement to the taxpayer's original hearing.<sup>113</sup>

Because the SO repeated her error and because there was nothing in the record reflecting a correction of that error, the Court found that the balancing test under IRC § 6330(c)(3)(C) could have been affected, and remanded the case back to Appeals for the limited purpose of reconsidering the balancing analysis in the light of the corrected facts and circumstances.

## CONCLUSION

CDP hearings provide instrumental protections for taxpayers to meaningfully address the appropriateness of IRS collection actions. Given the important safeguard that CDP hearings offer taxpayers, it is unsurprising that CDP remains one of the most frequently litigated issues. The U.S. Tax Court has jurisdiction over appeals from CDP hearings only if the taxpayer files a timely petition. If a taxpayer misses the deadline, the Tax Court does not have jurisdiction to review the IRS's determination and the taxpayers are deprived of their *rights to be informed, to appeal the IRS's decision in an independent forum, and to a fair and just tax system*.

Current law does not require the IRS to provide the date by which a taxpayer must file his or her CDP petition in the U.S. Tax Court, only the date of the determination that is subject to judicial review. Several recent court cases demonstrate that taxpayers misinterpret the calculation of the last day to file a request for a CDP hearing or to file a CDP or innocent spouse petition with the Tax Court. Thus, the *Cunningham* and *Duggan* decisions discussed herein illustrate the importance of complying with the filing deadlines for taxpayers to avail themselves of judicial review and exercise their *right to appeal an IRS decision in an independent forum*.<sup>114</sup> The *Cunningham* opinion reviewed the concept of equitable tolling, which is only available if the taxpayer shows diligent pursuit of rights and that timely filing

110 The Tax Court found in *Lindsay Manor Nursing Home, Inc. v. Comm'r*, 148 T.C. 9 (2017) that the § 6330(c)(3)(C) balancing test must consider a taxpayer's specific economic realities and the consequences of a proposed collection action.

111 *Cf. Sulphur Manor, Inc. v. Comm'r*, T.C. Memo. 2017-95, at 11 n.7 (finding harmless a poorly worded sentence in the Settlement Officer's (SO's) case activity report where the SO's notes elsewhere reflected proper calculation).

112 *Seminole Nursing Home, Inc. v. Comm'r*, T.C. Memo. 2017-102 (citing *Kelby v. Comm'r*, 130 T.C. 79, 86 n.4 (2008); *Lunsford v. Comm'r*, 117 T.C. 183, 189 (2001); *Churchill v. Comm'r*, T.C. Memo. 2011-182).

113 *Seminole Nursing Home, Inc. v. Comm'r*, T.C. Memo. 2017-102 (citing *Takeh v. Comm'r*, T.C. Memo. 2015-103, at 13; *Kelby v. Comm'r*, 130 T.C. at 86).

114 *Cunningham v. Comm'r*, 716 F. App'x 182 (4th Cir. 2018), *aff'g* No. 16-014090 (T.C. Dec. 7, 2016) and *Duggan v. Comm'r*, 879 F.3d 1029 (9th Cir. 2018), *aff'g* No. 15-4100 (T.C. June 26, 2015).

of an appeal was prevented by some extraordinary circumstance. A taxpayer's innocent misreading or misunderstanding of the filing deadline falls short of that standard.

In the CDP context, the burden is on taxpayers, and not the IRS, to keep track of when the 30-day appeal filing period begins, namely, the requirement in IRC § 6330(d)(1) that the taxpayer petition the Tax Court within 30 days of the date of an IRS notice. As stated above, the consequence of not filing of a timely petition is dire. If a taxpayer misses the deadline, the Tax Court does not have jurisdiction to review the IRS's determination.<sup>115</sup> Unsophisticated taxpayers are more likely to misinterpret the current language in the IRS notice of determination that states: "If you want to dispute this determination in court, you must file a petition with the United States Tax Court within 30 days from the date of this letter,"<sup>116</sup> while a close reading of the applicable regulations reveals that "the taxpayer may appeal such determinations made by Appeals within the 30-day period commencing the day after the date of the Notice of Determination."<sup>117</sup> To strengthen CDP rights of taxpayers, the National Taxpayer Advocate proposed a legislative recommendation to require the IRS calculate and provide the last date for filing an appeal on all CDP notices of determination to make them consistent with the requirements for statutory notices of deficiency under IRC § 6213(a).<sup>118</sup> The proposed legislative change would also deem requests timely filed for a CDP hearing and petitions to the Tax Court to review CDP and innocent spouse determinations as long as they are filed<sup>119</sup> by the "last date" listed in the IRS notice.<sup>120</sup>

*McCree v. Commissioner* shows that taxpayers contacted by the IRS after being flagged by an IVO filter<sup>121</sup> can be very confused about whether the wage verification process is an audit. The National Taxpayer Advocate has previously written about the similarities between "real" vs "unreal" audits.<sup>122</sup> The IRS considers taxpayer compliance contacts through programs and procedures such as identity and

115 If the taxpayer does not request a hearing within the 30-day period, the taxpayer may still be entitled to an equivalent hearing with Appeals but will not have any appeal rights allowing the taxpayer to file for judicial review of the equivalency hearing determination. Treas. Reg. §§ 301.6320-1(i); 301.6330-1(i).

116 IRS, Letter 3193, *Notice of Determination: Concerning Collection Action(s) Under Section 6320 or 6330 of The Internal Revenue Code* (July 2018).

117 See Treas. Reg. § 301.6320-1(f)(1) and 301.6330-1(f)(1); see also Most Serious Problem: *Collection Due Process Notices: Despite Recent Changes to Collection Due Process Notices, Taxpayers Are Still at Risk for Not Understanding Important Procedures and Deadlines, Thereby Missing Their Right to an Independent Hearing and Tax Court Review*, *supra*.

118 National Taxpayer Advocate 2017 Annual Report to Congress 299-306 (Legislative Recommendation: *Collection Due Process and Innocent Spouse Notices: Amend IRC §§ 6320, 6330, and 6015 to Require That IRS Notices Sent to Taxpayers Include a Specific Date by Which Taxpayers Must File Their Tax Court Petitions, and Provide That a Petition Filed by Such Specified Date Will Be Treated As Timely*).

119 The "statutory mailbox rule" in IRC § 7502 provides that if a time-sensitive document or payment arrives late but is postmarked on or before the due date, the postmark date is treated as the date the document or payment was filed with the IRS. Further, IRC § 7502(c) provides that registered or certified mail, or methods deemed substantially equivalent by the Secretary of Treasury, is *prima facie* evidence of delivery. The rule applies to documents and payments sent through the U.S. Postal Service, designated private delivery services, and electronic return transmitters. IRC § 7502(e). See National Taxpayer Advocate 2017 Annual Report to Congress 278 (Legislative Recommendation: *Electronic Mailbox Rule: Revise the Mailbox Rule to Include All Time-Sensitive Documents and Payments Electronically Transmitted to the IRS*).

120 Under this legislative recommendation taxpayers are allowed the later of the date on the notice or the last statutory date, which provides an additional protection if the IRS miscalculates the date on the notice.

121 See National Taxpayer Advocate 2016 Annual Report to Congress 151-160 (Most Serious Problem: *Fraud Detection: The IRS's Failure to Establish Goals to Reduce High False Positive Rates for Its Fraud Detection Programs Increases Taxpayer Burden and Compromises Taxpayer Rights*) and National Taxpayer Advocate FY 2019 Objectives Report to Congress 160-166 (Most Serious Problem: *Fraud Detection: The IRS Has Made Improvements to Its Fraud Detection Systems, But a Significant Number of Legitimate Taxpayers Are Still Being Improperly Selected by These Systems, Resulting in Refund Delays*).

122 See National Taxpayer Advocate 2017 Annual Report to Congress 49-63 (Most Serious Problem: *Audit Rates: The IRS Is Conducting Significant Types and Amounts of Compliance Activities That It Does Not Deem to Be Traditional Audits, Thereby Underreporting the Extent of Its Compliance Activity and Return on Investment, and Circumventing Taxpayer Protections*) and Nina Olson, "Real" vs. "Unreal" Audits and Why This Distinction Matters, NTA BLOG (July 6, 2018), <https://taxpayeradvocate.irs.gov/news/nta-blog-real-vs-unreal-audits-and-why-this-distinction-matters>.

wage verification are not “real” audits. Yet to taxpayers, the experience of receiving compliance contacts may feel like a “real” examination. This distinction between “real” and “unreal” audits has real-world consequences impacting taxpayer rights, including *the right to challenge the IRS’s position and be heard, the right to appeal an IRS decision in an independent forum, the right to finality, and the right to a fair and just tax system*. In *McCree*, the Tax Court reaffirmed the taxpayer’s *right to challenge the IRS’s position and be heard*, ruling that a taxpayer’s petition for review of a CDP determination should not lose in summary judgment, provided the taxpayer makes the necessary showing that there was a genuine issue of material fact for trial, and should be given an opportunity to contest the underlying liability, if the taxpayer had no prior opportunity to do so.

Finally, *Seminole Nursing Home, Inc. v. Commissioner* raises two important issues extensively discussed in prior reports to Congress. First, the case reemphasizes the importance of the CDP balancing test, whether the taxpayer is an individual or a business. It appears that even several years since the Tax Court decision in *Budish v. Commissioner*,<sup>123</sup> the IRS Office of Appeals continues to issue *pro forma* statements and boilerplate language (without proper analysis), in place of a proper balancing test, thereby violating the taxpayers’ *right to privacy*, which states that taxpayers have the right to expect that an IRS enforcement action will comply with the law and be no more intrusive than necessary. Appeals did not properly weigh the legitimate concerns of the taxpayer regarding the intrusiveness of the proposed collection action against the government’s interest in collecting the tax debt. By remanding the case back to Appeals the court reaffirmed the importance of a full balancing test analysis.<sup>124</sup> Educating IRS officers that conduct hearings and encouraging them to fully explain to the taxpayer and make a record of which factors they considered could go a long way in reducing future litigation.<sup>125</sup> By not giving proper attention to the balancing test, the IRS is missing opportunities to improve compliance, enhance taxpayer trust and confidence, and relieve undue burden on taxpayers.

The *Seminole* case also raised another important issue—the inability of a business taxpayer to claim economic hardship as a defense to an IRS collection action. IRC § 6343(a)(1)(D) requires the IRS to release a levy if “the Secretary has determined that such levy is creating an economic hardship due to the financial condition of the taxpayer.” However, defining economic hardship as the inability to pay reasonable basic living expenses means that only individuals (including sole proprietorship entities) can experience economic hardship.<sup>126</sup> As a result, it is more difficult for businesses to settle their tax debts with collection alternatives (rather than enforced collection). In essence, an otherwise viable business facing economic hardship may be forced to choose between terminating or laying off employees, and failing to meet its tax obligations. To mitigate these concerns, the National Taxpayer Advocate proposed a legislative change to amend IRC § 6343 to authorize the IRS to release a levy if it determines that the levy is creating an economic hardship due to the financial condition of the taxpayer’s viable trade

123 T.C. Memo. 2014-239.

124 IRC § 6330(c)(3)(C); IRM 8.22.4.2.2 (Sept. 25, 2014). See also H.R. REP. No. 105-599, at 263 (1998) (Conf. Rep.). For simplicity, we use the term “proposed collection action” referring to both the actions taken and proposed. IRC § 6330 requires the IRS to notify the taxpayer of the right to request a CDP hearing not less than 30 days before issuing the first levy to collect a tax. Pursuant to IRC § 6320 the taxpayer is notified of the right to request a CDP hearing within five business days after the first Notice of Federal Tax Lien (NFTL) for a tax period is filed. Thus, Treasury Regulations under IRC § 6320 require a Hearing Office to consider “whether the continued existence of the filed [NFTL] represents a balance between the need for the efficient collection of taxes and the legitimate concern of the taxpayer that any collection action be no more intrusive than necessary.” See Treas. Reg. § 301.6320-1(e)(3), A-E1(vi).

125 See National Taxpayer Advocate 2014 Annual Report to Congress 185-196 (Most Serious Problem: *Collection Due Process: The IRS Needs Specific Procedures for Performing the Collection Due Process Balancing Test to Enhance Taxpayer Protections*). See also Nina E. Olson, *Taking the Bull by Its Horns: Some Thoughts on Constitutional Due Process in Tax Collection*, 2010 Erwin N. Griswold Lecture Before the American College of Tax Counsel, 63 TAX LAW. 227 (2010).

126 Treas. Reg. § 301.6343-1(b)(4).

or business, and to require the IRS, in making the determination to release a levy against a business on economic hardship grounds, to consider the economic viability of the business, the nature and extent of the hardship (including whether the taxpayer exercised ordinary business care and prudence), and the potential harm to individuals if the business is liquidated.<sup>127</sup> These factors are already considered in bankruptcy proceedings, and address the IRS's concerns about advantaging non-viable businesses.<sup>128</sup>

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127 National Taxpayer Advocate 2017 Annual Report to Congress, Purple Book 34 (*Authorize the IRS to Release Levies That Cause Economic Hardship for Business Taxpayers*). See also Protecting Taxpayers Act, S. 3278, 115th Cong. § 303 (2018); Small Business Taxpayer Bill of Rights Act of 2018, S. 2689, 115th Cong. § 16 (2018); H.R. 4368, 112th Cong. § 1 (2012); Taxpayer Rights Act of 2015, H.R. 4128 114th Cong. § 304 (2015) and S. 2333, 114th Cong. § 304 (2015).

128 The United States Supreme Court has limited the application of the Trust Fund Recovery Penalty to help financially troubled companies maintain “minimum working capital .... to maintain operations and avoid liquidation of the business.” See *Slodov v. U.S.*, 436 U.S. 238 (1978) (holding that the individual's conduct was not willful when he used after-acquired funds for operating expenses of the business) and *In re Rossiter*, 167 B.R. 919 (C.D. Cal. 1994) (applying *Slodov* analysis).

MLI  
#6**Failure to File Penalty Under IRC § 6651(a)(1), Failure to Pay an Amount Shown As Tax on Return Under IRC § 6651(a)(2), and Failure to Pay Estimated Tax Penalty Under IRC § 6654****SUMMARY**

We reviewed 47 decisions issued by federal courts from June 1, 2017, to May 31, 2018, regarding additions to tax for:

- i. Failure to file a tax return by the due date under Internal Revenue Code (IRC) § 6651(a)(1);
- ii. Failure to pay an amount shown on a tax return under IRC § 6651(a)(2);
- iii. Failure to pay installments of the estimated tax under IRC § 6654; or
- iv. Some combination of the three.<sup>1</sup>

The phrase “addition to tax” is commonly referred to as a penalty, so we will refer to these additions to tax as the failure to file penalty, the failure to pay penalty, and the estimated tax penalty. Twelve cases involved the imposition of the estimated tax penalty in conjunction with the failure to file and failure to pay penalties; 35 cases involved the failure to file or failure to pay penalties without the estimated tax penalty; and there were no cases involving the estimated tax penalty as the only issue.

A taxpayer can avoid the failure to file and failure to pay penalties by demonstrating the failure is due to reasonable cause and not willful neglect.<sup>2</sup> The estimated tax penalty is imposed unless the taxpayer falls within one of the statutory exceptions.<sup>3</sup> Taxpayers were unable to avoid a penalty in 41 of the 47 cases.

**TAXPAYER RIGHTS IMPACTED<sup>4</sup>**

- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to a Fair and Just Tax System*

**PRESENT LAW**

Under IRC § 6651(a)(1), a taxpayer who fails to file a return on or before the due date (including extensions of time for filing) will be subject to a penalty of five percent of the tax due (minus any credit the taxpayer is entitled to receive and payments made by the due date) for each month or partial month the return is late. This penalty will accrue up to a maximum of 25 percent, unless the failure is due to

1 Internal Revenue Code (IRC) § 6651(a)(3) imposes an addition to tax if the tax required to be shown on a return, but which is not shown, is not paid within 21 calendar days from the date of notice and demand for payment. Because we only identified two cases involving this penalty, we did not include it in our analysis.

2 IRC § 6651(a)(1), (a)(2).

3 IRC § 6654(e).

4 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the IRC. See IRC § 7803(a)(3).

reasonable cause and not willful neglect.<sup>5</sup> For the taxpayer to avoid the penalty by showing there was a reasonable cause, the taxpayer must have exercised ordinary business care and prudence.<sup>6</sup> The failure to file penalty applies to income, estate, gift, employment, self-employment, and certain excise tax returns.<sup>7</sup>

When an income tax return is filed more than 60 days after the due date (including extensions), the penalty shall not be less than the lesser of two amounts—100 percent of the tax required to be shown on the return that the taxpayer did not pay on time, or a specific dollar amount, which is adjusted annually due to inflation.<sup>8</sup> The specific dollar amounts are as follows:

- \$215 for returns due on or after 1/1/2019;
- \$210 for returns due on or after 1/1/2018;
- \$205 for returns due between 1/1/2016 and 12/31/2017;
- \$135 for returns due between 1/1/2009 and 12/31/2015; and
- \$100 for returns due before 1/1/2009.

The failure to pay penalty, IRC § 6651(a)(2), applies to a taxpayer who fails to pay an amount shown or required to be shown as tax on the return. The penalty accrues at a rate of half a percent (0.5 percent) per month on the unpaid balance for as long as it remains unpaid, up to a maximum of 25 percent of the amount due.<sup>9</sup> When the IRS imposes both the failure to file and failure to pay penalties for the same month, it reduces the failure to file penalty by the amount of the failure to pay penalty (0.5 percent for each month).<sup>10</sup> The taxpayer can avoid the penalty by establishing the failure was due to reasonable cause; in other words, the taxpayer must have exercised ordinary business care and prudence but nonetheless was unable to pay by the due date, or that paying on the due date would have caused undue hardship.<sup>11</sup> The failure to pay penalty applies to income, estate, gift, employment, self-employment, and certain excise tax returns.<sup>12</sup>

Courts will consider “all the facts and circumstances of the taxpayer’s financial situation” to determine whether the taxpayer exercised ordinary business care and prudence.<sup>13</sup> In addition, “consideration will be given to the nature of the tax which the taxpayer has failed to pay.”<sup>14</sup>

5 IRC § 6651(a)(1), (b)(1). The penalty increases to 15 percent per month up to a maximum of 75 percent if the failure to file is fraudulent. IRC § 6651(f).

6 Treas. Reg. § 301.6651-1(c)(1).

7 IRC § 6651(a)(1).

8 IRC § 6651(a). The IRS typically announces various inflation adjustments by publishing a revenue procedure. See, e.g., Rev. Proc. 2018-18, 2018-10 I.R.B. 392.

9 IRC § 6651(a)(2). Note that if the taxpayer timely files the tax return (including extensions) but an installment agreement is in place, the penalty will continue accruing at the lower rate of 0.25 percent rather than 0.5 percent of the tax shown. IRC § 6651(h).

10 IRC § 6651(c)(1). When both the failure to file and failure to pay penalties are accruing simultaneously, the failure to file will max out at 22.5 percent and the failure to pay will max out at 2.5 percent, thereby abiding by the 25 percent maximum limitation.

11 Treas. Reg. § 301.6651-1(c)(1). Even when a taxpayer shows undue hardship, the regulations require proof of the exercise of ordinary business care and prudence.

12 IRC § 6651(a)(2).

13 Treas. Reg. § 301.6651-1(c)(1). See, e.g., *East Wind Indus. v. U.S.*, 196 F.3d 499, 507 (3d Cir. 1999).

14 Treas. Reg. § 301.6651-1(c)(2).

IRC § 6654 imposes a penalty on any underpayment of estimated tax by an individual or by certain estates or trusts.<sup>15</sup> The law requires four installments per tax year, each generally 25 percent of the required annual payment.<sup>16</sup> The required annual payment is generally the lesser of 90 percent of the tax shown on the return for the current tax year or 100 percent of the tax for the previous tax year.<sup>17</sup>

The amount of the penalty is determined by applying:

- The underpayment rate established under IRC § 6621;
- To the amount of the underpayment;
- For the period of the underpayment.<sup>18</sup>

The amount of the underpayment is the excess of the required payment over the amount paid by the due date. To avoid the penalty, the taxpayer has the burden of proving that one of the following exceptions applies:

- The tax due (after taking into account any federal income tax withheld) is less than \$1,000;<sup>19</sup>
- The preceding tax year was a full 12 months, the taxpayer had no liability for the preceding tax year, and the taxpayer was a U.S. citizen or resident throughout the preceding tax year;<sup>20</sup>
- The IRS determines that because of casualty, disaster, or other unusual circumstances, the imposition of the penalty would be against equity and good conscience;<sup>21</sup> or
- The taxpayer retired after reaching age 62, or became disabled, in the tax year for which estimated payments were required, or in the tax year preceding that year, and the underpayment was due to reasonable cause and not willful neglect.<sup>22</sup>

In any court proceeding, the IRS has the burden of producing sufficient evidence that it imposed the failure to file, failure to pay, or estimated tax penalties appropriately.<sup>23</sup>

## ANALYSIS OF LITIGATED CASES

We analyzed 47 opinions issued between June 1, 2017, and May 31, 2018, where the failure to file penalty, failure to pay penalty, or estimated tax penalty was in dispute. All but eight of these cases were either litigated in the United States Tax Court, or an appeal of a Tax Court decision. A detailed list appears in Table 6 in Appendix 3. Twenty-eight cases involved individual taxpayers and 19 involved businesses (including individuals engaged in self-employment or partnerships).

15 IRC § 6654(a), (l).

16 IRC § 6654(c)(1), (d)(1)(A).

17 IRC § 6654(d)(1)(B). If the adjusted gross income shown on the return of the individual for the preceding taxable exceeds \$150,000, the required annual payment increases to an amount 110 percent of the tax shown on the return of the individual for the preceding tax year (if preceding tax year was 2002 or after). IRC § 6654(d)(1)(C)(i).

18 IRC § 6654(a).

19 IRC § 6654(e)(1).

20 IRC § 6654(e)(2).

21 IRC § 6654(e)(3)(A).

22 IRC § 6654(e)(3)(B).

23 *Higbee v. Comm'r*, 116 T.C. 438, 446 (2001) (applying IRC § 7491(c)). An exception to this rule relieves the IRS of this burden where the taxpayer's petition fails to state a claim for relief from the penalty (and therefore is deemed to concede the penalty). *Funk v. Comm'r*, 123 T.C. 213, 218 (2004).

Of the 19 cases in which taxpayers appeared *pro se* (without counsel), the outcomes generally favored the IRS. In one case, the court granted partial relief to the taxpayer, and in one case, the court granted full relief to the taxpayer. The IRS prevailed in full in the remaining 17 cases. Taxpayers represented by counsel fared slightly better; of the 27 cases in which taxpayers had representation, taxpayers prevailed in full in four cases and were denied relief in the remaining 23 cases.

### Failure to File Penalty

In 41 out of the 46 cases reviewed where the failure to file penalty was at issue, the taxpayers could not prove that the failures to file were due to reasonable cause.<sup>24</sup> Taxpayers provided reasons such as physical injury or mental illness, reliance on an agent, and electronic filing errors as a basis for reasonable cause. Circumstances suggesting reasonable cause are typically outside the taxpayer's control.<sup>25</sup>

#### *Physical Injury or Mental Illness Defense*

A physical injury or mental illness may provide a basis for a taxpayer to establish reasonable cause for not filing, if the condition affected the taxpayer to such a degree that he or she could not file a tax return on time. When determining whether the condition establishes reasonable cause, the court analyzes how the taxpayer conducted his or her business affairs during the illness.

In *Rogers v. Commissioner*, the Tax Court found that married taxpayers had established reasonable cause for their failure to file their 2009 tax return based on illness.<sup>26</sup> The taxpayers testified that Mr. Rogers was hospitalized for an extended period in 2009 to treat his alcoholism, during which time there was no means of communication between Mr. and Mrs. Rogers.<sup>27</sup> After his release, Mr. Rogers continued to deal with his illness. Mrs. Rogers was preoccupied caring for her husband and taking on substantial additional responsibilities in their businesses.<sup>28</sup> The court also noted that the taxpayers timely filed their income tax returns in prior years under extension, and would have done so for 2009 if they had requested an extension for that year.<sup>29</sup> Mrs. Rogers experienced her own health problems with stress, anxiety, and depression in connection with her husband's illness and subsequent care. Acknowledging that "[i]llness or incapacity of a taxpayer or a member of his immediate family may be reasonable cause for late filing," the court found the taxpayers were not liable for the failure to file penalty.<sup>30</sup>

In contrast, a vague reference to illness does not establish reasonable cause. The taxpayers in *Barrett v. Commissioner* were unable to establish reasonable cause for filing their 2012 and 2014 tax returns late.<sup>31</sup> Although Mr. Barrett referred vaguely to illness as an excuse for not filing the 2014 return before the

24 Taxpayers avoided the failure to file penalty by successfully proving reasonable cause in four cases.

25 *McMahan v. Comm'r*, 114 F.3d 366, 369 (2d Cir. 1997) (citation omitted), *aff'g* T.C. Memo. 1995-547.

26 *Rogers v. Comm'r*, T.C. Memo. 2018-53.

27 *Id.* Mr. Rogers is a tax attorney and a CPA with over 40 years of experience. He has a *juris* doctor degree (J.D.) from Harvard University and a master of business administration degree (M.B.A.) from the University of Chicago. He was a partner at various law firms from January 1998 to May 2008, when he formed Rogers & Associates as a sole proprietorship. Mrs. Rogers has a bachelor's degree in chemistry, a master's degree in biochemistry, an M.B.A., a doctorate in educational administration, and a J.D. Before retiring in 2005, she worked as a high school chemistry and computer science teacher and an associate principal for over 20 years. She was licensed as a real estate broker in 1967 and an attorney in 1991. Since 2009, she represented clients in property tax appeals.

28 *Id.*

29 *Id.*

30 *Id.*

31 *Barrett v. Comm'r*, T.C. Memo. 2017-195.

IRS sent them a notice of deficiency, he did not offer any excuse for the late filing of the 2012 return.<sup>32</sup> The Tax Court found the taxpayers failed to establish reasonable cause for either of the late filings.<sup>33</sup>

### *Reliance on Agent Defense*

When a taxpayer relies on an agent to fulfill a known filing requirement, it does not relieve the taxpayer of the responsibility.<sup>34</sup> Taxpayers have a non-delegable duty to file a tax return on time.<sup>35</sup> In order for reliance on an agent to rise to the standard of reasonable cause for failing to fulfill the filing requirement, the taxpayer must make full disclosure of all relevant facts to the tax professional that he relies upon.<sup>36</sup> In other words, merely hiring a tax professional (*e.g.*, accountant, lawyer, or Enrolled Agent) to handle tax return filing is not enough to establish that the taxpayer used ordinary business care and prudence if there are facts that indicate otherwise.

In *Mazzei v. Commissioner*, the taxpayers entered into complex transactions marketed by the Western Growers Association, a trade association for farmers.<sup>37</sup> The transactions were designed to reduce taxes by routing funds from the Mazzeis' family business through foreign sales corporations and then into Roth Individual Retirement Accounts (IRAs) designed for this purpose.<sup>38</sup> Before entering into these transactions, the taxpayers presented the transaction paperwork to their personal accountant, Mr. Bedke, who approved their participation in the transaction.<sup>39</sup> Mr. Bedke had prepared the Mazzeis' tax returns for several years, had no connection with the Western Growers Association, and no expectation of profits from the taxpayers' transactions.<sup>40</sup> The Mazzeis did not, however, file Forms 5329, *Additional Taxes on Qualified Plans (Including IRAs) and Other Tax-Favored Accounts*, to report the transactions for each of the years at issue.

The Tax Court held that the taxpayers established reasonable cause for their failure to timely file the returns and failure to pay the amounts shown on those returns. The Tax Court applied the following three-part test from *Neonatology Associates, P.A. v. Commissioner*:<sup>41</sup>

Reliance on professional advice is reasonable and thus warrants reasonable cause abatement if:

- i. The advisor was a competent professional with sufficient expertise to justify reliance;
- ii. The taxpayer provided necessary and accurate information to the adviser; and
- iii. The taxpayer actually relied on the adviser's judgment in good faith.

The court found Mr. Bedke, a tax partner at an accounting firm where he had practiced for 29 years, was a competent professional with sufficient expertise to justify the Mazzeis' reliance. The Mazzeis

32 *Barrett v. Comm'r*, T.C. Memo. 2017-195.

33 *Id.*

34 The Supreme Court held in *U.S. v. Boyle* that reasonable cause may exist when a taxpayer relies on the erroneous advice of counsel concerning a question of law. To escape liability for the failure to file penalty, the taxpayer bears the heavy burden of proving both (1) that the failure did not result from 'willful neglect,' and (2) that the failure was 'due to reasonable cause.' 469 U.S. 241, 245, 250 (1985).

35 *U.S. v. Boyle*, 469 U.S. 241 (1985). The Court noted that "[i]t requires no special training or effort to ascertain a deadline and make sure that it is met." *Id.* at 252.

36 *Id.*

37 *Mazzei v. Comm'r*, 150 T.C. No. 7 (2018), *appeal docketed*, No. 18-72451 (9th Cir., Sept. 5, 2018).

38 *Id.*

39 *Id.*

40 *Id.*

41 *Neonatology Assocs., P.A. v. Comm'r*, 115 T.C. 43, 99 (2000); *aff'd*, 299 F.3d 221 (3d Cir. 2002).

had provided all the necessary transaction documents to Mr. Bedke.<sup>42</sup> Additionally, Mr. Bedke did not promote, participate in structuring, or profit from the transactions at issue.<sup>43</sup> Accordingly, the court found that the taxpayers reasonably relied on their accountant and therefore, were not liable for the failure to file and failure to pay penalties.<sup>44</sup>

### *Electronic Filing Errors Defense*

In several cases, taxpayers argued they had reasonable cause for failure to file their tax returns due to alleged malfunctions in their tax return electronic filing software. The courts uniformly rejected this defense.<sup>45</sup>

In *Spottiswood v. United States*, married taxpayers attempted to file their joint income tax return electronically using TurboTax software.<sup>46</sup> The IRS rejected taxpayers' return because the social security number and last name of a dependent on the return did not match the IRS's records.<sup>47</sup> TurboTax informed the taxpayers of the electronic filing rejection on or about the same day that they filed the return. However, the taxpayers did not check the email account associated with their TurboTax account, nor did they use the "check e-file status" TurboTax screen to confirm the IRS had accepted their return until many months later.<sup>48</sup> As a result, the court held that the taxpayers failed to establish reasonable cause for failing to file a return.<sup>49</sup>

Circumstances suggesting reasonable cause are typically outside the taxpayer's control.<sup>50</sup> In *Haynes v. United States*, taxpayers argued that the failure of the tax software to notify them when the IRS rejected their return was a circumstance beyond their control.<sup>51</sup> The court rejected this argument, holding that "an alleged software failure does not rise to the level of the Supreme Court's definition of a circumstance beyond Plaintiffs' control—disability, infirmity, objective incapacity—in *Boyle*."<sup>52</sup> Furthermore, the court noted that taxpayers had the option of filing their tax return on paper, electronically, or through any number of tax return preparers.<sup>53</sup> The court was careful in distinguishing cases in which reasonable cause may exist when taxpayers rely on erroneous advice of counsel on a question of law.<sup>54</sup> Accordingly, while it may have been reasonable for the taxpayers to retain an expert accountant to electronically file their return, their decision to do so does not rise to reasonable cause for the abatement of late-filing penalties. This case had generated much interest in the tax practitioner community.<sup>55</sup> On appeal, the Fifth Circuit vacated the judgment and remanded the case back to the district court, holding that it was

42 *Mazzei v. Comm'r*, 150 T.C. No. 7 (2018), *appeal docketed*, No. 18-72451 (9th Cir., Sept. 5, 2018).

43 *Id.*

44 *Id.*

45 See, e.g., *Spottiswood v. U.S.*, 121 A.F.T.R.2d (RIA) 1595 (N.D. Cal. 2018), *appeal docketed*, No. 18-16103 (9th Cir. June 14, 2018); *Haynes v. U.S.*, 119 A.F.T.R.2d (RIA) 2202 (W.D. Tex. 2017), *vacated and remanded*, No. 17-50816 (5th Cir. Jan. 29, 2019).

46 *Spottiswood v. U.S.*, 121 A.F.T.R.2d (RIA) 1595 (N.D. Cal. 2018), *appeal docketed*, No. 18-16103 (9th Cir. June 14, 2018).

47 *Id.*

48 *Id.*

49 *Id.*

50 *McMahan v. Comm'r*, 114 F.3d 366, 369 (2d Cir. 1997) (citation omitted), *aff'g* T.C. Memo. 1995-547.

51 *Haynes v. U.S.*, 119 A.F.T.R.2d (RIA) 2202 (W.D. Tex. 2017), *vacated and remanded*, No. 17-50816 (5th Cir. Jan. 29, 2019).

52 *Haynes v. U.S.*, 119 A.F.T.R.2d (RIA) 2202, 2017 U.S. Dist. LEXIS 106252, at \*27-28 (W.D. Tex. 2017) (citing *U.S. v. Boyle*, 469 U.S. 241, 250 (1985)), *vacated and remanded*, No. 17-50816 (5th Cir. Jan. 29, 2019).

53 *Haynes v. U.S.*, 119 A.F.T.R.2d (RIA) 2202 (W.D. Tex. 2017), *vacated and remanded*, No. 17-50816 (5th Cir. Jan. 29, 2019).

54 *Id.*

55 See <http://procedurallytaxing.com/delinquency-penalties-boyle-in-the-age-of-e-filing/> (last visited Sept. 4, 2018). The American College of Tax Counsel has filed an *amicus brief* in support of the taxpayers.

not yet necessary to consider whether an exception to the Boyle standard should be created for taxpayers who e-file.<sup>56</sup>

### Failure to Pay an Amount Shown Penalty

The failure to pay penalty is based on the amount shown on the tax return. If the taxpayer did not file a tax return, the IRS can only assess the IRC § 6651(a)(2) penalty if it has introduced a Substitute for Return (SFR) that satisfies the requirements of IRC § 6020(b). During litigation involving an SFR, if the IRS cannot produce the SFR, it fails to meet its burden of production under IRC § 7491 and the taxpayer can avoid a failure to pay penalty.<sup>57</sup>

As with the failure to file penalty, raising a reasonable cause defense to the failure to pay penalty requires that the taxpayer show that she exercised ordinary business care and prudence in the payment of her tax liabilities, but nevertheless was either unable to timely pay the tax or would suffer undue hardship if the payment was made on time.<sup>58</sup> Unsurprisingly, taxpayers often use medical illness or reliance on an agent as the basis for establishing reasonable cause to avoid the failure to pay penalty under IRC § 6651(a)(2), as they do for the failure to file penalty under IRC § 6651(a)(1).

In *Dykstra v. Commissioner*, the taxpayer filed her 2005 return late.<sup>59</sup> The taxpayer testified she became overwhelmed by work and had retained her longtime accountant, who did not prioritize her return.<sup>60</sup> When faced with the stress of the 2007 financial crisis, particularly given her job in real estate, the taxpayer said her delinquent tax returns started accumulating.<sup>61</sup> The taxpayer ultimately hired a new accountant and filed all of her overdue returns; however, the court did not excuse her failure to file her returns and pay the additions to tax.<sup>62</sup> The Tax Court acknowledged the difficult time the taxpayer endured, but held that her explanation did not demonstrate that she exercised ordinary care and prudence in meeting her obligations.<sup>63</sup> As a result, the court sustained the IRS's determinations as to the additions to tax.<sup>64</sup>

In contrast, the taxpayer in *Emery Celli Cuti Brinckerhoff & Abady, P.C. v. Commissioner*, a law firm, established reasonable cause for its failure to file an employment tax return and failure to pay an amount shown.<sup>65</sup> The law firm, Emery, Celli, Brinckerhoff & Abady, LLP (Emery LLP), paid wages to its employees during the first quarter of 1999 and made employment tax deposits for each of them.<sup>66</sup> However, the law firm's payroll service provider that made the employment tax deposits deposited them erroneously under Emery LLP's employer identification number (EIN).<sup>67</sup> The Tax Court held that the

56 *Haynes v. U.S.*, vacated and remanded, No. 17-50816 (5th Cir. Jan. 29, 2019).

57 See *Wheeler v. Comm'r*, 127 T.C. 200, 210 (2006), *aff'd*, 521 F.3d 1289 (10th Cir. 2008).

58 See Treas. Reg. § 301.6651-1(c)(1).

59 *Dykstra v. Comm'r*, T.C. Memo. 2017-156.

60 *Id.*

61 *Id.*

62 *Id.*

63 *Id.*

64 *Dykstra v. Comm'r*, T.C. Memo. 2017-156.

65 *Emery Celli Cuti Brinckerhoff & Abady, P.C. v. Comm'r*, T.C. Memo. 2018-55.

66 *Id.*

67 *Id.*

company nevertheless exercised ordinary business care and prudence.<sup>68</sup> The paramount factor was a timely filed return and timely deposited employment taxes, albeit under an incorrect EIN.<sup>69</sup>

### Estimated Tax Penalty

Courts routinely found taxpayers liable for the IRC § 6654 estimated tax penalty when the IRS proved the taxpayer:

- i. Had a tax liability;
- ii. Had no withholding credits;
- iii. Made no estimated tax payments for that year; and
- iv. Offered no evidence to refute the IRS.

The IRS has the burden under IRC § 7491(c) to produce evidence that IRC § 6654(d)(1)(B) requires an annual payment from the taxpayer.

The estimated tax penalty is calculated with reference to four required installment payments of the taxpayer's estimated tax liability.<sup>70</sup> Each required installment is equal to 25 percent of the taxpayer's "required annual payment."<sup>71</sup> The required annual payment equals the lesser of: (i) 90 percent of the tax shown on the individual's return for that year (or, if no return is filed, 90 percent of the individual's tax for such year); or (ii) if the individual filed a valid return for the immediately preceding tax year, 100 percent of the tax shown on that return (this can increase to 110 percent based on adjusted gross income).<sup>72</sup> The IRS has the burden to produce evidence that IRC § 6654(d)(1)(B) requires an annual payment from the taxpayer.<sup>73</sup> If a taxpayer did not pay enough tax throughout the year, either through withholding or by making estimated tax payments, the IRS will assess a penalty for underpayment of estimated tax.<sup>74</sup>

In *Plato v. Commissioner*, the Tax Court held that the IRS did not meet its burden of showing the taxpayer had an annual required payment.<sup>75</sup> Mr. Plato, the taxpayer, had recently separated from his wife and filed a married filing separately return for the first time during the tax year. If taxpayers, like Mr. Plato, who filed a married filing jointly return for the prior year, file married filing separately returns, the regulations provide a special rule for calculating their required annual payments.<sup>76</sup> Under

68 *Emery Celli Cuti Brinckerhoff & Abady, P.C. v. Comm'r*, T.C. Memo. 2018-55.

69 *Id.*

70 IRC § 6654(c)-(d).

71 IRC § 6654(d)(1)(A).

72 IRC § 6654(d)(1)(B). There are special rules on calculating the required annual payment for taxpayers who filed a married filing jointly return for the prior tax year but are filing married filing separately for the current year, and for taxpayers whose adjusted gross income exceed a certain amount. For instance, if a taxpayer's AGI for 2017 was more than \$150,000 (\$75,000 if the taxpayer's filing status for 2018 is married filing a separate return), the taxpayer must substitute 110 percent for 100 percent. See IRC § 6654(d)(1)(C) and Treas. Reg. § 1.6654-2(e).

73 IRC § 7491(c).

74 The law allows the IRS to waive the penalty if: (1) a taxpayer did not make a required payment because of a casualty event, disaster, or other unusual circumstance and it would be inequitable to impose the penalty, or (2) a taxpayer retired (after reaching age 62) or became disabled during the tax year or in the preceding tax year for which you should have made estimated payments, and the underpayment was due to reasonable cause and not willful neglect. IRC § 6654(e)(3).

75 *Plato v. Comm'r*, T.C. Memo. 2018-7.

76 Treas. Reg. § 1.6654-2(e).

Treasury Regulation § 1.6654-2(e), the taxpayers' prior year tax liabilities are the taxes the spouses would be liable for, if they each filed a married filing separately return for that year.<sup>77</sup>

However, the community property law where Mr. Plato and his wife resided, required that any withholding payments had to be allocated when married spouses chose to file separately. Yet the IRS did not provide evidence of allocation of the adjusted gross income and tax per the return for the prior year between Mr. Plato and his wife. Consequently, although the Tax Court could calculate 90 percent of the taxpayer's tax in the current year under clause (i) of the penalty calculation, it was unable to calculate the number equal to 100 percent of the tax shown on the taxpayer's prior year return under clause (ii). The IRS had the burden to prove the amount of a required annual payment, and failed to carry its burden of production. Thus, the Tax Court did not sustain the estimated tax penalty.<sup>78</sup>

## CONCLUSION

Taxpayers prevailed in full in only five of 47 (nearly 11 percent) of the failure to file, failure to pay, and estimated tax penalty cases analyzed in this report. One taxpayer prevailed in part (two percent), meaning the IRS won nearly 87 percent of the cases. The number of cases, in which failure to file, failure to pay, and estimated tax penalties were at issue, decreased by almost 23 percent from last year, and the portion of cases where the taxpayer received at least some form of relief decreased from 20 percent to 13 percent. This decline may be attributed to the general decline in tax litigation in recent years.<sup>79</sup>

It is critical that IRS employees thoroughly analyze all facts and circumstances of a case when assessing reasonable cause claims rather than solely relying on the Reasonable Cause Assistant (RCA) software,<sup>80</sup> which is designed to help IRS employees make fair and consistent abatement determinations.<sup>81</sup> The RCA program allows IRS employees to override the results in certain circumstances, but employees must understand the definition of reasonable cause to apply the override.<sup>82</sup> Thus, a close review by an employee is essential to ensure that the failure to file penalty or the failure to pay penalty is imposed appropriately. Additionally, it is imperative that taxpayers verify the IRS has accepted their electronically filed return. Although electronic filing instead of mailing has some benefits, to include receiving a refund much quicker, the IRS can reject an electronically-filed return for a wide range of reasons. In those cases, taxpayers will need to figure out the error and try filing again.

<sup>77</sup> Treas. Reg. § 1.6654-2(e)(1)-(2), Example (1).

<sup>78</sup> *Plato v. Comm'r*, T.C. Memo. 2018-7.

<sup>79</sup> David McAfee, *Tax Court: Tax Court Caseload Drops as Enforcement Lags: Former Chief Judge* 142 DTR 8 (July 24, 2018). Former Chief Judge L. Paige Marvel noted that the Tax Court's inventory is dropping, due in part to lax enforcement. This trend could correlate with the fewer litigated lien cases in the U.S. District Courts. See also Most Litigated Issue: *Civil Actions to Enforce Federal Tax Liens or to Subject Property to Payment of Tax Under IRC § 7403*, *infra*.

<sup>80</sup> The Reasonable Cause Assistant (RCA) can only consider failure to file or failure to pay penalties for certain individual tax returns.

<sup>81</sup> National Taxpayer Advocate 2010 Annual Report to Congress 198 (Most Serious Problem: *The IRS's Over-Reliance on Its "Reasonable Cause Assistant" Leads to Inaccurate Penalty Abatement Determinations*). See also IRS, *Reasonable Cause Assistant (RCA) Usability Test Final Report Summary* 4 (May 28, 2010). The test showed that employees using the RCA determined penalty abatement requests correctly in only 45 percent of the cases. An even more disturbing finding was that all of the employees in the study believed they were making correct legal determinations based on reasonable cause.

<sup>82</sup> Internal Revenue Manual 20.1.1.3.6.10(3) (Nov. 25, 2011) ("[F]air and consistent application of penalties requires employees to make a final penalty relief determination consistent with the RCA conclusion ... [U]nderstanding that the individual facts and circumstances vary for each case and that there may be unique facts and circumstances in certain cases that RCA cannot consider, an 'override (abort)' function is available in RCA.")

As previously recommended by the National Taxpayer Advocate, Congress should amend IRC § 6404 to authorize the Secretary of the Treasury to grant a one-time abatement of the failure to file penalty (IRC § 6651(a)(1)) and failure to pay penalty (IRC § 6651(a)(2)) for first-time filers and taxpayers who have a consistent history of compliance, where no countervailing factors are present.<sup>83</sup> Finally, taxpayers are encouraged to review their W-4 forms and make any adjustments if they have too little withheld from their paychecks. In a July 2018 report, the Government Accountability Office estimated that 21 percent—or 30 million taxpayers—will be under withheld and need to make up the difference when they file their 2018 tax return.<sup>84</sup> In response, the IRS will not apply estimated tax penalties to underpayments of tax as a result of the Tax Cuts and Jobs Act (TCJA). The National Taxpayer Advocate applauds these efforts by the IRS, but has noted there is no information on how the IRS will determine that an underpayment is pursuant to the TCJA nor how it will otherwise apply the policy. In sum, to promote voluntary compliance and to uphold a taxpayer's *right to a fair and just tax system* and the *right to pay no more than the correct amount of tax*, the facts of taxpayers' individual cases must be carefully considered.

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83 National Taxpayer Advocate 2001 Annual Report to Congress 188.

84 See Government Accountability Office (GAO), GAO-18-548, *Federal Tax Withholding: Treasury and IRS Should Document the Roles and Responsibilities for Updating Annual Withholding Tables* (July 2018), <https://www.gao.gov/assets/700/693582.pdf>.

MLI  
#7**Civil Actions to Enforce Federal Tax Liens or to Subject Property to Payment of Tax Under IRC § 7403****SUMMARY**

Internal Revenue Code (IRC) § 7403 authorizes the United States to file a civil action in U.S. District Court against a taxpayer who has refused or neglected to pay any tax, to enforce a federal tax lien, or to subject any of the delinquent taxpayer's property and rights to property to the payment of tax. Unlike cases in other Most Litigated Issues, lien enforcement cases are always initiated by the government through the Department of Justice rather than the taxpayer. We identified 39 opinions issued between June 1, 2017, and May 31, 2018, that involved civil actions to enforce liens under IRC § 7403. The IRS prevailed in 37 of these cases, one case was remanded for additional proceedings, and one case resulted in a split decision. The 39 cases identified for this reporting period represent a 35 percent decrease from the previous year.

**TAXPAYER RIGHT(S) IMPACTED<sup>1</sup>**

- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to Finality*
- *The Right to Privacy*
- *The Right to a Fair and Just Tax System*

**PRESENT LAW**

If a taxpayer is delinquent in satisfying a federal tax liability, IRC § 7403 authorizes the United States to initiate a civil action in the appropriate United States District Court to enforce its federal tax lien over the liability or to subject any of the delinquent taxpayer's property, right, title, or interest in property to the payment of that liability.<sup>2</sup> When the United States files a complaint in district court to enforce a lien under IRC § 7403, it is required to name all parties having liens on, or otherwise claiming interest in the relevant property, as parties to the action.<sup>3</sup> The law of the state where the property is located determines the nature of a taxpayer's legal interest in the property.<sup>4</sup> However, once it is determined that the taxpayer has an interest under state law in the property, federal law controls whether the property is exempt from attachment of the lien.<sup>5</sup>

IRC § 7403(c) directs the court to “finally determine the merits of all claims to and liens upon the property,” and if the United States proves a claim or interest, the court may order an officer of the court to sell the property and distribute the proceeds in accordance with the court's findings with respect to the interests of the parties, including the United States' claim for the delinquent tax liability.<sup>6</sup>

1 See Taxpayer Bill of Rights (TBOR), <https://taxpayeradvocate.irs.gov/taxpayer-rights>. The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 IRC § 7403(a); Treas. Reg. § 301.7403-1(a).

3 IRC § 7403(b).

4 *U.S. v. Nat'l Bank of Commerce*, 472 U.S. 713, 722 (1985).

5 *U.S. v. Rodgers*, 461 U.S. 677, 683 (1983).

6 IRC § 7403(c).

Ordering the sale of a taxpayer's property is a powerful collection tool and directly affects any parties who have an interest in the property subject to sale. Based on the Supreme Court case *United States v. Rodgers*, however, the court is not required to authorize a forced sale and may exercise limited equitable discretion. Under *Rodgers*, when a forced sale involves the interests of a third party who does not have a federal tax debt, the court should consider the following four factors when determining whether the property should be sold:

1. The extent to which the government's financial interests would be prejudiced if they were relegated to a forced sale of the partial interest of the delinquent taxpayer;
2. Whether the innocent third party with a separate interest in the property, in the normal course of events, has a legally recognized expectation that the property would not be subject to a forced sale by the delinquent taxpayer or taxpayer's creditors;
3. The likely prejudice to the third party in personal dislocation costs and inadequate compensation; and
4. The relative character and value of the non-liable and liable interests held in the property.<sup>7</sup>

In cases where the United States holds a first priority lien, it may offer bids at the sale of the foreclosed property up to an amount equal to the amount of the lien, plus selling expenses.<sup>8</sup> If a foreclosure action is initiated by another creditor, IRC § 7403(c) authorizes the United States to intervene in the action to assert any interests from a lien on the property subject to such action.<sup>9</sup>

If the case was initiated in a state court, the United States may remove the case to a U.S. District Court.<sup>10</sup> However, if the foreclosure action is adjudicated under state court proceedings, federal tax liens that are junior to other creditors may be effectively removed, even if the United States is not a party to the proceeding.<sup>11</sup> While the action is pending, the court may appoint a receiver empowered in equity to preserve and operate the property prior to the sale, upon the government's certification that it is in the public interest.<sup>12</sup>

The IRS must make the initial referral of a case to the Department of Justice (DOJ) and request the DOJ to file the foreclosure suit.<sup>13</sup> The Internal Revenue Manual (IRM) provides procedures with respect to what actions the IRS must take before requesting that the DOJ commence a foreclosure proceeding.<sup>14</sup> With respect to a recommendation to foreclose on a taxpayer's principal residence, there

<sup>7</sup> *Rodgers*, 461 U.S. at 709-11.

<sup>8</sup> IRC § 7403(c).

<sup>9</sup> However, if the application of the United States to intervene is denied, the adjudication will have no effect upon the federal tax lien on the property. IRC § 7424. Under 28 U.S.C. § 2410, the United States may be named a party in any civil action or suit in any district court, or in any state court having jurisdiction of the subject matter.

<sup>10</sup> 28 U.S.C. § 1444.

<sup>11</sup> *U.S. v. Brosnan*, 363 U.S. 237 (1960).

<sup>12</sup> IRC §§ 7403(d) and 7402(a).

<sup>13</sup> IRC § 7401. The IRS prepares a suit recommendation package, and then the IRS Office of Chief Counsel reviews it, and if it agrees sends a letter to the Department of Justice (DOJ) asking the DOJ to commence the litigation. Chief Counsel Directives Manual, 34.6.1.1.1, *Steps Prior to Litigation* (Oct. 7, 2015).

<sup>14</sup> Internal Revenue Manual (IRM) 5.17.4.8, *Foreclosure of Federal Tax Lien* (Aug. 1, 2010).

are special procedures that the IRS must follow before initiating a referral to DOJ.<sup>15</sup> The IRM instructs the IRS to refer a case to DOJ to pursue a suit to foreclose only when there are no other reasonable administrative remedies and the foreclosure would not create or exasperate hardship issues for the taxpayer.<sup>16</sup> Under IRM procedures, the IRS is required to take the following actions and describe the results in a suit recommendation narrative that accompanies the referral:

- Attempt to personally contact the taxpayer and inform them that a suit to foreclose the tax lien on the principal residence is the next planned action;
- Attempt to identify the occupants of the principal residence;
- Attempt to discuss administrative remedies with the taxpayer such as an offer in compromise (including Effective Tax Administration offer or an offer with consideration of special circumstances), when appropriate;
- Advise the taxpayer about TAS, provide Form 911, *Request for Taxpayer Advocate Assistance (and Application for Taxpayer Assistance Order)*, and explain its provisions;<sup>17</sup> and
- Include a summary statement in the case history, along with the information on the taxpayer and the occupants of the principal residence, including children.<sup>18</sup>

## ANALYSIS OF LITIGATED CASES

We reviewed 39 opinions issued between June 1, 2017, and May 31, 2018, that involved civil actions to enforce federal tax liens. Table 7 in Appendix 3 contains a detailed list of those cases. Of the 39 cases, taxpayers appeared *pro se* (without counsel) in 26 cases, and were represented in the remaining 13 cases. The IRS prevailed in all cases brought against taxpayers proceeding *pro se*.

### Foreclosure of Tax Liens Where Non-Liable Taxpayer Had Interest in Property

In *United States v. Wilhite*, the government filed suit to collect long-outstanding restitution obligations by foreclosing on a company owned and controlled in part by the taxpayer.<sup>19</sup> The taxpayer's restitution obligations stemmed from years of unpaid tax from fraudulent transfers, creating an enforceable federal

15 IRM 5.17.4.8.2.5, *Lien Foreclosure on a Principal Residence* (Jan. 8, 2016). In 2012, TAS issued an Advocacy Proposal to the IRS recommending that the IRS consider the negative impact on the taxpayer of a suit to foreclose on a principal residence prior to forwarding the case to the DOJ. TAS, *Memorandum for Director, Collection Policy* (Aug. 20, 2012). The National Taxpayer Advocate followed this advocacy proposal with a legislative recommendation that Congress amend IRC § 7403 to require that the IRS, before recommending that DOJ file a suit to foreclose, first determine whether the taxpayer's other property or rights to property, if sold, are insufficient to pay the amount due, and that the foreclosure and sale of the residence will not create an economic hardship due to the financial condition of the taxpayer. National Taxpayer Advocate 2012 Annual Report to Congress 537-43 (Legislative Recommendation: *Amend IRC § 7403 to Provide Taxpayer Protections Before Lien Foreclosure Suits on Principal Residences*). Following this recommendation, TAS worked closely with the IRS to develop an Internal Guidance Memorandum (IGM), which was incorporated into IRM 5.17.4.8.2.5 on March 30, 2015, to address the issues raised by the National Taxpayer Advocate. Prior to the release of the IGM in 2013, the IRM provisions relating to referring cases under IRC § 6334(e)(1) required the IRS to consider who is living in the residence in determining whether referral to DOJ was appropriate but the procedures under IRC § 7403 did not.

16 IRM 5.17.4.8.2.5, *Lien Foreclosure on a Principal Residence* (Jan. 8, 2016); See Most Serious Problem: *Economic Hardship: The IRS Does Not Proactively Use Internal Data to Identify Taxpayers at Risk of Economic Hardship Throughout the Collection Process*, *supra*.

17 If the taxpayer indicates that the planned foreclosure of the principal residence would create a hardship, the Revenue Officer (RO) will assist the taxpayer with the preparation of Form 911 and forward the form to the local TAS office if the RO cannot or will not provide the requested relief.

18 IRM 5.17.4.8.2.5, *Lien Foreclosure on a Principal Residence* (Jan. 8, 2016).

19 *U.S. v. Wilhite*, 2018 U.S. Dist. LEXIS 42318 (D. Colo., Mar. 14, 2018), *appeal docketed*, No. 18-1090 (10th Cir., Mar. 15, 2018).

tax lien which attached to the taxpayer's property, including his ownership interest in the company.<sup>20</sup> The taxpayer and his wife, a non-liable third party, jointly owned the company with an equitable interest of 73.9 percent and 26.1 percent, respectively.<sup>21</sup>

Having found the federal tax lien valid and that it attached to the taxpayer's equitable interest in the company, the court analyzed the *Rodgers* factors described above to determine the appropriateness of a forced sale of the company in its entirety, rather than a sale of just the portion owned by the taxpayer.

With respect to the first *Rodgers* factor, the court concluded that the partial sale of the company would prejudice the government's financial interest because no potential buyer would be likely to pay fair market value for a majority interest in the taxpayer's family-owned company, especially when one of the family members would remain heavily involved in the business.<sup>22</sup> Furthermore, the court noted that selling the taxpayer's interest at discounted price or not selling it at all would impede the government's right to collect on the taxpayer's outstanding restitution obligations.<sup>23</sup> Thus, the court found this factor weighed in favor of a sale of the company in its entirety.

With respect to the second *Rodgers* factor, the non-liable party's legally recognized expectation that the property would not be subject to a forced sale, the court determined that any belief held by the wife that the property would not be subject to a forced sale was unfounded. The court reasoned that the taxpayer's wife had knowledge of the taxpayer's outstanding tax liability from the point when the government publicly recorded the lien in 2001.<sup>24</sup> The court also noted that the taxpayer's wife was involved in activities to hinder and defraud the government from collecting the outstanding liability by starting the company and hiding the taxpayer's involvement in the company.<sup>25</sup> With such knowledge and involvement, the court concluded that the taxpayer's wife failed to present any legally cognizable expectation that her ownership interest would be protected from the sale.<sup>26</sup> Therefore, this factor also weighed in favor of a sale.

In addressing the third *Rodgers* factor, the likely prejudice to the third party in personal dislocation costs and inadequate compensation, the court recognized that the taxpayer's wife may suffer some prejudice. However, the court concluded that government's right to force the sale and collect the taxpayer's outstanding debt outweighed the minimal burden the wife would experience. Even if a sale would affect the wife's monthly income, she would be given the opportunity to make a bid at the foreclosure sale to protect her interests, or in the alternative, be adequately compensated after the sale in proportion to her interest in the company.<sup>27</sup> Thus, this factor still weighed in favor of a sale.

Finally, with respect to the fourth *Rodgers* factor, the relative character and value of the liable and non-liable party's possessory interest in the subject property, the court noted that the taxpayer was the true

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20 Taxpayer's restitution obligation imposed under the *Mandatory Victim's Restitution Act (MVRA)* created a federal lien. See 18 U.S.C. §§ 3663A; 3613. In this case, the government's action to enforce its lien is "in every real sense a proceeding in court to collect a tax." *Willhite*, 2018 U.S. Dist. LEXIS 42318, at \*3. The court previously found that under Colorado law, the taxpayer had a 73.9 percent ownership interest in the company, which was subject to the federal tax lien.

21 *Id.* at \*2.

22 *Id.* at \*9-10.

23 *Id.* at \*10.

24 *Id.* at \*10-11.

25 *Id.* at \*11.

26 *Id.*

27 *Willhite*, 2018 U.S. Dist. LEXIS 42318, at \*11-12. The court determined that government holds a first priority lien superior to other creditors.

beneficial owner, despite his wife's minority interest, because he controlled and operated the company.<sup>28</sup> Considering all the factors presented in this case, the court held that a forced sale of the entire company was appropriate.<sup>29</sup>

### Preservation of Federal Tax Lien Against Subsequent Purchasers of Property

If a person who owes a federal tax liability fails to pay after the IRS sends notice and demand for payment, then a lien arises in favor of the government upon all property or rights to property, whether real or personal, belonging to that person.<sup>30</sup> The Supreme Court has broadly interpreted this provision to apply to every interest the taxpayer may have in real property.<sup>31</sup> A federal tax lien arises automatically at the time an assessment is made, and continues until the assessed tax liability is satisfied or becomes unenforceable by reason of lapse of time.<sup>32</sup> In most cases, the “transfer of property subsequent to the attachment of the lien does not affect the lien,” which remains attached to the property regardless of ownership.<sup>33</sup> However, a lien will not be enforced against a subsequent purchaser of property if the purchaser acquires an interest without notice.<sup>34</sup> Notice includes “constructive notice,” which is determined by asking whether a reasonable and diligent inspection of the relevant local index would reveal the existence of the lien.<sup>35</sup>

In *United States v. Z Investment Properties, LLC*, the government sought to satisfy the federal tax liabilities owed by a taxpayer by enforcing a federal tax lien against a parcel of real property (hereinafter “the Property”) at that point owned by a third party.<sup>36</sup> Carroll Raines, the taxpayer, initially owned the Property with his wife, becoming the sole owner upon her death. In 2007, the IRS notified the taxpayer it had made an assessment against him for unpaid federal income taxes, penalties, and interest. In August 2010, the taxpayer's liabilities remained unpaid and the IRS filed a notice of federal tax lien in the county where the taxpayer owned the Property, which indicated that federal tax liens attached to all property and rights to property belonging to the taxpayer, including the Property. The notice filed by the IRS incorrectly spelled the taxpayer's first name, listing it as “Carrol” V. Raines instead of “Carroll” V. Raines.<sup>37</sup>

The taxpayer died intestate in 2009, and his son recorded an Affidavit of Heirship over the Property in November 2010. That month, all six of the taxpayer's heirs conveyed their interests in the Property through a quitclaim deed of trust to a land trust, one of the third-party defendants in this case. A search of the taxpayer's exact first and last name on the local recorder's electronic database would not have revealed the federal tax liens, but did display potential aliases, including “C V Raines” and “Carol

28 *Willhite*, 2018 U.S. Dist. LEXIS 42318, at \*12.

29 The court also granted the government's request under IRC § 7403(d) for a receiver noting that the government had made a prima facie showing that a substantial tax liability exists and that the government's collection efforts may be jeopardized if a receiver is not appointed. *Id.* at \*15.

30 IRC § 6321.

31 *U.S. v. Nat'l Bank of Commerce*, 472 U.S. 713, 719-20 (1985).

32 IRC § 6322. The lien remains in effect until the limitations period for collection of the tax expires, which is generally 10 years from the assessment date. See IRC § 6502.

33 *U.S. v. Bess*, 357 U.S. 51, 57 (1958).

34 IRC § 6323(a), (h)(6).

35 See *In re Spearing Tool & Mfg. Co.*, 412 F.3d 653, 656 (6th Cir. 2005) (internal quotation marks omitted); see also *Tony Thornton Auction Serv., Inc. v. U.S.*, 791 F.2d 635, 639 (8th Cir. 1986)

36 *U.S. v. Z Investment Properties, LLC.*, 121 A.F.T.R.2d (RIA) 1317 (N.D. Ill. 2018), *appeal docketed*, No. 18-1915 (7th Cir. Apr. 26, 2018).

37 *Z Investment Properties, LLC.*, 121 A.F.T.R.2d (RIA) at \*1.

Raines.”<sup>38</sup> A search for all last names beginning with “Raines” and first names beginning with “C” also would have revealed the existence of the liens, as would a “Sounds Like” search using the taxpayer’s first and last names.<sup>39</sup>

The court held that the minor misspelling in the notice of federal tax lien did not bar the enforcement of the lien. To find otherwise, the court stated, would impose a requirement that tax liens identify a taxpayer with absolute precision, which would unduly burden the government’s tax collection ability.<sup>40</sup> The court emphasized the availability of multiple, easily-executed and low-cost search options available on the local recorder’s website raised the standard for what constitutes a “reasonable” search.<sup>41</sup> The court also noted that the exact search of the taxpayer’s name revealed the alias, “Carol” V. Raines, actually used on the Notice of Federal Tax Liens. In such circumstances, the court held that “a reasonable search demands that the searcher act upon the notice of aliases provided by that initial search, for example by using one of the other, flexible search functions” available on the local reporter.<sup>42</sup> The court found the lien valid and enforceable. Finally, the court allowed the government to enforce the federal tax lien against the Property and sell the Property free and clear of all rights, titles, claims, and interests of the parties. This case shows the power of a lien as a collection tool and highlights the importance for taxpayers to exercise caution when transferring title to real property.

### Foreclosure of Tax Liens Against Property Held by a Taxpayer’s Nominee or Alter Ego

The number of opinions that involved foreclosure of federal tax liens against property titled in the name of a taxpayer’s nominee or alter ego showed an increase over last year, with 23 cases in 2018, compared to 15 in 2017. A nominee is one “who holds bare legal title to property for the benefit of another.”<sup>43</sup> Courts typically look at the following factors to assess whether an entity, trust, or a third party is a nominee of a taxpayer:

- The nominee paid no or inadequate consideration;
- The property was placed in the name of the nominee in anticipation of the tax debt or litigation while the transferor retained control;
- There is a close relationship between the transferor and the nominee;
- The parties to the transfer failed to record the conveyance;
- The transferor retained possession (or control); and
- The transferor continues to enjoy the benefits of property.<sup>44</sup>

Courts have also noted that the government is not required to prove the existence of each factor, and that no single factor is determinative.<sup>45</sup> Of the nominee factors, the courts routinely attach greater weight and importance to the taxpayer’s control of the assets.<sup>46</sup>

38 *Z Investment Properties, LLC.*, 121 A.F.T.R.2d (RIA) at \*2.

39 *Id.*

40 *Id.* at \*6.

41 *Id.*

42 *Id.*

43 Nominee, BLACK’S LAW DICTIONARY (10th ed. 2014). See also *U.S. v. Beeman*, 108 A.F.T.R.2d (RIA) 5074 (W.D. Penn. 2011).

44 See, e.g., *U.S. v. Balice*, 120 A.F.T.R.2d (RIA) 5444 (D. N.J. 2017), appeal docketed, No. 18-2528 (3d Cir. July 11, 2018). See also *U.S. v. Kraus*, 121 A.F.T.R.2d (RIA) 1323 (W.D. Wash. 2018), appeal docketed, No. 18-35516 (9th Cir. June 18, 2018).

45 *Dalton v. C.I.R.*, 682 F.3d 149, 158 (1st Cir. 2012).

46 *Shades Ridge Holding Co. v. U.S.*, 888 F.2d 725, 728; *U.S. v. Novotny*, 88 A.F.T.R.2d (RIA) 7194, at \*2 (D. Colo. 2001).

In *United States v. Wade*, the government filed suit to collect a taxpayer's outstanding federal tax liabilities for tax years 1993 through 2004 by foreclosing tax liens against taxpayer's interest in 19 real properties.<sup>47</sup> Taxpayer transferred his ownership interests in some of those properties to sham entities and trusts after he was convicted for tax evasion. In 2004, he transferred all other ownership interests to his wife by a way of gift.<sup>48</sup> In its motion for summary judgment, the government argued that the purported gift the taxpayer made to his wife was invalid and that the entities and trusts with ownership interests in the subject properties were mere nominees of the taxpayer.

The taxpayer had an outstanding tax liability and a valid tax assessment against him for tax years 1982 to 1984; however no formal tax assessment had been made for tax years 1993 to 2004 at the time of the alleged gift.<sup>49</sup> The taxpayer argued that the lien was invalid because the IRS had not made a formal tax assessment for the subject years, and he had made a proper gift of all his interests to his wife. However, even though there was no formal tax assessment, the court noted the taxpayer nevertheless still owed millions of dollars in unpaid federal income tax, making the government his creditor. Furthermore, the court noted that the taxpayer's transfer of his assets as a "gift" to his wife occurred after this liability had accrued, indicating the transfer was an intentional action to hinder, delay and defraud the United States.<sup>50</sup> Thus, the court found that the taxpayer had an outstanding tax liability for the tax years at issue and set aside the alleged gift to his wife as a fraudulent transfer under state law.

With respect to all the properties held by other alleged third-party entities and business trusts, the court applied the nominee factors mentioned above to determine whether the current legal titleholders were nominees of the delinquent taxpayer. First, the court noted that the taxpayer conceded that he transferred his interests in all properties to various entities and business trusts for inadequate consideration.<sup>51</sup> Second, the taxpayer transferred the properties after incurring an outstanding tax liability and intentionally and continuously failing to report his true taxable income.<sup>52</sup> The court stated that the taxpayer should have known that he could incur additional federal tax liability. Therefore, the first two factors clearly weighed in favor of government.

The court did not fully analyze the existence of the close relationship and the failure to record the conveyance, the third and fourth factors to determine nominee status. Instead, the court put greater focus on the fifth and sixth factors — the taxpayer's continued control and enjoyment of the benefits of the subject property. The court emphasized that the taxpayer clearly retained control of the property after the transfers because he continued to exercise the dominion over the properties and even continued operating an apartment rental business on them.<sup>53</sup> Moreover, the taxpayer continued to benefit from the property. He maintained a 50 percent ownership interest in the subject properties, as the partnership income distributions were still directed to the taxpayer. Based on all these factors, the court found that the legal title holders of the 19 properties were merely taxpayer's nominees, and thus, the government's liens validly attached to the subject properties.<sup>54</sup> The court granted the government's motion for summary judgment to enforce the tax lien against all 19 of the subject properties.

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47 *U.S. v. Wade*, 120 A.F.T.R.2d (RIA) 6004 (D. Utah 2017), *appeal docketed*, No. 18-4140 (10th Cir., Sept. 28, 2018).

48 *Id.* at \*6.

49 *Id.* at \*9-10.

50 *Id.* at \*13-14.

51 *Id.* at \*21.

52 *Id.* at \*22-23.

53 *Id.* at \*23.

54 *Id.*

In another nominee case, *Arlin Geophysical v. United States*, the Circuit Court of Appeals for the Tenth Circuit held that a federal tax lien could not be enforced against a property allegedly held by the taxpayer's nominee because the taxpayer and third party were not provided a meaningful opportunity to defend against the government's position.<sup>55</sup> The appellate court found the district court erred in basing its determination of the third party's nominee status on findings from a related dispute to which the taxpayer and third party were nonparties.<sup>56</sup> Thus, the appellate court vacated the judgment and the order of sale and remanded the case for further proceedings.<sup>57</sup>

## CONCLUSION

Lien enforcement cases continue to be a consistent source of litigation between the government and taxpayers. After peaking at 278 cases in 2012, the number of IRS lien enforcement cases received by the Department of Justice decreased to 215 in fiscal year (FY) 2013 and remained fairly constant in the years following.<sup>58</sup> In recent years, the number of cases received has fluctuated greatly, as the number of lien cases received increased by about five percent to 223 cases in FY 2017. However, in FY 2018, the number of cases received decreased to just 200, over a 10 percent decrease.<sup>59</sup> The 200 cases received is the lowest amount since FY 2011 and could explain why fewer lien cases were litigated during our reporting period. This trend is shown in Figure 3.7.1.<sup>60</sup>

55 *Arlin Geophysical v. U.S.*, 696 F. App'x 362 (10th Cir. 2017), *vacating and remanding* No. 2:08-cv-00414-DN (D. Utah Sept. 17, 2015). The court acknowledged that "[t]he fundamental requirement of due process is the opportunity to be heard 'at a meaningful time and in a meaningful manner.'" *Arlin*, 696 F. App'x 362, 368 (citing *Mathews v. Eldridge*, 424 U.S. 319, 333 (1976)). See also Nina E. Olson, 2010 Erwin N. Griswold Lecture Before the American College of Tax Counsel, *Taking the Bull by Its Horns: Some Thoughts on Constitutional Due Process in Tax Collection*, 63 *Tax Law* 227 (Spring 2010).

56 *Arlin Geophysical v. U.S.*, 696 F. App'x 362, 371.

57 *Id.* In this case, the taxpayer's subject property was sold at a judicial execution sale on May 24, 2017. While this case primarily involves the interests of the third party, we have chosen to include and highlight this case because it highlights how the rights of a taxpayer are frequently tied to the rights of a third party in nominee cases. On remand, the lower court granted the government's Motion for Summary Judgment, finding that the "undisputed material facts demonstrate that Fujilyte held title to the Properties as Worthen's nominee" and that "the United States is entitled to the funds on deposit in the court registry." *Arlin Geophysical & Laura Olson v. U.S.*, 2018 WL 4621748 (D. Utah 2018).

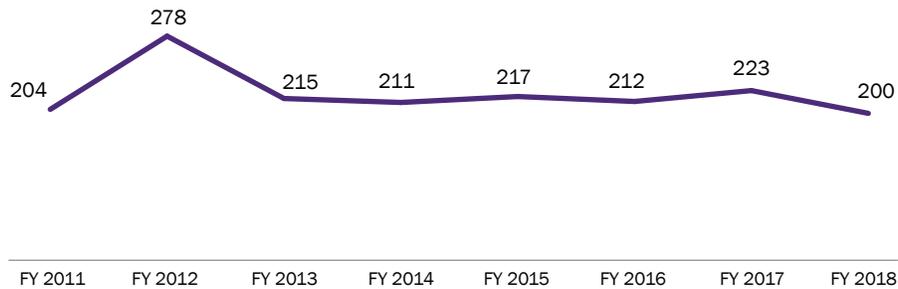
58 National Taxpayer Advocate 2016 Annual Report to Congress 496 (FY 2010 to FY 2016).

59 DOJ Tax Division, *Suits to Foreclose Tax Lien – Summary by Fiscal Year of Case Receipt* (Oct. 2018).

60 *Id.*

FIGURE 3.7.1

## Liens Cases Referred to U.S. Department of Justice



The reduction in cases received by the DOJ could be attributable in part to the IRS’s 2016 decision to refer fewer suits to foreclose tax liens on taxpayers undergoing a hardship or in situations where there are reasonable alternatives.<sup>61</sup> The National Taxpayer Advocate continues to urge Congress to adopt her 2012 recommendation to codify the approach used in the IRM so it cannot be reversed administratively.<sup>62</sup> In addition, the National Taxpayer Advocate recommends revising IRS guidance to instruct employees to more thoroughly consider the negative impact of foreclosing a principal residence.<sup>63</sup> The National Taxpayer Advocate suggests the use of an algorithm to better identify economic hardship cases early in the case selection process, which will help the IRS work with those taxpayers to find collection alternatives other than lien enforcement and foreclosure.<sup>64</sup>

Nominee cases represented 56 percent (23 out of 39) of lien cases seen in this reporting period. To address taxpayer burden and enhance the taxpayer *rights to privacy, to a fair and just tax system, and to appeal the IRS’s decision in an independent forum*, the National Taxpayer Advocate has also recommended that Congress amend IRC §§ 6320 and 6330 to extend Collection Due Process rights to “affected third parties,” known as nominees, alter egos, and transferees, who hold legal title to property subject to IRS collection actions.<sup>65</sup>

61 See IRM 5.17.4.8.2.5, *Lien Foreclosure on a Principal Residence* (Jan. 8, 2016).

62 National Taxpayer Advocate 2012 Annual Report to Congress 537-543 (Legislative Recommendation: *Amend IRC § 7403 to Provide Taxpayer Protections Before Lien Foreclosure Suits on Principal Residences*).

63 See National Taxpayer Advocate 2012 Annual Report to Congress 544-552 (Legislative Recommendation: *Amend IRC §§ 6320 and 6330 to Provide Collection Due Process Rights to Third Parties (Known as Nominees, Alter Egos, and Transferees) Holding Legal Title to Property Subject to IRS Collection Actions*).

64 See Most Serious Problem: *Economic Hardship: The IRS Does Not Proactively Use Internal Data to Identify Taxpayers at Risk of Economic Hardship Throughout the Collection Process*, *supra*.

65 National Taxpayer Advocate 2012 Annual Report to Congress 544-552 (Legislative Recommendation: *Amend IRC §§ 6320 and 6330 to Provide Collection Due Process Rights to Third Parties (Known as Nominees, Alter Egos, and Transferees) Holding Legal Title to Property Subject to IRS Collection Actions*).

MLI  
#8

## Charitable Contribution Deductions Under IRC § 170

## SUMMARY

Subject to certain limitations, taxpayers can take deductions from their adjusted gross incomes (AGIs) for contributions of cash or other property to or for the use of charitable organizations.<sup>1</sup> To take a charitable deduction, taxpayers must contribute to a qualifying organization<sup>2</sup> and substantiate contributions of \$250 or more.<sup>3</sup> Litigation generally occurred in this reporting cycle in the following three areas:

- Substantiation of the charitable contribution;
- Valuation of the charitable contribution; and
- Requirements for a qualified conservation easement.

TAS identified and reviewed 29 cases decided between June 1, 2017, and May 31, 2018, with charitable deductions as a contested issue. The IRS prevailed in 24 cases, taxpayers prevailed in four cases, and the remaining case resulted in a split decision. Taxpayers represented themselves (appearing *pro se*) in 10 of the 29 cases (34 percent), and the IRS prevailed fully in all 10 cases.

TAXPAYER RIGHTS IMPACTED<sup>4</sup>

- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to a Fair and Just Tax System*

## PRESENT LAW

Charitable contributions made within the taxable year are generally deductible by taxpayers, but in the case of individual taxpayers, a taxpayer must itemize deductions from income on his or her income tax return in order to deduct the contribution.<sup>5</sup> Transfers to charitable organizations are deductible only if they are contributions or gifts,<sup>6</sup> not payments for goods or services.<sup>7</sup> A contribution or gift will be allowed as a deduction under Internal Revenue Code (IRC) § 170 only if it is made “to” or “for the use of” a qualifying organization.<sup>8</sup>

1 Internal Revenue Code (IRC) § 170.

2 To claim a charitable contribution deduction, a taxpayer must establish that he or she made a gift to a qualified entity organized and operated exclusively for an exempt purpose, no part of the net earnings of which inures to the benefit of any private shareholder or individual. IRC § 170(c)(2).

3 IRC § 170(f)(8)(A).

4 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the IRC. See IRC § 7803(a)(3).

5 IRC §§ 63(d) and (e), 161, and 170(a).

6 The Supreme Court of the United States has defined “gift” as a transfer proceeding from a “detached and disinterested generosity.” *Comm’r v. Duberstein*, 363 U.S. 278, 285 (1960).

7 See also Treas. Reg. § 1.170A-1(g) (no deduction for contribution of services).

8 IRC § 170(c).

For individuals, charitable contribution deductions are generally limited to 60 percent of the taxpayer's contribution base (AGI computed without regard to any net operating loss carryback to the taxable year under IRC § 172).<sup>9</sup> However, subject to certain limitations, individual taxpayers can carry forward unused charitable contributions in excess of the 60 percent contribution base for up to five years.<sup>10</sup> Corporate charitable deductions are generally limited to ten percent of the taxpayer's taxable income and are also available for carryforward for up to five years, subject to limitation.<sup>11</sup> Taxpayers cannot deduct services that they offer to charitable organizations; however, incidental expenditures incurred while serving a charitable organization and not reimbursed, may constitute a deductible contribution.<sup>12</sup>

### Substantiation

For cash contributions, taxpayers must maintain receipts from the charitable organization, copies of cancelled checks, or other reliable records showing the name of the organization, the date, and the amount contributed.<sup>13</sup> Deductions for single charitable contributions of \$250 or more are disallowed in the absence of a contemporaneous written acknowledgement from the charitable organization.<sup>14</sup>

The donor is generally required to obtain the contemporaneous written acknowledgment no later than the date he or she files the return for the year in which the contribution is made, and it must include:

- The name of the organization;
- The amount of cash contribution;
- A description (but not the value) of non-cash contribution;
- A statement that no goods or services were provided by the organization in return for the contribution, if that was the case;
- A description and good faith estimate of the value of goods or services, if any, that an organization provided in return for the contribution; and
- A statement that goods or services, if any, that an organization provided in return for the contribution consisted entirely of intangible religious benefits, if that was the case.<sup>15</sup>

For each contribution of property other than money, taxpayers generally must maintain a receipt showing the name of the recipient, the date and location of the contribution, and a description of the property.<sup>16</sup> When taxpayers contribute property other than money, the amount of the allowable deduction is the fair market value of the property at the time of the contribution.<sup>17</sup> This general rule

9 This new 60 percent limitation was part of tax reform legislation that went into effect on January 1, 2018 and is an increase from the 50 percent prior limit. See Pub. L. No. 115-97, § 11023, 131 Stat. 2054, 2074-2075 (Dec. 22, 2017). In addition, the new legislation repealed the donee reporting provision contained in IRC § 170(f)(8)(D). See Pub. L. No. 115-97, § 13705, 131 Stat. 2054, 2169 (Dec. 22, 2017). We discussed a case involving this provision in our 2017 Annual Report. See National Taxpayer Advocate 2017 Annual Report to Congress 447-449 (discussing *15 West 17th Street LLC v. Comm'r*, 147 T.C. No. 19 (2016)).

10 IRC § 170(d)(1).

11 IRC § 170(b)(2) and (d)(2).

12 Treas. Reg. § 1.170A-1(g). Meal expenditures in conjunction with offering services to qualifying organizations are not deductible unless the expenditures are away from the taxpayer's home. *Id.* Likewise, travel expenses associated with contributions are not deductible if there is a significant element of personal pleasure involved with the travel. IRC § 170(j).

13 Treas. Reg. § 1.170A-13(a)(1).

14 IRC § 170(f)(8). See also Treas. Reg. § 1.170A-13(f).

15 IRS Pub. 1771, *Charitable Contributions Substantiation and Disclosure Requirements* (Rev. 3-2016).

16 Treas. Reg. §§ 1.170A-13(b)(1)(i) to (iii).

17 Treas. Reg. § 1.170A-1(c)(1).

is subject to certain exceptions that in some cases limit the deduction to the taxpayer's cost basis in the property.<sup>18</sup> For claimed contributions exceeding \$5,000, the taxpayer must obtain a qualified appraisal prepared by a qualified appraiser.<sup>19</sup>

## ANALYSIS OF LITIGATED CASES

TAS reviewed 29 decisions entered between June 1, 2017, and May 31, 2018, involving charitable contribution deductions claimed by taxpayers. Table 8 in Appendix 3 contains a detailed list of those cases. Of the 29 cases, the most common issues were: substantiation (or lack thereof) of the claimed contribution (18 cases), valuation of the property contributed (four cases), and contribution of an easement (nine cases).<sup>20</sup>

### Substantiation

Eighteen cases involved the substantiation of deductions for charitable contributions. When determining whether a claimed charitable contribution deduction is adequately substantiated, courts tend to follow a strict interpretation of IRC § 170. As noted earlier, deductions for single charitable contributions of \$250 or more are disallowed in the absence of a contemporaneous written acknowledgement from the charitable organization.<sup>21</sup>

In *RERI Holdings I, LLC v. Commissioner*, the taxpayer, a limited liability company, purchased the remainder interest of a property in Hawthorne, California in March 2002 for \$2,950,000.<sup>22</sup> In August 2003, the taxpayer assigned the remainder interest to the University of Michigan, a tax-exempt organization. On its 2003 Form 1065, *U.S. Return of Partnership Income*, the taxpayer claimed a charitable contribution deduction of \$33,019,000. The taxpayer attached a required Form 8283, *Noncash Charitable Contributions*, to its return that provided the date and manner of acquisition of the contributed remainder interest but, critical to this case, left blank the space for the "Donor's cost or other adjusted basis." The IRS initially reduced, then subsequently disallowed, the claimed charitable contribution deduction and asserted valuation misstatement penalties. The taxpayer challenged this disallowance and penalty assertion in Tax Court.

In addressing whether the taxpayer had properly substantiated its contribution of the remainder interest in the property and was entitled to claim a charitable contribution deduction, the court discussed the Deficit Reduction Act of 1984 (DEFRA).<sup>23</sup> The court noted that this legislation directed the Treasury Secretary to prescribe regulations under IRC § 170 that would require donors to meet stricter substantiation requirements to support claimed charitable contribution deductions. The court examined

18 Treas. Reg. § 1.170A-1(c)(1). Note that the deduction is reduced for certain contributions of ordinary income and capital gain property. See IRC § 170(e).

19 IRC § 170(f)(11)(C). "Qualified appraisal" and "qualified appraiser" are defined in IRC §§ 170(f)(11)(E)(i) and (ii), respectively. On July 27, 2018, after the close of our reporting period, the IRS released lengthy final regulations relating to IRC § 170. See T.D. 9836, 83 Fed. Reg. 36417-01 (July 30, 2018). These regulations provide guidance on cash, check, or other monetary gift substantiation requirements; noncash substantiation requirements; and new requirements for qualified appraisals and qualified appraisers. For example, the regulations provide that an email from a donee organization to a donor can qualify as a written communication and be used to substantiate a monetary contribution. However, a blank pledge card provided by a donee organization but filled out by a donor is insufficient substantiation.

20 Cases addressing more than one described issue are counted for each issue. For example, cases addressing the valuation of easements are counted once as a valuation issue case and again as a conservation easement issue case. As a result, the breakdown of case issues above will not add up to the total number of cases reviewed by TAS.

21 IRC § 170(f)(8). See also Treas. Reg. § 1.170A-13(f).

22 *RERI Holdings I, LLC v. Comm'r*, 149 T.C. No. 1 (2017), appeal docketed, No. 17-1266 (D.C. Cir. Dec. 18, 2017).

23 Deficit Reduction Act of 1984, Pub. L. No. 98-369, § 155(a)(1) and (2), 98 Stat. 494, 691 (1984).

the legislative history of DEFRA and stated that in enacting the legislation, Congress intended that the new substantiation requirements would alert the IRS to potential overvaluations of contributed property, thereby deterring taxpayers from claiming excessive charitable contribution deductions, which was a concern of Congress.

The court then noted that in response to Congress' directive in DEFRA, Treasury amended Treas. Reg. § 1.170A-13 to add new paragraph (c), which provided new substantiation requirements that apply to donors who contribute property worth more than \$5,000. To meet these requirements, donors must obtain a qualified appraisal of the contributed property, attach a "fully completed" appraisal summary to the return on which the deduction is first claimed, and maintain records containing specified information. The appraisal summary must provide the adjusted cost or other basis of the donated property. Under the regulations, a taxpayer that does not meet these requirements is denied a deduction for the contribution.

The court next discussed the doctrine of substantial compliance, which may allow a taxpayer to claim a charitable contribution deduction even if it fails to strictly comply with all reporting requirements. The court discussed two cases with different results and then applied them to this case. The court previously held in *Bond v. Commissioner* that the reporting requirements of Treas. Reg. § 1.170A-13 are "directory and not mandatory," meaning that a taxpayer who fails to strictly comply with reporting requirements may still be allowed to claim a charitable contribution deduction provided the taxpayer substantially complies.<sup>24</sup> In *Bond*, the taxpayers attached to their return an appraisal summary on Form 8283 that included all required information except for the appraiser's qualifications. However, the taxpayers provided this missing information around the time that the IRS began the audit of their return. The court in *Bond* stated that a denial of the deduction would be an unnecessary sanction and therefore allowed the deduction based on the substantial compliance doctrine.

The court then contrasted *Bond* with its holding in *Hewitt v. Commissioner*.<sup>25</sup> In *Hewitt*, the taxpayers donated non-publicly traded stock but did not obtain a qualified appraisal or attach an appraisal summary to their return. The IRS disallowed the taxpayers claimed charitable contribution deduction even though it did not dispute that the amount the taxpayers deducted was equal to the stock's value. The court in *Hewitt* upheld the IRS's disallowance of the deduction and rejected the taxpayers' substantial compliance argument, finding that the statutory language required an appraisal and the need for the IRS to be provided with appropriate information to be aware of potential overvaluations, thereby distinguishing this case from *Bond*. The court also mentioned the case of *Smith v. Commissioner*, where it articulated a standard for substantial compliance based on the *Bond* and *Hewitt* cases.<sup>26</sup> In *Smith*, the court noted that in determining whether there was substantial compliance, the court would consider whether the donor provided sufficient information for the IRS to evaluate the contribution, in accordance with congressional intent.

Turning to the case at hand, the court noted that the taxpayer's Form 8283, *Noncash Charitable Contributions*, appraisal summary showed that it had purchased the remainder interest in the property but left blank the space for "Donor's cost or other adjusted basis." Therefore, the taxpayer did not meet the requirements of the regulations.<sup>27</sup> The court then addressed whether the taxpayer should be allowed to claim the charitable contribution deduction based on the doctrine of substantial compliance.

24 *Bond v. Comm'r*, 100 T.C. 32, 40-41 (1993).

25 *Hewitt v. Comm'r*, 109 T.C. 258 (1997), *aff'd without published opinion*, 166 F.3d 332 (4th Cir. 1998).

26 *Smith v. Comm'r*, T.C. Memo. 2007-368, *aff'd*, 364 F. App'x 317 (9th Cir. 2009).

27 See Treas. Reg. § 1.170A-13(c)(4)(ii)(E).

The court noted that the taxpayer's omission of its basis in the remainder interest on the Form 8283 prevented the appraisal summary from accomplishing its intended purpose. The court reiterated that Congress had directed Treasury to adopt stricter substantiation requirements for charitable contributions to alert the IRS to potential overvaluations of contributed property, thereby deterring taxpayers from claiming excessive deductions. The court stated that the taxpayer had purchased the remainder interest in March 2002 for around \$3 million and claimed a charitable contribution deduction of approximately \$33 million for its assignment of the remainder interest in August 2003, a mere 17 months later. Had the taxpayer properly reported its cost basis on the Form 8283, the significant disparity between the purchase price of the property and its claimed fair market value would have alerted the IRS to a potential overvaluation of the property. Therefore, because the taxpayer failed to provide sufficient information on its Form 8283 for the IRS to evaluate its contribution, the court found that the taxpayer had not substantially complied with the substantiation requirements and was not entitled to any deduction.<sup>28</sup>

### Value of the Property Contributed

In *Gardner v. Commissioner*, the taxpayer, an avid big-game hunter, owned a vast collection of 'trophies' from his hunting expeditions.<sup>29</sup> The taxpayer sought to downsize his collection and, on the advice of a fellow hunter, decided to donate various unwanted specimens to the Dallas Ecological Foundation, a tax-exempt organization. Following the recommendation of the fellow hunter, the taxpayer contacted an appraisal expert, who agreed to appraise 177 specimens that the taxpayer wished to donate.

The appraisal expert prepared a report and used a replacement cost method to determine the fair market value of the items. Specifically, the appraiser estimated the cost to replace each item by calculating the expected out-of-pocket expenses for traveling to a hunting site, spending time on a safari, killing the animal, removing, preserving, and shipping the body, and taxidermy costs. The appraiser, who was aware that the taxpayer intended on claiming a charitable contribution deduction for the donation of the items, appraised the taxpayer's 177 specimens at \$1,425,900. Relying on this valuation, the taxpayer reported a charitable contribution of \$1,425,900 on his 2006 tax return. Due to charitable contribution deduction limits, the taxpayer only claimed a charitable contribution deduction of \$129,459 in 2006, but carried forward the excess contribution into the following tax years, deducting \$429,313 in 2007 and another \$783,509 in 2008.<sup>30</sup> The IRS examined the taxpayer's 2006-2008 returns and determined that the value of the 177 specimens was only \$163,045. The IRS therefore asserted deficiencies of \$137,647 and \$274,228 for 2007 and 2008, respectively.

The court first noted that under the regulations, the amount of the charitable contribution allowed as a deduction is generally equal to the fair market value of the property at the time the contribution is made.<sup>31</sup> The court also mentioned that the IRS and taxpayer agreed that the taxpayer had fulfilled all necessary procedural requirements, including obtaining a qualified appraisal. The court pointed out that the only dispute in this case was the fair market value of the 177 donated items and that the burden of proving it was on the taxpayer.

The court then discussed the valuation methodologies of the parties and noted their fundamental disagreement in this regard. The IRS took the position that fair market value is determined by

28 *RERI Holdings I, LLC v. Comm'r*, 149 T.C. No. 1 (2017) appeal docketed, No. 17-1266 (D.C. Cir. Dec. 18, 2017).

29 *Gardner v. Comm'r*, T.C. Memo. 2017-165.

30 See IRC § 170(b)(1)(C).

31 See Treas. Reg. § 1.170A-1(c)(1).

considering market prices for comparable items while the taxpayer insisted that, because of their unique nature, the specimens had no real comparables in the open market and valuation was appropriate using a replacement cost methodology.

The court noted that an important factor in the dispute between the IRS and the taxpayer was whether the specimens were more appropriately classified as “collectibles,” whose value depends on who shot the animal, where it was shot, and previous ownership, or “commodities,” which can be valued on the open market. The court stated that it had “no difficulty” concluding that the specimens were commodities and the IRS’s valuation based on the market price was appropriate. The court noted that the taxpayer did not call his appraiser as a witness or seek to enter his report into evidence. The court stated that the donated specimens were no longer available for inspection and that the expert witnesses on both sides had therefore relied on the appraisal report, which overrated many specimens, provided limited information about them, and did not explain why the appraiser had adopted a replacement cost approach.

The court then discussed the testimony of experts on both sides. It noted that the IRS’s expert was a certified taxidermy appraiser, who had conducted appraisals for museums, state and local governments, and the IRS. The expert’s testimony, which the court found “credible and convincing,” characterized the specimens as consisting primarily of “remnants and scraps” of a trophy collection. The expert valued the contributed specimens by consulting market data from brick and mortar auction houses, online auction sites, and websites specializing in hunting specimens. The expert assigned each specimen a price on the assumption that each specimen was in “excellent” condition, then reduced the appraised value by each observed defect from photographs in the appraisal report. Ultimately, the IRS’s expert valued the 177 contributed specimens at \$41,140 in excellent condition and, after viewing the appraisal photographs of the items that showed defects in many items, he reduced his appraisal to \$34,240.

Next, the court discussed the testimony of the taxpayer’s three experts. It noted that two of these experts did not put a dollar figure on the 177 specimens but rather sought to defend the replacement cost methodology. The court found their testimony, which essentially claimed that the market approach asserted by the IRS could not capture the true fair market value of the specimens because they were museum-quality pieces uniquely valuable for research, to be without any factual support and therefore “wholly unreliable.” The court pointed out various issues with their qualifications, lack of professional experience appraising taxidermy, improper assumptions, and overreliance on the original flawed appraisal report. The taxpayer’s third expert claimed that the 177 specimens had a replacement cost value of \$2,544,300, which was \$1,128,400 more than the replacement cost that the taxpayer had claimed as a charitable contribution on his tax return. This expert arrived at this figure by assuming that each of the 177 specimens would be obtained on a separate trip, crated and shipped back individually, and incur taxidermy and mounting expenses. The court noted that this expert conceded that multiple animals could be hunted in one trip and the taxpayer had in fact done so.

The court, which had adjudicated valuation disputes over charitable contributions of hunting specimens in the past, stated that it generally relied on a comparable sales method of valuation where an active market existed, and that the replacement cost method of valuation was proper only in the case of unique property with a limited market and no evidence of comparable sales. The court was persuaded by the testimony of the IRS’s expert that the specimens were mostly “remnants, leftovers, and scraps” and that the taxpayer was essentially discarding unwanted items. The court found the testimony of the taxpayer’s experts that all the specimens were of excellent quality to be unpersuasive, and noted that their assertions lacked a factual basis and were contradicted by the photographs contained in the initial

appraisal report. Therefore, the court found that the specimens were commodities, not collectibles, and that the market price for similar items, rather than replacement cost, should determine fair market value. The court stated that the IRS's expert had credibly determined that the fair market value of the specimens, depending on their condition, was between \$34,240 and \$41,140. The court held that the taxpayer had not carried his burden of proving that the fair market value of the specimens exceeded the \$163,045 value allowed by the IRS and therefore sustained the IRS's determination to disallow the taxpayer's charitable contribution deduction in excess of this amount.<sup>32</sup>

### Qualified Conservation Contribution

For a gift to constitute a qualified contribution under IRC § 170, the donor must possess a transferrable interest in the property and intend to irrevocably relinquish all rights, title, and interest to the property without any expectation of some benefit in return.<sup>33</sup> Taxpayers generally are not permitted to deduct gifts of property consisting of less than the taxpayer's entire interest in that property.<sup>34</sup> Nevertheless, taxpayers may deduct the value of a contribution of a partial interest in property that constitutes a "qualified conservation contribution,"<sup>35</sup> also known as a conservation easement. A contribution will constitute a qualified conservation contribution only if it is of a "qualified real property interest" made to a "qualified organization" and "exclusively for conservation purposes."<sup>36</sup> All three conditions must be satisfied for the donation to be deemed a "qualified conservation contribution." For the current reporting period, we identified nine charitable contribution deduction cases involving conservation easements, an increase from the five cases we identified in the 2017 reporting period.<sup>37</sup>

In *BC Ranch II, L.P. v. Commissioner*, the taxpayers, two limited partnerships, BCR I and BCR II, appealed to the United States Court of Appeals for the Fifth Circuit a Tax Court decision upholding the IRS's disallowance of their charitable contribution deductions for conservation easements grants.<sup>38</sup> In 2003 BCR I had purchased a 3,744-acre piece of land (the "ranch") and, in 2005, conveyed approximately 1,866 acres to BCR II. In 2003, the developers of the ranch approached the North American Land Trust ("NALT"), an IRC § 501(c)(3) organization, to determine if the ranch could qualify for a tax-deductible conservation easement. NALT advised the taxpayers that the land would qualify as a conservation easement, with one benefit of the easement being the protection of the nesting areas and habitat of the gold-cheeked warbler, which was listed as an endangered species.

Prior to donating the conservation easement, the taxpayers assembled extensive documentation from NALT's visits to the ranch site, including photographs, property maps, details of site visit by an NALT biologist, and maps of the gold-cheeked warbler habitat. The taxpayers also hired an environmental consultant to advise as to how the property should be developed to ensure compliance with the Endangered Species Act. The consultant completed a report that included detailed aerial photographs and topographic maps that had habitat surveys of the gold-cheeked warbler's probable nesting areas.

After the taxpayers and NALT assembled two binders of "baseline documents" detailing the conservation easements, the taxpayers, BCR I and BCR II, donated conservation easements to NALT in

32 *Gardner v. Comm'r*, T.C. Memo. 2017-165.

33 IRC § 170(f)(3).

34 *Id.*

35 IRC §§ 170(b)(1)(E) and (f)(3)(B)(iii).

36 IRC § 170(h)(1)(A)-(C).

37 See National Taxpayer Advocate 2017 Annual Report to Congress 447.

38 *BC Ranch II, L.P. v. Comm'r*, 867 F.3d 547 (5th Cir. 2017), *vacating and remanding* T.C. Memo. 2015-130.

2005 and 2007, respectively. Both easements were substantially similar and provided for the protection and preservation of the environment and its natural inhabitants, including the gold-cheeked warbler and other birds and animals. The easements granted perpetual rights to NALT over the conservation areas while reserving certain narrow rights to the taxpayers that could not impact the conservation purpose of the easements. The easements could only be amended with the NALT's consent and only to modify the boundaries of "homesite parcels," which were areas of land where limited partners could build homes on select five-acre sites. These modifications were allowed so long as they did not increase the homesite parcels above five acres. NALT regularly monitored the conservation area and found it to be in good condition and in compliance with the terms of the easements.

The taxpayers each claimed charitable contribution deductions of approximately \$8,000,000 for conservation easements they had donated to NALT in 2005 and 2007. The IRS disallowed these deductions and asserted that the taxpayers were liable for gross valuation misstatement penalties. The taxpayers petitioned the Tax Court, which held that the IRS had properly disallowed the charitable contribution deductions, as the conservation easements were not given in perpetuity. The taxpayer appealed to the United States Court of Appeals for the Fifth Circuit.

After reviewing the basic law governing conservation easements and noting that a conservation easement restriction must be made in perpetuity to qualify for a charitable contribution deduction, the court discussed the perpetuity requirement. The court discussed the basic terms of the easement, including the homesite modification provision. As mentioned above, this provision allowed the taxpayers, with NALT's consent, to amend the property covered by the easements but only for the limited purpose of modifying the boundaries of the five-acre homesite parcels and without increasing these parcels above five acres. The court stated that these modifications were only permitted if in NALT's reasonable judgment they did not interfere with any of the conservation purposes.

The Tax Court had agreed with the IRS that the homesite boundary modification provision violated the perpetuity requirement contained in IRC § 170(h)(2)(C). Relying on *Belk v. Commissioner*, the Tax Court held that an easement is not qualified real property granted in perpetuity if the boundaries of the property subject to the easement may be modified.<sup>39</sup> The Court of Appeals for the Fifth Circuit found that the Tax Court's reliance on the *Belk* case was misplaced and distinguished it. It noted that the easements in this case were significantly different than the one in *Belk*. For example, the easements in this case allowed only the homesite parcels boundaries to be changed and only within the tracts subject to the easement and without increasing the size of the homesite parcels. Unlike in *Belk*, where entire tracts of land could be swapped in and out of the easement, the exterior boundaries and total acreage of the easements in this case could not be changed. Any homesite parcel boundary adjustments would require NALT's consent and remain within the easements. The court noted that such adjustments might be necessary to account for new nesting sites for the warblers and would not provide any financial benefit to the easement donors.

After distinguishing the easements from the one in *Belk*, the court stated that they were more akin to ones in two conservation façade easements cases. In those cases, two courts of appeals held that conservation easements are perpetual even though trusts could consent to the partial lifting of restrictions to allow repairs and changes to the façades of buildings.<sup>40</sup> The Fifth Circuit noted that the courts in those cases had applied "common sense reasoning" to allow for the modification of an

39 *Belk v. Comm'r*, 774 F.3d 221 (4th Cir. 2014), *aff'g* 140 T.C. 1 (2013). We discussed the *Belk* case in our 2015 Annual Report. See National Taxpayer Advocate 2015 Annual Report to Congress 517-518.

40 See *Comm'r v. Simmons*, 646 F.3d 6 (D.C. Cir. 2011); *Kaufman v. Shulman*, 687 F.3d 21 (1st Cir. 2012).

easement to promote the underlying conservation interests and that this rationale applied in this case too. The court also noted that the perpetuity of the easement was ensured by the fact that NALT had “virtually unrestricted discretion” to withhold consent to any modifications.

The court finished its discussion of the perpetuity requirement by making two final points. First, it noted that the conservation easement provision under IRC § 170(h) was enacted at the urging of conservation activists, by an overwhelming majority of Congress, and with the goal of conserving thousands of acres of property. Therefore, the usual strict construction of statutory loopholes did not apply to conservation easements. When applying an ordinary standard of statutory construction, the court stated it was satisfied that its perpetuity analysis was correct. Also, the court attached to its opinion a copy of the conservation easement plan and stated that it provided visual confirmation that the homesite adjustment provision would not violate the perpetuity requirement.

The court then turned to the baseline documentation requirement issue. Under the regulations, if a donor of a conservation easement retains rights to property that may impair the conservation interests, the donor must make available to the donee, prior to the time the donation is made, documentation sufficient to establish the condition of the property at the time of the contribution.<sup>41</sup> The regulations provide various examples of proper baseline documents including different types of maps, land use history, and aerial and on-site photographs. The court emphasized that the regulations use the term “may include” rather than “shall include” to indicate that this list is flexible and not rigid.

The Tax Court had held that the taxpayers had failed to meet the baseline documentation requirement of the regulations and characterized the documentation provided by the taxpayers as “unreliable, incomplete, and insufficient” to accurately depict the condition of the property subject to the easements. In reaching this conclusion, the Tax Court determined that some of the documentation was untimely and inaccurate. The Court of Appeals for the Fifth Circuit criticized the Tax Court for its rigid approach and for failing to consider several items in the record that would have sufficiently established the condition of the property prior to the donation, including photographs, reports, and site plans. The Court of Appeals also stated that the timing of these items was appropriate and showed “a great deal of collaboration” between the donor and donee prior to the donation. In sum, the Fifth Circuit found that the taxpayers had provided “more than sufficient” documentation to NALT establishing the condition of the property prior to the donation of the conservation easement and therefore met the baseline documentation requirement.

Therefore, the Court of Appeals for the Fifth Circuit vacated the Tax Court’s holding with respect to the perpetuity and baseline documentation requirements. The court remanded the case to the Tax Court to consider other grounds asserted by the IRS to disqualify the easements that had not been previously addressed by the Tax Court.<sup>42</sup>

<sup>41</sup> See Treas. Reg. § 1.170A-14(g)(5)(i).

<sup>42</sup> *BC Ranch II, L.P. v. Comm’r*, 867 F.3d 547, 556 (5th Cir. 2017), *vacating and remanding* T.C. Memo. 2015-130.

## CONCLUSION

IRC § 170 and the accompanying Treasury Regulations provide detailed requirements with which taxpayers must strictly comply. The statutory and regulatory requirements to qualify for a deduction become more stringent as deductions increase in size and taxpayers should be mindful of the newly-released final regulations under IRC § 170.<sup>43</sup> Like last year, most of the charitable contribution cases we reviewed this year addressed issues regarding substantiation of contributions, while several cases discussed the value of the contributed property and the complex rules governing the donation of a conservation easement.

Under the new tax reform legislation, taxpayers may now deduct up to 60 percent of their contribution base through qualifying charitable contributions.<sup>44</sup> However, due to the increase in the standard deduction, fewer taxpayers are likely to itemize their deductions, leading to a potentially significant reduction in charitable giving and less litigated cases in this area.

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43 See T.D. 9836, 83 Fed. Reg. 36417-01 (July 30, 2018). Some parts of these final regulations do not go into effect until after July 30, 2018 and may lead to more litigation in future years when they become effective.

44 This bill was introduced as the Tax Cuts and Jobs Act but was passed under a different title. See Pub. L. No 115-97, § 11023, 131 Stat. 2054, 2074-2075 (2017).

## MLI #9 Itemized Deductions Reported on Schedule A (Form 1040)

### SUMMARY

For the first time since the National Taxpayer Advocate's Annual Report to Congress in 2002, itemized deductions reported on Schedule A of IRS Form 1040 are among the ten Most Litigated Issues.

We identified 23 cases involving itemized deductions that were litigated in federal courts between June 1, 2017, and May 31, 2018.<sup>1</sup> The courts affirmed the IRS position in 16 of these cases, or about 70 percent, while taxpayers fully prevailed in four cases, or about 17 percent of the cases. The remaining three cases, or about 13 percent, resulted in split decisions.

### TAXPAYER RIGHT(S) IMPACTED<sup>2</sup>

- *The Right to Be Informed*
- *The Right to Pay No More Than the Correct Amount of Tax*
- *The Right to Challenge the IRS's Position and Be Heard*
- *The Right to Appeal an IRS Decision in an Independent Forum*
- *The Right to a Fair and Just Tax System*

### PRESENT LAW

Individual taxpayers can deduct from taxable income a standard deduction, based on filing status, or may instead elect to itemize deductions.<sup>3</sup> Itemized deductions are specified “personal” and “other” expenses allowed as deductions from Adjusted Gross Income (AGI) arriving at taxable income.<sup>4</sup> Eligible taxpayers may claim itemized deductions by filing a Schedule A (Form 1040), *Itemized Deductions*, with their tax returns. Common personal expenses include: interest payments, such as mortgage interest and points on principal and secondary residences,<sup>5</sup> state and local income or sales taxes, property taxes,<sup>6</sup> medical and dental expenses exceeding a certain threshold of the AGI,<sup>7</sup> charitable contributions,<sup>8</sup> and

1 We excluded cases involving unreimbursed employee expenses and charitable deductions as they are discussed elsewhere in the National Taxpayer Advocate's Annual Report to Congress. See National Taxpayer Advocate 1998-2017 Annual Reports to Congress. Unreimbursed employee expenses are discussed in detail in Most Litigated Issue: *Trade or Business Expenses Under IRC § 162 and Related Sections*, *supra*. Cases involving charitable deductions are discussed in detail in Most Litigated Issue: *Charitable Contribution Deductions Under IRC § 170*, *supra*.

2 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

3 IRC § 63. Married taxpayers must generally both elect the standard deduction or itemize deductions, regardless of whether they file joint or separate returns.

4 See IRC § 62 for the calculation of adjusted gross income (AGI).

5 IRC § 163.

6 IRC § 164.

7 Under the Tax Cuts and Jobs Act (TCJA), any taxpayer may deduct unreimbursed medical expenses that exceed 7.5 percent of their AGI in tax years 2017 and 2018. Pub. L. No. 115-97, § 11027, 131 Stat. 2054, 2077 (2017); IRC § 213(f).

8 IRC § 170. Charitable contributions are discussed in a separate Most Litigated Issue: *Charitable Contribution Deductions Under IRC § 170*, *supra*.

casualty and theft losses.<sup>9</sup> Other deductible expenses include certain payments related to the production or collection of income, such as property management expenses,<sup>10</sup> investment interest expenses,<sup>11</sup> and gambling losses.<sup>12</sup> For tax years prior to 2018, itemized deductions also included miscellaneous deductions, such as tax advice and preparation fees, appraisal fees for purposes of charitable contributions or casualty losses, job search and moving expenses, subscriptions to professional journals, home office expenses, union or professional dues, and unreimbursed work-related travel expenses or employee expenses reimbursed under a nonaccountable plan.<sup>13</sup>

For tax years before 2018, taxpayers with AGI over a certain threshold amount are limited as to the total itemized deductions they can claim.<sup>14</sup> For taxpayers with AGI over the threshold, allowable itemized deductions are reduced by three percent of AGI above the applicable threshold to a maximum reduction of 80 percent of the total allowable deductions for the tax year. These limitations apply to charitable donations, the home mortgage interest deduction, state and local tax deductions, and miscellaneous itemized deductions, but do not apply to medical expenses, investment interest expenses, gambling losses, and certain theft and casualty losses.<sup>15</sup>

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9 IRC §§ 165(e) and 165(h).

10 IRC § 212.

11 IRC § 163(d).

12 IRC § 165(d).

13 Miscellaneous itemized deductions refers to deductions other than: (1) the deduction under IRC § 163 (relating to interest); (2) the deduction under IRC § 164 (relating to taxes); (3) the deduction under IRC § 165(a) for casualty or theft losses described in paragraph (2) or (3) of IRC § 165(c) or for losses described in IRC § 165(d); (4) the deductions under IRC § 170 (relating to charitable, etc., contributions and gifts) and IRC § 642(c) (relating to the deduction for amounts paid or permanently set aside for a charitable purpose); (5) the deduction under IRC § 213 (relating to medical, dental, etc., expenses); (6) any deduction allowable for impairment-related work expenses; (7) the deduction under IRC § 691(c) (relating to the deduction for estate tax in case of income in respect of the decedent); (8) any deduction allowable in connection with personal property used in a short sale; (9) the deduction under IRC § 1341 (relating to computation of tax where taxpayer restores a substantial amount held under claim of right); (10) the deduction under IRC § 72(b)(3) (relating to the deduction where annuity payments cease before investment recovered); (11) the deduction under IRC § 171 (relating to the deduction for amortizable bond premium); and (12) the deduction under IRC § 216 (relating to deductions in connection with cooperative housing corporations). See IRC § 67(b).

14 The TCJA suspended the overall limit on itemized deductions based on AGI for tax years 2018 through 2025. Prior to the TCJA, taxpayers' ability to claim itemized deductions was limited if their AGI exceeded certain thresholds based on filing status. For example, for Tax Year 2017, the threshold is \$313,800 for married taxpayers filing jointly or a qualifying widow(er) (\$261,500 for a taxpayer filing single). See Pub. L. No. 115-97, § 11046, 131 Stat. 2054, 2088 (2017); Rev. Proc. 2016-55, 2016-45 I.R.B. 707.

15 IRC § 68(c).

## Changes Made Under the Tax Reform Legislation<sup>16</sup>

The Tax Cuts and Jobs Act (TCJA) eliminated or restricted many itemized deductions beginning in 2018, and increased the standard deduction. Overall, 61 percent fewer taxpayers are expected to claim itemized deductions in 2018.<sup>17</sup> The TCJA made the following changes to itemized deductions:<sup>18</sup>

### 1. *Standard deduction*

For tax years 2018–2025, the TCJA roughly doubles the standard deduction amounts to \$12,000 for single individuals, \$18,000 for heads of household, and \$24,000 for joint filers.<sup>19</sup> These amounts are adjusted for inflation.<sup>20</sup>

### 2. *Medical expense deduction*

Under prior law, taxpayers whose unreimbursed medical expenses exceeded ten percent of their AGI could deduct that excess. For tax years 2013–2016, a taxpayer could deduct the excess over 7.5 percent of AGI if the taxpayer or his or her spouse had attained age 65 before the close of the taxable year. Under the TCJA, any taxpayer may deduct unreimbursed medical expenses that exceed 7.5 percent of his or her AGI in tax years 2017 and 2018.<sup>21</sup> This change was made retroactive to January 1, 2017.<sup>22</sup>

### 3. *State and local taxes*

The TCJA limits the aggregate amount of the itemized deduction taxpayers can claim for state and local income, sales, real estate, or personal property taxes to \$10,000 per year (\$5,000 in the case of a married individual filing a separate return) for tax years 2018–2025.<sup>23</sup> Prior to the TCJA law, there was no limitation on the amount of state and local taxes a taxpayer could take as an itemized deduction.

### 4. *Mortgage and home equity interest deduction*

For mortgages entered into after December 15, 2017, the TCJA generally allows a taxpayer to deduct interest only up to \$750,000 on mortgage debt used to buy, build, or improve a principal home (\$375,000 in the case of married taxpayers filing separate returns) for tax years 2018 through 2025.<sup>24</sup> However, the limit remains at \$1 million (\$500,000 in the case of married taxpayers filing separate tax returns) for mortgage debt incurred on or before December 15, 2017.

16 Pub. L. No. 115-97, 131 Stat. 2054 (2017). TAS has created a website, available in both English and Spanish, to educate individual taxpayers about items that were changed and not changed as a result of TCJA. For a detailed list of these changes, see TAS, *Tax Changes by Topic*, <https://taxchanges.us/> (last visited Sept. 9, 2018).

17 The Joint Committee on Taxation staff estimates the number of taxpayers who itemize will tumble from about 46.5 million in 2017 to about 18 million in 2018. J. Comm. on Tax'n, *Tables Related to the Federal Tax System as in Effect 2017 through 2026* (JCX-32-18) (Apr. 23, 2018).

18 Pub. L. No. 115-97, 131 Stat. 2054 (2017).

19 *Id.*

20 The TCJA employed a new Consumer Price Index. Specifically, the new index differs from the previous Consumer Price Index by attempting to account for the ability of individuals to alter their consumption patterns in response to relative price changes. See Pub. L. No. 115-97, § 11002, 131 Stat. 2054, 2059 (2017).

21 Pub. L. No. 115-97, § 11027, 131 Stat. 2054, 2077 (2017); IRC § 213(f).

22 *Id.*

23 Pub. L. No. 115-97, § 11042, 131 Stat. 2054, 2085 (2017); IRC § 164.

24 *Id.*; IRC § 163(h)(3).

The TCJA also eliminates the deduction for interest on home equity debt for tax years 2018-2025. However, home equity debt interest might still be deductible if the funds are used for a purpose where interest otherwise may be deductible, such as for home improvement, investment, or business purposes.<sup>25</sup>

#### 5. *Casualty and theft loss deductions*

The TCJA provides that, for tax years 2018-2025, taxpayers may not deduct any personal casualty or theft losses not compensated by insurance or otherwise, unless the casualty loss is attributable to a federally declared disaster.<sup>26</sup> The loss must still exceed \$100 per casualty and the total net loss must exceed ten percent of the taxpayer's AGI.<sup>27</sup>

#### 6. *Miscellaneous itemized deductions*

For tax years 2018-2025, the deduction for miscellaneous expenses subject to the two percent of AGI floor, such as certain professional fees, investment expenses, and unreimbursed employee business expenses, has been suspended under the TCJA.<sup>28</sup>

#### 7. *Charitable contribution deductions*<sup>29</sup>

For tax years 2018-2025, the limit on the deduction for cash donations to public charities is increased from 50 to 60 percent of AGI.<sup>30</sup> However, charitable deductions for payments made in exchange for college athletic event seating rights are eliminated.<sup>31</sup>

## ANALYSIS OF LITIGATED CASES

For the first time since the National Taxpayer Advocate's Annual Report to Congress in 2002, itemized deductions reported on Schedule A of IRS Form 1040 were among the ten Most Litigated Issues. This year, we analyzed 23 cases between June 1, 2017, to May 31, 2018, in which itemized deductions were in dispute. All but five of these cases were either litigated in the United States Tax Court or in a United States Court of Appeals on appeal of a Tax Court decision. A detailed list appears in Table 9 in Appendix 3.

Of the 15 cases in which taxpayers appeared *pro se* (without counsel), the IRS prevailed in nine. The taxpayer prevailed in three cases, while the other three cases resulted in a split decision. Taxpayers represented by counsel fared worse; of the eight cases in which taxpayers had representation, taxpayers prevailed in only one case and were denied relief in seven cases. Most of this year's 23 cases involved taxpayers claiming deductions for casualty and theft losses,<sup>32</sup> tax preparation fees or expenses associated

25 Pub. L. No. 115-97, § 11043, 131 Stat. 2054, 2086 (2017). See also IR 2018-32, *Interest on Home Equity Loans Often Still Deductible Under New Law*, (Feb. 21, 2018), <https://www.irs.gov/newsroom/interest-on-home-equity-loans-often-still-deductible-under-new-law> (last visited Nov. 26, 2018).

26 Pub. L. No. 115-97, § 11044, 131 Stat. 2054, 2087 (2017); IRC § 165(h).

27 IRC § 165(c)(3) & (h).

28 Pub. L. No. 115-97, § 11045, 131 Stat. 2054, 2088 (2017).

29 See also Most Litigated Issue: *Charitable Contribution Deductions Under IRC § 170*, *supra*.

30 Pub. L. No. 115-97, § 11023, 131 Stat. 2054, 2074 (2017).

31 *Id.*

32 IRC § 165.

with the production of income,<sup>33</sup> and medical care.<sup>34</sup> The Figure 3.9.1 categorizes the main issues raised by taxpayers in the 23 cases we identified:

**FIGURE 3.9.1, Itemized Deduction Issues<sup>35</sup>**

Itemized Deduction	Number of Cases	Percentage of Cases
Casualty/Theft Loss	7	30
Miscellaneous Subject to 2% Limit (i.e., Tax Preparation Fees or Production of Income)	6	26
Medical and Dental Expenses	3	13
Interest	3	13
Miscellaneous Not Subject to the 2% Limit (i.e., Gambling)	3	13
Property Taxes	3	13

A common factor in many cases was the court's finding, in nine (39 percent) of the cases, that taxpayers failed to substantiate the itemized deductions claimed.<sup>36</sup>

Although the cases originated because of varied circumstances, the overwhelming majority began as examination cases.<sup>37</sup> Of the 23 cases we reviewed this year, seven began as field exam cases;<sup>38</sup> six began as correspondence exam cases;<sup>39</sup> and five began as office exam cases.<sup>40</sup>

### Medical or Dental Expense Deduction

A taxpayer may deduct the cost of medical care for the diagnosis, cure, mitigation, treatment, or prevention of disease, or for the purpose of affecting any structure or function of the human body.<sup>41</sup> Medical expenses are only deductible to the extent they exceed a statutorily determined percentage of the

33 Treas. Reg. § 1.67-1T; IRC § 212.

34 IRC § 213.

35 The aggregate percentages may not equal 100 percent because of rounding. Additionally, several cases we identified had more than one of the issues listed in Figure 3.9.1.

36 See, e.g., *Fiedziuszko v. Comm'r*, T.C. Memo. 2018-75 (Court disallowed medical and dental expense deduction under IRC § 213 because taxpayers failed to substantiate expenses paid for physician-ordered treatment).

37 TAS analysis of litigated cases indicated that 18 originated as a result of the Small Business Self-Employed Division examination, six – as a result of correspondence examination, five – as a result of an office audit, and seven – as a result of field examination. From the remaining cases, two resulted from an Automated Under Reporter (AUR) program assessment, one – from Automated Substitute for Return (ASFR) under IRC § 6020(b), one case resulted from a contested liability in a Collection Due Process proceeding, and the last case originated from a taxpayer refund claim suit filed in the U.S. Court of Federal Claims. TAS data pull from AIMS, Sept. 2, 2018. The AUR Program verifies a discrepancy between the taxpayer's tax return and an information return, or between a tax return and information otherwise in the IRS's possession. See IRM 4.19.3 (Aug. 31, 2018); Rev. Prov. 2005-32, 2005-23 I.R.B. 1206. The ASFR program allows the IRS to assess tax by obtaining delinquent returns or creating assessments based on reported income. See IRM 5.18.1 (Dec. 31, 2017); IRC § 6020(b). See also *Pryde v. U.S.*, 120 A.F.T.R.2d (RIA) 6843 (Fed. Cl. 2017); *Dykstra v. Comm'r*, T.C. Memo. 2017-156.

38 See also Most Serious Problem: *Field Examination: The IRS's Field Examination Program Burdens Taxpayers and Yields High No-Change Rates, Which Waste IRS Resources and May Discourage Voluntary Compliance*, *supra*.

39 See also Most Serious Problem: *The IRS's Correspondence Examination Procedures Burden Taxpayers and are Not Effective in Educating the Taxpayer and Promoting Future Voluntary Compliance*, *supra*.

40 See also Most Serious Problem: *Office Examination: The IRS Does Not Know Whether Its Office Examination Program Increases Voluntary Compliance or Educates the Audited Taxpayers About How to Comply in the Future*, *supra*.

41 IRC § 213(d)(1).

taxpayer's AGI. For example, a taxpayer who elects to itemize deductions for tax years 2017 and 2018 may deduct medical expenses to the extent his or her medical expenses exceed 7.5 percent of the AGI, regardless of age. For tax years after 2018, the floor will return to ten percent. Medical expenses are also only deductible if they are for the taxpayer, the taxpayer's spouse, or the taxpayer's dependent.

In *Morrissey v. United States*, a homosexual male taxpayer claimed a medical expense deduction for costs associated with the *in vitro* fertilization process.<sup>42</sup> Although the taxpayer conceded that he was medically fertile, he argued the costs were necessary because it is not physiologically possible for two men to reproduce. Most of the taxpayer's expenses were incurred to identify, compensate, and provide medical care for the women who served as an egg donor and gestational surrogate. The court disallowed the medical expense deduction, reasoning that the expenses related to the egg donor and gestational surrogate were not incurred for the purpose of affecting any function of the taxpayer's own body, and the egg donor and gestational surrogate were not the taxpayer's spouse or the taxpayer's dependent.<sup>43</sup> In coming to its conclusion, the United States Court of Appeals for the Eleventh Circuit relied on existing Tax Court precedent that has consistently rejected efforts by male taxpayers to deduct *in vitro* fertilization-related expenses paid to cover the medical care of unrelated female egg donors and gestational surrogates.<sup>44</sup>

### Casualty and Theft Loss Deduction

A taxpayer whose personal property is lost or damaged due to fire, storm, shipwreck, or other casualty, or from theft, may be entitled to an itemized deduction for the amount of the loss that is not reimbursed by insurance or otherwise.<sup>45</sup> The taxpayer may claim a casualty or theft loss deduction only if the loss amount exceeds \$100 and the amount of the net loss exceeds ten percent of the taxpayer's adjusted gross income.<sup>46</sup>

In *Kohn v. Commissioner*, married taxpayers claimed a casualty loss for alleged damage to their docks during a flood.<sup>47</sup> From April through October 1993, St. Charles County, the area where the taxpayers' docks were located, became a federally declared disaster area under the Disaster Relief and Emergency Assistance Act.<sup>48</sup> The taxpayers purchased the docks in February 1993, before the flood, and sold the docks in October 1993 for \$2,600 less than the purchase price. In calculating the amount of the casualty loss deduction, the Tax Court employed the fair market value calculation approach; the fair market value of the property immediately before the casualty less the fair market value of the property immediately after the casualty.<sup>49</sup> Because the resulting \$2,600 was less than ten percent of the taxpayers' adjusted gross income, the court disallowed the casualty loss deduction.

42 *Morrissey v. United States*, 871 F.3d 1260 (11th Cir. 2017).

43 *Id.* at 1267-1268.

44 See, e.g., *Magdalin v. Comm'r*, T.C. Memo. 2008-293, *aff'd*, 2009 WL 5557509 (1st Cir. 2009).

45 IRC §§ 165(a), 165(c)(3).

46 IRC § 165(h).

47 *Kohn v. Comm'r*, T.C. Memo. 2017-159.

48 Taxpayers elected to claim the casualty deduction for the year preceding the year of the flood. Under IRC § 165(i), any losses attributable to a federally declared disaster may be considered for the taxable year immediately preceding the taxable year in which the disaster occurred.

49 The amount of the deduction is the lesser of: (i) the fair market value of the property immediately before the casualty reduced by the fair market value of the property immediately after the casualty; or (ii) the amount of the property's adjusted basis. Treas. Reg. § 1.165-7(b). See also *Helvering v. Owens*, 305 U.S. 468 (1939).

A deduction can include a loss based on theft that was not compensated for by insurance or otherwise.<sup>50</sup> A theft for purposes of the deduction includes any criminal appropriation of another's property to the use of the taker, including larceny, embezzlement, and robbery. The taxpayer bears the burden of proving both the occurrence of a theft and the amount of the loss.

*In re Nora* involved a homeowner who failed to make payments on her mortgage.<sup>51</sup> The mortgage company was successful in obtaining a judgment against the taxpayer, and the residence was sold at foreclosure.<sup>52</sup> The taxpayer was evicted sometime between August and November 2011, although the actual date of eviction could not be established. When the taxpayer arrived at her residence in November, she discovered the locks had been changed and her personal property had been removed and placed in storage. The taxpayer testified she made no attempts to retrieve the property, which included boxes of records, held in storage by the Sheriff's Department or at the storage company. In her 2012 tax return, the taxpayer claimed a casualty loss by theft, a Ponzi Scheme loss, and casualty loss of client files pursuant to IRC § 165.<sup>53</sup> However, she provided no documentary evidence to support deductions for the estimated 20 boxes of client records that had been destroyed or removed from her residence.

The Court found that the taxpayer failed to provide credible evidence to establish what was destroyed and its value in order to meet her burden to rebut the presumption of validity of the proof of claim.<sup>54</sup> Moreover, the court noted that the destroyed records were connected with her trade or business and the deduction for loss of property that arises from a casualty or theft applies only to property not connected with a trade or business.<sup>55</sup> Furthermore, the court noted that when property is taken under a lawful authorization, a taxpayer is not entitled to a theft loss deduction.<sup>56</sup> The United States Tax Court has specifically found that the value of personal property that is lost or damaged during a lawful eviction after foreclosure cannot be the basis of a casualty or loss-theft deduction.<sup>57</sup> Finally, the court noted that her claim for the theft of the business records as a business loss under IRC § 165(c)(1) was meritless.<sup>58</sup>

### Substantiation of Itemized Deductions

Taxpayers are required to substantiate expenses underlying each claimed deduction by maintaining records sufficient to establish the amount of the deduction and to enable the Commissioner to determine the correct tax liability.<sup>59</sup> Taxpayers were unable to substantiate their claimed itemized deduction in nine of the 23 cases we identified, or 39 percent of the cases.

In *Knowles v. Commissioner*, the Tax Court sustained the IRS's disallowance of a taxpayer's claimed deduction for real property taxes paid.<sup>60</sup> Although the taxpayer produced printouts from a county

50 IRC § 165(c)(3).

51 *In re Nora*, 581 B.R. 870 (D. Minn. 2018), *appeal dismissed*, 2018 WI 4520881 (D. Minn. 2018), *appeal docketed*, No. 18-3095 (8th Cir. Oct. 1, 2018).

52 *Id.*

53 The taxpayer is an attorney, who had stored client records in her basement. *Id.* at 873.

54 *Id.* at 879-80.

55 *Id.* at 880. See also IRC §165(c)3).

56 *Id.* at 880-81.

57 *Washington v. Commissioner*, T.C. Memo. 1990-386, *aff'd*, 930 F.2d 919 (6th Cir. 1991) (finding that when taxpayers were evicted pursuant to a court order there was no theft because the mortgage holder "proceeded under a lawful authorization or a least the color of legal authority,' and had no criminal intent").

58 *In re Nora* at 882.

59 IRC § 6001; *Higbee v. Comm'r*, 116 T.C. 438 (2001).

60 *Knowles v. Comm'r*, T.C. Memo. 2017-152.

website showing property taxes due, she provided no evidence that she paid those taxes. In general, a taxpayer can substantiate itemized deductions with documentary evidence such as receipts, cancelled checks, bills, or account statements.<sup>61</sup>

Substantiation is also important for the gambling loss deduction. A taxpayer who is not in the trade or business of gambling can deduct gambling losses as an itemized deduction, but only to the extent of gambling winnings.<sup>62</sup>

In *Boneparte v. Commissioner*, the Tax Court found that a taxpayer was not in the trade or business of gambling.<sup>63</sup> The court cited the following factors in its analysis: the taxpayer did not keep any records other than the win/loss statements provided by casinos, which generally provided only the aggregate amount won or lost during the year; he gambled only in his spare time while holding a full-time job; he had a history of gambling losses and did not earn even sporadic profits; and his gambling involved elements of personal pleasure and recreation. The Tax Court then used the taxpayer's casino win/loss statements to reconstruct his taxable gambling income. Since his gain was \$18,000, the taxpayer was allowed an itemized deduction of \$18,000.

Certain deductions are subject to stricter substantiation requirements. For example, a taxpayer claiming the medical expense deduction must be able to produce the name and address of each person to whom expenses for medical care were paid and the date of each payment.<sup>64</sup> The IRS may also request a statement or itemized invoice from the payee showing what kind of treatment was provided and to whom.<sup>65</sup>

In *Fiedziuszko v. Commissioner*, the Tax Court held that married taxpayers failed to substantiate the cost of their physician-ordered weight loss program.<sup>66</sup> At trial, Mr. Fiedziuszko prepared a statement with a list of dates and amounts they paid for the weight-loss program. The taxpayers also provided to the IRS a printout from the website of their healthcare provider, Palo Alto Medical Foundation, containing information about its weight-loss services. The Tax Court held that the Fiedziuszkos did not adequately substantiate their medical expenses because they failed to provide an itemized statement from the payee, Palo Alto Medical Foundation, with corroborating documentation of the claimed medical payments as required under the medical expense deduction regulations.<sup>67</sup>

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61 See *Cohan v. Comm'r*, 39 F.2d 540 (2d Cir. 1930); Treas. Reg. § 1.274-5T(b). See also IRS, Burden of Proof, <https://www.irs.gov/businesses/small-businesses-self-employed/burden-of-proof> (last visited Sept. 9, 2018) (describing the requirement to substantiate certain elements of expenses in order to shift the burden of proof according to IRC § 7491); see also IRS Publication 583, *Starting a Business and Keeping Records* (January 2015), for detailed recordkeeping guidance for taxpayers.

62 IRC § 165(d).

63 *Boneparte v. Comm'r*, T.C. Memo. 2017-193, *appeal docketed*, No. 18-2264 (3d Cir. June 8, 2018).

64 Treas. Reg. § 1.213-1(h).

65 *Id.*

66 *Fiedziuszko v. Comm'r*, T.C. Memo. 2018-75. The IRS considers obesity a disease for purposes of the medical expense deduction. See also Rev. Rul. 2002-19.

67 See Treas. Reg. § 1.213-1(h).

## CONCLUSION

The IRS Statistics of Income data show that 29.6 percent of individual return filers chose to itemize their deductions in tax year 2015.<sup>68</sup> We anticipate this number will decrease beginning in tax year 2018 because recent tax law changes increased the standard deduction and placed limitations on or entirely repealed many itemized deductions.

In the nine cases we reviewed this year in which taxpayers were unable to provide the necessary documentation to support their deductions, the courts identified the lack of documentation and preparation as the reason they ruled against the taxpayers.

The IRS should continue improving its means of communicating with and educating taxpayers about deductibility issues, including recordkeeping requirements. Proactive education and outreach will also promote taxpayers' *rights to be informed* and *to challenge the IRS's position and be heard*. By doing so, the IRS will encourage taxpayers to comply with their tax obligations and minimize the risk of litigation.

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68 IRS, *SOI Tax Stats—Individual Income Tax Returns Publication 1304*, “Table 1.2: All Returns: Adjusted Gross Income, Exemptions, Deductions, and Tax Items” (June 21, 2018), <https://www.irs.gov/statistics/soi-tax-stats-individual-income-tax-returns-publication-1304-complete-report>.

MLI  
#10Frivolous Issues Penalty Under IRC § 6673 and Related  
Appellate-Level Sanctions

## SUMMARY

From June 1, 2017, through May 31, 2018, the federal courts issued decisions in at least 19 cases involving the Internal Revenue Code (IRC) § 6673 “frivolous issues” penalty, and in at least three cases involving analogous penalties at the appellate level. These penalties are imposed for maintaining a case primarily for delay, raising frivolous arguments, unreasonably failing to pursue administrative remedies, or filing a frivolous appeal.<sup>1</sup> In many of the cases we reviewed, taxpayers escaped liability for the penalty but were warned they could face sanctions for similar conduct in the future.<sup>2</sup> Nonetheless, we included these cases in our analysis to illustrate what conduct will and will not be tolerated by the courts.

TAXPAYER RIGHT IMPACTED<sup>3</sup>

- *The Right to Appeal an IRS Decision in an Independent Forum*

## PRESENT LAW

The U.S. Tax Court is authorized to impose a penalty against a taxpayer if the taxpayer institutes or maintains a proceeding primarily for delay, takes a frivolous position in a proceeding, or unreasonably fails to pursue available administrative remedies.<sup>4</sup> The maximum penalty is \$25,000.<sup>5</sup> In some cases, the IRS requests that the Tax Court impose the penalty;<sup>6</sup> in other cases, the Tax Court exercises its discretion, *sua sponte*,<sup>7</sup> to consider whether the penalty is appropriate.

1 The Tax Court generally imposes the penalty under Internal Revenue Code (IRC) § 6673(a)(1). Other courts may impose the penalty under IRC § 6673(b)(1). U.S. Courts of Appeals are authorized to impose sanctions under IRC § 7482(c)(4), 28 U.S.C. § 1927, or Rule 38 of the Federal Rules of Appellate Procedure, although some appellate-level penalties may be imposed under other authorities.

2 See, e.g., *Fleming v. Comm’r*, T.C. Memo. 2017-120.

3 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the IRC. See IRC § 7803(a)(3).

4 IRC § 6673(a)(1)(A), (B), and (C). Likewise, the Tax Court is also authorized to impose a penalty against any person admitted to practice before the Tax Court for unreasonably and vexatiously multiplying the proceedings in any case. See IRC § 6673(a)(2). However, although we identified one case under this authority, we do not discuss it here as it is outside the scope of this most litigated issue. See *MacPherson v. Comm’r*, 702 Fed. App’x 621 (9th Cir. 2017), *aff’g May v. Comm’r*, T.C. Memo. 2016-43.

5 IRC § 6673(a)(1).

6 The standards for the IRS’s decision to seek sanctions under IRC § 6673(a)(1) are found in the Chief Counsel Directives Manual. See CCDM 35.10.2 (Aug. 11, 2004). For sanctions of any attorney or other person authorized to practice before the Tax Court, under IRC § 6673(a)(2), all requests for sanctions are reviewed by the designated agency sanctions officer (currently the Associate Chief Counsel (Procedure & Administration)). This review ensures uniformity on a national basis. See, e.g., CCDM 35.10.2.2.3 (Aug. 11, 2004).

7 “*Sua sponte*” means without prompting or suggestion; on its own motion. BLACK’S LAW DICTIONARY (10th ed. 2014). Thus, for conduct that it finds particularly offensive, the Tax Court can choose to impose a penalty under IRC § 6673 even if the IRS has not requested the penalty. See, e.g., *Williams v. Comm’r*, T.C. Memo. 2018-50, *appeal docketed*, No. 18-60536 (5th Cir. Aug. 1, 2018).

Taxpayers who institute actions under IRC § 7433<sup>8</sup> for certain unauthorized collection actions can be subject to a maximum penalty of \$10,000 if the court determines the taxpayer's position in the proceedings is frivolous or groundless.<sup>9</sup> In addition, IRC § 7482(c)(4),<sup>10</sup> §§ 1912 and 1927 of Title 28 of the U.S. Code,<sup>11</sup> and Rule 38 of the Federal Rules of Appellate Procedure<sup>12</sup> (among other laws and rules of procedure) authorize federal courts to impose penalties against taxpayers or their representatives for raising frivolous arguments or using litigation tactics primarily to delay the collection process. Because the sources of authority for imposing appellate-level sanctions are numerous and some of these sanctions may be imposed in non-tax cases, this report focuses primarily on the IRC § 6673 penalty.

Although outside of our reporting period, we note the recent Tax Court decision in the case of *Williams v. Commissioner*.<sup>13</sup> In *Williams*, the Tax Court considered whether IRC § 6751(b)(1) constrained the ability of the Tax Court to impose a penalty under IRC § 6673(a)(1). Section 6751(b)(1) generally prohibits the imposition of a penalty unless the penalty is approved, in writing, by the supervisor of the employee imposing the penalty or other higher level designee of the Secretary of Treasury.<sup>14</sup> Section 6673(a)(1) gives the authority to impose the penalty solely to the Tax Court, and permits the Tax Court to impose it either at the request of the Commissioner or *sua sponte* (of its own accord). The Tax Court looked to the legislative history of § 6751(b)(1) and § 6673(a)(1) to determine whether the two sections can coexist or whether § 6751(b)(1) supersedes § 6673(a)(1). The Tax Court found that the legislative intent behind § 6751(b)(1) was to prevent the IRS from using the threat of a penalty as a bargaining chip when negotiating with taxpayers, whereas the intent of § 6673(a)(1) was to dissuade taxpayers from wasting judicial resources. Because the Tax Court is not mentioned in § 6751(b)(1) or its legislative history, the Tax Court held that § 6751(b)(1) does not apply when it imposes a penalty pursuant to § 6673(a)(1).

## ANALYSIS OF LITIGATED CASES

We analyzed 19 opinions issued between June 1, 2017, and May 31, 2018, in which courts addressed the IRC § 6673 penalty. Eleven of these opinions were issued by the Tax Court and eight were issued by U.S. Courts of Appeals in cases brought by taxpayers seeking review of the Tax Court's imposition of the

8 IRC § 7433(a) allows a taxpayer a civil cause of action against the United States if an IRS employee intentionally or recklessly, or by reason of negligence, disregards any IRC provision or Treasury regulation in connection with collecting the taxpayer's federal tax liability.

9 IRC § 6673(b)(1).

10 IRC § 7482(c)(4) provides that the United States Courts of Appeals and the Supreme Court have the authority to impose a penalty in any case where the Tax Court's decision is affirmed and the appeal was instituted or maintained primarily for delay or the taxpayer's position in the appeal was frivolous or groundless.

11 28 U.S.C. § 1912 provides that when the Supreme Court or a United States Court of Appeals affirms a judgment, the court has the discretion to award to the prevailing party just damages for the delay, and single or double costs. 28 U.S.C. § 1927 authorizes federal courts to sanction an attorney or any other person admitted to practice before any court of the United States or any territory thereof for unreasonably and vexatiously multiplying proceedings; such person may be required to personally pay the excess costs, expenses, and attorneys' fees reasonably incurred because of his or her conduct.

12 Federal Rule of Appellate Procedure 38 provides that if a United States Court of Appeals determines an appeal is frivolous, the court may award damages and single or double costs to the appellee.

13 151 T.C. No. 1 (2018). This case will appear in the 2019 Most Litigated Issues section if Frivolous Issues is again a top ten issue, as the Tax Court imposed a penalty under § 6673(a)(1) for making frivolous arguments.

14 IRC § 6751(b)(2) provides an exception for additions to tax imposed under §§ 6651, 6654, or 6655. Or any other penalty automatically calculated through electronic means.

penalty. The Courts of Appeals sustained the Tax Court's position in all eight cases. Three decisions were issued by other courts on analogous penalties.<sup>15</sup>

In five cases, the Tax Court imposed penalties under IRC § 6673, with the amounts ranging from \$1,000 to \$10,000. In three cases, taxpayers prevailed when the IRS asked the court to impose a penalty. In most of these cases, the court warned the taxpayers not to bring similar arguments in the future.<sup>16</sup> All taxpayers appeared *pro se* (represented themselves) before the Tax Court, while one taxpayer was represented at the appellate level.<sup>17</sup> The taxpayers presented a wide variety of arguments that the courts have generally rejected on numerous occasions. Upon encountering these arguments, the courts almost invariably cited the language set forth in *Crain v. Commissioner*:

We perceive no need to refute these arguments with somber reasoning and copious citation of precedent; to do so might suggest that these arguments have some colorable merit. The constitutionality of our income tax system — including the role played within that system by the Internal Revenue Service and the Tax Court — has long been established.<sup>18</sup>

In the cases we reviewed, taxpayers raised the following issues that the courts deemed frivolous. Consequently, the taxpayers were subject to a penalty under IRC § 6673(a)(1) or other appellate level sanctions (or, in some cases, the court warned that such arguments were frivolous and could lead to a penalty in the future if the taxpayers maintained the same positions):

- **Taxes and procedures to collect taxes are unconstitutional:** We identified two cases this year where taxpayers made arguments that taxes or how they are collected are unconstitutional.<sup>19</sup> The taxpayer in *Schneider v. Commissioner* advanced common arguments regarding the constitutionality of the income tax and procedures to collect it, including that the income tax is an unconstitutional direct tax. The Court of Appeals for the Eighth Circuit affirmed the Tax Court's imposition of the IRC § 6673 penalty, and also imposed appellate level sanctions. In *Gardner v. Commissioner*, the taxpayer argued that the courts and the Commissioner of the IRS conspired to deny her First Amendment rights to free speech and freedom of religion.<sup>20</sup> In imposing a penalty of \$10,000, the Tax Court warned the taxpayer that if she continued to engage in similar tactics in the future, she would face a much larger penalty.
- **Taxpayers are not United States persons, they are exempt from the income tax, or wages are not income:** Taxpayers in at least five cases presented arguments that they are not United States persons subject to tax, they are exempt from tax for various reasons, or that wage income

15 We identified one decision in which the Court of Appeals addressed both the Tax Court's imposition of the IRC § 6673 penalty and an analogous appellate level penalty. *Schneider v. Comm'r*, 697 F. App'x 474 (8th Cir. 2017) (affirming a § 6673 penalty of \$2,500 and imposing an additional \$5,000 penalty). For purposes of the total number of cases reviewed for this report, we counted this case once. We reviewed a total of 21 cases for this reporting cycle.

16 See, e.g., *Lorusso v. Comm'r*, T.C. Memo. 2018-3. In declining to impose a penalty, the Tax Court noted that although the taxpayer had a history of litigation, the Tax Court had declined to warn the taxpayer in the past.

17 *Best v. Comm'r*, 702 F. App'x 615 (9th Cir. 2017), *aff'g* T.C. Memo. 2014-72, *reh'g, en banc, denied*, 2018 U.S. App. LEXIS 3452 (9th Cir., Feb. 14, 2018), *cert. denied*, 138 S. Ct. 2691 (June 25, 2018).

18 *Crain v. Comm'r*, 737 F.2d 1417, 1417-18 (5th Cir. 1984). See, e.g., *Jagos v. Comm'r*, T.C. Memo. 2017-202.

19 See *Schneider v. Comm'r*, 697 F. App'x 474 (8th Cir. 2017), *aff'g* No. 017566-14 (T.C. Sept. 1, 2016) and No. 029122-14 (T.C. Aug. 24, 2016), *cert. and reh'g denied*, 138 S. Ct. 1708 (2018); *Gardner v. Comm'r*, T.C. Memo. 2017-107.

20 See *Gardner v. Comm'r*, T.C. Memo. 2017-107. The taxpayers in this case were tax shelter promoters and the taxpayer wife argued that she could not receive income because she had taken a vow of poverty.

is not taxable.<sup>21</sup> In *Jagos v. Commissioner*, a taxpayer argued that only federal employees must pay income tax.<sup>22</sup> The court imposed a penalty of \$1,500.

## CONCLUSION

Taxpayers in the cases analyzed this year presented the same arguments raised and repeated year after year, which the courts routinely and universally reject.<sup>23</sup> Taxpayers avoided the IRC § 6673 penalty in only three cases where the IRS requested it. In these cases, the courts often warned the taxpayers not to bring similar arguments in the future, demonstrating the willingness of the courts to penalize taxpayers when they offer frivolous arguments or institute a case merely for delay. Where the IRS has not requested the penalty, the court may nonetheless raise the issue *sua sponte*, and in all cases identified either imposed the penalty or cautioned the taxpayer that similar future behavior will result in a penalty.<sup>24</sup>

As indicated in Appendix 3, Table 10, the penalty amount varies, regardless of the type of frivolous argument being raised. The Tax Court has indicated, however, that it can be lenient when it is the taxpayer's first court appearance.<sup>25</sup> Moreover, if the taxpayer has previously been sanctioned, the Tax Court may impose a higher penalty, but not necessarily close to the maximum.<sup>26</sup>

Finally, the U.S. Courts of Appeals have shown their willingness to uphold the penalties imposed by the Tax Court without fail in the cases analyzed for the period between June 1, 2017, and May 31, 2018, continuing a trend of upholding all penalties in cases we have analyzed since June 1, 2005.

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21 See, e.g., *Blair v. Comm'r*, T.C. Memo. 2017-153.

22 See *Jagos v. Comm'r*, T.C. Memo. 2017-202, *reh'g denied*, No. 18-1087 (6th Cir., Oct. 9, 2018).

23 See, e.g., National Taxpayer Advocate 2016 Annual Report to Congress 503-506.

24 See, e.g., *Zentmyer v. Comm'r*, T.C. Memo. 2017-197, *appeal docketed*, No. 18-72116 (9th Cir. July 26, 2018) (court raised the issue *sua sponte* and warned the taxpayer not to assert similar arguments in the future).

25 See, e.g., *Hawkbey v. Comm'r*, T.C. Memo. 2017-199.

26 See, e.g., *Fleming v. Comm'r*, T.C. Memo. 2017-155 (court imposed \$5,000 penalty after imposing \$1,500 in an earlier case).

## TAS Case Advocacy

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### OFFICE OF THE TAXPAYER ADVOCATE

Under Internal Revenue Code (IRC) § 7803(c)(2)(A), the Office of the Taxpayer Advocate, known as the TAS, has four principal functions:

- Assist taxpayers in resolving problems with the IRS;
- Identify areas in which taxpayers are experiencing problems with the IRS;
- Propose changes in the administrative practices of the IRS to mitigate problems taxpayers are experiencing with the IRS; and
- Identify potential legislative changes that may be appropriate to mitigate such problems.

The first function described in the statute relates to TAS's case advocacy, which involves assisting taxpayers with their cases by protecting taxpayer rights and reducing taxpayer burden.<sup>1</sup> The TAS Case Advocacy function is primarily responsible for direct contact with individual taxpayers, business taxpayers, tax-exempt entities, their representatives, and Congressional staff to resolve specific problems they are experiencing with the IRS. Information from these contacts and case results are vital to TAS's statutory mission to propose changes in the IRS's administrative practices to alleviate taxpayers' problems and to identify potential legislative changes to relieve such problems.<sup>2</sup> This section of the report discusses how TAS fulfills its mission to assist taxpayers with their specific issues and concerns involving IRS systems and procedures.<sup>3</sup>

### TAS CASE RECEIPT CRITERIA

Taxpayers typically seek TAS assistance with specific issues when:

- They experience a tax problem that causes financial difficulty;
- They are unable to resolve their issues directly with the IRS through normal channels; or
- An IRS action or inaction caused or will cause them to suffer a long-term adverse impact, including a violation of taxpayer rights.

TAS accepts cases in four categories: economic burden, systemic burden, best interest of the taxpayer, and public policy. See Figure 4.1.1, TAS Case Acceptance Criteria.

1 See Taxpayer Bill of Rights (TBOR), [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the Internal Revenue Code (IRC). See IRC § 7803(a)(3).

2 The National Taxpayer Advocate and her Attorney Advisors often use Case Advocacy's findings as the basis for many of the Most Serious Problems and Legislative Recommendations in the National Taxpayer Advocate's Annual Report to Congress.

3 TAS's other three functions involve identifying and proposing changes to systemic problems affecting taxpayers. TAS employees advocate systemically by: identifying IRS procedures that adversely affect taxpayer rights or create taxpayer burden; and recommending solutions, either administrative or legislative, to improve tax administration. (Note: taxpayers and practitioners can use the Systemic Advocacy Management System (SAMS) to submit systemic issues to TAS at [www.taxpayeradvocate.irs.gov/SAMS](http://www.taxpayeradvocate.irs.gov/SAMS)).

FIGURE 4.1.1

## TAS Case Acceptance Criteria

As an independent organization within the IRS, TAS helps taxpayers resolve problems with the IRS and recommends changes to prevent future problems. TAS fulfills its statutory mission by working with taxpayers to resolve problems with the IRS.<sup>1</sup> TAS case acceptance criteria fall into four main categories.

<b>Economic Burden</b>	Cases involving a financial difficulty to the taxpayer; an IRS action or inaction has caused or will cause negative financial consequences or have a long-term adverse impact on the taxpayer.
<b>Criteria 1</b>	The taxpayer is experiencing economic harm or is about to suffer economic harm.
<b>Criteria 2</b>	The taxpayer is facing an immediate threat of adverse action.
<b>Criteria 3</b>	The taxpayer will incur significant costs if relief is not granted (including fees for professional representation).
<b>Criteria 4</b>	The taxpayer will suffer irreparable injury or long-term adverse impact if relief is not granted.
<b>Systemic Burden</b>	Cases in which an IRS process, system, or procedure has failed to operate as intended, and as a result the IRS has failed to timely respond to or resolve a taxpayer issue. <sup>2</sup>
<b>Criteria 5</b>	The taxpayer has experienced a delay of more than 30 days to resolve a tax account problem.
<b>Criteria 6</b>	The taxpayer has not received a response or resolution to the problem or inquiry by the date promised.
<b>Criteria 7</b>	A system or procedure has either failed to operate as intended, or failed to resolve the taxpayer's problem or dispute within the IRS.
<b>Best Interest of the Taxpayer</b>	TAS acceptance of these cases will help ensure that taxpayers receive fair and equitable treatment and that their rights as taxpayers are protected. <sup>3</sup>
<b>Criteria 8</b>	The manner in which the tax laws are being administered raises considerations of equity, or have impaired or will impair the taxpayer's rights.
<b>Public Policy</b>	TAS acceptance of cases under this category will be determined by the National Taxpayer Advocate and will generally be based on a unique set of circumstances warranting assistance to certain taxpayers. <sup>4</sup>
<b>Criteria 9</b>	The National Taxpayer Advocate determines compelling public policy warrants assistance to an individual or group of taxpayers.

1 Internal Revenue Code (IRC) § 7803(c)(2)(A)(i).

2 TAS changed its case acceptance criteria to generally stop accepting certain systemic burden issues. See IRM 13.1.7.3(d) (Feb. 4, 2015).

3 See IRM 13.1.7.2.3 (Feb. 4, 2015).

4 See Interim Guidance Memorandum (IGM) TAS-0317-008, *Interim Guidance on Accepting Cases Under TAS Case Criteria 9, Public Policy* (Mar. 22, 2017).

In many of the economic burden cases, time is critical. If the IRS does not act quickly (*e.g.*, to remove a levy or release a lien), the taxpayer will experience additional economic harm.<sup>4</sup> Systemic burden cases include situations where an IRS process, system, or procedure has failed to resolve the taxpayer's issue.<sup>5</sup> Best interest of the taxpayer (Criteria 8) includes violations of the Taxpayer Bill of Rights (TBOR).<sup>6</sup>

With respect to public policy cases (Criteria 9), the National Taxpayer Advocate has the sole authority to determine which issues are included in this criterion and will designate them by memorandum. The National Taxpayer Advocate issued an Interim Guidance Memorandum (IGM) on March 22, 2017 (effective until March 22, 2019) that designated Criteria 9 cases include private debt collection; passport denial, revocation, or limitation; automatic exempt organization revocations due to failure to file an annual return or notice; and Congressional referred tax account-related inquiries that do not fit into any other category.<sup>7</sup>

### CASE RECEIPT TRENDS IN FISCAL YEAR 2018

In fiscal year (FY) 2018, TAS received 216,792 cases, over 49,000 more cases than received in FY 2017, an increase of almost 30 percent. TAS closed 198,820 cases. Of those closures, 1,119 were “quick closure” cases.<sup>8</sup> Quick closure cases are those that are resolved the same day without being assigned to a Case Advocate. These quick closures allow Case Advocates to focus on more complex cases requiring more analysis and multiple actions to resolve. Intake Advocates also resolved another 32,521 taxpayer calls without the need to establish a TAS case. TAS provided relief to taxpayers in approximately 79 percent of closed cases.<sup>9</sup> Another 10,866 taxpayers received relief directly from the IRS prior to TAS intervention.<sup>10</sup> Figure 4.1.2 compares FY 2017 and FY 2018 case receipts and relief rates by case acceptance category.

4 IRC § 7803(c)(2)(C)(ii); Internal Revenue Manual (IRM) 13.1.7.2.1, *TAS Case Criteria 1-4, Economic Burden* (Feb. 4, 2015).

5 IRC § 7803(c)(2)(C)(ii); IRM 13.1.7.2.2, *TAS Case Criteria 5-7, Systemic Burden* (Feb. 4, 2015).

6 IRC § 7803(c)(2)(C)(ii); IRM 13.1.7.2.3, *TAS Case Criteria 8, Best Interest of the Taxpayer* (Feb. 4, 2015). See TBOR, [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the IRC. See IRC § 7803(a)(3).

7 IRC § 7803(c)(2)(C)(ii); IRM 13.1.7.2.4, *TAS Case Criteria 9, TAS Public Policy* (Feb. 4, 2015). See IGM TAS-13-0317-008, *Interim Guidance on Accepting Cases Under TAS Case Criteria 9, Public Policy* (Mar. 22, 2017).

8 Data obtained from Taxpayer Advocate Management Information System (TAMIS) (Oct. 1, 2018).

9 *Id.*

10 *Id.*

**FIGURE 4.1.2, TAS Case and Intake Receipts and Relief Rates, FY 2017–2018<sup>11</sup>**

Case Categories	Receipts FY 2017	Receipts FY 2018	Percent Change	Relief Rates FY 2017	Relief Rates FY 2018	Percent Change
Economic Burden	90,868	124,755	37.3%	75.3%	76.7%	1.8%
Systemic Burden	75,795	91,160	20.3%	83.1%	81.7%	-1.7%
Best Interest of the Taxpayer	448	577	28.8%	82.4%	82.3%	-0.1%
Public Policy	225	300	33.3%	79.8%	83.0%	4.0%
<b>Subtotal</b>	<b>167,336</b>	<b>216,792</b>	<b>29.6%</b>	<b>78.9%</b>	<b>78.7%</b>	<b>-0.2%</b>
Calls Resolved by Intake Advocates	20,690	32,521	57.2%			
<b>Grand Total Receipts</b>	<b>188,026</b>	<b>249,313</b>	<b>32.6%</b>			

### Case Complexity

TAS monitors the complexity of its work to ensure it meets taxpayers' needs efficiently by assigning workload to match the skills of its employees. TAS measures case complexity in many ways, including whether a case involves multiple account-related issues or multiple tax periods and whether Case Advocates need technical advice, requiring more resources to resolve the matter.<sup>12</sup> TAS guidance requires Case Advocates to resolve all issues before closing a case.<sup>13</sup>

Case Advocates must identify primary and secondary core issue codes (PCIC and SCIC, respectively) on cases and record them in the Taxpayer Advocate Management Information System (TAMIS), to measure complexity.<sup>14</sup> TAS closed over 100,000 cases (51 percent of all closures) with one or more SCICs in FY 2018, a decrease from last year.<sup>15</sup> This decrease reflects a higher concentration of cases that generally involved a single issue, like wage verification, refund, and return processing issues, which usually involve a problem impacting a current year return only.<sup>16</sup> However, TAS continues to work complex cases requiring more resources, training, and direct time. In addition to providing technical advice in cases with multiple issues, TAS Technical Advisors assisted Case Advocates in understanding and resolving complex issues in over 9,600 TAS closed cases during FY 2018.<sup>17</sup>

11 Data obtained from TAMIS (Oct. 1, 2017; Oct. 1, 2018).

12 IRM 13.4.5.4, *Case Factors Screen* (Jul. 16, 2012). TAS uses a complexity factor screen in its case management system. This screen contains 24 factors, where the presence of any one of these factors indicates greater case complexity. For example, one factor is whether the case involves analysis of the assessment, collection, or refund statute date to determine if it is about to expire.

13 IRM 13.1.21.1.1, *Introduction* (Nov. 7, 2017).

14 IRM 13.1.16.13.1, *Issue Codes* (Mar. 28, 2017). IRM 13.1.16.13.1.2, *Primary Core Issue Code* (Mar. 28, 2017), states the primary core issue code (PCIC) is a three-digit code that defines the most significant issue, policy, or process within the IRS that underlies the cause of the taxpayer's problem. IRM 13.1.16.13.1.3, *Secondary Core Issue Code* (Mar. 28, 2017), states that the secondary core issue code (SCIC) identifies multiple issues involved in the case that TAS spent time researching or working to resolve. Additional factors may be identified as the case evolves.

15 Data obtained from TAMIS (Oct. 1, 2017; Oct. 1, 2018). In fiscal year (FY) 2017, 56 percent of closed cases reflected multiple issues.

16 *Id.*

17 Data obtained from TAMIS (Oct. 2, 2018).

### Most Prevalent Issues in TAS Cases, With a Focus on Economic Burden Cases

Figure 4.1.3 represents the top ten sources of TAS receipts by PCIC categories from all sources without regard to TAS criteria, comparing FY 2017 and FY 2018.<sup>18</sup>

**FIGURE 4.1.3, Top 10 Issues for Cases Received in TAS in FYs 2017–2018<sup>19</sup>**

Rank	Issue Description	FY 2017	FY 2018	FY 2018 Percent of Total	Percent Change FY 2017 to FY 2018
1	Pre-Refund Wage Verification Hold	20,014	66,048	30.5%	230.0%
2	Earned Income Tax Credit (EITC)	13,901	21,203	9.8%	52.5%
3	Identity Theft	23,248	13,787	6.4%	-40.7%
4	Processing Amended Returns	7,713	8,767	4.0%	13.7%
5	Unpostables and Rejects	4,942	8,673	4.0%	75.5%
6	Taxpayer Protection Program (TPP) Unpostables	6,906	7,947	3.7%	15.1%
7	Other Refund Inquiries and Issues	5,822	7,628	3.5%	31.0%
8	Open Audit (Not EITC)	3,959	5,823	2.7%	47.1%
9	Processing Original Returns	5,434	5,312	2.5%	-2.2%
10	Health Insurance Premium Tax Credit for Individuals under IRC § 36B	4,643	4,833	2.2%	4.1%
Other TAS Receipts <sup>20</sup>		70,754	66,771	30.8%	-5.6%
<b>Total TAS Receipts</b>		<b>167,336</b>	<b>216,792</b>		<b>29.6%</b>

### Economic Burden Cases

Economic burden (EB) cases often occur where an IRS action or inaction has caused or will cause negative financial consequences or have a long-term adverse impact on the taxpayer. More than half of TAS's case receipts continue to involve taxpayers experiencing EB.<sup>21</sup> Because these taxpayers face potential immediate adverse financial consequences, TAS requires employees to work the cases using accelerated timeframes.<sup>22</sup>

Figure 4.1.4 shows the top five issues driving EB receipts. TAS dedicates significant resources to resolving the systemic causes of these issues, and as discussed in the Most Serious Problems section of this and past reports, provides recommendations to the IRS to improve processes that cause taxpayers to experience economic or systemic burden.<sup>23</sup>

18 TAMIS Coding Reference Guide (Sept. 4, 2017).

19 Data obtained from TAMIS (Oct. 1, 2017; Oct. 1, 2018).

20 The "Other TAS Receipts" category encompasses the remaining 118 PCICs not in the top ten.

21 For the seventh consecutive FY, more than half of TAS's case receipts involve taxpayers' experiencing Economic Burden (EB). Data obtained from TAMIS (Oct. 1, 2012; Oct. 1, 2013; Oct. 1, 2014; Oct. 1, 2015; Oct. 1, 2016; Oct. 1, 2017; Oct. 1, 2018).

22 IRM 13.1.18.3(1), *Initial Contact* (May 5, 2016). The TAS employee is to contact the taxpayer or representative by telephone within three workdays of the taxpayer advocate received date (TARD) for criteria 1-4 cases and within five workdays of the TARD for criteria 5-9 cases to notify the taxpayer of TAS's involvement. Per IRM 13.1.18.1.1, *Working TAS Cases* (Feb. 1, 2011), TAS's policy is that cases involving EB will be worked sooner than other cases.

23 See Most Serious Problem: *Economic Hardship: The IRS Does Not Proactively Use Internal Data to Identify Taxpayers at Risk of Economic Hardship Throughout the Collection Process*, *supra*.

**FIGURE 4.1.4, Top Five Issues Causing Economic Burden, FY 2017–2018<sup>24</sup>**

Rank	Issue Description	FY 2017	EB Receipts as % Total EB Receipts for Issue FY 2017	FY 2018	EB Receipts as % Total EB Receipts for Issue FY 2018	EB Percent Change FY 2017 to FY 2018
1	Pre-Refund Wage Verification Hold	11,329	12.5%	45,834	36.7%	304.6%
2	Earned Income Tax Credit	10,937	12.0%	15,637	12.5%	43.0%
3	Identity Theft	13,360	14.7%	8,217	6.6%	-38.5%
4	Unpostables and Rejects	3,686	4.1%	5,947	4.8%	61.3%
5	Taxpayer Protection Program Unpostables	4,217	4.6%	5,237	4.2%	24.2%

### Pre-Refund Wage Verification Hold (PRWVH)

In FY 2018, Pre-Refund Wage Verification Hold (PRWVH) issues replaced Identity Theft as the number one reason taxpayers seek TAS assistance and accounted for nearly 31 percent of TAS casework.<sup>25</sup> TAS experienced a 230 percent increase in PRWVH case receipts and a 305 percent increase in EB PRWVH case receipts compared to the same period in 2017.<sup>26</sup> Over 69 percent of TAS's PRWVH cases were taken into TAS inventory as an economic burden, cases requiring expedite handling.<sup>27</sup>

To prevent issuing fraudulent refunds, the IRS employs various models and data mining techniques. The PRWVH is one of those techniques. Through that process, the IRS's Return Integrity Operations (RIO) organization delays issuing refunds until wage and withholding reported on the return can be verified. In the past, the IRS's actions have raised significant taxpayer rights issues and brought an increasing number of taxpayers to TAS.<sup>28</sup> In FY 2018, TAS experienced a surge in PRWVH cases as shown in Figure 4.1.5.

<sup>24</sup> Data obtained from TAMIS (Oct. 1, 2017; Oct. 1, 2018).

<sup>25</sup> *Id.*

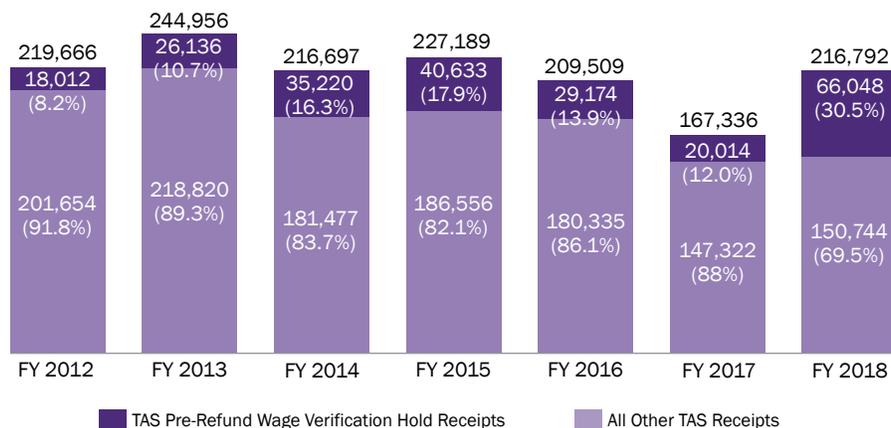
<sup>26</sup> *Id.* For a detailed discussion, see Most Serious Problem: *False Positive Rates: The IRS's Fraud Detection Systems Are Marred by High False Positive Rates, Long Processing Times, and Unwieldy Processes Which Continue to Plague the IRS and Harm Legitimate Taxpayers*, *supra*.

<sup>27</sup> Data obtained from TAMIS (Oct. 1, 2018).

<sup>28</sup> See also Most Serious Problem: *False Positives Rates: The IRS's Fraud Detection Systems Are Marred by High False Positive Rates, Long Processing Times, and Unwieldy Processes Which Continue to Plague the IRS and Harm Legitimate Taxpayers*, *supra*; National Taxpayer Advocate 2015 Annual Report to Congress 45–55 (Most Serious Problem: *Revenue Protection: Hundreds of Thousands of Taxpayers File Legitimate Tax Returns That Are Incorrectly Flagged and Experience Substantial Delays in Receiving Their Refunds Because of an Increasing Rate of "False Positives" Within the IRS's Pre-Refund Wage Verification Program*). For additional discussion, see National Taxpayer Advocate FY 2016 Objectives Report to Congress 143–145 (Area of Focus: *TAS Receipts Suggest the IRS Needs to Enhance Efforts to Detect and Prevent Refund Fraud*).

FIGURE 4.1.5<sup>29</sup>

## Pre-Refund Wage Verification Hold Receipts, FYs 2012-2018



When information reported on the taxpayer's return closely matched income and credit information in IRS systems, TAS provided a weekly listing of the cases to RIO, requesting they be reviewed, and the refunds released. This process, known as a Bulk Operations Assistance Request (OAR) provided an efficient way to provide relief in simple cases.<sup>30</sup> TAS sent 3,275 cases to RIO on Bulk OARs. If the information reported on the taxpayer's return did not match the information in IRS systems, TAS worked with the taxpayer and RIO to either confirm or correct the income reported on the return, using their existing procedures.<sup>31</sup>

TAS provided full or partial relief to taxpayers in 79 percent of PRWVH cases.<sup>32</sup> However, during FY 2018, TAS had to issue 469 Taxpayer Assistance Orders (TAOs) in cases involving PRWVH issues when RIO was unable to keep up with the backlog of OARs sent by TAS on cases requiring verification or correction. Of the 469 TAOs issued, 461 were complied with and eight were rescinded. Without TAS intervention, these taxpayers may have waited months for their refunds to be released or adjusted. TAS continues to work with RIO to identify improvements to existing procedures and find more efficient treatment streams to provide relief to taxpayers.<sup>33</sup>

29 Data obtained from TAMIS (Oct. 1, 2012; Oct. 1, 2013; Oct. 1, 2014; Oct. 1, 2015; Oct. 1, 2016; Oct. 1, 2017; Oct. 1, 2018).

30 For more information on how TAS uses OARs to resolve taxpayer issues, see TAS Operations Assistance Request (OAR) Trends, *infra*.

31 See IRM 25.25.3, *Revenue Protection Verification Procedures for Individual Master File Returns* (Sept. 17, 2018).

32 Data obtained from TAMIS (Oct. 1, 2018).

33 For additional information about fraud detection see Most Serious Problem: *False Positive Rates: The IRS's Fraud Detection Systems Are Marred by High False Positive Rates, Long Processing Times, and Unwieldy Processes Which Continue to Plague the IRS and Harm Legitimate Taxpayers*, *supra*. See also Nina E. Olson, *IRS Fraud Detection – A Process That is Challenging for Taxpayers to Navigate with an Outdated Case Management System Resulting in Significant Delays of Legitimate Refunds, Part 1*, NTA Blog, <https://taxpayeradvocate.irs.gov/news/nta-blog-irs-fraud-detection-process-is-challenging-for-taxpayers-to-navigate-part-1?category=Tax News>, (Dec. 6, 2018); Nina E. Olson, *IRS Fraud Detection – A Process That is Challenging for Taxpayers to Navigate with an Outdated Case Management System Resulting in Significant Delays of Legitimate Refunds, Part 2*, NTA Blog, <https://taxpayeradvocate.irs.gov/news/nta-blog-irs-fraud-detection-process-is-challenging-for-taxpayers-to-navigate-part-2?category=Tax News>, (Dec. 12, 2018).

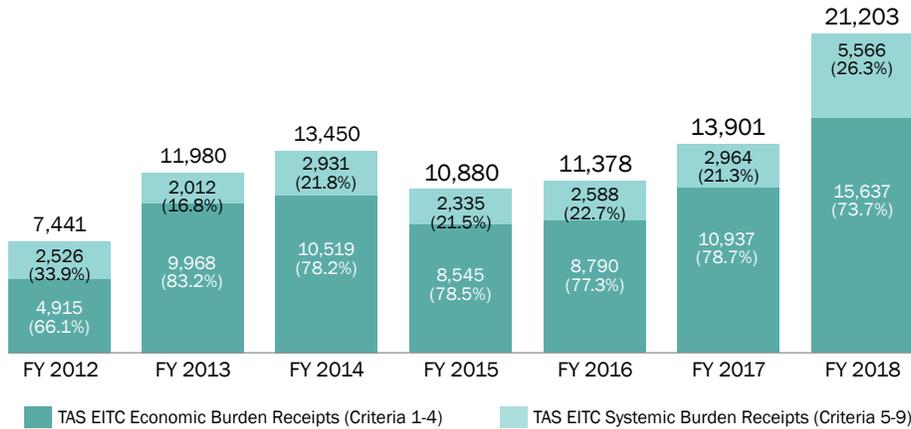
## Earned Income Tax Credit (EITC) Cases

The Earned Income Tax Credit (EITC) is a complex refundable tax credit for working low income taxpayers.<sup>34</sup> Certain limitations apply to the EITC related to residency,<sup>35</sup> filing status,<sup>36</sup> certain foreign benefits,<sup>37</sup> and status as a qualifying child of another taxpayer.<sup>38</sup> The enactment of the Protecting Americans from Tax Hikes Act of 2015 (PATH Act) required the IRS to hold the entire refund when any portion of the refund was composed of EITC to allow the IRS to verify internal data and information from the Social Security Administration—before paying out refunds.<sup>39</sup>

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- 34 IRC § 32. The maximum amount of the credit is available to a taxpayer with three or more qualifying children. For Tax Year 2018, the maximum credit available for a taxpayer with one qualifying child is \$3,461, with two qualifying children is \$5,716, with three or more qualifying children is \$6,431, and with no qualifying children is \$519. Rev. Proc. 2017-58, 2017-45 I.R.B. 489. An individual must meet five tests in order to be a qualifying child under IRC § 152(c): relationship, age, residency, support, and no joint return filed with the individual's spouse. An individual meets the **relationship** test to be a qualifying child if the individual is a child of the taxpayer or a descendant of a child of the taxpayer or a brother, sister, stepbrother or stepsister of the taxpayer or a descendant of such a relative, IRC § 152(c)(2). The term "child" means an individual who is a son, daughter, stepson, or stepdaughter of the taxpayer or an eligible foster child of the taxpayer. IRC § 152(f)(1)(A). A child legally adopted by a taxpayer or a child lawfully placed with a taxpayer for legal adoption is treated as a child of the taxpayer by blood. IRC § 152(f)(1)(B). An eligible foster child means an individual who is placed with the taxpayer by an authorized placement agency or by judgment, decree, or other order of any court of competent jurisdiction. IRC § 152(f)(1)(C). The terms "brother" and "sister" include a half-brother or a half-sister. IRC § 152(f)(4). To meet the **age** requirement, to be a qualifying child, an individual must be under the age of 19 at the end of the year, under the age of 24 at the end of the year and a "student," as defined in IRC § 152(f)(2), or any age if "permanently and totally disabled," as defined in IRC § 22(e)(3). IRC § 152(c)(3). To meet the **residency** requirement to be a qualifying child, an individual must have the same principal place of abode as the taxpayer for more than half of the taxable year. IRC § 152(c)(1)(B). See, however, IRC § 152(e) for a special rule for a child of parents who are divorced or separated or who live apart and IRC § 152(f)(6) for rules on the treatment of missing children. See also the regulations under section 152 for rules on temporary absences, children who were placed with the taxpayer in foster care or for adoption during the taxable year, or children who were born or died during the taxable year. To meet the **support** test to be a qualifying child, an individual must not have provided more than one-half of his or her own support for the calendar year in which the taxable year of the taxpayer begins. IRC § 152(c)(1)(D). The individual must not have filed a joint return with the individual's spouse for the taxable year in question. IRC § 152(c)(1)(E). For additional information about the Earned Income Tax Credit (EITC), see Most Serious Problem: *Improper Earned Income Tax Credit Payments: Measures the IRS Takes to Reduce Improper Earned Income Tax Credit Payments Are Not Sufficiently Proactive and May Unnecessarily Burden Taxpayers*, *supra*.
- 35 A taxpayer is not eligible for the EITC if he or she is a nonresident alien for any portion of the taxable year, unless the taxpayer files a joint return with a spouse who is a United States citizen or resident alien. IRC § 32(c)(1)(D).
- 36 A taxpayer is not eligible for the EITC if he or she files married filing separately. IRC § 32(d).
- 37 A taxpayer is not eligible for the EITC if he or she claims a foreign earned income exclusion or deducts or excludes a foreign housing cost amount. IRC § 32(c)(1)(C).
- 38 A taxpayer is not eligible for the EITC if he or she is the qualifying child of another taxpayer. IRC § 32(c)(1)(B).
- 39 Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Div. Q, Title II, § 201(a), 129 Stat. 2242, 3076 (2015) (codified at IRC §§ 6071(c) and 6402(m)) accelerated the due dates for filing Forms W-2, *Wage and Tax Statement*, and 1099-MISC, *Miscellaneous Income* to January 31 of the year following the taxable year and mandated a delay of any refund that includes a claim for EITC until February 15 of the year following the taxable year.

FIGURE 4.1.6<sup>40</sup>

**TAS Earned Income Tax Credit Economic and Systemic Burden Case Receipts, FYs 2012-2018**



Nearly ten percent of TAS case receipts involved EITC issues in FY 2018.<sup>41</sup> TAS experienced a nearly 53 percent increase in EITC cases from FY 2017 to FY 2018.<sup>42</sup> Over 73 percent of EITC cases were ones in which the taxpayer was experiencing EB. TAS analyzed the underlying cause for the increase in a study of TAS FY 2018 EITC case receipts through May 31, 2018,<sup>43</sup> and found the increase was primarily due to extensive delays in IRS evaluating the taxpayers’ documentation submitted during the audit process.

- In 32 percent of the tax years reviewed, RIO referred the returns to Examination after an inability to verify income in the PRWVH process.
- In 49 percent of the tax years reviewed, Examination selected the return to conduct a full scope pre-refund audit.<sup>44</sup>

The IRS audit process generally establishes a 30-day time frame to respond to taxpayer correspondence.<sup>45</sup> TAS found:

- In at least 15 percent of the tax years reviewed, the taxpayers submitted correspondence to the IRS 65 or more days prior to contacting TAS with no Examination determination; and

40 Data obtained from TAMIS (Oct. 1, 2012; Oct. 1, 2013; Oct. 1, 2014; Oct. 1, 2015; Oct. 1, 2016; Oct. 1, 2017; Oct. 1, 2018).

41 Data obtained from TAMIS (Oct. 1, 2018). This is the second highest category of case receipts in FY 2018, after Pre-Refund Wage Verification Hold (PRWVH), eclipsing Identity Theft.

42 Data obtained from TAMIS (Oct. 1, 2017; Oct. 1, 2018).

43 The study contained a population of 9,589 Open EITC Audit TAS case receipts. In some instances, the cases involved more than one tax year. TAS randomly selected 352 TAS case receipts (which involved 372 tax years). The random sample had a 95 percent confidence level with a confidence interval of +/- 5. Data obtained from TAMIS (June 1, 2018).

44 In 182 tax years, the cases had Audit Information Management System (AIMS) Project Codes 261, 289, and 623.

45 IRM 4.19.13.11, *Monitoring Overaged Replies* (Feb. 9, 2018).

- Taxpayers waited more than 106 days before the IRS reviewed their correspondence in nearly nine percent of tax years reviewed.<sup>46</sup>

On September 1, 2017, the IRS released new guidance to permit Campus Examination Operations to increase the number of days to respond beyond the normal timeframes to taxpayer's correspondence. Prior to the new guidance, Exam issued Letter 3500, *Interim Letter to Correspondence from Taxpayer*, to notify taxpayers of the IRS's receipt of their mail and advise them that IRS will respond within 75 days from receipt of their correspondence.<sup>47</sup> During peak periods, Exam may now notify taxpayers of a response beyond 75 days using their reports on the average number of days to review taxpayer correspondence.<sup>48</sup> Since most EITC cases are EB receipts, 75 days is unacceptable and taxpayers should not have to wait additional days beyond the normal 30 day timeframe. Taxpayers have a right to quality service and a right to finality.<sup>49</sup> This modification in Examination guidance adds to the burden taxpayers already face with the hold on their refund until February 15, after Examination has been slow in selecting the return and after the taxpayer has sent the information. The Examination delays violate taxpayer rights and have the potential to cause more harm to taxpayers.

### Identity Theft

In recent years, there has been a downward trend in individual taxpayers reporting that they have been victims of tax-related identity theft. As of September 30, 2018, the IRS-wide inventory of unresolved identity theft cases was just over 31,500, a 12 percent decrease from the previous year.<sup>50</sup> TAS has worked closely with the IRS to address and improve treatment of victims and implement processes designed to prevent fraudulent returns from posting to a victim's account, which has resulted in a steady decline in TAS case receipts.<sup>51</sup> TAS's identity theft receipts have been on the decline since FY 2015, when TAS received 56,174 cases and took an average of 68 days to work a case. In FY 2018, TAS received 13,787 cases and took 79 days to work a case.<sup>52</sup> While fewer taxpayers are coming to TAS seeking assistance with identity theft, those taxpayers that do seek our assistance face serious problems, leading to longer cycle times to resolve. Erroneous information resulting from identity theft can impact a victim's account for several tax periods, cause multiple issues, and can require coordinated actions by various IRS employees.

46 The EITC study found 343 tax years were open on the AIMS prior the TARD. Exam uses AIMS Status Codes to monitor the status of the audit. In 22 of the 343 tax years, the case had an AIMS Status Code 55, meaning the IRS received the taxpayer correspondence, but did not make a determination within 65 to 115 days. In 30 of the tax years, there was an AIMS Status Code 57, meaning the IRS received the taxpayer correspondence, but did not make a determination in more than 115 days.

47 IRM 4.19.13.10.1 (Sept. 1, 2017). The 75 days is calculated by adding 45 days to the normal 30-day time frame to respond to the taxpayer's correspondence.

48 IRM 4.19.13.10.1, Letter 3500, *Interim Letter, When Additional Time to Reply is Needed* (Sept. 1, 2017), renumbered to IRM 4.19.13.11.1 (Feb. 2, 2018).

49 See TBOR, [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the IRC. See IRC § 7803(a)(3).

50 IRS, *ID Theft Report* (Sept. 2018).

51 National Taxpayer Advocate 2015 Annual Report to Congress 180-187 (Most Serious Problem: *Identity Theft (IDT): The IRS's Procedures for Assisting Victims of IDT, While Improved, Still Impose Excessive Burden and Delay Refunds for Too Long*).

52 Data obtained from TAMIS (Oct. 1, 2017; Oct. 1, 2018).

## EMERGING ISSUES

### Taxpayers Continue to Face Serious Challenges When Requesting Individual Taxpayer Identification Numbers (ITIN)

For several years, the National Taxpayer Advocate has written about the problems created by the IRS's administration of the Individual Taxpayer Identification Numbers (ITIN) program.<sup>53</sup> In a recent blog, the National Taxpayer Advocate stated that, as a result of changes from the Tax Cuts and Jobs Act (TCJA),<sup>54</sup> the IRS has a major opportunity to make needed adjustments to the ITIN program.<sup>55</sup> First, the IRS could relax its strict requirement that taxpayers must apply for a new ITIN with a paper tax return during the filing season to show a tax administration purpose for the ITIN. Second, the IRS should reconsider its limitations on Certifying Acceptance Agents and Taxpayer Assistance Centers that prevent them from certifying all identification documents, so applicants could avoid sending original documents to the IRS, risking loss of documents. Finally, the IRS should reconsider the mail service it uses to return original identification documents since the number of ITIN applications is projected to plummet.

TAS has seen the devastating effects that requiring applicants to send original identification documents, and the potential loss of those documents, can have on taxpayers. TAS received a case from a parent who was a citizen of another country and was working in the U.S. on a visa.<sup>56</sup> The taxpayer applied for and was issued an ITIN for his young child but never received the child's passport and U.S. entry visa back from the IRS, leaving the child without legal identification and creating significant problems for the family. To apply for a new passport for the child, the parents and child would be required to travel back to their home country to receive a U.S. entry visa. Under the family's terms of admission into the U.S., they would have to leave the country and return in early 2019. The family had planned to take a short vacation to a contiguous country but without an entry visa for their child, they were required to return to their home country and go through the entire visa application and interview process again. Including airfare, accommodations, and living expenses, the estimated costs were approximately \$7,000, funds they did not have. This case shows how the IRS's mailing of original ID documents with no tracking system significantly harms taxpayers.<sup>57</sup>

Unfortunately, this was not an isolated experience. TAS reviewed 1,738 cases received between March 15, 2015 and March 15, 2017 where taxpayers came to TAS asking for assistance with recovering their passports or other original documents submitted with Form W-7, *Application for IRS Individual Taxpayer Identification Number*.<sup>58</sup> In over 200 cases, the response from the ITIN unit was that the

53 An individual taxpayer identification number (ITIN) is a 9-digit number issued by the IRS to individuals who are not eligible for a Social Security number. For a discussion of how the IRS fails to analyze the unique characteristics of the ITIN population and understand their needs, see National Taxpayer Advocate 2017 Annual Report to Congress 181-194 (Most Serious Problem: *Individual Taxpayer Identification Numbers (ITINs): The IRS's Failure to Understand and Effectively Communicate with the ITIN Population Imposes Unnecessary Burden and Hinders Compliance*).

54 Pub. L. No. 115-97, 131 Stat. 2054 (2017).

55 Nina E. Olson, *Now is the Perfect Time for the IRS to Make Improvements to the Individual Taxpayer Identification Number Program*, NTA BLOG, [https://taxpayeradvocate.irs.gov/news/nta-blog-ITIN-Improvements?category=Tax News](https://taxpayeradvocate.irs.gov/news/nta-blog-ITIN-Improvements?category=Tax+News) (Oct. 31, 2018).

56 In this instance, the taxpayer has provided written consent under IRC § 6103(c) for the National Taxpayer Advocate to use facts specific to the taxpayer's case. Release signed by the taxpayer on Oct. 27, 2018 and on file with TAS.

57 Late in 2018, after nearly five months, two physical inspections of the IRS ITIN unit by TAS employees, and multiple records searches and Taxpayer Assistance Orders (TAOs), as well as TAS conversations with the Department of State and home country officials, inexplicably the taxpayer received the child's passport in the mail. However, because the passport was reported lost, the passport was cancelled and the taxpayer and family must still return to their home country for a new visa and passport.

58 Data obtained from TAMIS (Oct. 1, 2018).

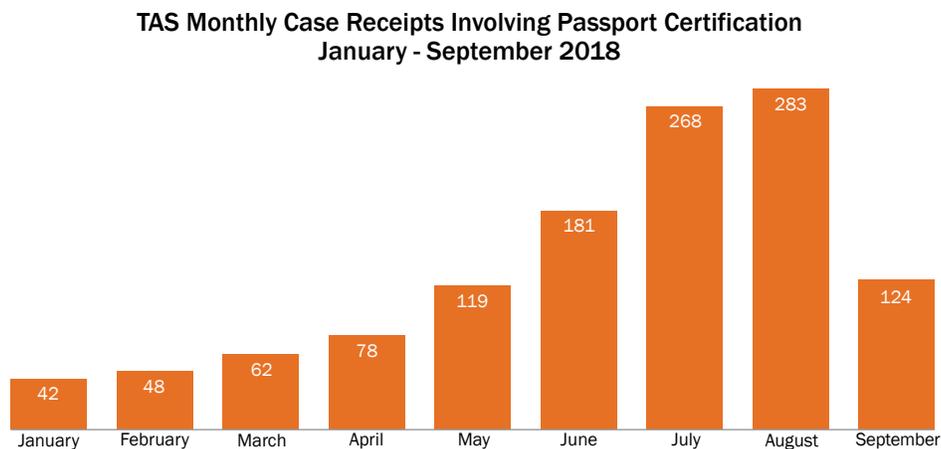
passport was not located or was already forwarded to the Embassy for the country of origin. There are likely more taxpayers who have been harmed and did not ask TAS for assistance. Through outreach efforts TAS will continuously work to reach underserved taxpayers and ensure that taxpayers have access to TAS at the earliest possible time.

### Passport Certification Due to Seriously Delinquent Tax Debt

In 2015, Congress passed the Fixing America's Surface Transportation (FAST) Act, which requires the Department of State to deny an individual's passport application and allows the Department of State to revoke or limit an individual's passport if the IRS has certified the individual as having a seriously delinquent tax debt.<sup>59</sup>

The IRS began certifying taxpayers with seriously delinquent tax debt in January 2018. By October 5, 2018, the IRS had certified 290,181 taxpayers to the Department of State.<sup>60</sup> TAS case receipts involving passport issues rose and fell in tandem with taxpayers certified by the IRS.

**FIGURE 4.1.7**<sup>61</sup>



In April 2018, the National Taxpayer Advocate issued guidance to TAS employees on advocating for taxpayers with a seriously delinquent tax debt, including when and how to issue TAOs in appropriate cases.<sup>62</sup> The guidance directs Local Taxpayer Advocates (LTAs) to issue TAOs in three situations:

- Delay the IRS from certifying an otherwise eligible taxpayer while TAS actively works with the taxpayer to resolve the debt;
- Resolve the taxpayer's seriously delinquent debt by meeting a certification exclusion, proving the certification was erroneous, or showing the taxpayer did not owe the liability; and

59 Fixing America's Surface Transportation (FAST) Act, Pub. L. No. 114-94, Div. C, Title XXXII, § 32101, 129 Stat. 1312, 1729-1733 (2015) (codified as IRC § 7345).

60 Email from the IRS in response to a TAS data request (Oct. 4, 2018).

61 Data obtained from TAMIS (Oct. 1, 2018). Monthly passport cases include cases with passport certification as a secondary issue code, since TAS uses the debt resolution sought by the taxpayer as the primary issue.

62 TAS-13-0418-0001, *Advocating for Taxpayers Facing Passport Revocation/Denial*, [https://www.irs.gov/pub/foia/ig/spder/tas-13-0418-0001\\_passport\\_igm.pdf.pdf](https://www.irs.gov/pub/foia/ig/spder/tas-13-0418-0001_passport_igm.pdf.pdf) (Apr. 26, 2018).

- Decertify the taxpayer when IRS systems fail to do so systemically or when the taxpayer has plans for foreign travel or other urgent need for their passport.

Figure 4.1.8 reflects the disposition of these three types of passport related TAOs TAS issued in FY 2018.

**FIGURE 4.1.8, Dispositions of FY 2018 TAOs Issued for Passport Related Issues as of October 4, 2018**<sup>63</sup>

TAO Disposition/Type of TAO	TAO Blocks Certification While TAS Works with Taxpayer to Resolve Debt	TAO to Resolve Debt, Apply Exclusion, or Correct Error to Remove Taxpayer from Certification Criteria	TAO Orders Manual or Expedite Decertification	Total
IRS Complied with the TAO	740	9	12	761
IRS Complied After the TAO Was Modified	8	1	0	9
TAS Rescinded the TAO	4	3	3	10
TAS TAO Pending (in process)	24	6	4	34
<b>Total</b>	<b>776</b>	<b>19</b>	<b>19</b>	<b>814</b>

Included in the 776 TAOs to block certification are 753 TAOs issued by the National Taxpayer Advocate on January 16, 2018, ordering the IRS Small Business/Self-Employed Division (SB/SE) to apply its broad discretionary authority and proactively exclude from certification taxpayers who were already working with TAS to resolve their tax debt at the time of certification.<sup>64</sup>

The National Taxpayer Advocate previously reported that the IRS is failing to provide adequate notice prior to certifying the taxpayer's seriously delinquent tax debt, which is an infringement on taxpayer rights and constitutional due process protections.<sup>65</sup> The National Taxpayer Advocate blogged about three examples from TAS cases that demonstrate the direct negative consequences of not providing a stand-alone notice prior to certification.<sup>66</sup>

### Form 4466 and Section 965 Transition Tax

Corporations, like individuals, must pre-pay their tax liabilities by making estimated tax payments throughout the year, but they frequently overpay for a variety of reasons, including to minimize the risk they may become liable for underpayment interest. If that happens, a corporation or an individual can file a return and claim a refund. However, unlike an individual, if the corporation needs the money before it has all of the information available to file its tax return it can file a Form 4466, *Corporation*

<sup>63</sup> Data obtained from TAMIS (Oct. 4, 2018).

<sup>64</sup> See National Taxpayer Advocate FY 2019 Objectives Report to Congress 80-113 (Area of Focus: *Some IRS Procedures for the Certification Program Related to Denial or Revocation of Passports Ignore Legislative Intent and Impair Taxpayer Rights*) for a more complete discussion of these TAOs and the Taxpayer Advocate Directive the Deputy Commissioner for Services and Enforcement rescinded on May 17, 2018 that would have precluded the need for these TAOs.

<sup>65</sup> National Taxpayer Advocate 2017 Annual Report to Congress 75-77 (Most Serious Problem: *Passport Denial and Revocation: The IRS's Plans for Certifying Seriously Delinquent Tax Debts Will Lead to Taxpayers Being Deprived of a Passport Without Regard to Taxpayer Rights*).

<sup>66</sup> Nina E. Olson, *TAS Cases Demonstrate the Harm Caused by IRS Policies on Passport Certification*, NTA Blog, <https://taxpayeradvocate.irs.gov/news/nta-blog-tas-cases-demonstrate-the-harm-caused-by-irs-policies-on-passport-certification?category=Tax%20News> (Aug. 22, 2018).

*Application for Quick Refund of Overpayment of Estimated Tax.*<sup>67</sup> Because of the way the IRS issued information about and administered the so called “transition tax” that was enacted as part of the TCJA on December 22, 2017, and codified at IRC § 965, some corporations made extra payments for 2017 that they could not recover.<sup>68</sup> Under IRC § 965(h) taxpayers could elect to pay the transition tax over an eight-year period without interest. The IRS provided guidance about IRC § 965 by posting Frequently Asked Questions (FAQs) and Answers on its website. In mid-March, the IRS posted “FAQ 10,” advising taxpayers to pay 2017 transition tax liabilities separately from other liabilities. FAQ 10 prompted some who had already paid more than enough, to make extra transition tax payments, which they assumed they could recover just like any other estimated tax overpayments. In some cases, they had paid enough to satisfy their regular tax liability plus the entire transition tax. Approximately a month after issuing FAQ 10 and a few business days before the filing and estimated tax payment deadline, the IRS posted new “FAQs 13 and 14” clarifying that if a taxpayer made payments in excess of its regular tax liability plus the first installment of the transition tax, the IRS would treat the excess as a prepayment of future installments of the transition tax liability that the taxpayer had elected to pay in future years.<sup>69</sup> After the National Taxpayer Advocate questioned the reasons underlying FAQs 13 and 14, the IRS Office of Chief Counsel released a memorandum that supplied its reasoning.<sup>70</sup> The memo concluded that there was no overpayment for it to refund or credit unless and until the taxpayer’s payments exceed the entire 2017 liability, including the 2017 transition that the taxpayer had elected to pay in future years.

TAS learned that the IRS also planned to deny Form 4466 applications by corporations whose estimated tax payments did not exceed both their regular tax liability and their entire transition tax liability. TAS asked the IRS Office of Chief Counsel to address a different legal question—whether the IRS had the legal authority to refund amounts requested on Form 4466 before any assessment for 2017 had been made—before denying those applications.<sup>71</sup> In TAS’s view the IRS had considerably more leeway to conclude that it was authorized to return funds when no tax or transition tax liability had been assessed. Moreover, a conclusion that it could not return them would run contrary to Congressional intent, which was to allow taxpayers to make transition tax payments over an eight-year period.<sup>72</sup> According to the IRS’s interpretation, those corporations who paid enough to satisfy the entire transition tax liability will not receive any of the benefits Congress provided by enacting IRC § 965(h).

TAS issued eight TAOs on behalf of taxpayers who made the IRC § 965(h) election and filed Forms 4466.<sup>73</sup> The TAOs generally ordered the IRS to refrain from processing the taxpayer’s Form 4466 pending further discussions between TAS and the IRS. Several of the TAOs were elevated to the National Taxpayer Advocate. As a result of TAS’s advocacy in these cases, those at the highest levels of the IRS, the Office of Chief Counsel, and Treasury considered the matter and informed TAS that, in their view, the IRS was not authorized to pay the refunds. In that way, the IRS complied with the

67 Per IRC § 6425, the overpayment must be at least ten percent of the expected tax liability and at least \$500.

68 Pub. L. No. 115-97, § 14103, 131 Stat. 2054, 2195 (2017).

69 IRS, *Questions and Answers about Reporting Related to Section 965 on 2017 Tax Returns*, <https://www.irs.gov/newsroom/questions-and-answers-about-reporting-related-to-section-965-on-2017-tax-returns> (FAQs 13 and 14, posted Apr. 13, 2018). Due to computer problems, the due date was extended to April 18. IR-2018-100 (Apr. 17, 2018).

70 See Program Manager Technical Assistance (PMTA) 2018-16 (Aug. 2, 2018), [https://www.irs.gov/pub/iraoa/pmta\\_2018\\_16.pdf](https://www.irs.gov/pub/iraoa/pmta_2018_16.pdf).

71 See Nina E. Olson, *IRS Administration of the Section 965 Transition Tax Contravenes Congressional Intent and Imposes Unintended Burden on Taxpayers*, NTA Blog, [https://taxpayeradvocate.irs.gov/news/nta-blog-irs-administration-of-the-section-965-transition-tax-contravenes-congressional-intent-and-imposes-unintended-burden-on-taxpayers?category=Tax News](https://taxpayeradvocate.irs.gov/news/nta-blog-irs-administration-of-the-section-965-transition-tax-contravenes-congressional-intent-and-imposes-unintended-burden-on-taxpayers?category=Tax%20News) (Aug. 16, 2018).

72 *Id.*

73 Data obtained from TAMIS (Oct. 1, 2018).

TAOs. On December 12, 2018, IRS issued FAQs clarifying how it will handle year two payments.<sup>74</sup> In FY 2019, TAS will continue to assist taxpayers who experience problems as a result of the way in which the IRS is administering IRC § 965(h).

### Private Debt Collection

In December of 2017, TAS issued interim guidance on handling inquiries from taxpayers whose balance due accounts had been assigned to a Private Collection Agency (PCA).<sup>75</sup> In FY 2018, TAS closed 157 cases involving taxpayers whose debts had been assigned to PCAs.<sup>76</sup> The tax liability was eliminated or reduced in 36 of those cases (23 percent).<sup>77</sup> TAS advocated for the processing of amended returns, transfer of misapplied payments, penalty abatements, audit reconsiderations, and other corrections to resolve the accounts. In 38 of the closed cases (24 percent), TAS recommended the accounts be placed in a currently not collectible status due to the taxpayers' economic hardship.<sup>78</sup> This level of service and relief would not have been available to taxpayers had they continued to work directly with a PCA. TAS established installment agreements for taxpayers in another 25 of the closed cases (16 percent). TAS will continue to accept cases from taxpayers whose debts were assigned to a PCA as a matter of public policy.<sup>79</sup>

## TAS OPERATIONS ASSISTANCE REQUEST (OAR) TRENDS

To assist taxpayers more efficiently, the Commissioner of Internal Revenue delegated to the National Taxpayer Advocate certain tax administration authorities that do not conflict with or undermine TAS's unique statutory mission, but allow TAS to resolve routine problems.<sup>80</sup> When TAS lacks the statutory or delegated authority to resolve a taxpayer's problem, it works with the responsible IRS Business Operating Division (BOD) or function to resolve the issue, a process necessary in 63 percent of TAS cases in FY 2018.<sup>81</sup> After independently reviewing the facts and circumstances of a case and communicating with the taxpayer, TAS issues OARs to convey a recommendation or request that the IRS take action to resolve the issue, and provides documentation that supports it. The OAR also serves as an advocacy tool by:

- Giving the IRS a second chance to resolve the issue;

74 IRS, *Questions and Answers about Tax Year 2018 Reporting and Payments Arising under Section 965* (Dec. 12, 2018), <https://www.irs.gov/newsroom/questions-and-answers-about-tax-year-2018-reporting-and-payments-arising-under-section-965>.

75 IGM, TAS-13-1217-006, *Interim Guidance on Advocating for Taxpayers Whose Modules the IRS Assigned to a Private Collection Agency* (Dec. 27, 2017). For a detailed discussion of Private Debt Collection (PDC) issues, see Most Serious Problem: *Private Debt Collection: The IRS's Expanding Private Debt Collection Program Continues to Burden Taxpayers Who Are Likely Experiencing Economic Hardship While Inactive PCA Inventory Accumulates*, *supra*. See also National Taxpayer Advocate 2017 Annual Report to Congress 10-21 (Most Serious Problem: *Private Debt Collection: The IRS's Private Debt Collection Program Is Not Generating Net Revenues, Appears to Have Been Implemented Inconsistently with the Law, and Burdens Taxpayers Experiencing Economic Hardship*); National Taxpayer Advocate FY 2019 Objectives Report to Congress 58-79. Nina E. Olson, *One Year Later, The IRS Has Not Adjusted Its Private Debt Collection Initiative To Minimize Harm To Vulnerable Taxpayers*, NTA BLOG, <https://taxpayeradvocate.irs.gov/news/nta-blog-the-irs-has-not-adjusted-its-private-debt-collection-initiative?category=Tax%20News> (June 6, 2018).

76 Data obtained from TAMIS (Oct. 1, 2018).

77 *Id.*

78 *Id.*

79 See TAS Case Receipt Criteria, *supra*.

80 IRM 1.2.50.3(1), Delegation Order 13-2 (Rev. 1) *Authority of the National Taxpayer Advocate to Perform Certain Tax Administration Functions* (Mar. 3, 2008).

81 TAS closed 133,844 cases with Operations Assistance Requests (OARs) in FY 2018. TAS can issue more than one OAR on a case. Data obtained from TAMIS (Oct. 2, 2018). If the IRS already has an open control on an account, TAS must use the OAR process and request that the IRS function take the requested actions.

- Giving TAS and the BOD a chance to resolve the issue without having to elevate it; and
- Documenting systemic trends that could lead to improvements in IRS processes.

All BODs agree to work TAS cases on a priority basis and expedite the process for taxpayers whose circumstances warrant immediate handling.<sup>82</sup> Form 12412, *Operations Assistance Request*, includes an “expedite” box that TAS Case Advocates may check when the BOD needs to act immediately to relieve the taxpayer’s significant hardship. Figure 4.1.9 shows the number of “expedite” OARs TAS issued to each BOD in FY 2018.

**FIGURE 4.1.9, Expedited and Non-Expedited OARs Issued by BOD, FY 2018<sup>83</sup>**

Business Operating Division	FY 2018 OARs Issued Requesting Expedite Action	FY 2018 OARs Issued without Expedite Request	FY 2018 Total OARs Issued
Appeals	278	475	753
Criminal Investigation	81	231	312
Large Business & International	275	761	1,036
Small Business/Self-Employed	14,661	19,008	33,669
Tax Exempt/Governmental Entities	242	245	487
Wage & Investment	104,435	81,074	185,509
<b>Total</b>	<b>119,972</b>	<b>101,794</b>	<b>221,766</b>

## TAS USES TAXPAYER ASSISTANCE ORDERS TO ADVOCATE EFFECTIVELY

The TAO is a powerful statutory tool, delegated by the National Taxpayer Advocate to LTAs to resolve taxpayer cases.<sup>84</sup> LTAs issue TAOs to order the IRS to take certain actions, cease certain actions, or refrain from taking certain actions.<sup>85</sup> A TAO may also order the IRS to expedite consideration of a taxpayer’s case, reconsider its determination in a case, or review the case at a higher level.<sup>86</sup> If a taxpayer faces significant hardship and the facts and law support relief, an LTA may issue a TAO when the IRS refuses or otherwise fails to take the action TAS requested to resolve the case.<sup>87</sup> Once TAS issues a TAO, the BOD must comply with the request or appeal the issue for resolution at higher management levels.<sup>88</sup> Only the National Taxpayer Advocate, Commissioner of Internal Revenue, or Deputy Commissioner may rescind a TAO issued by the National Taxpayer Advocate, and unless and until that rescission occurs, the BOD must abide by the action(s) ordered in the TAO.<sup>89</sup>

82 TAS has a Service Level Agreement (SLA) with each business operating division (BOD). Each SLA states the terms of engagement between TAS and the BODs, as agreed to by their respective executives, including timeframes and processes for communication in the OAR and TAO processes to assure that the IRS treats TAS cases with the agreed upon level of priority.

83 Data obtained from TAMIS (Oct. 1, 2018). As depicted in Figure 4.1.9, TAS issues OARs across all IRS BODs and Functions.

84 IRC § 7811(f) states that for purposes of this section, the term “National Taxpayer Advocate” includes any designee of the National Taxpayer Advocate. See IRM 1.2.50.2, *Delegation Order 13-1* (Rev. 1) (Mar. 17, 2009).

85 IRC § 7811(b)(2); Treas. Reg. § 301.7811-1(c)(2), IRM 13.1.20.3, *Purpose of Taxpayer Assistance Orders* (Dec. 15, 2007).

86 Treas. Reg. § 301.7811-1(c)(3); IRM 13.1.20.3, *Purpose of Taxpayer Assistance Orders* (Dec. 15, 2007).

87 IRC § 7811(a)(1)(A); Treas. Reg. § 301.7811-1(a)(1) and (c).

88 IRM 13.1.20.5(2), *TAO Appeal Process* (Dec. 9, 2015).

89 IRC § 7811(c)(1) and Treas. Reg. § 301.7811-1(b).

In FY 2018, TAS issued 1,489 TAOs,<sup>90</sup> the most TAOs ever issued in a FY and more TAOs issued than in FYs 2013–2017<sup>91</sup> combined. Of the 1,489 TAOs, 434 TAOs were issued in cases where the IRS failed to respond to an OAR, further delaying relief to taxpayers. Of these 434 TAOs, the IRS complied with 419 TAOs in an average of six days, meaning the IRS did not have a significant disagreement as to the resolution and the taxpayers could have had relief sooner if the IRS had been more responsive to TAS.<sup>92</sup> TAS issued 814 TAOs for taxpayers with hardships related to passport issues<sup>93</sup> and 469 to advocate for taxpayers with RIO issues.<sup>94</sup> Figure 4.1.10a reflects the results of all TAOs. Figure 4.1.10b shows the TAOs issued by fiscal year.

**FIGURE 4.1.10a, Actions Taken on FY 2018 TAOs Issued<sup>95</sup>**

Action	Total
IRS Complied with the TAO	1,357
IRS Complied after the TAO was modified	16
TAS Rescinded the TAO	43
TAS Pending (in Process)	73
<b>Total</b>	<b>1,489</b>

**FIGURE 4.1.10b, TAOs Issued to the IRS, FY 2013–2018<sup>96</sup>**

Fiscal Year	TAOs Issued
2013	353
2014	362
2015	236
2016	144
2017	166
2018	1,489

The examples presented in this report illustrate issues raised in cases where TAS issued TAOs to obtain relief. In issuing TAOs, TAS protects taxpayers' rights *to pay no more than the correct amount of tax, to quality service, to finality, and to a fair and just tax system.*<sup>97</sup> To comply with IRC § 6103, which generally requires the IRS to keep taxpayers' returns and return information confidential, the details of the fact patterns have been modified or redacted. As noted in certain examples, however, TAS has obtained the written consent of the taxpayer to provide more detailed facts.

90 Data obtained from TAMIS (Oct. 1, 2018).

91 Data obtained from TAMIS (Oct. 1, 2013; Oct. 1, 2014; Oct. 1, 2015; Oct. 1, 2016; Oct. 1, 2017; Oct. 1, 2018).

92 Data obtained from TAMIS (Oct. 1, 2018).

93 See Emerging Issues, *supra*.

94 See Pre-Refund Wage Verification Hold, *supra*.

95 Data obtained from TAMIS (Oct. 1, 2018).

96 Data obtained from TAMIS (Oct. 1, 2013; Oct. 1, 2014; Oct. 1, 2015; Oct. 1, 2016; Oct. 1, 2017; Oct. 1, 2018).

97 See TBOR, [www.TaxpayerAdvocate.irs.gov/taxpayer-rights](http://www.TaxpayerAdvocate.irs.gov/taxpayer-rights). The rights contained in the TBOR are also codified in the IRC. See IRC § 7803(a)(3).

### Taxpayer Assistance Orders to Examination Functions

In FY 2018, TAS issued 54 TAOs to examination units in Wage and Investment (W&I), SB/SE and Large Business and International (LB&I) BODs for issues including the EITC, audit reconsiderations, actions to complete open audits of original returns, penalty abatements, and appeal rights.<sup>98</sup> The IRS complied with 40 TAOs within an average of 13 days (a median of seven days).<sup>99</sup> In one example, a taxpayer was facing eviction while the IRS held the refund to audit the dependents, filing status, and EITC claimed on the taxpayer's tax return. Prior to requesting TAS assistance, the taxpayer submitted documentation to Exam but experienced continuous delays. TAS secured supporting documentation from the taxpayer to verify dependents, filing status, and EITC eligibility, and submitted it with an OAR to Exam. When Exam did not reply to the OAR timely, TAS issued a TAO directing Exam to review the additional documentation. Exam complied with the TAO, accepted the documentation, issued the refund, and closed the case.

### Taxpayer Assistance Orders on Collection Issues

TAS provided relief in more than 73 percent of collection cases in FY 2018, compared to approximately 79 percent on all issues.<sup>100</sup> In FY 2018, TAS issued 52 TAOs in collection cases where the IRS did not initially agree with TAS's recommendations.<sup>101</sup> Of these 52 TAOs, the IRS complied with 26 in an average of 21 days (a median of nine days), meaning the IRS's negative responses to TAS's requests unnecessarily delayed resolution, further harming the taxpayers, when there was no material disagreement on the resolution.<sup>102</sup>

TAS issued 11 TAOs involving levy cases in FY 2018.<sup>103</sup> The IRS complied with five of the 11 TAOs within an average of 29 days (a median of 19 days) for levies in FY 2018, with TAS subsequently rescinding three TAOs.<sup>104</sup> For several weeks, TAS advocated on behalf of a taxpayer for Automated Collection System (ACS) to return Federal Payment Levy Program (FPLP)<sup>105</sup> payments taken from the taxpayer's social security income over several months.<sup>106</sup> The LTA issued a TAO ordering a review of the adverse determination that ACS made on the OAR to return the FPLP payments. The ACS manager responded: "it isn't in the best interest of the government to return levied funds to this taxpayer." The manager's position is directly opposite of the guidance in IRM 5.11.2.4.1(4)<sup>107</sup> and in the note in IRM 5.11.7.2.7(3), where the guidance specifically says it *is* generally in the best interest of the

98 Data obtained from TAMIS (Oct. 1, 2018).

99 *Id.*

100 *Id.*

101 *Id.*

102 *Id.*

103 *Id.*

104 *Id.*

105 See IRC § 6331(h), which allows the IRS to collect a taxpayer's overdue taxes through a continuous levy on certain federal payments disbursed by the Bureau of Fiscal Service.

106 In this instance, the taxpayer has provided written consent under IRC § 6103(c) for the National Taxpayer Advocate to use facts specific to the taxpayer's case. Release signed by the taxpayer on Aug. 15, 2018, and on file with TAS.

107 IRM 5.11.2.4.1(4), *Current Authority for Returning Levied Property to the Taxpayer* (Oct. 26, 2017). Additionally, although not considered erroneous, proceeds from levies issued in the last nine months can be returned to the taxpayer at the discretion of the Service if: With the consent of the taxpayer or the National Taxpayer Advocate (NTA), returning the levy proceeds is in the best interests of the taxpayer (as determined by the NTA) and the government. IRS makes a determination that return of property is in the best interest of the United States and the NTA also determines that return of the property is in the best interest of the taxpayer.

government to return the FPLP payments in this situation.<sup>108</sup> After being advised of this IRM language, ACS complied with the TAO and agreed to issue a manual refund of the FPLP levy payments.

TAS continued to advocate in cases where the taxpayer or Power of Attorney (POA) correctly questioned the validity of a collection statute expiration date (CSED) calculation.<sup>109</sup> In general, the IRS has ten years from the date of assessment of tax to collect; however, this period may be tolled by certain actions.<sup>110</sup> In one case, a taxpayer came to TAS disputing the CSED on a tax liability for a tax period ending over 20 years previously. TAS computed the CSED and determined the CSED had expired. This case involved IA, OIC, and bankruptcy: three issues that added complexity to the computation of the CSED. TAS issued a TAO to zero-out the liability<sup>111</sup> and to write-off the remaining balance due.<sup>112</sup> The function agreed with TAS's CSED calculation and complied with the TAO but encountered numerous challenges and additional delays in getting the IRS database to accept the transactions needed to bring the balance due period to zero.

TAS also continued to use the TAO to advocate for taxpayers requesting a lien withdrawal. For example, a taxpayer who qualified for withdrawal of a notice of federal tax lien (NFTL) under the IRM<sup>113</sup> came to TAS after making a payment under a Direct Debit Installment Agreement (DDIA) which reduced the balance due to under \$25,000.<sup>114</sup> The taxpayer requested lien withdrawal. The lien withdrawal request was denied, because the IRS asserted the account would not be full paid within the 60-month time frame.<sup>115</sup> In addition to finding the taxpayer qualified for withdrawal under the DDIA provisions (TAS disagreed with the IRS determination that the DDIA would not full pay in 60 months), TAS found that the taxpayer qualified for abatement of penalties under first-time abatement.<sup>116</sup> Further, TAS determined that the withdrawal was in the best interest of the taxpayer and the government as it would allow the taxpayer to obtain better employment. Despite these facts, along with numerous email and telephone conversations, IRS refused to withdraw the lien. The LTA issued a TAO to further

108 IRM 5.11.7.2.7(3), *Returning FPLP Levy Proceeds* (Sept. 23, 2016). Note: In situations where the levy was released due to a finding of economic hardship or because the taxpayer entered into an installment agreement, the levied payment may be returned to the taxpayer subject to the nine-month look-back period stated in (2); generally, it is in the Government's best interest to do so. See IRM 5.11.2.4.1(4). However, if the taxpayer requests that the IRS keep the funds, the IRS should follow the taxpayer's instructions.

109 Nina E. Olson, *As a Result of TAS Advocacy, the IRS is Working to Address a Computer Glitch That Allowed Collection Activity on Accounts with Expired Collection Statute Expiration Dates but Many Issues Remain Unresolved*, NTA Blog, <https://taxpayeradvocate.irs.gov/news/NTA-blog-IRS-Working-to-Address-Collection-Activity-on-Accounts-with-expired-CSED> (Sept. 7, 2018).

110 The IRS generally has ten years to collect a tax debt once it is assessed, which is referred to as the collection statute expiration date (CSED). IRC § 6502. Some events may extend or suspend the CSED. For example, the CSED is suspended during the period an offer in compromise (OIC) is pending, for 30 days immediately following the rejection of the OIC, and for any period when a timely filed appeal from the rejection is being considered by Appeals. Treas. Reg. § 301.7122-1(i). Treasury Regulation § 301.6159-1(g) suspends the CSED while an installment agreement (IA) is pending, or 30 days after an IA is terminated or rejected, and during any appeal of that decision. The CSED is suspended in bankruptcy, and for six months thereafter. IRC § 6503(h)(2). Even if the suspension of the CSED under IRC § 6503(h) no longer applies, the CSED still may be suspended when substantially all the debtor's assets remain in the custody or control of the bankruptcy court. IRC § 6503(b).

111 IRM 5.19.10.4.5.1, *Correcting an Existing CSED No TC 550 on Account* (Feb. 1, 2014).

112 IRM 5.19.10.4.7, *Writing Off Expired Balances with TC 534* (Feb. 1, 2014).

113 IRM 5.17.2.8.7.2, *Withdrawal of Notice of Federal Tax Lien When Direct Debit Installment Agreement (DDIA) is in Effect* (Dec. 12, 2014).

114 *Id.*

115 IRM 5.12.9.3.2.1(5), *Special Provisions for Direct Debit Installment Agreements* (Oct. 14, 2013). TAS computed the IA will full pay in 53 months, and that the IA will full pay within the CSED which should have allowed for the lien to be released.

116 Reasonable cause is generally available with respect to penalties for failing to file returns or pay or deposit taxes. IRC §§ 6651(a) and 6656(a). Nevertheless, this abatement is available only if taxpayers exercised ordinary business care and not willful neglect. Treas. Reg. §§ 301.6651-1(c), 301.6656-1.

advocate that the taxpayer was entitled to relief under IRC § 6323(j)(1)(B) allowing withdrawal of an NFTL in certain circumstances.<sup>117</sup> After further discussion with the LTA, the IRS complied with the TAO and agreed to withdraw the NFTL.

### Taxpayer Assistance Orders to Appeals

Sometimes Appeals employees have questioned TAS's authority to issue a TAO to Appeals, however, Treas. Reg. § 301.7811-1(d) makes clear that TAS can issue a TAO to the Office of Appeals, an independent organization within the IRS, as it provides that "a TAO may be issued to any office, operating division or function of the IRS."

Further support for the conclusion that TAS can issue a TAO to Appeals can be found in Treasury Reg. § 301.7811-1 (c)(4), Example 3, which states:

L files a protest requesting Appeals consideration of IRS's proposed denial of L's request for innocent spouse relief. Appeals advises L that it is going to issue a Final Determination denying the request for innocent spouse relief. L files a Form 911, "Request for Taxpayer Advocate Service Assistance (And Application for Taxpayer Assistance Order)." The NTA reviews the administrative record and concludes that the facts support granting innocent spouse relief. The NTA may issue a TAO ordering Appeals to refrain from issuing a Final Determination and reconsider or review at a higher level its decision to deny innocent spouse relief. The TAO may include the NTA's analysis of and recommendation for resolving the case.<sup>118</sup>

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<sup>117</sup> IRC § 6323(j)(1)(B), in general the Secretary may withdraw a notice of a lien filed under this section and this chapter shall be applied as if the withdrawn notice had not been filed, if the Secretary determines that (B) the taxpayer has entered into an agreement under IRC § 6159 to satisfy the tax liability for which the lien was imposed by means of installment payments, unless such agreement provides otherwise.

<sup>118</sup> Treas. Reg. § 301.7811-1(c)(4).

During FY 2018, TAS issued nine TAOs to Appeals. One Appeals complied with, one was rescinded, four are pending, and three were appealed.<sup>119</sup> TAS continues to issue TAOs requesting face-to-face hearings.<sup>120</sup> For example, a POA contacted the National Taxpayer Advocate requesting that TAS advocate for a face-to-face Collection Due Process hearing. The Deputy Chief of Appeals indicated to the National Taxpayer Advocate that Appeals would grant face-to-face conferences, but that only applied to field Appeals cases, and this case was a campus Appeals case.<sup>121</sup> The Settlement Officer denied the requests for a face-to-face hearing without providing a specific reason. Despite TAS's advocacy, Appeals still refused to allow a face-to-face hearing, so TAS issued a TAO ordering that the taxpayer be afforded a face-to-face meeting. After elevated discussions within Appeals and TAS, the LTA secured an agreement to allow a collection alternative, which negated the need to have a face-to-face hearing. While TAS rescinded the TAO, using the TAO process allowed TAS to obtain relief for the taxpayer. On November 30, 2018, in response to the National Taxpayer Advocate's and Low Income Taxpayer Clinic's (LITCs) advocacy, Appeals reversed its position with respect to availability of face-to-face conferences in campus appeals cases.<sup>122</sup>

In another case, a POA requested TAS assistance after he was told by Appeals that the IRS erroneously assessed willful Foreign Bank and Financial Account Report (FBAR) penalties in excess of \$100,000 and the Appeals office treated the case as a post-assessment appeal.<sup>123</sup> Accordingly, any settlement would require approval from the Department of Justice (DOJ).<sup>124</sup> TAS held a conference with the IRS where the IRS acknowledged the assessment was erroneous. The correct processing of the case would have been to send it to Appeals *pre-assessment*. The Revenue Agent Group Manager confirmed that he did not intend to assess the FBAR penalties and was aware the taxpayer requested a pre-assessment hearing at the time of the assessments. The LTA issued a TAO to Appeals ordering Appeals to consult with the IRS Office of Chief Counsel and reconsider whether the IRS may abate the FBAR penalty erroneously assessed against the taxpayer and refrain from holding a hearing on the taxpayer's FBAR penalty until ten business days after a decision was rendered on the reconsideration (in consultation with Chief Counsel) as to whether the IRS may abate the erroneously assessed FBAR penalty. Appeals contacted the Office of Chief Counsel for an opinion on the authority to reverse the FBAR assessment and delayed the initial Appeals conference date with the taxpayer. Post-assessment FBAR cases in excess of \$100,000 cannot be compromised without the approval of the DOJ because the assessed penalty becomes a claim of the U.S. Government.<sup>125</sup> Working with the Office of Chief Counsel, the DOJ authorized the abatement. Chief Counsel worked with Exam and Appeals to abate the assessments. The penalties were abated in full.

119 Data obtained from TAMIS (Oct. 1, 2018).

120 National Taxpayer Advocate 2017 Annual Report to Congress 195-202; National Taxpayer Advocate 2016 Annual Report to Congress 206-210; National Taxpayer Advocate 2014 Annual Report to Congress 46-54; National Taxpayer Advocate 2014 Annual Report to Congress 311-314.

121 Prior to 2016, taxpayers could request to transfer cases out of the campus and to facilitate an in-person conference. That right was eliminated in 2016 and has not been restored. IRM 8.6.1.4.1, *Conference Practice* (Oct. 1, 2016). Compare IRM 8.6.1.2.2, *Transfers for the Convenience of Taxpayers* (June 25, 2015). See also IGM, Control No. AP-08-1017-0017 (Oct. 13, 2017).

122 IGM AP-08-1118-0013, *Appeals Conference Procedures* (Nov. 30, 2018). See also Most Serious Problem: *Appeals: Appeals Has Taken Important Steps Toward Increasing Campus Taxpayers' Access to In-Person, Quality Appeals, But Additional Progress is Required*, *supra*.

123 In this instance, the taxpayer has provided written consent under IRC § 6103(c) for the National Taxpayer Advocate to use facts specific to the taxpayer's case. Release signed by the taxpayer on Aug. 14, 2018 and on file with TAS.

124 See 31 USC § 3711(a)(2); 31 CFR §§ 902.1(a)(b). See also IRM 8.11.6.1(6), *FBAR Overview* (Feb. 2, 2015).

125 31 USC § 3711(a)(2); 31 C.F.R. §§ 902.1(a), (b).

## CONGRESSIONAL CASE TRENDS

Taxpayers often turn to their Congressional representatives when faced with IRS issues. The Congressional representatives refer these taxpayers to TAS, which is responsible for responding to tax account inquiries sent to the IRS by Members of Congress. Figure 4.1.11 reflects Congressional case receipts and TAS receipts from other contacts.

**FIGURE 4.1.11**<sup>126</sup>

**TAS Congressional Receipts, FYs 2012-2018**

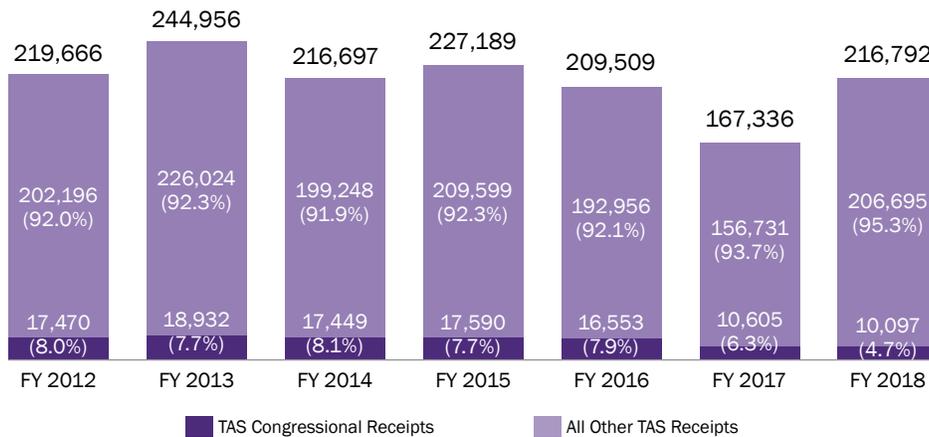


Figure 4.1.12 shows the top ten PCICs causing taxpayers to seek the assistance of their Congressional representatives. ID Theft receipts decreased by nearly 57 percent between FY 2017 and FY 2018 while PRWVHs increased by more than 152 percent.<sup>127</sup> Issues associated with the processing of amended returns decreased by more than four percent. These trends followed the overall TAS increase and decrease in receipts for these issues.<sup>128</sup>

<sup>126</sup> Data obtained from TAMIS (Oct. 1, 2012; Oct. 1, 2013; Oct. 1, 2014; Oct. 1, 2015; Oct. 1, 2016; Oct. 1, 2017, Oct. 1, 2018).

<sup>127</sup> Data obtained from TAMIS (Oct. 1, 2017; Oct. 1, 2018).

<sup>128</sup> PCIC 460 Application for Exempt Status cases from all sources, including Congressional referrals, were 407 cases in FY 2017 and 485 cases in FY 2018, an increase of 19.2 percent.

**FIGURE 4.1.12, TAS Top Ten Congressional Receipts by Primary Core Issue Code, FYs 2017–2018<sup>129</sup>**

Rank	Issue Description	FY 2017	FY 2018	Percent Change
1	Pre-Refund Wage Verification Hold	368	929	152.4%
2	Transcript Request	480	546	13.8%
3	Other Refund Inquiry/Issue	431	509	18.1%
4	Processing Original Return	543	440	-19.0%
5	Processing Amended Return	418	399	-4.5%
6	Identity Theft	911	394	-56.8%
7	Application for Exempt Status	288	353	22.6%
8	Open Automated Underreporter	323	328	1.5%
9	Installment Agreements	399	321	-19.5%
10	Unpostables and Rejects	206	319	54.9%
<b>Other Issues</b>		<b>6,238</b>	<b>5,559</b>	<b>-10.9%</b>
<b>Total Congressional Receipts</b>		<b>10,605</b>	<b>10,097</b>	<b>-4.8%</b>

<sup>129</sup> Data obtained from TAMIS (Oct. 1, 2017; Oct. 1, 2018).

## Appendix 1: Top 25 Case Advocacy Issues for Fiscal Year (FY) 2018 by TAMIS\* Receipts

Rank	Issue Code	Description	FY 2018 Case Receipts
1	045	Pre-Refund Wage Verification Hold	66,048
2	630x - 640	Earned Income Tax Credit (EITC)	21,203
3	425	Identity Theft	13,787
4	330	Processing Amended Return	8,767
5	315	Unpostable and Reject	8,673
6	318	Taxpayer Protection Program Unpostables	7,947
7	090	Other Refund Inquiries and Issues	7,628
8	610	Open Audit, Not EITC	5,823
9	310	Processing Original Return	5,312
10	920	Health Insurance Premium Tax Credit for Individuals Under IRC § 36B	4,833
11	71x	Levies	3,801
12	620	Reconsideration of Audits and Substitute for Return Under IRC § 6020(b)	3,612
13	040	Returned and Stopped Refunds	3,398
14	340	Injured Spouse Claim	3,231
15	670	Closed Automated Underreporter	3,041
16	75x	Installment Agreements	2,873
17	060	IRS Offset	2,739
18	72x	Liens	2,558
19	790	Other Collection Issues	2,557
20	151	Transcript Requests	2,110
21	320	Math Error	1,994
22	520	Failure to File (FTF) Penalty and Failure to Pay (FTP) Penalty	1,933
23	010	Lost or Stolen Refunds	1,867
24	450	Form W-7, Individual Taxpayer Identification Number (ITIN), and Adoption Taxpayer Identification Number (ATIN)	1,745
25	91x	Appeals	1,743
<b>Total Top 25 Receipts</b>			<b>189,223</b>
<b>Total TAS Receipts</b>			<b>216,792</b>

\* Taxpayer Advocate Management Information System (TAMIS).

## Appendix 2: Glossary of Acronyms

Acronym	Definition
AAB	Aggregate Assessed Balance
AARP	American Association of Retired Persons
ABA	American Bar Association
AC	Action Code
ACA	Affordable Care Act
ACH	Automated Clearing House
ACIO	Associate Chief Information Officer
ACS	Automated Collection System
ACSS	Automated Collection System Support
ACTC	Additional Child Tax Credit
ADA	Anti-Deficiency Act
AES	Advanced Encryption Standard
AFR	Agency Financial Report
AFSP	Annual Filing Season Program
AGI	Adjusted Gross Income
AIA	Anti-Injunction Act
AICPA	American Institute of Certified Public Accountants
AIMS	Audit Information Management System
AJAC	Appeals Judicial Approach and Culture
AJCA	American Jobs Creation Act
AKPFD	Alaska Permanent Fund Dividend Levy Program
ALE	Allowable Living Expenses
ALERTS	Automated Labor and Employee Relations Tracking System
AM	Accounts Management
AMS	Accounts Management System
AMT	Alternative Minimum Tax
AO	Appeals Officer
AOD	Action on Decision
AOTC	American Opportunity Tax Credit
APA	Administrative Procedure Act
APTC	Advance Premium Tax Credit
ARC	Annual Report to Congress
ARDI	Accounts Receivable Dollar Inventory
ASA	Average Speed of Answer
ASFR	Automated Substitute for Return
ATAO	Application for Taxpayer Assistance Order
ATE	Appeals Technical Employee
ATIN	Adoption Taxpayer Identification Number

Acronym	Definition
ATO	Australian Taxation Office
AUR	Automated Underreporter
BBA	Bipartisan Budget Act
BFS	Bureau of Fiscal Services
BIR	Bureau of Internal Revenue
BLS	Bureau of Labor Statistics
BMF	Business Master File
BOD	Business Operating Division
BPR	Business Performance Review
BSA	Bank Secrecy Act
BSM	Business Systems Modernization
BTA	Board of Tax Appeals
CA	Correspondence Audit
CAA	Certified Acceptance Agent
CADE	Customer Account Data Engine
CAP	Collection Appeals Program
CAR	Collection Activity Report
CBO	Congressional Budget Office
CC	Command Code
CCA	Chief Counsel Advice
CCDM	Chief Counsel Directives Manual
CCE	Compliance Center Exam
CCH	Commerce Clearing House
CDDDB	Custodial Detail Database
CDP	Collection Due Process
CDW	Compliance Data Warehouse
CEO	Chief Executive Officer
Cff	Collection Field Function
CFR	Code of Federal Regulations
CHIP	Children's Health Insurance Program
CI	Criminal Investigation (Division)
CIC	Coordinated Industry Cases
CIP	Compliance Initiative Projects
CIS	Collection Information Statement
CNC	Currently Not Collectible
COD	Cancellation of Debt
COIC	Centralized Offer in Compromise
CP	Computer Paragraph
CPA	Certified Public Accountant
CPE	Continuing Professional Education

Acronym	Definition
CRS	Congresional Research Service or Common Reporting Standard
CSED	Collection Statute Expiration Date
CSO	Communication and Stakeholder Outreach
CSR	Customer Service Representative
CTC	Child Tax Credit
CX	Customer Experience
CY	Calendar Year
DAS	Discriminant Analysis System
DCI	Data Collection Instrument
DDb	Dependent Database
DDIA	Direct Debit Installment Agreement
DEFRA	Deficit Reduction Act of 1984
DI	Debt Indicator
DIF	Discriminant Function
DJA	Declaratory Judgement Act of 1934
DMDC	Defense Manpower Data Center
DOD	Department of Defense
DOJ	Department of Justice
DSP	Disability Severance Pay
EA	Enrolled Agent
EB	Economic Burden
ECC	Enterprise Computing Center
ECM	Enterprise Case Management
EDCA	Executive Director Case Advocacy
EDP	Economic Development Program
EDSA	Executive Director Systemic Advocacy
EFDS	Electronic Fraud Detection System
EFTPS	Electronic Federal Tax Payment System
EGTRRA	Economic Growth and Tax Reconciliation Act of 2001
EIC	Earned Income Credit
EIN	Employer Identification Number
EITC	Earned Income Tax Credit
EO	Exempt Organization
EPST	Exam Planning Scenario Tool
EQRS	Embedded Quality Review System
ERO	Electronic Return Originator
ERS	Error Resolution
ESL	English as a Second Language
ESOP	Employee Stock Ownership Plan
ETA	Effective Tax Administration
FA	Field Audit
FAFSA	Free Application for Federal Student Aid

Acronym	Definition
FAST	Fixing America's Surface Transportation Act
FATCA	Foreign Account Tax Compliance Act
FBAR	Report of Foreign Bank and Financial Accounts or Foreign Bank Account Report
FCA	Financial Conduct Authority
FCR	First Call Resolution; or Federal Case Registry
FFI	Free File, Inc.; or Foreign Financial Institution
FIPIT	Field Inventory Process Improvement Team
FMIS	Financial Management Information System
FOIA	Freedom of Information Act
FPL	Federal Poverty Level
FPLP	Federal Payment Levy Program
FPR	False Positive Rate
FRCP	Federal Rule of Civil Procedure
FS	Filing Season
FTC	Foreign Tax Credit
FTD	Federal Tax Deposit
FTF	Failure To File
FTL	Federal Tax Lien
FTP	Failure To Pay
FY	Fiscal Year
GAO	Government Accountability Office
GPS	Global Positioning System
GSA	General Services Administration
HCD	Human-Centered Design
HCERA	Health Care and Education Reconciliation Act
HCO	Human Capital Office
HHI	Household Income
HHS	Health and Human Services
HIV	Human Immunodeficiency Virus
HMRC	Her Majesty's Revenue and Customs
HOH	Head of Household
HUD	Housing and Urban Development
IA	Installment Agreement
IBFD	Independent Bureau of Fiscal Documentation
IBTF	In-Business-Trust-Fund
IC	Industry Cases
IDES	International Data Exchange System
IDR	Information Document Request
IDRS	Integrated Data Retrieval System
IDS	Inventory Delivery System
IDT	Identity Theft
IGA	Intergovernmental Agreements

Acronym	Definition
IGM	Interim Guidance Memorandum
IIC	International Individual Compliance Cases
IMD	Internal Management Document
IMF	Individual Master File
IOAA	Independent Offices Appropriations Act
IPERA	Improper Payments Elimination and Recovery Act of 2010
IPERIA	Improper Payments Elimination and Recovery Improvement Act of 2012
IPIA	Improper Payments Information Act of 2002
IP PIN	Identity Protection Personal Identification Number
IRA	Individual Retirement Account
IRB	Internal Revenue Bulletin
IRC	Internal Revenue Code
IRM	Internal Revenue Manual
IRMF	Information Returns Master File
IRP	Information Return Program
IRS	Internal Revenue Service
IRSAC	Internal Revenue Service Advisory Council
IRTF	Individual Returns Transaction File
ISRP	Individual Shared Responsibility Payment
IT	Information Technology
ITA	Interactive Tax Assistant
ITIN	Individual Taxpayer Identification Number
IVO	Integrity and Verification Operation
JCT	Joint Committee on Taxation
JOC	Joint Operations Center
LB&I	Large Business and International Operating Division
LEP	Limited English Proficiency
LIF	Low Income Filter
LII	Low Income Indicator
LITC	Low Income Taxpayer Clinic
LLC	Limited Liability Company
LLP	Limited Liability Partnership
LOS	Level of Service
LM	Legal Memoranda
LR	Legislative Recommendation
LTA	Local Taxpayer Advocate
LUQ	Large, Unusual and Questionable Items
MANCOVA	Multivariate Analysis of Covariance
MAP	Monthly Assessment of Performance
MEA	Math Error Authority

Acronym	Definition
MFJ	Married Filing Joint
MFS	Married Filing Separately
MFT	Master File Transcript
MLI	Most Litigated Issue
MOU	Memorandum of Understanding
MSA	Metropolitan Statistical Area
MSP	Most Serious Problem
MTLP	Municipal Tax Levy Program
MVRA	Mandatory Victim's Restitution Act
NALT	North American Land Trust
NBER	National Bureau of Economic Research
NCLC	National Consumer Law Center
NDC	National Distribution Center
NDS	Notice Delivery System
NFTL	Notice of Federal Tax Lien
NIST	National Institute of Standards and Technology
NOL	Net Operating Loss
NPS	National Insurance and Pay-As-You-Earn Service
NQRS	National Quality Review System
NRP	National Research Program
NSA	National Society of Accountants
NTA	National Taxpayer Advocate
NTEU	National Treasury Employees Union
OA	Office Audit
OAR	Operations Assistance Request
OCC	Office of Chief Counsel
OD	Operating Division
OECD	Organisation for Economic Co-Operation and Development
OIC	Offer in Compromise
OLC	Office of Legal Counsel
OLS	Office of Online Services
OMB	Office of Management and Budget
OPA	Online Payment Agreement
OPI	Over the Phone Interpreter
OPR	Office of Professional Responsibility; or Operational Performance Rate
OS	Operations Support
OTC	Office of Taxpayer Correspondence
OUO	Official Use Only
OVD	Offshore Voluntary Disclosure
PAC	Program Action Case

Acronym	Definition
PACER	Public Access to Court Electronic Records
PATH	Protecting Americans from Tax Hikes
PAYE	Pay-As-You-Earn
PAYG	Pay-As-You-Go
PCA	Private Collection Agency
PCI	Potentially Collectible Inventory
PCIC	Primary Core Issue Code
PDC	Private Debt Collection
PII	Personally Identifiable Information
PIN	Personal Identification Number
PLR	Private Letter Ruling
PM	Program Manager
PMTA	Program Manager Technical Advice
POA	Power of Attorney
PPG	Policy and Procedure Guide
PPIA	Partial Payment Installment Agreement
PRVVH	Pre-Refund Wage Verification Hold
PSP	Payroll Service Provider
PTC	Premium Tax Credit
PTIN	Preparer Tax Identification Number
PTSD	Post-Traumatic Stress Disorder
PY	Processing Year
QBI	Qualified Business Income
QC	Qualifying Child
QTE	Qualified Tax Expert
RA	Revenue Agent
RAAS	Research, Analysis, and Statistics or Research, Applied Analytics, and Statistics
RAD	Research Analysis and Data
RAND	Research and Development
RAS	(Office of) Research, Analysis and Statistics
RCA	Reasonable Cause Assistant
RCEO	Refundable Credits Examination Operation
RCP	Reasonable Collection Potential
RD	Return Delinquency
RDC	Research Development Center
RDD	Return Due Date
RIA	Research Institute of America
RICS	Return Integrity and Correspondence Services
RIO	Return Integrity Operations
RO	Revenue Officer
RPC	Return Preparer Coordinator
RPM	Return Preparer Misconduct

Acronym	Definition
RPO	Return Preparer Office
RPP	Return Preparer Program
RRA 98	Internal Revenue Service Restructuring and Reform Act of 1998
RRP	Return Review Program
RUFI	Reduced User Fee Indicator
SAMS	Systemic Advocacy Management System
SBA	Small Business Administration
SB/SE	Small Business/Self-Employed Operating Division
SCIC	Secondary Core Issue Code
SCPP	Special Compliance Personnel Program
SERP	Servicewide Electronic Research Program
SFR	Substitute for Return
SIA	Streamlined Installment Agreement
SITLP	State Income Tax Levy Program
SL	Stakeholder Liaison
SLA	Service Level Agreement
SME	Small/Medium Enterprise
SMS	Short Messaging Service
SNAP	Supplemental Nutrition Assistance Program
SNOD	Statutory Notice of Deficiency
SO	Settlement Officer
SOI	Statistics of Income
SOL	Statute of Limitations
SP	Submission Processing
SPEC	Stakeholder Partnerships, Education & Communication
SPP	Service Priorities Project
SSA	Social Security Administration
SSDI	Social Security Disability Insurance or Income
SSF	Slippery Slope Framework
SSI	Supplemental Security Income
SSN	Social Security Number
TA	Taxpayer Advocate/Technical Assistance Memoranda
TAC	Taxpayer Assistance Center
TACT	Taxpayer Communications Taskgroup
TAD	Taxpayer Advocate Directive
TAMIS	Taxpayer Advocate Management Information System
TANF	Temporary Assistance to Needy Families
TAO	Taxpayer Assistance Order
TAP	Taxpayer Advocacy Panel
TAR	Tax Agency Reconciliations

Acronym	Definition
TARD	Taxpayer Advocate Received Date
TAS	Taxpayer Advocate Service
TASIS	Taxpayer Advocate Service Integrated System
TBD	To Be Determined
TBOR	Taxpayer Bill of Rights
TC	Transaction Code
TCE	Taxpayer Counseling for the Elderly
TCJA	Tax Cuts and Jobs Act
TCMP	Tax Compliance Measurement Program
TCO	Tax Compliance Officer
TDA	Taxpayer Delinquent Account
TDC	Taxpayer Digital Communication
TDI	Taxpayer Delinquent Investigation
TE	Tax Examiner
TEFRA	Tax Equity and Fiscal Responsibility Act
TE/GE	Tax Exempt & Government Entities Operating Division
TFRP	Trust Fund Recovery Penalty
TGR	Total Gross Receipts
TIA	Tax Injunction Act; or Tax Implementation Agreement
TIGTA	Treasury Inspector General for Tax Administration
TIN	Taxpayer Identification Number

Acronym	Definition
TIPRA	Tax Increase Prevention and Reconciliation Act
TLCATS	Tax Litigation Counsel Automated Tracking System
TP	Taxpayer
TPC	Tax Policy Center
TPI	Total Positive Income
TPNC	Taxpayer Notice Code
TPP	Taxpayer Protection Program
TRIO	Tax Reform Implementation Office
TY	Tax Year
UK	United Kingdom
UNAX	Unauthorized Access of Taxpayer Account
USPS	United States Postal Service
USVI	United States Virgin Islands
VAT	Value Added Tax
VBD	Voice Balance Due
VC	Voluntary Compliance
VITA	Volunteer Income Tax Assistance
VSD	Virtual Service Delivery
W&I	Wage and Investment Operating Division
WVP	Wage Verification Program
YTD	Year to Date

## Appendix 3: Most Litigated Issues Tables

**TABLE 1: Accuracy-Related Penalty Under IRC § 6662(b)(1) and (2)**

Case Citation	Issue(s)	Pro Se	Decision
<b>Individual Taxpayers (But Not Sole Proprietorships)</b>			
<i>Barrett v. Comm'r</i> , T.C. Memo. 2017-195	6662(b)(1), (2) - TPs (MFJ) did not keep adequate books and records; TPs substantially understated income tax; did not establish reasonable cause and good faith	No	IRS
<i>Beckey v. Comm'r</i> , T.C. Summ. Op. 2017-80	6662(b)(1), (2) - TPs (MFJ) substantially understated income tax and were negligent due to failure to keep adequate books and records	Yes	IRS
<i>Bell v. Comm'r</i> , T.C. Summ. Op. 2017-63	6662(b)(2) - TP substantially understated income tax; did not establish reasonable cause and good faith; no reasonable reliance on the advice of a tax professional	Yes	IRS
<i>Benjamin v. Comm'r</i> , T.C. Memo. 2018-70, <i>appeal docketed</i> , No. 18-72831 (9th Cir., Oct. 18, 2018)	6662(b)(2) - TPs (MFJ) substantially understated income tax; did not establish reasonable cause and good faith	Yes	IRS
<i>Boneparte v. Comm'r</i> , T.C. Memo. 2017-193, <i>appeal docketed</i> , No. 18-2264 (3d Cir., June 8, 2018)	6662(b)(1), (2) - TP was negligent; did not establish reasonable cause and good faith	Yes	IRS
<i>Bornet v. Comm'r</i> , T.C. Memo. 2017-201	6662(b)(2) - TP substantially understated income tax; did not establish reasonable cause	No	IRS
<i>Burke v. Comm'r</i> , T.C. Memo. 2018-18	6662(b)(2) - TPs (MFJ) substantially understated income tax; IRS did not meet burden of production by failing to present evidence that penalties were personally approved in writing by immediate supervisor before determination	No	TP
<i>Busch v. Comm'r</i> , T.C. Memo. 2017-169	6662(b)(1), (2) - TP substantially understated income tax; did not establish reasonable cause and good faith	No	IRS
<i>Cates v. Comm'r</i> , T.C. Memo. 2017-178, <i>appeal dismissed</i> , No. 18-10738 (11th Cir., Apr. 30, 2018)	6662(b)(2) - TPs (MFJ) substantially understated income tax; did not establish reasonable cause and good faith	Yes	IRS
<i>Christen v. Comm'r</i> , 698 F. App'x 450 (9th Cir. 2017), <i>aff'g</i> No. 16147-14 (T.C. 2016)	6662(b)(2) - TP substantially understated income tax	Yes	IRS
<i>Conrad v. Comm'r</i> , T.C. Memo. 2017-116	6662(b)(1), (2) - TP substantially understated income tax; did not establish reasonable cause; did not establish reasonable reliance on the advice of a tax professional	No	IRS
<i>Cortes v. Comm'r</i> , 691 F. App'x 899 (9th Cir. 2017), <i>aff'g</i> T.C. Memo. 2014-181, <i>reh'g en banc denied</i> , 121 A.F.T.R.2d 991 (9th Cir. 2018)	6662(b)(2) - TPs (MFJ) substantially understated income tax; did not establish reasonable cause and good faith; no reasonable reliance on advice of a tax professional	Yes	IRS
<i>Crissey v. Comm'r</i> , T.C. Summ. Op. 2017-44	6662(b)(1), (2) - TPs (MFJ) were negligent; did not establish reasonable cause and good faith; did not establish reasonable reliance on the advice of a tax professional	Yes	IRS
<i>Davidson v. Comm'r</i> , T.C. Memo. 2018-38	6662(b)(1), (2) - TPs (MFJ) established reasonable cause and good faith; reasonably relied on advice of a tax professional	Yes	TP
<i>Devine v. Comm'r</i> , T.C. Memo. 2017-111	6662(b)(1), (2) - TPs (MFJ) substantially understated income tax and were negligent; did not establish reasonable cause and good faith; no reasonable reliance on the advice of a tax professional	No	IRS
<i>Dulanto v. Comm'r</i> , 703 F. App'x 527 (9th Cir. 2017), <i>aff'g</i> T.C. Memo. 2016-34, <i>reh'g en banc denied</i> , 2018 U.S. App. LEXIS 7136 (9th Cir., Mar. 21, 2018)	6662(b)(2) - TPs (MFJ) did not establish reasonable cause and good faith; did not establish reasonable reliance on the advice of a tax professional	Yes	IRS

TABLE 1: Accuracy-Related Penalty Under IRC § 6662(b)(1) and (2)

Case Citation	Issue(s)	Pro Se	Decision
<i>Edwards v. Comm'r</i> , T.C. Summ. Op. 2017-52	6662(b)(2) - TP substantially understated income tax; established reasonable cause and good faith	No	TP
<i>Fann v. Comm'r</i> , T.C. Summ. Op. 2017-43	6662(b)(2) - TPs (MFJ) substantially understated income tax; TPs established reasonable cause	Yes	TP
<i>Fehr v. Comm'r</i> , T.C. Summ. Op. 2018-26	6662(b)(1), (2) - TP substantially understated income tax and was negligent due to failure to keep adequate books and records	Yes	IRS
<i>Fiscalini v. Comm'r</i> , T.C. Memo. 2017-163	6662(b)(1), (2) - TP was negligent; did not establish reasonable cause and good faith	Yes	IRS
<i>Ford v. Comm'r</i> , T.C. Memo. 2018-8, <i>aff'd</i> , 2018 U.S. App. LEXIS 31221 (6th Cir., Nov. 5, 2018)	6662(b)(1) - IRS did not meet burden of production by failing to present evidence that penalties were personally approved in writing by immediate supervisor before determination	No	TP
<i>Frias v. Comm'r</i> , T.C. Memo. 2017-139	6662(b)(2) - TPs (MFJ) established reasonable cause and good faith	No	TP
<i>Galloway v. Comm'r</i> , 2017 WL 4546791 (T.C. 2017)	6662(b)(2) - TPs (MFJ) substantially understated income tax; TPs failed to show substantial authority for TPs' position; failed to make an adequate disclosure and had no reasonable basis for position	No	IRS
<i>Gowen v. Comm'r</i> , T.C. Summ. Op. 2017-57	6662(b)(2) - TP substantially understated income tax; did not establish reasonable cause and good faith	No	IRS
<i>Graev v. Comm'r</i> , 2017 WL 6549899 (T.C. Dec. 20, 2017)	6662(b)(2) - TPs (MFJ) substantially understated income tax; IRS satisfied supervisory approval requirement of IRC § 6751(b)	No	IRS
<i>Hamilton v. Comm'r</i> , T.C. Memo. 2018-62	6662(b) - IRS did not meet burden of production by failing to present evidence that penalties were personally approved in writing by immediate supervisor before determination	No	TP
<i>Hexum v. Comm'r</i> , 721 F. App'x 512 (7th Cir. 2018), <i>reh'g denied</i> , 2018 U.S. App. LEXIS 6536 (7th Cir., Mar. 15, 2018), <i>aff'g</i> No. 13994-16 (T.C. Apr. 21, 2017)	6662(b)(1) - TP was negligent; did not establish reasonable reliance on the advice of a tax professional; did not establish reasonable cause and good faith	Yes	IRS
<i>Hickam v. Comm'r</i> , T.C. Summ. Op. 2017-66	6662(b)(1), (2) - TPs (MFJ) substantially understated income tax and were negligent; did not keep adequate books and records; the TPs established reasonable cause and good faith; TPs established reasonable reliance on the advice of a tax professional	Yes	TP
<i>Hudson v. Comm'r</i> , T.C. Memo. 2017-221	6662(b)(2) - TPs established reasonable cause and good faith based on reasonable reliance on the advice of a tax professional	No	TP
<i>Isaac v. Comm'r</i> , T.C. Summ. Op. 2017-55	6662(b)(2) - TP substantially understated income tax; did not establish reasonable cause and good faith	Yes	IRS
<i>Jagos v. Comm'r</i> , T.C. Memo. 2017-202, <i>aff'd</i> , 121 A.F.T.R.2d 2209 (6th Cir. 2018)	6662(b)(2) - TPs (MFJ) substantially understated income tax; did not establish reasonable cause and good faith	Yes	IRS
<i>Keefe v. Comm'r</i> , T.C. Memo. 2018-28, <i>appeal docketed</i> , No. 18-2357 (2d Cir., Aug. 10, 2018)	6662(b)(1), (2) - TPs (MFJ) substantially understated income tax and did not establish reasonable basis; TPs were negligent; did not establish reasonable cause and good faith	No	IRS
<i>Kohn v. Comm'r</i> , T.C. Memo. 2017-159	6662(b)(1) - TPs (MFJ) were negligent; did not establish reasonable cause	Yes	IRS
<i>Linde v. Comm'r</i> , T.C.M. (RIA) 2017-180 (T.C. 2017)	6662(b)(2) - TPs (MFJ) established reasonable cause and good faith; reasonable reliance on the advice of a tax professional	No	TP
<i>Logue v. Comm'r</i> , T.C. Memo. 2017-234	6662(b)(2) - TP substantially understated income tax; did not establish reasonable cause and good faith	No	IRS

TABLE 1: Accuracy-Related Penalty Under IRC § 6662(b)(1) and (2)

Case Citation	Issue(s)	Pro Se	Decision
<i>Lopez v. Comm'r</i> , T.C. Memo. 2017-171	6662(b)(1), (2) - TPs (MFJ) established reasonable cause and good faith; reasonable reliance on the advice of tax professional	Yes	TP
<i>Maciujec v. Comm'r</i> , T.C. Summ. Op. 2017-49	6662(b) - TP established reasonable cause and good faith; reasonable reliance on the advice of a tax professional	Yes	TP
<i>Marks v. Comm'r</i> , T.C. Memo. 2018-49	6662(b)(1), (2) - TP did not substantially understate income tax and was not negligent	No	TP
<i>McGuire v. Comm'r</i> , 2017 WL 3730620 (T.C. Aug. 28, 2017)	6662(b)(1), (2) - IRS did not meet burden of production with regards to negligence; TPs (MFJ) substantially understated income tax; TPs established reasonable cause and good faith	Yes	TP
<i>Mudrich v. Comm'r</i> , T.C. Memo. 2017-101	6662(b)(1), (2) - TP was negligent due to failed to show substantial authority for TPs' position; TPs had no reasonable basis for position; did not establish reasonable cause and good faith; no reasonable reliance on the advice of a tax professional	Yes	IRS
<i>Nicholson v. Comm'r</i> , T.C. Summ. Op. 2018-24	6662(b)(1), (2) - TP was negligent	Yes	IRS
<i>Ohde v. Comm'r</i> , T.C. Memo. 2017-137	6662(b)(1) - TPs (MFJ) were negligent and did not keep adequate books and records; did not establish reasonable cause	No	IRS
<i>Omoloh v. Comm'r</i> , T.C. Summ. Op. 2017-64	6662(b)(2) - TP substantially understated income tax; did not establish reasonable cause and good faith	Yes	IRS
<i>Partyka v. Comm'r</i> , T.C. Summ. Op. 2017-79	6662(b)(1), (2) - TPs (MFJ) were negligent; did not keep adequate books and records; did not establish reasonable cause and good faith	Yes	IRS
<i>Pexa v. United States</i> , 121 A.F.T.R.2d 1686 (E.D. Cal. 2018)	6662(b) - TPs (MFJ) substantially understated income tax; did not establish reasonable cause and good faith; no reasonable reliance on the advice of a tax professional	No	IRS
<i>Planty v. Comm'r</i> , T.C. Memo. 2017-240	6662(b)(2) - TPs (MFJ) substantially understated income tax; failed to show substantial authority for TPs' position; TPs had no reasonable basis for position	Yes	IRS
<i>Pourmirzaie v. Comm'r</i> , T.C. Memo. 2018-26	6662(b)(2) - TPs (MFJ) substantially understated income tax; did not establish reasonable cause and good faith; failed to show substantial authority for TPs' position	No	IRS
<i>Rademacher v. Comm'r</i> , T.C. Memo. 2018-43	6662(b)(1), (2) - TP was not liable for penalty; IRS did not meet burden of production by failing to present evidence that penalties were personally approved in writing by immediate supervisor before determination	No	TP
<i>Salloum v. Comm'r</i> , T.C. Memo. 2017-127	6662(b)(2) - TPs (MFJ) substantially understated income tax; did not establish reasonable cause and good faith; no reasonable reliance on advice of a tax professional	No	IRS
<i>Simonsen v. Comm'r</i> , 2018 WL 1320362 (T.C. Mar. 14, 2018)	6662(b)(2) - TPs (MFJ) established reasonable cause and good faith; IRS did not meet burden of production by failing to present evidence that penalties were personally approved in writing by immediate supervisor before determination	Yes	TP
<i>Tiller v. Comm'r</i> , T.C. Summ. Op. 2017-76	6662(b)(1), (2) - TP established reasonable cause and good faith with respect to a portion of the penalty; did not establish reasonable cause and good faith with respect to the other portion of the penalty	Yes	Split
<i>Turan v. Comm'r</i> , T.C. Memo. 2017-141	6662(b)(2) - TP did not establish reasonable cause	Yes	IRS
<i>Welemin v. Comm'r</i> , T.C. Summ. Op. 2017-54	6662(b)(2) - TP substantially understated income; did not establish reasonable cause	Yes	IRS

TABLE 1: Accuracy-Related Penalty Under IRC § 6662(b)(1) and (2)

Case Citation	Issue(s)	Pro Se	Decision
<i>Whitsett v. Comm'r</i> , T.C. Memo. 2017-100	6662(b)(1) - TP established reasonable cause and acted in good faith; TP had reasonable reliance on advice of a tax professional	No	TP
<i>Woolsey v. Comm'r</i> , T.C. Summ. Op. 2017-62	6662(b)(2) - TPs (MFJ) substantially understated income tax; established reasonable cause and good faith	No	TP
<b>Business Taxpayers (Corporations, Partnerships, Trusts, and Sole Proprietorships – Schedules C, E, F)</b>			
<i>Avrahami v. Comm'r</i> , 2017 WL 3610601 (T.C. Aug. 21, 2017)	6662(b)(2) - TPs (MFJ) substantially understated income tax; TPs established reasonable cause and good faith with respect to a portion of the penalties; reasonably relied on the advice of a tax professional with respect to a portion of the penalties; did not establish reasonable cause and good faith with respect to the other portion of the penalties	No	Split
<i>Azam v. Comm'r</i> , T.C. Memo. 2018-72	6662(b)(1), (2) - TPs (MFJ) were not liable for penalty; IRS did not meet burden of production by failing to present evidence that penalties were personally approved in writing by immediate supervisor before determination	Yes	TP
<i>Baham v. Comm'r</i> , T.C. Summ. Op. 2017-85	6662(b)(2) - TPs (MFJ) substantially understated income tax; did not keep adequate books and records; did not establish reasonable cause and good faith	Yes	IRS
<i>Balyan v. Comm'r</i> , T.C. Memo. 2017-140	6662(b)(2) - TP substantially understated income tax; did not establish reasonable cause	Yes	IRS
<i>Barnhart Ranch Co. v. Comm'r</i> , 714 F. App'x 376 (5th Cir. 2017), <i>reh'g denied</i> , Docket No. 16-60834 (5th Cir., Feb. 16, 2018), <i>aff'g</i> , T.C. Memo. 2016-170	6662(b)(1), (2) - TPs (MFJ) failed to show substantial authority for their position; did not establish reasonable cause and good faith	No	IRS
<i>Besaw v. Comm'r</i> , 695 F. App'x 276 (9th Cir. 2017), <i>aff'g</i> T.C. Memo. 2015-233	6662(b)(2) - TP substantially understated income tax	Yes	IRS
<i>Brookes v. Comm'r</i> , T.C. Memo. 2017-146	6662(b)(1) - TPs (MFJ) were negligent due to failure to keep adequate books and records; did not establish reasonable cause and good faith	No	IRS
<i>Brumbaugh v. Comm'r</i> , T.C. Memo. 2018-40	6662(b)(1), (2) - TPs (MFJ) were negligent; did not establish reasonable cause and good faith	No	IRS
<i>Cai v. Comm'r</i> , T.C. Memo. 2018-52	6662(b)(1) - TP established reasonable cause and had reasonable reliance on the advice of a tax professional	Yes	TP
<i>Conner v. Comm'r</i> , T.C. Memo. 2018-6, <i>appeal docketed</i> , No. 18-12997 (11th Cir., July 17, 2018)	6662(b)(1), (2) - TPs (MFJ) established reasonable cause and good faith; reasonably relied on advice of a tax professional	No	TP
<i>Cooper v. Comm'r</i> , 877 F.3d 1086 (9th Cir. 2017), <i>reh'g denied</i> , <i>reh'g, en banc denied</i> , 2018 U.S. App. LEXIS 4735 (9th Cir., Feb. 26, 2018), <i>aff'g</i> 143 T.C. 194 (2014)	6662(b)(1), (2) - TPs (MFJ) were negligent and substantially understated income tax; did not establish reasonable cause and good faith; did not establish reliance on the advice of a tax professional	No	IRS
<i>Derringer Trading LLC v. Comm'r</i> , T.C. Memo. 2018-59	6662(b)(1) - TP was negligent due to failure to keep adequate books and records; did not establish reasonable cause	No	IRS
<i>Dimitrov v. Comm'r</i> , T.C. Summ. Op. 2018-21	6662(b)(1) - TP was negligent; did not establish reasonable cause and good faith	Yes	IRS
<i>Duket v. Comm'r</i> , T.C. Summ. Op. 2017-84	6662(b)(1) - TP was negligent; did not provide sufficient evidence to show IRS determination was incorrect	No	IRS
<i>Dulik v. Comm'r</i> , T.C. Summ. Op. 2017-51	6662(b)(1) - TPs (MFJ) were not liable for portion of the penalty due to keeping adequate books and records, and establishing reasonable cause and good faith; TPs were negligent with respect to the other portion of the penalty and did not establish reasonable cause and good faith	Yes	Split

TABLE 1: Accuracy-Related Penalty Under IRC § 6662(b)(1) and (2)

Case Citation	Issue(s)	Pro Se	Decision
<i>Dynamo Holdings Ltd. P'ship v. Comm'r</i> , T.C. Memo. 2018-61	6662(b)(1), (2) - TP was negligent and had no reasonable basis for position; TP substantially understated income tax; did not establish reasonable cause	No	IRS
<i>Ellison v. Comm'r</i> , T.C. Memo. 2017-134, appeal dismissed, No. 18-72262 (9th Cir., Nov. 8, 2018)	6662(b)(1), (2) - TPs (MFJ) were negligent due to failure to keep adequate books and records; did not establish reasonable cause	Yes	IRS
<i>Fiedziuszko v. Comm'r</i> , T.C. Memo. 2018-75	6662(b)(2) - TPs (MFJ) did not establish reasonable cause and good faith	Yes	IRS
<i>Fleming v. Comm'r</i> , T.C. Summ. Op. 2017-83	6662(b)(1) - TP was negligent; did not establish reasonable cause; no reasonable reliance on advice of a tax professional	No	IRS
<i>Full-Circle Staffing, LLC v. Comm'r</i> , T.C. Memo. 2018-66	6662(b)(2) - TP substantially understated income tax; not liable for penalty because TP established reasonable cause and had reasonable reliance on the advice of a tax professional	No	TP
<i>Grecian Magnesite Mining, Industr. &amp; Shipping Co. v. Comm'r</i> , 149 T.C. No. 3 (2017), appeal docketed, No. 17-1268 (D.C. Cir., Dec. 18, 2017)	6662(b)(1), (2) - TP substantially understated income tax; TP established reasonable cause and good faith, and had reasonable reliance on the advice of a tax professional	No	TP
<i>Hatcher v. Comm'r</i> , 726 F. App'x 207 (5th Cir. 2018), aff'g T.C. Memo. 2016-188	6662(b)(2) - TPs (MFJ) substantially understated income tax; did not establish reasonable cause and good faith	No	IRS
<i>Howard v. Comm'r</i> , T.C. Summ. Op. 2017-65	6662(b)(1) - TP was negligent due to failure to keep adequate books and records; did not establish reasonable cause and good faith; no reasonable reliance on the advice of a tax professional	Yes	IRS
<i>Huzella v. Comm'r</i> , T.C. Memo. 2017-210	6662(b)(2) - TPs (MFJ) did not establish reasonable cause and good faith	Yes	IRS
<i>Hylton v. Comm'r</i> , 721 F. App'x 300 (4th Cir. 2018), reh'g and reh'g, en banc, denied, No. 17-1777 (4th Cir. Aug. 3, 2018), aff'g T.C. Memo. 2016-234	6662(b)(2) - TP substantially understated income tax	No	IRS
<i>Jabari v. Comm'r</i> , T.C. Memo. 2017-238	6662(b)(1), (2) - TPs (MFJ) were negligent; did not establish reasonable cause and good faith	Yes	IRS
<i>Justine v. Comm'r</i> , T.C. Memo. 2017-198	6662(b)(1), (2) - TPs (MFJ) were negligent and substantially understated income tax; did not establish reasonable cause and good faith	Yes	IRS
<i>Keenan v. Comm'r</i> , T.C. Memo. 2018-60	6662(b)(1), (2) - TP failed to show substantial authority for TPs' position; did not establish reasonable cause and good faith	No	IRS
<i>Knowles v. Comm'r</i> , T.C. Memo. 2017-152	6662(b)(1) - TP was negligent due to failure to keep adequate books and records; did not establish reasonable cause	No	IRS
<i>Larson v. Comm'r</i> , T.C. Memo. 2018-30	6662(b)(2) - TP substantially understated income tax; did not establish reasonable cause and good faith; no reasonable reliance on the advice of a tax professional	Yes	IRS
<i>Levine v. Comm'r</i> , T.C. Summ. Op. 2017-60	6662(b)(1) - TP was negligent due to failure to keep adequate books and records; did not establish reasonable cause	Yes	IRS
<i>Lewis v. Comm'r</i> , T.C. Memo. 2017-117	6662(b)(1) - TPs (MFJ) were negligent due to failure to keep adequate books and records; did not establish reasonable cause	Yes	IRS
<i>Losantiville Country Club v. Comm'r</i> , T.C. Memo. 2017-158, aff'd, 2018 U.S. App. LEXIS 28935 (6th Cir., Oct. 15, 2018)	6662(b)(1) - TP was negligent; did not establish reasonable cause and good faith; no reasonable reliance on the advice of a tax professional	No	IRS
<i>McNally v. Comm'r</i> , T.C. Memo 2017-93	6662(b)(2) - TPs (MFJ) did not establish reasonable cause	Yes	IRS

TABLE 1: Accuracy-Related Penalty Under IRC § 6662(b)(1) and (2)

Case Citation	Issue(s)	Pro Se	Decision
<i>Mileham v. Comm'r</i> , T.C. Memo. 2017-168	6662(b)(1), (2) - TP was negligent; did not keep adequate books and records; did not establish reasonable cause and good faith; no reasonable reliance on the advice of a tax professional	No	IRS
<i>Moore v. Comm'r</i> , T.C. Memo. 2018-58	6662(b)(1) - TPs (MFJ) were negligent and did not keep adequate books and records; did not establish reasonable cause and good faith	Yes	IRS
<i>Pemberton v. Comm'r</i> , T.C. Summ. Op. 2017-91	6662(b)(1), (2) - TP was not negligent and kept adequate books and records; established reasonable cause and good faith	Yes	TP
<i>Petersen v. Comm'r</i> , 2017 WL 2558852 (T.C. 2017), <i>appeal docketed</i> , No. 17-9003 (10th Cir., Aug. 8, 2017)	6662(b)(1), (2) - TPs (MFJ) established reasonable cause and good faith	No	TP
<i>Platts v. Comm'r</i> , T.C. Memo. 2018-31	6662(b) - IRS did not meet burden of production by failing to present evidence that penalties were personally approved in writing by immediate supervisor before determination	Yes	TP
<i>Pokawa v. Comm'r</i> , T.C. Memo. 2017-186	6662(b)(1), (2) - TPs (MFJ) were negligent due to failure to keep adequate books and records; did not establish reasonable cause and good faith	Yes	IRS
<i>Povolny Group, Inc. v. Comm'r</i> , T.C. Memo. 2018-37	6662(b)(2) - TPs (MFJ) substantially understated income tax; IRS did not meet burden of production with respect to individual TPs by failing to present evidence that penalties were personally approved in writing by immediate supervisor before determination; TP (C Corp) substantially understated income tax; TP (C Corp) did not establish reasonable cause and did not have reasonable reliance on the advice of a tax professional	No	Split
<i>Rodriguez v. Comm'r</i> , T.C. Memo. 2017-173	6662(b)(1), (2) - TPs (MFJ) were negligent due to failure to keep adequate books and records; did not establish reasonable cause and good faith	Yes	IRS
<i>Rutter v. Comm'r</i> , T.C. Memo. 2017-174, <i>appeal dismissed</i> , No. 17-73320 (9th Cir., Jan. 30, 2018)	6662(b)(2) - TP substantially understated income tax; did not establish reasonable cause and good faith; failed to show substantial authority for TPs' position; no reasonable reliance on the advice of a tax professional	No	IRS
<i>Samadi v. Comm'r</i> , T.C. Summ. Op. 2018-27	6662(b)(1), (2) - TPs (MFJ) substantially understated income tax and were negligent; did not establish reasonable cause and good faith	Yes	IRS
<i>Sarvak v. Comm'r</i> , T.C. Memo. 2018-68	6662(b)(1), (2) - TP did not establish reasonable cause and good faith; no reasonable reliance on the advice of a tax professional	No	IRS
<i>Simonelli v. Comm'r</i> , T.C. Memo. 2017-188, <i>appeal docketed</i> , No. 18-70664 (9th Cir., Mar. 9, 2018)	6662(b)(1) - TPs (MFJ) were negligent due to failure to keep adequate books and records; did not establish reasonable cause and good faith	Yes	IRS
<i>Smiling v. Comm'r</i> , T.C. Memo. 2017-196	6662(b)(2) - TPs (MFJ) substantially understated income tax; TP did not establish reasonable cause and good faith with respect to a portion of the underpayment; did not have reasonable reliance on the advice of a tax professional with respect to a portion of the underpayment; TPs did establish reasonable cause and good faith with respect to the other portion of the underpayment	No	Split
<i>Smith v. Comm'r</i> , T.C. Memo. 2017-218	6662(b)(2) - TPs (MFJ) substantially understated income tax; did not establish reasonable cause and good faith; did not establish reasonable reliance on the advice of a tax professional	No	IRS

TABLE 1: Accuracy-Related Penalty Under IRC § 6662(b)(1) and (2)

Case Citation	Issue(s)	Pro Se	Decision
<i>Stettner v. Comm'r</i> , T.C. Memo. 2017-113	6662(b)(2) - TP substantially understated income tax; did not establish reasonable cause	No	IRS
<i>Sun v. Comm'r</i> , 880 F.3d 173 (5th Cir. 2018), <i>aff'g</i> T.C. Memo. 2015-56	6662(b)(1) - TP was negligent; did not establish good faith; no reasonable reliance on the advice of a tax professional	No	IRS
<i>Syed v. Comm'r</i> , T.C. Memo. 2017-226	6662(b)(1), (2) - TPs were negligent; did not establish reasonable cause and good faith; no reasonable reliance on the advice of a tax professional	No	IRS
<i>Taylor v. Comm'r</i> , T.C. Memo. 2017-99	6662(b)(1) - TPs (MFJ) were negligent due to failure to keep adequate books and records; did not establish reasonable cause	Yes	IRS
<i>Transupport, Inc. v. Comm'r</i> , 882 F.3d 274 (1st Cir. 2018), <i>aff'g</i> T.C. Memo. 2015-179	6662(b)(2) - TP substantially understated income tax; did not establish reasonable cause and good faith; no reasonable reliance on the advice of a tax professional	No	IRS
<i>Triumph Mixed Use Inv. III, LLC v. Comm'r</i> , T.C. Memo. 2018-65	6662(b)(1), (2) - TP was negligent; did not establish reasonable cause and good faith	No	IRS
<i>Vallejo v. Comm'r</i> , T.C. Memo. 2018-39	6662(b)(1), (2) - TP was negligent due to failure to keep adequate books and records; did not establish reasonable cause and good faith	Yes	IRS
<i>Velez v. Comm'r</i> , T.C. Memo. 2018-46	6662(b)(1) - TP was negligent due to failure to keep adequate books and records; did not establish reasonable cause	Yes	IRS
<i>Watts v. Comm'r</i> , T.C. Memo. 2017-114, <i>appeal docketed</i> , No. 17-15282 (11th Cir., Nov. 29, 2017)	6662(b)(1), (2) - TPs (MFJ) established reasonable cause and good faith; reasonably relied on advice of a tax professional	No	TP
<i>Wax v. Comm'r</i> , T.C. Memo. 2018-63	6662(b)(2) - TPs (MFJ) substantially understated income tax; did not establish reasonable cause and good faith	Yes	IRS
<i>Wells v. Comm'r</i> , T.C. Memo. 2018-11, <i>appeal docketed</i> , No. 18-9007 (10th Cir., Aug. 15, 2018)	6662(b)(1), (2) - TP kept adequate books and records; TP established reasonable cause and good faith	No	TP
<i>Wendell Falls Dev. LLC v. Comm'r</i> , T.C. Memo. 2018-45	6662(b)(1) - TP established reasonable cause and good faith	No	TP
<i>Western Prop. Restoration, Inc. v. Comm'r</i> , T.C. Memo. 2017-190	6662(b)(1), (2) - TP substantially understated income tax and was negligent; did not establish reasonable cause; no reasonable reliance on the advice of a tax professional	No	IRS
<i>Williams v. Comm'r</i> , T.C. Memo. 2018-48	6662(b)(1), (2) - TP was negligent due to failure to keep adequate books and records; did not establish reasonable cause and good faith; did not establish reasonable reliance on the advice of a tax professional	No	IRS
<i>Wycoff v. Comm'r</i> , T.C. Memo. 2017-203	6662(b)(2) - TPs (MFJ) substantially understated income tax; did not establish reasonable cause and good faith; no reasonable reliance on advice of a tax professional	No	IRS
<i>Zia-Ahmadi v. Comm'r</i> , T.C. Summ. Op. 2017-39	6662(b)(1), (2) - TP (C Corp) was negligent and did not establish reasonable cause and good faith; TPs (MFJ) were negligent and did not establish reasonable cause and good faith	Yes	IRS
<i>Zudak v. Comm'r</i> , T.C. Summ. Op. 2017-41	6662(b)(2) - TP substantially understated income tax; did not establish reasonable cause, no reasonable reliance on the advice of a tax professional	Yes	IRS

**TABLE 2: Trade or Business Expenses Under IRC § 162 and Related Sections**

Case Citation	Issue(s)	Pro Se	Decision
<b>Individual Taxpayers (But Not Sole Proprietorships)</b>			
<i>Baham v. Comm'r</i> , T.C. Summ. Op. 2017-85	Schedule C startup costs properly deducted under § 195(b); Schedule A unreimbursed employee business expenses relating to animals in the classroom, research and literature, and cell phone expenses disallowed and not related to a trade or business	Yes	Split
<i>Balyan v. Comm'r</i> , T.C. Memo. 2017-140	Schedule C vehicle expense deductions disallowed due to inability to meet the requirements of § 274(d)	Yes	IRS
<i>Beckey v. Comm'r</i> , T.C. Summ. Op. 2017-80	Unreimbursed employee business expenses disallowed and disallowed as personal under § 262(a)	Yes	IRS
<i>Benjamin v. Comm'r</i> , T.C. Memo. 2018-70, <i>appeal docketed</i> , No. 18-72831 (9th Cir. Oct 18, 2018)	TPs were not away from home within the meaning of § 162; Schedule A expenses relating to maintaining two residences or relating to travel between them disallowed	Yes	IRS
<i>Cates v. Comm'r</i> , T.C. Memo. 2017-178, <i>appeal dismissed</i> , (11th Cir. Apr. 30, 2018)	Unreimbursed employee business expenses disallowed	Yes	IRS
<i>Colliver v. Comm'r</i> , T.C. Summ. Op. 2017-93	TP's education expense deductions unsubstantiated; unreimbursed employee business expenses disallowed	Yes	IRS
<i>Edwards v. Comm'r</i> , T.C. Memo. 2018-44	Vehicle expenses disallowed under § 274(d); unreimbursed employee business expenses disallowed	Yes	IRS
<i>Fehr v. Comm'r</i> , T.C. Summ. Op. 2018-26	Unreimbursed employee business expenses, including deductions for vehicle, travel, meals, entertainment, and other miscellaneous expenses, disallowed under § 274(d)	Yes	IRS
<i>Havener v. Comm'r</i> , T.C. Summ. Op. 2018-17	Schedule C deductions related to house remodeling deferred as capital expenses under § 263(a)(1)	Yes	IRS
<i>Jahangirian v. Comm'r</i> , T.C. Summ. Op. 2018-14	Unreimbursed employee business expenses related to travel disallowed	Yes	IRS
<i>Keefe v. Comm'r</i> , T.C. Memo. 2018-28, <i>appeal docketed</i> , No. 18-2357 (2nd Cir. Aug. 10, 2018)	Real estate holding was a capital asset, not a rental property used in a trade or business; associated interest required to be capitalized under § 263A	No	IRS
<i>Kruse-Colbert v. Comm'r</i> , T.C. Summ. Op. 2018-7	Miscellaneous unreimbursed employee business expenses partially allowed under § 274(d) and as related to being engaged in a trade or business	Yes	Split
<i>Lewis v. Comm'r</i> , T.C. Memo. 2017-117	TPs earned no income and thus were ineligible for under § 183 most claimed deductions would have also failed the documentation requirements of § 274(d)	Yes	IRS
<i>Linde v. Comm'r</i> , 2017 WL 4158701 (T.C. Sept. 18, 2017)	Unreimbursed employee business expense deductions related to travel disallowed; miscellaneous non-travel unreimbursed employee business expenses disallowed under § 274(d)	No	IRS
<i>Martinez v. Comm'r</i> , T.C. Summ. Op. 2017-42	Business mileage expense deduction disallowed as not related to being engaged in a trade or business and lacking substantiation; deductions for vehicle expenses, travel, meals, and entertainment disallowed under § 274(d); unreimbursed employee business expense deductions partially allowed	Yes	Split
<i>Rademacher v. Comm'r</i> , T.C. Memo. 2018-43	Miscellaneous unreimbursed employee business expenses, including meal and entertainment expenses, disallowed under § 274(d); mileage expense deduction partially allowed under § 274(d)	No	Split
<i>Farolan v. Comm'r</i> , T.C. Summ. Op. 2018-28	Unreimbursed employee business expense deductions, including clothing costs, dry cleaning costs, and meal and entertainment expenses disallowed as personal under § 262; travel expenses partially substantiated	Yes	Split

TABLE 2: Trade or Business Expenses Under IRC § 162 and Related Sections

Case Citation	Issue(s)	Pro Se	Decision
<i>Tiller v. Comm'r</i> , T.C. Summ. Op. 2017-76	Unreimbursed employee business expenses partially allowed under § 274(d)	Yes	Split
<i>Tucker v. Comm'r</i> , T.C. Memo. 2017-183, appeal docketed, No. 17-60833 (5th Cir. Dec. 19, 2018)	Loss deductions disallowed because related foreign transactions involving offsetting foreign currency options lacked economic substance	No	IRS
<i>Wooten v. Comm'r</i> , T.C. Summ. Op. 2017-58	Unreimbursed employee business expense deduction relating to commuting expenses disallowed; related meal expense deductions unsubstantiated	Yes	IRS
<b>Business Taxpayers (Corporations, Partnerships, Trusts, and Sole Proprietorships – Schedules C, E, F)</b>			
<i>Avrahami v. Comm'r</i> , 2017 WL 3610601 (T.C. Aug. 21, 2017)	Deductions claimed by captive insurance company for premiums unsubstantiated under § 162	No	IRS
<i>Azam v. Comm'r</i> , T.C. Memo. 2018-72	Deductions for vehicle expenses, travel, meals, and entertainment disallowed under § 274(d); miscellaneous Schedule C deductions unsubstantiated	Yes	IRS
<i>Barker v. Comm'r</i> , T.C. Memo. 2018-67	TP was engaged in the trade or business of producing music; business deductions unsubstantiated; net operating loss deduction disallowed under § 172	No	IRS
<i>Barrett v. Comm'r</i> , T.C. Memo. 2017-195	TP was away from home under § 162(a); various deductible expenses disallowed as unsubstantiated; deductions for meals, lodging, and entertainment disallowed under § 274(d)	No	Split
<i>Bass v. Comm'r</i> , 738 Fed. Appx. 178 (4th Cir. 2018), <i>aff'g</i> T.C. Memo. 2018-19	Vehicle expenses on Schedule C disallowed under § 274(d); miscellaneous expenses disallowed as unsubstantiated	Yes	IRS
<i>Becker v. Comm'r</i> , T.C. Memo. 2018-69	Miscellaneous business expense deductions, such as for consulting, unsubstantiated; deductions for travel and meals disallowed under § 274(d); depreciation deduction disallowed under § 167	No	IRS
<i>Besaw v. Comm'r</i> , 695 F. App'x 276 (9th Cir. 2017), <i>aff'g</i> T.C. Memo. 2015-233	Schedule C deductions for wages, travel, and meals and entertainment business expenses unsubstantiated	Yes	IRS
<i>Boneparte v. Comm'r</i> , T.C. Memo. 2017-193, appeal docketed, No. 18-2264 (3d Cir. June 8, 2018)	Deduction for gambling losses disallowed under § 183	Yes	IRS
<i>Bradley v. Comm'r</i> , T.C. Summ. Op. 2018-13	Business deductions, including those for research expenditures, unsubstantiated	Yes	IRS
<i>Brookes v. Comm'r</i> , T.C. Memo. 2017-146	Deductions for travel, meals, and entertainment, and vehicle expenses disallowed under § 274(d); art business deductions allowed under <i>Cohan</i> ; medical expense deductions substantiated	No	Split
<i>Brown v. Comm'r</i> , T.C. Summ. Op. 2018-6	Claimed deductible repair costs recharacterized as § 263 depreciable capital expenditures	No	IRS
<i>Burke v. Comm'r</i> , T.C. Memo. 2018-18	Bad debt deductions disallowed under § 166 because the debt was not <i>bona fide</i>	No	IRS
<i>Cai v. Comm'r</i> , T.C. Memo. 2018-52	Deductions for travel, business gifts, vehicle expenses, depreciation, and commission fees disallowed under § 274(d); deduction for office supplies partially allowed under § 274(d); rent and lease expenses substantiated	Yes	Split
<i>Canna-Care, Inc. v. Comm'r</i> , 694 F. App'x 570 (9th Cir. 2017), <i>aff'g</i> T.C. Memo. 2015-206	Medical marijuana dispensary business expense deductions disallowed as illegal activity under § 280E	No	IRS
<i>Carrick v. Comm'r</i> , T.C. Summ. Op. 2017-56	TP not engaged in a trade or business; Schedule C research and development costs ineligible for § 195 deduction, as TP had already claimed § 195(b) deduction	Yes	IRS

TABLE 2: Trade or Business Expenses Under IRC § 162 and Related Sections

Case Citation	Issue(s)	Pro Se	Decision
<i>Chen v. Comm'r</i> , T.C. Summ. Op. 2017-90	Schedule C additional deduction for real estate commission rebate disallowed as unsubstantiated	Yes	IRS
<i>Christopher C.L. Ng MD, Inc. v. Comm'r</i> , T.C. Memo. 2018-14	Deductions for rental expenses to corporation's sole shareholder unsubstantiated	Yes	IRS
<i>Conner v. Comm'r</i> , T.C. Memo. 2018-6, <i>appeal docketed</i> , No. 18-12997 (11th Cir. July 17, 2018)	Schedule C deductions disallowed because TPs were unable to prove that they were engaged in a trade or business; records were inadequate to establish net operating loss deduction under § 172	No	IRS
<i>Conrad v. Comm'r</i> , T.C. Memo. 2017-116	Deduction for net operating loss for partnership disallowed under § 172 as fictitious	No	IRS
<i>Crissey v. Comm'r</i> , T.C. Summ. Op. 2017-44	Expenses related to consulting business disallowed as they did not relate to being engaged in a trade or business; unreimbursed employee business expenses for job as outside salesman allowed; TP was engaged in a trade or business relating to day trading; home office deduction disallowed under § 280A	Yes	Split
<i>Cristo v. Comm'r</i> , T.C. Memo. 2017-239, <i>appeal docketed</i> , No. 18-71788 (9th Cir. June 19, 2018)	Meals and lodging expenses disallowed under § 274(d); miscellaneous travel expenses partially disallowed under § 274(d); Schedule C training expense deduction unsubstantiated	Yes	Split
<i>Curtis Inv. Co. v. Comm'r</i> , T.C. Memo. 2017-150, <i>appeal docketed</i> , No. 17-14573 (11th Cir. Oct. 12, 2018)	Deductions for losses and fees disallowed, as the transactions in question lacked economic substance and a business purpose	No	IRS
<i>Davis v. Comm'r</i> , T.C. Memo. 2018-56	Unreimbursed employee business expense deductions, including for mileage, travel, and meals and entertainment, disallowed under § 274(d)	Yes	IRS
<i>Derringer Trading, LLC v. Comm'r</i> , T.C. Memo. 2018-59	Business bad debt deductions for two partnerships disallowed under § 166 as abusive tax shelter-related activities; amortization of expenses related to the debt transactions unsubstantiated	No	IRS
<i>Dimitrov v. Comm'r</i> , T.C. Summ. Op. 2018-21	Schedule C mileage and vehicle expense deductions disallowed under § 274(d)	Yes	IRS
<i>Drah v. Comm'r</i> , T.C. Memo. 2017-149	Deductions for contract labor expenses and vehicle repair costs unsubstantiated; vehicle depreciation deduction disallowed under § 179, as taxpayer did not own the vehicle	No	IRS
<i>Duket v. Comm'r</i> , T.C. Summ. Op. 2017-84	Deductions for labor costs substantiated; miscellaneous expenses unsubstantiated; car and truck expenses disallowed under § 274(d)	No	Split
<i>Dulik v. Comm'r</i> , T.C. Summ. Op. 2017-51	Legal fees unsubstantiated because they did not result from being engaged in a trade or business	Yes	IRS
<i>Eaton Corp. v. Comm'r</i> , T.C. Memo. 2017-147	Deductions for employee compensation in the form of bonus payments substantiated	No	TP
<i>Ellison v. Comm'r</i> , T.C. Memo. 2017-134, <i>appeal dismissed</i> , No. 18-72262 (9th Cir. Nov. 8, 2018)	Deductions claimed under § 280A disallowed due to lack of testimony	Yes	IRS
<i>Enis v. Comm'r</i> , T.C. Memo. 2017-222	Net operating loss deductions under § 172 disallowed	No	IRS
<i>Feinberg v. Comm'r</i> , T.C. Memo. 2017-211, <i>appeal docketed</i> , No. 18-9005 (10th Cir. June 4, 2018)	Business expenses unsubstantiated	No	IRS
<i>Fiedziuszko v. Comm'r</i> , T.C. Memo. 2018-75	Travel, meals, and lodging expenses disallowed under § 274(d)	Yes	IRS

TABLE 2: Trade or Business Expenses Under IRC § 162 and Related Sections

Case Citation	Issue(s)	Pro Se	Decision
<i>Fleming v. Comm'r</i> , T.C. Summ. Op. 2017-83	Schedule C deductions disallowed as unsubstantiated and inestimable under <i>Cohan</i>	No	IRS
<i>Ford v. Comm'r</i> , 2018 WL 5794470 (6th Cir. Nov. 5, 2018), <i>aff'g</i> T.C. Memo. 2018-8	Deductions for § 172 net operating losses disallowed under § 183	No	IRS
<i>Geneser v. Comm'r</i> , T.C. Memo. 2017-110	Deduction for loan interest repayment disallowed under § 163; deduction for loan service fees unsubstantiated	No	IRS
<i>Gollnick v. Comm'r</i> , T.C. Summ. Op. 2017-94	Vehicle expenses disallowed under § 274(d); miscellaneous business expenses partially substantiated under <i>Cohan</i>	Yes	Split
<i>Grago v. Comm'r</i> , T.C. Summ. Op. 2017-67	TP's law enforcement badge database was not a trade or business under § 183, as he did not maintain adequate records and showed no profit motive	Yes	IRS
<i>Hatcher v. Comm'r</i> , 726 F. App'x 207 (5th Cir. 2018), <i>aff'g</i> T.C. Memo. 2016-188	Bad debt deduction disallowed under § 166 because the debt, part of which was recovered, did not become worthless during the year in question; deduction for net operating loss under § 172 disallowed	No	IRS
<i>Howard v. Comm'r</i> , T.C. Summ. Op. 2017-65	Unreimbursed employee business expense deductions disallowed; depreciation and amortization disallowed under § 167; Schedule C deductions disallowed under § 274(d)	Yes	IRS
<i>Hylton v. Comm'r</i> , 721 F. App'x 300 (4th Cir. 2018), <i>aff'g</i> T.C. Memo. 2016-234, <i>reh'g and reh'g, en banc, denied</i> , No. 17-1777 (4th Cir. Aug. 3, 2018)	Schedule F horse breeding, training, showing, and sales activity disallowed as not engaged in for profit under § 183 and related losses therefore disallowed	No	IRS
<i>Jacobs v. Comm'r</i> , 2017 WL 2733795 (T.C. 2017)	Deductions for meals and snacks allowed under § 274(n)	No	TP
<i>Justine v. Comm'r</i> , T.C. Memo. 2017-198	Schedule A and Schedule C deductions unsubstantiated	Yes	IRS
<i>Knowles v. Comm'r</i> , T.C. Memo. 2017-152	Schedule C business expense deductions unsubstantiated; TP's horse farm activities disallowed under § 183; deductions related to grill cleaning business unsubstantiated; unreimbursed employee business expenses disallowed	No	IRS
<i>Kohn v. Comm'r</i> , T.C. Memo. 2017-159	Deduction attributed to settlement unsubstantiated	Yes	IRS
<i>Lender Mgmt. v. Comm'r</i> , T.C. Memo. 2017-246	TP, an investment management services provider, was engaged in a trade or business	No	TP
<i>Levine v. Comm'r</i> , T.C. Summ. Op. 2017-60	Deduction for advertising expenses substantiated; vehicle expense deduction disallowed under § 274(d); TP was unable to prove claims of lost records or to reconstruct vehicle use; deduction for office supplies partially substantiated; utility expenses unsubstantiated	Yes	Split
<i>Main v. Comm'r</i> , 719 F. App'x 699 (9th Cir. 2018) <i>aff'g</i> T.C. Memo. 2016-127	9th Circuit affirmed without opinion Tax Court decision disallowing deductions for listed property under § 280F and miscellaneous unsubstantiated deductions; allowing depreciation deductions under § 167 and deductions for unsubstantiated expenses under § 162	Yes	IRS
<i>McMillan v. Comm'r</i> , 697 F. App'x 489 (9th Cir. 2017), <i>aff'g</i> T.C. Memo. 2013-40, <i>cert. denied</i> , 138 S.Ct. 1010 (2018)	TP was not engaged in horse trading for profit under § 183	Yes	IRS
<i>Meruelo v. Comm'r</i> , T.C. Memo. 2018-16, <i>appeal docketed</i> , No. 18-11909 (11th Cir. May 7, 2018)	Net operating loss deductions disallowed under § 172	No	IRS
<i>Moore v. Comm'r</i> , T.C. Memo. 2018-58	Meals and entertainment deductions unsubstantiated; vehicle expenses disallowed under § 274(d); miscellaneous Schedule C deductions unsubstantiated	Yes	IRS

TABLE 2: Trade or Business Expenses Under IRC § 162 and Related Sections

Case Citation	Issue(s)	Pro Se	Decision
<i>Nicholson v. Comm'r</i> , T.C. Summ. Op. 2018-24	Schedule C deductions partially substantiated and partially ruled as § 262 personal expenditures	Yes	Split
<i>Owens v. Comm'r</i> , T.C. Memo. 2017-157	TP was engaged in a trade or business of lending money; the bad debt was a <i>bona fide</i> debt and allowed under § 166	No	TP
<i>Pemberton v. Comm'r</i> , T.C. Summ. Op. 2017-91	Education expenses unsubstantiated as not ordinary and necessary and as relating to a new business, not TP's current business	Yes	IRS
<i>Pokawa v. Comm'r</i> , T.C. Memo. 2017-186	Schedule C deductions partially allowed under <i>Cohan</i> ; unreimbursed employee business expenses disallowed	Yes	Split
<i>Polovny Group, Inc., v. Comm'r</i> , T.C. Memo. 2018-37	Business bad debt deduction disallowed under § 166 because the debt was not <i>bona fide</i>	No	IRS
<i>Riggins v. Comm'r</i> , 122 A.F.T.R. 2d 5831 (11th Cir. 2018), <i>aff'g</i> T.C. Memo. 2017-106	Schedule C business deductions from law practice unsubstantiated	Yes	IRS
<i>RJ Channels, Inc. v. Comm'r</i> , T.C. Memo. 2018-27	Client expense deductions unsubstantiated; lawsuit deduction unsubstantiated; miscellaneous deductions unsubstantiated	No	IRS
<i>Rodriguez v. Comm'r</i> , T.C. Memo. 2017-173	Vehicle expenses, travel expenses, and meals and entertainment expenses disallowed under § 274(d); Schedule C utility expense disallowed as unsubstantiated	Yes	IRS
<i>Rogers v. Comm'r</i> , T.C. Memo. 2018-53	Bad debt deductions disallowed under § 166; deductions related to business use of home disallowed under § 280A; miscellaneous Schedule C deductions, including interest and insurance, unsubstantiated; business gift deductions partially substantiated; travel, meals, and entertainment unsubstantiated; vehicle expenses disallowed under § 274(d) and § 280F; legal and professional fees partially substantiated; deductions related to real estate holdings deferred as capital expenses under § 263A; miscellaneous deductions relating to TPs' (MFJ) business unsubstantiated under § 162 or disallowed under § 274(d); travel expenses disallowed under § 274(d); medical expenses deduction unsubstantiated	Yes	Split
<i>Rutter v. Comm'r</i> , T.C. Memo. 2017-174, <i>appeal dismissed</i> , No. 17-73320 (9th Cir. Jan. 30, 2018)	Business bad debt deduction disallowed under § 166, as transactions lacked economic substance and TP was not engaged in the trade or business of lending money or promoting companies	No	IRS
<i>Salloum v. Comm'r</i> , T.C. Memo. 2017-127	Schedule C deductions for repayment of funds unsubstantiated	No	IRS
<i>Samadi v. Comm'r</i> , T.C. Summ. Op. 2018-27	House flipping activity was not a trade or business under § 162 and thus related deductions disallowed	Yes	IRS
<i>Sarvak v. Comm'r</i> , T.C. Memo. 2018-68	Business bad debt deductions disallowed under § 166	No	IRS
<i>Simonelli v. Comm'r</i> , T.C. Memo. 2017-188, <i>appeal docketed</i> , No. 18-70664 (9th Cir. March 9, 2018)	Schedule C deductions disallowed under § 183	Yes	IRS
<i>Singh v. Comm'r</i> , 121 A.F.T.R.2d 5109 (9th Cir. 2018), <i>reh'g and reh'g en banc denied</i> , No. 17-71020 (9th Cir. July 2, 2018), <i>aff'g</i> No. 11063-09 (Feb. 1, 2017)	Business deductions unsubstantiated	Yes	IRS
<i>Smiling v. Comm'r</i> , T.C. Memo. 2017-196	Business expenses unsubstantiated; legal fees reported on Schedule C unsubstantiated	No	IRS
<i>Smith v. Comm'r</i> , T.C. Memo. 2017-218	Short term capital loss deductions disallowed, as S corporation's dissolution lacked economic substance	No	IRS

TABLE 2: Trade or Business Expenses Under IRC § 162 and Related Sections

Case Citation	Issue(s)	Pro Se	Decision
<i>Stettner v. Comm'r</i> , T.C. Memo. 2017-113	Car racing activity was not a trade or business under § 183	No	IRS
<i>Taylor v. Comm'r</i> , T.C. Memo. 2017-99	Vehicle expenses disallowed under § 274(d)	Yes	IRS
<i>Thompson v. Comm'r</i> , T.C. Summ. Op. 2018-11	Vehicle expenses disallowed under § 274(d); travel expenses partially substantiated; miscellaneous Schedule C expenses partially substantiated	Yes	Split
<i>Triumph Mixed Use Invs. III, LLC v. Comm'r</i> , T.C. Memo. 2018-65	Business bad debt deduction allowed under § 166	No	TP
<i>Vallejo v. Comm'r</i> , T.C. Memo. 2018-39	Schedule C expenses unsubstantiated under § 162 and disallowed under § 274(d)	Yes	IRS
<i>Velez v. Comm'r</i> , T.C. Memo. 2018-46	Vehicle expense disallowed under § 274(d)	Yes	IRS
<i>Venuto v. Comm'r</i> , T.C. Memo. 2017-123	Travel, meals, entertainment, car rental, and gasoline expenses partially allowed under § 274(d), partially disallowed as unevicenced or lacking business purpose; graphic design and website expenses substantiated; computer and computer maintenance expenses partially substantiated; miscellaneous expenses partially substantiated and related to being engaged in a trade or business; debt deductions disallowed under § 163	Yes	Split
<i>Vest v. Comm'r</i> , 690 F. App'x 210 (5th Cir. 2017), <i>aff'g</i> T.C. Memo. 2016-187	Expenses related to investigation of TP's parent's death properly disallowed under § 183	Yes	IRS
<i>VHC, Inc., v. Comm'r</i> , T.C. Memo. 2017-220	Bad debt deductions disallowed under § 166 because the debt was not <i>bona fide</i> ; deducted advances disallowed as unsubstantiated	No	IRS
<i>Wages v. Comm'r</i> , T.C. Memo. 2017-103	Business expense deductions for bail bonding and towing businesses unsubstantiated under <i>Cohan</i>	No	IRS
<i>Wax v. Comm'r</i> , T.C. Memo. 2018-63	Vehicle expenses, travel expenses, and meal and entertainment expenses disallowed under § 274(d); miscellaneous Schedule C deductions, including living expenses of TP's adult children, unsubstantiated and reclassified as personal	Yes	IRS
<i>Welch v. Comm'r</i> , T.C. Memo. 2017-229	Ranch activity was a single activity engaged in for profit under § 183	No	TP
<i>Wells v. Comm'r</i> , T.C. Memo. 2018-11, <i>appeal docketed</i> , No. 18-9007 (10th Cir. Aug. 27, 2018)	Deductions for expenditures relating to farm improvements had to be capitalized under § 263	No	IRS
<i>Williams v. Comm'r</i> , T.C. Memo. 2018-48	Schedule F ranch activity was not a trade or business under § 183; related deductions limited to the extent of income derived from the activity under § 183	No	IRS
<i>Wycoff v. Comm'r</i> , T.C. Memo. 2017-203	Management fees deduction partially disallowed for failure to substantiate reasonableness	No	IRS
<i>Zia-Ahmadi v. Comm'r</i> , T.C. Summ. Op. 2017-39	Deduction for vehicle depreciation disallowed under § 167(a); interest deductions for personal vehicles disallowed as unrelated to being engaged in a trade or business	Yes	IRS
<i>Zollinger v. Comm'r</i> , T.C. Summ. Op. 2017-81	Schedule C deductions unsubstantiated because loan repayments are nondeductible expenditures	Yes	IRS
<i>Zudak v. Comm'r</i> , T.C. Summ. Op. 2017-41	Film festival activity disallowed under § 183	Yes	IRS

**TABLE 3: Summons Enforcement Under IRC §§ 7602, 7604, and 7609**

Case Citation	Issue(s)	Pro Se	Decision
<b>Individual Taxpayers (But Not Sole Proprietorships)</b>			
<i>Aguirre, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 925 (W.D. Tex. 2018)	Summons enforced	Yes	IRS
<i>Ali, U.S. v.</i> , 874 F.3d 825 (4th Cir. 2017), <i>aff'g</i> 119 A.F.T.R.2d (RIA) 1145 (D. Md. 2016)	Lower court's contempt finding affirmed	No	IRS
<i>Arver, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5999 (W.D. Mich. 2017), <i>adopting</i> 120 A.F.T.R.2d (RIA) 5999 (W.D. Mich. 2017)	Summons enforced	Yes	IRS
<i>Barela, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 6494 (E.D. Cal. 2017)	TP held in contempt; Arrest warrant issued	Yes	IRS
<i>Berber, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 991 (C.D. Cal. 2018)	Summons enforced	Yes	IRS
<i>Beverly v. U.S.</i> , 121 A.F.T.R.2d (RIA) 1657 (C.D. Cal. 2018)	TPs' petition to quash summons denied for lack of jurisdiction	Yes	IRS
<i>Briseno, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 527 (E.D. Cal. 2018), <i>adopting</i> 120 A.F.T.R.2d (RIA) 6757 (E.D. Cal. 2017)	Summons enforced	Yes	IRS
<i>Briseno, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1540 (E.D. Cal. 2018)	TP held in contempt; Arrest warrant issued	Yes	IRS
<i>Caamano, U.S. v.</i> , 2018 U.S. Dist. LEXIS 28887 (C.D. Cal. 2018)	Summons enforced	Yes	IRS
<i>Canepa, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 768 (E.D. Cal. 2018), <i>adopting</i> 120 A.F.T.R.2d (RIA) 6621 (E.D. Cal. 2017)	Summons enforced	Yes	IRS
<i>Cavins, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 2220 (S.D. Ill. 2018)	Summons enforced	Yes	IRS
<i>Chavez, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1513 (C.D. Cal. 2017)	Summons enforced	Yes	IRS
<i>Chavez, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1512 (C.D. Cal. 2017)	Summons enforced	Yes	IRS
<i>Chrobak, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1824 (E.D.N.Y. 2018)	TP's petition to quash third-party summons denied	Yes	IRS
<i>Clement, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 6323 (M.D. Fla. 2017), <i>adopting</i> 120 A.F.T.R.2d (RIA) 6322 (M.D. Fla. 2017)	Summons enforced	Yes	IRS
<i>Conner, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 6244 (N.D. Tex. 2017), <i>adopting</i> 120 A.F.T.R.2d (RIA) 6241 (N.D. Tex. 2017), <i>appeal docketed</i> , No. 17-11417 (5th Cir., Dec. 1, 2017)	TP still held in contempt; TP's motion to vacate contempt order denied	No	IRS
<i>Connors, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 930 (S.D. Cal. 2018)	Summons enforced	No	IRS
<i>Connors, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 769 (S.D. Cal. 2018)	Summons enforced	No	IRS
<i>Cunamay, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1395 (S.D. Cal. 2018)	Summons enforced	Yes	IRS
<i>Davidson v. U.S.</i> , 121 A.F.T.R.2d (RIA) 782 (S.D. Tex. 2018), <i>adopting</i> 121 A.F.T.R.2d (RIA) 779 (S.D. Tex. 2018)	Summons enforced; TP's petition to quash third-party summons denied	No	IRS
<i>Elridge, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1341 (E.D. Ark. 2018)	Summons enforced	Yes	IRS
<i>Fink, U.S. v.</i> , 2017 U.S. Dist. LEXIS 95087 (S.D. Cal. 2017)	Summons enforced	Yes	IRS
<i>Fleishman, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 6168 (E.D. Tenn. 2017), <i>adopting</i> 120 A.F.T.R.2d (RIA) 6166 (E.D. Tenn. 2017)	Summons enforced	Yes	IRS
<i>Freitas, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5002 (E.D. Cal. 2017)	Summons enforced	Yes	IRS
<i>Givens-Schultz, U.S. v.</i> , 121 A.F.T.R.2d 365 (W.D. Wis. 2018)	Summons enforced	Yes	IRS
<i>Gonzales, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 896 (M.D. Fla. 2018), <i>adopting</i> 121 A.F.T.R.2d (RIA) 895 (M.D. Fla. 2018)	Summons enforced	Yes	IRS
<i>Grote, U.S. v.</i> , 2018 U.S. Dist. LEXIS 47896 (N.D. Iowa 2018), <i>adopting</i> 2018 U.S. Dist. LEXIS 48378 (N.D. Iowa. 2018)	Summons enforced	Yes	IRS
<i>Hanse v. U.S.</i> , 121 A.F.T.R.2d (RIA) 949 (N.D. Ill. 2018)	Summons enforced; TP's petition to quash third-party summons denied	No	IRS
<i>Hoff, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1306 (W.D. Wis. 2018)	Summons enforced	No	IRS

TABLE 3: Summons Enforcement Under IRC §§ 7602, 7604, and 7609

Case Citation	Issue(s)	Pro Se	Decision
<i>Hoff, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1296 (W.D. Wis. 2018)	Summons enforced	No	IRS
<i>Hsu v. U.S.</i> , 121 A.F.T.R.2d (RIA) 1789 (N.D. Cal. 2018)	TPs' petition to quash third-party summons granted in part and denied in part	No	Split
<i>Ifill, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 762 (D.N.J. 2017)	Summons enforced	Yes	IRS
<i>Jones, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1238 (S.D. Fla. 2018)	Summons enforced	Yes	IRS
<i>Jones v. U.S.</i> , 120 A.F.T.R.2d (RIA) 5887 (D. Utah 2017), adopting 120 A.F.T.R.2d (RIA) 5884 (D. Utah 2017)	TP's petition to quash third-party summons denied; lack of subject matter jurisdiction	Yes	IRS
<i>Kenny-Greenwood, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 799 (D. Mont. 2018)	Summons enforced	Yes	IRS
<i>Knutson, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 6756 (E.D. Cal. 2017), adopting 120 A.F.T.R.2d (RIA) 6588 (E.D. Cal. 2017)	Summons enforced	Yes	IRS
<i>Konate, U.S. v.</i> , 2017 U.S. Dist. LEXIS 194220 (M.D.N.C. 2017), adopting 2017 U.S. Dist. LEXIS 195010 (M.D.N.C. 2017)	Summons enforced	Yes	IRS
<i>Lui, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5332 (N.D. Cal. 2017)	Summons for documents and testimony enforced in part; TP not required to produce documents not in his possession	No	Split
<i>Lui, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1537 (N.D. Cal. 2018)	Government's motion for contempt denied as TP complied with court's order	No	TP
<i>Medina, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1239 (C.D. Cal. 2018)	Summons enforced	Yes	IRS
<i>Mellon, U.S. v.</i> , 719 F. App'x 74 (2d Cir. 2018), <i>aff'g</i> 121 A.F.T.R.2d (RIA) 453 (S.D.N.Y. 2017)	Summons enforced	No	IRS
<i>Mesa, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1849 (S.D. Fla. 2018)	Summons enforced	No	IRS
<i>Morton, U.S. v.</i> , 2017 U.S. App. LEXIS 20409 (6th Cir. 2017), <i>reh'g denied</i> , 2017 U.S. App. LEXIS 22757 (6th Cir. 2017), <i>aff'g</i> 119 A.F.T.R.2d (RIA) 362 (W.D. Mich. 2016)	Summons enforced	Yes	IRS
<i>Nevius v. U.S.</i> , 257 F. Supp. 3d 9 (D.D.C. 2017)	Summons enforced; TP's petition to quash third-party summons denied	Yes	IRS
<i>Pappace, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5804 (E.D. Cal. 2017), adopting 119 A.F.T.R.2d (RIA) 2361 (E.D. Cal. 2017)	Summons enforced	Yes	IRS
<i>Pardo, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1611 (C.D. Cal. 2018)	Summons enforced	Yes	IRS
<i>Pate, U.S. v.</i> , 721 F. App'x 556 (8th Cir. 2018), <i>aff'g</i> 118 A.F.T.R.2d (RIA) 5989 (W.D. Mo. 2016)	Summons enforced; TPs improperly invoked Fifth Amendment privilege	No	IRS
<i>Posner, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5812 (S.D. Cal. 2017)	TP held in contempt; Arrest warrant issued	Yes	IRS
<i>Radchik, U.S. v.</i> , 119 A.F.T.R.2d (RIA) 2039 (D.N.J. 2017)	Summons enforced	No	IRS
<i>Rains, In re</i> , 121 A.F.T.R.2d (RIA) 1896 (C.D. Cal. 2018), <i>appeal docketed</i> , No. 18-55992 (9th Cir., July 23, 2018)	TP's petition to quash third-party summons denied	No	IRS
<i>Reyes, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5287 (N.D. Cal. 2017)	Summons enforced	Yes	IRS
<i>Reyes, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5289 (N.D. Cal. 2017)	Summons enforced	Yes	IRS
<i>Rowe v. U.S.</i> , 121 A.F.T.R.2d (RIA) 1796 (E.D. La. 2018)	TPs' petition to quash third-party summons denied	No	IRS
<i>Servin, U.S. v.</i> , 721 F. App'x 156 (3d. Cir. 2018), <i>aff'g</i> 121 A.F.T.R. 2d (RIA) 646 (E.D. Pa. 2017)	Summons enforced; TP failed to show that attorney-client privilege or state rules of professional conduct shield information requested by IRS	Yes (Pro Se, but is attorney)	IRS

TABLE 3: Summons Enforcement Under IRC §§ 7602, 7604, and 7609

Case Citation	Issue(s)	Pro Se	Decision
<i>Smith v. IRS</i> , 121 A.F.T.R.2d (RIA) 586 (D. Del. 2018)	TP's petition to quash third-party summons denied	Yes	IRS
<i>Speidell v. U.S.</i> , 119 A.F.T.R.2d (RIA) 2285 (D. Colo. 2017), <i>adopting</i> 119 A.F.T.R.2d (RIA) 2269 (D. Colo. 2017)	TP's petition to quash third-party summons denied; Lack of subject matter jurisdiction	No	IRS
<i>Swatley, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 5052 (W.D. Tenn. 2018)	Summons enforced	Yes	IRS
<i>Takase, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5831 (D. Haw. 2017), <i>adopting</i> 120 A.F.T.R.2d (RIA) 5830 (D. Haw. 2017)	Summons enforced	Yes	IRS
<i>Tallis, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1725 (N.D. Tex. 2018), <i>adopting</i> 121 A.F.T.R.2d (RIA) 1722 (N.D. Tex. 2018)	Summons enforced	Yes	IRS
<i>Tjugum, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1307 (W.D. Wis. 2018)	Summons enforced	Yes	IRS
<i>Tower v. U.S.</i> , 120 A.F.T.R.2d (RIA) 6038 (D. Haw. 2017), <i>appeal dismissed</i> , No. 17–17055 (9th Cir. Jan. 22, 2018), <i>adopting</i> 120 A.F.T.R.2d (RIA) 6036 (D. Haw. 2017)	Summons enforced; TP's petition to quash third-party summons denied	Yes	IRS
<i>Umoren v. U.S.</i> , 120 A.F.T.R.2d (RIA) 5296 (D. Nev. 2017), <i>adopting</i> 120 A.F.T.R.2d (RIA) 5132 (D. Nev. 2017)	TP's petition to quash third-party summons denied for lack of jurisdiction	No	IRS
<i>Urbanski, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5283 (N.D. Cal. 2017)	Summons enforced	Yes	IRS
<i>Urbanski, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5285 (N.D. Cal. 2017)	Summons enforced	Yes	IRS
<b>Business Taxpayers (Corporations, Partnerships, Trusts, and Sole Proprietorships – Schedules C, E, F)</b>			
<i>BMP Family Ltd. P'ship v. U.S.</i> , 120 A.F.T.R.2d (RIA) 5442 (S.D. Fla. 2017), <i>aff'd</i> , 2018 WL 5734353 (11th Cir., Nov. 1, 2018)	TP's petition to quash third-party summons denied	No	IRS
<i>Coinbase, Inc., U.S. v.</i> , 120 A.F.T.R.2d (RIA) 6671 (N.D. Cal. 2017)	Summons enforced in part and denied in part; some requested items were not relevant at that stage of the proceeding	No	Split
<i>Coinbase, Inc., U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5239 (N.D. Cal. 2017)	Motion to intervene by a “John Doe” granted, challenging the government's attempt to enforce the summons. Petition to enforce the IRS summons granted in part and denied in part. Government wasn't entitled to additional summoned information that was overly broad or not considered relevant at this stage of proceedings	No	Split
<i>Earth, Wind, and Solar, Inc., U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5328 (E.D. Cal. 2017), <i>adopting</i> 119 A.F.T.R.2d (RIA) 2335 (E.D. Cal. 2017)	Summons enforced	Yes	IRS
<i>Cooper v. U.S.</i> , 120 A.F.T.R.2d (RIA) 5326 (D. Neb. 2017), <i>appeal dismissed</i> , No. 17–3049 (8th Cir. Dec. 1, 2017)	Summons enforced; TP's petition to quash third-party summons denied	Yes	IRS
<i>Elks, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 6732 (M.D. Fla. 2017), <i>adopting</i> 120 A.F.T.R.2d (RIA) 6731 (M.D. Fla. 2017)	Summons enforced	Yes	IRS
<i>Fleisner v. U.S.</i> , 120 A.F.T.R.2d (RIA) 5696 (E.D. Wis. 2017)	Summons enforced; TP's petition to quash third-party summons denied	No	IRS
<i>Green Sol. Retail, Inc. v. U.S.</i> , 121 A.F.T.R.2d (RIA) 772 (D. Colo. 2018)	Summons enforced; TP's petition to quash third-party summons denied	No	IRS
<i>HP Distrib., LLC v. IRS</i> , 120 A.F.T.R.2d (RIA) 6152 (D. Kan. 2017)	TP's petition to quash third-party summons denied; Lack of subject matter jurisdiction	No	IRS

TABLE 3: Summons Enforcement Under IRC §§ 7602, 7604, and 7609

Case Citation	Issue(s)	Pro Se	Decision
<i>Lefkoff, Duncan, Grimes, McSwain &amp; Hass, PC v. U.S.</i> , 121 A.F.T.R.2d (RIA) 1729 (M.D. Fla. 2017), <i>adopting</i> 121 A.F.T.R.2d (RIA) 1725 (M.D. Fla. 2017)	TP's petition to quash third-party summons denied	No	IRS
<i>Maxcrest Ltd. v. U.S.</i> , 703 F. App'x 536 (9th Cir. 2017), <i>cert. denied</i> , 138 S. Ct. 2002 (May 14, 2018), <i>aff'g</i> 205 F. Supp.3d 1099 (N.D. Cal. 2016)	Summons enforced; TP's petition to quash third-party summons denied	No	IRS
<i>Med. Store Pharm., Inc. v. U.S.</i> , 2017 U.S. Dist. LEXIS 211807 (N.D. Tex. 2017)	TP's petition to quash third-party summons denied; Lack of subject matter jurisdiction	No	IRS
<i>Ngo v. U.S.</i> , 699 F. App'x 617 (9th Cir. 2017), <i>aff'g</i> 118 A.F.T.R.2d (RIA) 5453 (N.D. Cal. 2015)	Summons enforced; TP's petition to quash third-party summons denied	No	IRS
<i>Owensboro Dermatology Associates, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5119 (W.D. Ky. 2017)	Summons denied; TP properly invoked attorney-client privilege	No	TP
<i>Pardue, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5283 (M.D. Fla. 2017), <i>adopting</i> 120 A.F.T.R.2d (RIA) 5281 (M.D. Fla. 2017)	Summons enforced	Yes	IRS
<i>Presley &amp; Presley, P.A. v. U.S.</i> , 121 A.F.T.R.2d (RIA) 1526 (S.D. Fla. 2018), <i>appeal docketed</i> , No. 18-11847 (11th Cir., May 2, 2018)	Summons enforced; TP's petition to quash third-party summons denied	No	IRS
<i>Rifle Remedies, LLC v. U.S.</i> , 120 A.F.T.R.2d 6385 (D. Colo. 2017)	Summons enforced; TP's petition to quash third-party summons denied	No	IRS
<i>S. Crow Collateral Corp. v. U.S.</i> , 121 A.F.T.R.2d (RIA) 1809 (D. Idaho 2018), <i>adopting</i> 121 A.F.T.R.2d (RIA) 1802 (D. Idaho 2018), <i>appeal docketed</i> , No. 18-35497 (9th Cir. June 8, 2018)	Summons enforced; TP's petition to quash third-party summons denied	No	IRS
<i>Sanmina Co. and Subsidiaries, U.S. v.</i> , 707 F. App'x 865 (9th Cir. 2017), <i>vacating and remanding</i> , 115 A.F.T.R.2d (RIA) 1882 (N.D. Cal. 2015)	Court vacated district court order denying the summons and remanded the case for <i>in camera</i> review of documents due to privilege concerns	No	TP
<i>Sciarroni, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 6621 (N.D. Cal. 2017), <i>adopting</i> 120 A.F.T.R.2d (RIA) 6618 (N.D. Cal. 2017)	Summons enforced	Yes	IRS
<i>Zavala, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1121 (M.D. Fla. 2018), <i>adopting</i> 121 A.F.T.R.2d (RIA) 1119 (M.D. Fla. 2018)	Summons enforced	Yes	IRS

**TABLE 4: Gross Income Under IRC § 61 And Related Sections**

Case Citations	Issue(s)	Pro Se	Decision
<b>Individual Taxpayers (But Not Sole Proprietorships)</b>			
<i>Acone v. Comm'r</i> , T.C. Memo. 2017-162	Taxpayer H did not qualify for foreign earned income exclusion	No	IRS
<i>Bell v. U.S.</i> , 290 F. Supp. 3d 166 (D. Conn. 2017)	Settlement proceeds under IRC § 104(a)(2)	Yes	IRS
<i>Bon Viso v. Comm'r</i> , T.C. Memo. 2017-154	Unreported gambling income	Yes	IRS
<i>Bormet v. Comm'r</i> , T.C. Memo. 2017-201	Unreported retirement account distribution	No	IRS
<i>Bullock v. Comm'r</i> , T.C. Memo. 2017-219	Unreported cancellation of debt income	Yes	TP
<i>Butler v. Comm'r</i> , T.C. Summ. Op. 2017-82	Unreported Social Security income	Yes	IRS
<i>Cates v. Comm'r</i> , T.C. Memo. 2017-178, <i>appeal dismissed</i> , No. 18-10738 (11th Cir., Apr. 30, 2018)	Unreported retirement plan distribution	Yes	IRS
<i>Collins v. Comm'r</i> , T.C. Summ. Op. 2017-74	Settlement proceeds under IRC § 104(a)(2)	Yes	IRS
<i>Devine v. Comm'r</i> , T.C. Memo. 2017-111	Settlement proceeds under IRC § 104(a)(2)	No	IRS
<i>Dovzhenok v. Comm'r</i> , T.C. Summ. Op. 2017-86	Unreported income not excludable under tax treaty	Yes	IRS
<i>Dulanto v. Comm'r</i> , 703 F. App'x 527 (9th Cir. 2017), <i>aff'g</i> T.C. Memo. 2016-34, <i>reh'g en banc denied</i> , 2018 U.S. App. LEXIS 7136 (9th Cir., Mar. 21, 2018)	Settlement proceeds under IRC § 104(a)(2)	Yes	IRS
<i>Fiscalini v. Comm'r</i> , T.C. Memo. 2017-163	Unreported long-term capital gains	Yes	Split
<i>Fleming v. Comm'r</i> , T.C. Memo. 2017-120	Unreported wage income	Yes	IRS
<i>Frias v. Comm'r</i> , T.C. Memo. 2017-139	Unreported 401(k) distribution	No	IRS
<i>Glennon v. Comm'r</i> , T.C. Memo. 2018-4	Unreported cancellation of debt income	Yes	IRS
<i>Gowen v. Comm'r</i> , T.C. Summ. Op. 2017-57	Unreported deemed distribution from 401(k)	No	IRS
<i>Hamilton v. Comm'r</i> , T.C. Memo. 2018-62	Unreported cancellation of debt income	No	IRS
<i>Harris v. Comm'r</i> , T.C. Summ. Op. 2017-72	Unreported IRA distribution	Yes	IRS
<i>Henley v. Comm'r</i> , T.C. Summ. Op. 2018-22	Unreported gambling income	Yes	IRS
<i>Johnson v. Comm'r</i> , T.C. Summ. Op. 2017-71	<i>Per diem</i> payments includable in gross income	Yes	IRS
<i>Kirkpatrick v. Comm'r</i> , T.C. Memo. 2018-20	Unreported IRA distribution	Yes	IRS
<i>Kiselev v. Comm'r</i> , T.C. Summ. Op. 2018-2	Research grant excludable under tax treaty	Yes	TP
<i>Klubo-Gwiedzinska v. Comm'r</i> , T.C. Summ. Op. 2017-45	Payments not excludable under tax treaty	Yes	IRS
<i>Krantz v. Comm'r</i> , T.C. Memo. 2018-17, <i>appeal docketed</i> , No. 18-1621 (6th Cir., May 31, 2018)	Unreported wage income	Yes	IRS
<i>Linde v. Comm'r</i> , T.C. Memo. 2017-180	Foreign earned income not excludable	No	IRS
<i>Maciujec v. Comm'r</i> , T.C. Summ. Op. 2017-49	Settlement proceeds not excludable from income under IRC § 104(a)(2)	Yes	IRS
<i>Marks v. Comm'r</i> , T.C. Memo. 2018-49	Unreported IRA distribution	No	TP
<i>Michaels v. Comm'r</i> , T.C. Summ. Op. 2017-70	Unreported wage income	Yes	IRS
<i>Oliver v. Comm'r</i> , T.C. Summ. Op. 2018-16	Unreported annuity payments	Yes	IRS
<i>Omoloh v. Comm'r</i> , T.C. Summ. Op. 2017-64	Unreported IRA distribution	Yes	IRS
<i>Pei Fang Guo v. Comm'r</i> , 149 T.C. No. 14 (2017), <i>appeal dismissed</i> , 2018 WL 3216499 (D.C. Cir., May 11, 2018)	Unreported unemployment income not excludable under tax treaty	Yes	IRS
<i>Platts v. Comm'r</i> , T.C. Memo. 2018-31	Unreported wage income and constructive dividends	Yes	IRS
<i>Powers v. Comm'r</i> , T.C. Memo. 2017-179	Unreported ordinary income	No	TP

TABLE 4: Gross Income Under IRC § 61 And Related Sections

Case Citations	Issue(s)	Pro Se	Decision
<i>Rafizadeh v. Comm'r</i> , 150 T.C. No. 1 (2018)	Unreported foreign earned income	No	IRS
<i>Racjoomar v. Comm'r</i> , T.C. Memo. 2017-129	Settlement proceeds under IRC § 104(a)(2)	Yes	IRS
<i>Ramsay v. Comm'r</i> , T.C. Memo. 2017-223, <i>aff'd</i> , 732 F. App'x 307 (5th Cir. 2018)	Unreported imputed income	Yes	IRS
<i>Ritter v. Comm'r</i> , T.C. Memo. 2017-185	Unreported payment from a qualified settlement fund	Yes	IRS
<i>Robbins v. Comm'r</i> , T.C. Memo. 2017-247	Unreported Social Security income	Yes	IRS
<i>Sarvak v. Comm'r</i> , T.C. Memo. 2018-68	Unreported S Corporation distributions	No	IRS
<i>Shank v. Comm'r</i> , T.C. Memo. 2018-33	Unreported IRA distribution	No	Split
<i>Simonsen v. Comm'r</i> , 150 T.C. No. 8 (2018)	Unreported cancellation of debt income	Yes	TP
<i>Stepp v. Comm'r</i> , T.C. Memo. 2017-191	Settlement proceeds under IRC § 104(a)(2)	No	IRS
<i>Taylor v. Comm'r</i> , T.C. Memo. 2017-132, <i>aff'd in part and dismissed in part</i> , 731 F. App'x 239 (4th Cir. 2018)	Unreported retirement income	Yes	IRS
<i>Trimble v. Comm'r</i> , T.C. Memo. 2018-36	Unreported income	Yes	TP
<i>Voigt v. Comm'r</i> , T.C. Summ. Op. 2018-25	Tuition waiver not excludable from gross income under IRC § 117	Yes	IRS
<i>Welemin v. Comm'r</i> , T.C. Summ. Op. 2017-54	Unreported indirect income	Yes	IRS
<i>Yoklic v. Comm'r</i> , T.C. Memo. 2017-143	Unreported unemployment income	Yes	IRS
<i>Zhongxia Ye v. Comm'r</i> , T.C. Memo. 2017-216	Wages not excludable under tax treaty	No	IRS
<b>Business Taxpayers (Corporations, Partnerships, Trusts, and Sole Proprietorships – Schedules C, E, F)</b>			
<i>Avrahami v. Comm'r</i> , 149 T.C. No. 7 (2017)	Unreported dividends and interest	No	Split
<i>Azam v. Comm'r</i> , T.C. Memo. 2018-72	Unreported interest, ordinary dividends, state tax refund, capital gains, gross receipts, and pension distribution	Yes	Split
<i>Becker v. Comm'r</i> , T.C. Memo. 2018-69	Unreported business income	No	Split
<i>Byrum v. Comm'r</i> , T.C. Memo. 2018-9	Unreported misappropriated funds	No	IRS
<i>Canatella v. Comm'r</i> , T.C. Memo. 2017-124, <i>appeal dismissed</i> , 2018 U.S. App. LEXIS 19771 (9th Cir., July 17, 2018)	Unreported business income	Yes	Split
<i>Crestek v. Comm'r</i> , 149 T.C. No. 5 (2017)	Unreported untaxed investment of controlled foreign corporation	No	IRS
<i>DWA Holdings LLC v. U.S.</i> , 889 F.3d 1361 (Fed. Cir. 2018), <i>modified</i> , 889 F.3d 1361 (Fed. Cir., May 30, 2018)	Extraterritorial income exclusion under the American Jobs Creation Act	No	TP
<i>Dynamo Holdings Ltd. P'ship v. Comm'r</i> , T.C. Memo. 2018-61	Unreported loan income and constructive distribution income	No	Split
<i>Ellison v. Comm'r</i> , T.C. Memo. 2017-134, <i>appeal dismissed</i> , 2018 U.S. App. LEXIS 31958 (9th Cir., Nov. 8, 2018)	Unreported gross receipts	Yes	IRS
<i>Enis v. Comm'r</i> , T.C. Memo. 2017-222	Unreported S Corporation income	No	IRS
<i>Full-Circle Staffing LLC v. Comm'r</i> , T.C. Memo. 2018-66	Unreported partnership income	No	IRS
<i>Ginsburg v. U.S.</i> , 136 Fed. Cl. 1 (2018), <i>appeal docketed</i> , No. 18-1788 (Fed. Cir., Mar. 30, 2018)	State tax credit for building rehabilitation not excludable from income	No	IRS
<i>Grecian Magnesite Mining, Industr. &amp; Shipping Co. v. Comm'r</i> , 149 T.C. No. 3 (2017), <i>appeal docketed</i> , No. 17-1268 (D.C. Cir., Dec. 18, 2017)	Capital gain not U.S. source income	No	TP

TABLE 4: Gross Income Under IRC § 61 And Related Sections

Case Citations	Issue(s)	Pro Se	Decision
<i>Jagos v. Comm'r</i> , T.C. Memo. 2017-202, <i>aff'd</i> , 121 A.F.T.R.2d 2209 (6th Cir. 2018)	Unreported business income and other income	Yes	IRS
<i>Justine v. Comm'r</i> , T.C. Memo. 2017-198	Unreported gross receipts	Yes	IRS
<i>Knowles v. Comm'r</i> , T.C. Memo. 2017-152	Unreported income	No	IRS
<i>Kohn v. Comm'r</i> , T.C. Memo. 2017-159	Unreported distributive share of cancellation of debt income and capital gains	Yes	IRS
<i>Losantiville Country Club v. Comm'r</i> , T.C. Memo. 2017-158, <i>aff'd</i> , 2018 U.S. App. LEXIS 28935 (6th Cir., Oct. 15, 2018)	Unrelated business taxable income not offset by sales losses	No	IRS
<i>New Jersey Council of Teaching Hosps. v. Comm'r</i> , 149 T.C. No. 22 (2017)	Non excludable unrelated business taxable income	No	IRS
<i>Perkins v. Comm'r</i> , 150 T.C. No. 6 (2018)	Income not excludable under Seneca Nation treaties	No	IRS
<i>Povolny Grp., Inc. v. Comm'r</i> , T.C. Memo. 2018-37	Unreported capital contributions, constructive dividends, and wages	No	IRS
<i>Rader v. Comm'r</i> , T.C. Memo. 2017-209	Unreported self-employment income	Yes	IRS
<i>RJ Channels, Inc. v. Comm'r</i> , T.C. Memo. 2018-27	Unreported business income	No	IRS
<i>Rogers v. Comm'r</i> , T.C. Memo. 2018-53	Unreported trustee fees and transfer of property to wholly owned S Corporation	No (TP husband is attorney POA)	IRS
<i>Rushing v. Comm'r</i> , T.C. Memo. 2018-23	Unreported rental income and gross receipts	No	IRS
<i>Siegel v. Comm'r</i> , T.C. Summ. Op. 2017-53	Unreported interest and self-employment income	Yes	IRS
<i>SIH Partner LLLP v. Comm'r</i> , 150 T.C. No. 3 (2018), <i>appeal docketed</i> , No. 18-1862 (3d Cir., Apr. 23, 2018)	Unreported controlled foreign corporation income	No	IRS
<i>Sun v. Comm'r</i> , 880 F.3d 173 (5th Cir. 2018)	Diverted trust income includable in gross income	No	IRS
<i>Triumph Mixed Use Inv. III, LLC, Fox Ridge Inv., LLC, Tax Matters Partner v. Comm'r</i> , T.C. Memo. 2018-65	Unreported gross receipts and net earnings from self-employment	No	Split
<i>Uniquist Del. LLC v. U.S.</i> , 294 F. Supp.3d 107 (W.D.N.Y. 2018)	Unreported state grant income	No	IRS
<i>W. Prop. Restoration, Inc. v. Comm'r</i> , T.C. Memo. 2017-190	Unreported dividend income	No	IRS

**TABLE 5: Appeals From Collection Due Process (CDP) Hearings Under IRC §§ 6320 and 6330**

Case Citation	Lien/Levy	Issue(s)	Pro Se	Decision
<b>Individual Taxpayers (But Not Sole Proprietorships)</b>				
<i>Alamo v. Comm'r</i> , T.C. Memo. 2017-215, appeal docketed, No. 18-60221 (5th Cir. Mar. 29, 2018)	Lien	TP precluded from challenging the underlying tax liabilities; notices of deficiency were properly mailed; proposed collection action sustained; no abuse of discretion	Yes	IRS
<i>Ashmore v. Comm'r</i> , T.C. Memo. 2017-233	Levy	No abuse of discretion; proposed collection action sustained	Yes	IRS
<i>Beam v. Comm'r</i> , T.C. Memo. 2017-200	Lien/Levy	No abuse of discretion; proposed collection actions sustained	Yes	IRS
<i>Berkun v. Comm'r</i> , 890 F.3d 1260 (11th Cir. 2018), <i>aff'g</i> No. 14-21816 (T.C. Feb. 3, 2015)	Levy	TP's petition appealing the Tax Court's dismissal of petition for lack of jurisdiction denied; notices were properly mailed to the last known address	No	IRS
<i>Bero v. Comm'r</i> , T.C. Memo. 2017-235	Lien/Levy	Refinancing of nontax debt not sufficient to justify remand and reconsideration of TPs' ability to pay. No abuse of discretion; proposed collection actions sustained	No	IRS
<i>Best v. Comm'r</i> , 702 F. App'x 615 (9th Cir. 2017), <i>aff'g</i> T.C. Memo. 2014-72 and T.C. Memo. 2014-194, <i>cert. denied</i> , 138 S. Ct. 2691 (2018)	Levy	Lower court affirmed; no abuse of discretion; proposed collection actions sustained; TP precluded from challenging the underlying tax liability	No	IRS
<i>Bruce v. Comm'r</i> , T.C. Memo. 2017-172	Levy	TP precluded from challenging the underlying tax liabilities; notices of deficiency were properly mailed; proposed collection action sustained, no abuse of discretion	Yes	IRS
<i>Bullock v. Comm'r</i> , T.C. Memo. 2017-161	Levy	TPs (MFJ) rejected IRS's proposed installment plan and failed to provide grounds for rejection or make counteroffer; no abuse of discretion	Yes	IRS
<i>Butler v. Comm'r</i> , T.C. Summ. Op. 2017-82	Levy	Rejecting OIC where no Form 656 or supporting financial documentation filed was not abuse of discretion; proposed collection actions sustained	Yes	IRS
<i>Chapman v. Comm'r</i> , 715 F. App'x 885 (11th Cir. 2017), <i>aff'g</i> Nos. 15-30014 (T.C. June 7, 2016) and 15-30031 (T.C. May 27, 2016) <i>cert. denied</i> , 138 S. Ct. 1710 (2018)	Levy/Lien	Tax Court ruling affirmed; COA refused to consider new arguments raised on appeal	Yes	IRS
<i>Copper v. Comm'r</i> , T.C. Memo. 2017-231	Levy	No abuse of discretion; proposed collection actions sustained; TP failed to submit documentation supporting proposed installment agreement	Yes	IRS
<i>Cunningham v. Comm'r</i> , 716 F. App'x 182 (4th Cir. 2018), <i>aff'g</i> No. 16-014090 (T.C. Dec. 7, 2016)	Levy	Tax Court dismissal of petition to review CDP determination affirmed; Petition for Tax Court review of CDP hearing was filed one day after statutory deadline and was dismissed because court lacked jurisdiction	No	IRS
<i>Day v. Comm'r</i> , 692 F. App'x 897 (9th Cir. 2017), <i>aff'g</i> T.C. Memo. 2014-215	Levy	No abuse of discretion; proposed collection actions sustained	Yes	IRS
<i>Duggan v. Comm'r</i> , 879 F.3d 1029 (9th Cir. 2018), <i>aff'g</i> No. 15-4100 (T.C. June 26, 2015)	Levy	Tax Court's dismissal of petition to review CDP determination affirmed; TP miscounted day after notice date as day zero when calculating filing deadline; filing deadline is jurisdictional	Yes	IRS
<i>Duncan, Estate of, v. Comm'r</i> , 890 F.3d 192 (5th Cir. 2018), <i>aff'g</i> T.C. Memo. 2016-204	Levy	Tax Court's ruling affirmed; no abuse of discretion; proposed collection actions sustained	No	IRS

TABLE 5: Appeals From Collection Due Process (CDP) Hearings Under IRC §§ 6320 and 6330

Case Citation	Lien/Levy	Issue(s)	Pro Se	Decision
<i>Faulk v. Comm'r</i> , T.C. Summ. Op. 2017-92	Levy	Tax debt was not discharged in bankruptcy; no abuse of discretion; proposed collection actions sustained	Yes	IRS
<i>Feldman v. Comm'r</i> , T.C. Memo. 2017-148, appeal dismissed, No. 18-1114 (3d Cir. June 5, 2018)	Lien	No abuse of discretion; proposed collection actions sustained	Yes	IRS
<i>Fine v. Comm'r</i> , 715 F. App'x 804 (9th Cir. 2018), aff'g T.C. Memo. 2016-217, reh'g and reh'g en banc denied, No. 17-71042 (9th Cir. Sept. 12, 2018)	Levy/Lien	Tax Court decision affirmed; denying requests for collection alternatives was not abuse of discretion since requested information was not provided; proposed collection action sustained	Yes	IRS
<i>Fleming v. Comm'r</i> , T.C. Memo. 2017-155	Levy	No abuse of discretion; proposed collection actions sustained	Yes	IRS
<i>Fujita v. Comm'r</i> , 699 F. App'x 725 (9th Cir. 2017), aff'g No. 15-10100 (T.C. Oct. 7, 2016), cert. denied 138 S. Ct. 2006 (2018)	Levy/Lien	Tax Court decision affirmed; no abuse of discretion and no violation of due process; proposed collection actions sustained	Yes	IRS
<i>Hawver v. Comm'r</i> , T.C. Memo. 2017-244	Levy/Lien	Court had jurisdiction to review underlying liability; no abuse of discretion in sustaining collection action.	No	IRS
<i>Jennette v. Comm'r</i> , T.C. Memo. 2018-47, appeal docketed No. 18-1861 (3d Cir. Apr. 19, 2018)	Levy	No abuse of discretion; proposed collection actions sustained	Yes	IRS
<i>Mack v. Comm'r</i> , T.C. Memo. 2018-54	Lien	No abuse of discretion; IRS rejected TP's proposed OIC amount because it was below RCP, based on local standards; TP bears the burden of providing sufficient information to justify a deviation from local standards; proposed collection actions sustained	Yes	IRS
<i>McCree v. Comm'r</i> , T.C. Memo. 2017-145	Levy	IRS improperly denied TP opportunity to challenge the underlying tax liabilities; TP properly raised issue of tax liability during CDP hearing thus de novo review granted; granted TP's motion for full trial	Yes	Split
<i>McNeill v. Comm'r</i> , 148 T.C. No. 23 (2017)	Lien/Levy	TP contested accuracy-related penalty through CDP hearing and Tax Court has jurisdiction to review	No	Split
<i>McNeill v. Comm'r</i> , T.C. Memo. 2017-206	Lien/Levy	IRS error in calculating assessment did not make imposition of 6662 penalty abuse of discretion; lien and levy actions sustained	No	IRS
<i>Metzger v. Comm'r</i> , T.C. Summ. Op. 2017-47	Levy	TP failed to supply required forms and supporting financial information; was not in compliance with his current tax obligations; no abuse of discretion in not affording face-to-face hearing	Yes	IRS
<i>Moreno v. Comm'r</i> , T.C. Summ. Op. 2018-19	Levy	TP failed to supply required forms and supporting financial information; was not in compliance with his current tax obligations; no abuse of discretion; collection action sustained	Yes	IRS
<i>Moriarty v. Comm'r</i> , 2018 WL 4924349 (6th Cir. Sept. 19, 2018), aff'g T.C. Memo. 2017-204, petition for reh'g filed, No. 18-1077 (6th Cir. Oct. 30, 2018)	Lien/Levy	TPs (MFJ) failed to submit documentation to demonstrate they qualified for lien subordination or that they qualified for the limited exception for including children's tuition expenses as allowable monthly living expenses for purposes of determining their ability to pay under IRM pt. 5.15.1.7(1); no abuse of discretion; collection action sustained	Yes	IRS

TABLE 5: Appeals From Collection Due Process (CDP) Hearings Under IRC §§ 6320 and 6330

Case Citation	Lien/Levy	Issue(s)	Pro Se	Decision
<i>Muir v. Comm'r</i> , T.C. Memo. 2017-224, appeal docketed No. 18-60336 (5th Cir. May 4, 2018)	Levy	No abuse of discretion; proposed collection actions sustained	Yes	IRS
<i>Potts v. Comm'r</i> , T.C. Memo. 2017-228, appeal docketed No. 17-73472 (9th Cir. Dec. 28, 2017)	Levy	TPs were prohibited from contesting underlying liability after POA consented to assessment; no abuse of discretion; proposed collection action sustained	No	IRS
<i>Pritchard v. Comm'r</i> , T.C. Memo. 2017-136	Levy	TP's withdrawal of IRA savings to pay tax debt was not a valid exception to the IRC § 72(t) ten percent penalty	No	IRS
<i>Robinson v. Comm'r</i> , T.C. Memo. 2017-207	Levy	After remand to Appeals, TP failed to provide documentation supporting challenge to underlying liability at the hearing; no abuse of discretion in pursuing collection action	Yes	IRS
<i>Roudakov v. Comm'r</i> , T.C. Memo. 2017-121	Lien	TP failed to provide financial or other information to support his assertion that the NFTL's filing could cause him to lose his job or otherwise interfere with his future gainful employment; no abuse of discretion; proposed collection actions sustained	Yes	IRS
<i>Rozday v. Comm'r</i> , 703 F. App'x 138 (3d Cir. 2017) <i>aff'g</i> No. 15-28318 (T.C. Sept. 19, 2016)	Lien	Tax Court's ruling affirmed; TP failed to challenge IRS determination; proposed collection action sustained	Yes	IRS
<i>Shum v. Comm'r</i> , T.C. Summ. Op. 2017-40	Levy	The IRS's determination to proceed with the proposed levy action balanced the need for efficient collection against taxpayer's concern that collection be no more intrusive than necessary; no abuse of discretion	Yes	IRS
<i>Sykes v. Comm'r</i> , 719 F. App'x 726 (9th Cir. 2018) <i>aff'g</i> No. 10386-11 (T.C. Sept. 16, 2013)	Levy	Tax Court's ruling affirmed; TP failed to raise any permissible issues or defenses at the CDP hearing; no abuse of discretion	Yes	IRS
<i>Sykes v. Comm'r</i> , 719 F. App'x 728 (9th Cir. 2018) <i>aff'g</i> No. 18787-12 (T.C. Nov. 22, 2013), <i>reh'g and reh'g en banc denied</i> , No. 14-70446 (9th Cir. July 10, 2018)	Levy	Tax Court's ruling affirmed; TP failed to raise any permissible issues or defenses at the CDP hearing; no abuse of discretion	Yes	IRS
<i>Talbot v. Comm'r</i> , 708 F. App'x 421 (9th Cir. 2017) <i>aff'g</i> T.C. Memo. 2016-191	Levy	Tax Court's ruling affirmed; Tax Court properly determined that mailing notices of deficiency to TP's last known address was not abuse of discretion	No	IRS
<i>Tenholder, In re</i> , 120 A.F.T.R.2d (RIA) 6916 (S. D. Ill. 2017)	Levy	TP's pending CDP hearing effectively tolled IRS's three-year collection period	No	IRS
<i>Vigon v. Comm'r</i> , 149 T.C. No. 4 (2017)	Lien	IRS abated the penalties, released the lien, and filed a motion to dismiss TP's petition on grounds of mootness; but Court denied IRS's motion because IRS did not concede TP's liability for the penalties and reserved the right to reassess later	Yes	TP
<i>Walker v. Comm'r</i> , T.C. Memo. 2018-22	Lien/Levy	TP's motion for summary judgment denied, IRS motion for summary judgment granted in part; proposed collection action sustained for tax liabilities for 2003 through 2006; IRS properly denied face-to-face hearing and opportunity to audio record any telephone hearing; no abuse of discretion in not considering collection alternatives; remanded to Appeals for supplemental determinations clarifying the record as to the grounds on which Appeals relied in precluding TP from challenging his 2007 and 2009 tax liabilities	Yes	Split

TABLE 5: Appeals From Collection Due Process (CDP) Hearings Under IRC §§ 6320 and 6330

Case Citation	Lien/Levy	Issue(s)	Pro Se	Decision
<i>Weber v. Comm'r</i> , T.C. Memo. 2017-225	Lien	Summary judgment in favor of IRS granted and proposed collection action affirmed; TP failed to supply required forms and supporting financial information; was not in compliance with his current tax obligations; no abuse of discretion	Yes	IRS
<i>Weiss v. Comm'r</i> , 121 A.F.T.R.2d 1853 (D.C. Cir. 2018) <i>aff'g</i> 147 T.C. 179 (2016)	Levy	Tax Court's ruling affirmed; TP argued that statute of limitations for collections had expired, however TP made timely CDP hearing request, which tolled the limitations period for collection	No	IRS
<i>Whitaker v. Comm'r</i> , 698 F. App'x 366 (9th Cir. 2017), <i>aff'g</i> No. 18639-15 (T.C. Aug. 1, 2016)	Levy	Tax Court decision affirmed; Tax Court properly granted summary judgment and properly determined that the IRS did not abuse discretion in rejecting the TPs' request for an installment agreement	No	IRS
<i>Whitaker v. Comm'r</i> , T.C. Memo. 2017-192	Levy	No abuse of discretion in sustaining proposed levy; all requirements of applicable law and administrative procedure were followed; TP raised no relevant issues and proposed no collection alternative	Yes	IRS
<i>Williams v. Comm'r</i> , 724 F. App'x 920 (11th Cir. 2018), <i>reh'g denied</i> (July 24, 2018), <i>aff'g</i> T.C. Memo. 2017-58	Levy	TP did not rebut IRS determination of tax liability; TP's argument that there was no personal or subject matter jurisdiction and that he is not subject to tax was deemed frivolous; lower court action sustained	Yes	IRS
<i>Williams v. Comm'r</i> , T.C. Memo. 2018-50, <i>appeal docketed</i> No. 18-60536 (5th Cir. Aug. 1, 2018)	Levy/Lien	No abuse of discretion in rejecting collection alternatives where TP offered none, failed to provide financial information, and was not current with filing and payment obligations	Yes	IRS
<b>Business Taxpayers (Corporations, Partnerships, Trusts, and Sole Proprietorships – Schedules C, E, F)</b>				
<i>Argosy Techs., LLC v. Comm'r</i> , T.C. Memo. 2018-35, <i>appeal docketed</i> No. 18-2027 (2d Cir. July 1, 2018)	Levy	No abuse of discretion; TP did not request collection alternatives; proposed collection action sustained	No	IRS
<i>Blackburn v. Comm'r</i> , 150 T.C. No. 9	Levy	No abuse of discretion; proposed collection action sustained	No	IRS
<i>Credex, Inc. v. Comm'r</i> , T.C. Memo. 2017-241	Levy	Appeals Officer abused his discretion and reneged on IRS's assurances to the Court of Appeals by not taking into account large amounts of stipulated credits; failed to consider relevant issues relating to the unpaid tax; inappropriately balanced IRS's need for the efficient collection of taxes with how the levy's intrusiveness could harm TP; and contravened applicable law and administrative procedure	No	TP
<i>Creditguard of Am., Inc. v. Comm'r</i> , 149 T.C. No. 17	Lien	Settlement Officer did not abuse discretion by assessing interest arising from retroactive revocation of tax-exempt status; NFTL properly filed	No	IRS
<i>Dykstra v. Comm'r</i> , T.C. Memo. 2017-156	Lien/Levy	No abuse of discretion in rejection of OIC; proposed collection action sustained	Yes	IRS
<i>Emery Celli Cuti Brinckerhoff &amp; Abady, P.C. v. Comm'r</i> , T.C. Memo. 2018-55	Levy	Settlement officer abused his discretion in failing to consider TP's equitable recoupment claim and the documentation it provided to support that claim; levy action sustained only to the extent that TP's underpayment of employment tax exceeds TP's overpayment of employment tax	No	TP
<i>Fagan v. Comm'r</i> , T.C. Summ. Op. 2017-61	Levy	IRS misapplied payments; continuing to pursue collection was an abuse of discretion	Yes	TP

TABLE 5: Appeals From Collection Due Process (CDP) Hearings Under IRC §§ 6320 and 6330

Case Citation	Lien/Levy	Issue(s)	Pro Se	Decision
<i>Garavaglia v. Comm'r</i> , T.C. Memo. 2017-131	Levy	IRS refusal to abate interest was not an abuse of discretion; proposed collection actions sustained	No	IRS
<i>Gardner v. Comm'r</i> , 704 F. App'x 720 (9th Cir. 2017), <i>aff'g</i> 145 T.C. 161 (2015)	Lien/Levy	Tax Court's ruling affirmed; TPs argued that they never had the opportunity to challenge IRS but court ruled they had opportunity at hearing; TPs challenged numerous penalties for promoting a tax shelter; Tax Court's factual findings on the amount of the penalty supported by the record and not clearly erroneous; penalty sustained	Yes	IRS
<i>Gardner v. Comm'r</i> , T.C. Memo. 2017-107	Levy	TP did not request a collection alternative and did not supply financial information; IRS did not abuse discretion; settlement officer properly sustained the proposed levy	Yes	IRS
<i>Heintz v. Comm'r</i> , 690 F. App'x 569 (9th Cir. 2017), <i>reh'g denied</i> (9th Cir. Dec. 28, 2017), <i>aff'g</i> No. 11-2769 (T.C. Mar. 14, 2012)	Levy	Tax Court's ruling affirmed; TP did not raise defenses at CDP hearing; TP precluded from challenging the underlying tax liabilities because of failure to raise it at prior opportunity to dispute issue	No	IRS
<i>Jarrett v. Comm'r</i> , T.C. Memo. 2018-73	Lien/Levy	No abuse of discretion; proposed collection action sustained	No	IRS
<i>Jivani v. Comm'r</i> , T.C. Summ. Op. 2018-20	Lien	Denying TP's request to apply remittance against tax liability and not abuse of discretion; proposed collection action sustained	Yes	IRS
<i>Jones v. Comm'r</i> , T.C. Summ. Op. 2017-75	Levy	TP did not avail himself of two opportunities for a CDP hearing; no abuse of discretion; proposed collection action sustained	Yes	IRS
<i>Leon-Guerrero v. Comm'r</i> , T.C. Memo. 2017-232	Levy	No abuse of discretion; TP did not request collection alternatives; proposed collection action sustained	Yes	IRS
<i>Mohamed v. Comm'r</i> , T.C. Summ. Op. 2017-69	Levy	TP fully participated in appeals hearing; he could no longer contest underlying liability	Yes	IRS
<i>Pantano Baptist Church v. Comm'r</i> , T.C. Summ. Op. 2018-3	Lien/Levy	Church precluded from challenging underlying tax liability because it failed to raise penalty issue in prior opportunity before the IRS Appeals; no abuse of discretion; proposed collection action sustained	Yes	IRS
<i>Preston v. Comm'r</i> , T.C. Summ. Op. 2018-4	Levy	IRS's refusal to accept an OIC and proposed installment agreement was not an abuse of discretion; TP did not present evidence to justify a departure from local or national standards; TP failed to show that levy would cause undue hardship	Yes	IRS
<i>Scanlon v. Comm'r</i> , T.C. Memo. 2018-51	Lien/Levy	Summary judgment granted against TP; Appeals officer's reliance, in part, on the TP's failure to pay current taxes or include them in the TP's proposed installment agreement as grounds for rejecting it was not an abuse of discretion; TP was barred from arguing intrusiveness of collection method because did not raise at CDP hearing	No	IRS
<i>Seminole Nursing Home, Inc. v. Comm'r</i> , T.C. Memo. 2017-102	Levy	Summary judgment against TP grant in part; corporations may not claim economic hardship as a justification for collection alternative; remanded the remainder of this case to the IRS Appeals Office for the limited purpose of reconsidering the balancing test	No	Split
<i>Snow v. Comm'r</i> , T.C. Summ. Op. 2017-38	Levy	No abuse of discretion in denying the TP's request for an installment agreement because TP was not in compliance with his current tax liabilities as of the date of the CDP hearing; Settlement officer properly balanced the government's need for the efficient collection of taxes with the legitimate concern of the taxpayer that the collection action be no more intrusive than necessary	Yes	IRS

TABLE 5: Appeals From Collection Due Process (CDP) Hearings Under IRC §§ 6320 and 6330

Case Citation	Lien/Levy	Issue(s)	Pro Se	Decision
<i>Solny v. Comm'r</i> , T.C. Memo. 2018-71	Lien	TP sought a collection alternative in the form of an OIC or an installment agreement but did not supply any of the required forms or necessary financial information; no abuse of discretion in sustaining the collection actions; summary judgment against TP granted and proposed collection action affirmed	No	IRS
<i>Vest v. Comm'r</i> , T.C. Summ. Op. 2018-18	Levy	Tax Court did not have jurisdiction to review Treasury offset of overpayment of TP's wholly-owned corporation, because corporation was not a party to the action; IRS Appeals Officer acted within discretion in sustaining levy	Yes	IRS
<i>Woodley v. Comm'r</i> , T.C. Memo. 2017-242	Lien/Levy	No abuse of discretion; TP declined the conditional offer of an installment agreement and proposed no other collection alternative; TP was not compliant with ongoing tax obligations; proposed collection action sustained	No	IRS
<i>W. Zintl Constr., Inc. v. Comm'r</i> , T.C. Memo. 2017-119	Lien/Levy	TP proved settlement officer's calculation of reasonable collection potential was unreasonable; IRS settlement officer abused his discretion in rejecting OIC; remanded to Appeals to redetermine TP's reasonable collection potential	No	TP
<i>Xibitmax, LLC v. Comm'r</i> , T.C. Memo. 2017-133	Lien/Levy	TP challenged underlying tax liability, failed to prove reasonable cause for failure to pay; proposed collection action sustained	No	IRS

**TABLE 6: Failure to File Penalty Under IRC § 6651(a)(1), Failure to Pay an Amount Shown as Tax on Return Under IRC § 6651(a)(2) and Failure to Pay Estimated Tax Penalty Under IRC § 6654**

Case Citations	Issue(s)	Pro Se	Decision
<b>Individual Taxpayers (But Not Sole Proprietorships)</b>			
<i>Azam v. Comm'r</i> , T.C. Memo. 2018-72	6651(a)(1), (2) - No reasonable cause	Yes	IRS
<i>Barrett v. Comm'r</i> , T.C. Memo. 2017-195	6651(a)(1), (2) - Vague reference to illness does not establish reasonable cause 6654 - No exception applies	No	IRS
<i>Blair v. Comm'r</i> , T.C. Memo. 2017-153	6651(a)(1), (2) - Taxpayer did not offer reasonable cause argument 6654 - No exceptions apply	Yes	IRS
<i>Bonaparte v. Comm'r</i> , T.C. Memo. 2017-193, appeal docketed No. 18-2264 (3rd Cir. June 8, 2018)	6651(a)(1) - No reasonable cause	Yes	IRS
<i>Christen v. Comm'r</i> , 698 F. App'x 450 (9th Cir. 2017), <i>aff'g</i> No. 16147-14 (T.C. 2017)	6651(a)(1) - Taxpayer offered no reasonable cause argument	Yes	IRS
<i>Duket v. Comm'r</i> , T.C. Summ. Op. 2017-84	6651(a)(1) - Blindness does not establish reasonable cause	No	IRS
<i>Dykstra v. Comm'r</i> , T.C. Memo. 2017-156	6651(a)(1), (2) - Financial crisis's impact and work stress did not establish reasonable cause 6654 - No exceptions apply	Yes	IRS
<i>Enis v. Comm'r</i> , T.C. Memo. 2017-222	6651(a)(1) - Relying on agent who was ill did not establish reasonable cause	No	IRS
<i>Fiscalini v. Comm'r</i> , T.C. Memo. 2017-163	6651(a)(1) - Taxpayer's inability to pay does not establish reasonable cause	Yes	IRS
<i>Fleming v. Comm'r</i> , T.C. Memo. 2017-120	6651(a)(1), (2) - Taxpayer offered no reasonable cause argument	Yes	IRS
<i>Hamilton v. Comm'r</i> , T.C. Memo. 2018-62	6651(a)(1) - No reasonable cause	No	IRS
<i>Haynes v. U.S.</i> , 119 A.F.T.R.2d (RIA) 2202 (W.D. Tex. 2017), <i>vacated and remanded</i> , No. 17-50816 (5th Cir. Jan. 29, 2019)	6651(a)(1) - Alleged efilng software malfunction did not establish reasonable cause	No	IRS
<i>Jabari v. Comm'r</i> , T.C. Memo. 2017-238	6651(a)(1) - No reasonable cause	Yes	IRS
<i>Jivani v. Comm'r</i> , T.C. Summ. Op. 2018-20	6651(a)(1), (2) - Taxpayer unable to substantiate when she learned of accountant's death; no reasonable cause 6654 - No exceptions apply	Yes	IRS
<i>Kraus, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1323 (W.D. Wa. 2018)	6651(a)(1), (2) - Taxpayer offered no reasonable cause arguments 6654 - No exceptions apply	Yes	IRS
<i>Laidlaw v. Comm'r</i> , T.C. Memo. 2017-167	6651(a)(1) - Taxpayers offered no reasonable cause argument; failed to timely file extension	No	IRS
<i>Mazzei v. Comm'r</i> , 2018 WL 1168766 (T.C. Mar. 5, 2018)	6651(a)(1), (2) - Taxpayer's reliance on tax professional who reported but did not promote transaction at issue established reasonable cause	No	TP
<i>Palmer, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1551 (E.D. Va. 2018), <i>adopting</i> 121 A.F.T.R.2d (RIA) 1544 (E.D. Va. 2018)	6651(a)(1) - Taxpayer offered no reasonable cause argument	Yes	IRS
<i>Parekh v. Comm'r</i> , T.C. Memo. 2017-227	6651(a)(1) - No reasonable cause	No	IRS
<i>Perkins v. Comm'r</i> , 2018 WL 1146343 (T.C. Mar. 1, 2018)	6651(a)(1) - Taxpayer offered no reasonable cause argument	No	IRS

TABLE 6: Failure to File Penalty Under IRC § 6651(a)(1), Failure to Pay an Amount Shown as Tax on Return Under IRC § 6651(a)(2) and Failure to Pay Estimated Tax Penalty Under IRC § 6654

Case Citations	Issue(s)	Pro Se	Decision
<i>Plato v. Comm'r</i> , T.C. Memo. 2018-7	6651(a)(1) - No reasonable cause 6651(a)(2) - IRS did not meet burden of production 6654 - No exceptions apply, but IRS did not meet its burden of production	Yes	Split
<i>Platts v. Comm'r</i> , T.C. Memo. 2018-31	6651(a)(1) - Taxpayer offered no reasonable cause argument	Yes	IRS
<i>Pryde v. U.S.</i> , 120 A.F.T.R.2d (RIA) 6843 (Fed. Cl. 2017)	6651(a)(1) - Taxpayer offered no reasonable cause argument	No	IRS
<i>Rader v. Comm'r</i> , T.C. Memo. 2017-209	6651(a)(1), (2) - Taxpayer offered no reasonable cause argument 6654 - Taxpayer did not argue any statutory exceptions apply	Yes	IRS
<i>Siegel v. Comm'r</i> , T.C. Summ. Op. 2017-53	6651(a)(1), (2) - No reasonable cause 6654 - No exceptions apply	Yes	IRS
<i>Spottiswood v. U.S.</i> , 121 A.F.T.R.2d (RIA) 1595 (N.D. Cal. 2018), <i>appeal docketed</i> , No. 18-16103 (9th Cir. June 14, 2018)	6651(a)(1), (2) - Taxpayer's failure to check e-filing status on tax preparation software did not establish reasonable cause	No	IRS
<i>Topsnik v. Comm'r</i> , 2017 U.S. App. LEXIS 22847 (D.C. Cir. 2017), <i>aff'g</i> 143 T.C. 240 (2014)	6651(a)(1), (2) - No reasonable cause 6654 - No exceptions apply	No	IRS
<i>Whittington v. Comm'r</i> , 698 F. App'x 515 (9th Cir. 2017), <i>aff'g</i> T.C. Memo. 2015-152	6651(a)(1), (2) - No reasonable cause 6654 - No exceptions apply	Yes	IRS
<b>Business Taxpayers (Corporations, Partnerships, Trusts, and Sole Proprietorships – Schedules C, E, F)</b>			
<i>Barker v. Comm'r</i> , T.C. Memo. 2018-67	6651(a)(1) - Victim of identity theft did not establish reasonable cause	No	IRS
<i>Byrum v. Comm'r</i> , T.C. Memo. 2018-9	6651(a)(1) - No reasonable cause	No	IRS
<i>Dynamo Holdings Ltd. P'ship v. Comm'r</i> , T.C. Memo. 2018-61	6651(a)(1) - Good faith belief that TP is not required to file return did not establish reasonable cause	No	IRS
<i>Emery Celli Cuti Brinckerhoff &amp; Abady, P.C. v. Comm'r</i> , T.C. Memo. 2018-55	6651(a)(1), (2) - Taxpayer's timely filing of employment tax return under an incorrect EIN due to vendor error established reasonable cause	No	TP
<i>Geneser v. Comm'r</i> , T.C. Memo. 2017-110	6651(a)(1), (2) - Taxpayer diagnosed with cancer but who was never hospitalized did not establish reasonable cause 6654 - No exceptions apply	No	IRS
<i>Grecian Magnesite Mining, Indus. &amp; Shipping Co. v. Comm'r</i> , 2017 WL 2992452 (T.C. July 13, 2017), <i>appeal docketed</i> , No. 17-1268 (D.C. Cir. Dec. 18, 2017).	6651(a)(1), (2) - Foreign taxpayer with little familiarity of US tax law established reasonable cause by relying on adviser to hire US tax preparer	No	TP
<i>Hall Family Trust Dated June 8, 2001, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 641 (S.D. Cal. 2018)	6651(a)(2) - Taxpayer offered no reasonable cause argument	No	IRS
<i>Keefe v. Comm'r</i> , T.C. Memo. 2018-28, <i>appeal docketed</i> No. 18-2357 (2d Cir. Aug. 10, 2018)	6651(a)(1) - Taxpayer offered no reasonable cause argument	No	IRS
<i>Kenny, U.S. v.</i> , 2018 WL 2723733, (N.D. Ohio May 30, 2018)	6651(a)(1), (2) - Taxpayer offered no reasonable cause argument 6654 - No exceptions apply	No	IRS
<i>Knowles v. Comm'r</i> , T.C. Memo. 2017-152	6651(a)(1) - Taxpayer's misrepresentation of date of father's death did not establish reasonable cause	No	IRS
<i>Mileham v. Comm'r</i> , T.C. Memo. 2017-168	6651(a)(1) - No reasonable cause	No	IRS
<i>Mustang Drilling Co., LLC v. U.S.</i> , 121 A.F.T.R.2d 765 (S.D. Miss. 2018)	6651(a)(2) - Taxpayer's inability to substantiate financial hardship did not establish reasonable cause	No	IRS

TABLE 6: Failure to File Penalty Under IRC § 6651(a)(1), Failure to Pay an Amount Shown as Tax on Return Under IRC § 6651(a)(2) and Failure to Pay Estimated Tax Penalty Under IRC § 6654

Case Citations	Issue(s)	Pro Se	Decision
<i>New Capital Fire, Inc. v. Comm'r</i> , T.C.M. (RIA) 2017-177	6651(a)(1), (2) - Short year return filed by taxpayer satisfied definition of return; statute of limitations barred IRS from assessing deficiency and penalties	No	TP
<i>Pizza Pro Equipment Leasing, Inc. v. Comm'r</i> , 719 F. App'x 540 (8th Cir. 2018), <i>aff'g</i> 147 T.C. 394 (2016)	6651(a)(1), (2) - No reasonable cause	No	IRS
<i>Riggins v. Comm'r</i> , T.C. Memo. 2017-106	6651(a)(1), (2) - No reasonable cause	Yes	IRS
<i>Rogers v. Comm'r</i> , T.C. Memo. 2018-53	6651(a)(1) - Taxpayer's extended hospitalization and illness established reasonable cause	Yes	TP
<i>Venuto v. Comm'r</i> , T.C. Memo. 2017-123	6651(a)(1), (2) - Taxpayer offered no reasonable cause argument	Yes	IRS
<i>Wages v. Comm'r</i> , T.C. Memo. 2017-103	6651(a)(1) - No reasonable cause; Taxpayer could not substantiate that he suffered a stroke or that former associate purloined records	No	IRS
<i>Xibitmax, LLC v. Comm'r</i> , T.C.M. (RIA) 2017-133	6651(a)(1), (2) - Assigning tax filing obligations to unqualified part-time employee did not establish reasonable cause	No	IRS

**TABLE 7: Civil Actions to Enforce Federal Tax Liens or to Subject Property to Payment of Tax Under IRC § 7403**

Case Citation	Issue(s)	Pro Se	Decision
<b>Individual Taxpayers (But Not Sole Proprietorships)</b>			
<i>Arlin Geophysical v. U.S.</i> , 696 F. App'x 362 (10th Cir. 2017), <i>vacating and remanding</i> 2014 U.S. Dist. LEXIS 62405 (D. Utah 2014)	Vacated and remanded lower court's decision to give TP and third party a meaningful opportunity to dispute government's claim that third party was nominee	No	TP (Procedural Win)
<i>Balice, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5444 (D.N.J. 2017), <i>appeal docketed</i> , No. 17-3143 (3rd Cir. Sept. 29, 2017)	Federal tax lien valid and foreclosed against TP's real property; TP controlled trust was nominee; government's foreclosure claim was timely	Yes	IRS
<i>Bogart, U.S. v.</i> , 715 F. App'x 161 (3d Cir. 2017), <i>aff'g in part, vacating in part, and remanding</i> , 115 A.F.T.R.2d (RIA) 1201 (M.D. Penn. 2015), <i>denying motion to vacate, U.S. v. Bogart</i> , 2018 U.S. Dist. LEXIS 100517 (M.D. Pa., June 15, 2018)	Federal tax lien valid and may be enforced against TP's interest in property held in tenancy by entirety; TP controlled company was nominee and fraudulent transferee, and conveyance did not destroy tenancy by entirety; <i>Rodgers</i> factors supported foreclosure in entirety; vacated in part and remanded to determine whether TP's wife waived her right to assert an interest in sale proceeds	Yes	IRS
<i>Bone, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 6161 (N.D. Ala. 2017)	Default judgment against TP and third parties; federal tax lien valid and foreclosed against TP's real property; federal tax lien subordinate to third parties' claims	Yes	IRS
<i>Cobos, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 6079 (N.D. Tex. 2017)	Federal tax liens valid and foreclosed against TP's real property; TP's children and wife were nominees and fraudulent transferees; federal tax lien superior to the third party's judgment lien for some years at issue; failure to defend interests extinguished wife and ex-wife's interest	Yes	IRS
<i>Cottonwood Dev. v. Moter</i> , 2017 U.S. Dist. LEXIS 178770 (W.D. La. 2017)	Federal tax lien valid and foreclosed against TP's real property; federal tax lien survived the sale to third party; local property taxes paid by third party purchaser entitled to priority over the federal tax lien pursuant to IRC § 6323(b)(6)(A)	Yes	IRS
<i>De Leon, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1223 (S.D. Tex. 2018)	Federal tax lien valid and may be enforced against TP's real property	No	IRS
<i>Dodson, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1534 (E.D. Okla. 2018), <i>adopting</i> 121 A.F.T.R.2d (RIA) 1532 (E.D. Okla. 2018)	Default judgment against TP and third parties; federal tax liens valid and may be enforced against TP's real property; transfer of property voided as fraudulent	Yes	IRS
<i>Harvey, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5859 (D. Idaho 2017), <i>adopting</i> 2017 U.S. Dist. LEXIS 155751 (D. Idaho 2017), <i>aff'd</i> , 738 F. App'x 469 (9th Cir. 2018)	Federal tax lien valid and may be foreclosed against TPs' property; TPs' controlled entity was nominee	Yes	IRS
<i>Henderson, U.S. v.</i> , 119 A.F.T.R.2d (RIA) 2123 (E.D. Ark. 2017)	Default judgment against TP and third parties; federal tax lien valid and may be enforced against TP's real properties	Yes	IRS
<i>Jones, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1701 (M.D. Fla. 2018), <i>denying motion to vacate, U.S. v. Jones</i> , 2018 WL 3096787 (M.D. Fla. June 22, 2018)	Default judgment against TP and third parties; federal tax lien valid and may be foreclosed against TP's real properties; TP controlled entity was nominee	Yes	IRS
<i>Kramer, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5627 (S.D. Ohio 2017), <i>aff'd</i> , 121 A.F.T.R.2d (RIA) 1418 (6th Cir. 2018), <i>cert. denied</i> 138 S.Ct. 2640 (2018)	Default judgment against TP and third parties; federal tax lien valid and may be foreclosed against TP's real property; TP controlled entity was nominee	Yes	IRS
<i>Kramer, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1418 (6th Cir. 2018), <i>aff'g</i> 120 A.F.T.R.2d (RIA) 5627 (S.D. Ohio 2017), <i>cert. denied</i> 138 S.Ct. 2640 (2018)	Federal tax lien valid and may be enforced against TPs' real property	Yes	IRS

TABLE 7: Civil Actions to Enforce Federal Tax Liens or to Subject Property to Payment of Tax Under IRC § 7403

Case Citation	Issue(s)	Pro Se	Decision
<i>Mealer, U.S. v.</i> , 120 A.F.T.R.2d 5139 (N.D. Tex. 2017)	Federal tax lien valid and foreclosed against TP's real property	No	IRS
<i>Mooney, U.S. v.</i> , 121 A.F.T.R. 2d (RIA) 1746 (D. Minn. 2018), <i>adopting</i> 121 A.F.T.R.2d (RIA) 1736 (D. Minn. 2018)	Federal tax liens valid and may be enforced against TP's real property; TP controlled entity was nominee	Yes	IRS
<i>Nelson, U.S. v.</i> , 2018-1 U.S.T.C. (CCH) 50,264 (D.S.D. 2018), <i>reconsideration denied</i> , 121 A.F.T.R.2d 5088 (D.S.D. 2018)	Default judgment against TP and third parties; federal tax lien valid and may be enforced against TP's real property; TP controlled trust was nominee; <i>Rodgers</i> factors supported foreclosure in entirety	Yes	IRS
<i>Pierson, U.S. v.</i> , 2018-1 U.S.T.C. (CCH) 50,269 (D.N.J. 2018)	Federal tax lien valid and may be enforced against TP's one-half interest in real property; third party judgment predating the federal tax lien had priority, but federal tax lien superior to mortgage because no secured interest was created by divorce judgment	No	IRS
<i>Rivercliff Farm, Inc., U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5465 (D. Or. 2017), <i>judgment entered by No. 3:16-cv-1248-SI</i> (D. Or. Aug. 15, 2017)	Default judgment against TPs and third parties; lien valid and foreclosed against TPs' real property; company is nominee, fraudulent transferee, and/or alter ego	Yes	IRS
<i>Robbin, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5456 (D. Minn. 2017), <i>denying motion to amend judgment</i> , 120 A.F.T.R.2d (RIA) 6214 (D. Minn. 2017)	Federal tax liens valid and foreclosed against TP's real property; <i>Rodgers</i> factors supported foreclosure in entirety; non-liable spouse to receive one-half of sales proceeds	Yes	IRS
<i>Santana, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 6398 (M.D. Pa. 2017)	Default judgment against TP and third parties; federal tax liens valid and may be enforced against TP's real property; TP's son was nominee	Yes	IRS
<i>Silverman, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 6668 (D. Minn. 2017)	Default judgment against TP; federal tax lien valid and may be enforced against TP's real property, including marital property; county property tax lien had priority through stipulation; government and non-liable spouse split remaining proceeds evenly	Yes	IRS
<i>Sullender, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1091 (D.N.H. 2018)	Default judgment against TP and third parties; federal tax lien valid and may be enforced against TP's real properties; third parties were nominees	No	IRS
<i>Wade, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 6004 (D. Utah 2017), <i>appeal docketed</i> , No. 18-4140 (10th Cir., Sept. 28, 2018)	Federal tax lien valid and may be foreclosed against TP's real property; TP's gift to his wife was invalid and a fraudulent transfer; business trusts and unincorporated business organizations were nominees and fraudulent transferees; TP's tax liability was exempted from bankruptcy discharge	No	IRS
<i>Winland, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 6889 (M.D. Fla. 2017)	Default judgment against TP and third parties; federal tax liens valid and foreclosed against TP's real property; TP's girlfriend was nominee and fraudulent transferee; federal tax lien superior to third parties' claims	Yes	IRS
<i>Z Investment Properties, LLC., U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1317 (N.D. Ill. 2018), <i>appeal docketed</i> , No. 18-1915 (7th Cir. Apr. 26, 2018)	Federal tax lien valid and may be enforced against TP's real property; reasonable search would have revealed federal tax liens despite minor misspelling of TP's first name	No	IRS
<b>Business Taxpayers (Corporations, Partnerships, Trusts, and Sole Proprietorships - Schedule C, E, F)</b>			
<i>Akins, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1640 (D. Md. 2018), <i>appeal docketed</i> , No. 18-1747 (4th Cir. July 5, 2018)	Federal tax lien valid against one TP and seized that TP's property; summary judgment against second TP denied because the government failed to show she demonstrated the requisite control so as to open herself to liability for trust fund recovery penalties	No	Split

TABLE 7: Civil Actions to Enforce Federal Tax Liens or to Subject Property to Payment of Tax Under IRC § 7403

Case Citation	Issue(s)	Pro Se	Decision
<i>Davis, U.S. v.</i> , 700 F. App'x 368 (5th Cir. 2017), <i>aff'g</i> 119 A.F.T.R.2d (RIA) 314 (W.D. La. 2017)	Affirmed lower court's decision; federal tax liens valid and foreclosed against TP's real property; <i>Rodgers</i> factors supported foreclosure in entirety; proceeds divided between government and third parties	No	IRS
<i>Isagba, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 6940 (M.D. Fla. 2017), <i>adopting</i> 120 A.F.T.R.2d (RIA) 6935 (M.D. Fla. 2017)	Default judgment against TP and third party; federal tax lien valid and may be foreclosed against TP's real property; trust was nominee and fraudulent transferee	Yes	IRS
<i>Kraus, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1323 (W.D. Wash. 2018), <i>appeal docketed</i> No. 18-35516 (9th Cir. June 18, 2018)	Federal tax lien valid and may be foreclosed against TP's real property; trust and company were nominees; renoted in part to consider effect of ex-wife's innocent spouse claim on liens arising from interest assessed after divorce	Yes	IRS
<i>Montana v. 6350 W. Montana Highway 200</i> , 121 A.F.T.R.2d (RIA) 1268 (D. Mont. 2018), <i>appeal docketed</i> , No. 18-35567 (9th Cir. July, 10, 2018)	Federal tax lien valid and foreclosed against TP's real property; third party was nominee; federal tax lien superior to the interest of state of Montana and other third parties	Yes	IRS
<i>Nassar, U.S. v.</i> , 699 F. App'x 46 (2d Cir. 2017), <i>aff'g</i> 118 A.F.T.R. 2d (RIA) 6007 (S.D.N.Y. 2016)	Affirmed lower court's decision; Federal tax liens valid and foreclosed against TP's real property; trust was nominee	No	IRS
<i>Pacheco, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5388 (E.D. Va. 2017), <i>adopting</i> 120 A.F.T.R.2d (RIA) 5380 (E.D. Va. 2017)	Default judgment against TP and third parties; federal liens valid and may be foreclosed against TP's real property; failure to defend interest precluded one third party's interest in the property, while other third party's interest was stipulated as subordinate to federal liens	Yes	IRS
<i>Pflum, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5778 (E.D. Cal. 2017)	Default judgment against TP; federal tax liens valid and foreclosed against TP's real properties; TP controlled entities were nominees	Yes	IRS
<i>Rod Riordan Inc., U.S. v.</i> , 2018 U.S. Dist. LEXIS 87661 (W.D. Tex. 2018)	Default judgment against TPs and third parties; federal tax lien valid and may be foreclosed against TP's real property	Yes	IRS
<i>Succullo, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 6943 (M.D. Fla. 2017), <i>stay denied</i> , <i>Succullo v. U.S.</i> , 2018 U.S. App LEXIS 12258 (11th Cir., Apr. 24, 2018)	Federal tax lien valid and may be foreclosed against TP's (estate) real property; transfer of property to trust was ineffective because of invalid deed and remained within TP's estate	No	IRS
<i>Swartout, U.S. v.</i> , 293 F. Supp. 3d 1377 (S.D. Fla. 2018)	Default judgment against TP (estate) and surviving heir; federal tax lien valid and may be enforced against TP's real property; family trust was nominee	No	IRS
<i>Tobey, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 372 (D.Minn. 2018), <i>adopting</i> 121 A.F.T.R.2d (RIA) 366 (D.Minn. 2017)	Default judgment against TP and third parties; federal tax lien valid and may be enforced against TP's real property	Yes	IRS
<i>Wilhite, U.S. v.</i> , 2018 U.S. Dist. LEXIS 42318 (D. Colo. 2018), <i>appeal docketed</i> , No. 18-1090 (10th Cir., Mar. 15, 2018)	Federal tax lien valid and enforced against TP's company; wife was nominee; <i>Rodgers</i> factors supported foreclosure in entirety; federal tax liens superior to third party's claim; court appointed a receiver to manage TP's assets during enforcement	No	IRS
<i>Williams, U.S. v.</i> , 120 A.F.T.R.2d (RIA) 5611 (M.D.N.C. 2017)	Default judgment against TP and third party; federal tax lien valid and may be enforced against TP's property; TP was alter ego of trust and personally liable; TP's son-in law controlled trust was nominee	Yes	IRS

**TABLE 8: Charitable Contribution Deductions Under IRC § 170**

Case Citations	Issue(s)	Pro Se	Decision
<b>Individual Taxpayers (But Not Sole Proprietorships)</b>			
<i>Azam v. Comm'r</i> , T.C. Memo. 2018-72	TPs failed to substantiate cash contributions	Yes	IRS
<i>Benjamin v. Comm'r</i> , T.C. Memo. 2018-70, appeal docketed, No. 18-72831 (9th Cir. Oct. 18, 2018)	Carryover contributions unsubstantiated	Yes	IRS
<i>Conner v. Comm'r</i> , T.C. Memo. 2018-6, appeal docketed No. 18-12997 (11th Cir. July 17, 2018)	TPs' charitable contribution deduction not limited under section 170(e)	No	TP
<i>Davis v. Comm'r</i> , T.C. Memo. 2018-56	Cash and non-cash contributions unsubstantiated	Yes	IRS
<i>Fakiris v. Comm'r</i> , T.C. Memo. 2017-126	TP's transfer of theater was conditional and not a completed gift	No	IRS
<i>Farolan v. Comm'r</i> , T.C. Summ. Op. 2018-28	TP failed to substantiate cash and non-cash contributions	Yes	IRS
<i>Fehr v. Comm'r</i> , T.C. Summ. Op. 2018-26	TP failed to substantiate non-cash contributions	Yes	IRS
<i>Fiedziuszko v. Comm'r</i> , T.C. Memo. 2018-75	TP failed to substantiate cash and non-cash contributions	Yes	IRS
<i>Fleming v. Comm'r</i> , T.C. Summ. Op. 2017-83	Cash and non-cash contributions substantiated in part, unsubstantiated in part	No	Split
<i>Gardner v. Comm'r</i> , T.C. Memo. 2017-165	TP failed to substantiate valuation of non-cash contributions	No	IRS
<i>Justine v. Comm'r</i> , T.C. Memo. 2017-198	Cash and/or non-cash contributions unsubstantiated	Yes	IRS
<i>Knowles v. Comm'r</i> , T.C. Memo. 2017-152	TP failed to substantiate cash and non-cash contributions	No	IRS
<i>Martinez v. Comm'r</i> , T.C. Summ. Op. 2017-42	TP failed to substantiate cash contributions	Yes	IRS
<i>Moore v. Comm'r</i> , T.C. Memo. 2018-58	Non-cash contributions unsubstantiated	Yes	IRS
<i>Ohde v. Comm'r</i> , T.C. Memo. 2017-137	TP failed to substantiate non-cash contributions	No	IRS
<i>Platts v. Comm'r</i> , T.C. Memo. 2018-31	Non-cash contributions unsubstantiated and improperly valued	Yes	IRS
<i>Rademacher v. Comm'r</i> , T.C. Memo. 2018-43	Cash contributions unsubstantiated	No	IRS
<i>Rogers v. Comm'r</i> , T.C. Memo. 2018-53	TPs lacked requisite donative intent	No	IRS
<i>Rutkoske v. Comm'r</i> , 149 T.C. No. 6 (2017)	TPs were not "qualified farmers" who could deduct 100% of contribution basis from bargain sale of conservation easement	No	IRS
<b>Business Taxpayers (Corporations, Partnerships, Trusts, and Sole Proprietorships - Schedules C, E, F)</b>			
<i>310 Retail, LLC v. Comm'r</i> , T.C. Memo. 2017-164	TP substantiated contribution of conservation easement	No	TP
<i>BC Ranch II, L.P. v. Comm'r</i> , 867 F.3d 547 (5th Cir. 2017), vacating and remanding T.C. Memo. 2015-130	Easement grants were made in perpetuity and TP met baseline documentation requirement	No	TP
<i>Big River Dev., L.P. v. Comm'r</i> , T.C. Memo. 2017-166	TP substantiated contribution of conservation easement	No	TP
<i>Palmolive Bldg. Inv., LLC v. Comm'r</i> , 149 T.C. No. 18 (2017)	TP's facade easement contribution was not a qualified conservation contribution	No	IRS
<i>RERI Holdings I, LLC v. Comm'r</i> , 149 T.C. No. 1 (2017), appeal docketed No. 17-1266 (D.C. Cir. Dec. 18, 2017)	TP failed to substantiate and overvalued non-cash contribution	No	IRS
<i>RP Golf v. Comm'r</i> , 860 F.3d 1096 (8th Cir. 2017), aff'g T.C. Memo. 2016-80	TP's donation of conservation easement was not a qualified conservation contribution	No	IRS
<i>Salt Point Timber, LLC v. Comm'r</i> , T.C. Memo. 2017-245	TP's contribution of conservation easement was not necessarily made to a "qualified organization"	No	IRS

TABLE 8: Charitable Contribution Deductions Under IRC § 170

Case Citations	Issue(s)	Pro Se	Decision
<i>Ten Twenty Six Inv. v. Comm'r</i> , T.C. Memo. 2017-115	TP failed to record deed and convey "qualified real property interest" in contribution of conservation easement	No	IRS
<i>Triumph Mixed Use Inv. III, LLC v. Comm'r</i> , T.C. Memo. 2018-65	Transfer was part of a <i>quid pro quo</i> arrangement and TP not entitled to charitable contribution deduction	No	IRS
<i>Wendell Falls Dev., LLC v. Comm'r</i> , T.C. Memo. 2018-45	TP donated conservation easement with expectation of receiving a substantial benefit and easement had no value	No	IRS

**TABLE 9: Itemized Deductions Reported on Schedule A (Form 1040)**

Case Citations	Issue(s)	Pro Se	Decision
<b>Individual Taxpayers (But Not Sole Proprietorships)</b>			
<i>Barry v. Comm'r</i> , T.C. Memo. 2017-237	Expense incurred for production of income under § 212 disallowed; legal fees paid were non-deductible personal expenses	No	IRS
<i>Benjamin v. Comm'r</i> , T.C. Memo. 2018-70	Miscellaneous itemized deduction for tax preparation fees disallowed; TP failed to substantiate expenses	Yes	IRS
<i>Bon Viso v. Comm'r</i> , T.C. Memo. 2017-154	Gambling loss deduction disallowed because TP elected to use standard deduction	Yes	IRS
<i>Boneparte v. Comm'r</i> , T.C. Memo. 2017-193, <i>appeal docketed</i> , No. 18-2264 (3d Cir., June 8, 2018)	Gambling loss allowed to the extent of gambling winnings; TP failed to substantiate claim that he was professional gambler and not entitled to nonwagering gambling expense deductions	Yes	Split
<i>Davis v. Comm'r</i> , T.C. Memo. 2018-56	Miscellaneous itemized deduction for tax preparation fees allowed; TP adequately substantiated expense	Yes	TP
<i>De Leon, U.S. v.</i> , 121 A.F.T.R.2d (RIA) 1223 (S.D. Tex. 2018)	Deduction for taxes paid allowed under § 164; home mortgage interest deductions allowed under § 163(h)	No	TP
<i>Dykstra v. Comm'r</i> , T.C. Memo. 2017-156	Home mortgage interest deduction under § 163(h) allowed; TP provided amended mortgage interest statement to IRS; IRS did not provide any reason why the amended mortgage interest statement is not sufficient	Yes	TP
<i>Fiedziuszko v. Comm'r</i> , T.C. Memo. 2018-75	Medical and dental expense deduction under § 213 disallowed; TPs failed to substantiate expenses paid for physician-ordered treatment	Yes	IRS
<i>Henley v. Comm'r</i> , T.C. Summ. Op. 2018-22	Gambling loss deduction disallowed because TP unable to substantiate winnings and losses; IRS conceded and allowed only a part of the itemized deduction for wagering losses	Yes	IRS
<i>Howard v. Comm'r</i> , T.C. Summ. Op. 2017-65	Miscellaneous itemized deductions for tax preparation fees and attorney and accounting fees disallowed; TP failed to substantiate expenses	Yes	IRS
<i>In re Nora</i> , 581 B.R. 870 (D. Minn. 2018)	Casualty loss deduction under § 165 disallowed; TP failed to substantiate value of destroyed items	Yes (TP is attorney rep herself)	IRS
<i>Justine v. Comm'r</i> , T.C. Memo. 2017-198	Medical expense deduction under § 213 disallowed; Taxes paid deduction under § 164 disallowed; TP failed to substantiate expenses	Yes	IRS
<i>Knowles v. Comm'r</i> , T.C. Memo. 2017-152	Real property taxes paid deduction under § 164 disallowed; TP unable to substantiate payment of property taxes	No	IRS
<i>Kohn v. Comm'r</i> , T.C. Memo. 2017-159	Casualty loss deduction under § 165 disallowed; TPs did not suffer loss claimed and also loss would not have exceeded the 10% adjusted gross income floor provided in section 165(h)(2)	Yes	IRS
<i>Morrissey v. U.S.</i> , 871 F.3d 1260 (11th Cir. 2017), <i>aff'g</i> 226 F. Supp. 3d 1338 (M.D. Fla. 2016)	Medical expense deduction under § 213 disallowed; TP could not deduct costs of egg donor's and surrogate's in vitro fertilization treatments because expenses did not affect a function of TP's own body	No	IRS
<i>Pryde v. U.S.</i> , 120 A.F.T.R.2d (RIA) 6843 (Fed. Cl. 2017)	Casualty loss deduction under § 165 disallowed; TPs could not establish an entitlement to relief under the theft loss safe harbor set forth in Revenue Procedure 2009-20	No	IRS
<i>Farolan v. Comm'r</i> , T.C. Summ. Op. 2018-28	Miscellaneous itemized deduction for tax preparation fees allowed; TP adequately substantiated expenses	Yes	TP

TABLE 9: Itemized Deductions Reported on Schedule A (Form 1040)

Case Citations	Issue(s)	Pro Se	Decision
<i>Rogers v. Comm'r</i> , T.C. Memo. 2018-53	Home mortgage interest deduction under § 163(h) disallowed because TPs failed to substantiate the payment and business purpose of the interest expense deduction; TP adequately substantiated some expenses relating to legal and professional fees and other miscellaneous expenses	Yes	Split
<b>Business Taxpayers (Partnerships and Sole Proprietorships - Schedules C, E, F)</b>			
<i>Conner v. Comm'r</i> , T.C. Memo. 2018-6, <i>appeal docketed</i> No. 18-12997 (11th Cir., July 17, 2018)	Real property held in an LLC was investment property, not in ordinary course of business under § 162, and subject to the investment interest limitations under §§ 212 and 163(d)	No	IRS
<i>Enis v. Comm'r</i> , T.C. Memo. 2017-222	Theft loss deduction under § 165 for participation in failed investment disallowed; TPs unable to prove required element of intent	No	IRS
<i>Hamilton v. U.S.</i> , 120 A.F.T.R.2d (RIA) 5701 (N.D. Ind. 2017)	Theft loss deduction under § 165 for participation in failed investment disallowed; TPs unable to prove there was no reasonable prospect of recovery	No	IRS
<i>McMillan v. Comm'r</i> , 697 F. App'x 489 (9th Cir. 2017), <i>aff'g</i> T.C. Memo. 2013-40	Casualty loss deduction under § 165 disallowed; death of horse from disease not a casualty loss	Yes	IRS
<i>Partyka v. Comm'r</i> , T.C. Summ. Op. 2017-79	Casualty loss deduction under § 165 partially allowed; TP ascertained with reasonable certainty that they could not obtain reimbursement for items; insufficient evidence to determine the fair market value of some of the items	Yes	Split

**TABLE 10: Frivolous Issues Penalty Under IRC § 6673 and Related Appellate-Level Sanctions**

Case Citations	Issue(s)	Pro Se	Decision	Amount
<b>Individual Taxpayers (But Not Sole Proprietorships)</b>				
<i>Blair v. Comm'r</i> , T.C. Memo. 2017-153	TP petitioned for redetermination of deficiency and additions to tax and asserted he had no federal tax liability	Yes	IRS	\$10,000
<i>Fleming v. Comm'r</i> , T.C. Memo. 2017-155	TP petitioned for review of IRS decision to sustain levy and asserted frivolous arguments or maintained proceedings solely for delay	Yes	IRS	\$5,000
<i>Fleming v. Comm'r</i> , T.C. Memo. 2017-120	TP petitioned for redetermination of deficiency and additions to tax; maintained proceedings solely for delay	Yes	TP	
<i>Gardner v. Comm'r</i> , T.C. Memo. 2017-107	TP petitioned for redetermination of IRS decision to proceed with levy and argued the IRS lied and defamed the TP and that the Commissioner and the courts conspired to deny her First Amendment rights to freedom of speech and religion	Yes	IRS	\$10,000
<i>Jagos v. Comm'r</i> , 121 A.F.T.R.2d 2209 (6th Cir. 2018), <i>aff'g</i> T.C. Memo. 2017-202, <i>reh'g denied</i> , No. 18-1087 (6th Cir., Oct. 9, 2018)	TPs (MFJ) petitioned for redetermination of deficiency and argued that only federal employees must pay income tax, the Commissioner failed to prepare a substitute for return, and the Commissioner had no independent knowledge of their income	Yes	IRS	\$1,000
<i>Lorusso v. Comm'r</i> , T.C. Memo. 2018-3	TP petitioned for redetermination of IRS decision to proceed with collection actions and instituted proceedings primarily for delay	Yes	TP	
<b>Business Taxpayers (Corporations, Partnerships, Trusts, and Sole Proprietorships – Schedules C, E, F)</b>				
<i>Hawkbey v. Comm'r</i> , T.C. Memo. 2017-199	TP petitioned for redetermination of deficiency and argued that the Emancipation Proclamation exempted him from taxation	Yes	TP	
<i>Rader v. Comm'r</i> , T.C. Memo. 2017-209	TP petitioned for redetermination of deficiencies and challenged the validity of a substitute for return in its entirety without assigning error to the IRS	Yes	IRS	\$2,000
<b>Section 6673 Penalty Not Requested or Imposed but Taxpayer Warned To Stop Asserting Frivolous Arguments</b>				
<i>Siegel v. Comm'r</i> , T.C. Summ. Op. 2017-53	TP petitioned for redetermination of deficiency, penalties, and additions to tax and argued he was not a taxpayer liable to pay taxes	Yes		
<i>Williams v. Comm'r</i> , T.C. Memo. 2018-50, <i>appeal docketed</i> , No. 18-60536 (5th Cir. Aug. 1, 2018)	TP petitioned for redetermination of IRS decision to sustain lien and intent to levy	Yes		
<i>Zentmyer v. Comm'r</i> , T.C. Memo. 2017-197, <i>appeal docketed</i> , No. 18-72116 (9th Cir. July 26, 2018)	TP petitioned for redetermination of deficiency and asserted that income is an abstraction that can't be taxed and that the notice of deficiency was deficient in all aspects	Yes		

TABLE 10: Frivolous Issues Penalty Under IRC § 6673 and Related Appellate-Level Sanctions

Case Citations	Issue(s)	Pro Se	Decision	Amount
<b>U.S. Courts of Appeals' Decisions on Appeal of Section 6673 Penalties Imposed by U.S. Tax Court</b>				
<i>Best v. Comm'r</i> , 702 F. App'x 615 (9th Cir. 2017), <i>aff'g</i> T.C. Memo. 2014-72, <i>reh'g, en banc, denied</i> , 2018 U.S. App. LEXIS 3452 (9th Cir., Feb. 14, 2018), <i>cert. denied</i> , 138 S. Ct. 2691 (June 25, 2018)	\$500 penalty affirmed	No	IRS	
<i>Schneider v. Comm'r</i> , 697 F. App'x 474 (8th Cir. 2017), <i>aff'g</i> No. 017566-14 (T.C. Sept. 1, 2016) and No. 029122-14 (T.C. Aug. 24, 2016), <i>cert. and reh'g denied</i> , 138 S. Ct. 1708 (2018)	\$5,000 penalty affirmed	Yes	IRS	
<i>Sykes v. Comm'r</i> , 719 F. App'x 728 (9th Cir. 2018), <i>aff'g</i> No. 018787-12 (T.C. Nov. 22, 2013), <i>reh'g, en banc, denied</i> , 2018 U.S. App. LEXIS 18760 (9th Cir., July 10, 2018)	\$25,000 penalty affirmed	Yes	IRS	
<i>Sykes v. Comm'r</i> , 719 F. App'x 726 (9th Cir. 2018), <i>aff'g</i> No. 10386-11 (T.C. Sept. 16, 2013), <i>reh'g, en banc, denied</i> , 2018 U.S. App. LEXIS 18760 (9th Cir., July 10, 2018)	\$25,000 penalty affirmed	Yes	IRS	
<i>Sykes v. Comm'r</i> , 719 F. App'x 730 (9th Cir. 2018), <i>aff'g</i> No. 24394-15 (T.C. July 27, 2016), <i>reh'g, en banc, denied</i> , 2018 U.S. App. LEXIS 18760 (9th Cir., July 10, 2018)	\$25,000 penalty affirmed	Yes	IRS	
<i>Sykes v. Comm'r</i> , 720 F. App'x 401 (9th Cir. 2018), <i>aff'g</i> No. 9793-13 (T.C. Sept. 26, 2014), <i>reh'g, en banc, denied</i> , 2018 U.S. App. LEXIS 18760 (9th Cir., July 10, 2018)	\$25,000 penalty affirmed	Yes	IRS	
<i>Waltner v. Comm'r</i> , 714 F. App'x 726 (9th Cir. 2018), <i>aff'g</i> T.C. Memo. 2015-146	\$15,000 penalty affirmed	Yes	IRS	
<i>Williams v. Comm'r</i> , 724 F. App'x 920 (11th Cir. 2018), <i>aff'g</i> T.C. Memo. 2017-58	\$5,000 penalty affirmed	Yes	IRS	
<b>Other U.S. Courts' Decisions on Sanctions Under Section 7482 (c)(4), FRAP Rule 38, or Other Authority</b>				
<i>Nevius v. Comm'r</i> , 694 F. App'x 447 (8th Cir. 2017), <i>aff'g</i> No. 011959-15 (T.C. Oct. 9, 2015)	TP appealed Tax Court's decision to dismiss his challenge to a notice of deficiency and asserted frivolous arguments	Yes	IRS	\$5,000
<i>Ramer, U.S. v.</i> , 699 F. App'x 596 (8th Cir. 2017), <i>aff'g</i> 2017 WL 214190 (W.D. Ark. 2017)	TPs (MFJ) appeal district court's entry of default judgment in action to enforce federal tax liens and alleged the lower court abused its discretion	Yes	IRS	\$8,000
<i>Schneider v. Comm'r</i> , 697 F. App'x 474 (8th Cir. 2017), <i>aff'g</i> No. 017566-14 (T.C. Sept. 1, 2016) and No. 029122-14 (T.C. Aug. 24, 2016), <i>cert. and reh'g denied</i> , 138 S. Ct. 1708 (Apr. 30 and June 25, 2018)	TP appealed Tax Court's grant of summary judgment, upholding of assessments, and imposition of penalties and asserted that income tax is an unconstitutional direct tax that must be apportioned	Yes	IRS	\$5,000

TABLE 11: Unpublished Tax Court Summary Judgment Orders

Case Name	Docket No.	Order Entered Date	Issue(s)	Pro Se	Decision	Corresponding MLI Topic
<i>Abraham v. Comm'r</i>	Docket No. 22070-15L	1/30/18	CDP (Levy); Additions to Tax Under Sections 6651 and 6654	Yes	IRS	CDP (Levy); FTP; Estimated Tax Penalty
<i>Akey v. Comm'r</i>	Docket No. 18153-17L	3/1/18	CDP	Yes	IRS	CDP
<i>Amaefuna v. Comm'r</i>	Docket No. 23235-16SL	8/29/17	CDP (Levy)	Yes	TP	CDP (Levy)
<i>Anderson v. Comm'r</i>	Docket No. 27551-16L	1/2/18	CDP (Levy); FTF and FTP Penalty	Yes	IRS	CDP(Levy); FTF; FTP Penalty
<i>Anthony v. Comm'r</i>	Docket No. 4001-17L	3/6/18	CDP (Lien and Levy)	No	IRS	CDP (Lien, Levy)
<i>ASC Insulation Fireproofing v. Comm'r</i>	Docket No. 28002-16L	2/20/18	CDP	Yes	IRS	CDP
<i>Babanari v. Comm'r</i>	Docket No. 6743-17L	1/23/18	CDP	Yes	IRS	CDP
<i>Bain v. Comm'r</i>	Docket No. 32489-15 L	7/6/17	CDP	Yes	IRS	CDP
<i>Barcelo v. Comm'r</i>	Docket No. 21856-16 L.	7/5/17	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Basdakis v. Comm'r</i>	Docket Nos. 26892-16L and 26893-16L	12/12/17	CDP (Lien)	No	IRS	CDP (Lien)
<i>Bashen v. Comm'r</i>	Docket No. 21924-15L	12/20/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Bashen v. Comm'r</i>	Docket No. 28472-15 L.	6/14/17	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Batten v. Comm'r</i>	Docket No. 13525-16L	10/5/17	CDP (Levy)	Yes	IRS	CDP(Levy)
<i>Bea v. Comm'r</i>	Docket No. 15970-17	12/22/17	Carryback of a Net Operating Loss	No	IRS	Trade or Business
<i>Berta v. Comm'r</i>	Docket No. 8809-16SL	12/21/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Black v. Comm'r</i>	Docket No. 16269-16SL	3/23/18	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Blank v. Comm'r</i>	Docket No. 19565-16SL.	6/20/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Blank v. Comm'r</i>	Docket No. 24882-16SL	10/20/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Bornstein v. Comm'r</i>	Docket No. 15985-16 L	7/26/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Boyett v. Comm'r</i>	Docket No. 21630-17L	4/12/18	CDP (Levy)	Yes	IRS	CDP(Levy)
<i>Bradbury v. Comm'r</i>	Docket No. 25963-15L	4/5/18	CDP (Lien)	No	TP	CDP (Lien)
<i>Brigulio v. Comm'r</i>	Docket No. 11087-12	4/6/18	Relieve from Joint and Several Liability	No	TP	Innocent Spouse Relief
<i>Broadus v. Comm'r</i>	Docket No. 15464-17L	4/27/18	CDP (Levy)	No	IRS	CDP (Levy)

TABLE 11: Unpublished Tax Court Summary Judgment Orders

Case Name	Docket No.	Order Entered Date	Issue(s)	Pro Se	Decision	Corresponding MLI Topic
<i>Brooks v. Comm'r</i>	Docket No. 28206-15	8/24/17	Charitable Contributions Substantiation Requirements	No	TP	Charitable Contributions
<i>Bujak v. Comm'r</i>	Docket No. 30963-15L	10/4/17	CDP	Yes	IRS	CDP
<i>Burkhalter v. Comm'r</i>	Docket No. 14345-16 L	7/12/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Burstein v Comm'r</i>	Docket No. 11816-17L	12/7/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Bushey v. Comm'r</i>	Docket No. 26557-15 L	7/12/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Butler v. Comm'r</i>	Docket No. 8884-17L	3/14/18	CDP	Yes	IRS	CDP
<i>Campion v. Comm'r</i>	Docket No. 28168-15 L	9/7/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Canzoneri v. Comm'r</i>	Docket No. 9545-17S	5/3/18	Underreported Income	Yes	IRS	Gross Income
<i>Carroll Jr. v. Comm'r</i>	Docket No. 4569-16W	7/11/17	Whether IRS Engaged in Unreasonable Delay in Denying Whistleblower Claims	No	IRS	Whistleblower Claims
<i>Cartagena v. Comm'r</i>	Docket No. 22212-16SL	8/3/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Carter-Castoreno v. Comm'r</i>	Docket No. 13519-16L	12/19/17	CDP	Yes	IRS	CDP
<i>Chambers v. Comm'r</i>	Docket No. 26549-16S	8/29/17	TP Filed a Return Erroneously Claiming a Net Premium Tax Credit of \$3,000	Yes	IRS	ACA; Other
<i>Chapman v. Comm'r</i>	Docket No. 10247-15L	1/31/18	CDP (Levy)	No	IRS	CDP (Levy)
<i>Clarke v. Comm'r</i>	Docket No. 11772-15 L.	6/19/17	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Clausen v Comm'r</i>	Docket No. 18947-16L	2/26/18	CDP (Levy)	No	IRS	CDP (Levy)
<i>Conway v. Comm'r</i>	Docket No. 6204-13S L	7/28/17	CDP (Lien)	Yes	Split	CDP (Lien)
<i>Cordova v. Comm'r</i>	Docket No. 20200-16 L	8/2/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Curran v. Comm'r</i>	Docket No. 7500-16 L	9/20/17	CDP (Levy)	Yes	Split	CDP (Levy)
<i>Cypress v. Comm'r</i>	Docket No. 7939-12 L.	6/15/17	CDP (Lien)	No	IRS	CDP (Lien)
<i>David v. Comm'r</i>	Docket No. 22230-16SL	3/16/18	CDP	Yes	IRS	CDP
<i>Davidson v. Comm'r</i>	Docket No. 27587-16L	4/2/18	CDP (Levy)	No	IRS	CDP (Levy)
<i>Davis v. Comm'r</i>	Docket No. 12320-16SL	7/12/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Del Rosario v. Comm'r</i>	Docket No. 26307-16L	12/20/17	CDP	Yes	IRS	CDP

TABLE 11: Unpublished Tax Court Summary Judgment Orders

Case Name	Docket No.	Order Entered Date	Issue(s)	Pro Se	Decision	Corresponding MLI Topic
<i>Denney v. Comm'r</i>	Docket No. 12192-16L	5/15/18	CDP	Yes	IRS	CDP
<i>Derringer Trading, LLC, v. Comm'r</i>	Docket Nos. 20872-07 and 6268-08	7/26/17	Whether TP's Basis in Investment based on Cost Basis or Carryover Basis; Accuracy Related Penalty	Yes	Split	Gross Income; Partnership Tax; Accuracy Related Penalty
<i>Dew v. Comm'r</i>	Docket No. 18966-15 L	9/13/17	CDP; Estimated Tax Payments; Trust Fund Recovery Penalties (TFRP)	Yes	IRS	CDP; TFRP
<i>Dixon v. Comm'r</i>	Docket No. 22154-16SL	11/30/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Dostert v. Comm'r</i>	Docket No. 27122-16 L.	8/28/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Du-Bois v. Comm'r</i>	Docket No. 1153-17	12/15/17	Substantiation for Deductions	Yes	TP	Itemized Deductions
<i>Duskin v. Comm'r</i>	Docket No. 5902-17 L	3/1/18	CDP	No	IRS	CDP
<i>Essential Planning, Inc., v. Comm'r</i>	Docket No. 4102-16SL	2/27/18	CDP	Yes	IRS	CDP
<i>Everson v. Comm'r</i>	Docket No. 17814-16L	3/7/18	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Farrel v. Comm'r</i>	Docket No. 20345-16	12/28/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Feloney v. Comm'r</i>	Docket No. 25446-16L	1/17/18	CDP (Lien, Levy)	No	IRS	CDP (Lien, Levy)
<i>Ferrin v. Comm'r</i>	Docket No. 25381-16SL	9/7/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Filipovich v. Comm'r</i>	Docket No. 19780-17L	3/16/18	CDP	Yes	IRS	CDP
<i>Forrest v. Comm'r</i>	Docket No. 586-17L	1/2/18	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Friedman v. Comm'r</i>	Docket No. 12333-17SL	3/30/18	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Friendly Market, Inc., v. Comm'r</i>	Docket No. 4622-17 L	3/7/18	CDP	Yes	IRS	CDP
<i>Fyke v. Comm'r</i>	Docket No. 31304-15 L.	6/2/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Gallagher v. Comm'r</i>	Docket No. 1968-17SL	11/29/17	CDP	Yes	IRS	CDP
<i>Gnidziejko v. Comm'r</i>	Docket No. 21201-16SL	10/3/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Goldsmith v. Comm'r</i>	Docket No. 21235-16 L	9/18/17	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Goldsmith v. Comm'r</i>	Docket No. 21235-16L	9/29/17	CDP (Lien, Levy)	Yes	IRS	CDP (Lien, Levy)
<i>Gonzalez v. Comm'r</i>	Docket No. 182-13W	5/22/18	Whistleblower Action	Yes	IRS	Whistleblower Claims
<i>Graham v. Comm'r</i>	Docket No. 9815-17SL	3/30/18	CDP (Levy)	Yes	IRS	CDP (Levy)

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Case Name	Docket No.	Order Entered Date	Issue(s)	Pro Se	Decision	Corresponding MLI Topic
<i>Grande v. Comm'r</i>	Docket No. 15914-16SL	9/18/17	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Gray v. Comm'r</i>	Docket No. 28011-16S	3/23/18	Affordable Care Act Advanced Premium Tax Credit	Yes	IRS	ACA; Other
<i>Grimes v. Comm'r</i>	Docket No. 594-17SL	12/18/17	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Grubb v. Comm'r</i>	Docket No. 16759-16SL	12/7/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Guzik v. Comm'r</i>	Docket No. 26364-16L	3/13/18	CDP (Levy)	No	IRS	CDP (Levy)
<i>Hansen v. Comm'r</i>	Docket No. 31451-15L	9/1/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Hansen v. Comm'r</i>	Docket No. 23103-17SL	5/7/18	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Harbick v. Comm'r</i>	Docket No. 6753-16 L	7/11/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Haynes v. Comm'r</i>	Docket No. 16420-17L	4/25/18	CDP (Lien, Levy); Trust Fund Recovery Penalty	No	IRS	CDP (Lien, Levy); TFRP
<i>Heintz v. Comm'r</i>	Docket No. 12669-17L	1/26/18	CDP (Lien, Levy)	No	IRS	CDP (Lien, Levy)
<i>Hendrickson v. Comm'r</i>	Docket No. 28648-15L	4/27/18	CDP (Lien); Employment Taxes; Trust Fund Recovery Penalty	Yes	IRS	CDP (Lien); Employment Taxes; TFRP
<i>Hernandez v. Comm'r</i>	Docket No. 27789-16L	1/29/18	CDP	Yes	IRS	CDP
<i>Herndon v. Comm'r</i>	Docket No. 21071-17L	5/7/18	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Hill v. Comm'r</i>	Docket No. 7183-17SL	1/4/18	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Hines v. Comm'r</i>	Docket No. 14762-16 L	9/28/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Hoffer v. Comm'r</i>	Docket No. 17545-15L	3/30/18	Underreported Retirement Income; Accuracy Related Penalty	Yes	IRS	Gross Income; Accuracy Related Penalty
<i>Hoffman Prop. II, L.P. v. Comm'r</i>	Docket No. 14130-15.	3/14/18	Noncash Charitable Contribution	No	IRS	Charitable Contributions
<i>Hoffman Prop. II, L.P. v. Comm'r</i>	Docket No. 14130-15.	7/12/17	Easement Contribution (IRS wins on factors 2, 3, but loses 1, 4, 5)	No	Split	Charitable Contributions
<i>Horwitz v. Comm'r</i>	Docket No. 13479-15L.	8/8/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Howell v. Comm'r</i>	Docket No. 8858-16	12/11/17	Adjustment of Retirement Income; Disallowance of an Adoption Credit	Yes	IRS	Family Status Issues; Itemized Deductions; Gross Income
<i>Hull v. Comm'r</i>	Docket No. 23243-16L	12/14/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Huminski v. Comm'r</i>	Docket No. 16614-16 L	8/17/17	CDP (Levy)	Yes	IRS	CDP (Levy)

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Case Name	Docket No.	Order Entered Date	Issue(s)	Pro Se	Decision	Corresponding MLI Topic
<i>Hurrington v. Comm'r</i>	Docket No. 8147-16 L	7/19/17	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Jacks v. Comm'r</i>	Docket No. 22610-16L	2/13/18	CDP (Levy)	No	IRS	CDP (Levy)
<i>Jennings v. Comm'r</i>	Docket No. 25587-15SL	12/18/17	CDP (Levy)	No	IRS	CDP (Levy)
<i>John L. Henss, Ltd., v. Comm'r</i>	Docket No. 30852-15 L	7/26/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Kamidoi v. Comm'r</i>	Docket No. 7508-16SL	6/1/17	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Karim v. Comm'r</i>	Docket No. 17407-15L	10/10/17	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Karjian v. Comm'r</i>	Docket No. 23416-16L	3/7/18	CDP (Levy); Underreported Income	Yes	IRS	CDP (Levy); Gross Income
<i>Katz v. Comm'r</i>	Docket No. 13587-16SL	12/21/17	CDP	Yes	IRS	CDP
<i>Keel v. Comm'r</i>	Docket No. 1410-17	1/16/18	Affordable Care Act Premium Assistance Tax Credit; COD Income	Yes	IRS	Gross Income; Other
<i>Kelly v. Comm'r</i>	Docket No. 4709-17L	1/29/18	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Kestin v. Comm'r</i>	Docket No. 18254-17L	5/7/18	Frivolous Issues; CDP (Levy, NFTL)	Yes	Split	CDP (Lien, Levy); Frivolous Issues
<i>Keys v. Comm'r</i>	Docket No. 9959-16 L	10/27/17	CDP; Installment Agreement	Yes	IRS	CDP
<i>Khan v. Comm'r</i>	Docket No. 21360-16 L	8/7/17	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Kidman v. Comm'r</i>	Docket No. 2626-16L	1/23/18	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Kirven v. Comm'r</i>	Docket No. 30393-15W	6/29/17	Whistleblower Claim	Yes	IRS	Whistleblower Claims
<i>Kolle v. Comm'r</i>	Docket No. 4636-16SL	4/13/18	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Krupa v. Comm'r</i>	Docket No. 11390-17 L	5/8/18	CDP	Yes	IRS	CDP
<i>Lambert v. Comm'r</i>	Docket No. 9617-14 L	7/31/17	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Langanki v. Comm'r</i>	Docket No. 20566-16 L	9/11/17	CDP	Yes	IRS	CDP
<i>Lazenberry v. Comm'r</i>	Docket No. 18389-16	1/18/18	American Opportunity Credit	Yes	IRS	Itemized Deductions
<i>Lee v. Comm'r</i>	Docket No. 19918-16SL	8/28/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Leon-Guerrero v. Comm'r</i>	Docket No. 19937-16L	11/22/17	CDP	Yes	IRS	CDP
<i>Lewis v. Comm'r</i>	Docket No. 20410-16 L	9/15/17	CDP (Levy)	Yes	IRS	CDP (Levy)

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Case Name	Docket No.	Order Entered Date	Issue(s)	Pro Se	Decision	Corresponding MLI Topic
<i>Loetscher v. Comm'r</i>	Docket No. 10197-17L	5/23/18	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Lomelo Design Assoc., Inc. v. Comm'r</i>	Docket No. 4180-17SL	8/3/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Lucian v. Comm'r</i>	Docket No. 16456-17L	1/16/18	CDP (Levy)	No	IRS	CDP (Levy)
<i>Luniw v. Comm'r</i>	Docket No. 17789-16SL	3/8/18	CDP (Levy)	Yes	Split	CDP (Levy)
<i>Maccou v. Comm'r</i>	Docket No. 9101-16 L.	6/26/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Marcopolos v. Comm'r</i>	Docket No. 20069-16S	11/20/17	CDP (Lien)	Yes	IRS	CDP(Lien)
<i>Margous v. Comm'r</i>	Docket No. 21972-16	12/18/17	Affordable Care Act Premium Tax Credit	Yes	IRS	ACA; Other
<i>McCroy v. Comm'r</i>	Docket No. 1332-17W	5/2/18	Whistleblower Claim	Yes	IRS	Whistleblower Claims
<i>McFarland v. Comm'r</i>	Docket No. 8828-14 L	8/25/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>McGee v. Comm'r</i>	Docket No. 13535-16SL	9/29/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>McHenry v. Comm'r</i>	Docket No. 25427-16L	4/9/18	CDP (Lien)	No	IRS	CDP (Lien)
<i>McLeod v. Comm'r</i>	Docket No. 10651-16L	10/3/17	CDP; Innocent Spouse Relief; Accuracy Related Penalty	Yes	IRS	CDP, Innocent Spouse; Accuracy Related Penalty
<i>Meehan v. Comm'r</i>	Docket No. 23432-14 L	8/29/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Meintz v Comm'r</i>	Docket No. 25321-16	2/14/18	Underreported Income (Wages, State Income Tax Refund, Interest, and Unemployment); FTF: FTP; Estimated Tax Penalty	Yes	IRS	Gross Income; FTF; FTP; Estimated Tax Penalty
<i>Meissner v. Comm'r</i>	Docket No. 17628-17SL	1/31/18	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Minority Health Coalition of Marion Co, Inc., v. Comm'r</i>	Docket No. 27175-14 L	10/19/17	CDP (Levy, Lien)	Yes	IRS	CDP (Levy, Lien)
<i>Mitchell v. Comm'r</i>	Docket No. 26779-16L	12/5/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Mollica v. Comm'r</i>	Docket No. 9722-16	1/31/18	Disallowal of the EITC Because TP is an Inmate	Yes	IRS	Family Status Issues (EITC)
<i>Moore v. Comm'r</i>	Docket No. 4290-16 L.	6/2/17	CDP (Levy)	No	IRS	CDP (Levy)
<i>Morris &amp; McClimon, PLLC, v. Comm'r</i>	Docket No. 5710-17L	3/6/18	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Morris v. Comm'r</i>	Docket No. 31634-15 L.	6/1/17	CDP (Levy)	Yes	IRS	CDP (Levy)

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Case Name	Docket No.	Order Entered Date	Issue(s)	Pro Se	Decision	Corresponding MLI Topic
<i>Myhre v. Comm'r</i>	Docket No. 13381-17SL	4/20/18	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Neher v. Comm'r</i>	Docket No. 13338-17SL	2/1/18	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Nelson v. Comm'r</i>	Docket No. 1403-17 L	8/28/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Nitschke v. Comm'r</i>	Docket No. 22349-16 L	12/19/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Norris v. Comm'r</i>	Docket Nos. 6997-15; 7032-15; and 7033-15	11/21/17	Underreported Income; FTF; FTP; Estimated Tax Penalty	Yes	IRS	Gross Income; FTF; FTF; Estimated Tax Penalties
<i>Nortex Corp. v. Comm'r</i>	Docket No. 25126-14.	6/20/17	§ 162 Deductions	No	TP	Trade or Business
<i>Nylen v. Comm'r</i>	Docket Nos. 16237-16 and 17600-16	8/17/17	Casualty Losses	No	TP	Itemized Deductions
<i>Orc Partners, LLC, v. Comm'r</i>	Docket No. 1041-16.	6/15/17	Conservation Easements	No	TP	Charitable Contributions
<i>Orth v. Comm'r</i>	Docket No. 18049-16	10/11/17	Underreported Income; FTF; FTP; Estimated Tax	Yes	IRS	Gross Income; FTF & FTP Penalties; Estimated Tax Penalties
<i>Owens v. Comm'r</i>	Docket No. 20316-16 L	9/6/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Parikh v. Comm'r</i>	Docket No. 19875-16L	10/10/17	CDP (Levy)	Yes	IRS	CDP (Levy); Family Status Issues
<i>Peele v. Comm'r</i>	Docket No. 24260-16L	12/14/17	CDP	Yes	IRS	CDP
<i>Perez v. Comm'r</i>	Docket No. 7003-17L	1/24/18	CDP	Yes	IRS	CDP
<i>Perkins v. Comm'r</i>	Docket No. 31152-14 L.	6/27/17	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Perkins v. Comm'r</i>	Docket No. 28215-14	3/5/18	FTF Penalty	No	Split	FTF Penalty
<i>Perry v. Comm'r</i>	Docket No. 4309-17L	12/19/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Peterson v. Comm'r</i>	Docket No. 7964-17 L	11/29/17	CDP	Yes	IRS	CDP
<i>Peterson v. Comm'r</i>	Docket No. 24315-13L	1/8/18	CDP	Yes	IRS	CDP
<i>Phillips v. Comm'r</i>	Docket No. 14567-16	11/21/17	Failure to Pay Penalty; Sch. A Itemized Deductions	Yes	IRS	FTP: Itemized Deductions
<i>PNC, LLC v. Comm'r</i>	Docket No. 5397-16L	1/26/18	CDP (Levy)	Yes	Split	CDP (Levy)
<i>Preston v. Comm'r</i>	Docket No. 844-16SL	1/31/18	CDP	Yes	IRS	CDP

TABLE 11: Unpublished Tax Court Summary Judgment Orders

Case Name	Docket No.	Order Entered Date	Issue(s)	Pro Se	Decision	Corresponding MLI Topic
<i>Pro Advocate Grp. v. Comm'r</i>	Docket No. 10139-16	9/25/17	Accuracy Related Penalty	Yes	Split	Accuracy Related Penalty
<i>Promise Building Serv., Inc., v. Comm'r</i>	Docket No. 15619-16 L	9/20/17	CDP (Levy)	No	IRS	CDP (Levy)
<i>Ramirez v. Comm'r</i>	Docket No. 21263-16L	8/28/17	CDP (Levy)	No	IRS	CDP (Levy)
<i>Rasmussen v. Comm'r</i>	Docket No. 7428-17L	11/29/17	CDP	Yes	IRS	CDP
<i>Raufeisen v. Comm'r</i>	Docket No. 15700-17L	12/18/17	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Ray v. Comm'r</i>	Docket No. 12358-16 L	12/22/17	CDP (Lien)	Yes	TP	CDP (Lien)
<i>Reed v. Comm'r</i>	Docket No. 998-17SL	3/30/18	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Remy v. Comm'r</i>	Docket No. 25836-16	1/12/18	Failure to Timely File; 10% Penalty on a Premature Withdrawal from Retirement Plan	Yes	IRS	FTF Penalty
<i>Richfield v. Comm'r</i>	Docket No. 15380-16W	8/28/17	Whistleblower Action Under Code Section 7623(b)	Yes	IRS	Whistleblower Claims
<i>Robins v. Comm'r</i>	Docket No. 22753-16	12/21/17	Gross Income; Itemized Deductions	Yes	IRS	Gross Income; Itemized Deductions
<i>Sajewski v. Comm'r</i>	Docket No. 6711-17L	12/21/17	CDP	Yes	IRS	CDP
<i>Sampson v. Comm'r</i>	Docket No. 9635-16 L.	6/15/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Scanlon v. Comm'r</i>	Docket No. 478-16L	4/14/18	Estimated Tax Payments; Failure to Timely Pay	No	IRS	CDP (Levy, Lien); FTF Penalty; Estimated Tax Penalty
<i>Schaller v. Comm'r</i>	Docket No. 7318-17	2/8/18	Underreported Income (Wages & Unemployment Compensation)	Yes	IRS	Gross Income
<i>Scharetg v. Comm'r</i>	Docket No. 13280-16 L	9/27/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Sheridan v. Comm'r</i>	Docket No. 26611-16L	1/11/18	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Sielatycki v. Comm'r</i>	Docket No. 24204-16L	11/13/17	CDP: FTP; Innocent Spouse Relief	No	IRS	CDP (Lien, Levy); FTP: Innocent Spouse
<i>Solomon v. Comm'r</i>	Docket No. 2067-17SL	2/9/18	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Sonntag v. Comm'r</i>	Docket No. 21507-16L	12/19/17	CDP	Yes	IRS	CDP
<i>Stokely v. Comm'r</i>	Docket No. 10258-15 L	1/31/18	CDP (Levy)	No	IRS	CDP (Levy)

TABLE 11: Unpublished Tax Court Summary Judgment Orders

Case Name	Docket No.	Order Entered Date	Issue(s)	Pro Se	Decision	Corresponding MLI Topic
<i>Stokes v. Comm'r</i>	Docket No. 26048-16 L.	8/18/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Sunday Bumps, Inc., v. Comm'r</i>	Docket No. 11481-17L	3/30/18	CDP	No	IRS	CDP
<i>Swiader v. Comm'r</i>	Docket No. 13239-17L	3/6/18	CDP	Yes	IRS	CDP
<i>Tamkin v. Comm'r</i>	Docket No. 19560-16 L	11/15/17	CDP (Lien, Levy)	Yes	IRS	CDP (Lien, Levy)
<i>Taylor v Comm'r</i>	Docket No. 19243-16L	10/10/17	CDP	Yes	IRS	CDP
<i>Teelon v. Comm'r</i>	Docket No. 18830-16L	12/1/17	CDP	Yes	IRS	CDP
<i>Tesoriero v. Comm'r</i>	Docket No. 20335-16 L	8/25/17	CDP (Levy)	No	IRS	CDP (Levy)
<i>Toney v. Comm'r</i>	Docket No. 25496-16SL	4/24/18	CDP (Lien); Trust Fund Recovery Penalties	No	IRS	CDP (Lien); TFRP
<i>Triggs v. Comm'r</i>	Docket No. 9623-15 L	9/8/17	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Trupp v. Comm'r</i>	Docket No. 3770-16L	7/10/17	CDP (Levy, Lien)	Yes	IRS	CDP (Levy, Lien)
<i>Vest v. Comm'r</i>	Docket No. 23325-15 L	2/1/18	CDP (Levy)	No	IRS	CDP (Levy)
<i>Villanueva v. Comm'r</i>	Docket No. 25017-16L	12/19/17	CDP	Yes	IRS	CDP
<i>Villareal v. Comm'r</i>	Docket No. 767-16L	11/21/17	CDP	Yes	IRS	CDP
<i>Walker v. Comm'r</i>	Docket Nos. 16108-14 L and 9435-15 L	2/28/18	CDP	Yes	IRS	CDP
<i>Walker v. Comm'r</i>	Docket No. 27754-15 L.	6/22/17	CDP (Levy)	Yes	TP	CDP (Levy)
<i>Walton v. Comm'r</i>	Docket No. 18325-16	12/14/17	FTF; FTP; Additions to Tax	Yes	IRS	FTF; FTP: Estimated Tax Penalties
<i>Watkins v. Comm'r</i>	Docket No. 13023-16 L	9/6/17	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Wendt v. Comm'r</i>	Docket Nos. 14535-17S and 11366-17S	3/30/18	Education Expenses; Hope Scholarship Credit; Lifetime Learning Credit; American Opportunity Tax Credit (AOTC)	Yes	IRS	Itemized Deductions
<i>Wessels v Comm'r</i>	Docket No. 12536-16SL	10/25/17	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>West v. Comm'r</i>	Docket No. 22353-16L	1/31/18	CDP	Yes	IRS	CDP
<i>Whistleblower v. Comm'r</i>	Docket No. 23711-15W	3/23/18	Whistleblower Action Under Code Section 7623(b)	Yes	IRS	Whistleblower Claims
<i>Wimalasiri v. Comm'r</i>	Docket No. 1170-17L	1/31/18	CDP (Lien)	Yes	IRS	CDP (Lien)

TABLE 11: Unpublished Tax Court Summary Judgment Orders

Case Name	Docket No.	Order Entered Date	Issue(s)	Pro Se	Decision	Corresponding MLI Topic
<i>Winters v. Comm'r</i>	Docket No. 15600-16SL	1/3/18	CDP (Levy)	Yes	IRS	CDP (Levy)
<i>Woods v. Comm'r</i>	Docket No. 14521-16	12/29/17	Underreported Railroad Retirement Income	Yes	IRS	Gross Income
<i>Woods v. Comm'r</i>	Docket No. 25294-16S	4/20/18	Form 1099-C, Cancellation of Debt (COD) Income	Yes	IRS	Gross Income
<i>Works of Arts Enterprises, LLC v. Comm'r</i>	Docket No. 2287-17L	4/5/18	CDP (Lien)	Yes	IRS	CDP (Lien)
<i>Wright v. Comm'r</i>	Docket No. 20546-16 L.	6/29/17	CDP (Lien)	Yes	IRS	CDP (Lien)

TABLE 12: Unpublished Tax Court Bench Opinions

Case Name	Docket No.	Order Entered Date	Issue(s)	Pro Se	Decision	Corresponding MLI Topic
<i>Adams v. Comm'r</i>	30816-14	11/27/17	Trade or Business (Schedule A); Itemized Deductions; Accuracy-Related penalty	Yes	Split	Trade or Business; Itemized Deductions; Accuracy Related Penalty
<i>Akhavan v. Comm'r</i>	10353-17	4/26/18	Innocent Spouse Relief	Yes	TP	Innocent Spouse
<i>Anderson v. Comm'r</i>	4993-17S	02/26/218	IRA Distribution and 10% additional tax; Accuracy Related Penalty	Yes	IRS	Gross Income; Accuracy Related Penalty
<i>Asong-Morfaw v. Comm'r</i>	10629-14	11/21/17	Trade or Business Expenses (Vehicle Expenses); Depreciation	Yes	IRS	Trade or Business Expenses
<i>Bailey v. Comm'r</i>	5359-17S	4/17/17	Schedules A, Itemized Deductions; Schedules C, Profit or Loss From Business; Schedules E, Supplemental Income or Loss; FTF; Accuracy Related Penalty	Yes	IRS	Trade or Business; FTF Penalty; Accuracy Related Penalty
<i>Barrett v. Comm'r</i>	15404-16 L	11/13/17	Levy; CDP	Yes	IRS	CDP
<i>Bartig v. Comm'r</i>	3255-17S	2/15/18	Dependency Exemption; HOH Filing Status	Yes	TP	Family Status Issues
<i>Benavides v. Comm'r</i>	619-17S	2/16/18	Dependency Exemption; CTC; EITC	No	TP	Family Status Issues
<i>Binyon v. Comm'r</i>	23656-16S	11/6/17	Health Care Tax Credit	Yes	IRS	Health Care Tax Credit; Other
<i>Bishop v. Comm'r</i>	8716-13	10/18/17	Innocent Spouse Relief	Yes	IRS	Innocent Spouse Relief
<i>Blokhina v. Comm'r</i>	23205-15	1/5/18	Underreported Income; Accuracy Related Penalty	Yes	TP	Gross Income; Accuracy Related Penalty
<i>Bongam v. Comm'r</i>	20104-14 L	11/17/17	Lien; CDP; Trust Fund Recovery Penalty	Yes	IRS	CDP; Trust Fund Recovery Penalty
<i>Boring v. Comm'r</i>	4030-16S	3/9/18	Schedules C, Profit or Loss From Business; Accuracy Related Penalty	Yes	IRS	Trade or Business; Accuracy Related Penalty
<i>Boss v. Comm'r</i>	24303-16S	11/3/17	Moving Expense Deductions	Yes	IRS	Trade or Business
<i>Brauer v. Comm'r</i>	21000-16S	10/27/17	Special Rules for Noncustodial Parents; EITC; CTC	Yes	TP	Family Status Issues
<i>Brenner v. Comm'r</i>	24305-16S	11/21/17	IRA; Casualty Loss Deduction; Accuracy Related Penalty; Foreign Tax Credit (FTC)	Yes	IRS	Gross Income; Accuracy Related Penalty
<i>Burkhalter v. Comm'r</i>	14345-16 L	2/6/18	CDP; Levy	Yes	IRS	CDP (Levy)
<i>Butcher v. Comm'r</i>	8308-16S	4/5/18	Dependency; Accuracy Related Penalty	Yes	Split	Family Status Issues; Accuracy Related Penalty
<i>Cabinda v. Comm'r</i>	10949-16	11/15/17	Gross Income; FTF Penalty	Yes	IRS	Gross Income; FTF Penalty
<i>Caltech Consulting Serv. V. Comm'r</i>	22011-16	3/20/18	Business Expenses; Rental Expenses; Accuracy Related Penalty	Yes	IRS	Trade or Business; Accuracy Related Penalty

TABLE 12: Unpublished Tax Court Bench Opinions

Case Name	Docket No.	Order Entered Date	Issue(s)	Pro Se	Decision	Corresponding MLI Topic
<i>Cato v. Comm'r</i>	4698-17SL	11/30/17	Charitable Contribution; CDP; Levy	Yes	IRS	Charitable Contribution; CDP
<i>Chaney v. Comm'r</i>	8765-16	1/22/18	Schedule C Deductions; Itemized Deductions; Accuracy Related Penalty; IRA Distribution	Yes	IRS	Trade or Business; Itemized Deductions; Accuracy Related Penalty
<i>Clark v. Comm'r</i>	16376-16	11/9/17	HOH Status; EITC; ACTC	No	IRS	Family Status Issues
<i>Cunningham v. Comm'r</i>	22908-16S	2/16/18	Schedule C Profit and Loss from Business; FTF; Accuracy Related Penalty	Yes	Split	Trade or Business; FTF Penalty; Accuracy Related Penalty
<i>Cusack v. Comm'r</i>	6628-17S	4/5/18	Accuracy Related Penalty	Yes	IRS	Accuracy Related Penalty
<i>David v. Comm'r</i>	22230-16SL	3/12/18	CDP; Levy	Yes	IRS	CDP (Levy)
<i>Dennis v. Comm'r</i>	2853-17	3/1/18	Innocent Spouse Relief	No	Split	Innocent Spouse Relief
<i>Desameau v. Comm'r</i>	13344-16	11/28/17	Dependency	Yes	IRS	Family Status Issues
<i>Dixon v. Comm'r</i>	5250-17	2/20/18	Underreported Gross Income	Yes	IRS	Gross Income
<i>Dorival v. Comm'r</i>	20719-15S	6/26/17	Underreported Income; American Opportunity Credit	Yes	IRS	Gross Income; Itemized Deductions
<i>Dowd v. Comm'r</i>	14595-15	11/20/17	Schedule C Expenses; Trade or Business; Accuracy Related Penalty	Yes	IRS	Trade or Business; Accuracy Related Penalty
<i>Edwards v. Comm'r</i>	17386-16S	12/11/17	Schedule C, Profit or Loss from Business; Accuracy Related Penalty	Yes	Split	Trade or Business; Accuracy Related Penalty
<i>Ellis v. Comm'r</i>	15337-16S	4/20/18	Underreported Form 1099-C	Yes	IRS	Gross Income
<i>Eotvos v. Comm'r</i>	21450-16S	11/9/17	Trade or Business Expenses; Accuracy Related Penalty	Yes	IRS	Trade or Business; Accuracy Related Penalty
<i>Farha v. Comm'r</i>	15686-16	6/8/17	Underreported Income; Ordinary and Necessary Business Expense Deductions	Yes	IRS	Gross Income; Trade or Business
<i>Forde v. Comm'r</i>	1280-16	11/15/17	Capital Gains; Miscellaneous Expenses; Accuracy Related Penalty	Yes	IRS	Gross Income; Accuracy Related Penalty
<i>Fuller v. Comm'r</i>	14627-17S	5/21/18	Schedule A, Itemized Deductions; Accuracy Related Penalty	Yes	IRS	Trade or Business; Accuracy Related Penalty
<i>Garcia v. Comm'r</i>	4267-17	2/27/18	Dependency Exemption; HOH Filing Status	No	TP	Family Status Issues
<i>Garza v. Comm'r</i>	1310-16SL	10/5/17	CDP; Levy	No	IRS	CDP (Levy)
<i>Gentry v. Comm'r</i>	15580-17S	5/14/18	Unreimbursed Employee Business Expenses	Yes	IRS	Trade or Business
<i>Gonzalez v. Comm'r</i>	12309-16	1/5/18	Dependency Exemption	Yes	IRS	Family Status Issues

TABLE 12: Unpublished Tax Court Bench Opinions

Case Name	Docket No.	Order Entered Date	Issue(s)	Pro Se	Decision	Corresponding MLI Topic
<i>Gore v. Comm'r</i>	21499-16	2/9/18	Sch A, Itemized Deductions; Medical Expenses; Charitable Contributions; Schedule C Unreimbursed Business Expenses	Yes	IRS	Trade or Business; Itemized Deductions; Charitable Contributions
<i>Green Sustainable Packaging, Inc., v. Comm'r</i>	23692-15 L.	12/21/17	CDP; Lien; FTF and FTP Penalty; Interest Abatement	No	IRS	CDP; FTF/FTP Penalty
<i>Grignon v. Comm'r</i>	22930-16S	11/7/17	Gross Income from Settlement Proceeds; Accuracy Related Penalty	Yes	IRS	Gross Income; Accuracy Related Penalty
<i>Hadrami v. Comm'r</i>	11377-17S	5/21/18	Schedule C, Profit or Loss From Business	Yes	IRS	Trade or Business
<i>Harding v. Comm'r</i>	25577-16S	5/4/18	Dependency Exemption; Additional Child Tax Credit	Yes	TP	Family Status Issues
<i>Head v. Comm'r</i>	3796-17	11/7/17	Schedule C; Accuracy Related Penalty	Yes	IRS	Trade or Business; Accuracy Related Penalty
<i>Huffaker v. Comm'r</i>	9622-16 L	6/2/17	CDP; Levy; Frivolous Issues	Yes	IRS	CDP (Levy); Frivolous Issues
<i>Ink Nuts, LLC v. Comm'r</i>	16959-16 L.	11/13/17	CDP; Levy	No	IRS	CDP (Levy)
<i>Jackson v. Comm'r</i>	546-17S	12/6/17	Education Credit and American Opportunity Credit	Yes	Split	Itemized Deductions
<i>Jamison v. Comm'r</i>	8255-17S	4/4/18	Innocent Spouse Relief; Accuracy Related Penalty	Yes	IRS	Innocent Spouse Relief; Accuracy Related Penalty
<i>Johnson v. Comm'r</i>	3115-17S	1/23/18	Schedule E; Accuracy Related Penalty	Yes	Split	Trade or Business; Accuracy Related Penalty
<i>Jurek v. Comm'r</i>	21821-16S	1/3/18	Schedule A Vehicle Expenses	No	IRS	Trade or Business
<i>Katz v. Comm'r</i>	13587-16SL	12/15/17	CDP; Lien	Yes	IRS	CDP (Lien)
<i>Kraemer v. Comm'r</i>	11935-16S	4/4/18	Affordable Care Act Premium Assistance Credits	Yes	IRS	Other (ACA)
<i>Kurtenbach v. Comm'r</i>	4608-16S	4/10/18	Business Expenses	Yes	Split	Trade or Business
<i>Lai v. Comm'r</i>	5699-17S	2/15/18	Business Expenses; Charitable Contributions	Yes	Split	Trade or Business; Charitable Contributions
<i>Lange v. Comm'r</i>	11492-17 L	4/27/18	CDP; Levy; Underreported Income; Frivolous Issues	Yes	IRS	CDP (Levy); Gross Income; Frivolous Issues
<i>Levinson v. Comm'r</i>	2003-17S	12/11/17	IRA Distribution; Dividend Income; Social Security Annuity; Accuracy Related Penalty	Yes	Split	Gross Income; Accuracy Related Penalty
<i>Madrid v. Comm'r</i>	1947-17	3/9/18	EITC; Dependency Exemptions; CTC; Schedule C Business Income	Yes	IRS	Family Status Issues; Trade or Business
<i>Mahan v. Comm'r</i>	7491-16	3/20/18	Innocent Spouse Relief	Yes	IRS	Innocent Spouse

TABLE 12: Unpublished Tax Court Bench Opinions

Case Name	Docket No.	Order Entered Date	Issue(s)	Pro Se	Decision	Corresponding MLI Topic
<i>Majdalawi v. Comm'r</i>	18013-16S	6/26/17	Dependency Exemption Deduction; Head of Household Filing Status; EICT; American Opportunity Credit	Yes	IRS	Family Status Issues
<i>Matinez v. Comm'r</i>	22818-16S	11/8/17	Self-Employment Tax; EITC; ACTC; Trade or Business Expenses	Yes	Split	Trade or Business; Accuracy Related Penalty
<i>Medina v. Comm'r</i>	8585-16	1/31/18	Underreported Income; Accuracy Related Penalty	Yes	IRS	Gross Income; Accuracy Related Penalty
<i>Merrigan v. Comm'r</i>	24331-16S	2/20/18	Sch. C Profit and Loss from Business; Accuracy Related Penalty	Yes	IRS	Trade or Business; Accuracy Related Penalty
<i>Meyers v. Comm'r</i>	15974-16S	1/12/18	Schedule A Deductions; Charitable Contribution; Accuracy Related Penalty	Yes	Split	Trade or Business; Charitable Contribution; Accuracy Related Penalty
<i>Monge-Ramirez v. Comm'r</i>	1302-17S	12/21/17	HOH Status; Standard Deduction; Child Care Credit (CTC); Accuracy Related Penalty	Yes	Split	Family Status Issues; Accuracy Related Penalty
<i>Morgan v. Comm'r</i>	14362-16	11/28/17	Affordable Care Act Premium Assistance Credits; IRA Distribution	Yes	IRS	Gross Income; Other
<i>Morgan v. Comm'r</i>	7695-17S	4/27/18	Itemized Deductions: Travel Expenses; Charitable Contribution	Yes	Split	Trade or Business; Itemized Deduction; Charitable Contribution
<i>Morsi v. Comm'r</i>	15920-16S	4/27/18	Substantial Understatement of Income	Yes	IRS	Accuracy Related Penalty
<i>Muhammad v. Comm'r</i>	23891-15	10/5/17	Interest Income; Dependent Exemption Deduction; HOH status; AOC; Charitable Contribution; Schedule C Business Expenses; Accuracy Related Penalty	Yes	Split	Charitable Contribution; Accuracy Related Penalty; Family Status Issues
<i>Munchus v. Comm'r</i>	13698-16	2/15/18	Schedule C Business Expenses; Accuracy Related Penalty	Yes	IRS	Trade or Business; Accuracy Related Penalty
<i>Nguyen v. Comm'r</i>	4556-16	11/9/17	Cancellation of Debt (COD) Income; Schedule C	Yes	IRS	Trade or Business; Gross Income
<i>Omebe v. Comm'r</i>	18522-17S	5/14/18	Dependency Exemptions; HOH Filing Status; EITC; CTC	Yes	IRS	Family Status Issues
<i>Orrick v. Comm'r</i>	16372-16S	10/19/17	Schedule C; Profit or Loss from Business; Accuracy Related Penalty	Yes	IRS	Trade or Business, Accuracy Related Penalty
<i>Pace v. Comm'r</i>	11308-14	1/25/18	Understatement; Addition to Tax	Yes	IRS	Accuracy Related Penalty
<i>Padilla v. Comm'r</i>	733-17	3/22/18	Innocent Spouse Relief	No	IRS	Innocent Spouse
<i>Palsgaard v. Comm'r</i>	2103-17S	1/5/18	Underreported Social Security Disability Benefits	Yes	IRS	Gross Income

TABLE 12: Unpublished Tax Court Bench Opinions

Case Name	Docket No.	Order Entered Date	Issue(s)	Pro Se	Decision	Corresponding MLI Topic
<i>Parella v. Comm'r</i>	823-17 L	3/20/18	CDP; Lien	Yes	IRS	CDP (Lien)
<i>Porch v. Comm'r</i>	4273-16	1/3/18	Itemized Deductions	Yes	Split	Itemized Deductions
<i>Pro Advocate Grp. V. Comm'r</i>	10139-16	11/17/17	Trade or Business Expense Deductions; Accuracy Related Penalty	Yes	IRS	Trade or Business; Accuracy Related Penalty
<i>Pugh v. Comm'r</i>	20323-16S	6/12/17	Dependency Exemption Deduction; Child Tax Credit; Education Expenses	Yes	IRS	Family Status Issues, Itemized Deductions
<i>Pulsipher v. Comm'r</i>	5409-17S	2/15/18	Schedule C Profit or Loss from Business; Accuracy Related Penalty	Yes	Split	Trade or Business; Accuracy Related Penalty
<i>Rankin v. Comm'r</i>	12237-17 L	3/29/18	CDP; Lien	No	IRS	CDP (Lien)
<i>Reffle v. Comm'r</i>	3562-17	3/20/18	Dependency Exemption Deduction; HOH Filing Status; EITC	Yes	IRS	Family Status Issues
<i>Sadighim v. Comm'r</i>	24342-16S	12/6/17	Accuracy Related Penalty; FTF Penalty; U/R Unemployment Compensation; Schedule C Profit or Loss From Business	Yes	Split	Gross Income; Trade or Business; FTF Penalty; Accuracy Related Penalty
<i>Sandoval v. Comm'r</i>	10400-17	3/29/18	Schedule C Expenses; Accuracy Related Penalty	Yes	Split	Trade or Business; Accuracy Related Penalty
<i>Sardy v. Comm'r</i>	12573-17S	4/5/18	Schedule C; Accuracy Related Penalty	Yes	TP	Trade or Business; Accuracy Related Penalty
<i>Schafer v. Comm'r</i>	21152-16S	10/23/17	Dependency Exemption Deduction; HOH Status	Yes	IRS	Family Status Issues
<i>Solutus, LLC v. Comm'r</i>	29600-13	11/14/17	Final Partnership Administrative Adjustment (FPAA); TEFRA; Accuracy Related Penalty	Yes	IRS	Partnership Issues; Accuracy Related Penalty
<i>Sorrentino v. Comm'r</i>	2967-17 L.	1/16/18	CDP; Levy	Yes	TP	CDP (Levy)
<i>Stevens v. Comm'r</i>	6114-16	6/2/17	Early retirement distribution; 10% additional tax on premature distribution	Yes	IRS	Gross Income
<i>Tagal v. Comm'r</i>	21565-16	6/19/17	Schedule C; Independent Contractor or Employee Determination	Yes	IRS	Trade or Business Expenses
<i>Tarverdyan v. Comm'r</i>	16652-16S	11/8/17	Schedule A; Accuracy Related Penalty	Yes	IRS	Trade or Business; Accuracy Related Penalty
<i>Tizcareno v. Comm'r</i>	14577-16S	1/5/18	COD; Discharge of Indebtedness Income	Yes	TP	Gross Income
<i>Toler v. Comm'r</i>	14297-17 L	3/29/18	CDP; Lien	Yes	TP	CDP (Lien)

TABLE 12: Unpublished Tax Court Bench Opinions

Case Name	Docket No.	Order Entered Date	Issue(s)	Pro Se	Decision	Corresponding MLI Topic
<i>Touchard v. Comm'r</i>	14013-15	4/30/18	Schedule C Expenses; Itemized Deductions; Accuracy Related Penalty; FTF Penalty	Yes	Split	Trade or Business; FTF Penalty; Itemized Deductions; Accuracy Related Penalty
<i>Tyz v. Comm'r</i>	14141-17 L.	3/29/18	CDP; Levy; FTP Penalty	Yes	Split	CDP (Levy); Failure to Pay penalty
<i>Van Ermen v. Comm'r</i>	23364-16	4/2/18	Underreported Income; Moving Expenses; Accuracy Related Penalty	Yes	IRS	Gross Income; Trade or Business; Accuracy Related Penalty
<i>Wahlin v. Comm'r</i>	23108-16S	2/23/18	Interest Deduction on Schedule E; Supplemental Income and Loss; Accuracy Related Penalty	Yes	Split	Trade or Business; Accuracy Related Penalty
<i>Wallace v. Comm'r</i>	16860-16S	11/22/17	Cancellation of Indebtedness (COD); Filing Status; Dependency Exemptions; EITC; Itemized Deductions; Education Credits	Yes	IRS	Family Status Issues; Gross Income
<i>Weber v. Comm'r</i>	760-17	1/3/18	Underreported Income; Accuracy Related Penalty	Yes	IRS	Gross Income; Accuracy Related Penalty
<i>Wendt v. Comm'r</i>	11366-17S, 14535-17S	3/30/18	Tuition and Fees Deduction	Yes	IRS	Itemized Deductions
<i>Whitney v. Comm'r</i>	15383-16	12/1/17	Dependency Exemption	Yes	IRS	Family Status Issues
<i>Wilson v. Comm'r</i>	1233-17	12/19/17	Dependency Exemption; Child Tax Credit (CTC)	No	IRS	Family Status Issues
<i>Wilson v. Comm'r</i>	3669-17S	12/13/17	Dependency Exemption	Yes	TP	Family Status Issues
<i>Zschau v. Comm'r</i>	9285-17S	4/4/18	Accuracy Related Penalty	Yes	IRS	Accuracy Related Penalty

## Appendix 4: Taxpayer Advocate Service Directory

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