

Area of
Focus #7**Additional Requirements for Appeals Access and Compressed Case Timelines Impair the Fundamental Rights of Taxpayers****TAXPAYER RIGHTS IMPACTED¹**

- *The right to appeal an IRS decision in an independent forum*
- *The right to a fair and just tax system*
- *The right to pay no more than the correct amount of tax*

The IRS Office of Appeals recently implemented the Appeals Judicial Approach and Culture (AJAC) project in hopes of enhancing “internal and external customer perceptions of a fair, impartial, and independent Office of Appeals.”² AJAC’s stated intent is to reinforce Appeals’ mission of administrative dispute resolution by clarifying and separating the negotiation and decision-making role of Appeals from the factual investigations and case development allocated to the Examination and Collection functions.³ For example, under AJAC, whenever taxpayers raise new issues or present additional evidence requiring further investigation, Appeals generally will send cases back to the Compliance function (Compliance) for development and evaluation.⁴

Unfortunately, Compliance has used AJAC to adopt a more stringent policy with respect to Information Document Requests (IDRs) and to close cases and bypass Appeals unless a taxpayer provides all requested documentation or certifies no additional information is available.⁵ For example, Letter 5262 was revised, over TAS’s objections, to read, “If you don’t provide the information requested on the enclosed Form 4564 or contact me to confirm you have no additional information to provide by the response due date listed above, we will close your examination based on the information we have now. If you don’t agree, you won’t be able to appeal within the IRS before we issue a notice of deficiency.”⁶

While the IRS agreed to discontinue the use of this letter after the National Taxpayer Advocate brought it to the attention of senior leadership, the creation of any additional obstacles or absolute prohibitions

1 See IRS, Taxpayer Bill of Rights, available at <http://www.irs.gov/Taxpayer-Bill-of-Rights>.

2 IRS, Internal Guidance Memo (IGM) AP-08-0714-0005, *Implementation of the Appeals Judicial Approach and Culture (AJAC) Project, Collection – Phase 2* (July 10, 2014).

3 IRS, *Reinforcing Appeals’ Philosophy: Appeals Judicial Approach and Culture (AJAC) Talking Points*, July 2, 2014, available at <http://appeals.web.irs.gov/about/ajac.htm>. Appeals states that AJAC is intended to emphasize its “quasi-judicial” nature. According to Black’s Law Dictionary, “quasi-judicial” is a term not easily definable, but generally connoting, “of, relating to, or involving an executive or administrative official’s adjudicative acts.” Black’s Law Dictionary (9th ed. 2009). Appeals’ use of the term “quasi-judicial” is apparently intended to distinguish factual investigations allocated to the Examination or Collection functions from dispute resolution activities on which Appeals would like to focus.

4 IRM 8.6.1.6.2, *General Guidelines* (Nov. 14, 2013). Compliance will be used hereafter as a collective term to refer to the Examination and Collection functions within the Small Business/Self-Employed Division (SB/SE) and the Wage & Investment Division (W&I). To the extent a portion of the discussion is limited to a particular IRS operating division, that division will be specifically referenced.

5 TAS is primarily aware of this practice arising within the SB/SE Examination function. TAS Elevated Issue Conference with SB/SE (July 30, 2014).

6 Letter 5262, *Examination Report Transmittal - Additional Information Due (Straight Deficiency)* (Aug. 2014); IRM 4.10.8.11, *Eligibility for Appeals Conference and Preliminary Letters (SB/SE Field and Office Examiners only)* (Sept. 12, 2014). Note: The referenced Statutory Notice of Deficiency (SNOD) would allow the taxpayer 90 days to appeal the IRS determination to the U.S. Tax Court.

to an appeal within the IRS under the guise of AJAC has many troubling aspects.⁷ As a threshold matter, Compliance should not stand as the gatekeeper to Appeals; Appeals, not Compliance, should determine its own jurisdiction. Compliance cannot be allowed to sit as both judge and jury in deciding whether IRS information requests are reasonable and whether some lesser degree of information or alternative form of substantiation might be sufficient to allow taxpayers to establish their cases, either in whole or in part. Moreover, a telephone call from a taxpayer confirming no additional information is available leaves the IRS identically situated to where it would be if the same taxpayer failed to respond to the IDR at all.⁸ Yet the outcomes are fundamentally different: in the first scenario, the taxpayer will be able to exercise his or her right to go to Appeals, while in the second, the same taxpayer will be barred from exercising that right.

When TAS objected to this policy, Compliance initially replied it expected mistakes would be made and the approach was subject to a learning curve, but the policy was consistent with AJAC.⁹ Fundamental appeal rights should not be so easily, and possibly inadvertently, forfeited by taxpayers and arbitrarily overridden by the IRS.¹⁰

Access to Appeals is crucial for several reasons. For example, Appeals considers evidence Compliance generally does not take into account. Among other things, Appeals will accept affidavits and weigh oral testimony. Further, Appeals, unlike Compliance, has the ability to settle cases based on the hazards of litigation.¹¹ Appeals will also seek to negotiate a case resolution with the taxpayer based on the existing factual record even if those facts are incomplete or not thoroughly documented. This policy, clarified by Appeals as part of AJAC, is contradicted and undercut by the approach Compliance now follows. For many taxpayers, the Compliance policy could prevent their cases from ever even reaching Appeals before the IRS automatically issues a SNOD.¹²

Another important settlement tool possessed by Appeals but not available in Compliance is application of the *Cohan* rule.¹³ *Cohan*, which originally developed via judicial case law, allows the fact finder to estimate deductible expenses where the fact of those expenses, although not their amount, can be substantiated.¹⁴ The *Cohan* rule, along with other settlement vehicles employed by Appeals, is an integral aspect

7 This agreement would need to be implemented by a revision to IRM 4.10.8.11, *Eligibility for Appeals Conference and Preliminary Letters (SB/SE Field and Office Examiners only)* (Sept. 12, 2014). In the meantime, SB/SE issued a June 9, 2015 memorandum temporarily suspending the use of Letter 5262, *Examination Report Transmittal - Additional Information Due (Straight Deficiency)*; Letter 5261, *Examination Report Transmittal - Additional Information Due (Claims for Refund)*; Letter 5441, *Response to Letter 5262 - Straight Deficiency*; and Office of Examination's use of Letter 950, *30 Day Letter - Straight Deficiency*. The memorandum addresses only those cases still open in SB/SE and does not contemplate any relief for taxpayers whose cases were closed using these suspended letters. TAS urges SB/SE to make this suspension permanent, to revise the policies that led to the issuance of these letters, and to work with TAS, Appeals, and others within the IRS to develop relief measures for taxpayers who have been denied access to Appeals through the policies embodied in these letters.

8 In many situations, this failure to respond could be attributable to circumstances beyond taxpayers' control, such as mail failures, health issues, or extended travel. Further, the required affirmation that the requested information does not exist ignores the possibility taxpayers may possess the information but may have objections to the scope, relevance, or legality of some of the information sought by the IDR.

9 TAS Elevated Issue Conference with SB/SE (July 30, 2014).

10 Such cases generally can be returned to Appeals by the U.S. Tax Court after a petition is filed in response to the SNOD. Nevertheless, this indirect approach ignores the unnecessary administrative burdens and overall stress to which taxpayers are subjected and the additional costs incurred by both taxpayers and the government.

11 IRM 8.6.2.5.4.2, *Resolved Based on Hazards of Litigation* (Oct. 18, 2007).

12 IRM 8.6.1.6.2 (2), *General Guidelines* (Nov. 14, 2013).

13 See *Cohan v. Comm'r*, 39 F.2d 540 (2d Cir. 1930).

14 The *Cohan* rule cannot be used in situations where IRC § 274(d) applies. Section 274(d) provides that unless a taxpayer complies with strict substantiation rules, no deductions are allowable for certain travel, entertainment, and other specified expenses.

of the voluntary compliance system and cannot be abridged without impairing the fundamental equity and effectiveness of that system.

Compliance's approach, which is wrong in principle, is made worse in practice by the compressed timelines it needlessly imposes on taxpayers before issuing the SNOD. In the typical SB/SE field examination, taxpayers receive an initial letter that includes an information request. In the event taxpayers do not respond within ten days, they are sent a second letter in the 5262 series demanding all requested information and threatening the loss of appeal rights if they do not provide the information or inform the IRS it is unavailable. If the 15-day period also elapses, or if the IRS is unsatisfied with the taxpayer's response, the SNOD is issued and Appeals is bypassed. As noted above, this practice was recently suspended, but it should be permanently revised so as to avoid confusion in the short run and resumption in the long run.

TAS has received comments from some tax practitioners who believed they were working with Compliance to provide information and resolve a case, only to be surprised by the unexpected arrival of a SNOD, effectively ending all current administrative dialogue with the IRS.¹⁵ In a recent op-ed piece from the *New York Times*, a tax practitioner observed that if the compressed time frames are not adhered to, "the consequences may be dire" and that "I could return home from a vacation or a stay in the hospital to find not only that I am being audited, but that my audit has already been closed and sent to the notice of deficiency unit."¹⁶ Core taxpayer rights, such as *the right to appeal an IRS decision in an independent forum*, *the right to a fair and just tax system*, and *the right to pay no more than the correct amount of tax*, which recently have been acknowledged and adopted by the IRS, mean little if the IRS implements policies impairing those rights.¹⁷

In some situations AJAC is being used as an instrument for limiting taxpayers' access to Appeals or coercing them into taking steps not in their best interests.

Further, according to some practitioners, Compliance has been using AJAC as a tool for "bullying" taxpayers in other circumstances.¹⁸ TAS has received some reports that Compliance, under the vague but broad cloak of AJAC, has aggressively been demanding taxpayers sign waivers of the statute of limitations on assessment, extending it for one to two years. These demands have been made even in cases where taxpayers have only sought a slight extension of time from the IRS to provide requested documents and where sufficient time remained under the existing statute of limitations for the case to be transferred to Appeals.¹⁹ The use of procedural leverage by the IRS to intimidate taxpayers, to threaten premature case closures, and to jeopardize taxpayers' access to Appeals is inconsistent with AJAC's avowed purpose.

AJAC has been promoted as having the goal of enhancing "external customer perceptions of a fair, impartial, and independent Office of Appeals."²⁰ However, in some situations AJAC is being used as an instrument for limiting taxpayers' access to Appeals or coercing them into taking steps not in their best interests.

15 TAS conference call with Low Income Tax Clinics practitioners (Apr. 22, 2015). The information gleaned from this and other similar TAS conference calls is anecdotal and cannot be taken as systemic proof or statistical evidence. Nevertheless, it is consistent with broader impressions formed by TAS from widespread interactions with taxpayers and their representatives.

16 David DuVal, *Beware the I.R.S.'s Speeded-Up Audit*, N.Y. TIMES, Apr. 29, 2015, available at http://www.nytimes.com/2015/04/30/opinion/beware-the-irss-speeded-up-audit.html?emc=eta1&_r=0.

17 See IRS, Taxpayer Bill of Rights, available at <http://www.irs.gov/Taxpayer-Bill-of-Rights>.

18 TAS conference call with practitioners associated with the American Bar Association Section of Taxation (Mar. 17, 2015).

19 *Id.* Generally, 365 days must be remaining on the statute of limitations for Appeals to accept a proposed deficiency case. IRM 8.21.3.1.1, *New Receipts and Transfers* (Aug. 28, 2014).

20 IRS, IGM AP-08-0714-0004, *Implementation of the Appeals Judicial Approach and Culture (AJAC) Project, Examination and General Matters - Phase 2* (July 2, 2014).

FOCUS FOR FISCAL YEAR 2016

- Provide guidance to TAS employees on how to advocate for taxpayers whenever AJAC is used to impair, rather than perpetuate, taxpayer rights;
- Issue Taxpayer Assistance Orders, where appropriate, to protect taxpayers' right to appeal;
- Educate internal and external stakeholders regarding the impact on taxpayers of AJAC implementation by Compliance and Appeals; and
- Advocate with the IRS to revise AJAC-related policies whenever those policies impose burdens on taxpayers and limit their rights.