

**MSP
#18****APPEALS: The IRS's Decision to Expand the Participation of Counsel and Compliance Personnel in Appeals Conferences Alters the Nature of Those Conferences and Will Likely Reduce the Number of Agreed Case Resolutions****RESPONSIBLE OFFICIALS**

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TAXPAYER RIGHTS IMPACTED¹

- *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

Effective October 2016, Appeals implemented a number of changes to its conference procedures. Among other things, Appeals revised the Internal Revenue Manual (IRM) to allow Hearing Officers to invite Counsel and/or Compliance to participate in Appeals conferences.² The ability to invite these additional participants exists regardless of whether taxpayers agree or object to their inclusion.

Appeals' option to involve Counsel and Compliance in such conferences has historically existed and occasionally has been used in selected cases by Hearing Officers.³ Appeals, however, views the IRM changes as part of a new and concerted trend toward expanded participation in Appeals proceedings by IRS personnel.⁴ As one example, effective May 1, 2017, Appeals began a pilot initiative designed to make the inclusion of representatives from the Large Business and International (LB&I) examination audit team a matter of "routine."⁵ Donna Hansberry, Chief of Appeals, has stated that "the purpose of having both parties in the room is to aid case resolution."⁶ Appeals further explains, "The goals for this initiative are to improve conference efficiency, reach case resolution sooner, and offer earlier certainty for issues in future years."⁷

Nevertheless, this change in conference procedures could have far-reaching negative consequences for Appeals' effectiveness in resolving cases with taxpayers. This potential downside is why a number of tax practitioner groups have expressed opposition to such a policy: "There should be a clean break between

1 See Taxpayer Bill of Rights (TBOR), www.TaxpayerAdvocate.irs.gov/taxpayer-rights. The rights contained in the TBOR are now listed in the Internal Revenue Code (IRC). See Consolidated Appropriations Act, 2016, Pub. L. No. 114-113, Division Q, Title IV, § 401(a) (2015) (codified at IRC § 7803(a)(3)).

2 Internal Revenue Manual (IRM) 8.6.1.4.4, *Participation in Conferences by IRS Employees* (Oct. 1, 2016).

3 Chelsea Looper-Stockwell, *Sitting Down with Appeals Chief, Donna Hansberry*, APPEALS QUARTERLY NEWSLETTER VOL. 3, ISSUE 1 1-2 (Feb. 2017).

4 *Id.*

5 *Appeals Team Cases: All Parties Conferences*, <https://www.irs.gov/pub/irs-utl/atclfaqs.pdf> (last visited Apr. 17, 2017).

6 *IRS Appeals Conference Procedure Change Follows Prior Guidance*, 2017 TNT 53-4 (Mar. 20, 2017).

7 *Id.*

Compliance and Appeals.”⁸ Appeals runs the risk that Hearing Officers could be perceived as part of a contingent representing the IRS in a “quasi-judicial” regime that fosters distrust and litigation, rather than negotiation and case resolution.

Specifically, the National Taxpayer Advocate is concerned that Appeals’ emphasis on expanding participation of Counsel and Compliance in Appeals conferences will:

- Fundamentally change the nature of Appeals conferences in which this approach is adopted;
- Jeopardize Appeals’ independence, both real and perceived; and
- Generate additional costs for the government and taxpayers in the form of fewer case resolutions, additional litigation, and reduced long-term compliance.

ANALYSIS

Background

Most cases brought by taxpayers to Appeals come directly from Compliance after taxpayers and Compliance reach an impasse.⁹ In these cases, the Hearing Officer receives the administrative file, which includes the taxpayer’s protest, the revenue agent’s report, and a transmittal memorandum prepared by Compliance.¹⁰ Upon receipt, Appeals reviews the administrative file to ensure completeness and to determine whether the case has been sufficiently prepared for potential disposition. If it has not, the case is to be returned to Compliance for further development under the terms of the Appeals Judicial Approach and Culture (AJAC) Project adopted in 2014.¹¹

Assuming that the case is ready for Appeals’ consideration, the Hearing Officer can invite Compliance and the taxpayer to a pre-conference meeting. The purpose of such a meeting is to discuss the issues of the case, the taxpayer’s protest, and the rebuttal prepared by Compliance.¹² Pre-conferences generally are used in more complex cases.¹³

Once a pre-conference is held or bypassed, the Appeals conference itself is scheduled. The conference is conducted informally and, in practice, is often conducted in stages.¹⁴ Taxpayers present their case, enter into dialogue with the Hearing Officer, and eventually commence settlement negotiations.¹⁵ Although Appeals strives to resolve cases after a single conference, additional conferences can be conducted where necessary.¹⁶

As the final administrative stop for most taxpayers within the IRS, Appeals’ role is to negotiate settlements with taxpayers in light of existing hazards of litigation to the government.¹⁷ This function, in which

⁸ ABA Members Comment on Recent Appeals Division Practice Changes, 2017 TNT 89-10 (May 10, 2017).

⁹ Appeals response to TAS information request (June 9, 2017), Tab 3. This category of cases is known as nondocketed Appeals. The other category, docketed Appeals, consists of cases that bypass Appeals on their way to the U.S. Tax Court and then are remanded to Appeals for further consideration.

¹⁰ MICHAEL I. SALTZMAN & LESLIE BOOK, IRS PRACTICE AND PROCEDURE 9.06 (2016).

¹¹ *Id.*

¹² IRM 8.7.11.8.1, *Purpose of Pre-Conference Meeting* (Mar. 16, 2015).

¹³ IRM 8.7.4.5, *Pre-Conferences in Estate and Gift Tax Cases* (Aug. 18, 2014).

¹⁴ IRM 8.6.1.4(5), *Conference Techniques used by Appeals Technical Employees (ATEs)* (Oct. 1, 2016).

¹⁵ MICHAEL I. SALTZMAN & LESLIE BOOK, IRS PRACTICE AND PROCEDURE 9.06 (2016).

¹⁶ *Id.*

¹⁷ IRM 8.6.2.6.4.2, *Resolved Based on Hazards of Litigation* (Oct. 18, 2007).

By definition, if taxpayers had been able to reach agreement with Counsel and Compliance, the case would not have been elevated to Appeals in the first place.

Appeals serves as the ultimate decision-maker, is different from mediation and similar types of alternative dispute resolution (ADR) in which an independent third party seeks to facilitate an agreement between adversaries with opposing positions.¹⁸ For example, in IRS mediation, which is voluntary, Compliance has a seat at the table, and Appeals attempts to facilitate a resolution that becomes binding only if Compliance and the taxpayer agree.¹⁹

By contrast, prior to Appeals' 2016 guidance changes, Counsel and Compliance generally did not attend Appeals conferences, although the IRS always had the right to include them.²⁰ Counsel and Compliance typically were granted their say via the case file and the pre-conference, if held. Thereafter, the Appeals conference itself generally was devoted to presentation of the taxpayer's case and settlement negotiations between the taxpayer and the Hearing Officer.

The manner in which Appeals will implement its new emphasis on including Counsel and Compliance in conferences is still somewhat vague. TAS has been assured that neither Counsel nor Compliance will be present during settlement negotiations between Hearing Officers and taxpayers.²¹ Nevertheless, in her comments before the U.S. House Ways and Means Committee, Subcommittee on Oversight, one practitioner testified as follows:

In a recent settlement conference with my client, the Appeals personnel openly asked Compliance what they thought was a fair settlement before reaching a final decision. After the conference, the taxpayer asked how it was possible for Appeals to maintain independence when they were seeking the opinion of the Compliance team.²²

Participation of Additional IRS Personnel Will Fundamentally Change the Nature of Appeals Conferences

The expansion of Appeals conferences to routinely involve Counsel and Compliance alters the relationship between the taxpayer and the Hearing Officer and makes interactions less negotiation-based.

By definition, if taxpayers had been able to reach agreement with Counsel and Compliance, the case would not have been elevated to Appeals in the first place. The inclusion of these now-contentious parties in an Appeals proceeding likely will create a dynamic in which the opposing sides present their arguments and then await the ruling of the Hearing Officer. While this model may well move closer to the

18 For an in-depth discussion of alternative dispute resolution (ADR) within the IRS, see National Taxpayer Advocate 2016 Annual Report to Congress 211-19.

19 IRM 8.26.3.1, *Objective and Authority for Fast Track Mediation* (Dec. 5, 2014); IRM 8.26.3.2, *Collaborative Dispute Resolution Process* (Dec. 5, 2014).

20 Chelsea Looper-Stockwell, *Sitting Down with Appeals Chief, Donna Hansberry*, APPEALS QUARTERLY NEWSLETTER VOL. 3, ISSUE 1 1-2 (Feb. 2017).

21 Appeals response to TAS fact check request (Nov. 13, 2017).

22 *IRS Reform: Resolving Taxpayer Disputes: Hearing Before the Subcomm. on Oversight of the H. Comm. on Ways and Means*, 225th Cong. (2017) (statement of Chastity K. Wilson, Am. Inst. Cert. Pub. Accts.).

“quasi-judicial” role for Hearing Officers envisioned by AJAC, it is neither an effective means of reaching a settlement in a particular case, nor of pursuing administrative dispute resolution on a broader scale.

Appeals should be sitting across the table from taxpayers with a complete file, based on which administrative case resolution can be sought. Anything that Compliance would have to say at that point would be redundant or, if new, would contradict the principles of AJAC. If Appeals is receiving incomplete case files, the solution is to insist on better case development from Compliance, not to expand its participation in Appeals conferences so that it can present verbally what should already have been provided in writing. Rather than confronting and resolving this issue directly, Appeals’ new approach simply creates more problems.

For example, this change, which allows Counsel and Compliance to reiterate their positions, converts Appeals to a more adversarial forum, and will limit negotiation between taxpayers and Hearing Officers. “Adding IRS employees to the Appeals conference turns the Appeals conference into more of a trial setting as opposed to the historic conduct of most Appeals conferences.”²³

As discussed above, the National Taxpayer Advocate has been assured by the Chief of Appeals that Counsel and Compliance will not be a party to the settlement discussions, which theoretically would occur later in the conference.²⁴ Even if that is the case, the entire Appeals conference can be accurately characterized as a settlement negotiation in which taxpayers and their representatives are attempting to establish a rapport with their Hearing Officer from which resolution of their case can be mutually explored.

When Counsel and Compliance are given a second opportunity and essentially allowed to present an oral argument setting forth their case, of which the Hearing Officer should already be aware, this in turn drives taxpayers and their representatives to present their own oral arguments. Aspects of the case in which the parties could reach agreement should previously have been addressed in the examination or even uncovered at an Appeals pre-conference. Including Counsel and Compliance in the Appeals conference itself deters, and runs the risk of poisoning the environment for, the meaningful dialogue between taxpayers, representatives, and the Hearing Officer, based on which resolution can occur.

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²³ Marie Sapirie, *IRS Appeals Chief Clarifies Policy Changes in Open Letter*, 2016 TNT 215-5 (Nov. 14, 2016).

²⁴ National Taxpayer Advocate Blog, *Appeals Should Facilitate Mutual Respect and Trust by Allowing Taxpayers a Choice in the Expanded Participation of Counsel and Compliance in Appeals Conferences* (June 21, 2017), <https://taxpayeradvocate.irs.gov/news/appeals-should-facilitate-mutual-respect-and-trust-by-allowing-taxpayers-a-choice-in-the-expanded-participation-of-counsel-and-compliance-in-appeals-conferences?category=Tax%20News>.

Expanding Conferences Will Jeopardize Appeals' Independence, Both Real and Perceived

Appeals recognizes that the achievement of its mission statement depends on resolving tax controversies on a basis that is fair and impartial to both the government and the taxpayer and in a manner that will enhance public confidence in the integrity and efficiency of the IRS.²⁵ Nevertheless, this initiative fundamentally imperils Appeals' ability to fulfill its mission and equitably settle cases.

Inviting Counsel and Compliance to attend conferences will make it difficult for Appeals to serve as an unbiased participant in the case resolution process. Compliance will be in a position to put pressure on Hearing Officers to adopt and sustain the prior asserted outcome and will have the opportunity to directly counter the arguments of taxpayers. As a practical matter, Compliance presumably will be granted a much broader latitude for extending arguments in person beyond the parameters existing within the four corners of the case file.

Where the views of Counsel are concerned, Revenue Procedure 2012-18 provides Appeals with the discretion to override Counsel. In reality, however, Hearing Officers may well be reluctant to do so when Counsel actually has a seat at the table.²⁶ A Hearing Officer may lack the personal confidence or the institutional support necessary to stand firm in exercising independent judgment in the face of opposition from Compliance regarding the factual strengths and weaknesses or the assessment of Counsel regarding hazards of litigation.²⁷ By inviting these parties to conferences as a routine matter, Appeals is undermining its own independent mechanisms for case resolution.

As has the National Taxpayer Advocate, the American Bar Association Section of Taxation has expressed concerns that "Appeals' independence is impaired by permitting, encouraging, or mandating that all three parties (Appeals employees, the taxpayer, and Compliance/Counsel personnel) attend all conferences with Appeals. Moreover, such a significant change in conference procedures could interfere with the ability of Appeals to conduct its traditional role of settling the case based on hazards of litigation."²⁸

Including all three parties in the Appeals conference may appear sensible, and tax practitioners sometimes find this approach to be helpful in resolving cases.²⁹ Mandating this inclusion, however, fundamentally disregards the very purpose of the Appeals conference, which is neither to give Compliance another bite at the apple nor to transform Appeals into a mediation forum. Instead, the credibility of Appeals hinges on its ability to undertake direct and independent settlement negotiations with taxpayers and their representatives.

Even if Appeals is able to generate case resolutions that are unbiased, the necessary perception of independence will inevitably be compromised by Appeals' new approach. Additional IRS participants cannot help but alter taxpayers' perception of the proceedings and the fairness of the outcomes. Taxpayers will not feel they are going before an independent and objective party to seek a resolution to their cases; instead, taxpayers will feel they are simply continuing their disagreements with the IRS as an institution,

25 IRM 8.1.1.1(1), *Accomplishing the Appeals Mission* (Feb. 10, 2012).

26 Rev. Proc. 2012-18, § 2.02(3)(b), 2012-10 I.R.B. 455.

27 The National Taxpayer Advocate has previously suggested steps that would enhance Appeals' independence, such as locating at least one Appeals Officer and Settlement Officer in every state, the District of Columbia, and Puerto Rico, and maintaining separate office space and communication facilities from other IRS personnel. National Taxpayer Advocate 2009 Annual Report to Congress 348. This independence could be further strengthened if, as also recommended by TAS, Appeals were provided with an independent Counsel to help Appeals evaluate positions adopted by IRS Counsel. National Taxpayer Advocate 2002 Annual Report to Congress 198.

28 *ABA Members Comment on Recent Appeals Division Practice Changes*, 2017 TNT 89-10, May 10, 2017.

29 TAS conference call with National Association of Enrolled Agents (NAEA) (Aug. 24, 2017).

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this time with an extra party or two added to the conversation — perhaps as overseers. Such an appearance is a far cry from the independent arbiter envisioned by the IRS Restructuring and Reform Act of 1998.³⁰ “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.”³¹

Other federal agencies likewise place a premium on the independence of their appeals process. Most of these agencies establish appeal to an Administrative Law Judge, or the equivalent, as the final stage in their administrative case resolution structure. Although negotiation is less of a central element in these disputes than in the context of IRS controversies, it is significant that, as far as TAS can determine, the agencies conducting large numbers of case appeals culminate their processes with proceedings in which claimants and their representatives can independently present their case to a final decision-maker without the presence of anyone from the agency who was involved in previous aspects of the case.³²

Adding Counsel and Compliance to Appeals Conferences Will Generate Additional Costs for the Government and Taxpayers in the Form of Fewer Case Resolutions, Additional Litigation, and Reduced Long-Term Compliance

As the American Bar Association has observed, “Taxpayers who choose traditional Appeals have chosen not to mediate, based at least in part on an assessment that the inclusion of Compliance could be counterproductive.”³³ To the extent that Appeals’ independence, either in reality or appearance, is diminished by mandating the presence of adversarial IRS personnel, taxpayers will be less likely to value and respect the outcome of Appeals proceedings. On the other hand, when people feel that a dispute resolution mechanism represents a fair and just process, they are highly likely to accept it. For example, one ADR survey found that over 90 percent of parties involved in arbitration voluntarily comply with the outcome.³⁴

By contrast, taxpayers who believe that Appeals has not made an objective, good-faith effort to resolve their cases will be much more likely to turn to the courts to obtain the independent review they are denied within the IRS. The National Taxpayer Advocate continues to note with concern that the proportion of docketed Appeals cases (which, by definition, require judicial involvement) in comparison to non-docketed Appeals cases has remained at over 40 percent between fiscal year (FY) 2013 and

30 The Internal Revenue Service Restructuring and Reform Act of 1998 (RRA 98), Pub. L. No. 105-206, Title III, Subtitle E, § 3465 (b) (July 22, 1998).

31 144 CONG. REC. S7622 (1998) (statement of Sen. Roth).

32 See, e.g., Board of Veterans Appeals, *How Do I Appeal?*, VA Pamphlet 01-15-02B 10-11 (May 2015), <https://www.bva.va.gov/docs/Pamphlets/How-Do-I-Appeal-Booklet-508Compliance.pdf>; Social Security Administration, *About Appeals*, Pub. No. 05-10041 (Jan. 2017).

33 *ABA Members Comment on Recent Appeals Division Practice Changes*, 2017 TNT 89-10 (May 10, 2017).

34 ABA, Sec. of Disp. Resol., *Benefits of Arbitration for Commercial Disputes*, http://www.americanbar.org/content/dam/aba/events/dispute_resolution/committees/arbitration/arbitrationguide.authcheckdam.pdf (last visited Apr. 18, 2017).

FY 2017.³⁵ This undesirable level of litigation activity, which may well be attributable to a growing alienation between taxpayers and Appeals, likely is perpetuated by a series of Appeals initiatives, including the AJAC project, the limitations placed on in-person conferences, and now the push to involve Counsel and Compliance in conferences regardless of taxpayers' views.³⁶

This troubling trend could be exacerbated by the possibility that, given the potential presence of Counsel, taxpayers and their representatives may decide to forego Appeals altogether out of concerns that Counsel will simply use the conference as a means of gathering insight regarding taxpayers' litigation strategies. Fewer resolutions in Appeals means more of a resource burden for taxpayers and the government on account of litigation, which forces taxpayers to incur extra expense, subjects them to tremendous personal stress, and wastes ever-dwindling government funds.

Appeals, administered with a careful eye toward taxpayer attitudes, can help generate the types of interactions and perceptions that will perpetuate the compliant behavior necessary to the success of the voluntary tax system.³⁷ Conversely, the implementation of procedures that allow for the addition of participants to conferences against taxpayers' wishes will likely foster disenfranchisement, litigation, and long-term noncompliance.

In many cases, the involvement of Counsel and Compliance in conferences may well generate the outcomes desired by Appeals. These beneficial results, however, will only occur where the participation of Counsel and Compliance is agreed to by taxpayers and their representatives, not where it is unilaterally mandated by Appeals. In order to facilitate short-term case resolutions and long-term tax compliance, Appeals should foster mutual respect and trust by allowing taxpayers a choice in the expanded participation of Counsel and Compliance in Appeals conferences.

CONCLUSION

Effective October 2016, Appeals implemented a number of changes to its conference procedures, including guidance in its IRM explicitly allowing Hearing Officers to invite Counsel and Compliance to participate in Appeals conferences. This step, however, may well have far-reaching negative consequences for Appeals' effectiveness in resolving cases with taxpayers. Among other things, Appeals' emphasis on expanding participation of Counsel and Compliance in conferences will fundamentally change the nature of conferences in which this approach is adopted and will jeopardize both the real and perceived independence of Appeals.

By allowing Hearing Officers the discretion to invite Counsel and Compliance personnel to join Appeals conferences, Appeals is altering the power dynamic between Hearing Officers and taxpayers. As a result, taxpayers are less likely to feel that their case has been fully heard, that they have been treated fairly, and

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- 35 National Taxpayer Advocate 2016 Annual Report to Congress 205. Examination-based cases represent the best data set for observing trends in this context, as Collection-based cases overwhelmingly give rise to non-docketed appeals (approximately 99.9 percent). Appeals response to TAS information request (Oct. 25, 2017). A docketed case arises when a taxpayer files a valid petition for review in the U.S. Tax Court and the case is referred back to Appeals for possible settlement. A prerequisite for this reassignment is that a taxpayer has not previously had an opportunity to present the case to Appeals. See IRM 8.4.1.4(1), *Appeals Authority Over Docketed Cases* (Oct. 26, 2016).
- 36 National Taxpayer Advocate 2017 Annual Report to Congress (Most Serious Problem: *The IRS Office of Appeals Imposes Unreasonable Restrictions on In-Person Conferences for Campus Cases, Even As It Is Making Such Conferences More Available for Field Cases*), *supra*; National Taxpayer Advocate 2016 Annual Report to Congress 203-10; National Taxpayer Advocate 2015 Annual Report to Congress 82-90.
- 37 Melinda Jone and Andrew J. Maples, *Mediation as an Alternative Option in Australia's Tax Disputes Resolution Procedures*, 27 AUSTL. TAX F. 525, 528 (2012); National Taxpayer Advocate 2007 Annual Report to Congress vol. 2, 138-71.

that the outcome of the proceeding should be respected. Instead, more litigation and less long-term tax compliance likely will be the unintended consequences of such an initiative. The IRS has acknowledged many of these issues, but has not yet committed to make any meaningful changes in the policy it has adopted.³⁸

RECOMMENDATIONS

The National Taxpayer Advocate recommends that the IRS:

1. Preserve its actual and perceived independence by adopting IRM procedures that separate Counsel and Compliance from Appeals conferences unless their inclusion is mutually agreeable to the taxpayer and Hearing Officer involved.
2. Continue to involve Counsel and Compliance in pre-conference hearings and if, after the Appeals conference itself is complete, additional information from Counsel and Compliance proves necessary, explain the need to taxpayers and convene a post-conference call or meeting in conformity with *ex parte* rules.
3. Track and analyze data relating to cycle times, outcomes, and subsequent litigation activity regarding conferences in which Counsel and Compliance participate so as to provide quantitative insight into the impact of such participation on Appeals proceedings.
4. Seek and carefully consider comments from tax practitioners and other stakeholders regarding when, and to what extent, the participation of additional IRS personnel in Appeals proceedings would contribute to case resolution.

38 Matthew R. Madara, *IRS Addressing Concerns Over Appeals Conference Pilot Program*, 2017 TNT 114-3 (June 15, 2017).