

# 2013 ORL

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## NTPI LEVELS 1&2

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**NATIONAL TAX PRACTICE INSTITUTE™**

**LEVEL 1**

### **Introduction to Appeals**

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**Sherrill Trovato, EA, USTCP**

Sherrill Trovato, EA, USTCP, MST, MBA has a Southern California firm specializing in tax prep and controversy representation. She has authored articles in CCH's Journal of Tax Practice and Procedure and NAEA's EA Journal. Trovato developed and teaches "Preparing to Practice before the US Tax Court" to tax practitioners who report an impressive pass rate on the Tax Court exam. She is a past NAEA president, NTPI Fellow and a regular instructor for the NAEA National Conference. She was recently appointed to IRSAC. Trovato teaches in the NTPI Levels 1, 3 and Graduate Level in Representation tracks.

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**COURSE OBJECTIVES**

**This course presents a description of the procedures needed during the Appeals process. After this course you will be able to**

- **Discuss the difference between a bare bones and a full protest and know when to use each type**
- **Compare and contrast Examination and Collection Appeals cases**
- **Identify the best strategies when presenting a case for Appeals consideration**

## APPEALS BASICS

The Internal Revenue Service (IRS) Appeals Office 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.”

The 2012 Strategic Priorities of the Appeals Office are:

- Increase taxpayer awareness of the Appeals process and their rights within the process.
- Increase taxpayer awareness of alternative dispute resolution programs.
- Improve our processes to meet customer needs and expectations and to reduce the length of the Appeals process while spending the right amount of time with each taxpayer.
- Promote employee productivity, engagement and satisfaction.

Information on the appeals process can be found in Part 8 of the Internal Revenue Manual (IRM).

Although an opportunity to go to Appeals is usually extended to taxpayers, there is no statutory right to an Appeals conference. Section 601.106(b) Statement of Procedural Rules and Rev Proc 87-24 afford a substantive right to an Appeals hearing, but such general statements of policy and rules do not have the force and effect of law, and are not binding on the issuing agency, according to the Tax Court.<sup>1</sup>

Since the Treasury Department was established by the Act of 1789 the Federal government has provided an administrative appeal to taxpayers who do not agree with proposed tax assessments. The Treasury’s general policy preference is that tax disputes be settled administratively rather than through litigation.

In 1927 a Special Advisory Committee was established by the Commissioner of the Internal Revenue Service to provide an appeal for cases pending before the Board of Tax Appeals (the predecessor of the United States Tax Court). From the start Appeals’ primary responsibility has been to “facilitate and expedite the settlement of tax disputes without formal trial.”<sup>2</sup> The Appeals Office (Appeals) has exclusive and final authority to determine liability for most taxes at the administrative level.

In the IRS Restructuring and Reform Act of 1998 (RRA 98) Congress mandated that Appeals be independent from IRS enforcement and compliance functions. It further deemed the Appeals function so important that it required the Service to make appeals conferences available in every state on a regular basis. Appeals must also consider the use of video conference for taxpayers who live in remote or rural areas.

The Appeals organizational structure was changed to better serve the American public by offering faster case resolution and other initiatives to assist the taxpayer. The primary Appeals division is now geographic with office headquarters in Baltimore, Manhattan, Nashville, Atlanta, Chicago, Dallas, San Francisco and Laguna Niguel. Appeals is also aligned by operating division. Wage and Investment Appeals Officers are centralized and conduct appeals primarily by telephone or correspondence while Small Business and Self-Employed (SB/SE) and Tax Exempt and Government Entities (TE/GE) Appeals Officers are dispersed geographically to mirror disbursement of SB/SE staff. Because of the heavy concentration of Large Business and International taxpayers (LB&I) in metropolitan areas, LB&I Appeals Officers are often located in those large cities with limited representation elsewhere in the country. Appeals Team Case leaders still report directly to the National Chief, Appeals who is based in Washington, DC.

As of 9/30/12 Appeals had more than 66,000 cases, with fewer than 40% dealing with Examination and nearly 44% dealing with Collection issues (the remaining inventory relates to penalty appeals, innocent spouse, and industry cases). Most cases are not docketed in the Tax Court.<sup>3</sup> There is no monetary limitation on Appeals' jurisdiction, although over-assessments exceeding \$1,000,000 are subject to review by the Chief Counsel and the Congressional Joint Committee on Taxation.

Agreement is reached with taxpayers on 85% of its examination cases overall, a level that has remained consistent over the past twenty-five years or so according to David Robison, who retired as Chief, Appeals for the National Office in May 2006.<sup>4</sup>

Appeals offer the only level of administrative appeal within the IRS and it permits any taxpayer to contest an IRS compliance action and some collection actions. The process is designed to give taxpayers who do not agree with the results of an examination of their tax returns or other adjustments to their tax liability another opportunity to resolve those results. An Appeals Officer gives the case a fresh look by considering any reason the taxpayer has for disagreement, except those based solely upon moral, religious, political, constitutional, or conscientious objection or similar grounds.

The Appeals employee has full settlement authority on any cases not previously seen. Cases seen by Appeals before a Tax Court petition is filed may be referred back to Appeals by Area Counsel, but it is not required. Generally if the proposed deficiency is more than \$50,000 Appeals has settlement authority until it is determined that no progress is being made or until the case is calendared for trial. If the deficiency is \$50,000 or less the case is generally referred back to Appeals for a period of 6 months, or until 2-4 weeks before the case is calendared.

#### **APPEAL CONFERENCES**

Appeals conferences are informal meetings which are handled by the local Appeals Office, which is independent of the IRS office that proposed the disputed action. Sometimes an appeal can be handled by telephone or through correspondence without requiring a personal appearance. However, the taxpayer has the right to request a face-to-face hearing if one is desired. The practitioner and Appeals Officer meet in an Appeals conference room to discuss

the pros and cons of the various positions taken by the taxpayer and by the IRS. Often a brief meeting or telephone call can resolve the case.

The practitioner or taxpayer presents taxpayer's case first with the opportunity to sell the merits of the taxpayer's case. The Appeals Officer asks questions to clarify facts and law or to obtain additional information. No testimony is taken under oath, although Appeals may require that matters alleged to be true be submitted in the form of affidavits or declarations that are signed under penalty of perjury.

**PRACTICE NOTE:** Do not let the informality lull you into a belief that this conference is not important. Prepare your case and put on the strongest possible position during the Appeals conference. Often the representative will be much more familiar with the facts than the Appeals Officer who did not prepare the case: use this to your advantage.

Impartial Appeals Officers will follow the law and must still protect the rights of the government and act as an advocate for the IRS.

**PRACTICE NOTE:** Over the past number of years, Appeals moved much of its work to campuses. Those employees generally are not as well trained as an Appeals Officer, and they may lack field experience. Make a written request for a face-to-face conference in your local office within ten days if your case has complicated issues.

#### **EXAM VS COLLECTION APPEALS**

There are differences in how examination and collection cases are processed and resolved in Appeals. Examination cases are resolved on the hazards of litigation standard, which allows the taxpayer to compromise an issue. By evaluating the hazards of litigation the Appeals employee can settle an Exam case in full or in part based upon the anticipated outcome of litigation. The taxpayer may win one or more issues, or may win a percentage of his or her case, depending upon its merits or strengths. In other words, the Appeals Officer can negotiate the settlement of a case on behalf of the government with the taxpayer and/or representative.

For Collection actions the Settlement Officer is seeking an alternative collection method to the proposed levy or enforced collection action. Taxpayers have the right to go to Appeals in several ways when taxes are owed: a final notice of intent to levy was issued, a federal tax lien was filed, an offer in compromise was rejected, or a taxpayer was denied innocent spouse relief. Our initial focus is on Examination cases with a look at Collection appeals later.

#### **HAZARDS OF LITIGATION**

Hazard of litigation refers to the probability the government's position may not be upheld by a court. Assessing the hazards of litigation include evaluating the likelihood that a court will rule against the government's position, estimating the costs to take the matter to trial, and evaluating whether there is doubt as to the legal conclusion, doubt as to how the court will view law and precedents, or no precedent. Appeals must assess trends the court has followed in similar cases, and weigh testimony and credibility of proposed witnesses. The Appeals

Officer uses research on various court decisions along with other information to determine the strength of the government's case.

Unlike the examining agent who must apply the facts at hand to the IRS's interpretation of tax law, the Appeals Officer can negotiate a settlement that considers other factors. Do the courts interpret the tax law in the same fashion as the IRS for that issue? Is there any legal authority on the issue, and if not, should there be? Have the various Circuit Court of Appeals ruled on the same issue in the same way? Is the taxpayer credible? Is the evidence credible?

**PRACTICE NOTE:** Additionally there are 'hazards' to the taxpayer in proceeding to Appeals, including the time and energy it takes and the cost of having a representative. IRS recently began offering Appeals Online Self-Help Tools to help taxpayers understand their appeal rights, what can be appealed, and what can be expected during the process. The tools cover Offers in Compromise, Innocent Spouse and Penalty appeals (for more information, see <http://www.irs.gov/Individuals/Appeals-Online-Self-Help-Tools>). If you are new to the process, or want to confirm whether a case is a candidate for one method or another, consider using these tools for guidance.

#### **AUDIT RECONSIDERATION**

IRC §6404(a) grants the IRS the discretionary authority to abate any unpaid tax determined to be excessive. Not the same as Appeals, audit reconsideration is:

- Evaluating a prior audit where additional tax was assessed and remains unpaid.
- When a taxpayer contests a Substitute for Return (SFR) and files a delinquent return – the original return is effectively an audit reconsideration.
- When taxpayer disagrees with an audit assessment s/he can request consideration to provide new information.
- Available when the taxpayer never appeared for an audit, or moved and did not receive examination correspondence.

Requests for audit reconsideration must be written. Generally the taxpayer must have filed a tax return which still has an unpaid assessment, and must provide additional information not considered during the original examination. The IRS will not reconsider the request if the assessment was made as a result of a closing agreement, or on Form 870-AD, *Offer to Waiver Restrictions on Assessment and Collection of Tax Deficiency and to Accept Overassessment*. An audit reconsideration is not a taxpayer right; since approval is discretionary, the taxpayer should be prepared to document their position when making that request.

See Publication 3598, *What you Should Know about the Audit Reconsideration Process* for more information.

## **JURISDICTION**

The Appeals process is voluntary and begins with the taxpayer filing the appropriate protest. The Appeals officer will evaluate the case, and may send it back to Examination or Collection if the case warrants additional development.

Much of the Appeals caseload growth is attributable to the change in Appeals' customer base that resulted from RRA 98; Appeals now has jurisdiction over Collection Due Process (CDP) hearings, Offer in Compromise (OIC), Earned Income Tax Credit (EITC) and joint and several liability under §6015 (innocent spouse) cases. Appeals also has jurisdiction over all federal income, estate, gift, employment and excises taxes, as well as liability for additional to tax (penalties). Appeals is most frequently involved in pre-assessment cases involving federal income, profits, estates and gift taxes, employment and certain tax liabilities, along with additions to tax (civil penalties). Appeals may also be involved in post-assessment cases involving penalties that are subject to reasonable cause determination, and/or are not subject to deficiency procedures.

Appeals also hear other matters, including:

- Collection actions, such as liens, levies, seizures, installment agreement determinations, and rejected OICs;
- Jeopardy levies;
- Administrative cost claims under §7430;
- Denial of innocent spouse requests,
- Imposition of the trust fund recovery penalty, among others.

In Appendix C find a list of the letters and notices that offer an Appeals opportunity.

## **EXHAUSTING ADMINISTRATIVE REMEDIES**

There are reasons to seek an Appeals conference beyond resolving tax controversies. Some Internal Revenue Code (IRC) sections require first that all IRS administrative remedies be exhausted. This occurs when either the taxpayer participates in an Appeals conference prior to filing a Tax Court petition or the taxpayer requested an Appeals conference that was denied. Appeals conferences are generally denied if there is less than 8 or 9 months remaining on the statute of limitations, but making the request is sufficient to satisfy those relevant IRC sections. The code sections requiring that all administrative remedies first be exhausted include:

- §6673 sanctions, which allows the Tax Court to penalize taxpayers and their counsel for frivolous or groundless positions, or those undertaken for purposes of delay when the taxpayer fails unreasonably to pursue available administrative remedies (including an Appeals conference). The taxpayer or counsel can be penalized up to \$25,000 for each occurrence.
- §7430 award of costs similarly requires that the taxpayer exhaust all administrative remedies within the IRS, including an appeals conference, in order to be awarded



reasonable administrative and litigation costs when the taxpayer substantially prevails. Even when the party believes it is an exercise in futility, the taxpayer must still participate in an appeals conference to meet the criteria. To be eligible, the taxpayer must actively participate and cannot merely show up and then refuse to disclose information the taxpayer knew, or should have known, was relevant at the time of the conference.

- §7491 shifting the burden of proof to the IRS in court proceedings also requires the taxpayer to participate in an Appeals conference before the burden shifts from the taxpayer to the IRS.

### **ADVANTAGE AND RISK TO APPEALS**

Generally it is less expensive to resolve tax controversies at the earliest possible opportunity. In other words, it is far less costly to settle an issue in Appeals than to rely upon the Tax Court, District Court, or Federal Court of Claims. If the issue will be litigated, the Appeals conference permits the taxpayer to see the strength of the government's case and for the IRS to learn about the taxpayer's case. The hazards of litigation may permit Appeals to offer a more favorable settlement than was possible in Examination. Filing a protest gives the taxpayer more time to negotiate an issue, or to learn about the IRS's case. Since no formal rules of evidence are used in Appeals, it may be easier to obtain information during Appeals rather than through the informal and formal discovery procedures available in Tax Court.

During whipsaw cases (also called interrelated, these are cases where the decision for or against one taxpayer will affect a different taxpayer's treatment of the same item, such as in an alimony case) Appeals may offer more flexibility in settling the case than in court.

A major risk is that Appeals may find and raise new issues that were not discovered or noted in the examination. The term "issues" relate to any position contrary to what was originally or previously taken by the taxpayer or the IRS. Since Appeals' purpose is to resolve disputes, not create new ones, Appeals policy is not to open new issues unless they are clearly wrong on their face, substantial, and the tax liability is material. Mere suspicion or conjecture that something could be wrong with the item is not substantial (IRM 8.6.1.6.1). New issues are not raised casually and the taxpayer or representative should be advised and given the opportunity to discuss the new matter before any further action is taken by Appeals.

New issues generally are anything concerning a taxpayer's return, the examiner's report, or the notice of deficiency not covered by the taxpayer in the protest or in the Tax Court petition (IRM 8.6.1.4.1). For non-docketed cases a new issue is any possible adjustment or change to the return that was not in dispute when Appeals received the case. For docketed cases a new issue is any adjustment or change that was not included in the notice of deficiency and is raised by Appeals after the Tax Court petition is filed; the IRS has burden of proof when it raises new issues in docketed cases.

With substantial unresolved issues related to an examined issue there is risk that the more highly trained Appeals Officer may see those issues and return the case to Examination for

additional development. Another risk is that the delay that occurs as the case moves through Appeals increases penalties and interest ultimately due.

**PRACTICE NOTE:** Everything in the administrative file can be reviewed in an Appeals case, so it is best not to provide extraneous information in Examination or Collection.

### **APPEALS OFFICE EMPLOYEES**

Appeals Officers generally work with examination issues and Settlement Officers generally work with collection issues. For simplicity sake, they will simply be referred here as Appeals Officers. They usually have college degrees and may be certified public accountants (CPAs) or attorneys. Generally they have the highest level of technical training available within the IRS. An Appeals Officer is likely to be better informed about tax laws and tax administration than the IRS employee who examined the return initially. Appeals Officers have many resources available to them to assess the hazards of litigation and they may request assistance from Area Counsel to answer legal questions. Experts in valuation and other issues are also available to the Appeals Officer.

With the Campus Specialization Initiative that moved some Appeals work to the campuses, it is likely that the lower level Appeals employees are not as educated or well trained as the Appeals Officers. Many were reassigned to Appeals after the efficiencies created by efilings eliminated the need for the employees to process tax returns. They are not the focus of this class other than as a reminder that you need to make a request for a face-to-face interview in order to have your case transferred to your local Appeals office. Note also that this request must be made before the start of actual appeals consideration or it will not be granted.

### **EX PARTE COMMUNICATIONS**

RRA 98 prohibits ex parte communications between anyone in Appeals and Examination employees that appear to compromise the independence of the appeals mission. Ex parte communications are those that take place without the taxpayer or the taxpayer's representative, whether the communication is oral or written. Communications that are ministerial, administrative, or procedural are permitted. Taxpayers must be given a "reasonable opportunity to participate" but if the taxpayer or representative elects not to participate, the prohibition against ex parte communication is waived for that contact without giving up the general right to be involved in discussions.

Communication encompasses discussion about the substance of the issues or positions taken in the case, including accuracy and relative importance of alleged facts in the case, and the perception of the "originating function" (IRS employee who heard the case originally) on the demeanor or credibility of the taxpayer or taxpayer's representative. In a case where prohibited ex parte communication occurred, the Tax Court judge said, "This needs to stop" then added, "ex parte contacts not only undermine the impartiality of the officer hearing the appeal, but are especially pernicious because they are so hard to detect."<sup>5</sup>

An 8<sup>th</sup> Circuit Court of Appeals case (*Robert v United States*, 4/24/04) held that even though prohibited ex parte communications occurred, that in itself was not grounds to quash a summons because Congress did not provide that remedy in RRA 98.

## EXAMINATION APPEAL ISSUES

If the taxpayer agrees with the examiner's proposed changes s/he can sign an agreement, and any additional tax can be paid at that time, or after the IRS submits a bill to the taxpayer. If the taxpayer does not agree with the proposed changes, and the examination takes place in an IRS office, the taxpayer can request an immediate meeting with the examiner's supervisor to explain his or her position. If an agreement is then reached, the case is closed.

If the examination did not take place in an IRS office, or the matter remains unresolved after meeting with the examiner's supervisor, the examiner prepares a report that explains both positions. The report is forwarded to the district office that will process the taxpayer's case. Within a few weeks after the closing conference with the examiner and/or supervisor, the taxpayer usually receives a package that includes:

- the 30 day letter that notifies the taxpayer of the right to appeal the proposed changes;
- a copy of the examination report that explains the examiner's proposed changes;
- an agreement or waiver form; AND
- a copy of Publication 5, *Your Appeal Rights and How to Prepare a Protest if You Don't Agree* (available online at [irs.gov](http://irs.gov)).

If the matter remains in dispute after examination, the IRS issues a Preliminary Notice of the Proposed Deficiency. This notice is also known as the 30-day letter because it generally gives taxpayers 30 days from the date of the letter to advise the IRS whether the proposed changes are accepted. It is possible to obtain an extension of another 30 days to file a protest if requested as far in advance as possible (any verbal request should be followed up with a written confirmation). Filing a protest sends the case to the IRS Appeals Office.

**PRACTICE NOTE:** If the taxpayer signs the examination report and returns it, or signs the agreement or waiver form, s/he agrees to the proposed changes. That action blocks any further administrative or judicial action on that matter. Be especially wary as a representative: do not sign the examination report or you can cost your client an Appeals conference, and open yourself to possible malpractice issues.

### PROTEST

When the taxpayer and the IRS do not agree on the results of an examination, the taxpayer may file a protest to Appeals to have the case considered by an impartial Appeals Officer. If the amount of disputed tax is less than \$2,500 a verbal request can be made. A brief written statement is required in field examinations involving from \$2,500 to \$10,000. A written protest is required for field examinations involving more than \$10,000 and for all:

- employee plan and exempt organization cases;
- partnership and S corporation cases; AND
- other cases, unless the case qualifies as a small case request procedure, including consideration of liens, levies, seizures or installment agreements.

**PRACTICE NOTE:** It is recommended all representative-prepared protests be written because verbal requests can be overlooked, forgotten or ignored. This can be easily be done on Form 12203, *Request for Appeals Review* (available online at irs.gov) or by letter following requirements stated in Publication 5. Always keep a copy of all correspondence in your files.

A written protest must be sent within the appropriate time period. Extensions of time to file the protest may be granted, but be sure to confirm in writing if any extension is granted. The Service is not required to grant an extension and generally will not without good reason. No specific form of written protest is required, but it must include the following information:

**IDENTIFICATION:** taxpayer name, identification number, current address and daytime telephone number;

**STATEMENT OF APPEALS:** a statement that the taxpayer wishes to appeal the IRS findings to the Appeals Office;

**LETTER DATE AND SYMBOLS:** copy of the letter that shows the proposed changes and disputed findings (or the date and symbols from the letter);

**TAX YEAR(S):** tax periods or years involved;

**SCHEDULE OF TAX CHANGES:** this list should agree with the Revenue Agent's Report of income tax changes. The taxpayer lists adjustments of disagreement and why;

**STATEMENT OF FACTS:** which support the position or issue the taxpayer disagrees with;

**STATEMENT OF LAW AND AUTHORITY:** if any, the taxpayer relies upon;

**EXHIBITS:** and documentation or affidavits may be attached and may lend credibility to the taxpayer's case; AND

**PERJURY STATEMENT:** taxpayer must sign the protest under penalties of perjury as follows:

"Under the penalties of perjury, I declare that I examined the facts stated in this protest, including any accompanying documents, and, to the best of my knowledge and belief, they are true, correct and complete."

If the taxpayer's representative prepares and signs the protest, a declaration must be substituted that s/he submitted the protest and accompanying documents, AND whether s/he knows personally that the facts stated in the protest and accompanying documents are true and correct.

The protest must be filed, in duplicate, as designated in the 30 day letter within thirty days of the notice date NOT the date it was received. Failure to file timely without an extension will cause the IRS to issue a notice of deficiency.

The protest will be reviewed by the examining agent who made the initial determination. The administrative file will be assembled and forwarded to Appeals along with pertinent documents, including the examiner's work papers. The Appeals Officer makes a preliminary review of the case. Since the Appeals Officer should not act as an investigator, if the case requires further factual development it is returned to the appropriate operating division. This happens in about 20% of all cases sent to Appeals so try to be complete in your protest.

**PRACTICE NOTE:** For maximum benefits to the taxpayer, write the protest using positive language. Do not attack the IRS or its employees as this is not perceived as convincing by Appeals.

**PRACTICE NOTE:** Because the protest is on top of the administrative file, it is typically the first taxpayer-prepared document the Appeals Officer sees. Do not just rely upon the IRS revenue agent's description; restate the issues as the taxpayer views them to make the protest persuasive. Focus on the facts, and take the opportunity to point out facts the agent ignored, which may or may not be disclosed in their report. Discuss procedural oversights or irregularities and all possible arguments in the taxpayer's favor. Structure the protest to show the issue is hazardous for the IRS to litigate. With careful drafting of the protest the practitioner leads the Appeals Officer to the preferred discussion issues. Use the protest to establish your credibility and that the taxpayer's position is serious. The key to a good protest is not length but rather readability. Try to tell a clear story supported by the facts, law and arguments.

Some effort must be made in order for the protest to be sufficient for an administrative appeal conference. A protest that contained no other information than the same information provided during the audit was rejected. Similarly a protest that described certain issues as "unagreed and protested" was rejected.

### **File Bare Bones or Fully Developed Protest?**

Writing an effective protest is time consuming and requires a thorough understanding of the facts and substantial legal research to apply law to those facts. Generally it is preferable, and more likely to achieve the desired outcome, if a fully developed protest is prepared with the appropriate recitation of facts and law. There are times when a taxpayer delayed too long in obtaining representation, giving the representative little time to prepare a fully developed protest. When possible, obtain an extension of time to file the protest; if that is not possible, provide a minimal basis in fact and law for the protest to preserve the taxpayer's appeal rights, but be prepared with all the facts and research prior to the appeals conference and indicate that will be the case on the protest.

### **Example of Bare Bones Protest:**

Taxpayer disagrees with the disallowance of expenses claimed on Schedule C and the disallowance of the claimed theft loss.

Taxpayers presented sufficient evidence to establish the Taxpayer-husband is in the business of being a song-writer and that all verified expenses should be allowed. Support will be available at or before the Appeals conference, as requested by the Appeals Officer.

Taxpayer can show that a cash hoard did exist, and they can and will support the availability of funds in the amount claimed at or before the Appeals conference, as requested by the Appeals Officer.

Taxpayers will submit appropriate legal citations concerning the theft loss at or before the Appeals hearing, as requested by the Appeals Officer.

### **Example of Fully Developed Protest:**

Taxpayer disagrees with the disallowance of expenses claimed on Schedule C and the disallowance of the claimed theft loss.

Schedule C loss: During examination, Taxpayer presented sufficient evidence to establish that Taxpayer-husband is in the business of being a song-writer. Husband has been writing songs for more than 8 years. During this time more than ten songs were recorded, many more were published, and his songs have been used in movies, television and radio commercials. A CD containing recordings of Taxpayer's songs will be provided at the Appeals hearing. In addition Taxpayer made a substantial investment in a sound studio to advance his work as a song writer; copies of relevant invoices and photos will be provided at the Appeals hearing.

Taxpayer has clearly met his burden of proof to establish he is in the songwriting business and that verified expenses should be allowed in full. Specifically the taxpayer asks that the following expenses be allowed in the amounts indicated (then list as appropriate).

Theft Loss: Taxpayer can show that a cash hoard did exist and can support the availability of the funds in the amount claimed. Taxpayer will provide affidavits from individuals who have personal knowledge of the cash hoard and the source of the hoard will be clearly shown.

In support of our position on the issue of the theft loss an analysis of the following court cases is provided:

In different cases (name and cite them) the court held against the taxpayer for several recurring reasons (then list). The taxpayer's case has none of the deficiencies found by the court as described above then distinguish those cases from facts at hand by listing the differences.

The taxpayer has carried their burden of proof relative to the theft loss issue.

#### **SMALL CASE PROCEDURE**

The small case procedure applies when the total amount for any tax period is not more than \$25,000. If there are multiple tax periods involved and any of them exceeds the \$25,000, a written protest is required for all affected periods.

The total amount includes any proposed increase or decrease in tax and applicable penalties. For OIC cases the total amount includes the total unpaid tax, penalty and interest due.

The small case request must be in writing, and must include 1) a request for Appeals consideration, 2) the changes the taxpayer does not agree with; AND 3) the reasons why the taxpayer does not agree.

#### **PREPARING FOR THE APPEALS CONFERENCE**

Upon receipt of the protest and administrative file, the Appeals Officer evaluates the facts, the quality and admissibility of evidence offered, the IRS's position on the matter, possible conflicting results in the various courts with jurisdiction, and the hazards of litigating the issue in court. The Appeals Officer evaluates the taxpayer's credibility along with availability of witnesses and evidence the taxpayer can present to support their case. The Appeals Officer prepares all taxpayer issues in an attempt to settle the case in one meeting.

The representative should be at least as well-prepared as the Appeals Officer, if not more so, to get the best possible resolution for the client. As with examination cases, the practitioner's role in Appeals is damage control, not obstruction of justice. Many of the steps for representing in Appeals are the same as for representing in Examination. Remember the Appeals Officer is better trained and has more latitude in settling a case than a Revenue Agent, but the representative needs to make a strong presentation for a favorable settlement.

During an Appeals conference it is possible to use affidavits (signed under penalty of perjury) along with direct evidence. Affidavits can also be submitted with the protest.

**PRACTICE NOTE:** If appropriate request a copy of the administrative copy, either informally to the Appeals Officer, or using a Freedom of Information Act (FOIA) request.

#### **THE REPRESENTATIVE'S ROLE IN APPEALS**

If the representative also handled the examination, duplicated steps may be omitted. If it is a new client engagement, the representative should:

- decide if the Appeals representation is one you wish to undertake after preliminary interview with the client. Ascertain the applicable facts and confirm them when possible. Learn what you can about the client.
- obtain the proper Form 2848, *Power of Attorney*, for the years and types of taxes at issue. Get an engagement letter and applicable retainer based upon your estimate of time it will take. Do not shortchange this process – it is likely that far more time will be spent in preparing for the case than in presenting it at the Appeals Conference.
- obtain and review the IRS records, including all notices and transcripts of the taxpayer's account, the Revenue Agent's Report and work papers.
- gather and review the client's records as needed and assess them for evidentiary value. Obtain missing information (documents or witnesses) that may support the taxpayer's position.
- establish privileged and confidential files, if they apply. Remember that practitioner-client privilege is very limited for nonattorneys but it can apply to an appeal of the return. It is the practitioner's responsibility to keep privileged documents safe and to disclose them only as appropriate.
- research the client's position, including relevant authority (code and regulations are the primary authority, along with other sources) and court cases in the relevant circuit. Pay attention to court cases pro and con to the taxpayer's position and be prepared to distinguish the current facts from cases where the taxpayer did not prevail. See the section on Precedent for more information.
- formulate arguments after investigating the facts and analyzing the applicable law.
- assess the client's exposure on the appeal – evaluate both sides of the position. Find out what resolution the client hopes to achieve and assess how realistic that is. Anticipate the IRS's case: what will the IRS argue and how can you counter those arguments? Develop the appeal strategy.
- prepare the protest.
- prepare for the Appeals conference, including reviewing the entire file and determining strengths and weaknesses. Organize the exhibits or affidavits so they are easy to follow and use. Find out about the Appeals Officer if possible.
- Meet with Appeals Officer as appropriate.
- communicate results with the client and agree upon any follow-up strategy in response to the Appeal.

**PRACTICE NOTE:** Remember that Appeals Officers are people doing their job. Respect that each of you has a role to play in the process. Make it easy for the Appeals Officer to agree with your position by making a strong presentation. Promptly follow-up with any issues raised during the Appeals conference. Always be courteous and professional in your demeanor.

#### **SETTLEMENT OFFERS**

The Appeals Officer will expect you to make a settlement offer first. The offer should be within a reasonable range to show you are serious but generally not your final position. If the



practitioner does not make a settlement offer, the Appeals Officer may offer an amount at the higher end of the permitted range. Lead with a settlement offer that allows for negotiations and reflects a good faith attempt by the taxpayer to resolve the case. It should capitalize on the taxpayer's favorable points and emphasize the government's risk of litigation. If the Appeals Officer declines a good faith offer s/he should either state an acceptable offer range, or the representative should inquire about that range. The representative should strive to settle the case, not to win at all costs. Most cases are resolved in Appeals but a full concession from the government is not the expected outcome unless the agent was very clearly wrong and that situation could have and perhaps should have been resolved with the examiner's manager while still in Exam.

**PRACTICE NOTE:** In any settlement offer also address the issue of interest netting, which equalizes the rates for overpayments and underpayments that are outstanding simultaneously. This results in no interest assessment if the taxpayer owes money to the government at the same time the government owes money to the taxpayer. Interest would still be assessed for any amount or during a nonsimultaneous time period.

It is possible to settle the case for a specified dollar amount, which allows the Appeals Officer to decide how much to allocate to tax, interest, and penalties.

#### **CASE RETURNED TO EXAMINATION**

If the Appeals Officer feels the case was not fully developed, or if the taxpayer provides new evidence at the Appeals conference, the case can be returned to Examination for further development under IRC Reg. 601.106(f)(6)). The Appeals Officer has some discretion to consider new evidence, so returning the case is not required. The returned case will generally be assigned to the same examiner who handled the original examination, who may perceive the action poorly.

### **COLLECTION APPEAL ISSUES**

Many IRS collection actions can be appealed, but the two main procedures are Collection Due Process (CDP) and Collection Appeals Program (CAP):

CDP is available if the taxpayer receives a Notice of Federal Tax Lien Filing, a Final Notice – Notice of Intent to Levy, a Notice of Jeopardy Levy, or a Notice of Levy on Your State Refund. Each of those notices is accompanied by a copy of Publication 5 (available online at [irs.gov](http://irs.gov)). If the issue remains unresolved after a CDP hearing, the taxpayer has the right for judicial review by the Tax Court. The Tax Court's jurisdiction over all CDP hearings was effective in late 2006.

CAP is generally quicker and is available for a broader range of collection actions, but no judicial review is possible.

**PRACTICE NOTE:** Changes in financial condition can change the outcome of a collection appeal, so make certain the taxpayers understand the importance of maintaining current financial records, and that they communicate with the practitioner throughout the process.

### **COLLECTION DUE PROCESS (CDP)**

Hearings under §§6320 and 6330 are available under CDP for lien and levy notices. The taxpayer requests a hearing by completing Form 12153, *Request for a Collection Due Process Hearing* (available online at irs.gov) within 30 days of the date on the notice. If the taxpayer receives both a lien and levy notice each may be appealed, but only one hearing relating to each notice for each taxable period is held. No extensions of time are permissible to request a CDP hearing; an untimely hearing request made within one year leads to an equivalent hearing. Collection action is not suspended and there is no Tax Court jurisdiction if the taxpayer receives an equivalent hearing.<sup>6</sup>

**PRACTICE NOTE:** It may be more advantageous to file for an equivalent hearing than the CDP hearing if the taxpayer is near the collection statute expiration date. CDP hearings toll the statute for the time the CDP is pending while an equivalent hearing does not.

Taxpayer must indicate which actions s/he disagrees with, and the reasons. In addition to identifying all of the reasons for the disagreement, the taxpayer can also raise issues regarding:

- appropriateness of collection actions;
- collection alternatives such as installment agreement, offer in compromise, or by posting bonds;
- appropriate spousal defenses; AND
- whether the tax is due, but only if no opportunity to dispute the tax was previously given either because a notice of deficiency was not issued, or one was issued to an incorrect address.

The representative should set forth all defenses to the levy, including:

- offer in compromise,
- amount of the liability,
- spousal defenses,
- currently not collectible (CNC) status,
- penalties,
- requests for installment agreement. It is wise to always request an IA to preserve that option in case other opportunities fail; it is better to pay a debt over time than to lose assets.

Unless the IRS has reason to believe that tax collection is in jeopardy, they will stop levy action during the 30 days following the levy notice. If an appeal is timely filed, collection activity also stops during the appeal process. With a timely appeal the 10 year collection statute of limitations is suspended until the date the determination is filed, or the taxpayer withdraws (in writing) the request for a hearing.

Appeals will issue a written determination letter when the hearing is completed. If the taxpayer agrees with the determination, s/he is obligated to that agreement, as is the IRS. If the taxpayer disagrees with the written determination, s/he has 30 days in which to commence a case with the Tax Court.

**PRACTICE NOTE:** On March 23, 2010 the IRS ruled that if a financial statement (Form 433) is not submitted with a Collection Due Process (CDP) request, the taxpayer is no longer eligible for a transfer to a local Appeals office for a face-to-face hearing. Appeals will ordinarily grant a taxpayer's request for a face-to-face CDP hearing if the taxpayer wishes to discuss any relevant, non-frivolous issue relating to the unpaid tax or proposed collection action, such as spousal defenses, challenges to the appropriateness of collection actions, offers of valid collection alternatives and nonfrivolous challenges to the existence or amount of the underlying tax liability.

#### **DISQUALIFIED EMPLOYMENT TAX LEVIES**

The Small Business and Work Opportunity Act of 2007 modified the CDP process for employment tax liabilities served on or after 9/22/07. Now the IRS can levy to collect employment taxes without first giving a taxpayer a pre-levy CDP notice if the levy is a "disqualified employment tax levy (DETL)."

A DETL under §6330(h) is a levy to collect a taxpayer's employment tax liability if the taxpayer, or a predecessor, requested a CDP hearing under §6330 for unpaid employment taxes arising in the two year period prior to the beginning of the taxable period for which the levy is served.

Requests for an equivalent hearing or untimely requests for CDP hearings do not satisfy the requirement of having had a prior hearing request and cannot be used as a basis for a DETL.

**EXAMPLE 1:** Taxpayer owes 4<sup>th</sup> quarter 2005 and requests a timely CDP levy hearing. Taxpayer accrues additional employment tax liability for the quarter ended 6/30/06. The additional liability qualifies for a DETL levy because a prior levy hearing was requested for a quarter (2005-4) within the 2 year look back period (4/1/04-4/1/06). Remember, the DETL was served for quarter 2006-2, so 4/1/06 begins that look back period.

**EXAMPLE 2:** Taxpayer owes 1<sup>st</sup> quarter 2006 (2006-1) and requests a timely CDP hearing. Taxpayer is assessed additional employment tax liability for the quarter ended 12/31/05. The additional liability does NOT qualify for DETL levy because the taxpayer requested a prior levy hearing for a quarter (2006-1) that is outside the two year look

back period (10/1/03-4/1/06). Here the DETL is served for 2005-4, so 10/1/05 begins that look back period.

### **CDP HEARINGS AND THE TAX COURT**

Under IRC 7803(c)(2)(B)(ii)(X) the National Taxpayer Advocate (NTA) in her annual report must identify the 10 tax issues most litigated in the Federal courts (which include the Tax Court, federal district courts, the Court of Federal Claims, and the bankruptcy courts). Ms. Olson's full 2012 Annual Report to Congress is available at [irs.gov](http://irs.gov).

Since 2003 CDP is almost always the most litigated issue and overwhelmingly the cases are still decided for the IRS. As the courts continue to impose appropriate sanctions for frivolous arguments, they see more nonfrivolous cases with significant issues pertaining to the scope of judicial review. The NTA continues to be concerned with Appeals' reluctance to grant face-to-face CDP hearings; specifically her concern is that the lack of local hearings increases the likelihood that taxpayers will not develop the administrative record in such a way that courts can conduct proper judicial review.

Frivolous issues are frequently raised in CDP hearings. These arguments appear often in one variation or another in Tax Court cases over the past few years. Taxpayers advancing these arguments will not prevail:

- IRS notices are invalid because they are not signed under penalties of perjury,
- an Appeals officer does not meet the requirement of §6330(1).
- a "procedurally proper" Notice and Demand for Payment was not issued.
- they are entitled to an examination interview or administrative appeal.

Documents arising under §6065 requiring signature under penalty of perjury refer to taxpayer's signature not an IRS signature requirement. Certified copies of Forms 4340 are enough to show the taxpayers are properly assessed and the notices are properly made. Form 4340 provides presumptive proof. Appeals Officers are only required to verify that an assessment has been made; they are not required to provide that assessment to the taxpayer. Prior to the issuance of a notice of deficiency taxpayers do not have the right to an examination interview or an administrative appeal. The IRS can use a computer generated Revenue Accounting Control System Report (RACS 006) instead of Form 23C.

Remember the taxpayer does not have the opportunity to discuss the underlying tax liability in a CDP hearing if that opportunity was previously given. If a notice of deficiency was issued or the taxpayer previously had the opportunity to dispute the tax, the taxpayer cannot raise the issue again. In *Rivera*<sup>7</sup> taxpayer was not permitted to contest the underlying tax liability because he had signed a consent to assessment, which waived his right to a notice of deficiency. The IRS was not permitted to argue that a self-assessed income tax (one shown on the face of the return prepared by the taxpayer) cannot be disputed in a CDP hearing. If the taxpayer was not given a notice of deficiency or otherwise had an opportunity to dispute the liabilities, it is appropriate to do so at a CDP hearing in *Montgomery*<sup>8</sup> and various other cases.

If taxpayers are not compliant with revenue laws they will receive an unfavorable ruling at their CDP hearing, which is not an abuse of discretion by the IRS. Also a taxpayer's proposed "pay as you go" installment plan was rejected in *McCorkle*<sup>9</sup> because it would be hard for the IRS to monitor (her income fluctuated monthly). She was not in compliance on the current return and had not paid any amounts due.

In *Collins*<sup>10</sup> taxpayer claimed that statements of balance due were not adequate notice and demand because they used the word "please" rather than "demand."

### **COLLECTION APPEAL PROGRAM (CAP)**

CAP procedures are available for more types of collection actions than the CDP. Appealable collection actions include:

- Notice of Federal Tax Lien – appeals can be made before or after the IRS files a lien. Denied requests to withdraw a lien can also be appealed. If the IRS files a Notice of a Federal Tax Lien the taxpayer also has appeal rights under CDP procedures.
- Notice of Levy – appeals can be made before or after the IRS places a levy on wages, bank accounts, or other property. Other CDP appeal rights may apply.
- Seizure of Property – appeals can be made before or after the IRS seizes property. Once the IRS seizes property the appeal must be made to the Collection manager within 10 business days after the Notice of Seizure is given to the taxpayer or left at his or her business or home.
- Denial or Termination of Installment Agreement – appeals can be made when the IRS notifies taxpayer that an installment agreement is denied or terminated.

The taxpayer can appeal these actions by telephone if the only collection contact is from a notice or telephone call by the IRS. If the employee at the IRS telephone number on the notice cannot resolve the issue, the taxpayer can verbally indicate a desire for an appeal. The employee must refer the matter to a manager who can speak with the taxpayer then, or who will return the telephone call within 24 hours. If the taxpayer and manager do not reach an agreement, the case is referred to an Appeals Officer for review.

If a Revenue Officer has been in contact with the taxpayer, the taxpayer must first request a conference with a Collection manager. If the disagreement is not resolved, the taxpayer can use Form 9423, *Collection Appeal Request* (available online at [irs.gov](http://irs.gov)) to request an appeal. The Collection Office must receive Form 9423 within two days of the Collection Manager conference or collection of the lien, levy or seizure will continue. For denials or terminations of installment agreements, the taxpayer has 30 days in which to submit a request to the Collection Office.

For denials/terminations of installment agreements, the IRS cannot levy until 30 days after its action. If a taxpayer files an appeal within the 30 day period all levy activity must stop until the appeal is completed.

In addition to the lack of judicial appeal, the major disadvantages with CAP are the requirement to first contact the group manager and the short time frame to file.

## SETTLEMENT AGREEMENTS

Appeals officers have flexibility to accomplish the Appeals Office mission of resolving tax controversies without litigation in a fair and impartial manner. A settlement may occur on all issues, or on some of them based upon the probable result in litigation, or upon the relative strength of the positions if there is uncertainty in the probable outcome. Settlement offers may not be used as evidence in court, so there is little risk to negotiating in Appeals.

Settlements are generally classified as:

- mutual concession settlements – where both the government and taxpayer make a concession for purpose of settling the case, generally because neither party, with justification, is willing to concede all issues in full because each has a strong position. Appeals is specifically permitted by Policy Statement P-8-47 to enter into such agreements;
- split issue settlements – this is similar to a mutual concession settlement in that there is substantial uncertainty about either the facts or the law, or both. As authorized by Policy Statement P-8-48, Appeals may enter into a settlement based on a percentage or stipulated amount of the tax in controversy. These should be used only where there is no other method of settlement; AND
- nuisance settlements, which are specifically prohibited by Policy Statement P-8-47, except that they may be considered once all critical issues are decided under IRM 8.6.4.1.3. A small nuisance settlement may be 5-10% of the amount of taxpayer's claimed amount, but the Appeals Officer will not concede frivolous items.

The Appeals Officer and taxpayer may come to a complete agreement on all items in controversy. Generally the Appeals Officer then requests the taxpayer sign Form 870, *Waiver of Restrictions on Assessment and Collection of Deficiency in Tax and Acceptance of Overassessment*. By law the running of interest is suspended for thirty days after this form is received, and is effective when received by the IRS.

If the case has concessions “for purposes of settlement” there likely was substantial uncertainty about how the court would interpret and apply the law. The settlement is then classified as a “mutual concession settlement.” Form 870-AD, *Offer of Waiver of Restrictions on Assessment and Collection of Deficiency in Tax and of Acceptance of Overassessment*, is used.

Form 870-AD differs from Form 870 in several ways. It contains a pledge against reopening the issues, although this pledge itself is sometimes litigated. Additionally, the running of interest is not suspended until 30 days after the agreement is executed by the government, and it is valid

only after it is accepted by or on behalf of the Commissioner of the IRS. In other words, this agreement must be signed by the IRS to be valid. A Form 870-AD agreement will not be reopened unless there is later a suspicion of fraud, concealment or misrepresentation, and even then, Appeals must approve the action.

**PRACTICE NOTE:** By executing Form 870-AD the taxpayer or representative gives up judicial rights, including the right to suit for a refund.

All settlements are reviewed by that Appeals Officer's supervisor, the Chief Appeals Officer, an associate chief, or the team chief of a local office. After settling a case the Appeals Officer prepares a transmittal memorandum and supporting statement that discusses the issues and evidence, the amount of the settlement, and the reasons to support the settlement. When a settlement is based upon binding arbitration, the issues of fact that the arbitrator decides upon are binding on the IRS and the taxpayer. If the settlement involves a refund or credit exceeding \$2,000,000 the refund or credit cannot be issued until at least 30 days after the IRS submits a report on the matter to the Joint Committee on Taxation. This often takes much longer as the practice of the service is to wait for the JCT to issue a clearance letter in almost every case.

Settlement offers may be withdrawn at any time prior to being signed by both parties, and they may be available only for a limited period of time. Do not delay in communicating your acceptance of the settlement offer if the Appeals Officer makes an offer the taxpayer desires. Binding precedent is an agreement form signed by both parties, not a handshake.

If the case is docketed in the Tax Court the settlement is reflected in a Stipulation and then a related Decision filed by the Tax Court.

The closing options in Appeals are much the same as for Exam. The taxpayer can agree and sign the report, pay the tax and file claim for refund, disagree with Appeals action and wait for the notice of deficiency, or ignore any action in Appeals and wait for the notice of deficiency. For most deficiency cases in income, gift, estate and some excise taxes, the notice of deficiency grants the taxpayer 90 days to petition the Tax Court for judicial review, as discussed later.

**PRACTICE NOTE:** Discuss settlement options with the client before meeting with Appeals. If the client is willing to settle for a certain dollar amount, it is possible to have a check already drawn and available to hand to the Appeals Officer. The client may provide specific settlement authority; if the Appeals Officer exceeds that authority, the representative can defer acceptance until the client is advised.

Settlement may have no binding effect on later years in which a similar issue may arise, but as a practical matter the settlement generally establishes precedent. Issues such as reasonableness of salaries, capital gain vs ordinary income treatment, hobby losses and so forth are resolved on the facts and circumstances for each tax year. A collateral agreement may be used to express in writing the understanding of both parties as to the tax effect in subsequent years.

## **CLOSING/COLLATERAL AGREEMENTS**

Some tax cases may involve matters that have a direct effect on either other taxes, related taxpayers, or other years and the taxpayer may wish to enter into a closing agreement. For example, a liquidating corporation may want a closing agreement in order to wind up its affairs. Settlement of these cases may require an additional agreement. §7121 authorizes the Secretary to enter into an agreement in writing with any person regarding that person's tax liability for any period, but they are used sparingly. A closing agreement can be entered into in any case where there appears to be an advantage of having the case permanently and conclusively closed.

Closing agreements are done on either Form 866 (very rare), which finalizes tax liability, or Form 906 (commonly), which finalizes specific matters.

Although not expressly provided for in the Internal Revenue Code, a collateral agreement covers matters related to a tax controversy, but collateral to the amount of tax to be assessed in the instant case. For example, a collateral agreement may commit a trustee or a beneficiary to use the same valuation for income tax purposes as was used for federal estate tax purposes. The collateral agreement does not bind the IRS and it is a one-sided commitment; the IRS does not enter into a collateral agreement and does not sign as a party. Collateral agreements are administrative in nature.

See IRM 8.13 for more information about closing agreements.

## **ALTERNATIVE DISPUTE RESOLUTION**

The same techniques that are useful in dealing with an Appeals Officer are also generally effective when using Alternative Dispute Resolution (ADR) such as mediation or arbitration. ADR's purpose is still to resolve the case but there may be differences in tactics and procedure to consider. Mediation is available when a limited number of legal and factual issues remain unresolved after settlement discussions in Appeals; the mediator's role is to help the parties reach their own negotiated settlement. Mediation is optional but arbitration is binding.

### **ARBITRATION**

Arbitration became available in 2006 for certain cases within Appeals jurisdiction that meet program requirements. Generally it is available for cases in which a limited number of factual issues remain unresolved following Appeals administrative process. It is also available after unsuccessful attempts to enter into a closing agreement under §7121, or for certain OIC cases involving unsuccessful attempts to enter into a compromise under §7122, and for certain Trust Fund Recovery Penalty cases. Taxpayers and Appeals may jointly request binding arbitration.

Arbitrators can come from within Appeals or from any local or national organization that provides a roster of neutrals, and the taxpayer and IRS jointly select the arbitrator. Due to the



inherent potential conflict of interest when using an Appeals employee, it may be to the taxpayer's benefit to select someone from outside the IRS even though it costs more.

Arbitration is not available for all issues, including legal issues, those already in any court, issues designed for litigation, collection cases (except for those detailed in announcement 2011-6), and frivolous issues. More information on arbitration can be found in Revenue Procedure 2006-44, IRM 8.26.6 and IRM 35.5.5.

### **FAST TRACK SETTLEMENT (SB/SE)**

Fast Track Settlement (FTS) for Small Business Self Employed taxpayers was designed to resolve audit issues during the examination process within a goal of 60 days from acceptance of the application in Appeals. Unlike Fast Track Mediation which offered a suggested alternative, Fast Track Settlement actually offers a resolution. A specially trained Appeals employee facilitates the discussion so the taxpayer (or representative) and the Revenue Agent (and/or group manager) can reach a mutually agreeable settlement.

Taxpayers and the group manager submit Form 14017, *Application for Fast Track Settlement*, along with the taxpayer's brief, concise and 'soundly' written response to the IRS's position. A response is due within 60 days for SB/SE and Tax Exempt Government Entities cases.

Generally FTS is available for cases under SB/SE jurisdiction if 1) issues are fully developed, 2) the taxpayer has stated a position in writing (or filed a small case request for cases in which the total for any tax period is less than \$25,000); AND 3) there are a limited number of unagreed issues.

Some cases cannot utilize Fast Track Settlement, including:

- Collection Appeals Program cases, Collection Due Process, Offer in Compromise and Trust Fund Recovery cases,
- Correspondence examination cases worked solely in a Campus/Service center;
- Cases in which the taxpayer has failed to respond to Service communications and no documentation has been previously submitted for consideration by Compliance;
- Issues designated for litigation;
- Issues for which the taxpayer has submitted a request for competent authority assistance;
- Frivolous issues;
- Whipsaw issues (where resolution for one party may result in inconsistent treatment for another party who is not participating in the FTS); AND
- Issues that were identified in a Chief Counsel Notice as being excluded from this process.

If one issue is deemed ineligible, all issues in the cases are ineligible for FTS.

See Announcement 2011-5 for more information on SB/SE FTS.

### **FAST TRACK SETTLEMENT (LB&I)**

Since 2003 Fast Track Settlement (FTS) for Large Business and International Division taxpayers has provided a way to resolve audit issues during the examination process in less than 120 days. FTS reduces the combined LB&I/Appeals process time by two years. More information can be found in Revenue Procedure 2003-40, IRM 8.26.1 and the Application for Fast Track Settlement.

### **FAST TRACK MEDIATION (SB/SE)**

Fast Track Mediation (FTM) gives SB/SE taxpayers and the IRS the opportunity to mediate disputes through an IRS Appeals officer who acts as a neutral party. Most tax disputes are resolved within 40 days compared to several months through the regular appeal process. The IRS and the taxpayer must request mediation using Form 13369. No formal protest is required, but taxpayers must provide a written position with the request for mediation. Most nondocketed cases qualify for FTM, but it cannot consider cases with issues for which there is no legal precedent, issues where court decisions differ between jurisdictions, campus and automated collection service (ACS) cases, Collection Appeal Program (CAP) cases and those with only frivolous arguments.

To be successful, all the decision-makers must be present at mediation. Taxpayers can withdraw from mediation at any time, and they retain all the usual appeal rights for items that are not resolved in FTM.

For more information see Publication 3605, *Fast Track Mediation*, IRM 8.26.3, and Revenue Procedure 2003-41.

### **EARLY REFERRAL**

RRA 98 extended the early referral program so it is now available to any taxpayer at his or her option and request. It is intended to resolve cases more expeditiously by having Appeals and the operating divisions work together to allow Appeals to resolve specific issues while Examination continues the audit. Early referral can be made for income tax matters and is also available for issues involving involuntary changes to accounting methods, employment tax, employee plans, and exempt organizations.

To be referred 1) the issue must be fully developed, and if resolved, can reasonably be expected to result in a quicker resolution of the entire case, AND 2) the taxpayer and operating division both must agree on the referral.

The request is similar to a formal protest, and must be made in writing by the taxpayer to the team leader or group manager. The request must include 1) the taxpayer's identity and the tax periods to which the issues relate, 2) each issue for which early referral is requested; AND 3) a statement of the taxpayer's position, including a brief discussion of the material facts and an analysis of the facts and law as they relate to each referral issue.

Some items cannot be referred early, including:

- whipsaw transactions (situations where the government is subject to conflicting claims by taxpayers).
- issues designated for litigation by the Office of Chief Counsel.
- issues for which the taxpayer filed a request for Competent Authority Assistance, although Appeals and Competent Authority can simultaneously consider the issue.

The taxpayer initiates early referral and can do so on any developed unagreed issues under jurisdiction of the operating division. Examination continues on all other unrefereed issues. The taxpayer is notified within 14 days if the request is denied. There are no formal appeal rights in this instance, but a conference can be requested to discuss the denial. The taxpayer retains the right to pursue the normal administrative appeal of any proposed deficiency at a later date.

If the early referral is accepted, within 30 days the IRS prepares Form 5701, *Notice of Proposed Adjustment*, or an equivalent form to the taxpayer for each early referral issue approved. The notification form describes the issue and explains the examiner's proposed adjustment; the taxpayer must respond in writing to each of the proposed adjustments. That response must contain an explanation of the taxpayer's position, and must be submitted to the team leader or group manager within 30 days. The taxpayer's reply must also be executed under penalty of perjury with the appropriate signature. If the taxpayer does not respond on any issue within the appropriate time frame, the taxpayers' early referral request is considered withdrawn for that issue.

If the IRS and the taxpayer reach an agreement, usually Form 906, *Closing Agreement on Final Determination*, is prepared to cover the specific items. If the early referral negotiations are unsuccessful and no agreement is made, Appeals will not consider an unagreed early referral issue again if the entire case is protested later to Appeals, unless there is a substantial change in circumstances.

More information can be found in Revenue Procedure 99-28 and IRM 8.26.4.

#### **POST APPEALS MEDIATION**

Mediation is an extension of the Appeals process; the mediator's role is to help resolve a dispute following unsuccessful good faith negotiations in Appeals. This non-binding process can be requested after Appeals has considered an issue and failed to reach an agreement with the taxpayer, or while the taxpayer is in the Appeals process with a qualifying issue. As a neutral third party, mediators help Appeals and the taxpayer reach their own negotiated settlement. The mediator acts as a facilitator to assist in defining the issues and to promote settlement negotiations. The mediator does not have settlement authority in the process and will not render a decision. Such issues include unsuccessful attempts to enter into a closing agreement under §7121, or for certain OIC cases involving unsuccessful attempts to enter into a compromise under §7122, and for certain Trust Fund Recovery Penalty cases. It is not available

for docketed court cases, but can be used for factual issues as well as legal issues. There are no dollar limits.

More information can be found in Revenue Procedure 2009-44 and IRM 8.26.5.

## **PRECEDENT AND THE APPEALS CONFERENCE**

Tax Court decisions are appealed based upon by the taxpayer's legal residence at the time the petition is filed, so it is critical consider court decisions in the relevant circuit. Under the *Golsen* rule (*Golsen v Comm'r*, 54 T.C. 742 (1970)), the Tax Court must "... follow a Court of Appeals decision which is squarely in point where appeal from our decision lies to that Court of Appeals." A taxpayer residing in California files an appeal in the 9<sup>th</sup> Circuit and at a Tax Court trial the parties are bound by that Circuit's decisions even when they differ from other circuits.

The Appeals Officer will research court decisions in the relevant Circuit to evaluate the current case based upon prior precedent when it is available. The practitioner must look at cases that favor the taxpayer as well as those that do not and be able to distinguish the taxpayer's facts and circumstances from court cases that support the government's position.

The Appeals Officer must also consider whether the IRS Chief Counsel has indicated a position for litigation on the issue(s) in this case. Technical advice may be sought by the IRS or the taxpayer as to the meaning of the Internal Revenue laws, regulations or related statutes as they apply to the case at issue. Appeals is bound by a favorable decision to the taxpayer, but is not bound by Technical Advice that is adverse to its position.

## **OTHER APPEALS JURISDICTION**

### **§6015 JOINT AND SEVERAL LIABILITY**

Revenue Procedure 2013-34 supersedes the earlier Revenue Procedure 2003-19 with respect to threshold requirements for any equitable relief requests, and indicates when the IRS will make streamlined relief determinations granting equitable relief from an understatement of income tax, or an underpayment of income tax reported on a joint return.

Request for relief from joint and several liability commences with filing Form 8857, *Request for Innocent Spouse Relief*. The nonrequesting spouse is called an "intervenor." The IRS must notify the nonrequesting spouse in §6015 cases who can provide information to IRS; all relevant information submitted must be considered. The nonrequesting spouse has Appeal rights on IRS decision to GRANT relief to requesting spouse, but does NOT have right to appeal a decision to deny relief to the requesting spouse. The nonrequesting spouse has no judicial appeal in the Tax Court.

The IRS issues a preliminary determination letter to the requesting spouse based upon merits of the claim. If the IRS grants full or partial relief, the IRS suspends processing of the claim for 45

calendar days to permit the nonrequesting spouse an opportunity to appeal the determination. To be eligible for a conference, it must be requested in writing within 30 calendar days of the mailing date of the notification letter. If the nonrequesting spouse files an appeal, the IRS suspends processing for relief until the appeal is heard.

The requesting spouse has the opportunity to file a written protest based upon the preliminary determination. If during the appeals conference the IRS increases the relief available, the IRS notifies the nonrequesting spouse and gives an opportunity for an Appeals conference to present his or her position before the final determination.

If both spouses file written protests requesting an Appeals conference, the IRS notifies each spouse of the other's request. The IRS holds separate appeals conferences and gives each the opportunity to submit information. The IRS may hold a joint conference.

**PRACTICE NOTE:** Be aware that Form 8857 has a box to be checked if the requesting spouse was a victim of domestic violence; the IRS is not to disclose the requesting spouse's location.

#### **POST ASSESSMENT PENALTY APPEALS**

The IRM contains provisions for post-assessment review of certain penalties. Generally these are penalties that can be immediately assessed without the deficiency procedures that permit the case to be appealed to the Tax Court before assessment. A post-assessment appeal exists for virtually any penalty (with the major exception of certain international and promoter penalties which do not currently any right to an administrative hearing) that may be avoided by showing reasonable cause, and generally occurs after the penalty is assessed, but before collection. Activities to collect the penalty are suspended during the appeals process.

Penalties associated with filing of the tax return are assessed, including those for late filing and late payment. Taxpayers can protest the penalty when they receive the billing notice. If the Service Center agrees with the taxpayer, the penalty is abated. If it rejects the taxpayer's explanation, a letter is sent to the taxpayer that outlines the process to file a written protest with Appeals.

Often only the most complex reasonable cause determinations are handled by the penalty appeal procedure, and the Appeals Officer can consider hazards of litigation. Appeals has 90 days to dispose of the penalty case. Most penalty cases are resolved only in writing or with telephone conversations between Appeals and the taxpayer. Conferences are only granted if the Appeals Officer believes they are necessary.

If the case involves a civil fraud penalty, the Appeals Office has the authority to eliminate it in any case not docketed in the Tax Court. During the period Appeals has jurisdiction over a Tax Court case there is also exclusive authority to eliminate the fraud penalty. Appeals may also partially concede the fraud penalty at less than 75% allowed by statute. If the case is

recommended for prosecution on criminal tax violations, Appeals can only concede or eliminate the fraud penalty with consent of area counsel.

More information about penalties is found at IRM Part 20; reasonable cause information is found at IRM 20.1.1.3.2.

#### **TRUST FUND RECOVERY PENALTY**

IRC §7501 provides a penalty for those who fail to pay over taxes that are required to be collected and withheld from other persons. The so called “100% penalty” is equal to 100% of the trust fund taxes. To be liable for the trust fund recovery penalty (TFRP) the person must be responsible (IRM 5.7.3.3.1) and must have willfully failed to collect or pay over the trust fund taxes. Unless collection of the TFRP is in jeopardy, the taxpayer must be given a preliminary notice (Letter 1153) at least 60 days before the date of notice and demand for payment. Appeals rights must be exercised within 60 days of this letter.

Appeals will have information developed by the Revenue Officer to justify imposition of the TFRP, including copies of bank statements and interview forms from the taxpayers and others.

**PRACTICE NOTE:** Be sure to carefully examine each quarter and whether TFRP exposure applies as circumstances can change during a tax year.

### **AFTER APPEALS, WHAT FOLLOWS?**

For income tax deficiencies, if the amount of tax either remains in dispute after Appeals, the taxpayer fails to respond, or the 30 day period expires, the IRS issues a notice of deficiency. For CDP cases the IRS issues a Notice of Determination.

#### **NOTICE OF DEFICIENCY**

In order for the Tax Court to have jurisdiction in a deficiency proceeding, the IRS must first determine that a deficiency exists. There is no required format for a notice of deficiency and not all demands for money permit a taxpayer to file a petition. The notice must identify that it is a ‘notice of deficiency,’ indicate an amount of tax due and the taxable period. If the notice of deficiency indicates a calculation of tax for several years, but only seeks a deficiency for one year, the Tax Court will only have jurisdiction over the specified year.

Also called the 90 day letter, this notice gives the taxpayer 90 days in which to file a petition with the Tax Court for a redetermination of the proposed deficiency. The taxpayer has 150 days to file the petition if the notice is mailed to an address out of the United States, or if the taxpayer is out of the country on the entire 24 hour period in which the notice is mailed. There are no extensions of time permitted. If the taxpayer’s petition is not filed in time, the Tax Court has no jurisdiction.

It is critical that the taxpayer not eliminate a deficiency before the notice of deficiency is issued; without a deficiency, there is no Tax Court jurisdiction. If a taxpayer makes a payment on a deficiency before the notice is issued, the amount of the payment is considered assessed and thus removed from Tax Court jurisdiction. Under §6213(b)(4) taxpayers can make a full or partial payment of an asserted deficiency after the notice is issued; this stops applicable interest and penalties from accumulating without losing Court jurisdiction.

### **NOTICE OF DETERMINATION**

In order for the Tax Court to have jurisdiction over non-examination cases the IRS generally must issue a notice of determination. If the taxpayer does not agree with Appeals' determination, judicial review is requested by petitioning the Tax Court for review. For CDP cases the taxpayer has 30 days to file a petition after receiving the notice of determination.

### **JUDICIAL REVIEW**

Taxpayers can generally choose to have their disputes heard in the United States District Court, the United States Claims Court or Bankruptcy Court, or in the United States Tax Court. All CDP cases are heard in the Tax Court. There are several advantages to using the Tax Court:

- the taxpayer does not have to prepay the amount of tax in controversy (but interest accrues on the underlying deficiency while the matter is under Court jurisdiction or on appeal).
- no trial by jury is permitted.
- judges are experts in tax law.
- discovery is restricted, and in general the proceedings are less formal and less expensive than those in other court venues.
- unless the notice of deficiency was issued by the IRS Appeals Division, all cases docketed to the Tax Court are subject to review by appeals, so filing a petition generally offers another administrative opportunity to settle the tax controversy with the IRS.
- small tax cases involving less than \$50,000 in income, gift, or estate tax can be heard in a less formal setting than regular cases.

Two elements are required to grant jurisdiction to the Tax Court for a deficiency case:

- a Notice of Deficiency issued by the IRS to the taxpayer's last known address  
--- AND ---
- a petition filed timely by the taxpayer (90 days generally).

The Tax Court can determine that a taxpayer owes more or owes less than indicated on the notice of deficiency.

Two elements are required to grant jurisdiction to the Tax Court for a collection case:

- a Notice of Determination issued by the IRS to the taxpayer's last known address

--- AND ---

- a petition filed timely by the taxpayer (30 days by statute).

When the underlying tax liability is properly at issue, the Tax Court reviews the determination de novo (for the first time). Under §6330(c)(2)(B), if the taxpayer receives a notice of deficiency and fails to file a petition for review with the Tax Court, the taxpayer cannot challenge the existence or amount of the tax liability in a CDP hearing; the Tax Court evaluates the CDP for Commissioner's abuse of discretion.

N/A/E/A



## **APPENDIX A – SAMPLE PROTEST LETTER**

### **P R O T E S T**

RE: Mr. and Mrs. Sample Clients • SSN: XXX-XX-XXXX  
Form 1040 • Tax year 200512 and 200612

Dear Mr. Revenue Agent:

We request a face-to-face conference with an Appeals Officer to review and discuss the IRS findings noted below.

We respectfully disagree and protest the examiner's report dated 8/22/08 on Form 4549-A for the 2005 tax year (which shows a balance due of \$16,563.60 and for the 2006 tax year (which shows a balance due of \$18,241.64). We supplied the examiner with the necessary and relevant documentation to justify business deductions claimed on the return for office supplies, repairs and maintenance, business meals including those related to the Taxpayer's Kiwanis Club and automobile travel related to his chiropractic business activities. In the few instances where there are not 100% receipted expenses, we feel the estimates requested are reasonable. Furthermore, we feel each of the deductions claimed is ordinary and necessary under Internal Revenue Code §162.

Relevant contact information for the taxpayer's representative is repeated below for your convenience:

Sherrill L Trovato, MBA, MST, EA, USTCP  
11300 Bluebell Avenue • Fountain Valley, CA 92708-1708  
Daytime phone: 714.777.9359

The protest and accompanying documents are submitted by a taxpayer representative. The facts stated in the protest are true and correct to the best of her knowledge and belief.

Sherrill L Trovato, MBA, MST, EA, USTCP

Enclosure:

Form 2848, Power of Attorney

August 22, 2008 Letter 950 – last date to respond is 9/22/08

Form 4549-A, Income Tax Discrepancy Adjustments

Other Expenses 200512 and 200516

## APPENDIX B – SAMPLE PROTEST LETTER PENALTY

# PROTEST

RE: Taxpayer, LP • EIN XX-XXXXXXX  
6/4/12 • #XX • LTR 854C  
Tax Year 2010 • \$11,700 §6698(a)(1) penalty

Dear Penalty Appeals Coordinator:

We disagree with the IRS's failure to abate this penalty. We believe we will provide the appropriate criteria to evaluate the penalty abatement request in this letter, but if the Penalty Appeals Coordinator does not concur, we request a face-to-face conference with the local Appeals Officer to review and discuss the above referenced penalty abatement request.

Our grounds for the appeal are as follows:

1) the proposed penalty under §6698(a)(1) is for \$11,700 based upon the number of partners (5) and the number of months the 2010 return was late. A copy of CP162 is provided with the original abatement request that is attached to this protest.

The actual abatement denial was based upon §6651 (see #XX dated 6/4/12). If that is the proper code section applied to this penalty abatement request, there is no penalty due since that late filing penalty is 5% of the amount of tax due. This is a partnership return, thus there is no tax due upon which the penalty can be calculated.

2) We believe the appropriate criteria to evaluate this request is found in Rev Proc 84-35 and under IRC §6231(a)(B)(i), which allows for an exception for small partnerships that has 10 or fewer partners, each of whom is an individual, a C corporation or an estate of a deceased partner. Taxpayer, LP is a small partnership as described in §6231.

Rev Proc 84-35 provides a multi-prong test that applies to domestic partnerships:

- 1) there are less than 10 partners, all of whom are natural citizens
- 2) there is no special allocation – each partner's share of each partnership item is the same as the partner's share of every other item
- 3) every partner timely filed and reported their respective share of income

Taxpayer, LP meets all these tests and has not elected to be subject to the rules for consolidated audit proceedings. There are 5 partners, all of whom are natural citizens. There was no special allocation. Additionally Taxpayer, LP is compliant with all tax return filings.

We previously requested reasonable cause relief for the late filing penalty as shown in a copy of the April 30, 2012 letter (see copy). Please also evaluate the penalty abatement request under Rev Proc 84-35. If you have any questions, please contact me.

The protest and accompanying documents are submitted by a taxpayer representative. The facts stated in the protest are true and correct to the best of her knowledge and belief.

Sherrill L Trovato, MBA, MST, EA, USTCP

Enclosures:

#XX, 6/4/12

4/30/12 original abatement request including POA and CP162 5/7/12

NAMEA

## APPENDIX C: LETTERS AND NOTICES GIVING APPEAL OPPORTUNITY

- **Letter 11 – Final Notice of Intent to Levy and Notice of Your Right to a Hearing**, notifies of unpaid taxes and an intent to levy to collected the amount owed
- **Letter 525 – General 30 Day Letter**, with computation of proposed adjustments. Protest required within 30 days to appeal proposed adjustments.
- **Letter 531 – Notice of Deficiency**, judicial review in Tax Court if petition is filed within 90 days.
- **Letter 692 – Request for Consideration of Additional Findings**, outlines options if taxpayer disagrees with proposed adjustments. Protest required within 15 days to appeal proposed adjustments.
- **Letter 915 – Letter to Transmit Examination Report**. Protest required within 30 days.
- **Letter 950 – 30 Day Letter-Straight Deficiency or Over-Assessment**. Protest required within 30 days.
- **Letter 1058 – Final Notice Reply Within 30 Days**. Must file Form 12153, Request for A Collection Due Process Hearing within 30 days (statutory time).
- **Letter 1085 – 30-Day Letter Proposed 6020(b) Assessment**, notifies of levy to collect tax due. **Must file Form 12153, Request for A Collection Due Process Hearing within 30 days** (statutory time).
- **Letter 1153 – Trust Funds Recovery Penalty Letter**, notifies of IRS efforts to collected trust funds. Protest within 60 days.
- **Letter 3016 – IRC Section 6015 Preliminary Determination Letter (30 Day)**, gives 30 days to appeal the termination of innocent spouse relief.
- **Letter 3391 – 30-Day Non-filer Letter**, notifies proposed adjustments for nonfilers. Protest required within 30 days.
- **Letter 3727 – 30-Day Letter Notifying Taxpayer No Change to Original Report Disallowing EIC Based on Failure to Meet Residency Test for Children Claimed**. Protest within 30 days.
- **Letter 3728 – 30-Day Letter Notifying Taxpayer No Change to Original Report Partially Disallowing EIC Based on Failure to Meet Residency Test for 1 Child**. Protest within 30 days.
- **Letter 3172 – Notice of Federal Tax Lien Filing and Your Rights to a Hearing under IRC 6320**. Must file Form 12153, Request for A Collection Due Process Hearing within 30 days (statutory time).
- **CP 90 – Final Notice of Intent to Levy**. Must file Form 12153, Request for A Collection Due Process Hearing within 30 days (statutory time).
- **CP 92 – Notice of Levy upon Your State Tax Refund**. Must file Form 12153, Request for A Collection Due Process Hearing within 30 days (statutory time).
- **CP 242 – Notice of Levy upon Your State Tax Refund**. Must file Form 12153, Request for A Collection Due Process Hearing within 30 days (statutory time).
- **CP 523 – IMF Installment Agreement Default Notice**, the IRS will terminate the installment agreement in 30 days. Follow instructions in the notice to request an appeal.
- **CP 2000 – IRS proposes adjustments to the tax return when 3<sup>rd</sup> party information does not match the tax return**. Protest to the issuing office/individual within 30 days.

Source: [irs.gov](http://irs.gov)

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## ENDNOTES

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1 *Estate of Jerry Weiss v Comm'r*, TCM 2005-284 (12/13/05)

2 IRS Document 7225, "History of Appeals," 7 (NOV 1987)

<sup>3</sup> IRS, DataBook, Table 21, Appeals Workload by Type of Case.

4 Comment made in June 2004 at an ALI-ABA conference in Boston, MA attended by the author

<sup>5</sup> *Industrial Investors v Comm'r*, TCM 2007-93

6 *Michael Craig v Comm'r*, 119 TC 15 (11/14/02)

7 *John R Rivera v Comm'r*, TCS 2003-55

8 *Montgomery v Comm'r*, 122 TC 1 (2004)

9 *Drina L McCorkle v Comm'r*, TCM 2003-34

10 *Ernest Collins v Comm'r*, TCM 2003-293