IRS PROCEDURES FOR EXAMINATIONS, APPEALS, AND TRIALS LOOKING BACK FROM THE OUTSIDE

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Chapter 13

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I INTRODUCTION

The authors of this paper collectively have more than sixty (60) years of experience in handling tax controversies before the Internal Revenue Service ("IRS") and the United States Tax Court ("Tax Court"). Mr. Tackett was a former Estate Tax Attorney with the IRS during which time he examined (audited) hundreds of taxable estates and gifts, was detailed periodically to old District Conference and Appeals to handle appeals of unagreed estate or gift tax cases, and also served as one of the first Estate Tax Attorneys on staff in the Austin Service Center handling a wide variety of substantive and procedural matters relating to federal estate and gift tax returns filed in the then Southwest Region. Mr. Brantley is an experienced trial lawyer and was a Senior Counsel in the Office of Chief Counsel of the IRS where he represented the government in complex federal income and estate/gift tax litigation. Mr. Brantley received the Office of Chief Counsel Special Act Award as lead counsel for the IRS in Estate of Stangi v Commissioner, T.C. Memo 2003-145 (Strangi III)., a widely reported and important estate tax case.

It is the purpose of the authors of this paper to share not only some procedural and substantive law dealing with the examination, appeal, and trial of estate and gift tax cases, but also to share some of their personal insights and experience both inside and outside the IRS in doing so.

II SCOPE AND DEFINED TERMS

This paper is concerned primarily with the examination (i.e., audit) of Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return ("Form 706")and with the appeal and/or trial of unagreed cases involving same. This paper is intended to be a general summary of the many issues and matters which the personal experiences of the authors have shown should be carefully considered both prior to and after the filing of the federal estate tax return. With regard to the preparation of the tax return itself, the paper is not intended to replace a number of published papers addressing the preparation of Form 706 essentially on a line-by-line basis or the .printed Instructions to Form 706, which are prepared by the Internal Revenue Service (the "IRS"), and a close review of those Instructions is always highly recommended as the starting point in the preparation of any Form 706. In addition to the Instructions for Preparing Form 706, it is recommended that you also obtain a copy of and familiarize yourself with the following IRS publications from the IRS website at www.irs.gov:

- Publication 1, "Your Rights as a Taxpayer"
- Publication 5, "Your Appeal Rights and How To Prepare a Protest If You Don't Agree"
- Publication 216, "Conference and Practice Requirements"
- Publication 556, "Examinations of Returns, Appeal Rights, and Claims for Refund"
- Publication 557, "Survivors, Executors, and Administrators"
- Publication 947, "Practice Before the IRS and Power of Attorney"
- Publication 950, "Introduction to Estate and Gift Taxes"
- Publication 3498, "The Examination Process"
- Publication 3498-A, "The Examination Process By Mail"
- Publication 4227, "Appeals"
- Publication 4245, "Power of Attorney"
- Circular No. 230, "Regulations Governing the Practice of Attorneys, Certified Public Accountants, Enrolled Agents, Enrolled Actuaries, And Appraisers Before the Internal Revenue Service"

In general, this paper utilizes a chronological approach to the authors' discussion of various problems or issues encountered by the Practitioner and taxpayer in the same sequence such problems or issues might arise during the normal course of the preparation, filing, and examination of Form 706 or Form 709 and in the trial of unagreed cases in the Tax Court.

As noted previously, the primary emphasis of the paper will be on Form 706, but most of the matters discussed herein will also have equal application to Form 709, United States Gift (and Generation-Skipping Transfer) Tax Return ("Form 709"). Although this paper deals primarily with audit and trial techniques and procedures, discussion of substantive law matters is necessarily required on occasion. You are advised that, except where specific statutory or regulatory authority or case law is cited, the opinions expressed in this paper are only the personal and professional opinions of one or both of the authors.

Unless otherwise indicated, all Section references in this paper are references to the Internal Revenue Code of 1986 (the "Code"), as amended, and the terms "Service" or "IRS" shall both refer to the Internal Revenue Service. Although agents or attorneys of the Service presently "examine" rather than "audit" returns, these terms have been used interchangeably throughout this paper. References to "IRM" will refer to the Internal Revenue Manual published by the Service.

With regards to any references in the paper to the Internal Revenue Manual or to any other IRS publications, a strong word of caution is warranted. The IRM and other IRS publications continue to undergo extensive revisions due to the ongoing reorganization of the Service, and many of the references in this paper to those publications are likely to change over time.

III RESTRUCTURING OF THE INTERNAL REVENUE SERVICE

A. IRS RESTRUCTURING AND REFORM ACT OF 1998

The Restructuring and Reform Act of 1998 ("RRA '98") was enacted by Congress and was intended to substantially reorganize and restructure the IRS. See Public Law No. 105-206, enacted on July 22, 1998, 105th Congress, 2d Session. The Service refers to this major restructuring as "modernization."

Although primarily driven by taxpayer and Congressional dissatisfaction with existing IRS performance and service (or more importantly, the actual or perceived lack thereof), a number of other related factors were probably also significant in the successful effort to restructure and reorganize the Service. For example, at the time of the reorganization, the total number of IRS employees was declining, and the IRS, as a governmental agency, was shrinking when compared to the economy as a whole. At the time of the reorganization, enforcement revenues from audit and/or collection activities of the Service accounted for only approximately 2% of all of the tax revenues then collected by the IRS. Consequently, with approximately 98% of the collected tax revenues then coming from non-enforcement activities, the Service needed to give more attention and apply more resources to the areas of taxpayer service and assistance in the voluntary reporting and payment of taxes. The past tax strategies and business practices of the Service were to a large degree determined by, and constrained by, the existing organizational structure which was deemed outmoded and not in conformity with general business practices and strategies which had proven successful in other private and public sectors of the economy. Finally, there had been increasing horror stories and criticism about "heavy-handed" enforcement activities (both audit and collection) which have undermined the support and reputation of the Service in the eyes of both the Congress and the public at large.

B. NEW IRS STRUCTURE

The RRA '98 directed the Commissioner of Internal Revenue ("Commissioner") to restructure the existing IRS by eliminating or substantially modifying the former three-tier geographic structure (national office, regional office, and district and local field offices) and replacing it with an organizational unit structure that emphasizes functional "operating units" serving particular categories of taxpayers with similar needs. See Joint Committee on Taxation, Summary of the Conference Agreement of HR 2676. The IRS Restructuring and Reform act of 1998, (JCX-50-98R), June 24, 1998. The Commissioner of Internal Revenue

remains the Chief Executive Officer of the IRS and continues to be appointed by the President, with the advice and consent of the Senate. There was, however, a significant reduction in the lower layers of management, including the elimination of the former position of District Director.

The new and modernized IRS is intended to be structured and operated around specific groups of taxpayers with relatively similar needs. The key operational units for the restructured IRS are 4 new Operating Divisions, each charged with full "end-to-end" responsibility for serving a designated class of taxpayers with similar needs. The 4 Operating Divisions are (1) Wage and Investment (W & I), (2) Small Business and Self Employed (SB/SE), (3) Large and Mid-Size Business (LMSB), and (4) Tax Exempt and Government Entities (TE/GE). Each new Operating Division generally has full responsibility and authority for serving a defined set of taxpayers, including customer education and assistance and compliance interaction (i.e., audit and collection activities).

The current responsibility for the processing and handling of estate and gift tax returns has been assigned by the IRS to the Small Business and Self-Employed Division. ("SB/SE"). The SB/SE Operating Division has a full compliance field organization assigned and associated with it, including both an examination and collection group. Various existing Service Centers were aligned with the new SB/SE Operating Division, including the Cincinnati Service Center. Although it continues to be referred to as a “Service Center” in IRS publications, within the IRS it is commonly referred to as the “Cincinnati Campus.”

Beginning in January, 2001, taxpayers were instructed by the Service to start sending specific tax returns to specific Service Centers designed to focus on specific customer segments. Therefore, the previous old Service Center activities which were historically based primarily on a taxpayer's geographic location without regard to the type of return or tax involved were reassigned to a specific Service Center primarily based on the type of return or tax, as well as the taxpayer's geographic location.

The Cincinnati and Ogden Service Centers were initially designated by the Service to handle the receipt and processing of the business tax returns for the SB/SE Operating Division, which business returns included both estate and gift tax returns. By the end of the 2002 filing season, the Service directed that all estate and gift tax returns be filed directly with the Cincinnati Campus. Pertinent information regarding the Cincinnati Campus is as follows:

(1) Mailing Address
Department of Treasury
Internal Revenue Service Center
Cincinnati, Ohio 45999

(2) Physical Address*
201 W. Rivercenter Boulevard
Covington, Kentucky 41011
(* yep, the Cincinnati campus is actually located across the river in Kentucky)

(3) Toll-Free Number
Estate and Gift Tax Operation
866-699-4083

IV PRACTICE BEFORE THE IRS

A. IN GENERAL

Practice before the IRS is regulated by the Director of the Office of Professional Responsibility (the "Director") who is appointed by the Secretary of the Treasury. The Director is responsible for administering and enforcing the regulations governing such practice. The regulations are published by the IRS in pamphlet form as Treasury Department Circular 230. See Treasury Department Circular 230 (Rev. 4-2008), "Regulations Governing the Practice of Attorneys, Certified Public Accountants, Enrolled Agents, Enrolled Actuaries, Enrolled Retirement Plan Agents, and Appraisers Before the Internal Revenue Service," Title 31 C.F.R., Subtitle A, Part 10, published September 26, 2007.

B. WHAT IS PRACTICE

Pursuant to Treasury Circular 230, practice before the Service comprehends all matters connected with presentation to the IRS or any of its officers or employees relating to a taxpayer's rights, privileges, or liabilities under laws or regulations administered by the IRS. See Section 10.2(a)(4). A person is considered to "practice" before the IRS if he or she (1) communicates with the IRS for a taxpayer regarding such taxpayer's rights, privileges, or liabilities under laws or regulations administered by the Service, (2) represents a taxpayer at conferences, hearings, or meetings with the IRS, (3) prepares and files documents with the IRS, or (4) corresponds and communicates with the IRS on behalf of a taxpayer. However, the mere furnishing of information at the direction or request of the IRS is not considered practice before the IRS. Likewise, merely appearing as a witness for a taxpayer is not considered practice.

C. WHO CAN PRACTICE

Generally, attorneys, certified public accountants, enrolled agents, enrolled actuaries, and enrolled retirement plan agents (referred to collectively as "Practitioners") can represent taxpayers before the IRS, if they are properly licensed and not currently under suspension or disbarment from practice. Under certain circumstances, other persons, including unenrolled tax return preparers, can also represent taxpayers before the Service for limited purposes. For example, individuals may represent themselves, a family member can represent members of his or her immediate family, an officer of a corporation, association, organized group or governmental unit can represent the organization of which he or she is an officer, a general partner can represent the partnership, a regular full-time employee can represent the employer, and a fiduciary can represent the entity it serves. Unenrolled return preparers, however, may represent taxpayers only concerning the tax liability for the period covered by the return in question, and may do so only before the Examination function of the IRS, and not before Collection, Appeals, or any other function of the IRS. For additional information on the qualifications and enrollment of persons to practice before the IRS, see Sections 10.3 through 10.8 of Treasury Department Circular 230; IRS Publication 947, "Practice Before the IRS and Power of Attorney"; and IRS Publication 470, "Limited Practice Without Enrollment."

D. RULES OF PRACTICE

Subpart B of Treasury Department Circular 230 sets forth and imposes both specific duties and certain restrictions on Practitioners who practice before the Service. See Sections 10.20 through 10.38. In addition, Practitioners cannot be incompetent or engage in "disreputable conduct," which is defined in Section 10.51. Practitioners who neglect or fail to comply with these Rules of Practice or otherwise engage in disreputable conduct are subject to disciplinary action by the Office of Professional Responsibility and/or suspension or disbarment from practice before the IRS by the Secretary of the Treasury after notice and opportunity for a proceeding. See Sections 10.50 through 10.82.

Practitioners have the following affirmative duties under Treasury Department Circular 230 in regard to practice before the Service.

1. Duty to Furnish Information. Practitioners must promptly submit records or information requested by officers or employees of the IRS, unless they believe in good faith and on reasonable grounds that the requested information or records are privileged. See Section 10.20. This duty and the issues of privilege and work product are becoming ever increasingly important in current audits.

2. Duty to Advise. A Practitioner who knows that a taxpayer has not complied with the tax laws or has made an error in or omission from any return or other document required to be filed with the IRS has the duty to advise the client promptly (not the IRS) of the non-compliance, error, or omission, and to also advise the taxpayer of the consequences of such

noncompliance, error, or omission. See Section 10.21.

3. Duty of Due Diligence. Practitioners must exercise due diligence in preparing, approving, and filing tax returns and other papers with the IRS, in determining the accuracy of oral or written representations made by them to the Service, and in determining the accuracy of oral or written representations made by them to clients with reference to any matter administered by the IRS. See Section 10.22.

4. Duty Regarding Tax Shelters. Practitioners who provide tax shelter opinions analyzing the federal tax effects of a tax shelter investment have a duty to comply with certain stringent requirements regarding their preparation. See Sections 10.35 through 10.37.

In addition to the affirmative duties noted above, Practitioners are also "restricted" under Treasury Department Circular 230 from engaging in certain designated conduct or practices. For example:

(a) Delays. Practitioners must not unreasonably delay the prompt disposition of any matter pending before the IRS. See Section 10.23.

(b) Improper Assistance. Practitioners must not knowingly directly or indirectly (a) employ, (b) accept assistance from, or (c) accept employment as associate, correspondent or subagent from any person who is under disbarment or suspension from practice before the Service. Practitioners are also prohibited from sharing fees with any such persons. Practitioners may not accept assistance from any former government employee where the provisions of Section 10.25 of Treasury Department Circular 230 or any other federal law would be violated. See Section 10.24.

(c) Practice by Former Government Employees, Their Partners and Associates. Practice before the Service is restricted under certain situations for former government employees, their partners, and their associates. See Section 10.25.

(d) Notaries. Practitioners employed as counsel, attorney, or agent in a matter pending before the IRS, or who otherwise have a material interest in such matter, may not engage in any notary activities relative to such matter. See Section 10.26. Therefore, when representing a client before the Service, do not act as a notary on any document you intend to submit to the Service.

(e) Fees. Practitioners may not charge an "unconscionable fee" for representation of a client before the Service. Practitioners are also prohibited from charging a contingent fee for services rendered in connection with any matter before the IRS, except those specific situations listed in Section 10.27(G).

(f) Conflicting Interests. Practitioners cannot represent parties with conflicting interests before the Service, except by the express consent of all directly interested parties (presumably including the IRS) after full disclosure has been made. See Section 10.29.

(g) Solicitations. Practitioners are restricted in regard to their advertising and solicitation of clients with respect to matters pending before the Service. See Section 10.30.

(h) Refund Checks. Practitioners who prepare tax returns must not endorse or otherwise negotiate any check issued to a taxpayer by the government in respect of a federal tax liability. See Section 10.31.

E. STANDARDS FOR ADVISING CLIENTS

In preparing tax returns, documents, affidavits, or other papers submitted to the IRS, a Practitioner must follow the standards set forth in Section 10.34.

F. NEW PREPARER PENALTIES

The Small Business and Work Opportunity Act of 2007 expanded the application of the return preparer penalties of Section 6694 and Section 6695 to preparers of federal estate and gift tax returns. In an interim guidance Memorandum SBSE-04-0509-009, dated May 8, 2009, the IRS issued procedures for IRS Estate Tax Attorneys to open preparer penalty cases. Provisions of the Memorandum were scheduled for incorporation into IRM 4.25.1 by April 24, 2010.

Preparers of Forms 706 and Forms 709 filed after May 25, 2007, can expect additional scrutiny of those tax returns for a possible imposition of these so-called "return preparer penalties".

Section 6694 provides penalties against tax return preparers due to an understatement of a taxpayer's liability due to "unreasonable positions" taken on a tax return. Under current law, an undisclosed position may be considered to be generally "unreasonable" unless there is or was substantial authority for it. If the position was disclosed (but isn't a position dealing with tax shelters or other reportable transactions), the position is unreasonable unless there is a reasonable basis for it. A "reasonable basis", although a lower standard than "substantial authority", is still a relatively high standard for tax reporting and is significantly higher than "not frivolous". According to the IRS, the reasonable basis standard is not satisfied by a return position that is merely "arguable".

The return preparer penalty is not to be proposed until the estate or gift tax audit is concluded and is not to be discussed by the Estate Tax Attorney in the presence of the taxpayer. Although the Estate Tax Attorney is strongly advised that the estate or gift tax examination is to be separate and distinct from any proposed return preparer penalty case, one can anticipate that more preparer penalty cases will be associated with unagreed examination cases. Practitioners should anticipate questions regarding documents received from the taxpayer, compensation paid, length of representation, facts and authorities relied on for any certain tax position taken on the return, meetings with taxpayer pertaining to those issues, and specifically whether the Practitioner is "aware" of errors, omissions, or mistakes on the return.

Where preparer penalties under Section 6694(b) and Section 6695(f) are asserted against a Practitioner authorized to practice before the Service, a referral to the Office of Professional Responsibility is also mandatory.

G. PROPOSED PREPARER TAX IDENTIFICATION NUMBERS

The IRS has proposed that all paid tax return preparers obtain a preparer tax identification number ("PTIN") which will be reflected on all tax returns or claims for refund filed after December 31, 2010. The IRS expects that Practitioners can obtain a PTIN online once the system is established, and the IRS expects that there will be a three (3) year registration fee between $75 and $300.

During the initial application process and subsequent thereto, Practitioners may be subject to personal tax compliance checks regarding their own personal filings and tax payment obligations, and any criminal background they might have.

V POWERS OF ATTORNEY AND TAX INFORMATION

A. IN GENERAL

Taxpayers may either represent themselves before the IRS or designate a representative to do so. Generally, the designated person must be a person authorized to practice before the Service as previously

discussed. If the taxpayer wants to have the designated person "represent" them before the Service, then either IRS Form 2848, Power of Attorney and Declaration of Representative, or a non-IRS Power of Attorney acceptable to the Service must be filed. Form 2848 is generally preferable to use for this specific purpose.

B. TAX INFORMATION AND AUTHORIZATION (FORM 8821)

A Power of Attorney form is not required to be filed with the Service if the taxpayer merely wants the IRS to disclose tax information to a designated person or entity, regardless of whether or not the person is authorized to practice before the Service. For this purpose (i.e., disclosure of tax information only), the taxpayer can file IRS Form 8821, Tax Information Authorization, instead. Form 8821 is strictly a disclosure authorization form and cannot be used to designate a person to represent a taxpayer before the Service.

C. POWER OF ATTORNEY (FORM 2848)

A Power of Attorney is the taxpayer's written authorization for a designated person to act for and/or represent the taxpayer in tax matters before the IRS. Use of IRS Form 2848 is highly recommended. If the Power is not limited, generally the designated representative or attorney-in-fact can perform most of the acts that the taxpayer can do. If the taxpayer wants the representative to represent him or her at a conference before the IRS or wants the representative to prepare and file any written response to the IRS, then a Power of Attorney form will be required whether or not the representative performs any of the other acts authorized by Form 2848 or any non-IRS Power. Generally, the taxpayer can only appoint a representative who is a Practitioner authorized to practice before the Service or is a person listed in Part II, Declaration of Representative, on Form 2824. The taxpayer may use Form 2848 to designate an unenrolled return preparer as a representative only as specifically provided in Publication 470, "Limited Practice Without Enrollment."

A taxpayer may specifically authorize the designated representative to substitute another representative or to add additional representatives by expressly adding such authority to line 5 of Form 2848.

A copy of Form 2848 should be filed with each IRS office with which the Practitioner is dealing. If there are no matters currently pending before the IRS, file the original Form 2848 with the Cincinnati Service Center where the related tax return was, or will be, filed. If the tax return was not previously filed, attach a copy of Form 2848 to the tax return for information purposes. It is recommended that the copy attached to a return be stamped "copy" so that it will not be mistaken by the Service for an original Power and removed from the return.

The IRS currently maintains a Centralized Authorization File ("CAF") in its Service Centers to maintain a file containing information regarding the authority of persons appointed under Forms 2848. The purpose of the CAF is to give Service personnel quicker and greater access to this information. Practitioners who represent clients before the IRS will be assigned a nine-digit CAF number. If you do not have a CAF number at the time, enter “None” on line 2 of Form 2848 and the IRS will issue you a CAF number. The CAF number is different from the new PTIN proposed to be assigned to all tax return preparers as previously discussed in Article IV.G. of this paper.

The IRS will accept a copy of a Form 2848 (and Form 8821 as well) that is submitted by facsimile transmission. Forms 2848 may be faxed directly into the CAF Unit at the Cincinnati Service Center where the related tax return was, or will be, filed.

Form 2848 may be revoked by either sending a "revocation copy" of the original Form 2848 itself to each IRS office where the form was previously filed or the taxpayer may submit a written "revocation statement" to the same IRS offices. Unless the taxpayer has specified otherwise, a subsequently filed Form 2848 for the same tax matter will automatically revoke a

previously filed Form 2848, but not a previously filed Form 8821.

Although the IRS will accept qualified non-IRS Powers of Attorney, the information in such document cannot be entered on the CAF. Generally, the authors do not recommend the routine use of non-IRS Powers.

For additional information regarding the preparation and uses of Powers of Attorney or other tax information authorizations, refer to IRS Publication 947, "Practice Before the IRS and Power of Attorney"; IRS Publication 216, "Conference and Practice Requirements"; and Instructions to IRS Form 2848 and Form 8821.

VI PREPARATION AND FILING OF RETURNS

A. IN GENERAL

Preparation for the audit of any tax return LOGICALLY begins with the careful preparation of the return itself. Prior to preparing the return, it is first necessary that all the decedent's pertinent records and documents be carefully scrutinized and that detailed consideration be given to any factual and/or legal issues which might be raised by such items. The initial review of all of the papers, documents and records of the decedent is often done by the personal representative(s) of the decedent's estate without the direct assistance or participation of the Practitioner. Therefore, in preparing both probate inventories and tax returns, it is common that the Practitioner will necessarily be required to rely substantially upon the information and/or documents supplied to the Practitioner by the personal representative(s) or by third parties. It should be noted that in preparing a tax return or in advising a client with respect to a position taken on a tax return, a Practitioner may generally rely in good faith, without independent verification, upon information furnished by the client. However, the Practitioner may not ignore the logical implications of information or documents furnished to, or actually known by, the Practitioner, and must make reasonable inquiries if the information provided appears to be incorrect, inconsistent, or incomplete. See Treasury Department Circular No. 230, §10.34(a) (3). The Practitioner should always employ the same techniques as those of the Estate Tax Attorney and closely review and consider all of the facts and information provided to him or her for both accuracy and overall consistency with the other facts or documents provided. As a general rule, if an error or omission is subsequently discovered after the return is prepared and filed, the return can be "supplemented" or a claim for refund filed for the estate. With the expansion of tax preparer penalties under Section 6694 and Section 6695 to estate and gift tax returns, all "tax positions" taken or disclosed on the tax return to be filed should be closely scrutinized in light of those new penalty provisions.

B. FILING REQUIREMENTS

The filing requirements for both federal estate and gift tax returns can most easily be determined by reference to the Instructions to Form 706 or Form 709, respectively. The Practitioner should take care to use the latest revision to such tax forms and instructions. The latest available revision to Form 706, United States Estate (and Generation-Skipping Transfer) Tax Return, is September 2009, and the latest revision to Form 709, United States Gift (and Generation-Skipping Transfer) Tax Return, is 2009. The latest revision to the published Instructions for each tax form corresponds to the date of revision of the form itself. Forms for prior years can be found on the IRS website at www.irs.gov. The actual statutory filing requirement for each type of return in set forth as follows:

1. Estate Tax Returns. The statutory filing requirements for federal estate tax returns are set out in Section 6018 of the Code. The Executor or other personal representative of the estate has the primary duty to file such return. See §6018 (a); Reg. 20.6018-2. However, if the Executor is unable to file a complete return, then the heirs, distributees, or third parties in possession or control of any of the property of the decedent may also be required to prepare and file a Form 706 for the

estate. See §6018 (b). Prior to 2010 and presumably in 2011 and thereafter, a federal estate tax return must be filed for a citizen or resident when the gross value of the estate exceeds the applicable exclusion amount in effect for the calendar year of the decedent's death, subject, however, to certain specified reductions. Therefore, it is the size of the gross estate and not whether any tax is actually due and payable which is the criteria to determine if Form 706 must be filed. If the gross estate is below, but close to, the statutory filing requirement, the taxpayer may still wish to file a return, particularly if (a) the estate consists of any hard-to-value assets such as real estate or closely-held business interests, or (b) the estate is determined to be below the statutory filing requirement because of one or more undisclosed "tax positions" taken with regard to the estate which the Service might find to be "unreasonable".

2. Gift Tax Returns. The statutory filing requirements for federal gift tax returns are set out in Section 6019 of the Code. If a federal gift tax return is required to be filed, it is generally the duty of the donor to file such return. If the donor dies prior to filing the required return, then it becomes the duty of the Executor or other personal representative of the donor's estate to file such return. See §6019; Reg. 25.6019-1.

3. Executor Defined. For federal tax purposes the definition of an Executor is much broader than that under local probate law. The term "Executor" means the duly appointed, qualified, and acting Executor or other personal representative of the decedent's estate. However, if no Executor or other personal representative is appointed, qualified, and acting within the United States, then every person in either actual or constructive possession of any of the decedent's property situated in the United States is "deemed" by federal law to be a statutory "Executor" for federal tax purposes and thereby becomes charged with the statutory duty to prepare and file the requisite federal estate and/or gift tax returns. See §2203; Reg. 20.2203-1; §6018(a); Reg. 20.6018-2. With an increasing number of decedents having done their estate planning by use of a revocable trust/pour-over Will plan, rather than just a traditional Will, if the pour-over Will is not admitted to probate and an "Executor" appointed by the Probate Court (or if such will is probated as a muniment of title only), then the Trustee of the revocable trust will find itself as a "statutory Executor" under the Code along with an affirmative duty to file an estate tax return for the decedent, if one is due.

If there are Co-Executors, all are jointly required to file the return together, although it is sufficient for only one of the Co-Executors to sign the return. See Reg. 20.6018-2; Instructions for Form 706, Signature and Verification, Page 2.

C. TIME TO FILE

1. General Rule. Section 6075 of the Code and its corresponding Regulations set forth the original statutory due dates for the filing of both the federal estate tax return and the federal gift tax return. See §6075; Reg. 20.6075-1; Reg. 25.6075-1. The published Instructions to both Form 706 and Form 709 also discuss in detail when each return is required to be filed.

2. Timely Mailing. Section 7502 of the Code and its corresponding Regulations set out certain circumstances under which the timely mailing of federal estate or gift tax returns will be treated as the timely filing of such returns. See §7502; Reg. 301.7502-1. As of July 30, 1996, the IRS was authorized to expand the timely-mailed-is-timely-filed rule to designated private delivery services. Section 7502(f) of the Code. The names of the IRS-approved private delivery services which can currently be used by the taxpayer are set forth on page 2 of the Instructions to Form 706.

3. Saturday, Sunday or Holiday. Section 7503 of the Code and its corresponding Regulations prescribe procedures for the timely filing of returns when the original due date for filing a return or for paying the tax due falls on a Saturday, Sunday or legal holiday. §7503; Reg. 301.7503-1.

D. EXTENSIONS OF TIME TO FILE AND/OR PAY TAX

1. Extension of Time to File. In cases where it is either impossible or impracticable for the Executor to file a reasonably complete return within the prescribed statutory time limit, the Service may, upon showing of good and sufficient cause, grant a reasonable extension of time to file the subject return.

Extensions of time to file an estate tax return are requested on Form 4768 and should be filed on or prior to the due date of the estate tax return. Currently, an estate will be allowed an automatic 6-month extension of time to file, if Form 4768 is timely filed. See Treas. Reg. 20-6081-1(b); Part II of Form 4768 and Instructions to Form 4768. Although the Service has the discretion to grant an extension of time to file that is filed late, it is the Service's position that failure to timely file Form 4768 before the due date may indicate negligence and constitute sufficient grounds for denial of the extension to file. See Treas. Reg. 20.6081-1(c). However, a U.S. District Court has recently held that the IRS' "summary denial" of a late-filed extension request without consideration of it on its merits was an abuse of discretion, and that the IRS cannot reject an extension request where good and reasonable cause existed without a legitimate reason. See Estate of Proke v United States, 2010 WL2178968 (D.N.J. May 25, 2010).

An extension of time to file a gift tax return can be obtained in two (2) ways. First, an extension of time to file the taxpayer's Form 1040 made on Form 4868 or Form 2350 will automatically extend the time (up to six (6) months) to file a Form 709. Second, if a donor is not requesting an extension of time to file his or her personal income tax return, then Form 8892, Application for Automatic Extension of Time to File Form 709 and/or Payment of Gift/Generation-Skipping Transfer Tax, may be used. See Form 8892 and Instructions; IRM 21.7.5.4.7.2.

An extension of time to file Form 706 or Form 709 does not extend the period of time for paying any estate or gift tax due with those returns. Therefore, a separate request for an extension of time to pay estate or gift tax must also be made.

Extension of Time to Pay. Upon a showing of reasonable cause, the Service may also grant an extension of time to pay all or any part of the taxes required to be shown on the return. See §6161; Reg. 20.6161-1; Reg. 25.6161-1.

Extensions of time to pay estate tax can also be made on Form 4768 at the same time an extension to file Form 706 is requested. You should always request a corresponding six (6) month extension of time to pay any estate tax which might be due on Form 706 when it is filed, unless such tax is paid with Form 4768 when it is filed with the Service.

An extension of time to pay gift taxes, however, cannot be requested on Form 8892, and a separate written request for payment of gift taxes due should be submitted with Form 8892 when it is filed.

Requests for extensions of time to file returns and to pay estate or gift tax due are filed with and processed by the Cincinnati Campus. See IRM 4.25.1.5.7.

Unlike an extension of time to file a return which is untimely filed, an extension of time to pay tax under Section 616 will not be considered unless the extension is filed timely. See Treas. Reg. 20.6166-1(b). For additional procedures for processing extensions of time to pay, see IRM 5.5.5.

E. WHERE AND HOW TO FILE

1. Where to File. Historically, estate and gift tax returns were filed with the Regional Service Center serving the geographic area where the donor lived and/or the decedent was domiciled at time of death. As part of the restructuring of the IRS, the Service has now

directed that all Forms 709 and Forms 706 be filed with the Cincinnati Campus.

2. How to File. The return should be filed directly with the Cincinnati Campus as directed by the Instructions. The Service Center has procedures to accept and acknowledge receipt of tax returns sent by either registered or certified mail, if verification of a specific received date by the Service is required or desirable. The authors recommend that all returns and most other documents mailed to the Service always be sent by registered or certified mail, return receipt requested.

F. COMPLETENESS OF RETURN

1. In General. The tax return should be as complete as .possible in all respects, and all required questions should be answered on the return. Failure to properly complete the return and thoroughly explain the entries therein can increase the return's chances of being at least "tentatively" selected for audit.

2. Documents and Information Required with Return. The Regulations and the Instructions to both Form 706 and Form 709 set out various documents and information that are required to be attached to or filed with the returns. These include such documents as certified copies of Wills, trust documents, Form 712, various tax elections and various other documents required to substantiate the entries made on the returns. Reg. 20.6018-3; Reg. 20.6018-4; Reg. 25.6019-3; Reg. 25.6019-4; Instructions to both Form 706 and Form 709.

3. Omitted Items or Entries. Failure to attach the required documentation or to fully address the factual or legal issues raised by specific entries on the return may "red flag" the return during the classification of the return. At the time of the initial classification of the return, the classifier is routinely reviewing a large number of returns to select only those returns which show the highest audit potential. A thorough and complete return, with all factual and legal issues identified and adequately discussed, will generally have a better chance of being "accepted as filed" rather than being selected for an audit. If the estate has previously been granted an extension of time to file the return and/or to pay the tax thereon, but Form 4768 is not attached to the return, delinquency penalties may be assessed upon processing of the return. If required tax elections are not attached to the return, then substantial tax benefits might be lost to the estate,

4. Incomplete Entries on Returns. Both federal estate and gift tax returns are initially processed at the Cincinnati Campus where they are reviewed for statutory form and proper execution and then math verified for accuracy. Failure to make complete and accurate entries on the appropriate lines of the returns or a failure to properly complete one or more required schedules of the return to support an entry made may result in a delay in the processing and acceptance of the return or even a recompilation by the Service Center of the tax reported on the return, with a resulting tax notice being sent to your client. For example, a marital deduction claimed and entered on the return may be reduced to "0" on the initial processing of the federal estate tax return if there is no supporting "Schedule M" attached to Form 706 which reflects the amount of property passing to the surviving spouse corresponding to that entry.

G. MISCELLANEOUS MATTERS

1. Decedent's Gift Tax Returns. In addition to preparing and filing any unfiled federal gift tax returns which may be required to be filed for the decedent, the personal representative of the estate also needs to accurately determine the previous gift history of the decedent, if any, in order to determine the correct amount of the decedent's "adjusted taxable gifts" for federal estate tax purposes. If the Executor is unsure if the decedent has ever filed any gift tax returns, the Executor may request copies of all of the decedent's previously filed federal gift tax returns, if any, from the Service under provisions of Section 6103(e)(3) of the Code. Under certain conditions set forth in Section 2204(d) of the Code, a good faith reliance by the personal representative of an estate on the documents furnished to it by the Service may serve to discharge the Executor

from any personal liability for any federal estate tax deficiency which might be attributable to an increase in the "adjusted taxable gifts" which may finally be required to be reflected on decedent's Form 706.

2. Credit for Tax on Prior Transfers. It is also advisable to obtain copies of all prior estate tax returns, audit reports, Estate Tax Closing Letters, inheritance tax returns, and any other information or documents required to substantiate a claimed credit for tax on prior transfers to the Service. If necessary, copies of the needed tax returns to substantiate the credit can be requested by the personal representative from the Service under authority of Section 6103(e)(l)(E) of the Code.

3. Notice of Fiduciary Relationship. Every person qualified and acting for another person in a fiduciary capacity is required to give notice thereof to the Service in writing. See Section 6036 and Section 6903. Form 56, Notice Concerning Fiduciary Relationship, is used for this purpose. The Form should be filed with the Cincinnati Campus where Form 706 has, or will be, filed and should be transmitted separately from the federal estate tax return. Proper filing of Form 56 will insure that all tax notices from the Service concerning the decedent's income, estate, or gift tax returns are directed to the personal representative. See §6903; Reg. 301.6903-1. A subsequently filed Form 56 can also be used to inform the service of the termination of a fiduciary relationship. The Service has begun to return Forms 2848, Power of Attorney, filed by Practitioners on behalf of fiduciaries who do not have a filed Form 56 on record.

4. Discharge of Personal Liability. The Executor can make a request for a prompt audit of a decedent's income, gift, and estate taxes, and for a discharge from personal liability for any tax deficiency thereafter found to be due on those returns. Within nine (9) months after the receipt of such request, the Service is to notify the Executor of any tax deficiency owed for those taxes. The Executor, on payment of any tax of which he is notified, or upon the expiration of the aforesaid nine (9) months is discharged from personal liability for payment of any tax deficiencies later assessed by the Service. See Section 2204 for estate tax and Section 6905 for decedent's income and gift tax. The filing of an Application for discharge pursuant to Section 2204 and/or Section 6905 does not shorten the Services statute of limitations for assessment of such taxes, but merely affects the Executor's personal liability for their payment. A request for discharge from personal liability can be made on Form 5495.

5. Request for Prompt Assessment. The Executor may also file a written request for a "prompt assessment" of a decedent's income and gift taxes (but not estate taxes). If such a request is filed, the normal 3-year statute of limitations for assessment of such taxes is reduced to 18 months. Such request is made pursuant to Section 6501(d) of the Code and is made on Form 4810. See Section 6501(d).

6. Section 645 Election. Form 8855 may be filed by the Executor and Trustee of a qualified revocable trust (QRT) to permit the QRT to be treated and taxed (for income tax purposes) as a part of its related estate. See Section 645.

VII PROCESSING OF RETURNS

A. FILING WITH CINCINNATI SERVICE CENTER

The initial processing of both Form 706 and Form 709 is now handled at the Cincinnati Campus.

B. CONTROL NUMBER

Both estate and gift tax returns are processed using the decedent's social security number. It is imperative that the correct social security number be used.

C. PROCESSING OF RETURNS

1. Receipt of Returns. Upon receipt of a tax return at the Cincinnati Campus, the return is "date-stamped" and any payment

accompanying the return is detached for crediting to the proper taxpayer account. Prior to final processing, the return will be assigned a digit document locator number (the so-called "DLN") for Internal Revenue Service control purposes. A portion of this DLN reflects the Gregorian calendar date on which the tax return was filed, and this number may be used to establish timely filing of the returns and any elections thereon or therewith. If the return is received by registered or certified mail, a record of such receipt is kept at the Service Center, and a return receipt to the taxpayer will be acknowledged if requested.

2. Verification of Returns. Before computer processing of the return takes place, it is first reviewed by Service Center personnel to insure that the return is properly executed and that the appropriate schedules and required documents are attached to the returns. In addition, each schedule is manually verified for any mathematical or clerical errors (i.e., obvious entries on the wrong line of the return) and such errors are corrected during processing. If any correction made to the return at the Service Center results in a change to the tax reported on the return as filed, the taxpayer will receive a computer-generated tax notice informing the taxpayer of the error and of the amount of any additional tax due or overpayment resulting from the correction of the mathematical or clerical error made on the return.

The Cincinnati Campus may also verify the valuation of listed and over-the- counter securities as a part of the return classification process.

3. Elections, Extensions and Penalties. During the initial processing of the return at the Cincinnati Campus, other matters requiring "special handling" are identified (i.e., Section 6166 elections, Section 2204 requests, etc.), and the returns are coded to reflect such matters. The assessment or waiver of any delinquency penalties on the return is also initially considered at this time and all statements or affidavits regarding "reasonable cause" for such delinquency are reviewed at the Service Center prior to assessment of the penalties.

4. Association with Gift Tax Returns. After processing, all federal estate tax returns are associated with any Forms 709 which the decedent may have previously filed.

D. ASSESSMENT OF TAX ON ORIGINAL RETURN

The Service has been given statutory authority to assess all taxes voluntarily determined or reported on federal tax returns filed by the taxpayer. This statutory authority also extends to the assessment of any interest or penalty due on such disclosed tax. See §6201(a)(l); Reg. 301.6201-1.

E. DEFICIENCY DEFINED

The term "deficiency" for federal estate or gift tax purposes means the amount by which the correct federal estate or gift taxes as finally imposed or determined exceeds the excess of the sum of the tax shown by the taxpayer on the original return plus any amounts previously assessed as a deficiency over the amount of any tax abatements. See §621 l(a); Reg. 301.6211-1.

F. ASSESSMENT OF A DEFICIENCY

1. Statutory Notice Required. Except for certain special limited exceptions (i.e., jeopardy assessments, bankruptcy and receivership cases, etc.), a statutory "deficiency" may not be assessed by the government until a formal Notice of Deficiency (the so-called "90-Day Letter") has been sent to the taxpayer by registered or certified mail, and such 90-day period has expired (150 days if the Notice of Deficiency is addressed to a person outside the United States). See §6212 and §6213.

2. Petition to Tax Court. Upon receipt of a statutory Notice of Deficiency, the taxpayer has 90 days (or 150 days as the case may be) to file a petition in the Tax Court requesting a predetermination of the purported deficiency. If such petition is timely filed, then no assessment of the proposed deficiency can be

made by the government, and no levy or other court proceedings for its collection may be made by the Service until the decision of the Tax Court has become final. See §6213; Reg. 301.6213-1. The trial in the Tax Court of an unagreed case is discussed in more detail later in this paper.

G. MATHEMATICAL AND CLERICAL ERRORS ON RETURNS

1. Corrected at Service Center. As previously discussed, all mathematical or clerical errors appearing or disclosed on the original return are "corrected" by the Service Center during the initial processing of the return.

2. Not a Deficiency. The amount of any understatement of tax resulting from such mathematical or clerical errors does not legally constitute a "deficiency" under Section 6211 of the Code and may be assessed by the Service Center without issuance of a formal Notice of Deficiency. In addition, the computer-generated notice received by the taxpayer from the Service Center informing him of a mathematical or clerical error on the return and the resulting adjustment to the tax reflected on the return is not a Notice of Deficiency, and, therefore, the taxpayer may not file a petition in Tax Court to prevent either its assessment or enforced collection by the Service. See §6213(b)(l).

3. Abatement on Demand. Within sixty (60) days after notice of an assessment resulting from a mathematical or clerical error is sent, the taxpayer may request abatement (i.e., removal) of such assessment and the Service Center is required to abate the tax. Thereafter, any reassessment of the tax must be made through normal deficiency assessment procedures, which means that the return will be selected for audit or examination. See §6213(b)(2)(A).

H. SUPPLEMENTAL RETURNS

1. Omitted or Newly Discovered Assets. After the filing of the original estate or gift tax return, the personal representative, donor or Practitioner may discover additional assets of the estate, additional gifts, or identify other errors or omissions on the return as filed which are sufficient enough to warrant consideration of the revision or correction of the original return previously filed. If such errors or omissions will result in a reduction (i.e., overpayment) of the tax previously reported, assessed, and paid, such corrections are properly reportable on Form 843, Claim for Refund. If such corrections, however, would result in an increase to the gross estate or gross gifts of the decedent or donor, then such additions are typically reported on a so-called "supplemental return."

2. No Amended Estate Tax Returns. Except as permitted under Reg. 20.2032A-8(d) and Reg. 20.6166-l(h), the federal estate tax return may not technically be "amended" after the expiration of the due date for filing the original return (including any period of extensions). See Reg. 20.608l-l(c). The Regulations, however, do specifically provide that "supplemental information" may be subsequently filed with the Service which may result in a finally determined tax different from that reported on the original estate tax return. It is not too surprising therefore, that such supplemental information is often presented to the Service in the Form of an "amended" or “supplemental” Form 706. If a supplemental return or information is filed which reflects a decrease in tax previously reported, it will be treated as an informal claim. As a general rule it is preferable to report any decrease in tax using Form 843, Claim for Refund, to which a supplemental or amended return or schedules might be attached to reflect the items on the return resulting in such tax decrease and reflecting the corrected calculation of the tax due.

3. Assessment of Additional Tax. Unless the statute of limitations for assessment has expired, any amount of additional taxes shown on the supplemental or amended return is treated under Section 6201(a)(l) as amounts voluntarily shown by the taxpayer "upon his return," and such amounts are routinely assessed by the Service without going through formal deficiency assessment procedures. However, if

the applicable statute of limitations for assessment under Section 6501 of the Code has already expired, the Service cannot make an additional assessment of tax unless such assessment is "voluntarily" requested by the taxpayer, and then only to the extent that additional taxes and/or interest are voluntarily paid by the taxpayer with such request. Voluntary payments of tax that are assessed and paid after the expiration of the period of limitation on assessment may be refunded to a taxpayer if a claim for refund is timely filed within the 2-year period after payment of such amount. The Service is prohibited from making any effort, real or implied, to solicit voluntary payments of any deficiency or delinquent account that is banned by statute. See IRS Policy Statement P-4-65; IRM 4.2.1.5. However, voluntary payments made freely by the taxpayer will be accepted and assessed. See IRM 1.2.1.4.18.

4. Issues to Consider. Frequently in estate administrations an omitted asset may surface after the return has been accepted or even audited by the Service and the normal statute of limitations for assessment (i.e., the 3-year statute) may or may not have yet expired. If the value of the omitted asset is not significant and the statute has expired, the taxpayer might consider merely forwarding an information letter to the Cincinnati Campus where the return was filed disclosing the omitted asset or assets as a part of the decedent's gross estate, but without requesting a "voluntary" assessment of any additional taxes and without making any "voluntary" payment of tax with such notification. In making such notification to the Service, the taxpayer should consider the application of Section 6501(e)(2) of the Code (dealing with substantial omissions of items from the gross estate or from the total amount of gifts of a donor). The mere disclosure of an omitted asset to the Service, without a request for a voluntary assessment and payment of the resulting tax, generally means that the estate will not be issued a "revised" Estate Tax Closing Letter. Because the statutory discharge of any estate tax liens on the newly discovered asset is frequently the primary or sole reason for reporting the omitted asset in the first place, the personal representative may have no real option but to request a voluntary assessment of the additional tax and to make payment of such tax and interest with his request.

There has been much discussion, and disagreement, among Practitioners within professional organizations and on list services on whether or not a taxpayer has a duty to file a supplemental estate tax return, and whether a Practitioner has a duty to inform/insist that the taxpayer do so, when a material item is discovered after the original tax return has been filed. Frankly, both the Code and Regulation are devoid of any provisions that expressly require a taxpayer to do so. While the Regulations indicate that in certain circumstances, a taxpayer "should" file an amended income tax return, there is no similar provision in the Regulations regarding an "amended" estate tax return. There is some judicial authority that a supplemental return may not be required. See Badaracco vs United States, 464 US at 393; Estate of Williamson, TC Memo 1996-426. The question of a Practitioner's duty under Circular 230 is far from clear. At best, it appears that a Practitioner may have duty to advise his client of the omission, but not otherwise.

VIII CLASSIFICATION OF RETURNS

A. ESTATE TAX RETURNS

After the initial processing of a federal estate tax return is completed by the Cincinnati Campus, all Forms 706 are now centrally classified at the Cincinnati Service Center, primarily by Estate Tax Attorneys detailed into the Service Center for that purpose. The Service Center also has some Estate Tax Attorneys permanently assigned to its staff. Returns selected for audit are sent to the audit groups for assignment, and the Service Center personnel prepares and mails Closing Letters on those returns which are accepted as filed. Should you need to inquire regarding the status of a particular return, you can contact the Estate Tax Group at the Cincinnati Service Center at 1-866-699-4083. If you have not received your Closing Letter within 6 months after the return was filed, there is a good possibility that the

return has at least been "tentatively" selected for audit.

B. GIFT TAX RETURNS

Forms 709 are generally classified by Estate Tax Attorneys detailed into the Cincinnati Service Center for that purpose. However, most examinations of Forms 709 have historically been a direct result of the audit of decedent's estate tax return, but Practitioners are reporting increased audits of Forms 709, particularly those reflecting the transfer of "discounted" business interests.

C. SELECTED RETURNS

Returns that are selected for examination by the Cincinnati Campus are sent to the appropriate Estate Tax Group to be assigned to an Estate Tax Attorney in the Group for audit. All of the returns are not immediately assigned to an Estate Tax Attorney for audit and some of the returns selected may be suspended by the Group in a so-called "Ready File" until the workload within the Group permits the Supervising Attorney to assign the selected case to an individual Estate Tax Attorney for audit. Although tentatively selected for audit, prior to the time that the Executor or Practitioner is actually contacted by the Estate Tax Attorney, the return may still be "surveyed" or accepted without examination by either the Supervising Attorney or the assigned Estate Tax Attorney. If surveyed, the return is returned to the Cincinnati Campus for final administrative processing.

IX AUDIT OR EXAMINATION OF RETURNS

A. WHO IS THE EXAMINER

Since 1968, graduation from an accredited law school and bar membership have been prerequisites to employment in the Estate Tax Groups, and examiners hold a commission as an "Estate Tax Attorney." In addition to a legal background, the Estate Tax Attorney will also have gone through specialized training courses in estate and gift tax laws and probably will have received some additional classroom instruction in the valuation of various types of assets, including real estate and closely held business interests.

In 2006, the Service announced that it planned to reduce the total number of Estate Tax Attorneys it employs nationwide to 157 positions. That planned reduction represented almost 50% of the 345 Estate Tax Attorneys it then employed. At this time, the Service has approximately 200+ Estate Tax Attorneys in its audit groups and on the Cincinnati Campus.

What are some possible effects of such reduced number of Estate Tax Attorneys on your case? A few possibilities are:

(1) Nationwide audit assignments are possible and the Estate Tax Attorney you deal with may not be located geographically near you.

(2) Professional relationships with service personnel may become harder to develop and maintain.

(3) Your Estate Tax Attorney may have little knowledge and less experience with local probate, trust, real estate, or property law.

(4) The Estate Tax Attorneys today generally have little, if any, administrative staff support and they have reduced resources for travel or appraisals.

(5) A number of Estate Tax Attorneys are nearing retirement which will only eventually increase the problems of number and lack of experience.

(6) Some of the last hired Estate Tax Attorneys were transferred within the Service from the Office of Chief Counsel and come to the table with the mindset of a "trial lawyer" and not a "fact finder".

B. INITIAL CONTACT

Most audits will be instituted by the Estate Tax Attorney by letter advising the Executor and Practitioner of the selection of the

return for examination. Generally, the Estate Tax Attorney will also inform the Practitioner of any additional information or documents which he or she will want to see or obtain during the course of the examination. If the valuation of real property is to be a major issue in the audit, the Estate Tax Attorney will frequently want to schedule an appointment to physically inspect the property in question. Although it is stated policy of the Service that examinations of returns selected for audit are to be initiated within 9 months of the date of filing of the return and completed within 18 months of that date, fewer and fewer audits are meeting these guidelines.

C. AUTHORITY OF PRACTITIONER

1. Declaration on Return. Page 2 of Form 706 contains a Declaration to be signed by the Practitioner authorizing the Service to release or discuss confidential tax information with the person listed, and also authorizing the named Practitioner to represent the taxpayer before the Service unless otherwise expressly extended. The instructions to Form 706 provide that by completing this Authorization on page 2 of the return one attorney, accountant, or enrolled agent may receive such confidential tax information. However, if the Practitioner has not already obtained either Form 2848, Power of Attorney, or Form 8821, Tax Information Authorization, signed by the Executor, the Estate Tax Attorney will frequently request that the Practitioner provide such form at or prior to the initial audit conference.

2. Form 2848. Form 2848, Power of Attorney, is used to grant more comprehensive authority to the Practitioner representing the estate before the Service. Form 8821 only authorizes the Practitioner to receive and inspect confidential tax information. If necessary or desirable, the power to execute tax returns and/or to redelegate authority to a substitute representative might be specifically added to Form 2848. The Practitioner should remember that, as with other non-durable Powers of Attorney, the Practitioner's authority to act will be terminated by the death or incapacity of the principal (i.e., the Executor or donor).

3. Representative Identification Numbers. The Service has established a Centralized Authorization File (CAF) at the service Centers to identify Practitioners who practice before the Service and the scope of their authority. The stated purpose and benefits of this CAF system are to permit the Service's computers to automatically generate copies for the Practitioner of all tax notices and computer-generated correspondence. The Practitioner should enter his assigned CAF number on all Forms 2848 or Forms 8821 filed with the Service.

D. SCOPE OF AUDIT

The Estate Tax Attorney is instructed to pursue only significant issues in an audit and to review all unusual large or questionable items reflected on the return. Although the Service instructs its Estate Tax Attorneys to specifically limit the focus or scope of their audits to substantial and material tax issues, recent audits have involved very time-consuming and expensive document and information production. See Appendix A for a recent example of the production required in an audit involving real estate and a family limited partnership.

E. TIME LIMITATION ON AUDIT

As previously noted, it is the stated policy of the Service to conclude its examination of the federal estate tax return within 18 months after the filing of the return. See IRM 1.2.1.4.16, P-4-52 (Approved 02-02-1959). Unfortunately, for a variety of reasons, many audits, particularly those involving family limited partnerships, are not getting started on a timely basis, and the authors have had a number of occasions where the audit was not concluded until immediately prior to the statute of limitations on assessment expiring, thereby precluding the taxpayer from having a right to a conference with the Appeals Office prior to the assessment of the proposed tax deficiency.

F. SECTION 2204 ELECTIONS

If the personal representative has filed an application for discharge of personal liability under Section 2204 of the Code, the Estate Tax Attorney is instructed to give priority to the examination of the return in order to determine the amount of any deficiency due by the estate within the 9-month period provided for by the statute. In reality, however, an election under Section 2204 generally neither increases the chances of an audit nor necessarily guarantees a more expeditious examination of the return if it is selected.

G. INCOME TAX RETURNS

During the course of the audit, the Estate Tax Attorney is required to review the decedent's final Form 1040, the Form 1040 for a full year preceding the date of death, and all Forms 1041 filed for the estate and any trusts. In preparing the estate tax return, the Practitioner should obtain copies of these returns for his or her file and review the returns for any apparent audit issues. The Estate Tax Attorney will inspect these returns to look for omitted assets such as interest on certificates of deposit or other savings, dividends paid on unreported stocks, unreported livestock, or crops deductions claimed on real estate or other assets, etc. In addition to estate tax issues, if the Estate Tax Attorney believes that the income tax returns provided to him reflect income tax issues of sufficient compliance value to warrant a separate audit of those returns by a Revenue Agent, the Estate Tax Attorney will prepare a so-called "information report" which sets out the nature of the potential audit issues. These information reports are subsequently reviewed and classified by Revenue Agents and those showing the highest audit potential may be assigned for field audit of the appropriate income tax return or returns.

If the decedent was the beneficiary of one or more trusts created by third parties (i.e., a bypass or QTIP trust), the Estate Tax Attorney may occasionally also want to review all Forms 1041 filed for those trusts as well.

H. CONDUCT OF AUDIT AND CONFERENCES

1. In General. The careful preparation of the return and organization of the file prior to examination of the return can greatly simplify the audit by having most, if not all, of the requested information on hand and available for the Estate Tax Attorney to review. In addition, the prior consideration (and perhaps legal research) of those issues which the Practitioner believes are most likely to be raised by the Estate Tax Attorney on audit can greatly assist the Practitioner in staying in control of the audit. The single most important rule to remember during the conduct of the audit is "LET THE ESTATE TAX ATTORNEY TAKE THE INITIATIVE IN THE CONDUCT OF THE AUDIT." Often those valuation matters or legal issues which the Practitioner is most concerned about frequently are not raised or only minimally reviewed by the Estate Tax Attorney during the audit.

2. Attendance of Executor at Conferences. The question of whether or not the Executor attends all or any of the audit conferences is basically a decision to be made by the Executor and the Practitioner. Occasionally, the Estate Tax Attorney will specifically request that the Executor be present, but such requests are the exception rather than the rule. Most Practitioners prefer to meet alone with the Estate Tax Attorney, at least prior to the time that the Estate Tax Attorney is ready to present his final "proposed" adjustments for consideration. A few Practitioners, however, like to fill their office or conference room with the Executor, family members, accountant, appraisers, etc. It is the personal preference of the authors to meet alone with the Estate Tax Attorney since we believe such conferences are much less formal and are more conducive to a frank exchange of information and opinions.

3. Discussion of Issues. The Estate Tax Attorney will generally begin audit conferences with discussion of any routine matters before moving to the more controversial items. Frankly, this procedure is a good one for both the Practitioner and the Estate Tax Attorney

to follow, and many of the less significant issues can be satisfactorily disposed of in this manner. Section 7521 allows either the taxpayer or the Service to audio record (not video) the "in person" interviews upon 10 days notice to the other side.

4. Major Audit Issues. Items which tend to be particularly good about attracting an audit are:

(a) a "yes" answer to any of the disclosure questions on the return;

(b) indication that assets have been sold or that sales are pending;

(c) litigation, particularly will contests, noted on the return;

(d) life insurance trust;

(e) inter vivos trust (looking for gifts from trust within 3 years of date of death);

(f) substantial gifts prior to death, particularly if made by an attorney-in-fact;

(g) disclosure of assets, the value of which are omitted from the gross estate;

(h) unanswered questions on Schedule G of the return;

(i) large tracts of real property;

(j) large mineral properties;

(k) family limited partnership, limited liability company, or other closely held business; and

(l) ANY MENTION OF THE WORD "DISCOUNT."

5. Authority of Examiner. Although the Estate Tax Attorney is responsible for the audit of the return and for the development of the facts and law applicable to the issues in controversy, the Practitioner should always remember that, unlike the Appeals Officer, the Estate Tax Attorney has not been delegated settlement authority by the Service and is not authorized to settle the case on the basis of "hazards of litigation." The Estate Tax Attorney, therefore, is required to "negotiate" with the taxpayer on the basis only of the law and facts applicable to the case however, the lines between "settlement" and "negotiation" often get blurred, and, therefore, some basis for compromise with the Estate Tax Attorney can generally be found.

6. Closing the Audit At the conclusion of the audit, the Estate Tax Attorney will make his or her audit adjustment proposals to the Executor and/or to the Practitioner. Depending on the acceptance or non-acceptance of such proposals by the Executor, the Estate Tax Attorney will close the audit of the return in one of the following ways: (1) no change, (2) agreed or partially agreed, or (3) unagreed. Each of these audit actions are discussed more fully below.

I. "NO-CHANGE" CASES

Frankly, most returns selected for audit are going to produce some change in tax to the estate or donor. It may be either a deficiency or a refund, but some tax change usually results. Indeed, the criterion for selection of the return for audit initially was that the return contained at least one audit issue likely to result in a tax change. On occasion, however, the Estate Tax Attorney will agree that there are simply no adjustments to be made to the return, and the examination will be closed. In such cases, the Executor will be advised that the return is being accepted as filed, and no official audit report will be sent to the Executor by the Estate Tax Attorney. Since the primary purpose of the classification process is to select those returns with the highest audit potential, it is not too surprising that the Estate Tax Attorney will generally show great reluctance to simply "no change" a case. Therefore, an agreement on one or more of the minor audit issues resulting in either a small increase in tax or a small refund of

tax is often preferable to the Estate Tax Attorney.

J. AGREED CASES

1. Waiver. If the Executor or donor wishes to conclude the examination on an "agreed basis" and accepts the final tax and valuation adjustments proposed by the Estate Tax Attorney, the Executor or donor will be requested to execute Form 890, Waiver of Restrictions on Assessment and Collection of Deficiency and Acceptance of Assessment-Estate and Gift Tax (the "Waiver"). This Waiver reflects the agreement of the Executor or donor to the assessment of the tax deficiency and/or penalty adjustments reflected on the Waiver. It further authorizes the Service to assess such amounts without the issuance of the formal statutory notice of deficiency otherwise required by Section 6212 of the Code.

2. Payments and Interest Assessments. Upon receipt of a signed Form 890, the Estate Tax Attorney will date and initial the Waiver to evidence its "official" date of receipt. The Practitioner should advise the client that the amounts reflected on the face of Form 890 do not include the statutory interest which will be assessed in addition to the tax and penalty shown on the Waiver. If the taxpayer wishes to stop the accrual of additional interest on the agreed tax deficiency, an advance payment of the amount of the tax deficiency should be submitted to the Estate Tax Attorney along with Form 890. Indeed, the Estate Tax Attorney is instructed to solicit an advance payment of the tax deficiency. This advance payment will be credited to the taxpayer's account, and interest on the tax deficiency paid will be assessed by the Service only up to the date of receipt of such payment. Interest, however, will also be due on the interest assessed but unpaid, and the client should be advised accordingly. If the taxpayer wants to pay all amounts due with Form 890 (i.e., tax, penalty and accrued interest), the Estate Tax Attorney should be able to calculate that amount. If payment of the tax deficiency is not submitted with Form 890, then upon assessment of the deficiency, the Service will also assess statutory interest on the deficiency up until 30 days after the received date reflected on the Waiver or until the actual date that payment of the tax deficiency is received, if earlier. Interest on the tax deficiency and upon the accrued interest on such deficiency will also be assessed. The taxpayer will subsequently receive a Notice of such assessment from the Service Center and will have 10 days from the date of such notice to make payment thereof before interest begins to run again.

3. Audit Report and Closing Letter. Following the receipt of the Waiver, the Estate Tax Attorney prepares an official examination report (the so-called "RAR"). Most Estate Tax Attorneys have direct access computers and such reports are now routinely computer-generated. After preparation of this RAR, the administrative file is returned to the Service Center for final administrative actions as needed. The Cincinnati Service Center now issues Closing Letters on all estate tax returns.

K. POST-AUDIT REVIEW

Although an agreement with the Estate Tax Attorney may have been obtained, the Practitioner should be aware that the Estate Tax Attorney's report and agreement are subject to an administrative quality control process within the Service. This review process consists of a verification of the mathematical computations made on the Examination Report as well as a technical review of the issues examined by the Estate Tax Attorney. If major errors are found by the Supervising Attorney or other reviewer, the case is returned to the Estate Tax Attorney for further action or response by the attorney. Although rare, it is possible that an assumed "agreement" with the Estate Tax Attorney may not, in fact, be ultimately accepted and the administrative file will be returned to the Estate Tax Attorney for further audit or correction of the Examination Report.

L. PARTIAL AGREEMENTS

It is not necessary that the Executor agree with all of the Estate Tax Attorney's proposed adjustments in order to close part of

the audit on an agreed basis. The Executor may execute a Form 890, Waiver, only with respect to those adjustments which the Executor is in agreement with the Estate Tax Attorney and not agree to any other audit proposals made by the Estate Tax Attorney. In such cases, the Estate Tax Attorney will prepare two reports: (1) an agreed report covering only those issues agreed upon, and (2) an unagreed report dealing with all remaining audit issues that were not agreed upon. The Executor may also wish to pay the agreed portion of the "proposed" tax deficiency while continuing to maintain the estate's right to contest those valuation or legal issues covered by the unagreed report. A partial agreement with a payment of the agreed portion of the proposed tax deficiency can reduce the overall interest cost to the estate or donor. Some Practitioners seem to believe that an "all-or-nothing" tactic will somehow influence or pressure the Estate Tax Attorney into making concessions on the more controversial matters or believe that they should retain even agreed upon issues until the appeal of the case is heard in order to "horse-trade" those items with the Appeals Office. It is the personal opinion of this writer that, unless the issues in question are material and are themselves the subject of dispute, they really have very little influence on either the Estate Tax Attorney or Appeals Officer; therefore, it is recommended that, as a general rule, all audit issues should be resolved at the earliest possible date.

M. UNAGREED CASES

If the Estate Tax Attorney's proposed adjustments are not acceptable to the Executor or donor, the examination of the return will be concluded by the attorney on an "unagreed" basis. In preparing the unagreed report, the Estate Tax Attorney will often make as many adjustments to the return as possible, some of which may not have even been specifically discussed during the examination of the return. For example, it is not uncommon for the Estate Tax Attorney to deny on the report a deduction for any debt, administration expense or charitable bequest which either remains unpaid at the conclusion of the audit or which was not otherwise substantiated by the Executor at that time.

The denial of unpaid or estimated attorney fees and commissions is another favorite adjustment of the Estate Tax Attorney on unagreed reports. Although most, if not all, of these items can be easily substantiated and corrected upon appeal of the Estate Tax Attorney's findings, it can often be confusing to the client, and somewhat embarrassing to the Practitioner, to explain how the Estate Tax Attorney's "proposed $50,000 tax deficiency" has suddenly become the $90,000 or $100,000 deficiency reflected on the Estate Tax Attorney's official audit report. Therefore, if an agreement cannot be reached with the Estate Tax Attorney, the Practitioner should determine from the Estate Tax Attorney what specific adjustments to the return he or she intends to make on the RAR and provide the Estate Tax Attorney with satisfactory documentation that the debts, commissions, attorneys fees and/or state death taxes claimed on the return have either been paid or satisfactorily provided for. At this point the unagreed tax deficiency cannot normally be assessed by the Service, and the estate or donor will generally be entitled to an administrative appeal within the Service prior to the issuance of the required statutory Notice of Deficiency. However if the audit has not concluded within 6 months prior to the statute of limitations for assessments expiring, the Statutory Notice of Deficiency will be issued to the taxpayer, and the right to an appeal with the Appeals Office will be lost.

X APPEALS

A. IN GENERAL

After the Estate Tax Attorney prepares his unagreed report on the audit of the return, the administrative case file will be reviewed by the Supervising Attorney or other reviewer and the case will be processed as an unagreed case.

B. 30-DAY LETTER

The IRS will send the Executor a copy of the Estate Tax Attorney's official examination

report advising the Executor that he will have a 30-day period in which to file a written protest (the "Protest") to the proposed adjustments and tax deficiency reflected in such audit report. The audit report is accompanied by IRS Publication 5 which sets out the specific requirements and procedures for preparing and filing a written Protest and for requesting a conference with an Appeals Officer in the Office of Appeals. Form 890, Waiver, is also enclosed with the 30-Day Letter in the event the Executor has changed his or her mind and now wishes to agree to the assessment of the proposed deficiency.

C. PREPARATION OF PROTESTS

In preparing Protests the Practitioner should be comprehensive and cite and discuss the facts, law and authorities on which he or she relies. This written Protest is probably the very best opportunity to convince the Appeals Officer of the merits of the taxpayer's position. Its function is similar to that of an appellate brief, and should be prepared with as much thoroughness. Traditionally, the Protests were initially received and reviewed by an Estate Tax Attorney who compares the issues and arguments set forth in the Protest and the position of the taxpayer thereon with the issues and positions previously taken during the audit of the return itself. This pre-Appeals review allows the Estate Tax Attorney to specifically review and respond to the taxpayer's arguments and authorities in his private administrative report.

D. EXTENSIONS TO FILE PROTESTS

Although there is no statutory requirement to do so, generally the Service will grant a reasonable extension of time in which to prepare and file the written Protest, if such request is made timely and for good cause. Extensions are usually granted in additional 30-day segments, and all such requests for extensions should be directed to the attention of the specific person or office reflected on the 30-Day Letter issued to the taxpayer.

E. ISSUANCE OF 90-DAY LETTER

If the written Protest is not timely filed, or an extension timely requested and obtained, the Service will issue its formal Notice of Deficiency (i.e., the so-called "90-Day Letter") advising the taxpayer that the proposed tax deficiency will be assessed unless a petition is timely filed by the taxpayer in the United States Tax Court within a 90-day period. After the 90-day period has expired, the Service may assess and collect the tax deficiency if the petition in the tax court was not timely filed by the taxpayer.

F. OFFICE OF APPEALS

If the taxpayer timely files a written Protest and requests an appeal, then the administrative case file and the taxpayer's Protest are forwarded to the Appeals Office for scheduling of an administrative hearing or appeal. The Appeals Office, however, will not generally accept a case within 6 months of the expiration of the statute of limitations. Upon receipt of the case in the Office of Appeals, it will be assigned to an Appeals Officer for hearing. At such hearing the taxpayer may be represented by the Practitioner. If the taxpayer is not present at such conference, the Practitioner will be required to file Form 2848, Power of Attorney, if the Practitioner has not previously done so with the Service. Such hearings or conferences are generally informal and generally only the Practitioner and the Appeals Officer are present. Testimony is not usually under oath, but most written information or documents are usually required to be submitted under declaration of penalty of perjury. Either side may make an audio recording (not video) of the conference upon 10 days written notice to the other side.

G. APPEALS OFFICER

The Appeals Officer holds a full-time position within the Appeals Office. At one time, many of the Appeals Officers who were assigned to hear disputed estate and gift tax cases were previously Estate Tax Attorneys themselves. This seems to be less and less

frequent. Therefore, some Appeals Officers may be former Revenue Agents, and therefore, may not have any legal training or significant practical experience in either estate and trust administration or in estate or gift tax matters. Depending upon the nature and complexity of the issues involved (and, of course, on the strengths or weaknesses of your case), you may wish to specifically request in your Protest or cover-letter transmitting same that the case be assigned to an Appeals Officer with prior estate tax training and experience.

H. SETTLEMENT AUTHORITY

Unlike the Estate Tax Attorney, the Appeals Officer has previously been delegated settlement authority for the Service and can consider the "hazards of litigation" in the resolution of the issues in the case as well as resolving any issues on the basis of law and fact. The Appeals Office has sole settlement authority for the Service over all cases which are not actually docketed for trial with the Tax Court, except for fraud cases. After a 90-Day Letter is issued and prior to the time that the case is actually docketed for trial by the Tax Court, both the Appeals Office and attorneys from the Chief Counsel's Office will jointly participate in further settlement negotiations. Some Practitioners prefer this joint settlement procedure in the belief that it puts added "pressure" on the Service to settle the case. My personal opinion is that it also puts added pressure on the taxpayer and the Practitioner, and I generally prefer to have the issues more thoughtfully considered at the Appeals Office. If an agreement cannot be obtained from the Appeals Office, once the 90-Day Letter has been issued and the petition in Tax Court filed, the Practitioner may thereafter bring Chief Counsel's Office into the negotiations at that time.

1. Agreed Cases. If an agreement can be reached with the Appeals Officer, the Executor or donor will be requested to execute either Form 890, Waiver, or Form 890-AD, Waiver. Use of Form 890, Waiver, is generally recommended because Form 890-AD contains language that purports to have the taxpayer consent to waive the right to file a claim for refund or otherwise subsequently challenge the positions agreed to with the Appeals Officer. The Appeals Officer will prepare an official report which reflects the agreement of the parties and sets forth the tax adjustments resulting therefrom. If the Executor or donor wishes to do so, payment of the agreed tax deficiency, if any, can be made to the Appeals Office along with the filing of the Waiver.

2. Unagreed Cases. If settlement of the case cannot be reached with the Appeals Officer, an unagreed report is prepared and a formal Notice of Deficiency is issued to the Executor or donor. The taxpayer will have a 90-day period following the date of mailing of this statutory Notice in which to file a petition in Tax Court. After a petition is filed with the Tax Court, the Appeals Office and Chief Counsel's Office will continue to try to negotiate a settlement of the case with the taxpayer up to the start of the session in which the case is set for trial. Thereafter, Chief Counsel's Office will have sole jurisdiction over the handling, trial and settlement of the case.

XI LITIGATION IN UNITED STATES TAX COURT

If a taxpayer has a dispute with the Internal Revenue Service (“IRS”) about the amount of a tax deficiency, he may have to resort to litigation. Depending on the circumstances, he may be able to choose which court to bring his lawsuit. Choices include:

A. FEDERAL DISTRICT COURT

One choice available to the taxpayer is the federal district court. Here the taxpayer must pay the deficiency alleged by the IRS and sue for a refund. Hence, federal district court is known as a “prepayment forum.” One advantage is that the taxpayer has the right to a jury trial if he chooses. However, many taxpayers do not want to pay the disputed deficiency as a condition of bringing a court action.

B. UNITED STATES COURT OF FEDERAL CLAIMS

If adverse precedent exists in the circuit in which the taxpayer resides, he should consider filing in the Court of Federal Claims. The Federal Courts Administration Act of 1992, P.L. No. 102-572, 106 Stat. 4506 (1992), changed the name of the United States Claims Court to the United States Court of Federal Claims. The Court of Federal Claims is the successor to the Claims Court in all respects.

C. UNITED STATES TAX COURT

Another choice available to the taxpayer is United States Tax Court ("Tax Court"). The taxpayer is not required to pay the disputed deficiency as a condition of filing suit, a distinct advantage to most taxpayers. Although there are no juries in Tax Court, the judges are knowledgeable concerning substantive tax law and tax litigation procedures. Most federal tax disputes are litigated in the Tax Court. This presentation focuses on tax litigation in Tax Court.

D. JURISDICTION OF TAX COURT

Jurisdiction refers to the authority of a court to make a legal pronouncement in a case. It is comprised of two concepts: jurisdiction over certain subject matters and jurisdiction over the parties.

1. Subject Matter Jurisdiction. Subject matter jurisdiction refers to the kind of cases a court is empowered to judge. The Tax Court's subject matter jurisdiction includes:

(a) Deficiencies. The Tax Court has the power to review and re-determine deficiencies in tax asserted by IRS in a notice of deficiency, also known as the "90-day letter." If the Tax Court's jurisdiction is properly invoked, the IRS is prohibited from assessing or collecting the disputed tax until a decision of the Tax Court becomes final. This is the most basic and often invoked jurisdictional grant. Many Tax Court cases involve alleged deficiencies in income, estate and gift tax, or excise tax on private foundations or pension plans.

(b) Overpayments. When the Tax Court obtains jurisdiction to redetermine a deficiency, it also acquires jurisdiction to determine whether there is an overpayment of the same tax by the same taxpayer for the same taxable period. Section 6512(b)(1) (unless otherwise indicated, Section references are to the Internal Revenue Code). In such cases, the Tax Court must also determine whether the taxpayer's claim for an overpayment is timely. Section 6512(b)(3); see Belloff v. Commissioner, 996 F.2d 607 (2d Cir. 1993) (holding that the Tax Court's overpayment jurisdiction allows it to decide whether an overpayment shown on a return for the year before the court was properly offset against a tax liability for another year).

(c) Interest Abatement. It has the authority to review IRS's failure to abate interest to taxpayers within certain net worth limits who bring an action within 180 days of IRS's final adverse determination, and to order abatement if IRS abused its discretion. Section 6404(i).

(d) Wrongfully Collected Amounts. It has the authority to order a refund of an amount wrongfully collected while IRS was prohibited from collecting a deficiency. In other words, if the IRS assesses and collects tax that is subject to a timely filed petition for a redetermination, the Tax Court can order a refund. Section 6213(a).

(e) Innocent Spouse Relief. It has the authority to determine innocent spouse relief when a notice of deficiency has been issued. Section 6015(e).

(f) Worker Classification Cases. It has the authority to determine worker classification in certain cases and to determine the correct amount of employment taxes. Section 7436.

2. Personal Jurisdiction. The Tax Court obtains jurisdiction over a taxpayer only if the taxpayer timely files a petition in Tax Court responding to a notice of deficiency. A notice of deficiency—also known as the 90 day letter—is the taxpayer's "ticket to Tax Court."

(a) Notice of Deficiency. If the IRS believes a taxpayer owes additional tax and the taxpayer does not agree—usually he will refuse to agree to the amount proposed in the 30-day letter—the IRS will issue a notice of deficiency, as provided by statute (hence, also known as the "statutory notice of deficiency"). It states that the IRS has determined a deficiency (in income, estate or gift tax, or excise tax on private foundations or pension plans). The notice of deficiency must describe the basis for and identify the amounts of tax, interest, additional amounts, additions to tax and assessable penalties. Section 7222. The IRS must send the notice of deficiency by certified or registered mail to the taxpayer at his "last known address."

(b) Last Known Address. The term "last known address" is a term of art about which there has developed a considerable body of case law. A detailed examination of these authorities is beyond the scope of this presentation. The basic rule is that the taxpayer's last known address is the address on his most recently filed tax return or the address given by the taxpayer to the IRS in a change of address form.

(c) Response to Notice of Deficiency. After receiving a notice of deficiency, the taxpayer has the following alternatives:

(1) Pay. Pay the tax and additional amounts and take no further action.

(2) Pay and Sue. Pay the tax and sue for refund, usually in a United States district court.

(3) Wait for Assessment. Take no action, let the tax be assessed, wait for collection action and then pay the tax or seek an offer in compromise or installment agreement.

(4) File a Tax Court Petition. The taxpayer can ask the Tax Court to re-determine the deficiency determined by the IRS by filing a petition with the Tax Court in Washington, D.C., in response to a notice of deficiency. It must be filed within 90 days (150 days if the notice is addressed to a person outside the U.S.) after the notice is postmarked. A petition is "timely" if filed with the Tax Court on or before the last date specified by IRS in the 90-day letter for filing it. Section 6213(a). "Filed" generally means that the envelope containing the petition is postmarked on or before the due date. However, note that new electronic filing rules will apply later this year.

(d) No Dismissals. Once a taxpayer files a valid petition, he may not withdraw the case from the Tax Court's jurisdiction. See Estate of Ming v. Commissioner, 67 T.C. 519 (1974).

(e) Untimely Filed Petition. The notice of deficiency must state the date determined by IRS as the last day on which the taxpayer may file a petition with the Tax Court. If the taxpayer does not file the petition timely, the IRS's

lawyers with the IRS Office of Chief Counsel will file a motion to dismiss for lack of jurisdiction. If the Tax Court grants the motion, the taxpayer can still pay the tax and sue for refund in a federal district court.

E. THE PETITION

A Tax Court case commences when a taxpayer files a petition with the court. Tax Court Rule 20(a). There is a $60 filing fee for each petition. The form of the petition should be substantially similar to Form 1 in Appendix I of the Tax Court Rules. Tax Court Rule 34(a). The petition should contain the following information:

- The petitioner's name and state of legal residence, if an individual, or name and principal place of business agent's office, if a corporation.
- The petitioner's mailing address and whether tax returns were filed for years at issue.
- The date notice of deficiency was issued, the amount of the deficiency, the nature of the tax, and the years for which the determination was made.
- Separately lettered statements of each error made by the IRS in the determination.
- A concise statement of the facts on which the petitioner relies, except for those issues on which the IRS has the burden of proof.
- A statement of the requested relief.
- The signature, mailing address and telephone number of the petitioner or his counsel.
- A redacted copy of the notice of deficiency (taxpayer identification numbers redacted). Tax Court Rule 34(b).

F. THE ANSWER

When a taxpayer timely files a petition to re-determine a deficiency determined by the IRS, he can also file a designation of place of trial in any city where the Tax Court conducts proceedings. The Clerk of the Tax Court serves the IRS's Chief Counsel in Washington DC, who forwards the case to the Area Counsel (formerly District Counsel) whose attorneys handle cases in the city designated by the taxpayer as place of trial. The IRS Counsel field attorney has 60 days to file the IRS's Answer to the Petition.

1. Chief Counsel Attorneys. In the Tax Court, the government is represented by the IRS Chief Counsel Attorneys. In the Court of Federal Claims and the federal district courts, the government is represented by the Department of Justice. The Chief Counsel attorneys are tax attorneys and are familiar with the Tax Court's emphasis on settling cases. Moreover, they have more settlement authority than Department of Justice attorneys. Settlement authority in Tax Court cases is delegated to the Area Counsel. Department of Justice attorneys are less likely to settle until extensive discovery has been completed. In addition, settlement authority within the Department of Justice Tax Division is highly centralized and, depending upon the amount of tax in dispute, may require the personal approval of the Assistant Attorney General in charge of the Tax Division. The Department of Justice attorneys are required to coordinate their positions with the IRS, and they are required to obtain the views of the IRS with respect to any prospective settlement. However, since the Department is independent of the IRS, it can take positions in litigation and in settlement that differ from the IRS.

2. Contents of Answer. Within 60 days of the Tax Court's service of the petition on the IRS, the IRS must file an answer, responding to the allegations in the petition. Tax Court Rule 36(a). The answer must advise the petitioner and the court fully of the nature of the

defense. Thus, the answer must admit or deny each material allegation of the petition, except where the IRS indicates that it is without knowledge or information sufficient to form a belief as to the truth of an allegation, which is treated as a denial. The IRS can also qualify or deny part of an allegation. The answer must also contain a clear and concise statement of every ground, including the supporting facts, on which the IRS relies and has the burden of proof. The paragraphs of the answer must be designated to correspond to the paragraphs of the petition to which they related. Tax Court Rule 36(c). The IRS must affirmatively plead any avoidance or affirmative defense in its answer. Such defenses include res judicata, collateral estoppel, waiver, duress, fraud, and statute of limitations. A mere denial is not sufficient to raise any such issue. Failure to raise an affirmative defense in the answer is a waiver of the defense and precludes the IRS from raising it at trial. Tax Court Rule 39.

3. Claim for Increase in Deficiency in the Answer. Once a timely petition has been filed, the Tax Court has jurisdiction to redetermine the correct amount of the deficiency, which may be more or less than the amount determined in the notice of deficiency. Section 6214(a). Thus, the IRS can raise new issues not included in the notice of deficiency in the Answer. If the increase in deficiency is a "new matter" the IRS bears the burden of proof. Tax Court Rule 142(a); Shea v. Commissioner, 112 T.C. 183, 190-91 (1999).

G. REFERRAL TO THE IRS APPEALS OFFICE

After the pleadings are closed, IRS Counsel generally refers a docketed Tax Court case to the Appeals Office for consideration of settlement. There are two exceptions to this procedure:

1. Appeals Issued Notice. If the Appeals Office issued the deficiency notice, Counsel probably will not refer the case back to the Appeals Office.

2. Designated for Litigation. If an issue in the case has been designated for litigation by the IRS, Counsel will not refer the case to the Appeals Office.

H. SETTLEMENT AUTHORITY

Counsel and Appeals can agree that Appeals has sole jurisdiction, work together, or transfer the case back and forth to promote efficient disposition of the case. The Counsel attorney should notify the taxpayer about who has the case and settlement authority.

I. SETTLEMENT OF DOCKETED CASES

Many Tax Court cases are settled by the taxpayer with the IRS Appeals Office after being referred by the Counsel attorney. If the taxpayer and IRS agree on a settlement, they enter into a written agreement stipulating the amount of any deficiency or overpayment. This stipulation is filed with the Tax Court as part of a stipulated decision. Treas. Reg. Section 601.106(d)(3)(i).

J. PRE-TRIAL PREPARATION

If the case does not settle with the Appeals Office, it is transferred back to the Counsel field attorney for trial preparation.

1. Scope of Discovery in Tax Court. A unique and important feature of Tax Court concerns how the parties conduct pre-trial discovery. Abusive discovery tactics, known by trial practitioners as "Rambo discovery," are not countenanced by the Tax Court. The primary goal of discovery in Tax Court is to prepare the stipulation of facts (including documents). The stipulation process has been called the "bedrock" of Tax Court procedures. It is designed to focus the parties on the issues for which a trial is required, to accommodate the limited amount of time the Court must devote to the actual trial and to protect the parties from needless litigation expense. The court requires the parties to engage in "informal" discovery to achieve these goals.

Discovery is allowed for any matter relevant to the case, so long as it is not privileged. Information may be sought that would be inadmissible at trial if it appears "reasonably calculated" to lead to the discovery of admissible evidence. T.C. Rule 70(b). But there is authority for the proposition that discovery may not be used to explore the possibility of raising additional issues. Estate of Woodard v. Commissioner, 64 T.C. 999 (1975), vacating 64 T.C. 457.

2. Informal Discovery. The Tax Court requires the parties to use informal consultation and communication to obtain the evidence necessary for trial. Tax Court Rule 70(a). If a party resorts to formal discovery requests without exhausting informal consultation and communication, the court may issue a protective order and direct the parties to make good-faith efforts to exchange information. See Branerton Corp. v. Commissioner, 61 T.C. 691 (1974). In a landmark case decided shortly after the Tax Court amended its rules to allow for formal discovery procedures, a taxpayer served interrogatories before participating in informal discovery. Id. The IRS moved for a protective order. The Tax Court granted the order, refusing to compel the IRS to answer the premature interrogatories. The Court said:

> "The discovery procedures should be used only after the parties have made reasonable informal efforts to obtain needed information voluntarily. For many years the bedrock of Tax Court practice has been the stipulation process, now embodied in Rule 91. Essential to that process is the voluntary exchange of necessary facts, documents, and other data between the parties as an aid to the more expeditious trial of cases as well as for settlement purposes. The … discovery procedures were not intended in any way to weaken the stipulation process."

3. Branerton Amplified. Occasionally the Tax Court has to remind litigants that it is serious about using informal discovery and the stipulation process instead of resorting to formal discovery. In 1976 the Tax Court, quoting Branerton in its holding, explained:

> "[Informal discovery] contemplates "consultation or communication," words that connote discussion, deliberation, and an interchange of ideas, thoughts, and opinions between the parties. Petitioners' refusal to enter into any informal discussion prior to receiving responses to interrogatories—whether formally submitted under Rule 71, or informally submitted in a letter—"sharply conflicts with the intent and purpose of Rule 70(a)(1) and constitutes an abuse of the Court's procedures."

International Air Conditioning Corp. v. Commissioner, 67 T.C. 89, 93 (1976) (citations and footnotes omitted).

4. Branerton Applied to IRS. More recently, it has been IRS Chief Counsel attorneys, not taxpayers, whom the court has had to chastise about launching formal discovery before exhausting informal discovery. In one case, the IRS attorney wrote a "Branerton" letter to the taxpayer's attorney consisting of 68 pages of questions and requests for production of documents. Because the taxpayer did not respond in writing within the allotted time of 30 days, the IRS attorney served 77 pages of interrogatories and a request for production of documents consisting of 78 pages. When faced with a motion for protective order, the IRS attorney insisted that he did not have to follow informal discovery in a case designated for litigation by the National Office. The Tax Court observed:

> "In the instant case, respondent has not demonstrated that most, if not all, of the information respondent needs could not be obtained through the informal procedures required by Rules 70(a), 90(a), and our Branerton opinion. Indeed, we believe that informal discovery would be particularly useful to respondent, where, as here, the examination phase of respondent's inquiry was truncated by a

premature issuance of the FPAA. … The actions of respondent's counsel in the instant case lead us to believe that he does not fully appreciate the importance of our Branerton opinion. His insistence on compliance with his formal discovery requests in advance of any conference between the parties does not effectively present an opportunity for the "discussion, deliberation, and an interchange of ideas, thoughts, and opinions between the parties" that our rules contemplate."

Schnieder Interests, L.L.P. v. Commissioner, 119 T.C. 151, 152 (2002) (citations and footnotes omitted).

K. FORMAL DISCOVERY

The Tax Court has broad discretion to limit frequency, sequence, and timing of formal discovery by protective orders for the convenience of parties and witnesses or in the interests of justice. Also, the use of procedures, described in more detail below, may not delay the progress of the case toward or during trial unless the Court otherwise allows.

In preparing for a Tax Court trial, Court rules provide, in appropriate cases, for obtaining of necessary evidence by:

1. Written Interrogatories. A party may serve upon any other party no more than 25 written interrogatories, including all discrete subparts. Tax Court Rule 71(a). A party must answer under oath and serve a copy of his answers on the propounding party within 30 days of service. The court may allow, or the parties may stipulate to, a longer or shorter time. If a party objects to an interrogatory in his response, the burden is on the propounding party to obtain an order compelling an answer. Interrogatories must be in the form of questions. Thus, a request that a petitioner fill out a Form 1040 is not a proper interrogatory. See Pleier v. Commissioner, 92 T.C. 499 (1989). If a party does not have sufficient knowledge to answer an interrogatory, he must state that he made a reasonable inquiry and that the information known or available to him is insufficient to enable him to answer the interrogatory. Tax Court Rule 71(b). If an interrogatory seeks information that may be derived from the served party's business records, that party has the option of producing those records for the propounding party. In such cases, the burden of the propounding party in deriving the information from the records may be no greater than the burden that would be imposed on the served party in deriving the same information. Tax Court Rule 71(e).

A party may obtain information concerning another party's expert witness by means of interrogatories. The interrogatories may request: (1) the name, address, occupation, and qualifications of the witness; (2) the subject matter of his anticipated testimony; and (3) the substance of the facts and opinions on which he is expected to testify, along with a summary of the grounds for each such opinion. A copy of the expert's report may be submitted in lieu of such information. Tax Court Rule 71(d).

Neither the interrogatories nor the responses should be filed with the court, unless the propounding party moves for an order compelling an answer. Tax Court Rule 71(c).

2. Requests For Admissions. If formal discovery is otherwise permitted, a party can serve upon the other party a written request for admissions. The admissions can include statements of fact or the application of law to fact, including the genuineness of any documents described in the request. Tax Court Rule 90(a). The request for admissions is served without leave of the court, but may not be served earlier than 30 days after joinder of issue under Tax Court Rule 38. The request for admissions must be completed, unless otherwise authorized by the court, no later than 45 days prior to the date set for call of the case from a trial calendar. Tax Court Rule 90(a). Each matter for which an admission is requested must be separately set forth. Copies of documents should be served with the request unless they are otherwise furnished or made available for inspection and copying. The party making the request serves a copy on the other party and files the original with proof of service with the court. Tax Court Rule 90(b).

The party served has 30 days to respond. The court can shorten or lengthen the 30-day response period. Tax Court Rule 90(c). A motion to extend the time to file responses must be made prior to the expiration of 30 days following service. A response must include: (1) a written answer specifically admitting or denying the matter involved, in whole or in part, or asserting that it cannot be truthfully admitted or denied and setting forth in detail the reasons why this is so; or (2) an objection, setting forth in detail the reasons for the objection. Tax Court Rule 90(c).

An objection based on relevance can be noted, but it is not regarded as just cause for refusal to admit or deny. An answering party cannot give lack of knowledge as a reason for failure to admit or deny unless the party states that it has made reasonable inquiry and that the information known or readily available to the party is insufficient to enable the party to admit or deny. Tax Court Rule 90(c).

3. Requests For Production of Documents. A party may serve on any other party a request for such party to produce and permit inspection and copying of designated documents or electronically stored information. Tax Court Rule 72(a). The party upon whom the request is served shall serve a written response within 30 days after service of the request, stating whether inspection will be permitted as requested, unless the request is objected to in whole or in part. Tax Court Rule 72(b)(2).

(a) Form of Production. A responding party shall produce documents (or electronically stored information) as they are kept in the usual course of business or shall organize and label them to correspond to the categories in the request. Tax Court Rule 72(b)(3).

(b) Objections. If the responding party objects to inspection, the party making the request must file a motion to compel inspection. Unless a party files such a motion, neither the request nor the response should be filed with the court. Tax Court Rule 72(b).

4. Depositions. Although the rules provide for depositions, in practice they are rarely used in Tax Court. The Tax Court permits two types of depositions: discovery depositions and depositions to preserve evidence. Tax Court Rules 74-85; Section 7456(a)(2).

(a) Discovery Depositions. The Tax Court Rules provide for three types of discovery depositions: (1) depositions with consent of the parties; (2) depositions without consent of the parties; and (3) depositions of expert witnesses.

(1) Depositions with Consent of the Parties. A deposition by consent is the only means by which the deposition of a party may be taken. If all parties agree, a party may take a deposition of another party or of a non-party witness upon the filing of a stipulation with the court. Tax Court Rule 74(a). The stipulation must contain the name and address of the deponent, the time and place for the deposition, the officer before whom the deposition is to be taken, any provision relating to the payment of the expenses of the deposition, and, if the deposition is to be videotaped, the name and address of the videotape operator and his employer. Tax Court Rule 81(d) and (b)(1).

(2) Depositions without Consent. Deposition of nonparties can be taken in extraordinary circumstances and is allowed only after the party seeking the deposition has attempted to obtain the information by informal

communications or by consent of the parties. Tax Court Rule 75(b). Such deposition may be taken only after a notice of trial has been issued or the case has been assigned to a judge. Tax Court 75(a). A party wishing to take the deposition of a non-party witness without consent must serve a notice of deposition on every other party. If the deposition is to be taken on written questions, a copy of the questions must be attached to the notice. The notice should not be filed with the court. Tax Court Rule 75(c). A party or the non-party witness must serve any objections to the deposition within 15 days of service of the notice of deposition. The objections are not filed with the court. The party seeking to take the deposition then has the burden of moving for an order to compel testimony. If such a motion is filed with the court, copies of the notice of deposition and the objections must be attached. Tax Court Rule 75(d).

(3) Depositions of Experts. Expert witnesses can be deposed by consent of all parties as provided in Tax Court Rule 74. In addition, they can be taken without consent if a party obtains a court order. Tax Court Rule 76. The deposition of the expert witness is limited to: (1) his qualifications; (2) his opinion in respect of matters relevant to the issues in dispute; (3) the facts that underlie his opinion; and (4) his analysis. Tax Court Rule 76(b). The deposition can be taken only after notice of trial is issued or after a case has been assigned to a judge and within the time for completing discovery. Tax Court Rule 76(c). The party desiring to depose the expert witness must file a motion with the Tax Court. Any objections must be filed within 15 days of service of the motion. Tax Court Rule 76(d). The deposition can serve as the expert witness report required by Rule 143(f)(1). Tax Court Rule 76(e). The party requesting the deposition must pay all costs other than costs for copies ordered by other parties.

(b) Depositions to Preserve Evidence. Depositions to preserve evidence can be taken in a pending case before trial or in anticipation of commencing a case in the Tax Court.

(1) Depositions to Perpetuate Testimony in Pending Case. A party may move for an order permitting a deposition to perpetuate testimony or preserve any document or electronically stored information. Tax Court Rule 81(a). Such depositions shall be allowed only if there is a substantial risk that the person, document or electronically stored information will not be available at the trial of the case. Tax Court Rule 81(a). The application should be substantially similar to Form 7 in Appendix I to the Tax Court Rules. It must be filed and served at least 45 days before the trial date. The other parties may file objections or a response within 15 days of service. The court will then rule on the application with or without a hearing. Tax Court Rule 81(b)(2). In lieu of the application, the parties can file a

stipulation to take the deposition by agreement. Tax Court Rule 81(d).

(2) Depositions before Commencement of Case. Depositions may also be taken before the filing a Tax Court petition if necessary to preserve testimony or to preserve any document, electronically stored information. The applicant must file with the Tax Court an application similar to Form 7 in Appendix I of the Tax Court Rules but must also state in the application facts showing: (1) that he intends to be a party to a Tax Court suit but is at present unable to file a petition; and (2) the subject matter of the expected suit and his interest in it. The application is placed on a special docket. If the court allows the deposition it can be used in the subsequent case in the same manner as if it had been taken after commencement of the case. Tax Court Rule 82 requires that the applicant show that the testimony will, in all probability, be lost before trial. See Reed v. Commissioner., 90 T.C. 698 (1988).

L. STANDING PRE-TRIAL ORDER

A Tax Court case is at issue after all of the pleadings have been filed. Tax Court Rule 38. The Clerk will then send the parties a notice of trial and standing pre-trial order.

1. Stipulation and Settlement. The standing pre-trial order requires the parties to begin settlement discussions and to stipulate facts and evidence to the maximum extent possible.

2. Pre-trial Memorandum. The Court also directs the parties to file a pre-trial memorandum at least 14 days before the call of the calendar. All documents not stipulated must be exchanged at least 14 days before calendar call. Documents not stipulated or exchanged may be excluded from evidence.

M. MOTION FOR SUMMARY JUDGMENT

A party may move for summary judgment 30 days after the pleadings have closed. Tax Court Rule 121(a). The motion, together with any supporting exhibits, is to be filed with the court and served on the other parties. If the pleadings, answers to interrogatories, admissions, affidavits, and other matters show that there is no genuine issue as to any material fact and that a decision may be rendered as a matter of law, the court may enter judgment for the moving party. A partial summary judgment may be entered where appropriate. Tax Court Rule 121(b).

1. Response to Motion for Summary Judgment. There is no automatic due date for filing a response to a motion for summary judgment. The Tax Court enters an order directing the filing of a response within the time specified by the Court in its order. Tax Court Rule 121(b). If the opposing party cannot present, by affidavit, facts essential to justify the party's opposition, the party should state the reasons for this by affidavit. Tax Court Rule 121(e).

2. Ruling on Motion for Summary Judgment. If the summary judgment ruling does not decide the whole case, a trial is still necessary. The Court may grant partial summary judgment, making an order specifying the material facts that appear to be without substantial controversy. This is done based on the pleadings and interrogating counsel. If this is done, the facts are deemed established. Tax Court Rule 121(c).

N. SUBMISSION WITHOUT TRIAL

Some cases may be decided based on the stipulated record without testimony by witnesses. Such cases may be submitted to the court at any time after joinder of issue under Tax

Court Rule 38. If not already calendared for trial, the case will be assigned to a judge, who will schedule the filing of briefs or any oral argument. Tax Court Rule 122(a). Submission of a case in this manner does not change the burden of proof. Tax Court Rule 122(b).

O. TRIAL

When a case is at issue, the Clerk places it on a trial calendar, giving the parties at least 90 days' notice of the date on which the case is to be called on the trial calendar. On that date, the attorneys for the parties must appear before the trial judge and estimate the time required for trial. Tax Court Rule 131.

1. Calendar Call. The "calendar call" usually starts at 10:00 am on a Monday specified in the notice of trial. At the calendar call, the judge will usually begin the session with a general explanation of the Tax Court and its procedures for the benefit of pro se taxpayers. The judge is accompanied by a clerk who proceeds to call each case in the order in which it appears on the calendar. As each case is called, petitioner or counsel for petitioner should make an appearance, followed by the Chief Counsel attorney. The parties should then state the status of the case. If the case has settled and a stipulated decision is not ready, the Court expects the parties to announce the terms of the settlement on the record. If the case is for trial, the Court will want to know the status of the stipulation of facts. If the stipulation is complete, it is "lodged" with the Court by presenting it to the Clerk. The Court will then want an estimate of trial time. The parties can then make motions, such as motions for continuance. Motions for continuance made at the call of the calendar are routinely denied. Upon completion of the calendar call, the Court normally takes a short recess during which it establishes the order of any hearings and all trials. Upon reconvening the session, the court announces the order of hearings and trials. If there are any subpoenaed witnesses present in the courtroom, this should be brought to the attention of the court so that the court can instruct the witnesses to appear on the designated trial date.

2. Trial. At the trial, the parties again enter an appearance with petitioner's attorney going first. Petitioner is allowed to make an opening statement, followed by respondent's attorney. After completion of the opening statements, the stipulation of facts and exhibits previously lodged with the Court should be offered into evidence. Then, the petitioner generally will present his case first on those issues upon which he had the burden of proof, followed by Respondent's case.

(a) Invoking the Rule Excluding Witnesses. After the stipulation is admitted, either party can move for the exclusion of witnesses from trial, so that they cannot hear the testimony of other witnesses. The court can also order the exclusion of witnesses on its own. A party who is a natural person, a representative of a party which is not a natural person, or a person whose presence is shown by a party to be essential to the presentation of the party's cause cannot be excluded under this rule. Tax Court Rule 145(a). Often, expert witnesses are allowed to hear the testimony of other witnesses.

(b) Rules of Evidence. The Tax Court applies the Federal Rules of Evidence Section 7453; Tax Court Rule 143(a). The Tax Court follows precedents of the D.C. Circuit in interpreting the Federal Rules of Evidence. See Conti v. Commissioner., 99 T.C. 369 (1992). Ex parte affidavits, statements in briefs, and unadmitted allegations in pleadings do not constitute evidence. Tax Court Rule 143(d)(1). Where the parties agree or by authorization of the court, a legible copy of a document may be submitted as evidence in lieu of the original. If an original document is submitted, it may be replaced with a legible copy with leave of the court. Tax Court Rule 143(d)(1). Exhibits are generally destroyed after a decision becomes final. If a party wishes the return of an exhibit, he must ask the Clerk of the court to

return the exhibit within 90 days after the court's decision becomes final. The exhibit is returned at the party's expense, and the party must suggest a practical manner of delivery. Tax Court Rule 143(d)(2).

(c) Subpoenas. The Tax Court may issue subpoenas to the parties to compel the appearance of a witness at trial. The subpoena is issued by the court in blank, to be filled in by the party seeking attendance of the witness. Section 7456(a)(1); Tax Court Rule 147(a). The subpoena may also compel the witness to produce documentary evidence at the trial. A motion to quash such a subpoena must be filed promptly, but no later than the time specified for compliance with the subpoena. The court may quash or modify the subpoena if it is unreasonable and oppressive. Tax Court Rule 147(b). The subpoena can be served by the United States Marshal or by any other person who is not a party. The subpoena must be delivered to the person, along with the fees for one day's attendance and the mileage allowed by law. Fees and mileage need not be tendered when the subpoena is issued on behalf of the IRS. Tax Court Rule 147(c).

(d) Depositions at Trial. Depositions are not evidence until offered and admitted. Tax Court Rule 143(c).

(e) Expert Witnesses. At least 30 days before the call of the calendar, parties must furnish the court and the opposing party with a written report prepared by every expert witness expected to testify at trial. An expert witness generally is not permitted to testify if a party fails to supply such a report, unless the failure is due to good cause and does not unduly prejudice the opposing party. The report must include the qualifications of the expert, the witness's opinion, the facts or data on which that opinion is based, and the reasons for the conclusion. The report is generally marked as an exhibit and received in evidence as the direct testimony of the expert, unless the court determines the witness is not qualified as an expert. Additional direct testimony is allowed only to clarify or emphasize matters in the report and to cover matters arising after the preparation of the report, except at the discretion of the court. Tax Court Rule 143(f)(1). See Sunoco, Inc. v. Commissioner, 118 T.C. 181 (2002).

P. BURDEN OF PROOF

Failure to produce evidence on an issue of fact on which the party has the burden of proof, and which has not been conceded by the other party, may be grounds for dismissal or determination of the issue against the party. While facts can be established by stipulation, the mere filing of a stipulation does not relieve the party with the burden of proof of the necessity of producing evidence in support of facts not adequately established by the stipulations. Tax Court Rule 149(b). At trial, the burden of proof is generally on the taxpayer, except where provided by statute or where the IRS raises a new matter, increases a deficiency, or asserts an affirmative defense. Tax Court Rule 142(a).

If the taxpayer introduces credible evidence relevant to ascertaining the taxpayer's income tax liability, the burden of proof in court proceedings shifts so that the IRS has the burden of proof with respect to a factual issue related to income, estate, gift, and generation-skipping transfer taxes. Section 7491. To qualify, the taxpayer must prove he cooperated with the IRS during the examination. This includes four facts:

1. Substantiation. The taxpayer must prove that he has complied with substantiation requirements imposed by the Internal Revenue Code and Treasury Regulations.

2. Record Keeping. The taxpayer must prove that he has complied with record-

keeping requirements imposed by the Internal Revenue Code and Regulations.

3. Reasonable Requests for Information. The taxpayer must prove that he has cooperated with reasonable IRS requests for meetings, interviews, witnesses, documents and information.

4. Net Worth Requirement. If the taxpayer is not an individual, he must meet the net worth limitations for awarding attorneys' fees (i.e., if a corporation, trust, or partnership, net worth does not exceed seven million dollars).

XII EXPERT WITNESSES IN TAX COURT

The estate tax is imposed on the fair market value of decedent's property on the date of death. The estate and the IRS typically rely on the expert witness testimony to determine the value of the estate.

A. OPINION EVIDENCE

Everybody has opinions. Those opinions may be well informed--based on facts--or they may be ill informed--based on speculation or prejudice. The law generally requires proof of facts. Courts are suspicious of opinion testimony because it is often tainted with speculation or grounded in bias. The Tax Court applies the Federal Rules of Evidence to determine the admissibility of opinion testimony. See *Little v. Commissioner*, T.C. Memo. 1996-270. Further, the Tax Court Rules impose additional procedural requirements for expert witnesses who offer expert testimony. Tax Court Rule 143(a).

B. FEDERAL RULE OF EVIDENCE 602

Federal Rule of Evidence 602 states:

> "A witness may not testify to a matter unless evidence is introduced sufficient to support a finding that the witness has personal knowledge of the matter …. This rule is subject to the provisions of the rule relating to opinion testimony by expert witnesses."

Federal Rule of Evidence 602 requires that witnesses testify only to matters that they observe, i.e. to facts. Under the Federal Rules of Evidence, there are two kinds of witnesses: "fact witnesses" (also called "lay witnesses") and "expert witnesses." Generally, lay witnesses cannot testify as to inferences and opinions, but there are important exceptions to this rule.

1. Lay Opinion Testimony: Federal Rule of Evidence 701. Federal Rule of Evidence 701 states:

> If the witness is not testifying as an expert, the witness' testimony in the form of opinions or inferences is limited to those opinions or inferences which are (a) rationally based on the perception of the witness, and (b) helpful to a clear understanding of the witness' testimony or the determination of a fact in issue, and (c) not based on scientific, technical, or other specialized knowledge within the scope of Rule 702.

2. The Two Categories of Lay Opinion Testimony. Although not explicitly stated in the rule, there are two categories of lay opinion testimony that may be allowed:

> **(a) The collective facts doctrine.** Under this exception, a witness is permitted to give an opinion concerning matters about which lay persons commonly and reliably infer from perceived facts. The opinion must be rationally based on lay perceptions and helpful to understanding of the facts. *Getter v. Wal-Mart Stores, Inc*., 66 F3d 1119, 1124 (1995) (admitting lay testimony concerning safety conditions in a slip-fall case).
>
> The classic modern example is testimony by a lay witness that in his opinion a car was speeding. Other

examples include the opinion of a lay witness that an individual was intoxicated or that a gun accidentally discharged. The collective facts doctrine does not often surface in tax disputes.

(b) Skilled Lay Observer Testimony. It is more likely to encounter this exception in tax cases. The rationale is that a non-expert witness is permitted to offer opinion testimony because the witness has had repeated, prior opportunities to observe the matter about which he opines. Examples include:

- **Identification of Handwriting:** A lay witness who has had numerous opportunities to observe a person's handwriting can express an opinion identifying the handwriting. *Perillo v. Commissioner,* 78 T.C. 534, 539 (1982).

- **Owner's Opinion of the Value of His Property:** Under the skilled lay exception, the witness has some special knowledge or information that mitigates in favor of the testimony. Because of his special relationship to the property, an owner may testify as a lay witness on the question of the value of the property. See *DiPlacido v. Commissioner*, T.C. Memo. 1993-169.

  While the owner's opinion is admissible, his lack of professional valuation experience and bias are taken in consideration in determining the weight to be given the testimony. In one case the Tax Court accepted the taxpayer's testimony that the value of a carport destroyed by a storm was $3,600 rather than $3,200 as determined by the IRS. The IRS determination was based on a contract signed by the taxpayer in which the contractor estimated the cost of repair at $3,200. The taxpayer had rescinded the contract because the contractor kept adding additional charges. The Tax Court accepted the taxpayer's opinion testimony. See *Sarzen v. Commissioner*, T.C. Memo. 1978-513.

- **Employee of Owner:** The Tax Court has held that an employee of the taxpayer does not qualify as an "owner" for purposes of Federal Rule of Evidence 701. See *Estate of McCampbell v. Commissioner*, T.C. Memo. 1991-141. The taxpayer offered testimony from an employee of the executor under Federal Rule of Evidence 701. The Tax Court also excluded the testimony when offered under Federal Rule of Evidence 702 because the witness did not have sufficient knowledge or expertise to assist the trier of fact.

- **Mental Condition:** Lay testimony that a defendant was sane at the time of a criminal offense has been admitted. See *United States v. Lawson*, 653 F.2d 299 (7th Cir. 1981). Surprisingly, the author could not find any Tax Court cases allowing lay testimony on sanity or competence. The issue surfaces in family limited partnership cases where the issue is whether the decedent was competent to sign documents forming the partnership. It seems likely that the Tax Court would allow the decedent's relatives to testify on

the issue of competence. It is also likely that it will come up in the future.

3. Pure Speculation Prohibited. Federal Rule of Evidence 701 does not negate the requirement that testimony must be based on personal knowledge. It provides that "testimony in the form of opinions or inferences is limited to those opinions which ... are rationally based on the perception of the witness ...."

C. EXPERT WITNESS TESTIMONY-FEDERAL RULE OF EVIDENCE 702

The second exception to the rule that prohibits opinion testimony is the rule allowing experts to testify as to opinions. It states:

> "If scientific, technical, or other specialized knowledge will assist the trier of fact to understand the evidence or to determine a fact in issue, a witness qualified as an expert by knowledge, skill, experience, training, or education, may testify thereto in the form of an opinion or otherwise, if (1) the testimony is based upon sufficient facts or data, (2) the testimony is the product of reliable principles and methods, and (3) the witness has applied the principles and methods reliably to the facts of the case".

In Tax Court, the parties typically rely on an expert's report and testimony to support their respective positions on valuation issues.

D. THE TAX COURT RULES AND EXPERT WITNESSES

We have seen that the Tax Court applies the Federal Rules of Evidence, which contain special provisions for expert testimony. In addition, the Tax Court has its own procedural rules. Those rules are substantially different from the procedural rules that apply in state and federal district courts. The most important rule as applied to expert witnesses is Tax Court Rule 143(g)(1). It states in relevant part:

> "Unless otherwise permitted by the court on timely request, any party who calls an expert witness shall cause that witness to prepare a written report for submission to the Court and to the opposing party. The report shall set forth the qualifications of the expert witness and shall state the witness' opinion and the facts or data on which that opinion is based. The report shall set forth in detail the reasons for the conclusion, and it will be marked as an exhibit, identified by the witness, and received in evidence as the direct testimony of the expert witness, unless the Court determines that the witness is not qualified as an expert. Additional direct testimony with respect to the report may be allowed to clarify or emphasize matters in the report, to cover matters arising after the preparation of the report, or otherwise at the discretion of the Court".

1. Drafting the Expert Witness Report. A well-drafted report is critical because it serves as direct testimony. It must contain:

> **(a) The Expert's Qualifications.** Usually this is a Curriculum Vitae ("CV") attached as an appendix. It should include the expert's educational background from college or university, including any advanced degrees; membership in professional associations or organizations; published articles or books; instructional courses for professional associations; and whether the expert has been recognized as such by any courts in prior testimony.
>
> **(b) Opinion and Detailed Reasoning.** The expert should state her summary opinion and conclusion succinctly and quickly. Following this, she should explain in detail the reasoning that supports the opinion.
>
> **(c) The Facts or Data Relied Upon by the Expert.** The report should state what facts and underlying data the expert relied on.

(d) Drafting a Persuasive Report. Some suggestions that I make to my experts include the following:

- Grammar: Write simple, understandable sentences. Do not try to impress the judge with your ability to parrot legalese.

- Limit Technical Terms and Jargon. You are the expert. It is your job is to explain a matter that is so complex that it requires an expert to understand. Your explanation is being considered by non-experts, so you must take technical jargon and translate it into terms that a layman can understand. You are a "professional explainer."

- Write for Your Audience. There are no jury trials in Tax Court. You are writing for the Tax Court and, in particular, the judge assigned to the case. (By the time you write your report, you will know who the judge is). Research his opinions and ask the attorneys assigned to the case about the judge. For example, a valuation report drafted for Judge Laro would, in my opinion, use more technical terms since he is highly knowledgeable in that area and expects it.

(e) Do Not Let the Lawyers Write or Revise Your Report. Drafts are discoverable. Thus, if you send a draft to a lawyer, the opposing side is entitled to see it and compare it with the final product. If it comes out that the lawyers assisted with the report (and if they did it, probably will), your report will have little value in the case at issue, and your reputation with the Tax Court will be tainted in future cases.

E. PRE-TRIAL SUBMISSION OF EXPERT REPORTS.

The expert witness report must be submitted to the court (with service to all parties) no later than 30 days before the call of the trial calendar on which the case shall appear. Tax Court Rule 143(g)(2). An expert witness's "testimony will be excluded altogether for failure to [timely submit the report] … unless the failure is shown to be due to good cause and unless the failure does not unduly prejudice the opposing party …." Tax Court Rule 143(g)(1). Failing to timely submit the report is usually fatal to admitting a valuation report because the "Court ordinarily will not grant a request to permit an expert witness to testify without a written report where the expert witness's testimony is based on third party contacts, comparable sales, statistical data, or other detailed, technical information …."

F. GETTING THE EXPERT REPORT ADMITTED

The expert witness report is the direct testimony of the expert witness. Tax Court Rule 143. This is entirely unique to Tax Court and has important ramifications. The procedure for admitting the report is as follows:

1. Qualifying the Expert. An expert witness possesses scientific, technical or other specialized knowledge that will assist the trier of fact. A witness is qualified as an expert when the proponent demonstrates that the witness possesses the requisite knowledge, skill, experience, training or education to assist the court in a matter involving technical or specialized knowledge. See Federal Rule Evidence 702. The examining attorney should qualify the valuation expert by establishing the educational background and professional experience of the expert. While this is already summarized in the CV attached to the expert report, this testimony is critical because the report has not yet been admitted in evidence. It also allows the expert to make an impression on the judge before cross-examination.

2. Voire Dire. When the examining attorney has completed his questions concerning your qualifications, he will pass the witness for "voire dire." This is a cross-examination within a direct examination and allows the opposing attorney to question the expert's qualifications in an effort to have him disqualified as an expert. After he has completed his questions, the attorney directing the examination asks the Tax Court judge to recognize the witness as an expert witness. If the Court rejects the witness as an expert, that concludes the testimony. If the Court rules that the witness qualifies as an expert, the report is offered in evidence.

3. Introducing the Report. The expert witness is asked to identify the expert witness report and it is offered in evidence as an exhibit. There may be objections, but usually it is admitted (so long as the procedural requirements set forth above have been met). Note that the report is "received in evidence as the direct testimony of the expert witness." Some Tax Court judges want the parties to comply strictly with this requirement. Thus, once the expert is qualified and the report admitted, the expert witness is passed for cross-examination without further direct examination. The Tax Court Rules give the Court the discretion to allow additional direct examination: "Additional direct testimony with respect to the report may be allowed to clarify or emphasize matters in the report, to cover matters arising after the preparation of the report, or otherwise at the discretion of the Court." Tax Court Rule 143(g)(1).

XIII SUMMONSES

In most examinations the IRS does not use formal compulsory methods to obtain information. Instead, examining agents routinely rely on informal requests to obtain data by issuing an Information Document Request (Form 4564) to the taxpayer. The Information Document Request asks the taxpayer to produce records and provide information (i.e., respond to written questions). If a taxpayer fails to comply, the examining agent has the authority to issue a formal summons, ordering the taxpayer to produce records and provide testimony under oath.

A. ESTATE TAX EXAMINING AGENTS

The IRS examining agent in an estate tax examination is an Estate Tax Attorney (referred to as the "IRS Estate Tax Attorney"). The IRS is divided into "Functions" and "Operating Divisions." Other functional units include the Collection Function, the Appeals Function and the Criminal Investigation Function. Operating divisions include Large and Mid-size Business, Tax Exempt & Government Entities, Wage & Investment and Small Business & Self-Employed.

IRS Estate Tax Attorneys are employed by the Examination Function and are part of the Small Business Self-Employed Division. The Internal Revenue Manual (IRM) directs the IRS Estate Tax Attorney, under the direction of the estate tax manager, to examine and process an estate tax return within 18 months of filing. See IRM 4.25.1.1.4 Inventory Management. The Estate Tax Attorney should initiate the examination "within 9 months of filing" and examinations "extending beyond 12 months may require frequent managerial involvement." IRM 4.25.1.1.4 Inventory Management.

B. EXAMINATION OF ESTATE TAX RETURNS

IRS Estate Tax Attorneys are directed to "Examine estate tax returns in a manner that will promote public confidence in the Mission of the Service . . . ." IRM 4.25.1.5.1 Estate Tax Examinations.

C. THE INTERVIEW EXAMINATION METHOD

IRS Estate Tax Attorneys are directed by the IRM to "use the interview examination method of examination unless information concerning questionable items appearing on a tax return can be readily furnished by mail." IRM 4.25.1.5.1 Estate Tax Examinations.

D. THE INFORMATION DOCUMENT REQUEST

The Interview Examination Method does not necessarily countenance an interview of the taxpayer directly by the IRS Estate Tax Attorney. The IRS Estate Tax Attorney will normally issue a Form 4564, Information Document Request ("IDR").

Practice Tip: The taxpayer's representative should provide the information and documents. The taxpayer's representative should provide the documents requested by the IDR and provide written responses to the questions after meeting with the client. Inform the IRS Estate Tax Attorney that you, as the representative, will provide all information and documents for the taxpayer. The taxpayer's representative can ask for a preliminary meeting with IRS Estate Tax Attorney to present the Form 2848 and establish the ground rules for the examination. The request for the preliminary conference is appropriate. In large case examinations, the IRM directs the examining agent to ask the taxpayer's representative for a pre-examination conference. IRM 4.3.11 Case Managers Handbook. Although the IRS Estate Tax Attorney is arguably not bound by large case procedures because they are part of the Small Business Self Employed Division, their cases are often as complicated as large case examinations, justifying a pre-examination conference.

At the preliminary conference the taxpayer's representative should tell the IRS Estate Tax Attorney that he/she should communicate with the taxpayer's representative under the Form 2848. Explain that all IDRs will be answered by the taxpayer's representative after consulting with the taxpayer. Assure the Estate Tax Attorney that you will respond to all IDRs so it will be unnecessary to interview your client.

E. RECENT TREND—USE OF EXAMINATION FUNCTION TO PREPARE FOR TRIAL

Practitioners who represent taxpayers in estate tax examinations are becoming increasingly alarmed (and justifiably so, in our opinion) because IRS Estate Tax Attorneys are misusing the examination function to prepare cases for trial. This results in greatly increased professional fees to the estate and is contrary to the examination function, which is to examine the estate tax return—not to prepare a case for trial. Some IRS Estate Tax Attorneys claim they have been instructed to interview the taxpayer directly under oath. They then threaten issuing a summons for the taxpayer's testimony if the representative refuses to submit his client to an interview. The taxpayer's representative should be well versed in the power the IRS Estate Tax Attorney has to issue a summons and, alternatively, the practical, procedural and administrative difficulties the IRS Estate Attorney faces when issuing a summons.

F. STATUTORY BASIS FOR ISSUANCE OF SUMMONS

The Internal Revenue Code contains provisions giving the IRS the authority to issue administrative summonses. These provisions are found in Subchapter A ("Examination and Inspection") of Chapter 78 ("Discovery of Liability and Enforcement of Title").

G. PURPOSE OF SUMMONS

Section 7602 authorizes the IRS to issue an administrative summons for the following purposes:

1. Correct Return. To ascertain the correctness of any return. This would include an estate tax return (Form 706) or a gift tax return (Form 709).

2. Tax Liability. To determine the tax liability of any person.

3. Substitute for Return. To "make a return where none has been filed" (i.e. prepare a substitute for return).

4. Transferee Liability. To determine the liability of a transferee or fiduciary.

5. Collection. To collect any internal revenue tax liability.

H. SCOPE OF SUMMONS

The two categories of data authorized by a summons issued under Section 7602 correspond to the IDR. The summons can require the taxpayer to produce:

1. Information. To appear and give testimony under oath as may be relevant or material to the inquiry; and

2. Documents. To produce relevant or material records.

I. JUDICIAL RESTRAINTS ON IRS ADMINISTRATIVE SUMMONSES

In a trilogy of cases, the United States Supreme Court addressed important questions about the scope of summons enforcement, affording taxpayers procedural and substantive safeguards against improper conduct by examining agents.

1. Reisman v. Caplan, 375 US 440 (1964). In this case, the Supreme, in essence, established procedural safe guards for taxpayers whose records are summoned.

Reisman, an attorney who represented taxpayers under investigation by the IRS Criminal Investigation Division, hired an accounting firm to analyze the taxpayers' financial records. The IRS special agent issued and served summonses on the accountants, directing them to produce audit reports, workpapers and correspondence. The accountants informed Reisman that they intended to comply with the summonses, despite Reisman's contention that the records were his attorneys' work product. Riesman brought an action for declaratory judgment and injunctive relief against the IRS and the accountants, asserting that the summonses were void, constituting an unreasonable seizure in violation of the Fourth Amendment.

Ruling for the IRS and the accountants, the Supreme Court denied Reisman's request for a declaratory judgment and injunction, stating that Reisman had an adequate remedy at law.

Although the IRS won the battle, it lost the war. As interpreted in later decisions, Reisman and its progeny created a procedural "bill of rights" applicable in all future cases:

- A summons may be challenged before the IRS presiding officer on the return date on constitutional or other grounds.

- The IRS presiding officer may reject the challenge, but cannot compel the taxpayer to comply or impose sanctions.

- If the IRS chooses to enforce the summons, it must proceed in federal district court under Section 7402(b).

- A district court must conduct an adversary hearing to determine if the summons is enforceable.

- If the district court rules for the IRS at the hearing, it may issue an order requiring the taxpayer to comply. That taxpayer is afforded an opportunity to comply with that order.

- The order enforcing the summons is appealable and a stay is granted pending appeal.

- An order of contempt for failing to comply with the district court's order of enforcement is also appealable.

2. United States v. Powell, 379 US 48 (1964). In Powell the Supreme Court explained what the IRS must prove at the adversary hearing to obtain an order enforcing the administrative summons. The IRS must show that:

- The investigation is conducted pursuant to a legitimate purpose.
- The inquiry is relevant to that purpose.
- The information is not already within the possession of the IRS.
- The IRS has followed the administrative steps required by the Internal Revenue Code.

3. Donaldson v. United States, 400 US 517 (1971). The Supreme Court held that before a district court could enforce an IRS administrative summons, the IRS must show that:

- The investigation is conducted pursuant to a legitimate purpose;
- The inquiry is relevant to that purpose;
- The information is not already within the possession of the IRS;
- The IRS has followed the administrative steps required by the Internal Revenue Code.

XIV CONCLUSIONS

The audit and trial of contested estate and gift tax cases are getting increasingly complex and adversarial, necessitating an earlier and greater collaborative effort between the Tax Practitioner and the trial attorney selected to handle the trial of the case, if necessary.