

# **YOUR APPEAL RIGHTS**

***BEFORE THE INTERNAL REVENUE SERVICE***

**Prepared By**



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Your Appeal Rights Before the IRS<sup>1</sup>  
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I. Examination of Returns

A. A tax return may be examined for a variety of reasons, and the examination may take place in any one of several ways.

B. After the examination, if any changes to the tax are proposed, the taxpayer can either agree with those changes and pay any additional tax the taxpayer may owe, or the taxpayer can disagree with the changes and appeal the decision.

II. Examination Selection Criteria.

A. DIF System

A tax return may be selected for examination on the basis of computer scoring. A computer program called the Discriminate Inventory Function System (DIF) assigns a numeric score to each individual and some corporate tax returns after they have been processed. If the tax return is selected because of a high score under the DIF system, the potential is high that an examination of the tax return will result in a change to the taxpayer income tax liability.

B. Third Party Communication

The tax return may also be selected for examination on the basis of information received from third-party documentation, such as Forms 1099 and W-2, that does not match the information reported on the tax return. Or, the tax return may be selected to address both the questionable treatment of an item and to study the behavior of similar taxpayers (a market segment) in handling a tax issue.

C. Other Sources

In addition, the tax return may be selected as a result of information received from other sources on potential noncompliance with the tax laws or inaccurate filing. This information can come from a number of sources, including newspapers, public records, and individuals. The information is evaluated for reliability and accuracy before it is used as the basis of an examination or investigation.

D. Notice of IRS contact of third parties.

1. The IRS must give the taxpayer reasonable notice before contacting other persons about the taxpayer's tax matters. The taxpayer must be given reasonable notice in advance that, in examining or collecting the taxpayer tax liability, the IRS may contact third parties such as the taxpayer neighbors, banks, employers, or employees. The IRS must also give the taxpayer notice

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<sup>1</sup> - *An Outline of IRS Publication 556*

of specific contacts by providing the taxpayer with a record of persons contacted on both a periodic basis and upon the taxpayer request.

2. This provision does not apply:
  - a. To any pending criminal investigation,
  - b. When providing notice would jeopardize collection of any tax liability,
  - c. Where providing notice may result in reprisal against any person, or
  - d. When the taxpayer authorized the contact.

### III. If the Tax Return Is Examined

#### A. Examination Process

Some examinations are handled entirely by mail. Examinations not handled by mail can take place in the taxpayer's home, the taxpayer's place of business, an Internal Revenue office, or the office of the taxpayer's attorney, accountant, or enrolled agent. If the time, place, or method is not convenient for the taxpayer, the examiner will try to work out something more suitable. However, the IRS makes the final determination of when, where, and how the examination will take place.

#### B. Representation.

##### 1. In General.

Throughout the examination, the taxpayer can act on the taxpayer's own behalf or have someone represent the taxpayer or accompany the taxpayer. If the taxpayer filed a joint return, either the taxpayer or the taxpayer spouse, or both, can meet with the IRS. The taxpayer can have someone represent or accompany the taxpayer. This person can be any federally authorized practitioner, including an attorney, a certified public accountant, an enrolled agent (a person enrolled to practice before the IRS), an enrolled actuary, or the person who prepared the return and signed it as the preparer.

##### 2. Form 2848

If the taxpayer wants someone to represent the taxpayer in the taxpayer absence, the taxpayer must furnish that person with proper written authorization. The taxpayer can use Form 2848 or any other properly written authorization. If the taxpayer want to consult with an attorney, a certified public accountant, an enrolled agent, or any other person permitted to represent a taxpayer during an interview for examining a tax return or collecting tax, the taxpayer should make arrangements with that person to be available for the interview. In most cases, the IRS must suspend the interview and reschedule it. The IRS cannot suspend the interview if the taxpayer are there because of an administrative summons.

3. Third party authorization.

If the taxpayer checked the box in the signature area of the taxpayer income tax return (Form 1040, Form 1040A, or Form 1040EZ) to allow the IRS to discuss the tax return with another person (a third party designee), this authorization does not replace Form 2848. The box the taxpayer checked on the tax return only authorizes the other person to receive information about the processing of the tax return and the status of the taxpayer refund during the period the tax return is being processed. For more information, see the instructions for the tax return.

C. Confidentiality privilege.

1. Generally, the same confidentiality protection that the taxpayer have with an attorney also applies to certain communications that the taxpayer have with federally authorized practitioners.

2. Confidential communications are those that:

- a. Advise the taxpayer on tax matters within the scope of the practitioner's authority to practice before the IRS,
- b. Would be confidential between an attorney and the taxpayer, and
- c. Relate to noncriminal tax matters before the IRS, or
- d. Relate to noncriminal tax proceedings brought in federal court by or against the United States.

3. In the case of communications in connection with the promotion of a person's participation in a tax shelter, the confidentiality privilege does not apply to written communications between a federally authorized practitioner and that person, any director, officer, employee, agent, or representative of that person, or any other person holding a capital or profits interest in that person.

4. A tax shelter is any entity, plan, or arrangement, a significant purpose of which is the avoidance or evasion of income tax.

D. Recordings.

The taxpayer can make an audio recording of the examination interview. The taxpayer request to record the interview should be made in writing. The taxpayer must notify the examiner 10 days in advance and bring the taxpayer own recording equipment. The IRS also can record an interview. If the IRS initiates the recording, the taxpayer must be notified 10 days in advance and the taxpayer can get a copy of the recording at the taxpayer expense.

E. Transfers to another area.

Generally, the tax return is examined in the area where the taxpayer lives. But if the tax return can be examined more quickly and conveniently in another area, such as where the taxpayer books and records are located, the taxpayer can ask to have the case transferred to that area.

#### F. Repeat examinations.

The IRS tries to avoid repeat examinations of the same items, but sometimes this happens. If the taxpayer tax return was examined for the same items in either of the two previous years and no change was proposed to the taxpayer tax liability, please contact the IRS as soon as possible to see if the examination should be discontinued.

### IV. The Examination

#### A. Overview

1. An examination usually begins when the taxpayer is notified that the tax return has been selected. The IRS will tell the taxpayer which records the taxpayer will need. The examination can proceed more easily if the taxpayer gather the taxpayer records before any interview.

2. Any proposed changes to the tax return will be explained to the taxpayer or the taxpayer authorized representative. It is important that the taxpayer understand the reasons for any proposed changes. The taxpayer should not hesitate to ask about anything that is unclear to the taxpayer.

3. The IRS must follow the tax laws set forth by Congress in the Internal Revenue Code. The IRS also follows Treasury Regulations, other rules, and procedures that were written to administer the tax laws. The IRS also follows court decisions. However, the IRS can lose cases that involve taxpayers with the same issue and still apply its interpretation of the law to the taxpayer situation.

4. Most taxpayers agree to changes proposed by examiners, and the examinations are closed at this level. If the taxpayer do not agree, the taxpayer can appeal any proposed change by following the procedures provided to the taxpayer by the IRS. A more complete discussion of appeal rights is found later under Appeal Rights.

#### B. If Taxpayer Agrees

1. If the taxpayer agrees with the proposed changes, the taxpayer can sign an agreement form and pay any additional tax the taxpayer may owe. The taxpayer must pay interest on any additional tax. If the taxpayer pay when the taxpayer sign the agreement, the interest is generally figured from the due date of the tax return to the date of the taxpayer payment.

2. If the taxpayer do not pay the additional tax when the taxpayer sign the agreement, the taxpayer will receive a bill that includes interest. If the taxpayer pay the amount due within 10 business days of the billing date, the taxpayer will not have to pay more interest or penalties. This period is extended to 21 calendar days if the amount due is less than \$100,000.

3. If the taxpayer are due a refund, the taxpayer will receive it sooner if the taxpayer sign the agreement form. The taxpayer will be paid interest on the refund.

4. If the IRS accepts the taxpayer tax return as filed, the taxpayer will receive a letter in a few weeks stating that the examiner proposed no changes to the tax return. The taxpayer should keep this letter with the taxpayer tax records.

C. If Taxpayer Does Not Agree.

1. If the taxpayer do not agree with the proposed changes, the examiner will explain the taxpayer appeal rights. If the taxpayer examination takes place in an IRS office, the taxpayer can request an immediate meeting with the examiner's supervisor to explain the taxpayer position. If an agreement is reached, the taxpayer case will be closed.

2. If the taxpayer cannot reach an agreement with the supervisor at this meeting, or if the examination took place outside of an IRS office, the examiner will write up the taxpayer case explaining the taxpayer position and the IRS' position. The examiner will forward the taxpayer case for processing.

D. Fast Track Mediation.

1. The IRS offers fast track mediation services to help taxpayers resolve many disputes resulting from:

- Examinations (audits),
- Offers in compromise,
- Trust fund recovery penalties, and
- Other collection actions.

2. Most cases that are not docketed in any court qualify for fast track mediation. Mediation can take place at a conference the taxpayer request with a supervisor, or later. The process involves an Appeals Officer who has been trained in mediation. The taxpayer may represent the him or herself at the mediation session, or someone else can act as the taxpayer representative. For more information, see IRS Publication 3605.

E. 30-day letter and 90-day letter.

1. Within a few weeks after the taxpayer closing conference with the examiner and/or supervisor, the taxpayer will receive a package with:

- A letter (known as a 30 day letter) notifying you of your rights to appeal the proposed changes within 30 days;
- A copy of the examination report explaining the examiner's proposed changes;
- An agreement or waiver form
- A Copy of IRS Publication 5.

2. The taxpayer generally have 30 days from the date of the 30-day letter to tell the IRS whether the taxpayer will accept or appeal the proposed changes. The letter will explain what steps the taxpayer should take, depending on which action the taxpayer choose. Appeal Rights are explained later.

F. 90-day letter.

1. If the taxpayer do not respond to the 30-day letter, or if the taxpayer later do not reach an agreement with an Appeals Officer, the IRS will send the taxpayer a 90-day letter, which is also known as a notice of deficiency.

2. The taxpayer will have 90 days (150 days if it is addressed to the taxpayer outside the United States) from the date of this notice to file a petition with the Tax Court. Filing a petition with the Tax Court is discussed later under Appeals to the Courts and Tax Court.

3. The notice will show the 90th (and 150th) day by which the taxpayer must file the taxpayer petition with the Tax Court.

V. Suspension of interest and penalties.

A. In General

1. Generally, the IRS has 3 years from the date the taxpayer filed the tax return (or the date the return was due, if later) to assess any additional tax. However, if the taxpayer file the tax return timely (including extensions), interest and certain penalties will be suspended if the IRS does not mail a notice to the taxpayer, stating the taxpayer liability and the basis for that liability, within a 36-month period beginning on the later of:

- The date on which the taxpayer filed the taxpayer tax return, or
- The due date (without extensions) of the taxpayer tax return.

2. If the IRS mails a notice after the 36-month period, interest and certain penalties applicable to the suspension period will be suspended.

3. The suspension period begins the day after the close of the 36-month period and ends 21 days after the IRS mails a notice to the taxpayer stating the taxpayer liability and the basis for that liability. Also, the suspension period applies separately to each notice stating the taxpayer liability and the basis for that liability received by the taxpayer.

B. Suspension Does Not Apply To.

The suspension does not apply to a:

- Failure-to-pay penalty,

- Fraudulent tax return,
- Penalty, interest, addition to tax, or additional amount with respect to any tax liability shown on the tax return or with respect to any gross misstatement,
- Penalty, interest, addition to tax, or additional amount with respect to any reportable transaction that is not adequately disclosed or any listed transaction, or
- Criminal penalty.

C. Seeking relief from improperly assessed interest.

1. The taxpayer can seek relief if interest is assessed for periods during which interest should have been suspended because the IRS did not mail a notice to the taxpayer in a timely manner.

2. If the taxpayer believe that interest was assessed with respect to a period during which interest should have been suspended, submit Form 843, writing "Section 6404(g) Notification" at the top of the form, with the IRS Service Center where the taxpayer filed the tax return.

3. The IRS will review the Form 843 and notify the taxpayer whether interest will be abated. If the IRS does not abate interest, the taxpayer can pay the disputed interest assessment and file a claim for refund. If the taxpayer claim is denied or not acted upon within 6 months from the date the taxpayer filed it, the taxpayer can file suit for a refund in the taxpayer United States District Court or in the United States Court of Federal Claims.

D. Unreasonable Error of Delay

1. If the taxpayer believe that an IRS officer or employee has made an unreasonable error or delay in performing a ministerial or managerial act (discussed later under Abatement of Interest Due to Error or Delay by the IRS), file Form 843 with the IRS Service Center where the taxpayer filed the tax return. If the Service denies the taxpayer claim, the Tax Court may be able to review that determination. See Tax Court can review failure to abate interest, later under Abatement of Interest Due to Error or Delay by the IRS.

2. If the taxpayer later agree.

If the taxpayer agree with the examiner's changes after receiving the examination report or the 30-day letter, sign and return either the examination report or the waiver form. Keep a copy for the taxpayer records. The taxpayer can pay any additional amount the taxpayer owe without waiting for a bill. Include interest on the additional tax at the applicable rate. This interest rate is usually for the period from the due date of the return to the date of payment. The examiner can tell the taxpayer the interest rate(s) or help the taxpayer figure the amount.

3. The taxpayer must pay interest on penalties and on additional tax for failing to file returns, for overstating valuations, for understating valuations on estate and gift tax returns, and for

substantially understating tax liability. Interest is generally figured from the date (including extensions) the tax return is required to be filed to the date the taxpayer pay the penalty and/or additional tax.

4. If the taxpayer pay the amount due within 10 business days after the date of notice and demand for immediate payment, the taxpayer will not have to pay any additional penalties and interest. This period is extended to 21 calendar days if the amount due is less than \$100,000.

#### E. How to Stop Interest From Accruing

##### 1. If the Taxpayer Owe Additional Tax

a. If the taxpayer think that the taxpayer will owe additional tax at the end of the examination, the taxpayer can stop the further accrual of interest by sending money to the IRS to cover all or part of the amount the taxpayer think the taxpayer will owe. Interest on part or all of any amount the taxpayer owe will stop accruing on the date the IRS receives the taxpayer money.

b. The taxpayer can send an amount either in the form of a deposit in the nature of a cash bond or as a payment of tax. Both a deposit and a payment stop any further accrual of interest. However, making a deposit or payment will stop the accrual of interest on only the amount the taxpayer sent. Because of compounding rules, interest will continue to accrue on accrued interest, even though the taxpayer have paid the underlying tax.

c. To stop the accrual of interest on both tax and interest, the taxpayer must make a deposit or payment for both the tax and interest that has accrued as of the date of deposit or payment.

##### 2. Payment or Deposit.

a. Deposits differ from payments in two ways:

(1) The taxpayer can have all or part of the taxpayer deposit returned to the taxpayer without filing for a refund. However, if the taxpayer request and receive the taxpayer deposit and the IRS later assesses a deficiency for that period and type of tax, interest will be figured as if the funds were never on deposit.

(2) Also, the taxpayer deposit will not be returned if one of the following situations applies:

b. The IRS assesses a tax liability.

(1) The IRS determines that, by returning the deposit, it may not be able to collect a future deficiency.

(2) The IRS determines that the deposit should be applied against another tax liability.

(3) Deposits returned to the taxpayer will include interest based on the Federal short-term rate determined under section 6621(b).

c. The deposit returned will be treated as a tax payment to the extent of the disputed tax. A disputed tax means the amount of tax specified at the time of deposit as a reasonable estimate of the maximum amount of any tax owed by the taxpayer, such as the deficiency proposed in the 30-day letter.

d. Notice not mailed.

(1) If the taxpayer send money before the IRS mails the taxpayer a notice of deficiency, the taxpayer can ask the IRS to treat it as a deposit. The taxpayer must make the taxpayer request in writing.

(2) If, after being notified of a proposed liability but before the IRS mails the taxpayer a notice of deficiency, the taxpayer send an amount large enough to cover the proposed liability, it will be considered a payment unless the taxpayer request in writing that it be treated as a deposit.

(3) If the amount the taxpayer send is at least as much as the proposed liability and the taxpayer do not request that it be treated as a deposit, the IRS will not send the taxpayer a notice of deficiency. If the taxpayer do not receive a notice of deficiency, the taxpayer cannot take the taxpayer case to the Tax Court. See Tax Court, later under

e. Appeal Rights.

(1) Notice mailed.

If, after the IRS mails the notice of deficiency, the taxpayer send money without written instructions, it will be treated as a payment. The taxpayer will still be able to petition the Tax Court.

(2) Money Sent.

If the taxpayer send money after receiving a notice of deficiency and the taxpayer have specified in writing that it is a "deposit in the nature of a cash bond," the IRS will treat it as a deposit if the taxpayer send it before either:

- The close of the 90-day or 150-day period for filing a petition with the Tax Court to appeal the deficiency, or

- The date the Tax Court decision is final, if the taxpayer have filed a petition.
3. Using a Deposit To Pay the Tax.
- a. If the taxpayer agree with the examiner's proposed changes after the examination, the taxpayer deposit will be applied against any amount the taxpayer may owe.
  - b. The IRS will not mail the taxpayer a notice of deficiency and the taxpayer will not have the right to take the taxpayer case to the Tax Court.
  - c. If the taxpayer do not agree to the full amount of the deficiency after the examination, the IRS will mail the taxpayer a notice of deficiency.
  - d. The taxpayer deposit will be applied against the proposed deficiency unless the taxpayer write to the IRS before the end of the 90-day or 150-day period stating that the taxpayer still want the money to be treated as a deposit. The taxpayer will still have the right to take the taxpayer case to the Tax Court.

#### VII. Installment Agreement Request

A. The taxpayer can request a monthly installment plan if the taxpayer cannot pay the full amount the taxpayer owe. To be valid, the taxpayer request must be approved by the IRS. However, if the taxpayer owe \$10,000 or less in tax and the taxpayer meet certain other criteria, the IRS must accept the taxpayer request.

B. Before the taxpayer request an installment agreement, the taxpayer should consider other less costly alternatives, such as a bank loan. The taxpayer will continue to be charged interest and penalties on the amount the taxpayer owe until it is paid in full.

C. Unless the taxpayer income is below a certain level, the fee for an approved installment agreement has increased to \$105 (\$52 if the taxpayer make the taxpayer payments by electronic funds withdrawal). If the taxpayer income is below a certain level, the taxpayer may qualify to pay a reduced fee of \$43.

D. For more information about installment agreements, see Form 9465, Installment Agreement Request.

#### VIII. Reduction of Interest.

##### A. Interest Netting.

If the taxpayer owe interest to the IRS on an underpayment for the same period the IRS owes the taxpayer interest on an overpayment, the IRS will figure interest on the underpayment and overpayment at

the same interest rate (up to the amount of the overpayment). As a result, the net rate is zero for that period.

B. Abatement of Interest Due to Error or Delay by the IRS.

1. The IRS may abate (reduce) the amount of interest the taxpayer owe if the interest is due to an unreasonable error or delay by an IRS officer or employee in performing a ministerial or managerial act (discussed later). Only the amount of interest on income, estate, gift, generation-skipping, and certain excise taxes can be reduced.

2. The amount of interest will not be reduced if the taxpayer or anyone related to the taxpayer contributed significantly to the error or delay. Also, the interest will be reduced only if the error or delay happened after the IRS contacted the taxpayer in writing about the deficiency or payment on which the interest is based. An audit notification letter is such a contact.

3. The IRS cannot reduce the amount of interest due to a general administrative decision, such as a decision on how to organize the processing of tax returns.

C. Ministerial Act.

This is a procedural or mechanical act, not involving the exercise of judgment or discretion, during the processing of a case after all prerequisites (for example, conferences and review by supervisors) have taken place. A decision concerning the proper application of federal tax law (or other federal or state law) is not a ministerial act.

Example 1.

The taxpayer move from one state to another before the IRS selects the taxpayer tax return for examination. A letter stating that the tax return has been selected is sent to the taxpayer old address and then forwarded to the taxpayer new address. When the taxpayer get the letter, the taxpayer respond with a request that the examination be transferred to the area office closest to the taxpayer new address. The examination group manager approves the taxpayer request. After the taxpayer request has been approved, the transfer is a ministerial act. The IRS can reduce the interest because of any unreasonable delay in transferring the case.

Example 2.

An examination of the tax return reveals tax due for which a notice of deficiency (90-day letter) will be issued. After the taxpayer and the IRS discuss the issues, the notice is prepared and reviewed. After the review process, issuing the notice of deficiency is a ministerial act. If there is an unreasonable delay in sending the notice of deficiency to the taxpayer, the IRS can reduce the interest resulting from the delay.

D. Managerial Act.

This is an administrative act during the processing of a case that involves the loss of records or the exercise of judgment or discretion concerning the management of personnel. A decision concerning the proper application of federal tax law (or other federal or state law) is not a managerial act.

Example.

A revenue agent is examining the taxpayer tax return. During the middle of the examination, the agent is sent to an extended training course. The agent's supervisor decides not to reassign the taxpayer case, so the work is unreasonably delayed until the agent returns. Interest from the unreasonable delay can be abated since both the decision to send the agent to the training class and not to reassign the case are managerial acts.

E. How to Request Abatement of Interest.

1. The taxpayer request an abatement (reduction) of interest on Form 843. The taxpayer should file the claim with the IRS service center where the taxpayer filed the tax return that was affected by the error or delay.

2. If the taxpayer have already paid the interest and the taxpayer would like a credit or refund of interest paid, the taxpayer must file Form 843 within 3 years from the date the taxpayer filed the taxpayer original return or 2 years from the date the taxpayer paid the interest, whichever is later.

a. If the taxpayer have not paid any of the interest, these time limitations for filing Form 843 do not apply.

b. Generally, the taxpayer should file a separate Form 843 for each tax period and each type of tax.

3. However, complete only one Form 843 if the interest is from an IRS error or delay that affected the taxpayer tax for more than one tax period or for more than one type of tax (for example, where 2 or more tax years were being examined).

4. If the taxpayer request for abatement of interest is denied, the taxpayer can appeal the decision to the IRS Appeals Office.

a. Tax Court can review failure to abate interest.

b. The Tax Court can review the IRS' refusal to abate (reduce) interest if all of the following requirements are met.

- The taxpayer filed a request for abatement of interest (Form 843) with the IRS after July 30, 1996.
- The IRS has mailed the taxpayer a notice of final determination or a notice of disallowance.

- - The taxpayer file a petition with the Tax Court within 180 days of the mailing of the notice of final determination or the notice of disallowance.
- c. The following requirements must also be met.
- For individual and estate taxpayers — the taxpayer net worth must not exceed \$2 million as of the filing date of the taxpayer petition for review. For this purpose, individuals filing a joint return shall be treated as separate individuals.
  - For charities and certain cooperatives — the taxpayer must not have more than 500 employees as of the filing date of the taxpayer petition for review.
  - For all other taxpayers — the taxpayer net worth must not exceed \$7 million, and the taxpayer must not have more than 500 employees as of the filing date of the taxpayer petition for review.

F. Abatement of Interest for Individuals Affected by Presidentially Declared Disasters or Military or Terrorist Actions

1. If the taxpayer are (or were) affected by a Presidentially declared disaster occurring after 1996 or a terrorist or military action occurring after September 10, 2001, the IRS may abate (reduce) the amount of interest the taxpayer owe on certain taxes.

2. The IRS may abate interest for the period of any additional time to file or pay that the IRS provides on account of the disaster or the terrorist or military action. The IRS will issue a notice or news release indicating who are affected taxpayers and stating the period of relief.

3. If the taxpayer are eligible for relief from interest, but were charged interest for the period of relief, the IRS may retroactively abate the taxpayer interest. To the extent possible, the IRS can take the following actions.

- Make appropriate adjustments to the taxpayer account.
- Notify the taxpayer when the adjustments are made.
- Refund any interest paid by the taxpayer where appropriate.

4. For more information on disaster area losses, see Disaster Area Losses in Publication 547. For more information on other tax relief for victims of terrorist attacks, see Publication 3920.

IX. Offer in Compromise

A. In certain circumstances, the IRS will allow the taxpayer to pay less than the full amount the taxpayer owe. If the taxpayer think the taxpayer may qualify, the taxpayer should submit the taxpayer offer by filing Form 656, Offer in Compromise.

B. The IRS may accept the taxpayer offer for any of the following reasons.

- There is doubt about the amount the taxpayer owe (or whether the taxpayer owe it).
- There is doubt as to whether the taxpayer can pay the amount the taxpayer owe based on the taxpayer financial situation.
- An economic hardship would result if the taxpayer had to pay the full amount owed.
- The taxpayer case presents compelling reasons that the IRS determines are a sufficient basis for compromise.

C. If the taxpayer offer is rejected, the taxpayer have 30 days to ask the Appeals Office of the IRS to reconsider the taxpayer offer.

D. The IRS offers fast track mediation services to help taxpayers resolve many issues including a dispute regarding an offer in compromise. For more information, see Publication 3605.

E. Generally, if the taxpayer submit an offer in compromise, the IRS will delay certain collection activities. The IRS usually will not levy (take) the taxpayer property to settle the taxpayer tax bill during the following periods.

- While the IRS is evaluating the taxpayer offer in compromise.
- The 30 days immediately after the offer is rejected.
- While the taxpayer timely-filed appeal is being considered by Appeals.

F. Also, if the IRS rejects the taxpayer original offer and the taxpayer submit a revised offer within 30 days of the rejection, the IRS generally will not levy the taxpayer property while it considers the taxpayer revised offer.

For more information about submitting an offer in compromise, see Form 656.

X. Appeal Rights.

A. Because people sometimes disagree on tax matters, the Service has an appeals system. Most differences can be settled within this system without expensive and time-consuming court trials.

B. However, the taxpayer reasons for disagreeing must come within the scope of the tax laws. For example, the taxpayer cannot appeal the taxpayer case based only on moral, religious, political, constitutional, conscientious, or similar grounds.

C. In most instances, the taxpayer may be eligible to take the taxpayer case to court if the taxpayer do not reach an agreement at the taxpayer appeals conference, or if the taxpayer do not want to appeal the taxpayer case to the IRS Office of Appeals. See Appeals to the Courts, later, for more information.

## XI. Appeal Within the IRS.

### A. In General.

1. The taxpayer can appeal an IRS tax decision to a local Appeals Office, which is separate from and independent of the IRS office taking the action the taxpayer disagree with.

2. The Appeals Office is the only level of appeal within the IRS. Conferences with Appeals Office personnel are held in an informal manner by correspondence, by telephone, or at a personal conference.

3. If the taxpayer want an appeals conference, follow the instructions in the letter the taxpayer received. The taxpayer request will be sent to the Appeals Office to arrange a conference at a convenient time and place.

4. The taxpayer or the taxpayer representative should be prepared to discuss all disputed issues at the conference. Most differences are settled at this level.

5. If agreement is not reached at the taxpayer appeals conference, the taxpayer may be eligible to take the taxpayer case to court. See Appeals to the Courts, later.

### B. Protests and Small Case Requests.

1. When the taxpayer request an Appeals conference, the taxpayer may also need to file either a formal written protest or a small case request with the office named in the letter the taxpayer received. Also, see the special appeal request procedures in Publication 1660.

2. In addition, for the appeal procedures for a spouse or former spouse of a taxpayer seeking relief from joint and several liability on a joint return, see Rev. Proc. 2003-19, which is on page 371 of the Internal Revenue Bulletin 2003-5 at [www.irs.gov/pub/irs-irbs/irb03-05.pdf](http://www.irs.gov/pub/irs-irbs/irb03-05.pdf).

### C. Written protest.

1. The taxpayer need to file a written protest in the following cases.

- All employee plan and exempt organization cases without regard to the dollar amount at issue.
- All partnership and S corporation cases without regard to the dollar amount at issue.

- All other cases, unless the taxpayer qualify for the small case request procedure, or other special appeal procedures such as requesting Appeals consideration of liens, levies, seizures, or installment agreements.

2. If the taxpayer must submit a written protest, see the instructions in Publication 5 about the information the taxpayer need to provide. The IRS urges the taxpayer to provide as much information as the taxpayer can, as it will help speed up the taxpayer appeal. That will save the taxpayer both time and money.

3. Be sure to send the protest within the time limit specified in the letter the taxpayer received.

#### D. Small case request.

1. If the total amount for any tax period is not more than \$25,000, the taxpayer may make a small case request instead of filing a formal written protest. In figuring the total amount, include a proposed increase or decrease in tax (including penalties), or claimed refund. If the taxpayer are making an offer in compromise, include total unpaid tax, penalty, and interest due.

2. For a small case request, follow the instructions in our letter to the taxpayer by sending a letter:

- Requesting Appeals consideration,
- Indicating the changes the taxpayer do not agree with, and
- Indicating the reasons why the taxpayer do not agree.

#### E. Representation

1. The taxpayer can represent the him or herself at the taxpayer appeals conference, or the taxpayer can be represented by any federally authorized practitioner, including an attorney, a certified public accountant, an enrolled actuary, or an enrolled agent.

2. If the taxpayer representative attends a conference without the taxpayer, he or she can receive or inspect confidential information only if the taxpayer have filed a power of attorney or a tax information authorization. The taxpayer can use a Form 2848 or any other properly written power of attorney or authorization.

3. The taxpayer can also bring witnesses to support the taxpayer position.

#### F. Confidentiality privilege.

Generally, the same confidentiality protection that the taxpayer have with an attorney also applies to certain communications that the taxpayer have with federally authorized practitioners. See Confidentiality privilege under If The tax return Is Examined, earlier.

X. Appeals to the Courts.

A. In General.

1. If the taxpayer and the IRS still disagree after the appeals conference, the taxpayer may be entitled to take the taxpayer case to the United States Tax Court, the United States Court of Federal Claims, or the United States District Court. These courts are independent of the IRS.

2. If the taxpayer elect to bypass the IRS' appeals system, the taxpayer may be able to take the taxpayer case to one of the courts listed above. However, a case petitioned to the United States Tax Court will normally be considered for settlement by an Appeals Office before the Tax Court hears the case.

3. If the taxpayer unreasonably fail to pursue the IRS' appeals system, or if the taxpayer case is intended primarily to cause a delay, or the taxpayer position is frivolous or groundless, the Tax Court may impose a penalty of up to \$25,000. See Appeal Within the IRS , earlier.

B. Prohibition on requests to taxpayers to give up rights to bring civil action.

1. The Government cannot ask the taxpayer to waive the taxpayer right to sue the United States or a Government officer or employee for any action taken in connection with the tax laws.

2. However, the taxpayer right to sue can be waived if:

- The taxpayer knowingly and voluntarily waive that right,
- The request to waive that right is made in writing to the taxpayer attorney or other federally authorized practitioner, or
- The request is made in person and the taxpayer attorney or other representative is present.

C. Burden of proof.

1. In General.

a. For court proceedings resulting from examinations started after July 22, 1998, the IRS generally has the burden of proof for any factual issue if the taxpayer have met the following requirements.

- The taxpayer introduced credible evidence relating to the issue.

- The taxpayer complied with all substantiation requirements of the Internal Revenue Code.
- The taxpayer maintained all records required by the Internal Revenue Code.
- The taxpayer cooperated with all reasonable requests by the IRS for information regarding the preparation and related tax treatment of any item reported on the taxpayer tax return.
- The taxpayer had a net worth of \$7 million or less and not more than 500 employees at the time the taxpayer tax liability is contested in any court proceeding if the taxpayer tax return is for a corporation, partnership, or trust.

b. The burden of proof does not change on an issue when another provision of the tax laws requires a specific burden of proof with respect to that issue.

## 2. Use of statistical information.

In the case of an individual, the IRS has the burden of proof in court proceedings based on any IRS reconstruction of income solely through the use of statistical information on unrelated taxpayers.

## 3. Penalties.

The IRS has the burden of initially producing evidence in court proceedings with respect to the liability of any individual taxpayer for any penalty, addition to tax, or additional amount imposed by the tax laws.

## D. Recovering litigation or administrative costs.

### 1. In General.

These are the expenses that the taxpayer pay to defend the taxpayer position to the IRS or the courts. The taxpayer may be able to recover reasonable litigation or administrative costs if all of the following conditions apply.

- The taxpayer are the prevailing party.
- The taxpayer exhaust all administrative remedies within the IRS.
- The taxpayer net worth is below a certain limit (see Net worth requirements, later).
- The taxpayer do not unreasonably delay the proceeding.

- The taxpayer apply for administrative costs within 90 days of the date on which the final decision of the IRS Office of Appeals as to the determination of the tax, interest, or penalty was mailed to the taxpayer.
- The taxpayer apply for litigation costs within the time frames provided by Tax Court Rule 231.

2. Prevailing party, reasonable litigation costs, and reasonable administrative costs are explained later.

Note. If the IRS denies the taxpayer award of administrative costs, and the taxpayer want to appeal, the taxpayer must petition the Tax Court within 90 days of the date on which the IRS mails the denial notice.

3. Prevailing party.

a. Generally, the taxpayer are the prevailing party if:

- The taxpayer substantially prevail with respect to the amount in controversy or on the most significant tax issue or set of issues in question, and
- The taxpayer meet the net worth requirements, discussed later.

b. The taxpayer will not be treated as the prevailing party if the United States establishes that its position was substantially justified. The position of the United States is presumed not to be substantially justified if the IRS:

- Did not follow its applicable published guidance (such as regulations, revenue rulings, notices, announcements, private letter rulings, technical advice memoranda, and determination letters issued to the taxpayer) in the proceeding (This presumption can be overcome by evidence.), or
- Has lost in courts of appeal for other circuits on substantially similar issues.

c. The court will generally decide who is the prevailing party.

4. Reasonable litigation costs.

Reasonable litigation costs include:

- Reasonable court costs.
- The reasonable costs of studies, analyses, engineering reports, tests, or projects found by the court to be necessary for the preparation of the taxpayer case.

- The reasonable costs of expert witnesses.
- Attorney fees that generally may not exceed \$170 per hour for calendar year 2007. The hourly rate is indexed for inflation. See Attorney fees, later.

5. Reasonable administrative costs.

These include the following costs.

- Any administrative fees or similar charges imposed by the IRS.
- The reasonable costs of studies, analyses, engineering reports, tests, or projects.
- The reasonable costs of expert witnesses.
- Attorney fees that generally may not exceed \$170 per hour for calendar year 2007. See Attorney fees, later.

6. Timing of costs.

Administrative costs can be awarded for costs incurred after the earliest of:

- The date the first letter of proposed deficiency is sent that allows the taxpayer an opportunity to request administrative review in the IRS Office of Appeals,
- The date the taxpayer receive notice of the IRS Office of Appeals' decision, or
- The date of the notice of deficiency.

7. Net worth requirements.

An individual taxpayer may be able to recover litigation or administrative costs if the following requirements are met.

- For individuals — the taxpayer net worth does not exceed \$2 million as of the filing date of the taxpayer petition for review. For this purpose, individuals filing a joint return are treated as separate individuals.
- For estates — the taxpayer net worth does not exceed \$2 million as of the date of the decedent's death.
- For charities and certain cooperatives — the taxpayer do not have more than 500 employees as of the filing date of the taxpayer petition for review.

- For all other taxpayers — as of the filing date of the taxpayer petition for review, the taxpayer net worth does not exceed \$7 million, and the taxpayer must not have more than 500 employees.

8. Qualified offer rule.

a. The taxpayer can also receive reasonable costs and fees and be treated as a prevailing party in a civil action or proceeding if:

- The taxpayer make a qualified offer to the IRS to settle the taxpayer case,
- The IRS does not accept that offer, and
- The tax liability (not including interest, unless interest is at issue) later determined by the court is equal to or less than the amount of the taxpayer qualified offer.

b. The taxpayer must also meet the remaining requirements, including the exhaustion of administrative remedies and the net worth requirement, discussed earlier, to get the benefit of the qualified offer rule.

9. Qualified offer.

a. This is a written offer made by the taxpayer during the qualified offer period. It must specify both the offered amount of the taxpayer liability (not including interest) and that it is a qualified offer.

b. To be a qualified offer, it must remain open from the date it is made until the earliest of:

- The date it is rejected,
- The date the trial begins, or
- 90 days from the date it is made.

10. Qualified offer period.

This period begins on the day the IRS mails the taxpayer the first letter of proposed deficiency that allows the taxpayer to request review by the IRS Office of Appeals. It ends 30 days before the taxpayer case is first set for trial.

11. Attorney fees.

a. For the calendar year 2007, the basic rate for attorney fees is \$170 per hour and can be higher in certain limited circumstances. Those circumstances include the level of difficulty of the issues in the case and the local availability of tax expertise. The basic rate will be subject to a cost-of-living adjustment each year.

b. Attorney fees include the fees paid by a taxpayer for the services of anyone who is authorized to practice before the Tax Court or before the IRS. In addition, attorney fees can be awarded in civil actions for unauthorized inspection or disclosure of a taxpayer's return or return information.

c. Fees can be awarded in excess of the actual amount charged if:

- The taxpayer are represented for no fee, or for a nominal fee, as a pro bono service, and
- The award is paid to the taxpayer representative or to the taxpayer representative's employer.

E. Jurisdiction for determination of employment status.

1. In General.

a. The Tax Court can review IRS employment status determinations (for example, whether individuals hired by the taxpayer are in fact the taxpayer employees or independent contractors) and the amount of employment tax under such determinations.

b. Tax Court review can take place only if, in connection with an audit of any person, there is an actual controversy involving a determination by the IRS as part of an examination that either:

- One or more individuals performing services for that person are employees of that person, or
- That person is not entitled to relief under Section 530(a) of the Revenue Act of 1978 (discussed later).

c. The following rules also apply to a Tax Court review of employment status.

- A Tax Court petition to review these determinations can be filed only by the person for whom the services are performed,
- If the taxpayer receive a Notice of Determination by certified or registered mail, the taxpayer must file a petition for Tax Court review within 90 days of the date of mailing that notice (150 days if the notice is addressed to the taxpayer outside the United States),
- If during the Tax Court proceeding, the taxpayer begin to treat as an employee an individual whose employment status is at issue, the Tax Court will not consider that change in its decision,

- Assessment and collection of tax is suspended while the Tax Court review is taking place,
- There can be a de novo review by the Tax Court (a review which does not consider IRS administrative findings), and
- At the taxpayer request and with the Tax Court's agreement, small tax case procedures (discussed later) are available to simplify the case resolution process when the amount at issue (including additions to tax and penalties) is \$50,000 or less for each tax period involved.

d For further information, see Publication 3953, Questions and Answers About Tax Court Proceedings for Determination of Employment Status Under IRC Section 7436.

e. Section 530(a) of the Revenue Act of 1978.

This section relieves an employer of certain employment tax responsibilities for individuals not treated as employees. It also provides relief to taxpayers under audit or involved in administrative or judicial proceedings.

F. Tax Court review of request for relief from joint and several liability on a joint return.

1. As discussed later, at Relief from joint and several liability on a joint return under Claims for Refund, the taxpayer can request relief from liability for tax the taxpayer owe, plus related penalties and interest, that the taxpayer believe should be paid by the taxpayer spouse (or former spouse).

2. The taxpayer also can petition (ask) the Tax Court to review the taxpayer request for innocent spouse relief or separation of liability if either:

- The IRS sends the taxpayer a determination notice denying, in whole or in part, the taxpayer request, or
- The taxpayer do not receive a determination notice from the IRS within 6 months from the date the taxpayer file Form 8857.

3. If the taxpayer receive a determination notice, the taxpayer must petition the Tax Court to review the taxpayer request during the 90-day period that begins on the date the IRS mails the notice. See Publication 971 for more information.

Note. The taxpayer spouse or former spouse may file a written protest and request an Appeals conference to protest the taxpayer claim of innocent spouse relief or separation of liability.

G. Tax Court

1. The taxpayer can take the taxpayer case to the United States Tax Court if the taxpayer disagree with the IRS over:

- Income tax,
- Estate tax,
- Gift tax, or
- Certain excise taxes of private foundations, public charities, qualified pension and other retirement plans, or real estate investment trusts.

2. For information on Tax Court review of a determination of employment status, see Jurisdiction for determination of employment status, earlier.

3. For information on Tax Court review of an IRS refusal to abate interest, see Tax Court can review failure to abate interest, earlier under Examination of Returns.

4. For information on Tax Court review of Appeals determinations with respect to lien notices and proposed levies, see Publication 1660.

5. The taxpayer cannot take the taxpayer case to the Tax Court before the IRS sends the taxpayer a notice of deficiency. The taxpayer can only appeal the taxpayer case if the taxpayer file a petition within 90 days from the date the notice is mailed to the taxpayer (150 days if it is addressed to the taxpayer outside the United States).

6. The notice will show the 90th (and 150th) day by which the taxpayer must file the taxpayer petition with the Tax Court.

Note. If the taxpayer consent, the IRS can withdraw a notice of deficiency. Once withdrawn, the limits on credits, refunds, and assessments concerning the notice are void, and the taxpayer and the IRS have the rights and obligations that the taxpayer had before the notice was issued. The suspension of any time limitation while the notice of deficiency was issued will not change when the notice is withdrawn.

7. After the notice is withdrawn, the taxpayer cannot file a petition with the Tax Court based on the notice. Also, the IRS can later issue a notice of deficiency in a greater or lesser amount than the amount in the withdrawn deficiency.

8. Generally, the Tax Court hears cases before any tax has been assessed and paid; however, the taxpayer can pay the tax after the notice of deficiency has been issued and still petition the Tax Court for review.

- a. If the taxpayer do not file the taxpayer petition on time, the proposed tax will be assessed, a bill will be sent, and the taxpayer will not be able to take the taxpayer case to the Tax Court.

b. Under the law, the taxpayer must pay the tax within 21 days (10 business days if the amount is \$100,000 or more). Collection can proceed even if the taxpayer think that the amount is excessive. Publication 594 explains IRS collection procedures.

9. If the taxpayer filed the taxpayer petition on time, the court will schedule the taxpayer case for trial at a location convenient to the taxpayer. The taxpayer can represent the his or herself before the Tax Court or the taxpayer can be represented by anyone admitted to practice before that court.

H. Small tax case procedure.

1. If the amount in the taxpayer case is \$50,000 or less for any 1 tax year or period, the taxpayer can request that the taxpayer case be handled under the small tax case procedure.

2. If the Tax Court approves, the taxpayer can present the taxpayer case to the Tax Court for a decision that is final and that the taxpayer cannot appeal. The taxpayer can get more information regarding the small tax case procedure and other Tax Court matters from the United States Tax Court, 400 Second Street, N.W., Washington, DC 20217. More information can be found on the Tax Court's website at [www.ustaxcourt.gov](http://www.ustaxcourt.gov).

I. Motion to request redetermination of interest.

In certain cases, the taxpayer can file a motion asking the Tax Court to redetermine the amount of interest on either an underpayment or an overpayment. The taxpayer can do this only in a situation that meets all of the following requirements.

- The IRS has assessed a deficiency that was determined by the Tax Court.
- The assessment included interest.
- The taxpayer have paid the entire amount of the deficiency plus the interest claimed by the IRS.
- The Tax Court has found that the taxpayer made an overpayment.

The taxpayer must file the motion within one year after the decision of the Tax Court becomes final.

J. District Court and Court of Federal Claims

1. Generally, the District Court and the Court of Federal Claims hear tax cases only after the taxpayer have paid the tax and filed a claim for a credit or refund.

2. As explained later under Claims for Refund, the taxpayer can file a claim with the IRS for a credit or refund if the taxpayer think that the tax the taxpayer paid is incorrect or excessive.

3. If the taxpayer claim is totally or partially disallowed by the IRS, the taxpayer should receive a notice of claim disallowance. If the IRS does not act on the taxpayer claim within 6 months from the date the taxpayer filed it, the taxpayer can then file suit for a refund.

4. The taxpayer generally must file suit for a credit or refund no later than 2 years after the IRS informs the taxpayer that the taxpayer claim has been rejected. However, the taxpayer can file suit if it has been 6 months since the taxpayer filed the taxpayer claim and the IRS has not yet delivered a decision.

5. The taxpayer can file suit for a credit or refund in the taxpayer United States District Court or in the United States Court of Federal Claims. However, the taxpayer cannot appeal to the United States Court of Federal Claims if the taxpayer claim is for credit or refund of a penalty that relates to promoting an abusive tax shelter or to aiding and abetting the understatement of tax liability on someone else's return.

6. For information about procedures for filing suit in either court, contact the Clerk of the taxpayer District Court or of the United States Court of Federal Claims. For information on District Court review of Appeals determinations with respect to lien notices and proposed levies, see Publication 1660.

## XI. Refund or Credit of Overpayments Before Final Determination

### A. In General.

1. Any court with proper jurisdiction, including the Tax Court, can order the IRS to refund any part of a tax deficiency that the IRS collects from the taxpayer during a period when the IRS is not permitted to assess that deficiency, or to levy or engage in any court proceeding to collect that deficiency.

2. In addition, the court can order a refund of any part of an overpayment determined by the Tax Court that is not at issue on appeal to a higher court. The court can order these refunds before its decision on the case is final.

3. Generally, the IRS is not permitted to take action on a tax deficiency during:

- The 90-day (or 150-day if outside the United States) period that the taxpayer have to petition a notice of deficiency to the Tax Court, or
- The period that the case is under appeal if a bond is provided.

### B. Claims for Refund

#### 1. In General

a. If the taxpayer believe the taxpayer have overpaid the taxpayer tax, the taxpayer have a limited amount of time in which to file a claim for a credit or refund. The

taxpayer can claim a credit or refund by filing Form 1040X. See Time for Filing a Claim for Refund, later.

b. File the taxpayer claim by mailing it to the Internal Revenue Service Center where the taxpayer filed the taxpayer original return. File a separate form for each year or period involved. Include an explanation of each item of income, deduction, or credit on which the taxpayer are basing the taxpayer claim.

c. Corporations should file Form 1120X, Amended U.S. Corporation Income Tax Return, or other form appropriate to the type of credit or refund claimed.

d. See Publication 3920 for information on filing claims for tax forgiveness for individuals affected by terrorist attacks.

2. Requesting a copy of the taxpayer tax return.

The taxpayer can obtain a copy of the actual return and all attachments the taxpayer filed with the IRS for an earlier year. This includes a copy of the Form W-2 or Form 1099 filed with the tax return. Use Form 4506 to make the taxpayer request. The taxpayer will be charged a fee, which the taxpayer must pay when the taxpayer submit Form 4506.

3. Requesting a copy of the taxpayer tax account information.

a. Use Form 4506-T, Request for Transcript of Tax Return, to request free copies of the taxpayer tax return transcript, tax account transcript, record of account, verification of nonfiling, or Form W-2, Form 1099 series, Form 1098 series, or Form 5498 series transcript.

b. The tax return transcript contains most of the line items of a tax return. A tax account transcript contains information on the financial status of the account, such as payments, penalty assessments, and adjustments.

c. A record of account is a combination of line item information and later adjustments to the account. Form W-2, Form 1099 series, Form 1098 series, or Form 5498 series transcript contains data from these information returns.

4. Penalty for erroneous claim for refund.

a. If the taxpayer claim an excessive amount of tax refund or credit relating to income tax (other than a claim relating to the earned income credit), the taxpayer may be liable for a penalty of 20% of the amount that is determined to be excessive.

b. An excessive amount is the amount of the claim for refund or credit that is more than the amount of claim allowable for the tax year. The penalty may be waived if the taxpayer can show that the taxpayer had a reasonable basis for making the claim.

C. Time for Filing a Claim for Refund

1. Generally, the taxpayer must file a claim for a credit or refund within 3 years from the date the taxpayer filed the taxpayer original return or 2 years from the date the taxpayer paid the tax, whichever is later. If the taxpayer do not file a claim within this period, the taxpayer may no longer be entitled to a credit or a refund.

2. If the due date to file a return or a claim for a credit or refund is a Saturday, Sunday, or legal holiday, it is filed on time if it is filed on the next business day. Returns the taxpayer filed before the due date are considered filed on the due date. This is true even when the due date is a Saturday, Sunday, or legal holiday.

D. Disaster area claims for refund.

1. If the taxpayer live in a Presidentially declared disaster area or are affected by terroristic or military action, the deadline to file a claim for a refund may be postponed. This section discusses the special rules that apply to Presidentially declared disaster area refunds.

2. A Presidentially declared disaster is a disaster that occurred in an area declared by the President to be eligible for federal assistance under the Disaster Relief and Emergency Assistance Act.

E. Postponed refund deadlines.

1. The IRS may postpone for up to 1 year the deadlines for filing a claim for refund. The postponement can be used by taxpayers who are affected by a Presidentially declared disaster. The IRS may also postpone deadlines for filing income and employment tax returns, paying income and employment taxes, and making contributions to a traditional IRA or Roth IRA. For more information, see Publication 547.

2. If any deadline is postponed, the IRS will publicize the postponement in the taxpayer area and publish a news release, revenue ruling, revenue procedure, notice, announcement, or other guidance in the Internal Revenue Bulletin.

3. A list of the areas eligible for assistance under the Disaster Relief and Emergency Assistance Act is available at the Federal Emergency Management Agency (FEMA) website at [www.fema.gov](http://www.fema.gov) and at the IRS website at [www.irs.gov](http://www.irs.gov).

F. Nonfilers can get refund of overpayments paid within 3-year period.

1. The Tax Court can consider taxes paid during the 3-year period preceding the date of a notice of deficiency for determining any refund due to a nonfiler. This means that if the taxpayer do not file the tax return, and the taxpayer receive a notice of deficiency in the third year after the due date (with extensions) of the tax return and file suit with the Tax Court to contest the notice of deficiency, the taxpayer may be able to receive a refund of excessive amounts paid within the 3-year period preceding the date of the notice of deficiency.

2. The IRS may postpone for up to 1 year certain tax deadlines, including the time for filing claims for refund, for taxpayers who are affected by a terrorist attack occurring after September 10, 2001. For more information, see Publication 3920.

G. Claim for refund by estates electing the installment method of payment.

1. In certain cases where an estate has elected to make tax payments through the installment method, the executor can file a suit for refund with a Federal District Court or the U.S. Court of Federal Claims before all the installment payments have been made. However, all the following must be true before a suit can be filed.

- The estate consists largely of an interest in a closely-held business.
- All installment payments due on or before the date the suit is filed have been made.
- No accelerated installment payments have been made.
- No Tax Court case is pending with respect to any estate tax liability.
- If a notice of deficiency was issued to the estate regarding its liability for estate tax, the time for petitioning the Tax Court has passed.
- No proceeding is pending for a declaratory judgment by the Tax Court on whether the estate is eligible to pay tax in installments.
- The executor has not included any previously litigated issues in the current suit for refund.
- The executor does not discontinue making installment payments timely, while the court considers the suit for refund.

2. If in its final decision on the suit for refund the court redetermines the estate's tax liability, the IRS must refund any part of the estate tax amount that is disallowed. This includes any part of the disallowed amount previously collected by the IRS.

E. Protective claim for refund.

1. If the taxpayer right to a refund is contingent on future events and may not be determinable until after the time period for filing a claim for refund expires, the taxpayer can file a protective claim for refund.

2. A protective claim can be either a formal claim or an amended return for credit or refund. Protective claims are often based on current litigation or expected changes in the tax law, other legislation, or regulations.

3. A protective claim preserves the taxpayer right to claim a refund when the contingency is resolved.

4. A protective claim does not have to state a particular dollar amount or demand an immediate refund. However, to be valid, a protective claim must:

- Be in writing and be signed,

- Include the taxpayer name, address, social security number or individual taxpayer identification number, and other contact information,
- Identify and describe the contingencies affecting the claim,
- Clearly alert the IRS to the essential nature of the claim, and
- Identify the specific year(s) for which a refund is sought.

5. Generally, the IRS will delay action on the protective claim until the contingency is resolved. Once the contingency is resolved, the IRS may obtain additional information necessary to process the claim and then either allow or disallow the claim.

6. Mail the taxpayer protective claim for refund to the address listed in the instructions for Form 1040X, under Where To File.

#### F. Exceptions

The limits on the taxpayer claim for refund can be affected by the type of item that forms the basis of the taxpayer claim.

#### G. Special refunds.

1. If the taxpayer file a claim for refund based on one of the items listed below, the limits discussed earlier under Time for Filing a Claim for Refund may not apply. These special items are:

- A bad debt,
- A worthless security,
- A payment or accrual of foreign tax,
- A net operating loss carryback, and
- A carryback of certain tax credits.

2. The limits discussed earlier also may not apply if the taxpayer have signed an agreement to extend the period of assessment of tax.

3. For information on special rules on filing claims for an individual affected by a terrorist attack, see Publication 3920.

#### H. Periods of financial disability.

1. If the taxpayer are an individual (not a corporation or other taxpaying entity), the period of limitations on credits and refunds can be suspended during periods when the taxpayer cannot manage the taxpayer financial affairs because of physical or mental impairment that is medically determinable and either:

- Has lasted or can be expected to last continuously for at least 12 months, or
- Can be expected to result in death.

2. The period for filing a claim for refund will not be suspended for any time that someone else, such as the taxpayer spouse or guardian, was authorized to act for the taxpayer in financial matters.

3. To claim financial disability, the taxpayer generally must submit the following statements with the taxpayer claim for credit or refund:

a. A written statement signed by a physician, qualified to make the determination, that sets forth:

(1) The name and a description of the taxpayer physical or mental impairment,

(2) The physician's medical opinion that the taxpayer physical or mental impairment prevented the taxpayer from managing the taxpayer financial affairs,

(3) The physician's medical opinion that the taxpayer physical or mental impairment was or can be expected to result in death, or that it has lasted (or can be expected to last) for a continuous period of not less than 12 months, and

(4) To the best of the physician's knowledge, the specific time period during which the taxpayer were prevented by such physical or mental impairment from managing the taxpayer financial affairs, and

(5) A written statement by the person signing the claim for credit or refund that no person, including the taxpayer spouse, was authorized to act on the taxpayer behalf in financial matters during the period described in paragraph (1)(d) of the physician's statement. Alternatively, if a person was authorized to act on the taxpayer behalf in financial matters during any part of the period described in that paragraph, the beginning and ending dates of the period of time the person was so authorized.

b. The period of limitations will not be suspended on any claim for refund that (without regard to this provision) was barred as of July 22, 1998.

#### I. Limit on Amount of Refund

If the taxpayer file the taxpayer claim within 3 years after filing the tax return, the credit or refund cannot be more than the part of the tax paid within the 3 years (plus the length of any extension of time granted for filing the tax return) before the taxpayer filed the claim.

Example 1. The taxpayer made estimated tax payments of \$1,000 and got an automatic extension of time from April 15, 2003, to August 15, 2003, to file the taxpayer 2002 income tax return. When the taxpayer filed the tax return on that date, the taxpayer paid an additional \$200

tax. Three years later, on August 15, 2006, the taxpayer file an amended return and claim a refund of \$700. Because the taxpayer filed within 3 years after filing the tax return, the taxpayer could get a refund of any tax paid after April 15, 2003.

Example 2. The situation is the same as in Example 1, except that the taxpayer filed the tax return on October 31, 2003, 2½ months after the extension period ended. The taxpayer paid an additional \$200 on that date. Three years later, on October 27, 2006, the taxpayer file an amended return and claim a refund of \$700. Although the taxpayer filed the taxpayer claim within 3 years from the date the taxpayer filed the taxpayer original return, the refund is limited to \$200. The estimated tax of \$1,000 was paid before the 3 years plus the 4-month extension period.

#### J. Claim filed after the 3-year period.

If the taxpayer file a claim after the 3-year period, but within 2 years from the time the taxpayer paid the tax, the credit or refund cannot be more than the tax the taxpayer paid within the 2 years immediately before the taxpayer filed the claim.

Example. The taxpayer filed the taxpayer 2002 tax return on April 15, 2003. The taxpayer paid \$500 in tax. On November 2, 2004, after an examination of the taxpayer 2002 return, the taxpayer had to pay \$200 in additional tax. On May 2, 2006, the taxpayer file a claim for a refund of \$300. The taxpayer refund will be limited to the \$200 the taxpayer paid during the 2 years immediately before the taxpayer filed the taxpayer claim.

#### K. Processing Claims for Refund

1. Claims are usually processed shortly after they are filed. The taxpayer claim may be denied, accepted as filed, or it may be examined. If a claim is examined, the procedures are almost the same as in the examination of a tax return.

2. However, if the taxpayer are filing a claim for credit or refund based only on contested income tax or on estate tax or gift tax issues considered in previously examined returns and the taxpayer do not want to appeal within the IRS, the taxpayer should request in writing that the claim be immediately rejected.

3. A notice of claim disallowance will then be promptly sent to the taxpayer.

4. The taxpayer have 2 years from the date of mailing of the notice of disallowance to file a refund suit in the United States District Court or in the United States Court of Federal Claims.

#### L. Explanation of Any Claim for Refund Disallowance

1. The IRS must explain to the taxpayer the specific reasons why the taxpayer claim for refund is disallowed or partially disallowed. Claims for refund are disallowed based on a preliminary review or on further examination. Some of the reasons the taxpayer claim may be disallowed include the following.

- It was filed late.
- It was based solely on the unconstitutionality of the revenue acts.
- It was waived as part of a settlement.
- It covered a tax year or issues which were part of a closing agreement or an offer in compromise.
- It was related to a return closed by a final court order.

2. If the taxpayer claim is disallowed for these reasons, or any other reason, the IRS must send the taxpayer an explanation.

#### M. Reduced Refund

1. The taxpayer refund may be reduced by an additional tax liability. Also, the taxpayer refund may be reduced by amounts the taxpayer owe for past-due child support, debts the taxpayer owe to another federal agency, or past-due legally enforceable state income tax obligations.

2. The taxpayer will be notified if this happens. For those reductions, the taxpayer cannot use the appeal and refund procedures discussed in this publication. However, the taxpayer may be able to take action against the other agency.

3. Offset of past-due state income tax obligations against overpayments. Federal tax overpayments can be used to offset past-due, legally enforceable state income tax obligations. For the offset procedure to apply, the taxpayer federal income tax return must show an address in the state that requests the offset. In addition, the state must first:

- Notify the taxpayer by certified mail with return receipt that the state plans to ask for an offset against the taxpayer federal income tax overpayment,
- Give the taxpayer at least 60 days to show that some or all of the state income tax is not past due or not legally enforceable,
- Consider any evidence from the taxpayer in determining that income tax is past due and legally enforceable,
- Satisfy any other requirements to ensure that there is a valid past-due, legally enforceable state income tax obligation, and
- Show that all reasonable efforts to obtain payment have been made before requesting the offset.

4. Past-due, legally enforceable state income tax obligation.

This is an obligation (debt):

- Established by a court decision or administrative hearing and no longer subject to judicial review, or
- That is assessed, uncollected, can no longer be redetermined, and is less than 10 years overdue.

N. Offset priorities.

Overpayments are offset in the following order.

1. Federal income tax owed.
2. Past-due child support.
3. Past-due, legally enforceable debt owed to a federal agency.
4. Past-due, legally enforceable state income tax debt.
5. Future federal income tax liability.

Note. If more than one state agency requests an offset for separate debts, the offsets apply against the taxpayer overpayment in the order in which the debts accrued. In addition, state income tax includes any local income tax administered by the chief tax administration agency of a state.

Note. The Tax Court cannot decide the validity or merits of the credits or offsets (for example, collection of delinquent child support or student loan payments) made that reduce or eliminate a refund to which the taxpayer were otherwise entitled.

O. Injured spouse exception.

1. When a joint return is filed and the refund is used to pay one spouse's past-due child support, spousal support, or a federal debt, the other spouse can be considered an injured spouse. An injured spouse can get a refund for his or her share of the overpayment that would otherwise be used to pay the past-due amount.

2. The taxpayer are considered an injured spouse if:
  - a. The taxpayer are not legally obligated to pay the past-due amount and
  - b. The taxpayer meet any of the following conditions:

(1) The taxpayer made and reported tax payments (such as federal income tax withheld from wages or estimated tax payments).

(2) The taxpayer had earned income (such as wages, salaries, or self-employment income) and claimed the earned income credit or the additional child tax credit.

(3) The taxpayer claimed a refundable credit, such as the health coverage tax credit or the refundable credit for prior year minimum tax.

Note. If the taxpayer residence was in a community property state at any time during the year, the taxpayer can file Form 8379 even if only item (1) above applies.

3. If the taxpayer are an injured spouse, the taxpayer can obtain the taxpayer portion of the joint refund by completing Form 8379. Follow the instructions on the form.

4. Relief from joint and several liability on a joint return.

a. Generally, joint and several liability applies to all joint returns.

(1) This means that both the taxpayer and the taxpayer spouse (or former spouse) are liable for any tax shown on a joint return plus any understatement of tax that may become due later.

(2) This is true even if a divorce decree states that a former spouse will be responsible for any amounts due on previously filed joint returns.

b. In some cases, a spouse will be relieved of the tax, interest, and penalties on a joint tax return. Three types of relief are available.

- Innocent spouse relief.
- Separation of liability.
- Equitable relief.

5. Form 8857.

a. Each kind of relief is different and has different requirements. The taxpayer must file Form 8857, Request for Innocent Spouse Relief, to request relief.

b. Form 8857 must be filed no later than 2 years after the date on which the IRS first attempted to collect the tax from the taxpayer.

c. See the instructions for Form 8857 and Publication 971 for more information on these kinds of relief and who may qualify for them.