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REFORMING HOW THE IRS RESOLVES TAXPAYER DISPUTES

HEARING

BEFORE THE

SUBCOMMITTEE ON OVERSIGHT

OF THE

COMMITTEE ON WAYS AND MEANS
U.S. HOUSE OF REPRESENTATIVES

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IRS REFORM: RESOLVING TAXPAYER DISPUTES

WEDNESDAY, SEPTEMBER 13, 2017

U.S. HOUSE OF REPRESENTATIVES,
COMMITTEE ON WAYS AND MEANS,
SUBCOMMITTEE ON OVERSIGHT,
Washington, DC.

The Subcommittee met, pursuant to call, at 2:10 p.m., in Room 1100, Longworth House Office Building, Hon. Vern Buchanan [Chairman of the Subcommittee] presiding.

[The advisory announcing the hearing follows:]

WAYS AND MEANS
CHAIRMAN KEVIN BRADY

Chairman Buchanan Announces Hearing on Reforming How the IRS Resolves Taxpayer Disputes

House Ways and Means Oversight Subcommittee Chairman Vern Buchanan (R-FL) announced today that the Subcommittee will hold a hearing on making reforms to the Internal Revenue Service (IRS). The hearing is entitled "IRS Reform: Resolving Taxpayer Disputes." The hearing will focus on the taxpayer perspective and consider ways the agency can resolve taxpayer disputes in a timely, efficient, and cost-effective manner. **The hearing will take place on Wednesday, September 13, 2017 in 1100 Longworth House Office Building, beginning at 2:00 PM.**

In view of the limited time to hear witnesses, oral testimony at this hearing will be from invited witnesses only. However, any individual or organization may submit a written statement for consideration by the Committee and for inclusion in the printed record of the hearing.

DETAILS FOR SUBMISSION OF WRITTEN COMMENTS:

Please Note: Any person(s) and/or organization(s) wishing to submit written comments for the hearing record must follow the appropriate link on the hearing page of the Committee website and complete the informational forms. From the Committee homepage, http://waysandmeans.house.gov, select "Hearings." Select the hearing for which you would like to make a submission, and click on the link entitled, "Click here to provide a submission for the record." Once you have followed the online instructions, submit all requested information. ATTACH your submission as a Word document, in compliance with the formatting requirements listed below, **by the close of business on September 27, 2017.** For questions, or if you encounter technical problems, please call (202) 225-3625.

FORMATTING REQUIREMENTS:

The Committee relies on electronic submissions for printing the official hearing record. As always, submissions will be included in the record according to the discretion of the Committee. The Committee will not alter the content of your submission, but we reserve the right to format it according to our guidelines. Any submission provided to the Committee by a witness, any materials submitted for the printed record, and any written

comments in response to a request for written comments must conform to the guidelines listed below. Any submission not in compliance with these guidelines will not be printed, but will be maintained in the Committee files for review and use by the Committee.

All submissions and supplementary materials must be submitted in a single document via email, provided in Word format and must not exceed a total of 10 pages. Witnesses and submitters are advised that the Committee relies on electronic submissions for printing the official hearing record.

All submissions must include a list of all clients, persons and/or organizations on whose behalf the witness appears. The name, company, address, telephone, and fax numbers of each witness must be included in the body of the email. Please exclude any personal identifiable information in the attached submission.

Failure to follow the formatting requirements may result in the exclusion of a submission. All submissions for the record are final.

The Committee seeks to make its facilities accessible to persons with disabilities. If you are in need of special accommodations, please call 202-225-1721 or 202-226-3411 TTD/TTY in advance of the event (four business days' notice is requested). Questions with regard to special accommodation needs in general (including availability of Committee materials in alternative formats) may be directed to the Committee as noted above.

Note: All Committee advisories and news releases are available at http://www.waysandmeans.house.gov/

Chairman BUCHANAN. The Subcommittee will come to order.

Welcome to the Ways and Means Oversight Subcommittee hearing on "IRS Reform: Resolving Taxpayer Disputes."

Before I begin my official statement, I would like to recognize the extraordinary effort of two of our witnesses today who made it up here from Florida.

I think you drove from Orlando. So that is pretty impressive.

Both Mr. Shinn and Ms. Wilson came from the great state of Florida. Thank you very much for your determination to be here. I know it wasn't easy.

And let me pause for a moment to thank all our first responders, local government officials, and community members who stepped up and responded to Hurricane Irma in my home state of Florida. It is impressive to see everyone working together. I am confident that we will continue to work together in the aftermath of the storm as well.

Today's hearing is another important step in the process of considering reforms to the IRS. I have stated previously I do not view this effort as an opportunity to degrade or discredit the good work being done by IRS employees.

However, I am a big believer in continuous improvement. That has been my philosophy in business. We can always be better. In

government, like business, we should always be looking for ways to improve.

In a system of voluntary tax compliance, even with the simplest of tax codes—and ours is currently not one of those—there are bound to be disputes between taxpayers and the IRS. What we hope to learn today is about the experience of those taxpayers.

These are folks that have been in the trenches working with a lot of those taxpayers involved in resolving disputes with the IRS. And whether there are ways to improve the current process, I believe there will be.

Nearly 20 years ago, the last time significant reforms were made to the IRS, one of the key legislative priorities for Congress was the creation of an independent appeals function. As recently as two years ago, Congress reaffirmed the importance of an independent forum when the right to appeal to such a forum was included in the Taxpayer Bill of Rights and codified as a responsibility of the Commissioner. Ensuring the independence and the availability of administrative review process for taxpayer disputes remains a top priority of this Subcommittee.

In addition to being independent, dispute resolution options need to be accessible and efficient. The process is failing if only large businesses with deep pockets feel equipped to dispute a determination made by the IRS. Individuals and small businesses should not have to weigh the cost of hiring outside help against paying the assessment.

For most taxpayers, their only interaction with the IRS is when they file their taxes once a year. But when the taxpayers find themselves in a dispute with the agency, they deserve a fair and prompt process.

I look forward to working with the Ranking Member on these issues and to hearing from our witnesses as we continue our efforts to examine reforms to the IRS.

I now yield to the distinguished Ranking Member from Georgia, Mr. Lewis, for the purposes of an opening statement.

Mr. LEWIS. Well, thank you, Mr. Chairman, for holding this hearing on resolving taxpayers' disputes with the Internal Revenue Service.

I welcome you back to Washington, Mr. Chairman. And on behalf of the citizens of Georgia, and especially the citizens of the Fifth District, we were able to welcome hundreds and thousands of people from Florida.

I went into a parking lot in downtown Atlanta on Saturday, and there were so many cars from Florida. And people had their dogs, walking their dogs through the parks, from Florida. We are neighbors.

And I want to, in particular, welcome Ms. Wilson and Mr. Shinn. I have relatives that live in Fort Lauderdale, and the only thing we had happen in my district was some, for the most part, pine trees coming down. I want to thank you for being here today.

Before we begin, Mr. Chairman, I would like to take a moment to extend my condolences to you and the millions of Americans who were impacted by the recent hurricanes in the Caribbean and the Southern States.

As you know, the hurricane damaged homes, downed trees, closed roads, and left about 1 million residents without power in my home State of Georgia. Now our citizens, our people, begin the difficult process of rebuilding their homes, their communities, and their lives. And I hope this committee will work together to do all we can to assist the recovery efforts.

Mr. Chairman, I have said it before and I will say it again: We must approach this effort to reform and improve the IRS with a great deal of care and thoughtfulness. I hope we will take our time to develop bipartisan solutions that serve the best interests of both taxpayers and the agency.

For many years, I have cautioned that we cannot get blood from a turnip. As you know, Congress cut the IRS budget by almost $1 billion since 2010. Over the last 3 years, the budget for the IRS Appeals Office dropped 11 percent, and there are about 24 percent fewer hearing officers.

Today, we will learn more about how these deep budget cuts have affected the ability of the agency to resolve disputes with taxpayers. Our citizens expect and deserve timely and efficient services. Simply said, Mr. Chairman, taxpayers will not get the level of service that they expect and deserve until we provide adequate funding to this agency.

As you know, this is the Subcommittee's fourth hearing to explore how we can improve the IRS. We have remained bipartisan and explored a good governance path to examine how the IRS operates and to identify possible improvement.

I hope and pray that our work product will be a model for our colleagues. This afternoon, we will also explore how to improve what can be a long and complicated appeals process. Together, we will listen and learn about possible remedies.

Some may suggest expanding the number of States that have permanent hearing officers, ensuring the independence of taxpayer conferences, and allowing taxpayers to request face-to-face conferences throughout the appeals process. Above all, Mr. Chairman, I hope we will continue to work together, as we have all year, to explore and address these issues.

In closing, Mr. Chairman, I look forward to hearing from our witnesses and learning more about their experiences with the agency. Again, Mr. Chairman, I want to thank you, my friend, for holding this hearing.

Chairman BUCHANAN. Thank you, Mr. Lewis. And I want to thank you for your thoughts and prayers. We do have a lot of our family and people who went to Georgia and other states, and I appreciate your thoughts on that.

And you know you have my commitment to work together on a bipartisan basis. We want to improve this together. There is a lot of work to be done. So I look forward to working with you.

Without objection, other Members' opening statements will be made part of the record.

Today's witness panel includes four experts: Kathy Petronchak, director of the IRS Practice & Procedures at the alliantgroup; Pete Sepp, president of the National Taxpayers Union; Byron Shinn, in our district—we are excited to have him and his lovely wife here today—he is the founder and managing partner of Shinn & Co.,

and I think he probably has 35 years of experience dealing with dispute resolution with the IRS; Chastity Wilson, principal of the National Tax Office of CliftonLarsonAllen, from Orlando, and a member of the AICPA.

The Subcommittee will receive your written statements, and they will be made part of the formal record. Each of you has 5 minutes to deliver your oral remarks. We will begin with Ms. Petronchak.

You may begin when you are ready.

STATEMENT OF KATHY PETRONCHAK, DIRECTOR OF IRS PRACTICE & PROCEDURES, ALLIANTGROUP, LP

Ms. PETRONCHAK. Chairman Buchanan, Ranking Member Lewis, and Members of the Subcommittee, thank you for inviting me to testify. It is an honor to provide comments today.

I interact with small and medium-sized businesses in my work with alliantgroup. I also spent 29 years at the IRS and feel this gives me a unique perspective into the Examination and appeals process. My testimony focuses on challenges that taxpayers face when dealing with the IRS and what IRS can do to improve the examination and appeals process.

I raise six issues in my written testimony, and I would like to highlight two of those issues. The first issue is the appeals process. Before heading to court, the final administrative step a taxpayer can take to contest an adverse determination by a revenue agent is through appeals.

Appeals is important for so many businesses seeking a fair review of their tax issues without having to incur additional costs to go to court. Taxpayers are appreciative of the opportunity to attend the Appeals conference in person.

They are not thrilled about the recent change by Appeals, indicating that they may not be granted an in-person meeting. Appeals has made telephone and virtual conferences first options for an appeal, only granting in-person conferences in limited circumstances.

We believe that not granting taxpayers an opportunity to have an in-person meeting would be highly prejudicial to taxpayers, restrict the ability of Appeals officers to adequately judge the credibility of witnesses, and make the conference more difficult in situations where the appeal is of highly technical and highly evidentiary-focused cases.

While we have seen Appeals officers flexible in granting in-person conferences, we believe that taxpayers should have a fundamental right to meet Appeals face to face. This in-person conference may be the only way a taxpayer believes there is an impartial resolution with a full understanding of the facts involved.

Another issue emerging in Appeals is the increased involvement of IRS Compliance employees in Appeals meetings. This change has created a perception for taxpayers that they may not get an independent hearing and decision as afforded by the Taxpayer Bill of Rights.

We believe the only involvement Exams should have at Appeals is in a preconference meeting. At a preconference, the originating function can attend an Appeals conference to present their views on the issues, the taxpayer's protest and assessment of litigating hazards in accordance with ex parte communication rules.

In a preconference setting, Exam would leave after their presentation. But as of late, rather than leaving at this point, Exam has been invited by Appeals to stay for the taxpayer's presentation. When this happens, the entire appeals atmosphere is altered, and there are opportunities for this to turn into an extension of the examination process for a taxpayer.

The independence of Appeals is hindered when Exam plays too great of a role in the appeals process. A representative recently described a situation where, in a preconference, it became clear that Exam had not fully addressed the position the taxpayer had brought forward in its response to the Exam team. After hearing the taxpayer orally present their position at the Appeals meeting, the Exam team made another 24-page submission to Appeals to attempt further support for their position on the issue, taking an alternative approach. It seems patently unfair that Exam can attempt to continue their process when the case is assigned to an independent forum to make a decision.

We disagree with Appeals having unilateral decisionmaking over Exam participation in a conference. Taxpayers who feel as if they have already been through a grueling process with Exam should be able to have the peace of mind that their case is being given a fresh look by Appeals and that the examination is over.

Today's comments on the issue of alternative dispute resolution focus on the IRS Fast Track Settlement program. This program was created to provide an expedited dispute resolution option for taxpayers to mediate their disputes during an examination with an Appeals official acting as a mediator. The use of Fast Track has the potential to be a highly effective tool when both parties come to the table willing to reach an agreement. Taxpayers and their representatives welcome the opportunity to resolve as many issues as possible at the lowest level in a cooperative manner. This same sense of urgency should be felt by the IRS.

In closing, I commend the committee for its work and oversight in ensuring that taxpayers receive fair treatment and good service from the IRS. Alliantgroup looks forward to working with the committee to further improve tax administration, and I would be glad to take your questions.

[The prepared statement of Ms. Petronchak follows:]

Statement of Kathy Petronchak

Director – IRS Practice and Procedure

alliantgroup, LP

Before United States House of Representatives

Committee on Ways and Means

Subcommittee on Oversight

Hearing on

"IRS Reform: Resolving Taxpayer Disputes"

September 13, 2017

Chairman Buchanan, Ranking Member Lewis, and Members of the Subcommittee:

Thank you for inviting me to testify today regarding the operations of the Internal Revenue Service. It is an honor to provide comments today for your hearing on IRS Reform: Resolving Taxpayer Disputes.

My name is Kathy Petronchak, and I am Director of IRS Practice and Procedure at alliantgroup, LP. I am a Certified Public Accountant and have been with the firm for almost four years. My experience prior to this, includes five years of work in a big 4 accounting firm in the tax controversy area and, I worked at the IRS for almost 29 years. My last position with the IRS was that of Commissioner, Small Business/Self Employed Division but during my public service career I also served in the Large & Mid-Size Business Division (now Large Business & International Division). I believe this experience gives me a unique perspective into how the examination process is currently being conducted for both small and mid-size businesses and allows me to be well positioned to speak to the issues you wish to discuss today.

The firm of which I am a part, alliantgroup, is a leading tax service consultant for small and medium sized businesses across the country. alliantgroup has over 700 professionals located nationwide, focused on assisting small and medium sized businesses to avail themselves of proper and available tax incentives, including tax credits, designed to create U.S. jobs, promote research and innovation, and otherwise help the United States remain the leader in the global economy. We also assist these businesses in tax controversy, and we represent them before the IRS and state tax regulators. In providing these services, we partner with the CPA firms of these businesses. We work with over three thousand CPA firms and thousands of businesses from all over the country in a remarkably diverse set of industries. Our work and daily interactions reveal that our CPA partners and clients share a common experience relating to their dealings with the IRS.

I speak today from the context of someone who was working at the IRS during the 1998 reforms and then in private practice with regards to ideas for rebuilding the IRS as stated in The Blueprint.[1] From

[1] A Better Way: Our Vision for a Confident America (June 24, 2016), *available at* https://abetterway.speaker.gov/_assets/pdf/ABetterWay-Tax-PolicyPaper.pdf.

my perspective the organizational changes that were implemented as part of the IRS Restructuring and Reform Act of 1998 were sound and are not in need of significant reorganization at this time. The premise then that operating units focused on particular taxpayer segments would provide better customer service and be competent in handling matters relevant to those taxpayers still rings true today. However, I believe there are issues that can and should be addressed to make the IRS more efficient and interactions with taxpayers much better without the disruptive effect of major changes to business units or the appeals function. I hope to address a couple of those issues in my testimony today. I also believe that some of the problems that exist today at the IRS stem or are exacerbated by the lack of adequate funding in recent years.

My testimony today focuses on the challenges taxpayers face when dealing with the IRS, and more specifically what the IRS can do to make the examination and Appeals process more fair, efficient, and transparent. The practices and procedures utilized by the IRS during examination and Appeals of small and mid-sized businesses would benefit from reform. We view the solutions to these issues as a benefit to taxpayers and the IRS. There are steps that can be taken by the IRS that will improve the examination and Appeals process for taxpayers while showing respect for taxpayer rights and improving the customer service provided.

We believe there is some inconsistent treatment of small versus large businesses by the IRS, as well as differing procedures being used in audits of these businesses. It is vitally important to remember that America's small businesses do indeed have needs, interests, and resources that may differ significantly from those of larger businesses. However, some of the procedures utilized in large business audits provide added transparency that would bring greater fairness to the small business examination. If these procedures were adopted for all taxpayers, the IRS can improve transparency in its examination of small businesses and better ensure they are treated fairly.

We strongly agree with The Blueprint basics that IRS employees should be held accountable to the Taxpayer Bill of Rights (TBOR). To that end we hope to address several specific provisions of the Taxpayer Bill of Rights including the right of all taxpayers to:

- Quality Service;
- Be Informed;
- Challenge the Positon of the IRS and Be Heard;
- Appeal a Decision of the IRS in an Independent Forum;
- Privacy;
- Confidentiality; and
- A Fair and Just Tax System.

As indicated, a number of issues that we will discuss today may be impacted by the funding problem that has plagued the IRS for a number of years now. We urge you to support adequate funding for the IRS including allowing the IRS to upgrade its IT systems, train its employees to ensure competence in handling tax issues, provide timely guidance to taxpayers, and ensure better service for American taxpayers as well as a fair administration of the Tax Code.

Today we would like to focus on the following issues: 1) decreased use of alternative dispute resolution processes; 2) emerging issues in an independent Appeals process; 3) lack of transparency; 4) third party contacts; 5) IRS education and outreach efforts; and 6) Taxpayer Bill of Rights.

1. The IRS is Decreasing its Use of Alternative Dispute Resolution

The IRS has a number of alternative dispute resolution tools at its disposal. Several of these such as Arbitration, Post Appeals Mediation and Early Referral seem more appropriate for large business taxpayers who have the experts and other resources to pursue these options.

Our focus for today is on the IRS Fast Track Settlement (FTS) program that was officially established in 2003.[2] It was created as an expedited dispute resolution option available for taxpayers who want to mediate their disputes during an examination with an Appeals Official acting as a neutral party or mediator. The purpose is to bring the examination team together with the taxpayer, so the two parties can discuss their positions and come to an agreement to settle an issue or the entire case at the earliest possible stage in an examination, without having to go through the formal administrative Appeals process or to court. Although the original adoption of the program in 2003 covered only large and mid-size businesses, it was expanded with Announcement 2011-5 to enable small businesses under examination to more quickly settle their differences with the IRS. With Revenue Procedure 2017-25, the FTS program was formally established for Small Business/Self Employed (SB/SE) Division taxpayers and made permanent. [3] For years FTS has been accepted as a powerful tool for taxpayers, allowing them to iron out their differences with the exam team on one or more contentious issues and reach a mutual agreement to close the case, allowing both parties to move on with their lives particularly since the goal is to resolve SB/SE cases within 60 days.[4]

However, in recent years, our experience has been that small and mid-sized businesses are less likely to be accepted into the FTS process. FTS must be agreed to by both the taxpayer and the revenue agent and in recent experience, revenue agents and managers seem more reluctant to utilize this dispute resolution tool.[5] This statement is based on two observations. First, statistics that were shared by IRS Appeals in a March 2016 presentation at a Federal Bar Association Tax Law Conference stated the number of fast track settlement cases for small businesses decreased from 230 in fiscal year 2014 to 177 in fiscal year 2015. Second, in our own anecdotal experience at alliantgroup, we have seen the number of fast track settlement cases drop from a peak of several per month to the current rate of roughly two per *year*. Causes for this could be reduced resource levels in examination and appeals that may be driving the reluctance to use the process or that the requirements from the IRS regarding those eligible to participate in FTS have become too stringent. We tend to think it is the latter cause that has led to this decrease.[6]

The use of FTS has the potential to be a highly effective tool in alternative dispute resolution when both parties come to the table willing to reach an agreement. Taxpayers and their representatives welcome the opportunity to resolve as many issues as possible at the lowest possible level in a cooperative

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[2] Rev. Proc. 2003-40, LMSB/Appeals Fast Track Settlement Procedure.
[3] Rev. Proc. 2017-25, Formal Establishment of Small Business/Self Employed Fast Track Settlement Program.
[4] Collections cases are handled in a process called Fast Track Mediation. Rev. Proc. 2003-41 SB/SE – Appeals Fast Track Mediation Procedure.
[5] *See* the discussion at the Federal Bar Association Tax Law Conference, Practice and Procedure Symposium, Recent Developments at Appeals Panel (March 4, 2016).
[6] IRS internal procedures regarding SB/SE FTS can be found in IRM 4.10.7.5.5 (March 3, 2015).

manner. This same sense of urgency should be felt by the IRS. Small and mid-sized businesses need to focus on their business at hand and having a disagreement with the tax authorities weighing on them for a long period of time distracts from their business needs and operation. Obtaining resolution earlier increases compliance of those taxpayers and allows the IRS to focus resources on other taxpayers and issues.

The fast track settlement process is authorized for all taxpayers and we strongly encourage its increased use by the Service. While we do not support a mandate to require the use of fast track on issues not otherwise excluded by the Revenue Procedures we do believe that IRS leadership can be more supportive and proactive in ensuring that this tool is used for efficient tax administration.

Experience has taught us that when unwilling players come to the table for a mediation type event there is a high likelihood there will not be a successful outcome. In considering changes to make the FTS program more effective we believe the establishment of any type mandate would need careful consideration based on the concern just noted. We do believe there is an opportunity for improvement to the process by authorizing the use of an outside mediator alongside the Appeals mediator. Just as the use of an outside mediator is an option for taxpayers in Post Appeals Mediation we support the idea of allowing taxpayers to make this election for the fast track process with the hope that it may lead to more agreements in this process. These changes would support the taxpayer's Right to Challenge the Positon of the IRS and Be Heard and the Right to a Fair and Just Tax System.

2. Emerging Turbulence in the Appeals Process

Before heading to court, the final administrative step a taxpayer can take to contest an adverse determination by a revenue agent is through IRS Appeals. The IRS Office of Appeals is "separate from and independent of the IRS office that proposed the adjustment. Issues should be fully developed by compliance functions before an administrative appeal."[7] Taxpayers can present their arguments and negotiate an administrative settlement with an IRS Appeals Officer. We appreciate the vital and important work of Appeals and want to state how important IRS Appeals is for so many businesses seeking a fair review of their tax issues without having to incur additional costs and go to court.

While the role of IRS Appeals is greatly appreciated by those seeking an administrative resolution there are improvements that taxpayers would like to see. First, the length of time it takes Appeals to resolve a case has steadily increased over the past few years. Again, due to budget cuts, Appeals Officers have incredibly large caseloads, may not be located in the geographic area of the taxpayer, and may be unable to hear cases for months or even up to a year. Even after a case is heard, it may take months thereafter for a settlement offer to be made. This means that the taxpayer's tax returns and status with the IRS is in a sort of purgatory, as it has to wait on the Appeals Officer to hear and then decide its case. While our small and mid-sized business owners are most appreciative of the opportunity to attend the conference and have a frank discussion with Appeals they are not as thrilled about the time it takes to reach a final resolution nor the recent change made to the Internal Revenue Manual (IRM) indicating that they may not be granted an in-person meeting.

One solution the IRS appears to have implemented to address the problem of too few appeals officers is to make telephone and virtual conferences first options for an appeal, only granting in-person

[7] IRM 1.2.17.2 (Nov. 4, 1998): Policy Statement 8-1.

conferences in limited circumstances. We whole-heartedly believe that not granting business owners an opportunity to have an in-person meeting would be highly prejudicial to taxpayers, restrict the ability of Appeals Officers to adequately judge the credibility of witnesses, and make the conference more difficult in situations where the appeal is of highly technical and highly evidentiary focused cases. The National Taxpayer Advocate Nina Olson, made this same argument to the Senate Committee on Appropriations in her July 26, 2017 testimony, in which she stated "it would be impossible for an Appeals Officer to judge the credibility of a witness without an in-person conference, and 'circuit riding' does not happen often, requiring taxpayers to wait months, or even a year or more, to obtain a face-to-face hearing."[8]

While in our practice we have seen Appeals Officers flexible in granting in-person conferences, we believe that requesting in-person conferences and the back and forth with the Appeals Officer immediately on a purely procedural matter starts the process off on the wrong foot and potentially undermines the taxpayer's relationship with the Appeals Officer. We believe that taxpayers, if willing to incur the time and cost, should have a fundamental right to meet Appeals face to face. Conducting in-person conferences should not have a material effect on the time it takes Appeals to hear a case – our experience in a case where an in-person conference was denied was that the conference still took hours to complete. Moving to virtual conferences as a default is not the answer to ensuring that a taxpayer's Right to Challenge the Position of the IRS and Be Heard is not violated.[9] Policy Statement 8-1[10] states that IRS is committed to the Appeals administrative dispute resolution process and follows certain principles including that Taxpayers are generally entitled to appeal disputes and to have a timely conference and resolution of their dispute. From a taxpayer perspective this in person conference may be the only way to believe there is an impartial resolution with a full understanding of the facts involved.

A second issue emerging in Appeals is the increased involvement of IRS Compliance (also referred to as Exam) and/or Counsel Employees at appeals meetings. The recent focus by Appeals to make it known that they have the discretion to invite Counsel and Compliance to the conference has created a perception for some taxpayers that they are not getting an independent hearing and decision.

As stated above, Appeals is an independent function of the IRS and should remain autonomous and separate from Exam. This concept is clear in IRM 8.10.1.3 where it states "Appeals is charged with providing an independent dispute resolution function with IRS. Appeals employees must make fully informed, independent judgments regarding:

-Strengths and weaknesses of respective positions of both the taxpayer and the government

-Application of law, regulations, and IRS policies and procedures based on the facts and circumstances of the case

-Evaluation of hazards of litigation."

During an examination, the Exam team has an opportunity to build its case fully, make a determination on the facts and applicable law, and to seek agreement from a taxpayer. It is well

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[8] Written Statement of Nina E. Olson National Taxpayer Advocate, Hearing on Internal Revenue Service FY 2018 Budget Request Before the Subcommittee on Financial Services and General Government, July 26, 2017, *available at* https://www.irs.gov/pub/foia/ig/tas/nta_written_testimony_hearing_irs_fy2018_budgetreq_7_26_2017.pdf.
[9] *See* IRM 8.6.1.4.1 (Oct. 01, 2016).
[10] IRM 1.2.17.2 (Nov. 4, 1998): Policy Statement 8-1.

understood that issues should be fully developed by compliance functions before an administrative appeal is offered to the taxpayer when a case is not agreed. Appeals has procedures for returning a case to Exam if it is considered a premature referral, not sufficiently developed for their consideration by Exam, or the taxpayer provides new information that was not considered by the Exam team. In any event it seems clear that Appeals expects that all fact finding and submission of relevant information took place before they are asked to consider the case.

Since it is solely Appeals decision as to whether Exam and Counsel are invited to a conference we believe the only involvement Exam should have at Appeals, is in a preconference meeting. In this situation the originating function, Exam for instance, can attend an Appeals Conference to present their views on the issues, the taxpayer's protest and assessment of litigating hazards in accordance with ex parte communication rules. While in the preconference setting Exam may have left after their presentation,[11] as of late, rather than leaving the conference after it presents its case, Exam has been invited to stay at the Appeals Officer's discretion for the taxpayer's presentation.[12] While we agree that a presentation to the Appeals Officer of key points from each party provides an opportunity for them to ask relevant questions in making an informed decision, this occurs with a preconference meeting. When exam stays, the entire Appeals atmosphere is altered and there are opportunities for this to turn into an extension of the examination process for a taxpayer.

Specifically, it is troubling when Exam has a second chance to build its case by directly engaging with the taxpayer by asking both factual and legal questions that may have been overlooked in the exam process. We believe that the mission of Appeals, specifically its independent function, is hindered when Exam plays too great of a role in the Appeals process and the Appeals Officer does not stop the exchange. There is also a concern that Exam may take this as an opportunity to add more information to the file when they realize potential weaknesses in their position. A representative recently described a situation where in a recent preconference it became clear that Exam had not addressed a position that the taxpayer had presented in its document request responses and in its protest. After hearing the taxpayer orally present their position at the Appeals meeting and seeming to get agreement from the Appeals Officer, the Exam team followed up with another submission to Appeals to attempt further support for their position on the issue taking another approach. It seems patently unfair to this taxpayer that the Exam team attempts to continue their process when the case is assigned to an independent forum to make a decision on what was obviously a contentious exam.

As a matter of process, if the taxpayer is not given a say in any decision regarding IRS employees' participation in appeals conferences, then a solution to this dilemma may be clear guidance in the Internal Revenue Manual on acceptable procedures/protocol for Exam during an Appeals conference. We do not agree with the Appeals policy of having unilateral decision making over Exam's participation in an Appeals conference as it changes the nature of the appeals process. If Appeals continues to take this approach, procedures and actions are necessary to ensure that the conversation is limited to original positions taken by Exam and not asking further questions of a taxpayer to develop new facts and positions in what should be an independent process.

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[11] *See* Rev. Proc 2012-18: Ex Parte Communications between Appeals and Other Internal Revenue Service Employees

[12] IRM 8.6.1.4.4 (Oct. 01, 2016).

The goal for these new procedures should be to limit the role of Exam during Appeals. Taxpayers who feel as if they have already been through a grueling process with Exam, should be able to have the peace of mind that their case is being given a fresh look by Appeals, and that Appeals is not more of the same.

In conclusion on this issue, we do not believe it is necessary to create a new dispute resolution function for taxpayers. By staying true to the original vison that Appeals offices are separate from and independent of the IRS office that proposed the adjustment, resolution should continue to be reached in a majority of cases. Changes may be needed to strengthen the independence of Appeals and to improve its accessibility for all taxpayers but a new small claims court function as outlined in The Blueprint is not needed in our opinion. These changes would further the taxpayer's Right to Challenge the Positon of the IRS and Be Heard and the Right to Appeal a Decision of the IRS in an Independent Forum.

3. Lack of Transparency during the Exam Process

An important aspect of an IRS examination is the information document request process. The IRS issues to taxpayers information document requests, or "IDRs," requesting books and records and email communications, as well as requesting supporting documentation and explanations of various items on their tax returns. The documents taxpayers provide in response to the IDRs give the revenue agent the information needed to determine whether a taxpayer has taken a correct or reasonable position on its tax return. The process is often lengthy and can take a taxpayer hours upon hours to gather, organize, and explain documents. And while it is important for the IRS to conduct fact finding in an examination, it is also vital for the IRS to understand that a small business does not have the resources that the Fortune 1000 have to deal with voluminous document requests. Additionally, the taxpayer can find an audit by the IRS intimidating since they do not have frequent interactions with the IRS.

The IRS' Large Business & International Division (LB&I) has refined the examination process with a goal to make it more transparent and efficient – worthy goals for any examination of a taxpayer, whether large or small, from the perspective of both the IRS and the taxpayer. LB&I agents are now required to ensure that IDRs are issue focused, have been discussed with the taxpayer before being issued in final form, and contain a response date that has been discussed with the taxpayer. Publication 5125, issued in February 2016, has required agents examining the tax returns of large and mid-size companies to open up communications with companies and to work closely with them. While neither perfect in design nor implementation, this process is intended to lead to increased transparency in the examination process with issues being clearly identified by the IRS and taxpayers receiving timely feedback on the responses that have been provided. We believe the IDR process in LB&I has improved as a result of this focus.

Small business examinations do not have similar procedures in place. Rather, there are only loose guidelines on issuing IDRs. The Internal Revenue Manual provides guidance on the use of "lead sheets" and work paper organization but provides little focus on how to work transparently and collaboratively, where possible, with taxpayers. It is our experience that these procedures can lead to IDRs that cover a number of issues within one request and with what seems short response times for a voluminous amount of documents.

The two processes described here have created a difference in treatment of large and small businesses in IRS examinations. While LB&I appears to be pushing for clarity and efficiency during the audit process, small businesses are generally left to the decisions of the individual revenue agents. However, there are no real procedures in place in SB/SE to encourage more discussion concerning the

course of an examination. This has only worsened as budgets have declined. We also would mention that one of the byproducts of this issue that we are experiencing is that in some examinations, the first clear indication of the primary issue of an examination is when a 30 day letter is received by the taxpayer. At this point the taxpayer needs to agree with the IRS or decide to file a protest with Appeals to have an impartial hearing on the issue. This is remarkably too late in the process to be having this discussion.

In our view, having a straightforward upfront meeting between the taxpayer and the IRS that lays out what the issues are, what the roadmap is going forward for documents and interviews, as well as expected timelines, is to everyone's benefit. The taxpayer understands the concerns of the IRS and can be better responsive to IRS questions and requests for documents. Thus, we believe that SB/SE should adopt many of the LB&I transparency measures.

In an IRS audit, the revenue agent has traditionally been the point of contact for the taxpayer and is supposed to be the individual that manages the audit and makes the ultimate determination. There are instances when specialists are needed for an examination and the IRS has a formal process for agents to request assistance from specialists such as engineers, appraisers, and computer audit specialists. However, we have experienced instances where some SB/SE agents hand cases off to specialists when valuation or highly technical issues are being addressed. While this assistance is necessary, the process is often mysterious and the taxpayer is left in the dark regarding who is conducting and deciding their examination and what the timeline for a decision may be.

We have advised a number of small and mid-sized businesses where this happened to them. For example, a revenue agent who lacks expertise or experience may simply hand the case over to an IRS engineer or technical expert and have them make the ultimate decision that is written up in an examination file. In the best case scenario the specialist/expert is involved in the case and openly advising on document requests and participating in discussions with the taxpayer. However, this is another area in which budget cuts have had a pernicious impact on the process. The specialists may not have adequate time to do a quality job. For example, in some of our cases revenue agents have only "consultations" with specialists/experts on a case rather than an accepted referral where detailed examination of the records takes place. Having only hours and not weeks to work an issue related to a specific taxpayer may not lend itself to a specialist being fully informed of the facts in a particular case. Moreover, in some of these cases, the taxpayer is not aware that this has occurred or has not had an opportunity to discuss technical conclusions that have been made.

Another experience with SB/SE agents creates a greater concern in the exam process for small businesses and whether they are being treated fairly. Recently we have been advised by revenue agents that there is an approval process for their final reports on certain technical issues by a "technical specialist." Agents may not specify who is reviewing their lead sheets and work papers prior to discussion and issuance to the taxpayer of a report. They have indicated that the specialists are looking at the cases and that their hands are tied in determining the proposed adjustment for those taxpayers. This is particularly troublesome if the specialist is making the ultimate decision when they are not intimately familiar with the facts of the taxpayer. To the extent this is happening, it is the antithesis of the transparency that should occur in an examination. We are even told by agents that they may agree with a taxpayer's position but have no authority over their own examination outcomes.

We see these actions as a violation of the taxpayer's Right to be Informed and the Right to a Fair and Just Tax System. When decision makers are involved in a taxpayer's case it should be transparent to a taxpayer who those persons are and the rationale for any decisions that are made.

4. Third Party Contact Procedures Are Prejudicial to Taxpayers

The IRS often reaches out to third parties that are not under audit, but may have information and documents relevant to a taxpayer that is under audit. Such contacts are permissible in certain circumstances, but the IRS must give the taxpayer under audit "reasonable notice in advance" of such a contact.[13] While these contacts are often times justified as necessary to corroborate a taxpayer's records/testimony or to obtain otherwise unavailable data, we are seeing increased use of the contacts in a fashion that warrants concern.

We would like to echo the findings made by the National Taxpayer Advocate, Ms. Olson, in her 2015 Annual Report to Congress.[14] First, the IRS is not always effective in providing notice to taxpayers, often times only providing them Publication 1, *Your Rights as a Taxpayer* or some similar general notice at the beginning of the exam and not at or anywhere near the date of a third party contact.[15] Such notice is useless and does not effectively apprise taxpayers that such contact will be made, to whom it will be made, or that the taxpayer can request a third party contact report from the IRS. Second, the Taxpayer Advocate found that the IRS did not first ask taxpayers for the information requested from third parties in 22.8 percent of examination cases.[16] This is unacceptable given the extraordinarily important taxpayer privacy protections that go out the window with third party contacts.

Ms. Olson also discussed other valid concerns: the disclosure of confidential taxpayer information protected under IRC § 6103;[17] that taxpayers are often not given the prior opportunity to volunteer information on their own; that third party contact requests can be vague;[18] and that the IRS does not automatically provide periodic third party contact reports.[19]

In our experience, it appears the IRS has seemingly been using these contacts on an increasing basis in general examinations, often times when the IRS already has the information they request from third parties, and other times when they haven't even requested the information from the taxpayer. Requesting the information from third parties in these situations is intrusive, burdensome and needless. It creates an unnecessary burden for small and mid-sized businesses, and the practice of issuing third party contacts should be modified to ensure notice and an opportunity to respond closer to the time a third party contact is to actually be initiated.

We encourage the Committee to consider what modifications can be made to the statute to ensure the IRS does not perfunctorily notify a taxpayer of these procedures at the beginning of the exam and only periodically provide a taxpayer with a list of third party contacts upon specific taxpayer request.

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[13] 26 USC § 7602(c).
[14] National Taxpayer Advocate 2015 Annual Report to Congress, *available at* https://taxpayeradvocate.irs.gov/reports/2015-annual-report-to-congress.
[15] *Id.* at 123.
[16] *Id.*
[17] *Id.* at 124.
[18] *Id.* at 126.
[19] *Id.* at 125.

The current IRS policy regarding third party contacts can be found in Internal Revenue Manual Section 25.27.1. General requirements state that it is their practice to obtain information directly from a taxpayer whenever possible and that reasonable notice should first be provided to the taxpayer before a third party request. However, this appears to be an area where the intent of the law and even the IRM is not honored. It appears the IRS takes the position that Publication 1 serves as the only "advance" notice. These changes would further the taxpayer's Right to Privacy, Confidentiality, and a Fair and Just Tax System.

5. IRS Needs Better Outreach and Taxpayer Education

Even with improvements to the Exam and Appeals process, the IRS can assist taxpayers and tax practitioners with education on the front end, to reduce tax compliance costs. In Ms. Olson's July 26, 2017 testimony, she stated that "Pre-filing outreach and education is particularly important for small businesses, which often need to learn and comply with complex rules that individual taxpayers do not encounter, such as rules governing eligible business expenses, equipment depreciation, and employment taxes. Yet the IRS has whittled down these outreach units to the point where they are barely functional." She went on to state that the IRS has only 98 outreach employees for the 62 million Small Business and Self-Employed taxpayers.

Due to budget constraints, taxpayers have difficulty getting answers from the IRS on tax matters and are often unaware of filing requirements and the substantive rules of the Internal Revenue Code that affect them. Proactive outreach by the IRS could go a long way in educating taxpayers on issues that the IRS is focusing on as well as new initiatives that are taking place. Such education efforts can reduce the compliance costs to both taxpayers and the Exam function.

In April 2017, alliantgroup signed onto a document with eight other tax practitioner organizations, outlining changes that the IRS can make to improve services provided to taxpayers and practitioners.[20] In the Statement of Purpose it was stated that "as tax practitioners, we advise millions of taxpayers on tax matters, assist them with compliance responsibilities, and represent them before the IRS. We understand what is working and not working with tax administration from both taxpayer and practitioner perspectives."

Although several issues were outlined in the document as a framework for ensuring a modern functioning IRS, we will focus on one specific recommendation today. This document recommended creating an executive level IRS Practitioner Service Unit. "A dedicated practitioner services unit would allow the IRS to rationalize, enhance, and place under common management the many current disparate practitioner impacting programs, processes, and tools." This Unit would have a high level executive lead for a centralized group similar to how identify theft efforts have been centralized at the IRS. The Unit would seek to coordinate and improve access of information to prevent unnecessary delays and inefficiencies. Included in this unit would be an online tax professional account, in which a tax professional could access all of their client's information and receive information and communications from the IRS in this single space. Practitioner priority hotlines with higher-skilled employees would allow practitioners to understand and discuss more complex technical and procedural issues that small and mid-sized businesses face and result in a quicker resolution of issues. Lastly, designated customer service

[20] Ensuring a Modern Functioning IRS for the 21st Century, April 3, 2017, pg. 1, *available at* https://www.aicpa.org/Advocacy/Tax/DownloadableDocuments/IRS-Service-Improvement-Practitioner-Report.pdf.

representatives for each geographic area would be helpful for issues that can't be solved through the priority hotline.

For those of us who signed the document it was noted that "we are committed to a service-oriented, modernized tax administration system that earns the respect and appreciation of all taxpayers and stakeholders." We believe that these changes would go far in increasing the likelihood of taxpayer and practitioner access and education, which could lead to fewer and less contentious interactions with the IRS. These changes are in line with the taxpayer's Right to Quality Service.

6. Taxpayer Bill of Rights

Although there currently exists a list of rights afforded to taxpayers,[21] referred to here as the Taxpayer Bill of Rights (TBOR), we believe more attention is needed by the IRS in ensuring that its employees understand and follow them. While taxpayers can clearly find information on the IRS website regarding their rights and understanding them it is unclear what training has been held for employees of the IRS. We raise this issue as recently in a case where a practitioner raised a concern as to taxpayer right's being violated he was informed by a revenue agent that she was not aware of them and did not believe she had violated anything.

Policy Statement 1-236 states in paragraph three that the tax law will be enforced with integrity and fairness.[22] It states specifically that "to ensure fairness to each taxpayer, we do our jobs with a focus on taxpayer rights, including due process and appeal rights. The Internal Revenue Code grants taxpayers' certain rights when working with the IRS, and these rights are embodied in Publication 1."

We would like to echo the findings made Ms. Olson in her 2016 Annual Report to Congress regarding these rights.[23] The perception of taxpayers is that IRS has not adequately incorporated the TBOR into its operations and this has negatively impacted taxpayers at times. It is unclear what options the taxpayer may have when this takes place. Ms. Olson addressed this in her May 19, 2017 testimony to this Committee stating that the practical impact of the TBOR provision was not clear and if a taxpayer were to assert that a right had been violated that it is not clear whether a court would "find the rights are legally cognizable."[24] I encourage this committee to take further action to ensure that taxpayer rights are clearly established and to review closely the recommendations laid out by the National Taxpayer Advocate in her testimony.

Conclusion

Thank you for affording me the opportunity to be here today to provide the Committee with this information. I look forward to your questions, and we would be happy to work with you in the coming months as you work on a more detailed plan to address the needs of taxpayers and practitioners.

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[21] 26 USC § 7803(a)(3).
[22] IRM 1.2.10.37 (Oct. 24, 2016): Policy Statement 1-236.
[23] National Taxpayer Advocate 2015 Annual Report to Congress, *available at* https://taxpayeradvocate.irs.gov/reports/2016-annual-report-to-congress.
[24] Written Statement of Nina E. Olson National Taxpayer Advocate, Hearing on IRS Reform: Perspectives from the National Taxpayer Advocate, Before the Subcommittee on Oversight, Committee on Ways and Means, US House of Representatives (May 19, 2017), *available at* https://www.irs.gov/pub/tas/nta_written_testimony_irs_reform_nta_perspectives_5_19_2017.pdf.

Chairman BUCHANAN. Thank you.
Mr. Sepp, you are recognized.

STATEMENT OF PETE SEPP, PRESIDENT, NATIONAL TAXPAYERS UNION & NTU FOUNDATION

Mr. SEPP. Mr. Chairman, Mr. Ranking Member, Members of the Committee, a number of my predecessors have actually testified in this very room on taxpayer rights issues, so I am particularly honored that you would ask me here to follow in their footsteps.

And we need to follow in the footsteps of all of our predecessors in developing a bipartisan solution to many of the problems that have cropped up since enactment of the IRS Restructuring and Reform Act of 1998.

One of my predecessors, Bob Kamman, put it this way: He called it taxpayers triage. What you need are a number of steps, a number of options, in resolving problems between the agency and taxpayers that provide a range of responses.

One of them is prevention, of course. We can simplify the tax system. We can educate taxpayers about their rights in advance so they know going into the process of interacting with the IRS what to expect, and perhaps problems can be resolved at that level, the preconference level, for example.

Then there is basic care. What we have now is the appeals process and a very nascent alternative dispute resolution process. We are going to hear a lot from the witnesses today about some of the malfunctioning systems within Appeals, and especially with the recent evolution in the large business and international division of strategies, like designating cases for litigation, that can be very harmful to the audit process. I hope we can discuss that in further detail later.

But the rise of alternative dispute resolution mechanisms around the world and its relatively flat usage here in the United States—actually declining at the Appeals level right now—suggests that we need very serious reforms if we are going to make that process workable in the future.

The third level of triage really is intensive care. That is when taxpayers and the IRS have to litigate an issue. And there, taxpayers' access to the courts beyond the tax court level is still highly problematic. Everything from the Anti-Injunction Act to the Declaratory Relief Act essentially prevents taxpayers from enforcing their rights in court in a meaningful manner. Largely, their choices are confined to litigating for damages after the acts have already been committed by the agency that have deprived a taxpayer of his or her income or right to earn.

The fourth level is essentially post-op observation, as I would call it, oversight. Now, current plans in several of the tax reform options being discussed would do away with the IRS Oversight Board. There are flaws in the Oversight Board certainly, but I would urge this committee to very carefully consider alternatives to the current IRS Oversight Board, which is essentially paralyzed due to a lack of a quorum.

We really need to establish and maintain that kind of consistent oversight in some manner. Specifically, I would make a few recommendations, and, again, we can further discuss these in detail.

The foundation for another taxpayer rights package really ought to be based on H.R. 3220, the Preserving Taxpayers' Rights Act. It is a bipartisan bill. It codifies the right to appeal, and it establishes a more business-like working relationship between the IRS and taxpayers in audits.

This will apply to large businesses, small businesses, individuals across the board. Section 3 of that bill, which essentially directs the Secretary to begin developing more dispute resolution procedures at Appeals, would pave the way for more effective use of Alternative Dispute Resolution (ADR) in a number of situations.

There are many, many other suggestions I could make that we should look at. The Taxpayer Bill of Rights Enhancement Act just introduced in the Senate yesterday, S. 1793, which would expand some of the assistance in the Volunteer Income Tax Assistance program, expanding low-income taxpayer clinics. All of these things need to be put into a package to work together to enhance the progress we have made in Taxpayer Bill of Rights I, T II, and the IRS Restructuring and Reform Act. And this is the committee where it all starts.

Every single piece of important IRS reform legislation began with Members of this Committee, your predecessors, and you now, such as with the RESPECT Act that just passed, coming together in a bipartisan fashion to do better for taxpayers. We can do it. We must do it.

I thank you for your leadership.

[The prepared statement of Mr. Sepp follows:]



Statement of

Pete Sepp
President
National Taxpayers Union

Prepared for

The Subcommittee on Oversight
Committee on Ways and Means
United States House of Representatives

Regarding the Subcommittee's Hearing on

"IRS Reform: Resolving Taxpayer Disputes"

Submitted September 13, 2017

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Introduction

Chairman Buchanan, Ranking Member Lewis, and Members of the Subcommittee, it is a great honor for me to provide comments today for your hearing, "IRS Reform: Resolving Taxpayer Disputes."

My name is Pete Sepp and I am President of National Taxpayers Union (NTU), a non-partisan citizen group founded in 1969 to work for less burdensome taxes, more efficient, accountable government, and stronger rights for all taxpayers. More about our work as a non-profit grassroots organization, and the thousands of members we represent across the nation, is available at www.ntu.org.*

Although we advocate for many structural changes to the tax system, from the comprehensive to the incremental, one common aspect on which NTU often specifically focuses is the *administrability* of such proposals. As policymakers define the rates, bases, deductions, credits, and other features of a tax system, what will the practical impact be on taxpayers' lives and their rights? Unless this question is adequately addressed, the result will be a tax system that burdens all and serves none. Taxpayers will be more fearful or mistrustful of their government, revenue officials will encounter greater difficulty in performing their public service, tax practitioners will become increasingly frustrated with complex rules, and all sectors of the economy will pour too many productive resources into compliance.

For these reasons, throughout its history NTU has led efforts in support of Congressional legislation to improve operations of the Internal Revenue Service (IRS) and provide greater balance in the tax enforcement process. During the late 1970s and 1980s, NTU informed Congress of taxpayers who experienced IRS maladministration firsthand, as well as organized a large coalition of civil liberties organizations that successfully persuaded Congress to enact the first "Taxpayers' Bill of Rights" as part of the Technical and Miscellaneous Revenue Act of 1988.

In 1997, NTU's then-Executive Vice President David Keating was named to the National Commission on Restructuring the Internal Revenue Service ("Restructuring Commission"), a federal panel whose recommendations later became the basis for the most extensive IRS overhaul in a generation. More recently we worked with the IRS National Taxpayer Advocate (NTA) and Congress in promulgating and finally codifying (in 2015) a set of 10 fundamental taxpayer rights.

This hearing is being held amid discussions of systemic tax reform – an exercise that NTU wholeheartedly supports. I wish to note at the outset, however, that even if Congress were not contemplating major revisions to the rates, base, and other operational aspects of the Tax Code, most of the proposals and policies discussed here can and should be able to stand on their own.

The following testimony is intended only to provide highlights surrounding taxpayer dispute resolution issues. They should be viewed through the broader prism of taxpayer rights and tax administration policy.

Over the past three years, I have been asked to testify before Subcommittees of the House Small Business Committee, and have submitted comments to the Senate Finance Committee, the Treasury, and the White House Transition Team on various aspects of tax administration. Some of these commentaries and analyses have been updated or modified for inclusion in various portions of this document.

**As a matter of organizational policy National Taxpayers Union neither seeks nor accepts any kind of grant, contract, or other funding from any level of government.*

I. Resolving Disputes: The Remedies behind Rights

Since NTU's founding, a fundamental element in the quest for an administratively equitable tax system has been remedies for when that equitable treatment falls short. It is therefore no surprise that most taxpayer rights laws have striven for either new procedures to resolve tax disputes or safeguards to help existing mechanisms work better. Among these:

- The Taxpayers' Bill of Rights in the 1988 Technical and Miscellaneous Revenue Act directed the IRS to create an administrative appeal procedure for liens, empowered what was then called the Taxpayer Ombudsman to issue Assistance Orders, allowed taxpayers to recover damages for certain unauthorized IRS actions, and strengthened taxpayer protections during the conduct of field audits.
- "Taxpayers' Bill of Rights II" in 1996 replaced the Ombudsman's office with a much more effective Taxpayer Advocate capable of assisting taxpayers more fully, established administrative review when installment agreements were terminated, expanded the availability of offers-in-compromise, and placed the burden on the IRS of proving its position was substantially justified if a taxpayer who wins a dispute sought a cost and fee award.
- The IRS Restructuring and Reform Act of 1998 ("RRA 98") further augmented the powers of the Taxpayer Advocate, altered burden of proof standards for factual issues in certain tax cases, sought to solidify taxpayer appeal rights, and set into motion other dispute resolution remedies described in sections to follow.
- The Protecting Americans Against Tax Hikes (PATH) Act of 2015 set into law 10 principles guiding administration of the tax system; three of the most relevant of these for purposes of resolving disputes are the "Right to Challenge the IRS's Position and Be Heard," the "Right to Appeal an IRS Decision in an Independent Forum" and the "Right to a Fair and Just Tax System."

Last year, House Ways and Means Committee Chairman Brady released a blueprint for tax reform entitled "A Better Way." This plan envisions a new tax administration authority whose functions will be divided along the lines of a families and individuals unit, a business unit (for firms of all types), and a "small claims court" independent of these units. A new commitment to individualized taxpayer assistance and a "Service First" mission that adheres to the PATH Act's taxpayer rights principles would be instituted. The post of Commissioner would be replaced by an Administrator who could serve no more than two three-year terms.

NTU believes that many elements of this approach have a great deal of promise to improve tax dispute resolution procedures. Yet, we also believe the job of protecting taxpayer rights will never be finished. As the Tax Code, the economy, and technology are all constantly evolving in new directions, so must the laws designed to prevent abuse of authority and provide appropriate remedies when such abuse occurs.

The following sections will explore the current challenges in doing so, both within the context of "A Better Way" and in other scenarios.

II. Why is Reform Still Needed? A Case Study in Small Businesses

Prior to reforms enacted in the 1988-98 period, taxpayers had only a few options in disputing an IRS assessment that did not involve considerable expense and time. Given the progress made since then, is it even necessary to consider additional steps? The circumstances that continue to surround small business taxpayers provide some clues.

In NTU's experience, IRS treatment of the small business community has historically served as a barometer for systemic reforms of the tax laws as well as tax administration. Thus, many of the first Americans to approach NTU's advocacy staff and share "horror stories" of treatment by the Internal Revenue Service were small business owners.

This is generally because they face the least ideal situations. Their tax returns tend to be more extensive and complex than that of a non-business household, yet they often lack the resources of larger businesses to maintain full-time tax compliance employees. A September 2014 report for the National Association of Manufacturers calculated that the regulatory cost *per worker* for all tax compliance activities in firms of any size was a whopping $960 (using 2012 data and expressing in 2014 dollars). For companies with fewer than 50 employees, the tab was much worse – over 50 percent more, at $1,518 per worker.

They are also likelier than other non-business households to come in contact with examinations, appeals, and other parts of the dispute resolution system. For example, the *IRS Data Book* indicates that the examination rate for all "large corporation" tax returns was 11.1 percent in Fiscal Year 2015, compared to 0.9 percent for "small corporations." On the other hand, businesses declaring income through the 1040 tax return instead of a corporate form do have much higher audit rates than the general filing population. Depending on the income level of the business, the rate can be three times higher than that of all individual tax returns, or even eight times higher than nonbusiness returns without Schedules C, E, F, or Form 2106.

The fact remains that some of the most contentious issues surrounding tax disputes center upon, or are a consequence of, audits. These matters range from the clarity and certainty of the laws themselves, to appeals of audit results, to IRS employee conduct, and to remedies in the courts.

Ranking Member Nydia Velázquez of the House Committee on Small Business eloquently summed up the problem in an opening statement from 2013, when she observed that, "In the past, small businesses have told us that complexity and uncertainty create difficulty when filing tax returns. Many business owners worry that one simple mistake can lead to a costly and timely audit. And, at a time when many businesses are striving to expand, every hour and dollar counts."

For businesses of all sizes, those dollars and hours add up quickly. An annual study published by our research affiliate, National Taxpayers Union Foundation (NTUF), calculated that for this year the federal personal and corporate tax system extracted 6.98 billion hours and $262.6 billion out of the economy (a trend that has been worsening). Other analyses suggest that two-thirds or more of these sums would be attributable to the business sector, including corporations, partnerships, and sole proprietorships. Unfortunately, these considerable outlays and resources do not buy peace of mind for small business owners who, as Ranking Member Velázquez stated, often operate in fear of vague laws being used against them.

Uncertainty has also crept its way into the audit selection process itself. A Government Accountability Office (GAO) report issued in January of 2016 on the Small Business/Self Employed (SB/SE) division of the IRS concluded that the "lack of strong internal control procedures" in the agency's 33 work streams for identifying and reviewing returns for possible audit "increases the risk that the audit program's

mission of fair and equitable application of the tax laws will not be achieved." The term of "fairness" in selecting returns was unclear or even contradictory in how it was defined among IRS staff, while "documentation and monitoring procedures were inconsistent" for ensuring that selection procedures met internal controls. Flawed inputs like these could have real-world consequences in terms of the effectiveness of audits for the government and equitable treatment for taxpayers.

Previous taxpayer rights laws have certainly improved audits and auditor behavior. Still, members of the tax representation community have observed that the conduct and attitudes of audit personnel have not been subjected to the same level of regulation as personnel involved in collection. A passage from a 2012 article appearing on AOL News by Ross Kenneth Urken, personal finance editor for TheStreet.com, is particularly illuminating:

> In response to the 'storm trooper' reputation, the IRS publicly tried to clean up its act during the Clinton administration. Yet most of the changes it made had to do with collections, according to Anthony Parent, the founding partner of IRS Medic, a law firm oriented toward those with tax troubles. There was a lot of congressional testimony about revenue officers' abuses, but there was no censuring of abusive auditors, nor were any concrete limitations placed on their powers. …
>
> Given that the typical auditor today was just a kid during the Clinton administration, Parent says, the public now can still expect 'skittish' auditors who 'if pushed into a defensive position, will lash out at a taxpayer.'

To this day, taxpayers and advisers continue to report on troublesome developments in IRS audits that range from isolated cases to broader policies. Here I am indebted to Daniel J. Pilla (an author and tax litigation expert), Leonard Steinberg, E.A. (a New York area tax representative), NTU's members, and others for providing me with background information on their challenges:

- Some auditors continue to ignore or deny protocols in the Internal Revenue Manual, including "audit reconsideration" procedures when, for instance, an individual files an amended return that could obviate the need for continuing an examination.
- IRS delays in resolving some cases allow the statutory clock to keep ticking on interest that is almost never abated, even though the agency's own lack of follow-up may be to blame.
- In other areas, however, "Speed Up Audits," brought on by what some say is a reduction in IRS enforcement resources, may be leading taxpayers to a financial dead end. Writing in *The New York Times* in 2015, Dave Du Val of TaxAudit.com explained that, "Examiners for the I.R.S. are giving taxpayers and their accountants much less time to respond to certain audit letters. … An initial request for an appointment is followed quickly – in some instances, on the same day – with a follow-up letter that states that the requested information has not been received." That second letter contains a threat that failure to respond to the first notice could result in loss of appeal rights. A taxpayer in this situation has little, if any, time to consider even a basic response, much less an appeal.
- The IRS "rounds up" in making its case against taxpayers. Restaurants, for example, become targets through no fault of their own because of the IRS's fixation on credit-card transactions as part of the audit determination process. These transactions include taxes and tips, generating an artificially larger cash-flow than records which would reflect only actual sales of menu items.
- Innocent "chit chat" between auditors and taxpayers can become the basis for wider investigations. An auditor might innocently raise the topic of where the citizen might have last gone for vacation, or ask for advice on buying a car based on what the taxpayer owned.

Correspondence from the IRS can intimidate as well, whether intentionally or not. According to Daniel J. Pilla, who has decades of experience in helping thousands of clients, the Revenue Agent's Report (RAR) mailed with the post-audit "30-day letter" can be misunderstood. As he wrote in his recent book, *How to Win Your Tax Audit*, "Citizens commonly mistake the RAR for a bill, which it is not. They do not understand that it is merely a proposed change, which they can appeal."

Thus, by its very nature, any IRS examination involves a considerable expenditure of time, effort, and money on the part of the business owner and the owner's professional advisors. Substantiating deductions or reconciling income often requires gathering or producing copious records. The owner's mental energy is shifted away from maintaining or growing the business and toward meeting what can seem like an endless list of IRS demands. And of course, the out-of-pocket expense for financial and legal advisors can take on enormous dimensions, sometimes out of proportion to the amount of tax at issue. With so much at stake, one would be led to believe that most small businesses would appeal adverse IRS determinations. This is not the case, and the reasons merit further analysis.

According to the *IRS Data Book*, 29 percent of all field audits and 57 percent of all correspondence examinations of small corporations in Fiscal Year 2015 involved no proposed change to the taxpayer's liability. Among 1040 returns reporting business income, the percentages were generally smaller, although those with business receipts above $200,000 subject to correspondence audits had a no-change rate of above 50 percent.

It is clear that the number of small business taxpayers who actually appeal their audits is quite low. There are several ways of measuring the appeal rate, but *Data Book* presentations show that 6,291 taxable nonfarm 1040 returns with business income of under $200,000 involved "unagreed recommended additional tax" out of 191,501 returns in that category examined. Even after throwing out "no change" returns and recommended decreases in tax liabilities, from these statistics alone the rate of appeals in audit situations appears to be paltry, hovering somewhere below 5 percent.

Is this apparent low frequency of disputes simply attributable to the IRS being correct in the position it takes from the vast majority of examinations? Numerous authorities, from prominent members of the tax advisory community, to the Government Accountability Office, to the National Taxpayer Advocate, would answer, not at all.

Many business people told lawmakers in hearings during the 1980s and 1990s that they believed the cost of disputing an IRS tax bill – even if they knew the agency was wrong – simply became too prohibitive. To be sure, appeal and abatement processes for audits have improved over time in terms of accessibility and affordability for taxpayers without extraordinary means. Unfortunately, many Americans facing IRS demands still felt helpless. According to a 1995 study by Daniel J. Pilla:

> The average individual face-to-face tax audit led to the assessment of $4,780 in additional tax and penalties, not including interest. However, just 5 percent of those found to owe more money appealed [*Pete Sepp comment: note 2015 statistics above showing how little this figure seems to have changed*]. The 5 percent number is significant in this way: the GAO has proven that the IRS's computer notices are wrong 48 percent of the time. Still, 95 percent of the public is persuaded that IRS audit results are correct or not worth fighting. That testifies to the degree to which the IRS has the public convinced that it cannot win when challenging an audit.

In short, all too many Americans thought it was cheaper to pay what the IRS said they owed rather than fight. Consider, for example, the average additional recommended tax in 2015 resulting from field audits of business 1040 tax returns with receipts between $25,000 and $100,000 – a total bill of $9,947 per return. Imagine the decisions this audited business owner – the very definition of "the little guy" – would face.

If he or she hires a tax professional for representation, the average fee, according to the National Society of Accountants' most current public data, would be $150 per hour. It would not be unusual for the accountant to spend 10 hours on this stage of the audit. Should the initial examination go against the owner, he or she could choose to retain the accountant for the administrative appeals process, perhaps involving an additional 10 hours of time. Meanwhile, the owner could have easily spent 10-20 hours of time gathering records, reviewing paperwork, etc., at an average compensation amount (according to the National Association of Manufacturers study mentioned previously) of $48.80 per hour.

To get this far into the audit process, the owner could have already spent roughly $4,000, more than one-third of the contested bill. Should the administrative route fail, the owner then has broad options to file a Tax Court petition or try to litigate in federal court. While many Tax Court petitions never advance, and often lead to settlements, this process could easily consume another 10 hours of a legal professional's time (at likely a higher rate of compensation). Should litigation actually take place, a qualified tax attorney might demand $300 per hour or more. If the owner prevails, his or her ability to recover the entirety of fees like these remains doubtful. The maximum amount that can be awarded is barely $200 per hour, and only if the court determines the IRS's position was not "substantially justified."

In a 2013 *Wall Street Journal* article, respected tax lawyer Robert Wood estimated that over the past decade, he identified at least 22 taxpayers involved in IRS disputes who received some kind of attorney compensation or litigation costs from courts, "although some rewards may later have been reduced." Other award cases may exist but their prevalence remains rare.

On the other hand, the IRS's litigation resources against small businesses are formidable. Over the past ten Fiscal Years, the IRS Chief Counsel's Office has typically closed some 70,000 "tax enforcement and litigation" cases per year. Roughly ¾ of those cases fell under the category of "Small Business and Self-Employed."

Confronted with this type of calculus, along with the "fear factors" described above, it is little wonder that many businesses are forced into either conceding completely to the IRS's position or making a compromise that substantially weakens their balance sheets. The latter course can actually backfire on the government, should the business become so infirm that it no longer is able to deliver receipts to the Treasury. In this context, striving to provide better tax dispute resolution processes makes perfect sense.

III. The Right to Appeal: A Concern for All Taxpayers

Dispute resolution is not confined solely to controversies involving small amounts or minor points of law. In fact, a set of issues stemming from examinations in the Large Business and International (LB&I) division of the IRS has implications for all taxpayers.

In recent years the IRS has envisioned shifting its LB&I examination focus away from industry-specific clusters and toward nine practice areas, four of which are regionally oriented and the remaining five subject-oriented (e.g., enterprise activities, pass-through entities, cross-border activities, withholding and individual international compliance, and treaty and transfer pricing operations). The LB&I audit approach is to be issue-based, outcome-driven, collaborative, and transparent.

In 2015, National Taxpayers Union enthusiastically joined as a member of the Coalition for Effective and Efficient Tax Administration (CEETA), which was formed to constructively engage both the Treasury and Congress on audit process issues as the LB&I reorganization took place. CEETA is comprised of more than a dozen trade associations and citizen groups.

Because it is so remarkably broad, this coalition has been able to gather the experiences of numerous companies and unify them around several themes embodying opportunities to improve the way business (and in some aspects individual) tax audits should be conducted. These themes were contained in an extensive November 2015 memorandum to IRS officials:

Lack of Centralized Management and Accountability in Audits. Under the new LB&I auditing process, more than one practice area (e.g., a regional area and an expertise area) may be assigned to a single audit. In addition, the IRS's chains of command for domestic and international audit issues are split. How will the IRS's personnel lines of reporting and most importantly, decision-making authority, be allocated in such a situation?

Lack of Transparency. Nowhere is greater transparency more urgent than in the way official guidance over highly complex issues raised in audits is promulgated through the IRS Chief Counsel. CEETA has determined that over the past 15 years, there has been a dramatic shift toward relying upon less formal Chief Counsel Advice (CCAs), which generally have no taxpayer participation, and away from Technical Advice Memorandums (TAMs), which require agreement between the taxpayer and the IRS on the facts surrounding a given question.

This development has serious downstream effects. CEETA noted in its November 2015 communication, "The lack of taxpayer involvement is bound to result in a less robust consideration of the facts and the issue. The use of CCAs can also hinder the resolution of cases in the Office of Appeals because Appeals officers may be disinclined to engage on an issue" after a CCA has been disseminated.

Breakdowns in the Information Document Request (IDR) Process. Through peer review, the IRS's own staff have acknowledged that IDRs are a major impediment to the workflow of audits. In 2013 LB&I clarified procedures for all IDRs going forward, requiring them to be issue-focused, discussed with the taxpayer prior to issuance, and guided by a deadline negotiated between the taxpayer and the agency.

Unfortunately, the execution of these otherwise sound procedures has been uneven and erratic. Problems have been reported such as IDRs with overbroad issue focuses, or "kitchen sink" IDRs for all types of irrelevant information before the initial audit conference has begun. Moreover, examiners have issued multiple IDRs with the same deadlines, or have requested information for tax years or entities not under audit. These problems and others can make the new process chaotic.

Delays in Closing Cases and Honoring Estimated Completion Dates. As noted previously, businesses have been experiencing both frustrating delays and demanding accelerations of audits at the hands of the IRS. In the case of LB&I, the prospects for resolving or appealing audits are less tenable. Increasingly, taxpayers are receiving multiple requests for extending the statutory period of examination, while estimated completion dates established in audit plans have become less meaningful.

The Catch-22 becomes evident in the Appeals division's policy requiring that 12 months always remain in the statutory examination period; this becomes a justification for the IRS to continue the audit rather than conclude the case. Taxpayers can never actually avail themselves of an appeal, and are forced into Tax Court.

A Litigation Mentality as Opposed to an Issue Resolution Mentality. In some instances CEETA members have observed that IRS exam teams seem more occupied with "preparing for litigation rather than ascertaining the correctness of a return and resolving issues." The end result "negatively affects the cooperative relationship, impedes transparent interaction, decreases efficiency, increases costs, and delays certainty for both taxpayers and the Service."

CEETA has identified several key matters that should be addressed through legislation in this Congress – while prudent inputs and adjustments can still be most effectively absorbed into the IRS's LB&I audit strategy. They are:

Properly Limiting the Designated Summons. Although the IRS has the conventional power to summon testimony and documents in examinations, the designated summons is a special authority intended, according to a top IRS audit official, for situations "only after the taxpayer under examination refuses to extend the statute of limitations … and the examiner has exhausted all other means to obtain the needed information." The designated summons, unlike conventional summonses, will act to suspend the assessment period when a court proceeding is brought to enforce or quash it. As a consequence, the designated summons can, if employed improperly, compel taxpayers into nearly endless extensions of the statutory examination period.

Until quite recently, designated summons enforcement was quite rare. But as CEETA's memo warns, "current and former IRS officials have publicly commented that designated summonses will become a more frequent IRS management tool." It bears mentioning here that like many weapons, the designated summons can be effective when employed as a threat, not just a reality.

Better Defining Circumstances for Designating Cases for Litigation. Just as the designated summons was designed to be used only under special circumstances, the IRS has given itself the authority – when approved by high-level agency and Chief Counsel officials – to force a case or audit issue into the courts. This power has never been authorized by Congress. It is again, intended to be wielded infrequently because doing so strips a taxpayer of the right to an administrative resolution unless the taxpayer unconditionally surrenders their position on the issue. IRS guidelines indicate that cases suitable for designation are those that "present recurring, significant legal issues affecting large numbers of taxpayers … and there is a critical need for enforcement activity with respect to such issues" (e.g., tax shelters).

In theory this power, carefully employed, could function effectively. But as CEETA notes, when used with less circumspection, or even threatened, designation has raised "concern [among taxpayers] regarding the predictability of their own audits and in particular the availability of Appeals."

Ending the Improper Use of Private Contractors in Examinations. In 2015, Senate Finance Committee Chairman Orrin Hatch made an important inquiry to Commissioner Koskinen regarding a $2.2 million contract extended to a private law firm in a large corporate audit; this contract permitted examination activities from the firm best described as overbearing and harsh. Chairman Hatch stated:

> The IRS's hiring of a private contractor to conduct an examination of a taxpayer raises concerns because the action: 1) appears to violate federal law and the express will of the Congress; 2) removes taxpayer protections by allowing the performance of inherently government functions by private contractors; and 3) calls into question the IRS's use of its limited resources.

From NTU's standpoint, the IRS's action is fraught with additional risks. Allowing more entities access to confidential taxpayer information only raises the likelihood of additional data security breaches in the future, on top of several recent hacking incidents and a continuing plague of tax-related identity theft. Furthermore, if the agency is allowed to continue this practice, by issuing a "temporary regulation" without a comment period or notification, the door will be open for other grave trespasses against taxpayers' rights affecting many constituencies.

All of These Factors, and More, Undermine Taxpayer Rights to Appeal. The Office of Appeals is approaching its 90th year of service, while the IRS Restructuring and Reform Act of 1998 created "firewalls" between Appeals and compliance functions as well as directed the Commissioner to ensure availability of impartial appeal options. Most recently the 2015 taxpayer rights legislation affirmed

that a taxpayer should be able to disagree with the Service's positions. Yet, these assurances are becoming eroded in a number of ways. Taxpayers need, and deserve, definitive statutory protections that provide, in crystal-clear detail, their right to appeal an audit without the duress of capitulating.

Daniel J. Pilla was among the first members of the tax representation community to recognize the danger that LB&I's approaches would pose to other types of taxpayers. In his 2014 book, *How to Win Your Tax Audit*, Pilla wrote:

> At the time of issuance, the [IRS's LB&I] memo was pointed at only large businesses. However, it is clear that the agency will push the practices 'more deeply' into the system, exposing more taxpayers to their pitfalls. I fully expect the IRS to utilize 'strong arm' tactics more often in pressing for documents in all audits, particularly those related to business income and particularly with respect to computerized recordkeeping systems. … I fully expect [the policy] to migrate deeper into the IRS sooner rather than later.

More recently, in an April 19th 2016 endorsement letter, the Small Business and Entrepreneurship Council (SBEC, a CEETA member) expressed just how relevant CEETA's stance was to its many thousands of supporters across the country:

> Small business owners do not have the resources to endure audits without end. They certainly do not have the resources to go up against a powerful $1,000-an-hour legal team in a tax dispute, Indeed, it's not hard to see how powerful, private attorneys doing the most complex and sensitive work of the IRS could lead to abuse and harassment, not to mention expensive legal bills.

Those who believe the IRS would never hire such "big guns" to pursue smaller businesses' tax liabilities should bear in mind that decisions by auditors and Appeals officers are guided first and foremost by the facts and the law. While the agency will weigh the danger of setting an adverse precedent for the government if a case might wind up in court, the "nuisance cost" is not a formal determinant. Even so, the opening given the IRS by this questionable practice could easily permit private attorneys commanding somewhat lower rates to routinely involve themselves in cases involving smaller liabilities.

There is a larger point to be explored here. How meaningful is the distinction between small and large businesses for the purposes of audits? LB&I's jurisdiction encompasses a wide range of entities called "large corporations," including not just major multinational firms but companies with assets at a minimum level of $10 million. Granted, the latter entities can hardly be described as "mom and pop" concerns, but neither are they massive conglomerates. They could be "hometown" companies employing several dozen, rather than thousands, of individuals. Census Bureau statistics show that an establishment of any type reporting receipts of between $35 million and $39.99 million had a payroll averaging fewer than 50 employees. Even those establishments in the $10 million-$14.99 million receipt category, an amount that still seems quite large, employed an average of fewer than 40. Assets and annual receipts are two different statistical snapshots, but they are often closely related parts in the mural of a company's finances.

Finally, audit and enforcement actions pursued against the very largest American businesses have "ripple effects" in the small business community that works with them. Large multinationals tend to have supplier, distributor, or contractor networks numbering hundreds or even thousands of member businesses. These often-small entities suffer adverse consequences to their own bottom lines when their larger customers must alter expansion plans or reconfigure business models due to tax concerns.

Ultimately the tax system must be viewed holistically. Otherwise, the rights of individual and business taxpayers become categorized, divided … and conquered by bureaucratic overreach.

IV. Alternative Dispute Resolution: Why Is the U.S. Lagging?

Given all of the developments described in the previous two sections of this testimony, one goal of taxpayer rights advocates has been to establish a less formal, less expensive way for taxpayers to obtain justice. The National Commission on Restructuring the IRS gave extensive consideration to improving Alternative Dispute Resolution (ADR) methods for use in federal tax controversies, including mediation as well as binding arbitration. Limited procedures were in place at that time, applying primarily to cases of over $10 million or more. ADR at the tax agency was a relatively new concept, following passage of the government-wide Administrative Dispute Resolution Act of 1996.

Ultimately, the Commission did not make major recommendations in this area, although the subsequent 1998 RRA did remove the dollar threshold, and establish a pilot program for binding arbitration. Unfortunately, the usefulness of ADR for most taxpayers has so far been questionable. As the Subcommittee is well aware, the National Taxpayer Advocate's 2016 Annual Report to Congress has made the IRS's failure to "effectively use ADR" as #15 on the "Most Serious Problems" list.

It is clear that when ADR is employed, the results are generally encouraging. For "Fast Track Settlement," which applies to factual and legal disputes during an examination, the average settlement rate for FY 2016 was above 80 percent and the average time to resolution was less than two months. At the same time, the utilization rate of ADR is pitiably low, at less than one half of one percent of all cases in the IRS Appeals division and dropping.

Why is all of this happening? It seems implausible, for example, that unlike taxpayers in other nations, Americans would prove uniquely resistant toADR. As the NTA's report pointed out, survey data indicates that more than 4 in 5 business people "report that arbitration is a fair and just process." Nor does the U.S. government seem uniquely unable to implement such reforms. The Environmental Protection Agency and the Social Security Administration are just two of several federal-level practitioners of ADR.

The NTA identified several reasons why the potential of ADR has yet to be fully achieved in tax matters. We offer the following observations of contributing factors, in order of priority.

Intentionally Narrow Scope. In a sense, ADR at the tax agency is a self-selecting process from the start. Most "Campus Collection" (e.g., non-field) cases are not eligible for ADR, as are cases which, in the IRS's opinion, could have "controlling precedent." Equally difficult is the fact that the IRS can refuse to engage in ADR when a taxpayer requests it.

Lack of Perceived Impartiality. Private-sector arbitration or mediation usually involves a completely neutral third party with no prior direct knowledge of the case or its parties. This is somewhat more difficult to achieve in public sector settings, since a specialized level of expertise as well as a government-supported forum are usually necessary. Nonetheless, as the NTA has pointed out, other federal agencies house their mediators in a stand-alone department staffed specifically for the purpose of ADR proceedings.

Not all ADR data is encouraging, but it is instructive. Post Appeals mediation cases in FY 2016 involved only about one-fourth of all ADR proceedings, with settlements of barely more than 10 percent. These cases can be especially difficult to settle, given their nature of taking place between the point of appeals and potential litigation. Still, it cannot be helpful that the mediator involved in this particular interaction is selected from the regular caseworker pool of the Appeals division to interact between the auditing team and the taxpayer.

NTU is long familiar with this perceived (and occasionally genuine) conflict of interest in tax cases. One hurdle that the older Problem Resolution Program for assisting taxpayers was that its staff were often housed in the very same IRS district office whose personnel were the subject of the taxpayer's complaint. Bob Kamman, an Arizona attorney who advised NTU on taxpayer rights matters, noted in testimony to Congress that sometimes a problem resolution officer would even refer that complaint directly back to person responsible for the problem, instead of his or her supervisor or another office. This perception took considerable effort to overcome on the part of the National Taxpayer Advocate.

IRS Culture Has Yet to Fully Adapt. The Internal Revenue Manual itself states that "mediation programs achieve [the] objective" of resolving "tax controversies at the lowest level without sacrificing the quality and integrity of those determinations." Yet, the Agency has often applied the ADR term loosely to processes that many experts would not characterize as such. These include Collection Due Process Appeals and the Collection Appeals Program. There is a tendency for any large agency or business to redefine existing operations to appear as if it is embracing change. But the IRS's culture has often presented especially difficult challenges. As the IRS Restructuring Commission's report indicated, "the culture of IRS is overly risk averse," and there is a "lack of structure to improve operations." Some 20 years later, this culture has been evolving, but not necessarily at the pace to support full implementation of ADR. Fast Track Settlement, to give one example, was not extended to small business and self employed taxpayers until late 2013.

Lack of Consistent Evaluation. Other federal entities (as well as international tax authorities) have attempted to measure the time and cost benefits of ADR for themselves and for taxpayers. The results are reported in various parts of this testimony. Yet, this presents a "chicken and egg" problem for the IRS. With so few cases currently being processed through ADR, would this type of data be statistically sufficient and valid to encourage further participation? Frankly, the agency has little choice in the matter but to proceed, even with what could be described as a limited data set. For ADR to take root and flourish in the field of tax disputes, even preliminary findings would be helpful. So would an honest evaluation of the agency's efforts to promote these ADR options, especially if Congress decides to instruct the IRS to expand them.

V. Resolving Taxpayer Disputes – New Approaches

With the 20th anniversary of RRA '98 approaching, it is fitting that the Subcommittee embrace the tradition of thoughtful, bipartisan cooperation that has succeeded in making a major difference in the lives of everyday taxpayers who, for one reason or another, encounter the IRS after filing their returns. Accordingly, NTU makes the following recommendations concerning resolution of taxpayer disputes, which involve many layers in all three branches of government.

Codify and Strengthen the "First Line" of Resolution – The Right to Appeal. One of the most important recommendations NTU can make in this communication is that Members of the Subcommittee support a recently-introduced bill to improve transparency, accountability, and resolution of administrative matters between citizens and the IRS. HR 3220, the Preserving Taxpayers' Rights Act sponsored by Reps. Jason Smith (R-MO), Terri Sewell (D-AL), and a strong bipartisan list of cosponsors, contains some of the most comprehensive improvements to tax administration since RRA '98. First, it would codify the right of taxpayers to have their appeal heard by an independent and impartial IRS Office of Appeals to ensure there is a timely and efficient resolution to tax disputes between the agency and the taxpayer. Second, it narrows the scope for which kinds of cases can be designated for litigation by clarifying the limits of the agency's prerogatives. In fact, this power has never been authorized by Congress, but is an administrative power the IRS has developed institutionally.

Third, HR 3220 would limit the IRS's ability to issue designated summonses, a tactic which law-abiding individuals and businesses acting in good faith have increasingly encountered. Under the proposed law,

this power could only be applied to taxpayers who are uncooperative and refuse to provide information or documents requested by the IRS. Finally, the language prohibits a growing, and unprecedented practice of the IRS outsourcing federal tax audits of citizens to third parties.

The provisions outlined in this bill represent a strong start toward restoring faith in the audit process and a more businesslike resolution environment between the IRS and the taxpayer. If adopted, the results will be lower IRS litigation costs, increased efficiency of agency resources and reduced uncertainty for taxpayers undergoing audits. It should be the foundation for further dispute resolution reforms.

Expand ADR and Other Taxpayer Resolution Options. Legislation introduced in the previous Congress, the Small Business Taxpayer Bill of Rights (HR 1828 authored by Rep. Mac Thornberry (R-TX)), provides a good starting point for discussion on how to jumpstart the utility of ADR in tax cases. The bill would allow a taxpayer to seek private, accredited mediation or arbitration from an "independent, neutral individual not employed by the Internal Revenue Service Office of Appeals." The taxpayer would under most circumstances share the cost of such a mediator.

The legislation would likely have to be augmented in other respects. Congress will need to either embed in statute or convince the IRS to widen the availability of ADR to campus cases, and should at least consider methods to limit the agency's prerogative to refuse mediation or arbitration.

Even if Congress finds this proposal wanting, a dedicated body of more neutral arbiters that taxpayers will come to respect is absolutely necessary for ADR to succeed. The NTA recommends a separate, distinct ADR branch housed at the IRS for such purposes. This is the minimum action that must be taken. Congress could direct the IRS to create this entity, with its own organic management and counsel as well as arbitration and mediation personnel. As a stronger alternative, Congress could give agency status to such an entity outside the IRS under Treasury, or even consider housing it at the Department of Justice. If Congress pursues the new tax agency structure outlined in the Better Way Blueprint, then the entity could serve as an adjunct to the proposed small claims court.

Other pieces of legislation introduced in the previous Congress contain numerous helpful augmentations to taxpayer rights. HR 1828 (114th Congress) would also:

- Strengthen safeguards against taxpayer abuses, such as a ban on ex parte communications between IRS case employees and appeals officers, and a prohibition on new issues being raised during a taxpayer's appeal process.
- Provide more avenues for redress when the IRS recklessly or intentionally disregards the law, including increases in the cap on damages and more options to recover attorney fees.
- Deliver additional opportunities for spousal relief, such as more time for filing petitions and clarifying that Tax Courts must follow applicable appellate procedures when reviewing such petitions.

Other reforms discussed in the Senate Finance Committee in the previous Congress merits the Subcommittee's attention. Among these was an amendment developed by Senators Grassley, Thune, and Cardin to tax identity theft legislation. Although it was authored prior to the PATH Act's codification of the Taxpayer Bill of Rights, the remainder of this amendment could still answer to many purposes under discussion in today's hearing. Highly desirable elements include clarified lien notice filing procedures, expedited "hardship" relief for businesses subjected to levies, and a new consultation requirement that will ensure that the IRS bureaucracy seeks early, systematic input from the Taxpayer Advocate before new regulations are published. Some of these concepts owe their genesis to Senator Grassley's bill from the 114th Congress, the Taxpayer Bill of Rights Enhancement Act (S.1578).

Look Abroad for Advice. Dispute resolution may seem to be an arcane matter to some, but across the world, it is a major underpinning of stability in tax administration systems. A March 2017 report from the International Monetary Fund (IMF) and the Organization for Economic Cooperation and Development (OECD) contained the results of a Forum on Tax Administration survey of tax authorities taken in January of this year. The results are enlightening.

The survey, drawn from 25 countries in the OECD, G20, and elsewhere, asked participants to rank 21 factors (on a scale of 1 to 5) that contribute "to tax uncertainty for business taxpayers in your country's tax system, regardless of whether or not the factors are within the control of the tax administration to influence." "Lengthy decision making of the courts, tribunals, or other relevant bodies" received the second-highest mean score among all 21 factors, with "Complexity in tax legislation" ranking first. Respondents were then asked to rank the importance of 25 various "tools to enhance tax uncertainty." Placing at #2 on the list (by media score) was "Effective domestic dispute resolution regimes," topped only by "Detailed guidance in tax regulations."

Of course, U.S. tax laws and their system of administration vary from those of other countries. Still, other nations have fine-tuned their dispute resolution systems to provide instructive guidance:

- Prior to a tax court case, Australian law subjects both the tax authority and the taxpayer to a mandatory requirement that they report on "genuine steps" taken to avoid litigation. As a result, ADR is more prominent in the dispute process.
- New Zealand's experience has received considerable evaluation from scholars there. In 2013 Melinda Jone at the University of Canterbury examined the country's tax dispute resolution structure, for which reforms such as mediation were being considered. In conducting both qualitative surveys and focus group interviews of practitioners, Jone and her colleague determined that "the most important aspect of the defined proposed regime is the inclusion of a mediator who is independent of both parties and moreover, that the mediator is foremost trained and qualified in mediation as opposed to being a specialist in tax law." Providing this as a cost-free service "should in turn enhance taxpayers' perceptions of fairness of the disputes procedures and therefore voluntary compliance."
- In 2011 Portugal initiated an ADR process for certain tax cases falling below prescribed amounts. If a given dispute meets those qualifications, revenue authorities are bound to engage in arbitration if the taxpayer requests it. An arbitration tribunal is empaneled that normally consists of the taxpayer's nominee, the government's nominee, and a third member agreed to by these two nominees. Qualification requirements for the nominees may apply in disputes of larger amounts, and generally arbitration results cannot be subject to another level of appeal.
- In the United Kingdom, Her Majesty's Revenue and Customs has been building experience with mediation-style ADR since making the option widely available in late 2013. Initial results have shown that roughly 4 in 5 cases for mediation among businesses were resolved; more than 4.5 million taxpayers in what are called "small and medium enterprises" are eligible for this form of ADR, and most have seen resolutions to their cases within 120 days. Considering that simply obtaining a hearing through the UK's First Tier Tax Tribunal entailed an average wait of nearly four times as long, this is a vast improvement. Even when ADR fails at its immediate task of a resolving a case, it can still perform a constructive purpose by sharpening issues under contention when they are litigated.*

**A useful guide in regard to the UK's recent ADR procedure is entitled "Mediation of Tax Disputes" by Carl Islam Barrister, TEP, available at* http://newsite.carlislam.co.uk/wp-content/uploads/2016/02/Guide-to-the-mediation-of-tax-disputes.pdf.

Numerous other sources cited by the NTA and international mediation organizations can point to useful information on dispute resolution abroad. I do hope, however, that the Subcommittee will avail itself of an additional resource. National Taxpayers Union is a founding member of World Taxpayers Associations (www.worldtaxpayers.org), a global alliance of dozens of organizations dedicated to taxpayer rights. They possess a wealth of knowledge surrounding tax administration procedures in their own nations that could richly inform and supplement the testimony NTU is providing today. I would look forward to connecting Subcommittee members and staff in the coming weeks with WTA leaders for focused dialogue on issues of mutual interest.

Look to States as Well. For more than a decade, independent state tax tribunals have been gaining in popularity. In 2006, the American Bar Association (ABA) developed model state legislation ("Model Act") to serve as an alternative to traditional income tax dispute methods, which tended to fall into administrative appeals heard by the tax authority and litigation in courts. Today, such tribunals are commonplace. Although ABA's model act has some provisions that resemble existing federal implements, (such as the U.S. Tax Court), there are nuances worth exploring:

- While the U.S. Tax Court permits Enrolled Agents and CPAs to represent taxpayers in proceedings if they pass an exam, some state tax tribunals offer fewer such restrictions.
- The Model Act stipulates that the tribunal resides in the executive branch of government.
- Even though they do not operate as courts, tribunals are still established as separate and distinct entities from the tax agency.

In a familiar theme to discussing underutilization of ADR procedures the Internal Revenue Service has developed, the Tax Executives Institute (TEI) characterized its support for tax tribunals by stating, "The most important attribute of a tax tribunal is its independence. An impartial process for resolving tax disputes is a hallmark of both equitable tax administration and a competitive business environment."

NTU would urge the Subcommittee to further consult with ABA, TEI, and the Council on State Taxation for views on tribunals that could prove pertinent to the fashioning of federal legislation.

Unlock the Courts for Changing Times. At the 2017 International Conference on Taxpayer Rights, Professor Kristin Hickman presented on the issue of "Administrative Law's Growing Influence on U.S. Tax Administration." Her abstract pointed out that in the 2011 Mayo Foundation decision, the U.S. Supreme Court "declared its reluctance 'to carve out an approach to administrative review good for tax law only.' [This and other] cases … aim ultimately to require Treasury and the IRS to do a better of complying with APA [Administrative Procedure Act] requirements and explaining their actions at the time they undertake them – and thereby provide for greater transparency and accountability for Treasury and the IRS."

As this jurisprudence develops, now would be a good time for Congress to explore whether legislative affirmations of APA would be helpful in hastening this outcome, which could markedly improve the quality of information in many instances of judicial dispute resolution.

NTU would add that the availability of courts themselves for dispute resolution could be dramatically improved. Although the 1988 and 1998 taxpayer rights laws provided for certain exceptions, taxpayers still generally cannot enforce their rights in court until after they have been violated. Under Section 7421 of the Internal Revenue Code, no lawsuit can be brought by any person in any court for the purpose of restraining the assessment or collection of a tax, except under limited circumstances.

The case law around the Anti-Injunction Act further impedes the ability to restrain the collection of the tax. Injunctions can be granted where the failure to grant relief would result in irreparable damage to the taxpayer. But an injunction will only be allowed where it is clear that under no circumstances would the government prevail (or the taxpayer would not owe the tax). Moreover, the Declaratory Relief Act, which allows citizens to file a suit that can persuade a court to declare their rights, indicates that the law applies "except with respect to federal taxes." The Federal Tort Claims Act presents additional barriers to tax-related controversies.

Congress should give serious consideration to providing citizens with the limited ability to stop the IRS from violating their rights through litigation. Doing so will involve some level of controversy, and will no doubt prompt lengthy deliberation. A passage from NTU testimony before Congress in 1995 indicates a solid starting point, which is by amending the Anti-Injunction Act:

> Taxpayers should be allowed to file suit in a federal district court to enjoin the IRS from enforcement action because: the deficiency assessment was made without knowledge of the taxpayer and without benefit of the appeal procedures provided by law; there has been an improper or illegal assessment; there has been an action in violation of the law or tax laws or regulations providing for procedural safeguards for taxpayers; the IRS has made an unlawful determination that collection of the tax was in jeopardy; the value of seized property is out of proportion to the amount of the liability if other collection remedies are available; or the IRS will not release the seized property upon an offer of payment of the U.S. interest in the property.

Increase Representation Options. Though first partially funded by the federal government through RRA '98, Low-Income Taxpayer Clinics (LTCs) have their roots in remarkably successful pro bono and nonprofit programs established decades before then. Prior to her position as NTA, Nina Olson was associated with the Virginia-based Community Tax Law Project. In remarks to this Subcommittee on September 26, 1997, she wrote:

> Our clients have cases involving complex issues, such as investment tax credits and depreciation deductions claimed by rural farmers; the taxable nature of severance pay received by a Navy pilot in combat status at the time of retirement from service; and the taxable nature of a payment received in the settlement of a complicated suit alleging anti-trust violations … Other cases involve the responsible person penalty (IRS 6672) and employee classification issues.

Today, the income eligibility thresholds for LITC assistance are set at 250 percent of poverty level (e.g., $61,500 for a family of four). This is helpful for working-class, some middle-class, and a limited number of small business owners. Should Congress follow the IRS reorganization proposal called for in the Better Way Blueprint, access to administrative, quasi-judicial, and legal remedies should be more affordable than it is today.

Nonetheless, Congress should remain sensitive to the needs of taxpayers who fear their capacity to assert their rights is limited by lack of representation. The Social Security Administration provides Administrative Law Judge services at no charge to participants in ADR procedures. Taxpayers face more complicated circumstances, as Olson's account above amply demonstrates. Short of providing a "public defender" office for taxpayers – likely the costliest policy option – Congress could simply recognize the valuable contribution of the current nonprofit LITCs and their volunteers. Raising the eligibility threshold (and concomitant funds) to 300% or 350% of poverty level would begin opening up assistance to more small business taxpayers in particular. Although Congress could employ a different measure of eligibility, such as size of tax dispute or AGI on the tax return in question, each carries with it pros and cons.

Beware of "Scoring" Traps. One technical aspect the Subcommittee is no doubt considering has to do with the "revenue loss" of any taxpayer rights provisions. While such a concern can be valid, NTU

would caution that many revenue estimates are highly dependent upon changes in behavior that are more complex to model than they would seem. Without wading into the static versus dynamic scoring debate, it is often easier to assume that collections will be dramatically impacted when restricting the tax agency's powers. Yet this has not necessarily proven true.

The National Commission on Restructuring the IRS found "no evidence that the rights to redress" under the 1988 and 1996 taxpayer rights laws "have caused significant disruption to IRS collection efforts." The Commission's report determined that the cost of providing reimbursement for representation fees under those laws was $5 million, rather than the $100 million originally estimated. In the final analysis, even if the "cost" turned out to be $50 million, or $100 million, the central question here is whether justice is being more effectively served. This is generally what policymakers ask when it comes to other issues of access to the legal system.

Furthermore, even from a cold, hard dollars-and-cents perspective, the *net* rather than the gross impact on revenue must be taken into account. For example, the very existence of dispute resolution mechanisms can have an additional, quantifiable fiscal benefit – better voluntary compliance. During a September 25, 1991 hearing before this Subcommittee, Ernest J. Dronenburg, then Vice Chairman of California's State Board of Equalization, provided an illustration of this point that is still potent today:

> Many tax administrators initially viewed taxpayer bills of rights with skepticism and apprehension. However, others immediately saw the Taxpayers' Bill of Rights as a 'two-fer.' By that, I mean it changes the attitudes about tax administration and the tax system, and it also sends an emphatic message to tax agency personnel that we are going to be doing business differently. Both of these changes create better compliance within the system and reduce the number of people who drop out of the system because they are afraid or unsure of it. …For example, a .5% increase in voluntary compliance resulting from taxpayer education and changing attitudes would increase revenue in my state by over $400 million annually. Conversely, doubling our current audit coverage from 3% to 6% would produce less than half that amount.

National Taxpayer Advocate Nina Olson has since expressed Dronenburg's point in other terms, but Dronenburg's contention that such procedures "make tax agencies more approachable, and encourage working relationships to solve problems" remains convincing to us.

In some instances, data does exist to help monetize the potential of administrative reforms. As the NTA reported, the Air Force's 17-year-old "ADR First" policy with contractor claims has saved the service $275 million, while case resolution times have dropped an average of 80 percent. Resolving issues through ADR typically costs EPA staff less than half the hours they would expend in traditional adversarial resolution proceedings. These experiences, as well as those from other governments and the private sector, ought to be incorporated into any cost projections for expanding ADR that the Joint Committee on Taxation and the Congressional Budget Office may attempt to calculate.

Maintain Oversight of the System – Even Without an Oversight Board. Few elements of RRA '98 were more sweeping and crucial to transforming the tax agency than the IRS Oversight Board – and few have been more difficult to preserve. In August 2013, William Hoffman of *Tax Notes* interviewed many of the principal actors in the passage of RRA '98. According to Russell Sullivan, who served as Senator Bob Graham's (D-FL) tax counsel during the evolution of the bill, "The biggest failure in the legislation [was] the Oversight Board. … [It] should have been the principal entity for giving impetus for the IRS to develop streamlined procedures from a tax administration standpoint and informing Congress to the extent that that's not happening, so Congress could act…" Senator Charles Grassley (R-IA) contended the Board has "been more of a tool for Treasury and the IRS to get what they want – and mostly more money – as opposed to zeroing in on abuse of taxpayers by the IRS."

Many causes have been given for the Oversight Board's apparent shortcomings in meeting the intent of RRA '98, including members who only served part-time and controversies over policing problems with the IRS's nonprofit division and with the Affordable Care Act. Both the White House and the Better Way Blueprint call for abolishing the Board. Nonetheless, NTU would caution the Subcommittee not to overlook the role that an oversight body outside the IRS and Treasury could have in ensuring that progress is made on future dispute resolution policies.

During our service with the IRS Restructuring Commission, it was evident to NTU that future legislation aimed at affecting the culture of the tax agency could not succeed without consistent guidance from a non-IRS entity. This was by no means a universally-held view. Five Commissioners dissented from the Commission's Oversight Board proposal, three of whom praised instead Treasury's efforts to institutionalize oversight with a Management Board consisting of public officials, as well as an IRS customer service task force (again comprised of government officials and employees).

The majority of Commissioners' intent, however, was to provide the "focus, expertise, and continuity that will be necessary for the IRS to meet the legitimate expectations of the American public" through an Oversight Board. That intent largely carried through to RRA '98, but struggled for recognition. The Clinton Administration did not send any Board nominations to the Senate for 18 months.

More than 15 years after that incident, the IRS Oversight Board lacks a quorum, for which there are practical consequences. The IRS's strategic plan receives less emphasis and monitoring from professionals with years of experience in successful business transformations. Information technology issues such as identity theft do not receive as robust a benefit from private sector expertise in developing comprehensive solutions. Furthermore, another source of innovative budgeting practices, again backed by private sector experience, is denied the IRS. Taxpayers ultimately suffer the most from this loss.

Congress could pursue several alternatives to the current Oversight Board. One is to work with the Administration to identify more full-time nominees and staff who can devote additional hours to the Oversight Board's mission. That mission could be further clarified so as to distinguish it from Treasury and IRS Advisory Groups as well as the National Taxpayer Advocate and Treasury Inspector General for Tax Administration. The Board could focus on providing practical private-sector guidance to the IRS on meeting the goals of its strategic plan and embracing innovation (such as ADR techniques). Further, the Board could analyze data and feedback from other bodies such as the Taxpayer Advocacy Panels to provide direct, ongoing input to Congress on legislative responses to some of the most pressing tax administration issues.

Congress could instead consider creating a new entity whose function is to coordinate inputs from various sources and hold IRS leadership publicly accountable for progress on taxpayer rights. During a July 18, 1991 hearing of this Subcommittee, HR 2472 (102nd Congress) was mentioned as a way of creating a "monitoring group" that would have consisted of two appointees from the House's oversight Subcommittee, two from Senate's equivalent, two from private life, and two from the IRS Commissioner. The group was to receive information on taxpayer rights issues and ensure that the IRS Commissioner annually reported on means of resolving them. Perhaps this structure could be modified (to include the National Taxpayer Advocate in place of one of the Commissioner's nominees) to fit current needs.

Another possible approach was brought to the attention of the Restructuring Commission during its Omaha, Nebraska field hearing on April 4, 1997. During those proceedings, Samuel Walker, a Professor of Criminal Justice at the University of Nebraska-Omaha, offered a proposal for an IRS citizen review board. This office, modeled after citizen review and complaint entities established in many cities for police departments, would not be charged with resolving tax administration problems (the mission of the National Taxpayer Advocate) or allegations of criminal behavior (investigated through the Inspector

General or the Department of Justice). Rather, it would hear taxpayer concerns over specific instances of mistreatment by IRS personnel and make recommendations for disciplinary action.

Walker outlined a structure whereby an External Independent Complaint Auditor, appointed in consultation with Congress, would oversee an Internal Office of Citizen Complaints to receive specific reports from citizens and, summarize annually any changes to personnel procedures that might help to minimize incidents and complaints in the future. The Restructuring Commission's final report proposed, instead, that the IRS should "centralize the cataloging and review of taxpayer complaints of IRS misconduct on an individual employee basis." This advice, subsequently embedded in RRA '98, has failed to provide a more formalized grievance procedure which, along with regular reporting on personnel remedies that a citizen review board can provide, could result in more productive resolution of disciplinary problems among tax agency employees.

Congress could request a study from the National Taxpayer Advocate to evaluate the experiences of city police department complaint entities since 1997, and explore the suitability of updating Walker's proposal to current circumstances with the tax agency.

Simplicity Is the Best Form of "Resolution." Finally, I would be remiss in failing to mention the single most effective method of resolving taxpayer disputes: avoiding them in the first place. Tax simplification can play a major role in this regard. When citizens and tax professionals can understand the laws more clearly, resolution procedures can function more properly as tools of last resort. How can such simplification become habitual?

NTU can offer numerous perspectives in fostering this consultation, but two suggestions come foremost to mind. Section 4022 (a) of RRA '98 required the IRS to produce an annual report to Congress on "sources of complexity in the administration of the federal tax laws."

The provision was successful, even though IRS compliance with it was limited. According to the National Taxpayer Advocate, the tax agency has issued just two annual reports compliant with the 1998 statute, but in both instances, "Congress adopted legislation to address each area of complexity referenced in the reports, and the IRS addressed the administrative problems they uncovered. Thus, the IRS's decision to discontinue the reports has likely contributed to tax complexity." The last report was published in 2002; Congress should order resumption of the annual reports now, so that a 2018 document can be readied.

NTU also concurs with the Taxpayer Advocate's recommendation that "the IRS establish a process to automatically provide the tax writing committee staff with a list of specific front-line technical experts who can discuss the administrability of pending (or existing) legislation directly with the tax-writing committees," as provided in Section 4021 of RRA '98. The most important results would be in budgetary savings to the IRS and reduced private-sector compliance costs – a win-win situation for taxpayers.

Regardless of the direction comprehensive tax reform may take in 2017, the need for a regular review of the tax laws with an eye toward clearing away unnecessary, conflicting, or cumbersome provisions will always be extant. NTU's staff recalls vividly from field hearings and other submissions to the Commission that many members of the private-sector tax community were willing to volunteer substantial time and energy to make suggestions for simplification. A panel, meeting once every four years, would harness this volunteer activity.

There are several models for a process such as this, among them creation of an executive branch body (e.g., via the Federal Advisory Committee Act). It's mission: to evaluate Title 26 of the U.S. Code and Title 26 of the Code of Federal Regulations in order to methodically identify specific opportunities for simplification, clarification, and repeal of provisions that are complex, contradictory, difficult to

administer, or outdated, and provide actionable recommendations that the Executive and Legislative Branches can implement in expedited fashion.

Members would include individual taxpayers, business taxpayers, tax practitioners, tax attorneys, academics, and former public officials with an expertise in tax administration (subject to federal employment rules). The Commission's management could be drawn from the National Taxpayer Advocate's Office or the Treasury Inspector General for Tax Administration. Participation and consultation of Congressional staff would be invited and encouraged. The Commission's report could be partitioned according to those requiring legislative action and those necessitating executive action. In order to precipitate such action, the legislative portion could be required by law to be received by the tax-writing committees and brought to the floor under privileged consideration. The executive portion could be automatically referred to the rulemaking process under APA.

The preceding outline would require additional details. NTU is ready and willing to assist in developing the charter for this Commission.

Conclusion

Just one week ago, the House of Representatives unanimously enacted HR 1843, the Clyde-Hirsch-Sowers RESPECT Act. This was an emblematic bipartisan moment for which Members of this Subcommittee deserve great praise, and for which taxpayers are most grateful. It is also a fitting tribute to the title of today's hearing. This legislation brought a much-needed resolution to a policy that had created ongoing taxpayer disputes with the IRS over its excessive, often abusive exercise of asset forfeiture powers.

Congress's statutory remedy, in the form of HR 1843, arrived about three years after many of the IRS's so-called "structuring" investigations made national headlines. Unfortunately, the agency had been engaged, along with the Justice Department, in these acts for a number of years prior.

NTU raises this point to encourage the Subcommittee in reaching bipartisan consensus on the plethora of taxpayer rights and remedies issues that have arisen since the IRS Restructuring and Reform Act. With HR 3220, for example, leading Democrats and Republicans on the Subcommittee and the full Committee have come together to address the right to appeal in a meaningful fashion. Other opportunities for such cooperation abound with your colleagues in the House and Senate. Indeed, the history of this movement for sensible progress on taxpayer rights has been written by Members of both parties, among them Bob Kerrey (D-NE), Rob Portman (R-OH), Chuck Grassley (R-IA), David Pryor (D-AR), Harry Reid (D-NV), and Bill Archer (R-TX).

Tax reform and simplification are integral parts of a long-lasting framework for taxpayer rights. Whatever shape these may take, the Members of this Subcommittee can build administrative foundations that will ensure the current and future tax system functions efficiently, effectively, and respectfully. Accordingly, NTU welcomes the leadership that each of you can provide at this critical moment.

I am most grateful to all of you for engaging in this hearing and for devoting so much attention to these lengthy remarks.

Chairman BUCHANAN. Thank you.
Mr. Shinn, you are recognized.

STATEMENT OF BYRON SHINN, FOUNDER AND MANAGING PARTNER, SHINN & CO.

Mr. SHINN. Thank you, Chairman Buchanan, Ranking Member Lewis, and Members of the Subcommittee. Thank you for the opportunity to discuss reforming how the IRS resolves taxpayer disputes.

As a practicing accountant for over 38 years and a Florida CPA, I have seen a lot of change.

Chairman BUCHANAN. Could you speak up a little bit more in the mike so everybody can hear?

Mr. SHINN. In my opinion, our focus should be taxpayer service first, improve tone with access, consistent controls, and require Fast Track steps.

I have a unique perspective as I have been involved in oversight of the Florida CPAs as a member of the Board of Accountancy's Probable Cause Panel for well over a decade. And most practitioners work hard to get it right. It is the handful of marginal practitioners and aggressive taxpayers that try to push the envelope. These are the practitioners and taxpayers that need to be reviewed.

First, I would like to discuss correspondence audits. They have been expanded in lieu of field exams for many individual returns. These exams require responses in a specific period of time. However, the IRS responses are taking considerably more time than the taxpayer is given.

These exams have a high probability of no change once the IRS receives the submitted responses. In several instances, the taxpayer's rights have been ignored by the issuance of 15-day letters and then, shortly thereafter, 90-day notice of deficiencies, thereby ignoring the 30-day letter and which grants the rights of the taxpayer for an administrative hearing and appeals, and that also breaks their Taxpayer Bill of Rights.

This also prevents the Fast Track Settlement opportunity. Therefore, I believe a standard, that it should exist, that the process must be maintained, and the Service, when it jumps over process, should lose the right to pursue additional revenue: Follow the rules or lose the adjustment. We also should require Fast Track to prevent the circumstances that are existing today.

I next want to speak about field exams. The process has been very taxpayer-unfriendly with a litigious and enforcement tone. Over my 38 years, we have reached a new low regarding the respect that the taxpayers and their professionals have with the Service. It is as if the taxpayer is guilty and has to prove the IRS wrong. The agents are doing several audits at the same time, and they tend to start and stop during the audit, many of them taking much more than 12 months. This just is not right.

We have new rules that are also killing the system. An example is the new partnership exam rules that have brought the process to a state of total chaos. In order to close issues and reduce the time necessary, we talk about the call centers and the local office access. Unfortunately, the wait time on the call centers is extremely long.

Overall, my experience is it has been good once you get to a qualified person. This shows how the Service needs to open up access. The Service should increase the call center available hours, making them earlier, later, and on weekends.

The Service has a very good e-service process. However, this has been reduced due to budget cuts. This needs to be expanded back in a much broader sense.

The local offices no longer allow walk-ins. This is just not—sorry. It is not taxpayer right. It is just not taxpayer first. They need to have reasonable access.

Another area of concern is foreign disclosure exams. We are seeing a situation growing with the continued disclosure of foreign assets and bank accounts going to Appeals, and the Appeals officers feel that they cannot settle, so the issue goes on to offshore technical advisers. Then it ends up all or nothing. We need to give them guidance on settlement.

Tax law complexity has created opportunities for debate. The Code in its current state remains the number one problem facing both the Service and the taxpayers. Since most of our career has been with small and medium-sized business, I can talk specifically about the challenges in compliance.

Identity theft. Since many ID thefts were in Florida, I was also a victim. We should require all taxpayers to have PIN numbers. My information was stolen through e-services on a data dump, and that shouldn't happen. If we had all taxpayers with PINs, that wouldn't happen.

And, lastly, I think that I would like to recommend a separate task force that answers to you, Congress, to assist the National Taxpayer Advocate in developing change in the business structure and processes.

Thank you very much.

[The prepared statement of Mr. Shinn follows:]

WRITTEN
TESTIMONY OF
BYRON E. SHINN, CPA
MANAGING PARTNER, SHINN & COMPANY, LLC.
BEFORE THE
HOUSE WAYS AND MEANS COMMITTEE
SUBCOMMITTEE ON OVERSIGHT
REFORMING HOW THE IRS RESOLVES TAXPAYER DISPUTES
SEPTEMBER 13, 2017

INTRODUCTION

Chairman Buchanan, Ranking Member Lewis, and Members of the Subcommittee, thank you for the opportunity to discuss "Reforming How the IRS Resolves Taxpayer Disputes".

As the 2016-2017 recent past Chairman of the FICPA Federal Tax Committee and the Managing Partner of a successful Southwest, Florida CPA firm since 1993, this is a topic that I have been professionally engaged in for over 38 years. During this time, I have experienced the conversion from paper filings to e-filing and the start of e-services and then helped with establishing filters for protecting the innocent taxpayer who had their identity stolen. In fact, my identity was stolen through an illegal request through e-services of my data and a false return was filed and I received the very letter from the filter that prevented the "bad guy" from getting illegal funds from the US Treasury.

"Taxpayer Service First"

I have a unique perspective as I have been involved in oversight of the Florida CPAs for well over a decade and most practitioners work hard to get it right. It is the handful of marginal practitioners and aggressive taxpayers that try to push the envelope. These are the practitioners and taxpayers that need to be reviewed. As the National Taxpayer Advocate, Nina Olson spoke of in her May 2017 report that "98 percent of all revenue is paid timely and voluntarily. Less than two percent is collected through enforcement actions". I agree completely. I want to give you several recommendations for improvement of services that will help both the taxpayer and the Service. Remembering the mission of "Taxpayer Service First," I have collected several concerns from fellow CPAs and Tax attorneys that I have worked with over the years and have also included their thoughts.

Correspondence Audits –

Correspondence audits have been expanded in lieu of field examinations for many individual returns. These exams have a high probability of no change once the IRS receives the submitted response. Taxpayers' rights are being ignored by the issuance

of 15-day letters and then shortly thereafter the issuance of a 90-day letter (Notice of Deficiency), and thereby ignoring the 30-day letter, which grants the taxpayer the right to request an administrative appeals hearing. Taxpayers are put in a position where a large proposed assessment is assessed against them, which in many cases they do NOT owe. The evidence to support their position has been previously submitted, in most cases by certified mail, and although proof of delivery is furnished, the Service moves on with issuing the 90-day letter with no further adjustments to the erroneous proposed assessments. The taxpayer is then left with having to spend more time and fees for representation in Tax Court or docketed Appeals because of the lack of contact availability with an examiner to correct the issue at hand.

All taxpayers are entitled to a fair and impartial administrative appeal of most IRS decisions, including correspondence examinations; but, by not issuing the proper 30-day letter, the Service is violating the taxpayers' rights to request an administrative appeals hearing as afforded by the Taxpayer Bill of Rights.

Solutions-

1. Have a standard that exists that the process must be maintained and if the Service jumps over the process the Service losses the right to pursue additional revenue. Only the largest taxpayers can afford to take on the Service when faced with the incredibly complicated and expensive track to clear up the issues. "Fast track" is not being considered since the option is only available to a certain point. It appears the Service wants to quickly close open exams because management is tracking the time that exams are open versus review of the process they are not having a proper sign off of each step prior to issuing a Notice of Deficiency.

2. We should always maintain proper process to protect the taxpayer and the Service. Simplify the steps and REQUIRE "Fast Track" to prevent the circumstances that exists today.

Field Examinations –

The process has become VERY TAXPAYER UNFRIENDLY with a litigious and enforcement tone. Over my 38 years, we have reached a new low regarding respect for the taxpayer and their professionals. It is as if, the taxpayer is guilty and they have to prove the IRS wrong. The agents are doing several audits at the same time and they tend to start and stop during the audit. This prolongs the process and time spent increases while reducing flow of issues and discussions start and stop repeatedly. The IRS personnel are trying to do their job; however, the process is very strong handed, as shown with the various statements required to be signed and agreed to at the beginning of the exam process. An example is the new partnership exam rules that have brought the process to a state of total chaos.

Solutions-

1. Simplifying the process, stay on task while maintaining proper tone and protecting taxpayer rights is imperative.

Telephone Calls and Local Office Access –

Unfortunately, the wait times on phone calls are extraordinarily long for the taxpayer or their professional to get to the right person that can handle the particular issue. Overall my experience has been good once you get to that person. This shows how the Service needs to open up the process to handle the communications reasonably.

Solutions-

1. The Service should increase call center available hours (earlier, later and weekends) and adding additional personnel would improve service.
2. The Service had a very good e-service process and that was reduced due to "budget cuts". Please expand that immediately with proper authentication of taxpayer/professional.
3. The local offices used to allow walk ins and this is now abandoned to an appointment only policy. This is just not TAXPAYER FIRST. The taxpayers need to have reasonable access.

Foreign Disclosure Examination-

We are seeing a situation growing with the continued disclosure of foreign assets and bank accounts going to appeals and the appeals officers feel like they can't settle, so the issue goes to an offshore technical advisor. Then it ends up "all or nothing" with no leeway. This creates more controversy, time and resources.

Solution-

1. Allow flexibility to Appeal Officers with guidance on settlement opportunities.

Tax Law Complexity –

The tax code, in its current state, remains the number one problem facing both the IRS and taxpayers. The complexity of the code creates enormous administrative challenges for the IRS and imposes huge compliance burdens on taxpayers. With a simpler code, the job of the compliance by the taxpayer and the IRS would be far easier.

Since most of my career has been with small and medium size businesses, I can talk specifically about the challenges complying with the law and rules. According to the

Tax Policy Center, 93% of small businesses are organized as pass-through entities, which is what we primarily file for our clients. Knowing this then:

1. Why do Partnerships and S Corporations have different rules for calculating Tax Basis, and how Business Debt is treated differently for partners of a partnership versus the shareholder of an S corporation. If the shareholder/owner guarantees the debt and this then reduces available borrowings, should it be different?

2. If the losses are from real negative cash flow shouldn't they be allowed regardless of PASSIVE RULES?

What have we created? Have we created more complexity than really needs to be in place? Can't we just converge the best into one set of rules. Reality and practical considerations should flow to the integrity of the law.

Parts of the Law have created cottage industries for areas such as the Research & Development credit which has become excessively complex breeding specialty industries to assist business. Is this taxpayer first?

We could go on and on.

Online Accounts –

I strongly support providing online account access to taxpayers, but I believe the IRS should continue to fully staff other service channels such as telephone and face-to-face service for taxpayers who want or need to interact with the IRS through personal contact. The population of the United States is large and diverse in its taxpayer service needs, and a one-size-fits-all approach is not appropriate for a tax collection agency. Moreover, voluntary compliance and trust in the tax system are best promoted by person-to-person contact. Thus, a multi-faceted service strategy based on the needs and preferences of taxpayers is required

New Entity ID Numbers-

We have experienced recently a serious slowdown in the assignment of new Federal Identification Numbers which has taken numerous follow up calls and refaxing of the application forms with weeks involved to issue said number. This has held up opening of accounts at banks and closings on purchases of real estate to name a few examples. It appears that layered LLC entities is causing a slowdown or paralyzing effect on the system.

Solutions-

1. A review of the process and streamlining similar to trusts and estate numbers should be considered.

Identity Theft and Refund Fraud –

Since many ID theft victims were in Florida, and I was also a victim and chair of the FICPA subcommittee on ID theft, we should REQUIRE all taxpayers, business and individual, to have a PIN number for authentication of the e-filing and with any communications. Same as in banking.

I concur completely with National Taxpayer Advocate – Nina Olson – with her assessment and have quoted her below from her May 23, 2017 Report to Congress entitled "Hearing on IRS Oversight":

"Taxpayer Service: The IRS must be a "taxpayer service first" agency. In my most recent annual report, I expressed concern that the IRS historically has viewed itself first and foremost as an enforcement agency, and its emphasis on enforcement over taxpayer service is detrimental to both taxpayers and tax compliance. High-quality taxpayer service helps taxpayers voluntarily comply with their tax obligations and builds trust. Facilitating front-end compliance is much more cost-effective than collecting from noncompliant taxpayers one audit at a time. This is critical because more than 98 percent of all revenue the IRS collects is paid timely and voluntarily. Less than two percent is collected through enforcement actions. There is no doubt that enforcement plays an important role in deterring noncompliance. But today the IRS spends 43 percent of its budget on enforcement and less than six percent on taxpayer outreach and education activities… We can and should do better."

Solution-

1. We should REQUIRE all taxpayers, business and individual, to have a PIN number for authentication of the e-filing and with any communications.

Conclusion-

I recommend a separate taskforce that answers to Congress to assist the National Taxpayer Advocate in developing change in the business structure and processes being used.

Practical, and reasonable changes must be put at the forefront to protect taxpayer rights and help the IRS with oversight.

Thank you in advance for the opportunity to share my thoughts with you and with your leadership we will have a much-improved Tax System.

Chairman BUCHANAN. Thank you.
Ms. Wilson, you are recognized.

STATEMENT OF CHASTITY WILSON, PRINCIPAL, NATIONAL TAX OFFICE, CLIFTONLARSONALLEN LLP

Ms. WILSON. Chairman Buchanan, Ranking Member Lewis, and other Members of the Subcommittee, thank you for the opportunity to testify.

The AICPA applauds your efforts to address the importance of the IRS resolving taxpayer disputes in a timely, efficient, and cost-effective manner. Today, I would like to share our thoughts on refining the independence and efficiency within the IRS dispute resolution process.

I will also address the importance for the IRS to understand the taxpayer's perspective and deliver customer-focused service.

First, let's start with penalties. Upon receipt of an IRS notice, taxpayers or their representatives may determine a reporting error was made. However, if the taxpayer made the effort to comply with the reporting requirements, the taxpayer may request relief from penalties.

Frequently, the initial IRS response is a routine denial. This process is currently handled independently within each of the primary IRS divisions. We recommend that the IRS undertake a review of this process across the agency to identify necessary training to ensure a consistent and fair treatment of all taxpayer disputes.

Next, let's discuss Appeals. Appeals is the primary forum for taxpayers' disputes. Their mission is to resolve tax controversies without litigation on a fair and impartial basis. We appreciate them holding conferences which provide a meaningful and unique opportunity for taxpayers to present their positions.

In October of 2016, Appeals made several changes to its conference procedures, which arguably impact the ability or perception to independently and objectively help taxpayers. We recommend that, one, the IRS limit settlement conferences to the appropriate Appeals personnel; and two, they provide taxpayers with the option of a face-to-face conference.

In one settlement conference, the Appeals officer openly asked the Exam team what they thought was a fair settlement. My client asked, how is it possible for Appeals to maintain their independence when they are seeking the opinion of the same IRS employee who examined them?

Although, in reality, IRS employees may or may not have influence over the appeals process, it is hard to view them as objective when other IRS employees are involved. We suggest that, once the taxpayer's presentation to Appeals begins, they should limit the meeting participants to the appropriate Appeals personnel and the taxpayer.

In another Appeals case, payroll obligations were not met until my client discovered the error. The Appeals officer said it took him a whole 5 minutes to determine there was no reasonable cause and asked not to discuss it.

In this particular situation, a conversation, much less a face-to-face conference, was considered unnecessary from his perspective. However, from the client's perspective, he was not heard. He was

unfairly denied the right to present his case. While it is possible to resolve some issues over the telephone, we think it is important that taxpayers have the option of a face-to-face conference.

For larger tax disputes, cases are assigned a team of IRS Appeals officers and a case leader who is designated settlement authority. In these situations, we urge the IRS to provide truly independent settlement authority to these case leaders and eliminate the approval process that was recently added.

Finally, a customer-focused service approach should extend to all IRS services. It will help reduce disputes in the first place. For example, the IRS should create a new dedicated, executive-level practitioner services unit that would centralize and modernize its approach.

With a mindset of understanding the taxpayers' perspective, the Service will enhance voluntary compliance and increase the public's confidence in the integrity of the Service.

We appreciate the opportunity to testify. I will be happy to answer any questions.

[The prepared statement of Ms. Wilson follows:]



WRITTEN STATEMENT OF CHASTITY K. WILSON

ON BEHALF OF THE

THE AMERICAN INSTITUTE OF CERTIFIED PUBLIC ACCOUNTANTS

BEFORE

THE UNITED STATES HOUSE OF REPRESENTATIVES
COMMITTEE ON WAYS AND MEANS
SUBCOMMITTEE ON OVERSIGHT

HEARING ON

"IRS REFORM: RESOLVING TAXPAYER DISPUTES"

SEPTEMBER 13, 2017

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INTRODUCTION

Chairman Buchanan, Ranking Member Lewis, and Members of the House Subcommittee on Oversight, thank you for the opportunity to testify today. My name is Chastity Wilson. I am a principal in charge of dispute resolution services at CliftonLarsonAllen LLP and specialize in Internal Revenue Service (IRS or "Service") controversy matters. I am also the Vice Chair of the IRS Advocacy & Relations Committee of the American Institute of Certified Public Accountants (AICPA). I am pleased to testify today on behalf of the AICPA.

The AICPA is the world's largest member association representing the accounting profession with more than 418,000 members in 143 countries and a history of serving the public interest since 1887. Our members advise clients on federal, state, local and international tax matters and prepare income and other tax returns for millions of Americans. Our members provide services to individuals, not-for-profit organizations, small and medium-sized businesses, as well as America's largest businesses.

We applaud the leadership taken by the Subcommittee to address how the IRS can better serve the public through focusing on the taxpayer perspective and the need for the agency to resolve taxpayer disputes in a timely, efficient and cost-effective manner.

The IRS Office of Appeals ("Appeals") offers taxpayers a number of viable options to resolve a dispute (fast track settlements, early referral, fast track mediation, post appeals mediation, etc.). However, without an independent and customer-focused approach, the dispute process is intimidating, inefficient or ineffective for most taxpayers.

The AICPA is committed to improving the taxpayer and tax preparer experience when interacting with the IRS. Our testimony primarily focuses on recommendations to improve the independence and efficiency of the dispute resolution process. We also offer suggestions to ensure that the IRS understands the taxpayer perspective and delivers "customer-focused" service.

PENALTY DISPUTES

Upon receipt of an IRS notice, taxpayers and/or the taxpayer representative will review the agency's claim and sometimes agree that there was a reporting error and the taxpayer owes the tax and related interest. However, if the taxpayer made an effort to comply with the requirements of the law, but were unable to meet the tax obligations due to circumstances beyond their control, the taxpayer may qualify for penalty relief (reasonable cause, first time penalty abatement, and statutory exception).[1]

The initial and most-efficient process for resolving taxpayer penalty disputes begins with the taxpayer sending a letter requesting penalty relief providing details on facts and circumstances

[1] Internal Revenue Manual (IRM) 20.1.1, Introduction and Penalty Relief.

that prevented the taxpayer from meeting their tax obligations. Penalty disputes are currently handled independently within each of the primary IRS divisions (Wage & Investment, Large Business & International, Small Business/Self-Employed and Tax-Exempt & Government Entities).

The IRS needs to ensure independent and consistent settlement of penalty disputes. It has been our experience that there is no consistency across the IRS divisions on the application of the penalty relief provisions. There is also concern that the IRS personnel assigned to penalty notices often do not have the necessary training or expertise to review the taxpayer's submission for penalty relief.

Frequently, the initial IRS response to the taxpayer's request for penalty relief is to deny abatement without full consideration of the taxpayer's technical arguments or reasonable cause submission. From a taxpayer perspective, this practice is inefficient because the request for penalty relief is the first and certainly the most expedient opportunity to resolve a taxpayer's dispute. This routine denial of requests for penalty relief has forced an increased number of taxpayers to simply pay the tax and penalties they view as unwarranted, or seek Appeals' involvement, in order to resolve their tax penalty notices.

We recommend that Appeals' leadership undertake a review of the penalty notice processes with other IRS divisions to identify necessary training, systemic problems and duplication of efforts to ensure a consistent settlement process of penalties. The review should reduce the number of taxpayers having to pursue Appeals – providing a more-timely, efficient and cost-effective process – while ensuring taxpayers have the opportunity to present their case in a fair and independent manner.

IRS APPEALS

Appeals is the primary administrative dispute resolution forum for any taxpayer contesting an IRS compliance action. The mission of Appeals is to "resolve tax controversies, without litigation, on a basis which is fair and impartial to both the government and the taxpayer in a manner that will enhance voluntary compliance and public confidence in the integrity and efficiency of the Service."[2]

To resolve tax controversies, without litigation, Appeals holds conferences. Conferences provide a meaningful and unique opportunity for taxpayers to present their positions and allow Appeals officers to independently consider settlement proposals in order to resolve tax disputes. We appreciate the successful efforts of Appeals to settle the majority of the cases that come within its jurisdiction in this less formal and less costly manner, relative to litigation.

In October 2016, Appeals implemented several changes to its conference procedures through revisions to the Internal Revenue Manual (IRM) seeking to improve the quantitative and

[2] IRM 8.1.1.1, Accomplishing the Appeals Mission.

qualitative aspects of the Appeals results.[3] Although we appreciate the IRS's efforts to reevaluate their processes, we suggest considering whether such changes affect Appeals' ability to independently and objectively help taxpayers resolve tax disputes.

To prevent erosion of the core values of independence and impartiality with regards to the IRS dispute resolution process, the AICPA suggests that the Subcommittee consider the following key areas:

- Limit appeals conferences to Appeals personnel, the taxpayer and/or the taxpayer's representative;
- Offer taxpayers the option of face-to-face conferences; and
- Provide the Appeals Team Case Leader delegated settlement authority.

1. Limit Appeals Conferences to Appeals Personnel, the Taxpayer and/or the Taxpayer's Representative

For Appeals to effectively accomplish its mission, it has long been recognized that Appeals needs adequate insulation and independence from influence of other IRS functions during settlement conferences.[4] Appeals officers should independently evaluate the facts and law in each case while attempting to reach a fair and impartial settlement. Historically, the settlement conference participants were the Appeals officer and the taxpayer and/or the taxpayer's representative.

One significant change to the IRM involved the participation of other IRS employees in the Appeals settlement conference. Appeals now has the discretion to invite the IRS Office of Chief Counsel ("Counsel") and/or representatives of the IRS's Examination divisions ("Compliance") to the settlement conference.

Independence is essential in order for Appeals to operate in a fair and impartial manner. However, the perception of an Appeals officer's independence, and the fairness of the Appeals process, is diminished if the conference attendees include the IRS compliance employees who examined the tax returns (and likely the team's manager), IRS specialists who participated in the issues before Appeals (and likely each specialist's manager), and IRS Counsel who assisted the Compliance team (and likely Counsel's manager). Taxpayers are easily outnumbered and can feel pressured into conceding to the IRS's request. Alternatively, if taxpayers question the fairness of the Appeals process, they may prefer costly and burdensome litigation as opposed

[3] As revised in October 2016, IRM 8.6.1.4.4 states: "1) Appeals has the discretion to invite Counsel and/or Compliance to the conference. The prohibition against ex parte communications must not be violated. See Rev. Proc. 2012-18. Appeals may also request that other experts attend conferences. 2) See other IRM Part 8 sections for participation by IRS employees in cases under the Alternative Dispute Resolution (ADR) Program. This includes IRM 8.26.5.4.7, Participants, that reflects Appeals' discretion to have Counsel, the originating function, or both participate in a Post-Appeals Mediation proceeding for a Non-Collection Case."

[4] IRS Restructuring and Reform Act of 1998, section 1001(a)(4). The IRS Restructuring and Reform Act of 1998 directed "an independent appeals function within the IRS."

to reaching a settlement. Without independence or the perception of independence, Appeals becomes an adversary to the taxpayer.

In a recent settlement conference with my client, the Appeals personnel openly asked Compliance what they thought was a fair settlement before reaching a final decision. After the conference, the taxpayer asked how it was possible for Appeals to maintain independence when they were seeking the opinion of the Compliance team. Although in reality, IRS employees may or may not have influence over the Appeals process, it is hard to view Appeals as "objective, impartial, and neutral in fact as well as appearance" when Compliance and/or Counsel is intimately involved in the settlement decision. Without the perception of independence, the Appeals process is not nearly as effective as it has been in the past.

Appeals should establish a conference process that highlights its independence by drawing distinct lines between its interactions with other IRS functions. If necessary, Appeals could invite IRS Counsel or Compliance, along with other appropriate experts, to a preconference. However, once the taxpayer's presentation to Appeals begins, it is crucial to limit the meeting participants to the appropriate Appeals' personnel, the taxpayer and taxpayer representative.

2. Offer Taxpayers the Option of Face-To-Face Conferences

As mentioned earlier, to resolve tax controversies without litigation, the Appeals office holds conferences with taxpayers. Historically, if a taxpayer or the taxpayer's representative requested a face-to-face conference, Appeals would automatically transfer the case to the appropriate field office, except in limited situations. However, in October 2016, the Appeals function revised its rules transferring the decision to have a face-to face conference from the taxpayer to Appeals. While a taxpayer can request a face-to-face conference, it is only permitted if Appeals deems it is necessary.

In my most recent experience with a penalty Appeals case, I had a young entrepreneur client with no financial background or experience. He hired and relied on an internal accountant who was incompetent although she represented herself otherwise. Unfortunately, payroll tax obligations were not met for several quarters until the client discovered the error. The Appeals officer called me and said it took him a "whole five minutes" to determine there was no reasonable cause and asked me not to discuss reasonable cause because it was a waste of his time. He had once been a former business owner, and based upon that experience, he said that all taxpayers that open a business should have the capacity to manage payroll. In this particular situation, where the client hoped to discuss his facts of the case, a conversation, much less a face-to-face conference, was considered unnecessary from the Appeals officer's perspective. The client's confidence in the voluntary compliance system eroded. From his perspective, he was not heard. He was unfairly denied the right to present his case without prior judgement.

For many taxpayers, the first opportunity to meet someone and talk about their case is at Appeals. For example, in correspondence exams, the taxpayer most likely will never speak to the same individual twice while trying to resolve their issue. In these cases, Appeals is the first

opportunity they have to present their case and have a discussion about their particular situation. By limiting face-to-face conferences, taxpayers lose the sense that their tax positions and perspectives are considered impartially. While it is possible to resolve some issues over the telephone, it is important that taxpayers have the option of a face-to-face conference.

3. Provide the Appeals Team Case Leader Delegated Settlement Authority

For most significant tax disputes, where the cases are technically complex and generally include sizeable proposed adjustments, cases are assigned a team of IRS Appeals officers and an Appeals Team Case Leader ("case leader") who is delegated settlement authority.[5] The effectiveness of the Appeals process heavily relies on the case leaders' capacity to analyze the technical merits of the respective parties' positions and independently assess the hazards of litigation associated with the merits of each side's case. A case leader brings a unique value and quick settlement to some of the most significant issues that arise within our tax system.

However, an additional step was recently added to the process before a case leader can finalize a settlement. Due to concerns regarding the manner that Appeals resolved penalty cases, the Chief of Appeals recently decided that an Appeals Team Manager ("team manager") must review a case prior to a case leader finalizing a settlement.[6]

Unfortunately, this new requirement slows down the Appeals process and, from a tax practitioner perspective, has been detrimental to taxpayers. The new process generally results in an outcome that is less favorable to the taxpayer (since "reviewers" tend to only increase settlement amounts). Also, the additional review by a team manager can result in differences of opinion between the two government employees (the case leader and the team manager), which they must resolve internally before finalizing any agreement. As a result, taxpayers have reluctantly paid additional tax and penalty amounts to finally resolve the dispute or considered pursuing costly tax litigation.

Historically, case leaders' settlement authority has been exercised judiciously and in a manner consistent with Appeals' overall mission to resolve tax disputes without litigation. We encourage Appeals to provide truly independent delegated settlement authority to the case leader, and eliminate the extra approval process that was recently added, to ensure the taxpayers can resolve disputes in a fair and efficient manner.

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[5] See Delegation Order 8-8 (Formerly D.O.-66, Rev-15).

[6] Case leaders are delegated settlement authority directly from the IRS Commissioner to settle tax disputes. However, the Chief of Appeals recently initiated a review of Appeals team case leaders' settlement authority due to a Treasury Inspector General for Tax Administration (TIGTA) report that highlighted discrepancies in the manner that Appeals resolved penalty cases. It was noted that the Appeals personnel making the initial decision on penalty disputes generally are less experienced than case leaders and without delegated settlement authority. Regardless, the Chief of Appeals determined that a team manager must review a case prior to the case leader finalizing a settlement.

"CUSTOMER-FOCUSED" SERVICE

It is essential that the IRS take into consideration the needs of tax practitioners and un-represented taxpayers especially when dealing with compliance responsibilities. A customer-focused service approach will help reduce disputes in the first place by ensuring taxpayers that the IRS has given full consideration to their technical arguments. Furthermore, a customer-focused service approach should extend beyond the dispute resolution process and to all interactions with taxpayers and tax preparers.[7] With a mindset of understanding the taxpayer perspective, the Service will enhance voluntary compliance and increase the public confidence in the integrity of the Service.

1. IRS Taxpayer Service

Congress and the administration should determine the appropriate level of service desired and needed by taxpayers. Agreed upon measures of success are necessary to improve both customer service and voluntary compliance.

To instill trust in the tax administration system, we recommend taxpayer service goals based on the following two guiding principles:

- The IRS should only initiate contact with a taxpayer if the IRS is prepared and able to devote the resources necessary for a proper and timely resolution of the matter.
- Customer satisfaction must be a goal in every interaction the IRS has with taxpayers, including enforcement actions. Taxpayers expect quality service in all interactions with the IRS, including taxpayer assistance, filing tax returns, paying taxes, and examination and collection actions.[8]

2. New Dedicated Tax Practitioners Services Unit

The IRS should create a new dedicated "executive-level" practitioner services unit that would centralize and modernize its approach to all practitioners. Over time, the IRS has established a number of functional departments. These individuals are dispersed across the IRS and are not coordinated in a way that enables practitioners to timely access critical information (such as, their clients' account status or the availability of dispute resolution opportunities). Nor do the current teams or processes systematically solicit, gather or evaluate practitioner feedback. Enhancing the relationship between the IRS and practitioners would benefit both the IRS and the millions of taxpayers served by the practitioner community.

A dedicated practitioner services unit would allow the IRS to rationalize, enhance, and place under common management the many current, disparate practitioner-impacting programs,

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[7] See AICPA comment letter, "Ensuring a Modern-Functioning IRS for the 21st Century," April 3, 2017.
[8] Verbatim quote of the two guiding principles, The National Commission of Restructuring the Internal Revenue Service, *A Vision for a New IRS, Report of the National Commission on Restructuring the Internal Revenue Service*, page 23, June 25, 1997.

processes, and tools. Moreover, by centralizing these programs, IRS employees would have a consolidated approach to timely resolving issues. This coordination and improved access of information would prevent unnecessary delays and inefficiencies (such as, requiring practitioners to submit the same information multiple times to multiple IRS employees). Finally, to ensure success of the practitioner services unit, it is essential for these services to approximate comparable private sector services and allow practitioners to resolve account issues for their clients in a timely and efficient manner.

Online tax professional account. The IRS should provide tax practitioners with a tax professional account as part of the IRS's online portal with account access to all of their clients' information (both individual and business accounts) where the practitioner has a valid power of attorney (POA) on file. Additionally, the secure tax professional account should allow the IRS to communicate directly to practitioners the information necessary to improve taxpayer awareness and allow practitioner correspondence with timely acknowledgement of receipt.

Furthermore, a centralized login system allowing for single sign-on authentication of the practitioner and immediate access to all client data, as opposed to practitioner authentication before accessing each client's account, is an indispensable efficiency for the IRS and practitioners alike.

Secure platform. The development of the online portal should include a comprehensive, agile platform that protects users' identities and their data, detects threats and immediately responds to potential security breaches. In order to enhance taxpayer protection, practitioners who want access to taxpayer accounts should consent to guidelines such as Circular 230 or other similarly approved requirements. Professional tax practitioners can become particularly active and safe users of online services if the IRS invests early in providing a digital mechanism for POA and disclosure authorization and creates practitioner accounts *contemporaneously* with individual online accounts.

To continue to improve efficiency, we also recommend that the IRS focus its attention on replacing the Centralized Authorization File with a consolidated online solution utilizing electronic signatures and an algorithmic-driven approval process that is as close to real time as possible.

Robust practitioner hotlines. IRS should provide tax practitioners with a robust practitioner priority hotline (or hotlines) with higher-skilled employees. These employees should have the experience and training to understand and address more complex technical and procedural issues. This expertise would allow the IRS to focus its training to a particular technical area allowing designated employees to resemble its counterparts in the private sector. The IRS should also consider hiring experienced people such as graduate students or retired practitioners seeking part-time or seasonal employment.

Designated customer service representatives. Under the practitioner services unit, the IRS should assign customer service representatives (also known as a single point of contact) to each

geographic area to address unusual or complex issues that practitioners were unable to resolve through the priority hotlines. We recommend allocating the number of representatives based on the number of practitioners in a specific geographic area.

CONCLUDING REMARKS

The dispute resolution function is a critical component in the IRS's ability to fulfill its mission and for taxpayers to properly comply with their filing obligations. The most efficient process for resolving disputes involves the initial request for penalty relief from taxpayers. The IRS should undertake a review of this process across the agency to identify necessary training, systemic problems and duplication of efforts to ensure a consistent and fair treatment of all taxpayer disputes.

If a taxpayer must take additional steps to resolve its dispute through the Appeals process, it is crucial to (1) limit settlement conferences to the appropriate Appeals' personnel, the taxpayer and taxpayer's representative and (2) provide taxpayers the option of a face-to-face conference. We would also urge the IRS to provide truly independent delegated settlement authority to the case leader, and eliminate the extra approval process that was recently added, to ensure the taxpayers can resolve disputes in a fair and efficient manner. The recent changes to the dispute resolution process jeopardize its customer-focused approach and their perception, or in some situations their assurance, of independence.

Furthermore, a customer-focused service approach should extend beyond the dispute resolution process and to all IRS taxpayer services, including a dedicated tax practitioner services unit. With a mindset of understanding the taxpayer perspective, the Service will enhance voluntary compliance and increase the public confidence in the integrity of the Service.

The AICPA appreciates this opportunity to testify and we urge this Subcommittee to consider our suggestions as Congress decides how to improve the dispute resolution process.

Chairman BUCHANAN. Thank you, all of you, for your excellent testimony.

I will now proceed to the question and answer session. In keeping with past precedent, I will hold my questions until the end.

I now recognize the gentleman from Michigan, Mr. Bishop.

Mr. BISHOP. Thank you, Mr. Chairman.

And thank you to the panel for your time and expertise. I appreciate it. Lots of questions. So little time.

Is it Ms. Petronchak? Pretty good? Close? Okay. Good. You indicated in your written testimony—I know you didn't have much time today, but you indicated in your written testimony that there were procedures in place by the IRS during an audit that would give larger businesses an advantage over smaller businesses, specifically having to do with transparency.

Can you elaborate on that? And can you tell us, is this something that the IRS is doing as a result of the Code, or is this an arbitrary kind of application of the rules?

Ms. PETRONCHAK. So, with regards to that, Congressman Bishop, in my testimony, in the Large Business and International Division, they have put out procedures in a publication and indicated that, when you are issuing information document requests to taxpayers, that you have a discussion. You identify what the issue is, and you talk about what documents you are going to request so that the taxpayer has an opportunity to have a discussion with the agent and say: Well, maybe I don't have those kinds of records; these might be more pertinent. But they understand what the IRS is looking at and where they plan on going with their examination.

In the Small Business Division, that just doesn't happen. What happens is you will get, you know, a letter saying, you are under exam. And then here is a 4-page document request with everything but the kitchen sink pretty much on the initial document request.

And then, instead of, as in Large Business Division, when that response is made to that document request, it is expected in Large Business that they would review that response and then have a discussion with the taxpayer to say, we think it is complete or it is not complete and it is an ongoing discussion.

In Small Business, you are more likely than not going to find out the results of their review at the end of an examination, which is way too late for a taxpayer to be understanding what issues are in dispute and even have the opportunity to use alternative dispute resolution.

Mr. BISHOP. Well, it begs a question then: Why are they treated differently? And, again, is this a result of the Code, or is this something that the IRS is doing independently at its discretion?

Ms. PETRONCHAK. Yes. Congressman Bishop, it is an administrative practice in the Large Business Division. So it is not required by Code. But certainly, although that procedure, you know, some would argue could be improved, it is a drastic change and different from that that is afforded to small and medium-sized businesses.

Mr. BISHOP. I still don't understand why. You all have done this before. Does anybody understand why small businesses are treated differently than large businesses in this area? It just seems like it is——

Ms. PETRONCHAK. I personally don't see a reason why they could not integrate some of those procedures into their examination practices. You know, having the discussion upfront meets the Taxpayer Bill of Rights to be informed and know what is going on, so I certainly don't see why it could not become a part of their work processes.

Mr. SEPP. I would agree that it should. Although, I would say that there has been some negative feedback, even from folks who have experienced audits in LB&I that the IDR requests are often poorly focused. So this might be a problem that is not only with small businesses but with the procedural latitude given to the IRS.

Mr. BISHOP. You indicated that the non-in-person exam or the Appeals Officer, is the expert for the IRS in the room with the examiner?

Ms. PETRONCHAK. So it is actually an Appeals meeting, and it is a telephone or they have moved to virtual conferences in some instances. The Appeals officer is in the room. They may have a technical specialist. And under the current rules, they could invite Exam to be on the phone as well. So that is a real concern, is that, well, who is on the phone. You have got so many parties. You don't know who is speaking, whose perspective are you hearing.

Mr. BISHOP. Is there a problem with ex parte communication in-house?

Ms. PETRONCHAK. That does not violate ex parte communications because the way ex parte works, if the taxpayer is invited to attend the conference where Exam or Compliance will be present, then it is not a violation of ex parte.

Mr. BISHOP. I get that in practice. In theory, you are 100 percent right. But in practice, it seems that that would be an absolute recurring problem.

Ms. PETRONCHAK. It could be.

Mr. BISHOP. And one other thing, if I might, Mr. Chair, is the appeal process de novo, or is it a continuing process—does your appeal take up all the evidence? Do they consider everything or only that which was considered in the previous review?

Ms. PETRONCHAK. So, in Appeals, they should be considering the information that was developed and presented to them by Exam as well as what the taxpayer submitted and then making an independent decision.

When they changed—I think Ms. Wilson referenced the IRM change—they said: We are not going to hear new facts, new evidence in Appeals. We are only going to rely on what is in the file to make our decision. So it should be exactly what is in front of them.

Mr. BISHOP. Thank you very much.

Thank you, Mr. Chair.

Chairman BUCHANAN. Thank you.

I now recognize the Ranking Member, Mr. Lewis, from Georgia.

Mr. LEWIS. Thank you very much, Mr. Chairman.

Ms. Wilson, thank you for being here today. I understand that you are the head of the national tax office at your firm. What type of issues are taxpayers trying to resolve when they come to your firm?

Ms. WILSON. Great question.

Mr. LEWIS. Small issues? Big issues? Global issues?

Ms. WILSON. That is the unique thing about our firm. I would say they run the gamut, so they are all the way from small $1,000 penalty issues up to very large exams. So, you know, we have a very unique client base, and we target mid-sized business, which by the nature of that, we have all range of issues that we see.

You know, recently, the significant issues I see are around penalties and penalties appeal. We have a lot of clients or clients in our base that, you know, have been onslaughted with information return penalties. And so we try to help them manage through that process.

Mr. LEWIS. In your experience, what are the biggest challenges you and your clients experience in resolving tax issues with the agency?

Ms. WILSON. That is a good question. You know, I think the largest issue is just being heard, making sure that you——

Mr. LEWIS. Do you have a hard time, a difficult time in sometimes just being heard, just getting a face-to-face meeting?

Ms. WILSON. Exactly. Exactly. And Appeals, as we discussed, as I discussed in my testimony, has dramatically changed that process. I have been doing this for many, many years where I focus just on IRS——

Mr. LEWIS. You haven't been doing it. You are too young to be doing it for many, many years, now.

Ms. WILSON. But, you know, face-to-face was the—that was the one time you got to sit down and face the IRS and really talk about the issues. And from a client's perspective, they felt like they were being heard because they sat across the table from that Appeals officer, and they could see them listening. They could see the head nodding.

And so, even if it didn't come in their favor, they felt like they were being heard. When you turn to these telephone conferences, which are now the standard practice, you know, you remove that.

And they question whether the Appeals officer—my clients do—are even listening, because you get to the end of the conference and—and I am not saying in every case, because a lot of times this process does work well. But in some cases, the client just walks away and says: I don't even think they were listening; in fact, I heard keystrokes on the computer, right.

And so, you know, I think, from the AICPA, that is one of our recommendations, is you really need to look at this new procedure. It is administrative. But you really need to look at it and say: What are we doing to taxpayers' services here? Are our taxpayers really feeling like they are being heard, because this is their last opportunity, Ranking Member? When they get to Appeals, their next option is litigation. And I can tell you, in my client base, 99 percent of them are not going to want to take it to litigation because, again, maybe the dollar amount isn't high enough, or they are just frightened by the whole concept of having to go to tax court.

Mr. LEWIS. Are you suggesting or recommending that we need to do more to humanize the IRS and not make it so distant, this unbelievable agency at someplace? How do we go about doing that? What are your recommendations? What are you suggesting?

Yes, Mr. Shinn.

Mr. SHINN. Ranking Member, that is why I got so choked up about doing it in person. You know, there are people that can afford to go to an enrolled agent or a CPA, but there are a lot of taxpayers out there that don't have that access. And having the opportunity to walk in and talk at the local agent office level is so important. And having that face-to-face humanizes the circumstances and the facts in the situation, and you actually feel what is going on.

Now, granted, we all understand that there are some States that don't even have an Appeal officer in them, and so Appeal officers have to come from out of State. So, like in Alabama and Mississippi, they are coming from out of State just to deal with it. So we have a staffing issue.

But having that conversation with the Appeals officer is a real opportunity to solve. And having the process, the process that you talked about with the small business audits, it is very much behind a dark curtain, and it is a very scary proposition.

When those taxpayers get those letters and those long, 4-page requests, it is intense and a very scary moment. And we don't get the chance, like with a large business audit, to have a face-to-face with the team.

And then, not being able to pick up the phone and call, we have situations where you will go on hold for over an hour, and it will be at the end of the day. And at 4:30, they will pick up the phone and put it back down again, and you restart the next day. That is not taxpayer-friendly.

Mr. LEWIS. Thank you.

Thank you, Mr. Chairman. I yield back.

Chairman BUCHANAN. Thank you.

The gentleman from Pennsylvania, Mr. Meehan, you are recognized.

Mr. MEEHAN. Thank you, Mr. Chairman.

And I thank each of the panelists for your service and dedication, because it is clear that you are here as voices for people who feel that they have—if they are not abiding by the rules, they wonder sometimes what is the technicality. They are not people who are out there deliberately trying to skirt the rules or beat the system.

There is a place for those who are deliberately recalcitrant, but so many of us are just caught in the melee. So I have some questions about trying to get your interpretations to make this a little better. It just seems so much of it is tied to a personal relationship, a sense that somebody is actually listening to me, and let's just resolve this thing while we are here.

I have a couple of questions. One had to do—and I think Mr. Shinn, it was you who was saying that there were—or, Ms. Wilson, it was you, according to my notes—that there were recording errors, penalty situations where there would be appeals, and they were just getting to be routine noes.

Now, when I was a prosecutor and you had a case, you might do a declination or you would do a prosecution memo, but whenever there was a decision point, it was justified. Even though it was all internal in the—should we be requiring that if there is an original inquiry and there is a routine "no" set out, that there is a justification that you can know that somebody has actually analyzed the

file and has said that there is a reason why we are just saying no right now?

Ms. WILSON. I would absolutely agree with you that there should be a requirement to, you know, document what the justification for denial was. And, again, you know, there is many a time where we do get the denial, and it does appear somebody has reviewed it because they have put specific facts in there.

Mr. MEEHAN. But you are comfortable with that because at least you know you can counsel your client: Here is what it is——

Ms. WILSON. Exactly. But there have been instances where clearly it wasn't read because they articulated—you know the way—and maybe Ms. Petronchak can speak to this, but they will take paragraphs. They have got modelled paragraphs that they can pull from a system to do a notice to a specific taxpayer. And it has been obvious that they just pulled those paragraphs and are dumping them into this letter——

Mr. MEEHAN. Pro forma.

Ms. WILSON [continuing]. And it is very irrelevant to what was even discussed.

Mr. MEEHAN. So what is the effect on the taxpayer? It just draws it out even further. Have penalties and fines been waived during this period, or is there further accumulation during the period in time that you are appealing this process?

Ms. WILSON. So, yeah, interest continues to accrue while we are going through this process.

Mr. MEEHAN. So the clock is ticking against the person who is appealing?

Ms. WILSON. Yes. And so, you know, that is a discussion you have to have with your clients. But then, you know, there have been instances where, you know, your client will come to you and say: Do I pay now because, you know, I don't want to accrue all the interest?

But then there is a different process. You have to file a different form, the form 843, to make a refund claim, and it is a different process. And you will end up in the same place, but, you know, there are a lot of considerations to take in when you are counseling clients of what path to go down.

But, you know, back to your point, I think the impact it has on my clients is that we are built on a voluntary compliance system. And, you know, what I have seen in some of this penalty administration recently just is that clients become very discouraged because they truly thought they were being compliant. And then when they get this notice that looks like they weren't even really looked at, it can be very discouraging to them.

Now, the positive note I will say is that, once we get to the appeals process in the penalty arena, a lot of times we do have success there. But it is that routine—it just seems to be when you make your initial request, it is just the routine——

Mr. MEEHAN. Well, maybe you can—and that appeals process, because that would be presuming we get to that point where you actually have somebody and now you are talking—but I am intrigued by the concept.

I think, Mr. Shinn, you were talking about it where you believed that the presence of the examiner also at the appeal was creating

kind of a piling on, and yet I wonder to the extent that if you are actually trying to get to a resolution, should there be some capacity for the person that knows the facts to be able to present them to—I know that the IRS person is supposed to be independent, so to speak, but I would believe that if I was doing an appeal I would want to have at my availability the person who knows the record.

Mr. SHINN. My experience has been the Appeals officers are extremely experienced and knowledgeable on the issues and if they weren't, they would assign another person. And so they can come to their own conclusions based on the facts as presented that came up. That file is transferred. They get to see the file.

Mr. MEEHAN. The file, but you don't have the benefit—so just explain to me the difference. Why is it preferable not to have that person in the room who knows the record?

Well, maybe for another time. Maybe if you have a thought that you want to share with us in written testimony or otherwise, we would benefit from it. Thank you so much.

Chairman BUCHANAN. Ms. DelBene, you are recognized.

Ms. DELBENE. Thank you, Mr. Chair.

Thank you all for being here with us today.

Ms. Petronchak, I wanted to follow up on comments you made earlier when we were talking about the challenges that small businesses face and the inconsistency that we see for small businesses versus large businesses.

What do you think we should do to address these issues? What procedures would you like to see? Or do you have recommendations on what you think we could do that would work for small businesses?

Ms. PETRONCHAK. So some of the things could be implemented administratively. I think Pete had talked about the IDR process, and LB&I isn't perfect by any means. But those are things, from a quality perspective, within the Service, I think they could take a look at and decide that they want to change those processes for taxpayers and indicate that, gee, when we are developing the facts, it is important to put the human element on it and actually having a discussion with the taxpayer about the information.

And although that is not perfect and you will still have disagreements and still have contentious exams, it is an administrative process that could be implemented by rolling out new procedures for their agents in how they interact with taxpayers on a routine basis.

I mean, they are developing the facts. We have all spoken to the independence issue in Appeals. So that initial fact finding, that document request, is critical to a taxpayer feeling like they have had the opportunity to present their position and be heard by someone at the Service who is going to be open about what it is they are looking at and the treatment they are going to decide on a particular tax issue.

So I don't know that anything needs to be mandated, but the IRS, in looking at their procedures, could say—I was Commissioner of Small Business, and, yes, when I was there, back when I left in—was one of those things I could have looked at and said, gee, there are ways we could be interacting on a much better basis with

our taxpayers to make them feel better about the voluntary compliance system.

Ms. DELBENE. Thank you.

Mr. Sepp, it seems the current procedures for small business leave room for improvement, and I know you talked about that in your testimony as well.

You also pointed out in your testimony that larger businesses also have some challenges when it comes to the right to appeal. And I wondered if you could talk a little bit about your assessment of why organizations, like members of the CEETA coalition, are facing the challenges in dealing with the IRS that you outlined. What are some of those challenges, and why do you think those are happening?

Mr. SEPP. Sure. That is the Coalition for Effective and Efficient Tax Administration. It is a coalition not only of large business groups but taxpayer advocacy groups, because we are concerned that some of the trends, both in Small Business and Self-Employed Division toward audits but LB&I, are leaking across to each other, and we are going to have auditing procedures that are taking the worst elements in all divisions to be used against taxpayers across the spectrum.

Some of the problems we are facing: designating certain cases for litigation, where they might have precedential value even though there really isn't a clear connection to precedential value or large numbers of taxpayers who might be affected. There is the designated summons, which is a rather extraordinary IRS power for getting information out of uncooperative taxpayers that is being increasingly used in cases where the taxpayers really are being cooperative. And, of course, there is the use of third-party counsel to work auditing situations, not to advise but, rather, to do things that approach deposing witnesses.

But all of this really matters to taxpayers across the board, because, again, as everyone has testified here, there is on paper a directive to the Secretary to provide procedures for fair and independent audit appeals, but, in reality, it is just not happening. And I see this in case after case.

Even small business owners who are getting things like the 90-day letter, if they are lucky enough to ever have gotten a 30-day letter in the first place, they think it is a demand to pay tax. They don't even realize it is the revenue officer's report that would allow them to take an appeal to Tax Court. They don't even understand the basic nature of the process, because they are so intimidated by it.

And, again, this is why we support H.R. 3220 as a start of a package that could begin addressing these things.

Ms. DELBENE. Thank you very much.

I yield back, Mr. Chairman.

Chairman BUCHANAN. Thank you.

Mr. Holding, you are recognized.

Mr. HOLDING. Thank you, Mr. Chairman. Thanks for holding this hearing.

You know, obviously, we don't usually hear from our constituents' interactions with the IRS unless they are negative. And I ap-

preciate the Committee looking into ways to enhance this experience.

So I am just concerned about what I think is a new diversionary tactic being used by the IRS to keep taxpayers from accessing administrative appeals. So we all know that cases docketed in the Tax Court are typically transferred to Appeals for consideration—are not typically docketed unless they are designated for litigation. And it has come to my attention that the IRS may be restricting taxpayer access to appeals in some cases that are docketed in Tax Court.

And the case that I am aware of was not designated for litigation nor referred to Appeals, the two standard options for making an audit dispute. And, instead, the case was kept in a purgatory-type status, waiting for litigation, under the justification of "sound tax administration." I put that in quotes because that is the term they used. And that was the only option available. The only option available to the taxpayer was litigation.

So my question—and I am going to ask Mr. Sepp to respond first and then open it up to the panel: In your experience as a practitioner, have you or any of your clients experienced something analogous to this?

Mr. SEPP. I should state I am not a practitioner, but people in the small business community——

Mr. HOLDING. Right.

Mr. SEPP [continuing]. Other taxpayers have come to us, and there has been that sort of experience relayed to us. And there are other experiences, such as what are called speed-up situations, where a taxpayer may receive a notice of audit and requests for documents, and suddenly they will find in the mail yet another determination, and they haven't even had a chance to respond to the first one. And it is a way of intimidating the taxpayer into taking a position that is detrimental to them.

Mr. HOLDING. Mr. Shinn, you are nodding your head there.

Mr. SHINN. Yes, sir. We have seen this in a very similar fashion with foreign penalties on foreign reporting. And I mention it in my verbal and in my written response. We have seen it numerous times.

That is why I make the comment that they need to follow the rules or there needs to be a repercussion to the Service. You follow it, or you lose your opportunity. Somehow, we have to hold them accountable to the process. That is why you have a taxpayer bill of rights.

Mr. HOLDING. Ms. Petronchak?

Ms. PETRONCHAK. Congressman, I am not sure of all the specifics around it, but in the revenue procedure that addresses cases, so if a taxpayer filed a Tax Court petition, they generally can get their case heard by Appeals before they actually end up in Tax Court if they have not already been to Appeals. I don't remember the revenue procedure that covers it. So there is a provision.

However, you used a term that shows up in several of the revenue procedures: sound tax administration. I don't know what that means, but in regards to sound tax administration, they don't have to offer alternative dispute resolution, the fast-track process that I talked about in my testimony.

So I think sound tax administration is a way that they can choose to treat cases differently than what we would see should be the normal treatment of a taxpayer and how their case would move through the system. What the answer is to that I don't know, but I think the use of sound tax administration they are using as leeway to do many different things with a taxpayer's case.

Mr. HOLDING. Thank you.

Ms. Wilson, do you want to add anything to that in the final few seconds?

Ms. WILSON. No. I just want to 100 percent agree with her that, you know, she is spot-on on the issue. And that is why you see my head going back and forth violently, because I couldn't agree with her more on that issue.

Mr. HOLDING. Thank you.

Mr. Chairman, I yield back.

Chairman BUCHANAN. Thank you.

The gentleman from Oregon, Mr. Blumenauer, you are recognized.

Mr. BLUMENAUER. Thank you, Mr. Chairman.

I find the conversation fascinating, but in the backdrop of my experience, when I visit our local IRS offices and when I have meetings, which I do routinely with tax practitioners, tax attorneys, accountants, part of this strikes me that it would be easier to resolve some of this if the IRS was equipped to operate in a modern economy, if it didn't have a computer system that is so far out of date that they have to delve into the archives, find somebody encased in amber that can figure out FORTRAN programming.

I have meetings with people who work at the IRS and have them break into tears because they don't have any time to talk to people on the phone to be able to maybe help guide a little bit. There are people who don't fully understand the rules and regulations and the opportunities within the agency and the training budget.

I hear from both people in the agency and from the practitioners who, interestingly, are not hostile to the IRS; they are frustrated. They are frustrated that they tell clients, "You have a good point. We can work together. We can resolve it and get your $3,700 back. But it will cost you more to work with me to get it."

And I just wonder what you think is attributed to the fact that we have slashed the budget, slashed the workforce. Congress, each year that I have been here, makes the Tax Code more complicated. And, in some cases, it is a rush to be able to actually get the stuff out in time, and sometimes we miss the deadline.

So at what point is Congress complicit in this by not taking the largest tax-collecting system in the world, which relies heavily on voluntary compliance and treats our employees and our taxpayers with respect and put the resources behind it to make it a—any of you have any thoughts on that?

Mr. Shinn?

Mr. SHINN. Yes. In Sarasota, at our office there in Sarasota, Florida, the number of people in there, the whole area that was set for walk-ins is gone. The number of agents has been reduced. I will be the first one to stand up and say it is going to take more resources.

If we are going to stand here and say we are going to provide more appellate officers, that takes dollars. If we need more access through the internet and to broaden our e-services, which obviously we are all nodding our head, we need to use technology to give access. And in those phone calls, extending the hours, all that takes money. And that is why we are here today.

Mr. BLUMENAUER. But would that be helpful for some of these things——

Mr. SHINN. Absolutely.

Mr. BLUMENAUER [continuing]. If there were extended hours, if there were more people, if there was more training, a modern computer system?

Ms. PETRONCHAK. Sir, I would say additional funding would be useful. I mean, IRS can do some things administratively, but you mentioned training. I mean, I was Commissioner of the Small Business Unit in 2008. And for me to have adequate training for my revenue agents who do the exams and the collection officers who—the revenue officers who did collection, it was a really high-focused training for one of those groups each year, but I couldn't afford to have a real highly focused training for each of those groups, even back in 2008. So you can imagine.

Well, how this plays out in terms of taxpayers and practitioners, I mean, we feel like we are having to try to educate the revenue agent on the issues, because they can't get the training they need within the Service. And they are working issues on exams that they have never seen before, and so then they tend to go to somebody for advice. But you know how it is. You talk to three different people; how much gets translated as it goes down the line and really actually comes to form a final conclusion.

Mr. SEPP. I would also make a quick plea for funding in another area, the Volunteer Income Tax Assistance program and the low-income tax clinics.

Right now, I think eligibility for the LITC program is 250 percent of poverty level. That is about $60,000 for a household of four. That is not going to capture all that many small business clients, for example, who might desperately need assistance and could get it through a nonprofit organization like that.

Mr. BLUMENAUER. Great.

Thank you for your patience, Mr. Chairman. I just hope at some point, when passions cool, to look at how we treat our accounts receivable and being able to think through the resource, the training, the computer, that I hope shouldn't be politicized, but I think the evidence is that that will pay for itself many times over and relieve blood pressure medication.

Thank you.

Chairman BUCHANAN. I hear what you are saying. They said the computers, some of them are back from the seventies and eighties and sixties. I can't imagine that, but that is part of the testimony we had.

The gentlelady from Indiana, Mrs. Walorski.

Mrs. WALORSKI. Thanks, Mr. Chairman.

And thanks to the witnesses again for being here today and lending your expertise to us. I think this has just been a fascinating conversation. And it has been a conversation, listening to your ex-

pertise and to questions that we have, and the unanimous response that we all have. We are all kind of talking about all these same issues.

One of the rights enshrined in the Taxpayer Bill of Rights is the right to pay no more than the correct amount of tax.

Mr. Sepp, I was struck that less than 5 percent of small business taxpayers appeal their audit determinations and that a big reason for this is taxpayers believe it is cheaper to just give up and pay the IRS rather than appeal. That, to me, is incredibly disheartening. If a taxpayer thinks they are paying more in taxes than they should, you know, my advice is absolutely fight it. The tools are there to fight it. Instead, their perception seems to be that appealing it isn't worth the time or the money. We need to change that perception, as well as the actual time and money associated with appealing.

But I just wanted to address this to Mr. Sepp and Ms. Petronchak. You both discussed dispute resolution and options that would be less formal, lower cost for taxpayers. You also noted that the IRS has failed to expand its use of these fast-track dispute resolutions.

Ms. Petronchak, can you explain how these fast-track procedures work and how they assist taxpayers in resolving cases quickly?

And I am just going to tell you, my follow-up question to both of you, Mr. Sepp as well, is, is there a way that we in Congress can do something about that, or is it purely just IRS authority?

So I would just like to hear about the options and then, what can we do.

Ms. PETRONCHAK. So, in fast-track settlement, it is an option where, you know, I am being examined by the IRS and we know that I have a dispute over—let's just make it simple—travel expenses. So they have said what their position is; I have said what my position is. So the taxpayer and IRS can agree that a fast-track settlement, having the use of an appeals mediator while it is in Exam, would be beneficial to all parties to come to resolution on the issue.

So, getting to your earlier comments, it brings quicker resolution. The taxpayer is hoping to get this resolved at least cost so they don't have to go on to formal appeals, much less go to Tax Court, which not only is cost, but many small- and medium-size taxpayers don't want their laundry aired out in public court.

Mrs. WALORSKI. Oh, absolutely. Right.

Ms. PETRONCHAK. So, even though they may think they are right, they are not going to choose that as the venue to go to, because they don't want their neighbors talking about their issues with IRS.

And so fast track, you know, we used to see a lot of them; we don't see as many anymore. But the procedures I talked about that Small Business is using for their exams, when they wait to the end of the process to have a discussion, doesn't lend itself to having that alternative dispute resolution.

Mrs. WALORSKI. And what can we do about it, Mr. Sepp?

Mr. SEPP. Based on my limited study of other countries' practices and what the taxpayer advocate has said, there seem to be several problems.

One, we have to restore the independence of the ADR process. In almost every case, from Australia to U.K., Portugal, all around the world where ADR is much more common and hundreds of thousands of cases will get resolved this way, they have to keep the mediator or arbitrator function well-insulated away from the tax authority.

We may not be able to use private accredited mediators here, much in the way that it appears in the Small Business Taxpayer Bill of Rights that was introduced in the last Congress, but we could have a situation where there is an office of mediation with specially trained people, rather than plucking people from Appeals who have some training in mediation and arbitration. You could even house that bureau somewhere in the Treasury so that it has further independence.

The other important thing, I think, is to instruct the IRS where mediation and arbitration can be used. The agency will often exclude so-called campus collection cases and other types of matters for ADR from the start. And we have to resolve those kinds of issues as well.

Mrs. WALORSKI. I appreciate it.

Mr. Shinn, did you want to add anything quickly?

Mr. SHINN. Yes. And in response, that is why I think, especially in small business, that it needs to be a requirement of the steps, so that that way people aren't afraid of appeals; it is part of the process. The fast track is there and is part of the sign-off.

Mrs. WALORSKI. I appreciate it.

Thanks, Mr. Chairman. I yield back.

Chairman BUCHANAN. I want to thank everybody for the opportunity, but let me run through—and this will be a question to all of us. We are trying to simplify the dispute resolution, trying to improve on the process. And I want all of you to take a minute on that.

But before I do, I want to say a couple of things. I do agree, with big corporations—it doesn't mean that there is not work to be done in dispute resolution, but I have been in that world. And you have CFOs, you have plenty of cash, and you have to go to court, you go to court. You don't want to, but they have resources.

What I am concerned about personally is individuals. I read in USA Today 62 percent of Americans—I use this a lot, but it was stunning to me when I read it—don't have $1,000 in the bank. So if you get a letter from the IRS that you owe $2,000, where are you going to go resolve that? A CPA, accountant, that is going to be a couple, $3-, $4,000. You probably are going to just say you are better off to write a check or get on a payment plan, just agree with the IRS and move on.

Small businesses, a dispute resolution, if you ever think about going to court, you could be talking over $100,000, $50,000.

Did you say, Ms. Wilson, you are in a law firm?

Ms. WILSON. No.

Chairman BUCHANAN. Okay, a CPA firm. But you know, when you hand it off to the tax lawyer, you are talking big money. And usually you just cave and say, you know, let's go make the best deal and get down the road. That has happened to me and others, I have heard of it, where they don't think they owe the money, but

at the end of the day, the $10- or $20,000, the $5,000, the $30,000, it costs you more with accountants and lawyers to go try to resolve it.

So the question I have for the individual taxpayer, the 62 percent who don't have $1,000 in the bank, how do we simplify this dispute resolution where people can have their day in court but it doesn't take six months, a year? Because, as that meter is running, there is no way you can afford to go to court or, you know, arbitration or work with someone to try to resolve that.

Mr. Shinn, I will give you the first opportunity from that standpoint. And I know you have dealt with that. But that is just my sentiment. That is what I have heard over the years.

Mr. SHINN. That is why I said we have to have the opportunity to have access through phone calls and walk-ins. And, also, when the taxpayer doesn't follow the deadlines, there are repercussions. When the IRS doesn't follow their protocol, there needs to be repercussions, because, to the taxpayer, it is hard and fast.

So I can give you one quick analogy that really struck me, is I helped an employee, a 90-year-old person of color who could not write. He was a night watchman at a packing house, worked several years there. Prior to that, he worked at another packing house, where they treated him as an independent contractor. And he got billed. And he didn't know what to do. It went all the way to collections, and they garnished his wages. He ended up with pancreatic cancer, and the employer asked me to step in.

I tried to get the collection officer to settle, and the employer was going to settle. They wouldn't take a dime less, and he passed away 2½ weeks later. I called that collection officer, I sent him a copy of a death certificate, and I said, that isn't in the taxpayer's best interest.

And that is what we are dealing with, and it is so sad.

Chairman BUCHANAN. Yeah.

Ms. Wilson?

Ms. WILSON. You know, I now work at an accounting firm, but I was a local taxpayer advocate and worked with Nina Olson. So, you know, this is near and dear to my heart, as exactly what you are talking about, Chairman Buchanan, in the sense that——

Chairman BUCHANAN. Let me just say with you and all, we are looking to do IRS reform, and this is one of the biggest areas. I think we have to find a way that people can get these disputes settled. So that is what we are looking for.

But go ahead.

Ms. WILSON. Yeah. And I think we need to simplify the process. I think it is intimidating, and I think, because it is intimidating, taxpayers feel that the only way they are going to resolve it and win is if they engage help. And, as your point, most taxpayers don't even have $1,000 in their account.

So I think, you know, that we need to find a way to simplify the process. We need to find a way to make it less intimidating for the taxpayers. And we need to focus on that bill of rights that says you shouldn't have to pay more tax than you actually owe.

Chairman BUCHANAN. Mr. Sepp?

Mr. SEPP. We have to find a way to institutionalize alternative dispute resolution mechanisms. We have got to learn from the ex-

periences in other countries, where millions of individuals have utilized the process, making it less formal but more actionable, with fewer delays, applying to a larger number of cases, with a more independent arbiter involved.

If we do those things—and H.R. 1828 from the last Congress is only a starting point for this—if we do that, I think we will dramatically increase the access to justice that taxpayers need.

Add to that things like the Low Income Taxpayer Clinics, add to that more resources for the Taxpayer Advocate's Office, and you have the beginning of a core of principles that will get to this point of giving taxpayers the justice that they need. And they still need it.

Chairman BUCHANAN. You get the last word.

Ms. PETRONCHAK. Okay, Chairman.

So fast-track settlement, I agree, should be available for all taxpayers. Just to give a little history, Large Business and International developed this process 2002, 2003, but it didn't become final and actually institutionalized for small business and self-employed taxpayers until 2015.

Chairman BUCHANAN. Yeah.

Ms. PETRONCHAK. So when I commented on a couple processes I think could make things more transparent and easy for taxpayers, there are some things that they have there.

Now, fast track isn't the answer to everything, because you may have reluctant IRS folks to use it. Pete mentioned, you know—I in my written testimony mentioned outside mediator or taxpayer. To them, hiring an outside mediator for $1,000, $1,500 is cheaper than taking this on to Appeals or Tax Court. I hadn't thought about the concept of a mediator group, you know, somewhere in Treasury or somewhere that serves as an independent mediator——

Chairman BUCHANAN. The problem is, if you owe $2,500 or $2,000, you can't pay $1,500, because you just say——

Ms. PETRONCHAK. Right.

Chairman BUCHANAN [continuing]. You know, I am going to go ahead and just write the check or figure out a way to write it.

Go ahead.

Ms. PETRONCHAK. But, again, you know, IRS hasn't shown that they are extremely interested in this alternative dispute resolution. I would caution against saying, well, we mandate you to use alternative dispute resolution, because if they don't come to the table willing to settle and fast track, the taxpayer and IRS have to agree, or they just walk away and the taxpayer still has their appeal rights.

So, somehow, I mean, maybe looking at some of the other systems, come up with, well, what is the happy medium here and how this could be changed. It is there; taxpayers would love to use it. Individual taxpayers need to be able to use it, which—now it is available really to businesses, small and large. But it needs to be expanded and made available and at least cost and be successful once it is used.

Chairman BUCHANAN. Well, I would appreciate for all of you to get your thoughts and your ideas to our Committee. We want to work together, the Ranking Member and myself, on a bipartisan basis, because this is an important issue.

And I have been in that world where larger organizations have the resources. I am concerned about the person that gets a $1,000, $1,500, $2,000 small business or individual tax bill. How do we resolve that without putting them into bankruptcy or putting them in a bad situation?

I agree with you—a lot of times you get that notice through the IRS. I have gotten more than my fair share; a lot of us have. You know, it is frightening to a lot of people. And this is an area we need to work on and get your thoughts and your ideas.

So, in closing, I would like to thank our witnesses for appearing before us today.

Please be advised that Members have two weeks to submit written questions to be answered later in writing. Those questions and your answers will be made part of the formal hearing record.

With that, the Subcommittee stands adjourned.

[Whereupon, at 3:24 p.m., the Subcommittee was adjourned.]

[Public Submissions for the Record Follows:]

CEETA Coalition for Effective and Efficient Tax Administration

STATEMENT OF
THE COALITION FOR EFFECTIVE AND EFFICIENT TAX ADMINISTRATION
TO
OVERSIGHT SUBCOMMITTEE OF
THE COMMITTEE ON WAYS AND MEANS
UNITED STATES HOUSE OF REPRESENTATIVES
HEARING ON
REFORMING HOW THE IRS RESOLVES TAXPAYER DISPUTES
SEPTEMBER 13, 2017

On behalf of the Coalition for Effective & Efficient Tax Administration ("CEETA"), we respectively submit this statement providing our perspective and recommendations with respect to Treasury regulations and Internal Revenue Service (the "IRS" or "Service") guidance and procedures for the resolution of disputes with taxpayers. We have provided a list of particular regulations and guidance that we believe require the immediate attention of Congress, the Department of the Treasury ("Treasury"), and the Service, as these items test the Service's adherence to its mission of fairness in the enforcement of Federal tax laws.

Additionally, in this statement, CEETA offers its public support for H.R. 3220, *Preserving Taxpayers' Rights Act*, a bipartisan bill introduced on July 13, 2017, by Representatives Jason Smith and Terri Sewell and referred to the Committee on Ways and Means. Enactment of H.R. 3220 will directly address certain concerns with current IRS overreach resulting in unnecessary disputes with taxpayers which is inefficient, time consuming, and expensive for taxpayers and the IRS.

CEETA is a coalition of companies and trade associations that seeks to effect constructive administrative and legislative changes to ineffective and inefficient IRS practices and procedures.[1] CEETA thanks the Committee on Ways and Means Oversight Subcommittee for the opportunity to submit this statement and expresses hope in a continued dialogue within the Subcommittee, and Committee generally.

[1] The coalition of business organizations comprised of: ACT | The App Association; Americans for Tax Reform; Citizens Against Government Waste; Financial Executives International; Information Technology Industry Council; National Association of Manufacturers; National Foreign Trade Council; Retail Industry Leaders Association; Small Business & Entrepreneurship Council; Software Finance and Tax Executives Council; TechNet; and U.S. Chamber of Commerce.

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Revenue Procedure 2016-22

Revenue Procedure (Rev. Proc.) 2016-22 generally provides a description of the administrative appeals process, within the IRS Office of Appeals, for cases docketed in the U.S. Tax Court. CEETA's concern with this revenue procedure is particular to Section 3.03, which provides:

- Chief Counsel will not refer to Appeals any docketed case or issue if IRS Division Counsel or a "higher level of Counsel official" determines that referral is not in the interest of "sound tax administration."

CEETA opposes any general IRS authority to deny a taxpayer the right to administrative resolution of disputes before the Office of Appeals. A taxpayer's right to an independent administrative review of examination results in the Office of Appeals is vital to efficient tax administration. Both taxpayers and the IRS alike seek to achieve mutually agreeable resolution of tax issues in Appeals thereby avoiding litigation. Resolution in Appeals conserves finances, resources, and time of taxpayers, the IRS, and the Federal judiciary. In recent years, use of broad IRS discretion has resulted in heightened Congressional oversight, ultimately weakening taxpayer trust in the agency and calling into question the integrity of the tax administration process. Such broad discretion to deny appeal rights is neither in the interest of the taxpayer nor the IRS. If any limitations were to be placed on a taxpayer's right to Appeals, the limitations should be particular and narrowly defined, preferably by statute (see below discussion of H.R. 3220). Allowing Counsel the unilateral authority to deny a taxpayer a right to Appeals in the interest of "sound tax administration," a wholly undefined and amorphous term, provides Counsel with any imaginable basis to deny a taxpayer a right to Appeals and force litigation, at the expense of all parties.

In past communications with the IRS and Treasury, CEETA recommended the deletion of Section 3.03 of Rev. Proc. 2016-22 and continues to maintain that recommendation.

Treasury Decision 9778 (I.R.C. § 7602)

On July 14, 2016, the IRS and Treasury finalized regulations under I.R.C. § 7602 that clarify that persons described in I.R.C. § 6103(n) and Treas. Reg. § 301.6103(n)-1(a) with whom the IRS or IRS Chief Counsel contracts for services (such as outside economists, engineers, consultants, or attorneys) may receive books, papers, records, or other data summoned by the IRS. Additionally, the final regulations provide that such contractors may, in the presence of an IRS officer or employee, participate fully in the interview of a person the IRS has summoned as a witness to provide testimony under oath.

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CEETA Coalition for Effective and Efficient Tax Administration

In a letter dated May 5, 2016, addressed to the IRS, CEETA respectfully requested that the proposed and temporary regulations (T.D. 9669) issued under section 7602 be withdrawn. CEETA maintains this position. CEETA believes the final regulations fall short on both policy and procedural grounds, thereby failing to promote a more effective and efficient tax administration. These regulations delegate, outside statutory allowance, inherently governmental functions to private contractors. Allowing contractors to fully participate in summons interviews and receive documents will result inevitably in deferring control of an examination to outside contractors. Undoubtedly, the regulations will lead to longer, more contentious, and less efficient examinations.

Accordingly, CEETA recommends the withdrawal of these regulations.

Senator Orrin G. Hatch, Chairman of the Senate Committee on Finance, expressed similar concerns when the IRS previously hired a private law firm to assist in the income tax examination of a corporate taxpayer. In a May 13, 2015, letter to IRS Commissioner John Koskinen, Chairman Hatch noted that the hiring of the private law firm to participate in the examination (1) appeared to violate Federal law and the express will of the Congress, (2) removed taxpayer protections by allowing the performance of inherently governmental functions by private contractors, and (3) called into question the IRS's use of its limited resources.

Retaining outside lawyers to conduct audits of private taxpayers is unprecedented in the history of the Service. At least one court has stated that it is "troubled" by the practice, noting, "[t]he idea that the IRS can 'farm out' legal assistance to a private law firm is by no means established by prior practice, and this case may lead to further scrutiny by Congress."

H.R. 3220, *Preserving Taxpayers' Rights Acts*

CEETA enthusiastically supports the enactment of H.R. 3220 as a step forward in ensuring efficiency and fairness in the Service's administrative procedures, as the bill directly addresses CEETA's concerns stated with Rev. Proc. 2016-22 and T.D. 9778, and more.

The bill would codify a taxpayer's right to an administrative appeal before the Office of Appeals and limit such right only in particular instances defined within the statute; there would no longer be any discretion for the Service to deny a taxpayer the right to an appeal on the grounds of "sound tax administration." Additionally, the bill appropriately, and statutorily,

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limits the Service's ability to "designate cases for litigation," an authority which allows the Service to deny a taxpayer administrative appeal rights.

The bill also modifies the Service's authority to issue "designated summons." A designated summons issued under I.R.C. § 6503(j) unilaterally suspends the period of limitations on assessment under I.R.C. § 6501, thereby lifting a very crucial protection to taxpayers. Periods of limitations are a cornerstone of statutory law at the Federal and state level. Periods of limitations ensure that the Service, and taxpayers alike, do not indefinitely sit on potential claims; either the Service or taxpayer must act within the statutory period or have the potential claim legally closed to further action. As the suspension of section 6501 is a serious consequence of the Service issuing a designated summons, H.R. 3220 establishes an additional check against this authority. The bill provides that it must be clearly established that the taxpayer "did not reasonably cooperate with reasonable requests by the Secretary for witnesses, documents, meetings, and interviews...." This requirement does not currently exist in section 6503(j). This is a well drafted addition to the authority of the Service to issue a designated summons.

Finally, H.R. 3220 amends I.R.C. § 7602 to expressly nullify the final regulations of T.D. 9778. The bill would amend section 7602 to prevent any person, other than an officer or employee of the IRS or for the sole purpose of serving as an expert, to receive any books, papers, records, or other data obtained in an examination. CEETA commends the drafters of H.R. 3220 for recognizing the final regulations of T.D. 9778 delegated inherently governmental functions to private contractors, and correcting the Service's and Treasury's overreach in issuing the regulations.

Publication of IRS Notices Asserting Future Regulations

Although not specific to dispute resolution procedures amongst the IRS and taxpayers, CEETA requests the Subcommittee consider the following scenario and consider necessary review and oversight.

There have been several recent occasions where the IRS has issued "Notice" guidance which provides that the Service and Treasury "expect" to issue regulations that incorporate the guidance or asserts that the Agency "will amend" existing regulations to incorporate the guidance. See, e.g., Notice 2016-73; Notice 2012-15; Notice 2012-39; Notice 2014-32. In the case of the Notices cited, despite the passage of time - in some cases several years - the regulations have not been issued. The result has been that taxpayers have been obligated to

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follow the Notice guidance as if it were regulatory law, despite the lack of Administrative Procedure Act compliance in the Notice issuance and lack of the clarity formal regulations would provide. See I.R.C. § 7805(b)(1)(C). The Notices oftentimes have an interrorem effect and bring attendant uncertainty. CEETA views this practice, whether intentional or unintentional, as circumvention of the requirements of the Administrative Procedure Act.

Conclusion

Thank you in advance for your consideration of the above matters. CEETA is happy to participate in any further discussions concerning the above-listed issues or more generally the procedures for resolving disputes between the IRS and taxpayers to minimize unnecessary litigation which is inefficient, time consuming, and expensive for taxpayers and the IRS. Please contact one of the following:

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Fitzgerald Kit Trucks & Sales LLC

Statement for the Record

"IRS Reform: Resolving Taxpayer Disputes"

Committee on Ways and Means

Subcommittee on Oversight

United States House of Representatives

September 18, 2017

Fitzgerald Kit Trucks & Sales LLC
Statement for the Record
"IRS Reform: Resolving Taxpayer Disputes"
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September 18, 2017

Fitzgerald Kit Trucks & Sales LLC ("Fitzgerald") commends the Subcommittee for holding this hearing on reforming the Internal Revenue Service ("IRS") to improve the tax dispute resolution process. Fitzgerald, is a family-owned business my brother and I started in 1989. For almost thirty years, the company has been repairing worn or wrecked tractors with glider kits and selling the repaired tractors to the public. Fitzgerald is now the largest glider assembler in the country.

While other businesses were shuttering their operations in the Upper Cumberland Region of Tennessee and Southern Kentucky, Fitzgerald was buying former manufacturing facilities and expanding its glider business. Fitzgerald has created a lot of good-paying jobs in economically challenged areas. Fitzgerald now employs in excess of 400 workers in its glider business and is responsible for thousands of other jobs at parts suppliers and other vendors who serve Fitzgerald's business.

Fitzgerald has been the subject of six IRS examinations over the last two decades, each of which turn on the same excise tax issue. For five consecutive examinations, that issue was resolved favorably for Fitzgerald by either the IRS Examination Division ("Exam") or the IRS Appeals Division ("Appeals"). On those five occasions, Exam and Appeals operated as independent functions of the IRS and the tax dispute resolution process worked as intended.

Sadly, Fitzgerald is once again in the IRS's crosshairs, only this time the process has utterly failed us. The IRS's sixth examination was like the five that preceded it and involved the same issue. Despite a post-appeals mediation in which Appeals fully conceded the excise tax issue in Fitzgerald's favor, Appeals has now backed out of the proposed resolution because ***Exam*** objected to it—a classic case of the tail wagging the dog. As a result, the IRS has assessed approximately $70 million of tax, penalties, and interest against Fitzgerald.

The IRS's conduct in our case is egregious and it should alarm Congress. Independence is essential in order for Appeals to operate in a fair and impartial manner and for the tax dispute resolution process to function properly. Indeed, the mandate of Congress in the Internal Revenue Service Restructuring and Reform Act of 1998, Pub. L. No. 105-206, 112 Stat. 685 (the "1998 RRA"), was to ensure an independent appeals function and prohibit ex parte communications between appeals officers and other IRS employees. It is important to highlight that in Fitzgerald's case the interaction between Appeals and Exam occurred not before the preconference, but after Fitzgerald and Appeals had reached a proposed resolution. How can small businesses like Fitzgerald feel confident that Appeals is operating independently and objectively when Exam can so freely override Appeals?

Fitzgerald now faces grave uncertainty. Exam's objection imperils 400 direct assembly jobs and thousands of indirect jobs. The specific excise tax issue is also much bigger than just Fitzgerald. More broadly, the IRS's actions are jeopardizing 15,000 to 20,000 jobs in the glider segment of the trucking industry.

The IRS is forcing Fitzgerald to litigate this matter. This bullying tactic and failure of impartiality runs headlong into the mission statement of Appeals, which seeks to resolve tax controversies without litigation on a basis which is ***fair*** and ***impartial*** to both the government and the taxpayer, and the 1998 RRA. The IRS's subjective policies and procedures must be corrected for the betterment of all taxpayers. No one should feel intimidated or forced into certain action because of a failure in the tax dispute resolution process.

I applaud the leadership of this Subcommittee for investigating and hearing from witnesses about the significant consequences such collusion can have on taxpayers. I am hopeful this discussion and inquiry into resolving taxpayer disputes will continue and I would welcome the opportunity to share Fitzgerald's personal story to the committee. We appreciate any assistance you may be able to offer in this matter. If you have any questions or need any background materials, please contact Jon Toomey at (202) 999-8880.

Sincerely,

Tommy C. Fitzgerald
President and Founder
Fitzgerald Kit Trucks & Sales LLC

cc: Congressman Diane Black

Attachment: Taxpayer Confidentiality Disclosure Waiver

Taxpayer Confidentiality Disclosure Waiver

In conjunction with attached letter, Fitzgerald Kit Trucks & Sales LLC, EIN 62-1811834, 752 Interstate Lane, Crossville, TN 38571, hereby authorizes and consents to disclosure under section 6103(c) to any member or any member's staff of the House Committee on Ways and Means, the Senate Committee on Finance, and any member of Congress copied on the attached letter to all tax return information pertaining to federal excise taxes (Form 720) and any related penalties for all quarters for the years including 1991 through 2016 tax years.

Tommy C. Fitzgerald
President and Founder
Fitzgerald Kit Trucks & Sales LLC

Submission by John Klotsche

House of Representatives
Committee on Ways and Means
Subcommittee on Oversight
Hearing on Resolving Taxpayer Disputes
1100 Longworth House Office Building
September 13, 2017
Room 1000, 2:00 pm EDT

I ask the House Ways and Means Oversight Committee to consider the proposal described below as a comprehensive administrative tool to resolve taxpayer disputes with the IRS.

The idea is a call to the IRS to do what Congress told it to do many years ago: import best Alternative Dispute Resolution practices from the commercial world to 1111 Constitution Avenue. The Agency has barely paid lip service to that mandate, and its efforts have failed to provide taxpayers embroiled in tax controversies with impartial, expeditious and cost effective tools to resolve their disputes.

Why not incorporate at the IRS proven Alternative Dispute Resolution principles and practices widely and effectively used in the commercial world and at other federal agencies? ADR has for more than 40 years been the tool of choice to resolve commercial disputes and there is no reason why it wouldn't be equally effective in the tax world. This proposal envisions the IRS seriously implementing the 19-year-old Congressional mandate to overhaul and modernize its dispute resolution system.

Congress in the 1998 Taxpayer Bill of Rights (*aka* Internal Revenue Service Revenue and Restructuring Act of 1998) instructed the IRS to develop mediation and arbitration procedures. Over the years, the Agency has cobbled together an *á la carte* menu of ADR programs – for which taxpayers have little appetite. During 2015, 113,870 cases got resolved at the IRS' Appeals Division; yet a paltry 99 taxpayer disputes were wrapped up using an ADR procedure. At the audit stage, only a scant 266 out of hundreds of thousands of disputed cases used an ADR program.

There are two reasons ADR hasn't caught on at the IRS. First, the Agency hasn't shown a serious commitment to ADR principles – its enforcement culture clings to the vintage, outdated model of timeless two-party adversarial negotiations. Second, its ADR offerings are conceptually flawed, so taxpayers find them unattractive and not compelling. Case in point: The Agency's faulty premise that its main dispute resolution arm, IRS Appeals, can truly function "independently" when the Appeals "neutral" is on the IRS payroll. Couple that with an exam team (who propose the tax liabilities) and IRS chief counsel (who litigate them) who are constantly and often aggressively looking over Appeals' shoulder, and you have a dysfunctional dispute resolution system.

A comprehensive and critical evaluation of the IRS's ADR programs can be found at ***www.ADRTax.org***, including a number of ideas and recommendations for change. Here are three key recommendations:

(a) New ADR Unit. IRS Appeals would be stripped of all ADR activities and a new Alternative Dispute Resolution Center would be established in Washington D.C., physically separate from IRS headquarters and completely detached from Appeals.

(b) Independent Neutrals. Following the lead of the commercial world and other successful federal agency programs, the use of truly *independent* third-party neutrals with no ties to either party to serve as mediators and arbitrators. The current IRS practice of using IRS Appeals employees as "neutrals" surely defies perception, if not reality.

(c) Mandatory Mediation. Following the practice followed in most state and federal courts, make the non-binding mediation process *mandatory*. That mediation is by definition and practice a non-binding procedure takes the sting out of the "mandatory" notion; the parties need only use their best efforts to resolve the dispute by mediation.

The Ways and Means Blueprint *Service First* goal is addressed at ***www.ADRTax.org*** that details proposals to provide taxpayers embroiled in tax controversies with impartial and cost effective mediation and arbitration tools to resolve their disputes. The new ADR Center would be dedicated to managing the intake, processing, and swift disposition of unresolved cases filed by taxpayers, as well as oversee the parties' selection from a pool of highly qualified, independent neutrals. Under this new structure, taxpayers would be given a clear choice to have their disputes resolved either by genuinely impartial neutrals at the ADR Center or by IRS employees through the traditional Appeals process.

Proposal. It's time to implement modern, proven, efficient and cost-effective ideas of the type outlined in ***www.ADRTax.org,*** which are widely and successfully used in the commercial world and at some federal agencies. The IRS should be required to take seriously its 1998 Congressional mandate to seize ADR as a strategic dispute resolution tool and put in place needed and meaningful ADR programs. This will also promote the IRS's overarching Mission of maximizing tax compliance and accelerating revenue collections through more collaboration and less confrontation.

* * * *

The author published this proposal in Tax Notes, **"Drain the IRS Swamp: Proposals to Disrupt the Nation's Tax Collector," Vol. 154, No. 7, p. 877 (February 13, 2017).** The idea is meant to be comprehensive in scope and would render moot and unnecessary a proposal formulated earlier by the Ways and Means Committee Blueprint calling for the creation of a "small claims court."

The State of Dispute Resolution at the Internal Revenue Service
Submission of the National Association of Enrolled Agents
September 27, 2017

> *"As a guiding principle, the Commission believes that taxpayer satisfaction must become paramount at the new IRS and that the IRS should only initiate contact with a taxpayer if the agency is prepared to devote the resources necessary for a proper and timely resolution of the matter."*
>
> *Report of the National Commission on Restructuring the IRS, June 1997*

Unfortunately, 20 years later, this vision is not being fulfilled.

Defining the Problem

Increasingly, enrolled agents are expressing the view that the quality of dispute resolution within the IRS has deteriorated to an unacceptable level over the last five years. The National Association of Enrolled Agents (NAEA) represents the interests of over 53,000 enrolled agents nationwide. Enrolled agents are tax experts, licensed by the Department of Treasury. They must pass a thorough three-part Treasury-administered exam covering all elements of the Internal Revenue Code. Additionally, they are subject to background checks and must meet continuing education and ethics requirements to continue as enrolled agents in good standing.

NAEA takes an expansive view of dispute resolution, encompassing the entire spectrum of tax administration. Our members represent taxpayers on a daily basis, dealing with notices, correspondence, examination, appeals and collection matters. Quality dispute resolution should not be an organizational value only for Appeals, but should be trained at every level of the agency. While the measure of the decline in quality is anecdotal, based on input from our membership, it can be demonstrated starkly by considering the answers to three important questions:

- Do key enforcement personnel have an adequate understanding of the Internal Revenue Code, the regulations, the Internal Revenue Manual and the "Taxpayer Bill of Rights?"
- Are cases resolved in a timely fashion?
- Do IRS enforcement personnel work to resolve cases fairly at the earliest point of the process?

While there are many skilled, conscientious, and dedicated employees at the IRS, enrolled agents are telling us that they must answer "no" to all three questions, too frequently to be acceptable.

Enrolled agents are finding that auditors and tax compliance officers often lack a basic understanding of the statutes and regulations they are tasked to administer. More disturbingly, they often do not know their own procedures as laid out in the Internal Revenue Manual (IRM).

Additionally, with few exceptions, dealing with the IRS has become a game of hurry-up-and-wait. Taxpayers and their enrolled agents respond in a timely fashion to notices or requests for audit responses, but then find themselves waiting long periods of time for an acknowledgment or response, let alone a resolution of their case.

While correspondence exams increase efficiency for the IRS, they typically increase taxpayer burden and can be more expensive and take more time than an in-person audit. Because there is only one chance for resolution, enrolled agents report that they expend substantial time and effort to present a relatively simple case that could be taken care of with a single telephone call.

When responses from taxpayers arrive at the correspondence examination unit, they can sit in a queue at the IRS processing center for weeks, or even months depending on the backlog, causing great anxiety on the part of taxpayers. These computer-generated cases are assigned to tax examiners only when a response is received from the taxpayer or their representative. If all goes well, the IRS issues a letter thanking them for their responses and informing them nothing more is needed. All too often though, taxpayers or their representatives respond with a timely submission of documentation, but the case does not receive proper consideration of facts and circumstances, and the only subsequent communication from the IRS is an audit report with a balance due notice enclosed.

If a protest of this assessment is submitted to the IRS, the response is often inadequately handled as well. In a number of cases, it is obvious that the protest was hastily reviewed by an inexperienced or under-trained employee, resulting in the denial of a valid protest. If this denial is appealed, similarly trained employees evaluate the argument, adding another step in an exercise in futility. Any further request for a referral to Appeals of these disputed items are all too often not considered or acknowledged, and a Statutory Notice of Deficiency is summarily sent to the taxpayer.

Once the computer has taken this action, filing a petition in Tax Court is the only way to get the case heard by a qualified Appeals Officer. Enrolled agents believe there must be greater accessibility to be heard by an independent Appeals Officer at multiple stages while the taxpayers' fate is being determined in these automated audit pipelines.

Enrolled agents have noticed that as mastery of the laws and regulations has declined, there has been a corresponding decline in resolving cases quickly and fairly. In some cases, we believe this change in culture means that rather than getting to the right answer and then moving on, IRS compliance personnel in the field and campuses are more inclined to "find something wrong" if they have invested substantial time on an examination. In other cases we have seen, the Service's desire to close cases as quickly as possible with their limited resources

spread thin has led to a hesitation on the part of IRS personnel to accept follow-up documentation or request an explanation when documentation is not understood.

Historically, Appeals Officers were experienced and knowledgeable and operated in a culture of resolving cases quickly and fairly. Over time, as resources have dwindled system-wide, more cost-effective alternatives have been developed by the IRS. In our experience, many of these cost-saving processes have led to severe reductions in service while taxpayer rights are increasingly being compromised. The end result has been reduced public confidence in the U.S. Tax system as fair and equitable.

The issue at hand is that there are not enough Appeals personnel to provide taxpayers with in-person conferences across the 50 states and territories. For example, between fiscal years (FYs) 2013 and 2016, the number of Appeals Hearing Officers available to resolve cases dropped by 24 percent[1]. Consequently, the IRS created Campus Appeals units, which rely on telephone and now video conferences to handle their workload.

Root Causes

Decline in the IRS Budget: In the last five years, the IRS budget has declined from $12.146 billion in 2012 to $11.235 billion in 2016. As a result, the number of revenue agents decreased 22 percent from 10,216 to 7,937, and the number of tax compliance officers decreased 28 percent from 1,154 to 832. Contact representatives within the Automated Collections System (ACS) has decreased 22 percent, from 2,426 in FY 2012 to 1,897 in FY 2016. Enforcement personnel are not typically seen as customer service. However, if a taxpayer receives a letter or notice about their account and then are not able to resolve the issue in a timely and accurate fashion, then the non-resolution does become a customer service issue.

Retirements: The IRS is hemorrhaging experienced, well-trained personnel. Since 2010, approximately 17,000 employees have departed from the IRS and 40% more are or will be eligible to leave the Service in the coming year. The loss of these experienced employees has necessitated the hiring, training and deployment of many inexperienced personnel in a short period of time. Exacerbating this problem is the fact that training at the IRS is done by taking experienced people out of the field to pass on their knowledge to the newly hired, creating an even larger vacuum.

Lack of Quality Training: The IRS training budget has been slashed from $172 million in FY 2010 to about $22 million in 2013 (unable to obtain more updated data), a staggering 87 percent reduction. Training is not only key to increasing knowledge and understanding of the tax code and regulations, but is also among the IRS's responsibilities under the taxpayer bill of rights.

On the collection side, revenue officers have been given very little discretion or training on resolving taxpayer cases. When a taxpayer's expenses exceed the financial standards for an

[1] Taxpayer Advocate Service 2017 Report, volume 2, page 112

Installment Agreement, the taxpayer must enter into a payment plan that is unaffordable, which greatly increases the likelihood of default down the road. In addition, the National Standards for Collection Information Statement analysis are unrealistic for taxpayers living in high cost areas. More flexibility in making determinations of collection potential would improve the public's perception that the system is fair and equitable.

Recommendations

To increase the quality and timeliness of dispute resolution within the IRS, Congress should consider the following policy and legislative changes:

Increase IRS budget for hiring Appeals Officers, compliance, and enforcement personnel. With this increased budget, the IRS should guarantee that taxpayers or their representatives do not have to travel more than 100 miles (where feasible) to have a face-to-face audit meeting or an in-person conference with an Appeals Officer. At the same time, it is important for the IRS to continue exploring video-conferencing and other options for increasing communications. Additionally, once a taxpayer responds to an IRS notice or letter, the IRS shall communicate a decision to the taxpayer within 30 days. Appeals and enforcement personnel should be given great authority to settle cases early and the IRS should evaluate them based on a singular focus on early and fair resolution of disputes.

Increase the Authority of and set higher standards for campus Appeals personnel. While we welcome and applaud the IRS for the recent addition of video conferencing as a substitute for some in-person Appeals hearings, we suggest additional provisions be implemented. The knowledge, experience and authority of the Appeals personnel should meet a higher standard than the campus Appeals Technical Employees, who may have very little authority and may not grasp the intricacies of the cases assigned to them.

Create and fund a dedicated training division within the IRS. A dedicated training division will streamline the IRS education process, ensuring that tax law and administrative policies be taught consistently throughout the country while guaranteeing that experienced personnel will not have to be taken offline to train new employees. Instructors will be tasked to research state-of-the-art tax administration techniques at the state, local and international levels and will help incorporate these techniques into their education materials and the Internal Revenue Manual. Additionally, as was done immediately after passage of the IRS Restructuring and Reform Act of 1998, IRS training shall focus on early and fair resolution of tax disputes. Only clear and consistent training will move the IRS to a more customer service-oriented organization.

Give Collections personnel wider discretion to reach agreements on payment plans. Congress and the IRS need to give collections personnel the authority and training to resolve cases quickly that might otherwise deviate slightly from the financial standards to facilitate payments by taxpayers. Additionally, the IRS should reevaluate the National Standards for Collection Information Statements by either adjusting the allowable living expenses for regional or local

cost of living variations, or by returning to use of a dollar range, based on gross monthly income (as was the case prior to the IRS decision in 2007 to apply a single dollar amount for food, clothing and other items, based on family size alone).

Give the Taxpayer Advocate Service authority to make adjustments, rather than merely making recommendations to IRS personnel. Taxpayer Advocates are at the forefront of problem resolution within the IRS. We recommend reinstituting a Problem Resolution group with representation from examination, appeals and collection housed in the Taxpayer Advocate department with fixed authority to resolve issues up to $10,000 and close cases.

Collections personnel must refrain from bypassing representatives with active powers of attorney. Congress should reemphasize and reaffirm the consequences of violations of 26 USC 7525, to ensure that IRS personnel shall not ignore valid powers of attorney by directly contacting taxpayers by telephone or at their residences or places of business.

Require IRS exam and collection personnel to offer alternative dispute resolution options. We commend the IRS for the expansion of Fast Track Settlement earlier this year, bringing the opportunity for small business and individual taxpayers to resolve unique examination issues through Appeals, allowing for consistency with large and mid-sized businesses. We recommend that the IRS expand alternative dispute resolutions options to all taxpayers and that exam and collection personnel be required to offer these options at the appropriate time.

To facilitate earlier resolutions to disputes, the IRS should debut online accounts for tax practitioners with a **robust and secure means of communicating with IRS personnel on audit and collections issues.** Access to secure online communication is especially important as the agency becomes increasingly reliant on correspondence audits that currently require snail-mailing documents to anonymous IRS campus employees. Communicating through the practitioner's online account would go a long way to improving resolution times and hopefully mitigate, if not eliminate, the lost documents experience.. Individual online accounts should display a Publication 1 equivalent when taxpayers utilize payment options in their accounts. The IRS should provide guidance on the use of electronic signatures for Forms 2848 and 8821 for Circular 230 practitioners.

The National Association of Enrolled Agents commends the Committee on Ways and Means in its bipartisan approach to improving the Internal Revenue Service. Our membership believes strongly that well funded, well trained IRS, fully cognizant of taxpayer rights and the value of Circular 230 tax practitioners to the process, will improve dispute resolution at every level of the organization. We look forward to continuing our work with the Committee.



Software Finance & Tax Executives Council

www.softwarefinance.org

Via Email

September 12, 1017

Hon. Vern Buchanan
Chairman
Subcommittee on Oversight
Committee on Ways and Means
U.S. House of Representatives
Washington, DC

Re: Hearing on Reforming How the IRS Resolves Taxpayer Disputes

Dear Chairman Buchanan:

I write to express the views of the Software Finance and Tax Executives Council (SoFTEC) with respect to the upcoming September 13, 2017 Oversight Subcommittee hearing entitled "Reforming How the IRS Resolves Taxpayer Disputes." SoFTEC supports your efforts at shining a light on procedures designed to protect taxpayers' rights in their dealings with the IRS. SoFTEC members are concerned current practices and procedures tilt too heavily in the IRS's favor, may result in unnecessary disputes, which are time consuming and expensive for taxpayers and the IRS. They believe legislation is needed to restore balance to the relationship between taxpayers and the IRS while preserving the IRS' ability ensure taxpayers pay the appropriate tax.

SoFTEC is a trade association providing software industry focused public policy advocacy in the areas of tax, finance and accounting. Because its member companies routinely are audited by the IRS and frequently have disputes with the agency, they have an interested in the practices and procedures used by the IRS in ascertaining the accuracy of their tax returns and in resolving disputes in an efficient manner for both taxpayers and the IRS.

SoFTEC supports H.R. 3220, the Preserving Taxpayers Rights Act, a bi-partisan bill recently introduced by Reps. Jason Smith and Terri Sewell, along with other co-sponsors. This bill, if enacted, would:

- Provide a statutory right to an internal IRS appeal prior to issuance by the IRS of a notice of deficiency if the taxpayer extends the statute of limitation by 12 months.
- Limit the ability of the IRS to negate this right to an appeal to only when the dispute involves a listed tax shelter transaction.
- Limit the ability of the IRS to issue a so-called "designated summons," which unilaterally tolls the statute of limitations, to cases where the taxpayer has been uncooperative, as intended in the legislative history.

- Prohibit the taking of witness testimony and examination of taxpayers' books and records by outside contractors.

SoFTEC believes enactment of these provisions would minimize unnecessary disputes that are time consuming, inefficient, and expensive for taxpayers, the IRS and the courts. This legislation would help restore balance to taxpayers' dealings with the IRS. We will discuss each of these provisions in turn.

1. **Statutory Right to an Appeal:**

As the hearing notice correctly points out, the IRS Restructuring and Reform Act of 1998 mandated that the IRS provide an independent Appeals function and make an Appeal Officer available in each state. However, the circumstances under which a taxpayer may take advantage of such an independent Appeals function remain a matter of administrative grace. We believe the IRS Office of Appeals serves and important function and helps whittle down disputes to those cases where the IRS and the taxpayer truly either cannot agree or are unable to compromise and the dispute must be adjudicated by either the Tax Court in a deficiency proceeding or by a federal judge in a refund civil action. We believe it is important to clarify that taxpayers generally have the right to have a Revenue Agent's determination reviewed by an Appeals Officer before being forced into costly and time consuming litigation, which is inefficient for taxpayers and the IRS. To balance the taxpayer's right to an independent Appeal while not prejudicing the IRS' ability to ensure the taxpayer pays the appropriate amount of tax, the bill requires the taxpayer to extend the statute of limitation by 12 months.

We are aware of cases where the IRS has issued statutory notices of deficiency to taxpayers, which starts the time running for filing a petition with the Tax Court, without first allowing such taxpayers the opportunity to have their cases heard by an independent Appeals Officer. Such circumstances deprive these taxpayers of the ability to have its case heard by an independent and seasoned Appeals Officer who might take a different view of the facts of the case, the applicable law, or both, than the Revenue Agent. Appeals officers have the ability to consider so-called "hazards of litigation" in ascertaining the relative strength or weakness of the Revenue Agent's determination, something Revenue Agents are unable to take into account. Depriving a taxpayer of an independent Appeal either forces the taxpayer to concede or undertake the burden an expense of a Tax Court proceeding, which is time consuming, expensive, and inefficient for the taxpayer, the IRS and the courts. Forcing cases into court that could have been settled at the Office of Appeals is wasteful of both taxpayer and government resources. H.R. 3320 would enshrine in statute a taxpayer's right to an independent Appeal.

2. **Limitations on the Statutory Right to an Appeal:**

While SoFTEC strongly believes the right of taxpayers to have disputes heard by an independent Appeals Office within the IRS, we do not advocate that such a right be unlimited. There likely are circumstances where a taxpayer may seek an Appeal for the purpose of delay or in an attempt to secure a different result than other similarly situated taxpayers. For instance, taxpayers involved in abusive tax shelters known as "listed transactions" may try to delay administrative proceedings by moving them to the Office of Appeals. In the case of listed

transactions, the IRS has an obvious interest in equal treatment of similarly situated taxpayers and a taxpayers should be on notice that they can't use the Appeals process to obtain a better result than other participants in a given tax shelter.

3. Independence of the Office of Appeals:

One of the key features of the IRS Office of Appeals is its independence from the Revenue Agents that conducted the audit. Historically, once a case was transferred to the Office of Appeals, there was no contact between the Appeals Officer handing the case and the Revenue Agent who conducted the audit. However, this independence is under siege.

To the dismay of tax practitioners, there is a new IRS initiative that allows Revenue Agents to be actively involved in discussions with the Appeals Officers after cases are transferred to the Office of Appeals. The risk that the Revenue Agent that conducted the audit will be involved in the consideration of the case by the Office of Appeals is causing some taxpayers to skip an Appeal altogether and going straight to time consuming and expensive Tax Court.

One of the benefits of the Office of Appeals is the opportunity it affords taxpayers to have a fresh set of eyes look at cases untainted by entrenched positions taken by the Revenue Agents. Having the Revenue Agent in the room risks bringing in whatever poisoned atmosphere might have clouded the audit and prevented resolution at the lower level.

We believe any legislation that impacts the IRS Office of Appeals should include a provision erecting a wall between that Office and the field team that conducted the examination of the return preventing their involvement in consideration of the case at the Appeals level. While such a provision was not included in the Preserving Taxpayers Rights Act, SoFTEC believes it should be considered.

4. Limitation on the Ability of the IRS to Issue a "Designated Summons:"

Generally, the IRS has three years from the filing of a tax return to conduct an audit of the return and propose a deficiency in tax. This three-year statute of limitations is designed to afford the IRS ample time to conduct the audit and protect taxpayers and the IRS from lengthy audits that prolong uncertainty. This three-year statute of limitations can be, and often is, extended with the agreement of the taxpayer to provide sufficient time to resolve an audit.

There is an exception to this three-year statute of limitations for instances where the IRS serves upon the taxpayer a so-called "designated summons" under I.R.C. Sec. 6503(j). Service of a designated summons tolls the three-year statute of limitation during the pendency of a summons enforcement action in a District Court. This statute gives the IRS the unilateral and unfettered authority to negate the statute of limitation and prolong a taxpayer's audit until it informs a court that it is satisfied the taxpayer has produced all relevant books and records.

The legislative history of the designated summons provision reveals its purpose was to protect the fisc from uncooperative taxpayers who might stall an audit and try to run out the

clock on the three-year statute of limitations. Its purpose was not to give the IRS an unfettered ability to extend the statute of limitations when the taxpayer has been cooperative and any delay on the conduct of the audit is the fault of the IRS. Giving the IRS this designated summons authority negates all of the purposes of the statute of limitations and provides an incentive for the IRS to be dilatory in the conduct of audits. The use of a designated summons was intended to be so extraordinary, that Congress required the IRS to annually inform the House and Senate tax writing committees of the number of designated summons that have been in the year.

The Preserving Taxpayers Rights Act restores the purposes of the statute of limitations by limiting the IRS's use of designated summons to situations where the IRS establishes that the taxpayer "did not reasonably cooperate with reasonable requests" for information. SoFTEC supports these provisions.

5. Use of Outside Contractors in the Conduct of an Audit:

Recently, the IRS has taken the unprecedented step of hiring outside contractors to assist in conducting and taking testimony in an audit. Specifically, these outside contractors are outside lawyers and have been retained for the specific purposes of assisting in the examination of the taxpayer's books and records and in the questioning of potential witnesses. The hiring of outside lawyers to assist and take testimony in the conduct of an audit signals to the taxpayer that the exam is not directed towards ascertaining the correctness of the return but is instead directed towards preparation of the case for litigation. And, because these outside attorneys' contracts contemplate their assistance at trial with an hourly billing rate, they have an incentive to inflate deficiencies and proffer untested and/or dubious legal theories.

In addition, hiring outside lawyers to participate and take testimony in a tax audit is a waste of government resources.

The Preserving Taxpayers Rights Act contains a provision that would prohibit the use of outside contractors for the purpose of examining taxpayers' books and record and the questioning of witnesses. SoFTEC supports these provisions.

6. Conclusion:

SoFTEC appreciates the opportunity to provide these comments and ask that they be made a part of the record of the Subcommittee's upcoming hearing. I may be reached at (202) 486-3725 or mnebergall@softwarefinance.org with any questions.

Respectfully submitted,



Mark E. Nebergall
President
Software Finance and Tax Executives Council

Testimony of Chief Judge L. Paige Marvel
United States Tax Court

Subcommittee on Oversight of the Committee on Ways and Means
United States House of Representatives

Hearing on Reforming How the IRS Resolves Taxpayer Disputes
September 13, 2017

Chairman Buchanan, Ranking Member Lewis, and Members of the Subcommittee, thank you for the opportunity to provide testimony.

The United States Tax Court (Tax Court) is an independent court of record established by Congress under Article I of the Constitution. The Tax Court's mission is to provide a national forum for the resolution of disputes between taxpayers and the Internal Revenue Service (IRS), to resolve tax cases expeditiously while giving careful consideration to the merits of each case, and to provide a consistent body of case law interpreting the Internal Revenue Code. The Tax Court's status as a court of law, exercising exclusively judicial powers, has been confirmed by the Supreme Court.[1] An understanding of the Tax Court's status and its practices and procedures (particularly as they relate to self-represented taxpayers) is instructive in evaluating proposed changes to administrative procedures affecting taxpayer interactions with the IRS.[2]

Evolution of the Status of the Tax Court

Before its designation as a court of record under Article I, the Tax Court was established by statute as an independent agency within the Executive Branch known as the Board of Tax Appeals (the Board). Congress created the Board in 1924 to address inadequacies with the Committee on Appeals and Review (the Committee), which had been established by the post-World War I Bureau of Internal Revenue (now the IRS). There were two primary criticisms of the Committee. The first criticism of the Committee was the lack of a readily available review that was independent of the Bureau. The second criticism was that the Committee's proceedings "were not adversarial, they were not public, they did not permit the introduction of new evidence, and they were not conducted pursuant to traditional judicial standards of practice and procedure."[3]

[1] Freytag v. Commissioner, 501 U.S. 868 (1991).
[2] See Harold Dubroff & Brant J. Hellwig, *The United States Tax Court: An Historical Analysis* (2d. ed., Government Publishing Office, 2014) (1979), https://www.ustaxcourt.gov/book/Dubroff_ Hellwig.pdf. (hereinafter Dubroff).
[3] Id. at 46.

Congress eventually concluded that it was anomalous that one executive agency would sit in judgment of the actions of another (the IRS). This concern led Congress, in 1969, to establish the Tax Court as an Article I court of law to ensure its independence from the Executive Branch.[4] As an Article I court of law, the Tax Court is not affiliated with the IRS.

The Tax Court's jurisdiction is statutorily based. It is one of three Federal courts in which taxpayers, including individuals and business entities, may obtain judicial review of a dispute with the IRS.[5] It is the only Federal court in which the taxpayer can obtain review before having to pay the disputed taxes in advance. Tax Court jurisdiction is broad and includes income, estate, gift, and certain excise tax deficiencies, declaratory judgment authority, TEFRA partnership proceedings, interest abatement actions, collection due process cases, review of awards under the IRS whistleblower program, and claims for spousal relief from joint and several liability. Decisions by the Tax Court are reviewable by the United States Courts of Appeals and, if certiorari is granted, by the Supreme Court.[6]

The Tax Court is authorized by statute to have 19 judges who are appointed to 15-year terms by the President, with the advice and consent of the Senate.[7] The Court's cases are also heard by senior judges (presidentially appointed judges whose terms have expired and are recalled by the Chief Judge of the Tax Court) and by special trial judges who are appointed by the Chief Judge. To make the Tax Court accessible to the public nationwide, Tax Court judges conduct trial sessions in 74 cities. This is consistent with the Court's statutory mandate to establish places of trial with a view to securing reasonable opportunity for taxpayers to appear before the Tax Court with as little inconvenience and expense as is practicable.[8]

The Court's caseload depends upon the scope of jurisdiction provided by Congress, the level of audit and enforcement activity by the IRS, and the choice of forum by taxpayers. The Court strives to resolve cases quickly while giving careful consideration to the merits of each case. To achieve this goal, the Court schedules cases for trial promptly after the pleadings are complete, usually within one year even in the cities with the fewest cases. Over the last several years, most active judges were assigned from 6 to 12 trial sessions per year, with each session typically including 100 to 150 cases. Although the majority of cases are closed as a result of settlement between the parties, many of those settlements require the active involvement of a judge in pretrial matters and for the management of settlement discussions. The disposition of a tried case by written opinion normally occurs within one year of trial. Since Fiscal Year 2009, the number of cases the Court has closed has exceeded the number of new cases filed each fiscal year.

Tax Court Programs Promoting Access to Justice for Self-Represented Taxpayers

More than 70 percent of all Tax Court petitioners are self-represented. Self-represented taxpayers receive significant support from the cooperative and coordinated efforts of the Tax Court with low-income taxpayer clinics (LITCs) and Bar-sponsored calendar call programs.

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[4] S. Rep. No. 91-552 (1969).
[5] The other Federal courts available are the U.S. Court of Federal Claims and the U.S. District Courts.
[6] I.R.C. secs. 7441, 7443, and 7482.
[7] I.R.C. secs. 7441, 7443, and 7444(c).
[8] I.R.C. sec. 7446.

LITCs are recognized by the IRS's Taxpayer Advocate Service and are either a stand-alone non-profit organization or affiliated with a law school. Bar-sponsored calendar call programs must be organized by a Bar association, integrated Bar, or similar professional organization whose members provide pro bono legal assistance to self-represented taxpayers before the Court.

The Tax Court has adopted a program to encourage LITCs and Bar-sponsored calendar call programs to participate in Court trial sessions in order to assist otherwise unrepresented taxpayers. Currently, taxpayers have access to legal assistance in each of the Court's 74 trial cities through 132 LITC programs as well as calendar call programs operated by volunteers working through the tax section of state and local bar associations in 16 cities.

The Tax Court provides every self-represented taxpayer who files a petition with the Court with contact information for local LITCs. This information is provided to taxpayers when the petition is filed, when the case is set for trial, and again 30 days before the trial session. At the calendar call at the beginning of a trial session, Tax Court judges announce the availability of LITC or Bar-sponsored practitioners who are in the courtroom to provide assistance to self-represented taxpayers. The Court also provides meeting space for LITC or Bar-sponsored representatives to meet with their clients on the day of calendar calls. The LITCs and calendar call programs annually report to the Court that hundreds of petitioners have received assistance.

The Tax Court provides significant institutional support to LITCs and Bar-sponsored programs as an integral component of the Court's commitment to expand access to justice for all self-represented taxpayers by ensuring the opportunity to consult with counsel.

Small Case Procedures

In addition to the LITC program, taxpayers with relatively modest amounts in dispute may take advantage of special procedures authorized in Internal Revenue Code section 7463 and outlined in the Tax Court Rules of Practice and Procedure.[9] When Congress designated the Tax Court as an Article I court of law in the Tax Reform Act of 1969, it also addressed concerns that taxpayers who had relatively small tax deficiencies did not have ready access to impartial review of IRS determinations.[10] To remedy this problem, Congress authorized a simplified and informal procedure for small cases. At the time, Internal Revenue Code section 7463 limited small case

[9] See Rules 170-174, Tax Court Rules of Practice and Procedure.
[10] Dubroff, at 883.

proceedings to deficiency disputes of $1,000 or less. In 1998, Congress increased the small case limit to its current level of $50,000 or less.[11]

A taxpayer who meets the criteria for small case treatment must make an election prior to trial that is concurred in by the Court. Although Tax Court decisions in small tax cases are not appealable, there are several benefits to the small case proceedings. First, there are more trial venues throughout the country for small tax cases compared to regular tax cases. As with all cases, the Court gives the parties about five months advance notice before a case is set for trial, along with general instructions about how best to prepare for trial. In small tax cases, taxpayers also receive a checklist of items to consider as part of trial preparation. Trials of small tax cases are conducted as informally as possible consistent with orderly procedure and any evidence deemed by the Court to have probative value may be admitted. Finally, as a general rule, neither briefs nor oral arguments are required in small tax cases.

Over the years, Congress has amended Internal Revenue Code section 7463 to expand the types of cases for which small case procedures are available to taxpayers. Today, the small tax case procedures are also available in certain excise tax cases, disputes involving IRS employment status determinations, and petitions for innocent spouse relief, review of collection actions, and requests for interest abatement.

The success of the small case procedures and their ease of use for taxpayers is evident in that in Fiscal Year 2016, 46 percent of the Court's cases were filed as small cases, and 91 percent of petitioners who elected small case status were self-represented (without counsel). Tax Court judges are committed to creating a courtroom environment for taxpayers that is inviting and understanding rather than intimidating, especially for small case and self-represented taxpayers.

In conclusion, I offer the Tax Court's assistance to you and your staff as you develop and consider proposals. We would be pleased to comment at the appropriate time on any procedural proposals.

Thank you.

[11] Internal Revenue Service Restructuring and Reform Act of 1998, Pub. L. 105–206, 112 Stat. 685, enacted July 22, 1998.

