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A PRACTICAL GUIDE TO THE NEW ROUND OF IRS EXAMINATIONS

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Introduction

Make no mistake about it: the Internal Revenue Service (IRS) is once again examining taxpayers in full force. The increased IRS examination activity is coming in all different forms. One common theme among the new breed of IRS examinations is that the IRS is making a targeted and coordinated effort to cover specific issues and industries. It is safe to say that the IRS is approaching examinations in today's climate with a sharpened pencil.

IRS Structure

IRS Operating Divisions

The IRS is broken into four operating divisions: Wage and Investment, Tax Exempt and Government Entities, Small Business/Self-Employed, and Large Business and International. All examinations conducted by the IRS on the civil side will fall within the purview of one of these four divisions.

The least likely divisions to come in contact with during an IRS exam are the Wage and Investment Division and the Tax Exempt and Government Entities Division. The Wage and Investment Division usually covers such items as non-matching W-2s. The Tax Exempt and Government Entities Division, as its name suggests, covers tax exempt and government entities.

The vast majority of audit activity is arising out of the Small Business/Self-Employed and the Large Business and International Divisions. The Small Business/Self-Employed (SB/SE) Division examines companies with \$10,000,000 or less in assets. The examiners in the SB/SE Division are typically much more interested in entrepreneurial-type issues such as compensation received from an entity directly and indirectly along with the deductibility of personal-type expenses. Agents in the SB/SE arena are also attuned to attributing personal-type expenses back to the ultimate taxpayer in the form of additional compensation or dividends. For businesses or entities with more than \$10,000,000 in assets, the Large Business and International (LB&I) Division is the designated division for examination. Interestingly, the

LB&I Division was formerly known as the Large and Mid-Sized Business Division. The IRS is focused so much on international issues that the IRS felt the need to change the name to Large Business and International.

Types of IRS Employees

Revenue Agents

Within the IRS, there are many different sections, and it is imperative to understand which group you are dealing with in representing a taxpayer. The most obvious group is the IRS Civil Examination Division. The revenue agents in the civil division of the IRS that you will be dealing with typically fall within the SB/SE and LB&I Divisions. Within these divisions, you will typically deal with a revenue agent who is an IRS examiner and who may or may not also be a CPA. In addition to revenue agents, who are civil examiners, there are also specialized types of agents—such as employee examiners, international examiners, excise tax specialists, and engineers. Each one of these agents within the IRS Examination Division functions at a different level. The international examiner is obviously brought into a case to develop international issues. The excise tax examiner is brought in to determine whether all excise taxes have been calculated correctly. The employment examiner is brought in to determine whether the taxpayer has been correctly classifying and accounting for the taxpayer's workers. Finally, the engineers for the IRS typically work in the area of providing appraisals in value for companies or assets. Within the area of appraisals, the IRS also has specialized appraisers for art.

SEP Agents

The civil division of the IRS also includes a special group of people in the Special Enforcement Program (SEP). If you find yourself working with an IRS agent in the SEP, it is very important to protect your taxpayer's rights. Cases assigned to the SEP group of the IRS Civil Examination Division are cases which the IRS believes have a potential for fraudulent activity. In some instances, the IRS determines there is no fraud, and in other instances, the IRS determines there is merely civil fraud, which must be proven by clear and convincing evidence. But at the other end of the spectrum, if the SEP agent determines there are firm indications of fraud, the SEP agent must cease the civil examination and prepare the case to refer to the IRS Criminal Investigation Division. In contrast to civil fraud, criminal fraud must be proven beyond a reasonable doubt.

Special Agents

A Special Agent in the IRS Criminal Investigation Division is not tasked with determining the correct amount of tax—the special agent must only determine whether or not there is proof of a tax crime. Not surprisingly, a Special Agent’s job is typically made much easier by taxpayers who talk to him or her. Once a taxpayer decides to talk to the IRS Special Agent on their own, the taxpayer has two options. The first option is to tell the truth, which unfortunately often results in an admission of criminal activity otherwise known as a confession. The second option is to “fudge” the truth, which results in a lie to the IRS Special Agent—which besides being a badge of fraud, is also a separate crime in and of itself. Never forget that Martha Stewart was not convicted of a crime for insider trading, but rather, obstruction of justice.

When the IRS Special Agent is on the scene, the taxpayer is faced with a choice: whether or not to talk to the Special Agent. In order to avoid confusion or misunderstanding, one rule applies to a taxpayer when faced with an IRS Special Agent: “Silence is golden.” If the taxpayer is going to talk to the IRS Special Agent, it is always better to do so with experienced criminal tax counsel present.

Other IRS Divisions and Offices

Appeals

When a civil examination is concluded without referral to the Criminal Investigation Division, the case will typically next progress to the IRS Appeals Division. The IRS Appeals Division is tasked with settling tax disputes between the IRS Examination Division and a taxpayer. The Appeals group within the IRS has historically been, and remains, a very effective group in settling disputes between the IRS and taxpayer. Often, cases move straight from the examination phase into the appeals phase. However, some cases move from the Tax Court litigation phase into the appeals phase as well.

Chief Counsel

The next group of IRS personnel a taxpayer may encounter is the Office of Chief Counsel, which houses the attorneys for the IRS. The Office of Chief Counsel is tasked with the job of defending the IRS in Tax Court, as well as assisting in various other legal matters for the IRS—ranging from analysis of refund claims, to assisting in criminal prosecutions, to acting as Special Assistant United States Attorneys in special cases. The Office of Chief

Counsel in a Tax Court case has the option of either litigating the case or settling the case before the necessity of a trial.

National Taxpayer Advocate

The National Taxpayer Advocate Office is often overlooked by taxpayers. In addition to presenting an annual report discussing various methods by which the IRS can improve, the Taxpayer Advocate Office also assists individual taxpayers. Specifically, a taxpayer with a problem can contact the Taxpayer Advocate Office and file a Form 911 Request for Taxpayer Advocate Service Assistance. The Request for Taxpayer Advocate Service Assistance can run the full range of any problem a taxpayer may have. In some cases, the Taxpayer Advocate Office can actually solve the problem directly. In the vast majority of cases, however, the Taxpayer Advocate Office works as a liaison between the taxpayer and the IRS division with which a taxpayer is in negotiations.

Office of Professional Responsibility

One office that practitioners would generally rather not come in contact with is the Office of Professional Responsibility (OPR). The OPR is tasked with enforcing Circular 230, which governs all tax practitioners who practice before the IRS. An OPR investigation can have severe consequences with respect to tax practitioners, ranging from a mere warning all the way to a temporary or permanent disbarment from the ability to practice in front of the IRS. Practitioners must take any contact from the OPR very seriously.

Whistleblower Office

One of the newer offices at the IRS is the Whistleblower Office, which is tasked with taking in information regarding taxpayers by informants with evidence of the taxpayer's noncompliance. The IRS is paying out large awards to taxpayers who use the Whistleblower Office. The most notable recent case is Bradley Birkenfeld, the ex-banker at UBS who turned over information from UBS to the IRS. After being released from jail for his role in tax fraud involving UBS in Switzerland, Bradley Birkenfeld received a substantial award from the IRS Whistleblower Office.

IRS Pre-Examination Considerations

The Boy Scout motto to "be prepared" definitely applies in the arena of IRS examinations. Accordingly, consider postponing the examination if everyone is not completely prepared. Nothing could be worse than just

walking in cold to an IRS examination. The IRS will have conducted quite a bit of pre-examination work and it is imperative that practitioners do the same.

Internal Due Diligence

Start the pre-examination preparation process with the items that the IRS is most likely to examine. Begin by reconciling the taxpayer's books. Compare the taxpayer's books of account with the general ledger, income statements, and balance sheets. Also, compare the taxpayer's books of account to the source documents within the business such as cash receipts, disbursement journals, and sales journals. After reconciling these items, the practitioner should next reconcile all of the taxpayer's accounting books with the actual filed tax return under examination. In doing so, it will be important to determine and review the adjusting journal entries that bridge the taxpayer's accounting books with the tax returns under examination.

Next, review the client's tax returns. A review should include all related returns and should cover all open years within the standard three-year statute of limitations. One thing the IRS will focus on is whether or not there is a pattern of errors over a three-year period. Additionally, do not forget to include related state and local returns. The IRS often reviews state and local returns for consistency when compared to the federal tax returns. Additionally, if there are prior IRS examination reports or prior examination reports from state taxing authorities, it is important to review those as well.

Additionally, evaluate the taxpayer's internal controls. Excellent internal controls may be used during the examination process to support the accuracy of return information. On the other hand, if strong internal controls do not exist, the IRS may give much less weight to information included on the tax returns in issue.

Next, identify large, unusual, or questionable items in the return. The IRS examiner is directed to look for these large, unusual, or questionable items when surveying the return on its face. Typically, the large, unusual, or questionable items fall into categories such as large losses in the neighborhood of seven figures. Additionally, the IRS examiner will look for large deductions on the Schedule C of a Form 1040 that do not have accompanying income to offset the deductions. Additionally, the failure to check the 263A box on the return in a business that very likely has inventory is another large, unusual, questionable (LUQ) item that the IRS will include in its focus.

Finally, determine if sensitive issues exist. Schedule C taxpayers should examine the expenses very closely as the IRS will focus on the Schedule C

expenses. Additionally, if a business is cash intensive, the IRS will give much additional focus to the cash portion of the business.

At the outset of an examination, the practitioner must be aware of the applicable privileges afforded to a taxpayer. The most common privilege is the attorney/client privilege. The attorney/client privilege may apply to tax opinions written by lawyers for the taxpayer or even to memoranda written by lawyers for the taxpayer. To the extent that memoranda were drafted in anticipation of litigation, those could also fall under the work product doctrine. Finally, do not forget I.R.C. § 7525 which includes an accountant client privilege. Accordingly, the practitioner should open a separate set of files which are maintained in a secure location specifically relating to the IRS examination which are separate and distinct from the tax preparation files.

External Due Diligence

Conduct some independent research on your client through the Internet. Start with Google and work your way on to other Internet sites. Take a look at Corporation Wiki.¹ You might be amazed at what you find in the public records and in property searches. Also, do not forget to look for prior legal actions. The IRS is very good at finding SEC actions and records in other civil litigation matters.

Consider, for a moment, civil litigation in which your client has been involved. The civil litigation is likely to include many allegations pled by the person either suing or being sued by your client. It is not beyond the pale to imagine that many of the allegations are at best misguided or at worst absolutely false. The IRS Examination Division has been known to follow leads from litigation records which are available in the public domain.

In certain situations, it may be appropriate to contact the IRS examiner in advance of the first scheduled meeting. By contacting the IRS examiner in advance, a practitioner has the opportunity to educate the IRS examiner on the taxpayer and the taxpayer's business. Many times, the early contact will result in the IRS examiner issuing a much more focused and narrow request for information which elicits exactly the information required by the IRS and avoids an unnecessarily large production of irrelevant documents. What could have been an entire warehouse of documents can be reduced down to the equivalent of a few bankers boxes in the appropriate circumstance.

¹ www.corporationwiki.com

IRS Audit Technique Guides

Do not forget to determine if there are any applicable IRS audit technique guides² that would apply to your client's business or circumstances. The audit technique guides cover a range of industries such as wine, retail, new car dealers, timber, farming, construction, aerospace, and attorneys. In addition to specific industries and professions, the IRS also has audit technique guides to cover specific issues such as the age-old question of capitalization versus repairs. Other issues include conservation easements, cost segregation, executive compensation, fringe benefits, foreign insurance, the old favorite hobby loss rule under I.R.C. § 183, §§ 48A and 48B advanced coal and gasification project credits, split-dollar life insurance, and stock-based compensation.

The oil and gas industry has its very own audit technique guide.³ The audit technique guide begins with a general description of the industry followed by types of ownership interests, accounting methods, and accounting records. Next, the oil and gas industry audit technique guide focuses on specific oil and gas industry issues such as unproductive versus productive issues. It also includes unique issues and the uniform capitalization rules, in addition to I.R.C. § 263A inventory rules.

The audit technique guide specifically lays out oil and gas examination techniques and includes initial interview questions and initial information document requests. The audit technique guide identifies areas typical in an oil and gas exam such as gross income, lease bonuses, delay rentals, royalty income, advance royalties, minimum royalties, shut-in royalties, production payments, damages, and shooting rights. Next the uniform capitalization rules in I.R.C. § 263A for inventory are covered along with capitalization as opposed to current deductibility for a variety of expenses.

The audit technique guide for the oil and gas industry also includes a chapter on financial products and specifically directs the examiner to look into markets and their participants, identifying the forward and futures markets in addition to options contracts and market participants in forward and future contracts. The financial products section also includes information regarding commodity notional contracts and swaps in addition to the use of commodity notional swaps to hedge risk.

² The audit technique guides are at [www.IRS.gov/Businesses/Small-Businesses-&-Self-Employed/Audit-Techniques-Guides-\(ATGs\)](http://www.IRS.gov/Businesses/Small-Businesses-&-Self-Employed/Audit-Techniques-Guides-(ATGs)).

³ The oil and gas guide is at www.IRS.gov/pub/irs-mssp/oilgas.pdf.

Completion of Pre-Examination Due Diligence

After conducting all the pre-examination due diligence, sit down and discuss the findings of all relevant information with the taxpayer before the beginning of the IRS examination. The discussion with the taxpayer will obviously direct the course of the IRS examination. For example, many taxpayers believe very strongly in immediately identifying return errors prior to or simultaneous with the first IRS examination meeting. Other taxpayers prefer to take a wait-and-see approach to determine which items, returns, and years the IRS will choose to examine.

The Examination

Cooperation and Forthrightness

The goal of every IRS examination is the same—early and complete resolution. The challenge to many practitioners is how to achieve this goal. Initially, to achieve the goal of early and complete resolution, it is important not to turn the examination into a hostile and adversarial event. To avoid unnecessary conflict in an IRS examination, cooperating with the examiner in a timely manner is a must. Within the ambit of cooperation, don't forget to humanize the audit process. Never forget that the IRS auditor is a fellow tax professional who is doing their best to complete their job as efficiently and ethically as possible. The instances where practitioners may not feel or believe that the IRS is conducting themselves in such a professional manner are few and far between.

During the examination itself, the practitioner must avoid providing misleading information of any kind. All a practitioner has working with the IRS is the practitioner's credibility and reputation. Once a practitioner loses their credibility with the IRS, it is rarely earned back.

Document Control

One of the most common mistakes practitioners make during an examination is lack of document control. Specifically, the practitioner at any point in time should be able to produce an exact duplicate of the documents provided to the IRS examiner. It is simply not enough that the practitioner can recreate the documents provided to the IRS. The practitioners must have exact copies, electronic or paper, of the documents provided along with a log of when the documents were provided. Many times, it is much easier for the practitioners and the IRS to refer back to previously provided documents when documents are actually stamped with sequential numbers starting with the

number one and going up to the last page provided to the IRS. This is often called “Bates numbering” the documents.

Interviews

Many practitioners are unsure of how to respond to an IRS request to interview the taxpayer. First, the practitioner must understand that in addition to interviewing the taxpayer, the IRS will also want to interview the tax preparer as well. When the tax preparer and the practitioner representing the taxpayer in the IRS examination are the same person, it is important to recognize that a potential conflict of interest may arise or already exist.

In a perfect world, the IRS examiner will provide written questions in advance. Written questions in advance provide the most opportunity for the interviewee, be it the taxpayer or the tax preparer, to contemplate and provide the most accurate information possible. Typically, the interview can be much more productive when held closer to the tail end of the audit once the issues have crystallized for the IRS and the taxpayer. Remember the interview does not have to take place at the IRS office, but can take place some place where a taxpayer is more comfortable.

During the interview itself, it is important not to take an adversarial stance with the IRS. The interviewee should be comfortable and personable in responding to IRS questions. The biggest mistake that most interviewees make is trying to answer the way the interviewee believes the IRS wants them to answer. Instead, a golden rule for answering IRS questions is simple—“tell the truth.” Do not try to slant the answers. The second most important rule when answering questions for the IRS examiner is to ask for clarity if the interviewee does not understand the question presented.

Tour of Business

Expect the IRS to request a tour of the business site. During the tour of the business, it is important to have someone knowledgeable about the business activities of a taxpayer available. In many cases, this is not the president or CEO or even accounting staff, but rather someone who understands the nature of the business. The designated person in charge of the business tour should explain the business practices and the different processes which are prevalent in the taxpayer’s business. Again, the business tour should not be designed to answer accounting and tax questions but rather to explain how it is the taxpayer conducts business. It is important to remember that the business tour does not have to disrupt business operations.

Information Document Requests

During the examination, the IRS will issue written requests for information known as information document requests (IDRs). Once a taxpayer receives an IDR, it is important to provide a timely and complete response. Taxpayers who do not provide timely and complete responses may be faced with a summons from the IRS, either directly to the taxpayer or to the taxpayer's professionals. It is very important that the taxpayer's professionals remember that a summons on its face does not result in a waiver of either the attorney/client privilege, the work product doctrine, the accountant/client privilege, or the duty of confidentiality that a CPA maintains with respect to its client in the State of Texas. Accordingly, the recipient of a summons should seek counsel from an experienced tax attorney prior to providing information to the IRS.

In many cases, information cannot be provided to the IRS absent the taxpayer's consent, which should be in written form. In most audits, the taxpayer wants to cooperate and provide information to the IRS in a timely and reasonable basis. Thus, in most situations, taxpayers gladly will provide the necessary consent for the recipient to comply with the IRS summons. However, in rare cases in which the taxpayer does not provide consent to comply with an IRS summons, the recipient of the summons may be in a position in which they cannot provide the information to the IRS absent a court order. Just as the issuance of a summons or subpoena on its face is not enough to require production, the mere existence of an enforcement proceeding is not enough to force production. A court order is required to release the practitioner from its obligations to maintain the confidentiality of taxpayer information in the rare case in which the taxpayer refuses to give consent.

Statute of Limitations Extensions

It is not uncommon for the IRS to request an extension of the statute of limitations beyond the general three year period. When faced with a request to extend the statute of limitations, many practitioners are not aware that the IRS does not consider a refusal to extend the statute of limitations an act of non-cooperation. So the question arises: Why does the IRS want the extension and how will that extension benefit the taxpayer in the examination process? If it is determined that the extension of the statute of limitations will benefit the taxpayer in the IRS examination process, the practitioner must next determine how to advise the taxpayer on the execution of the statute of limitations extension. A practitioner should never recommend to a taxpayer that a statute of limitations extension with an unlimited period of time be executed. This is simply one of the absolutes in tax controversy practice. A more difficult

question is how much time is reasonable to provide for the extension. Also consider whether to request a restricted statute of limitations extension based upon limited issues. The IRS is not always in favor of such a request.

Income-Probing Methods and Badges of Fraud

The IRS conducts an income probe in all examinations. When the IRS is not satisfied with the books and records of the business, the IRS will often employ an indirect method of determining income. In a basic situation, the IRS may decide to employ an indirect method of determining income when a tax return shows income of \$30,000 a year and yet the taxpayer lives in a \$1,000,000 home. The IRS examiner will look for unexplained bank deposits to determine if they actually represent income which did not find its way onto the tax return. The IRS examiner will also look for expenditures in excess of known financial resources. In every examination, in order to explain excessive expenditures, the IRS will ask whether or not the taxpayer has a cash hoard or other source of non-taxable funds such as loans or inheritances. Likewise, the IRS examiner will look for unexplained increases in net worth that are not supported by the tax returns in issue. This type of analysis applies to business returns as well. Be prepared to prove how the business obtained the funds used to operate when the source is not patently obvious on the face of the business returns.

The indirect methods of determining income may yield large amounts of unexplained income, which the IRS will determine in the civil examination whether or not certain badges of fraud exist. One of the biggest potential badges of fraud is the actual conduct of a taxpayer and the taxpayer's representative during the examination. Because of this, the interview of a tax preparer and the taxpayer become important items if it is determined in the pre-examination due diligence that substantial unreported income may exist. Another badge of fraud the IRS looks for is false or duplicate invoices and multiple sets of books and records. The IRS also looks for concealment activities—patterns of errors which the IRS believes are actually intentional and systemic check-cashing patterns. Finally, the IRS examiner will look into banking records to determine if the taxpayer has been moving large amounts of cash in and out of the bank.

Freedom of Information Act

At any point during the course of the audit, if a practitioner wants to determine what information the IRS has accumulated regarding a taxpayer, the tool to use is a Freedom of Information Act (FOIA) Request. The actual form for a FOIA Request is located on the IRS website. The FOIA form can be filed

at the very beginning of an audit, at any point during the audit, or after the conclusion of the audit.

The FOIA can often provide a trove of information to help explain to taxpayers why the IRS is making large proposed adjustments when the taxpayer does not understand the reason for such adjustments. In addition to the FOIA request, a taxpayer can also request that the IRS disclose a list of third-party contacts that the IRS has made throughout the course of the examination. Unfortunately, the IRS is permitted to withhold the identity of certain third parties contacted during the course of an examination if there is a potential for reprisal to the individual. Consider a current or ex-employee who has been cooperating with the IRS during the company audit as someone who could face reprisal for their actions.

Penalties

Should the examination result in an IRS finding of underpayment of tax, the IRS will often consider asserting penalties on the taxpayer, and may also include potential penalties on the tax preparer. Because of the potential for penalties on the tax preparer, a practitioner who has prepared the return should carefully consider whether or not to represent the taxpayer during the course of an examination. With respect to taxpayer penalties, taxpayers who relied on a tax professional can assert a reasonable cause defense as outlined in the Internal Revenue Manual § 20.1.1, "Introduction and Penalty Relief." Another method to avoid penalties is to file a Form 8275 Disclosure Statement. In filing a disclosure statement, it is important to be complete and accurate. The disclosure statement is not the place for aggressive and incomplete positions.

Post Examination

Once the examination is complete and the examiner has proposed a deficiency in tax and potential penalties, what is the next step? The next step includes the possibility of requesting a conference with the examiner's manager. At the manager meeting, the practitioner has the opportunity to explain to the manager the errors in the examiner's logic or findings. Practically, the examiner's manager has been involved in the process of the examination since the beginning, has been kept abreast of the examiner's findings, and is unlikely to make any changes. If an examiner acts in an abusive manner, however, the examiner's manager can provide a course of relief.

At the conclusion of an examination, the IRS will issue the revenue agent's report, also known as a 30-day letter. The revenue agent's report

outlines the IRS adjustments and ideally contains the rationale for the IRS adjustments. One option the taxpayer may take with respect to a revenue agent report is to file a protest within the 30-day deadline. Many practitioners are unaware that in certain circumstances they may request an extension of the 30-day period to file a protest. The protest lays out in detail a listing of all unagreed changes to the revenue agent report. The protest also includes the factual and legal basis upon which the taxpayer is challenging the IRS examiner's findings. The protest to the revenue agent's report is forwarded to the IRS examiner, who considers the protest and drafts a rebuttal report. The rebuttal report is not shared with the taxpayer, but is included in the IRS administrative file.

The protest also requests that the IRS Appeals Division consider the points raised by the taxpayer. The IRS Appeals Division is tasked with the job of independently negotiating a settlement with the taxpayer. The Appeals Division will receive a copy of the examiner's rebuttal report even though the taxpayer will not. When the IRS Appeals Division is settling the case, it may take into account the "hazards of litigation," which is a method of settlement that the IRS examiner is not permitted to consider in resolving the case at the examination level.

Should the case not be settled in the IRS Appeals Division as a result of the protest, or should the taxpayer not file a protest, the IRS will issue a notice of deficiency, which is typically referred as a 90-day letter.⁴ The most important aspect of a notice of deficiency is that the 90-day period to respond to the notice of deficiency is a hard deadline. No matter how sad the tragedy that befalls the taxpayer, the 90-day period of time cannot be extended. Once a taxpayer receives a notice of deficiency, the taxpayer can file a petition with the United States Tax Court, in which case the taxpayer will not be required to pay the amount in issue prior to bringing its lawsuit in the United States Tax Court. A conservative taxpayer, however, will post a bond before filing the Tax Court petition or make a payment after filing the Tax Court petition in order to stop the running of interest as the taxpayer moves forward to resolve the case. If a case is filed in the United States Tax Court, in some instances a taxpayer who has not already been to the Appeals Division of the IRS may attempt to settle its case there. In other instances, a taxpayer may have the opportunity to attempt to settle the case with the IRS counsel attorney. In certain rare cases, taxpayers will not be permitted to conduct settlement discussions because the case is designated for litigation.

⁴ In a partnership examination subject to TEFRA rules, the equivalent to a notice of deficiency is a Final Partnership Administrative Adjustment (FPAA), which contains a 90-day deadline for the Tax Matters Partner to file a tax court petition, and an additional 60-day period for a notice partner to file if the Tax Matters Partner did not.

A taxpayer who does not petition the United States Tax Court will be directly assessed for the tax and penalties proposed in the 90-day letter. After tax and penalties are assessed with accompanying interest, the taxpayer can pay the assessed amounts and file an administrative claim for refund. After six months, *if the IRS does not deny the claim for refund beforehand*, the taxpayer can then file a refund lawsuit in federal district court or the Court of Federal Claims.

Conclusion

The examination process with the IRS provides many opportunities to successfully achieve an early and complete resolution of a tax matter with the IRS. Utmost care should be exercised during the examination process to avoid it becoming adversarial and unduly burdensome. It is imperative during the examination process that the practitioner know exactly which division and who within that division the taxpayer is working with. For example, an examination with the SEP unit of Examination is a much different experience than an examination with the Large Business and International Division of the IRS. As a final cautionary note, practitioners who also prepared the return at issue should carefully consider whether or not a potential conflict of interest may exist in light of the IRS's proclamations that, in appropriate cases, preparer penalties will be considered during the course of an examination in addition to standard accuracy-related penalties for taxpayers.