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Tax Practice & Procedures

2010 Estate Tax Rules • Offshore Voluntary Disclosure Initiative • Due Diligence in Filing Extensions • 90-Day Letters and Undeliverable Mail • IRS Correspondence Examinations

Death and Taxes: Executors Beware

The Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010 (2010 Tax Relief Act), P.L. 111-312, was signed by President Barack Obama on December 17, 2010, and revised tax law for estates of decedents dying in 2010, 2011, or 2012. The pre-2001 rules will be reinstated for deaths starting in 2013 unless Congress acts again before 2013. The new rules apply for 2010 unless an executor elects to use prior law. This election is made on Form 8939, Allocation of Increase in Basis for Property Acquired from a Decedent. However, the IRS has not yet released a final version of Form 8939. Elections for 2010 decedents can be made at a time not less than nine months from December 17, 2010, so estates of decedents dying in early 2010 can still be made timely.

The 2010 Tax Relief Act provides a $5 million estate tax exemption (indexed for inflation after 2011), a step-up in basis to market value, a top rate of 35% on taxable transfers (Sec. 2001(c), as amended by the 2010 Tax Relief Act, §302(a)(2)), and portability of unused exemptions between spouses for 2011 and 2012. Portability allows the estate of the second spouse to die to claim the unused exemption not claimed by the estate of the first spouse to die *if* the executor of the first-to-die spouse makes a timely election on the estate tax return of the first-to-die spouse. This effectively creates a $10 million exemption for married couples.

The 2010 Tax Relief Act also increased the lifetime gift tax exemption to $5 million starting in 2011. The generation-skipping transfer (GST) tax was reinstated, but the rate is zero for transfers in 2010, with a $1 million exemption. The GST tax is reunified with the gift tax ($5 million exemption) for 2011 and 2012.

The election in the 2010 Tax Relief Act to apply prior law may create traps for executors and affect beneficiaries, so understanding the election and preparing scenarios for 2010 deaths using old and new law is critical post-death planning. Some commentators believe that executors (and tax return preparers) may face litigation if the election decision adversely affects some classes of beneficiaries and their interests are not fully considered (and possibly should even compensate those heirs hit with higher income taxes that will result if an election is made to use the old law modified carryover basis instead of the new law step-up to fair market value (FMV)).

The old law was the Economic Growth and Tax Relief Reconciliation Act of 2001 (EGTRRA), P.L. 107-16, which repealed the estate tax for decedents dying after December 31, 2009, but before January 1, 2011. For 2010, estates were allowed to pay no estate tax, but assets in the estate did not receive a step-up in basis to FMV at the date of death or alternate valuation date (Sec. 1022, as amended by EGTRRA, §542). The basis in heirs' assets was to be determined under the modified carryover basis rules under Sec. 1022, treating property as acquired by gift, with basis being the lower of the decedent's adjusted basis at date of death or FMV at death. Basis was subject to a special allocation of $1,300,000 (increased for unrealized losses and unused capital losses and net operating loss carryovers not exceeding FMV at death) plus an additional allocation of $3 million if distributed to a spouse (see also Joint Committee on Taxation, *Technical Explanation of the Revenue Provisions Contained in the "Tax Relief, Unemployment Insurance Reauthorization, and Job Creation Act of 2010"* (JCX-55-10), p. 42 (December 10, 2010)).

We do not yet know whether Congress will apply pre-EGTRRA rules ($1 million exemption, 55% rate) for deaths after 2012 or make further changes before 2013. This makes planning highly complex and perhaps further complicates it if there is a first-to-die spouse in 2010. However, if the increase to a $5 million exemption and portability between spouses of the exemption becomes permanent, fewer people may need estate planning and may rely on the exemptions to cover their needs.

For deaths in 2010, the new rules apply unless an executor elects to have the EGTRRA rules apply, which provide for no estate tax and modified carryover basis. The due date for filing an estate tax return, paying the estate tax, and making any disclaimer of assets will be not earlier than nine months after December 17, 2010 (2010 Tax Relief Act, §301(d)(1); Sec. 6075). Therefore, executors may be called upon to justify their choice of whether to use the old rules or the new rules by some classes of heirs, leading to possible litigation if the parties are negatively affected. The election will in some cases result in a lower estate tax but create income tax burdens for selected beneficiaries by using modified carryover basis.

For example, depending on the terms of the will, estate taxes may be paid from the residuary estate and not burden specific bequests. If an election is made to use the old rules and pay no estate tax, which benefits residuary beneficiaries, while giving up a step-up in basis, that election may negatively affect beneficiaries of specific bequests who get a lower basis in assets received and higher income tax if the asset is sold.

Similar issues may arise when the executor is called upon to make the special basis adjustments and one group of beneficiaries is favored over another. Will those affected have a cause against the executor and other tax planners? If the estate tax was to be paid by residuary beneficiaries, has the recipient or a specific beneficiary been injured? Will executors who are also beneficiaries have a conflict of interest when deciding whether to elect the old law or the new law?

There are other examples where the interests of parties could be affected by making the election. If the decedent is a first-to-die spouse with a well-written document leaving assets to a bypass trust and the surviving spouse, no immediate estate tax is due. What if the estate is asset rich, cash poor, but valued over $10 million? If the surviving spouse wants to convert assets to cash to pay estate tax upon his or her death, a step-up in basis may in some cases be the best choice to allow asset sales with little or no income tax while providing cash to pay the second-to-die estate tax. The tax planner would have to run the numbers using various scenarios.

Some commentators have suggested that executors air the issue with beneficiaries and even request a court determination before deciding whether to make the election. Accountants advising executors or preparing estate tax filings might well request some indemnification or make clear that this decision is made by the estate with an understanding of the impact on various classes of beneficiaries.

From Joseph D. Brophy, MBA, CPA/ABV, CVA, CM&AA

Offshore Voluntary Disclosure Initiative

On February 8, the IRS announced another special voluntary disclosure initiative designed to bring U.S. persons hiding assets offshore back into the U.S. tax system (IR-2011-14). This is potentially good news for those taxpayers who did not know about the first two initiatives, but the penalties associated with the disclosure are higher and the terms slightly different. This new initiative, the 2011 Offshore Voluntary Disclosure Initiative (2011 OVDI), will be available only through August 31, 2011. This item discusses some of the history related to the IRS effort to bring U.S. persons into compliance.

U.S. persons (individuals, corporations, partnerships, limited liability companies, and trusts) are required to report the income earned from investments held in foreign financial accounts. Any persons who have a financial interest in or signatory authority over any financial account or accounts, if the aggregate value of the accounts at any time during the year exceeds $10,000, must file Form TD F 90-22.1, Report of Foreign Bank and Financial Accounts (FBAR) (rev. October 2008). The penalties for failure to comply with the reporting and filing requirements are steep; the failure to check the box "yes" for disclosing foreign accounts on an individual tax return, Schedule B, is a potential felony. Therefore, taking advantage of the IRS's compliance programs avoids possible prosecution.

In addition, with the IRS currently implementing the Foreign Account Tax Compliance Act (FATCA), which was enacted as part of the Hiring Incentives to Restore Employment (HIRE) Act, P.L. 111-147, in 2010, Congress has provided the IRS with more transparency and better tools to track down Americans with offshore assets. Beginning with the 2011 tax year (for years beginning after March 18, 2010), in addition to the FBAR reporting requirements, U.S. individuals holding specified foreign assets with an aggregate value of all assets exceeding $50,000 will be required to file Form 8938, Statement of Foreign Financial Assets, with their tax return.

The IRS initiated the first offshore voluntary compliance program in 2003. Called the Last Chance Compliance Initiative, it resulted in very few individuals entering the program because there was little incentive to disclose offshore investments. The second initiative, which started in March 2009, was spiced with an added incentive for individuals to come forward based upon the August 2009 agreement between the United States and Switzerland to disclose the names of some of UBS AG's U.S. investors. The IRS and the Department of Justice Tax Division stated that they would prosecute investors with UBS accounts in Switzerland who did not enter into the 2009 Offshore Voluntary Disclosure Initiative (2009 OVDI) before they received notification from the IRS that they were under investigation.

One of these investors did plead guilty to tax evasion for the failure to report his income from foreign investments but was found not guilty for the willful failure to report his interest in the offshore bank accounts on the FBAR form. In this district court case, *Williams*, No. 1:09-cv-437

(E.D. Va. 9/1/10), the government had previous knowledge of the foreign bank accounts and had frozen the accounts; therefore, the failure to check the box on Form 1040, Schedule B, Part III, Foreign and Accounts and Trusts, and the failure to timely file the FBAR form was determined not to be a willful failure because the government already knew about them.

The 2009 OVDI ended on October 15, 2009. According to IRS Commissioner Douglas Shulman, the IRS received disclosures of approximately 15,000 taxpayer participants. During this time frame, the IRS discovered numerous other schemes and promoters in many foreign countries, not just UBS account holders.

The IRS Criminal Investigation Division worked with IRS management to develop a settlement in connection with the 2009 OVDI for taxpayers to pay back taxes and interest for six years (2003–2008) and agree to a 20% understatement penalty on the tax and a 20% penalty (reduced to 5% in certain very limited circumstances) based on the highest aggregate balance of their foreign accounts during that six-year period. This agreement was in lieu of all other penalties that the IRS could have assessed in its normal voluntary disclosure program (i.e., civil fraud penalties, FBAR penalties, Form 5320 penalties), which could possibly result in the confiscation of the entire foreign account(s).

The 2011 OVDI increased the penalty on the aggregate account balance to 25% and extended the number of years from six to eight, starting with 2003 and ending in 2010. The 25% penalty is reduced to 5% or 12.5% in limited circumstances. If the offshore accounts or assets do not exceed $75,000 in any calendar year, the 12.5% penalty might apply. The 20% accuracy-related penalty or the failure to file and pay penalties, if applicable, will be applied to the underpayment of tax for all years. Plus, interest will run on the tax and accuracy-related penalty from the due date of the return.

The 2009 OVDI appeared simple in concept, but the IRS had a bit of a bumpy road in implementing the program. Different procedures had to be worked out and changed and then changed again. Most of these changes have been implemented in the 2011 OVDI:

- Requiring powers of attorney with specified requirements;
- Requiring extensions of the civil statute of limitation on Form 872, Consent to Extend the Time to Assess Tax;
- Demanding the prompt filing of amended returns and FBARs (the 2011 OVDI requires all forms to be filed by August 31, 2011); and
- Mark-to-market computations as an alternative to the statutory PFIC computations with a 20% tax rate on the gains and a 7% interest charge on the 2003 tax from that gain.

The IRS assigned revenue agents without previous training in international tax issues to the 2009 OVDI. The rules relating to passive foreign investment companies (PFIC) became one of the biggest headaches for both agents and practitioners. Many of the foreign bankers invested taxpayer money in foreign mutual funds, which reinvested the capital gains back into the funds. The PFIC rules relating to throwback interest computations on this income made it difficult, if not impossible, to calculate due to the lack of historical information. The IRS did adopt a modified mark-to-market method, which simplified the requirements. For any PFIC investment retained beyond December 31, 2010, the taxpayer must continue using the mark-to-market method but will apply the normal statutory rules of Sec. 1296 as well as the provisions of Secs. 1291–1298, as applicable.

It is interesting that the IRS has started yet another OVDI program. Historically, some taxpayers with offshore accounts filed amended tax returns that included previously unreported income in a "quiet" disclosure. Under this method, the IRS did not assess penalties, and only the tax and interest were due with the filings. If the taxpayer made a "noisy" voluntary disclosure through the IRS Criminal Investigation Division, there was typically a civil audit, and fraud penalties might be assessed. Now the IRS warns professionals that a quiet voluntary disclosure will no longer be acceptable. Taxpayers who have already made a quiet disclosure are eligible for the 2011 OVDI.

In the meantime, countries that previously guarded their bank secrecy rules are entering into mutual assistance agreements and exchanging information with the United States much more rapidly than in the past. Commissioner Shulman warned taxpayers that the IRS is not letting up on the international tax issues and that the risk of getting caught will only increase. Professionals need to make sure their clients are filing in conformity with the rules and specifically making inquiries regarding offshore accounts or investments.

From Mary Lou Gervie, CPA, CFE, CFF, Bethesda, MD

The Need for Increased Due Diligence in Filing Extensions

The complexities associated with return preparation, tax law, and the April 15 deadline have required practitioners to devote more time to preparing returns. As a consequence, more extensions of time to file are being filed.

The IRS has indicated that taxpayers should file a Form 4868, Application for Automatic Extension of Time to File U.S. Individual Income Tax Return. The instructions for filing a Form 4868 require taxpayers to:

- Properly estimate their tax liability using the information available to them;
- Enter their total tax liability on line 4 of Form 4868; and
- File Form 4868 by the regular due date of their return.

Normally, filing this form results in an automatic six-month extension of time to file without any late-filing penalty. However, filing the form does not extend time to pay any income tax liability due. The estimated taxes due should be paid with the extension application. Interest is charged on a material underpayment of tax from the original due date of the return until the tax is paid, and a late payment penalty may also be due. The interest rate varies quarterly with the federal short-term interest rate.

Regulations provide relief from penalties only if the balance due on Form 1040 is less than 10% of the total tax shown on that form and is remitted with the return.

If the balance due is more than 10% or is not remitted with the return, the penalty may apply to the total of the balance due from the original due date of Form 1040 to the date of payment, unless the taxpayer establishes reasonable cause (Regs. Sec. 301.6651-1(c)(3)).

In addition to these concerns with the federal extension, applicable state extensions and the rules and regulations associated with them require the same careful consideration. The requirement to electronically file some state extensions raises the due diligence required by practitioners.

Office Procedures

Increased monitoring by the states and the IRS of both practitioners and tax returns may cause many practitioners to rethink their office procedures in dealing with clients who desire to extend their individual income tax returns.

First, there is the need to accurately estimate a client's tax liability when an extension is filed. Second, the practitioner should advise clients that if an extension is filed on their behalf, it is an extension of time to file only and not an extension of time to pay. Some clients have the misconception that the filed extension extends not only the time for filing but the time for paying the tax due. Clients should also know that penalty and interest apply to any balances due in excess of 10% of the total tax shown on the tax return. This could be done in the engagement letter with the client. Sample language can be found in the engagement letters included in the AICPA Tax Practice Guides and Checklists:

> If an extension of time to file is required, any tax due with this return must be paid with the extension. Any amounts not paid by the filing deadline may be subject to interest and penalties.

More information on sample engagement letters is available at www.aicpa.org/interestareas/tax/resources/taxpracticeimprovement/pages/default.aspx.

Third, the practitioner may want to have an affirmative indication from the client authorizing the filing of an extension, including the amount of federal and state withholding and estimated tax payments. This should contain language indicating that the taxpayer understands he or she may also be required to make estimated tax payments for the current tax year.

These office procedures would be consistent with IRS rules in Circular 230, particularly Sections 10.22 (Diligence as to Accuracy) and 10.33 (Best Practices). In addition, the IRS has indicated its desire for more oversight of all income tax preparers. Kip Dellinger argues that courts—and in particular the IRS—are increasing what constitutes return preparer due diligence (see Dellinger, "Return Preparer Due Diligence and the IRS: The Looming Battle," 128 *Tax Notes* 889 (August 23, 2010)). It is not inconceivable that the IRS could develop computer criteria in the future to invalidate extensions if the requirements of Sec. 6651 are not met. State revenue departments could also do this.

Reasons for Additional Office Procedures

Liability insurers have noted an increased number of claims resulting from extensions (Lee, "Frequent Tax Claims Against CPAs," *AZ CPA* (February 2007)). In addition, there have been some court cases that merit consideration of additional office procedures in the preparation of extensions.

In *Crocker*, 92 T.C. 899 (1989), the Tax Court held that the IRS could void the automatic extension because the taxpayers "did not make a bona fide and reasonable estimate of their tax liabilities nor did they make a bona fide and reasonable attempt to secure the information necessary to make such an estimate."

In *Haddad Motor Group, Inc. v. Karp, Ackerman, Skabowski & Hogan, P.C.*, 603 F.3d 1 (1st Cir. 2010), accountants were held liable in a civil suit brought by the client for the client's nonpayment of estimated quarterly taxes and estimated tax due with the extension of time to file the return. The court found the accountants liable for deceiving the client as to its tax liability related to the closeout of a margin-against-the-box transaction and conversion to an S corporation.

The client closed out the transaction in February 1999, thus incurring a built-in gains tax liability on the transaction. The accountants failed to have the client make any estimated payments based on the liability from the transaction. In December 1999, the accountants advised the client of the built-in gains tax liability and for other reasons recommended that the client file an extension of time to file taxes (Form 7004, Application for Automatic Extension of Time to File Certain Business Income Tax, Information, and Other Returns). However, the accounting firm did not consider the large built-in-gains tax in the estimated tax liability shown on Form 7004. Therefore, the IRS assessed penalties against the client for underpayment of estimated taxes and assessed interest for failing to pay tax from the original due date of the return through the extended due date.

In the client's suit against the accountants, the jury awarded damages for federal and state interest and penalties incurred (only) from the original due date through the extended due date. The judge also awarded damages for the interest and penalties on the failure to make adequate quarterly estimated tax payments, plus treble damages and attorneys' fees and court costs under MA Gen. Law, ch. 93A. Although the total amount the client was charged in interest and penalties attributable to the transaction was about $12,350, the firm ended up paying over $250,000 to the client as a result of the litigation.

Conclusion

Practitioners should consider including language on extensions in their engagement letters, regardless of whether positive or negative letters are used. The client should provide written confirmation of authorization to file the extension with withholding and estimated tax payments included. The extension authorization letter should include a notation that the client may be required to make estimated tax payments for the current year. In addition, documentation of any estimates and calculations should be retained in the client file for future reference. It takes only one engagement that goes astray to cause

many sleepless nights for a practitioner. These ideas are a means of preventing this from this happening.

From Gerard H. Schreiber Jr., CPA, Metairie, LA, and Valrie Chambers, Ph.D., CPA, Corpus Christi, TX

90-Day Letter Does Not Start If Mail Is Undeliverable, Rules One Court

In *Terrell*, No. 09-60822 (5th Cir. 11/1/10), the Fifth Circuit held that a statutory notice that was mailed to an incorrect address and returned by the Postal Service was null and void. Accordingly, the issue on which the circuits are split—whether the limitation period for filing a petition for review with the Tax Court begins when an incorrectly addressed notice is mailed or when it is actually received—was not implicated. The 90-day period did not begin until the IRS re-mailed the notice to the correct address.

Background

The IRS mailed the taxpayer a notice of the secretary's final determination denying innocent spouse relief and stating that she had 90 days to file a petition for review with the Tax Court. The taxpayer had moved before the date the notice was mailed; as a result, the Postal Service returned the notice to the IRS as undeliverable. Subsequent to the mailing of the original notice, but prior to the date the notice was returned, the taxpayer filed her 2006 income tax return listing her current address.

After receiving the returned notice, the IRS searched its database again and found the taxpayer's new address. The IRS then re-mailed the notice to her correct address, and the taxpayer received it. The re-mailed notice was identical to the original notice and listed the mailing date of the original notice as the determination date of the taxpayer's claim.

The taxpayer appealed the final determination to the Tax Court within 90 days of the date on which the notice was re-mailed but more than 90 days after the date of mailing of the original notice. The Tax Court determined that it did not have jurisdiction to hear the taxpayer's claim because she did not file her petition for review within 90 days of the mailing of the original notice. It found that the IRS had acted with reasonable diligence in determining her last known address for the purpose of the initial mailing and resending the notice to her correct address. Therefore, the 90-day period began on the date the IRS mailed the original notice.

Statutory Notice Requirement

Sec. 6015 requires that notice of the final determination be sent to the taxpayer's "last known address" and provides that the taxpayer has 90 days from the date of mailing of the notice to petition the Tax Court for review. To fulfill the statutory notice requirement, the IRS must use reasonable diligence in light of all of the facts and circumstances to determine the last known address, but, absent clear and concise notification by a taxpayer of a change of address, the IRS may generally consider the address on the taxpayer's most recently filed tax return as the taxpayer's last known address.

In cases in which the IRS failed to mail the notice to the last known address but the taxpayer subsequently received the notice anyway, the federal circuits are split on the issue of when the 90-day period in which an appeal must be filed begins to run. In dealing with analogous statutory notice provisions in other Code sections, the First, Second, Third, Sixth, Ninth, and Eleventh Circuits have adopted the rule that if a taxpayer actually received the notice that was sent and the delay did not prejudice his or her ability to petition the Tax Court for review, the 90-day limitation period begins on the date of mailing of the notice. On similar facts, the Fourth, Seventh, and D.C. Circuits have held that the limitation period begins on the date the taxpayer actually received the notice.

Fifth Circuit's Decision

The Fifth Circuit found that the Tax Court erred when it determined that the IRS had acted with reasonable diligence in mailing the original notice because the Postal Service had returned as undeliverable three prior mailings that the IRS had sent to the address to which it sent the original notice. The appeals court held that even though it had not yet received notification from the taxpayer that her address had changed, the IRS was on notice at the time it mailed the original notice that the address that it had on file was incorrect, and reasonable diligence required that it use the resources available to it to attempt to locate a valid address for the taxpayer.

The Fifth Circuit distinguished *Terrell* from the cases on which the other circuits have split on the issue of the commencement of the limitation period. In those cases, the taxpayer ultimately received the original notice that the IRS mailed. In *Terrell*, the Postal Service returned the original notice to the IRS. Accordingly, the court held that the original notice was null and void because the IRS did not mail it to the taxpayer's last known address and the taxpayer never received it. The 90-day limitation period began when the IRS remailed the notice to the correct address.

From John C. Slatten, J.D., CPA/PFS, Indianapolis, IN

IRS Correspondence Examinations

The IRS has expanded the use of correspondence examinations of individual income tax returns. The IRS initiates a correspondence examination by mailing either Letter 566 (CG), often termed an initial contact letter, advising the taxpayer that a return has been selected and listing the items to be verified, or a CP 2000 notice, which contains proposed adjustments based on information documents issued by third parties, such as Forms W-2, Wage and Tax Statement, 1099-MISC, Miscellaneous Income, and 1098, Mortgage Interest Statement. The examinations are handled at an IRS Service Center or campus.

Selection of Returns

When the IRS receives returns, it compares them against norms for similar types of returns. The IRS develops the norms from audits of statistical random samples of returns that are selected as part of the National Research Program, which the IRS conducts to update return selection information.

The IRS typically selects returns for correspondence examinations based on data indicating that the taxpayer has not reported income, claimed improper deductions, or claimed erroneous tax credits. Some typical items for which the IRS requests verification include alimony, moving expenses, various itemized deductions, casualty losses, employee expenses, Schedule C receipts and expenses, foreign tax credits, earned income credits, and education credits.

Responding to Correspondence

A practitioner should advise a client in advance, usually by having an explanatory paragraph in the tax engagement letter, to notify the preparer if the client receives correspondence from the IRS. Clients sometimes presume that notices are correct and pay proposed assessments without contacting their return preparers.

After securing a power of attorney from the client, the CPA should carefully study the IRS notice along with the tax return and supporting documents. If the CP 2000 notice is correct, the CPA should advise the taxpayer to sign the agreement sent with the letter and pay the deficiency.

If an assessment in a CP 2000 notice is incorrect or if a response is to be made to the initial contact letter, the practitioner should consider whether to ask that the matter be transferred from the IRS campus to a local office. The IRS tends to not want to transfer cases because of the possibility of delay, and it is usually more economical for the agency to handle the matter by correspondence. Regs. Sec. 301.7605-1(e)(1) provides that the IRS will consider, on a case-by-case basis, written requests to change the examination venue. Many IRS campuses take the view that correspondence examinations will be transferred only in instances of hardship. If there are problems in transferring an examination, the practitioner may want to contact the local taxpayer advocate's office and request assistance in having the matter transferred to the local IRS office.

If the practitioner sends a written response to the IRS Service Center, he or she should submit the necessary documentation and explain whether an adjustment is appropriate.

Unlike a field examination, a correspondence audit is not assigned to a specific examiner. When the IRS receives correspondence, the file is assigned to an auditor. If there is no response from the taxpayer, the process moves through an automated system. After a certain period of time, the IRS issues a second notice, and if there is no reply, it will issue a statutory notice of deficiency or a 90-day letter.

IRS Problems

The IRS has been having workload problems in timely responding to taxpayer or practitioner letters that provide the requested information or express disagreement with proposed adjustments. Often correspondence is not assigned to the auditor who reviewed earlier documents. Correspondence tends to not be reviewed for several months, resulting in the IRS sending letters advising the taxpayer that it needs additional time to review the correspondence. When the IRS finally issues reports, in some cases the proposed adjustments are not correct because proper consideration and evaluation have not been given to the documents and substantiation furnished by the taxpayer or his or her representatives.

Reports of Other Offices

In 2010, the Treasury Inspector General for Tax Administration (TIGTA) issued a report conducted as part of Treasury's fiscal year 2009 annual audit plan, which concluded that correspondence audit results are sometimes inaccurate and overstated and that there are operational problems with the program, including significant mail processing delays (TIGTA, *The Discretionary Examination Program Performance Results Are Incomplete; Therefore, Some Measures Are Overstated and Inaccurate* (August 6, 2009), available at www.treasury.gov/tigta/auditreports/2009reports/200940099fr.pdf). The delays can result in taxpayers who send documentation in a timely manner being assessed taxes and interest because their correspondence was not dealt with promptly once it reached the IRS.

In her report to Congress for the office's fiscal year 2011 objectives, Nina Olson, the national taxpayer advocate, expressed concern about the correspondence audit program. (See www.irs.gov/pub/irs-utl/nta2011objectivesfinal..pdf for the complete report.) She found that statutory notices of deficiency were prematurely issued due to various problems:

- The IRS was not considering requests for managerial conferences and Appeals hearings;
- The IRS was not considering requests to transfer correspondence audit cases to local offices;
- Documentation was not being associated with audit cases because of inadequate procedures for receipt, control, and routing; and
- Issues were not being resolved because the IRS was not having enough phone conversations with taxpayers.

Olson is working with IRS correspondence audit improvement teams to correct procedures that result in the premature issuance of deficiency notices. She has also challenged the IRS to develop telephone contact strategies within the audit program to address shortcomings in addressing taxpayer needs.

From Joe Marchbein, CPA, Chesterfield, MO

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