Tax Report #930

# New York State Bar Association

One Elk Street, Albany, New York 12207 • 518/463-3200



#### **TAX SECTION**

398-1999 Administrative Committee

STEVEN C. TODRYS Simpson Thacher & Bartlett 425 Lexington Avenue New York, NY 10017 212/455-3750 FAX 212/455-2502 HAROLD R. HANDLER 1st Vice-Chair Simpson Thacher & Bartlett 425 Lexington Avenue New York, NY 10017 212/455-3110 FAX 212/455-2502 ROBERT H. SCARBOROUGH 2nd Vice-Chair

Sidley & Austin 875 Third Avenue New York, NY 10022 212/906-2317 AX 212/906-2021 ROBERT A. JACOBS

Secretary Milbank Tweed et al 1 Chase Manhattan Plaza New York, NY 10005 212/530-5664 FAX 212/530-0231

June 15, 1998

The Honorable Daniel P. Moynihan Ranking Minority Member Senate Committee on Finance SD-219 Dirksen Senate Office Building Washington, D.C. 20510-6200

Dear Senator Moynihan:

Because of time constraints, this letter has not been reviewed and approved by the 1/ Executive Committee of the Tax Section.

The Bill would suspend interest and certain time-related penalties for individual taxpayers if a "notice of deficiency" is not issued within one year of the timely filing date of the return. The suspension period would then run until 21 days after tax was actually assessed (i.e., a "notice and demand" for payment is issued). I believe that there are a number of problems with this proposal.

First, it is not realistic to expect a notice of deficiency to be issued within one year of the filing of a return. Even if an audit is commenced promptly (e.g., six months) after the return is filed, the audit procedure must allow the taxpayer a reasonable period of time to accumulate the relevant information and records, and must allow the IRS a reasonable period of time to review the information provided and determine any proper adjustments. The taxpayer is then entitled to protest any adjustments within 30 days (or longer if an extension of time is permitted) to the IRS Office of Appeals. A notice of deficiency is only issued after the Appeals Office has considered, and rejected, the taxpayer's protest. Even if the taxpayer does not attempt to delay the process, the one-year timetable will be very difficult for the IRS to meet.

Third, the "penalty" imposed on the IRS for failing to meet the one-year deadline is quite severe. Once the one-year period has expired, interest and penalties do not begin to accrue until a tax liability is finally determined and assessed, which may be years later after judgment has been entered following a judicial proceeding. Absent substantially increased resources devoted to the audit function, the IRS may feel compelled to respond to the provision by issuing notices of deficiency based upon incomplete audits before the one-year period expires in order to avoid the interest and penalty suspension. An increase in the number of notices of deficiency may also increase the number of cases docketed in the Tax Court.

## Due Process in Collection Actions (Sec. 3401 of the Bill)

The Bill contains two provisions to protect taxpayers from improper liens and levies. Liens and levies are made when the IRS has assessed (or the taxpayer has self-assessed) a tax liability. Therefore, under current law, the taxpayer's obligation to pay at the time of lien or levy is, generally, not in dispute. The Bill would allow taxpayers who have been properly assessed tax liability to delay collection for significant periods of time and to assert substantive tax issues that they failed to assert at an earlier point in the audit process.

I understand that the IRS processes thousands of levies per year. If even a small percentage of liens and levies are challenged through Appeals Office and judicial proceedings, the resources of the IRS and the Tax Court could be overwhelmed. If Congress is concerned that improper liens and levies are being issued, perhaps an additional 30-day period could be provided to taxpayers in order to permit summary court review before an improper collection action is undertaken.

## Innocent Spouse (Sec. 3201 of the Bill)

Concerns have been expressed with respect to joint and several liability for taxes on joint returns, and the difficulty, under current law, of obtaining innocent spouse relief. However, the provision of the Bill permitting an election to limit joint and several liability is an extraordinarily complex reaction to the problem. First, the provision involves an election mechanism that, presumably, would be filed for almost every joint return. Second, the election is not available if the electing individual had actual knowledge of the item giving rise to the deficiency. (However, as we read the Senate Finance Committee Report, the IRS has the burden of proving knowledge.) Third, assuming a valid election, the provision requires a calculation of the separate tax liabilities of the spouses. Fourth, the provision contains a series of elaborate (but necessary) safeguards intended to prevent taxpayers from defeating liability through certain asset transfers.

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## Burden of Proof (Sec. 3001 of the Bill)

The Tax Section has previously commented on the proposal to shift the burden of proof to the IRS. The Bill is a substantial improvement over prior drafts of the proposal. However, we continue to oppose this provision since we believe that it may increase the likelihood of more intrusive audits, and create confusion for the courts, taxpayers and the IRS as to when the issue is to be brought before the court, and when the burden has shifted.

In sum, many of the provisions of the Bill will provide well-deserved relief to taxpayers. However, the provisions discussed above are likely to impede, rather than aid, the determination and collection of the correct amount of tax liability.

An identical letter has been sent to Chairman Roth, Chairman Archer and Congressman Rangel.

Very truly yours,

Stever, C. Todrys

cc: Honorable Donald C. Lubick Honorable Charles O. Rossotti Honorable Stuart L. Brown Lindy L. Paull, Esq.

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Secretary Milbank Tweed et al 1 Chase Manhattan Plaza New York, NY 10005 212/530-5664 FAX 212/530-0231

ROBERT A. JACOBS

June 15, 1998

The Honorable Charles B. Rangel Ranking Minority Member Joint Committee on Taxation House of Representatives 2354 Rayburn Building Washington, D.C. 20515

Dear Congressman Rangel:

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**ROBERT A. JACOBS** Secretary Milbank Tweed et al 1 Chase Manhattan Plaza New York, NY 10005 212/530-5664

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