

# Going Beyond The Audit and IRS Collection Letter

Advanced Tax Controversy Issues You Need To Know  
About



*Seymour Chwast*

*"Remember, son, these are your tax-free years.  
Make the most of them."*



*"I'm sorry about this, but I'm afraid I just  
can't wait till April 15th."*

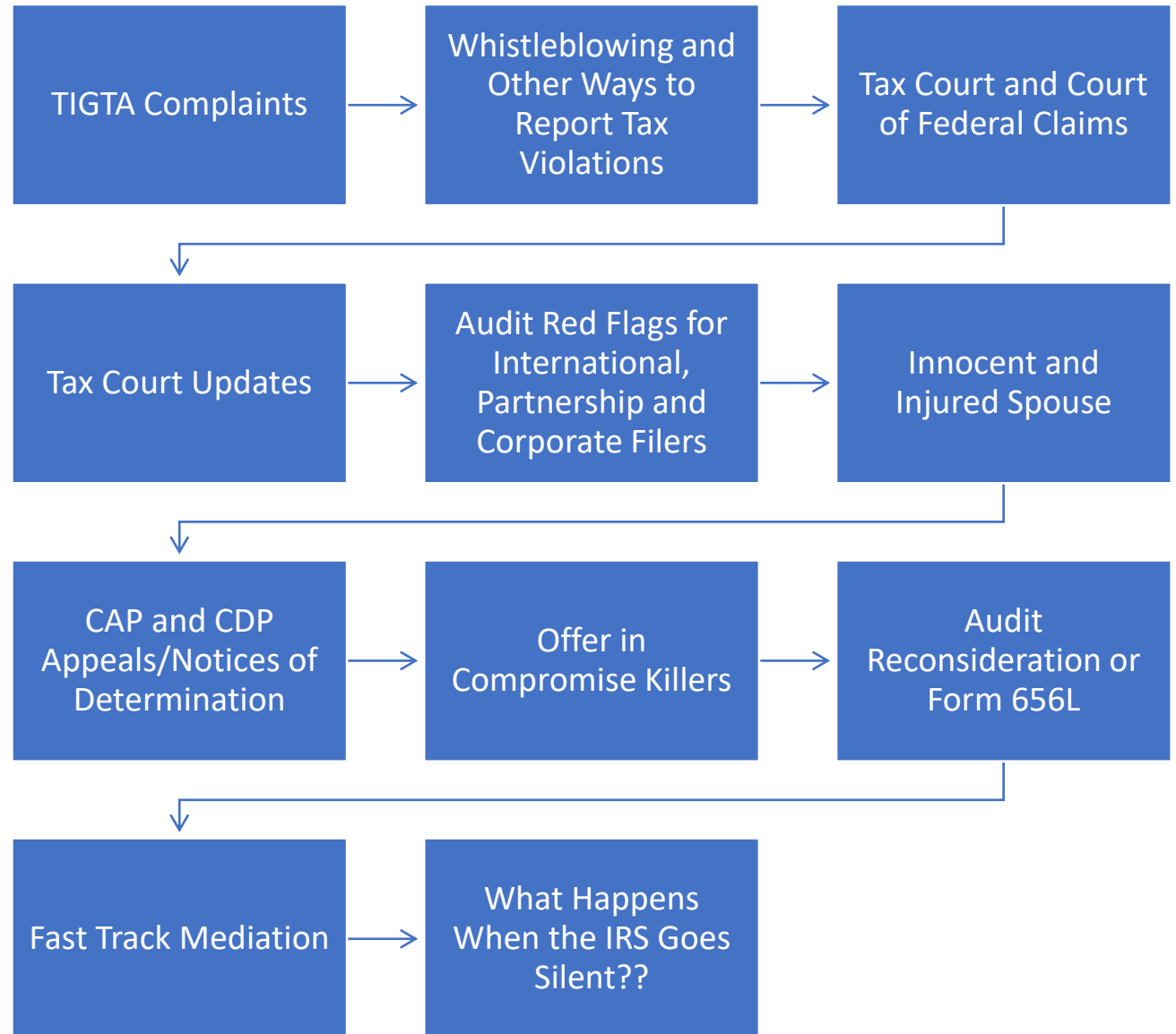
# Background

- Tax Attorney for 15 years. Started my firm six years ago. Practice mainly in Houston but can serve clients anywhere in the US
- Licensed in US Tax Court and Southern District of Texas
- How I can help you!
  1. IRS Letters
  2. Multistate
  3. Property Taxes/I sue appraisal districts!
  4. Tax Advisory



**Keith Cothroll**  
HOUSTON TAX ATTORNEY

# What we'll discuss today



# TIGTA Complaints: What are they?

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TIGTA complaints vary from complaints filed against IRS employees to whistleblowing and reporting tax fraud. [www.tigta.gov](http://www.tigta.gov)

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TIGTA also handles complaints by IRS employees against the public

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TIGTA handles the following types of cases:

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**Threat**

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**Tax Fraud/False Tax Returns**

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**Missing IRS Payments/Refunds**

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**Stolen IRS Payments/Refunds**

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**IRS Scams and Fraud**

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**Tax Preparer Fraud and Misconduct**

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**Bribery Attempts**

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**IRS Contacts and Correspondence**

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**IRS/TIGTA Contract Fraud**

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**IRS Employee Crime or Misconduct**

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**Whistleblower Retaliation**

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**Identity Theft**

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PUBLICATION 1:  
Why you might  
file a TIGTA  
complaint  
against an IRS  
employee

- The Right to Be Informed  
The Right to Quality Service  
The Right to Pay No More than the Correct Amount of Tax  
The Right to Challenge the IRS's Position and Be Heard  
The Right to Appeal an IRS Decision in an Independent Forum  
The Right to Finality  
The Right to Privacy  
The Right to Confidentiality  
The Right to Retain Representation  
The Right to a Fair and Just Tax System

# Whistleblowing Protections

- **Form 211** is filed by an eligible individual
- Award is between **15 and 30 percent** of the proceeds collected and attributable to the whistleblower's information
- No award until taxpayer had exercised all appeals rights and can no longer file a claim for refund
- **IRC 7623 (a) and (b) awards:**
  - **7623(a):** catch all
  - **7623(b)** to qualify:
    - Relate to a tax noncompliance matter in which the tax, penalties, interest, additions to tax, and additional proceeds in dispute exceed \$2,000,000; and
    - Relate to a taxpayer, and for individual taxpayers only, one whose gross income exceeds \$200,000 for at least one of the tax years in question

# What must be included in a Whistleblowing Action?

- A description of the alleged tax noncompliance, including a written narrative explaining the issue(s).
- Information to support the narrative, such as copies of books and records, ledger sheets, receipts, bank records, contracts, emails, and the location of assets.
- A description of documents or supporting evidence not in the whistleblower's possession or control, and their location.
- An explanation of how and when the whistleblower became aware of the information that forms the basis of the claim.
- A complete description of the whistleblower's present or former relationship (if any) to the subject of the claim (for example, family member, acquaintance, client, employee, accountant, lawyer, bookkeeper, customer).
- The whistleblower's original signature on the declaration under penalty of perjury (**a representative cannot sign Form 211 for the whistleblower**) and the date of signature.



# Additional IRS forms for reporting others to IRS

**Form 3949A**: to report a business or individual is not complying with tax laws

**Form 14242**: Reporting abusive tax promotions or preparers

**Form 13909**: Reporting exempt tax organizations

# Can I take the IRS to court? YES!

- **US Tax Court**
- **Who can file a Petition?** If you aren't pro se, you'll have to be admitted to US Tax Court to file. Attorneys simply send in a certificate of good standing from their local bar to get admitted. EA's and CPAs need to take an exam to be admitted.
- **When can it be filed?** After a Notice of Deficiency or Determination is filed by IRS. (**90/180 days and 30 days**)
- **Notice of Determination v. Deficiency:** Determination notice comes from collection side, Deficiency from the exam side. Determination: I don't owe because I'm not responsible, Deficiency: I don't owe because the IRS failed to accept my explanation of income/expenses.
- **Structure:** File petition, attend appeals conference, speak with IRS attorney, file paperwork with court to inform what issues are still pending. Present case and judge will issue opinion.
- **Appeals:** If it's an S Case (small tax case), nobody can appeal. If it's a non S case, can file 90 days after the decision is entered, or 120 days if the IRS appeals first.
- **US District Court or US Claims Court:** Pay the tax and make a claim for refund.

# What is a small tax case? Not appealable

## ***Not applicable to whistleblower or certification actions***

Vary slightly depending on the type of IRS action you seek to have the Tax Court review:

- (1) **If you seek review of a Notice of Deficiency, the amount of the deficiency (including any additions to tax or penalties) that you dispute cannot exceed \$50,000 for any year.**
- (2) **If you seek review of a Notice of Determination Concerning Collection Action, the total amount of unpaid tax cannot exceed \$50,000 for all years combined.**
- (3) **If you seek review of a Notice of Determination Concerning Relief From Joint and Several Liability Under Section 6015 (or if the IRS failed to send you any Notice of Determination with respect to a request for spousal relief that you submitted to the IRS at least 6 months ago), the amount of spousal relief sought cannot exceed \$50,000 for all years combined.**
- (4) **If you seek review of a Notice of Determination of Worker Classification, the amount in dispute cannot exceed \$50,000 for any calendar quarter.**
- (5) **If you seek review of a Notice of Final Determination for [Full/Partial] Disallowance of Interest Abatement Claim (or if the IRS failed to send you a Notice of Final Determination with respect to a claim for interest abatement that you filed with the IRS at least 180 days before), the amount of the abatement cannot exceed \$50,000.**

# Key Tax Court cases: Moore v US

- **Question:** How to tax unrealized income from foreign earnings in light of the TJCA bill's provisions on repatriated earnings from foreign income
- **Old Law:** No taxes on foreign income earned overseas in a foreign corp you owned until you brought profits back to US. 35% tax
- **2017 TCJA Bill** changed the way these earnings were taxed. They are now taxed one time at 15.5 percent applied to foreign earnings held in cash and 8 percent to other earnings held in illiquid assets. **IRC 965**
- Moores' investment saw a profit, but they received no income from it
- Moores' say tax violated 16<sup>th</sup> amendment because it applies to unrealized income and that it applies retroactively to past earnings amounting to property, contravening the 16<sup>th</sup> Amendment and subsequent case law generally requiring that income be clearly realized before it is taxed
- **Concern:** Is that billions of tax dollars could be at stake if tax is found unconstitutional. GILTI and corporate AMT taxes could be affected

# Reversal of Chevron Doctrine?

- The Chevron Doctrine has been around since 1984 and has led to the proposition that courts should defer to expert agency's interpretation of the law through their regs when the matter is ambiguous.
- Cases involve fishing operations, but could extend to other government regs like the Treasury regs if the court agrees with the Petitioners
- Case cites: *Loper Bright v. Raimondo* and *Relentless Inc. v. Department of Commerce*

# Tax Court Deadlines: When does the 90 days run out?

- **Nutt v. Commissioner, 160 TC No. 10**, Petition was filed at 11:05 pm central.
- **Sanders v. Commissioner**, the Tax Court dismissed a petition that was filed 11 seconds after midnight.
- **What controls? File the Petition by 11:59 pm eastern time on the 90th day to be timely**

## Misc. Tax Court cases

- **Child Support Interest:** In **Rodgers v. Commissioner, TC Memo 2023-56**, the Tax Court concluded that interest paid on a past-due child support obligation constitutes income to the recipient and not additional tax-free child support.
- **Pre Tax Employer Paid Disability:** In **Hailstone v. Commissioner, TC Summary Opinion 2023-17**, the Tax Court concluded that disability income was taxable to an individual whose premiums were employer-paid in pretax dollars
- **Partnership Conservation Easements:** In **Glade Creek Partners v. Commissioner, TC Memo 2023-82**, a partnership could only claim a conservation easement deduction to the extent of basis when the land had constituted inventory in the hands of the contributing partner.
- **Hobby Losses:** **Gregory v. Commissioner, 131 AFTR2d 2023-1864**, the Eleventh Circuit Court of Appeals ruled that expenses related to hobby losses can only be claimed as miscellaneous itemized deductions pre-2018 and post-2025
- **Flowthrough losses:** In **Keeton v. Commissioner, TC Memo 2023-35**, the Tax Court disallowed flowthrough losses from a partnership for an alleged bad debt found to constitute capital contributions to the "debtor" entity.
- **FBAR Penalties:** **Bittner v. United States, 131 AFTR2d 2023-799** Supreme Court ruled that \$10,000 penalty for nonwillful failure to file the FBAR report was measured per annual filing and not per bank account.
- **Form 5471:** In **Farhy v. Commissioner, 160 TC No. 6**, the Tax Court concluded that the IRS could not summarily assess a penalty for failure to file Form 5471, an information return with respect to foreign corporations.

# Hobby v. Business IRC sec. 183

- In general, IRC 162(a), the taxpayer must show that he or she engaged in the activity with an actual and honest objective of making a profit. Although the taxpayer's expectation of profit does not have to be reasonable, the intent to make a profit must be genuine.
- **Nine factors used to determine hobby v. business:**
  - (1) the manner in which the taxpayer conducts the activity;
  - (2) the expertise of the taxpayer or his advisers;
  - (3) the time and effort spent by the taxpayer in carrying on the activity;
  - (4) the expectation that assets used in the activity may appreciate in value
  - (5) the success of the taxpayer in carrying on other similar or dissimilar activities;
  - (6) the taxpayer's history of income or losses with respect to the activity;
  - (7) the amount of occasional profits, if any;
  - (8) the financial status of the taxpayer; and
  - (9) elements of personal pleasure.



# Recent Tax Court cases on Hobby v. Business

- **Woodries v. Commissioner, TC Memo 2022-5**: Court held that the cattle ranch was a business. Factors in their favor included they hired a professional foreman to run the ranch, prior history of successful business ops, business plan, pivoted to a new model when old one wasn't working, great records
- **Skolnick v. Commissioner, 131 AFTR2d 2023-968**: Horse breeding business was a hobby. Factors against them: no business plan, increased the acreage, but not the horses, didn't pay for the help, didn't spend time on the day to day of the business, no distinction between personal and business. No profit in 15 years-against industry norm

# Audit Red Flags for International, Corporate and Partnership taxpayers

- **International:**

1. **Form 8938:** Failing to report when foreign account was opened or not reporting foreign assets that the IRS gets wind of
2. Bottom of Schedule B not filled out and should be
3. Foreign Spouse with foreign income earned not reported
4. Failure to comply with Corporate Transparency Act?

# Audit Red Flags continued...

## Corporate (C Corp):

1. **Selling Stock:** IRS reviews sales to see if they were at FMV. If sold at a substantial discount, that's a potential red flag.
2. **Employee Shareholders:** small corps have members and family managing the corp. IRS may review compensation to determine if it is reasonable in light of the work performed. Excessive compensation could be a means to reduce the tax rate on corporate earnings.
3. **Schedule M-1:** because there is a difference between net income on the books and the amount shown for tax purposes, the IRS scrutinizes these schedules to determine if proper GAAP reconciliation has been applied.

## **Tales from the Tax Crypt:** Criminal NY Tax Case

4. **Bonuses:** have to be reasonable to be deductible. Property bonuses: FMV at time of transfer, not value of what corp paid for it.
  - What's reasonable? What's unreasonable?
  - Duties performed
  - Volume of business employee is responsible for
  - Time commitments
  - Skill set
  - Complexity of work performed
  - Bonuses and wages offered other employees

# More Corporate Red Flags for audit

- Filing forms 1096/1099 late
- Too much officer whole life insurance taken as an expense rather than as an asset
- High meals, entertainment and auto expense
- Claiming your Italian suits as a uniform expense (REAL CASE!)
- Not properly moving retained earnings from the prior period to the current year
- Profit margins that are inconsistent with prior years
- Claiming 100% business use on a vehicle when the driver has no personal vehicle
- The corporate balance sheet doesn't balance
- Loans to Officers that should be wages/Loans without interest or repayment
- Negative profits several years in a row/High NOL carryforward
- Retail business that starts with inventory every year and ends at zero inventory every year

# S Corps Red Flags

- No Schedule M if gross income exceeds 250k
- No salary
- Salary, but not reasonable compensation
- What is reasonable compensation? Whatever the people in this room say it is.
- “is the value that would ordinarily be paid for like services by like enterprises under like circumstances.” You must be paid wages comparable to similar services compensated for similar industries.

# Large Partnership Audits/Red Flags

- **IR-2023-166** by the end of September IRS would send audit notices to 75 partnerships with an average of \$10 billion in total assets, and during October send an additional 500 “soft notices” to partnerships with over \$10 million in assets and tax returns showing discrepancies in the millions of dollars between end-of-year balances and beginning balances the following year.
- **What is IRS auditing?** High Income K1 nonfilers
- offshore lending
- distributions in excess of basis,
- losses in excess of basis
- sales of partnership interests
- transfer pricing adjustments on related party loans (IRC 482)
- **When will the initiative start?** Likely late 2024. The IRS is hiring 3,700 agents to process the audits
- Don't forget about Schedule K2/K3 issues as well and of course the Corporate Transparency Act

# Innocent, Injured and Equitable Spouse

- **Injured v. Innocent Spouse:**

**Injured spouse relief** can help you reclaim your share of a federal tax refund that was applied to your spouse's taxes or other debts.

**Innocent spouse relief** can relieve you from paying additional taxes if your spouse did something wrong on your joint tax return and you didn't know about the errors.

- Who qualifies for injured spouse? Filed joint return, your refund was applied to spouse's overdue debts, you weren't responsible for those debts.

*Example:* your spouse owes child support to his ex. Joint refund gets applied to that debt. That isn't your debt and you can ask for your half of money back.

Form 8379 within 3 years from date the return was filed or 2 years from the date the tax was paid, whichever is later.

# Innocent Spouse Continued..

- Extremely hard to get because of the knowledge requirement (actual and/or reasonable) ***Tales from the Tax Crypt: Ft Leavenworth Case***
- **Eligibility:** Joint return, understated taxes due to errors you didn't know about and you live in a community property state. No agreement to pay through judicial or administrative means. **Form 8857**
- **Separation of Liability Relief:** You still pay your share of the return, but not your spouses
- **Equitable Relief Eligibility:**
- You aren't eligible for innocent spouse relief or separation of liability relief
- You filed a joint return with your spouse
- You and your spouse didn't transfer assets to commit fraud or avoid taxes
- You didn't knowingly file a fraudulent return
- Based on all the facts and circumstances, it would be unfair to hold you liable for the unpaid or understated tax



# Fairness Test under Equitable Relief

- Your marital status
- Economic hardship you might suffer without relief
- Whether you knew or had reason to know about your spouse's understated or unpaid tax
- Whether you're legally obligated to pay the tax
- Whether you significantly benefited from not paying tax or underreporting your tax
- Whether you complied in good faith with tax laws after requested
- Your mental and physical health

# CAP/CDP Appeals and Notices of Determination

- On the exam side, IRS offers appeals of the audit and other ADR type measures. On the collection side, you have CAP and CDP appeals.

## **CAP:**

1. **Used for:** appealing liens, garnishments and seizures of property, rejection, modification or termination of an IA
2. **File Form 9423:** File a CAP in the middle of the collection action

## **CDP:**

1. **File Form 12153**
2. **Timing:** Typically filed within the 30 day Final Notice letter/LT11 to prevent proposed levy or garnishment
3. An independent officer will review the proposed liability with you and give you options to enter into an installment agreement or offer.
4. Notice of Determination is issued: Granting or denying relief. Option to file tax court if you disagree.

Tales from the Tax Crypt

# CDP Hearings: What you can't do

1. A taxpayer may raise any appropriate spousal defense at a CDP hearing. IRC 6330(c)(2)(A)(i). A taxpayer may not, however, raise a spousal defense at a CDP hearing when the IRS has made a final determination as to the spousal defense in a final determination letter or statutory notice of deficiency.

## **IRM 35.3.23.2.4 (10-18-2016)**

- **Nonjusticiable Claims**

1. The existence and amount of the underlying tax liability cannot be challenged at a CDP hearing if the taxpayer received a statutory notice of deficiency for the taxes in question or otherwise had an earlier opportunity to dispute the tax liability. An opportunity to dispute a liability includes a prior opportunity for a conference with Appeals that was offered either before or after assessment of the liability.
2. An issue may not be raised at the CDP hearing if the issue was raised and considered at a previous hearing or judicial proceeding and the taxpayer participated meaningfully in the process
3. In seeking Tax Court review of the notice of determination, the taxpayer can generally only request that the court consider an issue that was raised in the taxpayer's CDP hearing. The Tax Court, however, can review whether the IRS complied with all applicable law and administrative procedures without regard to whether the taxpayer raised it at the CDP hearing.
4. Criminal Tax Matters: A taxpayer cannot challenge the amount of court-ordered restitution at a CDP hearing. The district court's restitution order is final and cannot be challenged or modified during the CDP hearing. The challenge to the amount of restitution is also prohibited under section 6330(c)(4), because the criminal tax case is considered a prior judicial hearing in which a taxpayer meaningfully participated.

# Offer in Compromise Killers

- Not paying estimated taxes (current year)
- Not filing all returns
- Large transfers of money, property or payoff other debts
- Equity enough to full pay the balance

# Audit Reconsideration/ Form 656L

- If you fail to respond to a CP2000 letter or fail to file a tax court petition within the 90 day window, you can still dispute the audit
- Collections will only sustain their actions for so long. Payment plan necessary?
- **Two options to file:**
  1. File audit reconsideration request to one of several addresses in the US.
  2. File a Form 656L Doubt as to Liability

## **What is a Form 656L?**

# Fast Track Mediation

- Alternative to an appeal request
- Faster than a regular appeal
- Applies to examination disputes, offers in compromise and trust fund penalty
- Independent mediator (IRS employee) facilitates it. IRS and taxpayer must agree to participate
- How do you get started? **File Form 14017**
- See also **publications 5022, 4539, 5092** depending on your entity status or individual
- See **publication 3605 and file Form 13369** for collection issues

# What Happens When The IRS Goes Silent??

- **Taxpayer Advocate: File Form 911**
- **Stakeholder Liaison:** Local employee that you can call or email for help
- Both of these are great resources when you have sent information or reached out to the IRS and nothing is happening after a long time. Both can utilize backchannels to find out what is happening in your case.

# How I can help you!

1. IRS Letters
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# QUESTIONS??



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