

# **Dealing with the IRS**

---

13<sup>th</sup> Edition

Tax Attorney Frederick W. Daily  
Erica Good Pless, J.D., LL.M.

# Table of Contents

---

<b>Chapter 1 – Inside the IRS: What You Need to Know About IRS Operations .....</b>	<b>1</b>
Learning Objectives .....	1
Introduction.....	1
IRS Inefficiency.....	3
Communicating With the IRS .....	4
Getting Your Tax File from the IRS.....	4
Obtaining Income Information .....	5
Getting Your Tax Data from the IRS.....	6
Rules of the Game—Tax Laws.....	6
Interpreting the Tax Code .....	7
Self-Assessment of Income Taxes .....	7
Winning the IRS Game .....	7
Review Questions.....	9
Review Answers .....	10
<b>Chapter 2 – Filing Tax Returns .....</b>	<b>13</b>
Learning Objectives .....	13
Introduction.....	13
How Long Must You Worry About Not Filing a Tax Return?.....	13
Consequences of Not Filing .....	14
IRS Hunting for Nonfilers .....	14
IRS Notifying Nonfilers.....	14
When the IRS Prepares Your Tax Return for You.....	15
Nonfiling May Be a Crime .....	15
It's Better to File Before the IRS Contacts You .....	16
Suggestions for Completing Late-Filed Tax Returns.....	16
Voluntary Filing to Minimize the Chance of a Criminal Investigation.....	18
What Will Happen When You File Late.....	19
Civil Penalties and Interest Added to Your Tax Bill .....	19
Criminal Charges May Be Brought .....	20
Refunds May Be Denied .....	20
Requesting an Extension to File.....	21
Filing a Return When You Can't Pay What You Owe.....	21
Filing a Tax Return When You Live Out of the United States.....	22
Reducing the Chance of an Audit When Filing.....	22
Amending Tax Returns .....	23
How to Amend a Tax Return.....	23
Audit Alert for Amended Tax Returns .....	23
A Word About “Aggressive” Tax Filing.....	23
Review Questions.....	26
Review Answers .....	27
<b>Chapter 3 – Winning Your Audit .....</b>	<b>29</b>
Learning Objectives .....	29
Introduction.....	29
How Long Do I Have to Worry About an Audit? .....	29
What to Expect at an Audit.....	31
Do I Have to Learn Tax Law to Win My Audit? .....	31
Audit Selection—Why Me, O Lord? .....	31
Computers and Classifiers—What's the Difference? .....	31
Unreported Income DIF Programs.....	32
Local IRS Makes Final Decision.....	32
The IRS Looks at Significant Items.....	33
Living Beyond Your Means .....	33

## Table of Contents

Market Segment Specialization Program.....	35
Other Reasons for Audits.....	36
When the IRS Increases Your Tax Bill without an Audit.....	37
Dealing with IRS Automated Adjustment Notices.....	38
Be Patient If You Don't Hear From the IRS Immediately.....	39
Types of IRS Audits.....	45
Correspondence Audits—Please, Mr. Postman.....	45
Office Audits—Heigh-Ho, Heigh-Ho, It's Off to the IRS We Go.....	45
Field Audits—Look Out, Here Comes the IRS.....	50
How a Field Auditor Approaches an Examination.....	53
Preparing for an Audit.....	56
Your Audit Goals.....	57
What Not to Bring to an Audit.....	58
Who Should Attend the Audit?.....	58
How to Act at an Audit.....	58
Mum's the Word.....	58
Don't Offer Any Favors to the Auditor.....	59
Try to Get Along With the Auditor.....	59
When a New Auditor Appears on the Scene.....	60
Standing Up to the Auditor.....	61
Negotiating With an Auditor.....	64
Ending the Audit.....	65
IRS Pressure on an Auditor to Finish—Extending the Audit Time Limit.....	65
Finishing Audits.....	66
Receiving the Examination Report.....	66
Understanding the Examination Report.....	66
Your Options After Getting the Examination Report.....	66
Serious Audit Problems.....	74
The Auditor Suspects You of Fraud.....	74
You're Billed for an Audit You Didn't Know About.....	74
Jeopardy Assessments of Assets.....	75
Review Questions.....	82
Review Answers.....	84
<b>Chapter 4 – Appealing Your Audit Within the IRS.....</b>	<b>87</b>
Learning Objectives.....	87
Introduction.....	87
Pros and Cons of Appealing an Audit.....	87
How to Appeal an Audit.....	88
Time Limit for an Appeal.....	88
How to Get Your Audit to the Appeals Office.....	88
IRS Form for Appeals Under \$25,000 (Small Case).....	89
Protest Letter for Appeals Over \$25,000 (Large Case).....	89
Requesting the Auditor's File.....	91
How the Appeals Office Works.....	92
Preparing for an Appeals Hearing.....	93
Organizing and Presenting Documents.....	93
Filling in the Gaps.....	94
Focusing on Challenged Items.....	94
Dealing with the Appeals Officer.....	94
Presenting a Case to an Appeals Officer.....	95
Negotiating a Settlement.....	96
Should You Hire a Tax Professional for Your Appeal?.....	99
If You Don't Settle on Appeal.....	99
Review Questions.....	101
Review Answers.....	102

Table of Contents

<b>Chapter 5 – Going to Tax Court: No Lawyer Necessary .....</b>	<b>103</b>
Learning Objectives .....	103
Introduction.....	103
Tax Court Facts .....	104
Small Tax Cases—People’s Court .....	104
The Small Tax Case Petition and Related Forms .....	105
Completing the Tax Court Forms .....	105
Filing the Tax Court Forms.....	105
Meeting With IRS Appeals Officers and Attorneys Before the Trial .....	108
Settlement Before Trial Is Likely.....	109
Notices From the Court Before Your Trial.....	109
Preparing Your Case for Trial.....	109
Awaiting the Judge’s Decision in a Small Case .....	114
The Tax Bill .....	114
Regular Tax Court Cases—Over \$50,000 .....	114
Bench Decisions .....	114
Not Contesting Amounts over \$50,000 .....	115
Other Federal Courts—Paying First Is Required.....	115
Bankruptcy Court.....	116
Review Questions.....	117
Review Answers .....	118
<b>Chapter 6 – When You Owe the IRS: Keeping the Tax Collector at Bay .....</b>	<b>119</b>
Learning Objectives .....	119
Introduction.....	119
When You Can’t Pay With Your Tax Return .....	121
Getting Time to Pay After the Tax Bill Comes.....	121
IRS Tax Billing Process.....	122
Delaying the Computerized Notice Cycle .....	122
Automatic Refund, Asset, and Wage Seizures .....	122
IRS Automated Collection System.....	123
Delaying the ACS Collector.....	123
Getting an Installment Agreement (IA) From the IRS.....	124
Requesting That Your File Be Sent to the Local Office .....	126
Revenue Officers—Frontline Collectors of the IRS .....	127
The First Visit.....	127
The Collection Interview—Meeting the Revenue Officer .....	127
Filling in IRS Collection Forms .....	129
Signing IRS Collection Forms—Proceed With Caution .....	135
Protecting Yourself after Making Financial Disclosures to the IRS .....	135
What the Collector Does Next .....	135
Installment Payment Plan: Individuals .....	136
Installment Agreement Set-Up Fee .....	138
Offers in Compromise (OICs).....	140
Grounds for Making an OIC .....	140
Offer in Compromise Forms.....	149
Your Minimum Offer Amount.....	149
OIC Payment Options .....	149
Special Circumstances: Effective Tax Administration (ETA) Exception .....	151
What Happens After You Send in Your OIC Application .....	152
If Your OIC Is Rejected .....	153
Using the Bankruptcy Code to Stop the IRS.....	153
Types of Bankruptcy .....	154
The Automatic Stay .....	154
Downsides of Bankruptcy.....	154
Taxes and Chapter 7 Bankruptcy .....	154
Taxes and Chapter 13 Bankruptcy .....	156

## Table of Contents

Taxes and Chapter 11 Bankruptcy .....	157
Taxes and Chapter 12 Bankruptcy .....	157
Protecting Your Assets From the IRS .....	157
Suspending Collection of Your Tax Bill .....	158
Review Questions .....	160
Review Answers .....	162
<b>Chapter 7 – IRS Enforced Collection: Liens and Levies .....</b>	<b>165</b>
Learning Objectives .....	165
Introduction .....	165
Federal Tax Liens .....	165
Notice of Federal Tax Lien .....	165
Effect of a Recorded Notice of Federal Tax Lien .....	166
Neutralizing a Recorded Federal Tax Lien .....	166
If the IRS Records a Tax Lien .....	167
Avoiding or Eliminating a Tax Lien .....	168
When the IRS Files a Tax Lien in Error .....	169
Getting a Tax Lien Released .....	169
Getting a Tax Lien Withdrawn .....	169
Tax Levies = Seizure of Assets .....	170
Significance of a Tax Levy .....	170
Dealing With the IRS Levy Process .....	170
Assets the IRS Can't or Won't Seize .....	171
Exempt Assets .....	171
Assets of Last Resort That the IRS Can Seize .....	171
You and Your Spouse's Income .....	172
Jointly Owned Assets .....	173
Avoiding a Levy .....	173
Transfer Your Assets .....	173
Convince the IRS That a Levy Would Be Uneconomical .....	174
Show That the Levy Would Prevent You from Working .....	174
Keep Mum about Your Assets .....	174
Keep Assets Out of Sight .....	175
Sell Your Assets .....	175
Move Financial Accounts .....	175
Rent, Don't Own .....	175
Deposit Money Into Retirement Accounts .....	175
File for Bankruptcy .....	175
Getting a Tax Levy Released .....	175
IRS Sales of Levied Assets .....	177
IRS Sales of Personal Property .....	177
IRS Sales of Homes and Other Real Estate .....	178
Levies of Business Assets .....	179
Levies of Joint Tax Refunds: Injured Spouse Claims .....	180
Suing the IRS for a Wrongful Levy .....	180
Review Questions .....	181
Review Answers .....	182
<b>Chapter 8 – The Taxpayer Advocate: A Friend at the IRS .....</b>	<b>183</b>
Learning Objectives .....	183
Introduction .....	183
Who Qualifies for Help From a Taxpayer Advocate? .....	183
Problems the Taxpayer Advocate Will Pursue .....	183
Problems the Taxpayer Advocate Won't Pursue .....	184
Contacting the Taxpayer Advocate Service .....	185
Emergency Help: Taxpayer Assistance Orders .....	186
What Constitutes a Significant Hardship to the IRS? .....	187

## Table of Contents

Getting Hardship Relief—Calling the IRS's 911 Line .....	187
Review Questions .....	190
Review Answers .....	191
<b>Chapter 9 – Family, Friends, Heirs, and the IRS.....</b>	<b>193</b>
Learning Objectives .....	193
Introduction.....	193
It's a Family Affair .....	193
Filing Tax Returns—Joint or Separate?.....	193
Divorce and the IRS.....	196
Parenting and the IRS.....	196
The IRS Can Take a Tax Refund for Certain Nontax Debts.....	197
Owning Property Jointly .....	197
Death and Taxes .....	198
Filing a Federal Estate Tax Return.....	198
IRS Audits of Estate Tax Returns.....	199
Joint Ownership and Death.....	201
Review Questions.....	202
Review Answers .....	203
<b>Chapter 10 – Fraud and Tax Crimes: Do You Really Have to Worry? .....</b>	<b>205</b>
Learning Objectives .....	205
Introduction.....	205
How People Commit Tax Fraud .....	205
If You Are Caught Cheating .....	205
The IRS Suspects You of Fraud.....	205
Options When the IRS Finds Fraud.....	208
IRS Criminal Investigations.....	209
How Special Agents Conduct Investigations.....	209
IRS Considerations in Deciding Whether or Not to Recommend Prosecution .....	211
Crimes You Can Be Charged With.....	211
If You Are Prosecuted.....	212
Should You Plead Not Guilty?.....	212
What the Government Must Prove .....	212
Possible Defenses .....	213
If You Are Convicted.....	213
Review Questions.....	215
Review Answers .....	216
<b>Chapter 11 – Small Business/Self-Employed: When IRS Trouble Comes .....</b>	<b>217</b>
Learning Objectives .....	217
Introduction.....	217
Self-Employed—You're a Prime Audit Target.....	217
Employees or Independent Contractors? .....	217
How to Classify a Worker.....	218
People Who Are Automatically Employees by Law.....	219
Exempt Employees and Small Business Owners.....	219
How Independent Contractor Rules Are Applied.....	219
How Business Owners Can Protect Themselves.....	220
Payroll Taxes—IRS Dynamite.....	220
The Dreaded Trust Fund Recovery Penalty.....	221
How the IRS Determines the Responsible People .....	222
Appealing a Trust Fund Recovery Penalty.....	223
If You Lose Your Trust Fund Recovery Penalty Appeal .....	225
Cash Transactions over \$10,000.....	226
Review Questions.....	228
Review Answers .....	229

## Table of Contents

<b>Chapter 12 – Penalties and Interest</b> .....	<b>231</b>
Learning Objectives .....	231
Introduction.....	231
Penalties Added to Tax Bills.....	231
Accuracy Penalties .....	231
Fraud Penalties .....	232
Failure to Withhold, Deposit, or Pay Taxes for Employees.....	232
Failure to File Information Returns .....	232
Failure to Pay Penalties .....	232
Late-Filing Penalties—Late Filing and Late Paying.....	232
Combined Penalties.....	232
Interest on Tax Bills .....	232
Understanding Penalty and Interest Notices.....	233
Reducing or Eliminating Penalties and Interest.....	233
Reasonable Cause for a Penalty Abatement.....	233
How to Request a Penalty Abatement.....	234
If Your Abatement Request Is Rejected.....	235
Abating Interest .....	237
How to Request an Interest Abatement.....	237
Designating Late Tax Payments.....	237
Advantages of Designating Your Payments.....	238
How to Designate a Payment.....	238
Review Questions.....	239
Review Answers .....	240
<b>Chapter 13 – Help Beyond the Book: Tax Professionals and Tax Information</b> .....	<b>241</b>
Learning Objectives .....	241
Introduction.....	241
Finding and Using a Tax Professional .....	241
How Tax Professionals Can Help.....	242
Types of Tax Professionals.....	242
Choosing the Right Tax Pro.....	243
What to Look for in a Tax Professional.....	243
Tax Professionals’ Fees.....	244
Tax Pros for Serious Problems.....	244
The Right Type of Tax Professional .....	245
Tax Professional Analysis after an Audit .....	245
Hiring a Tax Return Preparer .....	245
Researching Tax Questions.....	246
Free IRS Information.....	246
Private Tax Guides .....	247
Other Research Materials—Using the Library or Internet.....	247
Review Questions.....	249
Review Answers .....	250
<b>Chapter 14 – When You Owe State Income Taxes</b> .....	<b>251</b>
Learning Objectives .....	251
Introduction.....	251
The IRS and State Taxing Authorities .....	251
Does Your State Have a Taxpayer Bill of Rights?.....	251
State Time Limits to Assess and Collect Income Taxes.....	252
State Tax Collection Departments.....	252
State Tax Bills.....	252
Getting a State Payment Plan.....	252
Enforced Collection—Seizing Assets .....	253
Bankruptcy .....	253
Compromising a State Tax Assessment.....	253

## Table of Contents

Suspending Collection .....	254
When All Else Fails, Try Your Political Connections .....	254
Review Questions.....	255
Review Answers .....	256
<b>Chapter 15 – The Taxpayer Bill of Rights .....</b>	<b>257</b>
Learning Objectives .....	257
Introduction.....	257
Taxpayer Bill of Rights I .....	257
The Good .....	257
The So-So .....	258
The Window Dressing.....	258
Taxpayer Bill of Rights II .....	258
The Good .....	258
The So-So .....	259
The Window Dressing.....	259
Taxpayer Bill of Rights III .....	259
The Good .....	259
The So-So .....	261
The Window Dressing.....	261
Review Questions.....	265
Review Answers .....	266
<b>Chapter 16 – The 25 Most Frequently Asked Questions.....</b>	<b>267</b>
Review Questions.....	272
Review Answers .....	273
<b>Glossary of Tax Terms .....</b>	<b>275</b>
<b>Index .....</b>	<b>283</b>