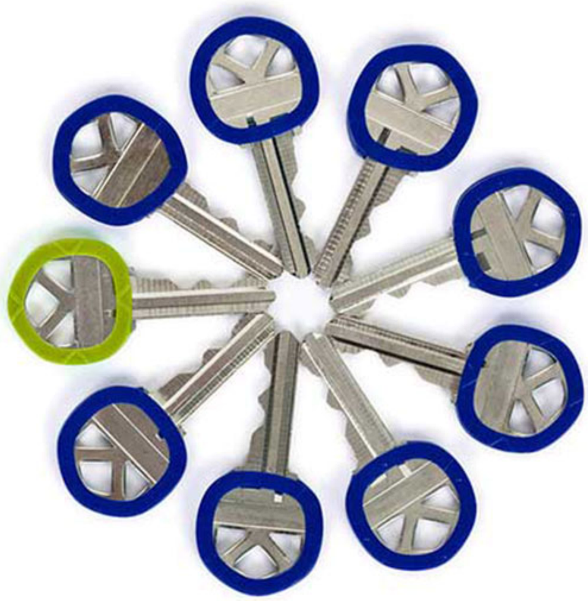

In this issue:

Informal Refund Claims – *Birger Engineering*

In *Birger Engineering, Inc. v. United States*,[1] the taxpayer filed two claims for refund before the expiration of the refund period of limitations; however, the taxpayer initially used the wrong form to claim the refunds. The IRS asked the taxpayer to resubmit its refund claims on the correct forms. After the taxpayer filed the correct forms, the IRS denied one claim as untimely and took no action on the second claim. The taxpayer sued, and the United States sought to dismiss the case based upon the taxpayer's failure to timely file the refund claim. The district court allowed the taxpayer's refund suit to proceed based on the formally invalid claims for refund that the taxpayer had submitted to the IRS before the period of limitations on the claims had expired.

[1] No. 18-10251-RGS (D. Mass. Aug. 20, 2018).

The Informal-Claim Doctrine

Before filing a lawsuit to recover improperly collected taxes, a taxpayer must timely exhaust its administrative remedies within the period of limitations.[2] The period of limitations for asserting a refund claim is the later of three years from the filing of the return or two years from the time the tax was paid.[3] The Regulations under section 6402 provide the basic requirements for a valid claim for refund or credit. The claim must:

1. Set forth in detail each ground upon which the refund or credit is claimed and facts sufficient to apprise the IRS of their exact basis;
2. Be verified by a written declaration made under penalties of perjury;
3. Be submitted on the appropriate form;
4. Be filed with the service center serving the district in which the tax was paid; and
5. In the case of income, gift, and unemployment taxes, be filed as a separate claim for each type of tax for each tax period.[4]

The Supreme Court has held that a claim for refund that the Internal Revenue Service (IRS) could otherwise disallow because it fails to meet these formal requirements will nonetheless be treated as a valid claim if:

1. The claim fairly advises the IRS of the nature of the taxpayer's claim and
2. The formal defects are later cured by the filing of an amended claim after the lapse of the statutory period for bringing such claims.[5]

Such claims are generally referred to as "informal claims."

The determination of whether a taxpayer has satisfied the requirements for an informal claim is made on a case-by-case basis and is based on all the facts and circumstances.[6] In American Radiator, the Court of Claims discussed at length the requirement that the informal claim fairly advise the IRS of the nature of the taxpayer's claim:

> Informal refund claims have long been held valid. But they must have a written component and should adequately apprise the [IRS] that a refund is sought and for certain years. It is not enough that the [IRS] have in its possession information from which it might deduce that the taxpayer is entitled to, or might desire, a refund; nor is it sufficient that a claim involving the same ground has been filed for another year or by a different taxpayer. On the other hand, the writing should not be given a crabbed or literal reading, ignoring all the surrounding circumstances which give it body and content. The focus is on the claim as a whole, not merely the written component. In addition to the writing and some form of request for a refund, the only essential is that there be made available sufficient information as to the tax and the year to enable the [IRS] to commence, if it wishes, an examination into the claim.[7]

In addition, even where a submission does not qualify as an informal claim under the informal-claim doctrine, it may be treated as a valid claim for refund if the IRS considers the submission as a claim for refund within the period of limitations.[8] In such cases, the IRS is said to have waived the formal refund claim requirements.

The Informal Claims in Birger Engineering

In *Birger Engineering*, the taxpayer filed two refund claims that were denied by the IRS, but which the district court held were valid under the informal-claim doctrine. The taxpayer's first claim was initially filed on a Form 941-X, *Adjusted Employer's QUARTERLY Federal Tax Return*, shortly before the period of limitations for filing the claim was set to expire. The Form 941-X stated that the taxpayer "made an extra payment due to a repetitive IRS assessment

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[2] *See* IRC § 7422(a).
[3] *See* IRC § 6511(a).
[4] *See* Treas. Reg. § 301.6402-2.
[5] *See United States v. Kales*, 314 US 186, 194 (1941).
[6] *See American Radiator & Standard Sanitary Corp. v. United States*, 318 F.2d 915 (Ct. Cl. 1963).
[7] *Id.* at 920 (citations omitted).
[8] *See Computervision Corp. v. United States*, 445 F.3d 1355, 1365 (Fed. Cir. 2006) (citing *United States v. Memphis Cotton Oil Co.*, 288 US 62 (1933) and *Angelus Milling Co. v. Comm'r*, 325 US 293 (1945)).

that had previously been credited in full." The IRS initially notified the taxpayer that it had approved the refund. After the promised refund failed to arrive, the taxpayer's representative contacted the IRS and was informed that a hold had been placed on the refund because the claim was made using the wrong form. Instead, the IRS asked the taxpayer to file a Form 843, *Claim for Refund and Request for Abatement*. The taxpayer filed the requested Form 843, which the IRS quickly denied because it was filed after the period of limitations expired.

The taxpayer's second claim was likewise initially filed on a Form 941-X. The Form 941-X explained that the assessment and overpayment arose from the misallocation of taxes between the third and fourth quarters of 2011. After being notified that it had filed the claim on the wrong form, the taxpayer promptly filed a Form 843. The IRS did not respond to the second claim.

The IRS argued that the taxpayer had failed to timely file its claims on a Form 843. The district court colorfully rejected this argument, calling it "a damp squib."[9] As the court saw it, the taxpayer had fully explained the grounds for each of its claims in its timely filed Forms 941-X, and the IRS was, therefore, fairly advised of the nature of each of the taxpayer's claims before the expiration of the refund period of limitations.

Conclusion

Birger Engineering is a helpful reminder that the informal-claim doctrine can provide equitable relief to a taxpayer that fails to satisfy the formal refund claim requirements. Taxpayers that have missed a deadline for filing a formal refund claim should carefully examine whether any of their tax filings or other communications with the IRS contain sufficient detail about a refund request to potentially qualify as an informal refund claim.

The Tax Court Addresses Whether an Omission of PFIC Gain is an Omission of Gross Income under Section 6501(e)(1)(A)(i)

The Tax Court issued an opinion addressing omitted passive foreign investment company (PFIC) and the application of the assessment statute of limitations. The court held that a taxpayer's omission of current-year PFIC gain is an omission of gross income for purposes of section 6501(e)(1)(A)(i) while an omission of non-current-year PFIC gain is not an omission of gross income for purposes of section 6501(e)(1)(A)(i).

Background

Toso v. Commissioner,[10] addresses a unique application of the exception under section 6501(e)(1)(A)(i) to the general, three-year period of limitations on assessments.[11] In general, the Internal Revenue Service (IRS) has a three-year period within which to assess an income tax liability. That period generally begins to run on the later of the date that the return establishing the liability is filed or the original due date of the return.[12] Section 6501(e)(1)(A)(i) provides an exception to the general, three-year period of limitations for an omission of gross income that is greater than 25% of the amount of gross income reported on the return. Under this exception, the IRS has a six-year period within which to assess an income tax liability.[13]

The taxpayers in *Toso* filed original returns for 2006, 2007, and 2008 that omitted gains from sales of PFIC stock. After the IRS issued a John Doe summons to the taxpayers' foreign bank, the taxpayers filed amended returns for these years that included, among other items, current-year and non-current-year PFIC gains attributable to PFIC stock that they held in an account that they held with the foreign bank.[14] If the current-year and non-current-year PFIC

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[9] *Birger Eng'g*, No. 18-10251-RGS.
[10] 151 T.C. No. 4 (2018).
[11] *See* IRC § 6501(a).
[12] *See* IRC § 6501(a) and (b)(1).
[13] *See* IRC § 6501(e)(1)(A).
[14] An amended return does not reduce the period of limitations that would otherwise apply under section 6501(e)(1)(A)(i) due to the filing of the original return. *See Badaracco v. Comm'r*, 464 US 386, 395 n.8 (1984) (agreeing with a series of Tax Court cases).

gains are included in gross income for purposes of section 6501(e)(1)(A)(i), then the taxpayers omitted more than 25% of the gross income reported on their original returns for all years at issue. However, if only current-year PFIC gains, but not non-current-year PFIC gains, are included in gross income, then the taxpayers omitted more than 25% of the gross income reported on their original return for 2006 but did not do so on their original returns for 2007 and 2008. Thus, to determine whether the exception under section 6501(e)(1)(A)(i) applied, the Tax Court addressed whether current-year and non-current-year PFIC gains are includible in the gross income reportable on a return.

Are PFIC gains includible in gross income?

The Tax Court began its analysis of these issues by defining "gross income" under section 6501(e)(1)(A)(i) as having the same meaning as "gross income" under section 61(a).[15] Section 61(a)(3) provides that "gross income" includes gains derived from dealings in property. The court then examined whether current-year and non-current-year PFIC gains are included in this broad definition of "gross income."

The court observed that, unless a taxpayer elects otherwise, PFIC gains are taxed under section 1291. Section 1291(a) provides that gain from the sale of PFIC stock is allocated ratably to each day in the taxpayer's holding period for the stock. PFIC gain that is allocated to the current year is included in the taxpayer's gross income as ordinary income.[16] By contrast, PFIC gain that is allocated to a non-current year is used to determine a "deferred tax amount". The "deferred tax amount" is the tax that would have been due for the non-current tax period (applying the then highest applicable tax rates) and interest calculated on such tax.[17] The "deferred tax amount" is added to the taxpayer's tax liability for the current year.[18]

The court quickly concluded that current-year PFIC gains should be included in gross income for purposes section 6501(e)(1)(A)(i) because they are included in gross income under section 1291. The court then examined whether non-current-year PFIC gains should also be included in gross income for purposes of section 6501(e)(1)(A)(i) and concluded that they should not be because the "deferred tax amount" is a separate tax computation that is added to a taxpayer's income tax for the current year, rather than as an amount included in gross income.[19]

The IRS argued that, although non-current-year PFIC gains are not included in the computation of "gross income" for the purposes of section 1291, non-current-year PFIC gains are "gross income" for the purposes of section 6501(e)(1)(A)(i) because they would have been included in gross income under section 61(a).[20] The court rejected this argument because section 1291 is the more specific provision, and it should, therefore, govern whether the non-current-year PFIC gains are included in gross income for purposes of section 6501(e)(1)(A)(i).[21]

The IRS also argued that section 6501(e)(1)(A)(i) should treat gains from the sale of PFIC stock and gains from the sale of regulated investment company ("RIC") stock similarly because the legislative history of section 1291 indicates that Congress enacted section 1291 to treat PFICs and RICs similarly.[22] And because the total gain from the sale of RIC stock is included in gross income for purposes of section 6501(e)(1)(A)(i), so too should all of the gain from PFIC stock be included.[23] The court rejected this policy argument because numerous technical differences between the PFIC and RIC provisions demonstrate that Congress did not intend PFICs and RICs to be identical in all respects.[24]

The court held that unreported current-year PFIC gains are included as unreported gross income under section 6501(e)(1)(A)(i) but unreported non-current-year PFIC gains are not so included. Computing the taxpayers' unreported gross income in accordance with these holdings, the court held that the taxpayers' unreported gross

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[15] *See Toso*, Slip. Op. at 9 (citing *CNT Inv'rs, LLC v. Comm'r*, 144 T.C. 161, 210 (2015)).
[16] *See* IRC § 1291(a)(1)(B).
[17] *See* IRC § 1291(c). The interest calculated under this section is the interest that would have been due for the period beginning on the due date for the non-current tax period and ending on the due date for the year that the property is disposed of. *See* IRC § 1291(c)(3).
[18] *See* IRC § 1291(a)(1)(C).
[19] *See Toso*, 151 T.C. No. 4, Slip. Op. at 11.
[20] *See id.*, Slip. Op. at 12 – 13.
[21] *See id.*, Slip Op. at 13.
[22] *See id.*, Slip Op. at 14.
[23] *See id.*
[24] *See id.*, Slip Op. at 18.

income for 2006 exceeded 25% of the gross income reported on their original return but their unreported gross income for 2007 and 2008 did not.[25]

The Second Circuit Affirms District Court in *Trusted Media Brands*

On August 10, 2018, the Second Circuit affirmed the decision of the district court in *Trusted Media Brands v. United States*[26] and held that the section 6511(d)(3) special 10-year refund statute of limitations applies only to refund claims based on foreign tax credits allowed under section 901, and not to refund claims based upon deductions of foreign tax for which a credit is allowable.

Background

Taxpayers may elect either a credit or a deduction for foreign taxes paid or incurred for any taxable year.[27] The taxpayer may, for a particular taxable year, claim the benefits of section 901 (or claim a deduction in lieu of a foreign tax credit) at any time before the expiration of the period prescribed by section 6511(d)(3)(A) (or section 6511(c) if the period is extended by agreement).[28]

Section 6511(d)(3) sets forth special rules relating to foreign tax credits and provides that, if the claim for credit or refund relates to an overpayment attributable to taxes paid or accrued to any foreign country for which a credit is allowed against income tax in accordance with section 901, in lieu of the three-year period of limitations, the period shall be ten years from the date prescribed by law for filing the return for the year in which such taxes were actually paid or accrued.[29]

Section 6511(d)(2) sets forth the special period of limitation with respect to NOL or capital loss carrybacks, and provides a three-year limitations period to claim a refund from the due date of the return for the year in which the NOL or capital loss carryback originated.

On December 14, 2011, Trusted Media Brands, Inc. (TMB) TMB filed Form 1120X, *Amended US Corporation Income Tax Return*, changing its election from claiming a foreign tax credit to deducting its foreign taxes paid or accrued in tax year ending (TYE) June 30, 2002, pursuant to section 164(a)(3). As a consequence of TMB changing its election from crediting foreign taxes to deducting foreign taxes for its TYE June 30, 2002, TMB's TYE June 30, 2002 NOL increased, and TMB filed a Form 1120X for its TYE June 30, 1997 to reflect the NOL carryback from TYE June 30, 2002, which reduced its taxable income for TYE June 30, 1997. The decrease in Trusted Media's taxable income for its TYE June 30, 1997 resulted in a decrease of the statutory limit on foreign tax credit Trusted Media could claim, thus reducing the amount of foreign tax credit it could claim for TYE June 30, 1997. As a result, some of the credit that Trusted Media had claimed in TYE June 30, 1997 to reduce its US tax liability could no longer be used to do so, but instead was available to be carried back to other tax years. Trusted Media then filed a Form 1120X for its TYE June 30, 1995 to carry back this excess foreign tax credit from its tax year 19970. As a result, Trusted Media determined that it had an overpayment of approximately $2.1 million for its TYE June 30, 1995.

Trusted Media argued before the District Court that its claim for refund filed in December 2011, for an overpayment of its TYE June 30, 1995 taxes was "attributable" to its election to deduct foreign taxes paid during its TYE June 30, 2002 and, thus, was timely under the special ten□year refund period in section 6511(d)(3). The Government moved to dismiss Trusted Media's claim, arguing that it had failed to file a timely refund claim with the IRS.

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[25] *See id.*, Slip Op. at 22.
[26] *Trusted Media Brands, Inc. v. United States*, No. 17-3733-cv (2d Cir. Aug. 10, 2018).
[27] *See* IRC § 901(a).
[28] *See* Treas. Reg. § 1.901-1(d).
[29] Treas. Reg. § 301.6511(d)-3 provides that, in the case of an overpayment of income tax resulting from a credit allowed under the provisions of section 901, for taxes paid or accrued to a foreign country, a claim for credit or refund must be filed by the taxpayer within ten years from the last date prescribed for filing the return (not including extensions) for the taxable year with respect to which the claim is made. The regulation also states that the ten-year period is in lieu of the three-year period in section 6511(a).

Refund litigation

District Court: The district court in *Trusted Media Brands* agreed with the Government and concluded that TMB's $2.1 million refund claim was untimely.[30] The court reasoned that, because TMB chose to change its election to deduct foreign taxes paid or accrued during its TYE June 30, 2002, no credit for foreign taxes was allowed, and the applicable limitations period for TMB's refund claim based upon its TYE June 30, 2002 NOL is three years after the time prescribed by law for filing the return, under section 6511(d)(2)(A). In addition, the court concluded that, even if the special ten-year rule under section 6511(d)(3) were held to be applicable, the refund that TMB seeks is time barred as it is attributable to TMB's carryback of foreign tax credits from TYE June 30, 1997 and is not attributable to its TYE June 30, 2002 change in election.

Second Circuit: The Second Circuit agreed with the district court's first reason for holding that the TYE June 30, 1995 refund claim was untimely.[31] The Second Circuit reasoned that the plain language of section 6511(d)(3) indicates that it only applies where a foreign tax credit is "allowed,"[32] which term the court interpreted as being synonymous with "claimed." The court supported its reading of section 6511(d)(3) by examining the regulations thereunder[33] and a related statutory provision[34]. In addition, the court explained that the underlying policy considerations favor an extended period of limitations with respect to foreign tax credits, which relate back to the tax year to which the payment relates, and do not favor an extended period of limitations with respect to foreign tax deductions, which are normally deducted in the year in which the foreign tax becomes fixed and determinable.[35] Finally, the court stated that regulations under section 901 that allow a taxpayer to toggle between foreign tax deductions and foreign tax credits during the 10-year period provided for in section 6511(d)(3) statute of limitations[36] are inapplicable because those regulations do not extend the limitations period for claiming a refund on the basis of such an election.

Strict and Substantial Compliance with Charitable Deduction Substantiation Requirements – *Belair Woods*

Introduction
In Belair Woods, LLC v. Commissioner,[37] the Tax Court rejected a taxpayer's assertion that it strictly or substantially complied with the substantiation requirements for claiming a charitable contribution deduction for donating a conservation easement to a charity because the taxpayer failed to disclose material information regarding the deduction on its federal income tax return. This case is a helpful reminder of the potential consequences of failing to comply with regulatory filing requirements.

Background

In 2007, HRH Investments, LLC (HRH), purchased a 1,490-acre property for $3,881,196, or approximately $2,605 per acre.[38] In December 2008, HRH contributed 145.15 acres of this property to Belair Woods, LLC (Belair). In December 2009, Belair executed a deed of conservation easement to a charity on 141.15 of those acres.[39]

On its 2009 return, Belair claimed a charitable contribution deduction of $4,778,000 for its donation of the easement.[40] Belair attached a Form 8283, *Noncash Charitable Contributions*, to its federal income tax return. The Form 8283 did

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30 *See Trusted Media Brands*, No. 15-CV-9872 (S.D.N.Y. Sept. 27, 2017).
31 *See Trusted Media Brands*, No. 17-3733-cv.
32 IRC § 6511(d)(3)(A).
33 Treas. Reg. § 301.6511(d)-3.
34 IRC § 6511(d)(3)(B).
35 *See Albemarle Corp. & Subsidiaries v. United States*, 797 F.3d 1011, 1017 (Fed. Cir. 2015).
36 *See* Treas. Reg. § 1.901-1(d).
37 T.C. Memo. 2018-159.
38 *See id.* at *39.
39 *See id.* at *40.
40 *See id.* at *42.

not include Belair's basis in the easement or the land covered by the easement.[41] Instead, Belair stated that it did not report its basis in the property because that information was unnecessary for computing the amount of the deduction. Belair included this statement in reliance on advice that a law firm previously provided to Forever Forests, LLC, a consulting company that handled many aspects of the easement transaction.

Subsequently, the Internal Revenue Service (IRS) informed Belair that the charitable contribution deduction would be denied because Belair's Form 8283 did not report the cost or adjusted basis in the donated property as required.[42] Belair provided the omitted cost basis information to the IRS one month after being so informed.

Discussion

Among other requirements, Treas. Reg. § 1.170A-13 requires a donor of noncash property to attach a fully completed appraisal summary to the federal income tax return on which the charitable contribution deduction is first claimed.[43] A fully completed appraisal summary must include the cost or adjusted basis of the donated property.[44] A Form 8283 is used to attach an appraisal summary to a return.[45] If a taxpayer is unable to provide any of the required information, the taxpayer is required to attach an appropriate explanation as to why the taxpayer was unable to provide the required information (the *regulatory reasonable cause defense*).[46] In addition, there is a statutory reasonable cause defense that is analogous to the reasonable cause defense that applies with respect to numerous Internal Revenue Code provisions.[47]

The IRS may disallow a noncash charitable contribution deduction if the taxpayer fails to attach a fully completed appraisal summary.[48] A regulatory exception provides that a deduction will not be disallowed if (1) the IRS requests the missing appraisal summary, (2) the taxpayer provides the appraisal summary within 90 days of the request, and (3) the taxpayer's failure to attach the appraisal summary was in good faith.[49]

Belair argued that it strictly complied with the reporting requirements of Treas. Reg. § 170A-13. However, because Belair failed to provide the cost or adjusted basis of the easement on the Form 8283, the court concluded that Belair did not strictly comply with the regulatory requirements. In the words of the court, "[a]sserting that one may ignore a requirement does not constitute strict compliance with it."[50]

Belair alternatively argued that it cured its failure to attach a fully completed Form 8283 by submitting the missing information after it was notified that the IRS planned on disallowing the charitable contribution deduction based upon its failure to provide the basis of the donated property on the Form 8283. The court rejected this argument because (1) Belair did not fail to attach a Form 8283 – it attached an intentionally incomplete Form 8283; and (2) the IRS never requested the information.[51]

The next issue the court addressed was whether Belair substantially complied with the regulatory substantiation requirements. Substantial compliance is a case-law doctrine that may excuse a failure to strictly comply with certain reporting requirements. The court stated that, to qualify as substantial compliance, the taxpayer must:

1. Either:
    a. "Provide most of the information required" or
    b. The omission must be "solely through inadvertence;"[52] and

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[41] *See id.* at *43.
[42] *See id.* at *44.
[43] *See* Treas. Reg. § 1.170A-13(c)(2)(i)(B).
[44] *See* Treas. Reg. § 1.170A-13(c)(4)(ii)(E).
[45] *See Belair Woods*, T.C. Memo. 2018-159, at *46 (citing *Jorgenson v. Comm'r*, T.C. Memo. 2000-38).
[46] *See* Treas. Reg. § 1.170A-13(c)(4)(iv)(C)(*1*).
[47] *See* IRC § 170(f)(11); *Belair Woods*, T.C. Memo. 2018-159, at *57.
[48] *See* IRC § 170(a)(1).
[49] *See* Treas. Reg. § 1.170A-13(c)(4)(iv)(H).
[50] *Belair Woods*, T.C. Memo. 2018-159, at *48.
[51] *Id.* at *49 – *50.
[52] *Id.* *51 (quoting *Hewitt v. Comm'r*, 109 T.C. 258, 265 n.10 (1997)).

2. "Satisfy those reporting requirements that 'relate to the substance or essence of the statute.'"[53]

After examining the legislative history behind the substantiation requirements for noncash charitable contribution deductions, the court concluded that the substantiation requirements were intended to "alert the Commissioner to potential overvaluations of contributed property."[54] The court observed that basis of the land covered by the easement was $2,605 per acre whereas the claimed value of the easement was based upon a per acre value of $33,707 and the claimed value of the land covered by the easement was based upon a per acre value of $35,990. According to the court, this 1,380% increase in value in only 2-1/2 years, during the worst real estate crisis since the Great Depression, "is precisely the sort of information that Congress wished the IRS to have."[55] The court therefore held that, by intentionally omitting the cost or adjusted basis of the donated property from its federal income tax return, Belair failed to satisfy the substance of the substantiation requirements and, thus, did not substantially comply with such requirements.

The court further held that the regulatory reasonable cause defense did not apply because that defense only applies "where the taxpayer had reasonable cause 'for being unable to provide the information required.'"[56] Here, by contrast, Belair was able to provide the required information but declined to do so.

Finally, because this case is still in the pre-trial stage, the court held that it lacked sufficient information to decide whether the statutory reasonable cause defense applied.[57] The court said that it would need to determine (1) whether the consulting firm that advised Belair was a "tax professional"; (2) whether the consulting firm was unburdened by conflicts of interest; (3) whether Belair could reasonably rely on legal advice it indirectly received; and (4) whether Belair reasonably relied in good faith on the advice it received.[58]

Conclusion

Belair Woods highlights the risks that taxpayers face in not strictly complying with tax reporting and substantiation requirements. It also reminds taxpayers that the IRS and the courts can be unsympathetic to taxpayers that employ measures to avoid disclosing material information to the IRS when so required.

In addition, taxpayers contemplating conservation easement transactions should be aware that the IRS recently launched a compliance campaign targeting syndicated conservation easement transactions.[59] The IRS has also designated specific syndicated conservation easement transactions as listed transactions.[60]

District Court Holds that Supervisory Approval is Only Required Once Under TEFRA

Following two Tax Equity and Fiscal Responsibility Act (TEFRA) partnership level proceedings that denied "massive artificial tax-shelter losses," the IRS assessed tax, penalties and interest against three partners.[61] The partners paid the amounts due and sued for a refund of the penalties and interest. In their complaint, the partners raised for the first time the Government's alleged failure to comply with Section 6751 in assessing the penalties against the partners.[62]

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[53] *Id.* (quoting *Bond v. Comm'r* 100 T.C. 32, 41 (1993)).
[54] *Id.* at *52 (citing *RERI Holdings I v. Comm'r*, 149 T.C. No. 1, Slip Op. at 22, (July 3, 2017)).
[55] *Id.* at *53 – *54.
[56] *Id.* at *57 (quoting Treas. Reg. § 1.170A-13(c)(4)(iv)(C)(*1*)).
[57] *Id.* at *59.
[58] *Id.*
[59] *See* https://www.irs.gov/businesses/irs-announces-the-identification-and-selection-of-five-large-business-and-international-compliance-campaigns-0.
[60] *See* Notice 2017-10.
[61] *Nix et al. v. United States*, No. 2:2017cv00434, 2 (E.D. Tex. 2018)
[62] *See* IRC § 6751

Section 6751(b)(1) requires supervisory approval before certain penalties can be assessed.[63] The US Tax Court, in *Graev v. Commissioner*, held that producing evidence of compliance with Section 6751(b)(1) is part of the IRS's burden of production under Section 7491(c).[64] The partners argued that the Government failed to establish that the IRS obtained written supervisory approval imposing penalties. before they were levied against each partner.

The question before the court was whether a partner can raise a Section 6751 compliance claim in a partner level TEFRA proceeding. The district court addressed this question by examining the two-tiered structure of TEFRA proceedings. The court explained that the first tier of TEFRA operates at the partnership level. The IRS performs a partnership level TEFRA audit and issues a final partnership administrative adjustment ("FPAA"). The tax matters partner can seek judicial review of the FPAA under Section 6226(d).[65]

The second tier of TEFRA operates at the partner level and that under TEFRA many adjustments may be directly assessed against the partners and bypass the deficiency proceedings. Some affected items require partner-level factual determinations, for which the IRS must issue an affected-item notice of deficiency, however, under *US v. Woods*, the assessment of a penalty is conclusively determined at the partnership level. Individual factual determinations that are required to determine the applicability of a penalty to an individual partner are made at the partner level.[66] There is no review of substantive issues in a refund suit because partnership level determinations under the FPAA or court review are conclusive.[67]

The court observed that the animating principle behind the TEFRA regime was to allow these determinations to be made at the partnership level and streamline the IRS's pursuit of partnership items. The opinion highlighted the operative phrase "initial determination" in Section 6751(b)(1) as indicative of the fact that supervisory approval is only required at the first stage of the TEFRA audit procedure (*i.e.*, at the partnership level) and that requiring written supervisory approval in a partner-level proceeding would obviate the rationale behind the TEFRA architecture and misconstrue the meaning of Section 6751. [68] The court therefore held that the partners are barred from raising a Section 6751 compliance claim in their refund suit.

US Ninth Circuit Court of Appeals Rules S Corp Shareholder Properly Amended Tax Return to Claim Position Inconsistent Treatment with Position Taken by S Corp On Tax Return

In *Rubin v. United States*,[69] The Ninth Circuit Court of Appeals reversed a district court's judgment, dismissing a taxpayer's claim for a refund. The appeals court found that the taxpayer, a shareholder of a subchapter S corporation, met the requirements for filing an individual tax return that is inconsistent with the S corporation's and remanded the case for further proceedings. In spite of the fact that the taxpayer prevailed in this case, the case serves as a reminder to taxpayers that the IRS can often react negatively to a taxpayer's failure to precisely follow the IRS's preferred method of information reporting.

The taxpayer was the sole shareholder of a Subchapter S corporation that experienced some financial turbulence, leading to an involuntary bankruptcy. After filing his 2000 tax return consistent with the treatment by the S corporation, the taxpayer disputed the S corporation's reported net income with respect to cancellation of indebtedness and bad debts and claimed that it was substantially overstated by the bankruptcy trustee who filed the S corporation tax return. As a result, the taxpayer filed an amended tax return for 2000 and took a position inconsistent with the S corporation's filing. The Taxpayer also filed amended returns for 1998 and 1999 to carryback losses from

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[63] *See* IRC § 6751(b)(1)
[64] *Graev v. Commissioner*, 149 T.C. No. 23 (2017)
[65] *See* IRC § 6226(d)
[66] *Id*. At 564
[67] *See* § 6230(c)(4); *see also* Treas. Reg. 301.6662-1(c)
[68] *See* IRC § 6751(b)(1)
[69] *Rubin v United States*, No. 16-56633 (9th Cir. 2018)

2000. In all of the amended returns the Taxpayer sought a refund for the overpayments made. The IRS denied the refunds, and the district court dismissed the taxpayer's refund suit.

The question before the appeals court was whether the taxpayer's amended returns failed to satisfy the requirements of 26 USC § 6037.[70] Section 6037 generally requires that the tax return of a shareholder of an S corporation must report income and loss consistent with the corporate return.[71] There is an exception to the requirement of consistent treatment, if "the shareholder files with the Secretary a statement identifying the inconsistency."[72] The Ninth Circuit had to consider whether the filings by the taxpayer qualified as a "statement identifying the inconsistency" per §6037.

The taxpayer amended his returns for the 1998, 1999 and 2000 tax years, together with a cover letter prepared by his accountant stating the returns should be reviewed in toto. The cover letter referenced an explanation for the changes in Part II of the amended returns. Attached to the amended return for 2000 was a two-page attachment. The first page provided a chart that summarized the changes to income and itemized deductions. The statement reported the figures: as originally reported, the net change, and as amended.

The second page of the attachment provided a written explanation describing the discrepancies with the S corporation's tax return and noted that the largest adjustments on the taxpayer's amended return flowed from the S corporation recalculated tax liability. Additionally, the taxpayer attached a pro-forma amended Form 1120S, Income Tax Return for an S Corporation, reporting the positions that the taxpayer thought reflected an accurate tax return of the S corporation. The taxpayer also included a revised Schedule K-1, Reporting a Partner's Share of Income, Deductions, Credits, that listed the correct amounts based on the pro-forma Form 1120S.

The IRS agreed that it was able to ascertain the revisions proposed by the taxpayer. In fact, the IRS initially rejected the taxpayer's return on substantive grounds. The court observed that in order for the IRS to make the determination that the taxpayer's claims lacked merit, the IRS necessarily had to identify the items that were treated inconsistently and evaluate them.

The IRS contended that the taxpayer failed to identify the right inconsistencies in his filing because he only identified how the amended returns were different from his original returns and not how they differed from the S corporation's return. Moreover, the IRS argued that precedent requiring the Service to compare the S corporation's return with the taxpayer's would be unduly burdensome, pointing to the fact that the S corporation's pro forma was 20 pages. The court was not persuaded by these arguments, finding that it elevated form over substance.

The court looked to Form 8082, Notice of Inconsistent Treatment or Administrative Adjustment Request, promulgated by the IRS to report inconsistencies in these situations, as the lodestar for proper filing of an inconsistent return. Form 8082 requires the taxpayer to describe the inconsistent items and indicate for each item whether the inconsistency stems from the amount of the item or its treatment on the original return. Form 8082 gives the taxpayer the option to list either the amount that appeared on the S corporation's return or the taxpayer's original return and contrast it with the amount reported on the amended return and the difference between the two. The court pointed out that the taxpayer filing provided the exact information required by Form 8082.

In addressing the IRS' alternative argument, the court held that this would not prevent the IRS from discharging its duties and that in situations with similarly large refund claims, the IRS would be expected to review the returns. The court found that this standard procedure cannot be ruled unduly burdensome.

On this basis, the court concluded that taxpayer complied with § 6037 and reversed the lower court's decision.[73] Although the taxpayer ultimately prevailed, this case illustrates for taxpayers the potential perils and hassle that taxpayers may experience if they fail to diligently follow the requirements of the IRS's Forms and instructions.

[70] *See* IRC § 6037
[71] Subsection 6037(c)(1)
[72] Subsection 6037(c)(2)(A)(ii)
[73] § 6037(c)(2)(A)(ii)