

Violation of IRS Appeals' *Ex Parte* Communications Proves to Have No Real Remedy for Taxpayers

By David M. Fogel¹

I. INTRODUCTION

In 1998, Congress passed the IRS Restructuring and Reform Act and the President signed it into law.² One of the law's provisions required the Internal Revenue Service ("IRS") to develop a plan to prohibit *ex parte* communications between Appeals Officers and other IRS employees to the extent that such communications appeared to compromise the independence of Appeals.³

At the time the law was enacted, I was an IRS Appeals Officer. Our office was very interested in this provision. We wanted to know which kinds of communications with other IRS employees were prohibited and we wanted to know what would happen to us (and to the taxpayer) if we inadvertently engaged in the prohibited *ex parte* communications. We also viewed the prohibition on *ex parte* communications as "having no teeth" since the statute did not provide a remedy to the taxpayer in the event such prohibited *ex parte* communications occurred.

About a year later, the IRS issued a proposed revenue procedure concerning the prohibition on *ex parte* communications.⁴ The proposed revenue procedure provided guidance in the form of a series of questions and answers that addressed situations that Appeals Officers might encounter during the course of an administrative appeal. After considering public comments, the IRS issued Revenue Procedure 2000-43.⁵

II. REVENUE PROCEDURE 2000-43

Revenue Procedure 2000-43 provides guidance on *ex parte* communications and is effective for communications that occurred after October 23, 2000.

Ex parte communications is defined in Rev. Proc. 2000-43 as communications that take place between an Appeals employee and an employee of another IRS function without the participation of the taxpayer or the taxpayer's representative.⁶ The revenue procedure clarifies that while Appeals Officers may contact the examining agent and ask questions that involve ministerial, administrative, or procedural matters, discussions about substantive matters—such as the accuracy and importance of alleged facts, the relative merits of the taxpayer's positions, or the demeanor or

credibility of the taxpayer—are prohibited *ex parte* communications unless the taxpayer or representative is given an opportunity to participate in these discussions.⁷ Under the revenue procedure, Appeals Officers may not engage in *ex parte* discussions about the strengths and weaknesses of a case if those discussions appear to compromise the Appeals Officer's independence.⁸

Revenue Procedure 2000-43 provides that for cases that are docketed before the United States Tax Court, discussions between Appeals Officers and IRS Counsel attorneys are not prohibited *ex parte* communications.⁹ For cases that are not docketed before the Tax Court, the Appeals Officer is permitted to communicate with the IRS Counsel attorney about the issues of a case as long as the Counsel attorney did not previously provide advice to the examining agent.¹⁰

If an Appeals Officer intends to engage in *ex parte* communications with another IRS employee, then the taxpayer/representative must be given a reasonable opportunity to participate in the discussions.¹¹ The taxpayer/representative may waive the prohibition on any or all *ex parte* communications.¹²

The revenue procedure recognizes that Appeals Officers cannot always fully control communications initiated by other IRS employees.¹³ Accordingly, it states that all IRS employees share the responsibility to ensure that communications do not appear to compromise the independence of Appeals.¹⁴

If a prohibited *ex parte* communication occurs, according to Rev. Proc. 2000-43 the Appeals Officer's violation will be handled under existing IRS administrative and personnel processes.¹⁵

III. TAXPAYERS' REMEDY WHEN PROHIBITED EX PARTE COMMUNICATIONS OCCUR

Revenue Procedure 2000-43 does not answer the question of what sort of relief taxpayers should receive if prohibited *ex parte* communications occur. This is because Congress did not include a specific remedy in the statute. As a result, taxpayers who have been damaged by such prohibited *ex parte* communications have sought relief from the courts.

Only four court cases have addressed the taxpayer's remedy where the Appeals Officer engaged in prohibited *ex parte*

communications with another IRS employee.¹⁶ In one instance, the court did nothing. In the other three cases, the court remanded the case back to Appeals for a new hearing before a different Appeals Officer.

*Robert v. United States*¹⁷ involved an Appeals Officer's consideration of the value of closely held stock for gift tax purposes. The Appeals Officer decided that the government's case had a substantial weakness in that the IRS appraiser did not follow the valuation methodology established in a prior related case.¹⁸ The Appeals Officer contacted the examining agent, *ex parte*, and asked him to contact the IRS appraiser to get a revised appraisal. During the course of the appeal, the Appeals Officer also discovered that there was a stock redemption of an additional 1,000,000 shares that potentially could result in a new gift tax issue. He again contacted the examining agent, *ex parte*, informed him of this issue and asked him to develop it.

While the case was still under the jurisdiction of Appeals, the examining agent started to develop the stock redemption issue by asking the taxpayer's representative for information. At that point, the representative learned about the *ex parte* communications and complained. Attempting to remedy the situation, the Appeals Officer's supervisor sent the case back to the examining agent, releasing Appeals' jurisdiction. The taxpayer refused to provide the agent with the information about the stock redemption, so the examining agent issued a summons, and in a proceeding in district court, the summons was enforced. The Eighth Federal Circuit Court of Appeals affirmed the district court's decision.

While the Eight Circuit concluded that the Appeals Officer violated the prohibition on *ex parte* communications, and that the violation was "serious," it nonetheless enforced the summons and provided no relief to the taxpayer, stating:

"[W]e will enforce the summonses in this case because Congress did not specifically legislate a limitation on the IRS summons power as a remedy for violation of the *ex parte* restrictions; the IRS did proscribe an administrative remedy to address violations of the *ex parte* restrictions; the Supreme Court has cautioned that we should be slow to erect barriers to enforcement of IRS summonses; and, we discern no improper purpose or bad faith behind issuance of the IRS summonses nor nexus between the improper communications and any improper purpose for the investigation."¹⁹

Relying upon language from the U.S. Supreme Court,²⁰ the Eight Circuit stated, "we generally will not fashion a remedy where Congress creates a right but fails to create an accompanying remedy."²¹

In *Drake v. Commissioner*,²² the taxpayer requested a Collection Due Process hearing under IRC §6330 after the IRS proposed a levy.²³ The Appeals Officer, *ex parte*, discussed the taxpayer's prior bankruptcy filing with an advisor from the IRS's Insolvency Unit, and the Appeals Officer requested related documents. Among the documents was a memorandum stating in part that the taxpayer had improperly used the Bankruptcy Court to bypass the Federal tax lien. The Tax Court concluded that the communications between the Appeals Officer and the advisor were prohibited *ex parte* communications that may have damaged the taxpayer's credibility before Appeals. As a remedy, the Tax Court remanded the case back to Appeals for a new hearing with an independent Appeals Officer who did not have any prior communications relating to the taxpayer's credibility.

In *Moore v. Commissioner*,²⁴ the taxpayer requested a Collection Due Process hearing under IRC §6320 after the IRS sent her a Notice of Federal Tax Lien.²⁵ The Appeals Officer, *ex parte*, communicated with two IRS Revenue Officers and a specialist who was assigned to work the taxpayer's Offer in Compromise ("OIC"). The Revenue Officers told the Appeals Officer that the taxpayer may have transferred assets to a nominee. The OIC specialist urged the Appeals Officer to reject the taxpayer's OIC due to nominee, transferee and fraud issues. The Tax Court held that these discussions were prohibited *ex parte* communications. As a remedy, the Tax Court remanded the case back to Appeals to "identify and apply an appropriate remedy to avoid prejudice attaching to petitioner as a result of the prohibited *ex parte* communications that occurred."

The IRS nonacquiesced to the *Moore* decision.²⁶ The IRS argued that while prohibited *ex parte* communications occurred because the Appeals Officer engaged in discussions with the Revenue Officers regarding substantive issues in the case without the participation of the taxpayer or her representative, there was harmless error. The IRS argued that the Appeals Officer cured the violation by disclosing the information to the taxpayer and giving her adequate opportunity to respond. But the IRS's argument here is contradicted by its own revenue procedure. Revenue Procedure 2000-43 provides that an "opportunity to participate" means allowing the taxpayer/representative to be present *during* the discussions, not afterwards.²⁷

Lastly, in *Industrial Investors v. Commissioner*,²⁸ the taxpayer (a corporation) requested a Collection Due Process hearing under IRC §6330 after the IRS proposed a levy. The taxpayer intended to submit an OIC to resolve the outstanding deficiencies. Accompanying the file on its way to Appeals was a cover letter from the Revenue Officer urging the Appeals Officer to summarily deny the OIC due to the

taxpayer's previous "delays" (i.e., litigation initiated by the taxpayer in Tax Court and the Court of Appeals over the amounts of the deficiencies). The Tax Court commented that the paper trail showed "an unusual haste" on the part of the Appeals Officer "to get the hearing over with and rule against the taxpayer . . . leaving no doubt that his impartiality was compromised." The Tax Court held that the cover letter was an *ex parte* communication because "It put the revenue officer's spin on what he thought of [the taxpayer and its representative], and blatantly advocated a particular result." As a remedy, and stating "This needs to stop," the Tax Court remanded the case back to Appeals for a new hearing with a different Appeals Officer who had not been exposed to the *ex parte* letter.

IV. WHAT SHOULD BE DONE ABOUT THE LACK OF A TAXPAYER REMEDY?

Congress needs to enact language that provides the taxpayer with relief when an Appeals Officer engages in prohibited *ex parte* communications with another IRS employee.

The remedy that the courts have fashioned in two of the cases discussed above (remand the case back to Appeals for a new hearing) is inadequate. Moreover, this "remedy" actually punishes the taxpayer because he or she must incur additional costs, such as paying a representative or taking off from work, to participate in a new Appeals hearing. Taxpayers should not be punished when IRS employees engage in prohibited conduct.

The remedy need not be harsh, but it should impose some sort of sanction upon the IRS so that the prohibition on *ex parte* communications is meaningful.

In my opinion, the legislation should include a requirement stating that in the event that an Appeals Officer engages in prohibited *ex parte* communications with another IRS employee, the taxpayer is entitled to a new hearing with an independent Appeals Officer who has no prior knowledge of, or involvement with the case. In addition, the legislation should award the taxpayer with at least \$500 as compensation for the damages suffered as a result of the prohibited *ex parte* communications. These provisions will put some "teeth" into the rules, and will ensure that taxpayers are treated fairly and that Appeals Officers remain independent.

ENDNOTES

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2. Pub. L. 105-206, 112 Stat. 689.
3. *Id.*, sec. 1001(a)(4).
4. Notice 99-50, 1999-40 I.R.B. 444 (October 4, 1999).
5. Rev. Proc. 2000-43, 2000-2 C.B. 404.
6. *Id.*, Sec. 3, Q&A-1, 2000-2 C.B. at 405.
7. *Id.*, Sec. 3, Q&A-5, 2000-2 C.B. at 405-06.
8. *Id.*, Sec. 3, Q&A-6, 2000-2 C.B. at 406.
9. *Id.*, Sec. 3, Q&A-11, 2000-2 C.B. at 407.
10. *Id.* at 406-07.
11. *Id.*, Sec. 3, Q&A-21, 2000-2 C.B. at 408.
12. *Id.*, Sec. 3, Q&A-22, 2000-2 C.B. at 408.
13. *Id.*, Sec. 3, Q&A-29, 2000-2 C.B. at 409.
14. *Id.*
15. *Id.*
16. There are two other cases in which the taxpayers alleged that the Appeals Officer engaged in prohibited *ex parte* communications with other IRS employees, but the Tax Court held that the discussions were not prohibited. See *Harrell v. Comm'r*, T.C. Memo. 2003-271; *Sapp v. Comm'r*, T.C. Memo. 2006-104.
17. *Robert v. United States*, 364 F.3d 988 (8th Cir. 2004), *aff'g* 91 AFTR2d (RIA) 2003-602, 2003-1 USTC (CCH) ¶50,212 (E.D. Mo. 2003).

18. The related case was *Swope v. Siegel-Robert, Inc.*, 74 F.Supp.2d 876, 879–910 (E.D. Mo. 1999), aff'd in part and rev'd in part 243 F.3d 486 (8th Cir. 2001).
19. *Robert v. United States*, 364 F.3d 988 (8th Cir. 2004), aff'g 91 AFTR2d (RIA) 2003–602, 2003–1 USTC (CCH) ¶50,212 (E.D. Mo. 2003).
20. *United States v. James Daniel Good Real Prop.*, 510 U.S. 43, 63 (1993) (“if a statute does not specify a consequence for noncompliance with statutory timing provisions, the federal courts will not in the ordinary course impose their own coercive sanction.”).
21. *Robert v. United States*, 364 F.3d 988 (8th Cir. 2004), aff'g 91 AFTR2d (RIA) 2003–602, 2003–1 USTC (CCH) ¶50,212 (E.D. Mo. 2003).
22. *Drake v. Comm'r*, 105 T.C. 201 (2005).
23. IRC §6330(a) provides that no levy may be made on any property or right to property of a person unless the Secretary first notifies the person in writing of the right to a hearing before the IRS Office of Appeals. Section 6330(c)(1) provides that the Appeals Officer must verify at the hearing that applicable laws and administrative procedures have been followed. At the hearing, the person may raise any relevant issue relating to the unpaid tax or the proposed levy, including appropriate spousal defenses, challenges to the appropriateness of collection actions, and collection alternatives. IRC §6330(c)(2)(A).
24. *Moore v. Comm'r*, T.C. Memo. 2006–171.
25. IRC §6320(b) gives a taxpayer the right to request a hearing within 30 days after the IRS sends a Notice of Federal Tax Lien to the taxpayer. The hearing is held before the IRS Office of Appeals and is conducted by an officer or employee who has had no prior involvement with the case. IRC §6320(b).
26. See Action On Decision 2007–2 (Feb. 27, 2007). A nonacquiescence is the IRS's formal statement that it disagrees with the court's decision.
27. See Rev. Proc. 2000–43, *supra*, Sec. 3, Q&A-21, 2000–2 C.B. at 408, “opportunity to participate . . . means that the taxpayer/representative will be given a reasonable opportunity to attend a meeting or be a participant in a conference call between Appeals and the originating function when the strengths and weaknesses of issues or positions in the taxpayer's case are discussed.”
28. *Industrial Investors v. Comm'r*, T.C. Memo. 2007–93.