

## MOST LITIGATED ISSUES: Introduction

Internal Revenue Code (IRC) § 7803(c)(2)(B)(ii)(X) requires the National Taxpayer Advocate to identify in her Annual Report to Congress (ARC) the ten tax issues most litigated in federal courts (Most Litigated Issues).<sup>1</sup> The National Taxpayer Advocate may analyze these issues to develop recommendations to mitigate the disputes resulting in litigation.

The Taxpayer Advocate Service (TAS) identified the Most Litigated Issues from June 1, 2013, through May 31, 2014, by using commercial legal research databases. For purposes of this section of the Annual Report, the term “litigated” means cases in which the court issued an opinion.<sup>2</sup> This year’s Most Litigated Issues are:

- Accuracy-related penalty (IRC § 6662(b)(1) (2), and (3));<sup>3</sup>
- Trade or business expenses (IRC § 162(a) and related Code sections);
- Summons enforcement (IRC §§ 7602(a), 7604(a), and 7609(a));
- Gross income (IRC § 61 and related Code sections);
- Collection due process (CDP) hearings (IRC §§ 6320 and 6330);
- Failure to file penalty (IRC § 6651(a)(1)), failure to pay penalty (IRC § 6651(a)(2)), and failure to pay estimated tax penalty (IRC § 6654);
- Civil actions to enforce federal tax liens or to subject property to payment of tax (IRC § 7403);
- Frivolous issues penalty (IRC § 6673 and related appellate-level sanctions);
- Charitable deductions (IRC §170); and
- Passive activity losses and credits (IRC § 469).<sup>4</sup>

All of these issues were identified as Most Litigated Issues last year, with the exception of passive activity losses and credits.<sup>5</sup> Accuracy-related penalties remained the top issue this year, although we identified 25 fewer cases.<sup>6</sup> The number of CDP cases decreased significantly this year with 105 cases in 2013, and only

1 Federal tax cases are tried in the United States Tax Court, United States District Courts, the United States Court of Federal Claims, United States Bankruptcy Courts, United States Courts of Appeals, and the United States Supreme Court.

2 Many cases are resolved before the court issues an opinion. Some taxpayers reach a settlement with the IRS before trial, while the courts dismiss other taxpayers’ cases for a variety of reasons, including lack of jurisdiction and lack of prosecution. Additionally, courts can issue less formal “bench opinions,” which are not published or precedential.

3 IRC § 6662 also includes (b)(4), (5), (6), and (7), but because those types of accuracy-related penalties were not heavily litigated, we have only analyzed (b)(1), (2), and (3).

4 This year we identified cases under IRC §§ 7402, 7407, and 7408 which involve injunctions against tax return preparers. While there was a high number of cases, most of the cases were conceded or not decided on the merits. Therefore, we have not included this issue in the top ten this year. However, the frequency of this issue underscores the need for regulation of tax return preparers, which the National Taxpayer Advocate has continuously recommended. See, e.g., National Taxpayer Advocate 2013 Annual Report to Congress 61 (Most Serious Problem: *Regulation of Return Preparers*); National Taxpayer Advocate 2008 Annual Report to Congress 423 (Legislative Recommendation: *The Time Has Come to Regulate Federal Tax Return Preparers*); National Taxpayer Advocate 2003 Annual Report to Congress 270 (Legislative Recommendation: *Federal Tax Return Preparers Oversight and Compliance*); National Taxpayer Advocate 2002 Annual Report to Congress 216 (Legislative Recommendation: *Regulation of Federal Tax Return Preparers*).

5 See National Taxpayer Advocate 2013 Annual Report to Congress 322.

6 See *id.* at 339.

76 in 2014.<sup>7</sup> Cases involving failure to pay and failure to file penalties saw the largest decrease of about 35 percent with 86 cases in 2013, and only 56 in 2014.<sup>8</sup>

Once TAS identified the Most Litigated Issues, it analyzed each one in four sections: summary of findings, description of present law, analysis of the litigated cases, and conclusion. Each case is listed in Appendix III, which categorizes the cases by type of taxpayer (*i.e.*, individual or business).<sup>9</sup> Appendix III also provides the citation for each case, indicates whether the taxpayer was represented at trial or argued the case *pro se* (*i.e.*, without representation), and lists the court's decision.<sup>10</sup>

We have also included a “Significant Cases” section summarizing decisions that are not among the top ten issues but are relevant to tax administration.<sup>11</sup> This year, the Significant Cases discussion includes three decisions issued by the Supreme Court that impact tax administration issues.<sup>12</sup>

## AN OVERVIEW OF HOW TAX ISSUES ARE LITIGATED

Initially, taxpayers can generally litigate a tax matter in four different types of courts:

- The United States Tax Court;
- United States District Courts;
- The United States Court of Federal Claims; and
- United States Bankruptcy Courts.

With limited exceptions, taxpayers have an automatic right of appeal from decisions of any of these courts.<sup>13</sup>

The Tax Court is a “prepayment” forum. In other words, taxpayers can access the Tax Court without having to pay the disputed tax in advance. The Tax Court has jurisdiction over a variety of issues, including

<sup>7</sup> National Taxpayer Advocate 2013 Annual Report to Congress 371.

<sup>8</sup> See *id.* at 384.

<sup>9</sup> Individuals filing Schedules C, E, or F are deemed business taxpayers for purposes of this discussion even if items reported on such schedules were not the subject of litigation.

<sup>10</sup> “Pro se” means “for oneself; on one’s own behalf; without a lawyer.” *Black’s Law Dictionary* (10th ed. 2014), available at Westlaw BLACKS. For purposes of this analysis, we considered the court’s decision with respect to the issue analyzed only. A “split” decision is defined as a partial allowance on the specific issue analyzed. The citations also indicate whether decisions were on appeal at the time this report went to print.

<sup>11</sup> Two of the cases discussed in the “Significant Cases” section of this report were decided outside the June 1, 2013, through May 31, 2014, period used to identify the ten most litigated issues, but we nonetheless have included these cases because of their impact on tax administration.

<sup>12</sup> *United States v. Clarke*, 134 S. Ct. 2361 (2014), *vacating and remanding* 517 F. App’x 689 (11th Cir. 2013), *vacating and remanding* 2012-2 U.S.T.C. (CCH) ¶ 50,732 (S.D. Fla. 2012), *on remand*, 573 F. App’x. 826 (2014); *United States v. Quality Stores, Inc.*, 134 S. Ct. 1395 (2014), *rev’g* 693 F.3d 605 (6th Cir. 2012), *aff’g* 424 B.R. 237 (W.D. Mich. 2010), *aff’g* 383 B.R. 67 (Bankr. W.D. Mich. 2008); *United States v. Woods*, 134 S. Ct. 557 (2013), *rev’g* 471 F. App’x 320 (5th Cir. 2012), *aff’g* 794 F. Supp. 2d 714 (W.D. Tex. 2011).

<sup>13</sup> See IRC § 7482, which provides that the United States Courts of Appeals (other than the United States Court of Appeals for the Federal Circuit) have jurisdiction to review the decisions of the Tax Court. There are exceptions to this general rule. For example, IRC § 7463 provides special procedures for small Tax Court cases (where the amount of deficiency or claimed overpayment totals \$50,000 or less) for which appellate review is not available. See also 28 U.S.C. § 1294 (appeals from a United States District Court are to the appropriate United States Court of Appeals); 28 U.S.C. § 1295 (appeals from the United States Court of Federal Claims are heard in the United States Court of Appeals for the Federal Circuit); 28 U.S.C. § 1254 (appeals from the United States Courts of Appeals may be reviewed by the United States Supreme Court). See also *Byers v. Comm’r*, 740 F.3d 668 (D.C. 2014), *cert. denied*, 83 U.S.L.W. 3189 (U.S. Oct. 6, 2014) (No. 14-74) (the D.C. Circuit will not transfer cases to another circuit in non-liability CDP cases unless both parties stipulate to transfer the case).

deficiencies, certain declaratory judgment actions, appeals from collection due process hearings, relief from joint and several liability, and determination of employment status.<sup>14</sup>

The United States District Courts and the United States Court of Federal Claims have concurrent jurisdiction over tax matters in which (1) the tax has been assessed and paid in full,<sup>15</sup> and (2) the taxpayer has filed an administrative claim for refund.<sup>16</sup> The United States District Courts, along with the bankruptcy courts in very limited circumstances, provide the only fora in which a taxpayer can receive a jury trial.<sup>17</sup> Bankruptcy courts can adjudicate tax matters that were not adjudicated prior to the initiation of a bankruptcy case.<sup>18</sup>

### ANALYSIS OF *PRO SE* LITIGATION

As in previous years, many taxpayers appeared before the courts *pro se*. Figure 3.0.1 lists the Most Litigated Issues for the review period of June 1, 2013, through May 31, 2014, and identifies the number of cases, broken down by issue, in which taxpayers appeared without representation. As the table illustrates, the issues with the highest rates of *pro se* appearance are failure to file, failure to pay, and estimated tax penalties and the frivolous issues penalty.

**FIGURE 3.0.1, *Pro se* cases by issue**

Most Litigated Issue	Litigated Cases Reviewed	<i>Pro Se</i> Litigation	% of Cases Involving <i>Pro Se</i> Taxpayers
Accuracy-Related Penalty	153	81	53%
Trade or Business Expenses	115	74	64%
Summons Enforcement	102	70	69%
Gross Income	89	55	62%
Collection Due Process	76	48	63%
Failure to File, Failure to Pay, and Estimated Tax Penalties	56	41	73%
Civil Actions to Enforce Federal Tax Liens or to Subject Property to Payment of Tax	52	26	50%
Frivolous Issues Penalty (and analogous appellate-level sanctions)	30	28	93%
Charitable Deductions	30	13	43%
Passive Activity Losses and Credits	28	17	61%
<b>Total</b>	<b>731</b>	<b>453</b>	<b>62%</b>

14 IRC §§ 6214; 7476-7479; 6330(d); 6015(e); 7436.

15 28 U.S.C. § 1346(a)(1). See *Flora v. United States*, 362 U.S. 145 (1960), *reh'g denied*, 362 U.S. 972 (1960).

16 IRC § 7422(a).

17 The bankruptcy court may only conduct a jury trial if the right to a trial by jury applies, all parties expressly consent, and the district court specifically designates the bankruptcy judge to exercise such jurisdiction. 28 U.S.C. § 157(e).

18 See 11 U.S.C. § 505(a)(1) and (a)(2)(A).

Figure 3.0.2 affirms our contention that overall, taxpayers are more likely to prevail if they are represented.

**FIGURE 3.0.2, Outcomes for *pro se* and represented taxpayers**

Most Litigated Issue	Pro Se Taxpayers			Represented Taxpayers		
	Total Cases	Taxpayer prevailed in whole or in part	Percent	Total Cases	Taxpayer prevailed in whole or in part	Percent
Accuracy-Related Penalty	81	11	14%	72	23	32%
Trade or Business Expenses	74	17	23%	41	11	27%
Summons Enforcement	70	0	0%	32	5	16%
Gross Income	55	4	7%	34	12	35%
Collection Due Process	48	2	4%	28	6	21%
Failure to File, Failure to Pay, and Estimated Tax Penalties	41	4	10%	15	3	20%
Civil Actions to Enforce Federal Tax Liens or to Subject Property to Payment of Tax	26	2	8%	26	3	12%
Frivolous Issues Penalty (and analogous appellate-level sanctions)	28	4	14%	2	1	50%
Charitable Contributions	13	2	15%	17	3	18%
Passive Activity Losses and Credits	17	1	6%	11	4	36%
<b>Total</b>	<b>453</b>	<b>47</b>	<b>10%</b>	<b>278</b>	<b>71</b>	<b>26%</b>