

Department  
of the  
Treasury

Internal  
Revenue  
Service

Office of  
Chief Counsel

**N o t i c e**

N(35)000-156

August 5, 1998

Internal Revenue Service

**Subject:** Restructuring and Reform Act of 1998 **Cancellation Date:** February 1, 1999

The purpose of this Notice is to summarize some of the changes made by the Internal Revenue Service Restructuring and Reform Act of 1998 (RRA), Pub. L. No. 105-206, 112 Stat. 685 (1998), which will affect the tax litigation function. The Act was signed into law on July 22, 1998. This Notice also provides some interim processing instructions for cases under these provisions. The effective dates of the provisions discussed in this Notice are set forth below.

#### **Burden of Proof RRA Sec. 3001; I.R.C. § 7491**

New section 7491(a) places the burden of proof on the Service in any court proceeding involving a factual issue if the taxpayer introduces credible evidence with respect to the factual issue relevant to ascertaining the taxpayer's tax liability. The Service will have the burden of proof under this section if the taxpayer: (1) complies with all the substantiation requirements of the Code; (2) maintains all the records required by the Code; (3) cooperates with the Service's reasonable requests for information; and (4) meets certain net worth requirements. The new section applies to income, estate, gift and generation skipping taxes. Corporations, trusts and partnerships whose net worth exceeds \$7 million are not eligible for the benefits of the new section. No net worth limitation is applicable to individuals.

Section 7491(b) places the burden of proof on the Service in any court proceeding where the Service reconstructs a taxpayer's income solely through the use of statistical information of unrelated taxpayers. With respect to this subsection, there is no requirement that the taxpayer maintain records or cooperate with the Service.

Section 7491(c) provides that the Service shall have the burden of production in any court proceeding relating to the appropriateness of applying penalties, additions to tax and additional amounts imposed by the Code to the taxpayer.

**Effective Date:** Court proceedings arising in connection with audits beginning after the date of enactment. Where there is no audit, the amendment applies to tax periods or events beginning after the date of enactment.

---

Filing Instructions: Binder Part (35 )                      Master Sets: NO X RO X  
NO: Circulate    Distribute X to: All Personnel    Attorneys X In: all divisions  
RO: Circulate    Distribute X to: All Personnel    Attorneys X In: all divisions  
Other National and Regional FOIA Reading Rooms  
Electronic Filename: RRA98.pdf Original signed copy in: CC:F&M:PA

### **Expansion of Authority to Award Costs and Certain Fees (RRA Sec. 3101; I.R.C. § 7430)**

RRA modifies section 7430 to allow for recoveries of reasonable administrative costs back to the date of the first letter of proposed deficiency that allows a taxpayer an opportunity of administrative review in the Office of Appeals. The point of determining the reasonableness of the Service's determination, however, has not changed. This point remains at the time the matter is finally determined by Appeals or at the time the notice of deficiency is issued. RRA also raises the hourly rate cap to the amount provided in the Equal Access to Justice Act, expands the reasons available for exceeding that hourly rate cap, considers losses in other circuits to be relevant to the issue of substantial justification, allows for the recovery of fees by pro bono representatives, and imposes a rule awarding litigation and administrative costs where the Service rejects a "qualified offer" during the "qualified offer period" and later recovers less than the amount offered. Specific further guidance on this last issue will be provided at a later time.

Effective Date: Costs incurred and services performed more than 180 days after the date of enactment.

Interim Instructions: Until further guidance is issued, any instance of a claimed "qualified offer" should be immediately brought to the attention of the Field Service Division.

### **Increase in Size of Cases Permitted on Small Case Calendar (RRA Sec. 3103; I.R.C. § 7463)**

RRA amends section 7463 to increase the dollar amount for small case treatment from \$10,000 to \$50,000. The notice of deficiency must be modified to reflect this change.

Effective Date: Proceedings commenced after the date of enactment.

Interim Instructions: Cases should be screened by district counsel attorneys when petitions are filed to determine if cases are appropriately under the small case procedures. Objections to small case treatment, where warranted, should be filed immediately after such screening.

### **Actions for Refund with Respect to Certain Estates Which Have Elected the Installment Method of Payment (RRA Sec. 3104; I.R.C. § 7422)**

RRA amends section 7422 by adding a special rule applicable to estates that under section 6166 pay the estate tax due in installments. Under this provision, federal district courts and the United States Court of Federal Claims have jurisdiction to determine the correct amount of estate tax liability, notwithstanding that the full amount of the estate tax liability has not been paid, provided that required payments are current. If, under this provision, a court redetermines the estate tax liability of an estate, no part of the estate tax liability that is

disallowed by a final court decision may be collected, and amounts paid in excess of the installments determined as currently due and payable, must be refunded by the Service.

Effective Date: Claims for refund filed after the date of enactment.

### **Administrative Appeal of Adverse Examination Determination of Tax-Exempt Status of Bond Issue (RRA Sec. 3105; No Code Section Affected)**

RRA directs the Service to modify its administrative procedures to allow tax-exempt bond issuers to appeal an adverse examination determination to the Appeals Division of the IRS as a matter of right. Section 3105 directs that the appeals be heard by senior appeals officers having experience in resolving complex cases. As a result, issuers of tax-exempt bonds, following an adverse examination determination, have the right to protest the determination to the Appeals Division, before the interest on the bonds is declared taxable.

Effective Date: Date of enactment.

### **Relief from Joint and Several Liability on Joint Returns - Petition for Review by Tax Court (RRA Sec. 3201; I.R.C. § 6015(e))**

RRA adds section 6015, which liberalizes the innocent spouse provisions formerly contained in section 6013(e) and provides taxpayers who are no longer married or who are legally separated or living apart the opportunity to limit their liability by electing to allocate the deficiency. The statute confers jurisdiction upon the Tax Court to review the determination of the Secretary as to the relief available under section 6015. In addition, under certain circumstances, where relief is unavailable under the section, the statute authorizes the Secretary to exercise equitable powers to fashion relief. This last provision will not be effective until rules and procedures are issued.

Effective Date: Generally applies to any liability for tax arising after the date of enactment and any liability for tax arising on or before such date but remaining unpaid as of such date.

Interim Instructions: Tax liabilities are generally unpaid on pending Tax Court cases; therefore, the new provisions apply to all pending Tax Court cases. All pending cases should be considered by Counsel and Appeals under the RRA provisions. No specific claim or election should be required in order for the new provisions to be applied to existing litigation.

### **Suspension of Statute of Limitations on Filing Refund Claims During Period of Disability (RRA Sec. 3202; I.R.C. § 6511)**

RRA amends section 6511 to provide that the statute of limitations for filing a refund claim shall be suspended during the period when a taxpayer is financially disabled. "Financially disabled" is defined as the time period when an individual's physical or mental impairment can be expected to result in death or to last for a continuous period of not less than 12

months. The provision shall not apply during the periods in which the taxpayer's spouse or another person is authorized to act on the taxpayer's behalf for financial matters.

Effective date: Periods of disability before, on or after the date of enactment. The amendment does not apply to any claim for refund or credit that, without regard to this section, is barred by operation of law as of the date of enactment.

### **Elimination of Interest Rate Differential on Overlapping Periods of Interest on Tax Overpayments and Underpayments (RRA Sec. 3301; I.R.C. § 6621(d))**

RRA amends section 6621 to eliminate the differential between interest charged on an overpayment and interest paid on an underpayment, for any type of taxes, when the overpayment and underpayment are for the same tax period. As of the date of enactment, this interest rate differential will be eliminated.

Effective Date: Generally applies to interest for periods beginning after the date of enactment. The amendment also applies to interest for periods beginning before the date of enactment if: (1) the taxpayer can reasonably identify and establish the overpayment and underpayment periods; and (2) the taxpayer requests such retroactive relief before December 31, 1999.

### **Increase in Overpayment Rate Payable to Taxpayers Other than Corporations (RRA Sec. 3302; I.R.C. § 6621(a)(1))**

RRA 3302 amends section 6621(a)(1) to modify the rate of interest paid on overpayments of tax. The new interest overpayment rate is the federal short term interest rate (AFR) plus three percentage points for taxpayers other than corporations. For corporations, the overpayment interest rate remains as AFR, plus two percentage points.

Effective Date: Interest for the second and succeeding calendar quarters beginning after the date of enactment.

### **Due Process in IRS Collection Actions (RRA Sec. 3401; I.R.C. §§ 6320, 6330)**

RRA adds new sections 6320 and 6330 to the Code, which establish formal procedures designed to ensure due process to taxpayers where the IRS engages in collection action by notice of lien or levy (including seizures). Under the new procedures, after a notice of intent to levy or notice of lien is issued, the taxpayer may demand a hearing before an appeals officer who has had no prior involvement with the taxpayer's case. Generally, the subjects of the hearing would be collection issues. However, the taxpayer could raise the merits of the tax liability if the notice of deficiency had not actually been received or the taxpayer had no opportunity to previously dispute the liability. Thereafter, the taxpayer may contest the written determination of the appeals officer in the Tax Court or, where appropriate, the district court, by filing a petition within 30 days of the date of the appeals officer's written

determination. The proper court is the Tax Court if the Tax Court has jurisdiction of that tax. If not, the proper court is the United States District Court. If an appeal is made to the incorrect court, the taxpayer shall have 30 days after the court's determination to file an appeal with the correct court. Where the merits of the tax liability was properly at issue in the hearing, the court will review that issue on a de novo basis. Where the merits of the tax liability was not properly part of the appeal, the court will review the appeal using an abuse of discretion standard. During the pendency of the hearings, the collection statute of limitations is suspended.

Effective Date: Collection actions initiated more than 180 days after the date of enactment.

**Confidentiality Privileges Relating to Taxpayer Communications (RRA Sec.3411; I.R.C. § 7525)**

RRA adds new section 7525 to the Code. This provision extends the attorney-client privilege of confidentiality to "tax advice" furnished to a taxpayer by any "federally authorized tax practitioner." A "federally authorized tax practitioner" is a person described in Circular 230 as subject to regulation. "Tax advice" means any advice given "with respect to a matter which is within the scope of the individual's authority to practice" under 31 U.S.C. § 330. The new privilege may only be asserted in any "noncriminal tax matter before the Service" and in "any noncriminal tax proceeding in federal court with respect to such matter," and may be asserted "to the extent the communication would be considered a privileged communication if it were between a taxpayer and an attorney." The new privilege may be waived in the same manner as the attorney-client privilege. This new privilege does not, however, apply to any written communications made between a corporation or its representative and a federally authorized tax practitioner in connection with the promotion of the direct or indirect participation of the corporation in any tax shelter.

Effective Date: Communications made on or after the date of enactment.

**Limitation on Financial Status Audit Techniques (RRA Sec. 3412; I.R.C. § 7602(d))**

RRA amends section 7602 to limit the use of financial status or economic reality examination techniques to determine the existence of a taxpayer's unreported income. The Service cannot use these techniques unless the Service has a "reasonable indication that there is a likelihood of unreported income."

Effective Date: Date of enactment.

**Software Trade Secrets Protection (RRA Sec. 3413; I.R.C. § 7612)**

RRA adds section 7612, which generally prohibits the issuance of a summons for tax related computer software source codes. The general prohibition does not apply to criminal tax investigations, to any tax-related computer software source codes developed by the taxpayer

for internal use rather than for commercial distribution, to communications between the owner of the source codes and the taxpayer or related person, or to any source codes which are required to be provided or made available pursuant to any other provision of the Code.

Section 7612 provides conditions under which a summons for source code may be issued, as follows: (1) the Service is unable to reasonably ascertain the correctness of any item on a return from the taxpayer's books and records or the software program and associated data, (2) the Service identifies with reasonable specificity the portion of the source code needed to verify the correctness of an item, and (3) the Service determines that the need for the source code outweighs the risk of unauthorized disclosure of trade secrets. The Service is considered to have satisfied the first two requirements if the Service makes a formal request for those items to the taxpayer and the owner of the software and the request is not satisfied within 180 days.

Section 7612 also authorizes courts in summons enforcement proceedings to issue any order necessary to prevent the improper disclosure of trade secrets and confidential information. In addition, the provision contains specific conditions with which the Service must comply when it receives computer source codes and/or software programs. The provision does not prevent the Service from using knowledge that it obtains during the course of an examination. The Service is not permitted, however, to use the source codes or software to examine other taxpayers.

Effective Date: Generally applicable to summonses issued, and software acquired, after the date of enactment. There are special effective date provisions for software acquired on or before the date of enactment.

**Notice of Deficiency to Specify Deadlines for Filing Tax Court Petition (RRA Sec. 3463; I.R.C. § 6213(a)) and Advise of Local Taxpayer Advocate (RRA Sec. 1102(b); I.R.C. § 6212 (a))**

RRA amends section 6213(a) to require the Service to include on the notice of deficiency the last day on which the taxpayer may file a petition in the Tax Court. If the petition is filed on or before the day specified in the notice of deficiency, the petition will be treated as timely filed. The RRA also requires the notice of deficiency to advise of the right to contact the local taxpayer advocate and to provide the location and telephone number of that office.

Effective Date: Notices mailed after December 31, 1998, except with respect to notification of local taxpayer advocate, which is effective on date of enactment.

**Refund or Credit of Overpayments Before Final Determination (RRA Sec. 3464; I.R.C. §§ 6213, 6512(a),(b))**

RRA amends sections 6213(a) and 6512(a) to allow any federal court with jurisdiction to order (1) a refund of any amount collected with respect to a deficiency during a period when

the Service was barred from collecting the deficiency and (2) a refund or credit of an overpayment the Service is authorized to refund or credit pending appeal. In addition, section 6512(b) is modified to grant the Service authority to refund or credit that portion of any overpayment determined by the Tax Court to the extent the overpayment is not contested on appeal.

Effective Date: Date of enactment.

### **IRS Procedures Relating to Appeals of Examinations and Collections (RRA Sec. 3465; I.R.C. § 7123)**

RRA recodifies existing section 7123 as section 7124. New section 7123 requires the Service to establish procedures for administratively addressing disputes. Section 7123 requires the following procedures to be established: (1) early referral of disputes from Collection or Examination to Appeals; (2) nonbinding mediation of issues that are unresolved at the end of the appeals procedure; (3) nonbinding mediation when the taxpayer and the Service have unsuccessfully attempted to enter into a closing agreement or offer in compromise; and (4) an Appeals pilot program for binding arbitration of unresolved issues including closing agreements and offers-in-compromise. In addition, section 7123 requires the Service to ensure that an appeals officer is regularly available in each state and to consider Appeals video conferences for rural or remote areas.

Effective Date: Date of enactment.

### **Prohibition on Request to Taxpayers to Give Up Rights to Bring Actions (RRA Sec. 3468; No Code Section Affected)**

RRA provides that the Service may not request taxpayers to waive their rights to sue the government or a government employee for an action taken relating to a tax law unless (1) the taxpayer knowingly and voluntarily waives his rights; or (2) the request is made in the presence of the taxpayer's representative or in writing to the taxpayer's representative.

Effective Date: Date of enactment.

### **Notification of Change in Tax Matters Partner (RRA Sec. 3507; I.R.C. § 6231)**

Under prior law, if the Service designated a Tax Matters Partner (TMP), the partnership, rather than the Service, was required to notify the partners of the designation. RRA provides that when the Service designates a TMP, the Service is required to notify all partners entitled to receive notice under section 6223(a) of the name and address of the person designated.

Effective Date: Selections of TMPs made by the Service after the date of enactment.

**Disclosure of Chief Counsel Advice (RRA Sec. 3509; I.R.C. § 6110)**

RRA amends section 6110 to establish a structured process by which the Service will disclose to the public certain written advice designated as "Chief Counsel Advice." Chief Counsel Advice is written advice prepared by the National Office of the Office of Chief Counsel and issued to an I.R.S. field office, service center, regional counsel or district counsel office that conveys: (1) a legal interpretation of a revenue provision; (2) any Service or Chief Counsel position or policy concerning a revenue position; or (3) any interpretation of state law, foreign law or other federal law relating to the assessment or collection of any liability under a revenue provision. This provision provides that Chief Counsel Advice are written determinations subject to section 6110. In the future, these determinations will routinely be made public, both in paper and electronic formats.

Effective Date: Generally effective for Chief Counsel Advice issued 90 days after enactment. There is a schedule for disclosure of Chief Counsel Advice issued after 1985 and before the 91st day after the date of enactment.

**Illegal Tax Protester Designation (RRA Sec. 3707; No Code Section Affected)**

RRA provides that the Service may not designate taxpayers as illegal tax protesters (or similar designations). Illegal tax protester designations must be removed from each taxpayer's master file beginning January 1, 1999. Service personnel must disregard any illegal tax protester designation contained in the taxpayer's file. The Service may designate an appropriate taxpayer as a "nonfiler" on the master file. Once designated as a "nonfiler," this notation may remain on the master file for all subsequent taxable periods until the taxpayer has timely filed returns (and paid all taxes shown thereon) for two consecutive years.

Effective Date: Date of enactment.

**Listing of Local IRS Telephone Numbers and Addresses (RRA Sec. 3709; No Code Section Affected)**

RRA provides that the district offices must, as soon as practicable, but no less than 180 days after the date of enactment, arrange for the publication of the addresses and phone numbers of local IRS offices in appropriate local telephone directories.

Effective Date: 180 days after the date of enactment.

Attorneys with questions concerning RRA sections 3001, 3103, 3104, 3202, 3301, 3302, 3401, 3411, 3412, 3463, 3464, 3465, 3468, 3507, 3509, 3707, or 3709 should contact the Procedural Branch of the Field Service Division at (202) 622-7940 or (202) 622-7950. Attorneys with questions concerning RRA sections 3101 or 3201 should contact the Income Tax & Accounting Branch of the Field Service Division at (202) 622-7900. Attorneys with



questions regarding RRA section 3105 should contact the Financial Institutions & Products Branch of the Field Service Division at (202) 622-7870. Attorneys with questions regarding RRA section 3413 should contact Branch 3 of the General Litigation Division at (202) 622-3630.

Following publication of this Notice, appropriate changes will be made to the Chief Counsel Directives Manual.

Summaries of these, and other RRA provisions, are also available from the IRS Intranet, accessible from the Chief Counsel Intranet. From CASE CN, click on IRS HQ Web, then to "News Flash/Latest Additions, then "Document 10829 Templates". The provisions are then accessible in "html" and "pdf" formats.

\_\_\_\_\_/s/\_\_\_\_\_  
JUDITH C. DUNN  
Associate Chief Counsel  
(Domestic)