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Estate & Gift Update Part 1: IRS Challenges to Your Client's Best-Laid Plans

Estate & Gift Update Part 2: Pitfalls When Handling the Estate

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Fiduciary Representation in Pre-Litigation Estate and Gift Tax Controversies

by Frank Agostino, Lawrence A. Sannicandro, and Jamie M. Zug

Table of Contents

I. Introduction

When the Tax Cuts and Jobs Act of 2017 ("TCJA") raised the estate and gift tax exclusion amount from $5 million to $10 million (as annually adjusted for inflation), it fundamentally altered estate and gift tax practice. With the exclusion amount so high, the number of taxpayers subject to federal estate tax (and therefore required to file Form 706) plummeted to a third of the pre-TCJA amount. Tax Policy Center, Briefing Book at Table 1, https://tinyurl.com/mryzjda4. However, barring unexpected legislative changes, this heightened exclusion amount will not last. Under current law, it will sunset on January 1, 2026. And proposed legislation could lower it even sooner, leaving today's taxpayers and tax practitioners in the liminal space between the exclusion amount's steep rise and its likely drop.

These circumstances create new needs and opportunities for taxpayers. More decedents than ever fall below the exclusion amount, and in doing so, leave an excess exclusion amount that can be ported to surviving spouses. Tax practitioners can port the decedent's exclusion amount to the surviving spouse by filing Form 706, potentially leading to substantial savings by sheltering bequests that would otherwise be subject to estate tax at the surviving spouse's death. Portability is thus an important tool for any estate where a surviving spouse could be subject to estate tax in the likely event that the exclusion amount is drastically lowered.

All the while, tax practitioners must continue preparing Forms 706 for those taxpayers still subject to federal estate tax. Doing so requires the utmost care since, whereas most tax forms *may* be reviewed by the Internal Revenue Service ("I.R.S." or "Services"), those forms *will* be reviewed and classified for audit potential—an I.R.S. policy driven by the high return rate of estate and gift tax audits.

This outline addresses Form 706 preparation both for portability purposes and for decedents subject to estate tax, providing detailed, practical guidance both for preparing Form 706 and for navigating the audit process.[1]

[1] This outline does not cover State taxes, which may include estate, inheritance, and/or gift taxes.

II. Overview of Estate and Gift Tax

A. General:

1. The Internal Revenue Code ("I.R.C." or "Code") generally imposes a gift tax on certain direct or indirect transfers of property that a U.S. citizen or resident makes by gift. I.R.C. § 2501(a)(1) (U.S. federal gift tax).[2] Additionally, the Code generally imposes an estate tax on the taxable estate of any person who was a citizen or resident at the time of death. I.R.C. § 2001(a). The taxable estate generally equals the decedent's worldwide gross estate less certain allowable deductions, including a marital deduction for certain bequests to the decedent's surviving spouse and a deduction for certain bequests to qualifying charities. I.R.C. §§ 2055(a) (charitable deduction), 2056(a) (marital deduction).

2. The gross estate to which the U.S. federal estate tax may potentially apply consists of all of the decedent's assets, wherever situated in the world, including but not limited to:

   a. Real estate in the decedent's name or in joint name with another to the extent that person contributed to the purchase of the real estate (I.R.C. § 2031(a);

   b. Proceeds of insurance policies on the decedent's life that the decedent owned at death or within three years of death (I.R.C. §§ 2042, 2035(a));

   c. Individual or joint investments (I.R.C. § 2031(a));

   d. Assets which the decedent transferred to another but in which the decedent retained an interest (I.R.C. §§ 2033, 2036(a)); and

   e. Personal property the decedent's name (I.R.C. § 2031(a)).

3. The U.S. federal gift and estate taxes are unified such that a single graduated rate schedule and exemption apply to an individual's cumulative taxable gifts and bequests. I.R.C. § 2001(b), (c). The unified exemption is $12.06 million for 2022 and $12.92 million for 2023 in cumulative taxable transfers from the U.S. federal gift tax or the U.S. federal estate tax of each decedent. Unused exemption as of the death of a spouse generally is available for use by the surviving spouse under a feature of the law sometimes referred to as "portability" (i.e., the deceased spouse's unused exclusion amount is generally ported to the surviving spouse). See

[2] Deductions are allowed for certain gifts to spouses and charities. See I.R.C. §§ 2522(a), 2523(a).

I.R.C. § 2010(c)(4), (5). Importantly, under current law, the applicable exclusion amount for taxable gifts and bequests will decrease to approximately $6.2 million at the end of 2025. See I.R.C. § 2010(c)(3)(C).

4. Finally, in addition to any U.S. federal estate or gift tax that the Code imposes on a transfer, the Code also imposes a separate transfer tax on generation-skipping transfers. I.R.C. § 2601. In general, the U.S. federal generation-skipping transfer tax is imposed on transfers, either directly or through a trust or similar arrangement, to a beneficiary who is at least 37 ½ years younger than the transferor. I.R.C. § 2601; see also I.R.C. § 2613(a). The U.S. federal generation-skipping transfer tax applies only to certain cumulative gifts and bequests totaling more than an exemption amount, which started at $1 million and was indexed for inflation beginning in 1999. See generally I.R.C. § 2631(a), (c).

B. Potential Changes to Exclusion Amount

1. Current Law

a. The TCJA's raised exclusion amount is set to sunset on January 1, 2026.

2. Highlighted Proposals

a. Senator Bernie Sanders' proposal (For the 99.5 Percent Act, S. 994, 117th Cong. (2021)) would:

(1) Decrease the individual estate tax exclusion to $3.5 million;

(2) Decrease the lifetime gift tax exclusion to $1 million;

(3) Decrease the annual gift tax exclusion to a $20,000 total for all beneficiaries.

b. President Biden's General Explanations of the Administration's FY2023 Revenue Proposals, or "Greenbook," did not propose lowering the exclusion amount but instead took aim at specific exclusion strategies for individuals.

III. Preparing Estate and Gift Tax Returns for Portability

A. Portability Definition: Portability is a mechanism for a surviving spouse to add a deceased spouse's unused exclusion amount to the surviving spouse's exclusion amounts. For instance, if a deceased spouse falls $3 million below the exclusion amount at death and portability is elected, the surviving spouse's exclusion amount will be $3 million higher at death than otherwise provided by law.

B. Availability: Portability is available if the decedent was a citizen or resident of the United States, died after 2010, is survived by a spouse, and did not use the full exclusion amount.

C. When Advisable to Elect Portability: Since the exclusion amount is at a record high and, barring legislative change, will continue to increase until January 1, 2026, surviving spouses who could conceivably have a taxable estate after the January 1, 2016 sunset or under proposed legislation should ensure portability is elected. See I.R.C. § 2010(c)(5).

D. Steps to Elect Portability: Portability is elected by timely filing a complete and properly prepared estate tax return. Filing Form 706 triggers portability automatically unless the filer affirmatively chooses not to elect portability and satisfies the requirements of Treas. Reg. § 20.2010-2(a)(3)(i). Treas. Reg. § 20.2010-2(a)(2).

1. Timeliness: As a general rule, the Form 706 must be filed any time within nine months after the decedent's date of death. See I.R.C. § 6075(a).

2. Extension of Time to File Estate Tax Return:

a. I.R.C. § 6081 provides for a six-month extension of time to file an estate tax return. See I.R.C. § 6081(a).

b. Under Rev. Proc. 2022-32, if the estate tax return is filed for portability purposes only within five years of the decedent's death, the return will be accepted as timely filed if the top of the return states: "FILED PURSUANT TO REV. PROC. 2022-32 TO ELECT PORTABILITY UNDER § 2010(c)(5)(A)."

c. If more than five years have passed since the decedent's death, a letter ruling to permit filing an estate tax return for portability purposes may be sought under Treas. Reg. § 301.9100-3.

E. Estimated Valuation Permitted for Certain Property: Treas. Reg. § 20.2010-2(a)(7)(ii) provides simplified reporting requirements for certain property when an estate tax return is filed for portability purposes:

1. General Rule: When an estate tax return is filed for portability purposes, if property is subject to the marital or charitable exclusion, the filer may estimate the value of such property. Id.

    a. A filer estimating the value of property subject to the marital or charitable exclusion must exercise due diligence in doing so, making the filer's best estimate of the of the property's value under penalties of perjury. Treas. Reg. § 20.2010-2(a)(7)(ii)(B).

    b. The filer must provide supporting documentation to demonstrate that the property with the estimated value is subject to the marital or charitable exclusion. See Treas. Reg. § 20.2010-2(a)(7)(ii)(C) at Examples 1 and 2.

2. Exceptions: Estimated valuation is not allowed if:

    a. The property value relates to, affects, or is needed to determine, the value passing from the decedent to a recipient other than the recipient of the marital or charitable deduction property (Treas. Reg. § 20.2010-2(a)(7)(ii)(A)(1));

    b. The property value is needed to determine the estate's eligibility for a generation-skipping transfer tax provision (Treas. Reg. § 20.2010-2(a)(7)(ii)(A)(2));

    c. The property value is needed to determine the value of another estate (id.);

    d. The property value is needed to determine eligibility to elect either the § 2032 alternate valuation date or § 2032A special use valuation (id.);

    e. The property's entire value is not subject to the marital or charitable deduction (Treas. Reg. § 20.2010-2(a)(7)(ii)(A)(3)); or

    f. A QTIP election is made respecting property subject to the marital or charitable deduction (Treas. Reg. § 20.2010-2(a)(7)(ii)(A)(4)).

IV. For Taxpayers Above the Exclusion Amount, Prepare Estate and Gift Tax Returns With the Audit in Sight

A. Filing the Federal Estate Tax Return

1. When Required: The personal representative of an estate generally must file Form 706, *United States (and Generation-Skipping Transfer) Tax Return*, in all cases where the gross estate on the date of death exceeds the basic exclusion amount in effect under I.R.C. § 2010(c) ($12.06 million for 2022, $12.92 million for 2023). As a general rule, the Form 706 must be filed any time within nine months after the decedent's date of death. See I.R.C. § 6075(a).

2. Extension of Time to File Estate Tax Return: I.R.C. § 6081 provides for the extension of time to file an estate tax return. See I.R.C. § 6081(a).

B. Filing the Federal Gift Tax Return

1. Filing Requirements

a. When Required: Generally, I.R.C. § 6019 requires a U.S. federal gift tax return to be filed by any individual who, subject to certain exceptions, makes a transfer by gift which (i) does not qualify for the marital deduction, (ii) does not qualify for the charitable deduction, (iii) is greater than the I.R.C. § 2503(b) annual exclusion amount of $10,000 as adjusted for inflation ($16,000 for 2022 and $17,000 for 2023), or (iv) is not a qualifying medical or educational expense. A gift tax return is made on a Form 709, *United States Gift (and Generation-Skipping Transfer) Tax Return*.

b. When Due:

(1) In General: As a general rule, gift tax return must be filed on or before April 15th of the close of the taxable year. I.R.C. § 6075(b).

(2) Extensions Allowed: I.R.C. § 6081(a) authorizes the Service to extend the filing of a gift tax return by up to six months. Any extension of time granted to a taxpayer for filing the taxpayer's Federal income tax return is deemed to be also an extension of time to file a gift tax return under I.R.C. § 6019.

2. The Period of Limitations on Assessment

a. In General: I.R.C. § 6501 requires the Service to assess a gift tax liability by the later of (1) three years after the due

date of the gift tax return, or (2) three years after the gift tax return was actually filed.

b. May Be Extended by Agreement: I.R.C. § 6501(c)(4) provides that the general three-year period of limitations on assessment may be extended if the Service and the taxpayer agree to do so in writing.

c. Situation in Which Gift Tax May Be Assessed at Any Time:

(1) General Rule: I.R.C. § 6501(c)(9) provides that if a gift is not shown on a gift tax return in a manner adequate to apprise the Service of the nature of the gift, then the gift tax may be assessed at any time with respect to that gift. Most typically, this additional assessment occurs in connection with the filing of the estate tax return.

(2) Adequate Disclosure Especially Important in Gift Tax Cases: Because the failure to adequately disclose a gift on a gift tax return means that the related gift tax can be assessed at any time, it is especially important for practitioners to adequately disclose the gift on the return.

(3) When Is a Gift Not Adequately Disclosed: Internal Revenue Manual ("I.R.M."), pt. 4.25.1.2.1.2 (Jul. 7, 2017) instructs that a gift may be inadequately disclosed if it is:

i. Omitted completely from the return; or

ii. Shown on the return, but the manner in which it is shown is not adequate to apprise the Service as to the nature of the gift.

(4) Protective Returns: In situations in which the taxpayer contends that a gift was not made (*i.e.*, in a bona fide sale for adequate consideration such as a promissory note), it is usually advisable to file a gift tax return reporting a zero tax liability with respect to the "sale." The protective return should disclose all facts and supporting documentation surrounding the "sale." The purpose of filing this protective return is to have the statute of limitations with respect to that "sale" expire from a gift tax perspective.

3. Prompt Assessment Requests

a. In General: Under I.R.C. § 6501(d), the personal representative of an estate may make a request for prompt assessment that will shorten the period of limitations on assessment to 18 months from the date of the written request therefor. Thus, in virtually every case in which a personal representative is filing a gift tax return on behalf of a decedent, it is good practice to make a request for prompt assessment. We discuss the method by which to make a prompt assessment request in Section V.D.3.

C. Planning: Plan With the Audit in Sight

1. Anticipate Your Audience: All estate planners should anticipate their audience from the planning stage forward. "Begin with the end in sight" is good advice to follow. This means you should plan to minimize your audit risks.

2. Practice Tip 1: Always Use Reputable Appraisal Firms: Use reputable and independent appraisal firms whenever valuing property for purposes of estate planning, whether it be in connection with lifetime gifts or preparing an estate tax return.

a. Make Use of the Tax Court Website to Know How Valuators May Be Perceived: Consider searching the United States Tax Court's ("Tax Court's") website related to opinions and orders to evaluate how the Tax Court has treated experts you may engage.

3. Practice Tip 2: Ensure Adequate Documentation for the Audit: Ensure that all necessary documentation is completed during the planning process and stored in a safe place so you can attach it to the estate tax return when necessary.

4. Practice Tip 3: Assume That All Relevant Evidence Will Be Reviewed By An Agent and a Judge: Plan with an expectation that all relevant evidence will be reviewed by an estate and gift tax examiner and/or Judge.

5. Practice Tip 4: Rely on Reference Books for Appraisal: Be sure to double check appraisals against standard references materials (*e.g.*, David Laro & Shannon P. Pratt, Business Valuation and Taxes: Procedure, Law, and Perspective (WG&L 2005)) and case law dealing with similar issues (*e.g.*, fractional interest discounts, discounts for lack of marketability and lack of control). You may not be an appraiser but you are an intelligent person.

D. Estate Tax Return Preparation: Prepare With the Audit in Sight

1. Overview: As noted below, it is a virtual certainty that the estate tax return you prepare will be reviewed by the Service. Like the planning process, estate tax returns should be prepared with the audit in sight.

2. Be Sure to Perfect the Return: An estate tax return, signed under penalties of perjury, certifies that the return is "true, correct, and complete." This means, in addition to making reasoned judgment calls as to how to present a return for examination, that the estate tax return includes all required information and attachments. A common reason for audit is that the estate tax return does not include all required information and attachments. Preparers often overlook (or ignore) the following items that should be included with the return:

    a. Certified copy of will, if decedent died testate;

    b. Certified copy of death certificate;

    c. Form 712, *Life Insurance Statement*, for all life insurance policies listed on return (*i.e.*, on the life of the decedent);

    d. If alternate valuation is elected, evidence of sale or distribution of assets made during the alternate period;

    e. If transfer is by trust, a copy of the instrument;

    f. Power of appointment instruments;

    g. Appraisals on included real estate;

    h. Appraisals on art objects, including paintings, sculptures, tapestries, silverware, or other artifacts, *which are required for art objects with an artistic or intrinsic value of more than $3,000*;

    i. Financial data on non-public enterprises;

    j. State certification of payment of state death taxes;

    k. Copies of Form 709 (gift tax returns) filed by and for the decedent;

    l. Form 706-CE, *Certificate of Payment of Foreign Death Tax*;

    m. For non-resident citizens, copies of inventory and other documents filed in a foreign probate court; and

    n. For non-resident, possibly a former citizen, documents relating to possible expatriation..

3. Secure Powers of Attorney Early:

a. Protection Against Unauthorized Disclosure: I.R.C. § 7213 makes it unlawful for any Federal employee to willfully disclose any return or return information to an unauthorized person. Therefore, the Service takes significant steps to prevent unauthorized disclosure of returns and return information.

b. Properly Execute Part 4 in the Form 706 Will Authorize Disclosure: A properly executed authorization in Part 4 of the Form 706 grants third party authorization. Be sure to complete this information (some return preparers do not). I.R.M., pt. 4.25.1.13(3) (Jul. 7, 2020). If Part 4 of the Form 706 is incomplete, a Form 2848, *Power of Attorney and Declaration of Representative*, should be obtained. Id.

c. Request a Form 2848 in Any Event: Practitioners representing the estate should, after letters of administration have been issued and upon the signing of an engagement letter, have the personal representative or personal representative sign a Form 2848 and/or State-equivalent power of attorney (*e.g.*, Form M-5008-R for New Jersey), so that the representative is authorized to discuss the return with the Service, request gift tax returns, etc.

4. Know What the Service Knows When the Return is Prepared: Before preparing the Form 706, arm yourself with the information the Service knows. Specifically, request or perform the following:

a. Account Transcripts: Request Service account transcripts, including (i) wage and income, (ii) account, (3) gift, and (4) related entity transcripts. Transcripts can be requested by telephone at (800) 908-9946 or online at http://www.irs.gov/Individuals/Get-Transcript;

b. Prior Years' Gift Tax Returns: Order prior years' gift tax returns from the Service by filing Form 4506, *Request for Copy of Tax Return*. Note the $43 fee for each return requested, which is nonrefundable if no return is found;

c. Copies of Predeceased Spouse's Estate Tax Return: If you were not the practitioner who prepared the predeceased spouse's estate tax return, request a copy of this return from the personal representative, or if necessary, the Service, by preparing Form 4506. The Service will request a copy of this return and you should have similar information available to you. Make sure that all assets reported on the predeceased spouse's return are accounted for (or their

disposition explainable by you) in connection with the preparation of the estate tax return before you.

d. Last Three Years of Income Tax Returns: Request the last three years of the decedent's federal and state income tax returns to understand sources of income and assets held (the estate tax return preparer may need to provide the last full year's return for some states);

e. Last Three Years of Bank Statements: Request the last three years of the decedent's bank statements to understand sources of income, potential liabilities, and claims against the estate;

f. FOIA Requests: Practitioners should submit to the Service Disclosure Office a Freedom of Information Request Act, 5 U.S.C. § 552, et seq. ("FOIA") with respect to the six years prior to the decedent's date of death. If the estate tax return is selected for audit, practitioners should make regular FOIA requests to the Service and request third parties to whom summonses have been issued to provide a copy of all records produced to the Service. This will allow the practitioner to monitor the case and ensures that they have all information in the Government's possession;

g. Credit Checks: Perform a credit check on the decedent to learn of liabilities and expenses of the estate;

h. Westlaw's Adverse Judgment Search: Use Westlaw to conduct an adverse judgment search to learn of liabilities and expenses of the estate;

i. Accurint: Use LexisNexis to conduct an Accurint search, which provides detailed information available on businesses and individuals, as well as their assets (including real estate), relatives, and associates;

j. TLO: Use Transunion TLOxp ("TLO"), to search personal information, bankruptcies, foreclosures, liens, judgments, assets, and professional licenses, in addition to other items; and

k. Google Searches: Use Google to understand the decedent and obtain any information about the decedent disseminated online.

5. Address Common Audit Issues in Preparing the Estate Tax Return: Make no mistake, much of your function as a lawyer is to protect your clients from themselves. Trust what your client tell you, but

verify it. Be sure to anticipate the most commonly audited issues when preparing the estate tax return and, topic-by-topic, ask yourself if you have done the following:

a. Adjusted taxable gifts

(1) Have all lifetime gifts been reported on Form 709 and line 4 of Form 706?

(2) Have you reported any gift tax the decedent paid with respect to lifetime gifts on line 7 of Form 706?

(3) If annual exclusions were claimed, did the donee receive a present interest in the transferred property?

b. Schedule A - Real Estate

(1) If the property was not sold, is the fair market value determined on the basis of a reliable appraiser with a copy of the appraisal attached to the return?

(2) If the property was sold in an arm's length transaction, is the sales price reflected?

(3) Are you improperly reporting real estate held jointly (that property should be reported on Schedule E) or real property held by a revocable trust (that property should be reported on Schedule G)?

c. Schedule A-1 - Alternate Use Valuation

(1) Was alternate use valuation property elected and applied on the tax return?

(2) Did you include a copy of the lien to the estate tax return?

(3) Did the estate have a qualified use, did it meet the material participation tests before and after death, and are the liquidity requirements met?

d. Schedule B - Stocks and Bonds

(1) Did you properly identify the securities held (*e.g.*, did you include the number of shares, the CUSIP number or ticker symbols, the exchange on which the stock is traded, and the type of security)?

(2) Did you properly account for accrued interests and dividends?

(3) Did you check the stocks and bonds reported against the dividends and interest reported on the decedent's Form 1040, *U.S. Individual Income Tax Return*?

(4) Are you improperly reporting stocks and bonds held by a revocable trust on Schedule B (those items should be reported on Schedule G)?

e. Schedule F - Closely Held Businesses[2]

(1) Does the governing entity instrument contain requirements for determining the sales price of the closely held business interest? If so, did you adhere to those standards?

(2) Does the closely held business have an established practice for determining the fair market value of the closely held business interest if not disclosed in the agreements? If so, were you consistent in following that approach on the estate tax return?

(3) Are there rights of first refusal which might result in a reduction of the fair market value?

(4) Is the value determines on the basis of a reliable appraisal? Review the entity's tax returns and financial statements to determine the fair market value of the shares.

(5) Have you reviewed for appropriate discounts (*e.g.*, lack of marketability, lack of control, built in gains, key person, etc.)? Is the discount reasonable in the light of existing case law?

f. Schedule C - Mortgages, Notes, and Cash

(1) Did you report self-canceling installment notes, forgiveness of indebtedness, installment sales, promissory notes that are not at arm's length, and below market loans? If so, did you comply with all requirements to take the treatment you are taking?

(2) Are you improperly reporting cash held by a revocable trust on Schedule C (those items should be reported on Schedule G)?

[2] Some States require the submission of additional information in the context of valuing a closely held business.

(3) Are you improperly reporting joint checking accounts on Schedule C (those items should be reported on Schedule E)?

g. Schedule D - Life Insurance

(1) Did you attach Forms 712 for all life insurance policies on the life of the decedent?

(2) To the extent the life insurance is excludible under a life insurance trust, have proper Crummey notices and powers been given?

(3) Did you attach copies of all trust agreements excluding the life insurance?

h. Schedule E - Joint Owned Property

(1) If you are reporting only a fraction of a property's fair market value because of joint ownership, do you have proof of contribution by another party (either by check or affidavit, if necessary)?

(2) Is the payment of expenses and mortgage indebtedness consistent with fractional ownership?

(3) If fractional interests are claimed,

(a) is the fractional interest warranted (*i.e.*, was the property held as tenants in common), and

(b) is the amount of the fractional interest reasonable in the light of existing case law?

i. Schedule F - Misc. Property

(1) Did you report jewelry, antique cars, club memberships, collectibles, etc.? Are these items reported on an insurance rider that the Service may request?

(2) If dealing with family limited partnerships, consider the following:

(a) Did the formation and funding of the partnership result in an indirect gift?

(b) Have you examined whether the interest is includible under I.R.C. § 2036 (retained life estate), I.R.C. § 2037 (transfers taking effect at death), or I.R.C. § 2038 (revocable interests)?

(c) If discounts are claimed, were the discounts reasonable in the light of existing case law?

j. Schedule G - Transfers During the Decedent's Life

(1) Did you report all taxable gifts within three years of death?

(2) Are there revocable trusts? If so, include a copy of the revocable trust agreement with the estate tax return.

(3) Has the value of all transfers to revocable trusts been reported on Schedule G?

(4) Did the decedent have a general power of appointment over a revocable trust that should be reported on Schedule H?

k. Schedule H - Powers of Appointment

(1) Did the decedent have a general power of appointment in a trust created during life?

(2) Did you include copies of the instrument granting the decedent the power of appointment?

l. Schedule I - Annuities

(1) Did you report annuities or a retirement benefit (*e.g.*, IRA, 401(k), etc.) the decedent owned that are payable to a beneficiary at death?

(2) Is the value of the annuity properly calculated?

(3) Did you check income tax returns to determine the annuities the decedent was receiving at death?

m. Schedule J - Expenses Incurred During Administration

(1) Are the expenses claimed as deductions necessarily and reasonably incurred by the estate for the collection of assets, payment of debts, or the distribution of property to the persons entitled to it;

(2) Are executors' commissions properly calculated in accordance with local law, the governing instrument, or otherwise?

(3) Is it better to claim attorneys' fees and accountants' fees on the estate's income tax return (*i.e.*, in which top marginal bracket will your beneficiaries be)?

(4) Were the expenses actually paid and reported on the executor's personal income tax return?

(5) Should you file a protective claim for refund in the event additional attorneys' fees or incurred in connection with the audit of the return?

n. Schedule K - Debts of the Decedent

(1) Were the debts actually paid?

(2) Do you have proof of the indebtedness?

o. Schedule M - Marital Deduction

(1) Were disclaimers filed? If so, attach a copy of the disclaimer to the estate tax return?

(2) Have you reduced the deductions on Schedule J, K, and L for any marital deduction claimed with respect to the asset?

p. Schedule O - Charitable, Public, and Similar Gifts and Bequests

(1) Have you complied with the substantiation requirements for charitable gifts and bequests?

q. Schedules R and R-1 - Generation Skipping Transfer Tax Return

(1) Have generation-skipping transfers been made at death or during life? Has the GST applicable exclusion amount been allocated correctly?

r. Portability

(1) Was portability properly elected by filing a Form 706 for the predeceased spouse?

(2) Have you examined the predeceased spouse's return for potential adjustments to the deceased spouse unused exclusion amount that would carry forward to the decedent's estate tax return?

E. Gift Tax Return Preparation: Prepare With the Audit in Sight

1. Overview: Like the planning process, gift tax returns should be prepared with the audit in sight.

2. Be Sure to Perfect the Return: A gift tax return, signed under penalties of perjury, certifies that the return is "true, correct, and complete." This means, in addition to making reasoned judgment calls as to how to present a return for examination, that the gift tax

return includes all required information and attachments. A common reason for audit is the gift tax return does not include all required information and attachments. Preparers often overlook (or ignore) the following items that should be included with the return:

a. If valuation discounts are claimed, a statement should be attached to the gift tax return that gives the basis for the claimed discounts and shows the amount of the discount(s) claimed;

b. To support the value of gifts, for stock of close corporations or inactive stock, "balance sheets, particularly the one nearest the date of the gift, and statements of net earnings or operating results and dividends paid for the 5 preceding years;"

c. For each life insurance policy transferred, attach a Form 712, *Life Insurance Statement*, for all life insurance policies listed on return (*i.e.*, on the life of the decedent);

d. If the gift was made by means of a trust, attach a certified or verified copy of the trust instrument to the return on which you report your first transfer to the trust. To report subsequent transfers to the trust, you may attach either a brief description of the terms of the trust or a copy of the trust instrument;

e. Attach copies of appraisals used to determine the value of real estate or other property, or, alternatively, a full explanation of how the value was determined; and

f. Attach necessary statements for all elections being made with respect to the gift (*e.g.*, allocations of the generation skipping transfer tax exemption).

V. The Estate and Gift Tax Audit

A. Overview

1. Returns Subject to Classification Will Be Examined: All estate tax returns are processed in Kansas City, Missouri. Unlike other returns, which are subject to a "lottery," all estate tax returns subject to "classification" are reviewed to determine audit potential and identify the key issues for examination. The returns subject to classification are:

a. Returns reporting a gross estate of $10 million or more minus exclusions, plus adjusted taxable gifts (I.R.M., pt. 2.3.11.106.2(5) (Jan. 8, 2021));

b. Returns that use special-use valuation, elect to pay in installments, or elect to postpone the part of the taxes due to a reversionary or remainder interest (I.R.M., pt. 2.3.11.106.2(4)(a) (Jan. 8, 2021)); and

c. Returns that show zero adjustable taxable gifts but also attach Form 709, *United States Gift (and Generation - Skipping Transfer) Tax Return* (I.R.M., pt. 2.3.11.106.2(4)(b) (Jan. 8, 2021)).

2. During classification, classifiers (as compared with examiners) are required to review all schedules on returns to identify any significant issues. I.R.M., pt. 4.25.3.4.1 (Jul. 23, 2018).

a. The Normal Scope of an Examination: As a general rule, all significant issues are to be identified during classification and detailed on a classification sheet. Normally, all issues addressed on the classification sheet should be addressed during the examination and documented in the examiner's workpapers. I.R.M., pt. 4.25.3.4 (Jul. 7, 2020).

b. Exceptions to the Normal Scope of an Examination: The exceptions to the normal scope of an examination are as follows:

(1) Limited Scope Examinations (*i.e.*, those where only one or two issues are selected for examination, typically conducive to a correspondence examination),

(2) Project Cases (*i.e.*, areas where the Service has identified a potential for abuse and a heightened interest), and

(3) Cases with documented managerial direction. *See* I.R.M., pts. 4.25.1.4, 4.25.1.4.1, 4.25.1.4.2 (Jul. 7, 2020).

c. Assignment of the Estate Tax Return and the Auditor: Depending upon the audit issue(s) classified, each case will be given a grade of complexity. Returns with more complex issues will be assigned to a more senior estate and gift tax examiner (usually an attorney); returns with less complex issues will be assigned to a less senior estate and gift tax examiner (sometimes an attorney).

3. Timing of Classification and Examination: Estate tax return audits are usually initiated within nine months after filing. Absent special circumstances (*e.g.*, someone filing a reward application two years after the estate tax return is filed), estate tax return audits are usually concluded no later than 18 months after filing. See I.R.M., pt. 4.25.1.7.1 (Jul. 7, 2020).

4. Using Transcripts to Understand the Events Following Classification:

a. In General: As a general proposition, the following events can happen post-classification: (a) the case is not selected for field consideration (*i.e.*, the return will be accepted as filed); or (b) the case is selected for field consideration (*i.e.*, the return is being audited).

b. Cases Not Selected for Field Consideration: After it has been determined that a return will be accepted as filed, the examiner will prepare a Form 5344, *Examination Closing Record*, and close the Audit Information Management System (AIMS) using disposal code 20 (Accepted as Filed or disposal code 35 (Surveyed Excess Inventory, applied when a return has audit potential but time prohibits starting the examination). I.R.M., pt. 4.25.10.2.5 (Jul. 30, 2019); IRS Document 6036. Letter 637, the Estate Tax Closing Letter is available on request for a fee. I.R.M., pt. 1.35.19.16.3 (Jun. 18, 2021); TD 9957.

c. Cases Selected for Field Consideration: For selected estate tax returns, the examiner will send the return to a field office for review, completing necessary forms along the way (*e.g.*, Form 3210, *Document Transmittal*). See I.R.M., pt. 4.25.3.10.3 (Jul. 23, 2018).

5. Statute of Limitations Applicable to Estate Tax Returns:

a. General Rule: When a taxpayer files a return, the Service is legally empowered to assess the reported tax. I.R.C. § 6201. As a general rule, the Service must assess the estate tax within three years from the later of (1) the due date of the return, or (2) three years of the date the return is filed. See I.R.C. § 6501(a).

(1) Common Exception # 1: False or Fraudulent Return: When a false or fraudulent return has been filed with the intent to evade tax, the tax may be assessed at any time. See I.R.C. § 6501(c).

(2) Common Exception #2: Omitted Income: The Code allows for an extended six-year statute of limitations on assessment where omitted items includible in a gross estate exceed 25% of the total gross estate reported on the estate tax return IRC 6501(e)(2).

(3) Recent Exception #3: Failure to Disclose Offshore Assets: I.R.C. § 6501(c)(8) provides for an extended statute of limitations for failure to notify the IRS of certain foreign assets. The failure to file two such forms discussed at the end of this outline may, in limited circumstances, extend the statute of limitations. The two forms are: (1) Form 3520, *Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts*; and (2) Form 3520-A, *Annual Information of Foreign Trusts With a U.S. Owner*.

b. Period of Limitations for Assessment of Estate Tax May Not Be Extended by Agreement: Although the Service and the taxpayer can agree to extend the statute of limitations, the statute of limitations on assessment of the estate tax cannot be extended. See I.R.C. § 6501(c)(4). This means that a deficiency must either be assessed or a statutory notice of deficiency mailed to the taxpayer, prior to the expiration of the statute of limitations.

c. DSUE Not Subject to Statute of Limitations on the First to Die: Review of the DSUE is not subject to the statute of limitations on the first to die, which means that the Service can examine a predeceased spouse's DSUE on audit of the surviving spouse's death. See I.R.C. § 2010(c)(5)(B).

d. Calculating the Statute of Limitations: The following chart may be helpful to calculate the period of limitations for assessment for estate and gift taxes:

Returns Without Filing Extensions	Statute Runs From:
Return mailed and received on or before due date	Due date of return
Return mailed and received after due date	Date return received
Return mailed on or before due date but received after due date	Due date of return
Returns With Filing Extensions:	**Statute Runs From:**
Return mailed and received on or before extension date	Date return received
Return mailed and received after extension date	Date return received
Return mailed on or before extension date but received after extension date	Postmark date of return

6. Characters in the Cast: The typical case of character in an estate tax audit include the following:

   a. *Personal Representative, Executor, or Administrator:* The personal representative, executor, or administrator is a court-appointed fiduciary of the estate charged with, among other fiduciary responsibilities, filing an estate tax return and representing the estate during the audit and any ensuing litigation;

   b. *Estate and Gift Tax Examiner:* The estate and gift tax examiner is an Internal Revenue Service ("Service") employee who is charged with auditing the estate tax return for compliance with the Federal estate and gift tax laws;

   c. *Appeals*: The Service's Office of Appeals ("Appeals") is an independent organization within the Service whose mission is to help taxpayers and the Service resolve tax disagreements without litigation;

d. *CI*: The Service's Criminal Investigation Division ("CI") is the law enforcement division of the Service;

e. *TAS*: The Taxpayer Advocate Service, which is an independent organization within the Service whose mission is to ensure that all taxpayers are treated fairly and that the taxpayers' rights are understood and respected; and

f. *Chief Counsel* and *Division Counsel*: The Service's Chief Counsel (based in Washington, D.C.) and its Division Counsel (based locally) are the Commissioner's attorneys who litigate cases and advise with respect to, among other things, estate tax audits.

7. The 80/20 Rule: Examination activity should be commensurate with the time charged to the case. I.R.M., pt. 4.25.1.7.3 (Jan. 9, 2014). Estate and gift tax examiners adhere to the mantra that 80% of the tax determined to be due will come from 20% of the issues identified for audit. I.R.M., pt. 4.10.3.2.1 (Feb. 26, 2016). Thus, estate tax return audits tend to be highly focused.

8. Key Revenue Raiser: Transfer taxes generated only a small percentage of the total Federal tax collected. However, anecdotally estate and gift tax auditors return for the tax authorities more tax dollars per capita than any other subdivision of tax. Therefore, the Service emphasizes audits in this area.

9. Auditors are Specially Trained: Examining agents in estate and gift tax audits are specially trained in estate and gift tax.

B. The Service's Process and Appropriate Countermeasures

1. Understand How the Service Will Examine the Return and Take Appropriate Countermeasures: The Service is methodical in its approach to examining estate tax returns. This means that we can generally know what to expect, and in turn, can take counteractive steps to ensure that you know everything the Service knows (and more). We first begin with an overview of the process and then offer practical tips for handling the audit.

a. The Estate Tax Audit, as Compared With Other Audits: As a general rule, auditors are required to make contact with the personal representative of an estate within 45 days of the file being assigned to them. I.R.M. 4.25.1.7.1 (Jul. 7, 2020). Because the statute of limitations cannot be extended, auditors are mindful of the need to work their cases quickly and efficiently. Thus, practitioners can generally expect an estate tax audit to be quicker in pace than other audits.

2. Step 1: The Examiner Will Obtain and Review IDRS Transcripts and Prints: The Service's Integrated Data Retrieval System ("IDRS") is designed to provide examiners with the most current information on tax accounts. The examiner will request a copy of the IDRS transcript, which includes information on the Master File (another IRS system), to ensure that items are internally coded correctly. I.R.M., pt. 4.25.1.2 (Jul. 7, 2020).

    a. Countermeasure: As noted above, you should have already requested copies of the Service account transcripts, including (i) wage and income, (ii) account, (3) gift, and (4) related entity transcripts. Once you know the estate tax return has been selected for examination, request these transcripts again.

3. Step 2: The Examiner Will Verify the Date on Which the Statute of Limitations Expires: Soon after a case is assigned, an examiner is required to verify the statute of limitations by comparing the original tax return received date and postmark date with the statute date reflected on the Master File. I.RM., pt. 4.25.1.2.1 (Jul. 7, 2020). The statute of limitations is calculated in accordance with I.R.C. § 6501.

    a. Countermeasure: As noted above, you have the tools to calculate the statute of limitations, and should do so. While estate tax auditors should fiercely protect the statute of limitations, this does not mean they do not miscalculate the assessment date. Be aware of when the statute of limitations expires, but do not volunteer your calculation.

4. Step 3: The Examiner Will Verify Assessments and Payments: Soon after a case is assigned, the examiner will also verify any assessments and payments made to the account by comparing the original tax return with a transcript of the tax account. I.R.M., pt. 4.25.1.2.2 (Jul. 7, 2020).

    a. Countermeasure: Service account transcripts previously requested will allow you to similarly determine the accuracy of related assessments and payments.

5. Step 4: Identify and Request Related Returns Necessary for Examination: The examiner should make a preliminary determination as to whether other returns are required to be examined (*e.g.*, a predeceased spouse's estate tax return, prior years' gift tax returns, a related entity's returns, individual income tax returns, estate or trust income tax returns). See generally I.R.M., pt. 4.25.1.3 (Jul. 7, 2020). These issues may be identified during the classification stage. As a general rule, estate tax

examiners will request copies of a predeceased spouse's estate tax return and copies of all gift tax returns previously filed by the decedent. Id.

a. Countermeasure: As part of your preparation of the estate tax return, you should have already requested copies of the predeceased spouse's estate tax return, prior years' gift tax returns, and relevant income tax returns. You should have already evaluated whether all assets reported on the predeceased spouse's return have been property reported, or their disposition accounted for, in preparing the estate tax return under audit.

6. Step 5: Complete a Case Activity Record for All Action Taken With Respect to a Case: The Form 9984, *Examining Officer's Activity Record*, is used to document the hours charged to a case and to briefly record the examiner's action.

   a. Countermeasure: Request the Case Activity Record (*i.e.*, the Form 9984) as part of your FOIA request to understand all actions the examiner is taking with respect to the estate tax return.

7. Step 6: Review Necessary Lead Sheets and Issue Spot: The Estate and Gift Examination function has developed comprehensive lead sheets that are intended to allow auditors to identify issues that may result in a deficiency. As summarized in I.R.M., pt. 4.25.1.9 (Jul. 7, 2020), among the lead sheets commonly reviewed (and completed) are the following:

   a. Estate Tax Mandatory Lead Sheet (to develop pre-audit plan, perform risk analysis, and address administrative items);

   b. Statute Verification Lead Sheet (to verify the correct statute of limitations date);

   c. Activity Record (to document the hours charged to a case and to briefly record the examiner's action);

   d. Penalty Approval Form (to determine whether an assessment of penalties is warranted in all cases with an increase in tax);[3]

[3] To the extent the penalty approval form does not comport with the requirements of I.R.C. § 6751(b)(1), which generally requires that the initial determination that the penalty applies be approved in writing by the person making such determination, the taxpayer may argue that the

e. Reasonable Cause Lead Sheet (to document a taxpayer or preparer's reasonable cause defense to the assessment of penalties);

f. Fraud Lead Sheet (to assist the examiner in determining whether the assessment of fraud penalties is warranted);

g. Plan to Close Lead Sheet (to develop a schedule and plan to close the audit); and

h. Issue Specific Lead Sheets (to help identify individual items on an estate tax return) (*see* I.R.M., pt. 4.25.5.2 (Jul. 28, 2020) include:

(1) Adjusted Taxable Gifts Lead Sheet (to document an examination of omitted gifts or gifts reported on a Form 709 or a Form 706)

(2) Schedule A - Real Estate Lead Sheet (to provide the examiner with a list of considerations when verifying ownership and valuation of real estate in a gross estate);

(3) Schedule A-1 - Section 2032A Valuation Lead Sheet (to document the examination of a Schedule A-1, 2032A, Special Use Valuation);

(4) Schedule B - Stocks and Bonds Lead Sheet (to focus on the value of traded securities and various bonds, including Series EE, HH and I bonds);

(5) Schedule C - Mortgage, Notes, and Cash Lead Sheet (to focus on verification of the outstanding balance of a mortgage or promissory note on the decedent's date of death);

(6) Closely Held Business Lead Sheet (to verify the fair market value of decedent's interest in a closely held business);

(7) Schedule D - Life Insurance Lead Sheet (provides guidance on verifying life insurance policies a decedent held an interest in on date of death);

(8) Schedule E - Jointly Owned Property Lead Sheet (to document the examiner's analysis and determinations regarding the completeness,

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penalty may not be assessed. See, e.g., Graev v. Commissioner, 149 T.C. 485 (2017) (following Chai v. Commissioner, 851 F.3d 190 (2d Cir. 2017)).

valuation, and accuracy of the estate's reporting of qualified joint interests and all other joint interests);

(9) Schedule F - Misc. Property Lead Sheet (to provide audit steps and reminders for verifying the fair market value of miscellaneous property not reportable under any other schedule);

(10) Family Limited Liability Entities (to provide guidance on issues arising during the examination of family limited liability entity assets and transfers;

(11) Schedule G - Transfers During Decedent's Life Lead Sheet (provides guidance on verifying the value of assets transferred during the decedent's life);

(12) Schedule H - Powers of Appointment Lead Sheet (to document their inspection of the Form 706 and related testamentary instruments to determine the extent and value of any includible powers of appointment held or exercised by the decedent);

(13) Schedule I - Annuities Lead Sheet (to document whether the decedent owned an annuity or a retirement benefit (*e.g.*, IRA, 401(k), etc.) payable to a beneficiary at the decedent's death, and the valuation of the annuity);

(14) Schedule J - Expenses Incurred During Administration Lead Sheet (to verify funeral expenses and miscellaneous expenses included in the administration or property subject to claims);

(15) Schedule J – Executor's Commission and Attorney Fees (to document examination steps and analysis of Schedule J and Schedule L personal representative commission and attorney fees deductions);

(16) Schedule J - Attorneys' Fees Lead Sheet (to verify the amount of estimated or large, unusual and/or questionable fees paid to an attorney or professional representative

(17) Schedule K - Debts of the Decedent Lead Sheet (to verify the amount of identified debts of the decedent);

(18) Schedule K - Mortgages and Liens Lead Sheet (to verify where there are classified, large, unusual or questionable deductions claimed that require the verification of claimed mortgages and liens);

(19) Schedule L - Net Losses During Administration Lead Sheet (to verify losses incurred due to casualty or theft);

(20) Schedule L - Property Not Subject to Claims Lead Sheet (to verify expenses claimed for the administration of trust assets);

(21) Schedule M - Marital Deduction Lead Sheet, Non-QTIP (to examine the validity of marital deductions claimed for outright bequests of property to the surviving spouse not subject to the qualified terminal interest property rules);

(22) Schedule M - QTIP Bequests to Surviving Spouse (to examine qualified terminal interest property transfers to the surviving spouse);

(23) Schedule O - Charitable, Public, and Similar Gifts and Bequests (to verify whether a charitable deduction represents a transfer to a qualified beneficiary, *i.e.*, charitable, public, or religious purpose);

(24) Portability (to determine if the deceased spousal unused exclusion amount was property elected, calculated, and carried forward to the decedent's estate tax return).

i. Countermeasure: In connection with the preparation of the estate tax return, you should have a good idea of where, if at all, the estate tax return is weak. If you did not prepare the estate tax return, critically analyze it to determine all issues that the auditor might look into. DO NOT, HOWEVER, VOLUNTEER ISSUES.

8. Step 5: The Examiner Will Make Contact With the Taxpayer: After the examiner has critically reviewed the estate tax return, the auditor will make contact with the taxpayer or the taxpayer's representative. Most often, assuming the practitioner is listed on Part 4 of page 2 of the estate tax return, the auditor will contact the representative by telephone to advise them of the audit. Other times, the examiner will contact the taxpayer or the taxpayer's

representative by mail correspondence in the form of an information document request ("IDR").

a. Countermeasure: As discussed more fully below, once the audit commences, request Service account transcripts, perform another FOIA request, run another credit check, check all adverse judgments, perform an Accurint search, run a TLO search, and run a Google search. Also as discussed below, perform an inquiry of third-party contacts the Service has made.

9. Step 6: The Examiner Will Review Information Provided and May Determine Adjustments to the Return: After the exchange and review of information, as well as discussions as to the propriety of those adjustments, the examiner may determine adjustments to an estate tax return or gift tax return. The examiner summarizes their determination in an estate tax audit on Form 1273, *Report of Estate Tax Examination Changes*. I.R.M., pt. 4.25.6.4 (Dec. 7, 2021). The examiner summarizes their determination in a gift tax audit on Form 3233, *Report of Gift Tax Examination*. Id. The Form 1273 shows the recommended net deficiency or over-assessment of estate tax. Id. The Form 1273 has two columns: "Tax Previously Assessed/Shown on Return" and "As Corrected Tax." Additionally, the following will likely be included with the Form 3233 or Form 1273:

a. Form 6180, *Adjustment to Taxable Estate*: Used to summarize the net changes on each schedule of the Form 706.

b. Form 886-A, *Explanation of Items*: Used in estate or gift tax reports to explain each adjustment shown on the columns entitled, "Tax Previously Assessed/Shown on Return" or "As Corrected Tax."

c. Copies of Appraisals and Reports: When an engineer, economist, or other expert report is prepared and the findings accepted by the examiner, a copy designated as the "Taxpayer's Copy" should be attached as an exhibit to the Form 1273 or Form 3233. Id. If the examiner previously submitted the report to the taxpayer, an additional copy of the appraisal does not need to be attached to the report. Id.

10. Step 7: Determine Whether the Representative Agrees or Disagrees With the Proposed Adjustments: Discussions about the propriety of the adjustments will reach a breaking point. At that point, examiners are counseled to solicit payment from the taxpayer and end the audit. The circumstances that follow, in turn, depend upon

whether the taxpayer agrees or disagrees with the proposed adjustments.

a. Fully Agreed Cases: If there is a change in the tax assessment and the case is agreed, the examiner will:

(1) Prepare a draft Form 1273, Form 6180 and Form 886-A in the case of an estate tax examination. I.R.M., pt. 4.25.10.6 (Jul. 31, 2020). The examiner will prepare a draft Form 1273 and Form 886-A in the case of a gift tax examination. Id. In either event, the reports will explain all changes made during the course of the examination. Id.

(2) Prepare and secure Form 890, *Waiver of Restrictions on Assessment and Collection of Deficiency and Acceptance of Overassessment*, which is used to document that the taxpayer agrees to the proposed adjustments and is waiving the statutory restrictions upon assessment and collection of the deficiency in tax. Id. The execution of this form permits the Service to assess the deficiency, schedule the over-assessment, or adjust the applicable credit amount immediately. Id. It also stops the running of interest from the 31st day after the date of receipt until notice and demand for payment is made. Form 890 does not constitute a final closing agreement. Id.

(3) Solicit payment for all agreed deficiencies with an interest computation through a specified date on which the deficiency is agreed to be paid. Id.

(4) Close the case with all due expedience. Id.

b. Partially Agreed Cases: If the taxpayer does not agree to all of the proposed adjustments, but agrees to some of the proposed adjustments, the case is partially agreed. In partially agreed cases, the examiner will:

(1) Prepare two reports; the first of which is intended to show which adjustments are agreed and which adjustments are not agreed;

(2) The first report, Form 1273 (for estate tax cases) or Form 3233 (for gift tax cases), will address the agreed adjustments. In general, the figures returned by the taxpayer will be reflected in the "Shown on Return" column. The agreed changes will be

reflected in the "As Corrected" column. A Form 6180, Forms 886-A and Form 890 should also be included; and

(3) The second report, Form 1273 (for estate tax cases) or Form 3233 (for gift tax cases), will address the unagreed adjustments. The unagreed changes will be reflected in the "As Corrected" column. A Form 6180, Forms 886-A and Form 890 should also be included. The unagreed portion of the case will then be processed as discussed immediately below. See I.R.M., pt. 4.25.10.8 (Jul. 30, 2019).

c. Unagreed Cases: In estate, gift, and generation skipping transfer tax examinations, if the taxpayer does not agree to the proposed adjustments, the case is unagreed. I.R.M., pt. 4.25.10.7 (Jul. 31, 2020) In such cases, the examiner will:

(1) Solicit a statement of the taxpayer's position on each unagreed issue and consider the taxpayer's position with appropriate documentation before concluding the examination. Id.

(2) Determine whether case is eligible and should use Fast Track Settlement procedures. Id.

(3) Confirm the date on which the statute of limitations expires. Id. If there are more than 210 days remaining on the statute of limitations on the date the taxpayer communicates disagreement with the proposed adjustments, a 30-day letter (or ticket to Appeals) may be issued. See I.R.M., pt. 4.25.10.7.3 (Jul. 30, 2019). The taxpayer should request that a 30-day letter, rather than a 90-day letter (or notice of deficiency) be issued to allow an opportunity to appeal to the Service prior to any appeal to Tax Court. If there are less than 210 days remaining on the statute of limitations on the date the taxpayer communicates disagreement with the proposed adjustments, then a 90-day letter (or notice of deficiency) letter is issued. I.R.M., pt. 4.25.10.7.4 (Jul. 30, 2019).

(4) The determinations of an unagreed case are set forth in Form 1273 (for estate tax cases) or Form 3233 (for gift tax cases). The unagreed changes will be reflected in the "As Corrected" column. A Form

6180 and Form 886-A should also be included. I.R.M., pt. 4.25.10.7.7 (Jul. 31, 2020).

d. Countermeasure: Be vigilant in protecting your client's right to exercise Appeals' rights in response to the 30-day letter or Tax Court deficiency rights in response to a 90-day letter. Note: If a taxpayer desires administrative review of an adjustment in excess of $25,000, then the taxpayer must submit a written formal protest to Appeals. See I.R.M., pt. 4.25.10.7.3.2 (Jul. 31, 2020). We advise that in this protest the taxpayer include (1) the factual basis for the disagreement, (2) the legal basis for the disagreement, and (3) a section reserving the right to amend or supplement the protest. These points are discussed more fully below.

11. Step 8: Close the File: After the Form 890 has been obtained or the 30-day letter issued, the examiner will proceed to close the file. The examiner is responsible for preparing the appropriate closure letter, but that letter is issued by the Service's Centralized Case Processing ("CCP"). In accordance with I.R.M., Exhibit 4.25.10-2, the Service may issue the following letters in connection with the closing of the examination:

Letter	Use and Preparation
Letter 590 (Straight No Change)	Letter 590 is used on examinations that resulted in no change to the reported tax liability. This letter notifies the taxpayer and/or representative that the examination report has been reviewed and accepted by the Chief, Estate and Gift Tax. Therefore, the examination proceeding is officially closed. The examiner will prepare the Letter 590, No-Change Final Letter, to be retained undated in the case file. The group manager will sign the letter. CCP will date, and mail the Letter 590 to the taxpayer and representative, if applicable.

Letter	Use and Preparation
Letter 1156 (Change/No Change estate)	Letter 1156 is used when an estate tax examination results in adjustments that do not change the taxpayer's liability in the year examined and do not impact any tax years for which returns were filed or other tax years for which returns are not yet due. Letter 1156 is also used when an examination results in no change in the tax liability, but changes to items impacting other tax periods. This final no-change letter notifies the taxpayer and/or representative that the report has been reviewed and accepted by the Chief, Estate and Gift Tax. Therefore, the examination proceeding is officially closed. The examiner will prepare the Letter 1156, Change/No Change Final Letter, to be retained undated in the case file. The group manager will sign the letter. CCP will date and mail the Letter 1156 to the taxpayer and/or representative, if applicable.
Letter 570 (Claim allowed in full)	Letter 570 (DO), Claim Allowed in Full, is used on examinations for claims allowed in full. This letter notifies the taxpayer and/or representative of the final findings of the claim examination. Therefore, the examination proceeding is officially closed. The examiner will prepare the Letter 570 (DO). The examiner will mark the box on Form 3198, "Fully Allowed - L570" for closing instructions to CCP. CCP will date, obtain the necessary signature, and mail the Letter 570 (DO) to the taxpayer and representative, if applicable.
Letter 950-G (Change/No-Change Gifts)	Letter, 950-G, Preliminary Determination Letter showing proposed changes to the value of gifts that does not generate a gift tax for certain periods. This letter will also explain the taxpayer's appeal rights under I.R.C. § 7477. Field examiners within the Estate and Gift Tax Program will use this letter.
Letter 950-F (Change/No-Change)	This letter is sent on unagreed examination cases for Change/No Change cases where the taxpayer wants to go to Appeals. The examiner should include Form 13683, Statement of Disputed Issues, with the mailing of the Letter 950-F. The examiner will prepare the Letter 950-F, Appeals Request for Change/No Change Cases. This case will be processed in the same manner as normal unagreed case and the case will be routed for Appeals consideration if a timely response is received and the statute of limitations permits.

C. Practice Tip 1: Manage Client Expectations

1. Clearly Explain the Potential Range of Outcomes in the Audit: Practitioners should be straightforward and honest with the client regarding the audit and its potential range of outcomes.

2. Clearly Define the Scope of Representation: Practitioners should use the engagement letter to clearly define the scope of representation.

3. Protect Yourself: Practitioners should protect themselves by taking the following steps:

   a. Plan for the possibility that the client may attempt to blame the tax professional to escape penalties, especially in fraud cases;

   b. Recognize when it may be prudent to bring in outside counsel or refer the case to another; and

   c. Maintain complete files, workpapers, and correspondence.

D. Practice Tip 2: Protect the Personal Representative From Personal Liability

1. In General: As discussed above, the personal representative faces potential exposure for certain of the estate's tax liability. In addition to indemnity contracts, which are discussed below and may be appropriate for certain personal representatives, a personal representative should file the following three forms, each of which is discussed more fully below, to protect the personal representative from exposure to tax liability:

   a. Form 56, *Notice Concerning Fiduciary Liability*;

   b. Form 4810, *Request for Prompt Assessment Under Internal Revenue Code Section 6501(d)*; and

   c. *Form 5495, Request for Discharge From Personal Liability Under Internal Revenue Code Section 2204 or 6905*.

2. Form 56, Notice Concerning Fiduciary Relationship:

   a. When to File: File Form 56 two times: first, when the personal representative is appointed to let the Service know who the personal representative is and where to send all tax notices; and second, when the personal representative completes their job and dies, resigns, or is discharged.

   b. Relevant Regulatory Requirement to File Up-Front: Treas. Reg. § 301.6903-1(a) provides as follows:

      (1) Every person acting for another person in a fiduciary capacity shall give notice thereof to the

district director in writing. As soon as such notice is filed with the district director such fiduciary must, except as otherwise specifically provided, assume the powers, rights, duties, and privileges of the taxpayer with respect to the taxes imposed by the Code. If the person is acting as a fiduciary for a transferee or other person subject to the liability specified in I.R.C. § 6901, such fiduciary is required to assume the powers, rights, duties, and privileges of the transferee or other person under that section. The amount of the tax or liability is ordinarily not collectible from the personal estate of the fiduciary but is collectible from the estate of the taxpayer or from the estate of the transferee or other person subject to the liability specified in I.R.C. § 6901.

c. Forward Mail: Have the decedent's mail forwarded to the personal representative or attorney to ensure that all proper financial and tax mailings are obtained.

d. Ensure Liquidity for the Estate: Promptly estimate the amount of cash required to discharge all liabilities and take early steps to ensure sufficient liquidity to prevent the assessment of penalties and interest.

e. Be Sure to File Following Discharge: If the personal representative dies, resigns, or is discharged from the fiduciary duty, file a second Form 56. In Estate of Hull v. Commissioner, T.C. Memo. 1990579, where a wife filed Form 56 with the Service, administered the estate, but did not file a second Form 56 providing notice that the fiduciary relationship had terminated, the Tax Court held that a notice of deficiency was validly issued.

3. Form 4810, Request for Prompt Assessment Under Internal Revenue Code Section 6501(d):

a. Determine Tax Exposure Through Form 4810: Determine whether the Decedent owed any back taxes by filing with the Service a Form 4810, through which a request is made for prompt assessment of income and gift taxes.

b. Relevant Statutory Provision: Normally, the period for limitations on assessment is three years. I.R.C. § 6501(a). The period of limitations on assessment may be extended by written agreement. I.R.C. § 6501(c)(4). Under I.R.C. § 6501(d), the personal representative of an estate may make a request for prompt assessment that will shorten the period

of limitations on assessment to 18 months from the date of the written request therefor. For an estate, the prompt assessment procedures apply to any tax (other than estate tax) for which a return is required and for which the decedent or the estate may be liable. As an aside, this provision also applies to a liquidating corporation.

c. Limit Distributions: A cautious personal representative will wait for the Service to respond to their assessment request prior to making any distributions to the beneficiaries of the estate. The benefit of filing the Form 4810 is that a personal representative can distribute assets to the estate's beneficiaries more quickly while limiting the representative's risk.

d. Cases and Administrative Guidance Involving Attempts to Reduce a Personal Representative's Exposure to Personal Liability:

(1) The Request for Prompt Assessment Does Not Extend the Three-Year Period of Limitations on Assessment in the Second Circuit: In Estate of Callaway v. Commissioner, 231 F.3d 106 (2d Cir. 2000), the Court of Appeals for the Second Circuit held that the 18-month period for making a prompt assessment does not extend the period of limitations on assessment beyond the normal three-year period. Under the facts of the case, taxpayers, husband (H) and wife (W), timely filed their income tax return for 1988 on April 15, 1988. In 1990, H died. On Dec. 23, 1991, W, acting as personal representative of H's estate, filed a prompt assessment request with respect to taxpayers' 1988 return. The Court held that the time for making an assessment expired on April 15, 1992, three years after the filing of the 1988 return, not on June 23, 1993, 18 months after the filing of the prompt assessment request. This was because, the Court held, the 18-month period for assessment (here ending on June 23, 1993) does not extend the period for making the assessment beyond the date three years after the filing of the return (here, April 15, 1992).

(2) The Request for Prompt Assessment Does Not Limit a Statute Extension: In Greenfield v. Commissioner, T.C. Memo. 2008-16, the Tax Court

held that a request for prompt assessment does not limit an agreement to extent the statute of limitations entered into by the taxpayer.

(3) Transferee Liability is Not Affected by a Request for Prompt Assessment: In Gen. Couns. Mem. 32904 (Aug. 27, 1964), the Service addressed whether transferee liability statutes are affected by a request for prompt assessment. The Service held that I.R.C. §§ 6501(d) and 6901(e), when read together, reveal that for purposes of computing the period of limitations on assessment against a transferee, the period of assessment against a deceased person, or dissolved corporation as a transferor, regardless of the fact that a request for prompt assessment has been made, is the period that would be in effect had death or termination not occurred (*i.e.*, the normal 3-year period from the date the return was filed rather than the 18-month period prescribed in I.R.C. § 6501(d)).

4. Form 5495, Request for Discharge From Personal Liability Under Internal Revenue Code Section 2204 or 6905:

a. General Rule for Liability:

(1) Regulatory Liability: Treas. Reg. § 20.2002-1 provides that a personal representative is generally personally liable for the tax debts of a decedent or estate. That section provides as follows:

(a) Every executor, administrator, or assignee, or other person, who pays, in whole or in part, any debt due by the person or estate for whom or for which he acts before he satisfies and pays the debts due to the United States from such person or estate, shall become answerable in his own person and estate to the extent of such payments for the debts so due to the United States, or for so much thereof as may remain due and unpaid.

(2) Liability Imposed: In Estate of Sivyer v. Commissioner, 64 T.C. 581 (1975), the Court held a personal representative fully liable for a deficiency to the extent of the remaining estate assets in the personal representative's control or in the control of the transferees.

b. Overview of Mechanisms to Discharge a Personal Representative From Liability: There are various provisions by which a personal representative can limit personal liability. Generally, the personal representative invokes the benefits of these statutory provisions by filing with the Service Form 5495. As suggested by the name of the form, *Request for Discharge From Personal Liability Under Internal Revenue Code Section 2204 or 6905*, the types of requests that can be made (and the statutory predicates) are as follows:

(1) Discharge From Personal Liability for Estate Tax: I.R.C. § 2204 provides that a fiduciary other than a personal representative (*e.g.*, a trustee of a revocable trust) may apply for discharge of personal liability for estate tax.

(2) Discharge From Personal Liability for Income and Gift Taxes: I.R.C. § 6905(a) provides, that after a decedent's individual (but not fiduciary) income or gift tax return has been filed, a personal representative may make written application to the Service office where the estate tax return is filed for release of the PR's personal liability for such income or gift tax.

c. Effect of Filing Form 5495: If, in response to the filing of a Form 5495, the personal representative pays the additional tax or if no notice is received from the Service within nine months from the date of filing Form 5495, then the personal representative is discharged from personal liability.

d. When to File: Practitioners or personal representatives should file Form 5495 separately but at the same time as the Form 4810.

e. Relevant Statutory and Regulatory Provisions:

(1) General Rule for Relief From Liability: I.R.C. § 2204(a) provides as follows:

(a) If the executor makes written application to the Secretary for determination of the amount of the tax and discharge from personal liability thereof, the Secretary (as soon as possible, and in any event within 9 months after the making of such application,

or, if the application is made before the return is filed, then within 9 months after the return is filed, but not after the expiration of the period prescribed for the assessment of the tax in I.R.C. § 6501) shall notify the executor of the amount of the tax. The executor, on payment of the amount of which he is notified (other than any amount the time for payment of which is extended under I.R.C. §§ 6161, 6163, or 6166), and on furnishing any bond which may be required for any amount for which the time for payment is extended, shall be discharged from personal liability for any deficiency in tax thereafter found to be due and shall be entitled to a receipt or writing showing such discharge.

(2) Good Faith Reliance on Gift Tax Returns: I.R.C. § 2204(d) provides as follows:

(a) If the executor in good faith relies on gift tax returns furnished under section 6103 (e)(3) for determining the decedent's adjusted taxable gifts, the executor shall be discharged from personal liability with respect to any deficiency of the tax imposed by this chapter which is attributable to adjusted taxable gifts which–

i) are made more than 3 years before the date of the decedent's death, and

ii) are not shown on such returns.

f. Time for Service to Respond: If Form 5495 is properly filed, the Service has nine months to notify the personal representative of any deficiency for decedent's applicable income or gift tax returns.

5. Indemnity Agreements and Refunding Bonds and Releases: Additionally, the personal representative can enter into contractual agreements with distributees in which the distributees agree to (1) indemnify the personal representative from any personal liability arising from the distribution, and/or (2) refund such amounts distributed as are necessary to satisfy the estate's debts, including

tax debts, and release the personal representative from personal liability for such distribution.

a. Indemnity Agreements: The personal representative can enter into contractual agreements with distributees in which the distributees agree to indemnify the personal representative from any personal liability arising from the distribution.

b. Refunding Bond and Releases: The personal representative (or any other fiduciary, such as a trustee) can condition a distribution upon the distributee signing a refunding bond and release, which is a contractual arrangement through which the distributee agrees to refund such amounts distributed as are necessary to satisfy the estate's debts, including tax debts, and release the personal representative from personal liability for such distribution

E. Practice Tip 3: Know What the Government Knows (and More)

1. Know What the Government Knows When the Audit Commences: Once the audit commences, request Service account transcripts, perform another FOIA request, run another credit check, check all adverse judgments, perform an Accurint search, run a TLO search, and run a Google search.

2. Additionally, Request a Third-Party Contact Sheet From the Service: As an added step, once the audit commences, periodically request from the Service a third-party contact sheet. Pursuant to IRC §7602(c)(2), the Service is required to provide a taxpayer with a list of third-party contacts periodically and also when requested by the taxpayer. See I.R.M., pt. 4.11.57.4 (Oct. 5, 2022).

3. Learn as the Government Learns: Periodically during the course of the audit, and at least every six months, request Service account transcripts, perform another FOIA request, run another credit check, check all adverse judgments, perform an Accurint search, run a TLO search, run a Google search, and request a third-party contact sheet pursuant to I.R.C. § 7602(c).

4. Do Not Underestimate Your Adversary: Assume the agent has read the file, is familiar with the potential issues, and understands those issues.

F. Practice Tip 4: Make a Conscious Choice as to How to Approach the Audit

1. Consciously Decide How to Approach the Audit: Early-on, practitioners should decide how to approach the investigation and

continually check that approach during the course of the audit. Will you:

a. Passively cooperate and produce requested documents; or

b. Aggressively represent your client, asserting all privileges and requiring the estate and gift tax examiner to issue summonses?

2. Suggested Approach: Ideally, practitioners should strike a proper balance between the two approaches. In some cases, practitioners will be more passively cooperative and in others, practitioners will be extremely protective.

G. Practice Tip 5: Know What to Expect in the IDR

1. The Service's Statutory Right to Examine Items: Congress has given the Service broad powers to compel production of information it requires to determine the liability of any taxpayer. In this regard, I.R.C. § 7602 permits the Service to perform any of the following: (1) examine any books, papers, records, or data which *may be relevant or material*; (2) summon a taxpayer or any other person, requiring the person to appear, to produce books and records, and to give testimony under oath; and (3) take testimony under oath.

2. Introduction to the IDR: The examiner's initial request for information and documentation is made in an information document request ("IDR"). The examiner's IDR should be clear and concise and cover all issues that are apparent in the return. I.R.M., pt. 4.25.1.7.4.3 (Jul. 7, 2020). This is not to say that the audit will be confined to what is in the initial IDR, but it is a good starting point.

3. Respect Deadlines and Request Extensions Ahead of Time: Requests for information will normally include a response date, such as a specific date or reference to a specific time frame (*e.g.*, "by November 20, 2014" or "within three weeks from the date on this letter"). All practitioners should respect these deadlines to the greatest extent possible.

4. Request Extensions in Writing and State the Reasons Therefor: Any requested extension to an IDR should be in writing. This is important because, if the case proceeds to trial and the taxpayer wishes to have the burden of proof shifted to the Government (usually a favorable outcome for the taxpayer), the taxpayer must demonstrate cooperation with the Service's reasonable requests for witnesses, information, documents, meetings, and interviews.

5. Supplemental IDRs: Do not be surprised if the Service issues multiple IDRs. These supplemental IDRs will give the practitioner insight into the items the auditor is focusing on in the examination.

H. Practice Tip 6: Identify the Issues to be Examined

1. In General: Fully research and document every potential issue. Look at the estate tax return or gift tax return like an auditor would look at it.

2. Commonly Encountered Issues on Estate and Gift Tax Returns: The issues that the Service focuses on evolves over time. However, certain issues tend to be frequently examined by the Service. Among the issues most common to be examined are the following:

a. Adjusted taxable gifts

(1) Have all lifetime gifts been reported on Form 709 and line 4 of Form 706?

(2) Have you reported any gift tax the decedent paid with respect to lifetime gifts on line 7 of Form 706?

(3) If annual exclusions were claimed, did the donee receive a present interest in the transferred property?

b. Real Estate

(1) If the property was not sold, is the fair market value determined on the basis of a reliable appraiser with a copy of the appraisal attached to the return?

(2) If the property was sold in an arm's length transaction, is the sales price reflected?

c. Stocks and Bonds

(1) Did you properly account for accrued interests and dividends?

(2) Are all stocks and bonds reported; did you check the stocks and bonds reported against the dividends and interest reported on the decedent's Form 1040?

d. Closely Held Businesses

(1) Does the governing entity instrument contain requirements for determining the sales price of the closely held business interest? If so, did you adhere to those standards?

(2) Does the closely held business have an established practice for determining the fair market value of the closely held business interest if not disclosed in the agreements? If so, were you consistent in following that approach on the estate tax return?

(3) Is the value determines on the basis of a reliable appraisal? Review the entity's tax returns and financial statements to determine the fair market value of the shares.

(4) Have you reviewed for appropriate discounts (*e.g.*, lack of marketability, lack of control, built in gains, key person, etc.)? Is the discount reasonable in the light of the facts and existing case law?

(5) Was there a bargain sale of the company?

e. Mortgages, Notes, and Cash

(1) Were there self-canceling installment notes, forgiveness of indebtedness, installment sales, promissory notes that are not at arm's length, and below market loans?

f. Life Insurance

(1) To the extent the life insurance is excludible under a life insurance trust, have proper Crummey notices and powers been given?

g. Jointly Owned Property

(1) If you are reporting only a fraction of a property's fair market value because of joint ownership, do you have proof of contribution by another party (either by check or affidavit, if necessary)?

(2) If fractional interests are claimed, (1) is the fractional interest warranted (*i.e.*, was the property held as tenants in common), and (2) is the amount of the fractional interest reasonable in the light of existing case law?

h. Misc. Property

(1) Were there family limited partnerships, and if so, the following issues:

(a) Did the formation and funding of the partnership result in an indirect gift?

(2) Are portions of the interest includible under I.R.C. § 2036 (retained life estate), I.R.C. § 2037 (transfers taking effect at death), or I.R.C. § 2038 (revocable interests)?

(3) If discounts are claimed, were the discounts reasonable in the light of existing case law?

i. Transfers During Life

(1) Were there deathbed transfers that should be included under section 2035?

j. Powers of Appointment

(1) Did the decedent have a general power of appointment in a trust?

k. Annuities

(1) Did the estate report all annuities or retirement benefits (*e.g.*, IRA, 401(k), etc.) the decedent owned that are payable to a beneficiary at the decedent's death? Also, is the value of the annuity proper?

l. Expenses Incurred During the Administration of the Estate

(1) Are the expenses claimed as deductions necessarily and reasonably incurred by the estate for the collection of assets, payment of debts, or the distribution of property to the persons entitled to it;

(2) Are executors' commissions properly calculated in accordance with local law, the governing instrument, or otherwise?

(3) Were the expenses actually paid and reported on the executor's personal income tax return?

m. Marital Deduction

(1) Were disclaimers properly executed?

(2) Did the estate reduce the deductions on Schedule J, K, and L for any marital deduction claimed with respect to the asset?

n. Charitable, Public, and Similar Gifts and Bequests

(1) Has the decedent complied with substantiation requirements for charitable gifts and bequests?

o. Generation Skipping Transfer Tax Return

(1) Have generation-skipping transfers been made at death or during life? Has the GST applicable exclusion amount been allocated correctly?

p. Portability

(1) Was portability properly elected by filing a Form 706 for the predeceased spouse?

(2) Are there any issues on the predeceased spouse's return that might otherwise adjust the deceased spouse unused exclusion amount carrying forward to the decedent's estate tax return)?

I. Practice Tip 7: Prepare, Prepare, and Prepare: It is important to prepare early and often. Ensure adequate documentation for all items.

J. Practice Tip 8: Establishing an Audit Defense and Preliminary Issues to Consider When Representing a Taxpayer Before the Service

1. Handling the Initial Audit Interview: You will have to answer the following questions:

a. Although subsequent interviews may be conducted remotely, the IRS typically conducts initial audit interviews face to face. I.R.M., pt. 4.10.3.3(1) (Feb. 26, 2016). Where should the initial audit interview take place?

(1) The Options: At the taxpayer's home or business, at your business, or at the Service's office?

(2) Pros and Cons of Meeting at the Taxpayer's Home or Business: It is useful to have books and records available, and the location of those documents may drive the location of the audit interview.

(3) Pros and Cons of Meeting at the Service's Office: The Service's Office may be less convenient if there are many books and records that must be transported or which cannot be left with the Service. However, holding the interview at the Service's Office will generally insulate the client from the examining agent.

b. Should the taxpayer attend?

(1) The Options: Yes or no.

(2) When to Consider Bringing the Taxpayer to the Interview: Consider whether the taxpayer has a credible explanation or compelling story that may

prevent penalties from being imposed. If yes, then it may make sense to bring the client to a subsequent meeting, but rarely (if ever) the first meeting.

(3) When to Consider Leaving the Taxpayer at Home: Consider whether the taxpayer is agitated over the audit, whether the taxpayer has unsympathetic qualities, or whether the taxpayer would do more harm than good.

(4) When in Doubt: When in doubt, leave the client home. Once harm has been committed, it will be very difficult to overcome.

(5) Criminal Concerns: If there is any concern that the case could turn criminal, leave the taxpayer home. It is a good idea to also hire an attorney to represent the taxpayer, either in-person before the Service or behind the scenes. The counsel that an experienced criminal tax attorney can provide during the audit stage will be invaluable if the case turns criminal.

(6) Pros and Cons of Meeting at the Service's Office: The Service's Office may be less convenient if there are many books and records that must be transported or which cannot be left with the Service. However, holding the interview at the Service's Office will insulate the client from the examining agent.

c. Let the Agent Identify the Issues: Never volunteer issues. Let the examining agent identify the scope of the audit.

2. Handling Requests for Information or Documents - The Good and the Bad:

a. The Good: Turning information over to the Service can build trust and good faith.

b. The Bad: However, there may be times where the taxpayer or taxpayer's representative deems the documents to be irrelevant or privileged. In that case, the Service may obtain the documents by summons or subpoena.

c. Caution: Do not turn over irrelevant or privileged documents solely on the belief that they are harmless. Irrelevant documents may lead to new inquiries, and privileged documents may constitute a waiver of privilege.

d. Streamline the Audit: By responding directly to the questions posed and providing responsive documents, you will help to keep the audit narrow and streamlined.

e. The Service's Subpoena Power: The Service may issue summonses or subpoenas for the purpose of "ascertaining the correctness of any return, making a return where none has been made, or determining the liability of any person for any internal revenue tax." Pursuant to its subpoena power, the Service may:

(1) Examine any books, papers, records, or other data that may be relevant or material to such inquiry, and

(2) Summon the person liable for tax or required to perform the act, or any officer or employee of such person, or any person having possession, custody, or care of books of account containing entries relating to the business of the person liable for tax or required to perform the act, or any other person the Service may deem proper to produce such books, papers, records, or other data.

f. Limitations on the Service's Subpoena Powers: The following may limit the Service's subpoena powers:

(1) Attorney-client privilege (beware of potential waiver of attorney-client privilege);

(2) Work product privilege;

(3) Tax practitioner's privilege;

(4) Physician-patient privilege (although there is no circuit court precedent allowing for a physician-patient privilege, the Supreme Court has noted that psychotherapist-patient disclosures are privileged);

(5) Relevance.

g. Handling Third-Party Contacts and Summonses:

(1) Right to Contact: The examining agent may contact third parties for information. By law, the agent is required to notify the taxpayer of such contact within three days following the contact. It is important to follow-up with the third-party to determine what questions were asked and what information was given. If possible, request to be

present at any meeting to protect against privileged information being revealed.

(2) Right to Summons: The examining agent may issue summonses for documents or to unwilling third-parties. Advise the third-party as to any issues or privilege concerns the taxpayer may have.

h. Settlement Attempts:

(1) Consider Dollar or Issue Settlements: The examining agent may be willing to settle based upon a dollar-figure amount or may be willing to settle on an issue-by-issue basis.

(2) Consider Which Points to Concede: Identify the strong vs. the weak issues; the important vs. the non-important issues; and decide which are worth conceding in order to achieve a settlement.

(3) Failed Settlement Attempts: If settlement does not work, request a copy of the Form 1273, *Report of Estate Tax Examination Changes*, or Form 3233, *Report of Gift Tax Examination*, as the case may be.

K. Practice Tip 9: Handling the Audit Itself

1. Establish Credibility Early:

a. Establish Credibility: Credibility begins prior to the audit by attaching all relevant information to the return. Maintain a comprehensive file and be prepared to justify the positions taken.

b. Be Reasonable: Although the advocate has a duty to zealously represent each client's interests, being reasonable with procedure can build and maintain credibility.

c. Adhere to Deadlines: Set deadlines for producing information or documents and stick to them.

d. Do Not Taint the Audit: Once the examining agent believes the donor or estate is hiding something or not being completely truthful, this belief may color the rest of the audit and can be very difficult to overcome.

2. Ascertaining the Issues:

a. Assume Familiarity With the Issues and Planning Techniques: Expect that the examining agent is familiar with estate planning techniques and is familiar with the gift and/or estate tax return.

b. Inquire as to Issues Identified at the Initial Conference: At the initial conference, ask the examining agent if any issues have been identified. This will help the practitioner know how to prepare an appropriate defense.

c. Use Computer Programs to Understand How the Issues Affect the Numbers: Use computer programs such as Inter-EST to understand how the issues identified will affect the deficiency. For those unfamiliar, Inter-EST is a computer program the Service sometimes has used to calculate the tax due as a result of any audit adjustments. The program is a useful tool in the practitioner's arsenal because it allows the practitioner to run several different scenarios to determine their "bottom-line" effect and can guide the defense strategy.

3. Addressing the Examining Agent's Requests to Speak With the Personal Representative:

a. Interviews with Fiduciaries: The agent can compel the testimony of the personal representative via subpoena. Thus, it is usually better to control the time and location of that interview by arranging for it. The interview will also tend to be less formal if agreed upon rather than compelled. Remember that the examining agent is usually an attorney, and usually has a firm grasp on the issues in the case, and will know what questions to ask. Conversely, the personal representative likely has had little or no experience being formally interviewed. Thus, preparation is key to ensure that the representative knows what to expect and how to properly answer questions.

b. Presence of Counsel: The representative's attorney should also be present to ensure that privileged information is not revealed and to correct any misstatements.

L. Practice Tip 10: Mind Deductible Expenses and Nondeductible Expenses

1. Overview: An issue commonly confused by preparers is what expenses can be deducted on the Form 706. This section is intended to address some of those questions.

2. Examples of Deductible Expenses: The following are examples of deductible funeral expenses and administration expenses:

a. Funeral Expenses: Cemetery plot (not prepaid); reasonable funeral or shiva luncheon; flowers; cost of the minister, priest rabbi; monument and lettering; costs of the funeral; acknowledgments; and travel for immediate family.

b. Administration Expenses: Appraisals; surrogate's fees; probate expenses; fee to notify creditors; death certificates; telephone charges (for the personal representative); cost of an personal representative's or administrator's bond; collection costs; court costs; cost on recovery or discovery of assets; storage of property if delivery to legatee not possible within a reasonable time.

c. Debts of Decedent Unpaid at Time of Death: Personal accounts; judgments; federal and State income and gift taxes; unpaid mortgage principal and interest on the decedent's date of death; charitable pledges; State, county, and local taxes *accrued before the date of death*; unpaid inheritance tax on interrelated estate.

3. Examples of Nondeductible Expenses: Contingent liabilities; debts paid by insurance; medical expenses paid prior to death; liabilities of corporation of which the decedent was a shareholder; real estate and property maintenance costs; storage expenses; State, county, and local taxes *accrued after death*; real estate brokers' commissions unless the property is directed to be sold in the Will.

4. Protective Claims Under I.R.C. § 2053:

a. Overview: A protective claim for refund may be filed when there is an unresolved claim or expense that will not be deductible under I.R.C. § 2053 before the expiration of the period of limitation under I.R.C. § 6511(a). To preserve the estate's right to a refund once the claim or expense has been finally determined, the protective claim must be filed before the end of the limitations period.

b. Purpose of Protective Claim for Refund: A protective claim for refund preserves the estate's right to a refund of tax paid on any amount included in the gross estate which would be deductible under I.R.C. § 2053 but which has not been paid or otherwise will not meet the requirements for deductibility under I.R.C. § 2053 until after the limitations period for filing the claim has passed under I.R.C. § 6511(a).

c. Schedule PC: For estates of decedents dying on or after January 1, 2012, a new Schedule PC was added to Form

706. Schedule PC allows personal representatives to make a protective claim for refund for expenses which are not currently deductible under I.R.C. § 2053. ***Schedule PC applies only to I.R.C. § 2053 protective claims for refund being filed with Form 706***.

d. How to Prepare Schedule PC: For a protective claim for refund, report the expense on Schedules J, K, or L but without a value in the last column. Then complete Schedule PC. The estate must indicate whether the Schedule PC being filed is the initial notice of protective claim for refund, notice of partial claim for refund, or notice of the final resolution of the claim for refund.

VI. Concluding the Audit

A. Overview

1. Overview: When the examining agent has reached a decision, the agent will discuss their findings with the taxpayer. As noted above, depending upon whether the case is agreed in full, agreed in part, or unagreed, the auditor will then take further steps that usually confer upon the taxpayer legal rights.

a. Fully Agreed Cases: If there is a change in the tax assessment and the case is agreed, the examiner will:

(1) Prepare a draft Form 1273, Form 6180 and Form 886-A in the case of an estate tax examination. I.R.M., pt. 4.25.10.6 (Jul. 31, 2020). The examiner will prepare a draft Form 1273 and Form 886-A in the case of a gift tax examination. Id. In either event, the reports will explain all changes made during the course of the examination. Id.

(2) Prepare and secure Form 890, *Waiver of Restrictions on Assessment and Collection of Deficiency and Acceptance of Overassessment*, which is used to document that the taxpayer agrees to the proposed adjustments and is waiving the statutory restrictions upon assessment and collection of the deficiency in tax. Id. The execution of this form permits the Service to assess the deficiency, schedule the over-assessment, or adjust the applicable credit amount immediately. Id. It also stops the running of interest from the 31st day after the date of receipt until notice and demand for payment is made. Form 890 does not constitute a final closing agreement. Id.

(3) Solicit payment for all agreed deficiencies with an interest computation through a specified date on which the deficiency is agreed to be paid. Id.

(4) Close the case with all due expedience. Id.

b. Partially Agreed Cases: If the taxpayer does not agree to all of the proposed adjustments, but agrees to some of the proposed adjustments, the case is partially agreed. In partially agreed cases, the examiner will:

(1) Prepare two reports; the first of which is intended to show which adjustments are agreed and which adjustments are not agreed;

(2) The first report, Form 1273 (for estate tax cases) or Form 3233 (for gift tax cases), will address the agreed adjustments. In general, the figures returned by the taxpayer will be reflected in the "Shown on Return" column. The agreed changes will be reflected in the "As Corrected" column. A Form 6180, Forms 886-A and Form 890 should also be included; and

(3) The second report, Form 1273 (for estate tax cases) or Form 3233 (for gift tax cases), will address the unagreed adjustments. The unagreed changes will be reflected in the "As Corrected" column. A Form 6180, Forms 886-A and Form 890 should also be included. The unagreed portion of the case will then be processed as discussed immediately below. See I.R.M., pt. 4.25.10.8 (Jul. 30, 2019).

c. Unagreed Cases: In estate, gift, and generation skipping transfer tax examinations, if the taxpayer does not agree to the proposed adjustments, the case is unagreed. I.R.M., pt. 4.25.10.7 (Jul. 31, 2020) In such cases, the examiner will:

(1) Solicit a statement of the taxpayer's position on each unagreed issue and consider the taxpayer's position with appropriate documentation before concluding the examination. Id.

(2) Determine whether case is eligible and should use Fast Track Settlement procedures. Id.

(3) Confirm the date on which the statute of limitations expires. Id. If there are more than 210 days remaining on the statute of limitations on the date the taxpayer communicates disagreement with the proposed adjustments, a 30-day letter (or ticket to Appeals) may be issued. See I.R.M., pt. 4.25.10.7.3 (Jul. 30, 2019). The taxpayer should request that a 30-day letter, rather than a 90-day letter (or notice of deficiency) be issued to allow an opportunity to appeal to the Service prior to any appeal to Tax Court. If there are less than 210 days remaining on the statute of limitations on the date the taxpayer communicates disagreement with the proposed

adjustments, then a 90-day letter (or notice of deficiency) letter is issued. I.R.M., pt. 4.25.10.7.4 (Jul. 30, 2019).

(4) The determinations of an unagreed case are set forth in Form 1273 (for estate tax cases) or Form 3233 (for gift tax cases). The unagreed changes will be reflected in the "As Corrected" column. A Form 6180 and Form 886-A should also be included. I.R.M., pt. 4.25.10.7.7 (Jul. 31, 2020).

B. The 30-Day Letter and Appeals

1. Appeals Preconference Procedures:

a. Overview: Preconference meetings may be held between Appeals Officers and examiners on unagreed cases containing unusual or complex issues. I.R.M., pt. 4.25.13.2.2 (Jul. 12, 2018). The preconference is held at the request of the examiner. Id. The I.R.M. states that the purpose of a preconference is to discuss the issues, protest, and the auditor's written rebuttal to the protest in cases containing complex or unusual issues. Id.

b. When it Occurs: Preconference meetings will take place prior to the Appeals/Taxpayer conferences. Id.

c. Ex Parte Communications: Historically, ex parte communication between Appeals officers and examiners was strictly prohibited. See, e.g., Service Restructuring and Reform Act of 1998, Pub. L. No. 105-206, § 1001(a), 112 Stat. 685; Rev. Proc. 2000-43, 2000-2 C.B. 404, modified, amplified, and superseded by Rev. Proc. 2012-18. However, in Rev. Proc. 2012-18 (Oct. 1, 2012), the Service softened its approach to ex parte communications. Nevertheless, the IRS's current policy provides that preconference meetings fall within the ex parte communications prohibition, such that a preconference meeting should only be held after giving the taxpayer or taxpayer's representative an opportunity to participate. I.R.M., pt. 4.25.13.2.1 (Jul. 12, 2018).

2. Fast Track Settlement:

a. Overview: The Service's Small Business/Self-Employed Unit ("SBSE") and the Appeals Fast Track Settlement ("FTS") is a jointly administered program offered by the Service to expedite case resolution at the earliest opportunity. I.R.M., pt. 4.25.13.3 (Jul. 12, 2018). FTS is

intended to enable taxpayers and the Service to work together in resolving disputed issues while the case remains in SBSE jurisdiction. Id. FTS is designed to streamline the settlement process of estate and gift tax cases because the taxpayer, the taxpayer's representative, the examiner, the estate and gift group manager, and an Appeals mediator actively participate in the outcome. Id. The FTS is estimated to be complete within 60 days.

b. When Available: FTS is generally available for all non-docketed SBSE cases with no regard to dollar amount. I.R.M., pt. 4.25.13.3.1. However, the following cases are specifically excluded from FTS:

(1) Docketed cases;

(2) Cases with numerous issues, whether simple or complex, which will require longer than 60 days to resolve;

(3) Cases where SBSE or the taxpayer are unable to meet during the 60 day time frame;

(4) High profile, sensitive taxpayers or issues;

(5) Cases where the taxpayers have failed to respond to Service communications and no documentation has been previously submitted for consideration (a/k/a "no-show cases");

(6) Non-filer cases;

(7) Frivolous filers; and

(8) Whipsaw issues. Id.

c. Steps to Commence: A request for FTS should be made by submitting an package to an Appeals Team Manager (ATM) that includes the following information:

(1) Signed Form 14017, *Application for Fast Track Settlement*;

(2) A summary of issues;

(3) The taxpayer's written position and response to the examiner; and

(4) In the case of a family limited partnership valuation issue, Form 1273, Form 6180, Form 886-A, the taxpayer's appraisal, and the Service's appraisal.

See I.R.M., pts. 4.25.13.3.2 (Jan. 12, 2018) and 8.26.2.7 (Jun. 23, 2017).

d. Ex Parte Communications: Note the IRS's position that the prohibition against communications between the Appeals Officer and other IRS employees does not apply in the FTS context. I.R.M., pt. 4.25.13.3(4)(a) (Jul. 12, 2018).

e. The FTS Conference: The examiner, the taxpayer, and the Appeals Officer participate in the FTS Conference. I.R.M., pt. 4.25.13.3.3 (Jul. 12, 2018). Appeals leads the session and conducts it as a mediator would.

f. Cases That Effectively Settled in FTS: If the parties resolve the issue(s) brought through the FTS process, and the examiner's group manager or territory manager agrees with the settlement, Appeals will prepare and execute the appropriate agreement form and a brief Appeals Case Memorandum. Id. Once the disputed issues are resolved or the decision is made that a resolution cannot be reached, the Appeals Official solicits signatures of the taxpayer and SBSE representative on a report (known as the "Fast Track Session Report"). Id. The Fast Track Session Report lists the issues in dispute as well as the resolution of the issues. Id. Both parties are given a copy of this report and are also notified the settlement is not final until the necessary closing documents or waivers are signed. Id.

g. Cases That Do Not Settle in FTS: If the parties are unable to resolve an issue, the taxpayer will retain all of the standard appeal rights and the examiner will close the case as "Unagreed." When Appeals receives an unagreed case after an FTS session, Appeals assigns it to a different Appeals Officer (assuming of course that a 90-day letter is not issued first, in which case an appeal would go to Tax Court, not Appeals). Id.

h. Withdrawal or Termination of FTS Allowed: A taxpayer's request to participate in the FTS process can be terminated or withdrawn at any time. I.R.M., pt. 4.25.13.3.4 (Jul. 12, 2018).

3. Post-Appeals Mediation

a. In General: Post-Appeals Mediation ("PAM") is a formal mediation procedure for cases in the Appeals administrative process that is conducted by third parties. I.R.M., pt. 8.26.5.1 (Aug. 17, 2015). PAM is a nonbinding

process that uses the service of a mediator or mediators, as neutral third parties, to help Appeals and the taxpayer reach a negotiated settlement. Id.

b. How it Works: Generally, an Appeals officer serves as a mediator and Appeals pays for all expenses associated with the use of the mediator. I.R.M., pt. 8.26.5.4.8 (Aug. 17, 2015). Additionally, the taxpayer may (at their own expense) elect to use a co-mediator who is not employed by the Service. I.R.M., pt. 8.26.5.4.9 (Aug. 17, 2015).

   i. Conference: The Appeals Team Manager will confer with the Appeals Officer of Tax Policy and Procedure before deciding to approve or deny a mediation request. I.R.M., pt. 8.26.5.2 (Aug. 17, 2015).

   ii. Time of Response: The Appeals Team Manager will generally respond within two weeks after receiving the mediation request. I.R.M., pt. 8.26.5.4.3 (Aug. 17, 2015).

   iii. Written Agreement Required: Assuming the request is approved, the taxpayer and Appeals will enter into a written agreement to mediate substantially in the form attached as Exhibit 2 to Rev. Proc. 2014-63. See Rev. Proc. 2014-63, § 8.01.

c. How to Request: To invoke the PAM procedures, the taxpayer should send a written request to the appropriate Appeals Team Manager and a copy to the appropriate Appeals Area Director (these individuals are listed in Exhibit 1 of the revenue procedure). Rev. Proc. 2014-63, § 7.02(1). The mediation request should include the following:

   i. The taxpayer's name, taxpayer identification number, and address (and, if applicable, the name, title, address, and telephone number of a different contact person, such as an authorized representative);

   ii. The name of the Team Case Leader, Appeals Officer, and/or Settlement Officer;

   iii. The taxable period(s) involved;

iv. A description of the issue for which mediation is requested, including the dollar amount of the adjustment or, if applicable, the offer in compromise amount in dispute; and

v. A representation that the issue is not an excluded issue under the revenue procedure. See Rev. Proc. 2014-63, § 7.02(2).

d. Availability of PAM: Rev. Proc. 2014-63 instructs that "[m]ediation may be used to resolve issues in cases that qualify under this revenue procedure while they are under consideration by Appeals. This procedure may be used only after Appeals settlement discussions are unsuccessful and, generally, when all other issues are resolved but for the issue(s) which mediation is being requested." Rev. Proc. 2014-63, § 4.01. Mediation is available under the revenue procedure for the following types of cases:

i. Legal issues;

ii. Factual issues;

iii. Compliance Coordinated Issues or Appeals Coordinated Issues, which are published online at www.irs.gov/appeals;

iv. Early referral issues when an agreement is not reached, provided that the early referral issue meets the requirements for mediation;

v. Issues for which a request for competent authority assistance has not yet been filed;

vi. Unsuccessful attempts to enter into a closing agreement under I.R.C. § 7121;

vii. Offer in compromise issues (as defined in the revenue procedure); and

viii. Trust fund recovery penalty issues (as defined in the revenue procedure). See Rev. Proc. 2014-63, § 4.04.

e. Unavailability of PAM: Mediation is not available under the revenue procedure for the following types of cases:

i. Cases in which mediation is improper under 5 U.S.C. § 572 or 575, which generally provide the authority and guidelines for use of alternative dispute resolution in the administrative process;

ii. Issues designated for litigation;

iii. Issues docketed in any court;

iv. Collection cases, except for certain offer in compromise and trust fund recovery penalty cases as detailed in the revenue procedure;

v. Issues for which mediation would not be consistent with sound tax administration, including but not limited to issues governed by closing agreements, res judicata, or controlling Supreme Court precedent;

vi. Frivolous issues;

vii. "Whipsaw" issues, or issues for which resolution with respect to one party might result in inconsistent treatment in the absence of participation of another party, such as, but not limited to, issues on a joint return where both spouses do not agree to participate in the same mediation proceeding or where one spouse is claiming innocent spouse treatment under I.R.C. § 6015;

viii. Cases in which the taxpayer did not act in good faith during settlement negotiations, such as, but not limited to, cases in which the taxpayer failed to timely respond to document requests or offers to settle, or failed to address arguments and precedents raised by Appeals;

ix. Cases that were previously mediated through a different alternative dispute resolution program within Appeals, such as FTS or FTM; and

x. Issues that have been otherwise identified in subsequent guidance issued by the IRS as excluded from the mediation program. See Rev. Proc. 2014-63, § 4.03.

C. The Notice of Deficiency or 90-Day Letter and Tax Court Litigation

1. Overview: If a case is unagreed within 210 days of the date on which the statute of limitations expires, or if the case otherwise fails to settle with Appeals, the Service will issue a notice of deficiency (a/k/a the "90-day letter") determining deficiencies in estate or gift tax. While a complete discussion of the United States Tax Court ("Tax Court"), the United States Court of Federal Claims ("Court of Claims"), or United States District Court

litigation is outside the scope of this outline, practitioners should be familiar with some basic concepts.

2. Estate Tax and Gift Tax Deficiency Cases Generally

   a. Background: I.R.C. § 6212 authorizes the Service to issue a notice of deficiency with respect to any of the following types of tax: (i) income tax (including individual, corporate, trust, and estate income taxes); (ii) estate and gift tax; or (iii) excise taxes on certain organizations and persons dealing with them.

   b. Tax Court's Basis for Jurisdiction: I.R.C. § 6213(a) grants jurisdiction to the Tax Court to redetermine a deficiency in any type of tax which is the subject of the issuance of a notice of deficiency. The Tax Court tends to be the preferred venue for litigating tax cases because, unlike the Court of Claims or the District Courts, the tax does not need to be prepaid in order to litigate in Tax Court.

3. Invoking the Tax Court's Jurisdiction: The Tax Court's jurisdiction to redetermine a deficiency depends upon a valid notice of deficiency and a timely filed petition. Both must be present before the Tax Court has jurisdiction over a case. I.R.C. § 6213(a); Tax Ct. R. Prac. & Proc. 20(a).

   a. Time to Petition the Tax Court: A taxpayer generally has 90 days to file a petition to redetermine a notice of deficiency unless the notice is addressed to a person outside of the United States, in which case the taxpayer has 150 days to file the petition.

4. Bring in an Experienced Tax Litigator Early: If you have not already brought a tax litigator on your team in connection with the audit or the Appeals process, it is usually a good idea to do so when the notice of deficiency is issued. Estate tax and gift tax litigation tends to be high-dollar, high-stakes litigation in which valuation is almost always at issue. Tax Court litigation is very specialized and its rules are very different than those in other federal or local courts.

VII. Federal and State Liability of the Personal Representative and Transferees

A. Overview

1. Personal Liability for a Personal Representative: A personal representative can become personally liable for unpaid Federal estate tax of the estate or for unpaid Federal income tax of the decedent. See 31 U.S.C. § 3713(a), (b). A personal representative can also become personally liable for unpaid State estate and inheritance taxes. See, e.g., N.J.S.A. 54:35-2.

2. The Relevant Statutes: 31 U.S.C. § 3713, entitled Priority of Government Claims, provides that a personal representative can be held personally liable to the United States is a personal representative pays a "debt" of the estate before satisfying the Government's claims.

   a. A claim of the United States Government shall be paid first when-

      (1) a person indebted to the Government is insolvent and-

         (a) the debtor without enough property to pay all debts makes a voluntary assignment of property;

         (b) property of the debtor, if absent, is attached; or

         (c) an act of bankruptcy is committed; or

         (d) the estate of a deceased debtor, in the custody of the executor or administrator, is not enough to pay all debts of the debtor.

   b. This subsection does not apply to a case under title 11.

   c. A representative of a person or an estate (except a trustee acting under title 11) paying any part of a debt of the person or estate before paying a claim of the Government is liable to the extent of the payment for unpaid claims of the Government.

3. Liability Can Extend to Certain Trustees: A trustee of a trust which was revocable until the decedent's death can, in certain circumstances, also be personally liable for the decedent's and the estate's taxes. See, e.g., Fla. Stat. §§ 737.3054(1) and 733.607(2).

4. United States Need Not Perfect Its Claim: The United States is not subject to State law requirements of filing proofs of claim.

5. United States May Assert a Claim After Discharge: The United States may make its claim long after the estate has been probated and the personal representative discharged by the probate court.

B. The King's Debtors Dying, the King Shall First Be Paid

1. The King Shall Be Paid First: A personal representative of an estate without enough property to pay all claims of the estate must pay the Federal tax claims before all other claims. 31 U.S.C. § 3713.

2. Creation of Liability: I.R.C. § 3713(b) creates the underlying liability for the personal representative and I.R.C. § 6901(a)(1)(B) provides the Service to use their standard assessment and collection methods for the liability which, as discussed below, is the issuance of a notice of liability.

3. The Notice of Liability: When proceeding pursuant to I.R.C. § 6901(a)(1)(B) the Service issues a notice of liability.

4. The Periods to Assess and Collect a Liability Under I.R.C. § 6901: The period of limitations on assessment with respect to a liability under I.R.C. § 6901 expires on the date that is the later of one year after (1) the liability arises, or (2) the expiration of the period of collection of the tax in respect of which the liability arises (*i.e.*, generally ten years). Thus, as a general rule, the Service can assess liability on the fiduciary under I.R.C. § 6901 up to ten years after assessment of the tax in respect of which such liability arises.

5. Means of Enforcing the Liability: The United States asserts this claim by filing suit against the personal representative in the appropriate federal district court pursuant to I.R.C. § 7402(a).

C. Federal Personal Liability for the Personal Representative

1. Overview: If the personal representative pays other creditors prior to paying the United States, the fiduciary may be held personally liable to the extent of the payments that the fiduciary turned over to non-governmental creditors. 31 U.S.C. § 3713(b); United States v. Coppola, 85 F.3d 1015, 1020 (2d Cir. 1996); I.R.M., pt. 5.5.3.9 (Mar. 26, 2010).

2. Requirements for Liability: Pursuant to 31 U.S.C. § 3713(b), the following requirements must be met for there to be personal liability imposed upon the personal representative:

a. The United States must have a claim;

b. The personal representative must have knowledge of the United States' claim or be placed on inquiry notice of the claim;

c. The personal representative must have paid a "debt", which term is generally defined to include the payment of a beneficiary's distributive share;

d. The debt must have been paid at a time when the estate is insolvent or the debt must have created the insolvency; and

e. The Service must have filed a timely assessment against the personal representative.

3. Impact on Offer in Compromise: The Third Circuit recently affirmed a Tax Court decision that amounts collectable against a personal representative are includable for purposes of determining reasonable collection probability for an offer in compromise. In re Estate of Kwang Lee v. Comm'r, 2022 U.S. App. LEXIS 23655 at *2-3 (3d Cir. Aug. 23, 2022), aff'g T.C. Memo. 2021-92.

4. Potential Criminal Liability of the Personal Representative and Attorney

a. In General: In rare circumstances, the United States has prosecuted the personal representative of an estate criminally.

b. Tales from the Crypt:

(1) Personal Representative Guilty of Making False Return: September 9, 2004 - Press Release: ROSEMARIE D. BRIA, "sentenced…. for subscribing a false estate tax return," "one-count Information charging her with filing a false estate tax return," "omitted estate assets from the estate tax return resulting in a tax loss to the Government."

(2) Attorney Guilty of Obstruction of Justice: May 2, 2012 – Press Release: SUZANNE LAND, "a Cincinnati attorney, pleaded guilty today to obstructing and impeding the Internal Revenue Service (IRS) while representing the estates of two deceased clients."

(3) Attorney Guilty of Making False Statements to the Service: December 28, 2012 – Press Release: William A. Hirst, "attorney pleaded guilty yesterday to one count of making a false statement to the

Internal Revenue Service," "Hirst told the IRS he found the three lost deeds in a file and recorded them, which was false since Hirst knew he signed the client's signature to the three deeds recorded on April 4, 2005."

(4) Lawyer Who Helped Seggerman Heirs Hide Inheritance Convicted: April 17, 2018 – https://tinyurl.com/2jpwkmu5: "The lawyer who taught New York's first family of tax evasion the tricks of the trade might be spending his golden years in prison. A Manhattan jury last week found Michael Little, 67, guilty of helping the adult children of a Wall Street executive tap into their Swiss bank accounts, which held millions in inheritance money, without alerting the IRS. . . . Federal authorities have charged more than 60 account holders with tax evasion and 30 bankers or lawyers with enabling them during the past eight years."

D. Federal Personal Liability for the Transferees of Estates and Gifts

1. General Lien Attached to Property: The United States has a lien on all property of the taxpayer for assessed and unpaid taxes. See I.R.C. § 6321 and 6322. The lien does not arise until the tax is assessed. Id.

2. Estate Tax a Lien on the Gross Estate: The United States has a special tax lien on the gross estate of an estate equal to the estate tax due. I.R.C. § 6324. This lien attached at the time of the decedent's death (*i.e.*, the tax need not be assessed before the lien attaches). See Treas. Reg. § 301.6324-1(a)(1). Thus, the Service can also attach the property of the gross estate to a special lien.

3. Transferee Liability Imposed: I.R.C. § 6901(a)(1)(A) also imposed transferee liability on any heir, legatee, devisee of an estate or a donee of any gift . See also Treas. Reg. § 301.6901-1(a)(1).

VIII. FOIA Requests

A. Background

1. Enactment of the Law: The Freedom of Information Act ("FOIA"), 5 U.S.C. § 552, is a federal freedom of information law that allows for the full or partial disclosure of previously unreleased documents within the control of the federal Government, including the Service.

2. Learn What the Government Knows: Practitioners should submit a FOIA request to the Service at various stages during the audit, Appeals, and post-audit or post-Appeals stages of a tax controversy.

3. Reason for Making the Request: Often, but not always, the FOIA will give the practitioner insight into the reasons that the Service determined a certain adjustment in the taxpayers' income, estate, or gift tax for a particular year. Additionally, FOIA might help certain taxpayers show that procedural due process requirements were not met (*e.g.*, I.R.C. § 6751's written supervisory approval of a penalty determination.[4] In this regard, a FOIA response can be of considerable value when taking an issue before Appeals or before a federal court.

B. Making FOIA Requests

1. Format of the FOIA Request: There is no required form for making a FOIA request. We advise that such request be made in writing to the Service's Disclosure Office. Attached as **Exhibit A** is a sample FOIA Request, though your requests should also be specifically tailored to the items you are most interested in learning about.

2. How to Make: FOIA requests can be sent by fax or by mail as follows:

a. By Fax: FOIA requests can be faxed to (877) 891-6035.

b. By Mail: FOIA requests can be sent by mail to the following address:

[4] As noted, I.R.C. § 6751(b)(1) generally requires that the initial determination that a penalty applies be approved in writing by the immediate supervisor of the person making the determination, the taxpayer may argue that the penalty may not be assessed. See, e.g., Graev v. Commissioner, 149 T.C. 485 (2017) (following Chai v. Commissioner, 851 F.3d 190 (2d Cir. 2017)).

(1) Internal Revenue Service
GLDS Support Services
Stop 93A
Post Office Box 621506
Atlanta, GA 30362-3006

3. Cost: FOIA requesters will not be charged fees unless the total amount of fees is $25.00 or more. I.R.M., pt. 11.3.5.2 (Oct. 18, 2021). Generally, once the $25.00 threshold is met, the fees are $.20 per page for paper copies, $50/hour of search and review time, and $30/hour of time spent scanning (the first 1,000 scanned pages are free of charge to requesters other than Commercial Users). I.R.M., pts. 11.3.5.2.1, 11.3.5.2.1, 11.3.5.2.3, 11.3.5.2.4 (Oct. 18, 2021). See also I.R.M., pt. 11.3.5.2.5. As a practical matter, the Service tends to issue its FOIA response for voluminous materials on a CD.

4. Limitations on the FOIA Request: There are, of course, limits to the FOIA request. Two of the more noteworthy limitations are as follows:

a. The Service is only required to look for an existing record or document in response to a FOIA request. FOIA does not require the Service to collect information it does not have or to research or analyze data for a person making a FOIA request; and

b. The Service is not obligated to create a new record to comply with a FOIA request. However, when records are maintained by a computer, the Service may be required to retrieve information in response to a FOIA request.

C. The FOIA Response

1. Time to Respond: Under FOIA, the Service must determine within 20 business days after the date a FOIA request is received whether and to what extent to comply with the FOIA request. 5 U.S.C. § 552. The Service can extend the 20-day period by an additional 10 days in unusual circumstances. See, e.g., 5 U.S.C. § 552 (a)(6)(B)(i)-(iii). Such unusual circumstances include, but are not limited to, the need to collect information from field offices, the need to review large numbers of documents, and the need to consult with other agencies. 5 U.S.C. § 552 (a)(6)(B)(i).

2. Denials in Whole or In Part: The Service tends to respond to the FOIA request and will generally produce some but not all documents. If a FOIA request is denied in whole or in part, the

Service must state the reasons for the denial. The request may be exempt from disclosure under FOIA because:

a. It concerns classified documents pertaining to national defense and foreign policy;

b. It is prohibited by internal personnel rules and policies;

c. The information is exempt under other laws, the most common of which cited in the tax contest is the prohibition on disclosure of other taxpayer information under I.R.C. § 6103;

d. It concerns trade secrets and confidential commerce or financial information;

e. It concerns interagency or intragency memorandums or letters;

f. It is exempt for personal privacy reasons, such as personnel, medical, and similar files, the disclosure of which would amount to an invasion of privacy;

g. It concerns information compiled for law enforcement reasons;

h. It concerns information that is contained in or related to examination, operating, or conditions reports prepared by, on behalf of, or for the use of an agency responsible for the regulation of a financial institution;

i. It covers geological and geophysical information, data, and maps concerning wells. See Posting of FOIA Requests: A Look Into the IRS Examination File to Tax Controversy (Civil and Criminal Report) blog, http://taxlitigator.me/2012/01/11/foia-requests-a-look-into-the-irs-examination-file/ (discussing the FOIA requirements and exemptions more fully).

D. FOIA Appeal Rights and Judicial Actions

1. Right to Appeal: Taxpayers can appeal a denial of a FOIA request, either in whole or in part, administratively to the Service. The appeal should include reasons why the Service response to the FOIA request was inadequate and must be postmarked within 35 days after the date of the denial letter or other adverse determinations.

2. Means of Appeal: An appeal is filed by sending a letter to Internal Revenue Service Office of Appeals, Attn: FOIA Appeals, 5045 E. Butler Avenue, M/Stop 55201, Fresno, California 93727-5136.

3. Contents of Appeal: The appeal should include copies of the FOIA request and the initial Service decision responding to the request. The envelope containing the appeal should be marked in the lower left-hand corner with the words "Freedom of Information Act Appeal."

4. Time for Appeal: The Service is required to make a decision on an appeal within 20 business days after the date of receipt of the appeal unless extended. Treas. Reg. § 601.702(c)(10)(iii).

5. Judicial FOIA Actions: If an administrative FOIA appeal before the Service is denied, a complaint against the Service seeking disclosure of the requested information may be filed to the appropriate federal District Court. 5 U.S.C. 552(a)(4)(B); Treas. Reg. § 601.702(c)(13). A copy of the complaint must be served upon the Commissioner of Internal Revenue, Attention: CC:PA, 1111 Constitution Avenue, N.W., Washington, D.C. 20224. Id.

6. Right to Attorneys' Fees: Reasonable attorneys' fees and litigation costs may be awarded if the taxpayer substantially prevails in the FOIA litigation.

IX. Gifts and Bequests From Non-U.S. Donors and Decedents – Reporting Requirements

A. *Form 3520, Annual Return to Report Transactions With Foreign Trusts and Receipt of Certain Foreign Gifts*

1. These persons must file Form 3520:

a. A responsible party for a "reportable event" that occurred during the tax year, meaning:

(1) The formation of a foreign trust by a U.S. person,

(2) The transfer of cash or other assets into a foreign trust, or

(3) The death of a citizen or resident of the United States if the decedent was treated as an owner under the grantor trust rules or if a portion of the trust was included in the decedent's gross estate.

b. U.S. persons that transferred property (including cash) to a related foreign trust (or a person related to the trust) in exchange for an obligation.

c. U.S. persons that hold a qualified obligation from a related foreign trust that is currently outstanding.

d. U.S. persons treated as the owner of a foreign trust under the grantor trust rules.

e. U.S. persons or executors of the estate of a U.S. person who received (directly or indirectly) a distribution from a foreign trust during the current tax year.

f. U.S. owners or beneficiaries of a foreign trust who, in the current tax year, received (or a U.S. person related to them received) (1) a loan of cash or marketable securities (including an extension of credit) directly or indirectly from such foreign trust, or (2) the uncompensated use of trust property.

g. U.S. owners or beneficiaries of a foreign trust if the trust owes an outstanding qualified obligation to them or to a U.S. person related to them in the current tax year.

h. U.S. persons who, during the current tax year, received, and treated as gifts or bequests, either:

(1) More than $100,000 from a nonresident alien individual or a foreign estate (including foreign persons related to that nonresident alien individual or foreign estate); or

(2) More than the I.R.C. section 6039F threshold amount from foreign corporations or foreign partnerships (including foreign persons related to such foreign corporations or foreign partnerships).

2. Purported Gifts § 1.672(f)-4

a. The IRS may re-characterize gifts received directly or indirectly from foreign partnerships or corporations to U.S. person as income that must be included in gross income.

b. Exceptions:

i. If the U.S. citizen or resident alien individual treated and reported the gift as a distribution for U.S tax purposes and as a gift to the U.S. donee OR

ii. A nonresident alien reported under the laws of their country of residence as a distribution to such individual and a subsequent gift or bequest to the United States donee, and the United States donee timely complied with the reporting requirements of section 6039F, if applicable.

3. When To File

a. The form is due when the income tax return of the U.S. entity (individual, partnership, corporation, etc.) is due, including any extensions of time to file. The form is not filed with the tax return.

4. Penalties

a. Greater of $10,000 or 35% of the gross reportable amount.

b. 5% per month for the amount of certain foreign gifts, up to 25%.

c. Penalties may be waived for reasonable cause.

i. The fact that disclosure is a crime in another country is not reasonable cause.

d. See I.R.C. §6677; IRS Notices 96-60; 97-34.

e. See I.R.C. §6662(j) for additional penalties.

5. Special Rules

a. Lerch v. Commissioner, T.C. Memo. 1987-295, where petitioners were assessed deficiencies and penalties in part for failing to report foreign sourced income on a Form 3520.

B. Form 3520-A, *Annual Information of Foreign Trusts With a U.S. Owner*

1. Who Must File

   a. A foreign trust with a U.S. owner must file Form 3520-A in order for the U.S. owner to satisfy its annual information reporting requirements. See I.R.C. § 6048.

   b. Exception: Canadian registered retirement savings plans (RRSP) and Canadian registered retirement income funds (RRIF) are not required to file Form 3520-A.

   c. Grantor must file if the foreign trust fails to file a timely Form 3520-A or does not provide the information required.

   d. See I.R.C. § 679(c) for changes made by the HIRE Act regarding loans, etc.

   e. See I.R.C. § 679(d) for presumption that the foreign trust has a US beneficiary.

2. When To File

   a. The Form is required to be filed three and a half months after the end of the tax year of the trust.

   b. For a trust using a calendar year, the deadline is March 15th.

   c. However, an extension of time can be requested on Form 7004, *Application for Automatic Extension of Time to File Certain Business Income Tax, Information, and Other Returns*.

3. Penalties

   a. The U.S. owner is subject to a penalty equal to 5% of the gross value of the portion of the trust's assets treated as owned by the U.S. person at the close of that year (or $10,000 if higher).

   b. Additional penalties may be imposed if noncompliance continues after the IRS gives the taxpayer notice.

   c. Criminal penalties may be imposed.

   d. The penalties may be waived for reasonable cause.

4. IRS Notice 97-34

   a. A U.S. person who is the owner of a foreign trust is responsible for ensuring that the trustee files IRS Form

3520-A. The U.S. Person is subject to a penalty of 5 percent of the gross reportable amount in the event of noncompliance, as well as additional penalties for continued noncompliance.

b. Be especially aware that the filing deadline is March 15, not April 15.

5. Special Rules

a. Para Technologies Trust v. Commissioner, T.C. Memo. 1994-366, where a foreign trust was not reported by its Officers and Trustees, and ultimately found to be disregarded, and its principal liable for negligence.

X. Offshore Accounts

A. Overview

1. Inquire Into Foreign Bank Assets: Where a decedent's gross estate includes foreign assets, it essential that the personal representative and representatives of the estate determine that the decedent has properly reported all foreign source income.

2. Compliance Options: If it is discovered that the decedent was not fully tax compliant, a controversies attorney should be consulted to explore options, including the IRS's Streamlined Filing Compliance Procedures.

3. FBAR Requirement Applies to Estates: Persons and estates with offshore accounts are required to file FinCEN Form 114, *Report of Foreign Bank and Financial Accounts* ("FBAR"), and report all income from these accounts and assets on their federal and state income tax returns annually.

   a. There are multiple programs available to correct noncompliance:

      (1) IRS Criminal Investigation Voluntary Disclosure Practice;

      (2) Streamlined Filing Compliance Procedures;

      (3) Delinquent FBAR submission procedures; and

      (4) Delinquent international information return submission procedures.

   b. Consult a controversies attorney to determine whether participating in any of these programs is advisable.

4. Additional Filing Requirements That May Apply:

   a. Form 926: *Return by a U.S. Transferor of Property*: reports a transfer of property (even if such property is not appreciated property) to a foreign corporation described in IRC § 6038B(a)(1)(A) or 367(d);

   b. Form 3520: *Annual Return to Report Transactions with Foreign Trusts and Receipt of Certain Foreign Gifts*;

   c. Form 3520-A: *Information Return of Foreign Trust with a U.S. Owner*;

   d. Form 5471: *Information Return of U.S. Persons with Respect to Certain Foreign Corporations*;

e. Form 5472: *Information Return of 25% Foreign-Owned U.S. Corporation or a Foreign Corporation Engaged in a U.S. Trade or Business*;

f. Form 8865: *Return of U.S. Persons with Respect to Certain Foreign Partnerships*;

g. Form 8938: *Statement of Specified Foreign Financial Assets*;

h. Form 8621: *Information Return by a Shareholder of a Passive Foreign Investment Company or Qualified Electing Fund*;

i. Form 8621-A: *Return by a Shareholder Making Certain Late Elections to End Treatment as Passive Foreign Investment Company*;

j. Form 8858: *Information Return of U.S. Persons with Respect to Foreign Disregarded Entities and Foreign Branches*;

k. Form 706 CE: *Certificate of Payment of Foreign Death Tax*; must be filed for foreign death tax credit to be permitted on Form 706;

l. Form 1116: *Foreign Tax Credit (Individual, Estate or Trust)*; must be filed to obtain foreign tax credit.

B. Miscellaneous Issues With Foreign Bank Accounts

1. Deductibility of Penalty: A penalty for offshore accounts is deductible.

2. Ensuring Compliance With Offshore Reporting Requirements: Where a decedent's foreign bank statements are not available, either to ensure that the decedent has properly reported any foreign source income or to be utilized for the preparation of amended tax returns and to provide to the Service in a disclosure, such documents may be requested from decedent's banking institution.

a. Obtain Documents With Court Documents: Typically, provision of estate documents such as Letters Testamentary or Letters of Administration showing who has been designated as the Executor or Administrator of an estate along with notarized signature are sufficient to gain authority to communicate with a decedent's bank and obtain necessary documents.

b. Obtain Documents With Blanket Authorization: An Administrator or Executor of an estate may also authorize

the decedent's foreign bank to provide documents and communicate with the estate's counsel and accountants.

3. FBAR Requirements Continue Until Safe Deposit Boxes Closed: As the responsibility to file an FBAR applies to an estate, estate representatives must continue to file FBARs until all foreign accounts including safety deposit boxes are closed.

4. Foreign Inheritances: If a foreign gift is received, the donee or beneficiary should file Form 3520.

Appendix A: Sample IRS FOIA Letter

TRANSCRIPT REQUEST
PRIVACY ACT, FOIA & IRC § 6103 REQUEST

By Facsimile ((877) 891-6035) and Certified Mail, R.R.R.

November 20, 20__

Internal Revenue Service
Disclosure Scanning Operation
Stop 93A
Post Office Box 621506
Atlanta, GA 30362-3006

ATTENTION: FOIA REQUESTS

Re: Taxpayer, Inc.
Tax Period ending: 12/31/20__
EIN: __-_____
Our File:1234

Dear Representative:

We represent Taxpayer ("Taxpayer"). Attached as Exhibit A is a copy of our Form 2848, *Power of Attorney and Declaration of Representative.* Pursuant to the provisions of I.R.C. §§ 6103 and 7602(c) of the Internal Revenue Code ("IRC") and the Freedom of Information Act (the "Act" or "FOIA"), 5 U.S.C. § 552, as amended, we request access to and copies of the following records maintained by the Internal Revenue Service ("IRS"):

1. All notices, letters, memorandum, contact history sheets, audit reports, correspondence, IRS forms, liens and levies prepared by or received by the IRS that refer or relate to the year(s) and/or period(s) referenced above.

2. All transcripts of account, records of assessments and abatements and any other documents reflecting all account activity and transactions that refer or relate to the year(s) and/or period(s) referenced above.

3. Copies of any documents (*e.g.* statute extensions, collection waivers) attached to the tax returns filed by Taxpayer for the years and/or period(s) referenced above (If these documents exist, they were attached to the subject returns by the IRS after the filing of said returns).

4. A record of persons contacted by the IRS with respect to the determination or collection of the tax liability of the taxpayer.

5. All notices reflecting the payment of state taxes that refer or relate to the years and/or period(s) referenced above.

6. All third party information received by the IRS that refers or relates to the years and/or period(s) referenced above.

7. All third party information in the IRS possession relevant to the preparation or verification of any item on the Taxpayer's returns for the years and/or period(s) referenced above.

8. History Transcript (Account Transcript) for the period(s) listed above.

In accordance with IRS Statement of Procedural Rules, Reg. section 601.702(c)(4)(ii), we agree to pay reasonable charges incurred in locating and copying the requested documents, to an upper limit not to exceed $200.

If you decide that any portion of a requested record is exempt from disclosure under the Act, I request that you send me the remaining nonexempt portion of that record. In addition, to the extent that access is denied to inspect any part of the requested administrative files and documents, please send me an index and a detailed description of the deleted material and a statement of the statutory basis for withholding each such document. As stated above, we have attached a copy of the Form 2848 authorizing us to make this request for Taxpayer. ***In accordance with the provisions of the Act, we expect to receive a reply within 20 working days.***

Kindly acknowledge receipt of this letter by countersigning the enclosed copy of this letter and returning the same in the enclosed self-addressed, stamped envelope.

Very truly yours,

John Smith, Esq.

JS/___

Enclosures (as stated)

cc: Taxpayer, Inc.

RECEIPT ACKNOWLEDGED:
INTERNAL REVENUE SERVICE
BY:_____
TITLE:_____
DATE:_____