



**COUNTRY  
COMPARATIVE  
GUIDES 2023**

# The Legal 500 Country Comparative Guides

## United States

# TAX DISPUTES

### Contributor

Mayer Brown LLP



#### Gary B. Wilcox

Partner | [gwilcox@mayerbrown.com](mailto:gwilcox@mayerbrown.com)

#### Joel V. Williamson

Partner | [jwilliamson@mayerbrown.com](mailto:jwilliamson@mayerbrown.com)

#### Sam Bear

Associate | [sbear@mayerbrown.com](mailto:sbear@mayerbrown.com)

#### Jeremy D. Himmelstein

Associate | [jhimmelstein@mayerbrown.com](mailto:jhimmelstein@mayerbrown.com)

This country-specific Q&A provides an overview of tax disputes laws and regulations applicable in United States.

For a full list of jurisdictional Q&As visit [legal500.com/guides](https://legal500.com/guides)

## UNITED STATES TAX DISPUTES



The  
**LEGAL  
500**

### **1. Is it necessary for a taxpayer to register with the tax authority? Are separate registrations required for corporate income tax and value added tax/sales tax?**

The IRS does not require registration. Individuals and businesses are tracked by their social security numbers and employer identification numbers (EINs). Businesses need EINs not only to file tax returns and withhold tax on employee wages, but also to open bank accounts, apply for local permits, and maintain credit scores. The U.S. tax system relies on voluntary compliance, but there are stiff penalties for not complying. The U.S. has no value added or federal sales tax. Most states, however, impose tax on sales of goods or services and require businesses to register to collect tax from customers or claim an exemption.

### **2. In general terms, when a taxpayer files a tax return, does the tax authority check it and issue a tax assessment - or there a system of self-assessment where the taxpayer makes their own assessment which stands unless checked?**

The U.S. tax system is generally one of self-assessment. When the taxpayer files its tax return, it self-assesses its tax liability. The IRS has a variety of mechanisms for encouraging self-assessment (e.g., failure-to-file penalties, summonses, etc.). The return ordinarily reports certain facts upon which the tax liability is computed, and the computation of the tax. Most of these self-assessments remain undisturbed. But each year, returns are selected for audit based on a computer scoring process, or because they don't match other related returns, or just randomly. And many large corporate taxpayers are routinely under audit. If the IRS disagrees with the taxpayer's self-assessment, then it proposes adjustments.

### **3. Can a taxpayer amend the taxpayer's return after it has been filed? Are there any time limits to do this?**

Generally, taxpayers may file an amended return within three years of the due date of the original return, or within two years after paying the tax, whichever is later. This relates to the statute of limitations for assessment. In other words, taxpayers may file an amended return so long as the tax year is still "open" for assessment.

### **4. Please summarise the main methods for a tax authority to challenge the amount of tax a taxpayer has paid by way of an initial assessment/self-assessment.**

Before the IRS can assess additional tax (let alone begin to collect it), it must comply with several administrative requirements. In order to assess tax, the IRS has to issue a Notice of Deficiency and then wait either 90 days for the taxpayer to petition the U.S. Tax Court or, if the taxpayer takes that option, until there is a final resolution of any such litigation.

If the IRS disputes the tax liability reported by the taxpayer, it will first issue a Notice of Proposed Adjustment (NOPA). The taxpayer typically has 30 days to respond to the NOPA, although a response is not mandatory. If the taxpayer agrees with the adjustment, it can sign and return the NOPA and then pay the tax due after receiving an assessment of the tax liability. If the taxpayer disagrees with the NOPA, the IRS ordinarily provides the taxpayer an opportunity to request a conference with the IRS Independent Office of Appeals (Appeals) to protest the adjustment, by issuing a "30-day letter" and a Revenue Agent's Report. If the taxpayer chooses not to pursue an appeal, it will receive a Notice of Deficiency. If the taxpayer pursues an appeal, Appeals may drop the adjustment entirely, reduce the proposed tax liability pursuant to settlement, or sustain the adjustment in full. If the taxpayer agrees with the Appeals resolution, it must pay the tax due after receiving an assessment of the tax liability. If the

taxpayer disagrees with the Appeals resolution, it will receive a Notice of Deficiency.

Once the IRS issues a Notice of Deficiency, the taxpayer has 90 days to consent to an assessment of the amount of the deficiency or to petition the Tax Court for redetermination. Unless the taxpayer consents to an assessment during this time, the IRS may not assess additional tax during the 90 day window. If the taxpayer consents to the assessment and pays the tax, it may still seek a refund in court. And if the taxpayer exercises its right to petition the Tax Court, then the IRS may not assess additional tax until there is a final resolution of the litigation (including after appeals to higher courts).

### **5. What is the procedure where a taxpayer has not registered so is unknown to the tax authority (for example a newly incorporated company or a foreign company operating through a permanent establishment?)**

A newly incorporated company in the U.S. needs an employer identification number (EIN) to file federal and state tax returns. Foreign individuals and foreign companies doing business in the U.S. are required to obtain an EIN and file a Form 1040-NR or Form 1120-F, respectively, even if there is no U.S. taxable income to report, or the income is exempt from U.S. tax under a tax treaty. Foreign individuals and foreign companies not doing business in the U.S., but are otherwise subject to U.S. withholding tax on U.S. source income, must file these returns only if the withholding tax is insufficient to cover the tax liability, or to claim a refund if the withholding tax is excessive. Non-U.S. citizens who are U.S. residents because they pass the green card test or substantial presence test must file a U.S. tax return just like a U.S. citizen, using their social security number. Non-U.S. citizens who are not U.S. residents and not engaged in U.S. business, but have wages from a U.S. employer or other U.S. income not covered by withholding tax, must file a U.S. return using an individual taxpayer ID number (ITIN).

### **6. What are the time limits that apply to such challenges (disregarding any override of these limits to comply with obligations to relief from double taxation under a tax treaty)?**

The time limits for the IRS to audit foreign individuals and foreign companies are the same for U.S. individuals and U.S. companies. The general limit is three years

after the due date or filing date (e.g., filing with a permitted extension), whichever is later. If the return understates 25% or more of gross income (including as a result of overstating tax basis), the limit is six years. If no return is filed or a fraudulent return is filed, there is no time limit. Further, if a foreign corporation doing business in the U.S. fails to file a Form 1120-F, it is later prohibited from claiming deductions and is, in effect, taxed on its gross income unless it can prove its failure to file was based on reasonable cause.

### **7. How is tax fraud defined in your law?**

Tax fraud exists where the taxpayer attempts to evade tax by intentionally concealing income, misleading tax authorities, or otherwise preventing collection. Tax fraud can occur in various cases, including those involving unreported income or inflated or bogus deductions. The IRS and courts generally consult the following “badges of fraud” in making determinations: understating income, keeping inadequate records, implausible explanations, concealing assets, refusing to cooperate with investigators, engaging in illegal activities, supplying false information to a tax return preparer, lacking credibility, filing false documents, failing to file tax returns, and dealing in cash.

### **8. How is tax fraud treated? Does the tax authority conduct a criminal investigation with a view to seeking a prosecution and custodial sentence?**

Tax fraud can be treated civilly or criminally. During an examination the IRS examiners will determine whether elements of tax fraud exist and, if so, whether the taxpayer may have committed criminal tax evasion. If the examiners believe that criminal elements are present, they will consult special agents in the IRS Criminal Investigation Division, who will review the case and refer it to the Department of Justice for prosecution if necessary. If the government decides to prosecute, the IRS will put its civil examination on hold until the criminal case concludes. At that point, whether or not the government has prosecuted a criminal case, the IRS will decide whether to impose a 75% civil fraud penalty. If the taxpayer disputes the penalty in court, the IRS will bear the burden of proof.

### **9. In practice, how often is a taxpayer audited after a return is filed? Does a tax authority need to have any justification to commence an audit?**

Audit rates depend on the type of taxpayer and amount of income, among other things. For individuals, audit rates in 2020 (last reported year) were 0.21% for income between \$25,000 and \$50,000, 0.19% for income between \$200,000 and \$1 million, 0.42% for income between \$1 million and \$5 million, and 1.36% for income of \$5 million or more. For corporations, audit rates in 2020 ranged, for example, from 0.3% for income between \$5 million and \$10 million, 0.41% for income between \$10 million and \$50 million, and 17.74% for income above \$20 billion. There are a variety of ways in which taxpayers are selected for audit. Some are selected based on a computer scoring process that identifies returns with high potential for unreported income or overstated deductions. Many individual and small business returns are selected because the return numbers don't match numbers reported on Forms W-2 and 1099. Others are selected because they have relationships with others already selected. Many large corporations are routinely audited annually; others are selected because of reported tax avoidance transactions or low effective tax rates. Internal controls, however, are intended to prevent the IRS from auditing specific taxpayers for political, personal or other non-objective reasons.

#### **10. Does the tax authority have to abide by any standards or a code of conduct when carrying out audits? Does the tax authority publish any details of how it in practice conducts audits?**

The IRS maintains procedural manuals that define in detail the conduct of IRS personnel in a variety of situations. These manuals focus mainly on the functions of Examination, Appeals and Counsel. Taxpayers do not have rights to legally enforce these rules of conduct, but can effectively enforce them by escalating their complaints to IRS management. The IRS does not publish details of specific audits, but is accountable to Treasury's Inspector General and Congress for audit results. The IRS does publish its general standards and goals for conducting audits. Taxpayers also have a statutory "bill of rights" that governs a taxpayer's dealings with the IRS, such as the rights to be informed, to be heard, and to have confidentiality. To help protect these rights, taxpayers may rely on the Taxpayer Advocate Service, an independent organization within the IRS that provides free taxpayer assistance.

#### **11. Does the tax authority have the power to compulsorily request information? Does**

#### **this extend to emails? Is there a right of appeal against the use of such a power?**

The IRS is authorized by statute to issue an administrative summons seeking any records or testimony that "may be relevant" to the particular inquiry, providing such information is not privileged. If the taxpayer does not comply, the IRS may cause the Justice Department to seek an order enforcing the summons from a federal district court. Taxpayers may oppose the summons in the district court action, and may appeal an adverse decision to a circuit court. The IRS's summons authority does extend to emails, although it is not clear whether taxpayer is required at the audit stage to provide the emails in a searchable format or otherwise provide the underlying metadata or other electronically stored information (ESI) relating to the emails. However, the IRS sometimes claims it can seek ESI at the audit stage. Taxpayers typically provide the IRS with only paper or pdf copies of emails that are reasonably retrievable. In active litigation, however, the government is entitled to seek ESI in the discovery process.

#### **12. Can the tax authority have the power to compulsorily request information from third parties? Is there a right of appeal against the use of such a power?**

The IRS is authorized by statute to issue an administrative summons to a third party, seeking any records or testimony that "may be relevant" to the particular inquiry, providing such information is not privileged. The IRS must notify the taxpayer within a certain time period. The taxpayer may object to the summons by filing a motion to quash in federal district court. In that case the third party is not required to produce the requested information unless ordered by the court, subject to taxpayer's right to appeal an adverse decision to a circuit court.

#### **13. Is it possible to settle an audit by way of a binding agreement, i.e. without litigation?**

The resolution of a dispute with the IRS can be done on a binding or non-binding basis. Tax disputes may be resolved during audit based on an application of the law to the facts. If the dispute is not resolved at the examination phase, a taxpayer may pursue an appeal with the IRS Independent Office of Appeals (Appeals). Appeals has the authority to settle tax disputes (after audit) based on the "hazards of litigation." In both cases, these resolutions are non-binding on the taxpayer if they

are reflected in either a Form 870 (at examination) or a form 870-AD (at Appeals). That is, in both cases, a taxpayer may choose to agree to pay the re-computed tax liability upon being assessed, and then seek a refund pursuant to refund litigation in a federal district court or the Court of Federal Claims. However, the government is typically precluded in most cases (e.g., based on rules precluding multiple examinations, or other policies on case closure) from asserting an additional tax liability once a Form 870 or a Form 870-AD has been executed, even though those forms are not technically binding from a legal standpoint. In order to legally prevent the taxpayer from seeking a refund, and to legally prevent the IRS from asserting additional tax liability within the statute of limitations period, it is necessary for both parties to sign a binding closing agreement (Form 906).

#### **14. If a taxpayer is concerned about how they are being treated, or the speed at which an audit is being conducted, do they have any remedies?**

The IRS maintains procedural manuals that define in detail the conduct of IRS personnel in a variety of situations, including treatment of taxpayers and the conduct of an audit. These manuals focus mainly on the functions of Examination, Appeals and Counsel. Taxpayers do not have rights to legally enforce these rules of conduct, but can effectively enforce them by escalating their complaints to IRS management. Taxpayers also have a statutory “bill of rights” that governs a taxpayer’s dealings with the IRS, such as the rights to be informed, to be heard, and to have confidentiality.

#### **15. If a taxpayer disagrees with a tax assessment, does the taxpayer have a right of appeal?**

At the end of an examination, the IRS may propose an adjustment. The taxpayer then has the option to protest that adjustment with the IRS Independent Office of Appeals (Appeals), which will review the case and determine whether to drop the adjustment entirely, reduce the proposed tax liability pursuant to settlement, or sustain the adjustment in full. If the taxpayer agrees with the Appeals resolution, it must pay the tax due after receiving an assessment of the tax liability. If the taxpayer disagrees with the Appeals resolution, it will receive a Notice of Deficiency.

After the IRS issues the Notice of Deficiency, the taxpayer can litigate the tax in one of three judicial forums: (i) the Tax Court, (ii) the Court of Federal Claims,

or (iii) the District Court in which the taxpayer resides. The Tax Court is the only forum in which the taxpayer may litigate without prepaying the tax. However, interest accrues while the dispute is pending in the Tax Court.

#### **16. Is the right of appeal to an administrative body (independent or otherwise) or judicial in nature (i.e. to a tribunal or court)?**

Taxpayers may choose to dispute their tax liability in the IRS Independent Office of Appeals (Appeals) or court or both. Although Appeals is a division of the IRS, it is separate from the examination and collection divisions of the IRS. Taxpayers may prefer to seek relief in Appeals before resorting to court, because Appeals proceedings are not as formal or expensive. Taxpayers should know that they do not forfeit their right to go to court by going (or not going) to Appeals.

#### **17. Is the hearing in public? Is the decision published? What other information about the appeal can be accessed by a third party/the public?**

Proceedings in the IRS Independent Office of Appeals are confidential to the public, and third parties do not have access to the contents of the final administrative decision. In most cases, the public will not even know that a proceeding is taking place. By contrast, court proceedings are not confidential, and third parties can obtain certain documents such as motions, court orders and decisions, and trial transcripts. In some cases, however, a judge might “seal” specific documents or an entire case to protect the taxpayer’s rights (e.g., to safeguard proprietary information).

#### **18. Is the procedure mainly written or a combination of written and oral?**

Proceedings in the IRS Independent Office of Appeals are informal and may consist of both written and oral procedures. Taxpayers may submit detailed legal arguments in writing, but they may also participate in settlement conferences or mediation programs. Court proceedings are formal, and the procedures governing what can be stated in writing or otherwise are set forth in the relevant judicial forum’s published rules (e.g., Tax Court Rules of Practice and Procedure, Federal Rules of Evidence, Federal Rules of Civil Procedure).

**19. Is there a document discovery process?**

Although the IRS may obtain information and documents from the taxpayer and certain third parties, there is no formal discovery process in the Independent Office of Appeals (Appeals). However, taxpayers are expected to submit relevant and up-to-date documents and information so that Appeals can make an informed decision.

There is a document discovery process in court. However, the formalities may vary depending on the judicial forum and the forum's rules. For example, the Tax Court requires that parties engage in informal discovery before asking the judge to entertain formal requests (e.g., before filing a motion to compel production of documents or seeking a deposition).

**20. Are witnesses called to give evidence?**

The IRS Independent Office of Appeals may ask third parties to provide relevant information or documents, but they will not be asked to testify under oath. By contrast, in court the taxpayer and other witnesses may be required to answer interrogatories (written questions), participate in a deposition, and testify under oath during a trial.

**21. Is the burden on the taxpayer to disprove the assessment the subject of the appeal?**

The IRS's determinations in a Notice of Deficiency are generally presumed correct, and the taxpayer bears the burden of proving them erroneous. To prevail, taxpayers must present sufficient evidence to support their factual assertions and ultimately must persuade the judge or jury that their position is correct. In some cases the burden of proof can shift to the IRS, and in other cases the IRS may bear the burden of proof at the outset (e.g., in fraud cases).

**22. How long does an appeal usually take to conclude?**

The timing of an appeal will vary depending on the complexity of the issues and the taxpayer's choice of forum. When an audit is not resolved and moves to the IRS Independent Office of Appeals (Appeals), it can take at least a year to hold the Appeals conference and finally resolve the case. If the matter moves to litigation, it can take several years to hold a trial and ultimately have a decision. This is particularly true in complex cases involving large tax deficiencies.

**23. Does the taxpayer have to pay the assessment pending the outcome of the appeal?**

The Tax Court is the only judicial forum in which the taxpayer may litigate without prepaying the tax. However, interest accrues while the dispute is pending in the Tax Court. To dispute the case in the Tax Court, the taxpayer must file a Tax Court petition within 90 days of receiving the Notice of Deficiency. To dispute the case in the Court of Federal Claims or District Court, the taxpayer must prepay the tax and file a refund claim. Prepaying the tax will stop the accrual of interest.

**24. Are there any restrictions on who can conduct or appear in the appeal on behalf of the taxpayer?**

Regulations embodied in a document called "Circular 230" specify who can represent a taxpayer in an administrative proceeding before the IRS. These regulations generally limit representation to certified public accountants, attorneys, enrolled agents, enrolled actuaries, and other similar practitioners.

The rules are more strict in court, where practitioners must be admitted to practice. The Tax Court will permit a non-attorney to represent a taxpayer, but non-attorneys must pass a written examination before filing an application for admission. However, only licensed attorneys can represent taxpayers in cases before the Court of Federal Claims and District Court.

**25. Is there a system where the "loser pays" the winner's legal/professional costs of an appeal?**

The prevailing party in a dispute may be awarded both reasonable administrative costs in connection with an administrative proceeding and reasonable litigation costs in connection with a judicial proceeding, but there are many conditions. To be the "prevailing party," the taxpayer must do more than prevail; it must also show that the IRS's position was not substantially justified. And, the IRS must agree (at least, if the dispute was resolved administratively). If the dispute was resolved in court, then only the court must agree. In order to recover litigation costs, the taxpayer must have exhausted its administrative remedies. So, if the taxpayer did not first attempt to resolve the dispute with the IRS Independent Office of Appeals before filing suit then it cannot recover litigation expenses. At the same time, the taxpayer must not have unreasonably protracted proceedings. And finally, the taxpayer must

not exceed certain net worth thresholds.

## **26. Is it possible to use alternative forms of dispute resolution - such as voluntary mediation or binding arbitration? Are there any restrictions on when this alternative form of dispute resolution can be pursued?**

Alternate dispute resolution is not available during the examination phase. If there are unagreed issues after examination, and the case moves to the IRS Independent Office of Appeals (Appeals), there are several options for mediation outside of the regular Appeals process. Fast Track Mediation and Fast Track Settlement (FTS) provide opportunities for small business and large business taxpayers, respectively, to settle factual and legal disputes with IRS examination, where IRS Appeals acts as a mediator. If the case does not settle, the regular Appeals option is still available. Rapid Appeals Process is similarly intended to provide quick access to an Appeals officer who acts as a mediator, without foreclosing the regular Appeals option if settlement is not reached. If no settlement is reached at regular Appeals, taxpayers may request post-Appeals mediation, where mediators selected by taxpayer and Appeals attempt to facilitate a resolution; this option is not available where a taxpayer has used FTS prior to Appeals. While there is no option for binding arbitration in IRS examination or Appeals, that option (as well as non-binding mediation) is available in litigation.

## **27. Is there a right of onward appeal? If so, what are all the levels of onward appeal before the case reaches the highest appellate court.**

Following an audit, all taxpayers generally have a right to appeal the determined deficiency either administratively or judicially (or both). The taxpayer has no obligation to seek resolution administratively with the IRS Independent Office of Appeals (Appeals) before pursuing judicial remedies. However, the potential for swifter and more affordable resolution in Appeals is an attractive option.

Because interest and penalties continue to accrue during the appeals process (again, either administratively or judicially), taxpayers may choose to pay the contested liability and then proceed with the appeal. If the taxpayer does not pre-pay the contested liability, it may only appeal administratively or to the U.S. Tax Court. If the taxpayer does pre-pay the contested liability, then it may appeal the determination to the U.S. Court of Federal Claims or to any U.S. District Court with

jurisdiction. And if the taxpayer disagrees with the court's judgment, it has a further right of appeal to whichever U.S. Court of Appeals has jurisdiction. Finally, if the taxpayer disagrees with the decision of the U.S. Court of Appeals then it may petition the U.S. Supreme Court to hear its case. However, the U.S. Supreme Court rarely grants such petitions.

## **28. What are the main penalties that can be applied when additional tax is charged? What are the minimum and maximum penalties?**

When a taxpayer is charged with additional tax liability, the IRS may impose accuracy-related penalties equal to 20 percent of the underpayment that is attributable to either (i) negligence or disregard of the tax rules or regulations or (ii) a substantial understatement of income. The maximum the IRS may impose for accuracy-related penalties increases to 40 percent if the underpayment is attributable to particularly large valuation misstatements or certain inadequately-disclosed transactions.

"Negligence" is determined by testing a taxpayer's conduct against that of a reasonable, prudent person. A substantial understatement penalty is not imposed with respect to the tax treatment of an item if the taxpayer had substantial authority for the position or if the taxpayer adequately disclosed the position and had a reasonable basis for such treatment. The substantial authority standard is an objective standard that requires an "analysis of the law and application of the law to the relevant facts." A taxpayer may rely on the advice of a professional tax advisor to meet this standard.

If the understatement is attributable to a "tax shelter," the penalty is avoided only if the taxpayer, at a minimum, can establish both (1) substantial authority for its tax treatment of the transaction and (2) its belief that this tax treatment was more likely than not proper. A taxpayer may rely on the advice of a professional tax advisor to meet these requirements.

If the Service finds that the understated tax liability was the result of fraud, then it may impose civil penalties equal to 75 percent of the underpayment attributable to fraud. Occasionally, the IRS also pursues criminal fines for taxpayers that wilfully attempt to evade or defeat tax, which are limited to \$100,000 for individuals and \$500,000 for corporations, as well as imprisonment.

## **29. If penalties can be mitigated, what**

### factors are taken into account?

Accuracy-related penalties may not be imposed with respect to any portion of an underpayment if it is shown that there was reasonable cause for such portion of tax on which the penalty was assessed. The determination of whether a taxpayer acted with reasonable cause and in good faith is made on a case-by-case basis, taking into account all pertinent facts and circumstances. These circumstances include the experience, knowledge, sophistication, and education of the taxpayer. They also include the situation when a taxpayer takes a reasonable position based upon an ambiguously written tax law. Generally, the most important factor is the extent of the taxpayer's effort to assess the taxpayer's proper tax liability. Reliance on the advice of an experienced, credentialed tax advisor helps to satisfy this requirement.

### 30. Within your jurisdiction, are you finding that tax authorities are more inclined to bring challenges in particular areas? If so, what are these?

Individual taxpayers and small businesses are often challenged for failing to substantiate business (including home office) deductions or charitable donations, withhold taxes on employees, and report taxable income, or for claiming personal expenses as business expenses. As for large businesses, nearly all the areas of IRS focus are listed in over 50 "campaigns" on the IRS website, and those areas tend to be frequently audited. Examples in the cross-border space include delinquent or non-filed Forms 1120-F, foreign tax credits, Subpart F sales income and section 965 transition tax. Non-campaign areas that are nevertheless heavily audited include transfer pricing of sales of goods and services, outbound transfers of intellectual property, worthless stock deductions, and intercompany financing.

---

## Contributors

**Gary B. Wilcox**  
Partner

[gwilcox@mayerbrown.com](mailto:gwilcox@mayerbrown.com)



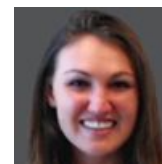
**Joel V. Williamson**  
Partner

[jwilliamson@mayerbrown.com](mailto:jwilliamson@mayerbrown.com)



**Sam Bear**  
Associate

[sbear@mayerbrown.com](mailto:sbear@mayerbrown.com)



**Jeremy D. Himmelstein**  
Associate

[jhimmelstein@mayerbrown.com](mailto:jhimmelstein@mayerbrown.com)

