



June 26, 2018

Internal Revenue Service
CC:PA:LPD:PR (REG-132434-17)
1111 Constitution Avenue, NW
Washington, DC 20224
Submitted Electronically

Docket ID: IRS-2018-0008-0001

Dear Sir or Madam:

On behalf of National Taxpayers Union's (NTU's) supporters across the nation, I am honored to submit the following comments in response to proposed changes to existing regulations clarifying that "Certain Non-Government Attorneys [are] Not Authorized to Participate in Examinations of Books and Witnesses as a Section 6103(n) Contractor."

NTU was founded in 1969 to work for less burdensome taxes, more accountable government, and stronger rights for all taxpayers. One of NTU's greatest privileges was having its then-Executive Vice President David Keating named to the National Commission on Restructuring the Internal Revenue Service (Commission) in 1997, a federal panel whose recommendations later became the basis for the most extensive Internal Revenue Service (IRS) overhaul in a generation – the IRS Restructuring and Reform Act of 1998.

NTU has long maintained a vital interest in the issue of non-IRS employees having access to taxpayer returns and information under IRC Sections 7602 and 6103(n). Over the past four decades, we advocated for legislation and rulemaking that carefully limited the circumstances under which such access was allowed, due to concerns for the financial privacy and other rights of millions of tax filers. We also supported reforms peripheral but complementary to the general intent of Section 6103(n), such as increased penalties for unauthorized browsing among IRS employees.

More recently, NTU has sought both legislative and administrative repeal of the summons-related directives promulgated in 2014 and finalized in 2016 (T.D. 9778). Accordingly, we have supported H.R. 3167¹ (114th Congress), S. 2809 (114th Congress), H.R. 3220² (115th Congress), and H.R. 5444 (115th Congress, which recently passed the House). NTU was also one of the organizations cited in the

¹ See NTU letter of endorsement for HR 3167, December 9, 2015, <http://www.ntu.org/governmentbytes/detail/ntuofferssupport-forthetax-administration-integrity-act>.

² See NTU letter of endorsement for HR 3220, July 17, 2017, <http://www.ntu.org/governmentbytes/detail/ntu-endorses-legislation-thatwill-codify-taxpayer-rights-and-rein-in-the-irs>.

current proposed rule document as supporting “removal of the regulations” in response to Notice 201738.³

We commend the Treasury and the IRS for recognizing the overly broad nature of T.D. 9778, and offering modifications through the proposed rule. Nonetheless, NTU continues to recommend complete withdrawal of T.D. 9778, for the following reasons.

1) Government Efficiency Must be Balanced with Taxpayer Rights.

NTU stands second to none among organizations supporting private-sector contracts to perform certain public services when the primary goal is to deliver such services more efficiently and effectively. Throughout NTU’s history, we have advocated contracting for functions ranging from transportation security to public building maintenance.

Yet even the IRS concedes that contracting non-IRS employees in examinations and legal proceedings is a level well above traditional outsourcing, noting:

The actions of the non-governmental attorney while questioning witnesses could foreclose IRS officials from independently exercising their judgment. Managing an examination or summons interview is therefore best exercised solely by government employees, including government attorneys, whose only duty is to serve the public interest. These concerns outweigh the countervailing need for the IRS to use non-government attorneys, except in the limited circumstances set forth in proposed paragraph (b)(3)(ii).

NTU agrees with this assessment, and would contend that the “limited circumstances” provided in the proposed rule do not sufficiently justify the government’s position with REG-132434-17 or serve the public interest. Some members of the tax community may dispute that the contracted services enabled under T.D. 9778 constitute an “inherently governmental function,” but all ought to agree that safeguarding taxpayers’ rights should be an innately governmental responsibility.

In NTU’s decades-long history, one overriding theme we have encountered in questions of tax administration is this: does the policy at hand undermine or enhance public confidence in the impartiality of the rights and remedies afforded them? There are few more blunt ways for undermining such confidence than creating additional, artificial advantages by which government can disproportionately enforce its position against a taxpayer. Allowing the IRS to marshal highly-compensated private sector attorneys in the pursuit of other private sector actors – however carefully deployed – should be avoided.

Taxpayers’ rights to privacy likewise remain at stake with this proposal. Indeed, one could argue that despite narrowing the scope of individuals permitted access to taxpayer information, as the proposed rule attempts to do, the risk to confidentiality may not be significantly affected. The specialists in nonfederal tax law or other areas of law may have little experience with information-privacy safeguards developed to shield sensitive taxpayer data from being compromised. Certain disclosures could, to an untrained eye, appear innocuous even though they could inflict considerable financial damage on an individual or business taxpayer.

³ See National Taxpayers Union Comments to the Hon. Steven Mnuchin, July 31, 2017, Docket ID TREAS-DO-2017-0012, <https://www.ntu.org/publications/detail/ntus-pete-sepp-outlines-tax-reform>.

The IRS has only recently begun to salvage a measure of public confidence in its ability to manage and secure taxpayer information after a 2016 data breach of more than 700,000 records and efforts to resolve ID theft cases that had commonly languished for 10 months. In the interest of continuing this salutary trend, NTU believes that withdrawing T.D. 9778 entirely, rather than amending it, is the best course.

Finally, we would note that T.D. 9778 began as a “temporary regulation” without a public comment period. Such an inauspicious start, backed by a policy which engendered considerable apprehension in the tax community,⁴ could best be addressed by repeal of T.D. 9778. Doing so would, in our opinion, better comport with the spirit of the Executive Orders which prompted the analysis under Notice 201738 in the first place.

2) Continuing Even Some Policies in T.D. 9778 Could Contribute to Public Skepticism over the Dispute Resolution System.

REG-132434-17 helpfully stipulates that it “would not permit IRS to hire an attorney for nonsubstantive specialized knowledge, such as civil litigation skills.” On the other hand, the regulation document also notes that the agency may “hire a contractor who may happen to be an attorney, but who is hired for knowledge, skills, or abilities other than providing legal services as an attorney.” Taxpayers may be forgiven for wondering how this duality will be reconciled at the field level. Would it, for example, permit the hiring of “consultants” who would not otherwise act as attorneys on the particular factual issues of an examination, but who could provide analysis of the impact if the government prevailed in a given scenario? Such professional advice is available to a taxpayer only at a significant and often prohibitive cost.

As NTU has testified before Congress in 2015, 2016, and 2017, a great deal turns on this question of the taxpayer’s cost in disputing an IRS determination. Last year, for example, we provided the following illustration of the calculus a small business owner faces:

Consider ... the average additional recommended tax in 2016 resulting from field audits of business 1040 tax returns with receipts between \$25,000 and \$100,000 – a total bill of \$10,617 per return. Imagine the decisions this audited business owner – the very definition of “the little guy” – would face. If he or she hires a tax professional for representation, the average fee, according to the National Society of Accountants’ most current public data, would be \$150 per hour. It would not be unusual for the accountant to spend 10 hours on this stage of the audit. Should the initial examination go against the owner, he or she could choose to retain the accountant for the administrative appeals process, perhaps involving an additional 10 hours of time. Meanwhile, the owner could have easily spent 10-20 hours of time gathering records, reviewing paperwork, etc., at an average compensation amount (according to the National Association of Manufacturers study mentioned previously) of \$48.80 per hour.

⁴ See, for example, Kroh, Eric, “Tax Pros Wary after IRS Hires Quinn Emanuel Litigators,” Law360, April 6, 2015, <https://www.law360.com/articles/639327/tax-pros-wary-after-irs-hires-quinn-emanuel-litigators>; and Frankel, Alison, “Microsoft Tax Case Highlights Conflict Concerns When U.S. Hires Private Firms,” Reuters, November 24, 2015, <http://blogs.reuters.com/alisonfrankel/2015/11/24/microsoft-tax-case-highlights-conflict-concerns-when-u-s-hires-private-firms/>.

To get this far into the audit process, the owner could have already spent roughly \$4,000, more than one-third of the contested bill. Should the administrative route fail, the owner then has broad options to file a Tax Court petition or try to litigate in federal court. While many Tax Court petitions never advance, and often lead to settlements, this process could easily consume another 10 hours of a legal professional's time (at likely a higher rate of compensation). Should litigation actually take place, a qualified tax attorney might demand \$300 per hour or more. If the owner prevails, his or her ability to recover the entirety of fees like these remains doubtful. The maximum amount that can be awarded is barely \$200 per hour, and only if the court determines the IRS's position was not 'substantially justified.'⁵

NTU has for several years warned that T.D. 9778 raises the "intimidation factor" that taxpayers with small and large cases alike would feel. Imagine, again, the situation of a taxpayer in an examination who discovers that the IRS has arrayed one or several outside "experts" to buttress the tax agency's case. Whether she is an individual 1040 form filer or business filer, a pro se litigant or one represented by skilled counsel, her resources are limited. And once again, as above, she must weigh whether it is economically viable to continue asserting a position she knows to be right, or simply settle the case.

Some would contend that even in light of the IRS's standard operating procedures, the Service is not immune to prioritizing its own resources and that REG-132434-17 is written mostly with Large Business and International Division cases in mind. After all, would the agency really consider spending millions of dollars on outside contractors to help pursue a small business examination involving tax issues worth perhaps thousands of dollars? In most circumstances, the answer would be "no." In certain cases, however, relating to potentially precedential issues, emerging industries with highly specialized functions, or complex questions involving minor financial amounts immediately at stake, the IRS could very well opt to do so.

In fact, the tax practitioner community has made this point consistently with clients and in communications with the general public: while the IRS considers many "hazards of litigation" in deciding whether to settle cases resulting from examinations, the actual financial cost to the government of litigating is generally not among those hazards. This same community has also cautioned that tools and policies initially targeted toward one class or type of taxpayer can be cleverly wielded against others.⁶

Furthermore, taxpayers are especially sensitive to what NTU contends is the harsh procedural climate in which examinations are now occurring. The most recent manifestation of this is the May 14, 2018 U.S. District Court decision in *Facebook vs. IRS*, dismissing with prejudice the plaintiff's contention that it had an enforceable right to refer its tax case to the IRS Appeals Office under the Taxpayer Bill of Rights (enacted first administratively in 2014 and statutorily in 2015).

3) Congress Is Heavily Scrutinizing – and Acting to Limit – the Activities Envisioned in the Proposed Rule.

⁵ For further details, see Testimony of Pete Sepp, National Taxpayers Union, before the Subcommittee on Oversight, House Ways and Means Committee, September 13, 2017, <https://waysandmeans.house.gov/wp-content/uploads/2017/09/20170913-OS-Testimony-Sepp.pdf>.

⁶ See, for example, Daniel J. Pilla cited in Testimony of Pete Sepp, National Taxpayers Union, before the Subcommittee on Economic Growth, Tax, and Capital Access, House Committee on Small Business, June 22, 2016, <https://www.ntu.org/publications/detail/statement-ofpete-sepp-to-house-subcommittee-regarding-irs-small-business-reforms>.

In 2015, Senate Finance Committee Chairman Orrin Hatch (R-UT) made an important inquiry to then-Commissioner Koskinen regarding a \$2.2 million contract extended to the private law firm of Quinn Emanuel for assistance with a near-decade-long tax dispute involving Microsoft; this included examination activities best described as overbearing and harsh. Chairman Hatch noted that:

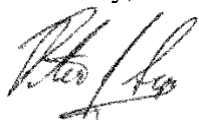
The IRS's hiring of a private contractor to conduct an examination of a taxpayer raises concerns because the action: 1) appears to violate federal law and the express will of the Congress; 2) removes taxpayer protections by allowing the performance of inherently government functions by private contractors; and 3) calls into question the IRS's use of its limited resources.

From NTU's standpoint, the IRS's action was fraught with additional risks, as described throughout these comments. In any case, the legislative branch has been actively pursuing remedies to abiding concerns among key Members of Congress that the door should be closed – rather left cracked open – to the practices enabled under T.D. 9778.

Based on events in Congress this year, it is increasingly likely the door could not only be closed, but also locked. Aside from the three hearings in which NTU participated (in each instance scrutinizing T.D. 9778), as well as the high-profile introductions of H.R. 3167, S. 2809, and H.R. 3220, just two months ago the House of Representatives unanimously voted to pass H.R. 5444. Section 308 of this legislation effectively nullifies the substance of T.D. 9778, as well as REG-132434-17. Key Members of both parties on the Senate Finance Committee have voiced interest in a cooperative legislative package that would build upon the momentum the House has given to H.R. 5444. We believe the IRS's constructive deference to previous and pending Congressional actions that aim to excise T.D. 9778 would be the wisest course.

For all of the reasons outlined here, NTU urges you to withdraw REG-132434-17 and the underlying regulation it modifies that was originally issued through T.D. 9778. In so doing, you will be upholding critical protections of taxpayers' rights and fulfilling even more fully the intent of Executive Orders 13771 and 13777. NTU is eager to further assist you in your deliberations, and we are grateful for your consideration of our views.

Sincerely,

A handwritten signature in black ink, appearing to read "Pete Sepp", written in a cursive style.

Pete Sepp President