



Department of the Treasury
Internal Revenue Service

Publication 556
(Rev. May 1997)
Cat. No. 15104N

Examination of Returns, Appeal Rights, and Claims for Refund



This publication (reprinted 9/98) does not reflect the provisions of the Taxpayer Relief Act of 1997 or the IRS Restructuring and Reform Act of 1998. The 1998 version will be updated for the new law and available in the next few months. (See *New Tax Provisions* at the end of this publication.)



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Introduction

The Internal Revenue Service (IRS) accepts most federal tax returns as filed. However, the IRS examines (or audits) some returns to verify accuracy of income, expenses, and credits.

If your return is selected for examination, it does not suggest that you made an error or are dishonest. Returns are chosen by computerized screening, by random sample, or by an income document (for example, Form W-2 or 1099) matching program.

This publication discusses general rules and procedures that we follow in examinations. It explains what happens during an examination and your appeal rights within the IRS and in the federal court system. It also explains how to file a claim for refund of tax you already paid.

As a taxpayer you have the right to be treated fairly, professionally, promptly and courteously by IRS employees. Publication 1, *Your Rights as a Taxpayer*, explains your rights when dealing with the IRS.

Useful Items

You may want to see:

Publication

- 1** Your Rights as a Taxpayer
- 594** Understanding the Collection Process
- 910** Guide to Free Tax Services
- 1546** How to Use the Problem Resolution Program of the IRS

Form (and Instructions)

- 843** Claim for Refund and Request for Abatement
- 2848** Power of Attorney and Declaration of Representative
- 1040X** Amended U.S. Individual Income Tax Return
- 4506** Request for Copy or Transcript of Tax Form

See your income tax package for information about getting these publications and forms.

Examination of Returns

We may examine your return for a variety of reasons, and the examination may take place in any one of several ways. After the examination, if we propose any changes to your tax, you can either agree with those changes and pay any additional tax, or you can disagree with the changes and appeal the decision.

If Your Return Is Examined

We handle some examinations entirely by mail. Examinations not handled by mail can take place in your home, your place of business, an Internal Revenue office, or the office of your attorney, accountant, or enrolled agent. If the time, place, or method is not convenient for you, the examiner will try to work out something more suitable. However, the IRS makes the final determination of when, where, and how the examination will take place.

Throughout the examination, you can act on your own behalf or have someone represent you or accompany you. If you filed a joint return, either you or your spouse, or both, can meet with the IRS. You can have someone represent or accompany you. This person can be an attorney, a certified public accountant, an enrolled agent (a person enrolled to practice before the IRS), or the person who prepared the return and signed it as the preparer.

If you want someone to represent you in your absence, you must furnish that representative with written authorization. Make the authorization on Form 2848, *Power of Attorney and Declaration of Representative*, or any other properly written authorization. If you want to consult an attorney, a certified public accountant, an enrolled agent, or any other person permitted to represent a taxpayer during an interview for examining a tax return or collecting tax, we will stop and reschedule the interview. We cannot suspend the interview if you are there because of an administrative summons.

Tape recordings. You can make an audio recording of the examination interview. Your request to record the interview should be made in writing. You must notify the examiner 10 days in advance and bring your own recording equipment. We also can record an examination. If we initiate the recording, we will notify you 10 days in advance and you can get a copy of the recording at your expense.

Transfers to another district. Generally, your return is examined in the IRS district where you live. But if your return can be examined more quickly and conveniently in another district, such as where your books and records are located, you can ask to have the case transferred to that district.

The Examination

An examination usually begins when we notify you that your return has been selected. We will tell you which records you will need. If you gather your records before the examination, it can be completed with the least effort.

If we propose any changes to your return, we will explain the reasons for the changes to you or your authorized representative. It is important that you understand the reasons for any proposed change. You should not hesitate to ask about anything that is unclear to you.

The IRS must follow tax laws set forth by Congress in the Internal Revenue Code. The IRS also follows Treasury Regulations, other rules and procedures that were written to administer the tax laws. We also follow court decisions. However, we can lose cases that involve taxpayers with the same issue and still apply our interpretation of the law to your situation.

Most taxpayers agree to changes proposed by examiners, and the examinations are closed at this level. If you do not agree, you can appeal any proposed change by following the procedures provided to you by the IRS. A more complete discussion of appeal rights is found later.

Repeat Examinations

We try to avoid repeat examinations of the same items, but sometimes this happens. If we examined your tax return for the same items in either of the 2 previous years and proposed no change to your tax liability, please contact us as soon as possible so we can see if we should discontinue the examination.

Problem Resolution Office

The IRS has a Problem Resolution Program for people who have been unable to solve their problems with the IRS. Before contacting the Problem Resolution Program, you should first discuss any problem with the employee's supervisor. Your local Problem Resolution Officer will assist you if you are unable to resolve the problem with the supervisor.

This office cannot change the tax law or technical decisions, but it can help you solve administrative or procedural problems. If you have an administrative or procedural problem you cannot clear up through normal channels, write to your Internal Revenue Service District Director or call your local IRS office and ask for Problem Resolution assistance. The Problem Resolution Office can help you clear up problems that resulted from previous contacts.

If You Agree

If you agree with the proposed changes, you can sign an agreement form and pay any additional tax you may owe. You must pay interest on any additional tax. If you pay when you sign the agreement, the interest is generally figured from the due date of your return to the date of your payment.

If you do not pay the additional tax when you sign the agreement, you will receive a bill that includes interest. If you pay the amount due within 10 business days of the billing date, you will not have to pay more interest or penalties. This period is extended to 21 calendar days if the amount due is less than \$100,000.

If you are due a refund, we can refund your money more quickly if you sign the agreement form. You will be paid interest on the refund.

If the IRS accepts your tax return as filed, we will mail you a letter in a few weeks stating that the exam-

iner proposed no changes to your return. You should keep this letter with your tax records.

If You Do Not Agree

If you do not agree with the proposed changes, the examiner will explain your appeal rights. You can request an immediate meeting with the examiner's supervisor to explain your position if your examination takes place in an IRS office. If an agreement is reached, your case will be closed.

If you cannot reach an agreement with the supervisor at this meeting, or if the examination took place outside of an IRS office, the examiner will write up your case explaining your position and the IRS's position. The examiner will forward your case to the district office for processing.

Within a few weeks after your closing conference with the examiner and/or supervisor, we will send you a package with:

- A letter (known as a **30-day letter**) notifying you of your right to appeal the proposed changes within 30 days,
- A copy of the examination report explaining the examiner's proposed changes,
- An agreement or waiver form, and
- A copy of Publication 5, *Appeal Rights and Preparation of Protests for Unagreed Cases*.

You generally have 30 days from the date of the 30-day letter to tell us whether you will accept or appeal the proposed changes. The letter will explain what steps you should take, depending on which action you choose. Be sure to follow the instructions carefully. *Appeal Rights* are explained later.



*If you do not respond to the 30-day letter, or if you later do not reach an agreement with an Appeals officer, we will send you a **90-day letter**, which is also known as a notice of deficiency.*

You will have 90 days (150 days if it is addressed to you outside the United States) from the date of this notice to file a petition with the Tax Court. Filing petitions with the Tax Court is discussed later under *Appeals to the Courts*.

If you later agree. If you agree with the examiner's changes after receiving the examination report or the 30-day letter, sign and return either the examination report or waiver. Keep a copy for your records. You can pay any additional amount you owe without waiting for a bill. Include interest on the additional tax at the applicable rate. This interest rate is usually for the period from the due date of the return to the date of payment. The examiner can tell you the interest rate(s) or help you figure the amount.

You must pay interest on penalties and on additional tax for failing to file returns, for overstating valuations, for understating valuations on estate and gift tax returns, and for substantially understating tax liability. Interest is generally figured from the date (including extensions) the tax return is required to be filed to the date you pay the penalty and/or additional tax.

If you pay the amount due within 10 business days after the date of the notice and demand, you will not have to pay any additional penalties and interest. This period is extended to 21 calendar days if the amount due is less than \$100,000.

How to Stop Interest from Accruing

If you think that you will owe additional tax at the end of the examination, you can stop the further accrual of interest on the amount you think you will owe. You can do this by sending money to the IRS to cover all or part of the amount you think you will owe. Interest will stop accruing on any part of the amount you cover when we receive your money.

You can send an amount either in the form of a deposit (cash bond) or as a payment of tax. Both a deposit and a payment stop any further accrual of interest. However, making a deposit or payment of tax will stop the accrual of interest on only the amount you sent. Because of compounding rules, interest will accrue on accrued interest, even if you have paid the underlying tax.



To stop the accrual of interest on both tax and interest, you must make a deposit or payment for both the tax and interest that has accrued as of the date of deposit or payment.

Payment or Deposit

Deposits differ from payments in two ways:

- 1) You can have all or part of your deposit returned to you without filing for a refund. However, if you request and receive your deposit and we later assess a deficiency for that period and type of tax, we will figure the interest as if the funds were never on deposit. Also, we will not return your deposit if one of the following situations apply:
 - a) We assess a tax liability.
 - b) We determine, that by returning it, we may not be able to collect a future deficiency.
 - c) We determine that it should be applied against another tax liability.
- 2) Deposits do not earn interest. No interest will be included when a deposit is returned to you.

Notice not mailed. If you send money before we mail you a notice of deficiency, you can ask the IRS to treat it as a deposit. You must make your request in writing.

If, after being notified of a proposed liability but before we mail you a notice of deficiency, you send an amount large enough to cover the proposed liability, we will consider it a payment unless you request in writing that it be treated as a deposit.

If the amount you send is the same as or is more than the proposed liability and you did not request that it be treated as a deposit, we will not send you a notice of deficiency. If we do not send you a notice of deficiency, you cannot take your case to the Tax Court. See *Tax Court*, later.

Notice mailed. If, after we have mailed the notice of deficiency, you send money without written instructions, we will treat it as a payment. You will still be able to petition the Tax Court.

If you send money after receiving a notice of deficiency and you have specified in writing that it is a “deposit in the nature of a cash bond,” we will treat it as a deposit if you send it before either:

- The close of the 90-day or 150-day period for filing a petition with the Tax Court to appeal the deficiency, or
- The date the Tax Court decision is final, if you have filed a petition.

Using a Deposit to Pay the Tax

We will apply your deposit against any amount you may owe if you agree with the examiner’s proposed changes after the examination. We will not mail you a notice of deficiency and you will not have the right to take your case to the Tax Court.

If you do not agree to the full amount of the deficiency after the examination, we will mail you a notice of deficiency. Then, we will apply your deposit against the proposed deficiency unless you write to us before the end of the 90-day or 150-day period, stating that you still want the money to be treated as a deposit. You will still have the right to take your case to the Tax Court. See *If You Do Not Agree*, discussed earlier.

Interest Due to Error or Delay by the Internal Revenue Service

We may lower the interest on tax you owe when the interest is due to an error or delay by an IRS official performing a ministerial act (discussed later). We will only lower the interest on income, estate, gift, generation-skipping, and certain excise taxes.

We will not lower the interest if you or anyone related to you contributed significantly to the error or delay. Also, we will only lower the interest if the error or delay happened after we contacted you in writing. An audit notification letter is such a contact.

Ministerial act. This is a procedural or mechanical act, not involving the exercise of judgment or discretion, that occurs during the processing of your case after all prerequisites (for example, conferences and review by supervisors) have taken place. A decision concerning the proper application of federal tax law (or other federal or state law) is not a ministerial act.

Example 1. You move from one state to another before the IRS selects your tax return for examination. A letter stating that your return has been selected is sent to your old address and then forwarded to your new address. When you get the letter, you respond with a request that the examination be transferred to the district office closest to your new address. The examination group manager approves your request. After your request has been approved, the transfer is a ministerial act. We may reduce the interest because of any delay in transferring the case.

Example 2. An examination of your return reveals tax due for which we will issue a notice of deficiency (90-day letter). After you and the IRS discuss the issues, the notice is prepared and reviewed. After the review process, issuing the notice of deficiency is a ministerial act. If we delay sending the notice of deficiency to you, we may reduce the interest resulting from the delay.

How to request reduction of interest. You request a reduction of interest on Form 843, *Claim for Refund and Request for Abatement*. You should file the claim with the IRS Service Center where you filed the tax return that was affected by the ministerial error or delay. If you do not remember the Service Center where you filed that tax return, send your claim to the Service Center where you filed your last tax return.

Generally, you should file a separate Form 843 for each tax period and each type of tax. However, complete only one Form 843 if the interest is from our error or delay and affected your tax for more than one tax period or for more than one type of tax (for example, where we were examining two or more tax years). You do not have to figure the dollar amounts of interest that you want lowered.

If your request for reduction of interest is denied, you can appeal the decision to the Appeals Office.

Failure to lower interest may be reviewable by Tax Court. The Tax Court has jurisdiction over certain actions brought by taxpayers concerning an IRS refusal to lower interest. The Tax Court can decide the issue when certain requirements are met:

- For individual and estate taxpayers — your net worth must not exceed \$2 million as of the filing date of your petition for review. For this purpose, individuals filing a joint return shall be treated as one taxpayer, except in the case of an innocent spouse relieved of liability (See discussion on *Innocent Spouse Exception*, later).
- For charities and certain cooperatives — you must not have more than 500 employees as of the filing date of your petition for review.
- For all other taxpayers — your net worth must not exceed \$7 million, and you must not have more than 500 employees as of the filing date of your petition for review.

The action must be brought within 180 days after the IRS mails its final determination.

Appeal Rights

Because people sometimes disagree on tax matters, the Service has an appeals system. Most differences can be settled within this system without expensive and time consuming court trials.

However, your reasons for disagreeing must come within the scope of the tax laws. For example, you cannot appeal your case based only on moral, religious, political, constitutional, conscientious, or similar grounds.

If you do not want to appeal your case within the IRS, you can take your case directly to court.

Appeal Within the IRS

You can appeal an IRS tax decision to a local Appeals Office, which is separate and independent of your local IRS District, Service or Compliance Center. The Appeals Office is the only level of appeal within the IRS. Conferences with Appeals Office personnel are conducted in an informal manner.

If you want an appeals conference, follow the instructions in our letter to you. We will send your request to the Appeals Office to arrange a conference at a convenient time and place. You or your representative should be prepared to discuss all disputed issues at the conference. Most differences are settled at this level.

If agreement is not reached at your appeals conference, you can, at any time, take your case to court. See *Appeals to the Courts* later.

Written Protests

When you request a conference, you may also need to file either a written protest or a brief written statement of disputed issues with the office named in our letter to you.

Written protest or brief statement not required. You do not have to file a written protest or brief statement of disputed issues if you meet one of the following requirements:

- The proposed increase or decrease in tax, or refund determined by the examination, is not more than \$2,500 for any of the tax periods involved, or
- Your examination was handled by mail or in an IRS office by a tax auditor.

Written protest or brief statement required. If the proposed increase or decrease in tax, including penalties, or refund, determined by the IRS is more than \$2,500 but not more than \$10,000, you must provide a brief written statement of the disputed issues. If the proposed increase or decrease in tax, including penalties or claimed refund is more than \$10,000, you must submit a written protest of the disputed issues to obtain an Appeals Office conference. All partnerships, S corporations, employee plans, and exempt organizations must also submit written protests.

If you must submit a written protest, you should send it within the time limit specified in the letter you received with the examination report. Your protest should contain:

- 1) Your name and address,
- 2) A statement that you want to appeal the IRS findings to the Appeals Office,
- 3) The date and office symbols from the letter showing the proposed changes and findings you disagree with,
- 4) The tax periods or years involved,
- 5) An itemized schedule of the changes with which you disagree,

- 6) A statement of facts supporting your position on any issue with which you disagree,
- 7) A statement stating the law or other authority on which you rely, and
- 8) A declaration that the statement of facts under (6) is true under penalties of perjury.
Do this by adding the following signed declaration: "Under the penalties of perjury, I declare that I have examined the statement of facts presented in this protest and in any accompanying schedules and, to the best of my knowledge and belief, it is true, correct, and complete."

If your representative submits the protest for you, he or she can substitute a declaration stating:

- 1) That he or she prepared the protest and accompanying documents, and
- 2) Whether he or she knows personally that the statement of facts in the protest and accompanying documents are true and correct.

Representation

You can represent yourself at your appeals conference, or you can be represented by an attorney, certified public accountant, or an enrolled agent.

If your representative attends a conference without you, he or she can receive or inspect confidential information only if you have filed a power of attorney or a tax information authorization. You can use a Form 2848, *Power of Attorney and Declaration of Representative*, or any other properly written power of attorney or authorization.

You can also bring witnesses to support your position.

Appeals to the Courts

If you and the IRS still disagree after the appeals conference, you can take your case to the United States Tax Court, the United States Court of Federal Claims, or the United States District Court. These courts are independent of the IRS.

If you elect to bypass the IRS' appeals system, you also can take your case to one of the courts listed above. However, a case petitioned to the United States Tax Court will normally be considered for settlement by an Appeals Office before the Tax Court hears the case.



If you unreasonably fail to pursue the IRS' appeals system, or if your case is intended primarily to cause a delay, or your position is frivolous or groundless, the Tax Court may impose a penalty of up to \$25,000. See Appeal Within the IRS, earlier.

Recovering litigation or administrative costs. These are the expenses that you pay to defend your position to the IRS or the courts. You may be able to recover reasonable litigation or administrative costs if you are the prevailing party and if:

- You exhaust all administrative remedies within the IRS,
- Your net worth is below a certain limit (see *Net worth requirements*, later), and
- You do not unreasonably delay the proceeding.

Prevailing party. Generally, you are the prevailing party if :

- 1) You substantially prevail with respect to the amount in controversy or on the most significant tax issue or set of issues in question, and
- 2) You meet the net worth requirements, discussed later.

You will not be treated as the prevailing party if the United States establishes that its position was substantially justified. The position of the United States is presumed not to be substantially justified if the IRS did not follow its applicable published guidance (such as regulations and revenue rulings) in the administrative proceeding. This presumption can be overcome by evidence.

The court will generally decide who is the prevailing party.

Reasonable litigation and administrative costs. These costs generally include the following:

- 1) Both litigation and administrative costs. These include:
 - a) The costs of studies, analyses, engineering reports, tests, or projects that were agreed to be necessary for the preparation of your case, and
 - b) Attorney fees that generally may not exceed \$110 per hour. For calendar years beginning after 1996, the hourly rate is indexed for inflation.
- 2) Litigation only. These costs include:
 - a) Reasonable amounts for court costs, and
 - b) Expenses of expert witnesses.
- 3) Administrative only. These costs include:
 - Any administrative fees, or
 - Similar charges imposed by the IRS.

Net worth requirements. An individual taxpayer may be able to recover litigation or administrative costs when certain requirements are met:

- For individual and estate taxpayers — your net worth must not exceed \$2 million as of the filing date of your petition for review. For this purpose, individuals filing a joint return shall be treated as one taxpayer, except in the case of an innocent spouse relieved of liability (See discussion on *Innocent Spouse Exception*, later).
- For charities and certain cooperatives — you must not have more than 500 employees as of the filing date of your petition for review.

- For all other taxpayers — your net worth must not exceed \$7 million, and you must not have more than 500 employees as of the filing date of your petition for review.

Tax Court

You can take your case to the United States Tax Court if you disagree with the IRS over:

- Income tax,
- Estate tax,
- Gift tax, or
- Certain excise taxes of private foundations, public charities, qualified pension and other retirement plans, or real estate investment trusts.

To take your case to the Tax Court, the IRS must first send you a notice of deficiency. Then, you can only appeal your case if you file a petition within 90 days from the date this notice is mailed to you (150 days if it is addressed to you outside the United States).

Note. If you consent, the IRS can withdraw any notice of deficiency. Once withdrawn, the limits on credits, refunds, and assessments concerning the notice are void, and you and the IRS have the rights and obligations that you had before the notice was issued. The suspension of any time limitation while the notice of deficiency was issued will not change when the notice is withdrawn.



After the notice is withdrawn, you cannot file a petition with the Tax Court based on the notice. Also, the IRS can later issue a notice of deficiency in a greater or lesser amount than the amount in the withdrawn deficiency.

Generally, the Tax Court hears cases before any tax has been assessed and paid; however, you can pay the tax after the notice of deficiency has been issued and still petition the Tax Court for review. If you do not file your petition on time, we will assess the proposed tax. We will send you a bill and you cannot take your case to the Tax Court. Under the law, you must pay the tax within 10 days. After 10 days, the tax is subject to immediate collection. This collection can proceed even if you think that the amount is excessive. Publication 594, *Understanding the Collection Process*, explains our collection procedures.

If you filed your petition on time, the Court will schedule your case for trial at a location convenient to you. You can represent yourself before the Tax Court or you can be represented by anyone admitted to practice before that Court.

Small case procedure. If the amount in your case is \$10,000 or less for any one tax year or period, the Tax Court has a simple alternative to solve your case. At your request and if the Tax Court approves, your case can be handled under the “small tax case

procedures.” In this procedure, you can present your case to the Tax Court for a decision that is final and you cannot appeal. You can get more information regarding the small tax case procedures and other Tax Court matters from the United States Tax Court, 400 Second Street, N.W., Washington, DC 20217.

District Court and Court of Federal Claims

Generally, the District Court and the Court of Federal Claims hear tax cases only after you have paid the tax and filed a claim for a credit or refund. As explained next under *Claims for Refund*, you can file a claim for a credit or refund if you think that the tax you paid is incorrect or excessive. If we reject your claim, we will inform you unless you signed a Form 2297, *Waiver of Statutory Notification of Claim Disallowance*. If we have not acted on your claim within 6 months from the date you filed it, you can then file suit for a refund. You must file suit for a credit or refund no later than 2 years after we inform you that we have rejected your claim or you file Form 2297.

You can file suit for a credit or refund in your United States District Court or in the United States Court of Federal Claims. However, you cannot appeal to the United States Court of Federal Claims if your claim is for credit or refund of a penalty that relates to promoting an abusive tax shelter or to aiding and abetting the understatement of tax liability on someone else's return.

For information about procedures for filing suit in either court, contact the Clerk of your District Court or of the United States Court of Federal Claims.

Claims for Refund

Once you have paid your tax, you have the right to file a claim for a credit or refund if you believe the tax is too much. You can claim a credit or refund by filing Form 1040X, *Amended U.S. Individual Income Tax Return*.

File your claim by mailing it to the Internal Revenue Service Center where you filed your original return. File a separate form for each year or period involved. Include an explanation of each item of income, deduction, or credit on which you are basing your claim.

Corporations should file Form 1120X, *Amended U.S. Corporation Income Tax Return*, or other form appropriate to the type of credit or refund claimed.

Requesting a copy of your tax return. You can obtain a copy of an earlier year tax return from the IRS. Use Form 4506, *Request for Copy or Transcript of Tax Form*, from your local IRS district office, or call 1-800-829-3676 (1-800-TAX-FORM). You will be charged a fee, which you must pay when you submit Form 4506.

Requesting a copy of your tax account. You can also obtain a free copy of the tax account (a transcript) for your individual income tax return. To get your transcript, call or write to your local Internal Revenue Service office. You cannot get this information by calling the toll-free number given above. The transcript will give you the following information:

- Type of return filed,
- Marital status,
- Tax shown on return,
- Adjusted gross income,
- Taxable income,
- Self-employment tax, and
- Number of exemptions.

Time for Filing a Claim for Refund

You must file a claim for a credit or refund within 3 years from the date you filed your original return or 2 years from the date you paid the tax, whichever is later. If you do not file a claim within this period, you may no longer be entitled to a credit or a refund.

If the due date to file a return or a claim for a credit or refund is a Saturday, Sunday, or legal holiday, it is filed on time if it is filed on the next business day. Returns you filed before the due date are considered filed on the due date. This is true even when the due date is a Saturday, Sunday, or legal holiday.

Limit on Amount of Refund

If you file your claim within 3 years after filing your return, the credit or refund cannot be more than the part of the tax paid within the 3 years (plus any extension of time for filing your return) before you filed the claim.

Example 1. You made estimated tax payments of \$500 and got an automatic extension of time to August 15, 1996, to file your 1995 income tax return. When you filed your return on that date, you paid an additional \$200 tax. Three years later, on August 15, 1999, you file an amended return and claim a refund of \$700. Because you filed within the 3 years plus the 4-month extension period, you could get a refund of \$700.

Example 2. The situation is the same as in Example 1, except that you filed your return on October 31, 1996, 2½ months after the extension period ended. You paid an additional \$200 on that date. Three years later, on October 25, 1999, you file an amended return and claim a refund of \$700. Although you filed your claim within 3 years from the date you filed your original return, the refund is limited to \$200. The estimated tax of \$500 was paid before the 3 years plus the 4-month extension period.

Claim filed after the 3-year period.

If you file a claim after the 3-year period, but within 2 years from the time you paid the tax, the credit or refund cannot be more than the tax you paid within the 2 years immediately before you filed the claim.

Example. You filed your 1995 tax return on April 15, 1996. You paid \$500 in tax. On November 3, 1997, after an examination of your 1995 return, you had to pay \$200 in additional tax. On May 2, 1999, you file a claim for a refund of \$300. Your refund will be limited to the \$200 you paid during the 2 years immediately before you filed your claim.

Exceptions for Special Refunds

If you file a claim for refund based on one of the items listed below, the limits discussed earlier (under *Time for Filing a Claim for Refund*) may not apply. These special items are:

- A bad debt,
- A worthless security,
- A payment or accrual of foreign tax,
- A net operating loss carryback, or
- A carryback of certain tax credits.

The limits discussed earlier also may not apply if you have signed an agreement to extend the period of assessment of tax.

Processing Claims for Refund

Claims are usually processed shortly after they are filed. Your claim may be accepted as filed or it may be examined. If a claim is examined, the procedures are the same as in the examination of a tax return.

However, if you are filing a claim for credit or refund based only on contested income tax or on estate tax or gift tax issues considered in previously examined returns and do not want to appeal within the IRS, you should request in writing that the claim be immediately rejected. A notice of claim disallowance will then be promptly sent to you. You have 2 years from the date of mailing of the notice of disallowance to file a refund suit in the United States District Court or in the United States Court of Federal Claims.

Reduced Refund

Your refund may be reduced by an additional tax liability.

Also, your refund may be reduced by amounts you owe for past-due child support or by debts you owe to another federal agency. We will notify you if this happens. For those reductions, you cannot use the appeal and refund procedures discussed in this publication, but you may be able to take action against the other agency.

Innocent spouse exception. Under certain circumstances, you may not have to pay the tax, interest, and penalties on a joint return. You must establish that you did not know, and had no reason to know, that there was a substantial understatement of tax because your spouse did not report income or claimed a deduction, credit, or property basis in an amount for which there is no basis in fact or law.

The facts and circumstances must also indicate that it is unfair for you to pay the tax due. One consideration is whether you significantly benefited from the understatement. Normal support is not a significant benefit. Another consideration may be whether you were later divorced or deserted by your spouse.

For more information, see Chapter 2 of Publication 17, *Your Federal Income Tax*.

New Tax Provisions

The following is a list of the provisions which will be covered in the 1998 revision of Publication 556.

Taxpayer Relief Act of 1997

- Abatement of interest for those in disaster areas.
- Period for filing claims for refunds.
- Time for filing for award and appealing denial of administrative costs.
- Appeal of Tax Court overpayment determinations.
- Use of motion to seek redetermination of interest.
- Situations in which Tax Court can determine employment status.

For discussions of these topics, get Publication 553, *Highlights of 1997 Tax Changes*.

IRS Restructuring and Reform Act of 1998

- Changes to burden of proof in court proceedings.
- Expansion of authority to award costs and certain fees.
- Increase in size of cases permitted on small case calendar.
- Refund for estates electing the installment method of payment.
- Relief from joint and several liability on a joint return.
- Suspension of statute of limitations on refund claims during periods of disability.
- Suspension of interest and penalties where the IRS fails to contact the taxpayer.
- Specification of deadline for filing Tax Court petition on notice of deficiency.
- Refund or credit of overpayments before final determination.
- Early referrals to the Office of Appeals.
- Prohibition on requests to taxpayers to give up rights to bring civil action.
- Clarification of taxpayer's right to be represented by any person authorized to practice before the IRS.
- Clarification of taxpayer's right to suspend an interview with the IRS.
- Disclosure of criteria for examination selection.
- Explanation of any claim for refund disallowance.
- Offset of past-due State income tax obligations against overpayments.
- Elimination of interest differential on overlapping periods of interest on overpayments and underpayments.
- Uniform application of confidentiality privilege to taxpayer communications with federally authorized practitioners.