CLIENT ALERT

What You Need to Know About Congress's Role in Refund Claims

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Taxpayers are often surprised to learn that Congress has a role in reviewing large refunds claims that are otherwise handled by the Internal Revenue Service (IRS), or for settlements of tax litigation, by the IRS Chief Counsel or Department of Justice (DOJ).

The Joint Committee on Taxation recently released a report, “TAX REFUND CLAIMS: An Overview of the Joint Committee on Taxation's Review Process.”[1][1] Accordingly, it is a good time for a short primer on the Joint Committee's role in refund claims and litigation settlements. This information is relevant for taxpayers seeking a refund or credit in excess of $2 million (or $5 million for corporations) on an amended return, during an audit, or when settling a case in litigation.

What is the Joint Committee?

The Joint Committee is a nonpartisan committee of both houses of Congress. It has 10 members—five members from the Senate Finance Committee (three from the majority and two from the minority) and five members from the House Ways and Means Committee (three from the majority and two from the minority). The Joint Committee employs a full-time staff of economists, attorneys, and accountants. There is a separate group within the Joint Committee staff to handle review of refund claims. In the past, this group consisted largely of ex-IRS or Appeals personnel, although there are some reports that the makeup of the staff has expanded to include others.

What types of cases have to go to the Joint Committee?

Under Section 6405 of the Code, any case in which the government will pay a refund of more than $2 million ($5 million for C corporations) has to be reviewed by the Joint Committee. The $2 million ($5 million for C corporations) threshold is referred to as the “jurisdictional amount.”

Specifically, the Joint Committee has review over all cases meeting the jurisdiction requirement that involve a “refund or credit of any income, war profit, excess profits, estate, or gift tax, or any tax imposed with respect to public charities, private foundations, operators' trust funds, pension plans, or real estate investment trusts under chapter 41, 42, 43, or 44.”[2][2] Additionally, the Joint Committee has review over cases involving tentative carryback adjustments under Section 6411 that exceed $2 million ($5 million for C corporations).[3][3] The tentative allowances are refunded before reporting to the Joint Committee, but they are still subject to Joint Committee review.[4][4]

Taxes not subject to the Joint Committee's review include employment taxes, trust fund recovery penalty cases, windfall profit taxes, and certain excise taxes.[5][5] The IRS does not need to report to the Joint Committee a refund or credit of estimated or withheld income tax that is made without examination.[6][6] Additionally, the IRS does not need to report any refunds resulting from court order after a trial (as opposed to cases settled in court).[7][7]

What is included in the jurisdictional amount?

As discussed above, the Joint Committee has jurisdiction over the above matters, if they involve a refund or credit of more than $2 million ($5 million for C corporations). The jurisdictional amount includes the underlying tax, any refund of penalties paid, and previously assessed and paid interest to be refunded.[8][8]

The $2 million ($5 million for C corporations) threshold is not per year, but per refund.[9][9] For example, if the IRS agrees to a refund of $1.2 million for tax year 2016 and $900,000 in year 2017, the case has to go the Joint Committee. But any prior refunds already made before the current examination cycle are not considered.[10][10]

Deficiencies only offset the jurisdictional amount when the deficiency and the refund are for the same tax entity, for the same category of tax, and in the same examination cycle.[11][11]

How does the IRS prepare cases for review by the Joint Committee?

The IRS has a specialized team within its Large Business and International Division that reviews and prepares a report for each proposed refund submitted to the Joint Committee. The IRS's Joint Committee Review (IRS-JCR) team reviews the case file for procedural, computational, and technical accuracy and prepares the report.[12][12] Depending on its review, the IRS-JCR team may return the case to exam (*e.g.*, if there is a substantial error or corrections favorable to the taxpayer).[13][13]

Once the IRS-JCR team completes its review, it prepares a Joint Committee report, which generally includes (1) taxpayer information including history and related parties, (2) proposed refunds and deficiencies, (3) reason for the refund, (4) calculation spreadsheets, (5) prior examination history and current examination activity of the refunds, and (6) information on statutes of limitations for each refund and source year.[14][14]

The IRS-JCR team will send a letter notifying the taxpayer that the case has been submitted to the Joint Committee.[15][15] The taxpayer does not submit anything to the Joint Committee or formally participate in the preparation of the report. However, taxpayers are not precluded from contacting the Joint Committee staff in appropriate circumstances.

What happens during the Joint Committee review?

After the Joint Committee receives the report, its staff attorneys review the report and other IRS-JCR documentation as necessary. If the Joint Committee staff attorneys have questions for the IRS, they are usually resolved informally (phone calls or emails).[16][16]Alternatively, the staff attorneys may send a written inquiry to the IRS.[17][17] There are some reports that the Joint Committee staff is asking more questions of IRS-JCR than in the past, although this is difficult to verify. The IRS-JCR will handle the staff's request. Occasionally, the IRS-JCR will have the Joint Committee staff attorney directly contact the Exam or Appeals team.[18][18]

The Joint Committee focuses its review on the technical aspects of the IRS's analysis. In the report released this month, the Joint Committee said it is particularly concerned with cases "where taxpayers claim tax benefits that do not appear to have been intended by the relevant statute."[19][19]

If the Joint Committee agrees with the IRS's position, it will issue a clearance letter and the case will be returned to the IRS.[20][20] The IRS will then issue the refund.[21][21]

If the Joint Committee disagrees with the IRS's position, the Joint Committee will issue a Staff Review Memorandum, which outlines the areas where the Joint Committee disagrees with the IRS's position and recommends a different outcome. The IRS and DOJ are not required to accept the Joint Committee's recommendation. However, it is IRS's general policy to not process a refund until the dispute is resolved.[22][22]

How long does the Joint Committee have to review the report?

Technically, the IRS only has to give the Joint Committee 30 days to review the report.[23][23] If the Joint Committee does not object within those 30 days, the IRS can issue the refund or credit.[24][24] However, it is IRS policy to wait until the Joint Committee finishes its review.[25][25] The Department of Justice, which similarly must submit any proposal settlements with qualifying refunds, states that it will not authorize a refund until the Joint Committee has advised whether it has any adverse criticism to the settlement.[26][26]

In our experience, there are significant delays involved in completing a settlement with Exam or Appeals when the case will require Joint Committee review. Most of this delay is while the case is before the IRS or Appeals, rather than when the case is before the Joint Committee. This is because of the additional documentation and levels of review that must occur before the case is even forwarded to the Joint Committee.

When the Joint Committee Chief of Staff, Thomas Barthold, spoke at Crowell & Moring's Tax Seminar in September 2016, he stated that more than 85 percent of Joint Committee cases are closed within 45 days of receipt by the Joint Committee staff.

Bottom line

If you have a refund claim subject to the review of the Joint Committee, the IRS or DOJ personnel negotiating the settlement will need to complete additional layers of documentation and review, which can significantly delay completion of the settlement. To prevent further delay, respond promptly to any IRS requests for information while the IRS is preparing the Joint committee report or while the Joint Committee is reviewing the report.

Taxpayers should offer to work with the IRS to develop a Joint Committee report that fully explains that the refund is technically proper and that it is consistent with Congressional intent.

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[1] Staff of the J. Comm. on Taxation, 115th Cong., TAX REFUND CLAIMS: An Overview of the Joint Committee on Taxation's Review Process (Comm. Print 2019), *available here*.

[2] I.R.C. § 6405(a).

[3] I.R.C. § 6405(b).

[4] IRM § 4.36.2.2(1).

[5] IRM § 4.36.2.3.

[6] IRM § 4.36.2.3.

[7] IRM § 4.36.2.3.

[8] IRM § 4.36.2.4.1.

[9] IRM § 4.36.2.4(3).

[10] IRM § 4.36.2.4(6).

[11] IRM § 4.36.2.4.2(1).

[12] IRM § 4.36.4.1(1).

[13] IRM § 4.36.4.2(2).

[14] IRM § 4.36.5.

[15] IRM § 4.36.4.6.1.

[16] IRM § 4.36.1.4(4).

[17] IRM § 4.36.1.4(4).

[18] IRM § 4.36.3.9(3).

[19] TAX REFUND CLAIMS: An Overview of the Joint Committee on Taxation's Review Process, at 12.

[20] IRM § 4.36.1.4(4).

[21] IRM § 4.36.1.4(4).

[22] IRM § 4.36.1.4(4).

[23] I.R.C. § 6405(a).

[24] I.R.C. § 6405(a).

[25] IRM § 4.36.1.4(4).

[26] Department of Justice Tax Division, Settlement Reference Manual, at 17 (Rev. Sept. 2012), *available here*.

For more information, please contact the professional(s) listed below, or your regular Crowell & Moring contact.

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