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From:
Sent: Monday, April 27, 2009 10:35:20 AM
To:
Cc:
Subject: FW: Underpayment vs. Understatement

I need to partially amend my prior advice on this topic. I previously advised that if (1) a spouse did not raise IS relief during the audit, (2) agreed to the liability by signing a Form 870-AD or other waiver, or by filing a joint amended return including the items, but did not pay the tax, (3) the Service assessed and attempted to collect and then (4) the spouse raised IS relief; then the Service should only consider relief under section 6015(f) as the liability should be classified as an underpayment. After further consideration of this issue, only the filing of a joint amended return including the items would result in an underpayment. Agreeing to the liability on a Form 870, a Form 4549, Income Tax Examination Changes, or similar forms would result in the liability being an understatement for purposes of section 6015.

This is because signing a waiver is not equivalent to filing an amended return. IRM 4.10.8.13.5.1d. provides as follows:

> A Form 870 signed by taxpayers, husband and wife, is not a return under IRC section 6020(a) and it is not an election to file a joint return under IRC section 6013. This holding also applies to Form 1902, Report of Individual Income Tax Audit Changes (obsoleted 1988), and Form 4549, Income Tax Examination Changes, and any successor forms to these forms, because these documents do not purport to be returns and do not contain a "jurat" with a penalties of perjury clause.

Support for the language in the IRM is found in Rev. Rul. 2005-59. Although the facts of situation 3 of the ruling are that no original return was filed and the H&W signed the Form 870 before section 6020(b) returns were prepared, the conclusion - that signing a Form 870 does not meet the Beard test - would also apply when a joint original return was filed and that return was under examination.

Furthermore, there is case law that supports the conclusion that signing a Form 4549 is not the equivalent of signing and filing a joint amended return and thus the liability should be treated as an understatement for purposes of section 6015. In Haltom v. Commissioner, T.C. Memo. 2005-209, the Service audited the original return (which excluded embezzlement income) and the spouses executed a Form 4549-CG, agreeing to the total deficiency and consenting to immediate assessment (and not paying). The

parties and the court agreed that section 6015(b) was applicable and that the return contained an understatement attributable to the erroneous item of the NRS. Section 6015(b)(1)(B) provides that if "on such return there is an understatement of tax" and the only "return" filed in the waiver situation is the original return (while in the amended return situation there is "an income tax liability that was properly reported but not paid." See Rev. Proc. 2003-61, section 4.03(2)(a)(iii)(A)). Compare with Billings v. Commissioner, T.C. Memo. 2007-234, where the court confirmed that a liability resulting from the inclusion on a joint amended return of embezzlement income excluded from the original joint return resulted in an underpayment not an understatement and that the spouse was entitled to only be considered for relief under section 6015(f). (Note, however, that we disagree with the court's conclusion in Billings that the spouse's knowledge of whether the NRS would pay the tax is judged at the time of filing the original return. We think such knowledge should be tested at the time the return reporting the unpaid tax – the amended return in this situation – was filed.

Please let me know if you have any questions and I apologize for any confusion on this matter.