

### **Nice Work: Taxpayer Wins a Fee Award in a Payroll Tax Dispute.**

To help taxpayers vindicate their rights in a dispute with the IRS, Section 7430 of the Internal Revenue Code authorizes an award of attorneys' fees and costs (such as fees paid to experts) if the taxpayer is a prevailing party. I.R.C. § 7430(a). To qualify, the taxpayer must exhaust his administrative remedies. I.R.C. § 7430(b). There are also limitations on the amount recoverable and the availability of an award for those whose net worth exceeds statutory limits.

Fees are not available, however, if "the position of the United States" in the dispute is "substantially justified." I.R.C. 7430(c)(4)(B). Since the taxpayer must exhaust administrative remedies by pursuing an administrative appeal to obtain a fee award, you would expect that process to weed out most cases where the government's position is shaky. Yet in a recent case from the Southern District of Illinois, an individual who was assessed with liability for trust fund taxes under Section 6672 prevailed on the merits and was awarded fees, *Tarpoff v. United States*, 2012 U.S. Dist. LEXIS 85065 (S.D. Ill. June 20, 2012).

The defendant in *Tarpoff* was the head cattle buyer for a slaughterhouse and beef-packing company known as Gateway Beef. When Gateway failed to pay its withholding taxes, the IRS assessed Mr. Tarpoff under Section 6672. After contesting the assessment administratively, Mr. Tarpoff brought a refund action, prevailing after a three day jury trial. 2012 U.S. Dist. LEXIS 85065, slip op. at \*2-\*3. Mr. Tarpoff then sought to recover attorneys' fees.

As the court notes in *Tarpoff*, a losing position can be substantially justified, so long as it has a reasonable basis in law and fact. 2012 U.S. Dist. LEXIS 85065, slip op. at \*10 (citations omitted). Section 7430(c)(7) of the Code defines "position of the United States" in terms of the position that it formally adopts in judicial proceedings, and as the position adopted by the IRS either at the time a notice of deficiency is issued or the date the taxpayer is notified of a decision by the IRS Office of Appeals. I.R.C. § 7430(c)(7)(A), (B). As a consequence, the district court focused its substantial justification analysis on two key phases of Mr. Tarpoff's dispute with the IRS: first, it examined the basis for the position adopted by the Office of Appeals; then it examined the basis for the government's position at the time it filed an answer to Mr. Tarpoff's refund claim. 2012 U.S. Dist. LEXIS 85065, slip op. at \*9. At both phases, the government's case came up short.

The decision of the appeals office had simply rested upon a determination of an individual revenue officer who had focused upon the fact that Tarpoff appeared to have authority to sign checks; Mr. Tarpoff contended that the revenue officer had a grudge against him. The district court did not address the revenue officer's motives, but did note that her conclusions that Mr. Tarpoff was responsible for payroll taxes were contradicted by documentary evidence and an affidavit that he had provided. 2012 U.S. Dist. LEXIS 85065, slip op. at \*15-\*25. The administrative record also included evidence that Mr. Brach, Gateway's owner, had sole authority to determine which bills would be paid; an affidavit from the company's office manager stated that Brach had decided not to pay the taxes that had been withheld. *Id.* at \*26-\*29. Against this background, the district court concluded that the government's position in administrative proceedings was not substantially justified, given its failure to investigate further after receiving evidence that contradicted the revenue officer's findings. *Id.* at \*29-\*34.

By the time the government filed its answer to the complaint, it had developed no additional evidence that would support Mr. Tarpoff's liability, and had received additional exculpatory

evidence from a corporate official who informed the government that Tarpoff was not responsible for payroll taxes. *Id.* at \*34-\*36. As a consequence, its position was not substantially justified.

The result in *Tarpoff* reflects skillful lawyering: the time spent to develop documentary evidence and obtain independent testimony plainly paid off in both Mr. Tarpoff's success in defending the claim under Section 6672 of the Code and in recovering a portion of his attorneys' fees.

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