

Can You Get Tax Advice On Contingency?

By Robert W. Wood

Contingent legal fees are the norm in personal injury cases. Increasingly, they are the norm in employment lawsuits too. Indeed, the types of cases in which contingent fees are common is expanding widely. These days, even large law firms handle some cases on contingency.

So, can you charge contingent fees in tax matters? It should not be surprising that clients ask for this. Why *wouldn't* a client want legal or accounting fees tied directly to the tax result we can obtain for them? As with so many tax questions, the answer is it depends.

You may have received a flyer in the mail from a company that says it will lower your property tax bill. Pay nothing up front, just a percentage of the tax savings. Against this background, it may sound almost un-American to ask what contingent fees are *allowed* in the tax arena. Allowed by whom?

The IRS has pushed hard to regulate in this area. The IRS has the authority to regulate the practice of taxpayer representatives before the IRS. In regulations known as Circular 230, the IRS says that a practitioner cannot charge a contingent fee for services rendered in connection with *any* matter before the IRS. But Circular 230 has three exceptions:

1. A contingent fee can be charged in connection with an IRS audit or challenge to (a) an original tax return; or (b) an amended tax return or refund claim if it was filed within 120 days of the taxpayer receiving a written notice of the examination of, or a written challenge to the original tax return.
2. A contingent fee can be charged in connection with a refund claim filed for penalties or interest assessed by the IRS.
3. A contingent fee can be charged in connection with any judicial proceeding arising under the Internal Revenue Code.

If you want to keep the IRS happiest, abide by these rules. However, in *Ridgely v. Lew*, 55 F. Supp. 3d 89 (D.D.C. 2014), a federal district court held that the IRS had overstepped some of its authority. It is unclear where this leaves contingent fees, but the IRS still thinks it is right in its three exceptions above. How do they apply in practice?

Abe. The IRS notifies Abe that he owes \$1 million in tax. Abe wants you to negotiate an offer in compromise for him for less. He offers you a fee equal to 30 percent of any tax savings you can achieve for him. Can you do it?

Sure, provided that your services are rendered in connection with IRS action on Abe's original return or an amended return. Most likely, the \$1 million tax liability grows out of an IRS exam/challenge to a filed return. If not, presumably the offer in compromise will not move forward without bringing the relevant tax issues to the IRS's attention, which could trigger some kind of examination or challenge. What if the liability is already established, and this is just a collection matter? Here, too, a contingent fee would seem to be okay.

Billy. Billy tells you he wants to sue the IRS for a refund. He wants you to handle it on a contingent fee basis. He filed his 2015 return reporting ordinary income on a big contract disposition. Later, he filed an amended 2015 return, claiming that it was capital gain. He didn't get his refund, and now he wants to sue. Can you do it for a contingent fee? Yes. Billy is suing, so you will be rendering services in connection with a judicial proceeding.

Billy # 2. What if Billy comes to you *before* he files his amended return for 2015? With this timing change, can you represent him for a contingent fee? At least partially, yes. If the matter goes to court, you can charge a contingent fee for your services. If the matter stays *out* of court, the IRS says you cannot charge a contingent fee for services rendered in connection with the preparation of an amended return — only in connection with an IRS *examination of, or challenge to*, the amended return.

This is where the *Ridgely* case could come in. Under *Ridgely*, preparing an amended tax return, by itself, is not *practice* before the IRS. *Ridgely* suggests that the IRS can't regulate this, so you should be OK here too.

Cathy. Cathy filed her 2014 return, and was promptly audited by the IRS. She received a notice of deficiency (also called a 90 day letter) and wants to file in Tax Court. There is \$1 million in dispute, but she wants you to handle it for a contingent fee. She proposes to pay you 30 percent of any money you save her. So, if the \$1 million tax bill sticks, you earn no fee. If you eliminate the entire \$1 million in additional tax, you earn \$300,000. Can you do this?

Yes. There is no need to invoke *Ridgely* here. The contingent fee is permitted because your services *will* be rendered in connection with the IRS's challenge to Cathy's original return. The contingent fee is also permitted because your services will be rendered in connection with a judicial proceeding. Even so, the IRS also says you cannot not charge an unconscionable fee. Surely 30 percent is not unconscionable, but that might depend on the case and the issues.

Dennis. Dennis's 2013 tax return was audited. His accountant represented him, but eventually, the IRS issued a 30-day letter (Notice of Proposed Adjustment). IRS proposes additional taxes of \$1 million. Dennis asks you to represent him in a protest and thereafter at IRS Appeals on a contingent fee basis. He offers you 50 percent of all the money you save him. Can you do it?

Yes. Once again, the contingent fee should be permitted because you are being engaged in connection with the IRS's challenge to Dennis's original return. However, is a 50 percent contingent fee unconscionable these days?

Conclusion

Tax advice and tax representation for contingent fees are becoming more common, but they still are the exception, not the norm. One place where they may be especially useful is where the taxpayer is trying to get back money from the IRS in a lawsuit. That context may lend itself to contingent fees. But in all of these settings, just be aware that the IRS has views about what is permitted.

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