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# An empirical investigation to detect the presence of confirmation bias in the decision-making strategies used by litigants in tax court memorandum cases

Mary M. Anderson  
*Louisiana Tech University*

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AN EMPIRICAL INVESTIGATION TO DETECT THE  
PRESENCE OF CONFIRMATION BIAS IN THE  
DECISION-MAKING STRATEGIES USED  
BY LITIGANTS IN TAX COURT  
MEMORANDUM CASES

By

Mary M. Anderson, MPA, BSBA

A Dissertation Presented in Partial Fulfillment  
Of the Requirements for the Degree  
Doctor of Business Administration

COLLEGE OF ADMINISTRATION AND BUSINESS  
LOUISIANA TECH UNIVERSITY

August 2005

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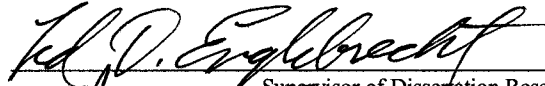
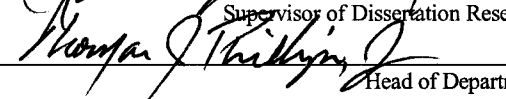
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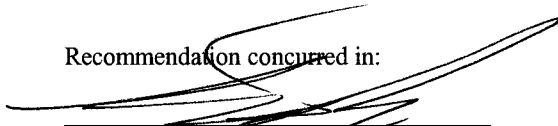
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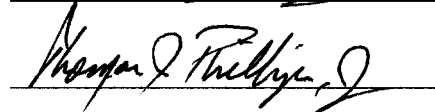
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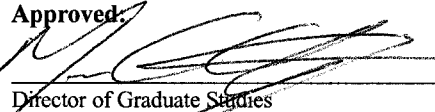
  
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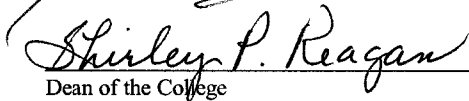
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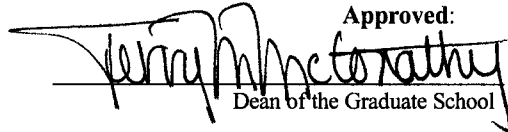




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## ABSTRACT

Normative decision theory describes the judgment and decision-making process as a cost/benefit analysis based upon maximum utility. One assumption of the theory is full rationality for choices made throughout the process. Due to bounded rationality, however, mental shortcuts become necessary. Use of these shortcuts does not necessarily diminish the quality of the decision. However, a suboptimal use of a heuristic results in a biased decision.

Kahneman and Tversky (1979) identify three basic heuristics: availability, representativeness, and anchoring and adjusting. One suboptimal use of the anchoring and adjusting heuristic, confirmation bias, is the unconscious search for and evaluation of information that confirms one's desired decision outcome while ignoring disconfirming information. In an adversarial legal contest, relying on biased research diminishes the probability of prevailing (Johnson 1993).

The intent of this research inquiry is to use archival data to test for the presence of confirmation bias in the defenses presented by the litigants in Tax Court Memorandum Opinions. The data sample consists of the briefs presented to the Court by both litigants, taxpayer and Internal Revenue Service, in 106 of the 288 rendered Memorandum Decisions in 2004.

Summary statistics from the data show that 51.85% of taxpayers represent themselves (i.e., pro se) in the contentious proceedings. The remaining taxpayers

employ tax professionals to provide the defense. The IRS has a contingent of legal counsel to present their position. Non-parametric statistical testing provides evidence that defenses presented by pro se taxpayers show more bias than defenses provided by tax professionals. In turn, taxpayers' professional representatives present more biased defenses than do the IRS professional representatives.

This research inquiry adds external validity to the extant literature on biased research recommendations resulting from the tax research task. That is, numerous identified incentives promote susceptibility to the use of confirmatory decision-making strategies. As shown in this study, incentives impact practitioners differently than government employees. Remedial measures, including education, task-specific experience, and accountability can reduce this proclivity. Pro se taxpayers, with no legal education, experience, or accountability, show a greater degree of bias in their defenses than do tax professionals.

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Author Mary M. Anderson  
Date August 10, 2005

## DEDICATION

In loving memory of my brother, Damian E. Morgan

In his eyes and tongue-in-cheek enjoyment of my inability  
to accept convention provided much inspiration then  
and wonderful, warm memories now.



## TABLE OF CONTENTS

DEDICATION .....	iv
LIST OF TABLES .....	x
LIST OF FIGURES .....	xiii
ACKNOWLEDGMENTS .....	xiv
CHAPTER 1 INTRODUCTION.....	1
Background.....	3
Judgment and Decision-Making.....	3
Tax Professionals.....	6
Tax Administration.....	9
Research Questions .....	11
Organization of this Dissertation.....	13
CHAPTER 2 LITERATURE REVIEW .....	15
Incentives Research .....	17
Individual Psychological Factors .....	17
Cognitive Factors.....	17
Experience .....	17
Task-Specific Experience.....	21
Knowledge.....	22
Education.....	23
Problem-Solving Ability .....	24
Affective Factors .....	25
Advocacy.....	26
Risk Perceptions .....	27
Ethics .....	28
Professional Status and Firm Size .....	29
Environmental Factors.....	33
Internal Revenue Service.....	33
Audit.....	33
Penalties.....	35
Client Characteristics.....	35
Tax Payment.....	36
Risk Preference.....	37

Client Status.....	39
Ambiguity.....	41
Substantial Authority.....	46
Compliance v. Planning.....	47
Confirmation Bias Research.....	51
Summary.....	56
CHAPTER 3 METHODOLOGY .....	58
Hypothesis Development.....	59
Data.....	61
Subjects.....	61
Random Sampling .....	63
Study Instruments .....	64
Court Briefs .....	64
Court Opinion.....	65
Dependant Variable .....	66
Instances of Confirmation Bias .....	66
Independent Variables .....	68
Litigants.....	68
Professional Status.....	69
Monetary Incentives .....	69
Statistical Methodology.....	72
Hypothesis 1 .....	72
Hypotheses 2 through 6 .....	73
Hypothesis 7 .....	73
Model Assumptions.....	73
Summary.....	74
CHAPTER 4 EMPIRICAL FINDINGS.....	76
Input Data .....	77
Instances of Confirmation Bias .....	79
Testing the Assumptions .....	85
Independence Assumption.....	86
Normality Assumption .....	86
Constant Variance Assumption .....	88
Hypotheses Analysis .....	90
Hypothesis 1 .....	90
Hypothesis 2 .....	91
Hypothesis 3 .....	93
Hypothesis 4 .....	94
Hypothesis 5 .....	95
Hypothesis 6 .....	96
Hypothesis 7 .....	97
Summary.....	99

CHAPTER 5 SUMMARY AND CONCLUSIONS.....	100
Summary of the Empirical Findings.....	101
Implications of the Findings.....	104
Contributions of this Study.....	106
Limitations of the Study .....	107
Opportunities for Future Research .....	108
APPENDIX A CASE LISTING.....	110
APPENDIX B SAMPLE BRIEFS AND OPINIONS.....	115
APPENDIX C DATA COLLECTION INSTRUMENT.....	149
REFERENCES .....	152

## LIST OF TABLES

TABLE 2.1 .....	16
Factors Tested for Association with Tax Accountants' Judgment/ Decision-Making	
TABLE 2.2 .....	31
Summary of Literature on the Impact of Individual Psychological Factors on Judgment/Decision-Making in Tax Research	
TABLE 2.3 .....	42
Summary of Literature on the Impact of Environmental Factors on Judgment/Decision-Making in Tax Research	
TABLE 2.4 .....	49
Summary of Literature on the Impact of Task Input Factors on Judgment/Decision-Making in Tax Research	
TABLE 2.5 .....	50
Summary of Literature on the Impact of Task Output Factors on Judgment/Decision-Making in Tax Research	
TABLE 2.6 .....	56
Summary of Literature on Confirmation Bias' Presence in Judgment/Decision-Making in Tax Research	
TABLE 3.1 .....	70
Monetary Assessment Rankings	
TABLE 3.2 .....	71
List of Variables	
TABLE 4.1 .....	78
Profession of Litigants	
TABLE 4.2 .....	79
Prevailing Party by Litigant and Profession (Percentage by Litigant Class) (Percentage by Cases)	

TABLE 4.3 .....	80
Measurement of Confirmation Bias Dependent Variable CB(L)	
TABLE 4.4 .....	81
Measurement of Confirmation Bias Dependent Variable CB(J)	
TABLE 4.5 .....	82
Frequency of Instances of Confirmation Bias	
TABLE 4.6 .....	85
Instances of Confirmation Bias Descriptive Statistics by Profession of Litigant Descriptive Statistics by Win/Lose	
TABLE 4.7 .....	88
Normality Tests on Dependent Variables	
TABLE 4.8 .....	89
Constant Variance Test on Dependent Variables	
TABLE 4.9 .....	91
T-test of Confirmation Bias Variables by Class of Litigants	
TABLE 4.10 .....	92
Hypothesis 2: Confirmation Bias – Pro se v. Professional Representatives Descriptive Statistics	
TABLE 4.11 .....	94
Hypothesis 3: Confirmation Bias – Taxpayer’s Lawyers v. IRS Lawyers Descriptive Statistics	
TABLE 4.12 .....	95
Hypothesis 4: Confirmation Bias – Martindale-Hubbell Non-Rated Lawyers v. Martindale-Hubbell Rated Lawyers Descriptive Statistics	
TABLE 4.13 .....	96
Hypothesis 5: Confirmation Bias – Martindale-Hubbell “A” Rated Lawyers v. Martindale-Hubbell “B” Rated Lawyers Descriptive Statistics	
TABLE 4.14 .....	97
Hypothesis 6: Confirmation Bias – Martindale-Hubbell Non-Rated Taxpayer Lawyers v. Martindale-Hubbell Non-Rated IRS Lawyers Descriptive Statistics	

TABLE 4.15 ..... 98  
Correlation Coefficients – Monetary Incentive to Litigants

## LIST OF FIGURES

FIGURE 2.1.....	20
Cognitive Model of Tax Research (Marchant et al. 1989)	
FIGURE 4.1.....	87
Normal Probability Plots of Dependent Variables	

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## CHAPTER 1

### INTRODUCTION

A code of professional ethics governs tax professionals, whether they are certified public accountants or attorneys. For certified public accountants, regulation is provided by the state legislatures. Regulatory power is delegated to state boards of accountancy by Uniform Accountancy Act Section 4(h)(4). As such, the American Institute of Certified Public Accountants (hereinafter referred to as AICPA) has adopted the *Code of Professional Conduct*<sup>1</sup> as a general standard. Additionally, the AICPA has adopted *Standards of Responsibility in Tax Practice* to delineate guidelines for tax practice. These guidelines set parameters for aggressive tax positions. Alternatively, the American Bar Association's *Model Rules of Professional Conduct* governs attorneys with regulation provided by states' supreme courts. For federal tax practice, tax professionals are also subject to the rules of the Internal Revenue Service (hereinafter referred to as IRS or Service) and the rules of the court where a matter is pending. In all instances, guidance is provided for the quality of services to be rendered to clients. Both professional codes mandate "unbiased" research as the foundation of the services provided by these professionals.

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<sup>1</sup> The Code of Professional Conduct of the American Institute of Certified Public Accountants, adopted by the membership to provide guidelines that govern the performance of professional responsibilities, consists of two parts: Principles and Rules. Interpretations of these Principles and Rules are adopted after an exposure period. Noncompliance with the standards ultimately leads to disciplinary actions where necessary.

In a simplistic definition, Webster (1997) defines "unbiased" research as a studious inquiry or examination aimed at the discovery and interpretation of new knowledge without prejudice. This process necessarily requires alternative choices. Normative economic theory stipulates that choice is based upon maximizing utility under a natural cost/benefit analysis. That is, under the same facts and circumstances, there is a rational and optimal choice. Early studies, however, have found that optimization in a cost/benefit context is representative of instinctive lower animal behavior; the human condition is characterized by violations of this normative model (Killeen 1978; Rachlin and Burkhard 1978; Staddon and Motheral 1978). Causes of this suboptimal behavior have led to identification of a plethora of human judgment biases, cognitive illusions, and deficiencies, resulting in biased judgment processes. Thus, "unbiased" research, as mandated by regulating authorities, is the ideal condition.

Biased decisions by tax professionals, as with all professionals, lead to refutable positions. Refutable positions, as the foundation of recommendations to clients or actions taken in another's behalf, as an employee, may result in undesirable consequences. Undesirable consequences run the gamut from challenges by taxing authorities to collapse of a business (e.g., Enron). Thus, unbiased decision-making, as the mandated foundation for professional judgment and decisions, is elemental to the effectiveness of professions and individual professionals. Education, experience, and accountability, in theory, mitigate the effect of biases. Thus, awareness of the presence of bias is necessary before causes can be isolated. At that point, steps necessary to mitigate susceptibility to cognitive illusions can be implemented. The

increasing incidence of legal claims against accountants in recent times mandated that the knowledge necessary to elicit unbiased professional decision-making be enhanced. The focus of this research inquiry is to examine the support presented by litigants in challenges by taxing authorities, under a set of stipulated facts, to ascertain if confirmation bias exists. By isolating the presence of this bias, a step toward enhancing unbiased tax research may be taken.

## Background

### Judgment and Decision-Making

Judgment is the process of estimating outcomes and related consequences (Libby 1981). Decision-making refers to the process of identifying and evaluation of consequences for alternative choices and actions. Preferences and judgments are the inputs into decision-making. The term "decision" denotes the choice made (Shields et al. 1995). Thus, judgment and decision-making (hereinafter referred to as JDM) processes involve the acquisition of knowledge. Knowledge is dynamic and continually evolving. This epistemic process (Heaton and Kruglanski 1991) involves two stages. The stages, hypothesis generation (information gathering) and hypothesis validation (information evaluation), are continually repeated until a decision is determined. Under the normative model, JDM is free of bias.

However, the same fact pattern using the same available information, which under normative theory has one outcome, can result in diametrically opposite and, seemingly, defensible positions. This is the result of different individuals making different choices during the epistemic process.

Among other assumptions, the normative economic theory of rational choice implies full rationality. In Herbert Simon's seminal work (1983), Simon contends that full rationality is an unrealistic standard. A more realistic standard, a bounded (e.g., limited) rationality, inhibits the acquisition of full knowledge. That is, the scarcity of resources (i.e., conscious attention and time) limits ability. Kahneman and Tversky (1979) developed an additional perspective on bounded rationality. Human beings rely on heuristics, or mental shortcuts, to enhance the information processing abilities. In complex decision-making, the use of heuristics routinely facilitates good JDM. Even though the use of heuristics is efficient in the use of time and effort, it may produce systematically biased JDM. Kahneman and Tversky (1979) identify three heuristics: availability, representativeness, and anchoring and adjusting. Uses of these shortcuts are identifiable by the types of biases (e.g., departures from the normative models) that evolve from such usage.

Of the three heuristics identified by Kahneman and Tversky (1979), two of the shortcuts, availability and representativeness, are indicative of processes people use while making a particular type judgment. The availability heuristic is useful when making frequency and probability judgments. The representativeness heuristic is beneficial when categorical logic is necessary. The anchoring and adjustment shortcut, however, is "generic" in that it involves the inferential thought processes of the mind. As such, anchoring and adjusting is useful in all JDM. A fundamental tenet of psychology is that the human mind initially performs an unconscious process on information before passing a thought to the consciousness. Anchoring and adjustment is a model of this process.

During the epistemic process, people will anchor on one belief and adjust from that belief for new information. For example, in a comparison of skill levels, one may anchor on their own skill level and adjust for the skill of others (Kruger 1999). Additionally, in a confidence probability situation, people will anchor on the extremeness of information, then adjust in accordance with the credibility of other information (Griffin and Tversky 1992).

During the anchoring and adjusting process, among other strategies, a decision maker may reach a judgment by attending to information consistent (e.g., confirming) with the initial anchor. Biased JDM may result because inconsistent (e.g., nonconfirming) information is not used or is undervalued (Snyder and Swann 1978). Research shows that this confirmatory decision-making strategy is engaged in during both the information gathering (Snyder and Swann 1978) and information evaluation stages (Lord et al. 1979) of the epistemic process.

This bias, referred to as confirmation bias, is such that while the adjustment away from the anchor for new information may be appropriate in direction, it is generally not of sufficient magnitude to alleviate the bias (Slovic and Lichtenstein 1971; Tversky and Kahneman 1974). Experimentally provided anchors have been shown to affect the initial anchor in the decision-making process.

Individuals cannot avert biases unless they are aware of those biases (Petty and Wegener 1993; Wilson and Brekke 1994). Without awareness, incentives can be instrumental in the anchoring process. Tversky and Kahneman (1974) demonstrated that incentives did not reduce anchoring. However, Wright and Anderson (1989)

found a minimal reduction in anchoring when the tested incentives were the monetary payment for accuracy of judgment and public awareness of accuracy rates.

### Tax Professionals

By signing an income tax return before filing it, every taxpayer is stating that, under the penalty of perjury, the return has been examined and, to the best of his/her knowledge and belief, the return is true, correct, and complete. The Internal Revenue Code of 1986 (hereinafter referred to as the Code) cannot and does not purport to address every conceivable factual taxing situation. In the alternative, statutory guidelines are presented, and consequently, uncertainty exists. Under these conditions, signing one's tax return that includes an ambiguous transaction infers that the position taken on the tax treatment of such event represents substantial authority.

Among other functions, tax professionals are charged with the responsibility of defending vague positions challenged by the Service. For the alternative tax treatments of the ambiguous transactions, the role of the professional is to research and present authoritative support.<sup>2</sup> Likelihood that the position recommended, based upon the client's facts and circumstances, will prevail on its merits upon challenge reduces the risk of uncertainty faced by the taxpayer. An assessment of alternative tax treatments may be the result of an open-fact (planning) task for the professional. In this instance, the professional is involved in structuring the transactions before

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<sup>2</sup> In this context, authoritative support is defined by an enumerated listing of authoritative sources in IRC Section 6662(d)(2)(B)(i). This listing, however, is not presented in a ranking context. Sources of primary authority have the force and effect of law. Statutes, legislative interpretations, and case law exemplify primary authority. Secondary authority, without the force and effect of law, provides guidelines and are accorded substantial weight. Interpretive regulations, IRS Rulings, and technical advice memoranda are examples of secondary authority. Lacking an explicit guideline, tax professionals must rely on judgment to weight authoritative sources. Reg. § 1.6662-4(d)(3) also provides an enumerated listing. The Secretary of the Treasury is mandated by Code Section 6662(d)(2)(D) to provide an annual listing in the *Federal Register* of positions for which there is not substantial authority.

occurrence. Upon completion of the transactions, the position taken is reported on an income tax return prepared by the tax professional for the taxpayer as a client. In other instances, closed- fact (compliance) tasks, a tax professional becomes involved in the challenge towards the end of the process rather than from the beginning. That is, the position has been taken by the taxpayer upon filing a return either self-prepared or prepared by another paid professional. Professional standards mandate that unbiased assessments of alternative tax treatments of clients' facts and circumstances be made (AICPA 1994, 18,055-18,059). Professional tax service models assume unbiased assessments (Phillips and Sansing 1998; Beck et al 1996).

Prior psychological research gives evidence that incentives impede the detachment necessary to generate unbiased research assessments (Koehler 1991). In both planning and compliance scenarios, several multi-directional incentives are present. While not all inclusive, incentives present in the tax professional-client relationship include compliance, professional enhancement/damage, and client advocacy. As the preparer, a position taken on a tax return concerning an issue that lacks a *realistic probability of success*<sup>3</sup> will result in IRS sanctioned preparer penalties. This compliance incentive will be present when the tax professional, or firm, is the preparer. Professional reputation is acquired by provision of quality services. Quality services are a matter of judgment. Prevailing in the challenge to a client's desired outcome is an enhancing measure of professional quality while not prevailing in an action is detrimental. Professional reputation enhancement/damage has been shown to be a stronger incentive than the monetary compliance incentives

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<sup>3</sup> IRC Section 6694 defines a realistic probability of success as a one in three probability. The monetary amount of this sanction, \$250, is symbolic. Invoking this penalty against a tax practitioner results in reporting of the infraction to professional regulatory agencies for disciplinary actions.

(Wright and Anderson 1989). Client advocacy is both a "right and responsibility" in tax practice (AICPA 1994). Primary loyalty lies with the client (Ayres et al. 1989; IRS 1987).

With incentives, decision-makers may place more emphasis on information confirming the desired outcome during an information search and evaluation. Over emphasis on confirming information, "confirmation" bias, may result in overly aggressive assessments and recommendations by tax professionals to support the client-preferred treatment. While all incentives may not be present in every tax litigation scenario (e.g., compliance incentives are present only as preparers), the dichotomous nature of the incentives performs checks and balances to insure, in theory, that disputed positions proceeding to litigation have strong support.

Tax research is performed in a hierarchical manner. Working under a supervisor, staff accountants and staff lawyers begin research initiated by a superior. Substantial support for the position recommended is the outcome of this task. Research has shown evidence of the presence of systemic bias in this decision-making process. One such systematic bias, confirmation bias, purports that in the decision-making process one searches more for information confirming one's desired outcome than for information disputing one's desired outcome. Since experience, education, and accountability should mitigate the presence of biases, bias should disperse as hierarchical research levels increase. Because of the filtering properties of dichotomous incentives and hierarchical levels, unbiased defenses for litigated cases should evolve. Empirical results on the mitigating effects of education (Cloyd and



Spilker 2000), experience (Biggs and Mock 1983; Kida 1984; Kaplan and Reckers 1989), and accountability (Hatfield 2000) on confirmation bias, however, are mixed.

Tax litigation involves adversarial stances on an alternative tax treatment situation. With the same research sources available, it is possible for adversarial parties to strongly defend positions both for and against the same facts and circumstances. Confirmation bias could be one explanation for this anomaly.

### Tax Administration

The IRS, a subsidiary agency of the Department of the Treasury, is charged with the administration of the tax laws. Among other duties, the IRS is charged with identifying delinquent tax payments for assessment and collection. In discharging this duty, the Service selects returns to audit. This selection, based on mathematical formulas, is engineered to derive those returns most likely to be erroneous and yield substantial additional taxes upon review.

The audit of a selected tax return can be in the form of an office audit (i.e., correspondence examination) or a field audit (i.e., interview examination). An office audit is performed through correspondence with the taxpayer and is generally limited to simple matters. A field audit entails analytical and judgment issues. This audit is accomplished on the premises of the taxpayer. This initial procedure can culminate in acceptance of the return as filed. In the alternative, the IRS auditor will propose certain adjustments in the Revenue Agent's Report (RAR). This report will undergo an internal review.

At this juncture, the taxpayer and IRS may agree to a settlement of the issues (Reg. Sec. 601.105(c)(1)(ii)). The Service, however, cannot settle based upon the

probability of winning the case in litigation, the "hazards of litigation." The taxpayer, with the tax professional as a representative, may consider all relevant issues. If an agreement is reached, the taxpayer signs Form 870. By signing this form, interest on any deficiency is limited to 30 days following this signing. Additionally, the taxpayer is agreeing to waive the right to petition the Tax Court.

If an agreement is not reached, the taxpayer receives a copy of the RAR and a 30-day letter. This letter states that the taxpayer has 30 days to request an appeal to the IRS Appeals Division (Reg. Sec. 601.105(c)(1)(ii)). This division has the authority to settle the matter with consideration of the probability of prevailing under litigation (Internal Revenue Manual, Sec. 8711(2)). Thus, negotiation and trading off issues is available in this appeals process. Costs of litigation would be an instrumental consideration for both the Service and the taxpayer. If the taxpayer does not request this hearing, a 90-day letter (Notice of Deficiency) is issued (Reg. Sec. 601.105(c)(1)(iv)). At this point, all parties are aware of the bases for the arguments supporting the position being advocated.

After the issuance of a Notice of Deficiency, the taxpayer may pay the stipulated amount and sue for refund.<sup>4</sup> Alternatively, the taxpayer may choose to forgo payment and petition for litigation. That is, the taxpayer controls the choice of litigation venue. However, in all venues other than the Tax Court, the Notice of Deficiency must be paid.

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<sup>4</sup> After receipt of the Notice of Deficiency, the taxpayer has to petition the Tax Court within 90 days. In the alternative, after expiration of 90 days, the taxpayer must pay the assessment and institute a suit for refund in either the U.S. District Court or the U. S. Court of Federal Claims. Of these courts of original jurisdiction, the Tax Court is the only court limited to hearing tax matters. As such, it is considered the court of technical expertise in tax litigation.

If the Tax Court judge decides that proceedings are frivolous, groundless, primarily for delay, or the taxpayer failed to pursue the available administrative remedies, Sec. 6673 allows the Court to invoke a penalty not in excess of \$25,000. This sanction can be applied to either the taxpayer or the Service. Similar to the district courts, attorneys or other persons, having “multiplied the proceedings in any case unreasonably or vexatiously”, can be required to pay the excess costs associated with such conduct (Sec. 6673(a)(2)).

### Research Questions

Tax litigation provides a natural anchor. The Notice of Deficiency sets a monetary amount for the litigation. The review and appeals process within the IRS has been completed. The taxpayer and their tax professional representative then choose either to pay a certain settlement to the Service and/or to litigate. In choosing to litigate, they are hoping that litigation will result in either no deficiency or a smaller deficiency. The IRS, by contrast, cannot choose to litigate. However, the hazards of litigation are incorporated in the settlement negotiation process. As such, a failure to further negotiate indicates the Service's realization that there exists a realistic probability of their success in litigation. In addition, both parties are aware of the substantial authority supporting the adversarial position. Thus, the tax professional and the IRS legal representative, having the set of facts and the basis of support for both positions, each conclude that the position they support has the strength to litigate. Normative economic theory of rational choice, however, does not support this outcome.

Although education, experience, and accountability should mitigate confirmation bias through the hierarchical process of research in both the tax professional's and the IRS legal representative's stances, the failure of normative theory (i.e., the same outcome) indicates an anomaly. Research indicates that the presence of incentives in the decision-making process of knowledge acquisition may result in confirmation bias in the anchoring and adjusting heuristic used. That is, each professional has weighted materials confirming the desired outcome inappropriately or has failed to weight nonconfirming materials adequately.

Fischhoff (2002), a noted psychological researcher in heuristics and biases, states that these anomalies of the normative model are in the public domain. Applied fields with high stakes are subject to erroneous beliefs (Bunker et al., 1977; Byrne, 1986; and Gilovich, 1991). Expert judgment provides a central role in public policy. Practitioners, however, seldom read research literature. The research into heuristics and biases provides evidence that experts, like the laity, oftentimes must rely upon judgment. Rachlinski (1994, 1998) provides support for biased judgments in legal decision-making. In a context similar to this research inquiry, Rachlinski investigated actual tort suits for hindsight bias. The generalizability of lab studies is supported by such findings. By demonstrating bias in the lab and, of immense importance, in the public domain, debiasing opportunities can be pinpointed.

This study addresses the following research questions:

Is there confirmation bias exhibited in the substantial authority presented in support of the stance taken on an ambiguous tax issue by tax professionals in litigation before the Tax Court?

If confirmation bias is present, which litigants exhibit a propensity to use confirmatory strategies in their JDM processes?

If confirmation bias is present, is there a correlation between instance of bias, litigants, and the monetary amount of the Notice of Deficiency and related penalties?

Prior studies that have found evidence of confirmation biases in the tax research task used experimental conditions. This study attempts to use actual court cases from the 2004 session of the Tax Court. While the stipulated facts may be more complex than those presented under experimental conditions, actual litigants have more time, more materials, and more resources to determine their recommended positions. Additionally, incentives are present rather than conjectured. Decisions are actually made rather than purported to be made.

With "unbiased" research being the mandate, awareness of the presence of bias is a necessary first step in mitigating the effects of using confirmatory strategies while conducting tax research. Mitigating those effects approaches the ethical standard.

#### Organization of this Dissertation

This dissertation is organized into five chapters. Chapter 1 introduces the topic of confirmation bias inherent in decision-making processes and relates this bias to parties in the tax litigation forum. The purpose of this study is presented. Chapter 2 reviews the relevant psychology and accounting literature. A survey of the stream of accounting literature on the effect of incentives on professionals' recommendations in the tax research task is followed by a survey of the studies investigating the presence of confirmation bias in the JDM of tax professionals. Chapter 3 presents the research hypothesis to be explored along with discussions of the data, test instruments, and

analytical methodologies to be employed in the research. Chapter 4 presents the empirical results of the study. Chapter 5 provides a summary and conclusions drawn from the research findings. Also, a discussion of the limitations of the study is presented and opportunities for further research are identified.

## CHAPTER 2

### LITERATURE REVIEW

A sequence of choices governs the dynamics of judgment and decision-making processes. While normative JDM theory views these choices as a cost/benefit analysis for maximized utility, psychological research provides evidence that choices are individualized and, as such, are based upon individualized criteria. Theoretical psychology studies by Beach and Mitchell (1978) and Payne and Johnson (1993) enumerate numerous characteristics that drive JDM strategy choices. These factors may impact and subordinate the outcome of the JDM process. These characteristics include accountability, ambiguity, complexity, familiarity, information display, instability, irreversibility of response, response mode, significance of outcomes, and time constraints.

In a supplementary manner, Roberts (1998) introduces an economic psychology-processing model (EPP) for use by JDM researchers investigating the tax research process. This EPP model, depicted in Table 2.1, categorizes previously tested factors that may skew the outcome of the tax research process by impacting choices. These relevant factors<sup>5</sup> are categorized into five groupings that are based on a theoretical framework of the sequential processes involved in decision-making.

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<sup>5</sup> Studies in Roberts' EPP model are limited to those inquiries investigating the behavior of tax accountants. As such, the model is not all-inclusive of the influences driving suboptimal JDM.

TABLE 2.1  
Factors Tested for Association with Tax Accountants' Judgment/Decision-Making  
(Roberts 1998)

<p>Individual Psychological Factors</p> <p>Cognitive</p> <ul style="list-style-type: none"> <li>▪ Years of experience</li> <li>▪ Task experience</li> <li>▪ Knowledge</li> <li>▪ Knowledge of transactions</li> <li>▪ Formal education</li> <li>▪ Job title/position in firm</li> <li>▪ Age</li> <li>▪ Problem-solving ability</li> </ul> <p>Affective</p> <ul style="list-style-type: none"> <li>▪ Advocacy</li> <li>▪ Tax accountant's risk preference</li> <li>▪ Ethical attitude</li> <li>▪ Attitudes related to professional status</li> <li>▪ Attitudes related to firm size</li> <li>▪ Attitudes associated with gender</li> </ul> <p>Environmental Factors: Risks and Rewards</p> <p>IRS Position</p> <ul style="list-style-type: none"> <li>▪ Audit probability</li> <li>▪ Audit success prediction</li> <li>▪ Penalties</li> <li>▪ IRS position on the issue</li> <li>▪ Probability of issue being examined on audit</li> <li>▪ Applicable regulatory standard for reporting</li> <li>▪ Tax rate structure</li> </ul> <p>Client Characteristics</p> <ul style="list-style-type: none"> <li>▪ Dollar amount of tax savings at stake</li> <li>▪ Client payment status</li> <li>▪ Client risk preference</li> <li>▪ Client importance</li> <li>▪ Client tenure</li> </ul>	<ul style="list-style-type: none"> <li>▪ Client preference for tax-reporting position</li> <li>▪ Client sophistication</li> <li>▪ Amount of income/operating performance</li> <li>▪ Client dependability</li> <li>▪ Client records</li> <li>▪ Conformity of item with client's financial report</li> </ul> <p>Firm Expectations</p> <ul style="list-style-type: none"> <li>▪ Economic benefit to firm</li> </ul> <p>Task Factors: Inputs</p> <ul style="list-style-type: none"> <li>▪ Ambiguity</li> <li>▪ Structural similarity of authoritative sources</li> <li>▪ Surface similarity of authoritative sources</li> <li>▪ Outcome of authoritative sources</li> <li>▪ Amount of legal authority</li> <li>▪ Complexity of law</li> <li>▪ Staff recommendation</li> </ul> <p>Task Factors: Outputs</p> <ul style="list-style-type: none"> <li>▪ Planning vs. compliance context</li> </ul> <p>Processing Factors</p> <ul style="list-style-type: none"> <li>▪ Information order</li> <li>▪ Structured problem-solving approach</li> <li>▪ Decision aid availability</li> <li>▪ Framing of issue as gain/loss</li> <li>▪ Certainty of outcome</li> <li>▪ Confirmation bias</li> <li>▪ Hindsight bias</li> <li>▪ Accountability</li> <li>▪ Time pressure</li> <li>▪ Group discussion</li> </ul>
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The purpose of this chapter is to review the extant empirical literature of decision-making in the hierarchical tax research process. The first section generally follows the factors as depicted in Roberts' EPP model. The selected studies provide evidence of the effect of numerous incentives present in this JDM process on the



recommendations of tax professionals. The second section of the chapter details the research focusing on the presence of confirmation bias in the JDM processes of tax researchers. Understanding this literature is critical in designing and accomplishing the objective of this research inquiry.

### Incentives Research

#### Individual Psychological Factors

Tax professionals develop an expertise in taxation with time and experience. Early psychological studies state that a decade or more of intense preparation is necessary to achieve expert knowledge in a chosen area (Ericsson and Crutcher 1990; Bloom 1985; Hayes 1981; Simon and Chase 1973). Intense preparation in the quest of knowledge necessitates the use of heuristic JDM strategies. Using heuristics increases the susceptibility of JDM processes to illusions. Individual psychological factors that lead to misimpressions are both cognitive (internal) and affective (external) influences. The impact of these illusional factors may result in suboptimal decisions by tax professionals.

#### Cognitive Factors

Internal (cognitive) influences can affect individuals involved in JDM processes. For this reason, numerous studies focus on cognitive attributes. Individual characteristics of experience, task-specific experience, task-relevant knowledge, education, problem solving ability, and gender are investigated.

Experience. It is intuitive that experience enhances one's decision-making capabilities. Numerous early studies incorporate EXPERIENCE as a variable in researching the impact of individual cognitive attributes on tax professionals'

recommendations to clients (Chang and McCarty 1998; Kaplan et al. 1988; LaRue and Reckers 1989). Nevertheless, measuring an EXPERIENCE variable proves to be problematic. One measure of EXPERIENCE is the passage of time (e.g., years). However, the researcher must take care in linking the JDM process under scrutiny with this measure because YEARS OF EXPERIENCE can proxy for many between-subject differences. As a result, studies generally define EXPERIENCE explicitly by such measures as the amount of time spent in tax research, the number of encounters with the tax issue, or the number of IRS encounters. Additionally, other variables that can proxy for EXPERIENCE must be controlled by the use of separate variables. Client advocacy and risk preferences are examples of variables needing separate measures (Roberts 1998). This review presents studies that recognize and incorporate these distinctions.

EXPERIENCE as a variable is statistically significant in identifying relevant tax issues (Bonner et al. 1992; Spilker and Prawitt 1997; Roberts and Klersey 2004). Other studies show a significant relationship between EXPERIENCE and the ability to correctly determine proper tax treatment (Chang and McCarty 1988; Kaplan et al. 1988; LaRue and Reckers 1989; Helleloid 1989; Hite and McGill 1992; Newberry et al. 1993; Roberts and Klersey 2004). Additionally, EXPERIENCE is a significant variable when subjects are locating substantial authority for an ambiguous tax situation (Cloyd 1995b; Spilker and Prawitt 1997).

Differences in EXPERIENCE are found to be not statistically significant in studies that rank authoritative tax sources (Chow et al. 1989; Bain and Kilpatrick 1990) and in stock valuation tasks (Roberts 1990). In addition, Duncan et al. (1989),

Schisler (1994) and Carnes et al. (1996) report no significant differences for EXPERIENCE when asking subjects to evaluate itemized deductions. Madeo et al. (1987) has similar results when study subjects are asked to predict the percentage of income reported by individuals.

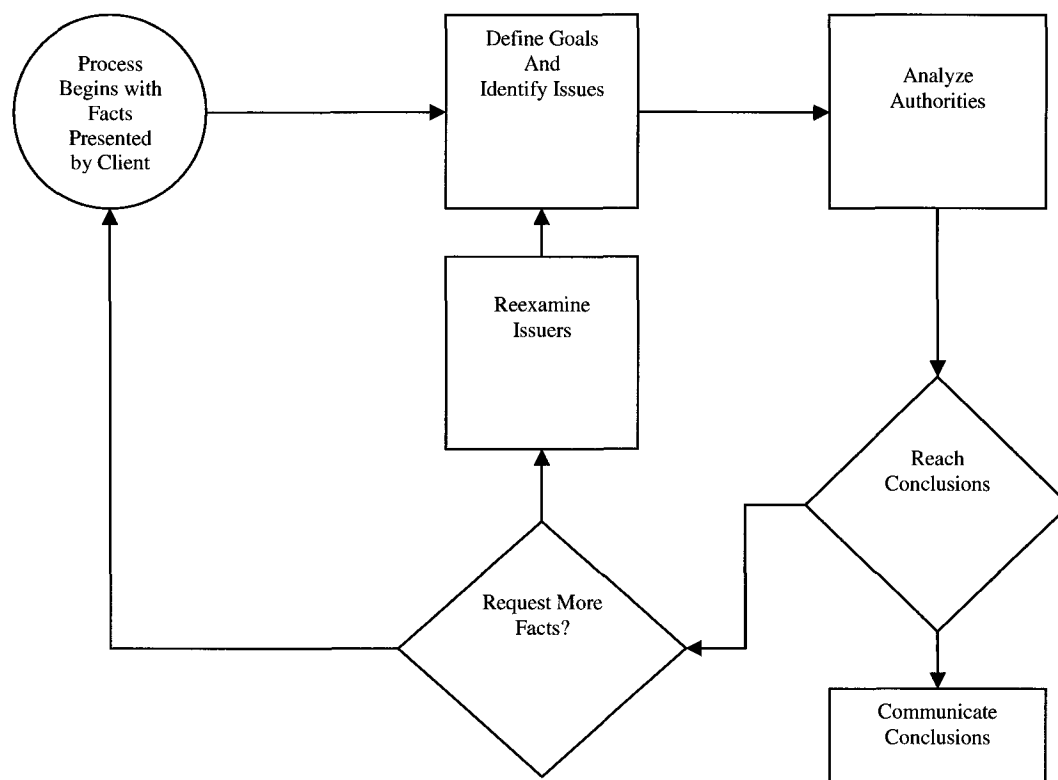
Marchant et al. (1989) present a model, depicted in Figure 2.1, of tax research that describes the cognitive processes of legal reasoning. Analogical reasoning<sup>6</sup> is the foundation for this model. Ostensibly, the model is a diagram used to research ambiguous tax issues. In their 1991 study, Marchant and his co-researchers test analogical reasoning in the problem solving processes of “novice” and “expert” tax professionals. The manipulation results in a reduction of knowledge transfer for the “experts” and an increase in knowledge transfer for the “novices.” Thus, results of the Marchant et al. (1991) study are counter-intuitive. The authors theorize that the highly proceduralized rule used in their study interferes with the knowledge transfer of the experts. That is, proceduralizing a principle of a solved problem may result in inflexibility when dealing with a new problem.

Marchant et al. (1992) refine their experiment. Using a complete analog<sup>7</sup>, the results are also counter-intuitive. With the manipulations between complete analog, incomplete analog, and no source analog, this study observes a greater effect on the student subjects than on the professionals. Additionally, professionals are misled by

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<sup>6</sup> Holland et al. (1986) define analogy as a reasoning mechanism dependent upon recognizing, after selective abstracting, seemingly unrelated situations as related. With the use of analogy, existing knowledge of a previously solved problem extends into the reasoning process of a current problem. Specific determined court cases set the precedent in tax research to which all following cases with the same issues are to be compared.

<sup>7</sup> An analog consists of a source analog (solved problem) and a target problem. In a complete analog, all the necessary logical parts between the source analog and the target problem match up. In contrast, an incomplete analog will have parts between the source analog and the target problem that do not match up.



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FIGURE 2.1  
Cognitive Model of Tax Research  
(Marchant et al. 1989)

the incomplete analog condition; that is, they cannot successfully protect against the misuse of incomplete analogs. The authors offer the use of an easy target problem as a possible explanation for the results. Also, taxpayer advocacy could be instrumental in the complete analog because the ruling included in the testing instrument is contrary to the taxpayer's preferred tax treatment.

In light of these earlier findings, Marchant et al. (1993) manipulate the direction of the source analog. That is, both rulings that support the taxpayer's preference and rulings that refute the taxpayer's preference are incorporated. An additional manipulation takes place with regard to the nature (complete versus incomplete) of the source analogs. With these refinements, the authors report that the knowledge transfer both in complete and incomplete analog manipulations is influenced by the outcome of the source analog.

Task-Specific Experience. Bonner and Walker (1994) and Davis and Solomon (1989) theorize that performance in JDM improves with task-specific experience assuming the existence of the ability to perform, motivation to perform, and feedback. This theory leads to an additional technical refinement of the definition of EXPERIENCE as a construct. The findings of empirical research which explore this refined EXPERIENCE variable produce mixed results.

Numerous variables develop to measure TASK-SPECIFIC EXPERIENCE. Duncan et al. (1989) find that the percentage of clients involved in tax shelters is statistically significant for tax professionals' recommendations with regard to tax shelter deductions. The professional's familiarity with like-kind exchanges, as a measure of TASK-SPECIFIC EXPERIENCE, is significant in tax managers' recommended reporting decisions (Reckers et al. 1991). Newberry et al. (1993) report that recommendations regarding deductibility of asbestos abatement costs are significantly related to a percentage of fees derived from real estate activities.

Alternatively, Karlinsky and Koch (1987) note that self-reported time spent with the Code is not statistically significant in answering a brief quiz. Subjects in this

study, however, self-report low task-specific experience. Roberts (1990) reduces the task to a highly structured context by relying on problem-solving heuristics. His study reports that task-specific knowledge is not statistically significant in observed differences for business valuation judgments.

Knowledge. In contrast, empirical research testing TASK-SPECIFIC KNOWLEDGE supports a more stable relationship with JDM performance differences. The majority of studies find this relationship statistically significant. Using multiple-choice questions from textbook testbanks or the Uniform CPA exam, Cloyd (1995b), Spilker (1995), and Bonner et al. (1992) each show the significance of task-relevant knowledge on JDM performance. Memory recall of relevant information provides the basis for the relationship demonstrated by Roberts and Klersey (2004), Davis and Mason (2003), and Bonner et al. (1992). When subjects identify tax issues in a given set of client facts (Bonner et al. 1992) or select authority using electronic resources (Cloyd 1995b, 1997; Spilker 1995), the results produce statistically significant relationships. Using highly technical partnership tax issues as the measure for TASK-SPECIFIC EXPERIENCE, Cloyd (1995b) and Roberts and Klersey (2004) each report a significant relationship. Additionally, Davis and Mason (2003) find a significant relationship when subjects identify unique features in tax cases. However, one measure of KNOWLEDGE in Davis and Mason (2003) is not significant. In this memory recall study, the KNOWLEDGE variable is significant in detailing how distinguishing tax features are identified, but is not significant in explaining similar tax features.

Cloyd's (1995b) study providing evidence of the effect of prior knowledge on the information search and evaluation behavior of tax professionals is of particular interest in this research inquiry. Using subjects from a national accounting firm, Cloyd (1995b) establishes a prior knowledge distribution by administering a multiple-choice questionnaire on the chosen tax issue. By structuring experimental scenarios to mirror examples illustrated in the IRS regulations, the researcher controls ambiguity<sup>8</sup>. From the results of the prior knowledge questionnaire, subjects are divided into two TASK-SPECIFIC KNOWLEDGE categories. Results of the experiment indicate that prior knowledge is negatively correlated with overall use of the topical index of the provided source materials and with the number of topics selected. Alternatively, TASK-SPECIFIC KNOWLEDGE is positively correlated with the accuracy of topics selected. Additionally, a significant positive relationship exists between prior knowledge and the number of accurate topics selected in the first loop of the iterative information search process. Thus, the authors conclude that prior knowledge affects the information strategy used, the amount of information located, the speed of retrieval, the attention (measured by time) paid to relevant information, and the ability to distinguish the relevance of information.

Education. Education is one method of acquiring knowledge. Oftentimes, KNOWLEDGE/EDUCATION is measured by the degree earned and teaching methodologies. In testing reading comprehension, Karlinsky and Koch (1987) note that the degree earned affects JDM performance. Among other theories, Bonner et al.

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<sup>8</sup> Scholes and Wolfson (1992) and Pratt (1994) note that "precise" tax rules delineate requirements for a specific particular tax outcomes. By providing "roadmaps," precise rules control uncertainty. Ever mindful of this distinction between tax issues, the majority of empirical JDM research inquiries incorporate ambiguous issues with the desire of expeditiously eliciting behavioral characteristics from the subjects.

(1992) investigate the relationship between knowledge, type of pedagogy, and practice experiences. Formal education is statistically significant in explaining different scores on a knowledge test. That is, participants' exposure to case studies pedagogy enhances the integration of tax transaction knowledge and tax rules. Cloyd and Spilker (2000) hypothesize that the type of academic training tax professionals receive impacts the extent of observable bias. They theorize that law students, as opposed to accounting students, should attend to both positive and negative research in an information search because law school education provides extensive exposure to cases and legal arguments. With this training, law students should exhibit less bias in JDM than accounting students. The Cloyd and Spilker (2000) hypothesis is supported. Carnes et al. (1996) find a positive relationship between aggressiveness and formal education. In their study, EDUCATION is correlated with FIRM SIZE ( $r = .2403$ ,  $p = .0001$ ) and PROFESSIONAL STATUS ( $r = .2403$ ,  $p = .0353$ ). Therefore, additional models are investigated incorporating only one of the correlated variables. PROFESSIONAL STATUS and EDUCATION are significantly related to the aggressiveness of the tax positions taken by subjects in high-ambiguity scenarios, but not in low ambiguity scenarios.

Problem-Solving Ability. The presence of cognitive faculties that enhance problem-solving abilities varies among individuals. Thus, individualized problem-solving abilities could impact JDM choices. One aspect of Bonner et al. (1992) studies tax professionals' general problem-solving abilities and JDM. Problem-solving abilities are tested using a cued recall test instrument. This ability is statistically significant for the difficulty of issues identified, but is not significantly



associated with the number of tax issues identified. Additionally, study results indicate that problem-solving ability relates to better performance in subjects with low levels of tax knowledge.

Davis and Mason (2003) formulate a feature-mapping model that describes how tax professionals evaluate precedent. While Treasury Regulation 1.6661-3(b)(3) mandates the weighing of conflicting authorities in determining "substantial authority" and the AICPA *Code of Professional Conduct* requires unbiased research (i.e., research defined as looking at both confirming and disconfirming information in formulating a position), these researchers find that only common features are used to make similarity judgments. Thus, while the evaluation of precedent proves instrumental to tax research, the evaluation is generally flawed in that only common (and not distinctive) features impact perceived similarity.

In summary, experience, knowledge, and education should enhance one's ability to perform the technical requirements of tax research. Empirical results, however, produce mixed results with regard to experience, including task-specific experience. Task-relevant knowledge, however, provides a significant cognitive measure to link with the requirements of tax research tasks. Education and experience are each shown to have mitigating effects on aggressiveness of tax professionals' recommendations.

### Affective Factors

In addition to internal (cognitive) influences, external (affective) factors affect individuals, especially in the areas of motivation and effort. Kennedy (1995) observes a positive impact from affective influences in that a more thorough analysis or a wider

solution set results during tax research tasks. Johnson (1993), however, shows a negative effect from external factors through the presence of confirmation bias. Roberts' (1998) EPP model lists advocacy, risk preference, ethics, professional status, firm size, and gender attitudes as affective factors in tax research studies.

Advocacy. Although the *AICPA Code of Professional Conduct* mandates “unbiased” research, the *Standards of Responsibility in Tax Practice* recognizes that tax professionals have the “right and responsibility” to act as client advocates in tax-related tasks. While the statutes require “substantial authority” to support an ambiguous tax position taken on a tax return, the IRS penalizes preparers when a position taken does not have a “reasonable possibility” of prevailing in a litigious arena. “Reasonable possibility” is defined as a one in three (33.3%) probability of prevailing. Thus, vague guidelines emanate from both the professional regulators and the governmental regulators. As a result, a plethora of studies investigating client advocacy have evolved. Major studies that investigate the effect of advocacy on JDM are reviewed.

Recognizing that the degree of client advocacy is a personally interpreted guideline (i.e., a cognitive trait), Johnson (1993) dichotomizes the professional subjects of her study into strong client advocates and less strong client advocates. This categorization is accomplished through an analysis of the residuals from a regression of NETSCORE<sup>9</sup> on RECOMMENDATION. From this differentiation, the inquiry investigates the evaluation of evidence strategies used in analyzing and

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<sup>9</sup> NETSCORE represents a measure derived from analysis of authority chosen in support of client preferences; therefore, a confirmation bias measure is determined.

making recommendations.<sup>10</sup> The anchoring and adjusting heuristic and the resulting confirmation bias comprise the focus of the inquiry. Johnson's results indicate that professionals use confirmatory decision strategies when evaluating judicial cases for their clients' ambiguous issues. This bias inhibits the ability to properly assess the likelihood of prevailing in a judicial challenge. Improperly high assessments lead to stronger recommendations. Degree of advocacy contributes to use of confirmation strategies. Consequently, degree of advocacy directly impacts the strength of recommendations. Davis and Mason (2003) demonstrate that, as degree of advocacy increases, professionals assign more weight to common features if the outcome is favorable to client preference and less weight if the outcome is unfavorable. Cuccia (1995) links advocacy attitudes to increased effort in identifying support for deductions in response to increases in penalty threats.

Risk Perceptions. In a theoretical work, Milliron (1988) reports that one result of interviews with tax practitioners suggests that professionals believe their own risk propensities do not influence the aggressiveness of their recommendations. Carnes et al. (1996) provide evidence disputing this belief. Their study identifies professional-specific factors that influence decision-making among tax professionals. Possible determinants incorporated into the study include experience, firm type, gender, education level, and risk propensity. Their third hypothesis states in the alternative form:

Tax professionals who are more inclined to accept risk will be more likely to recommend aggressive tax positions than will professionals who are less inclined to accept risk.

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<sup>10</sup> As previously noted, the use of ambiguous tax issues is instrumental in observing strategy. As such, the majority of studies, including this study, incorporate ambiguous issues for clarity.

Results indicate a higher propensity for risk leads to more aggressive recommendations.

In a belief-revisioning study, Pei et al. (1990) explore several tax preparer attitudes as determinants of professional behavior. An 11-point Likert-type scale measures a preparer's perception of income tax reporting. One extreme of the scale, business risks (i.e., cost/benefit analysis), contrasts with a purely moral assessment as the other extreme. The derived variable acts as a covariate in the study. Movement along the scale toward business risk analysis correlates with stronger support of the client-preferred position. While client preference does influence recommendations of professionals with little moral obligation, scores of professionals who exhibit greater moral obligation are not effected by preferred outcome. LaRue and Reckers (1989) note that aggressive reporting recommendations become statistically linked to those practitioners that consider risk-propensity and perceive the tax system as unfair.

Ethics. The accounting profession embarked on an assessment focusing on professional standards following the enactment of preparer penalties and several adverse court cases in the 1980s. With this impetus, Burns and Kiecker (1995) test and report that ethical orientation is significant in explaining tax professionals' ethical judgments of encouraging clients to overstate deductions. Ethical orientation is determined by analyzing management facilitators (encouragements) and management inhibitors (reprimands) using the Hunt-Vitell model<sup>11</sup>. Thus, results indicate that managers would facilitate ethical decisions and inhibit unethical decisions. However,

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<sup>11</sup> The Hunt-Vitell (1986) model is one of three early ethical decision-making models designed for use by business scholars in business environments. This model is used primarily in marketing research before the subject study. The model is intended to determine why an individual chooses between ethical and unethical behavior. An additional determination concerns why individual perceptions differ in an ethical/unethical context.

the degree of behavior encouragements or behavior reprimands depends on possible economic benefits to the firm. As a consequence, unethical behavior with greater economic benefits to the firm is viewed as less serious than unethical behavior with negligible benefits to the firm.

Professional Status and Firm Size. Unlike accounting practitioners who offer auditing services and expertise, tax professionals are not required to maintain professional certification to perform as a tax preparer. Designation as a *certified public accountant* (hereinafter referred to as CPA) is achieved through successful completion of a comprehensive examination and stipulated experience requirements. As such, professional status, CPA or non-CPA, is hypothesized as one factor effecting attitudinal differences among tax preparers. Prior empirical studies consistently provide evidence of the existence of attitudinal differences between CPAs and non-CPAs. Cuccia (1995), Jackson et al. (1988), and the IRS (1987) each support that CPAs exhibit more loyalty to clients than do non-CPAs. Ayres et al. (1989) and Cuccia (1995) find that CPAs more aggressively report clients' ambiguous tax issues than non-CPAs. In a study that maximizes systematic variation in professional position, Roberts and Klersey (2004) report PROFESSIONAL STATUS significantly associates with evaluations of client-favored treatment. In support of these results, CPA firms are noted as that group "least compatible" with the IRS mission in a 1987 report prepared by Westat, Inc. Conversely, Karlinsky and Koch (1989) find no statistically significant difference between CPAs and non-CPAs on a reading comprehension test. Collins et al. (1990) also reports no significant differences between professional statuses when identifying appropriate preparer penalties.

Firm size can represent different firm cultures and client characteristics. For example, firm size may dictate the ability to pursue specialization within the profession. Different type preparers serve different clientele.<sup>12</sup> As such, large v. small firm differences are significant in studies that investigate mileage deductions (Helleloid 1989) and capital gains treatment for sales of real estate (Chang and McCarty 1988). These results are supported when testing income and deductions (Carnes et al. 1996), prizes, capital gains, education expenses, and travel expenses (Sanders and Wyndelts 1989).

No FIRM SIZE differences are found in studies investigating reading comprehension (Karlinsky and Koch 1989), ranking of tax authorities (Chow et al. 1989), determining appropriate preparer penalties (Collins et al. 1990), and formulating closely-held business valuations (Roberts 1990).

In light of these mixed results, later studies that investigate FIRM SIZE refine the attitudinal constructs measured by this factor.

Gender. McGill (1988), Sanders and Wyndelts (1989), and Roberts (2004) all support the cognitive psychologists who report that males have a greater propensity for risk than females (Levin et al. 1988). These studies report males as more aggressive in their recommendations than females in a compliance context. While testing for framing effects<sup>13</sup> in tax practitioners' decisions under uncertainty, only one of five tests conducted by Sanders and Wyndelts (1989) does not reveal statistical significance. Responses from female subjects showing a risk neutral preference are

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<sup>12</sup> Larger accounting firms typically serve wealthier clients than do smaller firms (Helleloid 1989). Those serving lower-income clients express greater government loyalty (Helleloid 1989). Therefore, large firms see themselves as client advocates to a greater degree than do smaller firms.

<sup>13</sup> Framing effects, defined as the variations in the framing of available choice options in terms of gains and losses, yield systematically different preferences in JDM (Tversky and Kahneman 1974).

not significant. Earlier empirical works fail to find a relationship between aggressiveness and gender (Ayres et al. 1989; Cuccia 1994).

In summary, researchers present evidence that both cognitive and affective influences provide sources of bias in the JDM processes of tax professionals when used to search for and provide recommendations to clients in tax research contexts. Table 2.2 summarizes the results of the reviewed extant literature on the impact of individual psychological factors on JDM processes of tax professionals while searching and evaluation information in support of tax issues.

**TABLE 2.2**  
Summary of Literature on the Impact of Individual Psychological Factors on  
Judgment/Decision-Making in Tax Research

Author(s)	Factor	Results*
Ayres, Jackson & Hite, 1989	Gender	Not Significant
	Professional Status	Significant
Bain & Kilpartick, 1990	Experience	Not Significant
Bandy, Betancourt & Kelliher, 1994	Client status	Not Significant
Bonner, Davis & Jackson, 1992	Experience	Significant
	Knowledge	Significant
	Education	Significant
	Problem-solving	Mixed
Bonner & Walker, 1994	Experience	Significant
Burns and Kiecker 1995	Ethical Judgment	Significant
Carnes, Harwood & Sawyer, 1996	Experience,	Not Significant
	Education,	Not Significant
	Gender	Significant
	Risk perceptions	Significant
	Firm size	Significant
Chang and McCarthy 1988	Experience	Significant
	Firm size	Significant
Chow, Shields & Whittenburg 1989	Experience	Not Significant
	Firm size	Not Significant
Cloyd 1995a	Experience	Significant
	Knowledge	Significant
Cloyd 1995b	Knowledge	Significant
Cloyd 1997	Knowledge	Significant
Cloyd & Spilker 2000	Education	Significant
Collins, Milliron & Toy, 1990	Firm size	Not Significant
Connor, 1994	Gender	Significant
Cuccia, 1994	Experience	Significant
	Gender	Not Significant

TABLE 2.2 (Continued)

Cuccia, 1995	Advocacy	Significant
	Firm size	Significant
Davis & Mason, 2003	Knowledge	Mixed
	Problem-solving	Significant
	Advocacy	Significant
Davis & Solomon, 1989	Experience	Significant
Duncan, LaRue & Reckers, 1989	Experience	Mixed
Helleloid, 1989	Experience	Significant
	Firm size	Significant
Hite & McGill, 1992	Experience	Significant
Internal Revenue Service, 1987	Professional status	Significant
Jackson, Milliron & Toy, 1988	Professional status	Significant
Johnson, 1993	Advocacy	Significant
Kaplan & Reckers, 1989	Experience	Significant
Kaplan, Reckers & West 1988	Experience	Significant
Karlinsky & Koch 1987	Experience	Not Significant
	Education	Significant
	Professional status	Not Significant
	Firm size	Not Significant
LaRue & Reckers, 1989	Experience	Significant
	Risk perceptions	Significant
Madeo, Schepanski & Ueker, 1987	Experience	Not Significant
Marchant, Robinson, Anderson & Schadewald, 1989	Model	N/A
Marchant, Robinson, Anderson & Schadewald, 1991	Experience	Not Significant
Marchant, Robinson, Anderson & Schadewald, 1992	Experience	Not Significant
Marchant, Robinson, Anderson & Schadewald, 1993	Experience	Not Significant
McGill, 1988	Gender	Significant
Milliron, 1988	Risk perceptions	Not Significant
Newberry, Reckers & Wyndelts, 1993	Experience	Significant
Pei, Reckers & Wyndelts, 1990	Risk perceptions	Significant
Reckers, Sanders & Wyndelts, 1991	Experience	Significant
Roberts, 1990	Experience	Not Significant
	Firm size	Not Significant
Roberts, 2004	Gender	Significant
Roberts & Klersey, 2004	Experience	Significant
	Knowledge	Significant
	Professional status	Significant
Sanders & Wyndelts, 1989	Gender	Mixed
	Firm size	Significant
Schisler, 1994	Experience	Not Significant
Spilker, 1995	Knowledge	Significant
Spilker & Prawitt, 1997	Experience	Significant
Westat, Inc.	Professional status	Significant

\*Significant/Not Significant designation is, generally, based upon p-value, with an  $\alpha$  of .05. However, in survey and interview studies, the designation may be the result of self-reports.



### Environmental Factors

Roberts' EPP model identifies three sources of environmental factors that may influence tax professionals' JDM. These sources include IRS position, client characteristics, and firm expectations. As the regulatory agency monitoring tax compliance, actions by the IRS influence JDM behavior. Client characteristics, such as preference for a reporting position, status/tenure as a client, dependability and sophistication, may influence professionals in their information search and evaluation. Additionally, firm expectations provide influences in decision-making. Firm expectations, however, are interrelated with several client characteristics; therefore, this review aggregates studies related to firm expectations and client characteristics.

### Internal Revenue Service

The IRS, as the primary government regulatory agency, attempts to enhance compliance with the voluntary tax reporting system through their ability to perform audits and penalize noncompliance.

Audit. Normative decision-making strategies assume a cost/benefit analysis. As such, a rational tax professional faced with the probability of an audit would weigh the benefits of an aggressive reporting position with the inherent costs. Aggressive tax recommendations should negatively correlate with high audit probability because of the associated costs. Nonetheless, interactions of audit probability with other attitudinal characteristics result in mixed findings. Roberts (2004), Newberry et al. (1993), Hite and McGill (1992), and Kaplan et al. (1988) provide evidence of the significant negative relationship between audit probability and tax professionals' aggressive recommendations. Audit probability interacts significantly with amount of

tax savings (Hite and McGill 1992; Kaplan et al. 1988) and likelihood of client defection (Roberts 2004). Kaplan et al. (1988) reports that audit probability considerations only affect less experienced subjects.

Audit probability as a construct is operationalized using numerous measures. While high/low probability is defined differently, studies which assign numerical values to probability generally report the relationship not statistically significant. However, numerical measures have not closely correlated with realistic audit probabilities. Alternately, studies verbalizing audit probability<sup>14</sup> generally find the relationship as significant.

In a refinement of audit probability, Hite and McGill (1992) dichotomizes audit the variable into the probability of the return being selected for audit and the probability of the position being examined in the event of an audit, finding each component significant. Conner (1994) praises this dichotomy because audit selection is based upon mathematical formulas while position examination is based upon technical expertise of IRS agents.

Duncan et al. (1989) and Kaplan et al. (1988) hypothesize and support the theory that recent successful audit experiences would lead to more aggressive client recommendations. Perception of ability to prevail in litigation, used as a covariate, is significantly associated with willingness to recommend an aggressive reporting position (Newberry et al. 1993). Interestingly, the mean of the covariate is 61 percent, which signifies that the mean of the likelihood of prevailing upon challenge is 61

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<sup>14</sup> Verbalizations include “high v. low” audit probability (McGill 1990) and “reasonably possible v. remote” (Roberts and Cargile 1994).

percent, as reported by practitioners. Hite et al. (1992) report a threshold of 70 percent as the taxpayer's (i.e., the client) desired likelihood of prevailing upon challenge.

Penalties. Results of surveys (Cuccia 1995; McGill 1988; Milliron 1988; IRS 1987), predictions of taxpayer behavior (Madeo et al 1987), and experiments of tax professionals' recommendations (Cuccia 1994; Reckers et al 1991; Hite and McGill 1992) all support the negative relationship between penalties and aggressive reporting recommendations. Furthermore, Cuccia (1994) reports that an increase in penalties has a positive correlation with CPAs search efforts but a negative correlation with non-CPAs search efforts.

Schisler (1994, 1995) reports that penalties do not significantly affect JDM. Roberts (1998) points out a weakness in the Schisler's PENALTY measurement. By definition, the low penalty condition in Schisler's (1994, 1995) studies contains only a taxpayer penalty, while the high penalty condition contains both taxpayer and professional penalties. With this definition, other attitudinal characteristics are inadvertently incorporated (e.g., client importance).

As previously noted, normative decision-making strategy assumes an implicit cost/benefit analysis. As a result, the Service attempted to lessen the advocacy position of tax professionals by statutorily strengthening preparer penalties in 1986. Still, Cuccia (1994) notes that psychological rewards accrue for professionals who view the relationship as a competitive exercise.

#### Client Characteristics

Since client characteristics vary, they may have significant differential affects on tax professionals' JDM strategies. Tax professionals' interviews suggest that tax

law ambiguity is interpreted in accordance with client preferences (Milliron 1988). In an attempt to explain this behavior, Milliron (1988) devises a model of variables which effect aggressive behavior in a tax compliance context. The model incorporates both client and tax professional attributes. Milliron (1988) reports that professional attributes are more important in the model. Subsequent studies establish the impact of numerous client characteristics. Investigated characteristics include tax payment status, client risk preference, and client status.

Tax Payment. The objective of a tax return is to determine the tax liability on the transactions contained therein. Prepayments of the tax liability require either estimates or withholdings.<sup>15</sup> Therefore, at the time of filing, calculations may determine either an overpayment (refund) or underpayment (balance due). If the prepayment requirements under IRC Chapter 68 have not been met, penalties will accrue. This cash flow characteristic (payment status) may influence the approach taken in preparation of the return. Milliron (1988) suggests that the amount of tax savings positively influences aggressiveness. Faced with a balance due, it is hypothesized that taxpayers and professionals will exhibit risk-seeking behavior to minimize this additional, possibly unexpected cash outflow. Conversely, a desire to increase the amount of refund can

Kaplan et al. (1988) find a significant relationship between professional aggressiveness and the dollar amount of tax liability. LaRue and Reckers (1989) support these results. Their study notes an interaction effect involving three variables: payment status, professional experience level, and tax savings.

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<sup>15</sup> Prepayment requirements are set forth in IRC Chapter 68.

Several studies examine the impact of overwithholding and underwithholding with mixed results. Weak main effects are found by Duncan et al. (1989) when testing the theory that professionals are more aggressive when the taxpayer is in a balance due rather than a refund status. However, payment status most often results as significant in terms of an interaction. Client preference (Schisler 1994, 1995), experience, and amount of tax savings (LaRue and Reckers 1989) show statistically significant interactions with payment status. Recommendations to clients with underpayments are aggressive only when the client's description includes an aggressive mien. However, holding these interactive characteristics constant results in non-significance of payment status (Sanders and Wyndelts 1989).

Risk Preference. Most empirical work in the area of client risk preference chooses "aggressive v. conservative" to represent the taxpayer's preference. Four of the following five studies find client risk preferences statistically significant relative to professional recommendations.

Cuccia et al. (1995) incorporate a defamation settlement in their study. In order to manipulate client risk preference, clients are described as aggressive/conservative or risk-averse/risk taking. Risk preference operationalizes as the independent variable PREPARER INCENTIVE. The variable is significant ( $p < .001$ ) which suggests preparers recommend aggressively to aggressive clients and more conservatively to conservative clients. Cloyd (1995a) replicates these results when using start up costs and a purchase price allocation as the ambiguous tax issue. His study asserts that professionals are likely to consider their vulnerability to certain risks (reputation, litigation, loss of client) if they make aggressive recommendations. Duncan et al.

(1989) report the same findings for recommendations when one incorporates client risk preferences as conservative, fearful of audit, and avoids gray areas as opposed to aggressive, not fearful of audit, and aggressive in gray areas.

While the previously examined between-subject studies find client preference as significant, some explanation is provided by Schisler's (1994) within-subject experiment. Initial recommendations are elicited from the professional with no knowledge of client preference. A second recommendation is recorded after injecting client preference into the available information. With this manipulation, client preferences become significant in the recommendation of the professional.

In contrast, Helleloid (1989) elicits opposite results in a study of aggressive recommendations and client preference when investigating client documentation efforts regarding business auto expenses. No significant relationship is determined. Roberts (1998) suggests that the tax issue is the pivotal factor in Helleloid's study. While most studies involve an ambiguous tax issue, Helleloid's study considers a tax deduction with statutorily required detailed recordkeeping as a prerequisite, which has the effect of incorporating "precise" elements into the tax issue. This distinction could be causal to the atypical findings.

In one of the few studies on tax research from the taxpayer perspective,<sup>16</sup> Hite and McGill (1992) examine taxpayers' preference for aggressive reporting. That is, taxpayers report their tolerable risk levels as opposed to professionals using perceived

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<sup>16</sup> Many prior studies, including Duncan et al. (1989), report taxpayer attitudes and risk preferences. These attitudes and preferences, however, are from practitioner self-reports rather than taxpayer responses.

taxpayer risk levels in JDM processes. Using a very conservative null hypothesis<sup>17</sup>, results indicate taxpayers prefer a conservative position under uncertainty. This study provides no evidence supporting a taxpayer demand for aggressive tax reporting. These results follow findings by Hite et al. (1992) that reported 70 percent certainty as a threshold by small business owners for probability preferences on ambiguous issues.

Client Status. Client status refers to those characteristics that could influence the tax professional's valuation of the taxpayer. Firms intuitively take more risk for a highly valued client than a less valued client. That is, economic dependence elicits a cost/benefit analysis in the JDM process as a recommendation evolves. Both vaguely measurable (e.g., importance) or specifically measurable (e.g., tenure, payment status) constructs proxy the value of a client to the professional.

Empirical research inquiries operationalize CLIENT IMPORTANCE in terms of taxpayer gross income interacting with referrals (Reckers et al. 1991) and out-of-state residence (i.e., influential proximity) with past referrals (Bandy et al. 1994). Reckers et al. (1991) efforts provide evidence of a significant relationship, while the Bandy study finds no significance between the CLIENT IMPORTANCE construct and reporting recommendations. Roberts (1998) notes that the tax reporting issue used by Bandy is less ambiguous than Reckers et al. Criticisms of these works include the inability to precisely define "importance".<sup>18</sup> Without an explicit definition, studies using CLIENT IMPORTANCE as a variable are confounded and, consequently, weak

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<sup>17</sup> Preference for conservative advice would reject the null. Preference for aggressive advice or a neutral stance by the taxpayer would not reject the null.

<sup>18</sup> Bandy et al. (1994) criticizes Reckers et al. (1991) on this aspect. It is noted that, in the context used, importance could be measuring client sophistication, tenure, or gross income.

Operationalizing CLIENT STATUS as tenure provides stable results of a significant relationship with aggressive reporting recommendations. Milliron (1988) uses self-reports of tenure. Roberts (2004) and Newberry et al. (1993) define client status as the risk of losing the client if the professional recommendation runs counter to client preferences. Each study provides support for a significant relationship between client tenure and aggressive recommendations.

In empirical works that incorporate CLIENT INCOME as a construct, this variable proxies for several characteristics. Madeo et al. (1987) use income to represent the opportunity to evade taxes. With the reasoning that greater incomes provide more opportunities for tax evasion, Madeo and co-researchers find a significant association between the interaction of income amount and income source with professionals' predictions of taxpayer compliance. Reckers et al. (1991) also measure client importance with client income for a significant relationship.

Business settings provide the context for empirical work on client characteristics in Roberts (2004). In this work, financial condition becomes a significant variable for aggressive tax reporting by professionals. Cloyd (1995a) hypothesizes that consistency of tax/financial reporting, perceived as lowering audit risk, will effect professional recommendations. His study supports the assertion that tax professionals' recommendations are significantly influenced by financial accounting treatment of a tax transaction.

To summarize, researchers present evidence that environmental factors provide motivations for bias in the JDM processes of tax professionals when used to search for and provide recommendations to clients in tax research contexts. Table 2.3



summarizes the results of the reviewed extant literature on the impact of environmental factors on the JDM strategies of tax professionals.

### Ambiguity

Whether reporting for income tax or excise tax purposes, signing and filing the appropriate return is paramount to establishing the taxpayer's position on all tax issues included on that return. Oftentimes, well-defined rules govern tax treatment of an event. For example, IRC Section 163 allows for the deduction of primary home mortgage interest from adjusted gross income. Thus, these "precise" rules provide guidance about what is a primary home and what comprises home mortgage interest. The taxpayer is allowed this deduction if the particular facts and circumstances meet the enumerated criteria. On the other hand, some tax rules are ambiguous. Little guidance is given with regard to the interpretation of the terminology used in the Code. For instance, the proper characterization of the gain/loss on the disposal of real estate is governed by IRC Sections 1221 and 1231. Meeting the guidelines determines the characterization of the transaction (e.g., ordinary gain/loss or capital gain/loss). However, the guidelines are vague, resulting in characterizations of real estate gains and losses that have become a source of constant litigation. Case law develops a test of factors used by the judiciary to aid in a resolution for this question (Englebrecht and Bundy 2004). Judgment is instrumental in determining the proper application of these ambiguous rules and the evolved judicial factors to the taxpayer's particular set of facts and circumstances. As previously noted, studies investigating JDM processes employed during tax research must incorporate an ambiguous issue because the application of precise rules does not necessitate choices. As such, the following

TABLE 2.3  
Summary of Literature on the Impact of Environmental Factors on  
Judgment/Decision-Making in Tax Research

Author(s)	Factor	Results*
Bandy, Betancourt & Kelliher, 1994	Client status	Not Significant
Cloyd 1995a	Risk preference	Significant
	Client status	Significant
Cuccia, 1994	Penalties	Significant
Cuccia, 1995	Penalties	Significant
Cuccia, Hackenbrack & Nelson, 1995	Risk preference	Significant
Duncan, LaRue & Reckers, 1989	Audits	Significant
	Tax payment	Significant (Interaction)
	Risk preference	Significant
Helleloid, 1989	Risk preference	Not Significant
Hite, Cloyd & Stock, 1992	Audits	Significant
	Risk preference	Significant
Hite & McGill, 1992	Audits	Significant
	Penalties	Significant
	Risk preference	Significant
Internal Revenue Service, 1987	Penalties	Significant
Kaplan, Reckers & West 1988	Audits	Significant
	Tax Payment	Significant
LaRue & Reckers, 1989	Tax Payment	Significant (Interaction)
Madeo, Schepanski & Ueker, 1987	Penalties	Significant
	Client status	Significant
McGill, 1988	Penalties	Significant
Milliron, 1988	Penalties	Significant
	Tax Payment	Significant
	Risk preference	Significant
	Client status	Significant
Newberry, Reckers & Wyndelts, 1993	Audits	Significant
	Client status	Significant
Reckers, Sanders & Wyndelts, 1991	Penalties	Significant
	Client status	Significant
Roberts, 2004	Audits	Significant
	Client status	Significant
Sanders & Wyndelts, 1989	Tax payment	Not Significant
Schisler, 1994	Penalties	Not Significant
	Tax payment	Mixed
	Risk preference	Significant
Schisler, 1995	Penalties	Not significant
	Tax payment	Significant (Interaction)
Scotchmer, 1989	Risk preference	Significant

\*Significant/Not Significant designation is, generally, based upon p-value, with an  $\alpha$  of .05. However, in survey and interview studies, the designation may be the result of self-reports.

studies are included elsewhere in this literature review based on other variables in the research.

Taxpayers are interested in filing an accurate tax return. Numerous studies investigate the motivation behind the use of tax professionals for the preparation of tax returns. The Code has become increasingly complex over time. Time management, audit risk, and liability minimization are among the motivations that evolve from early studies (Yankelovich, Skelly, and White, Inc. 1984; Hite 1987; Collins et al. 1990; Hite et al. 1992). Scotchmer (1989) determines that taxpayers who use professional preparers view the primary function of the professionals to be the resolution of uncertainty. Additional findings of this study indicate that tax law ambiguity is usually resolved according to client preferences. Scotchmer's (1989) findings support Hogarth and Einhorn's (1990) assertion that, when faced with ambiguity and uncertainty, individuals exhibit cautious behavior. The inquiry concludes that the more risk averse the taxpayer, the more highly they value their tax professional.

Interestingly, findings on the compliance of professionally prepared returns are mixed.<sup>19</sup> Higher dollar audit adjustments are found on audited returns prepared by CPAs and attorneys than those returns prepared by other preparers (Smith and Kinsey 1986). In a later study in the same context, Smith and Kinsey (1987) control for income, tax shelters, over age 65, number of forms, joint returns, and self-employed status. By controlling for the enumerated items, degree of uncertainty is limited. The controlled items, particularly tax shelters and self-employment status, are areas of considerable ambiguity and uncertainty. With this control, the result for CPA and

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<sup>19</sup> Data for the following studies were derived from the IRS's Taxpayer Compliance Measurement Program (TCMP). As such, a compliance distinction between legal tax avoidance and illegal tax evasion was not made.

attorney prepared returns is not significantly different than other return preparers. Erard (1990) analyzes the decision to employ a paid preparer with compliance while controlling for tax return characteristics. Non-compliance is greater for paid preparers. However, controlling for return characteristics limits the ability to generalize results of both studies to ambiguous tax issues.

Klepper and Nagin (1989) differentiate these mixed results. Analyzing the audited returns line-by-line, they posit that tax professionals play dichotomous compliance roles. For tax issues with precise rules, professionals become “enforcers”; for tax issues with ambiguous rules, professionals become “exploiters.” That is, tax professionals are aggressive when faced with ambiguous tax issues, exploiting that vagueness. Precise areas are not exploited. Spilker et al. (1999) comments that the Klepper and Nagin (1989) study, because of the use of TCMP data and IRS audited amounts, could be confounded by the IRS agents resolving ambiguity in favor of the Service.

Consistent with these findings, when audit and penalty risks are low, CPAs’ recommendations to clients are more aggressive (McGill 1988). Playing the “audit lottery” can play a role in tax professional decision-making (Kaplan et al. 1988). Testing the effects of a recent IRS audit experience, Kaplan et al. (1988) find that a recent audit experience leads to aggressive recommendations only when the interpretation of the law contains ambiguities.

CPAs provide more aggressive tax reporting recommendation decisions than non-CPAs (Ayres et al. 1989). Additionally, client preferences weigh more heavily in the position taken by CPAs than in the position taken by non-CPAs when the issue

contains ambiguous elements. As noted earlier, CPA firms are reported to be that group “least compatible” with the IRS mission in Westat, Inc.’s 1987 report.

Krawczyk (1994) studies the influence of tax law and the organization of clients’ facts on professional judgment. She determines that only the form of law, objective (i.e., precise) or subjective (i.e., ambiguous)<sup>20</sup>, affects the selection and weighting of cues. Form of law and organization of client facts are significant in the number of cues selected. Experience enhances the selection ability. Even though all subjects in her study work at the same firm, the participants represent different levels of experience. This study gives indirect support to the findings that professionals interpret ambiguity in the direction of client preferences. Additionally, these results justify Dawes’ (1979) findings that people, generally, are better at selecting cues than in weighting them.

Spilker et al. (1999) manipulate ambiguity to test concerns that tax professionals exploit the vagueness of the tax law to minimize taxes for their clients. Manipulating ambiguity is achieved by comparing recommendations when the tax law requires trust distributions by a certain date (precise rule) vs. by a “reasonable time” after year-end (ambiguous rule). Their results provide evidence that in compliance decision contexts professionals are more likely to recommend an aggressive position to the client for an ambiguous issue than a precise one. However, recommendations in planning contexts appear more conservative than in compliance contexts.

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<sup>20</sup> In her study, objective form is defined as structured lists of specific relevant cues while subjective form considers all facts and circumstances.

## Substantial Authority

Treasury Regulation 1.6662-4(d)(3) states:

There is substantial authority for the tax treatment of an item only if the weight of the authorities supporting the treatment is substantial in relation to the weight of authorities supporting contrary treatment...The weight of those authorities is determined in light of the pertinent facts and circumstances...The weight accorded an authority depends on its relevance and persuasiveness and the type of document providing the authority.

These regulations do not provide explicit guidance. What the regulations do provide is a methodology. An ordinal comparison of supporting and non-supporting authority is statutorily mandated. Authoritative support is defined by an enumerated listing of authoritative sources in IRC Section 6662(d)(2)(B)(i).<sup>21</sup> This listing, however, is not presented in an ordinal context. Sources of primary authority have the force and effect of law. Statutes, legislative interpretations, and case law exemplify primary authority. Secondary authority, without the force and effect of law, provides guidelines and is accorded substantial weight. Some examples of secondary authority include interpretive regulations, IRS rulings, and technical advice memoranda. Because they lack an explicit guideline, tax professionals must rely on judgment in ordering and weighting authoritative sources.

Chang and McCarty (1988) provide tax professionals and tax accounting students with relevant authoritative sources and 32 variations of a case with the purpose of comparing and contrasting the resultant rankings. Subjects rank the support for the different variations of case facts. One observation reveals a high degree of consensus among the judgments of the professionals. This consensus and

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<sup>21</sup> Reg. § 1.6662-4(d)(3) also provides an unordered enumerated listing. The Secretary of the Treasury is mandated by Code Section 6662(d)(2)(D) to provide an annual listing in the *Federal Register* of positions for which there is not substantial authority.

the determined weights are consistent with previous research. However, the use of students is problematic and provides support that students are not appropriate subjects for tests of expert knowledge.

In contrast, Chow et al. (1989) ask fifty-three experienced tax practitioners to rank fifty-six authoritative sources in relation to the substantial authority standard. They report that preparers are highly consistent in their priority rankings of authoritative support, reporting a mean correlation of .79. However, with a mean correlation of .45, the study reports a low degree of consensus among preparers when asked to explain actually what constitutes substantial authority.

In summary, researchers present evidence that task input factors provide sources of bias in the JDM processes of tax professionals when used to search for and provide recommendations to clients in tax research contexts. Ambiguous issues provide the context while the vague regulatory guidelines provide the ability for motivational characteristic to infiltrate judgment and decision-making processes. Table 2.4 summarizes the results of the reviewed extant literature of the impact of task input factors on the JDM strategies of tax professionals.

#### Compliance v. Planning

When making aggressive recommendations to clients, professionals consider their exposure to risks. These risks include damage to reputation, litigation, and loss of the client (Cloyd 1995b; Milliron 1988). Risks are present in both the planning and compliance context. In planning contexts, additional risk exists because the professional gives advice before the event has taken place. The necessary fact pattern can be structured to comply with the relevant authority with the intention of reducing

uncertainty. Compliance recommendations are rendered after the transaction has occurred. As such, the facts are pre-determined and the professional must work within the transaction as structured. The incremental risk in planning results because the practitioner may provide advice that proves ineffective; therefore, justifying their recommendations becomes instrumental to the engagement (Margo 1999). Tax professionals cannot shift all risk of aggressive-reporting recommendations to clients, but they can shift more of the risk in compliance engagements than in planning engagements on the pretext that the client should have sought advice earlier (Cloyd 1995b).

After providing evidence of confirmation bias, Johnson (1993) extends her research to planning versus compliance situations. Planning tasks afford more flexibility than compliance tasks. For this reason, Johnson (1993) hypothesizes that planning research would show greater use of confirmation bias than compliance research. Results support this hypothesis.

Spilker et al. (1999) base their hypotheses on the theory that risks for the professional remain higher in a planning context than a compliance context. Because risk exposure is reduced when the tax rule is precise, the study manipulates the ambiguity of the tax issue. The sixty-three tax professional participants in the study have little knowledge of the tax issue involved. This allows the manipulation of ambiguity without consequences of prior knowledge. That is, the professional planning the structure of the tax transaction will be more conservative, even though they have the flexibility not present in a compliance context. Spilker et al. (1999) report that professionals interpret ambiguity more conservatively in planning



TABLE 2.4  
Summary of Literature on the Impact of Task Input Factors on  
Judgment/Decision-Making in Tax Research

Author(s)	Factor	Results*
Ayres, Jackson & Hite, 1989	Ambiguity	Significant
Barrick, Cloyd & Spilker, 2004	Substantial authority	Significant
Chang and McCarthy 1988	Substantial authority	Significant
Chow, Shields & Whittenburg 1989	Substantial authority	Mixed
Cloyd & Spilker, 1999	Substantial authority	Significant
Kaplan, Reckers & West 1988	Ambiguity	Significant
Klepper & Nagin, 1989	Ambiguity	Significant
Krawczyk, 1994	Ambiguity	Significant
McGill, 1988	Ambiguity	Significant
Scotchmer, 1989	Ambiguity	Significant
Smith & Kinsey, 1986	Ambiguity	Significant
Smith & Kinsey, 1987	Ambiguity	Mixed
Spilker, Worsham & Prawitt, 1999	Ambiguity	Significant

\*Significant/Not Significant designation is, generally, based upon p-value, with an  $\alpha$  of .05. However, in survey and interview studies, the designation may be the result of self-reports.

engagements. While seemingly in contrast to the results in Johnson (1993), the authors note that the level of risk in her study is minimized by incorporating an allowable deduction with the exposure being only the extent of the deduction. In the present study, the risk incorporates the possibility of overturning the entire transaction. This results in a taxable transaction rather than a nontaxable return of equity. The authors infer that planning situations mitigate bias relative to compliance situations. To provide evidence to the extent of this mitigation, the researchers compared the planning/precise subject's recommendations to those of the planning/ambiguous subjects. In planning decision contexts professionals exploit precise tax rules by recommending aggressive, client preferred positions. These results replicate the Hackenback and Nelson (1996) findings that making a more conservative recommendation is a way professionals use to mitigate the incremental risk associated with a planning context.

In summary, researchers present evidence that task output factors, the engagement contexts, provide sources of bias in the JDM processes of tax professionals when used to search for and provide recommendations to clients in tax research contexts. Table 2.5 summarizes the results of the reviewed extant literature of the impact of task output factors on the JDM of tax professionals.

**TABLE 2.5**  
Summary of Literature on the Impact of Task Output Factors on Judgment/Decision-Making in Tax Research

Author(s)	Factor	Results*
Cloyd 1995b	Compliance v. planning	Significant
Hackenbrack & Nelson, 1996	Compliance v. planning	Significant
Johnson, 1993	Compliance v. planning	Significant
Margo, 1999	Compliance v. planning	Significant
Spilker, Worsham & Prawitt, 1999	Compliance v. planning	Significant

\*Significant/Not Significant designation is, generally, based upon p-value, with an  $\alpha$  of .05. However, in survey and interview studies, the designation may be the result of self-reports.

### Confirmation Bias Research

While ambiguous information can hamper an unbiased search, the anchoring and adjusting heuristic may result in the decision maker's use of a confirmatory decision strategy. The subsequent bias, confirmation bias, can result in less than optimal decisions, even though information asymmetry is not a condition. This research inquiry presents a review of the studies related to the presence of confirmation bias in tax research.

Confirmation bias results when individuals evaluate information based upon their initial belief. That is, the process of assessing relevance, reliability, and validity of information becomes distorted. People fail to consider the possibility of irrelevance in information confirming their initial belief. Likewise, disconfirming information is

challenged (Ross 1977). Consequently, individuals remember the weakness of disconfirming information and underweight this source. On the other hand, the perceived strength of confirming information is weighted at face value (Lord et al. 1979) or overweighted. Distorted weights in JDM result in suboptimal judgments. Anderson et al. (1980) demonstrate the strength of this distortion. Their study provides evidence that people fail to revise their beliefs even after evidence has been discredited.

Johnson (1993) tests 107 tax preparers to assess how professionals evaluate authoritative evidence for an ambiguous tax issue. Subjects review the authority, assess the probability that the position favorable to their client would prevail upon challenge, and recommend a position for the client's tax return. Test administrators provide participants with the appropriate Code Sections, applicable Regulations, and four court cases. The outcomes of the judicial decisions are manipulated as the treatment in the experiment. Weights that participants assign the relevance of the court cases support the presence of the confirmation process. Those decisions believed to be adjudicated in favor of the taxpayer rate higher than those cases where the IRS is believed to prevail. The variable NETSCORE is derived by the subjects' relevance ratings for supporting and opposing decisions. A net positive rating indicates that supporting cases are more highly rated than opposing decisions; a positive NETSCORE suggests confirmation bias. The variable POSTPROB is derived from participants' assessments of the probability of success for the recommended position upon challenge. The significant ( $p < .003$ ) direct relationship between NETSCORE and POSTPROB supports the hypothesis that use of the confirmatory

process results in higher assessed probabilities of judicial success. Further testing provides evidence that higher assessed probabilities result in stronger client recommendations. Thus, client advocacy results in the use of a confirmation mechanism in judgment processes. The researchers also find a direct relationship between the strength of pro-client recommendations and the degree of client advocacy.

Cloyd and Spilker (1999) extend the research into the causes and effects of confirmation bias. Psychological studies indicate that, by overweighting information in confirming one's belief, professionals will likely increase their assessment that the belief is true (Koehler 1991). Cloyd and Spilker (1999) postulate that advocacy, by affecting information search, has an indirect effect on likelihood assessments that the client-preferred tax position will prevail under challenge. The seventy-two tax professionals participating in their study have diverse educational backgrounds. Thirty-five percent earned bachelor's degrees in accounting, fifty-eight percent possess master's degrees in accounting, and seven percent of the participants have law degrees. Utilizing twenty-four actual court cases on dealer vs. investor status, manipulations are performed on the client's preferred tax treatment. Evidence of confirmation bias is presented. Roberts (1998) notes that the results of this study show that confirmation bias can cause professionals to recommend a clearly incorrect aggressive position, thus exposing both the client and the professional to unanticipated risk.

To test the mitigating effect of education on confirmation bias, Cloyd and Spilker (2000) focus on the pedagogical differences between an academic accounting education and a legal education. Because of the increased exposure to court cases and

legal arguments, the authors hypothesize that law students will show significantly less confirmatory strategies in their tax research than do accounting students. Thirty-six law students in the second or third year of law school and 43 Masters of Accounting students are asked to assess court cases to support a client's set of facts. The desired client outcome is manipulated within groups. While both groups exhibit confirmation bias in their search strategies, law students' average usage was significantly less than that of accounting students. Without the ability to randomize, the authors address the possibility of differences being attributable to conditions other than academic training. Demographics and self-reports of knowledge are assessed to alleviate these arguments.

Placing the tax research task in a social context, Hatfield (2000) hypothesizes that accountability to a supervisor will moderate the extent of confirmation bias evident in information search by staff accountants. Hatfield (2000) bases his research on prior psychological research of accountability predicaments. Schlenker and Weigold (1989) state that an accountability predicament occurs when the decision maker's actions may not match those expected by the evaluating audience. Relating this to the tax research task, Hatfield (2000) designs his study so that the staff accountant's initial belief differs from the supervisor. The tax research analysis requires justification to the supervisor. Three JDM strategies are available in an accountability predicament: multiple advocacy, belief shifting, and defensive bolstering (Tetlock 1985). Hatfield's (2000) study focuses on belief shifting (i.e., the staff changes the initial belief (client preferred) to support the supervisor) and defensive bolstering (i.e., the staff justifies the initial belief). He coins the term secondary confirmation bias to denote an information search strategy that will confirm

a supervisor's belief. Fifty-six tax accountants are placed in an accountable or non-accountable position for the study. The subjects' choices of JDM strategies are then evaluated. Main effect of ACCOUNTABILITY is not significant. However, an interaction between ACCOUNTABILITY and STAFF OPINION is significant. Further research indicates that the accountable subjects with conservative initial beliefs who used the belief shifting strategy are less likely to confirm their initial belief than those with aggressive initial beliefs ( $p = .06$ ). More importantly, those accountable subjects who used defensive bolstering strategies support a confirmation bias ( $p = .0025$ ). The presence of bias affects final recommendations ( $p = .03$ ), as hypothesized.

Hatfield (2001) extends his prior research to evaluate the objectivity of the supervisor during a tax research task. Experience mitigates confirmation bias by reducing the likelihood of use of the strategy (Kaplan and Reckers 1989; Kida 1984). Therefore, this study investigates whether supervisors recognize the potential lack of unbiased research from lower-level staff accountants. Results indicate that supervisors recognize that staff accountants' perceived objectivity diminishes when the research confirms the staffs' initial belief. As such, more weight is accorded to a report that disconfirms an initial belief than is given to a confirming report. Therefore, supervisors are aware of the potential for confirmation bias in tax research tasks performed by staff accountants. The review process mitigates some of the bias.

Barrick et al. (2004) define accuracy and advocacy as the two primary objectives when researching tax issues. A third objective inherent in the hierarchical research process requires experienced supervisors to provide corrective feedback

necessary to enhance staff learning. With experience mitigating confirmation bias, supervisors can correct this bias in subordinate's research tasks and elicit an accurate recommendation. If this recommendation is synchronized with the client preferred position, all objectives are met. If this recommendation is not synchronized, there is a resulting tension. Designing their study to mirror this tension situation, the researchers investigate the extent to which supervisors' judgments are affected by confirmation bias in staff research reports. This study finds evidence that supervisors rate accurate tax reports as more persuasive than biased reports when the advocacy objective is not met. Additionally, supervisors find that biased reports which advocate client preference, even though incorrect, appear more persuasive than correct reports that do not advocate the preferred position. Commenting on this finding, the authors note this result suggests that supervisors find research reports that provide encouragement in tension situations more persuasive than those that do not. Additional work for biased reports (i.e., when accuracy and advocacy objectives are not the same) is requested more than when tension does not exist when evaluating the tax issues.

To summarize, researchers present evidence that processing factors provide sources of bias in the JDM processes of tax professionals when used to search for and provide recommendations to clients in tax research contexts. The use of confirming strategies in JDM, with awareness, can be mitigated by feedback (accountability) and experience. Table 2.6 summarizes the results of the reviewed extant literature on confirmation bias' presence in the JDM process of tax professionals.

TABLE 2.6  
Summary of Literature on Confirmation Bias' Presence in  
Judgment/Decision-Making in Tax Research

Author(s)	Factor	Results*
Barrick, Cloyd & Spilker, 2004	Confirmation bias	Significant
Cloyd & Spilker 2000	Confirmation bias	Significant
Hatfield 2000	Confirmation bias	Significant
Hatfield, 2001	Confirmation bias	Significant
Cloyd & Spilker 1999	Confirmation bias	Significant
Johnson, 1993	Confirmation bias	Significant
Kaplan & Reckers, 1989	Confirmation bias	Significant

\*Significant/Not Significant designation is, generally, based upon p-value, with an  $\alpha$  of .05. However, in survey and interview studies, the designation may be the result of self-reports.

### Summary

Taxpayers use tax professionals primarily to resolve uncertainty. However, improper tax advice, as opposed to improper tax return preparation, is the most prevalent error resulting in litigation liabilities to the tax professional (Katch 1992). Although regulatory agencies mandate unbiased research, illusions inherent in heuristic decision-making strategies may result in systematic biases in tax professionals' recommendations. Prior research in JDM among tax researchers supports the presence of incentives and heuristics that inhibit unbiased research.

The more salient individual motivational cognitive incentives providing biases include task-relevant knowledge and gender. Advocacy and professional status consistently suggest a significant relationship between recommendations proffered and client preferred positions. Results suggest a misunderstanding concerning acceptable risk between tax professionals and their clients. Environmental factors, including penalties and payment status, lead to aggressive recommendations. Ambiguity and the lack of guidance in the application of "substantial authority" allow professionals to confirm desired results. Although planning contexts inherently have more



professional risk, the results are mixed concerning professional JDM dependent upon context. Once systemic bias is identified, the reduction of systemic bias in JDM necessitates attention to JDM processing influences. Experience and education are shown to be effective in mitigating systemic biases.

This research inquiry incorporates various constructs from the extant literature in investigating the defense presented by litigants in tax court cases. Specifically, professional status, payment amount, client penalty, and professional penalty will be tested. Incorporating litigants at the apex of the tax administration process will implicitly assay the mitigating effects of experience, education, and accountability. Existing research views JDM in an experimental context. By using actual court transcripts, results will be based upon reality rather than conjecture. Additionally, this inquiry extends the research of confirmation bias in the JDM processes of tax professionals by providing external validity to prior findings where generalizations are confounded by internal validity needs.

## CHAPTER 3

### METHODOLOGY

The purpose of this research inquiry is to examine defenses utilized by the litigants in tax cases for evidence of the use of confirmatory processes in the search and evaluation of authoritative support. Use of confirmatory processes can inhibit one's ability to produce an unbiased defense. As previously noted, education, experience, and accountability have been identified in the tax research task literature as mitigating this suboptimal processing strategy. Nonetheless, studies of the cognitive sequences employed during tax research tasks consistently identify confirmation bias. Judgment biases and dependencies cannot be addressed unless the susceptible individuals are aware of them (Petty and Wegener 1993; Wilson and Brekke 1994). The intent of this study is to provide evidence of a dependency, if such exists, in order that tax professionals may become aware of and reduce behaviors which inhibit the ability to produce the unbiased decisions mandated by professional standards.

This chapter details how the research is conducted by establishing the hypotheses, describing the data, explaining the testing instruments, and presenting the statistical tools to be used for evaluation of the data.

### Hypothesis Development

The outcome of a compliance tax research task should be the presentation of substantial authority affirming or disaffirming the position taken by the taxpayer on an ambiguous tax issue. The previous chapter presents numerous incentives which impact the JDM processes of tax practitioners, resulting in recommendations which affirm the desired client outcome rather than an unbiased research conclusion. Although these incentives may impact the original position recommended, movement through the hierarchical review levels inherent in the research process should filter such bias out in that each step provides a review by personnel with more experience. In theory, an unbiased recommendation should evolve.

When a return establishing a position on an ambiguous tax issue is selected for audit by the appropriate regulatory agency, the position presented by the professional is challenged by disconfirming substantial authority resulting from the information search and evaluation performed by IRS tax professionals. Therefore, information asymmetry between opposing parties is disseminated with this encounter. Each litigant is made aware of seemingly disconfirming information for their position. Thus, the opportunity to attend to disconfirming information is now afforded to each party.

If the contested issues are unresolved through the audit process, the taxpayer has the right to present the case in a legal forum with legal representation. As previously noted, lawyers are less susceptible to confirmatory processing strategies than other tax professionals. Additionally, professional standards for both the accounting and legal professions mandate unbiased research. To have a reasonable

probability of prevailing in this challenge, the substantial authority outcome presented must be unbiased. If this authority is fraught with bias, the probability of prevailing is sabotaged.

In summary, the presence of incentives could inhibit unbiased recommendations. However, the hierarchical review process and the audit experience provide opportunities for resolving biases. Lawyers, because of their education and professional standards, should present unbiased defenses when representing a case in court. Therefore, the following research hypotheses are presented for empirical investigation:

- H<sub>o1</sub>: Confirmation bias is not present in the substantial authority presented by litigants in tax issues litigation before the Tax Court.
- H<sub>a1</sub>: Confirmation bias is present in the substantial authority presented by litigants in tax issues litigation before the Tax Court.
- H<sub>o2</sub>: Confirmation bias, if present, is not more prevalent in the substantial authority presented by pro se<sup>22</sup> representatives than professional representatives.
- H<sub>a2</sub>: Confirmation bias, if present, is more prevalent in the substantial authority presented by pro se representatives than professional representatives.
- H<sub>o3</sub>: Confirmation bias, if present, is not more prevalent in the substantial authority presented by taxpayers' professional representatives than professional representatives.
- H<sub>a3</sub>: Confirmation bias, if present, is more prevalent in the substantial authority presented by taxpayers' professional representatives than IRS professional representatives.
- H<sub>o4</sub>: Confirmation bias, if present, is not more prevalent in the substantial authority presented by Martindale-Hubbell rated professionals than Martindale-Hubbell non-rated professionals.

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<sup>22</sup> As in most judicial forums, taxpayers litigating before the Tax Court may represent themselves.

- H<sub>a4</sub>: Confirmation bias, if present, is more prevalent in the substantial authority presented by Martindale-Hubbell rated professionals than Martindale-Hubbell non-rated professionals.
- H<sub>o5</sub>: Confirmation bias, if present, is not more prevalent in the substantial authority presented by Martindale-Hubbell “A” rated professionals than Martindale-Hubbell “B” rated professionals.
- H<sub>a5</sub>: Confirmation bias, if present, is more prevalent in the substantial authority presented by Martindale-Hubbell “A” rated professionals than Martindale-Hubbell “B” rated professionals.
- H<sub>o6</sub>: Confirmation bias is not more prevalent in the substantial authority presented by Martindale-Hubbell non-rated taxpayer professionals than Martindale-Hubbell non-rated IRS professionals.
- H<sub>a6</sub>: Confirmation bias is more prevalent in the substantial authority presented by Martindale-Hubbell non-rated taxpayer professionals than Martindale-Hubbell non-rated IRS professionals.
- H<sub>o7</sub>: The amount of the Notice of Deficiency and related penalties does not correlate to the presence of confirmatory processing strategies for pro se representatives, taxpayer professional representatives, or IRS professional representatives.
- H<sub>a7</sub>: The amount of the Notice of Deficiency and related penalties does correlate to the presence of confirmatory processing strategies for pro se representatives, taxpayer professional representatives, or IRS professional representatives.

### Data

### Subjects

In deciding to litigate an IRS challenge, taxpayers are presented with a choice of forums. Three tribunals are available to adjudicate tax cases. One may petition for a hearing before the U. S. Tax Court (hereinafter referred to as Tax Court). By petitioning the Tax Court, abeyance of the tax deficiency is automatic until a final decision is rendered. In the alternative, taxpayers may pay the deficiency and sue for a refund in either the U. S. District Court for their jurisdiction or the U.S. Court of

Federal Claims. U.S. District Courts are empowered to decide all areas of litigation, including tax matters. The U.S. Court of Federal Claims is charged with the responsibility of deciding any claim made against the United States. The Tax Court, however, is a tribunal for tax matters only. As such, it is considered the court of technical expertise. Thus, the Tax Court is the forum chosen for investigation by this research inquiry.

Decisions rendered by the Tax Court which require an interpretation of law are "Regular" opinions. Decisions that require an interpretation of facts are "Memorandum" opinions. Therefore, those Memorandum Decisions rendered by the Tax Court during 2004 comprise the census of data for this study.

The population of Memorandum Decisions issued during 2004 is identified from tax case databases provided by Research Institute of America, Commerce Clearing House, and West Law. Two hundred and eighty-eight cases emerge as viable subjects for investigation. Each case presents two defenses of the facts and circumstances, that of the taxpayer representative and the IRS representative. Thus, the cases provide 576 defenses available for analysis.

### Sample Size

The equation for calculating the required sample size is

$$n = \left( \frac{(|z_0| + |z_0|) \sigma}{\mu_0 - \mu_1} \right)^2$$

where	$\mu_0 - \mu_1$	=	amount of acceptable error
	$ z_0  +  z_0 $	=	degree of confidence required
	$\sigma$	=	variability

With this finite population of Memorandum Decisions, using the finite population correction factor in conjunction with the required sample size formula produces the

appropriate sample size for the study. The finite population correction factor is calculated as

$$\text{finite population correction} = ((N - n) / (N - 1))^{1/2}$$

Selecting  $\alpha$  as .05 chance of the estimated population parameter being incorrect, the degree of confidence of this inquiry is set at 1.96. Instances of confirmation bias for the study are counted using a scale of zero through ten. As such, the amount of acceptable error is set as .5, or one-half of a point. The standard deviation for use in the formula, determined by a preliminary statistical analysis of thirty observations, is 2.589. From a population of 288 cases, the sample size generated in accordance with these formulas is 83 cases.

#### Random Sampling

There are two broad categories of traditional sampling methods: probability and non-probability. Probability methods incorporate the premise that each element of the population has a known probability of being selected. When properly executed, probability sampling methods ensure that the sample is representative of the census under investigation. By assigning each element in the population with an equal probability of selection, thus minimizing selection bias, simple random sampling is used to generate the subjects to be analyzed. Using the random number generator in the software package SPSS, eighty-three numbers are generated from a population of 288. These numbers are then matched to the sequential numbers assigned by the Tax Court to Memorandum Decisions based upon the date of release. A listing of cases selected is presented in Appendix A.

### Study Instruments

In the extant literature of confirmatory processing strategies used by professionals during the tax research process, the experimental instrument used to assess bias is a collection of adjudicated court cases. Manipulations are incorporated into the judicial decisions by controlling the outcome (i.e., who prevailed, the taxpayer or the IRS). Unaware of this manipulation, subjects are asked to choose and/or weight which cases they would recommend as support for a particular set of client facts and circumstances. Subjects are aware of the desired client outcome (Johnson 1993; Cloyd and Spilker 1999, 2000; Hatfield 2000, 2001).

For this research inquiry, the briefs each party submits to the court in litigation and the resulting decision issued by the judge are a replication of this schemata in an actual decision context.

Court Briefs. Adversarial defendants in tax litigations file briefs<sup>23</sup> with the Court. The Clerk of the Court then serves each party with the briefs filed by the opposition. In general, these briefs are organized as follows: *Preliminary Statement, Questions Presented, Request for Finding of Fact, Ultimate Finding of Fact, Points Relied Upon, Arguments, and Conclusion.* The section entitled *Points Relied Upon* lists, according to rank, the citations the taxpayer is presenting as support for the position taken on the relevant tax situations being litigated. As an alternative, some briefs cite the relevant authorities in a section entitled *Listing of Citations.* Cited court cases are the strongest primary authority and are listed alphabetically. In the

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<sup>23</sup> Briefs are written statements delineating one's arguments used in the litigation. Rule 151 of the United States Tax Court Rules permits an opening brief, an answering brief, and a reply brief by each party at stipulated times. If a party fails to file a timely opening brief, answering or reply briefs are not permitted for that party unless permission is granted by the Court.



following section, *Arguments*, the defendant details the reasoning used for each article of support in the listing. This discussion presents confirming information and, for unbiased research, differentiates disconfirming information relative to the facts and circumstances of the case at issue. If initially ignored in their opening brief, answering and reply briefs afford an opportunity for a defendant to differentiate the disconfirming information presented by the adversary. Note that information filed as confirming one position is disconfirming information for the opposing position.

Relative to the experimental context, a composite listing of court cases presented by both parties in *Points Relied Upon* provides the cases available to choose from. The decisions used by each party in their own briefs provide the cases chosen from the available cases. A reading of the *Arguments* section of the brief delineates the reasoning behind the inclusion of each case (i.e., as confirming information or as disconfirming information).

All briefs filed for a sample case are provided in Appendix B.

Court Opinion. The Tax Court judge renders a finding by issuing a Tax Court Memorandum Decision. In general, the document consists of two parts: Memorandum Finding of Facts and Opinion. In the Opinion section, the judge delineates the cited cases from the filed briefs that are used in resolving the tax issues at bar.

Analogous to the lab experiment, the judge's Opinion provides the expert judgment of those cases submitted by the opposing parties that actually defend the particular facts and circumstances without the anchor of desired client outcome.

The judge's opinion relative to the sample briefs is also provided in Appendix B. For the random sample of cases included in this study, twenty-eight judges rendered opinions. With nineteen presidentially appointed regular judges, this sample includes opinions from all the regular judges, 5 of the senior judges (i.e., retired and recalled as needed), and four special judges (i.e., specially appointed by the chief judge).

#### Dependant Variable

Instances of Confirmation Bias. Confirmation bias (CB) is symptomatic of attending to/overweighing confirming and ignoring/underweighing disconfirming information when using the anchoring and adjusting heuristic. By receiving briefs from the adversary, each defendant is given the opportunity to distinguish one's position from disconfirming information. If this opportunity is never taken, this inquiry counts the lapsed opportunity as an instance of confirmation bias. That is, the disconfirming information has been ignored by the professional.

One either does or does not use a confirmatory strategy in decision-making. As such, confirmation bias is a dichotomous variable (i.e., either present or not present). An element of conservation is incorporated into this inquiry by the use of relative measurement methods.

Two methodologies are employed in determining instances of confirmation bias. In accordance with a literal interpretation of the definition of this bias, the first method of determining a measurement of the dependent variable CB is that all cases presented by each party in the litigation will be compared. That is, all cases presented by the adversary should be addressed in the opposing party's briefs. If a case

presented by the adversary is either not distinguished or favorably compared with the facts of the case, an instance of bias will be recorded. One may argue that presenting a case as confirming/disconfirming information does not guarantee that interpretation. Therefore, the opposing party may determine that the adversary's interpretation of the cited case is erroneous and, consequently, chose to not mention the citation. Failing to address this inconsistency, however, presumes the correctness of one's own interpretation. This measurement is dependent variable CB(L).

In a more conservative measurement, cases presented by each party are compared with those cited by the judge in the published opinion. This method allows for a judgment that irrelevant cases can be ignored. To be included as an instance of bias, any citation by the judge must be included in a brief from either party. This condition insures that each party is made aware of the particular case. When the opposing party does not address that citation, an instance of bias is recorded. This measure of the dependent variable is CB(J).

The final count under each measurement method of instances of CB will be standardized relative to 10. As such, cases with less than or more than 10 suits cited will be placed on a comparable basis. The Data Collection Instrument is found in Appendix C.<sup>24</sup>

Other subjective areas in recording bias include litigants who do not cite cases in their briefs or fail to file any briefs. These cases will be coded as 10 Instances of Bias. Cases filed pursuant to a Motion for Summary Judgment generally do not

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<sup>24</sup> An additional methodology may also be appropriate. Combining the two chosen methodologies, a third measurement would compare cited cases between lawyers for instances of bias. Additionally, bias would be recorded for cases presented by litigants but not mentioned by the judge. This method is not used in this study because subjectivity could be problematic with this count.

involve the filing of brief. This Motion purports, by the Internal Revenue, that no issue is in contention as to interpretation of fact. The taxpayer may rebut this position by presenting cases, either through the brief process or during the trial, that present contentious interpretation of situational facts. As such, the IRS will receive a measure of 0 in Motion for Summary Judgment cases, while the taxpayer bias will be based upon filed briefs.

### Independent Variables

The focus of this inquiry is the presence of confirmation bias in the defenses presented. As such, a t-test on the dependent variable will suffice. However, if the use of confirmatory decision strategies is identified, additional investigation into the types of litigants and types of cases susceptible to the use of this strategy will follow. The following variables are collected in order to enhance this investigation of relevant characteristics.

Litigants. Four diverse groups may provide representation in tax matters before the Tax Court. The initial group is composed of taxpayers who chose to represent themselves (i.e., pro se).. However, representation before judicial forums is generally provided by lawyers. As such, these parties have been exposed to the pedagogy provided by law schools. Consequently, they are less susceptible to confirmatory strategies (Cloyd and Spilker 2000). Without a legal education, taxpayer representatives practicing before the Tax Court must qualify. Successful completion of extensive testing of legal knowledge is required. A second group of litigants, therefore, are taxpayer representing themselves who are professionally qualified. The

third group of litigants is tax professionals in private practice engaged to defend a taxpayer.

Legal counsel for the government in tax litigations are employees of the IRS. As a government employee, it is intuitive that the experience one receives differs from that of a private employee/owner. Many of the incentives introduced in the EPP model of Chapter 2 are not elemental to a government employee. Namely, environmental factors are of minimal consideration. IRS tax professionals, therefore, consist of the fourth group of litigants.

Professional Status. With the subjects of this study generally members of the legal profession, legal ability ratings are included in this study for dimensionality. *Martindale-Hubbell Law Digest* provides a peer reviewed rating for this characteristic. In order to be rated, an attorney must have been endorsed as adhering to professional standards of ethics. Legal ability is categorized as A (very high to prominent), B (high to very high), and C (good to high). This rating considers one's ability in the area of practice. These ratings are expected to improve over time. As such, they proxy for experience and expertise. The ability variable is operationalized as MHR and consists of four levels: A, B, C, or Not Rated.

Monetary Incentives. The crux of tax litigation is the Notice of Deficiency and the related penalties and interest. This monetary component of each legal exercise can be framed in the context of opposing gains and losses. A gain for the IRS is a loss for the taxpayer while a loss for the government is a gain to the taxpayer. The magnitude of the assessment could drive a perceived need to confirm a desired outcome. In addition to the amount of tax deficiency, several penalties are probable when a Notice

of Deficiency is issued. IRC Section 6651 invokes a penalty for the failure to pay taxes when they are due. IRC Section 6662 provides an accuracy-related penalty. This sanction is imposed when the tax amount due is defined as a "substantial understatement."<sup>25</sup> As such, not all taxpayers will be subject to this penalty. IRC Section 6694 imposes a sanction on the return preparer if a position taken on a return is deemed to be "unrealistic." Interest on the alleged tax deficiency is imposed under Section 6601. The cumulative amount of these monetary assessments constitutes the continuous variable MONEY.

The monetary assessment variable ranges from \$128 to \$37,709,602. To facilitate comparisons, the MONEY variable is scaled on a range of one to five. The ranges applied are depicted in Table 3.1.

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TABLE 3.1  
Monetary Assessment Rankings

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	Range
Rank 1	Below \$24,999
Rank 2	\$25,000 - \$99,999
Rank 3	\$100,000 - \$499,999
Rank 4	\$500,000 - \$999,999
Rank 5	Above \$1,000,000

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<sup>25</sup> A "substantial understatement" is defined in IRC Section 6662(d)(1)(A) as a situation in which the amount of understatement of income tax (the Notice of Deficiency amount) exceeds the greater of 10% of the tax required to be shown on the return for the year or \$5,000.

Outcome. Most often, one party prevails in the subject cases. However, the opinion may result in a “split” decision. Neither party prevails in the entirety. For example, the IRS may prevail as to the issue of inclusion of an omitted asset on an estate tax return, while the taxpayer may prevail as to the value of an omitted asset. The decision for each case will be recorded in accordance with the prevailing party as listed by Research Institute of America’s database record of the official opinion. Split decisions will be recorded as a win for each party.

A summary list of the variables examined by this study is found in Table 3.2.

TABLE 3.2 List of Variables		
CB(L)	=	Instances of Confirmation Bias – Comparison to Adversary
CB(J)	=	Instances of Confirmation Bias – Comparison to Judge
LITIGANTS	=	Four levels: Pro Se Pro Se Lawyer Taxpayer Representative Lawyer IRS Representative Lawyer
MHR	=	Four levels: Not Rated “A” Rating “B” Rating “C” Rating
MONEY	=	Cumulative Monetary Assessment
MONEYRANK	=	Monetary Assessment Rank from Table 3.1
OUTCOME	=	Win = 1 Lose = 0

With the use of actual information (i.e., the briefs filed with the Court) this archival study will have a greater degree of external validity than other research methods (i.e., experiments and simulations). With this real-life assessment, external validity threats of assumptions being at odds with reality are not inherent (Wallace 1991).

### Statistical Methodology

Analysis of variance (ANOVA) and Analysis of covariance (ANCOVA) models are used in this study. As a statistical tool, ANOVA assesses the difference in group means by testing if the group means of the independent variables are different enough to have happened not by chance. If the group means are not significantly different, they have no effect on the dependent variable. This relationship is tested for each independent variable separately and as an interaction with all other pertinent independent variables. Linear relationships are not assumed. ANCOVA identifies those variables that influence the dependent variable through assessing the error variance. After being identified as influential, the variable enters into the analysis as a covariate.

### Hypothesis 1

Hypothesis 1 investigates the presence of confirmatory strategies in defenses submitted by taxpayer representatives in Tax Court litigations. The overall test for H1 is to determine if Instances of Confirmation Bias (CB(L) and CB(J)) is significantly greater than zero for all litigants. One-variable ANOVA on the response variable CB with a test statistic of zero will elicit a statistically significant presence of this bias.



### Hypotheses 2 through 6

With significant results from Hypothesis 1, an ANOVA model will be utilized in analyzing Hypotheses 2 through 6. Hypotheses 2 and 3 are tested using a one-way ANOVA model with CB as the dependant variable and specific factor levels of the variable LITIGANT for the independent variable. A one-way ANOVA model with CB as the dependent variable and specific factor levels of the variable MHR as the independent variable will be employed to investigate Hypotheses 4 through 6.

If the data violates the assumptions of ANOVA, the non-parametric Mann-Whitney U Test will test the differences between the factor levels of each hypothesis. As a non-parametric test, the Mann-Whitney U ranks the values of the tested variables before assessing the appropriate population parameters.

### Hypothesis 7

The Pearson's Correlation Coefficient will be the statistical methodology utilized to assess any relationship between CB, the factor levels of LITIGANT, and MONEYRANK variables. In the event that the parametric assumptions are violated, Spearman's Rank Correlation Coefficient will be substituted for Pearson's to investigate any correlative relationship. Spearman's Rank Correlation Coefficient, a non-parametric method, operates identically to Pearson's Correlation Coefficient on the ranks assigned to the original data values.

### Model Assumptions

ANOVA and ANCOVA models are generally robust against violations of a normal distribution of error terms (Neter et al. 1996). However, goodness of fit of the models must be tested for serious departures from the three basic assumptions of the

models. These assumptions are: errors are independent, errors appear to have constant variances (homogeneity of variance), and errors seem to be a random sample from a normal distribution (normalcy).

Independence of the error terms is ensured by randomization. This study will randomly sample the population of cases. Consequently, the independence assumption should be satisfied

Because the factor levels of the variable LITIGANT are not equal, it is likely that the homogeneity of variances assumption is violated. Levine's Test of Homogeneity of Variances will be utilized to test for violations of this assumption.

The normality assumption can be tested by plotting error terms for the dependent variable in the form of a normal probability plot, or Q-Q plot. This plot shows the observed values against the expected values if the sample data are drawn from a normal distribution. Clustering around the expected value (i.e., the straight line) denotes meeting the assumption. Shapiro-Wilk's and Kolmogorov-Smirnov testing will assess the distributions evidenced by the study data.

Serious violations of one or more of the assumptions will confound the results of parametric testing. In the face of such violations, distribution-free methods that do not require assumptions about the distributions of the population parameters are appropriate. The non-parametric methods previously discussed will be utilized.

### Summary

Awareness of a bias is the first step necessary for mitigation. Additionally, external validity of the findings of prior research is challenged when results are experimentally derived. This study will provide an assessment of the laboratory

research findings on the confirmation bias symptomatic of the anchoring and adjustment heuristic in application. Chapter 1 presents three questions worthy of investigation. In this chapter, seven hypotheses are developed from those research questions. Additionally, the research sample is identified, the sample size is determined, and the sampling method employed is explained. Next, the data is defined and testing instruments are presented. The dependant and independent variables are described, along with an explanation of counting methodologies employed. Finally, appropriate statistical tools for assessing each hypothesis are delineated. Chapter 4 discusses the results of these statistical analyses.

## CHAPTER 4

### EMPIRICAL FINDINGS

The previous chapters contain an introduction to normative decision theory and some heuristics that individuals find essential in making judgments and decisions due to scarce resources. While these heuristics facilitate good judgment and decision-making, incentives may act to inhibit optimal JDM processes. Suboptimal processing results in biased decisions. Remedial factors, however, can mitigate the influence of negative incentives. Chapter 2 presents a review of the extant literature of the tax research task, based upon the Roberts' Economic Psychology Processing Model. From the literature, numerous incentives are identified that inhibit the JDM processes. Additionally, factors which mitigate the influence of incentives are identified. The development of hypotheses and the statistical methodology used to test the impact of incentives and remedial measures in the context of tax research and the use of confirmatory strategies are explained in Chapter 3. Chapter 4 delineates an analysis of the results derived through this testing. A descriptive summary of the data is presented first. A discussion of the results related to each hypothesis follows.

### Input Data

Of the 288 Tax Court Memorandum Decisions from the year 2004, 106<sup>26</sup> are included in this research inquiry. Generally, each decision provides two observations for the study: a taxpayer representative defense and an IRS representative defense. In most instances, each case is concerned with litigating only one tax issue. Two cases, however, provide a distinctive discussion of two separate tax issues to be determined. These two decisions, therefore, provide four observations. With 104 cases presenting one issue and 2 cases providing two issues each, there are 108 observable tax issues presented in the data. Because each party prepares a defense, there are 216 observations in the sample. The observations are distributed equally between taxpayer representatives and Service representatives. Each class contains 108 observations.

The Internal Revenue Service employs attorneys to litigate contentious issues with taxpayers. Each of the 108 defenses presented for the Commissioner, therefore, are prepared by lawyers. The taxpayer, however, may choose self-representation or the services of a professional. Of the cases in this inquiry, taxpayers represent themselves (i.e., pro se) in 56 cases and hire professional representatives in 52 instances. Of the 56 pro se defenses, three are prepared by lawyers representing themselves. The other 53 pro se representatives are from diverse backgrounds and career paths. Table 4.1 reflects this breakdown of litigants.

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<sup>26</sup> Using the required sample size equation, finite population correction factor, and the asymptotic relative efficiency adjustment described on page 91, the required sample size for this research inquiry is 86. Briefs for twenty observations in excess of the random sample requirements were secured in case some briefs were not useable for some reason. Because all cases in the sample were usable, the additional cases then were included in the study.

TABLE 4.1  
Profession of Litigants

	PRO SE	PRO SE LAWYER	LAWYER
Taxpayer Representative	53	3	52
Internal Revenue Representative	0	0	108
Total	53	3	160

In an adversarial relationship, one party generally prevails. However, in this forum, a “split” decision is possible. For example, the IRS may contend in court that there are \$10M assets omitted from an estate tax return. While the judge may rule that there are indeed omitted assets, the value may be established at \$2M. With this scenario, the IRS prevailed but not to the desired extent. Thus, each party is considered a winner. Of the 108 challenges included in this study, eight cases result in split decisions. Therefore, there are 116 successful and 100 unsuccessful defenses. The taxpayer representative prevailed in 24 decisions and the Internal Revenue won in 92 cases. Conversely, the petitioner lost in 84 challenges while the Commissioner lost in only 16 instances. Demographics by profession and litigant are provided in Table 4.2.

TABLE 4.2  
 Prevailing Party by Litigant and Profession  
 (Percentage by Litigant Class)  
 (Percentage by Cases)

	TOTAL BY CASES	PRO SE	PRO SE LAWYER	TAXPAYER REPRESENTA TIVE LAWYER	INTERNAL REVENUE LAWYER
WON	116 (100.00%)	5 (9.434%) (4.311%)*	1 (33.333%) (0.862%)*	18 (34.615%) (15.517%)*	92 (85.185%) (79.310%)*
LOST	100 (100.00%)	48 (90.566%) (48.00%)*	2 (66.667%) (2.00%)*	34 (65.385%) (34.00%)*	16 (14.815%) (16.00%)
TOTAL BY CLASS	216	53 (100.00%)	3 (100.00%)	52 (100.00%)	108 (100.00%)

\* Total by Cases

#### Instances of Confirmation Bias

Each of the briefs filed with the Court Clerk for the 108 tax issues are analyzed for instances of confirmation bias. As previously discussed, this measurement is generated using two schemes. The first measurement is generated by a comparison of the cases cited by each litigant. That is, the listing of cases presented by the taxpayer is compared to the listing submitted by the IRS. If a case cited by the petitioner is not defended by the respondent, an instance of bias is recorded for the Service. Conversely, a citation by the respondent not distinguished by the petitioner results in an instance of bias for the taxpayer. The variable resulting from this counting is labeled CB(L). An example of this methodology is provided in Table 4.3.

TABLE 4.3  
Measurement of Confirmation Bias  
Dependent Variable CB(L)

Cases Presented Taxpayer	Cases Presented Internal Revenue	Instances of Bias Taxpayer	Instances of Bias Internal Revenue
Abeles	Abeles	0	0
Rizzo		0	1
Johnson		0	1
Tadros	Tadros	0	0
	Maranto	1	0
	Elgart	1	0
	Honts	1	0
	Alta Sierra Vista	1	0
	Pyo	1	0
	Reddock	1	0
	Wallin	1	0
Score		7	2
		$7/11 = 6.36$	$2/11 = 1.82$

The alternative measurement methodology compares those cases the judge determines as instrumental in the decision process with those cases presented by the litigants. A cited case must be included in at least one brief. This stipulation assures that both litigants had the opportunity to investigate that case. If one litigant fails to discuss a listed case, one instance of bias is counted. If both litigants address a listed case, no instances of bias are recorded. The resulting variable is named CB(J). An example of this measurement is detailed in Table 4.4. Each of the 108 challenged issues is analyzed using the instrument depicted in Appendix C. For comparability, instances of bias are recorded as a percentage, with 10 representing 100%.



TABLE 4.4  
Measurement of Confirmation Bias  
Dependent Variable CB(J)

Cases Presented Taxpayer	Cases Presented Internal Revenue	Cases Cited Judge	Instances of Bias Taxpayer	Instances of Bias Internal Revenue
Abeles	Abeles	Abeles	0	0
Rizzo		Rizzo	0	1
Johnson		Johnson	0	1
Tadros	Tadros	Tadros	0	0
	Maranto	Maranto	1	0
	Elgart	Elgart	1	0
	Honts	Honts	1	0
	Alta Sierra	Alta Sierra	1	0
	Vista	Vista		
	Pyo	Pyo	1	0
	Reddock			
	Wallin			
		Monge		
		Normac		
		Marks		
		Ward		
		Union Texas		
		International		
		Co.		
		Bell		
		Karosen		
Score			5	2
			$5/9 = 5.56$	$2/9 = 2.22$

If a representative failed to file any briefs or mentioned no cases in the filed briefs, the defense is deemed fully biased and is scored as a 10. Cases presented under a Motion of Summary Judgment by the IRS are counted as zero instances of bias. With this Motion, the Service contends that the litigation does not involve an interpretation of fact; therefore, no cases are necessary. Having the burden of proof,

taxpayers must then present cases to overcome this contention through briefs or oral testimony. Thus, the taxpayer may demonstrate a confirmatory strategy in the briefs offered.

As expected, measurements range from zero to ten (100%). Frequency of scores is depicted in Table 4.5.

TABLE 4.5  
Frequency of Instances of Confirmation Bias

	CB(L)			CB(J)		
	Frequency	Percent	Cumulative Percentage	Frequency	Percent	Cumulative Percentage
0.00	53	24.5	24.5	98	45.4	45.4
.28	1	.5	25.0	-	-	-
.57	1	.5	25.5	-	-	-
.63	1	.4	25.9	-	-	-
.64	1	.5	26.4	-	-	-
.77	1	.5	26.9	-	-	-
.83	-	-	-	1	.5	45.9
.91	1	.4	27.3	1	.4	46.3
.93	1	.5	27.8	-	-	-
.94	1	.6	28.2	-	-	-
1.11	1	.5	29.7	-	-	-
1.18	1	.5	29.2	1	.5	46.8
1.25	2	.9	30.1	1	.4	47.2
1.27	1	.5	30.6	-	-	-
1.33	1	.4	31.0	-	-	-
1.42	1	.5	31.5	-	-	-
1.43	1	.4	31.9	-	-	-
1.54	-	-	-	1	.5	47.7
1.67	2	1.0	32.9	2	.9	48.6
1.82	2	.9	33.8	2	.9	49.5
1.88	1	.5	34.3	-	-	-
2.00	2	.9	35.2	6	2.8	52.3
2.10	1	.4	35.6	-	-	-
2.22	-	-	-	2	.9	53.2
2.25	1	.5	36.1	-	-	-
2.45	1	.5	36.6	-	-	-
2.50	5	2.3	38.9	6	2.8	56.0
2.56	1	.5	39.4	-	-	-
2.61	1	.4	39.8	-	-	-
2.73	1	.5	40.3	1	.5	56.5
2.86	-	-	-	2	.9	57.4
3.00	1	.4	40.7	-	-	-
3.10	1	.5	41.2	-	-	-

TABLE 4.5 (Continued)

3.16	1	.5	41.7	-	-	-
3.18	1	.4	42.1	-	-	-
3.33	-	-	-	7	3.2	60.6
3.40	1	.5	42.6	-	-	-
3.43	1	.5	43.1	-	-	-
3.45	1	.4	43.5	-	-	-
3.50	1	.5	44.0	-	-	-
3.51	1	.4	44.4	-	-	-
3.53	1	.5	44.9	-	-	-
3.57	1	.5	45.4	1	.5	61.1
3.58	1	.4	45.8	-	-	-
3.61	1	.5	46.3	-	-	-
3.67	1	.5	46.8	-	-	-
3.70	1	.4	47.2	1	.5	61.6
3.75	1	.5	47.7	-	-	-
3.79	1	.4	48.1	1	.4	62.0
3.93	2	1.0	49.1	-	-	-
4.00	2	.9	50.0	1	.5	62.5
4.12	1	.5	50.5	-	-	-
4.14	1	.4	50.9	-	-	-
4.18	1	.5	51.4	-	-	-
4.19	1	.5	51.9	-	-	-
4.21	1	.4	52.3	-	-	-
4.38	2	.9	53.2	-	-	-
4.50	1	.5	53.7	-	-	-
4.52	1	.5	54.2	-	-	-
4.53	1	.4	54.6	-	-	-
4.59	1	.5	55.1	-	-	-
4.60	1	.5	55.6	-	-	-
4.71	-	-	-	1	.5	63.0
4.75	1	.4	56.0	-	-	-
4.76	2	.9	56.9	-	-	-
5.00	7	3.2	60.1	6	2.7	65.7
5.17	1	.5	60.6	-	-	-
5.29	1	.5	61.1	-	-	-
5.33	1	.5	61.6	-	-	-
5.37	1	.4	62.0	-	-	-
5.42	1	.5	62.5	-	-	-
5.46	1	.5	63.0	-	-	-
5.48	1	.4	63.4	-	-	-
5.51	1	.5	63.9	-	-	-
5.56	1	.5	64.4	1	.5	66.2
5.71	1	.4	64.8	-	-	-
5.79	1	.5	65.3	-	-	-
5.83	-	-	-	1	.5	66.7
5.91	1	.4	65.7	-	-	-
6.00	-	-	-	1	.4	67.1
6.15	1	.5	66.2	-	-	-
6.25	3	1.4	67.6	-	-	-
6.36	1	.5	68.1	1	.5	67.6
6.40	1	.4	68.5	-	-	-
6.50	1	.5	69.0	-	-	-
6.52	1	.5	69.5	-	-	-
6.67	2	.9	70.4	5	2.3	69.9

TABLE 4.5 (Continued)

6.74	2	.9	71.3	-	-	-
6.88	1	.5	71.8	-	-	-
6.92	-	-	-	1	.5	70.4
7.14	2	.9	72.7	-	-	-
7.50	-	-	-	4	1.8	72.2
7.62	1	.4	73.1	-	-	-
7.71	1	.5	73.6	-	-	-
7.78	1	.5	74.1	-	-	-
7.90	1	.4	74.5	-	-	-
7.92	1	.5	75.0	-	-	-
8.00	1	.5	75.5	1	.5	72.7
8.13	1	.4	75.9	-	-	-
8.18	-	-	-	1	.4	73.1
8.24	1	.5	76.4	-	-	-
8.30	-	-	-	2	1.0	74.1
8.33	2	.9	77.3	-	-	-
8.50	1	.5	77.8	-	-	-
8.63	1	.4	78.2	-	-	-
8.67	1	.5	78.7	-	-	-
8.75	1	.5	79.2	-	-	-
8.81	1	.4	79.6	-	-	-
9.64	1	.5	80.1	-	-	-
10.00	43	19.9	100.00	56	25.9	100.00

Descriptive statistics of Instances of Confirmation Bias (CB) by profession of the litigant are presented in Table 4.6. As shown, IRS counsel has the smallest mean, with 1.0829 (CB(J)) and 1.8596 (CB(L)), while lawyers who represent themselves in tax litigation have the largest mean of 10 (CB(J)) and 9.8147 (CB(L)).

TABLE 4.6  
Instances of Confirmation Bias  
Descriptive Statistics by Profession of Litigant  
Descriptive Statistics by Win/Lose

	TOTAL	PRO SE	PRO SE LAWYER	TAXPAYER LAWYER	IRS LAWYER	WIN	LOSE
Number	216	53	3	52	108	116	100
Mean - CB(L)	4.4416	8.4899	10.0000	5.3682	1.8596	2.5675	6.6212
Mean - CB(J)	3.7615	8.6701	10.0000	3.9617	1.0829	1.5479	6.3292
Median - CB(L)	4.0590	10	10	5.2725	.7035	1.3345	6.7710
Median - CB(J)	2.0000	10	10	3.3370	0	0	9.1500
Mode - CB(L)	0	10	10	5	0	0	10
Mode - CB(J)	0	10	10	0	0	0	10
Standard Deviation							
CB(L)	3.73480	2.71892	.00000	2.53297	2.30255	2.97239	3.34295
CB(J)	4.24275	2.91656	.00000	3.77353	2.22753	2.81101	4.18489
Minimum - CB(L)	0	0	10	0	0	0	0
Minimum - CB(J)	0	0	10	0	0	0	0
Maximum - CB(L)	10	10	10	10	8.63	10	10
Maximum - CB(J)	10	10	10	10	10	10	10

#### Testing the Assumptions

Parametric tests for determining the differences among several population means assume three population parameters are satisfied for the use of the procedures in testing hypotheses. These assumptions are:

- Independent random sampling from each of the populations (i.e., independence assumption),
- Populations under study are normally distributed with means  $\mu_i$  that may or may not be equal (i.e., normality assumption), and
- Equal variances  $\sigma^2$  (i.e., constant variances assumption).

ANOVA and ANCOVA procedures are robust against violations of the normality assumption (Neter et al. 1996). However, serious violations of one or more of the

assumptions will confound the results of parametric testing. In the face of such violations, distribution-free methods that do not require assumptions about the distributions of the population parameters are appropriate. Each of these assumptions will now be assessed in turn.

#### Independence Assumption

Independence of the error terms is ensured by randomization. Random sampling is used to distribute idiosyncratic characteristics of the population in order to diffuse selective bias among the test subjects (Kirk 1982). This study randomly samples the population of cases. Consequently, the independence assumption should be satisfied.

#### Normality Assumption

The normality assumption is tested by plotting error terms for the dependent variable in the form of a normal probability plot, or Q-Q plot. This plot shows the observed values against the expected values if the sample data are drawn from a normal distribution. Clustering around the expected value (i.e., the straight line) denotes meeting the normality assumption. Normal Q-Q plots for the dependent variables CB(L) and CB(J) are depicted in Figure 4.1

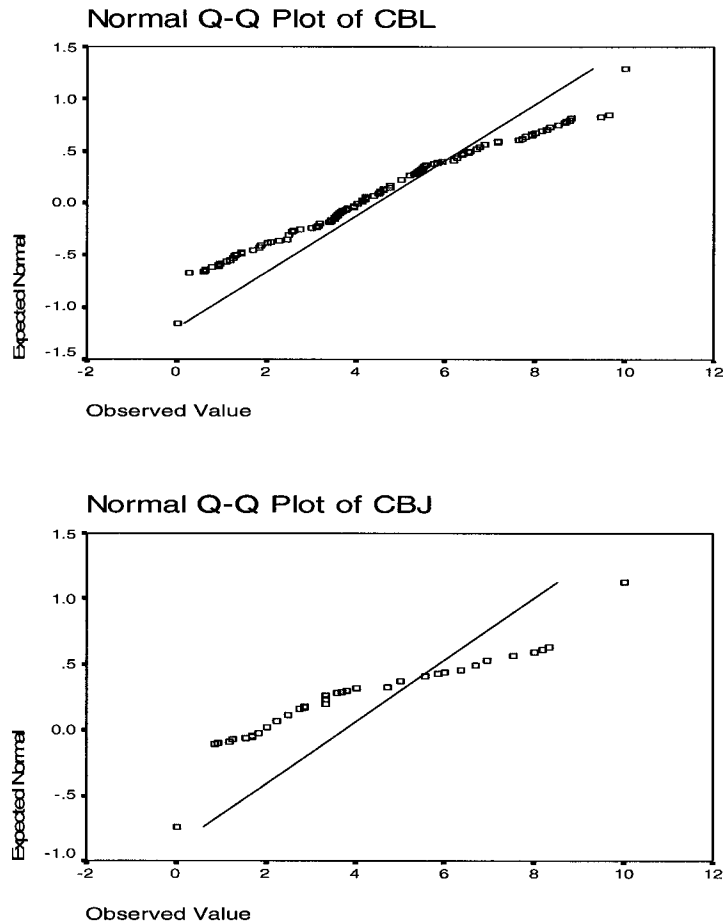


FIGURE 4.1  
Normal Probability Plots of Dependent Variables

With these plots, there is reason to doubt that the assumption of normality is met. Shapiro-Wilk's and Kolmogorov-Smirnov tests are used to derive significance levels for the data. If significance levels are small, there is strong evidence that the normality assumption is violated. With a small p-value, the null hypothesis that the samples are from a normal distribution is rejected. Results of both tests are entered in Table 4.7.

TABLE 4.7  
Normality Tests on Dependent Variables

	Kolmogorov-Smirnov <sup>a</sup>			Shapiro-Wilk		
	Statistic	df	Sig.	Statistic	Df	Sig.
CBJ	.266	216	.000	.751	216	.000
CBL	.128	216	.000	.875	216	.000

a Lilliefors Significance Correction

Both tests of normality for the dependent variables derive a p-value of .000. Therefore, the null hypothesis is rejected and there is strong evidence that the normality assumption is violated.

#### Constant Variance Assumption

The constant variance assumption is tested by deriving the p-value for the null hypothesis that the error variances are equal in the populations from which the samples were taken. The Levene's Test for Homogeneity of Variance derives this value. Table 4.8 reports the results for the test.

Using the Levene's Test for Homogeneity of Variance, each dependent variable is tested for constant variances among the factor levels. Although the study has four factor levels of litigants, the class of pro se/lawyer is not included because all values of bias for the class are constant at 10 instances. The test derives mixed results. CB(L), with p-values ranging from .493 to .963, does not reject the null of equal variances. CB(J), however, rejects the null, with a p-value of .000.



TABLE 4.8  
Constant Variance Test on Dependent Variables

Test of Homogeneity of Variance<sup>a</sup> – CB(L)

	Levene Statistic	df1	df2	Sig.
Based on Mean	.122	2	210	.885
Based on Median	.709	2	210	.493
Based on Median and with adjusted df	.709	2	172.885	.493
Based on trimmed mean	.038	2	210	.963

a CBL is constant when LITIGANT = Pro se/Lawyer. It has been omitted.

Test of Homogeneity of Variance<sup>b</sup> - CB(J)

	Levene Statistic	df1	df2	Sig.
Based on Mean	16.636	2	210	.000
Based on Median	15.205	2	210	.000
Based on Median and with adjusted df	15.205	2	192.039	.000
Based on trimmed mean	16.585	2	210	.000

b. CBJ is constant when LITIGANT = Pro se/Lawyer. It has been omitted.

With both measurements of Instances of Confirmation Bias violating the normality assumption and one measurement violating the constant variance assumption, relevant hypotheses for this research inquiry are tested using non-parametric statistical methods.

Nonparametric techniques are oftentimes necessary when the data is a count, as is the dependent variable, Instances of Confirmation Bias, in this study. As the name implies, nonparametric techniques derive no parameters. Without parameters, it

is difficult to quantify statements about the differences between two populations. Additionally, nonparametric methods convert data to ranks. In doing so, the original values are discarded; information is lost. As such, nonparametric tests are less powerful in detecting differences than are parametric methods, when parametric tests can be used.

Asymptotic relative efficiency (ARE) describes the sample size ratio necessary for a parametric procedure and nonparametric procedure to have the same ability in order to reject a null hypothesis. For the Mann-Whitney U Test, the basic nonparametric technique used for analysis in this research study, the ARE is .955. The required sample size equation, previously discussed in Chapter 3, generates a sample size of 83 cases to be randomly generated from the finite population of Tax Court Memorandum Opinions. Using 106 cases far exceeds the required ratio to achieve static ability between parametric and nonparametric methods.

### Hypotheses Analysis

#### Hypothesis 1

$H_{01}$ : Confirmation bias is not present in the substantial authority presented by litigants in tax issues litigation before the Tax Court.

$H_{a1}$ : Confirmation bias is present in the substantial authority presented by litigants in tax issues litigation before the Tax Court.

The principal hypothesis in this study is to determine whether litigants exhibit confirmatory decision strategies in the defenses presented in litigation. To assess this, the Instances of Confirmation Bias variables are tested. A one-tailed t-test, testing that the mean is greater than zero, tests Hypothesis 1. Rejecting  $H_{01}$  (t test = 17.471,  $p < .000$  for CB(L) and t test = 13.030,  $p < .000$  for CB(J)),  $H_{a1}$  is supported.

Confirmatory decision-making strategies are present in the defenses of litigants using both a precise interpretation of confirmation bias and a more conservative definition.

To determine if a specific class of litigants drives this result, each class is tested separately. As shown in Table 4.9, no class is responsible for this finding. Although the means of each class differ, each mean is significantly greater than 0. Thus, this study provides evidence from Tax Court Memorandum Opinions that confirmation bias is present in the substantial authority presented by all litigants involving tax issues litigations.

TABLE 4.9  
T-test of Confirmation Bias Variables by Class of Litigants

	t-value	df	Sig. (1-tailed)	Mean Difference	95% Confidence Interval of Mean Difference	
					Lower	Upper
Pro Se – CB(J)	21.642	52	.000	8.6701	7.8662	9.4740
Pro Se – CB(L)	22.732	52	.000	8.4899	7.7405	9.2393
Pro Se Lawyer – CB(J)	*					
Pro Se Lawyer – CB(L)	*					
Taxpayer Lawyer – CB(J)	7.571	51	.000	3.9617	2.9112	5.0123
Taxpayer Lawyer – CB(L)	15.283	51	.000	5.3682	4.6630	6.0734
IRS Lawyer – CB(J)	5.052	107	.000	1.0829	.6580	1.5078
IRS Lawyer – CB(L)	8.393	107	.000	1.8596	1.4204	2.2988

\* t cannot be computed because the standard deviation is 0.

### Hypothesis 2

Having rejected  $H_{01}$  that confirmation bias is not present in the substantial authority presented by litigants in Tax Court Memorandum Decisions, the additional hypotheses are tested.

$H_{02}$ : Confirmation bias is not more prevalent in the substantial authority presented by pro se representatives than professional representatives.

H<sub>a2</sub>: Confirmation bias is more prevalent in the substantial authority presented by pro se representatives than professional representatives.

The extant literature provides support that exposure to law school pedagogy serves to mitigate the tendency of one to use confirmatory decision strategies while engaged in a tax research task (Cloyd and Spilker 2000). Hence, it follows that materials presented by pro se litigants should exhibit more confirmation bias than the citations provided by lawyers. To test this hypothesis, the four classes of litigants are collapsed into two groups. Group One (i.e., non-lawyers) includes only those taxpayers who represent themselves and are not a lawyer by profession. Group Two (i.e., lawyers) includes the remaining three classes of litigants: pro se/lawyer, taxpayer representative lawyers, and IRS lawyers. With only two groups, the Mann-Whitney U Test provides the appropriate statistical barometer. Descriptive statistics are provided in Table 4.10.

TABLE 4.10  
Hypothesis 2: Confirmation Bias – Pro se v. Professional Representatives  
Descriptive Statistics

	CB(L)		CB(J)	
	Lawyers	Non-Lawyers	Lawyers	Non-Lawyers
Number	163	53	163	53
Mean	3.1287	8.4899	2.1654	8.6701
Mean Rank	87.80	172.15	87.98	171.61
Sum of Ranks	14312.00	9124.00	14340.50	9095.50

The Mann-Whitney U Test derives a statistic of 946.00 (CB(L)) and 974.50 (CB(J)) and both report asymptotic significance levels (1-tailed) of .000. Thus,  $H_{02}$  that confirmation bias for pro-se litigants is not significantly greater than confirmation bias for professional representatives is rejected. As expected, pro se litigants exhibit more confirmation bias than professional representatives.

### Hypothesis 3

- $H_{03}$ : Confirmation bias is not more prevalent in the substantial authority presented by the taxpayers' professional representatives than the IRS professional representatives.
- $H_{a3}$ : Confirmation bias is more prevalent in the substantial authority presented by taxpayers' professional representatives than IRS professional representatives.

As with Hypothesis 2, Hypothesis 3 concerns the difference between two groups of litigants: taxpayer's professional representatives and IRS professional representative. The focus of this hypothesis is to delineate a difference between two groups of lawyers. Assumptions of this hypothesis are that mitigating characteristics of task specific experience, task specific knowledge, education, and accountability are equal between groups. Differences are related to incentives that are, intuitively, dissimilar between government employees (i.e., IRS employees) and private practitioners. Descriptive statistics are provided in Table 4.11.

The Mann-Whitney U Test derives a statistic of 882.000 (CB(L)) and 1467.00 (CB(J)) and both report asymptotic significance levels (1-tailed) of .000. Thus,  $H_{03}$  that confirmation bias for taxpayer hired professional representative is not significantly greater than confirmation bias for IRS professional representatives is rejected.

TABLE 4.11  
Hypothesis 3: Confirmation Bias – Taxpayer’s Lawyers v. IRS Lawyers  
Descriptive Statistics

	CB(L)		CB(J)	
	Taxpayer’s Lawyers	IRS Lawyers	Taxpayer’s Lawyers	IRS Lawyers
Number	52	108	52	108
Mean	5.3682	1.8596	3.9617	1.0829
Mean Rank	117.54	62.67	106.29	68.08
Sum of Ranks	6112.00	6768.00	5527.00	7353.00

#### Hypothesis 4

$H_{04}$ : Confirmation bias is not more prevalent in the substantial authority presented by Martindale-Hubbell non-rated professionals than Martindale-Hubbell rated professionals.

$H_{a4}$ : Confirmation bias is more prevalent in the substantial authority presented by Martindale-Hubbell non-rated professionals than Martindale-Hubbell rated professionals.

Martindale Hubbell provides a peer review system for rating the technical ability of lawyers. This is a service that is requested. Having no rating is not a commentary on ability. Of the 163 legal representatives included in the sample, thirty-three possess a rating and 130 of the lawyers are not peer-reviewed. Table 4.12 presents descriptive statistics for these groups.

The Mann-Whitney U Test derives a statistic of 966.000 (CB(L)) and 1413.50 (CB(J)). Asymptotic significance levels (1-tailed) of .000 (CB(L)) and .002 (CB(J)) are reported. Thus,  $H_{04}$  that confirmation bias for Martindale-Hubbell rated lawyers is

not significantly greater than confirmation bias for Martindale-Hubbell non-rated lawyers is rejected.

TABLE 4.12  
Hypothesis 4: Confirmation Bias – Martindale-Hubbell Non-Rated Lawyers v.  
Martindale-Hubbell Rated Lawyers  
Descriptive Statistics

	CB(L)		CB(J)	
	Martindale-Hubbell Rated Lawyers	Martindale-Hubbell Non-rated Lawyers	Martindale-Hubbell Rated Lawyers	Martindale-Hubbell Non-rated Lawyers
Number	33	130	33	130
Mean	5.4108	2.5452	3.8461	1.7388
Mean Rank	117.73	72.93	104.17	76.37
Sum of Ranks	3885.00	9481.00	3437.50	9928.50

#### Hypothesis 5

$H_{05}$ : Confirmation bias is not more prevalent in the substantial authority presented by Martindale-Hubbell “A” rated professionals than Martindale-Hubbell “B” rated professionals.

$H_{a5}$ : Confirmation bias is more prevalent in the substantial authority presented by Martindale-Hubbell “A” rated professionals than Martindale-Hubbell “B” rated professionals.

Martindale-Hubbell provides three levels of rating. Of the thirty-three rated lawyers, 25 possess an “A”, 8 receive a “B”, and no lawyers in the group have a “C” rating. Descriptive statistics for these two groups are provided in Table 4.13.

TABLE 4.13  
Hypothesis 5: Confirmation Bias – Martindale-Hubbell “A” Rated Lawyers v.  
Martindale-Hubbell “B” Rated Lawyers  
Descriptive Statistics

	CB(L)		CB(J)	
	Martindale-Hubbell “A” Rated Lawyers	Martindale-Hubbell “B” Rated Lawyers	Martindale-Hubbell “A” Rated Lawyers	Martindale-Hubbell “B” Rated Lawyers
Number	25	8	25	8
Mean	5.4956	5.1456	3.6769	4.370
Mean Rank	17.38	15.81	17.02	16.94
Sum of Ranks	434.50	126.50	425.50	135.50

The Mann-Whitney U Test derives a statistic of 90.50 (CB(L)) and 99.50 (CB(J)). Exact significance levels (1-tailed) of .696 (CB(L)) and .984 (CB(J)) are reported. Thus,  $H_{05}$  that confirmation bias for Martindale-Hubbell “A” Rated attorneys is not significantly greater than confirmation bias for Martindale-Hubbell “B” Rated attorneys is not rejected.

#### Hypothesis 6

- $H_{06}$ : Confirmation bias is not more prevalent in the substantial authority presented by Martindale-Hubbell non-rated taxpayer professionals than Martindale-Hubbell non-rated IRS professionals.
- $H_{a6}$ : Confirmation bias is more prevalent in the substantial authority presented by Martindale-Hubbell non-rated taxpayer professionals than Martindale-Hubbell non-rated IRS professionals.



Twenty of the taxpayers' professional representatives are not rated by Martindale-Hubbell; none of the IRS representatives possess a rating. Descriptive statistics for these two groups are presented in Table 4.14.

TABLE 4.14  
Hypothesis 6: Confirmation Bias – Martindale-Hubbell Non-Rated Taxpayer  
Lawyers v. Martindale Hubbell Non-Rated IRS Lawyers  
Descriptive Statistics

	CB(L)		CB(J)	
	Martindale-Hubbell Non-Rated Taxpayer Lawyers	Martindale-Hubbell Non-rated IRS Lawyers	Martindale-Hubbell Non-Rated Taxpayer Lawyers	Martindale-Hubbell IRS Non-rated Lawyers
Number	20	108	20	108
Mean	5.5296	1.8596	4.4544	1.0829
Mean Rank	102.38	57.49	94.60	58.93
Sum of Ranks	2047.50	6208.50	1892.00	6364.00

The Mann-Whitney U Test derives a statistic of 322.50 (CB(L)) and 478.00 (CB(J)). Asymptotic significance levels (1-tailed) of .000 (CB(L)) and .000 (CB(J)) are reported. Thus,  $H_{06}$  that confirmation bias for Martindale-Hubbell non-rated taxpayer attorneys is not significantly greater than confirmation bias for Martindale-Hubbell non-rated IRS attorneys is rejected.

#### Hypothesis 7

$H_{07}$ : The amount of the Notice of Deficiency and related penalties does not correlate to the presence of confirmatory processing strategies for pro se representatives, taxpayer professional representatives, or IRS professional representatives.

H<sub>a7</sub>: The amount of the Notice of Deficiency and related penalties does correlate to the presence of confirmatory processing strategies for pro se representatives, taxpayer professional representatives, or IRS professional representatives.

The extant literature on the tax research task supports the positive impact of monetary incentives on aggressive recommendation for client's tax issues. Hypothesis 7 tests the correlation of this monetary incentive (Money) to Instances of Confirmation Bias by the classes of litigants. Spearman's Rank Correlation Coefficient is the most frequently used non-parametric statistic for measuring the correlation between two variables. This statistic is a derivative of the Pearson's Correlation Coefficient applied to ranked data (Aczel 2002). As a two-tailed test, a positive and a negative relationship is tested. The results of the correlation tests are shown in Table 4.15.

---

TABLE 4.15  
Correlation Coefficients – Monetary Incentive to Litigants

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Spearman's Rho Correlation Coefficient with CB(L)

	MONEYRNK	PRO SE	TAXPAYER LAWYER	IRS LAWYER
MONEYRNK Correlation Coefficient	1.000	.068	-.165	-.028
Sig. (2-tailed)	.	<b>.676</b>	<b>.322</b>	<b>.803</b>
N	174	40	38	82

Spearman's Rho Correlation Coefficient with CB(J)

	MONEYRNK	PRO SE	TAXPAYER LAWYER	IRS LAWYER
MONEYRNK Correlation Coefficient	1.000	.169	-.163	.005
Sig. (2-tailed)	.	<b>.298</b>	<b>.329</b>	<b>.966</b>
N	174	40	38	82

---

With significance levels as shown, H<sub>07</sub> is not rejected. Although there is no significant correlation for any class of litigant with the monetary assessment incentive, it is of

note that taxpayer lawyers and IRS lawyers, for the CB(L) variable, show a negative relationship. As expected, for knowledgeable litigants, as the monetary stakes rise, an unbiased defense is presented.

### Summary

With the violations of assumptions exhibited in the data, non-parametric methods of analysis are employed to investigate the hypotheses presented in Chapter 3. The empirical findings in this chapter support  $H_{a1}$ . Specifically, statistically significant results detect the presence of confirmation bias in the defenses presented by all litigants before the Tax Court. Further testing provides an evaluation by professional status of the litigants. Additionally, Chapter 5 provides a summary and a discussion of the implications of this study. Also, the limitations of the study are noted and opportunities for future research are identified.

## CHAPTER 5

### SUMMARY AND CONCLUSIONS

Optimal judgment and decision-making mandates searching for and analyzing information both confirming and disconfirming a certain perspective. Prior studies, in the experimental context, support the impact incentives have on JDM relative to a specific tax research task. These incentives prompt the researcher, unconsciously, to search and analyze information supporting the desired outcome while ignoring information that disconfirms this outcome. Extending this research, subsequent studies introduce remedial measures that serve to mitigate this unconscious tendency. Incorporating subjects from an applied situation, this study exhibits the premise that debiasing techniques are effective. Although these remedial processes are useful in reducing instances of bias in the perusal of information, the research also presents evidence that the influence of incentives remains. Thus, the degree of effectiveness of remediation needs to be improved. Enhanced awareness of this latent influence is the initial step.

First, this chapter summarizes the empirical findings of this research inquiry. Next, the implications of these results are discussed. Third, contributions and limitations of the research are delineated. Finally, suggestions for future research are considered.

### Summary of the Empirical Findings

The primary objective of this research is to detect the presence of confirmatory decision-making strategies presented by litigants in Tax Court Memorandum proceedings. Where the use of these strategies is confirmed, a secondary objective is to discern characteristics of those litigants who exhibit usage of this suboptimal JDM strategy.

The use of confirmatory JDM strategies is identified in the defenses advanced by these litigants to the Court. These professionals, through the educational process, have been exposed to methodologies necessary to accomplish unbiased research. Additionally, professional standards mandate client recommendations that are without prejudice. This finding, at the apex of the contentious legal process, is indicative of the strength that incentives exhibit in JDM. Further investigation of litigants' characteristics is warranted.

Three classes of litigants can practice before the Tax Court: pro se, lawyers, and other professional representatives that have qualified before the Court through extensive testing. Very few professionals attempt to qualify in this manner. This is supported by the representative sample randomly chosen from the 2004 proceedings. All litigants are either pro se or legal representatives; that is, none of the litigants are other qualified professionals.

Because taxes are a highly complex and technical area of expertise, it is intuitive that few taxpayers would choose to attempt their own defense. Task specific education and experience, along with accountability, are all factors that enhance the ability to prevail in a legally adversarial situation. These remedial measures are the

result of law school pedagogy and in-firm hierarchical research techniques. These factors are not characteristics found in the general population. Surprisingly, fifty-three non-lawyer taxpayers chose to present their own tax issues. The results for Hypothesis 2 support the premise that the delineated remedial measures do reduce one's susceptibility to the use of confirmatory strategies. Pro se petitioners derive a mean for Instances of Confirmation Bias of 8.4899 (CB(L)) and 8.6701 (CB(J)). These means are significantly greater than lawyers' derived means of 3.1287 (CB(L)) and 2.1654 (CB(J)). Not surprisingly, pro se litigants rarely are successful in their challenges. Self-representatives prevailed in only 9.434% of the attempts; conversely, they lost in 90.566% of the proceedings. Taxpayers who chose to represent themselves in proceeding before the Tax Court are not technically qualified to do so; consequently, they are not successful. Thus, findings of prior research on the remedial effect of education, experience, and accountability are supported in this real life application.

Having provided support for the effect of remedial measures on the propensity to use confirmatory decision strategies, testing turns to the effect of incentives on these JDM processes. Legal professionals provide a triptych: pro se representative that are also lawyers, taxpayer legal representatives, and IRS legal representatives. For pro se/legal representatives, the outcome is personal and direct. As such, incentives are subjective. However, the factors assessed in the Roberts' EPP model are incentives that impact both taxpayer legal representative and IRS legal representatives. The principle dichotomy which exists between these two groups that can influence the impact of these factors is the employment perspective. Taxpayers'

representatives practice in the private sector; therefore, their remunerations are directly and indirectly dependent upon the quality of that practice. As government employees, IRS legal representatives are not partial to this dependency. Consequently, they are not as susceptible to the impact of incentives. This theory is supported by the results of testing Hypothesis 3. With means of 5.3683 (CB(L)) and 3.9617 (DB(J)), confirmation bias exhibited by taxpayers' legal representatives is significantly greater than that exhibited by IRS legal representatives who reported means of 1.8596 (CB(L)) and 1.0829 (CB(J)) (asymptotic significance levels of .000). Taxpayer representatives are successful in the defenses in only 34.615% of their attempts. IRS representative are successful 85.185% of the time. Unbiased defenses enhance the ability to prevail.

Martindale-Hubbell provides a peer rating systems for lawyers who request a review. This rating generally improves over time. The results of Hypothesis 4 indicate that rated lawyers exhibit more bias than do non-rated lawyers (asymptotic significance levels of .000 for (CB(L)) and .002 for (CB(J))). On the surface, this finding may be counter-intuitive. Further investigation of the data indicates that very few (20.245%) lawyers are rated. Of these, no IRS lawyers are reviewed. Having demonstrated that IRS representatives have the fewest instances of confirmation bias, this large group drives the findings of Hypothesis 4.

Only the highest rated two of the three available Martindale-Hubbell ratings are incorporated in the data for this study: A ratings and B ratings. There is no significant difference in the confirmatory strategies exhibited between these groups (exact significance levels of .696 (CB(L)) and .984 (CB(J))).

The extant literature on the tax research task supports the positive impact of monetary incentives on aggressive recommendations for client's tax issues. This study finds a negative correlation between the amount of the monetary assessment and confirmatory JDM strategies used by taxpayers' legal representatives. This relationship, however, is not statistically significant. No significant correlations are found. It is noted that the mean of monetary assessment is much less for pro se litigants (mean = \$101,708) than for taxpayers' professional litigants (mean = \$2,674,479). Thus, when larger amounts are at risk, taxpayers generally employ professional representation.

#### Implications of the Findings

Petitioning the Tax Court to review the appropriateness of the Commissioner's tax deficiency determination for contested tax issues is the culmination of a long and arduous audit procedure. The process is informative for disconfirming stances. That is, there is no paucity of opportunities to reassess one's position and the probability of prevailing. The participants of the process are assumed to be lawyers and accountants at the apex of their profession in both education and experience. For these reasons, supportable defenses should evolve. On the whole, this assumption is not supported as investigation of the data determines that over half (51.85%) of the taxpayers represent themselves. The appropriateness of this decision is called into question when only 9.434% of these attempts prevail. With very little prospect of success, pro se litigants may have inappropriate incentives for proceeding through the audit process to the Tax Court level of contention.



Representing oneself in tax litigation is a right and a personal choice. Inappropriate personal choice, however, are a supercilious use of community resources. With Section 6674, the Tax Court is capable of monitoring apropos contests. Similar to the circuit courts ability to adjudicate a case as “frivolous” and assess repayments of excess costs, this section allows the Tax Court to assess up to \$25,000 for repayment for stipulated conditions. Section 6674, however, is rarely invoked. Of the 108 contested issues, three result in assessments under Section 6674. In numerous opinions, the judge discusses invoking this assessment but then provides the reasoning why he defers from acting on it. This explanation generally involves the taxpayer or representative heeding a warning early in the proceedings. This logic, however, conveys the notion that frivolity is applicable only to the legal process and not the audit process. It also infers that taxpayers are responsible for knowledge of only portions of the Tax Code. Section 6674, a procedural statute, has been a part of the Code as long as Section 162, a taxing statute. Strengthening this statute by a more frequent invocation where appropriate could reduce this supercilious use of resources. Additionally, presenting this statute to the taxpayer early in the audit process may serve to change the taxpayer’s and tax professional’s assessment of the viability of challenging the Commissioner’s determinations.

This study supports the extant literature in the areas of the impact of both incentives and remediations in the tax research task. An awareness of the influence of incentives on the unconscious heuristic processes constitutes the initial remedial step. The significant relationships of the dependent variable and the four classes of litigants provide support of the strong influence of incentives. Additionally, the effectiveness

of debiasing measures is shown. The degree of necessary effectiveness, however, is lacking. Professional standards are not being met. While one may argue that unbiased research would result in no challenges, the reality is that unbiased research will result in fewer challenges. The resulting proceedings should be on point. The dichotomy between defenses will then be a result of different weightings of confirming/disconfirming information. Within this context, contests are not frivolous but necessary. Underweighting disconfirming information is subjective while ignoring disconfirming information is objective.

Adherence to professional standards mandating unbiased research is questioned by the findings of this research. The study of cognitive biases in the legal profession is a relatively young and quite controversial stream of research. Additionally, in self-reports from taxpayers, the expected probability for prevailing in a challenged tax issue is 70% (Hite et al. 1992). There is a large margin between the actual percentage of prevailing (34.615%) and 70%. Elemental to this disparity is the definition of client advocacy. These findings imply that the way tax professionals define advocacy may differ from their clients' understanding of advocacy.

#### Contributions of this Study

A major criticism of experimental studies is the lack of external validity. To date, the studies investigating confirmation bias in the tax research task are in an experimental context. Similar to the findings in Rachlinski's (1994) research inquiry into hindsight bias and tort cases, this study, with the applied setting, provides insight into real life situations and support for the laboratory findings. Evidence for the presence of confirmatory decision strategies in application serves to bring the research

out of the laboratory. As such, this study reiterates the effect of incentives, the mitigation provided by remedial measures, and the need for more extensive debiasing in the tax research task.

#### Limitations of the Study

One assumption of the present study is that challenges to tax issues are engaged in with the intent of prevailing. This is, in fact, a limitation of the study. A reading of the briefs and formal opinions leads one to recognize that presenting an unbiased defense is oftentimes not the reason behind some challenges. This is seen ubiquitously in the pro se litigants. The forum is seen as a place to, among other reasons, vent frustration or request leniency. On one hand, a variation of this is the tax protester who states that the tax laws are baseless, either constitutionally or because of complexity. Another variant is the taxpayer who respects the tax laws but for a professed reason, usually sickness, could not comply. The court reminds these taxpayers that the judicial jurisdiction is to enforce compliance with laws; Congress makes the laws and defines acceptable exceptions. On the other hand, the IRS has been known to repeatedly challenge a tax issue deemed inappropriately addressed by statute. The logic of this strategy is that attention is being generated for perceived loopholes. Hopefully, the attention may result in appropriate statutes. Thus, this research is limited by the assumption that tax issue challenges are all statutorily founded.

For one measure of Instances of Confirmation Bias, judges provide the expert judgments used to measure the bias. Judges are, in fact, humans too. To assess the “expert” ability of judges, a study of appealed cases is necessary. This is beyond the

scope of this work. Thus, assuming that judges are unbiased is a limitation of this inquiry. A small number of cases are appealed and an even smaller number are overturned and remanded at the appellate level. Thus, the prejudices and biases potentially brought to the Court by judges are not considered a serious limitation.

Defenses are often inherited from other professional practitioners (i.e., compliance contexts). This study assumes that inappropriate defenses will be changed as the process evolves. The impact of this inter-professional relationship is beyond the scope of this study and, as such, is a limitation.

Most importantly, this study's strength is the external validity. The effects of incentives and remediations are seen in the diversity of defenses presented. Specific incentives or remedial measures cannot be singled out as would be the methodology of an experiment with treatment effects. Without this ability, one must look to dissimilarities among the classes of litigants for obvious characteristics and rely on prior research to interpret these differences.

#### Opportunities for Future Research

In the context of testing in an applied situation, the current research could be extended to include a testing of the judge's expert judgment. Appealed cases would provide the data for such a study. Additionally, the same technique used in this study could be employed to assess the use of confirmatory decision strategies in defenses presented in the other available venues for challenging the Commissioner (e.g., the United States Court of Claims). Differing results would provide additional opportunities for research.

Other cognitive bias may lend themselves to operationalization and research through the information provided in Tax Court briefs.

Central to this dissertation is the assertion that awareness is the initial step in mitigating suboptimal processing. Publication in appropriate periodicals and presentations in proper forums aimed at educating tax professionals about this proclivity are necessary.

APPENDIX A  
CASE LISTING

## APPENDIX A

### CASE LISTING

#### TAX COURT MEMORANDUM DECISIONS (106 Cases / 108 Decisions)

T.C. Memo 2004-1	InterTAN, Inc. v. Commissioner
T.C. Memo 2004-4	Csaba L. Magassy and Frances H. Magassey v. Commissioner
T.C. Memo 2004-5	Life Care Communities of American, Ltd., A Florida Limited Partnership, Robert W. McMichal, A Partner other than the Tax Matters Partner
T.C. Memo 2004-10	Robert K. Lowry and Dawn E. Lowry v. Commissioner
T.C. Memo 2004-11	Graceann Berry v. Commissioner
T.C. Memo 2004-14	Alfred J. Martin v. Commissioner
T.C. Memo 2004-20	Scott Roman v. Commissioner
T.C. Memo 2004-24	Vicki S. Pless and Coy E. Pless, Jr. v. Commissioner
T.C. Memo 2004-27	Estate of Emanuel Trompeter, Deceased, Robin Carol Trompeter Gonzales and Janet Ilene Trompeter Polachek, Co-Executors v. Commissioner
T.C. Memo 2004-29	Sunoco, Inc. and Subsidiaries v. Commissioner
T.C. Memo 2004-31	Paul R. Peete v. Commissioner
T.C. Memo 2004-33	Tony J. Cavender v. Commissioner
T.C. Memo 2004-34	Dolores Nelson v. Commissioner
T.C. Memo 2004-37	H. Dee Johnson, Jr. and Mary L. Johnson n.k.a. Mary L. Alpine v. Commissioner
T.C. Memo 2004-41	Alec Jeffrey Megibow v. Commissioner
T.C. Memo 2004-43	Charlotte's Office Boutique v. Commissioner
T.C. Memo 2004-48	Edward P. Heaphy v. Commissioner
T.C. Memo 2004-50	Albert G. Cooper v. Commissioner
T.C. Memo 2004-53	Vision Info Services, LLC v. Commissioner
T.C. Memo 2004-56	Gerald E. Johnson and Dorothy Johnson v. Commissioner
T.C. Memo 2004-57	Pamela J. Ellison v. Commissioner

T.C. Memo 2004-60	Edward D. Tonitis v. Commissioner
T.C. Memo 2004-65	Phillip Aaron and Gladies Aaron v. Commissioner
T.C. Memo 2004-70	Gary T. Mackey v. Commissioner
T.C. Memo 2004-72	Early Robertson, Jr. v. Commissioner
T.C. Memo 2004-76	Cindy Driggers v. Commissioner
T.C. Memo 2004-81	Thomas W. Hunter, Jr. v. Commissioner
T.C. Memo 2004-84	Andrea J. Vuxta v. Commissioner
T.C. Memo 2004-88	Dennis Burbridge and Rosemary Burbridge v. Commissioner
T.C. Memo 2004-89	Catherine Rosenthal v. Commissioner
T.C. Memo 2004-90	Virginia Ferguson fka Virginia. Del Bosque and Estate of Armand J. Del Bosque, Deceased, Lori Del Boeque, Special Administrator, et al. v. Commissioner
T.C. Memo 2004-93	Theresa E. Bartman fka Theresa Albrecht v. Commissioner
T.C. Memo 2004-97	Scott William Katz v. Commissioner
T.C. Memo 2004-98	Jay Mukherjee v. Commissioner
T.C. Memo 2004-101	Segudino Razo, et uv. v. Commissioner
T.C. Memo 2004-102	Angela Barriga fka Angela Robledo v. Commissioner
T.C. Memo 2004-107	William H. Johnston and Nancy S. Johnston v. Commissioner
T.C. Memo 2004-111	James J. Milner and Marilyn R. Milner v. Commissioner
T.C. Memo 2004-114	Victor Woods v. Commissioner
T.C. Memo 2004-119	Antionette J. Dato-Nodurft v. Commissioner
T.C. Memo 2004-123	Estate of Michel Dunia, Deceased, Renee Hawley and Michel Dunia, Jr., Executors and Trustees v. Commissioner
T.C. Memo 2004-126	Jack Carson Coleman v. Commissioner
T.C. Memo 2004-129	Marion Goldin v. Commissioner
T.C. Memo 2004-135	William L. Kidd and Marsha G. Kidd v. Commissioner
T.C. Memo 2004-138	James Dirks v. Commissioner
T.C. Memo 2004-139	Robert B. Kemp, Jr. v. Commissioner
T.C. Memo 2004-142	Roy J. Chase v. Commissioner
T.C. Memo 2004-145	Manuel Julian Diaz v. Commissioner
T.C. Memo 2004-146	Paul McGowan v. Commissioner
T.C. Memo 2004-150	Estate of Jose Martinez, Deceased, Patrick G. Martinez, Personal Representative v. Commissioner
T.C. Memo 2004-153	Robert B. Kemp, Jr. v. Commissioner



T.C. Memo 2004-156	Jerry L. Hill and Valerie J. Hill v. Commissioner
T.C. Memo 2204-159	Charles Edwin Lykes v. Commissioner
T.C. Memo 2004-165	Mary J. Toney v. Commissioner
T.C. Memo 2004-168	Peggy A. Farley v. Commissioner
T.C. Memo 2004-171	Thomas G. Collier v. Commissioner
T.C. Memo 2004-173	Edman Hackworth and Debbie Kay Hackworth v. Commissioner
T.C. Memo 2004-175	Kenneth J. Barella v. Commissioner
T.C. Memo 2004-179	Ragnhild A. Westby v. Commissioner
T.C. Memo 2004-181	Annette L. Morello v. Commissioner
T.C. Memo 2004-182	Vincent Michael Coomes v. Commissioner
T.C. Memo 2004-183	Nancy M. O'Neill, Petitioner and Robert B. Wollow, Intervenor v. Commissioner
T.C. Memo 2004-185	Herbert C. Haynes, Inc. v. Commissioner
T.C. Memo 2004-188	Robert D. Shirley and Ana M. Shirley v. Commissioner
T.C. Memo 2004-189	Kaing Chin and Hae Kyung Baek v. Commissioner
T.C. Memo 2004-190	Maureen Monsour v. Commissioner
T.C. Memo 2004-196	Amaro A. Taibo v. Commissioner
T.C. Memo 2004-200	John Weller Wood, Jr. and Magdalena Frances Wood v. Commissioner
T.C. Memo 2004-202	Thomas G. Brenner v. Commissioner
T.C. Memo 2004-203	George N. Gerakois aka Jorge N. Gerakois v. Commissioner
T.C. Memo 2004-206	Timothy J. Phelan and Deborah A. Phelan v. Commissioner
T.C. Memo 2004-207	Menard, Inc. and John R. Menard v. Commissioner
T.C. Memo 2004-209	Albert M. Kun v. Commissioner
T.C. Memo 2004-212	Della H. Knorr, Petitioner, and Duane J. Knorr, Intervenor v. Commissioner
T.C. Memo 2004-214	Mark R. Halcott v. Commissioner
T.C. Memo 2004-215	Jane Freed v. Commissioner
T.C. Memo 2004-217	Margie E. Robertson v. Commissioner
T.C. Memo 2004-218	Joseph A. DelVecchio and Carol DelVecchio v. Commissioner
T.C. Memo 2004-219	Beiner, Inc. v. Commissioner
T.C. Memo 2004-223	Richard Hamzik v. Commissioner
T.C. Memo 2004-227	Norma A. Cohen v. Commissioner
T.C. Memo 2004-229	Mitchell F. Skrizowski v. Commissioner

T.C. Memo 2004-230	Wendlyn H. Albin v. Commissioner
T.C. Memo 2004-231	Kathryn Ann Picchiottino v. Commissioner
T.C. Memo 2004-237	Theodore W. Banis, Jr. v. Commissioner
T.C. Memo 2004-238	Hector Castillo and Mooneem Castillo v. Commissioner
T.C. Memo 2004-243	Thomas F. Noons v. Commissioner
T.C. Memo 2004-245	Delinda Vianne Rogers v. Commissioner
T.C. Memo 2004-246	John R. Rinn and Donnie J. Rinn v. Commissioner
T.C. Memo 2004-248	Richard Rewerts v. Commissioner
T.C. Memo 2004-251	David G. Turner v. Commissioner
T.C. Memo 2004-253	Thomas Samuel Lear v. Commissioner
T.C. Memo 2004-254	Robert Lee McElroy, Jr. v. Commissioner
T.C. Memo 2004-256	Greg William Gouveia, et ux., et al. v. Commissioner
T.C. Memo 2004-260	Joseph R. Rollins v. Commissioner
T.C. Memo 2004-262	Roger Leslie Wolman and Caroline R. Wolman v. Commissioner
T.C. Memo 2004-264	Robert Lee, Jr. v. Commissioner
T.C. Memo 2004-266	Donald J. Barnes and Beverly A. Edwards fka Beverly A. Barnes v. Commissioner
T.C. Memo 2004-269	Gary D. Hansen and John F. Hansen v. Commissioner
T.C. Memo 2004-276	James G. Jaroff and Linda C. Jaroff v. Commissioner
T.C. Memo 2004-279	Glenn A. Mortensen v. Commissioner
T.C. Memo 2004-280	Delaware Corp., et al. v. Commissioner
T.C. Memo 2004-281	Orneal Kooyers ad Martha Kooyers, et al. v. Commissioner
T.C. Memo 2004-283	Stephen James Caputi v. Commissioner
T.C. Memo 2004-286	Estate of Howard Gilman, Deceased, Bernard D. Bedrgreen and Natalie Moody, Executors v. Commissioner
T.C. Memo 2004-287	Michael J. Barkley v. Commissioner

**APPENDIX B**

**SAMPLE BRIEFS AND OPINIONS**

## APPENDIX B

## SAMPLE BRIEFS AND OPINIONS

United States Tax Court.  
 Thomas W. HUNTER, Jr. Petitioner,  
 v.  
 COMMISSIONER OF INTERNAL REVENUE, Respondent.  
 No. 9856-02.  
 April 21, 2003.

Brief for the Petitioner  
 James David Leckrone (LJ0735), 3100 West End Avenue, American Center, Suite 1050,  
 Nashville, TN 37203, (615) 292-8300.

## \*2 TABLE OF CONTENTS

I. Citations ...	3
II. Preliminary Statement ...	4
III. Statement of the Issue ...	4
IV. Proposed Findings of Fact ...	4
V. Statement of Points Relied upon by the Petitioner ...	6
VI. Legal Argument ...	7
VII. Conclusion ...	16

## \*3 CITATIONS

## CASES:

Abeles v. Commissioner, 91 T.C. 1019 (1988), acq. 1989-31 I.R.B. 4 ... 8, 10, 12,  
 14, 15

Rizzo, Virgil v. Davis, (1979, D.C.P.A.) 43 A.F.T.R. 2nd 79-985, 79-1 U.S.T.C.  
 Para. 9310, Affd. (1980, CA3) 624 F2nd 1091, Cert. Den. (1981, SCT) 450 U.S. 919  
 ... 10

Lewis E. Johnson v. Commissioner, (1980 C.A. 5) 611 F 2nd 1015, 45 AFTR 2nd 775  
 ... 11

## CODE SECTIONS:

Internal Revenue Code Section 6212(b) ... 6, 8, 10, 15

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## TREASURY REGULATIONS:

Treasury Regulations Section 302.6212-1(a) ... 9, 11, 12

## INTERNAL REVENUE PRONOUNCEMENTS:

Revenue Procedure 90-18, 1990-1 C.B. 491 ... 9, 12, 13, 14

Revenue Procedure 2000-18, 2001-8 I.R.B.(2/20/2002) ... 9

## CHIEF COUNSEL ADVICE:

CCA 200230033 (7/26/2002) ... 10, 16

\*4 II.

## PRELIMINARY STATEMENT

This case involves deficiencies determined by the Respondent on income taxes for the taxable years 1991, 1992, 1993, 1994, 1995, and 1996. Notices of Deficiency were dated January 28, 1999. Petitioner filed his Petition with the Tax Court on June 10, 2002. Respondent filed a Motion to Dismiss for lack of jurisdiction on October 1, 2002 and the Petitioner filed a Motion to Dismiss for lack of jurisdiction on October 28, 2002. Motions were heard before the Honorable Stephen J. Swift on February 10, 2003, in Nashville, Tennessee. Stipulations of Fact were submitted at the hearing, as well as testimony from the Petitioner.

III.

## STATEMENT OF THE ISSUE

The issue to be decided in this case is whether or not the Notices of Deficiency dated January 28, 1999 were sent to the Petitioner's last known address, as required Section 6212(b) of the Internal Revenue Code.

IV.

## PROPOSED FINDINGS OF FACT

The Petitioner requests that the Court find the following facts:

1. On November 19, 1998, the Internal Revenue Service Center in Memphis, Tennessee processed a Form 2848, Power of Attorney and Declaration of Representative dated October 23, 1998 from the Petitioner. (Stip. Paragraph 5)
2. The Form 2848 filed by the Petitioner reflects in box 1 that the Taxpayer's name and address was Thomas W. Hunter, 2200 New Hope Road, Hendersonville, TN #5 37075. (Stip. Paragraph 5, Exhibit 1-J)
3. The listing of the address as 2200 New Hope Road was a typographical error and the taxpayer's actual address is 2220 New Hope Road. Petitioner testified that there is no such address as 2200 New Hope Road and he would have received any correspondence addressed to 2200 New Hope Road. (Petitioner's testimony)
4. Box 7 of the Form 2848 which was filed with the Internal Revenue Service directs that original notices and other communications be sent to the Petitioner

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and a copy to the first and second representatives listed on the Power of Attorney. (Stip. Paragraph 5, Exhibit 1-J)

5. January 28, 1999, the Respondent issued statutory notices of deficiency for the taxable years 1991, 1992, 1993, 1994, 1995 and 1996, addressed to the Petitioner at 122 Wayne Drive, Gallatin, TN 37066. (Stip. Paragraphs 9, 10, and 11)

6. Petitioner did not and has never received copies of any Notices of Deficiency issued by the Internal Revenue Service for the years 1991, 1992, 1993, 1994, 1995, and 1996. (Petitioner's testimony)

## ULTIMATE FINDINGS OF FACT

7. Petitioner's filing Form 2848, Power of Attorney and Declaration of Representative on October 23, 1998, was clear and concise notification to the Internal Revenue Service of a different address than that contained on his last previously filed tax return or any previous Form 2848 and constitutes the last known address made known to the Internal Revenue Service.

\*6 8. The Notices of Deficiency issued by the Internal Revenue Service for the taxable years 1991, 1992, 1993, 1994, 1994, 1995 and 1996 on January 28, 1999 were not issued to the Petitioner's "last known address" in accordance with Section 6212(b) of the Internal Revenue Code.

## V.

## STATEMENT OF POINTS RELIED UPON BY THE PETITIONER

The Petitioner is entitled to a finding that the Respondent failed to issue Notices of Deficiency for the years 1991, 1992, 1993, 1994, 1995 and 1996 to the Petitioner's last known address as required by Section 6212(b) of the Internal Revenue Code because:

1. Section 6212(b) of the Internal Revenue Code requires that Statutory Notices of Deficiency be mailed to the taxpayer's "last known address".

2. Case law, Internal Revenue Procedures, and Treasury Regulations all define a taxpayer's last known address as the address that appears on the taxpayer's most recently filed and properly processed Federal Tax Return unless the Internal Revenue Service is given clear and concise notification of a different address.

3. The Petitioner moved from his old address, at 122 Wayne Drive, Gallatin, TN 37066 to his new address at 2220 New Hope Road, Hendersonville, TN 37075 in September of 1998.

4. Petitioner filed a Form 2848 Power of Attorney on October 23, 1998 with the Internal Revenue Service Center in Memphis, Tennessee which was processed on November 19, 1998. This Power of Attorney notified the Service of his new address.

\*7 5. Respondent mailed Notices of Deficiency for the taxable years 1991, 1992, 1993, 1994, 1995 and 1996 addressed to the Petitioner at 122 Wayne Drive, Gallatin, TN 37066 on January 28, 1999.

6. Petitioner did not and has never received copies of the above Notices of Deficiency issued by the Internal Revenue Service.

7. Treasury Regulation 301.6212 states "a taxpayer's last known address is the address that appears on the taxpayer's most recently filed and properly processed Federal Tax Return, unless the Internal Revenue Service (IRS) is given clear and concise notification of a different address.

## VI.

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## LEGAL ARGUMENT

## FACTS

The facts in this case are fairly undisputed. The parties submitted and agreed to stipulations of the facts and the Petitioner testified at the hearing for the Tax Court on February 10, 2003. Respondent issued the Statutory Notices for the taxable years involved on January 28, 1999 addressed to the Petitioner at 122 Wayne Drive, Gallatin, TN 37066. According to the Petitioner's testimony, which was undisputed by the Respondent, the Petitioner had moved from this address in September of 1998. Some time after July 29, 1997, the beginning of the Respondent's examination of the Petitioner's income tax returns, Petitioner had submitted a Form 2848 Power of Attorney directly to the Revenue Agent. On November 19, 1998, the Memphis Service Center processed a new Form 2848 Power of Attorney dated October 23, 1998 which was filed by the Petitioner changing his authorized representatives and his address. That \*8 form provided the Service with his new address of 2220 New Hope Road, Hendersonville, TN 37075. The Power of Attorney did contain a typographical error in that the address was shown as 2200 New Hope Road, Petitioner testified at the trial that there is no such address as 2200 New Hope Road and he would have received any correspondence or mail addresses to 2200 New Hope Road.

It is not clear whether or not the Respondent is relying on the address contained in the original Power of Attorney filed with the Revenue Agent or the Petitioner's most recently filed tax return prior to January 28, 1999. There is no indication in the record of this case what address was included on the Petitioner's most recently filed tax return prior to January 28, 1999. For purposes of the major portion of this argument, Petitioner is assuming that this most recently filed tax return was the 1997 tax return and the address would have been 122 Wayne Drive, Gallatin, TN 37066. If this were not the case, the only issue to be decided is whether or not the Power of Attorney filed with the Memphis Service Center in the fall of 1998 superseded the Power of Attorney previously filed with the Revenue Agent.

## HISTORY

Section 6212(b) of the Internal Revenue Code clearly requires the Internal Revenue Service to send a Statutory Notice of Deficiency to the taxpayer's last known address by certified or registered mail. What constitutes the "last known address" is not defined by statute and has produced much litigation. The Tax Court has defined the taxpayer's last known address as the address which appears on his most recently filed and properly processed Federal Tax Return unless the Internal Revenue Service has been given clear and concise notification of a different address, *Abeles v. Commissioner*, 91 T.C. 1019 (1988), acq. 1989-31 I.R.B.4. The Abeles \*9 opinion contains a thorough discussion of the term "last known address". The Internal Revenue Service acquiesced in that opinion and also issued Revenue Procedure 90-18, explaining its position on how a taxpayer is to inform the Internal Revenue Service of a change of address. Rev. Proc. 90-18, 1990-1 C.B. 451. The Abeles case and Revenue Procedure 90-18 contained the primary guidance in effect on January 28, 1999 when the Notices of Deficiency in this case were issued by the Internal Revenue Service. Revenue Procedure 90-18 was amplified and superseded by Revenue Procedure 2001-18, 2001-8 I.R.B. (02-20-2001), subsequent to the date the Notices were issued herein. While there were no Treasury

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Regulations addressing "last known address" at the time the Notices of Deficiency were issued in this case, Treasury Regulations were subsequently issued which referred to Revenue Procedure 90-18. Treasury Regulation Section 301.6212-2. The Treasury Regulations specifically state that the "last known address" is the address that appears on the **taxpayer's** most recently filed and properly processed Federal Tax Return, unless the Internal Revenue Service is given clear and concise notification of a different address.

## ARGUMENT

The primary focus of the Abeles opinion is directed to whether or not the Service could issue Notices of Deficiency to a **taxpayer** at the address on his or her tax returns filed for the **taxable** years which were covered by the Notices of Deficiency or was required to exercise reasonable care and diligence in ascertaining and mailing of the Notice of Deficiency to the last address given to the Internal Revenue Service by the **taxpayer**.

There seems to be no cases decided in the United States Tax Court directly addressing the effect of the filing of a Power of Attorney on the "last known address" rule. The question has \*10 been addressed by a United States District Court in *Virgil R. Rizzo v. Status*, 79-1 U.S.T.C. Par. 9310; 43 A.F.T.R. 2nd 985 (1979). In that case, the Internal Revenue Service sent the Notice of Deficiency to the address contained on a Power of Attorney which the **taxpayer** had filed with the Internal Revenue Service on April 4, 1977. The Notices were issued on October 20, 1977. The address contended for by the Plaintiff was the address that appeared on the Plaintiff's returns from 1976 to 1979. The court stated that the Internal Revenue Service was justified in relying on the address contained in the Power of Attorney as the **taxpayer's** "last known address".

With regard to the Power of Attorney itself, Petitioner would address the court's attention to an advice issued by the Chief Counsel of the Internal Revenue Service on May 15, 2002. CCA 200230033. In this advice, Chief Counsel for the Internal Revenue Service addresses the role of a Power of Attorney in the context of issuing Notices of Deficiency under Section 6212 of the Internal Revenue Code. While the advice involves Powers of Attorney which were filed with the tax returns, the Chief Counsel does note in Paragraph 3 of his Conclusions that "where there is a valid Power of Attorney, the directive of the **taxpayer** regarding notices and other written communications as indicated on Line 7 of Form 2848 is to be respected only by the year(s) covered by the Power of Attorney. Line 7 on the Power of Attorney filed by the Petitioner specifically directs that original notices and other written communications were to be sent to the Petitioner and it would seem unreasonable to require the **taxpayer** to add additional language on the Power of Attorney stating that "those notices should be sent to the address I am giving you with this Power of Attorney".

In his analysis of the law, the Chief Counsel for the Internal Revenue Service states, in referring to the Abeles case, that the phrase "last known address" does not necessarily mean the \*11 **taxpayer's** actual address, but instead means the last address that the **taxpayer** makes known to the Service (emphasis supplied). In discussing the Power of Attorney, the Chief Counsel further notes that a Power of Attorney that is valid contains a "clear and concise expression of the **taxpayer's**



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intention as to the scope of the authority being granted to the representative". It appears to the Petitioner that the Chief Counsel for the Internal Revenue Service considers a valid Power of Attorney to be "clear and concise".

That the Internal Revenue Service itself has recognized that a Power of Attorney would serve as notice for a change of address is also found in the Internal Revenue Service Manual. While Petitioner has been unable to ascertain the exact language that was contained in the Internal Revenue Service Manual in 1999, there is a 1980 case which quotes the language at that time. In *Lewis E. Johnson v. Commissioner*, 611 5th F2d 1015; 45 A.F.T.R. 2nd 775, the Court quotes Paragraph 4462.1(3) of the Internal Revenue Service Manual as follows:

"Ordinarily, the statutory notice will be sent to the address shown on a taxpayer's return. However, be very careful in determining the address to be used if the taxpayer has specifically notified the Service of a different address. Thus, a statutory notice sent to the last known home address of the taxpayer would be invalid if a power of attorney is submitted which specifically directs that all correspondence, documents, etc., relating to the tax matter be sent to the taxpayer in care of the taxpayer's attorney. Therefore, if there is any doubt as to what constitutes the last known address of the taxpayer, duplicate original statutory notices should be sent by certified mail to each known address. Internal Revenue Service Manual Section 4462.1(3)." *Johnson*, at 1018.

The Court's attention is also directed to the current Treasury Regulation 301.6212-2(a). Although this Treasury regulation was not adopted until January 29, 2001, it does refer to Revenue Procedure 90-18 for further information. It seems clear that the Treasury Department \*12 views this Treasury regulation as being based on the law as established in the *Abeles* case and the Internal Revenue Service's position as established in Revenue Procedure 90-18. That regulation clearly states:

"Except as provided in paragraph (b)(2) of this section, a taxpayer's last known address is the address that appears on the taxpayer's most recently filed and properly processed Federal tax return, unless the Internal Revenue Service (IRS) is given clear and concise notification of a different address. Further information on what constitutes clear and concise notification of a different address and a properly processed Federal tax return can be found in Rev. Proc. 90-18 (1990-1 C.B. 491) or in procedures subsequently prescribed by the Commissioner."

It is the Petitioner's position that the United States Tax Court in the *Abeles* case, the Internal Revenue Service and Revenue Procedure 90-18 and the Treasury Regulation 301.6212-2 clearly establish that for the "last known address" to be determined there be:

1. Clear and concise;
2. Notification;
3. Of a different address.

Let's review each of these requirements separately. First of all, Petitioner does not understand how anyone can argue that a properly completed and executed Form 2848 Power of Attorney which is produced by the Internal Revenue Service is not clear and concise. The fact is that the Chief Counsel for the Internal Revenue

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Service recognizes that the language of a valid Power of Attorney is a clear and concise notification by the **taxpayer** and a clear and concise expression of the **taxpayer's** intention. The printed language on the form which was produced by the Internal Revenue Service, clearly states the directive of the **taxpayer** to the Internal Revenue \*13 Service to send all original notices and other written communications to the **taxpayer**. In drafting the Form 2848, it doesn't appear that the Internal Revenue Service felt it necessary to additionally state on Line 7 on Form 2848 that these notices would be sent to any address other than the address provided by the **taxpayer** on Line 1 of Form 2848.

Secondly, Form 2848 is clearly a notification and was filed with the Internal Revenue Service Center as specifically required by Section 4.02 of Revenue Procedure 90-18.

Thirdly, there also seems to be no doubt that the address contained in the Form 2848 filed by the Petitioner was a different address than the address which had previously been provided to the Internal Revenue Service.

Section 4.02 of Revenue Procedure 90-18 clearly states that:

"if the **Taxpayer** no longer wishes the address of record to be the one shown on the most recently filed return, for instance, because the **Taxpayer** moved after the return was filed, clear and concise written notification of a change of address must be sent to the Internal Revenue Service Center serving the **Taxpayer's** old address or to the **Taxpayer** Service Division in the local district office."

In this case, there is no dispute that the Power of Attorney with the Petitioner's new address was sent to the Internal Revenue Service Center serving the Petitioner's old address. The only question seems to be whether or not the clear and concise notification to the Internal Revenue Service actually contains the words "this is a change of address". It should be noted that the filing of a **tax** return which includes a new address does not contain any specific direction from the **taxpayer** that the Internal Revenue Service should change his address. In addition, it should be noted that presently the Internal Revenue Service automatically updates its records for changes of address filed with the United States Post Office. This procedure is described in the present \*14 Treasury Regulation Section 301.6212(b)2 and there is no requirement by the Service in that procedure for a **taxpayer** to have specifically told the Internal Revenue Service that he desired his address to be changed.

It appears that the only other argument that the Respondent can make that Form 2848 was not a clear and concise notification of a different address would be that Revenue Procedure 90-18 5.04(1) requires that the notification also includes a statement by the **taxpayer** that the **taxpayer** "wishes the address of record changed to a new address". Revenue Procedure 90-18 purports to set out the law as it was established in the Abeles case. Nowhere in the Abeles case is there any statement which requires the notification to express the desire of the **taxpayer**. The Court specifically holds that "a **taxpayer's** last known address is that address which appears on the **taxpayer's** most recently filed return, unless Respondent has been given clear and concise notification of a different address". Further indication that there is no requirement or need for a statement of the desire or wishes of the **taxpayer** is found when we look at the only two other methods of establishing a

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"last known address". Under the Revenue Procedures and the Abeles case the methods of establishment of a "last known address", other than clear and concise notification, is the filing of a tax return or a notification of change of address to the United States Post Office. Neither the filing of the Federal Tax Return or the filing of a change of address with the United States Post Office, represents any expression or statement on the part of the tax payer to the Internal Revenue Service that he desires or wishes to have his address changed.

The Court in Abeles addressed the fairness of the methods it set forth for taxpayer's to use to inform the Internal Revenue Service of a new address. This purpose was to establish certainty for the Internal Revenue Service and for taxpayers in the determination of a taxpayer's \*15 "last known address". The Abeles opinion states that the Court's previous decisions have been partly based upon who they were willing to attribute knowledge of the information contained in a recently filed return. They noted that "the state of the Internal Revenue Service's computer capabilities is such that a computer search of the information retained with respect to a certain taxpayer, including their last known address, may be performed by a Respondent's Agent with unreasonable effort or delay". Abeles, at 1029. The Court further stated "in so holding, we are merely reiterating our position that what is of significance is what Respondent knew at the time the Statutory Notice was issued \*\*\* and attributing to Respondent information which Respondent knows or should know with respect to a taxpayer's last known address, through the use of its computer system." Abeles, at 1030.

At the beginning of this argument the Petitioner noted that this argument is based on the assumption that the Respondent is relying on the "last known address" of the Petitioner as being the most recently filed tax return, although there is nothing in the record to indicate the address that was on that return. In the event Respondent's position is that the "last known address" was the address included on the Power of Attorney filed with the Revenue Agent at the beginning of Petitioner's tax examination then Respondent is admitting that it is proper for the Internal Revenue Service to rely on the filing of a Power of Attorney in establishing a taxpayer's "last known address" for purposes of Section 6212(b) of the Internal Revenue Code. Then the only question at issue is whether or not the Service should be required to check the computer file for any subsequent Powers of Attorney filed. The Court in the Abeles case recognized that "today, however, the state of the IRS's computer capabilities is such that a computer search of the information obtained with respect to a certain taxpayer, including their last known address, may \*16 be performed by Respondent's agent without unreasonable effort or delay." Abeles, at 1029. If the Court were to hold that the Internal Revenue Service could rely upon a previously filed Power of Attorney obtained in an agent's file for purposes of issuing a Statutory Notice of Deficiency without checking for subsequently filed Powers of Attorney, the Service could completely ignore a subsequently filed Power of Attorney which might specifically direct the Service to send original notices to a taxpayer's representative. This would completely undermine the opinion of the Chief Counsel to the Internal Revenue Service that the directive of the taxpayer regarding notices and other communications, as indicated on Line 7 Form 2848 was to be respected by the Internal Revenue Service. CCA 200230033 Para. 3 of Conclusions.

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**Taxpayers** should be able to know that when they file a Power of Attorney with the Service in accordance with the instructions given by the Service that the Service will take note of the information contained in that Power of Attorney. The statute provides a means for the **taxpayer** to be provided notice of a proposed **tax** deficiency in order for the **taxpayer** to avail himself or herself of the opportunity to litigate the determination of a deficiency before he or she has to make payment of the liability. To this end, the Internal Revenue Service should be required to use reasonable care and diligence in ascertaining the **taxpayer's** correct address and mailing the Statutory Notice to that address.

## VIII.

## CONCLUSION

Wherefore, petitioners pray that this Court determine that the Petitioners are entitled to the relief sought and such other and further relief as the Court may deem fit and proper.

**Thomas W. HUNTER, Jr.** Petitioner, v. **COMMISSIONER OF INTERNAL REVENUE**, Respondent.  
2003 WL 23518410  
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United States Tax Court.  
 Thomas W. HUNTER, Jr., Petitioner,  
 v.  
 COMMISSIONER OF INTERNAL REVENUE, Respondent.  
 No. 9856-02.  
 May 9, 2003.

Answering Brief for Respondent  
 B. John Williams, Jr., Chief Counsel, Internal Revenue Service.

Of Counsel: Kevin M. Brown, Division Counsel, (Small Business/Self-Employed),  
 Jeff P. Ehrlich, Area Counsel, (Small Business/Self-Employed; Area 3), William W.  
 Kiessling, Associate Area Counsel (SB/SE), Rebecca Dance Harris, Senior Attorney  
 (SB/SE), 810 Broadway, Suite 400, Nashville, TN 37203, (615) 250-5500.

\*i CONTENTS

PRELIMINARY STATEMENT ...	1
RESPONDENT'S OBJECTIONS TO PETITIONER'S PROPOSED FINDINGS OF FACT ...	2
ARGUMENT ...	3
CONCLUSION ...	14

\*ii CITATIONS

CASES:

Aboles v. Commissioner, 91 T.C. 1019 (1988) ...	6, 10-12
Alta Sierra Vista, Inc. v. Commissioner, 62 T.C. 367 (1974) ...	7
Elgart v. Commissioner, T.C. Memo. 1996-379 ...	10
Honts v. Commissioner, T.C. Memo. 1995-532 ...	10
Maranto v. Commissioner, T.C. Memo. 1999-266 ...	10
Pyo v. Commissioner, 83 T.C. 626 (1984) ...	7
Reddock v. Commissioner, 72 T.C. 21 (1979) ...	10
Tadros v. Commissioner, 763 F.2d 89 (2nd Cir. 1985) ...	7, 8

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Wallin v. Commissioner, 744 F.2d 674 (9th Cir. 1984) ... 7

## CODE SECTIONS:

I.R.C. § 6212 ... 5  
 I.R.C. § 6212(b) ... 6  
 I.R.C. § 6213(a) ... 5, 13  
 I.R.C. § 7502 ... 5, 13

## REGULATIONS:

Treas. Reg. § 301.6212-2 ... 11

## \*iii MISCELLANEOUS:

Revenue Procedure 61-18, 1961-2 C.B. 550 ... 10  
 Revenue Procedure 90-18, 1990-1 C.B. 491 ... 8-12  
 Revenue Procedure 2001-18, 2001-1 C.B. 708 ... 9

## \*1 PRELIMINARY STATEMENT

A hearing was held before the Honorable Stephen J. Swift on February 10, 2003 on the cross-motions to dismiss for lack of jurisdiction. The evidence consists of a written Stipulation of Facts containing paragraphs 1 through 14 and Exhibits 1-J through 6-I and 7-R. The Court designated April 11, 2003, as the date for the petitioner to file an opening brief and May 12, 2003, as the date for the respondent to file an answering brief. Additionally, the Court limited the parties' briefs to twenty (20) pages. All references to federal statutes are to the Internal Revenue Code of 1986, as in effect during the tax years in issue, unless otherwise specified.

## \*2 RESPONDENT'S OBJECTIONS TO PETITIONER'S PROPOSED FINDINGS OF FACT

The respondent agrees and objects to the Petitioner's proposed findings of fact as follows:

1. No objection.
2. No objection.
3. The respondent objects to that portion of this proposed finding of fact which states that the "listing of the address as 2200 New Hope Road was a typographical error" on the basis that the only proof in the record for this statement is the petitioner's self-serving statement.
4. No objection.

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5. No objection.

6. The respondent objects to this proposed finding of fact on the basis that the only proof in the record is the petitioner's self-serving statements.

The respondent objects to the petitioner's proposed requests for ultimate findings of fact as follows:

7. The respondent objects to this proposed finding of fact on the basis that it is not a fact but a conclusion not supported by the evidence.

8. The respondent objects to this proposed finding of fact on the basis that it is not a fact but a conclusion not supported by the evidence.

## \*3 ARGUMENT

Before addressing the legal arguments in this case, a brief review of the facts is warranted. Sometime prior to July of 1997, the respondent initiated an examination of the petitioner's 1991, 1992, 1993, 1994, 1995 and 1996 income tax returns. During the course of that examination and prior to the petitioner's alleged move to 2220 New Hope Road, Hendersonville, Tennessee 37075, the petitioner, on July 29, 1997, submitted a Form 2848, Power of Attorney and Declaration of Representative, directly to the Internal Revenue Service revenue agent working the case. (Stip., ¶ 2). On August 6, 1998, the respondent issued his Revenue Agent's Report (the "30 day letter") with respect to the taxable years 1991, 1992, 1993, 1994, 1995 and 1996. The 30-day letter was addressed to the petitioner at 122 Wayne Drive, Gallatin, Tennessee 37066. (Stip., ¶ 3). The petitioner received the 30-day letter on August 13, 1998. (Stip., ¶ 4). The petitioner did not, however, respond in any way to the 30-day letter. (Stip., ¶ 8).

Having had no response to the 30-day letter, the respondent, on January 28, 1999, issued statutory notices of deficiency with respect to the taxable years 1991, 1992, 1993, 1994, 1995 and 1996. Three (3) separate notices of deficiency were issued to the petitioner. One was for the taxable year 1991, one was for the taxable years 1992, 1993 and 1994 and one was for the taxable \*4 years 1995 and 1996. (Stip., ¶¶ 9-11). Each of the notices of deficiency was addressed to the petitioner at 122 Wayne Drive, Gallatin, Tennessee 37066, which was the address on the petitioner's most recently filed income tax return. (Stip., ¶¶ 9-12). The notice of deficiency for the taxable year 1991 and the notice of deficiency for the taxable years 1995 and 1996 were returned to the respondent as unclaimed by the petitioner despite three (3) attempts at delivery. (Stip., ¶¶ 13 and 14). There is nothing in the record to indicate that the notice of deficiency for the taxable years 1992, 1993 and 1994 was ever returned to the respondent. On January 28, 1999, the petitioner and his wife still owned the property at 122 Wayne Drive, Gallatin, Tennessee. (Ex. 7- R; Tr. 16-17).

On November 19, 1998, after issuance of the 30-day letter but prior to the issuance of the notices of deficiency, the petitioner filed a Form 2848 with the respondent's Memphis Service Center. (Stip., ¶ 5). Unlike with the Form 2848 filed on July 29, 1997, the petitioner did not file this Form 2848 with the Internal Revenue Service revenue agent working his case nor did he provide a copy of this

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Form 2848 to the Internal Revenue Service revenue agent working his case. (Stip., ¶ 6). The Form 2848 filed by the petitioner on November 19, 1998, does not provide that the respondent is to send original notices and written communications to the petitioner's representative. \*5 (Ex. 1-J). Additionally, the Form 2848 filed by the petitioner on November 19, 1998, contained an address of 2200 New Hope Road, Hendersonville, Tennessee 37075. (Ex. 1-J).

Over three (3) years after the issuance of the notices of deficiency, the petitioner, on June 10, 2002, filed a petition with this Court with respect to the notices of deficiency for the taxable years 1991, 1992, 1993, 1994, 1995 and 1996. On October 1, 2002, the respondent, pursuant to I.R.C. §§ 6213(a) and 7502, filed a Motion to Dismiss for Lack of Jurisdiction on the basis that the petition was not timely filed. Thereafter, the petitioner, on October 29, 2002, filed a Motion to Dismiss for Lack of Jurisdiction alleging that the notices of deficiency were invalid because they were not mailed to the petitioner's "last known address."

The issues in this case are straight forward. First, were valid notices of deficiency issued to the petitioner? In particular, were the notices of deficiency issued to the petitioner's "last known address" within the meaning of I.R.C. § 6212? And, if the notices of deficiency issued to the petitioner are valid, was the petition timely filed within the meaning of I.R.C. §§ 6213 (a) and 7502? As set forth in more detail below, the notices of deficiency issued to the petitioner on January 28, 1999 were issued to the petitioner at his "last known address" and are, therefore, valid. As such, when the \*6 petitioner did not file his petition with this Court until June 10, 2002, said petition was not timely and this Court does not have jurisdiction.

Section 6212(b) of the Internal Revenue Code of 1986 requires the Internal Revenue Service to send the notice of deficiency to the taxpayer's "last known address." In determining whether a notice of deficiency has been mailed to a taxpayer's "last known address," this Court held in *Abeles v. Commissioner*, 91 T.C. 1019 (1988), that a taxpayer's last known address "is that address which appears on the taxpayer's most recently filed return, unless respondent has been given clear and concise notification of a different address." 91 T.C. at 1035. The parties stipulated that the address on the petitioner's "most recently filed return" on the date the notices of deficiency were issued was the 122 Wayne Drive, Gallatin, Tennessee address. (Stip., ¶ 12). Thus, the issue in this case hinges on whether the respondent received "clear and concise notification of a different address" prior to the issuance of the notices of deficiency.

The Tax Court has established the following frequently cited rule:

while the Commissioner is bound to exercise reasonable diligence in ascertaining the taxpayer's correct address, he is entitled to treat the address appearing on a taxpayer's return as the last known in the absence of clear and concise notification from the \*7 taxpayer directing the Commissioner to use a different address.

*Alta Sierra Vista, Inc. v. Commissioner*, 62 T.C. 367, 374 (1974) (citations omitted); See *Wallin v. Commissioner*, 744 F.2d 674, 676 (9th Cir. 1984). Establishing a presumption that the taxpayer's "last known address" is the address on his most recent return also establishes a clear starting point for the Internal



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Revenue Service's determination. A notice of deficiency mailed to that address will be sufficient, unless the taxpayer subsequently communicates "clear and concise" notification of a change of address.

Correspondence bearing an address different from that on the most recent return does not, by itself, constitute clear and concise notice. See, eg., *Tadros v. Commissioner*, 763 F.2d 89, 92 (2nd Cir. 1985) (letter from taxpayer did not indicate that taxpayer had permanently moved or that address on letterhead was his new place of residence, nor did it mention the old address or indicate that it was no longer to be used); *Alta Sierra Vista*, 62 T.C. at 375 (new address on letterhead insufficient to notify Internal Revenue Service "that such address had replaced [taxpayer's] former address and that the former address was no longer to be used"); Cf. *Byo v. Commissioner*, 83 T.C. 626, 637-38 (1984) (filing of Form 872 bearing old address did not supplant address on most recent return). In order to supplant the address on his most recent return, the taxpayer must clearly indicate \*8 that the former address is no longer to be used. *Tadros*, 763 F.2d at 92.

At the time the notices of deficiency were issued in the case at bar, Revenue Procedure 90-18, 1990-1 C.B. 491, prescribed the procedure for providing "clear and concise notification" to the Internal Revenue Service. For situations relevant herein, Revenue Procedure 90-18 provides that a taxpayer can either send "clear and concise written notification of a change of address" to the Service Center serving the taxpayer's old address, to the Chief, Taxpayer Service Division in the local district office or, if a taxpayer is under audit, to the Internal Revenue Service employee who is working the taxpayer's case. Rev. Proc. 90-18, 1990-1 C.B. 491, 492. Revenue Procedure 90-18 specifically defines "clear and concise written notification" as

a statement signed by the taxpayer informing the Service that a taxpayer wishes the address of record changed to a new address. In addition to the new address, this notification must contain the taxpayer's full name, signature, old address, and social security number and/or employer identification number. . . . In all cases, clear and concise written notification must be specific as to a change of address.

1990-1 C.B. 491, 494. Revenue Procedure 90-18 further states that "[t]he Service is currently developing a new form (Form 8822) that taxpayers will be able to use to send clear and concise written notification of a change of address to the Service". 1990-1 C.B. at 492. The Form 8822, Change of Address, \*9 was available and in use during 1998 and 1999. (Although Revenue Procedure 90-18 has been amplified and superseded by Revenue Procedure 2001-18, 2001-1 C.B. 708, the portions cited herein have not changed other than to specifically provide that a Form 8822 may be used as a clear and concise written notification of a change of address).

The petitioner did not file a Form 8822. (Stip., ¶ 7). Instead, the petitioner relies upon a Form 2848 filed with the respondent's Memphis, Tennessee Service Center on November 19, 1998, to argue that he provided "clear and concise written notification" to the Internal Revenue Service of his change of address. The petitioner's reliance on the Form 2848 filed on November 19, 1998 is misplaced. First, the address on the Form 2848 is not even the petitioner's correct address. (Ex. 1-J; Tr. 18-19). Secondly, and more importantly, the purpose of a Form 2848

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is not to notify the Internal Revenue Service of a change of address but to establish a person or persons who are authorized by a taxpayer to represent him/her/it before the Internal Revenue Service. The Form 2848 filed by the petitioner does not contain a "statement signed by the taxpayer informing the Service that a taxpayer wishes the address of record changed to a new address" nor does it contain the taxpayer's old address. 1990-1 C.B. at 494. Moreover, the Form 2848 is, in no way, "specific as to a change of address." Id.

\*10 The one exception to a Form 2848 not constituting a change of address is when the Form 2848 specifically provides that the respondent is to send original notices and written communications to the representative (rather than the taxpayer). In that case (and that case only), the respondent has stated that he will treat the address of the taxpayer's representative as the taxpayer's "last known address." See Revenue Procedure 61-18, 1961-2 C.B. 550. This Court recognizes this exception. See *Reddock v. Commissioner*, 72 T.C. 21 (1979); *Maranto v. Commissioner*, T.C. Memo. 1999-266; *Elgart v. Commissioner*, T.C. Memo. 1996-379; *Honts v. Commissioner*, T.C. Memo. 1995- 532. This exception is not, however, present in the case at bar. The Form 2848 filed by the petitioner on November 19, 1998, provided that the originals were to be sent to the petitioner with copies to his representatives.

The petitioner acknowledges that this Court's decision in *Abeles* and Revenue Procedure 90-18 "contained the primary guidance in effect on January 28, 1999 when the Notices of Deficiency in this case were issued by the Internal Revenue Service." Page 9, Brief for the Petitioner. Interestingly, however, the petitioner offers no explanation for why he ignored the specific guidance provided by Revenue Procedure 90-18. Clearly, the petitioner could have filed a Form 8822 and avoided this problem. Moreover, in failing to follow the requirement set forth in Revenue Procedure 90-18, 1990-1 C.B. 491, 494, that the notification contain "a statement signed by the taxpayer informing the Service that a taxpayer wishes the address of record changed to a new address," the petitioner argues that neither the filing of a tax return nor the filing of a change of address with the United States Post Office represents a statement by the taxpayer "that he desires or wishes to have his address changed." Page 14, Brief for the Petitioner. With respect to the filing of a tax return, what the petitioner fails to recognize is that there is no need for the taxpayer to provide such a statement with this document as the law specifically provides that the filing of a return will constitute a change in the petitioner's "last known address." *Abeles v. Commissioner*, 91 T.C. 1019 (1988). As regards the filing of a change of address with the United States Post Office, while the law has recently changed, the law in effect on January 28, 1999, the date the notices of deficiency were issued in the case at bar, specifically provided that "notification to the U.S. Postal Service does not constitute the clear and concise written notification that is required to change a taxpayer's address of record with the Service." Rev. Proc. 90-18, 1990-1 C.B. 491, 492. (Treas. Reg. § 301.6212-2 which is relied upon by the petitioner for the proposition that the filing of a change of address with the United States Post Office constitutes notice to the Internal Revenue Service of a change of address was not adopted until January 11, 2001 and thus, was not in effect on January 28, 1999).

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The petitioner would like this Court to believe that any document which contains a new address constitutes "clear and concise notification" of a change of address. This is simply not the law. As recognized by Revenue Procedure 90-18, not every document which contains an address constitutes "clear and concise notification" of a change of address. For instance, a new address on a Form 4868, Application for Automatic Extension of Time to File U.S. Individual Income Tax Return, "will not be used by the Service to update the taxpayer's address of record." Rev. Proc. 90-18, 1990-1 C.B. 491, 494. Clearly, if a Form 4868 which is so closely related to a Form 1040 does not constitute "clear and concise notification" of a change of address, a Form 2848 which merely provides for another individual(s) to represent a taxpayer can not be said to constitute "clear and concise notification" of a change of address.

In conclusion, the Form 2848 submitted by the petitioner and received at the Memphis Service on November 19, 1998 does not constitute "clear and concise notification" of a change of the petitioner's address. *Abeles v. Commissioner*, 91 T.C. 1019, 1035 (1988); Rev. Proc. 90-18, 1990-1 C.B. 491. The address on the petitioner's most recently filed tax return was 122 Wayne Drive, \*13 Gallatin, Tennessee 37066. The notices of deficiency at issue in this case were addressed to the petitioner at 122 Wayne Drive, Gallatin, Tennessee 37066. As such, the notices of deficiency were issued to the petitioner's "last known address" and are valid. The petitioner did not file his petition with this Court until June 10, 2002, which date is 1229 days after the mailing of the notices of deficiency. The petition was not filed with the Court within the time prescribed by I.R.C. §§ 6213(a) or 7502. The respondent's Motion to Dismiss for Lack of Jurisdiction should, therefore, be granted.

## \*14 CONCLUSION

It follows that the Respondent's Motion to Dismiss for Lack of Jurisdiction should be granted.

Thomas W. HUNTER, Jr., Petitioner, v. COMMISSIONER OF INTERNAL REVENUE,  
Respondent.  
2003 WL 23518411  
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United States Tax Court.  
 Thomas W. HUNTER, Jr., Petitioner,  
 v.  
 COMMISSIONER OF INTERNAL REVENUE, Respondent.  
 No. 9856-02.  
 July 8, 2003.

Reply Brief for the Petitioner  
 James David Leckrone, 3100 West End Avenue, American Center, Suite 1050,  
 Nashville, TN 37203, (615) 292-8300.

## \*2 TABLE OF CONTENTS

I. Citations ...	3
II. Argument ...	4
IV. Conclusion ...	7

## \*3 I.

## CITATIONS

## CASES:

Abeles v. Commissioner, 91 T.C. 1019 (1988) ...	5,6,7
Tadros v. Commissioner, 763 F.2d 89 (2nd Cir. 1985) ...	4

## CODE SECTIONS:

I.R.C. Section 6212 ...	5
-------------------------	---

## MISCELLANEOUS:

Revenue Procedure 61-18, 1961-2 C.B. 550 ...	4
Revenue Procedure 90-18, 1990-1 C.B. 491 ...	4,5,6

## \*4 II.

## ARGUMENT

A. The following are specific comments regarding the Answering Brief filed by the Respondent in this case.

1. Page 4 of the Respondent's Brief, Respondent recognizes that the Petitioner filed a Form 2848 on November 19, 1998 with Respondent's Memphis Service Center.

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Respondent emphasize that the Petitioner did not file this Form 2848 with the Internal Revenue Agent working his case or provide the Agent with a copy of the Form 2848. Revenue Procedure 90-18, 1990-1 C.B.491 specifically provides for clear and concise written notification to be sent to the Internal Revenue Service Center serving the taxpayer's old address.

2. Respondent notes in the first full paragraph on page 5 of the Answering Brief that Petitioner filed a Petition with this Court over three (3) years after the issuance of the original issuance of the Notices of Appearance. Respondent's records would show that during this three (3) year period, Petitioner was pursuing all avenues for administrative relief that were available to him.

3. Page 7 of Respondent's Brief. Respondent cites the Tadros case at 763 f.2nd 1992, stating that the Taxpayer must clearly indicate that the former address was to no longer be used. The Tadros case merely notes this as one item which was missing in the taxpayer's notification.

4. On page 13 of Respondent's Brief, Respondent cites Revenue Procedure 61-18, 1961-2 C.B. 550, for the proposition that Form 2848 is only to constitute a change #5 of address when the Form 2848 specifically provides that the Respondent is to send original notices and written communications to the Taxpayer's representative. That Revenue Procedure simply states that the Internal Revenue Service will recognize the address of the Taxpayer's duly authorized representative as constituting the last known address of the Taxpayer when a filed Power of Attorney requests that all communications be mailed to the representative's address. It further specifically states "a determination as to what is the Taxpayer's last known address will still be made on the basis of the particular facts involved, the requirements of Section 6212(b) of the Code and the applicable case law". *Id.*

B. Respondent relies heavily on Revenue Procedure 90-18. Page 11 of Respondent's Brief refers to Revenue Procedure 90-18 as being the law in effect on January 28, 1999. Revenue Procedure 90-18 provides guidance regarding a change of address, but it is merely the position of the Internal Revenue Service as to its interpretation of the law as expressed in *Abeles v. Commissioner*, and other cited cases interpreting the language of Section 6212 of the Internal Revenue Code. In order to determine what the law requires, the focus must be on the court's opinion in the *Abeles* which states,

"the taxpayer's last known address is that address which appears on the taxpayer's most recently filed return unless Respondent has been given clear and concise notification of a different address." (emphasis added) *Id.* at 1035.

Clearly, the Form 2848 gave clear and concise notification of a different address. The court #6 further states that "what is significant is what respondent knew at the time the statutory notice was issued." *Id.* Respondent recognizes that when the Form 2848, Power of Attorney, designates the taxpayer's representative to receive original notices and written communications it is to be recognized as a new address. In that instance the Respondent recognizes that it has knowledge of the contents of the Power of Attorney. However, if the block on the form is not checked to send the communications to the taxpayer's representative, the Respondent denies that it has knowledge of the information in the Power of Attorney.

Respondent's argument and the general guidance in Revenue Prop. 90-18 is directed primarily to the fact that the "clear and concise notice" must not only notify the

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Respondent of a taxpayer's new address but also specifically state to the Service that the taxpayer's records be changed to reflect this new address. Nowhere is this requirement found in the Abeles case. Rather the court in Abeles clearly states

"so holding, we are merely reiterating our position that what is of significance is what Respondent knew at the time the statutory notice was issued ... and attributing to Respondent information which Respondent knows, or should know, with respect to a taxpayer's last known address, through the use of it's computer system" Id.

Box 1 of Form 2848 clearly states that the information contained in that box is the taxpayer's "name and address". Respondent specifically recognizes that the information on the Form 2848 is information which is "known" to the Respondent if the box is checked which designates the Taxpayer's representative to receive original notices and communications but is not "known" if this box is not checked. This logic is ludicrous. The court in the Abeles case correctly focused \*7 on the knowledge of the Commissioner. The cases recognizing that the Form 2848 may designate the taxpayer's representative to receive notices simply conclude that the respondent may rely on that designation in issuing a statutory notice of deficiency. If the respondent is to recognize the Form 2848 as clear and concise notice of a different address if a block is checked, it should recognize the Form 2848 as clear and concise notice of a different address when the block is not checked but the Form 2848 has a different address for the tax payer.

## VIII.

## CONCLUSION

This court should hold that the properly submitted Form 2848, Power of Attorney, containing a different address for the Petitioner than on his previously submitted income tax return was clear and concise notification of a different address as the law is interpreted in Abeles v. Commissioner, Id. Petitioner's Motion for Dismissal should be granted.

Thomas W. HUNTER, Jr., Petitioner, v. COMMISSIONER OF INTERNAL REVENUE,  
Respondent.  
2003 WL 23518412  
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T.C. Memo. 2004-81

UNITED STATES TAX COURT

THOMAS W. HUNTER, JR., Petitioner v.  
COMMISSIONER OF INTERNAL REVENUE, Respondent

Docket No. 9856-02.

Filed March 23, 2004.

James David Leckrone, for petitioner.

Rebecca Dance Harris, for respondent.

MEMORANDUM OPINION

HOLMES, Judge: In September 1998, petitioner Thomas Hunter moved from Gallatin to Hendersonville, Tennessee. He knew when he moved that the IRS was auditing his tax returns. In October 1998, he hired new accountants to represent him, and filed a power-of-attorney form that both directed the IRS to send copies of all correspondence to their office in Nashville and listed his

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own new address in Hendersonville. In January 1999, respondent sent notices of deficiency for the tax years under audit to petitioner at his old address in Gallatin. He never received them. Respondent did not mail duplicates to him at his new address, nor did he mail duplicates to petitioner's accountants in Nashville.

The case comes to us on the parties' cross-motions to dismiss for lack of jurisdiction. The question presented is whether petitioner, by filing this power-of-attorney form, gave respondent a clear and concise notification of his change of address.

#### Background

This case turns on the timing of a few key events:

August 14, 1997	Petitioner files 1991-1995 returns.
July 30, 1998	Petitioner files 1996 return. The parties assume that this return listed petitioner's Gallatin address.
August 13, 1998	The revenue agent issues her findings on petitioner's 1991-1996 tax liability in a revenue agent's report that she sends to petitioner at his Gallatin address. He receives it, but doesn't respond.
September 1998	Petitioner moves to Hendersonville, Tennessee.
October 23, 1998	Petitioner signs Form 2848 ("Power of Attorney and Declaration of Representative") listing his Hendersonville address and naming three accountants as his designated representatives for the 6 tax years under audit. The form directs



respondent to send copies of all correspondence to both the first and second accountants named on the form.

November 19, 1998 The IRS service center in Memphis receives and processes the Form 2848.

January 28, 1999 Respondent issues three notices of deficiency covering all 6 tax years. Respondent sends these notices to the Gallatin address. All are sent by certified mail; two are returned to the IRS as unclaimed, and there is no record of what happened to the third.

July 1999 Petitioner receives statements of account for each of the years in question from the IRS, sent to him at his Hendersonville address.

September 1999 Petitioner begins suggesting compromise to resolve all years in question.

July 2000-  
April 2002 Petitioner continues settlement talks, first with a revenue agent and then with the IRS Appeals office.

June 10, 2002 Petitioner files petition. (In lieu of the notices of deficiency, which he still hasn't received, he attaches the revenue agent's reports from August 1998).

Petitioner continues to be a resident of Tennessee, as he was when he filed his petition. When the case neared trial in Nashville, both parties moved to dismiss the petition for lack of jurisdiction--petitioner on the ground that respondent never sent a notice of deficiency to his last known address, and respondent on the ground that petitioner filed his petition well outside our 90-day jurisdictional limit. The parties have stipulated or not

contested the key facts and documents.<sup>1</sup>

Discussion

Our jurisdiction to redetermine deficiencies exists only when the Commissioner issues a notice of deficiency and a taxpayer files a timely petition to redetermine that deficiency. Rule 13(a), (c); Monge v. Commissioner, 93 T.C. 22, 27 (1989); Normac, Inc. v. Commissioner, 90 T.C. 142, 147 (1988). The Internal Revenue Code says that a notice of deficiency shall be "sufficient" if "mailed to the taxpayer at his last known address." Sec. 6212(b)(1).<sup>2</sup> There is no statutory definition of "last known address," and the resulting gap has been filled with a "plethora of caselaw decided by this and other courts." Marks v. Commissioner, T.C. Memo. 1989-575, affd. 947 F.2d 983 (D.C. Cir. 1991).<sup>3</sup>

In Abeles v. Commissioner, 91 T.C. 1019, 1035 (1988), we

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<sup>1</sup> The most important fact that the parties did not stipulate is whether petitioner ever received a notice of deficiency. Petitioner testified at the short hearing held before the case was submitted that he never had. Respondent objected to the proposed finding of fact citing that testimony, but only by characterizing the testimony as "self-serving." On this crucial point, we agree with petitioner--noting especially that respondent, in his own motion to dismiss, asserted only that he sent three notices of deficiency to petitioner--the three concededly sent to petitioner's old address in Jan. 1999.

<sup>2</sup> Subsequent section references are all to the Internal Revenue Code.

<sup>3</sup> Respondent has issued a regulation, sec. 301.6212-2, *Proced. & Admin. Regs.*, defining "last known address." The regulation's effective date, however, is Jan. 29, 2001, after the events giving birth to these motions.

held that

a taxpayer's last known address is that address which appears on the taxpayer's most recently filed return, unless respondent has been given clear and concise notification of a different address.

We also held in Abeles that once a taxpayer notifies the IRS that his address has changed, the Commissioner "must exercise reasonable care and diligence in ascertaining, and mailing the notice of deficiency to, the correct address." Id. at 1031. And we focus in deciding whether he's exercised reasonable care on "the information that would be available to the IRS at the time that it issued the deficiency if it had used reasonable diligence."<sup>4</sup> Ward v. Commissioner, 907 F.2d 517, 521 (5th Cir. 1990), revg. and remanding 92 T.C. 949 (1989). So the specific question to be answered is whether petitioner, by listing his new address on his power-of-attorney form, gave respondent "clear and concise notification" of his new address.

Two courts have already answered the question. In Rizzo v. Davis, 43 AFTR 2d 985, 79-1 USTC par. 9310 (W.D. Pa. 1979), the

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<sup>4</sup> Most circuits consider the "last known address" issue to be a purely factual question, e.g., McPartlin v. Commissioner, 653 F.2d 1185, 1189 (7th Cir. 1981), or a "mixed question" which is "essentially factual", King v. Commissioner, 857 F.2d 676, 678 (9th Cir. 1988), affg. 88 T.C. 1042 (1987); cf. Armstrong v. Commissioner, 15 F.3d 970, 973 (10th Cir. 1994), affg. T.C. Memo. 1992-328. In a case involving "the extraordinary circumstances of taxpayers whose address had changed twice \* \* \* even though they have never moved," the Second Circuit reviewed de novo the "legal conclusion as to the [Commissioner's] satisfaction of the reasonable diligence requirement". Sicari v. Commissioner, 136 F.3d 925, 928 (2d Cir. 1998), revg. T.C. Memo. 1997-104. The Sixth Circuit has not decided what standard of review applies.

court found--at the Government's insistence--that the taxpayer's Form 2848 established a "last known address" different from the one appearing on the taxpayer's most recently filed return. And in Johnson v. Commissioner, 611 F.2d 1015, 1020 (5th Cir. 1980), revg. and remanding T.C. Memo. 1977-382, the Fifth Circuit similarly held that a Form 2848 is sufficient to change a last known address, even if the IRS later loses the form. We ourselves have repeatedly held that a power-of-attorney form directing the IRS to send all original documents to a representative is an adequate notification of a change of address: Maranto v. Commissioner, T.C. Memo. 1999-266; Elgart v. Commissioner, T.C. Memo. 1996-379; Honts v. Commissioner, T.C. Memo. 1995-532.

This case would seem only a bit different--here petitioner directed that copies be sent to his accountants, and it is he rather than respondent who is claiming that a Form 2848 effectively makes a change of address. Petitioner suggests neither of these distinctions makes a difference. In his view, for a filing to change a "last known address" it must only be (1) clear and concise, (2) a notification, (3) and show a different address from the last one sent to the IRS. He then insists that his October 1998 power-of-attorney form meets all three requirements. It was "clear and concise" because the Form 2848 was the IRS's own form; it was a notification because it was

sent to the appropriate IRS service center, as the IRS required, see Rev. Proc. 90-18, sec. 4.02, 1990-1 C.B. 491, 492, and it definitely showed a different address.<sup>5</sup>

Respondent chose not to file a reply brief and so missed his chance to grapple with Rizzo and Johnson. Instead, he argues that petitioner's proposed test leaves out a critical fourth element: An express statement of intent by a taxpayer that his address of record be changed to his new address. See Rev. Proc. 90-18, sec. 5.04(1), 1990-1 C.B. at 494.<sup>6</sup> This failure, which respondent strongly suggests could easily have been cured by using Form 8852--the IRS's official change-of-address form--in his view vitiates petitioner's attempt to use a Form 2848 to effect a change of address.

Respondent finds this fourth element not in any case involving powers of attorney, but in other cases stating seemingly broad principles of "last known address" law. He begins with Alta Sierra Vista v. Commissioner, 62 T.C. 367, 374 (1974), a case where we noted that "Administrative realities

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<sup>5</sup> Respondent suggests that petitioner could have given the form to the revenue agent working on the audit. This is true, but hardly decisive--respondent's own procedure allows a taxpayer to mail the form to the Service Center that received his last return.

<sup>6</sup> Note that we have held that revenue procedures generally, and Rev. Proc. 90-18, supra, in particular, do not bind this Court. Westphal v. Commissioner, T.C. Memo. 1992-599.

demand that the burden fall upon the taxpayer to keep the Commissioner informed as to his proper address." Id. at 374 (citations omitted). Alta Sierra Vista spoke of respondent's "entitlement" to treat the address on a taxpayer's most recent tax return as his last known address. Respondent insists that this "entitlement" creates a presumption which simply listing a new address on a power-of-attorney form does not rebut.

Respondent then cites cases in which various documents other than power-of-attorney forms were found insufficient to rebut this presumption. His leading case is Tadros v. Commissioner, 763 F.2d 89 (2d Cir. 1985). Tadros featured a taxpayer who lived in New York when he filed his 1981 tax return, but who moved to New Jersey in January 1983. In March 1983, the Commissioner sent a notice of deficiency to his old New York address, but the Postal Service returned it as "undeliverable".

Tadros argued that he had told the Commissioner of his move to New Jersey in a letter he had written to the IRS in January 1983 on stationery printed with his New Jersey address. His letter asked for copies of correspondence and said that he needed the copies to replace originals that he had "'lost or misplaced in the process of moving.'" Id. at 92.

The Second Circuit held that the letter was a mere "routine inquiry," not amounting to an official change of address:

Tadros's letter \* \* \* indicated neither that Tadros had permanently moved, nor whether the Jersey City address

on the letterhead was his new place of residence. Nor did it mention the old address or indicate that it was no longer to be used.

The steps taken by the IRS when the March 8 notice was returned as undeliverable show that it exercised reasonable care to ascertain Tadros's new address.

Id. (emphasis added).

The letter Tadros had sent the IRS was not an IRS form, and not in a format drafted by the IRS itself. Respondent would nevertheless have us find that petitioner's power of attorney is like Tadros's stationery--it too made no mention of his old address and did not expressly indicate that the old address was no longer to be used. We do not, however, read Tadros as listing requirements needed to make an effective change of address in all cases. Instead, we read it as suggesting ways in which the letter in that case could have sufficed--for example, by identifying the old address and noting that it had been replaced by the new one.

Respondent next points to Pyo v. Commissioner, 83 T.C. 626 (1984), which does at least feature an IRS-designed form--Form 872, the form the IRS customarily uses to extend the statute of limitations. The IRS had itself incorrectly filled out the taxpayer-address portion of the form with the Pyos' old address before sending it to their accountant. The Pyos did not catch the mistake before returning the form to the IRS. A year later, the IRS sent a notice of deficiency to the old address, despite

having traded letters with the Pyos at their new address in the meantime.

When the notice was returned as undeliverable, the IRS relied on the erroneously completed Form 872 as evidence that the Pyos' old address was their "last known address." The Court rejected this argument, holding that an "inadvertent" failure by a taxpayer to correct an IRS mistake on a form would be insufficient to establish a last known address, especially when so much time had passed since the Pyos sent back the Form 872 and the IRS had begun writing to them at their new address. Pyo does not support the proposition that a form filed for a purpose other than changing an address will not create a new "last known address"; rather, it teaches that taxpayers will not be penalized for inadvertently failing to correct IRS mistakes.

Petitioner's Form 2848, in contrast, calls upon taxpayers to fill it out themselves and include their address. "[I]t seems anomalous to permit \* \* \* [respondent] to prescribe the medicine and then punish the patient for taking it." Johnson, 611 F.2d at 1019. And our caselaw--beginning at least with Honts--holds that a power-of-attorney form works as a change of address. Respondent tries to limit those cases' force by arguing that the Form 2848 is sufficient notice of an address change only when it directs originals of all notices and communications be sent to the taxpayer's representative instead of the taxpayer. He argues



that petitioner's case is different? His form directed only copies go to his representatives, and merely informed respondent of his address, without saying that he wished the new address to supplant the old.

But we reject the assertion that a valid change-of-address notification must use language equivalent to "please note that this is a change of address." As petitioner points out, no such glaring notification exists on a tax return, or on the power-of-attorney forms given effect in Rizzo and Johnson.

We also think that respondent's position overlooks a more general theme in the case law; namely, that the IRS is chargeable with knowing the information that it has readily available when it sends notices to taxpayers. As courts have repeatedly observed, the steady advance of technology continues to lighten the IRS's burden in searching its own records for current address information. Union Tex. Intl. Co. v. Commissioner, 110 T.C. 321, 334 (1998).

Petitioner is thus right in noting that address information on the Form 2848 is not mere surplusage. The IRS asks for that information and solicits taxpayer's directions on what address should be used for original and duplicate notices. This strongly implies that respondent will actually incorporate the information on the form into its databases and use the information when sending notices to a taxpayer's "last known address."

Respondent's position is essentially that it is up to taxpayers to flag change-of-address information in a way so obvious as to be immune from occasional bureaucratic irregularities. But the minimal burden to the IRS must be balanced against the potentially serious consequences for taxpayers who rely on the IRS to process in a businesslike way the information that it receives. The Tadros decision itself recognized that the IRS has an "obligation" to "exercise reasonable care in determining an address." Tadros, 763 F.2d at 91-92. And as we announced in Abeles:

the IRS' computer system was available to respondent's agent responsible for mailing the notice of deficiency, and \* \* \* the system would have reflected the [correct address] had such agent caused a computer search of petitioner's TIN.

Abeles at 1034.<sup>7</sup> In short, the IRS should not "ignore that which it obviously knows." United States v. Bell, 183 Bankr. 650, 653 (S.D. Fla. 1995).

Respondent's failure to act on what he knew continued even after the notices were returned as "unclaimed". Respondent's own manual suggests that he should have kept trying to find the right

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<sup>7</sup> The record in this case contains scant information on the procedures and database capabilities of respondent. We are guided, however, by the stipulation of the parties that the Form 2848 was processed on Nov. 19, 1998; and by Rev. Proc. 90-18, which indicates that the IRS requires 45 days to process address information. The 45-day period, even counting from the time the Form 2848 was filed, would have ended well before Jan. 28, 1998--the date that the IRS sent out the notices of deficiency.

address. 1 Audit, Internal Revenue Manual (CCH), sec. 4243.2(6)(b) (as in effect January 1999) (if mail undeliverable, IRS should "check all possible sources in the case files").<sup>9</sup> Instead, the stipulated facts show no effort to redeliver the notices even after respondent began using petitioner's Hendersonville address in correspondence, and while he continued to meet with petitioner's accountants in settlement talks for several years. The caselaw calls this evidence of lack of reasonable care and due diligence. See Pyo, 83 T.C. at 638 (corresponding with taxpayers at new address suggests knowledge of new address); Honts, T.C. Memo. 1995-532 (Commissioner should verify address if in regular contact with taxpayer's representative). And we ourselves have stressed that the Commissioner can protect himself from last-known-address problems by sending copies to each possible address. Elgart v. Commissioner, T.C. Memo. 1996-379; Karosen v Commissioner, T.C. Memo. 1983-540. No such steps are on record here, even though petitioner had asked on his Form 2848 for copies of all correspondence to go to two of his accountants.

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<sup>9</sup> Respondent points out that there is no record of the third notice's being returned. Because we find that respondent failed to issue any of these notices to petitioner's last known address, the ambiguity surrounding the ultimate fate of this one notice is irrelevant. Respondent also argues that the house number on the Form 2848 was incorrectly listed as 2200, rather than 2220. This would only be relevant if respondent had used it to address the notices of deficiency at issue.

Nothing compels the Commissioner to ask taxpayers to list their address on a Form 2848. By doing so, and by using that requested information to identify taxpayers within IRS records, respondent bears the burden of conforming his actions to the knowledge at his disposal. See Alta Sierra Vista, 62 T.C. at 374. This is important not only because of the statutory requirements of section 6213, but also because, as petitioner points out, taxpayers are put in the position of quite reasonably assuming that the address information they provide to the IRS will be noted and acted upon.

We agree with petitioner that listing his Hendersonville address on the Form 2848 provided respondent with "clear and concise" notification of his change of address. His Hendersonville address thus became his "last known address" under section 6213. We shall therefore grant his motion to dismiss this case for lack of jurisdiction, and deny respondent's.

To reflect the foregoing,

An order will be entered  
granting petitioner's, and denying  
respondent's, motion to dismiss  
for lack of jurisdiction.

## APPENDIX C

### DATA COLLECTION INSTRUMENT

APPENDIX C

DATA COLLECTION INSTRUMENT

MEMORANDUM NUMBER \_\_\_\_\_

CASE NAME \_\_\_\_\_

Measure of Confirmation Bias:

Taxpayer \_\_\_\_\_

Internal Revenue \_\_\_\_\_

Outcome \_\_\_\_\_

Firm Name and Address of Taxpayer's counsel:

\_\_\_\_\_  
\_\_\_\_\_  
\_\_\_\_\_

Martindale-Hubbell Rating \_\_\_\_\_

IRS Counsel: \_\_\_\_\_

Martindale-Hubbell Rating \_\_\_\_\_

Amounts:

Deficiency: \_\_\_\_\_

Penalty: \_\_\_\_\_ Section \_\_\_\_\_

Penalty: \_\_\_\_\_ Section \_\_\_\_\_

Penalty: \_\_\_\_\_ Section \_\_\_\_\_



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