

**NOT FOR PUBLICATION**

UNITED STATES COURT OF APPEALS

FOR THE NINTH CIRCUIT

**FILED**

**DEC 04 2006**

CATHY A. CATTERSON, CLERK  
U.S. COURT OF APPEALS

ROBERT C. MCKEE; et al.,

Petitioners - Appellants,

V.

COMMISSIONER OF INTERNAL  
REVENUE,

Respondent - Appellee.

No. 04-74846

IRS No. 4036-03

MEMORANDUM\*

Appeal from a Decision of the  
Internal Revenue Service

Argued and Submitted November 16, 2006  
San Francisco, California

Before: KLEINFELD and THOMAS, Circuit Judges, and LEIGHTON\*\*, District  
Judge.

The IRS assessed a tax deficiency of \$164,765 upon the McKees for tax  
years 1999-2000. After negotiations in which the IRS acknowledged key errors

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\* This disposition is not appropriate for publication and may not be  
cited to or by the courts of this circuit except as provided by 9th Cir. R. 36-3.

\*\* The Honorable Ronald B. Leighton, United States District Judge for  
the Western District of Washington, sitting by designation.

were made in calculating that figure, a settlement was reached in which the deficiency was reduced to \$44,535. The McKees petitioned for reasonable litigation costs under 26 U.S.C. § 7430, but were denied by the Tax Court. Because we find that the Tax Court abused its discretion in finding that the position of the IRS was “substantially justified” we reverse the Tax Court and grant the McKees’s petition.

The IRS bears the burden of proving that its position in the proceedings below was “substantially justified.”<sup>1</sup> In the settlement negotiations, the IRS admitted that it made errors in applying its own code and regulations. The Tax Court’s finding that the IRS was excused because its own regulations were “complex” was an abuse of discretion.

The settlement resulted in a net reduction in the deficiency by 73%. Thus the McKees “substantially prevailed” with respect to the total amount in

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<sup>1</sup> 26 USCS § 7430(c)(4)(B).

controversy.<sup>2</sup> Under IRS regulations, the McKees are excused from further exhaustion of remedies.<sup>3</sup>

We remand to the Tax Court for an award to the McKees of \$31,078.28, their reasonable litigation costs under the Internal Revenue Code.<sup>4</sup>

PETITION GRANTED. The decision of the Tax Court is REVERSED and REMANDED.

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<sup>2</sup> See 26 USCS § 7430(c)(4)(A)(i).

<sup>3</sup> See CFR § 301.7430-1(g) example 5.

<sup>4</sup> See 26 USCS § 7430.