The Joint Audit Planning Process

A COOPERATIVE EFFORT OF THE LARGE AND MID-SIZE BUSINESS DIVISION OF THE INTERNAL REVENUE SERVICE AND THE TAX EXECUTIVES INSTITUTE.

September, 2003

TABLE OF CONTENTS

LMSB JOINT AUDIT PLANNING PROCESS TEAM **2**

MISSION STATEMENT **2**

OBJECTIVES **2**

LMSB JOINT AUDIT PLANNING PROCESS **3**

- **INTRODUCTION** 3
- **PLANNING & MONITORING TOOL** 7
  - *Role of the Team Manager* *11*
  - *Involving the Specialist* *12*
  - *Involving Counsel* *13*
  - *Risk Analysis* *15*
  - *Materiality Agreements* *17*
  - *Claims* *19*
  - *Limited Issue Focused Examination (LIFE)* *19*
  - *Information Document Request (IDR) Management Process* *20*
  - *Issue Management and Resolution* *22*
  - *Rules Of Engagement* *37*
- **SUMMARY** 39

LMSB Joint Audit Planning Process Team

LMSB Participants	Tax Executives Institute Participants*
Jack L. Schroeder, Director, Field Operations	Denise M. Lukowitz, Schneider National, Inc.
James P. Dever, Territory Manager	Victoria McInnis, General Motors
Erwin D. Walker, Territory Manager	Christopher Riley, Archer Daniels Midland
Jeffrey A. Myers, Team Manager Engineering	Mark Silbiger, Lubrizol Corporation
Douglas Chong, Team Manager Financial Products	Bob Zysk, Northwestern Mutual Insurance
Larry H. Smoller, Senior Team Coordinator NTEU	Mary L. Fahey, Tax Counsel, Tax Executives Institute

Mission Statement

To develop a joint, issue driven, audit planning process that engages all members of the audit team, including specialists, in conjunction with the taxpayer.

Objectives

- To provide a consistent approach to the joint audit planning process that includes all audit team members working in conjunction with the taxpayer.
- To develop an issue focused plan that encourages audit efficiency.
- To establish accountability in executing the jointly developed audit plan.
- To enhance taxpayer disclosure during the joint audit planning process.

*Although TEI members and staff participated in this project, the report is not an official position of Tax Executives Institute.

LMSB Joint Audit Planning Process

Introduction

The Internal Revenue Service is focused on ways to improve the examination process. The Large and Mid-Size Business (LMSB) division recognizes that thoroughly involving the taxpayer in audit planning is an initiative that will have a positive impact on the way future examinations are conducted. Joint participation in this process benefits both taxpayers and the Service by increasing the currency of examinations. It also provides certainty of results for both taxpayers (i.e. financial statements) and the Service (i.e. completed examinations) by minimizing open tax years.

Working within the framework of LMSB's Post-Filing Design Team's Guiding Principles, LMSB approached the Tax Executive Institute (TEI) requesting their participation in an attempt to initiate true joint audit planning. As a result, volunteers from both LMSB and TEI were solicited to form a team to accomplish this task. From this collaborative effort emerged a planning and monitoring tool that captures the concepts that were identified as being key to efficiently planning and conducting an examination. The tool will assist both the IRS and the taxpayers in overseeing their examinations.

Key to the success of the audit process is communication, trust and openness. Both the taxpayers and the Service should share a common goal, completing the examination in the most efficient manner possible. The examination plan is the road map relied upon to accomplish this and its effectiveness depends largely upon the assumptions made as the plan comes together. The ideal plan evolves in an atmosphere of mutual cooperation and trust, synergy that can only be obtained when the parties involved in the process are committed to open and honest communication. The taxpayer needs to be included in the development of the audit plan from its inception.

At the start of the examination and prior to the opening conference, preliminary meetings should be held between the taxpayer and the Service to exchange information critical to the preparation of a quality risk analysis. Administrative matters should also be discussed at this time and the examination timeline set. Since specialists' input is critical to the joint audit planning process and completion of the risk analysis, team managers and coordinators should include specialists and specialist managers in preliminary meetings. The audit areas specialists have responsibility for may require significant resources, thus potentially impacting the examination timeline.

Generally, an Information Document Request (IDR) should not be issued until the team member requesting the information has met with the taxpayer to discuss what is needed and the best way to obtain it. By working together at every stage of the examination, audit and cycle time should be reduced, alleviating burden on both sides. Both sides have a common interest in completing the audit timely, efficiently, and fairly. Specific actions that can be taken to minimize conflict and increase cooperation are as follows:

- The IRS and taxpayer should candidly discuss potential issues and required compliance checks early in the planning phase so that the taxpayer can make the necessary resources available when needed and present pertinent information to the examination team during the preliminary meetings. In addition, the taxpayer should inform the IRS about potential affirmative issues and/or claims that might be filed for the years under audit.

- The taxpayer can contribute to reducing examination time by providing a meaningful orientation to the audit team. Such orientations can include presentations at preliminary meetings on such topics as organizational structure, degree of centralization, industry operating philosophies and procedures, accounting records, and other information that will facilitate the examination. The orientations can also include brief meetings with key operating, accounting, or tax personnel and/or facility and plant tours. The taxpayer may also provide the audit team with informative company videos, handbooks, and other information normally given to new hires.

- The use of IRS specialists is an integral part of the examination process; these specialists include computer audit specialists (CAS), international examiners (IE), financial products examiners, engineers, economists, employment tax examiners, excise tax examiners, TE/GE examiners and others. Barring unforeseen circumstances, the IRS will inform the taxpayer which specialists will be utilized before the examination is started. Once it is determined which specialists will be assigned, the taxpayer, specialist managers, specialists, team manager and team coordinator are encouraged to hold preliminary meetings to discuss the development of the specialists' portion of the audit plan. It is critical that the IRS and taxpayer coordinate their schedules early in the planning process so that the responsible company personnel will be available to secure the information the specialists request. It is likewise very important that the taxpayer, specialist managers, team manager, team coordinator and the specialists meet their commitments to each

other in terms of providing information, requesting follow-up information and holding scheduled meetings.

- The taxpayer should provide the audit team with a book to tax reconciliation ideally in the form of a "cross-referencing" disk or conversion code workpaper at the earliest possible stage of the examination. This will reduce the number of IDR's issued, require less use of the taxpayer's computer system, and save time for both the IRS and the taxpayer.

- When Coordinated Issues are identified, and where practical and appropriate, discussions between the taxpayer and the technical advisors are encouraged.

- The IRS and the taxpayer should agree to make every effort to resolve issues at the examination level, taking advantage of the issue management initiatives when appropriate.

- New issues identified by the IRS during the audit process that are not in the audit plan should be discussed with the taxpayer prior to commencing extensive audit work.

The above specific actions are not all-inclusive. They represent the initial joint audit planning process steps the IRS and the taxpayer need to take to enhance the quality and timeliness of examinations.

After successfully completing the initial steps of the joint audit planning process, the IRS will furnish a draft audit plan to the taxpayer for review. Afterwards, taxpayer concerns or questions will be addressed and agreed upon changes or corrections will be made to the plan. When possible, the taxpayer should be provided the final plan for concurrence and signature on the date of the formal opening conference. In any event, the audit plan should be finalized before any substantial amount of examination work is accomplished.

The joint audit planning process includes several key elements that impact timeliness and quality. These elements, which are critical to examination planning are:

- Role of the Team Manager
- Involving the Specialist
- Involving Counsel

- Risk Analysis
- Materiality
- Claims
- Limited Issue Focused Examination (LIFE)
- IDR Process
- Issue Management and Resolution
- Rules of Engagement

The following “Planning and Monitoring Tool” addresses these elements and other specific actions that both the IRS and taxpayers can take to enhance the quality and timeliness of their examinations. In addition, this tool outlines the specific joint and individual responsibilities of all participants, thereby increasing the efficiency of the audit process by focusing the available time and resources on the most important areas.

Large and Mid-Size Business Division Joint Audit Planning Process Planning & Monitoring Tool

Taxpayer:	Exam Year(s):
Tax Manager:	
Team Manager:	POA:
This document is intended to assist the IRS and the taxpayer to efficiently plan and oversee their examination. This tool should be used to both plan and monitor the audit process; it is applicable to both Coordinated Industry (CIC) and Industry (IC) Cases.	

Preliminary Meetings and Discussions	**Comments**
1. The audit team should gather publicly available information (e.g., annual reports, SEC filings, taxpayer's web site, etc.) and current transcripts to reduce taxpayer burden.	
2. After the audit team's initial review of the tax returns and related information, multiple preliminary meetings and other informal discussions (based upon taxpayer size, return complexity, and proposed staffing levels) should be held with the taxpayer regarding: a. prior cycle results, to determine if areas of review can be limited or eliminated b. timeframes for pre-audit and initial risk analyses c. the taxpayer's anticipated filing of claims d. potential industry/coordinated issues e. new audit initiatives and general administrative procedures (i.e. LIFE, IDR procedures, issue resolution strategies). f. whether the IRS or the taxpayer will prepare the schedule of rollover adjustments that results from the prior cycle. g. the audit team having access to the taxpayers e-mail system to facilitate the communication of IDRs, IDR responses, records, 5701s, etc.	
3. The taxpayer and the audit team should advise each other of peak times, vacation plans, training, and other significant factors that may result in delays or increase burden.	
4. The taxpayer should provide a meaningful orientation to the IRS audit team, including a general overview of business activities (particularly if there is a new team), financials, return results and known significant changes from the prior cycle.	
5. The taxpayer should provide the audit team with a list of significant transactions for the cycle and any other information that is new and different from the previous cycle (acquisitions, dispositions, tax shelters, accounting method changes - Forms 3115).	
6. In order to reduce the number of IDRs issued, the taxpayer should provide routine start-of-audit information (significant M-1s, access to general ledger, tax workpapers, etc.).	
7. The taxpayer should provide financial information (such as the general ledger) in electronic format to allow the audit team to review information directly, reducing the number of IDRs issued.	
8. The taxpayer should deliver a list of claims and requested audit adjustments (with all supporting documentation made readily available) to allow these items to be included in the audit plan.	
9. Based upon the initial risk analyses and review of preliminary documents (i.e., annual statements, tax returns, historical files, etc.), the audit team should advise the taxpayer of potential examination areas/issues, and/or business units it plans to review.	

Large and Mid-Size Business Division
Joint Audit Planning Process
Planning & Monitoring Tool

Involvement of IRS Counsel, Specialists, Technical Advisors	Comments
1. The availability of appropriate IRS and taxpayer personnel should be discussed.	
2. The IRS will notify the taxpayer if significant involvement by technical advisors, Office of Associate Chief Counsel and/or specialists is anticipated.	
3. Arrangements should be made for specialists to meet with relevant taxpayer personnel to discuss areas to be reviewed prior to issuing IDRs.	
4. When their assistance is needed, coordination with the Office of Associate Chief Counsel should be made as early as possible. Contact can be informal via telephone or e-mail, or formal, that is, through Technical Advice Memorandum (TAM), Technical Expedited Advice Memorandum (TEAM), or Reviewed Advice Memorandum (RAM).	
5. Specialists, specialist managers and when appropriate, Counsel, will be invited to attend key issue meetings between the taxpayer and the IRS.	
6. Attempts should be made to reach agreement on the facts, prior to the extensive involvement of a technical advisor.	
7. The Computer Audit Specialist (CAS) should have advance access to the taxpayer's electronic data. This is usually accomplished at the end of the current cycle examination, three to six months prior to the start of the next cycle.	
Scope of Audit	**Comments**
1. The audit team should consider and discuss the applicability or inapplicability of Limited Issue Focused Examination (LIFE).	
2. The audit team will share a copy of the draft audit plan with the taxpayer and allow the taxpayer an opportunity to provide feedback prior to finalizing the plan.	
3. New issues identified by the IRS during the audit process that are not in the audit plan should be discussed with the taxpayer prior to the commencement of extensive audit work.	
4. The need for support audits and third party contacts should be considered early in the examination.	
5. Materiality agreements should be considered when determining the scope of the examination (whether or not LIFE applies). Since each taxpayer and each year is unique, materiality thresholds should be set on a case-by-case, year-by-year basis.	
6. The audit team will share subsequent risk analysis results (i.e., 50% or 75% risk analysis) with the taxpayer, indicating the scope, depth, and status of the audit with a view to reducing the number of issues (but with the understanding that the determination of which audit items to pursue rests with the IRS).	
7. The audit team should consider the use of statistical sampling or alternative testing methods (e.g. mutually agreed upon judgment sampling) if records are voluminous.	
8. The taxpayer should discuss or provide preliminary information on issues with the intent to narrow the scope of the audit and focus on the most significant issues.	
9. The taxpayer should be informed that if issues are dropped or narrowed, additional issues will not routinely be substituted or added.	
10.The taxpayer will be advised that the examination may be expanded if tax shelters, listed transactions or similar transactions are discovered during the course of the examination.	
11.The audit team and taxpayer should jointly develop a plan to attain and maintain currency.	

Large and Mid-Size Business Division
Joint Audit Planning Process
Planning & Monitoring Tool

Audit Timeline/ Monitoring Progress	**Comments**
1. The taxpayer and audit team should jointly prepare an audit timeline with target milestone dates (i.e. exam plan completion date, 50% risk analysis review, last date for IDRs to be issued, last date for claims to be filed, last date for Forms 5701 to be issued, RAR issuance target date).	
2. The taxpayer and the audit team should jointly plan the matching of audit issues to available taxpayer and examination team resources to avoid delays during the audit.	
3. Microsoft Project or similar tool(s) should be used to establish and track timeline milestones and targets.	
4. The IRS and taxpayer should sign an agreement and/or the audit plan setting joint commitments (i.e. audit timeframes, materiality, IDRs, 5701s, affirmative issues, etc.).	
5. An understanding should be reached that impasses and significant concerns that cannot be resolved at the IRS team manager/taxpayer audit manager level will be immediately elevated to the next level, IRS territory manager/senior tax officer or equivalent.	
6. An understanding should be reached that the team manager and the tax manager will jointly monitor the examination and determine who will attend the regular audit progress meetings, including meetings to address the following: ▪ ongoing risk analysis ▪ status of issues ▪ status of IDRs ▪ obstacles/anticipated delays and possible solutions, and ▪ anticipated changes to the audit timeline.	
7. An understanding should be reached to record all agreements and actions items (noting the responsible parties) to be completed at all IRS/taxpayer meetings to avoid delays and misunderstandings.	
8. Feedback from audit participants should be collected at prescribed intervals, such as: the end of the planning phase, the 50% mark, and the end of the examination, to determine the quality as well as the quantity of progress and to suggest ways to make the on-going and following examination better.	
Information Document Requests (IDRs)	**Comments**
1. An understanding should be reached that all IDRs and responses will go through the IRS team coordinator or primary revenue agent.	
2. An understanding should be reached that all IDRs and responses will go through the designated taxpayer representative.	
3. Discussions should be held prior to IDR issuance, unless agreed otherwise. Consider: ▪ The taxpayer should be informed of the intent of an IDR. ▪ The purpose of the IDR should be stated on the IDR (i.e., identify the issue).	
4. Prior to issuance of an IDR the Service and the taxpayer should meet to review the IDR for completeness. All IDRs should be entity specific unless agreed otherwise.	
5. The taxpayer should be informed of any coordinated and/or industry issues under audit.	
6. The audit team should reach an agreement with the taxpayer regarding a standard response time for IDRs, and an understanding that the taxpayer will advise the audit team as early as possible if additional time is needed.	
7. The audit team should advise the taxpayer within an agreed timeframe, after receiving an IDR response, whether it considers the response complete and if additional information or action is required.	

8. IDRs should be reviewed by the team coordinator or primary agent to insure that they are resolution-focused. (Do the questions asked "add value" to the identification or development of an issue?)	
Issue Resolution/Notices of Proposed Adjustments – Form 5701	**Comments**
1. All issues should be discussed with the taxpayer prior to issuance of Form 5701. Consider: ▪ The need to reach agreement, or to agree to disagree, on the facts ▪ The discussion of applicable area law ▪ The identification of specific areas of contention or disagreement	
2. Timeframes should be established with regards to the issuance and response to Form 5701.	
3. An understanding should be reached with the taxpayer that Notices of Proposed Adjustment will be issued throughout the examination instead of at the end of the examination, to facilitate early issue resolution.	
4. An understanding should be reached that when issues are agreed, the audit team will utilize abbreviated proposed adjustment write-ups (5701s).	
5. An understanding should be reached that the taxpayer and the audit team will engage in an earnest effort to resolve all issues.	
6. An understanding should be reached with the taxpayer that the audit team, within an agreed upon timeframe, will advise the taxpayer when an issue is closed.	
7. An understanding should be reached regarding the audit team's intentions to inform the taxpayer as early as practical that it is considering penalties, and to afford the taxpayer the opportunity to address them.	

Additional Comments

Role of the Team Manager

The team manager is the key to successfully centralizing the management of LMSB examinations in order to achieve the best possible coordination of work and the highest possible degree of uniformity and consistency in raising and resolving tax issues. This is especially true in Coordinated Industry cases as they usually require the efforts of many agents, and many times the efforts of agents in several locations. Since these cases cross so many industry and geographic lines, and involve numerous examiners, uniformity and consistency in their management is necessary so that those involved will know how to coordinate and cooperate with each other. With case management authority centralized in a team manager, the Service is assured of uniformity of decisions regarding the case and reducing the likelihood of a duplication of effort.

A principal benefit taxpayers receive from the Coordinated Industry Case Program is the centralization of control over all examination activity by the team manager. Through the team manager, taxpayers can expect a timely and well-managed examination will be made of their returns.

In both Coordinated Industry and Industry Case examinations, the management of specialists is a shared responsibility between the team manager and the specialist manager, who may operate under a different management structure. Application of planning input from specialists is left to the discretion of the team manager. The team manager is responsible for organizing, motivating, controlling and directing skillful and experienced agents in all examinations. In Coordinated Industry cases team managers are more deeply and directly involved in each aspect of the case from initial planning to final examination actions. They are responsible for scope and depth of the examination, for specific assignments to team members and for approval of plans for accomplishing their part of the examination.

Each specialist must work with other team members so that individual efforts are blended into a quality examination product. The team managers are the catalyst in accomplishing this. Therefore, they must:

- Involve specialists as early in the examination as possible.
- Provide the same amount of support to specialists and the same amount of attention given any other team member having comparable responsibilities.
- Provide the same direction, control and motivation to specialists as is given non-specialist team members.

It would be proper for a specialist team member to go to their regular manager for procedural or technical advice. This is in accordance with the specialist manager's

shared responsibility for the management of the specialist's activities. The team manager having responsibility for the examination should always be advised and involved in significant decisions, which may affect the examination. Also see IRM 4.45.13, Coordinating and Monitoring Audit Process, for additional guidance.

Involving the Specialist

When specialists are assigned to an examination they must be involved, along with their managers, in each phase from planning to closing. Unlike other team members, specialists regularly work on multiple cases and thus they face distinct challenges in building successful working relationships, both with taxpayers and other team members. The issues which specialists address generally involve complex and often untested areas of law. These types of issues may also require the assistance of other specialists. To further complicate matters, specialist's issues are often factually intense, demanding laborious record retrieval and analysis.

Planning

To ensure that specialists are available to service both CIC and IC examinations, their planned time needs to be front-end loaded. This allows specialist managers to properly plan resource utilization and better meet customer needs. Specialist managers participate with CIC team managers in meetings to design the annual plan for CIC work. This activity ensures that specialist managers are timely informed and can plan the commitment of their resources up front. At a minimum, specialist managers need to be provided with a listing of potential CIC cases starting in a fiscal year along with the anticipated start and stop dates. Specialist managers need to be involved with on-going resource planning as changes are made. Where specialist managers do not participate in early planning, resource problems can develop and deadlines can be missed because resources are applied late or haphazardly to an audit.

Role Definitions/ Decision Making

All team members must be held responsible for fulfilling team goals and performing a unified quality examination of all the pertinent issues rather than individual examination of various specialty areas. Since specialists serve all operating divisions (not just LMSB) plus Appeals and Counsel, advance planning to the extent possible is critically important.

Team building begins early in the examination process. Both the specialist and his/her manager are expected to attend the initial planning meetings and have a voice in

determining the scope and depth of their examination. If specialists and specialist managers do not attend meetings that affect the development or resolution of their issues, problems can quickly develop and relationships can become strained.

During meetings with taxpayers, information should be shared identifying the full team including all the specialist managers. Taxpayers need to know who is involved in making the decisions on issues raised by specialists. The role of the specialist and specialist manager needs to be clarified at these early meetings. This communication can prevent problems later during the examination when specialist managers appear at the audit site for visitations and meetings. It also provides the taxpayer with another channel of communication if problems or concerns surface. Prior to visiting case sites, specialist managers should notify either the team coordinator or team manager to advise them that they will be on-site, especially if they intend to meet with the taxpayer.

Issue Development and Resolution

Specialist issues can be highly factual and contentious. Some issues involve emerging tax shelter schemes where the tax law is not clear and/or the IRS strategy has not yet been formulated. Specialists are expected to keep the team manager and team coordinator informed of the status of their work on a regular basis. They also use Counsel assistance and facilitate the development and resolution of their issues. Specialist managers can play a critical role in this stage of the audit assisting their employees with decision making, risk analysis and negotiations that lead to the resolution of issues.

Where taxpayers employ specialists as part of their examination team, either from other company divisions or outside vendors and consultants, the same concerns and potential problems may surface. The examination team can avoid delays by accommodating the needs of these specialists.

Involving Counsel

Internal Revenue Manual (IRM) Section 4.45.7, Planning the Examination and Constructing the Plan, encourages early consultation with Counsel during the risk analysis process to ensure appropriate legal assistance is expeditiously requested. As Counsel develops and implements its new published guidance and case related guidance processes, LMSB field personnel are encouraged to contact their local field Counsel attorney during the planning and risk analysis phases to obtain legal assistance early in the examination process. This applies to all LMSB cases.

The current LMSB Division Counsel practice is to have a local counsel attorney assigned to the taxpayer case before the audit begins on a Coordinated Industry Case. Early LMSB Division Counsel involvement in the risk analysis process and in the audit process is desirable in all LMSB cases. Counsel is available to assist in risk analysis but is not required to be involved. This approach provides flexibility, for example, in those cases where the involvement of a Technical Advisor would suffice or where the facts have not been established or developed to determine the need for legal advice. This will ensure resources are efficiently utilized.

Advice Procedures

The goal of Treasury and Chief Counsel is to increase published guidance that can be relied upon, especially regulations and revenue rulings. Past legal advice vehicles such as Field Service Advice are generally no longer available. Division Counsel is available to provide case advice that reasonably implements technical positions consistent with the facts and tax administration. If published guidance is not clear, Division Counsel will coordinate with the National Office. Division Counsel is also available to develop and execute litigation strategies.

Coordination with the Office of Associate Chief Counsel should be made at the earliest possible stage in any proceeding. Contact can be informal via telephone or e-mail, or formal, that is, through Technical Advice Memorandum (TAM), Technical Expedited Advice Memorandum (TEAM), or Reviewed Advice Memorandum (RAM). Formal coordination, the preferred method, is not required to obtain advice on matters concerning routine case development or litigation questions involving the application of well settled principles of law.

Informal coordination with the Office of Associate Chief Counsel is obtained through Division Counsel. To obtain informal coordination, the Division Counsel attorney calls the Associate Chief Counsel attorney and records the conversation in an e-mail or memorandum to the file. The field can then be advised in writing and when necessary this written advice can be pre-reviewed (RAM) by Chief Counsel.

A RAM involves a Division Counsel attorney preparing a memorandum to LMSB based on informal advice. If an attorney is uncertain about the analysis the attorney can submit it to Associate Chief Counsel for pre-review. Associate Chief Counsel then has 15 days to agree, modify or change the submission to another form of advice. RAMs

usually involve the application of an established legal position. They are redacted and published under § 6110.

Formal coordination with Associate Chief Counsel is required where there is no clear guidance on the proposed position, where there is no uniformity regarding the disposition of an issue or when the issue is unusual or complex (TAM or TEAM required). It is appropriate for the Division Counsel attorney to make a pre-advice telephone call to the Associate Office to determine if formal advice is needed and what form it should take.

A TAM has a targeted time frame of 120 to 180 days where it is pending in National Office. The taxpayer does not have to participate in the process. If the taxpayer does participate, LMSB and the taxpayer do not have to agree on the facts. In the event the decision is adverse to the taxpayer there will be an adverse conference offered. Where the taxpayer and LMSB disagree on the facts and the Associate rules the same for both sets of facts the TAM issued will note that the factual disagreement is immaterial. If the Associate rules differently on the sets of facts, the TAM will be issued addressing both the taxpayer's and the field's facts. LMSB will be required to process the case consistently with the legal analysis in the TAM as applied to the fields or area office's facts.

A TEAM is technical advice issued in an expedited manner. It has a targeted time frame of approximately 60 days where it is pending in National Office. A pre-submission conference is mandatory and only one other conference is allowed, otherwise the TEAM process is similar to the TAM process.

There are two other types of legal advice from the National Office that are rarely used in LMSB. A Strategic Advice Memorandum (SAM) deals with non-routine factual development. It evaluates the strengths and weaknesses of a case and analyzes the hazards of litigation. It is mostly redacted. A Background Advice Memorandum (BAM) results in a generic analysis of law and the Service's position with respect to that law. It includes only the facts needed to describe a transaction and is mostly unredacted.

Risk Analysis

Risk analysis (IRM 4.45.7.2) is an essential component of an effective issue management strategy. It should engage managers, examiners and taxpayers at the earliest stage of the examination to determine the appropriate scope and duration of the

examination. It should be used on all LMSB tax returns, Coordinated Industry Cases (CIC) and Industry Cases (IC), although the detail and depth of the process will vary according to the complexity of the tax return.

Issue priority should be established through a process, which compares the potential benefits to be derived from examining an area to the resources required to perform the examination. This process, referred to as the preliminary risk analysis, is an integral part of the planning process to ensure efficient and effective use of resources. Some factors to be considered are:

- Compliance considerations
- Adjustment potential
- Potential impact on future years
- Historical examination data
- Industry issues, practices, and trends
- Appeals and litigation consideration
- Financial condition of the company
- Taxpayer's systems and controls
- Resources.

Risk analysis is a subjective process even when mathematical models are employed. It is based on experience, judgment, and objective analysis. Once the potential benefits and resources are considered, priorities can be established. Virtually all the factors discussed above are difficult to establish and subject to change. Therefore, the risk analysis process should be periodically revisited and updated. Risk analysis considered during the process should be documented by the team manager and maintained in the manager's binder.

Effective use of a consistent risk analysis process will assist in improving customer satisfaction and business results. It will focus examinations on tax returns and issues that have the highest risk of error or non-compliance and highlight opportunities to reduce the scope of examinations. This will lead to reduced cycle time and improved currency.

A consistent approach will also assist in improving employee satisfaction (both managers and examiners) by clearly specifying responsibilities and procedures in an area that currently causes confusion and differences of practice in the field.

In addition to assisting in identifying audit risk, this approach will help to alert managers and taxpayers to opportunities for the use of issue management techniques such as Alternative Dispute Resolution procedures and Pre-Filing Initiatives.

Materiality Agreements

Materiality agreements provide an opportunity to improve the efficiency of an examination. When materiality agreements are properly used, the IRS and the taxpayer do not spend time on insignificant items. In addition, audit cycle time should decrease resulting in examinations that are more current.

The examination team is responsible for establishing the materiality threshold. The IRM briefly discusses materiality in relation to the scope of an examination. Short-term timing issues should not be pursued, as they are not a good use of resources. Timing issues with long-term, indefinite or permanent deferral features should be considered. Unplanned timing issues, which arise as correlative adjustments during an examination of non-timing issues, should be made if it is cost effective to do so.

The IRS and the taxpayer should discuss possible areas for materiality agreements during the preliminary meetings. At this time it should be determined if there will be any exceptions to the materiality agreement. Materiality considerations may involve an evaluation of:

- Comparison of an expense item to the total deductions on the return
- Comparison of an income item to the total income reported on the return
- Comparison of a credit to the tax on the return
- Comparison of tax impact of an item to the tax per return
- Sheer dollar value of an item or transaction
- The absence of an item may be material
- Comparison of the item to gross receipts
- Comparison of the item to gross assets

During these preliminary meetings the taxpayer should advise the audit team of the materiality thresholds used in preparing the financial statements and tax return, so that the IRS is aware that certain adjustments considered immaterial by the taxpayer were not made.

Issues will be identified as accounting method issues and non-accounting method issues. A non-accounting method issue that is less material than an accounting method issue may be given a higher priority because by definition they are not timing issues. For example, research credit and § 274(b) ($25 gift limitation) are not timing issues. If the issue is an accounting method issue, materiality will be determined based upon the total of the § 481(a) adjustment and the current year adjustments for all filed returns subsequent to the year of change.

Accounting method issues may be delayed until a subsequent examination cycle when time does not permit the completion of the issue in the current examination cycle. In addition, accounting method issues that require an extensive amount of factual development may be developed over two examination cycles. The taxpayer should be provided written notification that the issue is under consideration but is being delayed until a subsequent examination cycle. The taxpayer and the examination team should discuss which facts would be necessary to make a determination of the proper amount. The taxpayer should start to gather these facts and have them available when the IDR is issued in the subsequent examination cycle.

The IRS and the taxpayer should review reports from prior cycles noting areas of agreement. If the facts and circumstances haven't changed significantly similar agreements could be reached in the current cycle. If this is done the IRS and the taxpayer could substantially reduce the amount of examination time required to resolve these issues. They should also look at areas of prior disagreement to see if they can jointly arrive at a solution that will satisfy both parties.

For complex tax computations, recurring in nature, a reasonable estimate may be used for the RAR with the understanding that exact amounts will be computed and used in all subsequently filed tax returns when possible. For example, the IRS and taxpayer agree to approximate a LIFO adjustment using an agreed upon "short-cut" method rather than requiring the taxpayer to go through a very lengthy and time-consuming recalculation for years in which returns have already been filed. Any necessary corrections would be made on the next filed return.

Each taxpayer, each cycle (CIC), each year (IC) is unique. A materiality threshold set for one cycle or year may or may not be appropriate for another year or cycle. A threshold must be set specifically for one taxpayer for one examination period and cannot be automatically rolled from one cycle into the next.

Claims

Several things are driving the need to improve the claims process. Under the current system, taxpayers often file both formal and informal claims late in the audit cycle or in Appeals. This causes workload problems for the Service as well as frustration for the taxpayer when closing dates are extended in order to address claims and affirmative issues. Contributing to the problem is the increase in marketed (contingency fee) claims and often the lack of documentation submitted with these claims.

A design team was formed to develop a process to better manage claims. The team was asked to draft procedures that will ensure consistent and timely processing, identify recurring and emerging issues, and issue timely guidance for claims. As a result of their efforts several initiatives are being developed.

Limited Issue Focused Examination (LIFE)

The Limited Issue Focused Examination (LIFE) (Information Release 2002-133), an alternative to the traditional broad-based examination process, may be considered for any LMSB examination where all parties (Service and taxpayer) commit to the process. It is equally applicable to domestic, international or other specialty areas. Agents and specialists will use risk analysis and materiality considerations to limit their examination of a return to the critical few issues. Most of the mandatory examination steps and compliance checks may be waived. LMSB will enter an agreement with the taxpayers to cover key aspects of the examination and require them to share in the responsibility for timely completion of the examination.

The focus of LIFE is on streamlining and accelerating the examination process by engaging taxpayers to share in the responsibility for completing the examination.

The key features of LIFE are:

- full risk analysis by the entire team
- setting materiality threshold(s) for issue selection
- full engagement of taxpayers to share in responsibility for timely completion of the examination
- memorandum of understanding (MOU) to govern key aspects of the examination
- many of the mandatory compliance checks may be waived
- scope is limited - may not be expanded without managerial approval

- LIFE process may be terminated by either the Service or the taxpayer if commitments specified in the MOU are not met.

The LIFE process is not one-sided. The Service will agree to limit the scope (to forego issues that would normally be included in the examination) in order to better manage our resources. In exchange, the taxpayer must agree to be a more responsive and accountable participant in the process. The commitment to support a Limited Issue Focus Examination is demonstrated by the taxpayer and the audit team entering into a Memorandum of Understanding (MOU) for the timely completion of the examination.

The elements addressed in this Memorandum of Understanding are:

- Key areas in which the taxpayer will brief the examination team (significant or unusual transactions, industry/business/market trends, key events, and accounting practices during the years under examination)
- IDR response times for the taxpayer and a commitment that the agent should respond to the taxpayer's IDR responses timely
- A commitment to discuss Notices of Proposed Adjustments as they are issued
- Filing of claims (timing, adherence to materiality thresholds, providing supporting documentation)
- Taxpayer responsibility to provide computations for all agreed rollover and recurring issues
- Materiality (to govern both issues raised by the examination team and those submitted in affirmative issues and claims)
- Lines of communication (how frequently meetings will be held, who will participate, etc.)
- Termination of the LIFE process.

An example illustrating how each of the above elements can be incorporated into the Memorandum of Understanding is posted on the LMSB LIFE Home Page.

Information Document Request (IDR) Management Process

LMSB has implemented the Information Document Request (IDR) Management Process (IRM 4.45.13.4.10) for use in Coordinated Industry Cases (CIC) and Industry Cases (IC). This formal, structured process to request and secure information from the taxpayer promotes cost effectiveness and quality examinations with the least burden on both the taxpayer and the government. The importance of timely responses is emphasized, as it will improve cycle time and currency of cases, while at the same time

focus on early issue resolution. This process does not preclude the examination team from using judgment on an "issue by issue basis". Realistic and cooperatively reached "due dates" for information requested by an IDR is key to the process.

The IDR Management Process accomplishes the following:

- Provides more complete and timely responses to IDRs
- Provides open and meaningful communication between all team members and the taxpayer
- Provides consistent treatment of taxpayers
- Heightens taxpayer understanding of expectations
- Improves the timeliness and the quality of documentation received
- Establishes a sound foundation for issue development
- Promotes earlier issue resolution
- Heightens Territory Manager and Team Manager's involvement
- Promotes better written and complete IDRs
- Improves awareness of outstanding IDRs.

To ensure IDR responses address the specific needs of the examiner, it is a good practice to have a "pre-IDR" meeting. At this meeting the agent and the taxpayer discuss exactly what is needed in order to eliminate any ambiguity. Once the "pre-IDR" meeting is held, the taxpayer and the examiner should agree to the due date, and such date should be realistic for the information being sought. There is also latitude for the team coordinator (CIC) or revenue agent team member (IC) to extend the IDR due date.

Since the IDR Management Process centers on an effective collaboration between the IRS and the taxpayer it is essential to conduct collaborative meetings with the taxpayer at key points of the Information Document Request (IDR) Management Process. IRM guidelines stipulate a series of meetings with the taxpayer to follow up on IDRs on the 15th, 30th, and 45th calendar day of delinquency. These conferences would not preclude the examination team from having monthly or quarterly meetings with corporate officials to discuss outstanding IDRs. The degree of managerial involvement and at what stage will vary, but the team manager should be involved when the IDR approaches the 45th day of delinquency. In cases where an IDR is delinquent more than 90 calendar days, a joint IDR status meeting should be held with the territory manager, IRS Counsel, team manager, the IDR requester, and senior tax officer of the taxpayer to address the issue and records that are needed for making a determination. Any recommendation to deviate from the process is made by the team coordinator

(CIC) or revenue agent team member (IC) and is subject to the team manager's approval.

Issue Management and Resolution

One of LMSB's strategic initiatives is issue management. Through effective issue management, LMSB seeks to resolve issues of tax controversy on a more current basis. This includes increasing the efficiency of the examination process and seeking alternative issue resolution tools. While LMSB is focusing on resolving tax differences at the lowest level, it is committed to preserving the quality and integrity of those determinations. To accomplish this goal it has expanded its use of pre-filing initiatives and post-filing dispute resolution techniques. In addition, LMSB has piloted several issue resolution programs believed to offer significant potential benefits for taxpayers as well as the Service.

While in the early years, LMSB's first successes were in the area of pre-filing agreements (PFA) for a single taxpayer and single year, they are now expanding efforts toward broad resolution tools that resolve an issue for multiple taxpayers and extend beyond one year. Future successes will be measured by the number of taxpayers impacted by an effort. Settlement by notice, instead of by appeal, will positively impact customer satisfaction, employee satisfaction, and business results. As the Service moves to an issue-driven compliance process, the goal is to position LMSB to allocate resources for taxpayer issues as opposed to resourcing for taxpayer returns. As the use of issue management products allows LMSB to save staff hours and redirect these resources to areas of other high compliance risks, they will need to evaluate whether the highest risk is in the area of pre-filing versus post-filing.

Pre-Filing Initiatives

- **Pre-Filing Agreement Program**

  Revenue Procedure 2001-22 (2001-9 I.R.B. 745; IRM 4.45.15.6) provides the basic information for taxpayers, subject to the jurisdiction of LMSB, to participate in the Pre-Filing Agreement (PFA) Program. A pre-filing examination can often resolve issues more effectively and efficiently than a post-filing examination because the taxpayer and the Service have more timely access to the records and personnel relevant to the issue. PFAs allow a taxpayer to request examination of specific issues involving factual questions and well-settled principles of law before the return is filed. A

pre-filing examination also provides the taxpayer with a greater level of certainty regarding the examined issue at an earlier point in time than a post-filing examination. Thus, the use of pre-filing examinations will benefit both taxpayers and the Service by improving the quality of tax compliance while reducing its costs, burdens and delay.

The Service generally will consider entering into an LMSB PFA on any issue that represents either (i) a factual determination or (ii) an application of legal principles to agreed upon facts in which the legal principles are well established in their application to such facts. The Revenue Procedure provides a list of excluded issues and an exclusive list of international issues that will be included in the PFA program. The LMSB Industry Director (or his duly authorized designee) with jurisdiction over the taxpayer will make the final decision whether to proceed with the taxpayer's request for an LMSB PFA.

If the taxpayer and Service are able to resolve the examined issues prior to the filing of the return, the Revenue Procedure authorizes the taxpayer and the Service to finalize their resolution by executing an LMSB PFA. The Director, Field Operations (or other authorized official) may execute an LMSB PFA. An LMSB PFA between the Service and the taxpayer is a closing agreement under § 7121, and accordingly, must comply with the requirements of Revenue Procedure 68-16,1968-1 C.B.770, regarding the form and content of closing agreements. LMSB PFAs are not written determinations under §6110, and accordingly, are exempt from disclosure to the public under the Freedom of Information Act (FOIA).

If the Service and the taxpayer cannot reach agreement prior to the filing of the return, the Service and the taxpayer may continue to attempt to resolve the issue. If the LMSB PFA is executed subsequent to the filing of the original return the taxpayer will acknowledge the expectation that an amended return will be filed and that if such return is not filed the Service will assess any additional tax due. A copy of the LMSB PFA must be attached to the amended return.

A request for an LMSB PFA should be submitted to the LMSB team manager in charge of the examination, in the case of a taxpayer whose return is currently under examination. In the case of a taxpayer whose return is not

currently under examination, the request should be mailed or faxed to the Manager, Pre-Filing Services. The inspection of records and testimony under the LMSB PFA procedures will not be considered an inspection or examination as defined in IRC § 7605(b). At any time prior to the execution of the LMSB PFA, either the taxpayer or the Service may withdraw from consideration of all or part of the request.

Taxpayers are subject to a user fee only if they are selected to participate in the LMSB PFA program. The user fees are based on the amount of assets held by the taxpayer per its most recently filed return.

- **Pre-Filing Determination**

  The purpose of a pre-filing determination (Revenue Procedure 2003-1, 2003-1 I.R.B. 1; IRM 4.45.15.5) is to provide an opportunity for the Service and taxpayer to agree on the treatment of completed transactions prior to the filing of the return to which they relate. A pre-filing determination is not concluded with a closing agreement and does not have the finality associated with closing agreements. It does relieve taxpayer burden by allowing the taxpayer to file more accurate tax returns and gives the taxpayer a high degree of assurance that the tax treatment of the transaction, as reflected on the filed return, will be accepted by the Service.

Generally, the examination team performing the examination of the in-process cycle will make the determination of the tax treatment on the transactions for which the tax return has not been filed. A pre-filing determination will usually not be issued for a question concerning a return to be filed by the taxpayer if the same question is involved in a return already filed. In addition, the Service ordinarily will not issue determination letters in certain areas because of the factual nature of the problem involved or because of other reasons. Revenue Procedure 2003-3 and Revenue Procedure 2003-7 provide a list of these areas. This list is not all-inclusive because the Service may decline to issue a determination letter when appropriate in the interest of sound tax administration or on other grounds.

All LMSB taxpayers may request one or more pre-filing conferences with the team manager of the taxpayer's in-process examination to explore the suitability of a pre-filing determination request. The pre-filing conference will clarify what information, documentation and analysis are likely to be needed and whether timeframes will be adequate to enable a pre-filing determination letter to be issued. If the Service and

the taxpayer concur on the suitability of a request, the taxpayer will then submit a written request containing the information in Section 8.01 of Revenue Procedure 95-1 or the successor Revenue Procedure with one exception. The information required in Section 8.01(2) need not be included in the written request but must be made available to the team members assigned to review the request. Failure by the taxpayer to provide any information required by these procedures when requested will be cause for the request to be rejected and to terminate the determination request.

The taxpayer must request a pre-filing determination in writing. See Revenue Procedure 2003-1 as to procedures for submission. The inspection and/or review of the taxpayer's books and records prior to the filing of the tax return to consider a pre-filing determination request is not considered an inspection or examination as defined in IRC § 7605(b). The Service or the taxpayer can withdraw from the pre-filing determination process at any time.

A pre-filing determination letter will not be issued if:
(a) The taxpayer has directed a similar inquiry to the National Office
(b) The same issue involving the same taxpayer or related taxpayer is pending in a case in litigation or before an Appeals Office or is being addressed in an in-process examination; or
(c) The determination letter is requested by an industry, trade association or similar group.

Pre-filing determination letters are not reviewed by the National Office. However, they must apply the principles and precedents previously announced by the National Office to a specific set of facts. They are issued only when a determination can be made based on clearly established rules in the statute, a tax treaty, or the regulations, or based on a conclusion in a revenue ruling, opinion or court decision published in the Internal Revenue Bulletin that specifically answers the question presented.

If a taxpayer does not agree with a pre-filing determination letter, the taxpayer may ask the territory manager for reconsideration. The Director of Field Operations has final authority on whether to accept or reject a pre-filing determination request for reconsideration.

If a taxpayer takes a contrary position to the pre-filing determination letter but attaches it to the applicable tax return and advises that it is taking an adverse position, then this action should satisfy the adequate disclosure provisions under the penalty provisions of the IRC sections 6661/6662. In the event a contrary position is taken by a non-CIC taxpayer, the taxpayer must also attach a Form 8275 and/or Form 8275-R to the applicable tax return to advise the Service that the taxpayer is taking an adverse position. In any event, a CIC taxpayer, under Revenue Procedure 94-69, has 15 days to advise the Service that it has taken a position contrary to the pre-filing determination after the disclosure statement is requested by the team manager.

The text of determination letters is open to public inspection under § 6110. The Service makes deletions from the text before it is made available for inspection. To help the Service make the deletions required by § 6110(c), a request for a determination letter must be accompanied by a statement indicating the deletions desired.

For applicable user fees see section 15 and appendix A of Revenue Procedure 2003-1.

- **Letter Ruling**

  A "letter ruling" (Revenue Procedure 2003-1, 2003-1 I.R.B.1) is a written statement issued to a taxpayer by the National Office that interprets and applies the tax laws to the taxpayer's specific set of facts. A letter ruling includes the written permission or denial of permission by the National Office to a request for a change in a taxpayer's accounting method or accounting period. Once issued, a letter ruling may be revoked or modified for any number of reasons, as explained in section 12 of Revenue Procedure 2003-1, unless it is accompanied by a closing agreement.

The taxpayer must request a letter ruling in writing. See Revenue Procedure 2003-1 as to procedures for submission. The inspection and/or review of the taxpayer's books and records prior to the filing of the tax return to consider a letter ruling request is not considered an inspection or examination as defined in IRC § 7605(b).

In income tax matters, the National Office generally issues a letter ruling on a proposed transaction and on a completed transaction if the letter ruling request is submitted before the return is filed for the year in which the transaction that is the

subject of the request was completed. The National Office ordinarily does not issue a letter ruling if, at the time the letter ruling is requested, the identical issue is involved in the taxpayer's return for an earlier period and that issue – (a) is being examined by a field office; (b) is being considered by an area office; (c) is pending in litigation in a case involving the taxpayer or a related taxpayer; (d) has been examined by a field office or considered by an area office and the statutory period of limitations on assessment or on filing a claim for refund or credit of tax has not expired; or (e) has been examined by a field office or considered by an area office and a closing agreement covering the issue or liability has not been entered into by a field office or by an area office.

A letter ruling will be used by a field office in examining the taxpayer's return. The field office must ascertain whether: (1) the conclusions stated in the letter ruling are properly reflected in the return; (2) the representations upon which the letter ruling was based reflected an accurate statement of the controlling facts; (3) the transaction was carried out substantially as proposed; and (4) there has been any change in the law that applies to the period during which the transaction or continuing series of transactions were consummated. If, when determining the liability, the field office finds that a letter ruling should be revoked or modified, the findings and recommendations of the field office will be forwarded through the appropriate director to the National Office for consideration before further action is taken by the field office.

The Service ordinarily will not issue letter rulings in certain areas because of the factual nature of the problem involved or because of other reasons. Revenue Procedure 2003-3 and Revenue Procedure 2003-7 provide a list of these areas. This list is not all-inclusive because the Service may decline to issue a letter ruling when appropriate in the interest of sound tax administration or on other grounds.

The text of letter rulings is open to public inspection under § 6110. The Service makes deletions from the text before it is made available for inspection. To help the Service make the deletions required by § 6110(c), a request for a letter ruling must be accompanied by a statement indicating the deletions desired.

For applicable user fees see section 15 and appendix A of Revenue Procedure 2003-1.

- **Advanced Pricing Agreement (APA)**

  An advanced pricing agreement (APA) (Revenue Procedure 96-53, 1996-2 C.B. 375) is an agreement between the Service and the taxpayer on the transfer pricing methodologies (TPM) to be applied to any apportionment or allocation of income, deductions, credits, or allowances between or among two or more organizations, trades, or businesses owned or controlled, directly or indirectly, by the same interests. The TPM thus represents the application to the taxpayer's specific facts and circumstances of the best method within the meaning of the income tax regulations under § 482 of the Internal Revenue Code, as agreed pursuant to negotiations between the Service and the taxpayer.

  Under the APA request procedure, the taxpayer proposes a TPM and provides data intended to show that the TPM is the appropriate application of the best method within the meaning of the regulations for determining arm's length results between the taxpayer and specified affiliates with respect to specified intercompany transactions. The Service evaluates the APA request by analyzing the data submitted and any other relevant information. After discussion, if the taxpayer's proposal is acceptable, the parties execute an APA covering the proposed TPM. APAs often involve agreements with foreign competent authorities under income tax conventions. In negotiations for APAs involving one or more foreign competent authorities ("bilateral" and "multilateral" APAs), the initial negotiating position of the U.S. competent authority will reflect the Service's opinion, based on consultation with the taxpayer, of the best method within the meaning of the regulations and the appropriate TPM.

  The taxpayer must propose an initial term for the APA. For example, the APA could take effect at the beginning of the taxable year during which it was requested or signed, and last for three taxable years. The term should be appropriate to the industry, product, or transaction involved.

  Application of the TPM to tax years prior to those covered by the APA ("rollback" of the TPM) is an effective means of enhancing voluntary compliance and an effective use of resources in addressing unresolved transfer pricing issues. It is Service policy that, whenever feasible (based, for example, on consistency of facts, law, and available records in the prior years), the TPM should be used for resolving such issues for prior taxable years. In addition, as provided in section 8 of Revenue Procedure 96-53, the taxpayer may request that the Service consider a rollback in

connection with a particular request. When applying the TPM to prior years, whether or not at the request of the taxpayer, adjustments may be made to reflect differences in facts, economic conditions, and applicable legal rules.

For applicable user fees see section 5.14 of Revenue Procedure 96-53.

Post-Filing Dispute Resolution Techniques

- **Technical Advice**
  Technical Advice Memorandum (TAM)
  Technical Expedited Advice Memorandum (TEAM)
  "Technical Advice" means advice or guidance in the form of a memorandum (referred to as a TAM) furnished by the National Office upon the request of a Director and/or Area Director, Appeals, submitted in accordance with the provisions of Revenue Procedure 2003-2, in response to any technical or procedural question that develops during any proceeding on the interpretation and proper application of tax law, tax treaties, regulations, revenue rulings, notices, or other precedents published by the National Office to a specific set of facts. Such proceedings include: (1) the examination of a taxpayer's return; (2) the consideration of a taxpayer's claim for refund or credit; (3) any matter under examination or in appeals pertaining to tax-exempt bonds, tax credit bonds, or mortgage credit certificates; and (4) any other matter involving a specific taxpayer under the jurisdiction of the territory manager or the Area Director, Appeals. Requests generally originate with the examining agent or appeals officer assigned to the case and are submitted through the supervisory chain to the Director or Area Director, Appeals. While a case is under the jurisdiction of a Director or Area Director, Appeals, a taxpayer may request that an issue be referred to the National Office for a TAM. The request may be oral or written and should be directed to the examining agent or appeals officer. The TAM procedures no longer require that there be an agreed upon set of facts for a TAM to be issued. Instead, a TAM will be issued addressing both the taxpayer's and the field's facts.

  "Technical Expedited Advice Memorandum" means technical advice issued in an expedited manner (referred to as a TEAM) subject to agreement among the taxpayer, field or area office, and the National Office. Any issue eligible for a TAM can be submitted for TEAM treatment. A TEAM has several characteristics that are different from a TAM, including a mandatory pre-submission conference involving the taxpayer (except in two situations where taxpayer concurrence is not required for

TEAM procedures). The procedures associated with the issuance of a TEAM help expedite certain aspects of the TAM process and eliminate some of the requirements that may delay or frustrate the TAM process. A TEAM will generally be issued within 60 days of receipt of the TEAM request. In the event that a taxpayer chooses not to participate in a request for a TEAM, the request will usually be treated as a request for a TAM.

A TAM or a TEAM should be requested when there is a lack of uniformity regarding the disposition of an issue or when an issue is unusual or complex enough to warrant consideration by the National Office. A taxpayer may not rely on a TAM or TEAM issued by the Service for another taxpayer. See § 6110(k)(3).

TAMs and TEAMs help Service personnel close cases and also help establish and maintain consistent technical positions throughout the Service. A Director or an Area Director, Appeals may raise an issue in any tax period, even though a TAM or TEAM may have been requested and furnished for the same or similar issue for another tax period.

The text of TAMs and TEAMs are open to public inspection under § 6110 (a). The Service deletes certain information from the text before it is made available for inspection. To help the Service make the deletions required by § 6110(c), the taxpayer must provide a statement indicating the deletions desired. If the taxpayer does not submit the deletions statement, the Service will follow the procedures in section 14.06 of Revenue Procedure 2003-2.

- **Delegation Order 236 (Rev. 3)**

  Application of Appeals Settlement to CIC Taxpayers

  Delegation Order 236 (IRM 4.45.15.2) gives team managers limited settlement authority with respect to certain issues. It does not restrict nor reduce the issue resolution capabilities otherwise vested with team managers. Its purpose is to assist in relieving taxpayer burden and reducing both Service and taxpayer costs when similar issues exist which are beyond examination's resolution capabilities.

  Delegation Order 236 settlement authority may be exercised only if all of the following factors are present:

  1. The issue is in a Coordinated Industry Case under the jurisdiction of the compliance function (draft Delegation Order 236 (Rev. 4) expands authority to Industry Cases);

2. A settlement has been effected by Appeals in the same, previous or subsequent tax period;
3. The facts are substantially the same as the facts in the Appeals settled tax period;
4. The legal authority is unchanged;
5. The underlying issue was settled by Appeals independently of other issues;
6. The issue was settled in Appeals, with respect to: the same taxpayer (including consolidated or unconsolidated subsidiaries), or another taxpayer who was directly involved in the same transaction or taxable event in the settled period (i.e. whipsaw case).

To ensure consistency and to effect a more binding and permanent agreement with the taxpayer, Form 870-AD and/or closing agreement must be used in all instances where Examination Settlement Authority is exercised.

- **Delegation Order 4-25**

  Settlement Authority for Coordinated Issues

  Team managers should look to Delegation Order 4-25 (which superceded DO 247 (Rev. 1)), instead of Delegation Order 236, whenever Coordinated Issues are being considered for settlement. Since Delegation Order 236 does not specifically state that team managers have the authority to settle Technical Guidance coordinated issues previously acted upon by Appeals, these kinds of issues may be settled only if Delegation Order 4-25 applies.

  Technical Guidance coordinated issues can be settled by the team manager only if Appeals has issued written settlement guidelines. Appeals has issued significant numbers of written settlement guidelines and is in the process of developing written guidelines for the remaining coordinated Technical Guidance issues; and will develop guidelines for future coordinated issues as they are identified. Accordingly, most coordinated issues would be subject to examination settlement authority.

  The delegation order also grants the authority to execute closing agreements, or the Form 870-AD necessary to effect any settlement reached.

- **Fast Track Settlement**

  "Fast Track Settlement" (FTS) (IRS News Release No: IR-2003-44) is a process for large corporations to settle tax disputes before the audit of their return is complete.

LMSB and the Office of Appeals offer a joint process that uses Appeals personnel as mediators in LMSB cases. Based on the Appeals Officer's analysis of the issues, Appeals may also recommend a settlement.

Full implementation of the program followed a successful pilot, during which the taxpayer and the IRS reached agreement on 91 percent of the issues. The average time span to resolve a dispute was about one-tenth the usual time span for an Appeals settlement.

FTS is optional for the taxpayer. FTS does not eliminate or replace existing dispute resolution options, including the taxpayer's opportunity to request a conference with a manager or a hearing before Appeals. In the FTS process, Appeals' role is to provide a neutral party, someone who will help the taxpayer and LMSB understand the nature of the dispute and reach a mutually satisfactory resolution. The Appeals Officer may also recommend a settlement.

The taxpayer may withdraw from the FTS process at any time. The LMSB team manager or the Appeals Officer may stop the Fast Track process as well, if either determines that they are not progressing toward resolution of the issues. If there are any issues at the end of the FTS process, the taxpayer retains all applicable appeal rights.

Official guidance for enrolling in FTS will be available in a forthcoming revenue procedure.

- **Accelerated Issue Resolution (AIR)**
  Accelerated Issue Resolution (AIR) (Revenue Procedure 94-67; 1994-2 C.B. 800; IRM 4.45.15.4) is an examination process to advance the resolution of the same or similar issues arising from an examination of a CIC taxpayer from one or more tax periods to other tax periods. Extending the examination of issues to more current tax periods allows the audit team to examine books and records that are more contemporary and more accessible. In all likelihood, taxpayer personnel knowledgeable with the underlying transactions of the issue will still be with the company and available for discussion. AIR also promotes a more efficient use of resources. Advancing the resolution of the same issues to later tax periods using the same audit team and taxpayer personnel ensures continuity and reduces the learning curve a new audit team must overcome. Finally since AIR is voluntary,

there is an underlying presumption that all parties will expeditiously work to resolve not only the AIR issues but also the entire examination.

An AIR agreement is a closing agreement under § 7121 of the Internal Revenue Code. Revenue Procedure 94-67 provides the requirements for AIR agreements. With few exceptions including Advanced Pricing Agreements, Employee Plans, and TEFRA items, an AIR agreement may be entered into with respect to any issue under the jurisdiction of the Director, Field Operations (DFO) arising from the audit of a CIC taxpayer for a taxable period(s) ending prior to the date of the agreement. The suggestion for an AIR agreement can originate either with the team manager, team members or the taxpayer. However, the taxpayer must formally initiate the procedure with a written AIR request. The taxpayer and/or Service can withdraw from the process anytime prior to execution of the AIR closing agreement.

The information received or generated by the Service during the AIR agreement process constitutes return information and therefore is not open to public inspection under § 6110.

AIR does not alter in any way the authority team managers have to resolve issues. Unlike Delegation Order 236, AIR does not give managers added settlement authority.

- **Early Referral to Appeals**

  Early referral (Revenue Procedure 99-28; 1999-2 C.B. 109) is a process to resolve cases more expeditiously through the field and Appeals working simultaneously. Early referral is optional and may be requested by any taxpayer.

  Examination issues appropriate for early referral are limited to those that:

  1. if resolved, can reasonably be expected to result in a quicker resolution of the entire case;
  2. both the taxpayer and the field agree should be referred to Appeals early;
  3. are fully developed; and
  4. are part of a case where the remaining issues are not expected to be completed before Appeals could resolve the early referral issue.

Early referral does not include an issue:

1. with respect to which the 30-day letter has been issued;
2. that is designated for litigation by the Office of Chief Counsel;
3. for which the taxpayer has filed a request for Competent Authority assistance, or issues for which the taxpayer intends to seek Competent Authority assistance; or
4. that is part of a whipsaw transaction.

If an agreement is reached with respect to an early referral issue generally, a Form 906, Closing Agreement on Final Determination Covering Specific Matters, is prepared. The closing agreement is used to compute the corrected tax as a partial agreement prior to or concurrently with the resolution of any other issues in the case.

If early referral negotiations are unsuccessful and an agreement is not reached with respect to an early referral issue:

1. Taxpayers may then request mediation for the issue, provided the early referral issue meets the requirements for mediation. See Announcement 98-99, 1998-46 I.R.B. 34, or any subsequent procedures. If mediation is not requested, Appeals will close the early referral file and return jurisdiction over the issue to the field. Appeals will send a copy of the Appeals Case Memorandum for the issue to the team/group manager.
2. Appeals will not reconsider an unagreed early referral issue if the entire case is later protested to Appeals, unless there has been a substantial change in the circumstances regarding the early referral issue.

If the only unagreed issues present in the case at the time the examination is concluded are issues that were considered by Appeals under the early referral process and returned to the field unagreed, no 30-day letter will be issued. Instead, a statutory notice of deficiency (90-day letter) will be issued.

- **Appeals Arbitration**

Announcement 2002-60 (2002-26 I.R.B.28) modifies and extends the test of the arbitration procedure set forth in Announcement 2000-4, 2000-1 C.B. 317, for an additional one year period beginning on July 1, 2002.

This procedure allows taxpayers to request binding arbitration for factual issues that are already in the Appeals process. Under the procedure set forth in Announcement 2000-4, the taxpayer and Appeals must first attempt to negotiate a settlement. If

those negotiations are unsuccessful, the taxpayer and Appeals may jointly request arbitration. The arbitration program is consistent with IRS' efforts to improve tax administration, provide customer service, and reduce taxpayer burden.

- **Appeals Mediation**

Revenue Procedures 2002-44 (2002-26-I.R.B.10) formally establishes the Appeals mediation procedure; and modifies and expands the availability of mediation for cases that are already in the Appeals administrative process.

The mission of Appeals is to resolve tax controversies, without litigation, on a basis which is fair and impartial to both the Government and the taxpayer. Mediation is an extension of the Appeals process and will enhance voluntary compliance. Mediation is a nonbinding process that uses the services of a mediator, as a neutral third party, to help Appeals and the taxpayer reach their own negotiated settlement. This mediation procedure requires the use of an Appeals employee who is a trained mediator. The taxpayer may also elect to use a non-Internal Revenue Service co-mediator, at the taxpayer's expense. The mediator will act as a facilitator, assist in defining the issues, and promote settlement negotiations between Appeals and the taxpayer. The mediator will not have settlement authority in the mediation process and will not render a decision regarding any issue in dispute.

Mediation may be used only after Appeals settlement discussions are unsuccessful, and, generally, when all other issues are resolved but for the issue(s) for which mediation is being requested.

Mediation is available for:

1. Legal issues;
2. Factual issues;
3. Coordinated Issues;
4. An early referral issue when an agreement is not reached, provided the early referral issue meets the requirements for mediation; and
5. Issues for which the taxpayer intends to seek competent authority assistance, provided a request for competent authority assistance has not as yet been filed.

Industry Wide Resolution Programs

- **Industry Issue Resolution (IIR) Program**

  The objective of the Industry Issue Resolution (IIR) Program (Rev. Proc. 2003-36; 2003-18 I.R.B. 1) is to provide guidance to resolve frequently disputed or burdensome tax issues common to a significant number of business taxpayers. The Large and Mid-Size Business Division (LMSB) and Small Business/Self-Employed Division (SB/SE) will jointly undertake the operational responsibility for the projects in the program. Resolution of contentious issues other than by the examination process is a strategic goal of both LMSB and SB/SE.

  Taxpayers, as well as industry associations and other groups representing taxpayers, are invited to suggest issues and possible options for resolution. Parties submitting suggestions may be asked to meet with government representatives and to provide additional information. After analysis and review, the Service, the Office of Chief Counsel, and Treasury intend to select issues to address in the IIR program.

  The form of resulting guidance may vary depending on the issue. However, the most likely form of guidance will be a Revenue Ruling or a Revenue Procedure that permits taxpayers to adopt a recommended treatment of the issue on future returns.

  Issues most appropriate to the program generally will have two or more of the following characteristics:

  - There is uncertainty about the appropriate tax treatment of a given factual issue.
  - The uncertainty results in frequent, often repetitive examinations of the same issue.
  - The uncertainty results in significant taxpayer burden.
  - The issue is material and impacts a significant number of taxpayers, either within an industry or across industry lines.
  - Factual determination is a major component of the issue.

  The following issues are not suitable for the IIR program:

  - Issues unique to one or a small number of taxpayers.
  - Issues under the jurisdiction of the Commissioner, Tax Exempt and Government Entities Division (e.g., employee plans).
  - Issues regarding transactions that lack a bona fide business purpose or are done with a significant purpose of reducing or avoiding federal taxes.
  - Issues involving transfer pricing or international tax treaties.

No particular format is required for submissions. However, submissions should briefly describe the proposed issue and explain why there is a need for guidance. Submissions may include an analysis of how the issue may be resolved. In addition, submissions should state the number of taxpayers estimated to be affected by the issue. All submissions will be available for public inspection and copying in their entirety. Therefore, comments should not include taxpayer specific information of a confidential nature.

- **Coordinated Issues**
  Coordinated Issues (IRM 4.40.1.1.1.7) may be proposed by Technical Advisors to ensure that key issues within particular industry or issue areas are raised, developed and resolved on a consistent basis. The purpose of Coordinated Issues is to provide examiners with guidance on significant national issues to ensure consistent resolution. Coordinated Issues establish uniform positions within industry or issue areas. Examiners cannot deviate from such positions without the concurrence of the Industry/Issue Technical Advisor teams.

Rules Of Engagement

IRM 4.51.1 presents guidelines for case interactions by LMSB executives and senior leadership. These guidelines, which were developed to support decisions to elevate issues upward, are formally known as “Rules of Engagement”.

Each level or individual participating in a case needs to understand his or her own accountability and authority. In addition other parties need to understand why an individual is or is not involved in a case. The approach to case interaction should be clear and ensure end-to-end accountability, with emphasis on:

- Getting to the right answer for a particular case
- Consistency among similar taxpayers
- Timeliness of work and service to the taxpayer
- Organizational efficiency and employee empowerment.

The IRM lists the criteria developed to support decisions to advance issues to a higher level and explains executive and senior leadership tactical and strategic responsibilities. Executive and senior leadership case interaction can commence at any level, but should be guided by these criteria and by the strategic/tactical responsibilities at each management level. Case interaction is defined to be a case related, positive contact to

achieve a shared outcome. It may occur at any phase of post-filing, from the filing of the tax return through the examination/processing phase to the collection phase. In addition, case interaction may occur in pre-filing (e.g. Industry Issue Resolution, Pre-Filing Agreement, and Advanced Pricing Agreement).

Executive/senior leader interaction in cases is triggered either by the needs of the case or the team and by opportunities. When this interaction occurs the senior leader or executive is required to meet with the examination team to keep them fully apprised of decisions made that impact the examination process of the case. Meetings conducted by the senior leader or executive should occur at the opening and closing of the case interaction, and at any other time when necessary for effective communication with the examination team.

To help clarify and define roles and case interactions the following principles have been established:

- The executive/senior leader is part of the overall team and the team must act as one
- The team should work through ideas, issues, or concerns internally before deciding to elevate them
- Push decision-making to those closest to the facts
- Ensure ethics and integrity are used in decision making
  - Do nothing to compromise decision-making
  - Ensure that decisions are made with the team
  - When necessary decisions may be made without the team. If this is required the decision and rationale for the decision must be communicated and understood by the team
- Involvement of executives/senior leadership in the case must add value and build trust
- Ensure fairness and consistency in tax administration.

Roles vary across the different levels, reflecting the distribution of strategic and tactical responsibilities as well as consistent treatment on cases not under line authority. The fundamental roles of executives and senior leaders include:

- Identify, market, implement best practices
- Remove obstacles
- Facilitate discussion, consistency, and issue resolution
- Foster positive relationship with taxpayer

- Communicate vision, initiatives, and new information
- Empower staff to make decisions at lowest level
- Provide mentoring and coaching
- Deliver resources and support to the team
- Promote cooperation among groups, territories, and industries.

Understanding and applying the rules and guidelines set forth in IRM 4.51.1 will help to establish clear communication with end-to-end accountability and help the examination team and the taxpayer get to the right answer for their case. The process will also help to achieve consistency among similar taxpayers, improve the timeliness of examinations, enhance organizational efficiency and empower employees.

Summary

This document discusses common audit practices and procedures, and also introduces a planning and monitoring tool, which can effectuate sound and productive planning for both LMSB and the taxpayer. The premise is simple; get the right people involved; get them involved early; agree on the examination parameters and pursue the examination in a mutually cooperative framework. This means the team manager must involve Counsel and the appropriate specialists early; and the audit team must base their examination planning decisions on quality risk analyses and reasonable materiality thresholds. Additionally, progress needs to be closely monitored and adjustments and corrections made as needed to facilitate the examination. If and when problems arise, they should be resolved quickly using all available tools and whatever level of authority is required to assure a fair outcome. Underlying the success of the “Joint Audit Planning Process” is the need to build relationships that can sustain a true working partnership based upon mutual trust and openness. If the guidelines in the planning and monitoring tool are followed the examination process will become more efficient and less contentious. These gains in efficiency and reduction in factious interactions will translate into reduced time expenditures, improved currency and better working relationships.