

TAX EXECUTIVES INSTITUTE – COMMISSIONER OF INTERNAL REVENUE AND LARGE
BUSINESS & INTERNATIONAL DIVISION
LIAISON MEETING
FEBRUARY 26, 2015
MINUTES

On February 26, 2015, a delegation from Tax Executives Institute met with John A. Koskinen, Commissioner of Internal Revenue, and other officials of the Internal Revenue Service. The following minutes were prepared by Tax Executives Institute and, although reviewed by the IRS, they have not been formally approved by the Agency. The agenda for the meeting was submitted in advance and was published in the May/June 2015 issue of Tax Executive magazine and on TEI's website.

IRS Delegation

John A. Koskinen, *Commissioner of Internal Revenue*
John M. Dalrymple, *Deputy Commissioner Services and Enforcement*
William J. Wilkins, *IRS Chief Counsel*
Kirsten Wielobob, *Chief, Appeals*
Heather C. Maloy, *Commissioner, Large Business and International (LB&I) Division (by phone)*
Douglas O'Donnell, *Deputy Commissioner (International), LB&I*
J. David Varley, *Director, Transfer Pricing Operations (Acting)*
Nikole Flax, *Special Assistant to the Chief, Appeals*
Thomas Brandt, *Chief Risk Officer*
Kimberly Edwards, *Director, Field Operations (North West) Acting (by phone)*
Rosemary Sereti, *Assistant Deputy Commissioner for Services and Enforcement*
Terry Lemons, *Chief, Communications and Liaison*
John Lipold, *Chief, Relationship Management, Office of National Public Liaison*
Kathryn Gregg, *Stakeholder Liaison Program Manager, LB&I*

TEI Delegation

Mark C. Silbiger, The Lubrizol Corporation, *TEI International President*
Charles N. (Sandy) Macfarlane, Chevron Corporation, *TEI Senior Vice President*
Janice L. Lucchesi, *TEI Secretary*
Robert L. Howren, BlueLinx Corporation, *TEI Treasurer*
Paul Magrath, AstraZeneca Canada, Inc., *TEI Executive Committee*
Karen E. Miller, FusionStorm, *TEI Executive Committee*
Gary P. Steinberg, Level 3 Communications, Inc., *TEI Executive Committee*
David E. Stevens, Cook Inlet Region, Inc., *TEI Executive Committee*
Ernest N. Gates, Wal-Mart Stores, Inc., *Chair, TEI IRS Administrative Affairs Committee*
Gary P. Hickman, Oldcastle, Inc., *Chair, TEI Federal Tax Committee*
Eli J. Dicker, *TEI Executive Director*
W. Patrick Evans, *TEI Chief Tax Counsel*
Benjamin R. Shreck, *TEI Tax Counsel*
Lee Gillespie-White, *TEI Corporate Counsel*

Welcome and Introductions

Mr. Silbiger expressed his gratitude for the open dialogue between the Commissioner, TEI members, and the IRS's operating divisions during TEI's annual liaison meetings and thanked the Commissioner and members of his staff for hosting the meeting and taking the time to meet with the Institute's delegation.

Commissioner's 2015 Priorities

The Commissioner welcomed TEI and outlined the major challenges the IRS is facing with budget cuts. He added that the IRS must continue to work effectively even while facing declining resources. One of the ways to manage resource constraints, he said, is to move more quickly into the digital world. Questions that are facilitated by digital exchanges allow for quick responses.

The ultimate goal, he said, is to become more efficient, even while facing added tax administration responsibilities, such as the Affordable Care Act reporting regulations, implementation of the Achieving a Better Life Experience Act, and the certification requirement for professional employer organizations.

The Commissioner summarized the range of items on the IRS's agenda, including cyber security to avoid ID theft and refund fraud, and improper payments of the earned income tax credit, among others. He noted that the IRS may ask for Form W-2 in January, when certain states receive them, to start the filing season earlier.

Leveraging Stakeholders

The Commissioner said that TEI is a valued stakeholder and stressed the importance of hearing concerns from various IRS constituencies and receiving constructive feedback. He added that the idea of conducting a joint training program with TEI was intriguing and he would be delighted to pursue the opportunity if appropriate. He noted that the IRS is currently partnering with tax preparers on training.

TEI's delegation added that it would like to further interact with the IRS to complement TEI's business knowledge with the IRS's technical knowledge to their mutual benefit. The ensuing discussion focused on how to make collaboration on both technical and procedural matters affordable and workable.

The Commissioner agreed that the fair administration of the tax process was a joint goal that required more joint training. He said he was pleased to learn at a Forum on Tax Administration meeting that the compliance assurance process (CAP) was identified as a successful example of how a tax authority can work collaboratively with large business taxpayers. Collaboration can lead to agreement between taxpayers and the IRS on issues to address and, in many instances, is a more efficient way to achieve revenue administration goals than a traditional audit. He added that he had a recent discussion about the CAP program on Capitol Hill.

Compliance Assurance Process

The TEI delegation said that the CAP program is a model for best practices in tax administration and that the monthly conference calls between TEI's CAP subcommittee and LB&I officials who oversee the CAP program are a good example of communications between taxpayers and the IRS where issues can be discussed and efficiently resolved in an informal setting. TEI's

delegation expressed enthusiastic interest in continuing these informal interchanges with new LB&I leadership. TEI outlined some concerns with the evolution of CAP, including that some auditors tend to revert to traditional audit practices, rather than recognizing they are operating in the CAP environment and adhering to established materiality thresholds. In addition, there are difficulties in examining research credit issues under CAP and a disconnect between the 24-month timeline of the Transfer Pricing Audit Roadmap and the timing of a CAP audit. Ms. Maloy stated that the IRS needs to look more closely at how transfer pricing issues fit into a CAP audit. TEI asked whether LB&I anticipated allocating increased resources to training agents on CAP principles and CAP audits. Ms. Maloy replied that CAP has been a good experience for the IRS and they would like to continue to build on the program.

TEI asked whether it was possible to develop a simplified approach to processing transfer pricing adjustments by booking the entire adjustment in the current audit cycle, rather than filing amended returns for prior years, similar to what is done under section 481A. Interest could then be calculated as if amended returns were filed and processed with the other adjustments. Such a process would also simplify corresponding state income tax filings. Mr. O'Donnell commented that this was not a new issue, as it exists in the Mutual Agreement Procedure (MAP) process and, in this context, procedures and regulations of the foreign country counterparty would need to be considered. Mr. Varley added that if such an arrangement were adopted, it would need to be added to bi-lateral agreements. TEI noted that adoption of a simplified process would save significant time and resources for both taxpayers and the IRS and encouraged LB&I leadership to continue to study it.

LB&I Examination Process

Reengineered, Issue-Focused Process

TEI expressed optimism that LB&I could successfully implement an issue-based examination process that is more effective and efficient than the current case-based process and stated that the Institute stands ready to continue to work with LB&I in its efforts. The delegation welcomed an update on LB&I's progress and asked for LB&I's current thinking on whom in the chain of command would have overall responsibility for managing the various LB&I issue teams in an issue-based exam. Ms. Maloy replied that LB&I had received many comments, from both external and internal stakeholders, and continues to revise the process in light of those comments. She added, however, that there is no official timeframe for when the process will be rolled out to the field. Ms. Edwards said that the LB&I project development team had received some feedback voicing concern over who would exercise overall control over the case. She added that LB&I's vision is to have one case manager who exercises primary administrative responsibility for coordinating the various issues in a case. LB&I is committed to an issue-based approach, however, which may result in different LB&I personnel responsible for resolving different issues depending on the issue and the team's expertise. The issue manager and case manager (who may be the same person) will need to collaborate and coordinate with each other to move the case to closure.

TEI's delegation noted that working with different issue teams and having more than one person responsible for deciding matters depending on the issue will make it difficult to keep the audit moving forward. Ms. Maloy said she understood the point and noted that the LB&I project team is looking at best practices around the country to incorporate into the new examination process. She acknowledged that the process may not work perfectly from the start and added that the plan is to adjust the approach over time based on feedback. Ms. Edwards explained that part of the approach is to push down judgment to the lowest level on the LB&I side, so the process is

nimble and agile enough to respond to specific situations. She added that at the planning stage of the examination there would be flexibility for the audit team and taxpayer to agree on a specific approach.

TEI's delegation asked what the overall goal of the new process was and if it would result in faster audit cycles. Ms. Maloy responded that the point of the new audit approach is to make the audit process more efficient by implementing best practices identified in LB&I's peer review of its examinations, but the new process would not necessarily result in shorter examinations. The length of an audit will depend on the issues examined and taxpayer cooperation.

Opportunities for Streamlined Processes

TEI asked whether the IRS would be interested in evaluating a new rapid issue resolution procedure whereby taxpayers would proactively identify a material tax item at the beginning of an audit and agree to provide cooperative disclosures in exchange for the IRS giving that item priority status on examination and in Appeals if unresolved on audit.

Ms. Maloy expressed skepticism in such a process, noting that putting items on different tracks seemed inefficient. She asked how this might differ from a Pre-filing Agreement (PFA) and Fast Track Settlement with Appeals. TEI responded that a PFA is available to resolve issues before an item is reported in a return and the proposed streamlined process would apply in a post filing environment. Moreover, some taxpayers may not wish to avail themselves of the Fast Track procedure, which entails Appeals' intervention into a case while the case is still in the jurisdiction of the Examination Division. Ms. Maloy was unmoved as to the merits of such a process, but stated LB&I would consider a proposal if put in writing.

Affirmative Claims

TEI's delegation expressed concern over LB&I's plans to limit the time period for filing affirmative claims during the course of an examination. Ms. Maloy reaffirmed LB&I's intention to do so, but added that details concerning the limitation and exceptions to the limitation were still being discussed.

Risk Assessment and Issue Selection

The TEI delegation asked how the risk assessment and issue identification process would change in connection with the move to an issue-based examination model. Ms. Maloy said that LB&I is working on how to improve the process but opted not to provide further details.

TEI's delegation asked whether the IRS's risk assessment process would consider taxpayers' corporate governance and internal tax control framework. TEI explained that other tax authorities do this as part of their risk-based assessment of taxpayer returns and it was also recommended in a 2014 Internal Revenue Service Advisory Council (IRSAC) report in which IRSAC suggested that LB&I refine its risk assessment program by creating a working group of CAP taxpayers. TEI asked for LB&I's views on this proposal and the 2014 Report generally. Ms. Maloy stated that something similar was attempted before by a previous IRS Commissioner, but feedback from taxpayers was negative.

Increased Use of Email

The TEI delegation commented that an issue-based examination approach would likely increase offsite examination work, which would further highlight the need for efficient communications between examiners and taxpayers. The delegation stated that there seemed to be a divergence among examiners, some of whom are willing to correspond with taxpayers through email and others who will not, and asked LB&I to explain its current email policy. Ms. Maloy explained that there are tools in place, such as e-fax and secure e-mail, to facilitate electronic correspondence. Examiners are free to accept documents via email at any time, but a formal agreement is needed before an agent will send documents to a taxpayer via email.

Coordination with Other IRS Divisions Auditing the Same Taxpayer

The TEI delegation noted that taxpayers at times undergo simultaneous examinations administered by different IRS divisions (*e.g.*, LB&I for income tax and the SB/SE Division for employment and excise taxes), but frequently there is no coordination among the divisions. This absence of coordination places an extreme burden on taxpayers, which are often forced to respond to overlapping information document requests with short deadlines. TEI inquired as to whether the IRS is doing anything to improve coordination among its different divisions. Ms. Edwards responded that LB&I was aware of the problem, but time constraints and more pressing matters have limited LB&I's consideration of the issue. Ms. Maloy added that she was not aware of any current efforts to improve coordination across IRS divisions and noted further that the divisions' examination plans are separate and processes are different, so such coordination would be difficult.

Revised IDR Process

The TEI delegation requested an update on implementing the revised IDR process, noting that there is confusion in the field about how to apply the process to audits underway when the process changed. Ms. Maloy said that the IDR directives clearly address examiner obligations and if taxpayers are having problems they should elevate the issue. TEI next asked about the status of promised amendments to the Internal Revenue Manual reflecting the IDR process and noted that TEI members are particularly interested in the types of extenuating circumstances that would warrant renegotiating IDR due dates. Ms. Maloy stated that the IRM updates were in progress. The TEI delegation asked whether there had been an increase in summonses issued in connection with the new IDR enforcement procedures. Mr. Wilkins replied that the data showed there had been no increase.

Maximizing Specialists' Resources

TEI's delegation requested an update on the rollout of Issue Practice Groups (IPGs) and International Practice Networks (IPNs). In addition, TEI asked LB&I to explain the process for taxpayers to interact directly with IPG or IPN experts. Mr. O'Donnell responded that LB&I has been publicly releasing international practice units that were designed to train agents on international issues. Mr. Varley added that a new batch of practice units would be finalized following a review process and that public rollout was moving forward steadily. Concerning taxpayer access to IPGs, Ms. Maloy stated that policies are in place and if a taxpayer wants to talk to an IPG official working the taxpayer's case this should be permitted.

FATCA

TEI's delegation referenced the Institute's extensive comments on FATCA guidance since the statute's enactment and noted that many TEI members have foreign affiliates that meet the foreign financial institution (FFI) definition in the Act. TEI's delegation explained a situation where taxpayers may not know whether they satisfy the test for a non-financial group until well into a taxable year because the test is based on financial information for the immediate prior year and asked whether these taxpayers would be afforded a grace or "cure" period to report the FFI. Similarly, a taxpayer may acquire another group of companies that includes an unregistered FFI, which would cause the taxpayer to fail the non-financial group test upon the acquisition. Mr. O'Donnell said that LB&I would look into the possibility of a grace or cure period under those circumstances.

Effects of the OECD's Base Erosion and Profit Shifting initiative (BEPS) on U.S. Tax Enforcement

The TEI delegation expressed its gratitude to U.S. Treasury officials for playing a leading role in the BEPS project and asked if the IRS would provide comments about the problems it foresaw in sharing information contained in the country-by-country reporting template and if it expects to implement the template for U.S. headquartered taxpayers.

Mr. O'Donnell said that the IRS would not have been able to share the country-by-country reporting template upon request, but since the revised information sharing approach is to share the template automatically via an electronic data exchange, similar to FATCA, the IRS should be able to accomplish this. But, he noted, there needs to be universal agreement on what data must be disclosed. Once agreement is reached, the IRS can begin producing forms and publications for taxpayers to provide the information to the IRS. He added that the agreed upon *de minimis* threshold for reporting would substantially reduce the volume of data exchange, which is helpful because the IRS will be a large outbound supplier of the template. Mr. O'Donnell noted that data protection and use are a substantial issue and added that the IRS is working to ensure that template information provided by taxpayers remains confidential. He noted that the IRS will likely use the information in the template for issue spotting, but the IRS already receives high quality information on other forms, and thus, it is likely that the template will be more helpful to other tax authorities than the IRS.

The TEI delegation asked about Action 14 of the BEPS initiative that addresses potential improvements to the MAP process. Mr. O'Donnell said that the IRS has been disappointed that mandatory binding arbitration has not gained traction and will likely be excluded from the final OECD recommendations under Action 14. He also noted that in MAP cases generally the delay in the process is due to the lack of resources in the treaty partner. Frequently, the IRS will be ready to proceed on a MAP case, but must wait until its partner's resources become available to work on the matter.

Transfer Pricing Operations, Including the APMA Program

Status/Progress of the Reorganization of Transfer Pricing Operations (TPO)

The TEI delegation asked for an update on LB&I's TPO and specifically what impact TPO has had on the development of transfer pricing issues and the group's litigation practice and approach. Mr. Varley said that the team had been very impressed with the caliber of people in the

TPO. They continue to face attrition issues, he noted, but the original goals of creating TPO remain and are to provide quality issue and case development and to prepare such cases for litigation if appropriate. He added that in improving issue development, TPO is at the forefront and its approach may be duplicated in other subject matter areas. He noted that it is important for LB&I to improve its track record in transfer pricing litigation. He added that Hareesh Dhawale is now serving as the director of the APMA program and is no longer acting in that role.

Advanced Pricing and Mutual Agreement (APMA) Program

The TEI delegation asked for an update on APA and MAP statistics, including progress reducing case backlog and the average time that APAs and MAP cases are in inventory. Specifically, the TEI delegation inquired whether additional resources would be employed in this area to further decrease backlogs and improve taxpayer services. Mr. O'Donnell responded that TPO is working to remedy reductions in efficiency and noted that U.S. initiated adjustments entering the MAP process had increased, which is a change from prior experience. Mr. Varley added that a sizable portion of case inventory (over 250 cases) involves India and TPO is close to reaching agreement on a framework for moving these cases to resolution. Once these cases are cleared from inventory, TPO hopes to recommence bilateral APAs with India.

Appeals

Update on Appeals Operations

The TEI delegation invited an update on the status of the Appeals Office operations, including overall case volume, case closure rate, and average time-to-closure for Coordinated Industry Cases (CICs) and Industry Cases (ICs).

Ms. Wielobob responded that Appeals had recently seen a decline in new case filings. She added that Appeals has been closing more cases than received for the past couple years. Days to an opening conference for CIC/IC (statistics are now combined) is approximately 144 days, and time to case closure is approximately 794 days for non-docketed CIC cases and 470 for non-docketed IC cases.

Ms. Wielobob reported that as of January 31 Appeals staffing was 1,638 professionals and by fiscal year end staffing was expected to decline to 1,600 due to retirements. She added that these are the lowest staffing levels in recent memory.

The TEI delegation asked about Appeals access to experts, such as engineers, economists, international specialists and other subject matter experts, to work specific cases. Ms. Wielobob said that coordination between Appeals and those experts continues to be difficult in part because of heavy restrictions on travel budgets and staffing reductions. She added that what used to be called Technical Guidance is now split between Domestic Operations (which includes engineers) and International Operations (which includes international specialists, economists, and financial products specialists) within Appeals' Specialty executive area.

Implementation of "Appeals Judicial Approach and Culture"

The TEI delegation asked Ms. Wielobob for an update on the appeals judicial approach and culture initiative (AJAC). Ms. Wielobob reported that implementation of AJAC was proceeding well. A member of TEI's delegation explained a matter involving the member's employer in which an Exam specialist tried to raise a new issue in a case, but the Appeals Team Case Leader did an

excellent job of ensuring only the issues initially raised were addressed by Appeals. Ms. Wielobob agreed that Appeals professionals had effectively implemented the policy against raising new issues and also noted that the AJAC project was completed to the IRS's satisfaction.

Regulatory Guidance Expectations and Strategic Litigation Update

Guidance Expectations

The TEI delegation invited a discussion and update on the areas in which taxpayers can expect guidance in the next few weeks or months and other guidance that may be issued over the course of this year. TEI's delegation also asked how budgetary issues impacted prioritizing guidance. Mr. Wilkins explained that the IRS had been doing a pretty good job of providing guidance in a resource-constrained environment. Challenges include handling attrition, reviewing and gaining final approvals for regulation projects, and working with a smaller staff at the Treasury Department. He said that the Office of Chief Counsel planned to take the opportunity as they develop next year's guidance plan to limit it to projects that will be started in the near term. A member of the TEI delegation asked if the agency planned to issue any guidance concerning rescissions. Mr. Wilkins stated that there had been no change in IRS policy in this area. He explained that the agency conducted a comprehensive review of existing guidance and concluded that it could not publish anything that would improve the guidance for issues that arise in rescissions beyond the current revenue procedure and existing case law.

Strategic Litigation

TEI's delegation asked in what areas/issues the IRS is focusing its strategic litigation program and what impact does the IRS anticipate the OECD's BEPS project having on the process. TEI also inquired about the IRS's hiring of outside counsel to assist the government in its transfer pricing dispute with Microsoft Corporation. Mr. Wilkins replied that hiring outside counsel is more likely to be a unique circumstance, than a regular approach. In this case, the suggestion to hire counsel was made by IRS personnel close to the case. Mr. Wilkins stated that the IRS will continue to monitor the process with a focus on lessons that can be learned and transferred to IRS lawyers handling other cases.

Examination of Large Partnerships

TEI asked about the GAO report regarding difficulties faced by the IRS in examining large partnerships. Ms. Sereti responded that the IRS is currently working on its audit selection process for complex, multi-tiered pass-through entities and is focusing on the partners most impacted by audit adjustments. The agency is also reviewing the TEFRA procedures to see what can be improved. She noted that substantial work has been undertaken in identifying the tax matters partner (TMP) for pass-throughs to ensure that the partner acting as TMP is qualified to do so. This work includes amending the letter distributed to TEFRA partnerships. The agency is also crafting and testing a new IDR for all new examinations of TEFRA partnerships in the Financial Services Industry and the Global High Wealth Industry.

Conclusion

In concluding its inquiries, the TEI delegation asked to what extent is the IRS concerned about losing its most experienced professionals through attrition. Mr. Wilkins responded that most attrition of seasoned professionals results from retirement. Mr. Varley added that the IRS is

focusing on knowledge management so it does not lose the years of experienced compiled by a professional when he or she retires.

On behalf of the TEI delegation, Mr. Silbiger thanked the IRS/LB&I representatives for their attendance and participation in the meeting. Ms. Maloy said that the LB&I office appreciated the dialogue during the meeting.