

Information Document Requests (IDRs)

These IDRs are not mandatory:

- Generic Section 118 Pro-Forma IDR 5/25/07 (46KB):
<http://www.irs.gov/businesses/article/0,,id=174840,00.html>
- Universal Service Support Pro Forma IDR (55KB)
<http://www.irs.gov/businesses/partnerships/article/0,,id=169261,00.html>
- Underground Storage Tank IDR included in IDD #8:
<http://www.irs.gov/businesses/article/0,,id=209361,00.html>

Litigation Update

USF and Section 118: The U.S. District Court for the Southern District of Georgia issued a decision in the erroneous refund suit, United States v. Coastal Utilities, Inc., 514 F. 3d 1184 (11th Cir. 2008), *adopting district courts order*, 483 F. Supp. 2d 1232 (S.D.Ga 2007). The case was appealed and affirmed.

Issue: Whether subsidies received by Coastal Utilities, Inc. from the Federal Universal Service High Cost Support Program and the Georgia Universal Access Fund constitute income under section 61 or capital contributions under Section 118(a). A three-judge panel of the U.S. Court of Appeals for the 11th Circuit affirmed the district court's order and adopted in full its analysis and opinion that Coastal utilities may not exclude federal and state USF payments from income under Section 118.

AT&T, Inc. v. United States of America. (2009 U.S. Dist. LEXIS 38224), 103 A.F.T.R. 2d. (RIA) 2072 (W.D. Tex. 2009). July 16, 2009: District Court for the Western District of Texas adopted the Magistrate Judge's recommendation granting the Government's Motion for Summary Judgment, holding that payments received by AT&T from federal and state universal service programs must be included in income, and did not qualify for exclusion under Section 118 as non-shareholder contributions to capital. On July 21st, AT&T filed a Notice of Appeal to the Fifth Circuit Court of Appeals.

Executing IMT Strategy for Tier I Issues

Audit Teams Should:

- ☐ Establish the Tier I Issue on IMS using the UIL code per the ID Directive.
- ☐ Research the issue on the Tier I website.
- ☐ Communicate with IMT early to determine the strategy and any special requirements for the issue.
- ☐ Consider the issue in the audit planning and risk assessment in accordance with the IMT strategy.
- ☐ Utilize the audit tools and techniques provided by the IMT to develop the issue.
- ☐ Resolve the issue using all resolution tools in alignment with the IMT strategy.

Issue Management Team (IMT)

Issue Executive Owner - Lavena Williams

Issue Champion - Tom Williams, Territory Manager
RFPH

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Tier 1



Tier I



Section 118 Abuse

Includes: Universal Service Fund (USF), State and Local Tax Incentives (SALT), Bioenergy Subsidies, Environmental Remediation and purview of all transactions involving IRC §118 and §362(c).

Quick Reference Guide

October 2010

Issue Owner Executive (IOE)

Lavena Williams, DFO

**Communications, Technology
& Media**

Tier I: Section 118 Abuse Includes USF, SALT, Bioenergy Subsidies, Environmental Remediation and purview of all transactions involving IRC §118 and §362(c).

Issue Description

The Tier I issue, taxable income vs. non-shareholder contributions to capital under Section 118, includes four sub-issues:

1. Universal Service Fund issue (USF) affects telecommunications providers, primarily LECs, and concerns the proper tax treatment of disbursements received from federal and state universal service funds.
2. Tax Incentive issue is a cross industry issue that affects all types of corporations who have received a reduction, abatement, or rebate of state and/or local taxes as an inducement.
3. Bio Energy Program Subsidies issue affects primarily the agricultural industry and concerns the proper tax treatment of increased ethanol production subsidy payments.
4. Environmental Remediation issue affects primarily the petroleum industry but could affect any entity that removes an underground storage tank and then is subsequently reimbursed for their Section 162 currently deductible expenses associated with the tank removal or soil remediation.

Administrative Codes

Universal Service Fund UIL Codes:

- Non Shareholder Contribution to Capital v. Income - 61.40-1
- Basis Adjustment Under Section 362(c) - 118.01-03

Tax Incentive UIL Codes:

- Non Shareholder Contribution to Capital v. Income - 118.01-02
- Basis Adjustment Under Section 362(c) - 118.01-03

Bioenergy Program Payments UIL Codes:

- Non Shareholder Contribution to Capital v. Income Bioenergy 118.01-04
- Basis Adjustment Under Section 362(c) - 118.01-03

Exclusions of Income: Non-corporate Entities and Contributions to Capital UIL Codes:

- Non Shareholder Contribution to Capital v. Income - 118.01-05
- Basis Adjustment Under Section 362(c) - 118.01-03

Industry Director Directives (IDDs)

- **Industry Issue Directive #1** - Section 118 Does Not Apply to Non-Corporate Entities:
<http://www.irs.gov/businesses/partnerships/article/0,,id=165641,00.html>
- **Industry Issue Directive #2** - Provides field direction on a Tier I Issue relating to USF Programs:
<http://www.irs.gov/businesses/partnerships/article/0,,id=169260,00.html>
- **Industry Issue Directive #3** - Non-Corporate Entities and Common Law Arguments:
<http://www.irs.gov/businesses/article/0,,id=174839,00.html>
- **Industry Issue Directive #4** - State and Local Tax Incentives.
<http://www.irs.gov/businesses/article/0,,id=185418,00.html>
- **Industry Issue Directive #5** - Bioenergy Program (BEP) Payments:
<http://www.irs.gov/businesses/article/0,,id=186805,00.html>
- **Industry Issue Directive #6** - USF in Monitoring status:
<http://www.irs.gov/businesses/article/0,,id=204153,00.html>
- **Industry Issue Directive #7** - BEP in Monitoring status:
<http://www.irs.gov/businesses/article/0,,id=209373,00.html>
- **Industry Issue Directive #8** - Provides field direction regarding owners and operators of USTs:
<http://www.irs.gov/businesses/article/0,,id=209361,00.html>

Current Status of Issue

A. **USF:** The 11th Circuit's decision favorable to government on Coastal Utilities. **USF is currently in monitoring status.**

B. **State and local tax incentives:** Coordinated Issue Paper was issued May 28, 2008 and Compliance Initiative Project is in process.

C. **Bioenergy subsidies:** Coordinated Issue Paper issued April 8, 2008. Alternative touch compliance project was completed in November 2008. **BEP is currently in monitoring status.**

D. **Environmental USTs:** Coordinated Issue Paper was issued February 5, 2009.

E. **Exclusion of Income-Non-corporate Entities and Contributions to Capital:** Coordinate Issue Paper was issued November 2008.

Administrative & Technical Guidance

Universal Service Fund

- Revenue Ruling 2007-31 communicates the Service's position in relation to the USF distributions that telephone providers receive from the Universal Service Administration Company in accordance with FCC guidelines. It concludes that USF payments are taxable in accordance with IRC Section 61 and not a non-shareholder capital contribution under IRC Section 118(a). <http://www.irs.gov/pub/irs-drop/r-07-31.pdf>
- **TAM 200332025** - Released August 11, 2003, this TAM concludes that payments received by a taxpayer from Federal and State USF programs do not constitute a contribution to capital under IRC Section 118(a). <http://www.irs.gov/pub/irs-wd/0332025.pdf>
- Coordinated Issue Paper on Universal Service Fund Reimbursements:
http://www.irs.gov/pub/irs-utl/universal_service_fund_final.pdf

State and Local Tax

- Nonrefundable State and Local Tax Incentives (SALT). See Coordinated Issue Paper: <http://www.irs.gov/businesses/article/0,,id=183193,00.html>
⇒ Refundable tax credits: See FAA20085201F dated November 26, 2008 for non-precedential advisory. CIP amendment is under consideration.
<http://www.irs.gov/pub/irs-lafa/085201f.pdf>

Bioenergy Payments Program

- Coordinated Issue Paper on Bioenergy Payments Program:
<http://www.irs.gov/businesses/article/0,,id=181205,00.html>

Environmental Remediation

- Coordinated Issue Paper issued February 5, 2009:
<http://www.irs.gov/businesses/article/0,,id=203968,00.html>

Non Corporate Entities

- Coordinated Issue Paper on Non-corporate entities:
<http://www.irs.gov/businesses/article/0,,id=200263,00.html>