



DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
WASHINGTON, D.C. 20224

TAX EXEMPT AND
GOVERNMENT ENTITIES
DIVISION

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MEMORANDUM FOR: ALL FEDERAL, STATE AND LOCAL GOVERNMENTS (FSLG)
MANAGERS AND EMPLOYEES

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Federal, State and Local Governments Division

SUBJECT: Procedures for Providing IRC 3402(d) Relief During FSLG
Examinations

Purpose

The memorandum establishes procedures to follow when credit is allowed under IRC 3402(d) during an examination. These new procedures supplement existing examination procedures contained in IRM 4.23.10.16.2 and will appear in the next revision of IRM 4.90.12.

Procedural Change

To properly assess either income taxes under IRC 3402, or backup withholding taxes under IRC 3406, together with any applicable penalties and interest, examiners will follow a modified Partial Assessment procedure when penalties are to be assessed.

If the examination does not propose penalties, the partial assessment process is not to be used. The examiner will compute the tax due on Form 4668 or Form 4668-B, based on the net adjustment using the accepted amounts from the secured Forms 4669. The amount on Line 12 of Form 4668, or Line 20 of Form 4668-B will reflect the remaining amount of tax available for abatement after the IRC 3402(d) credit has been allowed during the examination. The Form 4666 and 2504 will also show this net figure. The assessment information and the credits and tax adjustments section of the RCCMS

closing record will also reflect the net adjustments using the accepted amounts from the secured Forms 4669.

Note: Remember that IRC 3402(d) does not apply to the portion of federal income tax that is computed using IRC 3509 rates. If only IRC 3509 rates are used, Form 4668, line 12, "Maximum Tax available for abatement under IRC 3402(d)," should be labeled "NONE."

If penalties are to be assessed, then the modified Partial Assessment process must be used. This is a two-step process which ensures that the gross amount of tax, penalty, and interest are computed and assessed and that the IRC 3402(d) credit is only allowed against this gross amount. The two-step process results in the generation of an initial billing notice for the gross amounts shown on the Form 2504. The taxpayer will subsequently receive a second notice containing the abatements allowed in the examination upon final processing of the Forms 4669 during the closing process.

The examiner should discuss the two-step process with the taxpayer using the statement included on the Form 4666. This should alleviate taxpayer concerns that the Forms 4669 were not properly processed upon receipt of the first notice. See IRM 4.23.10.16.3.

The first step is to create a partial closing record to assess the full tax and penalties as reflected on the Form 2504 (and/or Form 2504-WC if 3509 rates are not used).

In RCCMS, create a Closing Record for the Partial (following the procedures in the RCCMS Case Closing Guide).

On the Closing Record for the Partial, ensure that the "Partial" box is checked.

On the Partial Closing Record, complete only the fields that are necessary for the partial assessment: ARDI code, disposal code, assessment information, and credit and tax adjustments.

All adjustments for the examination, including any other employment tax issues other than the IRC 3402(d) items (fringe benefits, IRC 3509, penalties, etc.), are to be included on the partial closing record. Enter TC 308 (or "300" if not interest free) for the gross tax amount. Enter the appropriate transaction code for the assessment of penalties based upon the gross tax amount. Enter all applicable reference fields for adjustments of all social security and Medicare wages and FICA/income tax/backup withholding taxes that are reflected on Forms 2504 and 2504-WC for the return.

The second step is to create a "full" closing record. The IRC 3402(d) credit and all closing record items will be entered on the "full" closing record.

On the full closing record, the Partial box will not be checked. ARDI and Disposal Code will be entered, as well as Examiner's Time, Technique Code, and Specialist's Name.

The adjustments on the full closing record will reflect only amounts related to the IRC 3402(d) credit-allowed portion. For the transaction code, enter the amount of tax credit allowed based on Forms 4669 allowed in exam as a "309" (or "301" if not interest free) and the corresponding reduction in the income tax withholding or backup withholding in the reference number fields. Other sections to complete include: related return information, principal issues codes, and employment tax/GE (under additional data).

FSLG Specialists should follow the instructions provided in IRM 4.23.10.16.3 to prepare Forms 4666, 4668 and 2504 when IRC 3402(d) applies.

Effect on Other Documents

This guidance supplements procedures contained in IRM 4.23.10.16 and will be incorporated into IRM 4.90.12 no later than May 29, 2013.

Effective Date

This memorandum is effective May 29, 2012.

Contact

If you have any questions, please contact Phyllis Burnside, CPM Manager, at (401) 528-1852.