Compliance Assurance Process (CAP)
Recalibration

Discussion Document
September 28, 2018
CAP Goals Remain Largely Intact – Change is Needed

CAP has an overall objective: Improved service to taxpayers and compliance with tax laws through real time monitoring, review and issue resolution.

With this objective came expectations of significant savings of time in terms of hours spent per tax year by the IRS and reduced duration of months spent on each tax year.

While progress has been made in several areas, hours charged and months spent have been much greater than expected resulting in a program that, on an average return basis, is more resource intensive than normal post-filing examinations of similarly sized taxpayers.
Success of the program is dependent on consistent application of procedures and accountability by taxpayers and IRS in adhering to the program requirements in all phases of the process:

- Admission
- Participation
- Post-Filing Review

Greater discipline is needed by both IRS and taxpayers to ensure adherence to program requirements.
Process Improvements

Management of

**Issue Identification**
- TP Issues List
- Materiality
- Risk Analysis

**Issue Resolution**
- Fast Track
- Transfer Pricing
- Research Credit
- 90 Days

**Streamlined Procedures**
- Pre-Filing
- Opening Conference
- Quarterly Meetings
- Quarterly Review
- Quarterly Risk
- Post Filing

Leveraging:
Time & Issue Monitoring,
Bridge Phase, and Removing Unsuitable Taxpayers
Eligibility Criteria

❖ Current
  ▪ Asset Size ($10 million)
  ▪ Access to Certified Financial Statements (Publicly and Privately Held)
  ▪ Access to Corporate Tax Records
  ▪ Number of Open Filed and Unfiled Returns

❖ Update
  ▪ Exceptions for “claims” and returns that have been reopened, placed in LB&I Suspense or Closed from Group
  ▪ 2020 New applicants must be publicly held C-corporations and
  ▪ All applicants must adhere to the tax control framework requirement

❖ Benefits
  ▪ Simplify and clarify the rules for counting the number of open filed and unfiled returns.
Suitability Criteria

❖ Update: Since the CAP Program is based on the transparent and cooperative interaction between the taxpayer and the IRS, a taxpayer that does not exhibit this type of behavior is not suitable for this Program.

❖ Examples of significant or material failures include:
  ▪ Not adhering to IDR response times or providing incomplete responses to IDRs,
  ▪ Not engaging in meaningful or good faith issue resolution discussions,
  ▪ Failing to thoroughly disclose a material item in a timely manner,
  ▪ Failing to disclose a tax shelter or listed transaction,
  ▪ Failing to disclose an investigation or litigation that limits IRS access to current corporate records,
  ▪ Frequently filing claims or failure to resolve issues in pre and post filing, and
  ▪ Not adhering to any other commitment in the relevant MOU

❖ Benefits: Provides guidance for determining suitability
No new applications accepted for 2019.

We expect to accept new applications for the 2020 CAP year

Application window, 10/1/2018 – 11/30/2018: Extended window for 2019 to allow you additional time to review the changes to the program and compile information before the applications are due. Additional documents are required to be submitted with the application form:

- If the TP has international cross-border activity they are required to complete the Material Inter-Company Transaction Template (MITT) and provide a copy of their Worldwide Tax Organization Chart
  - SME team (TTPO, CBA etc.) will review these documents and assist the CAP team with identifying transfer pricing issues in addition to determining the most efficient way to work, e.g., APA
- If the TP has R&E activities they are required to complete the Research Credit Questionnaire
  - SME team (Engineer, Research Credit Risk Team etc.) will review this document and assist the CAP team with selecting or deselecting research credit issues
- Preliminary Issues List – List of material recurring and non-recurring issues that the taxpayer expects to disclose and be worked in the upcoming tax year
  - Preliminary list will act as the starting point for the joint development of an issues list
Differences Between CAP and Compliance Maintenance

- A key difference between the CAP and Compliance Maintenance Phases is the volume and complexity of the material issues for the taxpayers selected for these phases.
- A taxpayer in the CAP has a history of generally receiving partial acceptance letters and has more issues to be considered.
- A taxpayer in the Compliance Maintenance has a history of generally receiving full acceptance letters and has relatively few issues to be considered.
- The processes and procedures for the Compliance Maintenance Phase are fundamentally the same as the process and procedures for the CAP Phase.
- The expectation is that there is much less time required for the IRS and taxpayers in the Compliance Maintenance Phase.
- We expect all taxpayers to aspire to Compliance Maintenance.
The new Bridge Phase is recognition that compliance risk is very low and expending time by the IRS and taxpayer is not in the best interest of tax administration.

Taxpayers remain in the CAP program

For any year selected for this phase, the team will not accept any disclosure, conduct any review, or provide any assurance.

If the taxpayer has a specific issue that it wants certainty on, the taxpayer may request a pre-filing agreement (PFA) for that issue.

Taxpayers will apply for CAP annually. A taxpayer selected for the Bridge Phase will be considered as a returning taxpayer when applying for CAP the next year.

The length of the bridge is currently limited to one year and may increase in the future.
Issues List

- LB&I will request this Initial Issues List from taxpayers with the CAP application (which the 2019 application period will open Oct. 1 and close Nov. 30th).
- This list is preliminary and expected to be updated throughout the CAP year, subject to established materiality thresholds and the new LB&I add an issue process.
- Taxpayers are still required to provide material Disclosures throughout the CAP year and CAP teams may still identify additional issues as well subject to established materiality thresholds.
- Along with the Issues List and if applicable, we require specific transfer pricing (referenced earlier) and research credit information with the CAP application.
- Our goal is to utilize this information for upfront risk assessment and planning in the areas of transfer pricing and research credit, two issues that continuously provide challenges to both the Service and Taxpayers in a pre-file environment. It will also allow LB&I and Taxpayers to coordinate and collaborate earlier in the CAP year as we work to risk assess and update the Initial Issues List provided with the CAP application prior to the Opening Conference date.
- The Opening Conference is expected to be held by March 31st for calendar year taxpayers or the end of first quarter of the CAP year for fiscal year taxpayers.
Prior to the Opening Conference, LB&I expects to 1) risk out of an issue included on the Issues List, 2) work the issue, or 3) recommend an APA for transfer pricing issues. These decisions are based on the materiality of the issue or transaction (both from a quantitative and qualitative perspective); resource availability and other factors.

An Updated Issues List will be prepared and discussed prior to the Opening Conference. It serves as the starting point for the planning and allocation of resources (e.g., time budget).

Process will be in place to add issues that are identified or disclosed during the CAP year that meet the established materiality threshold guidelines.

The Taxpayer and the Territory Manager must discuss any addition of issues. We expect that Taxpayers will notify the DFO if issues are added without consultation.

This process provides consistency and accountability for both LB&I and Taxpayers. Taxpayers only disclose material items while the IRS only reviews those issues that are strategic, material issues or transactions that we believe as an organization resources should be allocated.
90-Day Target to Develop and Resolve Issue

- **Current**
  - No standard target to develop and resolve issue

- **Update**
  - Establish a target for timely disclosure of issues. Additional details to be provided as available.
  - Establish a target for all disclosures to be completed by 90 days from the close of the tax year
  - Establish a target of 90 days, from the date the taxpayer has provided all relevant information including the planned tax position, to work and resolve the issue
  - Taxpayer to notify team when all of the relevant information has been provided, taxpayer and team must agree
  - Exception process - Territory Manager approval required to extend the 90 days
  - The LB&I case management system, IMS, will be modified so the date starting the 90 days will be captured.

- **Benefits**
  - Provides consistent target to develop and resolve issues
Mandatory Fast Track (Pilot Process)

- **Current**
  - Fast Track is encouraged but not required

- **Update**
  - If issue is not resolved within 90 days of when all the relevant information has been received, an application to Fast Track will usually be submitted
  - If offered to taxpayer, the Fast Track process must be used
  - Taxpayers retain access to Appeals in the normal course if Fast Track does not result in an agreement

- **Benefits**
  - Will encourage issue resolution in the pre-filing time period
Within 30 days of the date the return is filed, the taxpayer will provide a Post-Filing Representation Letter executed by an officer of the taxpayer with authority to sign the return that includes:

- A statement from the taxpayer that all the material issues were disclosed and resolved as of the date that the return was filed or a full description of all the material issues that were not disclosed or resolved as of the date that the return was filed;

- A statement from the taxpayer that all the resolved issues were reported as agreed as of the date that the return was filed or a full description of all the resolved issues that were not reported as agreed as of the date that the return was filed; and

- A declaration under penalties of perjury that the representations in the letter are true, correct, and complete.
Partial and Full Acceptance Letters will not be provided until after the return is filed and the Post-Filing Representation Letter is received and reviewed.

After the receipt and review of the Post-Filing Representation Letter, the IRS determines that the taxpayer has fully complied with the terms of the MOU and all material issues have been disclosed and resolved through simple factual clarification, issue resolution agreement, or closing agreement, the IRS will timely provide the taxpayer with a Full Acceptance Letter.

If, after the receipt and review of the Post-Filing Representation Letter, the IRS determines that the taxpayer did not disclose all material issues or that the IRS and the taxpayer cannot resolve all identified material issues, the IRS will timely provide the taxpayer with a Partial Acceptance Letter.
After a taxpayer files its return, the Account Coordinator will secure a copy of the return and initiate the post-filing review. The goal for completing this review is within 60 days of the filing of the return.

During the post-filing review, the IRS and the taxpayer will jointly review the filed return to verify that all material issues were disclosed and resolved and that all resolved issues were reported as agreed.

- If the review verifies that all material issues were disclosed and resolved and that all resolved issues were reported as agreed, the IRS will issue a No Change Letter concluding the examination of the taxpayer's books for purposes of IRC § 7605(b).

- If there are material issues that were not disclosed and resolved or there are resolved issues that were not reported as agreed, the IRS may examine any such issues through the post-filing examination process.
Future Program Changes

- Consistent with the overall goals of CAP, eligibility requirements will include limits on the number of open filed and unfiled returns.
- In the future, the program will be open to additional taxpayers who meet eligibility criteria and program requirements.
- For future years, taxpayers will be required to provide certification of a tax control framework. Additional details will be shared as available.
- Consistent with LB&I’s strategic vision, and mindful of resource constraints, LB&I is considering whether issue-based resolutions and assurance may be appropriate as the program is expanded.
- As taxpayers and LB&I gain experience with the 2019 changes, modifications will be made as appropriate.
Next Steps

- Initial Training of employees – September 2018
- Internal weekly calls with CAP teams – beginning October 2018
- Additional internal Training – starting February 2019
- Stakeholder input – from both employees and taxpayers – will be essential as we move forward.
- LB&I will monitor the operation of all changes and remain open to improvement as we move forward.
- CAP taxpayers may elevate concerns through the Account Coordinator or submit feedback or comments to: lbi.irs.cap.program@irs.gov