

CHAPTER 17

**OBTAINING PRIVATE GUIDANCE  
FROM  
THE INTERNAL REVENUE  
SERVICE**

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## ¶ 1700 FORWARD

In 1962, Commissioner of Internal Revenue Mortimer Caplin, in an article dealing with the private letter ruling program of the Internal Revenue Service (IRS), wrote:

With complex tax laws and high tax rates, it is understandable why taxpayers frequently hesitate to move on

important business transactions without some official assurances of the tax consequences.<sup>2</sup>

In 1962, John F. Kennedy was President of the United States, the world's attention was riveted by the Cuban missile crisis, the Vietnam war was a small-scale military skirmish in the backwaters of southeast Asia, and construction was about to begin on the Watergate complex on the banks of the Potomac river in Washington, D.C.

As for complexity in the tax law, in 1962, the first reverse triangular merger was three years away, today's complex original issue discount rules were two decades away, the consolidated return regulations covered 47 pages in the CCH paperback edition (as opposed to 354 pages in the 2001 edition), and the word "derivative", if used in the context of corporate finance (or taxation), would have drawn blank stares.

Despite recurring calls for (and promises of) "tax simplification", the trend inevitably seems to be in the other direction. Accordingly, it seems likely that IRS programs for providing private guidance to taxpayers will continue to play an important part in the administration of the tax laws. The private letter ruling program, having survived two major (and a multitude of minor) IRS restructurings, is now in its seventh decade and will undoubtedly continue to play a significant role in assisting taxpayers and their advisors in coping with the complexity of the tax system. New avenues for providing guidance, such as the pre-filing agreement program announced in 2000 by the new Large and Mid-Size Business Division, discussed below, provide additional tools for taxpayers and the IRS in their efforts to ensure compliance with intricate and comprehensive tax laws.

This article deals with the nuts and bolts of the private letter ruling program and the new pre-filing agreement program. It includes something for everyone, from those who devote a large part of their practice to such requests to those

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<sup>2</sup> Caplin, *Taxpayer Rulings Policy of the Internal Revenue Service: A Statement of Principles*, 20 N.Y.U. Tax Inst. 1 (1962).

who have never made a submission and want a comprehensive guide. It provides an inside look at the history and development of the private letter ruling and pre-filing programs, and describes how to determine which program to choose. It also walks the reader step by step through the details of each program, highlighting potential pitfalls and providing practical hints.

## ¶ 1701 BACKGROUND

Private letter rulings, with one major exception, are issued by the Office of the Chief Counsel. Pre-filing agreements, on the other hand, are issued by the new Large and Mid-Size Business Division on what many refer to as “the Commissioner’s side of the house.” As a preliminary matter, it is important to understand the current organization of the IRS (including the Office of Chief Counsel).

As a result of the IRS Restructuring and Reform Act of 1998,<sup>3</sup> the IRS in the last two years has undergone its first major, top-to-bottom reorganization in almost 50 years. Virtually every major function of the IRS, including the Office of the Chief Counsel (“Chief Counsel” or “Counsel”), has been affected by this reorganization.

Under its new organizational structure, the IRS includes four operating divisions, each responsible for serving the needs of a specified group of taxpayers. These new operating divisions are:

- The Large and Mid-Size Business Division (LMSB), which generally serves corporations, S corporations, and partnerships with assets in excess of \$10 million;
- The Small Business/Self-Employed Division (SB/SE), which generally serves (1) corporations, S corporations and partnerships with assets less than or equal to \$10 million, (2) estates and trusts, (3) individuals filing an individual federal income tax return with accompanying Schedule C (Profit or Loss from Business (Sole Proprietorship)), Schedule E (Supplemental Income

<sup>3</sup> Pub. L. No. 105-206 (1998).

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and Loss), Schedule F (Profit or Loss from Farming), Form 2106 (Employee Business Expenses), or Form 2106-EZ (Unreimbursed Employee Business Expenses), and (4) individuals with international tax returns;

- The Wage and Investment Division (W&I), which generally serves individuals with wage and investment income only (and with no international returns) filing an individual federal income tax return without accompanying Schedule C, E, or F, Form 2106 or 2106-EZ; and
- The Tax Exempt and Government Entities Division (TE/GE), which serves three distinct taxpayer segments; employee plans, exempt organizations, and government entities.

In general, the field operations of the Chief Counsel's office have been realigned to correspond to the new operating divisions. Thus, for example, the LMSB is served by a counterpart LMSB organization in Chief Counsel headed by a Division Counsel.

The National Office functions of Chief Counsel, although not directly affected by the overall IRS restructuring, have also been significantly restructured in the last two years. One of the principal changes is that the office of the Associate Chief Counsel (Domestic) no longer exists and the Assistant Chief Counsel offices within that office have been elevated to the status of Associate Chief Counsel. Thus, for example, the former office of the Assistant Chief Counsel (Corporate) is now the Office of the Associate Chief Counsel (Corporate). In addition, the field service functions formerly located in the Office of the Assistant Chief Counsel (Field Service) have been relocated to the appropriate Associate Chief Counsel offices.

Despite the massive scope of this restructuring, the private letter program has been relatively unaffected. Those organizations that issued private letter rulings prior to the reorganization are the same organizations that currently issue private

letter rulings, albeit with, in some cases, slightly different organizational titles. On the other hand, the pre-filing agreement program is a specific initiative of the new LMSB, which was created by the restructuring.

## ¶ 1702 THE PRIVATE LETTER RULING PROGRAM

The IRS has been issuing guidance to taxpayers concerning the tax effects of proposed transactions for more than 60 years. This guidance is provided in the form of a private letter ruling (PLR).

For many tax attorneys, accountants, and other tax professionals (*e.g.*, members of corporate tax departments), the preparation and submission of requests for PLRs is an everyday occurrence. For others, it may happen once in a lifetime or sporadically at best. This article is designed to provide all readers with a basic understanding of the history and current status of the PLR program and a guided tour through the details of the process.<sup>4</sup>

The first Internal Revenue Bulletin (I.R.B.) published by the IRS each year (*e.g.*, I.R.B. 2002-1) contains revenue procedures that revise, update and restate the procedures for obtaining PLRs from the IRS.<sup>5</sup> The practices and procedures relating to the PLR program generally do not change dramatically from year to year. However, the careful practitioner will always review the most recently published IRS guidance before submitting a request for a PLR. The first I.R.B. of the year should always be the starting point for any practitioner seeking a PLR.

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<sup>4</sup> For a somewhat dated, but still extremely useful discussion by a former IRS Chief Counsel of many of the topics discussed in this article, see Rogovin, *The Four R's: Regulations, Rulings, Reliance, and Retroactivity — a View from Within*, 43 *Taxes* 756 (1965). See also Osteen, *supra* note 1.

<sup>5</sup> The I.R.B. is published weekly and is the instrument of the Commissioner for announcing official rulings and procedures of the IRS and for published Treasury Decisions, Executive Order, Tax Conventions, legislation, court decisions and other items of general interest. Items published in the I.R.B. that are of a permanent nature are consolidated semi-annually into Cumulative Bulletins.

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## ¶ 1703 TYPES OF GUIDANCE ISSUED BY THE IRS

### ¶ 1703.1 In General

Although this portion of the article is concerned with the PLR program, it is helpful as background to understand generally where PLRs fit in the overall scheme of legal guidance provided to taxpayers by the Treasury Department and the IRS.

### ¶ 1703.2 Regulations

Treasury Regulations are the highest form of guidance issued under the tax laws. Courts generally give Treasury Regulations a great deal of deference in interpretative matters.<sup>6</sup> Regulations are prepared cooperatively by the IRS and Office of Tax Policy of the Treasury Department and are signed by both the Commissioner and the Assistant Secretary of the Treasury for Tax Policy. Within the IRS, attorneys in the National Office of Chief Counsel are responsible for participating in the initial preparation and review of draft regulations. In exercising this responsibility, Counsel coordinates with and receives comments from all affected functions within the IRS (e.g., the LMSB and LMSB Division Counsel).

### ¶ 1703.3 Revenue Rulings

A revenue ruling is an interpretation of the tax laws by the IRS that is published in the I.R.B. and reproduced in the Cumulative Bulletin (C.B.). Revenue rulings represent the conclusions of the IRS on how the law is applied to a specific set of facts.<sup>7</sup>

Revenue rulings, unilaterally issued by the [IRS], do not rise to the dignity of those rules and regulations' which under the authority of Section 7805(a)<sup>8</sup> are prescribed by

<sup>6</sup> See *Comm'r v. Estate of Noel*, 380 U.S. 678 (1965).

<sup>7</sup> Rev. Proc. 2002-1, 2002-1 I.R.B. 1, § 2.05.

<sup>8</sup> Unless otherwise indicated, all "Section" references are to the Internal Revenue Code of 1986, as amended, and all "Treas. Reg. Section" references are to the regulations thereunder.



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[the IRS] with the approval of the Secretary'.<sup>9</sup>

Until revoked, modified or clarified, revenue rulings are binding upon the IRS (i.e., they can be relied on by taxpayers), but are not binding upon the courts or taxpayers.<sup>10</sup> However, taxpayers, IRS personnel, and other concerned parties should always consider the effect of subsequent changes in the statute, regulations, court decisions, revenue rulings, notices and announcements.<sup>11</sup>

Because revenue rulings represent the position of the IRS on a specific issue, taking a position contrary to a position contained in a revenue ruling is an invitation to litigation. Occasionally, an issue raised in a request for a PLR will subsequently be addressed in a published revenue ruling.

#### ¶ 1703.4 PLRs

A PLR is a written statement issued to a taxpayer by the National Office that interprets and applies the tax laws to that taxpayer's specific set of facts.<sup>12</sup> PLRs are often referred to as letter rulings, private rulings, or advance rulings.

#### ¶ 1703.5 Determination Letters

A determination letter is a written statement issued by a director that applies principles and precedents previously announced by the IRS National Office to a particular set of facts.<sup>13</sup> In general, for purposes of Revenue Procedure 2002-1, the term "director" is defined to include directors in the various divisions of the IRS (e.g., the Director, Field Operations, LMSB).<sup>14</sup>

A determination letter is issued only when a determination can be made on the basis of clearly established rules in the statute, a tax treaty, or the regulations, or by a revenue

<sup>9</sup> *Estate of Lang v. Comm'r*, 64 T.C. 404, 407 n.4 (1975).

<sup>10</sup> *Minnis v. Comm'r*, 71 T.C. 1049 (1979).

<sup>11</sup> Rev. Proc. 2002-1, 2002-1 I.R.B. 1, § 2.05.

<sup>12</sup> *Id.* § 2.01.

<sup>13</sup> *Id.* § 2.03.

<sup>14</sup> *Id.* § 1.

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ruling, opinion, or court decision published in the I.R.B. that specifically answers the questions presented. In situations where a director is likely to issue a determination letter, there may be little need to go to the expense and time involved in obtaining it. Another alternative, such as a well-reasoned opinion of counsel, may be an acceptable substitute.

#### ¶ 1703.6 Information Letters

An information letter is a statement issued either by the National Office or by a director that calls attention to a well-established interpretation or principle of law (including a tax treaty) without applying it to a specific set of facts.<sup>15</sup> For example, an information letter may be issued when a taxpayer is seeking general information or when a PLR request does not meet all the requirements of Revenue Procedure 2002-1 for obtaining a PLR or determination letter. As a practical matter, information letters are not generally requested because they have no binding effect and rarely go beyond what is stated in published guidance. The primary advantages of an information request is that no user fee is required and they may receive a rapid response.

Notwithstanding the above, no penalty or interest may be imposed if a taxpayer relies on written advice from the IRS and the penalty or interest is not the result of the taxpayer's failure to provide adequate or accurate information.<sup>16</sup>

#### ¶ 1703.7 Technical Advice Memoranda

A technical advice memorandum (TAM) is furnished by the National Office upon the request of a director or an area director, appeals, in response to a technical or procedural question that develops during any proceeding regarding 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. The procedures for requesting a TAM with respect to issues under the jurisdiction of the various offices in Chief Counsel are set

<sup>15</sup> *Id.* § 2.04.

<sup>16</sup> I.R.C. § 6404(f).

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forth in the first I.R.B. published each year.<sup>17</sup> The procedures for requesting technical advice from the office of Commissioner TE/GE are also published annually in the first I.R.B.<sup>18</sup>

A TAM is prepared by the National Office in much the same manner as a PLR. As noted above, the procedures for requesting technical advice are set forth in detail in Revenue Procedures 2002-2<sup>19</sup> and 2002-5.<sup>20</sup>

Situations in which a request for a TAM may be appropriate include an examination of a taxpayer's return, consideration of a taxpayer's claim for refund or credit, any matter under examination or in appeals pertaining to tax-exempt bonds or mortgage credit certificates, and any other matter involving a specific taxpayer under the jurisdiction of a director or the processing and consideration of a nondocketed case under the jurisdiction of an area director, appeals.

Except in rare or unusual circumstances, the holding in a TAM that is favorable to a taxpayer is applied retroactively.<sup>21</sup> Moreover, because TAMs are issued only with respect to closed transactions, their holdings, if adverse to the taxpayer, are also applied retroactively, unless the appropriate office exercises the discretionary authority under I.R.C. Section 7805(b) to limit the retroactive effect of the holding.<sup>22</sup>

A director or area director, appeals, initiates requests for TAMs, but a taxpayer may ask that the request be submitted.<sup>23</sup>

If a TAM adverse to the taxpayer is issued, it prevents the taxpayer from obtaining a favorable settlement on the issue at the director level and reduces the opportunity for a favorable settlement at the area director, appeals, level.

<sup>17</sup> Rev. Proc. 2002-2, 2002-2 I.R.B. 82.

<sup>18</sup> Rev. Proc. 2002-5, 2002-1 I.R.B. 173.

<sup>19</sup> 2002-2 I.R.B. 82.

<sup>20</sup> 2002-1 I.R.B. 173.

<sup>21</sup> Rev. Proc. 2002-2, 2002-2 I.R.B. 82, § 17.02.

<sup>22</sup> See, e.g., Rev. Proc. 2002-2, 2002-2 I.R.B. 82, § 18.02.

<sup>23</sup> *Id.* § 6.02.

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### ¶ 1703.8 Closing Agreements

A closing agreement is an agreement between the IRS and the taxpayer on a specific issue. Closing agreements are entered into under the authority of I.R.C. Section 7121. Closing agreements are final unless there is fraud, malfeasance or misrepresentation of a material fact.<sup>24</sup>

A closing agreement is a contract between the taxpayer and the IRS settling issues permanently and conclusively. There is no appeal or further modification of the agreement. In some instances, the IRS may require a closing agreement as a condition to the issuance of a PLR. If more than twenty-five taxpayers are involved in the specific settlement of a matter, the IRS will enter into a “mass closing agreement” with the taxpayer who is authorized by the other taxpayers involved to represent the entire group.<sup>25</sup> In addition, closing agreements may be used in resolving tax liability arising out of the examination of a tax return. Such agreements are final in nature.

### ¶ 1703.9 Announcements

Announcements are used by the IRS to give a “plain language” summary of the law, generally without substantive interpretation. Announcements may also be used to announce what regulations will say when regulations are certain to be published in the immediate future. They may also be used to notify taxpayers of an approaching deadline for exercising an election. Although published in the I.R.B., announcements are not reproduced in the C.B.. Announcements that contain substantive or procedural guidance constitute “authority” for purposes of I.R.C. Section 6662 and may be relied upon by taxpayers.<sup>26</sup>

### ¶ 1703.10 Notices

Notices are published guidance from the IRS that involve substantive interpretation of the Code or other provisions of

<sup>24</sup> Rev. Proc. 2002-1, 2002-1 I.R.B. 1, § 2.02.

<sup>25</sup> *Id.* § 2.02.

<sup>26</sup> Treas. Reg. § 1.6662-4(d)(3)(iii).

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the tax law. They are initially published in the I.R.B. and are preserved in the C.B. Lengthy documents that address a large number of issues may be more effectively published as notices, rather than as revenue rulings.

Notices may be used for the type of material that would be appropriate for an announcement, but for the need to preserve the guidance in the C.B., e.g., guidance as to what regulations will say when the regulations may not be published in the near future. Notices that contain substantive or procedural guidance are authority for purposes of I.R.C. Section 6662 and may be relied upon by taxpayers.<sup>27</sup>

#### ¶ 1703.11 News Releases

A news release is a nontechnical document targeted at the nonpractitioner taxpaying public. News releases are issued by the Communications Division of the IRS.

### ¶ 1704 THE HISTORY OF THE PLR PROGRAM

#### ¶ 1704.1 1913 — 1919

In 1913, the IRS, then known as the Bureau of Internal Revenue, unofficially adopted a policy of “answering all legitimate and proper questions.”<sup>28</sup> Answers were not limited to completed transactions, but were given on prospective transactions and hypothetical questions as well. However, the IRS was not bound by the information it provided.

#### ¶ 1704.2 1919 — 1935

In 1919, the IRS formally limited rulings to completed transactions and required a full statement of facts and the names of all interested parties.<sup>29</sup> This was the first statement published by the IRS concerning its ruling policy.

<sup>27</sup> *Id.*

<sup>28</sup> See Caplin, *supra* note 2.

<sup>29</sup> Comm’r’s Mimeographed Published Opinion (Mim.) 2228, 1 C.B. 310 (1919).

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**¶ 1704.3 1935 — 1938**

In 1935, the IRS reiterated its policy of not issuing rulings with respect to prospective transactions, noting that such rulings would only be issued when required by law (e.g., under the provisions of Section 112(i) of the Revenue Act of 1934, the predecessor of I.R.C. Section 367).<sup>30</sup>

**¶ 1704.4 1938 — 1940**

In 1938, the pendulum began to swing when Congress enacted legislation giving the Commissioner discretionary authority to enter into formal closing agreements with respect to proposed transactions, which discretion was to be used “only where such exercise is in the interest of a wise administration of the revenue system.”<sup>31</sup> In 1939, the IRS revised its procedures to reflect this expanded authority with respect to closing agreements.<sup>32</sup>

**¶ 1704.5 1940 — 1954**

Within two years, it became clear that the closing agreement arrangement was not effective as a mechanism for providing timely guidance with respect to proposed transactions. Accordingly, the IRS in 1940 informally liberalized its interpretation of Mim. 4963 and began to treat each ruling request as a potential request to enter into a formal closing agreement without requiring that the taxpayer actually enter into a closing agreement.<sup>33</sup> This marked the beginning of the PLR process as it exists today.

Despite an internal proposal in 1946 to return to the old policy of ruling only on completed transactions,<sup>34</sup> the informal (and unpublished) procedure established in 1940 continued throughout the 1940’s and into the 1950’s. Finally, in 1953, the IRS for the first time publicly referred to its practice of

<sup>30</sup> Mim. 4369, XIV-2 C.B. 592 (1935).

<sup>31</sup> H.R. Rep. No. 1860, 75<sup>th</sup> Cong., 3<sup>rd</sup> Sess. 67, reprinted in 1939-1 (Part 2) C.B. 728, 777.

<sup>32</sup> Mim. 4963, 1939-2 C.B. 459.

<sup>33</sup> Caplin, *supra* note 2, at 5.

<sup>34</sup> *Id.*

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issuing rulings on prospective transactions without the necessity of a closing agreement.<sup>35</sup>

**¶ 1704.6 1954 — 2002**

In 1954, the IRS issued the first detailed public guidance concerning the PLR process in Revenue Ruling 54-172.<sup>36</sup> A key provision of the revenue ruling was the following sentence relating to the ability of taxpayers to rely on PLRs:

[I]t is the general policy of the Internal Revenue Service to limit the revocation or modification of a ruling issued to or with respect to a particular taxpayer to a prospective application only, (a) if there has been no misstatement or omission of material facts, (b) the facts subsequently developed are not materially different from the facts on which the ruling was based, (c) there has been no change in the applicable law, and (d) such taxpayer acted in good faith in reliance upon such ruling and a retroactive revocation would be to his detriment.

This general policy of allowing taxpayers to rely upon PLRs is the foundation of the PLR process. Without it, PLRs would not be worth the paper they are written on.

Until the mid-1970's, PLRs were just that, private. That is, they were issued to particular taxpayers and were not published or otherwise made available to the public. In 1952, there was a movement in Congress to require that the IRS make public all rulings issued to taxpayers. Instead, the IRS made a commitment to publish (in the I.R.B.) all communications to taxpayers and field offices involving substantive questions and procedures affecting the rights and duties of taxpayers.<sup>37</sup> Details of this program were published by the IRS in Revenue Ruling 2.<sup>38</sup>

<sup>35</sup> Rev. Rul. 10, 1953-1 C.B. 488.

<sup>36</sup> 1954-1 C.B. 394.

<sup>37</sup> See Portney, *Letter Rulings: An Endangered Species?*, 36 Tax Law. 751, 752 (1983).

<sup>38</sup> 1953-1 C.B. 484.

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In the mid-1970's, the IRS lost two freedom of information cases seeking disclosure of PLRs and TAMs.<sup>39</sup> Shortly thereafter, as part of the Tax Reform Act of 1976, Congress enacted I.R.C. Section 6110, setting forth rules applicable to the public inspection of PLRs, determination letters and TAMs. Since 1977, the IRS has released PLRs and TAMs approximately three months after they are issued, deleting any information that would serve to identify the taxpayer with respect to whom the PLR or TAM was issued.

During the 1980's, the IRS adopted in some areas a policy of not issuing so-called “comfort rulings”, that is, rulings with respect to issues that are clearly and adequately addressed by published authorities. These are discussed below in ¶ 1708.

## ¶ 1705 THE EFFECT OF PLRS

### ¶ 1705.1 In General

Except to the extent incorporated in a closing agreement, PLRs may be modified or revoked if found to be in error.<sup>40</sup> However, except in rare or unusual circumstances, the IRS will not apply the revocation of a PLR retroactively if certain conditions are met.<sup>41</sup> The principal condition for avoiding retroactive revocation is that there must have been no misstatement or omission of material facts. Assuming that all the conditions in Section 12.05 of Revenue Procedure 2002-1<sup>42</sup> are met, a taxpayer who completes a transaction in reliance on a PLR will be protected by it.

If a ruling relates to a continuing action or series of actions, the IRS will ordinarily limit the retroactivity of revocation or modification of that ruling to a date that is not earlier than the date on which the ruling is revoked or modified.<sup>43</sup>

<sup>39</sup> *Tax Advocates & Analysts v. I.R.S.*, 505 F.2d 350 (D.C. Cir. 1974) and *Fruehauf Corp. v. I.R.S.*, 522 F.2d 284 (6<sup>th</sup> Cir. 1975).

<sup>40</sup> Rev. Proc. 2002-1, 2002-1 I.R.B. 1, § 12.04.

<sup>41</sup> *Id.* § 12.05.

<sup>42</sup> *Id.*

<sup>43</sup> *Id.* § 12.07.



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**¶ 1705.2 PLRs as Precedent**

I.R.C. Section 6110(j)(3) provides that PLRs, determination letters and TAMs may not be used or cited as precedent. Accordingly, PLRs and TAMs contain the following admonishment:

This ruling is directed only to the taxpayer who requested it. Section 6110(j)(3) provides that it may not be used or cited as precedent.

A useful, and often overlooked, distinction is the difference between “published” guidance and “released” guidance. Although PLRS (and TAMs and other forms of informal guidance) are released to the tax services and reported in the tax press (see ¶ 1704.6, *supra*), they do not constitute “published guidance.” This distinction is clearly set forth in the introduction to each issue of the I.R.B., which provides as follows:

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, *but they may be relied upon as precedent. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases.* [Emphasis added]

The debate over whether or not PLRs and TAMs should be treated as precedent has been lively over the years.<sup>44</sup> Because PLRs and TAMs are in the public domain, there is undoubtedly a tendency on the part of tax practitioners to view them, if not as precedent, at least as strong evidence of the IRS’s thoughts on a given issue. On the other hand, those who argue that PLRs and TAMs should be accorded formal status as precedent do so at their peril. Although PLRs that raise important new issues may be subjected to review at higher levels, most PLRs are currently issued at the “Branch” level within the appropriate Chief Counsel office. If PLRs and TAMs were treated as precedent, and thus binding on the IRS in cases other than the one involving the taxpayer requesting

<sup>44</sup> Compare Portney, *supra* note 37, with Holden & Novey, *Legitimate Uses of Letter Rulings Issued to Other Taxpayers — A Reply to Gerald Portney*, 37 Tax Law. 337 (1984).

the PLR, the IRS would be forced to subject each PLR to much higher levels of review, up to and including review by the Treasury Department. As a result, the time needed to process each PLR would inevitably increase significantly. Because time is of the essence in most of today's complex transactions, the additional review time required to process a "precedential" PLR might well increase the overall processing time to the point where the PLR, when issued, would be of little use to the taxpayer because time constraints would have forced the parties to either proceed with the transaction without the PLR or abandon it altogether. It is probably not an overstatement to conclude that according precedential status to PLRs would significantly cripple, or perhaps even kill, the program. In this situation, the old admonition to "be careful what you wish for" (because you might get it) undoubtedly applies. Considering all sides of the debate, the present situation (with PLRs published, but not to be used as precedent) will likely continue in the future.

In *Rowan Companies v. U.S.*,<sup>45</sup> the Supreme Court cited PLRs to illustrate inconsistent application of the law rather than as precedent. More recently, the Sixth Circuit noted that, in the absence of regulations on point, a PLR may be viewed as evidence of the IRS's treatment of tuition remissions.<sup>46</sup> A U.S. District Court has also ruled that PLRs "reflect the IRS's position concerning the application of the I.R.C. to fact specific situations."<sup>47</sup>

### ¶ 1705.3 PLRs as Substantial Authority

PLRs and TAMs issued after October 31, 1976, are treated as authority for purposes of the substantial understatement penalty found in I.R.C. Section 6662.<sup>48</sup> However, the fact that PLRs constitute authority for purposes of the penalty provisions in no way alters the fact that they may not be relied upon by taxpayers as precedent for positions taken.

<sup>45</sup> 452 U.S. 247, 261 n.17 (1981).

<sup>46</sup> *Wolpaw v. Comm'r*, 47 F.3d 787 (6<sup>th</sup> Cir. 1995).

<sup>47</sup> *Merchant v. Haglund, Garnsev & Kahn*, 874 F. Supp. 300 (D. Colo. 1995).

<sup>48</sup> Treas. Reg. § 1.6662-4(d)(3)(iii).

**¶ 1705.4 Adverse PLRs**

Because a PLR represents only the IRS's interpretation of the tax laws as they relate to the taxpayer's specific set of facts, the recipient of an adverse ruling is entitled to disregard it. As a practical matter, taxpayers withdraw their requests for rulings in virtually all situations in which the IRS indicates that an adverse ruling will be issued.

**¶ 1706 FIXING THE "BROKEN TRANSACTION"**

Although often overlooked, one of the most significant benefits of the PLR program is the fact that the IRS, in effect, conducts a pre-transaction audit. During the processing of a PLR request, IRS personnel may identify one or more aspects of the proposed transaction that might lead to problems if not corrected.

For example, in processing a request for rulings under I.R.C. Section 368(a)(1)(B), which contains a "solely for voting stock" requirement, the IRS might identify some aspect of the transaction that could be construed as providing consideration other than voting stock, thus disqualifying the transaction as a "Type B" reorganization. In many cases, such transactional problems can be "fixed" without significantly altering the underlying transaction. Thus, a transaction that might have resulted in disastrous consequences on audit is transformed into a transaction with advance approval by the IRS. On the other hand, if the problem cannot be fixed, the practitioner is at least on notice and may wish to consider other alternatives to achieve the client's goals.

**¶ 1707 OFFICES WITHIN THE IRS THAT ISSUE PLRS**

Historically, the offices that issued PLRs and TAMs and drafted revenue rulings and revenue procedures were not considered to be "legal divisions", and were located on the Commissioner's "side of the house." The Chief Counsel's Office, through the Interpretative Division, rendered legal opinions on issues (in the form of General Counsel Memoranda ("GCMs")) to the rulings divisions at its request. The

other “technical” division in Chief Counsel, the Legislation and Regulations Division, was responsible primarily for the legislative activities of the Chief Counsel’s Office and for the preparation (in conjunction with the Treasury Department) of regulations.

Prior to 1974, the Office of the Assistant Commissioner (Technical), through several Divisions, was responsible for the issuance of all PLRs and TAMs and for the publication of revenue rulings and revenue procedures. In 1974, the Office of the Assistant Commissioner for Employee Plans and Exempt Organizations (EP/EO) was created pursuant to the Employee Retirement Income Security Act (ERISA). This office had jurisdiction for ruling matters involving pension trusts and the status of exempt organizations. The remaining ruling matter areas were under the jurisdiction of the Corporation Tax and Individual Tax Divisions of the Office of the Assistant Commissioner (Technical).

In 1978, the “legal” functions (GCMs, legislation, and regulations) that corresponded jurisdictionally to the Office of the Assistant Commissioner (EP/EO) were shifted within the Chief Counsel’s Office to the newly created EP/EO Division.

In 1982, the Office of the Assistant Commissioner (Technical) was abolished and the Corporation Tax and Individual Tax Divisions were transferred to the Chief Counsel’s Office and placed under the supervision of the Associate Chief Counsel (Technical), who also continued to supervise the Interpretative, Legislation and Regulations and EP/EO Divisions.

In 1986, the Office of the Associate Chief Counsel (International) was created within the Chief Counsel’s Office to bring together in one organization all technical (e.g., legislation and regulations, PLRs, TAMs, and published revenue rulings and revenue procedures) and litigation functions involving international tax provisions.

In 1988, the Office of the Associate Chief Counsel (Technical) was reorganized to reflect the “functionally integrated” concept. In addition to the renamed EP/EO, four new offices

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were created, each of which was responsible for all functions within its substantive area. Each of the new offices was headed by an Assistant Chief Counsel. These four new offices were:

- Assistant Chief Counsel (Corporate)
- Assistant Chief Counsel (Financial Institutions and Products)
- Assistant Chief Counsel (Passthroughs and Special Industries)
- Assistant Chief Counsel (Income Tax and Accounting)

Because their functions had been integrated into the new organizations, the Interpretative, Legislation and Regulations, Corporation Tax and Individual Tax Divisions were abolished.

In 1991, the Office of the Assistant Chief Counsel (EB/EO) was removed from the Office of the Associate Chief Counsel (Technical) and elevated to the status of Associate Chief Counsel. At the same time, the Office of the Associate Chief Counsel (Technical) was renamed the Office of the Associate Chief Counsel (Domestic).

In 2000, the office of the Associate Chief Counsel (Domestic) was abolished and the Assistant Chief Counsel offices within that office were elevated to the status of Associate Chief Counsel offices. Other changes that occurred as part of the 2000 reorganization included the integration of the subject matter branches of the Assistant Chief Counsel (Field Service) into their respective technical offices and the establishment of a new office of the Associate Chief Counsel (Procedure and Administration).

In summary, as of January, 2002, PLRs are issued by the following organizations:

1. Chief Counsel's Office
  - Associate Chief Counsel (Tax Exempt/Government Entities)
  - Associate Chief Counsel (International)

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- Associate Chief Counsel (Corporate)
- Associate Chief Counsel (Financial Institutions & Products)
- Associate Chief Counsel (Income Tax & Accounting)
- Associate Chief Counsel (Passthroughs & Special Industries)
- Associate Chief Counsel (Procedure and Administration)
- Commissioner, Tax Exempt/Government Entities

The basic operating unit within each Associate Chief Counsel's Office is the Branch, each with approximately 10-12 attorneys, including a Branch Chief, a Senior Technician Reviewer and an Assistant to the Branch Chief.

### ¶ 1708 COMFORT RULINGS

The processing and issuing of PLRs is a resource-intensive service provided by the IRS to enable taxpayers to be certain of tax consequences when entering into transactions or making commercial decisions. To make sure that its resources are effectively deployed, the IRS has adopted a policy of not issuing so-called "comfort rulings" in several designated areas. For example, the Office of the Associate Chief Counsel (International) has adopted a general policy against the issuance of comfort rulings:

A "comfort" ruling will not be issued with respect to an issue that is clearly and adequately addressed by statute, regulations, decisions of a court, tax treaties, revenue rulings, or revenue procedures absent extraordinary circumstances (e.g., a request for a letter ruling required by a governmental regulatory authority in order to effectuate the transaction).<sup>49</sup>

The other offices that issue PLRs have not adopted a general policy against "comfort rulings." However, offices within the Chief Counsel's office other than the Office of the

<sup>49</sup> Rev. Proc. 2002-7, 2002-1 I.R.B. 249, § 3.02(6).

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Associate Chief Counsel (International) have designated specific areas within their jurisdictions in which PLRs that would, in effect, constitute comfort rulings, will not be issued. For example, PLRs will generally not be issued with respect to certain specified types of corporate transactions (e.g., subsidiary liquidations governed by I.R.C. Section 332, certain reorganizations governed by I.R.C. Section 368) unless the transaction raises a significant issue.<sup>50</sup>

## ¶ 1709 THE PLR PROCESS IN GENERAL

### ¶ 1709.1 Introduction

Prior to 1988, the IRS generally would not issue PLRs in any area in which there was a pending regulations project, which often meant that PLRs could not be obtained for months, or even years, after the enactment of new legislation. Recognizing the urgent need for guidance, the IRS in 1988 adopted procedures under which it would issue PLRs prior to the promulgation of regulations or other published guidance in specific circumstances.<sup>51</sup>

Without doubt, the single most important document for the practitioner seeking a PLR or other form of guidance from the IRS is the first I.R.B. published each year. This I.R.B. contains, among other things, (1) the revenue procedures setting forth the rules and procedures for obtaining guidance in areas under the jurisdiction of the various offices of the Chief Counsel's Office (Revenue Procedure 2002-1 (PLRs),<sup>52</sup> Revenue Procedure 2002-2 (TAMs),<sup>53</sup> Revenue Procedure

<sup>50</sup> Rev. Proc. 2002-3, 2002-1 I.R.B. 117, § 3.01(30). Note, however, that with respect to this specific "comfort ruling" category, the IRS has retreated from its prior position of ruling only on the significant issue and not on the overall transaction. See Announcement 2001-25, 2001-11 I.R.B. 895. Accordingly, once it has been established that a transaction governed by this policy does in fact raise a significant issue, the PLR that is issued will address the tax consequences of the entire transaction and not just those associated with the significant issue.

<sup>51</sup> The circumstances under which PLRs will be issued prior to the promulgation of regulatory guidance or other published guidance are described Rev. Proc. 2002-1, 2002-1 I.R.B. 1, § 5.14.

<sup>52</sup> 2002-1 I.R.B. 1.

<sup>53</sup> 2002-2 I.R.B. 82.

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2002-3 (no-ruling areas),<sup>54</sup> Revenue Procedure 2002-7 (no ruling areas, Associate Chief Counsel (International)),<sup>55</sup> and (2) the procedures established by the office of Commissioner TE/GE (Revenue Procedure 2002-4 (PLRs)<sup>56</sup> and Revenue Procedure 2002-5 (TAMs)).<sup>57</sup>

### ¶ 1709.2 Mandatory Ruling Areas

In some areas, taxpayers must obtain a ruling or the consent of the IRS before taking action. For example, a taxpayer generally must secure the permission of the IRS before it changes its accounting period or makes a change in accounting method by filing a request using Forms 1128 and 2553 (accounting period) and 3115 (accounting method).

### ¶ 1709.3 Discretionary Ruling Areas

In areas other than those in which rulings are mandatory, the taxpayer has discretion as to whether or not to seek a PLR from the IRS. Generally, if a transaction or issue does not fall within a “no-ruling” area, the IRS will issue a PLR. However, the IRS “may decline to issue a [PLR] when appropriate in the interest of sound tax administration or on other grounds whenever warranted by the facts or circumstances of a particular case.”<sup>58</sup>

The decision by the tax practitioner and the client as to whether or not to seek a PLR is based on various factors, including

- Uncertainty of the tax law
- Potential tax liability
- Basis for issuing a legal opinion

<sup>54</sup> 2002-1 I.R.B. 117.

<sup>55</sup> 2002-1 I.R.B. 249.

<sup>56</sup> 2002-1 I.R.B. 127.

<sup>57</sup> 2002-1 I.R.B. 173.

<sup>58</sup> Rev. Proc. 2002-1, 2002-1 I.R.B. 1, § 7.01. Note, particularly, that the IRS will not issue PLRs on “frivolous issues.” See Rev. Proc. 2002-3, 2002-1 I.R.B. 117, § 7.04. Note also the policy under which the IRS will not issue certain “comfort rulings,” discussed in ¶ 1708 above.



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The practitioner should generally not consider seeking a PLR in the following circumstances:

- When the taxpayer cannot wait for the ruling. Most ruling requests take between three and four months to process. Requests involving complex or highly sophisticated transactions may take longer, some longer than six months. Very few PLRs are issued in fewer than 60 days.
- When the taxpayer, for whatever reasons, must consummate the transaction and cannot alter its structure.
- When the tax law seems certain.
- When the taxpayer's position is contrary to the position the IRS has taken in other PLRs or when the nature of the issue is such that the practitioner can reasonably anticipate that the IRS might adopt a “no rule” posture.
- When related issues may be raised by the IRS as a result of requesting the ruling.
- When the taxpayer is unwilling to disclose all relevant facts to the IRS.
- When the cost of obtaining a ruling outweighs the benefit.
- When other options exist, e.g., rendering a well-reasoned tax opinion.

#### ¶ 1709.4 No Ruling Areas

Before deciding to request a PLR, a practitioner should (indeed must) always consult the current “no rule” revenue procedures, (e.g., Revenue Procedure 2002-3<sup>59</sup> and the revenue procedures modifying it) to make certain that the issue or transaction that would be the subject of the request is not one with respect to which the IRS has announced that it will not issue rulings. See discussion in ¶ 1711, below. Few things

<sup>59</sup> 2002-1 I.R.B. 117.

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could be more embarrassing to a practitioner than to have to inform the client that the IRS has rejected a ruling request on which he or she has spent considerable time because the issue involved is listed in a “no rule” revenue procedure. The collection of fees would seem highly doubtful.

## ¶ 1710 IRS RULING GUIDELINES

### ¶ 1710.1 “Automatic” Revenue Procedures

#### A. *Accounting Periods*

The IRS has published several revenue procedures setting forth circumstances in which taxpayers, if they meet or comply with specified conditions, are permitted (or required) to adopt, retain or change taxable years.<sup>60</sup> This is done by filing a Form 1128 (or other appropriate form, e.g., Form 2553 in the case of an S corporation) with the Service Center where they file their returns, rather than with the National Office.

#### B. *Accounting Methods*

The IRS has also published several “automatic” revenue procedures in the accounting methods area. As above, these revenue procedures set forth conditions or circumstances under which taxpayers may (or are required to) proceed without obtaining a ruling from the National Office.<sup>61</sup>

### ¶ 1710.2 Guideline Revenue Procedures

In addition to providing practitioners with extensive general guidance with respect to the preparation and submission of requests for PLRs in Revenue Procedure 2002-1,<sup>62</sup> the IRS

<sup>60</sup> See, e.g., Rev. Proc. 2000-11, 2000-3 I.R.B. 309 (procedures by which certain corporations that have not changed their accounting period within the prior six calendar years or other specified time may obtain automatic approval to change their annual accounting period under I.R.C. Section 442); Notice 97-20, 1997-1 C.B. 406 (guidance to corporations changing tax-year end in order to elect S status).

<sup>61</sup> See, e.g., Rev. Proc. 99-49, 1999-2 C.B. 725 (where applicable, provides the exclusive procedure for requesting a change in method of accounting); Rev. Proc. 98-58, 1998-2 C.B. 710 (procedures under which a taxpayer may automatically change its method of accounting under certain deferred payment sales contracts to the installment method for alternative minimum tax purposes).

<sup>62</sup> 2002-1 I.R.B. 1.

also provides specific guidelines for obtaining rulings in many areas. The practitioner seeking a PLR in a given area should always determine at the outset whether the IRS has published a guideline revenue procedure relating to that area. For example, a list of current guideline revenue procedures is contained in Section 9 of Revenue Procedure 2002-1.<sup>63</sup>

Because new guideline revenue procedures are often published or existing guidelines revised during the year, the careful practitioner will always make sure the guideline revenue procedure he or she is working with is the most current.

#### **¶ 1710.3 “Self-Help” Ruling Guidelines**

Even if the IRS has not published a guideline revenue procedure in a specific area, a practitioner seeking a ruling in that area can usually construct his or her own “ruling guideline.” As noted above in ¶ 1704.6, the IRS has since 1977 released all PLRs for public inspection approximately three months after they are issued. These documents are reprinted by the tax services and are readily available to the practitioner. By carefully reviewing the last few PLRs issued in a particular area, the practitioner can identify virtually all the facts and representations the IRS will require before issuing a PLR in that area.

Even if there is a guideline revenue procedure in the area, the careful practitioner will always review the most recent PLRs issued in the area to identify any new factual requirements or representations that have been developed by the IRS since the guideline revenue procedure was published.

### **¶ 1711 NO RULING AREAS**

Each year, the offices within Chief Counsel that issue PLRs publish revenue procedures listing those areas in which, because of the inherently factual nature of the issues involved or for other reasons, PLRs or determination letters will not

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<sup>63</sup> *Id.*

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be issued.<sup>64</sup> “No rule” policies for those areas under the jurisdiction of the Commissioner TE/GE are contained in Revenue Procedure 2002-4.<sup>65</sup>

Additions or deletions to the “no rule” revenue procedures are published by the IRS throughout the year. Accordingly, the careful practitioner will always review all revenue procedures modifying the current “no rule” revenue procedures to make certain that his or her issue or factual situation has not been added to or deleted from the “no ruling” lists.

## ¶ 1712 PREPARATION OF REQUESTS FOR PLRS

### ¶ 1712.1 Introduction

The procedures utilized by the various IRS offices that issue PLRs are generally similar. However, the careful practitioner will always refer to the revenue procedures issued by the office that has jurisdiction over the area in which a PLR is being requested.

There are two ways to approach a request for rulings. Some practitioners simply throw their request together in a hurry to get it in. Although this may start the clock running somewhat sooner (assuming the request is not rejected for incompleteness), this approach will cost the taxpayer and the taxpayer’s representative time and money in the long run.

The better (far better) approach is to do it right the first time. Careful practitioners will become completely familiar with their client’s facts, the issues involved in the proposed transaction and the current IRS ruling posture relating to the proposed transaction or similar transactions. In effect, they will know their case cold. They will then translate that knowledge into a complete, well-documented and well-researched request for a PLR. There are two principal advantages to this approach. The extra time and effort involved in supplemental submissions will, for the most part, be avoided.

<sup>64</sup> See Rev. Proc. 2002-3, 2002-1 I.R.B. 117 (all Chief Counsel offices other than the Associate Chief Counsel (International)); Rev. Proc. 2002-7, 2002-1 I.R.B. 249 (office of the Associate Chief Counsel (International)).

<sup>65</sup> 2002-1 I.R.B. 127.

Secondly, and of equal importance, the practitioner will establish credibility with the IRS professionals working the case. They will know that the homework has been done. This type of ruling request is virtually always processed in less time than the thrown together type. Because in most cases timing is everything, the additional effort put in up front will pay handsome dividends on the back end.

Once they have developed their facts, many practitioners will contact the appropriate office within Chief Counsel or the Office of Commissioner TE/GE that will handle their request to discuss their case. The professionals at the IRS are almost always willing to discuss issues with taxpayers who have done their homework and are not merely calling to get an easy assist in their research. (As a caution, few things are more irritating to an IRS attorney or tax law specialist than to receive a call from a practitioner concerning an issue about which there is a revenue ruling directly on point.)

#### **¶ 1712.2 Pre-Submission Conferences**

Prior to submitting a formal request for a PLR, the practitioner should consider requesting a “pre-submission” conference.<sup>66</sup> These conferences are often helpful in ferreting out latent issues that the taxpayer’s representative may not be aware of or emerging IRS “no rule” positions. See ¶ 1706 (“Fixing the ‘Broken Transaction’), above. Pre-submission conferences may be done in person or by telephone. If a pre-submission conference is scheduled, the taxpayer will generally be requested to provide a draft ruling request or other detailed description of the proposed transaction prior to the conference. Pre-submission conference discussions are advisory only and are not binding on the IRS. Moreover, there are no assurances that the IRS attorneys who participate in the pre-submission conference will end up being the ones who will actually be assigned to work on the subsequent PLR request.

<sup>66</sup> See Rev. Proc. 2002-1, 2002-1 I.R.B. 1, § 11.07.

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### ¶ 1712.3 Format

Generally, there is no required format for requests for PLRs.<sup>67</sup> Section 8 of Revenue Procedure 2002-1 contains general instructions for requesting PLRs and sets forth information that must be contained in all requests.<sup>68</sup> Keep in mind, however, that the IRS has published many guideline revenue procedures requiring the practitioner to set forth specific information when requesting rulings in certain areas. See ¶ 1710.2, above.

Most requests for PLRs are prepared in letter format. They should be addressed as follows:

Internal Revenue Service  
Attn: CC:PA:T  
P.O. Box 7604  
Ben Franklin Station  
Washington, D.C. 20044

If a private delivery service is used, the address is:

Internal Revenue Service  
Attn: CC:PA:T, Room 6561  
1111 Constitution Ave., N.W.  
Washington, D.C. 20224

The request for rulings should be addressed to the attention of the appropriate office, determined by the subject matter of the ruling or rulings requested. If a transaction or situation with respect to which rulings are being requested involves issues in more than one area (e.g., a corporate reorganization that also encompasses pension plan issues), the practitioner may submit separate ruling requests to each office involved, or may submit a single ruling request covering all issues. In the latter instance, the office to which the request is addressed will coordinate with the other office or offices for the rulings within their jurisdiction. If separate ruling requests are submitted, each should reference the other. In either

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<sup>67</sup> *But cf.* Form 3115 (application for change of accounting method); Form 1128 (application for change of accounting period).

<sup>68</sup> *See also* Appendix B of Rev. Proc. 2002-1, 2002-1 I.R.B. 1, which provides a sample format for a PLR request.

instance, only one “user fee” (user fees are discussed in ¶ 1715, below) applies.

Generally, only one copy of the request is required. However, two copies of the request are required if the taxpayer is requesting (1) separate PLRs on different issues, (2) deletions other than names, addresses, and identifying numbers (see ¶ 1712.5, below), and/or (3) a closing agreement.

#### ¶ 1712.4 Content

Any practitioner preparing a request for a PLR must carefully review Section 8 of Revenue Procedure 2002-1,<sup>69</sup> which sets forth the information that must be included in a request for a PLR. Section 8.01 sets forth a list of certain information that is required for all requests for PLRs. Section 8.02 sets forth additional information required in certain circumstances. Among the items that must be included in a request for a PLR pursuant to Section 8.01 are:

- A complete statement of all facts relating to the transaction, including the names, addresses, telephone numbers, and taxpayer identification numbers of all interested parties. However, the term “all interested parties” does not include all shareholders of a widely-held corporation requesting a PLR relating to a reorganization or all employees where a large number may be involved;
- The annual accounting period, and the overall method of accounting (cash or accrual) for maintaining the accounting books and filing the federal income tax return, of all interested parties;
- A description of the taxpayer’s business operations;
- A complete statement of the business reasons for the transaction;
- A detailed description of the transaction. Although the IRS generally does not issue PLRs on only one step of a larger, integrated transaction,<sup>70</sup> if such a PLR is

<sup>69</sup> 2002-1 I.R.B. 1.

<sup>70</sup> *Id.* § 7.03.

¶ 1712.5 U.S.C. LAW SCHOOL TAX INSTITUTE 17-32

requested, the facts and circumstances relating to the entire transaction must be described.

- Copies of all contracts, wills, deeds, agreements, instruments, other documents, and foreign laws;
- Analysis of material facts. All material facts in documents must be included in this analysis, rather than merely incorporated by reference;
- Statements as to whether (i) the same issue arises in an earlier return of the taxpayer (or a related taxpayer or a member of the same affiliated group as the taxpayer), and (ii) the same or a similar issue was previously ruled on or a ruling was requested or is currently pending;
- A statement of supporting authorities, if the taxpayer advocates a particular conclusion.

Generally, the request should set forth the specific rulings requested. Don't reinvent the wheel. Review prior PLRs and copy (word for word) the language used in those rulings. You may think your language is better, but the IRS often works on the principle that "if it ain't broke, don't fix it."

The request should contain an extensive analysis of the law supporting the taxpayer's conclusion. The IRS also encourages, but does not require, that a "statement of contrary authorities" be submitted and suggests that, if the taxpayer concludes that there are no contrary authorities, a statement to that effect will be helpful.

**¶ 1712.5 Deletions Statement**

A request for a PLR must contain a statement identifying information to be deleted from the PLR for public inspection under I.R.C. Section 6110. The deletions statement should not be included in the body of the request, but instead must be made in a separate document.

The taxpayer may submit a statement that no deletions need be made except names, addresses and identifying numbers. If the taxpayer wishes to have other sensitive information deleted from the PLR (in addition to names, addresses



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and identifying numbers), the taxpayer may request that all appropriate information be deleted pursuant to I.R.C. Section 6110. To request such deletions, the taxpayer must submit a copy of the ruling request, indicating by the use of brackets those portions that the taxpayer believes should be deleted from the copy of the ruling to be made public.

The deletions statement must be signed and dated by the taxpayer or the taxpayer's authorized representative.

#### ¶ 1712.6 Signature

A request for a PLR must be signed by the taxpayer or the taxpayer's authorized representative. If the taxpayer is represented by an authorized representative, a power of attorney must be provided. The IRS prefers that Form 2848 be used.<sup>71</sup> The power of attorney should authorize the IRS to communicate with the representative and to send the representative a copy or the original of the PLR.

#### ¶ 1712.7 Penalties of Perjury Statement

A request for a PLR must contain a "Penalties of Perjury" statement, in the following form: "Under penalties of perjury, I declare that I have examined this [request for a PLR], including accompanying documents, and, to the best of my knowledge and belief, the [PLR request] contains all the relevant facts relating to the request, and such facts are true, correct and complete."

In the case of a corporation, the person who signs the perjury statement must be an officer who has personal knowledge of the facts and whose duties are not limited to obtaining a PLR from the IRS. If the corporate taxpayer is a member of an affiliated group filing a consolidated return, a penalties of perjury statement must also be signed and submitted by an officer of the common parent of the group.

The person signing for a trust, a state law partnership, or a limited liability company must be, respectively, a trustee, general partner, or member-manager who has personal knowledge of the facts.

<sup>71</sup> *Id.* § 8.01(14).

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The Penalties of Perjury statement must be signed by the taxpayer, not by the taxpayer's representative.

#### ¶ 1712.8 Checklists

The IRS provides a "Checklist for a [PLR] request"<sup>72</sup> that must be completed, signed and dated by the taxpayer or the taxpayer's representative. If the checklist is not submitted with the ruling request, the taxpayer or the taxpayer's representative will be asked to submit one, which may delay processing of the request.

If the issue or transaction for which a PLR is being requested is one with respect to which the IRS has published a guideline revenue procedure (see ¶ 1710.2, above), the checklist contained in the revenue procedure may require that specific representations be made by the taxpayer. This is particularly true in connection with corporate reorganizations, liquidations and distributions.

#### ¶ 1712.9 User Fee Statement

A request for PLRs must contain a statement that indicates the amount of user fees being paid and the reason why the particular amount applies. See ¶ 1715, below.

#### ¶ 1712.10 Miscellaneous

The IRS ordinarily processes requests for PLRs in order of the date received. Expedited handling is granted only in rare and unusual cases. If there is a need for expedited handling, this fact should be set forth both in the request and in a separate cover letter.<sup>73</sup>

The ruling request should always ask for a conference in the event the IRS proposes to rule adversely. The practitioner should also volunteer to attend any conference the IRS deems necessary to process the ruling request.

Although not necessary, it may be appropriate to reserve the right to withdraw the request or to supplement the factual statement or legal analysis.

<sup>72</sup> Rev. Proc. 2002-1, 2002-1 I.R.B. 1, Appendix C.

<sup>73</sup> *Id.* § 8.02(4).

Information required pursuant to guideline revenue procedures or other specific guidance should be attached to the ruling request as an exhibit. Each item set forth in the guidelines should be addressed; those that do not apply should be indicated by “N.A.” or “N.A. because . . .”

### ¶ 1713 TWO-PART RULING REQUESTS

A technique for expediting response to ruling requests is to submit what is known as a “two-part” ruling request.<sup>74</sup> Under the “two-part” procedure, the taxpayer or the taxpayer’s representative, in addition to submitting a fully developed ruling request, also submits a summary statement of facts considered to be controlling in reaching the requested ruling or rulings. In effect, the taxpayer drafts the factual summary for the IRS. Frequently, taxpayers’ representatives will submit a proposed draft of the entire ruling letter. The IRS will not utilize the draft ruling if it is inappropriate (e.g., if the factual summary omits material facts). Currently, the Chief Counsel’s Office is using WordPerfect 8.0 in preparing its PLRs. By submitting a copy of the ruling request, as well as the proposed PLR under the two-part procedure, in WordPerfect 8.0 format, the taxpayer may be able to speed the response time.

### ¶ 1714 PROCEDURES INVOLVED IN OBTAINING A PLR

- As noted above (¶ 1712.10), the IRS generally processes ruling requests in the order received, i.e., first in, first out. However, in appropriate circumstances, the IRS will expedite the handling of a ruling request. The situations in which the IRS grants expedited treatment are rare.
- When a request for a PLR is received, it is assigned to a Branch in the appropriate office (e.g., Corporate, Financial Institutions and Products, etc.) and studied by an attorney or other professional.

<sup>74</sup> *Id.* § 8.02(3).

- Within twenty-one calendar days after a request for rulings is received by the Branch, someone from the Branch (usually the “docket” attorney or other professional assigned to the request) will contact the taxpayer or the taxpayer’s representative to informally discuss procedural and substantive issues relating to the request.<sup>75</sup> However, in complex ruling situations, the taxpayer’s representative should not anticipate a detailed substantive discussion at the initial contact. If further information is required to process the ruling request, the taxpayer’s representative will be so advised. Such further information must be provided within twenty-one calendar days of the initial contact unless an extension of time is granted.<sup>76</sup>
- Assuming there are no problems with the request, a draft ruling letter will be prepared by the docket attorney and examined by a reviewer. At any point in this process, the taxpayer or the taxpayer’s representative may be contacted to discuss any problematic areas of the request or requested to make “supplemental submissions” providing additional information or documentation.
- Most PLRs are issued at the Branch level. Whether or not the PLR is reviewed at higher levels depends on the significance and or complexity of the issues involved. If the PLR requires review above the Branch level, the time frame in which it will be issued may be extended.
- A taxpayer may request a conference regarding a letter ruling request. Normally, a conference is scheduled only when the National Office considers it to be helpful in deciding the case or when an adverse decision is indicated. However, as discussed above (¶ 1712.2) the IRS, in certain circumstances, will hold so-called “pre-submission” conferences.

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<sup>75</sup> *Id.* § 10.02.

<sup>76</sup> *Id.* § 10.06.

- A taxpayer is entitled, as a matter of right, to only one conference in the National Office, unless new or additional issues are raised.<sup>77</sup> Normally, conferences are scheduled only if the IRS considers it helpful in deciding a case or if an adverse decision is indicated.
- The conference must be held within twenty-one calendar days after the IRS finally notifies the taxpayer. Procedures regarding an extension of the twenty-one-day period are set forth in Section 11.01 of Revenue Procedure 2002-1.<sup>78</sup> If additional information is required, the taxpayer has twenty-one calendar days from the date of the conference to provide such information.
- The taxpayer may withdraw a request for rulings at any time before the ruling letter is signed.<sup>79</sup> A ruling request is usually withdrawn when the IRS indicates that it will issue an adverse ruling letter. Because taxpayers virtually always withdraw their requests when advised that an adverse ruling will be issued, almost all PLRs released by the IRS to the public are favorable rulings.
- When a taxpayer withdraws a ruling request, the National Office may advise the appropriate IRS official of the particular matter.
  - If a taxpayer withdraws or the IRS declines to grant (for any reason) a request to change from or to adopt a different method of accounting, the National Office will notify (and may provide its views on the issues) by memorandum to the appropriate operating Division that has examination jurisdiction of the taxpayer's return and to the Change in Method of Accounting Technical Advisor.<sup>80</sup>

<sup>77</sup> *Id.* § 11.02 and 11.05.

<sup>78</sup> 2002-1 I.R.B. 1.

<sup>79</sup> *Id.* § 8.07.

<sup>80</sup> *Id.* § 8.07(2)(a).

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- With respect to all other ruling requests that are withdrawn or with respect to which the IRS declines to rule, the National Office will generally notify, by memorandum, the appropriate operating Division that has examination jurisdiction of the taxpayer's return and may give its views on the issues.<sup>81</sup> However, this procedure generally will not apply if the taxpayer withdraws the request for ruling and submits a written statement that the transaction has been or is being abandoned, or if the National Office has not formed an adverse opinion.
- A memorandum issued under Section 8.07(2)(a) or Section 8.07(2)(b) of Revenue Procedure 2002-1 may constitute Chief Counsel Advice subject to disclosure under I.R.C. Section 6110.<sup>82</sup>
- Even though a request for rulings is withdrawn, all correspondence and exhibits will be maintained by the IRS and will not be returned. In appropriate cases, the IRS may publish its conclusions in a revenue ruling or revenue procedure (without, of course, identifying the particular taxpayer involved).
- Once a favorable PLR is issued, the careful practitioner always reviews it line by line to make sure the IRS has correctly stated all the material facts and all the rulings requested were in fact issued. Such a review also provides the practitioner with the opportunity to make certain that the IRS has made all the deletions that were requested.

### ¶ 1715 USER FEES FOR PLRS

The Revenue Act of 1987 required the IRS to establish user fees for requests for rulings, opinion letters, determination letters and similar requests.<sup>83</sup> Although the user fee program

<sup>81</sup> *Id.* § 8.07(2)(b).

<sup>82</sup> *Id.* § 8.07(2)(a), (b), and (c).

<sup>83</sup> Revenue Act of 1987, Pub. L. No. 99-514, 101 Stat. 1330-413, Section 10511.

as originally enacted in 1987 was scheduled to expire on September 30, 1990, the expiration date has been extended several times and it seems reasonable to conclude that user fees for PLRs are a permanent fact of life.

User fees for requests handled by Associate Chief Counsel offices within Chief Counsel are listed in Appendix A to Revenue Procedure 2002-1.<sup>84</sup> User fees applicable to issues under the jurisdiction of the Commissioner, Tax Exempt/Government Entities are set forth in Revenue Procedure 2002-8.<sup>85</sup>

User fees apply to PLRs and other forms of guidance issued by the IRS (e.g., determination letters) and vary depending on the type of guidance sought. For 2002, the basic user fee for PLRs issued by the Associate Chief Counsel offices of Chief Counsel is \$6,000.<sup>86</sup> However, a reduced user fee of \$500 applies to requests (i) relating to personal issues from persons with gross income of less than \$250,000 and (ii) requests relating to business-related tax issues from persons with gross income of less than \$1 million.<sup>87</sup>

If a request for rulings concerning a single transaction involves more than one Associate Chief Counsel office, only one fee will apply, namely the highest fee that otherwise would apply, even though separate requests may be submitted to each office.<sup>88</sup>

Each request for rulings must be accompanied by a check or money order payable to the IRS in the amount of the required fee. Cash is not acceptable.<sup>89</sup> The fee is generally not refundable even if the ruling request is later withdrawn.<sup>90</sup>

If the check accompanying the ruling request is larger than the required amount, the request will be accepted and the

<sup>84</sup> 2002-1 I.R.B. 1.

<sup>85</sup> 2002-1 I.R.B. 252.

<sup>86</sup> Rev. Proc. 2002-1, 2002-1 I.R.B. 1, Appendix A, § 3(c).

<sup>87</sup> *Id.*, Appendix A, §§ 4(a) and (b).

<sup>88</sup> *Id.* § 15.06.

<sup>89</sup> *Id.* § 15.08.

<sup>90</sup> *Id.* § 15.10.

excess will be refunded. If the check accompanying the ruling request is less than the required amount, or if no payment accompanies the request, the IRS will exercise discretion in deciding whether to return the request immediately. If a request is not returned immediately, the taxpayer will be contacted and given a reasonable amount of time to submit the proper fee. If the proper fee is not received within a reasonable amount of time, the entire request will then be returned. However, the IRS will usually defer substantive consideration of a request until proper payment has been received. The return of a request to the taxpayer may adversely affect substantive rights if the request is not perfected and resubmitted to the IRS within thirty days of the date of the cover letter returning the request.<sup>91</sup> Accordingly, calculation of the appropriate user fee can be very important to the practitioner because an underpayment will result in lost time because the IRS will not begin to process the request until it is received with the proper user fee enclosed.

### **¶ 1716 USING PLRS WHEN NOT OBTAINING A PLR**

Despite the many benefits that result when a PLR is requested and received, there are many situations in which a practitioner may legitimately decide not to seek a PLR. Time constraints may make it impossible to obtain a PLR before proceeding with the transaction, or the size of the transaction may not justify the expense involved. Even when the decision is made to proceed without seeking a PLR, however, a careful practitioner will not conclude that the PLR process has nothing to offer. Far from it. Although the reliance factor will not be available if a PLR is not obtained, the knowledgeable practitioner can obtain many benefits from the process without actually seeking a PLR.

It may not be literally true that there is nothing new under the sun, but it is true that there are only so many variations on a theme. Unless someone involved in the transaction is unusually creative, chances are the transaction contemplated,

<sup>91</sup> *Id.* § 15.09.



or something close to it, has been done before. There is also a good chance that somewhere along the line, someone has asked for and received a PLR. Because PLRs are released to the public, it is often possible to “piggyback” on the work of others in providing the best possible representation for the client.

If a proposed transaction is covered by a guideline revenue procedure, the first thing the careful practitioner will do is review the procedure and determine the facts and representations the IRS requires taxpayers to provide to secure a favorable PLR. To the extent possible, the transaction should be structured as closely as possible to the situation covered by the guideline revenue procedure. If variations are necessary, the practitioner should satisfy himself that the required variations do not conflict with the spirit of the transaction described in the revenue procedure.

The client should be consulted to ensure that if a request for a PLR were being submitted, the required representations could be made. If the representative is writing an opinion on the transaction, the representations should be included as part of the factual discussion. If necessary, the transaction should be modified to conform to the representations. If this cannot be done, study the reasons for the required variations and make certain they do not fundamentally alter the transaction and thus remove it from the ambit of the guideline revenue procedure.

Even when there is no guideline revenue procedure, all is not lost. As noted above, assuming the transaction does not fall within one of the “no ruling” areas, there is a good chance that there are PLRs out there that cover transactions that are close to or even identical to the proposed transaction. The careful practitioner will locate those PLRs, study them and isolate the crucial facts and representations that led to their issuance. In effect, the practitioner will make his or her own informal guideline revenue procedure, compare the transaction with those described in the PLRs and pinpoint any variation that may cause problems. If the practitioner concludes that a variation would cause the IRS to change its

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conclusion in the prior PLRs, then it may be prudent to advise the client to rethink the transaction to determine whether to proceed or accomplish the desired objectives some other way.

## **¶ 1717 SUMMARY OF PLR PROCESS**

The authors hope that the information provided in this portion of the article will enable the reader to more easily cope with a process that is basically designed as a resource through which taxpayers can obtain guidance in the complicated world of tax law. There are two key points that we hope you will always keep in mind when you are working with the PLR process:

When preparing requests for PLRs, make sure that all relevant facts are set forth and that your research is complete on all salient points. Thoroughness is important, both in preserving your reputation and in preventing avoidable time delays in the processing of your request.

Finally, remember that when you submit your request for rulings, you will be dealing with professionals who have spent a good deal of time acquiring expertise in an area to which you may be relatively new. Deal with them as you would with other professionals and the process will usually proceed smoothly to a timely and successful conclusion.

## **¶ 1718 THE PRE-FILING AGREEMENT PROGRAM — INTRODUCTION**

Pre-Filing Agreements (PFAs) are a new form of private guidance developed by the IRS. In Notice 2000-12,<sup>92</sup> the IRS announced a pilot version of the PFA program for large and mid-size business taxpayers under which taxpayers could request examination and resolution of specific issues likely to be disputed in post-filing audits, in a cooperative manner, prior to the time for filing the taxpayer's returns. The PFA program was made permanent and expanded in Revenue Procedure 2001-22,<sup>93</sup> which sets out the ground rules for the program.

<sup>92</sup> 2000-1 C.B. 727.

<sup>93</sup> 2001-9 I.R.B. 745.

Like PLRs, PFAs concern a particular taxpayer with respect to a single issue or transaction. However, the most noteworthy aspects of the PFA process are that (i) the taxpayer, by requesting a PFA, invites an early examination of a specific issue, and (ii) if, at the conclusion of the examination, the IRS and taxpayer agree on the treatment of the item(s) in question, they enter into a closing agreement with respect thereto.

### ¶ 1719 ELIGIBLE TAXPAYERS AND YEARS

PFAs are available to taxpayers under the jurisdiction of the LMSB.<sup>94</sup> Currently, these are business taxpayers reporting assets of \$10 million or more on their returns. A taxpayer may request a PFA with respect to the current taxable year and any prior year for which the return is not yet due (including extensions) and is not yet filed.<sup>95</sup> PLRs generally are sought and issued before a transaction, though in limited cases may be obtained afterwards. By contrast, PFAs effectively are limited to completed events or transactions. Although participation in the process may be requested prior to completion of the transaction, the process itself contemplates a determination of the facts relating to the issue through an examination by LMSB. At the other end of the time window, the goal of the PFA program is to provide a determination prior to the taxpayer's filing its return with respect to the item in question.<sup>96</sup> The rules contemplate the possibility that agreement will not be reached by the filing deadline and that the process (either examination or negotiation of the agreement) may extend beyond the taxpayer's filing (except with respect to certain partnership items, for which the process must terminate no later than thirty days before the extended filing deadline<sup>97</sup>).<sup>98</sup> However, the likelihood that a PFA can be completed before the filing deadline

<sup>94</sup> *Id.* § 3.01.

<sup>95</sup> *Id.* § 3.02.

<sup>96</sup> *Id.* § 1.02.

<sup>97</sup> *Id.* § 6.04.

<sup>98</sup> *Id.* § 6.06.

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is a criteria for selecting applicants for the program,<sup>99</sup> so a taxpayer seeking a PFA should apply as early as possible.

## ¶ 1720 ELIGIBLE ISSUES

The PFA program is designed to resolve issues involving factual questions under well-settled principles of law. In this way it differs from the PLR program, which is designed to resolve questions involving the application of the law to assumed facts. Because PLRs are issued by the National Office based on represented facts, generally regarding events that have not yet occurred, they are well suited to answering legal questions about posited facts, but cannot be used to obtain the IRS's concurrence in factual determinations. Conversely, because PFAs are issued by LMSB after examination of the actual facts, they are ideally suited for obtaining the IRS's concurrence in factual determinations, but not designed for resolving novel legal questions. Accordingly, PFAs and PLRs are each suited to different types of questions, with no intended overlap (or opportunities for "forum shopping").

Specifically, LMSB will consider entering into a PFA on a factual determination or an application of legal principles to agreed upon facts in which the legal principles are well established in their application to such facts.<sup>100</sup> The PFA program is not intended to resolve disputes between the taxpayer and the IRS regarding the correct interpretation of the law.<sup>101</sup> Resolution of issues outside the zone of well established law may only occur under LMSB's authority under Delegation Order No. 236 (Application of Appeals Settlement to Coordinated Examination Program Taxpayers) or No. 247 (Authority of Examination Case Managers to Accept Settlement Offers and Execute Closing Agreements on Industry Specialization Program and International Field Assistance Program Issues).<sup>102</sup>

<sup>99</sup> *Id.* §§ 3.02 and 5.02.

<sup>100</sup> *Id.* § 3.03.

<sup>101</sup> *Id.* § 1.04.

<sup>102</sup> *Id.*

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**¶ 1720.1 Domestic Issues**

Revenue Procedure 2001-22 provides a non-exclusive list of domestic tax issues likely to be suitable for resolution under the PFA program.<sup>103</sup> This list is merely illustrative of issues that may satisfy the general criteria. The twelve listed examples are:

1. the current valuation of specific assets (except in the context of transfer pricing), but not the appropriateness of a valuation methodology;
2. the allocation of the purchase or sale price of a business among the assets bought or sold;
3. the identification and documentation of hedging transactions;
4. issues relating to in-house research expenses under I.R.C. Section 41;
5. the allocation of costs among different categories of deductible and capital items, in contexts where there is a published revenue ruling, e.g., repairs,<sup>104</sup> advertising,<sup>105</sup> and Y2K costs;<sup>106</sup>
6. identification of investigatory costs incurred to determine whether to enter a new business and, if so, which business to enter, for purposes of qualifying such costs as start-up costs under I.R.C. Section 195;<sup>107</sup>
7. whether a taxpayer's financial statement presentation of its last-in, first-out (LIFO) inventory is consistent with the LIFO conformity requirement under Treas. Reg. § 1.472-2(e);
8. whether a taxpayer's inventory contains "sub-normal" goods within the meaning of Treas. Reg. '1.471-2(c), and the valuation of such goods;

<sup>103</sup> *Id.* § 3.04.

<sup>104</sup> Rev. Rul. 94-12, 1994-1 C.B. 36.

<sup>105</sup> Rev. Rul. 92-80, 1992-2 C.B. 57.

<sup>106</sup> Rev. Proc. 97-50, 1997-2 C.B. 525.

<sup>107</sup> *See* Rev. Rul. 99-23, 1999-1 C.B. 998.

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9. whether a taxpayer is considered to be the tax owner of the property being produced under Treas. Reg. § 1.263A-2(a)(1)(ii)(A);
10. whether a manufacturing contract newly entered into by the taxpayer is required to be accounted for as a long-term contract under I.R.C. Section 460;
11. the determination of appropriate classification under I.R.C. Section 168(e) for depreciable property placed in service during the eligible taxable year; and
12. whether a security became worthless during the eligible taxable year, for purposes of I.R.C. Section 165(g).<sup>108</sup>

**¶ 1720.2 International Issues**

In the international area, there is an exclusive list of six issues likely to be suitable for resolution under the PFA program. LMSB will not entertain requests regarding other international issues.<sup>109</sup> The six issues are:

1. the valuation of specified assets, but not a retrospective change in the methodology of valuation or a determination of appropriate valuation methodology;
2. the proper SIC or NAIC classification code(s) for the taxpayer's line(s) of business;
3. whether the taxpayer's apportionment of deductions, including general and administrative expenses, that are related to all gross income properly reflects the factual relationship between deductions and gross income as required by Treas. Reg. § 1.861-8(f)(5);
4. whether, as a factual matter, an expense relates to fewer than all members of an affiliated group for purposes of Treas. Reg. § 1.861-14T(c)(2);
5. the verification of amounts of foreign taxes paid and the applicable exchange rates, but not whether such taxes are creditable; and

<sup>108</sup> Rev. Proc. 2001-22, 2001-9 I.R.B. 745, § 3.04.

<sup>109</sup> *Id.* § 3.05.

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6. whether the taxpayer must recapture a dual consolidated loss following a triggering event under I.R.C. Section 1503(d).<sup>110</sup>

**¶ 1720.3 Excluded Issues**

Finally, there is a list of types of issues that specifically are excluded from consideration, on either procedural or substantive grounds.<sup>111</sup> These are:

1. Transfer pricing issues that are addressed under the Advance Pricing Agreement program;
2. Issues for which the taxpayer has filed a request for Competent Authority assistance;
3. Issues that can be resolved by requesting a change in method of accounting on Form 3115;
4. Issues of reasonable cause, due diligence, good faith, clear and convincing evidence, or any other similar standard under Subtitle F of the Code;
5. Issues involving the application of any penalty or criminal sanction;
6. Issues that are, or will be, the subject of a pending or contemplated request for a PLR, accounting method change request, determination letter or TAM;
7. Issues for which the taxpayer proposes a resolution that is contrary to a PLR, accounting method change request, determination letter, TAM or closing agreement previously issued to or regarding the taxpayer;
8. Issues for which the taxpayer proposes a resolution that is contrary to a position proposed by the IRS in response to a PLR, determination letter or accounting method change request that was withdrawn by the taxpayer;
9. Issues that are the subject of litigation between the IRS and the taxpayer with respect to an earlier taxable period;

<sup>110</sup> *Id.* § 3.05.

<sup>111</sup> *Id.* § 3.06.

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10. Issues that have been designated for litigation by the Office of Chief Counsel;
11. Issues involving a tax shelter described in I.R.C. Section 6662(d)(2)(C)(iii); and
12. Issues that require a determination of whether the taxpayer, rather than another entity, is the common law employer.<sup>112</sup>

The term “taxpayer”, as used here, also includes affiliates and certain other related parties.<sup>113</sup>

#### ¶ 1720.4 Accounting Methods Issues

Special limitations exist when the issue relates to an accounting method employed by the taxpayer. A PFA cannot be used to obtain the IRS’s consent to a method change.<sup>114</sup> Where the PFA’s application of the law to the facts might result in a change of treatment that would constitute a change of method, the PFA can be used to resolve only the factual characterization of the items at issue, and then the method change must be obtained using the applicable administrative procedures.<sup>115</sup> The extent to which this limitation creates a disincentive to use the program for issues that may involve established methods may depend on the expected difficulty of obtaining the consent to the method change (e.g., little where an automatic consent is available).

#### ¶ 1721 ADMINISTRATIVE DISCRETION

A noteworthy feature of the PFA program is that, once a taxpayer applies, participation is at the discretion of the relevant LMSB Industry Director or his delegate.<sup>116</sup> LMSB is organized into five “industry” groupings, each of which is headed by an Industry Director. LMSB has indicated that its

<sup>112</sup> *Id.* § 3.06.

<sup>113</sup> *Id.* § 3.08.

<sup>114</sup> *Id.* §§ 3.07 and 7.03.

<sup>115</sup> *Id.* § 3.07.

<sup>116</sup> *Id.* § 5.01.



selection criteria will include several factors listed in Revenue Procedure 2001-22, Section 5.02.<sup>117</sup>

#### ¶ 1721.1 Suitability of Issue

One of the selection criteria is the suitability of the issue for the program.<sup>118</sup> Thus, if the application appears facially to involve an issue off limits to the program, the application will be rejected. This does not preclude LMSB from concluding that the issue is unsuitable at a later point, as the LMSB Industry Director is authorized to enter into a PFA only if the issue is suitable.<sup>119</sup>

#### ¶ 1721.2 Availability of Service Resources

One particularly interesting criterion for selection is “[t]he availability of Service resources.”<sup>120</sup> Although the IRS can deny issuance of a PLR in the interests of sound tax administration, it does not refuse to rule in particular cases (outside of published “no-rule” areas) as a function of staffing availability. By contrast, acceptance of a taxpayer’s request to participate in the PFA program is discretionary with the management of the relevant LMSB industry grouping. Because the PFA program draws on resources otherwise deployed in the IRS’s examination program, the availability of appropriate staffing is a significant determinant of its willingness to accept a request for a PFA.

Larry Langdon, LMSB Division Commissioner, recently stated that LMSB is reconsidering the extent to which the PFA program should be the centerpiece of its resolution initiatives, because the program is resource-and personnel-intensive.<sup>121</sup> He said that the program was successful and should continue, but that LMSB had revised its expected acceptance rate downward to a target of thirty cases for fiscal 2002.<sup>122</sup>

<sup>117</sup> *Id.* § 5.02.

<sup>118</sup> *Id.* § 5.02(1).

<sup>119</sup> *Id.* § 7.01.

<sup>120</sup> *Id.* § 5.02(3).

<sup>121</sup> 2001 TNT 185-2 (Sept. 21, 2001).

<sup>122</sup> *Id.*

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**¶ 1721.3 Ability and Willingness of Taxpayer to Dedicate Sufficient Resources**

Two other criteria are related to the resources consideration: “[t]he ability and willingness of the taxpayer to dedicate sufficient resources to the LMSB PFA process” and “the overall probability of completing the process and entering into an LMSB PFA by the proposed date for filing the taxpayer’s return.”<sup>123</sup> In effect, LMSB is authorized, based on what it knows about the issue and the taxpayer (from what is both within and outside the application) to estimate the probability of successfully completing the audit and reaching agreement by the expected filing date, and to reject applications when it does not have high hopes.

This, too, is unlike the procedures for PLRs, where the IRS considers all requests and generally tries to work as far as it can with the taxpayer before it concludes that a PLR cannot be issued. The good news for taxpayers about PFAs is that the application is not nearly as extensive as that required for a PLR, so the potential downside for wasted effort is more limited. Nevertheless, a taxpayer should consider discussing a PFA request with the IRS before completing an application. If the taxpayer currently is under examination, the taxpayer should seek out the team manager of the examination. If the taxpayer is not under examination, a call to the LMSB Manager of Pre-Filing Services and/or the office of the relevant LMSB Industry Director might be advisable. If the taxpayer does apply, it should say in its application encouraging things about the condition of its records and its willingness to cooperate promptly to facilitate the progress of the audit. And the taxpayer should mean it.

**¶ 1721.4 Contact by LMSB Representative**

A taxpayer that requests a PFA will be contacted by a representative of LMSB to discuss the application before the application is accepted or rejected.<sup>124</sup> If LMSB decides to reject the application, the taxpayer is not entitled to a

<sup>123</sup> Rev. Proc. 2001-22, 2001-9 I.R.B. 745, §§ 5.02(4) and (7).

<sup>124</sup> *Id.* § 5.03.

conference.<sup>125</sup> In that case, the taxpayer would have to file its return based on its own factual determinations.

### ¶ 1722 REQUESTING A PFA

Section 4 of Revenue Procedure 2001-22<sup>126</sup> outlines the procedures for requesting a PFA and the information required to be presented. In addition to providing information identifying the taxpayer, the request must discuss the issue to be resolved in the PFA. The taxpayer must summarize the relevant facts and applicable law, and discuss the suitability of the issue for the program given the criteria discussed above. It must also discuss the potential for the issue to affect other years of the taxpayer and other taxpayers. Finally, the taxpayer must address the IRS's administrative concerns by discussing whether the issue can be resolved by the date on which the taxpayer intends to file its relevant return and by describing the availability, organization and location of the taxpayer's records and other substantiation for its proposed position.<sup>127</sup> Requests are signed by the taxpayer under penalties of perjury.<sup>128</sup> If the taxpayer currently is under examination, the request is filed with the team manager of the examination. Otherwise, it is filed with LMSB's Manager, Pre-Filing Services, in Washington.<sup>129</sup>

### ¶ 1723 OPERATION OF THE PFA PROGRAM

If the LMSB Industry Director selects the taxpayer's PFA request for inclusion in the program, an orientation meeting is scheduled to plan the development of facts and resolution of the issue.<sup>130</sup> In addition, taxpayers whose applications to participate in the PFA program are accepted are subject to a user fee that varies from \$1,000 to \$10,000, depending on the amount of taxpayer's total assets.<sup>131</sup>

<sup>125</sup> *Id.* § 5.04.

<sup>126</sup> 2001-9 I.R.B. 745.

<sup>127</sup> *Id.* § 4.02.

<sup>128</sup> *Id.* §§ 4.03 and 4.05.

<sup>129</sup> *Id.* § 4.06.

<sup>130</sup> *Id.* § 6.01.

<sup>131</sup> *Id.* § 10.02.

From this point forward, the process proceeds like a normal examination, except that it is limited to a single issue and the IRS and the taxpayer are expected to work quickly towards producing and evaluating the relevant information. If the parties reach an agreement, a PFA is drafted and executed.

### ¶ 1724 EFFECT OF A PFA

A PFA is a closing agreement under I.R.C. Section 7121.<sup>132</sup> As such, it only will be completed if the taxpayer and the IRS reach an agreement on the treatment of the items in question; there can be no such thing as an “adverse PFA.” Once signed, it is binding on the IRS and the taxpayer. It is unlike a PLR, which can be revoked under certain circumstances.<sup>133</sup> A closing agreement has a higher degree of finality.<sup>134</sup>

If the taxpayer has not yet filed the relevant return, it must file in accordance with the agreement reached in the PFA and attach a copy of the PFA to its return.<sup>135</sup> If the PFA is completed after the taxpayer has filed its return and the agreed position differs from that taken on the return, the taxpayer must agree to amend its return to reflect the agreed position, and attach a copy of the PFA to the amended return.<sup>136</sup> A PFA typically will contain little in the way of subsequent conditions, as a closing agreement is intended to dispose of an issue with “finality.”<sup>137</sup> As a practical matter, the PFA does not depend on representations to be validated at a later date, because the facts have been examined by the IRS before entering into the PFA. Under normal circumstances, subsequent examination effectively will be limited to ascertaining that the taxpayer followed the terms of the agreement.

<sup>132</sup> *Id.* § 7.02.

<sup>133</sup> *Id.* § 12.04.

<sup>134</sup> *See* I.R.C. § 7121(b).

<sup>135</sup> Rev. Proc. 2001-22, 2001-9 I.R.B. 745, § 6.05.

<sup>136</sup> *Id.* § 6.06.

<sup>137</sup> I.R.C. § 7121.

## ¶ 1725 UNAGREED ISSUES

The PFA process will not always result in a closing agreement. Even after a PFA request is accepted into the program, either the IRS or the taxpayer may stop the process at any time by withdrawing the request in writing.<sup>138</sup> Thus, for example, LMSB can terminate the process if it finds that the taxpayer is not being prompt or complete in responding to requests for information or documents. A taxpayer can withdraw because it does not like the direction of the examination, or because the IRS does not agree with its proposed position. The only things the taxpayer cannot do are obtain a refund of its user fee and, more importantly, keep the IRS from coming back to the issue (and perhaps to its earlier position) when the taxpayer's return comes up for examination after filing.<sup>139</sup> If the examination of the issue is completed but the IRS and the taxpayer do not reach agreement, after the return is filed, the issue is considered ripe for expedited resolution techniques such as Accelerated Issue Resolution,<sup>140</sup> and, failing resolution, Early Referral to Appeals.<sup>141</sup>

Regarding unagreed issues, the PFA program differs materially, at least in theory, from the PLR program. Although (and, perhaps, because) a PLR is not binding on the taxpayer, the IRS can issue a PLR with a conclusion contrary to that requested by the taxpayer, although the taxpayer generally can avoid this result through timely withdrawal of the ruling request.<sup>142</sup> However, as noted above, an "adverse PFA" is, even in theory, not possible.

## ¶ 1726 DISCLOSURE

A PFA is a closing agreement reflecting the results of a completed examination, albeit limited to a specific issue. Thus, it is confidential return information protected under

<sup>138</sup> Rev. Proc. 2001-22, 2001-9 I.R.B. 745, § 8.01.

<sup>139</sup> *Id.* §§ 10.04 and 8.02.

<sup>140</sup> See Rev. Proc. 94-67, 1994-2 C.B. 800.

<sup>141</sup> See Rev. Proc. 99-28, 1999-2 C.B. 109; Rev. Proc. 2001-22, 2001-9I.R.B. 745, § 9.

<sup>142</sup> See Rev. Proc. 2002-1, 2002-1 I.R.B. 1, § 8.07.

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I.R.C. Section 6103 of the Code from disclosure by the IRS.<sup>143</sup> Unlike PLRs, they are not made public even in redacted form.<sup>143</sup> It's not clear the public is missing anything — PFAs should not make interesting reading. A PLR is issued on the strength of the taxpayer's representations, which are recited in detail so that an examining agent later can determine whether the representations match the true story. A PFA is completed after the examination, so there is no administrative need to tell a story that can be verified later. A PFA needs to have enough detail to determine what the parties agreed upon. In many cases, that agreement should be reduced to one or more dollar amounts.

The IRS is required to publish a report annually on the operation of the PFA program, much like it does regarding Advance Pricing Agreements. These reports should give some indication of the scope of the program, both in terms of subjects covered and the number of requests resulting in actual agreements.

## ¶ 1727 REASONS TO SEEK A PFA

Why would a taxpayer ask to be audited?

O.K., a PFA is not every taxpayer's solution to every problem. Nonetheless, there may be good reasons to request one in a specific case.

### ¶ 1727.1 Timely Access to Relevant Records and Personnel

Revenue Procedure 2001-22<sup>145</sup> notes that a pre-filing examination can often resolve issues without significant cost, burden and delay, because the taxpayer and the IRS have more timely access to the records and personnel relevant to the issue.<sup>146</sup> There is some truth to this. If a business or subsidiary member of a consolidated group recently has been, or is about to be, sold, the taxpayer or consolidated group often is dependent on the buyer to preserve the records and

<sup>143</sup> Rev. Proc. 2001-22, 2001-9 I.R.B. 745, § 11.01.

<sup>143</sup> *Id.*

<sup>145</sup> 2001-9 I.R.B. 745.

<sup>146</sup> *Id.* § 1.02.

personnel necessary to substantiate factual issues. Often, the buyer can't be relied on to do this over the long term. The PFA process can accelerate the examination to a time where the information is more likely to remain accessible. Similar benefits may exist where a business experiences high turnover of personnel whose presence would be useful in defending an audit. In the case of valuation issues, it may be easier to resolve questions in the context of the current market than several years from now.

#### **¶ 1727.2 Greater Level of Certainty at an Earlier Point in Time**

Revenue Procedure 2001-22<sup>147</sup> also indicates that a PFA provides the taxpayer with a greater level of certainty at an earlier point in time.<sup>148</sup> This, too, may have value to a taxpayer, particularly if the issue is likely to recur in later returns. Although the PFA will only govern the year examined, the early resolution is likely to benefit the taxpayer in preparing its returns, designing its recordkeeping systems, and/or general tax planning. A PFA may be particularly useful if the greater need for certainty comes from the fact that the taxpayer's position also affects other parties, assuming the PFA can be obtained before the taxpayer must take its position, for example, on a Form W-2 or 1099 (although the IRS has some interest in avoiding cases that subject it to significant whipsaw potential).<sup>149</sup> A further advantage in terms of certainty is the possibility that early resolution of an issue may allow a taxpayer a better presentation of its tax liability for financial disclosure purposes (i.e., without "cushions" or noted disclosures of potential risks).

### **¶ 1728 SUMMARY OF PFA PROGRAM**

In summary, a PFA is an interesting new option for large and mid-sized business taxpayers seeking an expedited resolution of factual issues, something not previously available from the IRS.

<sup>147</sup> 2001-9 I.R.B. 745.

<sup>148</sup> *Id.* § 1.02.

<sup>149</sup> *Id.* § 5.02(5).

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