
National Research Program

Employment Tax Reporting Compliance Study



Module 2

Examination Guidelines

Student Guide

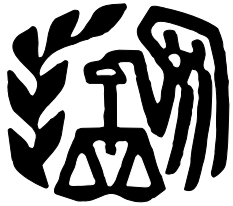
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Department of the Treasury
Internal Revenue Service

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Internal
Revenue
Service

Mission

Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.



Department of the Treasury
Internal Revenue Service
Document 9300 (9-94)

Ten Core Ethical Principles *

Honesty
Integrity/Principled
Promise-Keeping
Loyalty
Fairness
Caring and Concern for Others
Respect for Others
Civic Duty
Pursuit of Excellence
Personal Responsibility/Accountability

The Five Principles of Public Service Ethics *

Public Interest
Objective Judgment
Accountability
Democratic Leadership
Respectability

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Module 2

Examination Guidelines

Student Guide Contents

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General Contents

This student guide and the accompanying Articulate (e-learning) presentation introduce you to the National Research Program (NRP) Employment Tax examination process. Together, they cover topics such as how to initiate an NRP examination, prepare an effective initial Information Document Request (IDR), how to conduct a research examination, and other procedural items.

Complete this self-study student guide before viewing the Articulate presentation that covers this module.

Student Guide Objectives

Upon completion of this student guide and the accompanying Articulate presentation, students will be able to:

- Initiate NRP examinations
 - Address taxpayer's questions on research examinations
 - Utilize NRP examination guidelines and procedures
 - Determine when a case can be excluded
 - Transfer an NRP Employment Tax key case
 - Explain the quality review process for NRP cases
-

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Student Guide Contents, Continued

Student Guide Structure

Sections	The student guide consists of seven sections. The first six sections are to be completed before viewing the Articulate presentation. The last section contains information used in the Articulate presentation.
Topics and block lines	Each section of the student guide consists of several topics. The topic is identified in the heading on each page. Subtopics are identified in the left hand column and separated by block lines.
Italicized lines	Italicized lines distinguish key points or actions.
NRP logo	The NRP logo emphasizes topics or subtopics unique to NRP.
Answers	Answers to exercises are located in a separate section at the end of the text.


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Section 1

Assigning NRP Cases & Initiating the Examination

Assigning NRP Cases

NRP Case Assignment

 *NRP cases must only be assigned to trained examiners.*

NRP cases must only be assigned to examiners that have completed all applicable training modules.

	Articulate Overview
Module 1	NRP Overview
Module 2	Examination Guidelines
Module 3	Report Generation Software (RGS), Reporting Compliance Case Management System (RCCMS) and Data Capture Instruments (DCI 1 and DCI 2) for Examiners.

NRP Pre-Audit Analysis/Case Building

Guidelines



NRP Employment tax returns must be examined unless exclusion criteria (discussed later) are met.

Guidelines for examining NRP returns include:

- All NRP returns must be examined unless exclusion criteria, discussed later, are met.
- NRP returns may not be surveyed before or after assignment unless the return is approved for exclusion.
- An NRP return consists of all four quarters of the 2008 tax year. Any quarters that were filed by the taxpayer will be established on AIMS by the NRP office. Any Non-Filed TY 2008 quarters must be established on AIMS if there was determined to be a filing requirement. If there were no filing requirement, clear and concise comments must be made in the electronic case file.

Guidelines on Issues

All NRP key cases include mandatory, required and examiner-identified issues that must be addressed through the pre-loaded lead sheets in the Data Capture Instrument (DCI). There are two DCI's—DCI 1-Workpapers and DCI 2-NRP ET Report.

NRP Case Building Process

NRP Case Building Process

The tax return, Examination Return Charge-Out (Form 5546), CBRS, ChoicePoint, IDRS information, and other case building items are packaged into either a paper NRP case file or are included in the NRP RGS/RCCMS case file. The case built files are forwarded to the designated BOD NRP case assigners for assignment to the groups and NRP trained examiners for audit.

NRP is moving toward a fully electronic case file, the only paper case building documents included in the case files will be the Case Building Inventory Sheet (that the Campus uses to document the items in the paper case file), the Examination Return Charge-Out and any CP-2100 notice, if applicable. All other case building material will be provided electronically in the NRP RGS/RCCMS case file.

Case building tools help the NRP examiners by providing valuable return and financial information that may lead to or support any adjustments to the tax return.

NRP Case Building Process Elements

Case Built Return Elements

With the number of NRP case files undergoing examination, it is important that the information under review be presented in a consistent and consolidated format. Case building information is organized in a uniform manner to increase efficiency and effectiveness during the examination. Following are the contents of a NRP case built return and a brief statement as to the information they provide.

The paper case file will include:

1. NRP Case Building Inventory Sheet provides a list of case building items contained in either the paper case file or the NRP RGS/RCCMS case file.
2. Examination Return Charge-Out (Form 5546) verifies that the tax return has been established on AIMS and provides other information such as audit history, CAF indicator for power of attorney, etc.
3. CP2100 ("B" Notice) – This provides information on improperly filed 1099's with an invalid TIN, no TIN, or mismatched TIN. This notice is also provided electronically.

In addition to the paper case file, the electronic case file will include the following:

4. Imaged returns of the NRP Employment key case will be placed in the RGS/RCCMS Office Documents folder.
5. CBRS provides financial information related to reported large cash transactions. A summary sheet will be provided.
6. ChoicePoint documents provide taxpayer locator and asset information. This information is only available for individual taxpayers.
7. IDRS prints for specific command codes provide taxpayer return and financial data. These include:
 - **AMDISA**–This command requests information on current audits.
 - **BMFOL E** – Displays entity information.

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NRP Case Building Process Elements, Continued

Case Built Return Elements, (continued)

- **BMFOL I** – Displays an index of business master file tax modules.
- **BMFOL R** – Displays return information (DLN, cycle posted, income, FICA) etc.
- **BMFOL T** – Displays a list of posted transactions to a specific period.
- **BMFOL U** – Displays a reconciliation of the filed 941/945/Sch.H wages and tax to the W-2's filed with Social Security and 1099-R's that show taxes withheld.
- **BMFOL Z** – Displays audit history information.
- **PMFOL S** – Displays Payer Master File information such as whether the entity filed W-2s and/or 1099s.
- **PMFOL B** – Displays an explanation of B Notices (CP-2100) used in back-up withholding tax cases.
- **BRTVU** – Displays online Business Master File tax return information.
- **INOLE S** – Displays entity information (names, address, cross reference TIN's, filing requirements, and exempt status, etc).
- **INOLE X** – Displays cross reference for additional TIN's or name controls.
- **SUMRY** – Displays a summary screen showing all modules on IDRS. Useful for determining if Collection, the Campus, or Criminal Investigation is actively working a case.

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NRP Case Building Process Elements, Continued

**Case Built
Return
Elements,
(continued)**

8. Related Return – This includes the related income return and or the Exempt Organization returns – (Form 1040, Form 1120, Form 1120-S, Form 1065, Form 990, Form 990-PF and 990-T.)
 9. Information Return Analysis System (IRAS) – Electronic versions of forms W-2 and 1099 will be provided. You will use an Access program called *IRAS* to analyze the W-2's and 1099's for potential issues. Certain reports, discussed later in this module, are required on ALL NRP cases.
 10. Capital IQ – This provides corporate entity information which includes SEC reports, executive reports and new information. (LMSB cases only.)
 11. MeF XML Converter – This Access program converts the electronic Form 1120 tax return into Excel for further analysis. (1120 cases only.)
 12. CP2100 ("B" Notice) – This provides information on improperly filed 1099's with an invalid TIN, no TIN, or mismatched TIN.
-

NRP Working With the Taxpayer During the Examination

Guidelines



NRP examinations should be conducted in the same professional manner as any operational examination.

Guidelines for conducting an NRP examination are no different than any other operational examination and include:

- The examination process can be completed in a professional and timely manner when the IRS and taxpayer/representative work cooperatively. Time is a valuable resource for both taxpayers and examiners.
- Throughout the audit process, examiners should be available to meet with taxpayers or representatives to resolve issues or address any concerns about the audit. Group/Team Managers should also be available to assist examiners and taxpayers/representatives as needed.
- Examiner responsiveness to taxpayer inquiries consistently resulted in higher taxpayer satisfaction ratings during the prior NRP studies.

Mutual Responsibilities

Mutual responsibilities include:

- Identifying and discussing potential areas of examination (including adjustments in the taxpayer's favor) on the tax return.
- Requesting and providing pertinent information necessary to determine the proper employment tax treatment of an issue.
- Applying relevant tax authority, including the Internal Revenue Code (IRC), the Treasury Regulations (Regs.), court cases, etc., required to make a correct determination.
- Keeping all parties advised of any unavoidable delays.
- Addressing all parties' questions and concerns expressed during the examination.
- Keeping all parties fully informed about the information needed, the adjustments being proposed, and the progress of the examination throughout the audit process.
- Performing the above responsibilities in a timely manner.

Continued on next page

NRP Working With the Taxpayer During the Examination, Continued

NRP How to Contact a Taxpayer



Examiners should initiate taxpayer contact as quickly as possible after the case is assigned.

Guidelines for contacting a taxpayer for an NRP examination include:

- Initiate taxpayer contact as quickly as possible after the case is assigned.
- Revenue Agents or Revenue Officer Examiners can either initiate contact using Letter 3851-B (2009) or by telephone.
- Letter 3851-B is a call back letter which affords the taxpayer and the examiner an opportunity to discuss the NRP examination process. Examiners can also gain a better understanding of the types of records that the taxpayer maintains.
- If there is no response to the initial contact letter(s), then contact by telephone should be attempted.
- IRM 4.23.3.6 states that for field examinations, a telephone call or letter will be used in all instances to schedule an appointment in the field for an employment tax interview. If the initial contact is by telephone, it is important that the revenue agent ensures that the taxpayer knows that this is an NRP examination. During the initial telephone call, the agent will also gain a better understanding of the taxpayer's business and should set-up the initial appointment. A follow-up letter (L3850-B) will be mailed to the taxpayer confirming the time/place of the examination along with the initial IDR's. These procedures must be documented in the case activity record/chronology. Also see IRM 4.10.2.7.4.1 and IRM 4.10.2.7.4.2.

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NRP Working With the Taxpayer During the Examination, Continued

**NRP How to
Contact a
Taxpayer,
(continued)**

- Notice 1332 (1-2007), Notice 609 (12-2004), and Publication 1 (5-2005) must be used as enclosures with initial call-back letters (L3851-B) or confirmation letters (L3850-B). Notice 1332 explains to the taxpayer how and why their return was selected for an NRP examination. To view Notice 1332, see page D-19. In addition, to view other notices, publications, and letters refer to irs.gov.

All possible efforts should be made to contact taxpayers whose returns are to be examined.

- If no contact is made see the following IRM sections for guidance:
 1. IRM 4.10.2.7.2 - Locating the Taxpayer
 2. IRM 4.10.2.7.2.1- Undeliverable Initial Contact Letters
 3. IRM 4.10.2.7.2.2 - Unlocatable Taxpayers-Mandatory Steps to Locate
 4. IRM 4.10.2.7.2.3 – Additional Resources for Locating Taxpayers
 5. IRM 4.10.2.7.2.4 – IDRS/CFOL Command Codes Useful in Locating the Taxpayer
 6. IRM 4.10.2.7.2.5 – Using Credit Bureau Information to Locate a Taxpayer
 7. IRM 4.10.2.7.2.6 – Third Party Contacts
 8. IRM 4.23.3.7.6 – Third Party Power of Attorney

Continued on next page

NRP Working With the Taxpayer During the Examination,
Continued

**Additional
Recommended
Actions
Necessary for
Unlocatable
Taxpayers**

As noted above, third party contacts are appropriate means to help locate a taxpayer. Disclosure rules allow for this type of third party contact as long as specific tax return information is not disclosed. Examples of acceptable third party contacts include contacting the preparer of the NRP Employment tax returns, IRP information, or contacts identified on Accurint, Capital IQ, Westlaw, or other web research.

**4.23.3.7.4
(03-24-2009)
Scheduling
the
Appointment**

(1) In arranging for a convenient time and place to start an examination, it is advisable to telephone the taxpayer or the representative. If the initial appointment is scheduled by telephone, mail an appointment letter 3850-B to confirm the appointment and summarize the list of records to be made available during the examination.

(2) At all times endeavor to make appointments at a time and place that will meet the convenience of the taxpayer and be consistent with Federal Administrative and Procedural Regulations § 301.7605-1 on time and place of examination.

(3) Examinations should be conducted at the place where the taxpayer maintains the business operations. However, the examination may be conducted at a place other than the location of the business operation if agreed to by the examiner and the taxpayer or the authorized representative. Once the appointment is made, try to avoid cancelling it.

Also see IRM 4. 10.2.7.6 – Place of Examination.

Continued on next page

NRP Working With the Taxpayer During the Examination, Continued

Notice 1332

Notice 1332 (1-2007) should be used as an enclosure to the NRP initial contact letter. This notice explains to the taxpayer how and why their return was selected for an NRP examination.

Why Your Return is Being Examined

Your return was selected at random for a compliance research examination. We usually select returns for general examinations because there is some indication that the return is incorrect. We also randomly select returns for compliance research examinations in order to gather data for use throughout the Service to improve our tax system. We recognize that taxpayers who consistently meet all of their tax obligations bear their fair share of the overall tax burden. Our mission, however, includes examining enough tax returns to ensure that the federal tax system is administered fairly and that any errors on the examined returns will be corrected.

The random selection of your return does not mean it contains errors, but allows the IRS to collect information in a statistically valid manner about how taxpayers meet their tax responsibilities. This information will help us determine what changes to IRS forms, publications, and tax laws may improve voluntary compliance. It will also be used to guide improvements to how the tax laws are enforced, and to programs designed to help taxpayers understand and comply with the tax laws. All this improves the fairness of the tax system.

There may not be any errors in your return; however, if there are, we will tell you and give you a chance to explain them. If you overpaid your tax, we will send you a refund plus interest. If any tax is due, we will ask you to pay it plus any penalties and interest due as required by law.

It is to the advantage of all taxpayers that everyone pays their fair share of taxes in accordance with the laws enacted by Congress. We appreciate your cooperation with the examination of your return.

Department of the Treasury
Internal Revenue Service
Notice 1332 (Rev. 1-2007)
Catalog Number 38915Y

NRP Examination Location

Guidelines



Examiners should follow operational procedures when determining examination location.

IRM 4.10.2.7.6 provides guidance on where examinations should take place. Examiners should follow operational procedures when determining the examination location.

- The location of the taxpayer's representative will generally not be a consideration in determining the place of the examination.
- Field examination cases should generally be conducted at the location where the original books, records, and source documents are maintained.
- If the business is so small that a field examination would essentially require the taxpayer to close the business or would unduly disrupt business operations, the examiner will conduct the examination in the IRS office closest to the taxpayer's business or at the representative's office.
- If the examination cannot be performed at the taxpayer's place of business, a tour of the business is to be made and documented in the workpapers.

Note: If you should need further help, Treasury Regulation 301.7605-1(e), Time and Place of Examination, provides guidance for establishing the time and place of examination.

Section 2

NRP Examinations and Customer Perceptions

Customer Perceptions



NRP examinations will often generate additional questions and concerns from the taxpayer.

NRP examinations will often generate additional questions and concerns for both the taxpayer and representative. The examiner should be thorough in response to taxpayers' questions.

Some of the more likely questions will be:

- Why me (us)?
- What did I (we) do wrong?
- How long will this take?
- How much cost and lost time?

Notice 1332 provides explanations to taxpayers about NRP examinations. Examiners should be familiar with this notice to help in addressing taxpayer concerns and questions.

Examiners should strive to create a cooperative atmosphere. In some situations, difficulties will be encountered. Examiners should confer with their group/team manager in dealing with problem situations.

Continued on next page

NRP Examinations and Customer Perceptions, Continued

**Customer
Perceptions:
Exercise A**

You contact the NRP taxpayer using letter 3851-B. The taxpayer informs you their employment tax return has been examined 2 out of the last 3 years. You check IDRS and the taxpayer is correct. However, there were substantial agreed adjustments and additional taxes assessed each year. The taxpayer will not listen to any of your efforts to explain NRP and that the examination will need to progress. What do you do?

- A. Be very stern with the taxpayer and tell them the examination will go on with or without their cooperation.
- B. Inform the group/team manager of the taxpayer's lack of cooperation and jointly develop a plan of action in dealing with this examination.
- C. Tell the taxpayer that they qualify for repetitive audit procedures and discontinue the examination.
- D. Immediately summons the taxpayer and third-party records.

Answer:

NRP Examinations and Customer Burden (Specific IDR Guidelines)

Guidelines



The initial IDR(s) should list the specific records, information, and documents that the taxpayer should have available at the initial interview. Examiners should always carefully consider what is necessary and avoid requesting more information than is essential to resolve the issues. Examiners should prepare the initial IDR(s) after discussing the examination process, issues selected for examination, and types of books and records available with the taxpayer or their representative. Follow your operational guidelines.

Examiners should refer to IRM 4.10.2.9.2, Requesting Information or Documents from the Taxpayer, for specific guidance when preparing IDRs throughout the examination process. Although examiners must request information that is relevant and necessary to resolve the issues and areas under consideration, they should also be cognizant of the burden each IDR places on the taxpayer and/or the representative.

Background of the NRP Program

During audits of the NRP Tax Year (TY) 2001 Individual study and TY 2003 and 2004 S Corporation study, the Treasury Inspector General Tax Administration (TIGTA) concluded that some taxpayers were asked for unnecessary information. Similar findings were also noted by NRP Area Quality Review Teams. The TIGTA reports noted that in over 35% of the NRP cases reviewed that IDR(s) were overly general or used technical jargon or requested unnecessary items or requested items that the IRS already had access to. TIGTA cited an example of an IDR requesting data related to interest and dividend income although the taxpayer's return and all of the IRS' information sources clearly indicated the taxpayer received no dividend or interest income. TIGTA stated that "clear and concise information requests are critical to minimizing taxpayer confusion and speeding the examination process." TIGTA also stated that, "IDRs that request unnecessary items are counterproductive to the IRS efforts to reduce taxpayer burden resulting from NRP studies."

Continued on next page

NRP Examinations and Customer Burden (Specific IDR Guidelines), Continued

Background of the NRP Program, (continued)

To reduce the burden on future NRP taxpayers, TIGTA recommended that the Service strive to improve the clarity of written information requests provided to taxpayers. In an effort to lessen the burden of future research studies on taxpayers and to improve on the quality of requests for information, the Service agreed to address initial IDR preparation in subsequent NRP training, as well as publish additional guidance on effective IDR preparation. The following article on effective IDR preparation appeared in the February 2007 edition on the *Technical Digest*.

Technical Digest Article Preparing Effective IDRs

During a recent audit of NRP Form 1120S cases, TIGTA observed that a number of IDRs requested unnecessary information, were vague, or were not specific as to what information was needed. Area Review Teams have found similar items in their review of NRP cases.

IDRs that request unnecessary information or are vague can be counterproductive to both the taxpayer and the examiner and create unnecessary burden. Effective IDRs should be tailored to the taxpayer and request only the information that is necessary to complete a quality examination. IDRs should also be clear and concise and include the appropriate tax period. This will minimize taxpayer confusion and expedite the examination process.

The preparation of effective IDRs begins in the pre-planning phase of the examination as this is when the entire file is reviewed to determine what information is available or needs to be requested from internal sources such as IDRS. Copies of the same original returns that are in the case file should not be requested from the taxpayer. Employment tax returns should generally not be requested when the IDRS data can be obtained internally. To decrease taxpayer burden, examiners should use internal sources of information, e.g., Corporate Files On Line (CFOL) and Midwest Automated Compliance System (MACS), to complete required filing checks. If discrepancies are noted or other sources of internal information lack sufficient detail, then the examiner should request specific items or returns from the taxpayer or obtain them internally. An alternative procedure would be to ask the taxpayer questions when they respond to the call back letter (see below) or during the initial interview.

Continued on next page

NRP Examinations and Customer Burden (Specific IDR Guidelines), Continued

**Technical
Digest Article
Preparing
Effective IDRs
(continued)**

Field examinations use call back letters to set the initial appointment. When the taxpayer calls in response to the letter, an opportunity is provided to determine the type of books and records available. When discussing the issues and records available, clarify what types of documentation/records the taxpayer uses to determine income and expenses.

The initial and subsequent IDRs should request documentation in terms that the taxpayer readily understands. Once the IDR is prepared, take a second look at what is being requested. Is the request specific, tailored to the taxpayer, and written in clear understandable terms? Are items requested relevant and necessary to resolve the issues under audit?

The use of IDR templates by examiners is acceptable as long as items are deleted that do not apply to the taxpayer. When a taxpayer receives the initial IDR(s), it can be rather lengthy, and the taxpayer may naturally assume that is all the information they will have to provide. The statement “Additional records may be requested as the examination progresses” lets the taxpayer know that additional information may be needed. The examiner should also include a due date for the requested information. For additional information, see IRM 4.10.2.9.2 (Requesting Information or Documents from the Taxpayer) and IRM 4.10.2.3.4 (Required Filing Checks).

Continued on next page

NRP Examinations and Customer Burden (Specific IDR Guidelines), Continued

IDR Preparation – Points to Remember

Examiners should remember the following points when preparing IDR(s) in NRP cases:

- An IDR should not be sent with Letter 3851-B, the NRP initial contact letter. Letter 3851-B is a callback letter that allows the examiner an opportunity to discuss the examination process, issues, types of books and records maintained by the taxpayer.
- Examiners should be familiar with the taxpayers’ accounting and recordkeeping systems before issuing the initial IDR. When the taxpayer or representative calls to discuss the initial appointment, the examiner should learn more about the availability, location and types of books and records maintained by the taxpayer. When auditing business returns do not ask for journals, subsidiary ledgers, etc. that the taxpayer does not maintain.
- The initial IDR(s) should list specific records, information, and documents that taxpayers should have available at the first appointment. The IDR should use terminology familiar to the taxpayer. **The IDR should be specific and should avoid requesting more information than is essential to resolve the issues identified.**
- Facts in each case will determine what is considered an adequate description of the requested data. An IDR must sufficiently specify the books, papers, records, or other data. The request should also include the particular activity and time period.
- Examiners may have access to pro-forma type IDR(s) that include a list of items which are commonly requested in examinations. Use of pro-forma IDR(s) or focused text is acceptable; however, the IDR must be modified or tailored to the particular return being examined. Items not applicable or duplicated should be deleted. Examiners must be careful not to use a “shot-gun” approach and request everything on the list if some of the items may not be relevant to the return under examination.

Continued on next page

NRP Examinations and Customer Burden (Specific IDR Guidelines), Continued

IDR Preparation – Points to Remember (continued)

To decrease taxpayer burden, examiners should use internal sources of information, e.g., CFOL and BRTVUs to complete required filing checks. Following are two links for helpful IDRS/CFOL guides.

IDRS Command Codes Job Aid

http://serp.enterprise.irs.gov/databases/irm-sup.dr/job_aid.dr/command-code.dr/idrs_command_codes_job_aid.htm

CFOL Express, An CFOL/IDRS Reference Guide, A user guide for field personnel.

<http://sbse.web.irs.gov/AIMS/docs/CFOLexpress.pdf>

- If after analysis of the internal sources of information it is determined that additional return information is needed, the returns should be requested from internal sources or the taxpayer for inspection.
 - It is advisable to include a statement on the initial IDR(s) indicating that the examiner will probably request additional records as the examination progresses.
 - The IDR(s) must include a date for taxpayer submission of the requested documents or information.
 - If it is necessary to make a second request for the same information or documents, the date(s) of previous request(s) will be entered in the appropriate space.
 - **For LMSB Examiners Only** – The LMSB mandatory tax shelter IDR will need to be issued for all cases where there is no income tax team coordinator assigned. Always get the latest IDR from the following link:
http://lmsb.irs.gov/hq/pftg/otsa/CollateralPrograms/Mandatory_IDR.
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Section 3

Conducting an NRP Examination

NRP Examination Scope

Guidelines



Some inquiry or inspection of records or documents must be made on all NRP Employment Tax Returns.

Guidelines on Issues

Examiners must address all Mandatory, Required and potential employment tax issues. Potential employment tax issues include any necessary and relevant General, Tier 1, Tier 2 and Worker Classification issues.

NRP Change of Scope and Examination of Related Returns

Guidelines



*Due to the nature of Employment Taxes, issues for examination must be established at the Examiner level. An “issue list” will be provided as part of the Data Capture Instrument (DCI) and any issues that affect the entity will define the minimum scope of the examination. If examiners are aware of other issues, regardless of materiality, the scope must be expanded to include these issues. In determining whether to examine a related return (entity), the same judgment should be used as is used in performing all operational examinations. The related entity examination is not a NRP key case sample return so the scope of the examination is determined by the examiner. **Examiners need to use source code 91, project code 0087, and 9508 tracking code on any related return opened for examination. NRP key cases and all related employment tax returns examined need to be included on the Report Generation Software (RGS) or Reporting Compliance Case Management System (RCCMS) file server.***

According to IRM 4.23.3.7.3, Scope of the examination, it is recognized that examinations, whether change or no-change, vary in the scope of the examination. Normally, the examiner is expected to:

- a. Conduct the examination to a point where the reported employment tax liability is determined to be substantially correct,
- b. Determine whether information returns and wage statements have been correctly filed, and
- c. Determine whether all applicable Federal return requirements have been met.

For NRP cases, the employment tax examination is different. **The scope includes all identified tax issues on all 4 quarters of the 2008 tax year.** Any and all issues and must be included in the DCI 1 – Workpapers file.

Refer to IRM 4.22.10 which discusses expanding the scope of the NRP key case and the examination of related entities. The following summarizes the IRM requirements:

- Due to the research nature of NRP audits, examiners should be aware of all issues that impact the NRP Employment Tax year. Examiners must expand the scope of the NRP year examination to other issues, regardless of materiality.

Continued on next page

NRP Change of Scope and Examination of Related Returns, Continued

Guidelines (continued)

- All filed TY 2008 quarters will be initially established on AIMS. Any additional 2008 quarters must be added if there was a filing requirement. If there was no filing requirement, clear and concise comments must be made in the lead sheets.
 - In certain circumstances related entities may need to be examined. When this occurs the examiner needs to document and discuss the reason(s) why.
 - Copies of the prior and subsequent year returns will be inspected. Expand the audit to include open periods where the issue is recurring or where there appears to be other large, unusual or questionable items.
 - Related return examinations are not NRP sample returns. The scope of the examination on the related entity will be determined by the examiner. **Related returns are not subject to the NRP guidelines.**
 - When establishing AIMS control for the examination of prior and subsequent year returns or related entities, source code 91, project code 0087, and tracking code 9508 will be used.
 - Prior/subsequent and related employment tax returns under examination need to be on the RGS/RCCMS file server. This will also be discussed during the NRP RGS/RCCMS training.
-

NRP Change of Scope and Examination of Related Returns, Continued

Employment Tax Return Related Questions

Following are possible related return questions examiners should consider in determining if a related entity should be examined:

- Does the taxpayer own an interest in any:
 - ▶ S-Corporations
 - ▶ C-corporations
 - ▶ Partnerships
 - ▶ Trusts
 - ▶ Schedule C
 - ▶ Non-Profit Entities

- Does the taxpayer have to file Form 8027?
- Does the taxpayer have household employees?
- Does the taxpayer have withholding on pensions or gambling winnings?
- Are the executives being paid out of a different payroll entity?
- Are there contracts between related parties?

Continued on next page

NRP Change of Scope and Examination of Related Returns, Continued

Related Return Decision Points

It may not be possible to determine an entity's level of compliance without full consideration of the entity's financial interests in, and relationships with, related entities and individuals. This is especially true of entities where the owners:

- Are actively involved in the business operations.
- Have significant influence over business decisions.
- Have access to business assets (including cash).
- Lack competing interests with other owners.
- Can divert business assets (including cash) without detection.
- Show ownership of a foreign entity, offshore relationship, or foreign bank account.
- Are involved in complex transactions.
- Have IRC Section 482 issues (allocation of income, deductions, etc.).

Examiners should consider alternative positions (see IRM 4.23.10.17.3) and Whipsaw issues (see IRM 4.10.7.4.9 below).

IRM 4.10.7.4.9 Whipsaw (a/k/a Correlative Adjustments)

- (1) The term whipsaw refers to situations where the government is subjected to conflicting claims by taxpayers. A potential whipsaw situation exists whenever there is a transaction between two parties and correct reporting of the transaction may benefit one and adversely impact the other for tax purposes.

Continued on next page

NRP Change of Scope and Examination of Related Returns, Continued

IRM
4.10.7.4.9
Whipsaw
(a/k/a
Correlative
Adjustments)
(continued)

(2) A potential whipsaw situation could be present in almost any transaction; however, experience has shown the following issues to generate the majority of whipsaw cases:

- a. Goodwill vs. covenant not to compete
- b. Alimony vs. child support
- c. Allocation of purchase price
- d. Buyer vs. seller
- e. Sale vs. rental/royalty
- f. Employee vs. independent contractor
- g. Payments to widows (gift vs. taxable income)
- h. Dependency exemptions for children of divorced parents
- i. Husband and wife filing separate returns
- j. Grantor, trust, and beneficiaries
- k. Parent and child
- l. Decedent and decedent's estate
- m. Taxpayers in which the Commissioner has invoked the provisions of IRC section 482
- n. Parent and subsidiary corporations

(3) When whipsaw issues require (i.e. material tax consequence) an examination of both parties, examiners will secure the name, address, and the tax identification number (TIN) of the related party. A transcript will be requested to determine the related party's examination status.

- a. If a related party is under examination, then the examiner assigned to the case will be notified.
- b. If the related party is not under examination, then the examiner will determine if they can examine the return or if a referral is needed. If a collateral examination is warranted, then Form 6229, Collateral Examination, will be prepared.

(4) The primary objective of requiring support examinations of these returns is to assure consistent treatment of related taxpayers or taxpayers involved in the same transaction.

Continued on next page

NRP Change of Scope and Examination of Related Returns, Continued

4.23.10.17.3 Alternative Position in Unagreed ET Cases

An alternative position may be proposed for an unagreed case in order to strengthen the Service's position in Appeals with respect to that particular case. Backup withholding is a strong alternative position in a reclassification case in which the employer did not issue Form 1099 and did not get TINs from the workers. The primary reason for the examination adjustment should be written as the primary position. The secondary reason for the adjustment will usually address a different set of law and arguments supporting the adjustment made and is called the alternative position.

Non-Specialty Tax Related Returns

During the course of your examination, you may encounter issues outside of the scope of employment taxes that require examination. In these instances a referral should be made to appropriate business unit division.

All referrals should be made according to existing operational guidelines. When making a referral, it is important to remember to use the appropriate NRP codes – source code 91, project code 0087 and tracking code 9508.

If a referral is made using form 5346, NRP requires that an electronic copy of the completed form is saved in the Office Documents folder of RGS/RCCMS.

NRP Required Filing Checks

Guidelines



Required Filing Checks are necessary on NRP examinations. They are the same as operational examination procedures.

Examiners should complete all required filing checks on NRP Employment Tax Return as in any other examination. In order to reduce taxpayer burden, examiners should utilize case building materials to the extent possible to meet these requirements.

“Required Filing Checks (RFCs) are necessary to ensure voluntary compliance. Examiners should determine that taxpayers are in compliance with all Federal tax return filing requirements and that all returns reflect the substantially correct tax.” (IRM 4.10.5.1)

IRM 4.22.10 – Required Filing Checks

If the related entity is deemed worthy of examination, the examiner needs to timely request controls on the related return and open an examination on that entity. If the related entity is outside the group control, the examiner will follow the procedures outlined in the IRM for collateral examinations.

Refer to the chart in IRM 4.10.5.1, Required Filing Checks, which summarizes compliance checks and minimum requirements.

For LMSB Cases where there is no Income Tax Team Coordinator, an additional required filing check is needed for corporate officers’ return. See IRM reference 4.46.3.6.7 – Corporate Officers’ Return.

(1) LMSB’s Executive Compensation Strategy - This strategy requires the assessment of compliance risk of corporate officers and other key executives as part of any LMSB examination.

(2) Inspection of Officer and Key Executive Returns –The team manager, at a minimum, will secure and inspect the individual returns of the top officers of the corporation and other key executives or highly compensated employees. The team should include the top officers of the largest subsidiaries in meeting the minimum requirement for inspection purposes if the taxpayer filed a consolidated return. The inspection generally will be limited to the officer/shareholder returns for IC taxpayers.

NRP Examination Depth Guidelines

Guidelines



Examiners must use their professional judgment concerning the depth of examination required for any particular item on the tax return, bearing in mind the research nature of the examination. However, the overall depth of the examination on NRP employment tax return(s) and related returns is still the same as is used in operational examinations.

Examiner's professional judgment determines the depth of the examination for each examined issue. The depth of the examination on a NRP examination is the same as is used in operational audits. Therefore, NRP taxpayers are not held to a higher standard or more in-depth audit procedures. A photo copy of documents reviewed should only be included in the case file when necessary.

Issues should only be pursued to the depth necessary to reach a supportable conclusion.

- Because NRP results are to be used for updating Tax Gap information it is essential that examinations be thorough.
- Adjustments must reflect the actual error patterns found on the returns regardless of the amount and must be free of any bias resulting from judgmental errors on the part of the examiner.
- The examiner's report package (DCI 2) for the NRP Employment tax year is separate from the workpaper package (DCI 1). The examination report (DCI 2) should be prepared according to existing operational guidelines. Examiners may choose not to issue a report or issue a de minimis report if the overall deficiency amount is less than tolerance. (refer to LEM 4.10.2.3.1).
- Regardless of the report issued to the taxpayer, it is important to remember that DCI 1 must reflect **ALL** adjustments. Materiality is never a consideration for the completion of DCI 1.
- Disposal code 01 is used if there are any adjustments recorded on the DCI 1, but a no-change or de minimis report is issued to the taxpayer.
- Disposal code 02 is only used for valid no-change cases.

Continued on next page

NRP Examination Depth Guidelines, Continued

IRM 4.22.4.4.2 – Evaluation of Books and Records

IRM 4.22.4.4.2 further discusses the evaluation of books and records and consideration of various types of evidence as follows:

1. The research nature of these examinations requires care in evaluating evidence. Evidence tends to prove a fact or point in question.
2. NRP examiners should gather facts to determine the accuracy of any issue identified for examination. This determination should include all the facts supporting both sides of an issue.
3. Documentary evidence is emphasized in the conduct of an NRP examination. Records kept contemporaneously with the occurrence of an event generally reflect accurately that event. Books of original entry should be obtained if they exist. The contemporaneous records, invoices, bank statements, cancelled checks, and any other documents to support the books and records should be inspected to a depth adequate to support the accuracy of those books and records.
4. In situations where contemporaneous books and records do not exist or are incomplete, secondary written records (e.g., copies of original documents obtained from third parties) or other reconstructions of records, if credible, may be used.
5. Oral testimony by a taxpayer is direct evidence that must be thoroughly considered. The degree of reliability placed on a taxpayer's oral testimony must be based on the credibility of the taxpayer and the surrounding circumstantial evidence.
6. Oral testimony by other than the taxpayer may also be credible if that person has first-hand knowledge of the facts and circumstances.
7. The steps to obtain evidence and the evaluation of it should be documented in the issue's workpapers.
8. The guidelines contained in IRM 4.10.7.3, Evaluating Evidence, should be utilized to make reasonable determinations in NRP examinations.

Continued on next page

NRP Examination Depth Guidelines, Continued

Exercise B

The owner of an 1120S construction company that generates over \$1 Million of income paid himself a wage of \$10,000 for tax year 2008. In order to perform an audit of the issue, you should:

- A. Accept the amount of wages as reported and not address the issue.
- B. Examine every expense item of the business.
- C. Interview the taxpayer to gather facts about the extent of services performed by the officer.
- D. Determine if additional payments or property or fringe benefits were paid or given.

Answer:

NRP Examination Lead Sheets

Guidelines



Electronic Lead Sheets must be prepared and included in the RGS/RCCMS case file. This requirement exists so reviewers of the case files such as GAO can determine facts, procedures and conclusions when the physical case file is not available. In addition, we are moving toward a paperless case file. Audit procedures and conclusions for each item audited must be supported by written comments in the workpapers.

- All Lead Sheets must be prepared electronically and included in the RGS/RCCMS case file.
- The Data Capture Instruments include the specific Lead Sheets (DCI1) for the employment tax return NRP case and the NRP ET Report (DCI2). These DCIs will be discussed in the RGS/RCCMS and Data Capture Instruments classroom training. You will know the mandatory Lead Sheets because they will be coded, ETM--, for example ETM02. Each business unit may have different mandatory Lead Sheets.
- Operational issue lead sheets must also be completed electronically for NRP cases. In addition, all electronically prepared workpapers (spreadsheets, etc.) should be included in the electronic RGS/RCCMS Office Documents folder.

Examination Lead Sheets and workpapers must include the following as described in IRM 4.22.10

- Audit procedures and conclusions for each issue audited must be supported by written comments in the workpapers. This is necessary to ensure that the statistical data gathered for NRP is accurate and complete.
- Examiners must describe what inquiry or inspection of records or documents was made to verify reported or possible unreported wages, fringe benefits, and other employment tax issues.
- The workpapers must describe the steps the examiner took to determine what was looked at, for example, oral testimony, third party contact, etc., to determine the resolution to each specific employment tax issue.

NRP Examination Lead Sheets, Continued

NRP Examination Required Issues and Analysis



As discussed earlier, the scope of the NRP employment tax examination will consist of all issues that are identified through the examination. However, there are a few required issues that **MUST** be addressed on every case. These are 1099 Filing Checks, Back-up Withholding and Fringe Benefits.

Form 1099 Filing Checks ask the following questions:

1. Were payments made to employees in the Accounts Payable system that should have been included in compensation?
2. Were there Accounts Payable vendors that should have been included in Form 1099s issued?
3. If a B-Notice (CP2100) was issued, did the taxpayer take appropriate action?
Determine whether the Service Center issued any B-notices by reviewing IDRS command code PMFOL B.
4. Did the taxpayer make B-notice corrections?
5. Review Forms 1099 issued to individuals for EE/IC issues:
 - a. Did any employees receive both Forms 1099 and W-2?
 - b. Should those employees have received only a W-2?
 - c. Should any of the vendors who were treated as an IC have received only a W-2?
6. Does the taxpayer qualify for Section 530?
7. Does the worker classification settlement program apply?
8. Are the exercises of stock options correctly reported on Form 1099?

This is a vehicle to exam 1099 compliance and also identify whether a worker classification issue exists and any other related issues.

Continued on next page

NRP Examination Lead Sheets, Continued

**NRP
Examination
Required Issues
and Analysis
(continued)**

The second required issue relates to **Back-up Withholding** tax. It addresses the following questions:

1. Are the amounts reported on the 1099 correct?
2. Was there a difference between PMFOL and the taxpayer's Forms 1099?
3. Did the taxpayer have the payee TIN on file at the time the reportable payments were made?
4. Did the Service notify the payor that the TIN furnished by the payee is incorrect?
 - i. How many B-Notices were corrected by the taxpayer?
 - ii. How many B-Notices were there back-up withholding on?
 - iii. How many B-Notices were not resolved?

Continued on next page

NRP Examination Lead Sheets, Continued

NRP Examination Required Issues and Analysis (continued)

The third required issue is **Fringe Benefits**. There are two lead sheets for fringe benefits. They are executive and non-executive. Both must be addressed on each case.

Below are the specific fringe benefits that must be addressed for each type. If benefits are identified you must include them. For any fringe benefits identified by the examiner a corresponding lead sheet must be prepared. Any benefits identified, but not listed should be included and identified as Other Taxable Fringe Benefits.

Executive Fringe Benefits	<i>Non-Executive Fringe Benefits</i>
Aircraft Personal use	
Bonus Payments (exec)	<u>Accountable Plans</u>
Covenants Not to Compete	<u>Auto Personal Use</u>
Golden Parachute Payments	<u>Back Pay</u>
Loans as Compensation and Discharge of Indebtedness (exec)	<u>Bonus Payments</u>
Million Dollar Cap - IRC 162(m)	<u>Cafeteria Plans</u>
Nonqualified Deferred Compensation	<u>Cell Phones</u>
Split-Dollar Life Insurance	<u>De Minimus Fringe</u>
Stock Based Compensation - General	<u>Educational Assistance Plans</u>
<u>Stock Based Compensation - Nonstatutory Options</u>	<u>Group Term Life Insurance</u>
<u>Stock Based Compensation - Incentive Stock Options</u>	<u>Lawsuit Settlements</u>
<u>Stock Based Compensation - Employee Stock Purchase Plans</u>	<u>Legal and Financial Planning</u>
<u>Stock Based Compensation - Restricted Stock</u>	<u>Loans as Compensation and Discharge of Indebtedness</u>
<u>Stock Based Compensation - SARS, Phantom Stock, Other</u>	<u>Meals or Lodging for the Convenience of the Employer</u>

Continued on next page

NRP Examination Lead Sheets, Continued

Other Fringe Benefits	<i>Non-Executive Fringe Benefits, Continued</i>
Accountable Plans	Moving Expenses
Auto Personal Use	No Additional Cost Services
Back Pay	Other Taxable Fringe Benefits
Cafeteria Plans	Per Diem Allowances
Cell Phones	Prizes, Awards, Gifts, Vacations
De Minimus Fringe	Qualified Employee Discounts
Educational Assistance Plans	Rental Value of Property Furnished
Group Term Life Insurance	Settlements
Lawsuit Settlement	Severance Pay
Legal and Financial Planning	Spousal Travel
Meals or Lodging for the Convenience of the Employer	Supplemental Unemployment Compensation
Moving Expenses	Tax Preparation
No Additional Cost Services	Tips and Gratuities
Other Taxable Fringe Benefits	Tool Reimbursement Plans
Per Diem Allowances	Working Condition Fringe
Prizes, Awards, Gifts, Vacations	
Qualified Employee Discounts	
Rental Value of Property Furnished	
Settlements	
Severance Pay	
Spousal Travel	
Supplemental Unemployment Compensation	
Tax Preparation	
Working Condition Fringe	

NRP Examination Lead Sheets, Continued

NRP Examination Required Issues and Analysis (continued)

Aside from the NRP Required issues, there are certain reports and analysis that must be completed for ALL NRP cases using the IRAS program. (See the page D-14 for a description of the IRAS program.)


While your professional judgment should determine the scope of the final analysis, at a minimum the following reports are required for each taxpayer according to your BOD:

Report:	SBSE	LMSB	EO	FSLG
Test for no FICA Wages	✓	✓	✓	✓
Test for no Medicare Wages	✓	✓	✓	✓
Test for invalid SSN's	✓	✓	✓	✓
Test for Workers getting W-2 and 1099	✓	✓	✓	✓
Test for no or low income tax withholding	✓	✓	✓	✓
Test for no Taxable Wages	✓	✓	✓	✓
Test for Excess Deferred Compensation	✓	✓	✓	✓
Test for Box 12, Code V Stock Options	✓	✓	✓	
Test for Box 12, Code Z 409A amounts	✓	✓	✓	
Test for Box 12, Code Y for nonqualified deferred compensation	✓	✓	✓	
Test for variances in Box 1 wages versus Box 5 Medicare Wages	✓	✓	✓	✓
No Retirement Compensation				✓

The appropriate analysis for each BOD can be found on the Mandatory Lead Sheet ETM14 – Payroll Reconciliation. Additionally, the reports for each BOD are included as part of the “NRP Easy Button” on the NRP IRAS program. ALL reports must be saved electronically in the RGS/RCCMS Office Documents folder.

NRP Preparing Effective Lead Sheets

Guidelines

 *NRP Employment Tax lead sheets include additional research elements as well as existing operational elements. NRP lead sheets are designed so that information entered by the examiner can be extracted and provided to the stakeholder requesting the information.*

All lead sheets are presented in an *Excel* format and included in the NRP DCI 1-Workpapers file. Information on how to access and complete the lead sheets will be provided in the new training Module RGS/RCCMS and Data Capture Instruments (DCI).

- **ETM – Mandatory Lead Sheets.** These lead sheets are designed for each BOD and are required to be completed for all cases.
- **ETG – Lead Sheets.** These are the first issue related Lead Sheets and include additional questions to ask and audit techniques. Aside from the back-up withholding issue that is required for each case, all other issues are mandatory only if they are applicable to the taxpayer.
- **ET218 – 218 Agreement Lead Sheet** – This lead sheet applies for only TE/GE FSLG audits.
- **ETECOO – Fringe Benefits (Corporate Officer/Executive) Lead Sheets** - This summary lead sheet is required for all NRP employment tax cases. Separate electronic lead sheets are required for any and all benefits identified during the examination. There will be links to the specific fringe benefits from the summary sheets.
- **ETFBOO – Fringe Benefits (Non-Executive)** - This summary lead sheet is required for all NRP employment tax cases. Separate electronic lead sheets are required for any and all benefits identified during the examination. There will be links to the specific fringe benefits from the summary sheets.
- **ETT – Tier 1 Issues** – Currently, in the DCI1, there is only one Tier 1 lead sheet and this is offshore employee leasing. This is not required unless this issue is identified on the return.

Continued on next page

NRP Preparing Effective Lead Sheets, Continued

Exercise C Which issue is not required to be addressed on ALL NRP Key cases?

- A. 1099 Filing Checks
- B. Alien Employment Tax Issues
- C. Backup Withholding
- D. Fringe Benefits

Answer:

**Guidelines
(continued)**

- **ETBS – Tier 1 Monitoring Issues (Back-dated Stock Options)** – LMSB or SB/SE issue. Could apply to publicly traded or private companies.
- **ETCW – Worker Classification Issues** - Working through the Form 1099 filing check issue, the examiner will identify worker classification issues.
- **ETG14 – Other Issues** – Use **this lead sheet** for any other identified issues.

Continued on next page

NRP Preparing Effective Lead Sheets, Continued

Type	IssueCd	Issue Name	SBSE	LMBS	FSLG	EO
Mandatory	ETLM01	LMSB Administrative Leadsheet		X		
	ETM02	NRP Administrative Lead Sheet	X	X	X	X
	ETM03	Employment Tax Plan to Close Check Sheet	X		X	
	ETM04	Group Manager Concurrence Meeting Check Sheet	X			
	ETM05	Initial Taxpayer Contact Sheet	X		X	X
	ETM06	Initial Appointment	X	X	X	X
	ETM07	Multi-Year & Related	X	X	X	X
	ETM08	Records Check List	X		X	
	ETM11	Mandatory Issues Check Sheet	X		X	X
	ETM13	Closing Conference Agenda	X		X	X
	ETM14	Payroll Reconciliation	X	X	X	X
	ETM15	Fraud Indicators	X		X	X
	ETM16	Penalty Approval	X	X	X	X
	ETLM17	Report Writing		X		
Required	ETM09	Form 1099 Filing Checks	X	X	X	X
	ETG04	Backup Withholding	X	X	X	X
	ETFC00	Fringe Benefits (Executive)	X	X	X	X
	ETFB00	Fringe Benefits (Non-Executive)	X	X	X	X
General	ETG01	Abatement (withholding)	X	X	X	X
	ETG02	Agricultural	X	X	X	
	ETG03	Alien Employment Tax Issues	X	X	X	X
	ETG05	Currency Banking and Retrieval System (CBRS)	X	X		X
	ETG06	Citizens or Residents of the US Living Abroad	X	X	X	X
	ETG07	Corporate Officer with W2	X	X		X
	ETG08	Excess Benefit Transactions - 501(c)(3) and 501(c)(4)				X
	ETG09	Gaming	X	X		X
	ETG10	Reasonable Cause (Penalties)	X	X	X	X
	ETG11	Schedule C	X			
	ETG12	Third Party Payor	X	X	X	X
	ETG13	Tip Exam - Restaurant	X	X		X
	ETG14	Other	X	X	X	X
	ET218-01	FICA Coverage for Government Employees			X	
Offshore Leasing	ETT01	Offshore Employee Leasing (Notice 2003-22)	X	X	X	X
BSO	ETBSO01	§ 162(m) Compensation Limitation	X	X		
	ETBSO02	ISO to NSO Due to Backdating	X	X		
	ETBSO03	409A - Tax Due to Backdating	X	X		
Worker Class	ETWC01	Worker Class - Corp. Officer No W2	X	X		X
	ETWC02	Worker Class - CSP	X	X	X	X
	ETWC03	Worker Class - Statutory Employee	X	X		X
	ETWC04	Worker Class - 530	X	X	X	X
	ETWC05	Worker Class - Common Law	X	X	X	X

NRP Preparing Effective Lead Sheets, Continued

Preparing Effective Lead Sheets

- Lead sheets should adequately document the facts, audit steps and conclusions reached for each issue examined so that someone looking at the electronic case file can determine exactly what the examiner did, found, and concluded based on the examination of the issue. In other words, Document Your Steps (DYS).
- A lead sheet entry such as "See Attached" is not acceptable unless you have attached the related electronic workpaper file in the RGS/RCCMS case file.
- If the related file(s) are not attached to the applicable issue, the file should be named in a manner to associate the workpaper with the issue.
- On the Lead Sheet ETM07 - NRP Multi Year and Related Return Lead Sheet, if there is a related return it is recommended that additional information about the related return (ownership, type of business, etc.) be included on the Lead Sheet if the return is not opened for examination. For LMSB examiners where there is no income tax coordinator, executive filing reporting compliance will be addressed on ETM07.
- IRM 4.10.9.2.4 discusses issue lead sheets. Items listed include a header, dollar per return/as adjusted, pre exam analysis and a brief conclusion of the examiner's decision.

Note: Include only relevant workpapers for issues and not voluminous copies of taxpayer documents that do not reconcile to the Lead Sheet.

NRP Examination Workpaper Documentation

Workpaper Reminders



Audit procedures and conclusions for each audited issue must be supported by written comments in the workpapers.

- Examiners are required to use the DCI 1 electronic lead sheets for all issues examined. Lead sheets must contain the adjustment amount, facts, audit procedures and conclusion.
- The examiner must use issue-specific lead sheets. However, in some instances, the use of the ETG-14 - Other ET Lead Sheet is appropriate. In either case, the examiner is required to tailor the auditing steps to their specific taxpayers.
- All applicable lead sheets need to be completed for the key case. The examiner is expected to complete the lead sheets and workpapers contemporaneously.
- All workpapers must be prepared electronically and included in the RGS/RCCMS case file. This includes the NRP 941 Examiner and Manager Case Closing Checksheets discussed in Section 5 on Quality Review.
- Significant emphasis is placed on examiner professional judgment when completing Lead Sheets. When a box is checked on a Lead Sheet, the examiner is indicating that they have completed the task. Often the facts and circumstances change, and the examiner should remember to revisit the items previously checked and make any corrections.
- Checking the box does not alleviate the examiner from creating workpapers or to make comments when appropriate. Checking a box is not a short cut for doing an audit step. The work performed to reach a decision must be shown, typically on subsidiary workpapers.

Continued on next page

NRP Examination Workpaper Documentation, Continued

Workpaper Reminders (continued)

The following are workpaper reminders that are applicable only to examiners:

- The examiner lead sheets are required to be used in each entity case file, according to existing operational guidelines.
- For all SB/SE GS-12 examiners, the group manager Concurrence Meeting Check Sheet, ETM03, is mandatory (follow local procedure). If a thorough examination of a related entity is warranted, the concurrence meeting should be held within 14 business days of the initial appointment. If a thorough examination of the related entity is not warranted, the concurrence meeting for the related entity becomes more of a formality.
- Risk analysis tools to limit the scope of the audit are not applicable when an examiner is expanding the scope on the NRP key case return. The research nature of the examination and the resulting correct tax liability is the overriding factor. Therefore, the risk analysis Lead Sheet is not required for expanding the scope on the key case return. The risk analysis lead sheet should be included in the key case file whenever a prior or subsequent year or related return is picked up for examination.

LMSB NOTE: LMSB agents will follow operational and IMS guidelines for preparing an initial risk analysis, and if needed, a mid-cycle risk analysis. However, the mid-cycle risk analysis will not be used to limit the scope of the NRP year.

NRP De Minimis Adjustments

Guidelines



Due to the research nature of NRP employment tax examinations, de minimis adjustments must be made to all NRP employment tax returns.

Due to the research nature of NRP examinations, de minimis adjustments must be made to the NRP employment tax returns for research purposes. To simplify de minimis adjustment procedures, examiners must make **all** adjustments, even small ones, and include them in the DCI 1 – Workpapers file.

Completion of the Employment Tax Report (DCI 2) is independent of any adjustments recorded on the DCI 1 – Workpapers file. The DCI 2 Report file for the NRP year should be prepared according to existing operational guidelines.

For NRP purposes, if adjustments are recorded on the DCI 1 file, but the total tax due for the NRP year is below the tolerance, the correct examination disposal code is 01, no change with adjustments.

Disposal code 02 – No Change, is only applicable to valid no-change cases.

LEM 4.10.2.3.1 guidelines should be used if a no change report should be issued to the taxpayer. This criteria is based on a total tax year deficiency, not on a quarterly basis.

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NRP De Minimis Adjustments, Continued

Exercise D

De minimis procedures apply only to the NRP key cases. Operational procedures including a risk analysis for employment tax examiner should be followed when making adjustments to any prior/subsequent year return or related return.

During the examination of the NRP key case return, you find that all mandatory issues have been fully verified except for fringe benefits. The NRP key case claimed \$2,710 in officer use of company car but the taxpayer has verification for only \$2,230. The corporate officer did not repay the excess reimbursement. There are no other adjustments, and the estimated tax due is \$ 193 for the recharacterization of the \$480 as wages.

What action should be taken regarding recharacterization of the unverified \$ 480 of the car allowance?

- A. Record the total adjustment in the DCI 1 – Workpapers file. Prepare a report for the NRP year using the DCI 2 – Report according to operational guidelines.
- B. Ignore the adjustment since it is immaterial and no-change the issue.
- C. Expand the scope of the examination to try to avoid a no change.

Answer:

NRP Use of Specialists

Guidelines



Examiners should follow operational guidelines when determining if specialists are needed on NRP returns.

The following are guidelines for using specialists on NRP returns:

- Specialist Referral System (SRS) is used to request computer audit specialists and international agents if needed on your case. Other types of specialists may be engineers, economists and evaluation specialists. These specialists should be viewed as assets for completion of the NRP cases. <https://srs.web.irs.gov/> This link provides you with the ability to request formal or informal assistance. Indicate “ET NRP” in the narrative when requesting a specialist through SRS.
- <http://lmsb.irs.gov//TAHome.asp>. This web site provides you with a list of LMSB technical advisors and industry specialists. If specialists are assigned to a case, the examiner to whom the NRP return is assigned will be relieved of responsibility for certain issues assumed by specialists but will **NOT** be relieved of the responsibility for the timely completion of the examination.

Audit Technique Guides

The Exam Specialization Program has been developed to:

- Increase the level of expertise of examiners;
- Obtain knowledge useful for developing examination guidelines specific to the business environment; and
- Develop for each market segment compliance strategies that will be easier to understand and apply.

Examination specialists, subject matter experts, and technical advisers have a working knowledge of the market segments they have studied. Audit Technique Guides, see link below, are available to assist examiners in the most efficient approach to audit each issue on the NRP case.

<http://www.irs.gov/businesses/small/article/0,,id=108149,00.html>

NRP Returns and Penalty Usage

Guidelines



Examiners are required to consider the application of appropriate penalties before the conclusion of every audit.

The following are the guidelines for penalty usage in NRP returns:

- Examiners are required to consider the application of appropriate penalties before the conclusion of every audit, including all NRP examinations. This does not mean that because it is an NRP return, it generates penalties. Examiners should follow the same considerations as used in any operational audit.
- All employees who administer penalties should use the Penalty Handbook (IRM 20.1) for guidance to applying penalties. Another source is IRM 4.10.6 (see below).
- The Penalty Approval Lead Sheet should be completed for all NRP tax cases to document penalty assertion or non-assertion.

4.10.6.1 – Overview

- (1) The Service maintains an ongoing effort to develop, monitor, and revise programs designed to help taxpayers comply with legal requirements and avoid penalties. As indicated in Policy Statement P-1-18, the Service uses penalties to encourage voluntary compliance by:
 - a. Helping taxpayers understand that compliant conduct is appropriate and that noncompliant conduct is not;
 - b. Deterring noncompliance by imposing costs on it; and
 - c. Establishing the fairness of the tax system by justly penalizing the noncompliant taxpayer.

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NRP Returns and Penalty Usage, Continued

4.10.6.1 – Overview (continued)

- (2) Policy Statement P-1-18 also states that the IRS administers a penalty system that is designed to:
- a. Ensure consistency
 - b. Ensure accuracy of results in light of the facts and the law
 - c. Provide methods for taxpayers to have their interests heard and considered
 - d. Require impartiality and commitment to achieve the correct decisions
 - e. Allow for prompt reversal of initial determinations when sufficient information has been presented to indicate that the penalty is not appropriate
 - f. Ensure that penalties are used for their proper purpose and not as bargaining points in the development or processing of cases
-

NRP Unagreed and Partially Agreed Examinations

Guidelines



Do not compromise adjustments to secure an agreement in NRP examinations.

The following are guidelines for unagreed and partially agreed NRP examinations:

- Examiners should follow local procedures for all unagreed and partially agreed examinations. All adjustments need to be recorded in the DCI 1 – Workpaper file for NRP purposes.
 - Reports are prepared using DCI -2 for the NRP year.
 - Adjustments should not be compromised to secure an agreement in NRP examinations.
-

NRP Collectibility Considerations

Guideline



Collectibility of deficiencies will not be a consideration in conducting NRP examinations.

Remember, NRP is all about the data. Since collecting quality data is paramount, collectibility of any deficiencies will not be a consideration in conducting NRP examinations.

The data collected from NRP examinations will be used to measure the tax gap associated with employment taxes, improve workload selection models, increase taxpayer assistance efforts and allow the IRS to focus its limited resources.

NRP Examination Information Resources

NRP Examination Information Resources



If you need additional information, it is readily available.

There are many information resources available for NRP:

- Printed IRS materials
 - IRS Internet and intranet sites
 - Other research materials
-

Printed IRS Materials & Intranet Sites

Printed IRS materials & Intranet Sites include:

- NRP course material
 - Publications, forms, and instructions
 - IRMs, including NRP IRM 4.22
 - Audit Technique Guides (ATGs)
 - Exam Specialization and Technical Guidance
<http://sbse.web.irs.gov/TG/default.htm>
 - SB/SE Employment Tax
<http://sbse.web.irs.gov/sp/EmploymentTax/Default.htm>
 - LMSB Employment Tax
http://lmsb.irs.gov/hq/fs/employment_tax/index.asp
 - NRP Web Site <http://NRP.web.irs.gov/>
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NRP Examination Information Resources, Continued

Other Research Materials Other research materials include:

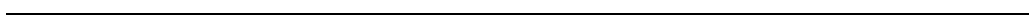
- Accurint research results
 - State and local tax data (communication and liaison)
 - DMV
 - Online county assessor's offices
 - CCH, Lexis-Nexis, Westlaw
 - Internet searches including stock price and historic dividend web sites
 - Google and various other search engines
 - Capital IQ (Publicly traded)
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Section 4

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