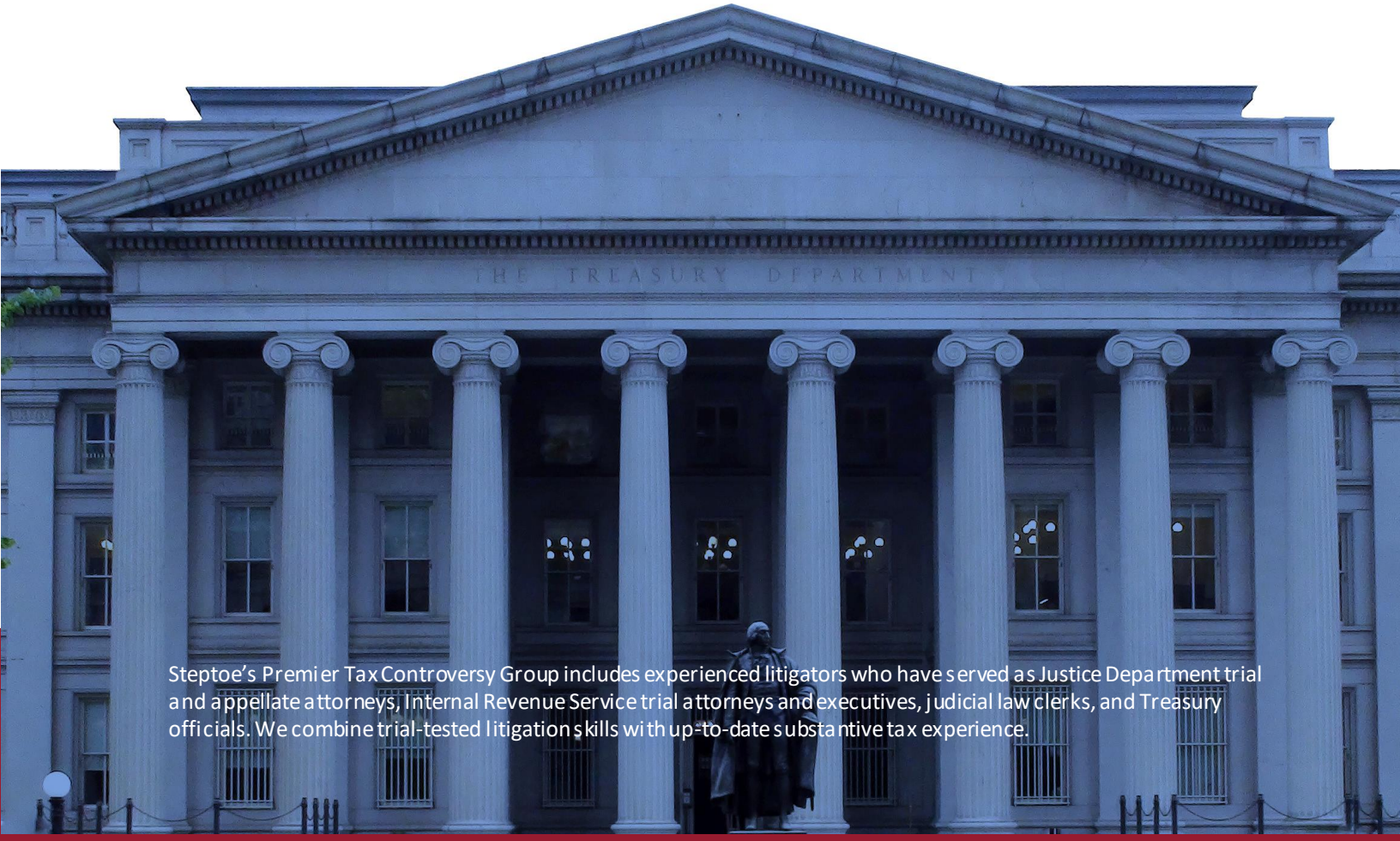
Steptoe

Focus on Tax Controversy

NEWSLETTER

January 2022



Steptoe's Premier Tax Controversy Group includes experienced litigators who have served as Justice Department trial and appellate attorneys, Internal Revenue Service trial attorneys and executives, judicial law clerks, and Treasury officials. We combine trial-tested litigation skills with up-to-date substantive tax experience.

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YEAR-END TAX CONFERENCE & CELEBRATION

Steptoe hosted our Year-End Tax Conference and Celebration at The Yale Club in New York, on Monday, December 6.

Attendees included senior in-house tax professionals from financial institutions including Bank of America, Citigroup, Commerzbank, Deutsche Bank, Goldman Sachs, Jefferies, JP Morgan, Morgan Stanley, Rabobank, and UBS. They also included tax executives from multinational corporations including Marsh McClennan, New York Life, Trane Technologies, Spotify, Swiss Re, and other organizations. In addition, there were former senior officials from the Treasury Department and Capitol Hill. The Conference featured a series of interactive panel discussions on significant tax developments, including a real-time update and analysis of the Biden tax legislation.

Panel topics included:

- Ethics
- Legislative developments
- Corporate tax/Financial products
- Transfer pricing
- International tax
- State and local taxation
- Cryptocurrency and Blockchain
- Tax controversy
- Private Clients, Trusts & Estates, Exempt Organization

To view conference handouts, click the links below.

- TAX POLICY HANDOUT
- PRIVATE CLIENT HANDOUT
- CORPORATE PHILANTHROPY HANDOUT
- AN INTRODUCTION TO COMPANY FOUNDATIONS

IRS ISSUES CLARIFYING GUIDANCE ON RESEARCH CREDIT CLAIM REQUIREMENTS

On January 5, 2022, the IRS issued Interim Guidance LB&I-04-0122-0001 and Frequently Asked Questions to address the implementation of Chief Counsel Memorandum 20214101F (CCM) regarding section 41 research credit refund claims.

As described in our November newsletter, Chief Counsel Memorandum 20214101F imposes onerous new requirements for section 41 research credit refund claims.

The newly issued guidance provides some detail as to how to comply with the CCM; however, several questions raised by the CCM remain unanswered.

The Interim Guidance revises the procedures in the Internal Revenue Manual for determining whether a research credit claim is valid. The Interim Guidance clarifies how to provide the "five items of information" that the CCM requires. These five items of information required on research credit refund claims are as follows:

(1) All business components to which the Section 41 research credit claim relates for that year.

(2) For each business component, identify all research activities performed and (3) name the individuals who performed each research activity, (4) as well as the information each individual sought to discover.

(5) The total qualified employee wage expenses, total qualified supply expenses, and total qualified contract research expenses for the claim year.

BUSINESS COMPONENT-LEVEL IDENTIFICATION

For the third and fourth requirements, the Interim Guidance clarifies that the identification of all individuals who performed each research activity may be provided in a list, table, or narrative form, but the claim must include either the first and last name or the title or position of the person and identify the person by business component. Additionally, the claim must identify the information each individual sought to discover. The FAQs further allow for aggregation of a group of individuals who all sought to discover the same information for a business component and listing of those employees by title or position.

While this guidance may relax the CCM's specificity requirements from the CCM, businesses typically do not keep records of employees' activities in this manner. A business component is "any product, process,

computer software, technique, formula, or invention, which is to be held for sale, lease, license, or used in a trade or business of the taxpayer."[1] An entity rarely keeps time records at the "product" or "process" level. Furthermore, for businesses that incur contract research expenses,[2] the taxpayer's contractor may not be able to provide records to the taxpayer at the "business component" level, preventing the taxpayer from claiming the research credit for such activity.

STATISTICAL SAMPLING

Despite the specificity of the "five items of information", FAQ 15 provides, with little elaboration, that taxpayers may use statistical sampling in accordance with the applicable Revenue Procedure. Rev. Proc. 2011-42 does not provide for the use of statistical sampling on a return. Instead, it provides criteria that must be met if the IRS is to accept statistical sampling "as adequate substantiation for a return position." Taxpayers often negotiate the use of statistical sampling with the IRS during an exam. Indeed, Rev. Proc. 2011-42 states that whether statistical sampling is appropriate "is a facts and circumstances determination." Whether statistical sampling is appropriate is frequently the subject of dispute with the IRS, usually involving dueling statisticians and sometimes resulting in litigation.[3]

The statistical sampling provision in FAQ 15 raises many questions. How does the taxpayer document that its sample is appropriate? Does the refund claim need to include the written sampling plan or calculation of the confidence limits? Should the claim include an affidavit about whether the sample is valid? If the IRS deems the claim deficient, will the deficiency letter explain why?

DEFICIENT CLAIMS

The Interim Guidance provides a transition period of January 10, 2022 through January 9, 2023 for implementation of the CCM requirements. During the transition period, taxpayers will be notified if the IRS deems the claim to be deficient and given the opportunity to cure. The Interim Guidance expands the cure period from 30 to 45 days. During the transition period, the IRS will issue Letter 6428, Claim for Credit for Increasing Research Credit Activities - Additional Information Required, in response to deficient claims, and the 45-day period to perfect the claim will run from the date of the letter. Information satisfying the five required items must be supplied within the 45-day period; otherwise, the IRS will issue Letter 6430, No Consideration, Section 41 Claim, to the taxpayer.

While this longer arbitrary cure period is an improvement, it still leaves the taxpayer with minimal time to catalog detailed information. The 45-day period begins when the IRS issues Letter 6428. But with current USPS delivery times, one to two weeks may elapse before the taxpayer receives the letter. If the taxpayer does not have the information assembled, it will be difficult to generate records broken down by business component and by employee within a month's time.

POST-TRANSITION PERIOD

For claims filed after January 9, 2023, if the examiner determines the claim is deficient, the IRS will issue Letter 6430 (No Consideration, Section 41 Claim). The Interim Guidance states that management and counsel must concur that the claim does not contain the five required items of information. The examiner is then directed to

[1] Section 41(d)(2)(B).
[2] *See* section 41(b)(3).
[3] *See Bayer Corp. v. United States,* 850 F. Supp. 2d 522 (W.D. Pa. 2012); *CRA Holdings US, Inc. v. United States,* 119 AFTR 2d 2017-577 (W.D.N.Y. 2017).

"not consider the claim issues or include claim language in a report."

What redress will taxpayers have for claims that are deemed deficient? The Interim Guidance does not state that Letter 6430 will provide reasons why the claim was deemed deficient. Can the taxpayer simply file another refund claim, assuming the statute is open?

The Interim Guidance does not address the strategy contained in the CCM for the IRS to delay processing of refund claims until after the statute of limitations has expired to prevent taxpayers from curing imperfect claims. The Interim Guidance states only that examiners should determine whether a claim is valid within 30 days after the receiving the claim. FAQ 5 avers that "[t]he IRS will make every attempt to review Research Credit refund claims as expeditiously as possible and make determinations on such claims within 6 months of receipt." Given the IRS's current claim processing backlog and the lack of recourse for late processing of these claims, it seems doubtful that the IRS will adhere to this promised timeline. Coupled with the CCM's assertion that taxpayers cannot seek judicial review when the IRS determines a refund claim to be deficient, it is unclear whether taxpayers will ever be able to challenge a claim once the IRS deems it deficient. The American Bar Association Section of Taxation raised this issue (among others) in a comment letter submitted in response to the CCM.[4]

AVENUES FOR CHALLENGING THE CCM

The CCM articulates new requirements that research credit refund claims must meet or the IRS will summarily deny them. These requirements are not included in any regulations, including those issued under section 41 or Treas. Reg. § 301.6402-2. In fact, the rules contained in the CCM were not issued subject to the notice-and-comment procedures under the Administrative Procedure Act (APA).[5] Generally, "a rule that 'intends to create new law, rights or duties' is [a] legislative" rule that must be issued through the notice and comment procedures of the APA.[6] For example, a listing notice was held to "likely constitute[] a legislative rule because it expands the footprint of 26 C.F.R. § 1.6011-4(b) by creating new rights and duties regarding reporting requirements…."[7] On its face, the CCM appears to be a legislative rule because it imposes new duties on taxpayers regarding the information that must be included in refund claims and alters taxpayers' rights to cure imperfect claims.

> The Supreme Court's *CIC Services* opinion may pave the way for a pre-enforcement challenge to the CCM.

Litigants have brought similar APA challenges to IRS rulemaking and those challenges have

[4] https://www.americanbar.org/content/dam/aba/administrative/taxation/policy/2022/010622comments.pdf.
[5] *See* 5 U.S.C. § 553.
[6] *Tenn. Hosp. Ass'n v. Azar,* 908 F.3d 1029, 1042 (6th Cir. 2018) (quoting *Michigan v. Thomas,* 805 F.2d 176, 182-83 (6th Cir. 1986)).
[7] *CIC Services., LLC v. Internal Revenue Serv.*, No. 3:17-CV-110, 2021 WL 4481008, at *5 (E.D. Tenn. Sept. 21, 2021).

thus far survived jurisdictional challenges. In *CIC Services,* a material advisor brought suit challenging a disclosure requirement that it asserted was unduly burdensome and would force it to incur significant costs.[8] CIC Services asserted the listing notice that created the disclosure requirement was invalid under the APA because the IRS issued it without following any notice-and-comment procedures. The Supreme Court rejected the IRS's jurisdictional challenge under the Anti-Injunction Act (AIA). [9]Likewise, the DC Circuit allowed a challenge to excise tax refund claim procedures despite similar jurisdictional objections by the government under the APA.[10] The court found that notice to be invalid for failing to meet the notice-and-comment requirements under the APA.[11] These decisions may indicate a roadmap for challenging the burdensome requirements of the CCM, which appears to result from similarly deficient agency action.

Caitlin R. Tharp

[8] *CIC Services, LLC v. Internal Revenue Serv.*, 141 S. Ct. 1582 (2021).
[9] *Id. at 1588-89*.
[10] *Cohen v. United States,* 650 F.3d 717, 725 (D.C. Cir. 2011).
[11] *In re Long-Distance Tel. Serv. Fed. Excise Tax Refund Litig.*, 853 F. Supp. 2d 138, 140 (D.D.C. 2012), *aff'd*, 751 F.3d 629 (D.C. Cir. 2014).

IRS TO INCREASE JOHN DOE SUMMONSES FOR CRYPTOCURRENCY TAX ENFORCEMENT IN 2022

Speaking at tax conferences in December 2021, two IRS officials stated the IRS will continue to use John Doe summonses to obtain the identity of taxpayers who fail to report cryptocurrency transactions.

At the American Bar Association Section of Taxation conference, Steve Dyson of the IRS's Office of Fraud Enforcement stated, "I think we're going to see an increase in John Doe summonses activity."

FEDERAL COURTS HAVE AUTHORIZED JOHN DOE SUMMONSES ON CRYPTOCURRENCY EXCHANGES

The IRS uses a John Doe summons when it suspects the existence of fraud, but does not know the name of a taxpayer or group of taxpayers whose records are sought. These summonses allow the IRS to obtain the names, information, and documents relating to all taxpayers in a specific group.[12] The government must obtain court approval before issuing a John Doe summons.[13] To obtain a court order enforcing a John Doe summons, the IRS must first establish "good faith" by showing that the summons: (1) is issued for a legitimate purpose; (2) seeks information relevant to that purpose; (3) seeks information that is not already in the IRS's possession; and (4) satisfies all of the administrative steps set forth in the Internal Revenue Code.[14]

Last year, the IRS Office of Fraud Enforcement launched "Operation Hidden Treasure" to investigate potential fraud in cryptocurrency transactions. And in that investigation, federal courts authorized the issuance of John Doe summonses for information on a group of customers on the cryptocurrency exchanges Circle[15] and Kraken.[16] In a press release on the Kraken investigation, IRS Commissioner Chuck Rettig stated, "[t]his John Doe summons is part of our effort to uncover those who are trying to skirt reporting and avoid paying their fair share."[17] In the summonses, the IRS sought to identify taxpayers with accounts of at least $20,000 of cryptocurrency transactions in any one year

[12] 26 U.S.C. § 7609(f); *See also United States v. Bisceglia*, 420 U.S. 141 (1975).
[13] 26 U.S.C. § 7609(f).
[14] *United States v. Powell,* 379 U.S. 48, 57-58 (1964) ("The government's burden is a slight one, and may be satisfied by a declaration from the investigating agent that the *Powell* requirements have been met").
[15] *In the Matter of Tax Liabilities of John Does*, 127 A.F.T.R.2d 2021-1545 (D. Mass. 2021).
[16] *In the Matter of Tax Liabilities of John Does*, 127 A.F.T.R. 2d 2021-1456 (N.D. Cal. 2021).
[17] Press Release, US Department of Justice, Court Authorizes Service of John Doe Summons Seeking Identities of U.S. Taxpayers Who Have Used Cryptocurrency (May 5, 2021), *available at* https://www.justice.gov/opa/pr/court-authorizes-service-john-doe-summons-seeking-identities-us-taxpayers-who-have-used-1

and sought documents in six areas: account registration records, Know-Your-Customer due diligence, account-related correspondence, anti-money laundering exception reports, account activity records, and account funding records.

In the summons related to Circle, the Massachusetts District Court found the IRS met the requirements for the issuance of the John Doe summons. But in the Kraken case, the District Court for the Northern District of California required the IRS to "show cause" and narrow their request before ultimately granting the summons.[18] The Northern California District Court had previously ordered the enforcement of a John Doe summons in 2017 on the cryptocurrency exchange Coinbase to investigate tax noncompliance.[19]

PRO-ACTIVE VOLUNTARY DISCLOSURES TO THE IRS CAN LIMIT CRIMINAL TAX INVESTIGATIONS

The threat of more frequent and expansive John Doe summonses raises the specter of criminal consequences for taxpayers who do not report cryptocurrency income. If a taxpayer willfully fails to report income from a cryptocurrency transaction, the taxpayer may face criminal charges. But taxpayers may avoid criminal consequences if they make a timely voluntary disclosure to the IRS.

Under the IRS's Voluntary Disclosure practice, a taxpayer can voluntarily report previously undisclosed income by filing an amended or delinquent return. A voluntary disclosure is timely if the IRS receives it before the IRS discovers the information through some other means (like receiving information from a third-party via a John Doe summons).[20] According to the IRS, voluntary disclosure may enable taxpayers to resolve non-compliance and limit exposure to criminal prosecution.[21]

Taxpayers are required to submit Form 14457 to the IRS when considering making a voluntary disclosure, which requires preclearance from the IRS Criminal Investigation division before submitting the voluntary disclosure and filing amended tax returns.

> Although it offered one for foreign-bank-account reporting, The IRS is not yet contemplating a voluntary disclosure program for non-compliance involving virtual currency.

Initiating a voluntary disclosure may be advantageous because it can provide a certain level of penalty certainty. If unsure about cryptocurrency questions, counsel should be retained to ensure the voluntary disclosure process is the proper option.

Nick Sutter

[18] *In the Matter of Tax Liabilities of John Does,* 127 A.F.T.R. 2d 2021-1456 (N.D. Cal. 2021)
[19] *United States v. Coinbase, Inc.,* 120 A.F.T.R.2d 2017-6671 (N.D. Cal. 2017).
[20] *See* Internal Revenue Service, *IRS Criminal Investigation Voluntary Disclosure Practice* (August 2021) *available at* https://www.irs.gov/compliance/criminal-investigation/irs-criminal-investigation-voluntary-disclosure-practice.
[21] *Id.*

ELEVENTH CIRCUIT INVALIDATES TREASURY REGULATION UNDER APA

On December 29, 2021, the Eleventh Circuit reversed a Tax Court's order disallowing taxpayers' carryover deduction for the donation of a conservation easement.

In *Hewitt v. Commissioner,* the Eleventh Circuit concluded that the Commissioner's interpretation of Treasury Regulation § 1.170A-14(g)(6)(ii) was arbitrary and capricious, and the regulation violated the Administrative Procedure Act's (APA) procedural requirements because it failed to respond to significant comments about the provision on post-donation improvements. [22] The court remanded the case for further proceedings.

BACKGROUND

On June 17, 2020, the Tax Court issued a memorandum opinion determining that the Hewitts were not entitled to the charitable contribution deduction for the donation of the Easement. The Tax Court explained that Treas. Reg. § 1.170A-14(g)(6) "does not permit the value of post easement improvements to be subtracted from the proceeds before determining the donee's share." The Tax Court also rejected the Hewitts' challenge to Treas. Reg. § 1.170A-14(g)(6)(ii)'s procedural and substantive validity.

THE APA AND TREAS. REG. § 1.170A-14

The APA "prescribes a three-step procedure for so-called 'notice-and-comment rulemaking.'"[23] First, an agency "must issue a '[g]eneral notice of proposed rulemaking,' ordinarily by publication in the Federal Register."[24] Second, "if 'notice [is] required,' the agency must 'give interested persons an opportunity to participate in the rule making through submission of written data, views, or arguments,'" and the agency "must consider and respond to significant comments received during the period for public comment."[25] Third, in promulgating the final rule, the agency "must include in the rule's text 'a concise general statement of [its] basis and purpose.'"[26] The taxpayers argued that Treas. Reg. § 1.170A-14(g)(6) was issued in violation of the APA three-step procedure.

In 1986, Treasury issued final Treas. Reg. § 1.170A-14(g)(6)—governing the allocation of proceeds between the donor and donee. Treas. Reg. § 1.170A-14(g)(6) provides for some complex rules that govern whether the donor has truly donated an easement. Under those rules, there is not a donation unless the transaction "gives rise to a property right, immediately vested in the donee

[22] __ F.4th __, 2021 WL 6133999 (11th Cir. Dec. 29, 2021).
[23] *Perez v. Mortg. Bankers Ass'n,* 575 U.S. 92, 96 (2015); *accord* 5 U.S.C. § 553.
[24] *Perez*, 575 U.S. at 96 (alteration in original) (quoting § 553(b)).
[25] *Id.* (quoting § 553(c)).
[26] *Id.* (quoting § 553(c)).

organization, with a fair market value that is at least equal to the proportionate value that the perpetual conservation restriction at the time of the gift, bears to the value of the property as a whole at that time...." Those rules prescribe that if the easement is later extinguished, then the donee "must be entitled to a portion of the proceeds at least equal to that proportionate value of the perpetual conservation restriction." Courts later held that these rules precluded the donor from recovering the entirety of any post-donation improvements.

The IRS determined that an "improvement clause" in the taxpayers' easement deed violated these rules. The taxpayers claimed that Treasury failed to comply with the procedural requirements of the APA in promulgating Treas. Reg. § 1.170A-14(g)(6)(ii) because Treasury failed to adequately respond to significant comments in the final regulation's "basis and purpose" statement. They asserted that Treas. Reg. § 1.170A-14(g)(6)(ii), as interpreted by the Commissioner, was arbitrary and capricious under the APA.

ANALYSIS

The Eleventh Circuit noted that following Treasury's request for public comments to Treas. Reg. § 1.170A-14(g)(6), it received more than 700 pages of commentary from ninety organizations and individuals. In the most detailed comments, the New York Landmarks Conservancy (NYLC) urged Treasury to delete the proposed proceeds regulation because it contained pervasive "problems of policy and practical application." The Landmarks Preservation Council of Illinois, The Trust for Public Land, the Nature Conservancy, and the Maine Coast Heritage Trust raised similar concerns about Treas. Reg. § 1.170A-14(g)(6). After a public hearing, Treasury adopted the proposed regulations with revisions. Treasury did not, however, discuss or respond to the comments made by NYLC or by the others about the extinguishment proceeds regulation. Thus, the issue before the Eleventh Circuit was whether Treasury violated the APA when it failed to respond to those comments.

> The Circuit Court concluded after careful consideration of the agency record that Treas. Reg § 1.170A-14(g)(6)(ii) was arbitrary and capricious under the APA for failing to comply with the APA's procedural requirements and is thus invalid.[27]

The Circuit Court found that NYLC's comments were significant ("NYLC challenged a fundamental premise underlying Treasury's proposed regulation") and thus

[27] The Court cited to *Lloyd Noland Hosp. v. Heckler,* 762 F.2d 1562 (11th Cir. 1985) as instructive. In that case, the plaintiffs challenged a malpractice insurance rule related to Medicare reimbursements that was promulgated by the Secretary of Health and Human Services. *Id.* at 1563. In addressing the plaintiffs' challenge, the court concluded that the malpractice insurance rule was procedurally inadequate under the APA; specifically, it violated § 553(c), which requires an agency "to incorporate into a new rule a concise general statement of its basis and purpose." *Id.* at 1566. The Secretary had failed to respond to comments that a study the agency relied on, which contained limited data that the authors cautioned against generalizing, was unreliable. *Id.*

required a response from Treasury. Treasury's mere statement that it had considered "all comments" without more discussion was insufficient. The Eleventh Circuit held that the Commissioner did not "enable [us] to see [NYLC's] objections and why [Treasury] reacted to them as it did."[28]

The ruling is not a model of clarity. It is ambiguous as to whether the Eleventh Circuit invalidated the regulation or the Commissioner's interpretation of the regulation. It is unlikely that this is the final word on the subject. There is litigation currently pending in the Sixth Circuit on the issue.[29] Moreover, the Tax Court is bound by this decision only in the Eleventh Circuit[30] and may reaffirm its opinion in subsequent cases. In any event, the opinion is a big setback for the IRS in its mission to shut down conservation easement transactions.

Richard A. Nessler

[28] __ F.4th __, 2021 WL 6133999, at *36 (11th Cir. Dec. 29, 2021) (citing *Lloyd Noland*, 762 F.2d at 1566).
[29] *See Oakbrook Land Holdings LLC v. Commissioner*, T.C. Memo. 2020-54, *appeal docketed*, No. 20-11251 (11th Cir. April 14, 2021).
[30] *See Golsen v. Commissioner,* 54 T.C. 742 (1970), *aff'd* 445 F.2d 985 (10th Cir. 1971).

LEGISLATIVE CHANGES AFFECTING TAX CONTROVERSY IN THE BUILD BACK BETTER ACT

President Biden's top domestic policy legislation, the Build Back Better Act (BBB Act), includes significant funding increases for programs across the federal government that is paid for through a number of individual, corporate, and international tax changes to raise new revenue to offset the cost of the bill.

The BBB Act focuses on addressing the "tax gap" and tax compliance to raise revenue. The legislation increases funding for the IRS and makes procedural changes related to the IRS's approval of tax penalties.

The BBB Act passed the House of Representatives in November 2021, but has since stalled in the Senate due to opposition from both Senator Joe Manchin (D-WV) and Senator Kyrsten Sinema (D-AZ).

On December 11, 2021, the Senate Finance Committee released an updated draft version of the BBB Act. That version retained the tax controversy provisions that passed the House and are described below. Congress and the Biden Administration are expected to continue working on scaled-back compromise legislation to gain the support of Senators Manchin and Sinema.

The BBB Act would provide $80 billion in additional mandatory funding for the IRS over the next 10 years, with $45.6 billion allocated for enforcement, $25.3 billion for operations support, $4.7 billion for systems modernization, and $3.1 billion for taxpayer services.[31]

ADDITIONAL IRS FUNDING FOR TAX ENFORCEMENT

In a letter to the Senate Budget Committee, the Congressional Budget Office estimated funding for tax enforcement would raise an

[31] Section 128401, Senate Finance Committee Proposed Amendment (December 11, 2021).

additional $207 billion in revenue for the federal government over the next 10 years.[32]

MODIFICATION OF IRS PROCEDURAL REQUIREMENTS FOR PENALTY ASSESSMENTS

The BBB Act would retroactively repeal section 6751(b)(1), which requires IRS agents to obtain written approval from their immediate supervisor prior to an initial determination to impose any tax penalty.[33]

Congress added this supervisory approval requirement in 1998 as part of the Internal Revenue Service Restructuring and Reform Act. Under that section, any initial determination of a tax penalty requires written approval from the IRS agent's immediate supervisor.

In 2013, the Treasury Inspector General for Tax Administration (TIGTA) issued a report that stated the IRS was not complying with the requirements of section 6571(b).[34] In recent years, section 6571(b) has been heavily litigated and the IRS has often lost in court for failure to comply with the statutory requirements.[35]

The House-passed version of the BBB Act would repeal section 6751(b) retroactive to the provisions enactment in the Internal Revenue Service Restructuring and Reform Act of 1998 (P.L. 105-206). With that repeal, IRS supervisors would not be required to obtain written approval. In its place, the proposal mandates that appropriate IRS supervisors certify quarterly to the Commissioner that the penalty notices issued by their employees comply with the statutory requirements of section 6751(a) and administrative policies intended to ensure voluntary compliance.

The Joint Committee on Taxation estimates the repeal of section 6751(b) will raise $1.4 billion in new revenue for the federal government over the next 10 years.[36]

ANALYSIS

Funding increases for the IRS should raise the likelihood of audits for high-income and high-wealth individuals, large corporations, and partnerships. Congress added section 6751 to prevent the IRS from adding penalties as a way to force taxpayers to concede or back down. The retroactive repeal of the section 6571(b) procedural requirements would absolve the IRS for past failures to obtain written supervisory approval, which may in turn embolden the IRS to use penalties as a bargaining chip.

Nick Sutter

[32] Letter for Lindsay Graham, Ranking Member, Committee on the Budget, U.S. Senate, from Phillip Swagel, Director, Congressional Budget Office (November 21, 2021), https://www.cbo.gov/system/files/2021-11/57620-IRS.pdf.
[33] Section 128403, Senate Finance Committee Proposed Amendment (December 11, 2021).
[34] Treasury Inspector General for Tax Administration, *Improvements Are Needed in Assessing and Enforcing Internal Revenue Code Section 6694 Paid Preparer Penalties* (September 9, 2013), https://www.treasury.gov/tigta/auditreports/2013reports/201330075fr.html.
[35] *See, e.g. Graev v. Commissioner* (Graev II), 147 T.C. 460 (2016); *Chai v. Commissioner*, 851 F.3d 190 (2d Cir. 2017); *Graev v. Commissioner* (Graev III), 149 T.C. 485 (2017).
[36] Staff of the Joint Committee on Taxation, *JCX-45-21: Estimated Budget Effects Of The Revenue Provisions Of Title XIII – Committee On Ways And Means, Of H.R. 5376, The "Build Back Better Act," As Reported By The Committee On The Budget, With Modifications (Rules Committee Print 117-18)* (November 4, 2021).

IRS ANNOUNCES CIVIL EXAMINATION PRIORITIES FOR 2022

Speaking at the American Bar Association's Criminal Tax Fraud/Tax Controversy Conference in December 2021, De Lon Harris, Commissioner of Examinations in the IRS Small Business/Self Employed Division, announced the IRS's examination priorities for 2022. They include a focus on Bank Secrecy Act violations, virtual currency, and a special enforcement program.

The IRS announced this expanded list of examination priorities in anticipation of increased funding provided by Congress for Fiscal Year 2022 and later years. For Fiscal Year 2022, the House-passed Financial Services and General Government appropriations bill would provide the IRS with $13.6 billion.[37] In addition, the Build Back Better Act would also provide $80 billion in additional mandatory funding to the IRS over the next 10 years.[38]

Virtual currency and cryptocurrency transactions are expected to be a focus of the IRS for 2022.

The Infrastructure Investment and Jobs Act that Congress signed into law in November includes new cryptocurrency reporting requirements.[39]

The ten examination areas that Harris highlighted as IRS priorities in 2022 are:

- High-net-worth and high-income non-filers
- Global high wealth individuals
- Large passthrough entities
- Large corporate compliance
- Employment tax
- Transfer pricing
- Non-filer virtual currency
- Bank Secrecy Act
- Abusive transaction promoters
- Special enforcement program

In addition to these listed priorities, the IRS is also expected to continue focusing on micro-captive insurance arrangements and syndicated conservation easements. About these

[37] H.R. Rep. No. 117-79 for H.R. 4345, Financial Services and General Government Appropriations Bill, 2022 at 27 (2021) *available at* https://www.congress.gov/117/crpt/hrpt79/CRPT-117hrpt79.pdf.
[38] Section 128401, Senate Finance Committee Proposed Amendment (December 11, 2021) *available at* https://www.finance.senate.gov/imo/media/doc/12.11.21%20Finance%20Text.pdf.
[39] Section 80603, Infrastructure Investment and Jobs Act, P.L. 117-58 (2021).

transactions, Harris noted, "These are things we've been looking at for a period of time, and we are not letting up in those areas." Last year, the IRS urged participants in abusive micro-captive insurance arrangements to exit these transactions as soon as possible.[40]

Nick Sutter

[40] Press Release, Internal Revenue Service, IRS urges participants of abusive micro-captive insurance arrangements to exit from arrangements (April 9, 2021) *available at* https://www.irs.gov/newsroom/irs-urges-participants-of-abusive-micro-captive-insurance-arrangements-to-exit-from-arrangements.

IRS ANNOUNCES NEW FAST TRACK LETTER RULING PROCEDURES

On January 14, 2022, the IRS issued Rev. Proc. 2022-10, which implements a new18-month pilot program that allows taxpayers to request fast-track processing for letter ruling requests.

Eligible requests for letter rulings must fall within the jurisdiction of the IRS Office of Associate Chief Counsel (Corporate). The pilot program's goal is to provide the letter ruling within 12 weeks.

SUBMISSION REQUIREMENTS

To request fast-track processing, the taxpayer must first request a pre-submission conference with the IRS. Before the pre-submission conference, the taxpayer must provide the same general information required for a letter-ruling request under section 10.07(3) of Rev. Proc. 2022-1. Additionally, the taxpayer must provide a statement setting forth the reasons for requesting fast-track processing, the length of the specified period the taxpayer requests (if other than 12 weeks), any matters that could affect the feasibility of fast-track processing, and any issues under the jurisdiction of an Associate office other than the Associate Chief Counsel (Corporate) relevant to the transaction.

In the pre-submission conference, the taxpayer should be prepared to address both the substantive issues and the taxpayer's request for fast-track processing.

The requester must also show that fast-track processing is feasible. In making the determination of whether fast-track processing is feasible, the branch reviewer will consider the following:

(a) All the facts, representations, and circumstances, including the complexity of the proposed transactions, the issues presented, and other obligations of the attorneys assigned to process the request;

(b) Whether the letter ruling request fully and clearly describes and analyzes the relevant facts and issues;

(c) Whether the draft letter ruling satisfies the requirements set forth in section 4.03 of this revenue procedure;

(d) The taxpayer's need for fast-track processing, and

(e) Any concerns communicated by another Associate office.

The branch reviewer will also consider the need for cooperation between the Office of Associate Chief Counsel (Corporate) and other associate offices. If a request also seeks rulings within the jurisdiction of other associate offices, those other offices must agree to fast-track processing.

The taxpayer must also provide a proposed draft of the requested letter ruling.

Upon request, the Service will agree to a specified period shorter than 12 weeks if the branch reviewer determines that the taxpayer has a real business need to obtain a letter ruling within that specified period, and that processing is feasible. The following facts alone do not demonstrate a need for a

specified period shorter than 12 weeks: (i) the scheduling of a closing date for a transaction, a meeting of a board of directors or shareholders of a corporation, or any other corporate action within the control of the taxpayer or other parties to the transaction, or (ii) the possible effect of fluctuation in the market price of stocks on a transaction.

No later than seven business days after the day the letter ruling request is received by the branch representative and branch reviewer, the branch representative or branch reviewer will contact the taxpayer to (i) acknowledge receipt of the letter ruling request, (ii) provide contact information for the branch representative and branch reviewer, and (iii) notify the taxpayer that the request for fast-track processing is granted, denied, or still pending. If the request is granted, the branch representative or branch reviewer will inform the taxpayer of the length of the specified period and the date the specified period will end. If the request is denied, the branch representative or branch reviewer will explain the reasons for the denial.

The pilot program for fast-track processing replaces the expedited handling request procedures for eligible letter ruling requests. Accordingly, expedited handling under Rev. Proc. 2022-1 is not available for requests that are eligible under the new program.

FAST-TRACK VS. EXPEDITED

Rev. Proc. 2022-10 carves out one major exception to the fast-track pilot program: "Fast-track processing is not available for requests for extension of time to make elections or other applications for relief under section 301.9100 of the Procedure and Administration Regulations (26 CFR part 301) (section 9100 relief)." Those requests may, however, seek expedited handling under Rev. Proc. 2022-1.

PILOT PROGRAM TERM

The pilot program applies to all letter ruling requests postmarked or, if not mailed, received by the Service after January 14, 2022. The program will extend through July 14, 2023. Taxpayers with letter ruling requests already pending on January 14 may seek fast-track processing under Rev. Proc. 2022-10 by agreeing to follow the pilot program procedures. No pre-submission conference is required.

Richard A. Nessler

ABOUT STEPTOE'S TAX CONTROVERSY PRACTICE

Steptoe's Tax Controversy Group combines trial-tested litigation skills with up-to-date substantive tax experience.

The team includes experienced litigators who have served as Justice Department trial and appellate attorneys, judicial law clerks, and Treasury officials. This combination enables us to take on the most challenging cases and achieve outstanding results for our clients. Over their careers, our lawyers have litigated cases on a wide variety of federal and international tax issues, including transfer pricing, foreign tax credits, insurance taxation, various tax incentives such as research credits, and other substantive and procedural issues.

Our lawyers have proven skills and extensive experience in all aspects of tax controversy and litigation, including managing IRS audits, filing and presenting protests to IRS Appeals, negotiating litigation settlements, trying cases, and arguing appeals.

Our active controversy and litigation docket keeps us at the cutting edge of evolving administrative and judicial practice and procedures, strategy, and tactics.

Steptoe also represents clients with respect to international tax controversy matters before the IRS, Treasury, Congress, and foreign tax authorities. Our tax controversy lawyers have proven experience at the IRS and in court across a broad range of subjects.

For more informsion on Steptoe's Tax Controversy practice, click here.

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ABOUT STEPTOE'S TAX PRACTICE

The tax practice at Steptoe brings clients decades of advisory, transactional, and advocacy experience in federal and state taxation.

Clients rely on us for practical and creative solutions to issues that span the spectrum of tax law through all stages of the business lifecycle.

- Tax Controversies & Litigation
- Tax Policy
- International Tax
- Private Client
- Trusts & Estates
- Transactional Tax
- State & Local Tax
- Employee Benefits & Executive Compensation
- Insurance Tax
- Exempt Organizations

Our team includes an extraordinary group of professionals, including former senior government officials from Congressional offices, the IRS, Treasury, and Justice Department, who have vast experience in sophisticated tax planning, audit, and controversy work. Our clients include some of the world's largest corporations and tax-exempt organizations, as well as high-net-worth individuals. And we advise them with respect to their most important tax matters.

Our strength is our effective advocacy for our clients. We represent clients before the IRS, the Treasury Department, the courts, and in Congress, as well as before foreign tax authorities, for example through competent authority proceedings. We advise clients on the tax aspects of mergers, acquisitions, joint ventures, financings, and investment arrangements and draw on our deep understanding of corporate, partnership, and international tax, as well as our extensive experience in evolving judicial practice and procedures, strategy, and tactics.

Our lawyers contribute to developing the field of tax law. We regularly speak on important tax subjects, teach in educational institutions, author texts and articles on tax subjects, and participate in leadership roles in tax professional organizations.

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In more than 100 years of practice, Steptoe has earned an international reputation for vigorous representation of clients before governmental agencies, successful advocacy in litigation and arbitration, and creative and practical advice in structuring business transactions. Steptoe has more than 500 lawyers and other professional staff across offices in Beijing, Brussels, Chicago, Hong Kong, London, Los Angeles, New York, San Francisco, and Washington.

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