

## Part III

### Administrative, Procedural, and Miscellaneous

26 CFR 601.105: Examination of returns and claims for refund, credit, or abatement; determination of correct tax liability.

(Also Part I, §§ 446, 481, 6213, 6405, 6621, 7121, 7123, 7430; 1.446-1, 1.481-1, 1.481-2, 1.481-4, 301.6213-1, 301.6405-1, 301.6621-1, 301.7121-1, 301.7430-1.)

## **Rev. Proc. 99-28**

### **TABLE OF CONTENTS**

#### **SECTION 1. PURPOSE AND BACKGROUND**

#### **SECTION 2. EXAMINATION EARLY REFERRAL PROCEDURES**

- .01 In general
- .02 Appropriate issues for early referral
- .03 Issues excluded from early referral
- .04 Initiating the early referral request
- .05 Statement of issues and position
- .06 Perjury statement
- .07 Signatures
- .08 Notification of action
- .09 Appeal of denial of early referral request
- .10 Administrative appeal at a later time
- .11 Issuance of notice of proposed adjustment or explanation of adjustment
- .12 Taxpayer response to Notification Form
- .13 Early referral file sent to Appeals
- .14 Resolving the early referral issue
- .15 Agreement reached
- .16 Agreement not reached
- .17 Effect of conclusion of examination
- .18 Appeals consideration after 30-day letter
- .19 Withdrawal from the early referral process

#### **SECTION 3. INTERNAL REVENUE SERVICE INITIATED CHANGE IN METHOD OF ACCOUNTING EARLY REFERRAL PROCEDURES**

- .01 In general
- .02 Appropriate issues for early referral

#### **SECTION 4. EMPLOYMENT TAX EARLY REFERRAL PROCEDURES**

- .01 Background
- .02 In general
- .03 Appropriate issues for early referral
- .04 Issuance of employment tax report
- .05 Agreement reached
- .06 Agreement not reached

#### **SECTION 5. COLLECTION EARLY REFERRAL PROCEDURES**

- .01 In general
- .02 Appropriate issues for early referral

#### **SECTION 6. EMPLOYEE PLANS/EXEMPT ORGANIZATIONS (EP/EO) EARLY REFERRAL PROCEDURES**

- .01 In general
- .02 Employee Plans issues excluded from early referral
- .03 Exempt Organizations issues excluded from early referral

#### **SECTION 7. NO USER FEE**

#### **SECTION 8. EFFECT ON OTHER DOCUMENTS**

#### **SECTION 9. EFFECTIVE DATE**

## SECTION 1. PURPOSE AND BACKGROUND

This revenue procedure describes the method by which a taxpayer may request an early referral of one or more unresolved issues from the Examination or Collection Division to the Office of Appeals (Appeals). Section 7123 of the Internal Revenue Code (IRC), as added by § 3465 of the Internal Revenue Service Restructuring and Reform Act of 1998, Pub L. No. 105-206, 112 Stat. 685, provides that the Secretary shall prescribe procedures by which any taxpayer may request such an early referral. Early referral is a process to resolve cases more expeditiously through the District and Appeals working simultaneously. This process is optional and may be requested by any taxpayer. This revenue procedure also describes the method by which a taxpayer may request early referral of one or more unagreed issues with respect to an involuntary change in method of accounting, employment tax, employee plans, or exempt organizations.

## SECTION 2. EXAMINATION EARLY REFERRAL PROCEDURES

**.01 In general.** Except as provided in section 2.03 of this revenue procedure, a taxpayer may request early referral to Appeals of any developed, unagreed issue under the jurisdiction of the District Director arising from an audit. The District will continue to develop issues that have not been referred to Appeals. This revenue procedure does not alter the District Director's authority to audit the returns of a taxpayer as to other issues nor limit or expand the District Director's authority to resolve any other issues, including the authority in Delegation Order No. 236 (Rev. 3).

**.02 Appropriate issues for early referral.** Appropriate issues for early referral are limited to those that:

- (1) if resolved, can reasonably be expected to result in a quicker resolution of the entire case;
- (2) both the taxpayer and the District agree should be referred to Appeals early;
- (3) are fully developed; and
- (4) are part of a case where the remaining issues are not expected to be completed before Appeals could resolve the early referral issue.

Industry Specialization Program (ISP) issues can also be referred to Appeals for early resolution under these early referral procedures. ISP issues are listed in Exhibit 8.7.1-1 of the Internal Revenue Manual. For specific procedures for the early referral of issues arising during the examination of the tax-exempt status of a bond issue, see Notice 98-58, 1998-49 I.R.B. 13.

**.03 Issues excluded from early referral.** Early referral does not include an issue:

- (1) with respect to which a 30-day letter has been issued. Thus, a qualified offer under § 7430(c), may not be made as part of the early referral process because such offers may only be made subsequent to the issuance of a 30-day letter;
- (2) that is not fully developed;
- (3) when the remaining issues in the case are expected to be completed before Appeals could resolve the early referral issue;
- (4) that is designated for litigation by the Office of Chief Counsel;
- (5) for which the taxpayer has filed a request for Competent Authority assistance, or issues for which the taxpayer intends to seek Competent Authority assistance. Taxpayers are encouraged to request the simultaneous Appeals/Competent Authority procedure described in section 8 of Rev. Proc. 96-13, 1996-1 C.B. 616, or a subsequent revenue procedure. If a taxpayer enters into a settlement with Appeals (including an Appeals settlement through the early referral process), and then requests Competent Authority assistance, the U.S. competent authority will endeavor only to obtain a correlative adjustment with the treaty country and will not take any actions that would otherwise amend the settlement. See section 7.05 of Rev. Proc. 96-13; or
- (6) that is part of a whipsaw transaction. (The term “whipsaw” refers to the situation produced when the government is subjected to conflicting claims of taxpayers. A potential whipsaw situation exists whenever there is a transaction between two parties and differing characteristics of transactions will benefit one and hurt the other for tax purposes.)

**.04 Initiating the early referral request.** A request for early referral must be submitted in writing by the taxpayer to the case/group manager. The case/group manager may suggest that a taxpayer make such a request.

**.05 Statement of issues and position.** The taxpayer’s early referral request must:

- (1) identify the taxpayer (and, where applicable, all related persons involved in the issues) and the tax periods to which those issues relate;
- (2) state each issue for which early referral is requested; and
- (3) describe the taxpayer's position with regard to the relevant early referral issues. This statement must contain a brief discussion of the material facts and an analysis of the facts and law as they apply to each early referral issue.

**.06 Perjury Statement.** The early referral request, and any supplemental submission (including additional documents), must include a declaration in the following form:

**Under penalties of perjury, I declare that I have examined this request [or submission], including accompanying documents, and to the best of my knowledge and belief, the facts presented are true, correct, and complete.**

This declaration must be signed by any person currently authorized to sign the taxpayer's federal income tax returns.

**.07 Signatures.** The early referral request must be signed by the taxpayer or the taxpayer's authorized representative. It is preferred that Form 2848, Power of Attorney and Declaration of Representative, be used to designate an authorized representative, with regard to an early referral request under this revenue procedure.

**.08 Notification of action.** The case/group manager will, where feasible, notify the taxpayer of the decision to accept or reject an issue in the early referral request within 14 days of receiving the request.

**.09 Appeal of denial of early referral request.** There is no formal taxpayer appeal if the early referral request is denied in whole or in part; however, the taxpayer can request a conference with the Internal Revenue Service supervisor of the case/group manager who denied the early referral request.

**.10 Administrative appeal at a later time.** If the case/group manager does not approve the early referral request with respect to any issue, the taxpayer retains the right to pursue the administrative appeal of any proposed deficiency related to that issue at a later time.

**.11 Issuance of notice of proposed adjustment or explanation of adjustment.** The District will complete a Form 5701, Notice of Proposed Adjustment, or an equivalent form (the Notification Form) for each early referral issue approved pursuant to this revenue procedure. The District will send the Notification Form to the taxpayer generally within 30 days from the date the early referral request was accepted. The Notification Form will describe the issue and explain the District's proposed adjustment. The issuance of the Notification Form for the early referral issue is not treated as the first letter of proposed deficiency for purposes of computing increased interest under § 6621(c), or for the award of administrative costs under § 7430(c).

**.12 Taxpayer response to Notification Form.** The taxpayer must respond in writing to each of the District's proposed adjustments set forth in the Notification Form. The response must contain an explanation of the taxpayer's position regarding the issues. The response shall be submitted to the case/group manager within 30 days (unless

extended by the case/group manager) from the date that the proposed adjustment (the Notification Form) is sent to the taxpayer. The procedural requirements of sections 2.06 and 2.07 of this revenue procedure (perjury statement and signatures) also apply to the taxpayer's response to the Notification Form. If a response is not received for any issue within the time provided, the taxpayer's early referral request will be considered withdrawn regarding that particular issue without prejudice to the taxpayer's right to an administrative appeal at a later date. See section 2.18 of this revenue procedure.

**.13 Early referral file sent to Appeals.** Once the taxpayer has responded to the Notification Form, the District will send the early referral file to Appeals. Appeals will then take jurisdiction over the issues accepted for early referral. All other issues in the case remain in the District's jurisdiction. The early referral file should include copies of:

- (1) applicable portions of tax returns and workpapers;
- (2) the approved early referral request;
- (3) the Notification Form;
- (4) the taxpayer's written response to the Notification Form;
- (5) the District's response to the taxpayer's position, if any; and
- (6) an estimate of the potential tax effect of the proposed adjustment.

**.14 Resolving the early referral issues.** The taxpayer's written response to the Notification Form generally serves the same purpose as an Appeals protest. Established Appeals procedures, including those governing submissions and taxpayer conferences, apply to early referral issues. See section 601.106 et seq. of the Statement of Procedural Rules.

**.15 Agreement reached.** If an agreement is reached with respect to an early referral issue generally, a Form 906, Closing Agreement on Final Determination Covering Specific Matters, is prepared. See § 7121 and also Rev. Proc. 68-16, 1968-1 C.B. 770, which describes the preparation of closing agreements. The closing agreement is used to compute the corrected tax as a partial agreement prior to or concurrently with the resolution of any other issues in the case. If an early referral issue results in a refund or credit requiring a report described in § 6405 that must be submitted to the Joint Committee on Taxation, the report must include a copy of the proposed closing agreement signed by or for the taxpayer, but not signed by or on behalf of the Commissioner. The Service will not sign the proposed agreement until after review by the Joint Committee.

**.16 Agreement not reached.** If early referral negotiations are unsuccessful and an agreement is not reached with respect to an early referral issue:

- (1) Taxpayers may then request mediation for the issue, provided the early referral issue meets the requirements for mediation. See Announcement 98-99, 1998-46 I.R.B. 34, or any subsequent procedure. If mediation is not requested, Appeals will close the early referral file and return jurisdiction over the issue to the District. Appeals will send a copy of the Appeals Case Memorandum for the issue to the case/ group manager.
- (2) Appeals will not reconsider an unagreed early referral issue if the entire case is later protested to Appeals, unless there has been a substantial change in the circumstances regarding the early referral issue.

**.17 Effect of conclusion of examination.**

- (1) If the District concludes its examination of any issues not referred as part of the early referral process, it will issue a preliminary notice of deficiency ("30-day letter") with respect to unagreed issues. The letter will include any issues referred under the early referral process that are still pending in Appeals at the time the examination is concluded. The issuance of the 30-day letter generally will constitute the first letter of proposed deficiency which allows the taxpayer an opportunity for administrative review for purposes of the increased underpayment rate of interest for large corporations as provided in § 6621(c), or for the award of administrative costs under § 7430(c).
- (2) If the only unagreed issues present in the case at the time the examination is concluded are issues that were considered by Appeals under the early referral process and returned to the District unagreed, no 30-day letter will be issued. Instead a statutory notice of deficiency ("90-day letter") will be issued. If a 90-day letter is issued instead of the 30-day letter, the 90-day letter will constitute the first letter of proposed deficiency for purposes of §§ 6621(c) and 7430(c).

**.18 Appeals consideration after 30-day letter.** If Appeals takes jurisdiction of the remaining issues in the case following the issuance of a 30-day letter, all issues including all early referral issues that have not yet been settled by Appeals will be considered under established Appeals procedures. The only exception is previously considered early referral issues described in section 2.16(2) of this revenue procedure. These issues will not be reconsidered.

**.19 Withdrawal from the early referral process.** If the taxpayer withdraws an early referral request with respect to one or more of the early referral issues after Appeals has taken jurisdiction over the issues, such withdrawal will be treated in the same manner as if no agreement of those early referral issues was reached. See section 2.16 of this revenue procedure. The withdrawal request must be communicated in writing to the Appeals Officer assigned the early referral.

### **SECTION 3. INTERNAL REVENUE SERVICE INITIATED CHANGE IN ACCOUNTING METHOD EARLY REFERRAL PROCEDURES**

**.01 In general.** The IRS published a proposed revenue procedure, Notice 98-31, 1998-22 I.R.B. 10, that outlines procedures under § 446(b) for changes in accounting methods initiated by the IRS. Although the early referral procedures in section 2 of this revenue procedure generally apply to all examination issues, section 3.02 of this revenue procedure provides accounting method issues that are appropriate for early referral.

**.02 Appropriate issues for early referral.** Examples of appropriate issues for early referral include whether :

- (1) the taxpayer's practice is a method of accounting;
- (2) the IRS is precluded from changing the taxpayer's method of accounting because, for example, the taxpayer obtained audit protection by initiating a voluntary accounting method change;
- (3) the taxpayer's present method of accounting clearly reflects income under § 446;
- (4) the method of accounting proposed by the IRS clearly reflects income under § 446;
- (5) the methodology used by the IRS to compute the § 481(a) adjustment is appropriate; or
- (6) the methodology used by the IRS to compute the § 481(b) adjustment is appropriate.

### **SECTION 4. EMPLOYMENT TAX EARLY REFERRAL PROCEDURES**

#### **.01 Background.**

- (1) In 1996, the Service adopted the classification settlement program (CSP) for worker classification cases for a two-year test period. The Service announced in Notice 98-21, 1998-15 I.R.B. 14, that the CSP would be extended until further notice. The CSP is an optional settlement program that allows businesses and tax examiners to resolve worker classification cases as early in the administrative process as possible, thereby reducing taxpayer burden. In the CSP, examiners can offer a business under audit a worker classification settlement using a standard closing agreement developed for this purpose. The CSP procedures also ensure that the taxpayer relief provisions under § 530 of the Revenue Act of 1978, as amended, are properly applied. When a taxpayer does not agree with the CSP terms offered by the Service or is not eligible for a settlement under the CSP,

- consideration should be given to requesting early referral to Appeals under these procedures.
- (2) Section 530 provides businesses with relief from federal employment tax obligations if certain requirements are met. It terminates the business' employment tax liability under IRC Subtitle C (Federal Insurance Contributions Act and Federal Unemployment Tax Act taxes, federal income tax withholding, and Railroad Retirement Tax Act taxes) and any interest or penalties attributable to such liability for employment taxes (Rev. Proc. 85-18, 1985-1 C.B. 518). Section 530 does not affect the employment tax liability of a worker.
  - (3) Section 530(e)(3) is generally effective after December 31, 1996 and clarifies that the determination of whether a business is entitled to relief under § 530 is not dependent upon whether the relevant workers are first determined to be employees. As a result, IRS examiners will now consider the taxpayer's eligibility for relief under § 530 before initiating any examination of the relationship between a business and a worker.
  - (4) Taxpayers that disagree with the District's position regarding the application of § 530 have the option of immediately requesting early referral of the issue from the District to Appeals. In attempting to resolve the § 530 issue, Appeals will follow the procedures set forth in this revenue procedure. If the § 530 issue remains unresolved, or if it is determined that the taxpayer is not eligible for relief under § 530, the case will be returned to the District for consideration of the worker classification issues. If the taxpayer and the District are unable to agree on the worker classification issues, the taxpayer will be encouraged strongly to request early referral of the unagreed issue from the District to Appeals. It is not necessary for a taxpayer to request early referral when the IRS examiner determines that the taxpayer is not entitled to relief under § 530. The taxpayer also may wait until the IRS examiner has determined the § 530 and worker classification issues before requesting early referral of the issues to Appeals.
  - (5) The Taxpayer Relief Act of 1997, Pub. L. No. 105-34, 111 Stat. 788, added § 7436 to the Code, which provides new judicial review rights concerning certain employment tax determinations. Generally, § 7436 became effective on August 5, 1997 and applies to employment tax cases in which the Service has determined that at least one worker should be reclassified as an employee and that the taxpayer is not entitled to relief under § 530. The law requires that any employment tax that depends upon such determinations cannot be assessed unless the taxpayer has been given an opportunity to file a petition for United States Tax Court review of the Service's determinations on those two issues. In all cases involving worker classification and § 530 issues, the District will inform taxpayers about the opportunity to seek Tax Court review at the same time as they are informed of their appeal rights. See Notice 98-43, 1998-33 I.R.B. 13.

**.02 In general.** The early referral procedures in section 2 of this revenue procedure generally apply to employment tax issues. Sections 4.03 through 4.06 of this revenue procedure specifically apply to the early referral of employment tax issues.

**.03 Appropriate issues for early referral.** Examples of appropriate employment tax issues for early referral include:

- (1) Worker classification issues, including whether a worker is an employee or independent contractor under the common law; whether a worker is a statutory employee or statutory non-employee.
- (2) Liability issues, including whether § 530 applies; whether § 3509 rates are appropriate; and whether the taxpayer qualifies for an interest-free adjustment.
- (3) Other issues, including whether certain payments are excepted from the definition of "wages" (e.g., a fringe benefit that would be excludable from the employee's gross income under § 132); and whether certain services are excepted from the definition of "employment."

**.04 Issuance of employment tax report.** If an issue is approved for transfer from the District to Appeals, the District will prepare an employment tax report for each early referral issue approved pursuant to this revenue procedure, by following the procedures in section 2.11 of this revenue procedure. The issuance of the employment tax report is not treated as the first letter of proposed assessment of tax for purposes of computing increased interest under § 6621(c), or for the award of administrative costs under § 7430(c).

**.05 Agreement reached.** If an agreement is reached with respect to an employment tax early referral issue, a Form 2504, Agreement to Assessment and Collection of Additional Tax and Acceptance of Overassessment -- Excise or Employment Tax, or a Form 2504 AD, Excise or Employment Tax -- Offer of Agreement to Assessment and Collection of Additional Tax and Offer of Acceptance of Overassessment, should be labeled "Partial Agreement" and may be used for factual or non-complex issues that do not affect subsequent years. Notice 98-43 provides that if a taxpayer settles a § 530 or worker classification issue on an agreed basis, the taxpayer must formally waive the restrictions on assessment contained in §§ 7436(d)(1) and 6213. The following waiver must be included:

**I understand that by signing this agreement, I am waiving the restrictions on assessment provided in §§ 7436(d) and 6213(a) of the Internal Revenue Code of 1986.**

A closing agreement generally will be prepared for issues where a settlement is complex or affects subsequent years. See § 7121 and also Rev. Proc 68-16, 1968-1

C.B. 770, which describes the preparation of closing agreements. Appeals will coordinate effects on subsequent years with the District and District Counsel.

**.06 Agreement not reached.**

- (1) If one or more of the early referral employment tax issues are unagreed, the case will be returned to the District. The employment tax dependent upon a § 530 or worker classification issue may not be assessed at that time. See § 7436(d)(1) and Notice 98-43. Instead, the District must send the taxpayer, via certified or registered mail, a "Notice of Determination Concerning Worker Classification Under Section 7436."
- (2) With respect to any unagreed early referral employment tax issues that do not relate to a § 530 or worker classification issue (so that the unagreed issue(s) is not subject to § 7436), a 30-day letter will not be issued. Rather, the District will process the portion of the case that is not dependent upon a § 530 or worker classification issue for assessment of tax due from the taxpayer that relates to that portion of the case only, which will start the period for the increased underpayment rate for large corporate underpayments under § 6621(c), or for the award of administrative costs under § 7430(c).

## **SECTION 5. COLLECTION EARLY REFERRAL PROCEDURES**

**.01 In general.** Early referral to Appeals is also available for collection issues. Procedures for utilizing the early referral process are described in Publication 1660, "Collection Appeal Rights." Each taxpayer subject to a lien, levy or seizure will receive a copy of Publication 1660. Early referral of collection issues is a different process than the due process procedures described in § 6320 for liens and § 6330 for levies. Specifically, denial of relief pursuant to the early referral procedures will not be reviewable in the Tax Court or in a U.S. District Court. In addition, the early referral procedures apply to a broader range of collection issues than the due process procedures.

**.02 Appropriate issues for early referral.** Appropriate collection issues for early referral include proposed:

- (1) notices of federal tax liens;
- (2) levies;
- (3) seizures; and
- (4) denials or terminations of installment agreements.

## **SECTION 6. EMPLOYEE PLANS/EXEMPT ORGANIZATIONS (EP/EO) EARLY REFERRAL PROCEDURES**

**.01 In general.** The early referral procedures in section 2 of this revenue procedure generally apply to EP/EO issues. Thus, for example, only issues under audit are eligible for early referral. EP/EO issues excluded from the early referral process are identified in sections 6.02 and 6.03 of this revenue procedure.

**.02 Employee Plans issues excluded from early referral.** Early referral does not apply to:

- (1) procedural issues relating to matters that may be eligible for Administrative Policy Regarding Self-Correction, or submitted under VCR, Walk-in CAP, or the Audit Closing Agreement Program. See Rev. Proc. 98-22, 1998-12 I.R.B. 11, or its successors;
- (2) issues relating to excise taxes in § 4975; or
- (3) issues concerning plan qualification if such issues are not covered by published precedent or are issues for which there may be nonuniformity between offices.

**.03 Exempt Organizations issues excluded from early referral.** Early referral does not apply to:

- (1) issues subject to § 7428, including issues related to exemption or private foundation status;
- (2) issues arising in Church tax inquiries and examinations subject to § 7611;
- (3) issues relating to excise taxes in § 507 and Chapters 41 and 42 of the IRC; or
- (4) issues relating to the revocation of exempt status.

## **SECTION 7. NO USER FEE**

There is no user fee for an early referral request.

## **SECTION 8. EFFECT ON OTHER DOCUMENTS**

Rev. Proc. 96-9 is superseded.

**SECTION 9. EFFECTIVE DATE**

This revenue procedure is effective for requests for early referral filed after July 19, 1999, the date this revenue procedure is published in the Internal Revenue Bulletin.

**DRAFTING INFORMATION**

The principal authors of this revenue procedure are Thomas Carter Louthan, Director, Office of Alternative Dispute Resolution and Customer Service Programs, and Sandy Cohen from the Office of Alternative Dispute Resolution and Customer Service Programs, National Office Appeals. For further information regarding this revenue procedure, please contact Mr. Louthan at (202) 694-1842, or Mr. Cohen at (202) 694-1818 (not toll-free numbers).