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*This thought leadership is about the 13 compliance campaigns recently issued by IRS Large Business and International ('LB&I') division.*

The IRS Large Business and International ('LB&I') division forms a huge part of the IRS. First, it is responsible for the tax compliance enforcement (*US domestic and US international*) with respect to all corporations, subchapter S corporations, and partnerships with assets greater than US\$ 10 million. Second, the division deals with individual international tax compliance, including offshore voluntary disclosures.

On January 31, 2017, this LB&I division announced 13 specific issues which it will be targeting in a new audit strategy known as 'campaigns'. The issues identified cover a broad range of topics including partnerships, insurance, an energy tax credit, tax techniques used by the television broadcast industry, and foreign businesses and taxpayers. We understand that these issues were identified through extensive data analysis, suggestions from IRS compliance employees, and feedback from the tax community.

Amongst the 13 issues identified, the ones which are of paramount importance for foreign multi-nationals with operations/set-ups in the US are:

- Repatriation campaign;
- Form 1120 - F non-filer campaign;
- Inbound distributor campaign; &
- Related party transactions campaign.

These 13 campaigns can be broadly divided into two parts, namely, international campaigns and domestic campaigns. These campaigns are listed below:

**International campaigns:**

- **OVDP declines - withdrawals campaign**

The Offshore Voluntary Disclosure Program ('OVDP') allows US taxpayers to voluntarily resolve past non-compliance related to unreported offshore income and failure to file foreign information returns. This campaign addresses OVDP applicants who applied for pre-clearance into the program but were either denied access to OVDP or withdrew from the program of their own accord. Taxpayers, who have yet to resolve their non-compliance and who meet the eligibility criteria, are encouraged to consider entering one of the offshore programs currently available. The IRS will address continued non-compliance through a variety of treatment streams including examination.

- **Repatriation campaign**

LB&I is aware of different repatriation structures being used for purposes of tax free repatriation of funds into the US in the mid-market population. It has also been determined that many of the taxpayers do not properly



report repatriations as taxable events on their filed returns. The goal of this campaign is to simultaneously improve issue selection filters while conducting examinations on identified, high risk repatriation issues and thereby increase taxpayer compliance.

- **Form 1120 - F non-filer campaign**

Foreign companies doing business in the US are often required to file Form 1120 - F LB&I has data suggesting that many of these companies are not meeting their filing obligations. In this campaign, LB&I will use various external data sources to identify these foreign companies and encourage them to file their required returns. The treatment stream for this campaign will involve soft letter outreach. If the companies do not take appropriate action, LB&I will conduct examinations to determine the correct tax liability. The goal is to increase voluntary compliance by foreign corporations with a US business nexus.

- **Inbound distributor campaign**

US distributors of goods sourced from foreign-related parties have incurred losses or small profits on US returns, which are not commensurate with the functions performed and risks assumed. In many cases, the US taxpayer would be entitled to higher returns in arms-length transactions. LB&I has developed a comprehensive training strategy for this campaign that will aid revenue agents as they examine this IRC Section 482 issue. The treatment stream for this campaign will be issue-based examinations.

### **Domestic campaigns:**

- **IRC 48C energy credit campaign**

This campaign ensures that only those taxpayers whose advanced energy projects were approved by the Department of Energy, and who have been allocated a credit by the IRS, are claiming the credit. These credits must be pre-approved through extensive application to the DOE. The treatment stream for this campaign will be soft letters and issue-focused examinations.

- **Domestic production activities deduction, multi-channel video program distributors (*MVPD's*) and TV broadcasters**

MVPD's and TV broadcasters often claim that 'groups' of channels or programs are a qualified film eligible for the IRC Section 199 deduction. Taxpayers are asserting that they are the producers of a qualified film when distributing channels and subscriptions packages that often include third-party produced content. Additionally, MVPD taxpayers maintain that they provide online access to computer software for the customers' direct use (*incident to taxpayers' transmission activities, including customers' use of the set-top boxes*). LB&I has developed a strategy to identify taxpayers impacted by these issues and will develop training to aid revenue agents in examining them. The treatment streams for this campaign include the development of an externally published practice unit, potential published guidance, and issue based exams, when warranted.

- **Micro-captive insurance campaign**

This campaign addresses transactions described in Transactions of Interest Notice 2016-66, in which a taxpayer attempts to reduce aggregate taxable income using contracts treated as insurance contracts and a related company that the parties treat as a captive insurance company. Each entity that the parties treat as an insured entity under the contracts claims deductions for insurance premiums. The manner in which the contracts are interpreted, administered, and applied is inconsistent with arm's length transactions and sound business



practices. LB&I has developed a training strategy for this campaign. The treatment stream for this campaign will be issue-based examinations.

- **Related party transactions campaign**

This campaign focuses on transactions between commonly controlled entities that provide taxpayers a means to transfer funds from the corporation to related pass through entities or shareholders. LB&I is allocating resources to this issue to determine the level of compliance in related party transactions of taxpayers in the mid-market segment. The treatment stream for this campaign is issue-based examinations.

- **Deferred variable annuity reserves & life insurance reserves IIR campaign**

The IRS and Chief Counsel have agreed to accept the deferred variable annuity reserves and life insurance reserves issues into the IIR program (*pursuant to Rev. Proc. 2016-19*) to develop guidance to address uncertainties on issues important to the Life Insurance industry. The issues include amounts to be taken into account in determining tax reserves for both deferred variable annuities with guaranteed minimum benefits, and life insurance contracts. The campaign's objective is to collaborate with industry stakeholders, Chief Counsel and Treasury to develop published guidance that provides certainty to taxpayers regarding these related issues.

- **Basket transactions campaign**

This campaign addresses structured financial transactions described in Notices 2015-73 and 74, in which a taxpayer attempts to defer and treat ordinary income and short-term capital gain as long-term capital gain. The taxpayer treats the option or other derivative as open until a barrier event occurs, and, therefore, does not recognize or report current period gains. The gains are deferred until the contract terminates, at which time the overall net gain is reported as a long-term capital gain. LB&I has developed a training strategy for this campaign. The treatment streams for this campaign will be issue-based examinations, soft letters to material advisors and practitioner outreach.

- **Land developers - completed contract method ('CCM') campaign**

Large land developers that construct in residential communities may be improperly using the CCM of accounting. A developer, whose average annual gross receipts exceed US\$ 10 million, may only use the CCM under a home construction contract. In some cases, developers are improperly deferring all gain until the entire development is completed. LB&I will provide training for revenue agents assigned to work this issue. The treatment stream includes development of a practice unit, issuance of soft letters, and follow-up with issue based examinations when warranted.

- **TEFRA linkage plan strategy campaign**

As partnerships have become larger and more complex, LB&I has regularly revised processes to assess tax on the terminal investors. Recent legal advice provides an opportunity to make significant changes to how we approach this process. This campaign focuses on developing new procedures and technology to work collaboratively with the revenue agent conducting the TEFRA partnership examination to identify, link and assess tax to the terminal investors that pose the most significant compliance risk.

- **S corporation losses claimed in excess of basis campaign**

S corporation shareholders report income, losses and other items passed through from their corporation. The law limits losses and deductions to their basis in the corporation. LB&I has found that shareholders claim losses and deductions to which they are not entitled because they do not have sufficient stock or debt basis to absorb



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these items. LB&I has developed technical content for this campaign that will aid revenue agents as they examine the issue. The treatment streams for this campaign will be issue-based examinations, soft letters encouraging voluntary self-correction, conducting stakeholder outreach, and creating a new form for shareholders to assist in properly computing their basis.

IRS while issuing these campaigns inform that these represent the first wave of LB&I's issue-based compliance work. More campaigns will continue to be identified, approved and launched in the coming months. The taxpayers both domestic and foreign should keep an eye on these campaigns and also start preparing for the same.

Source: IRS.