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RE: Suggested Revisions to the Internal Revenue Manual Regarding
Bond Examinations and Technical Advice

Dear Ms. Harrigal and Mr. Chamberlin:

The National Association of Bond Lawyers (“NABL”) respectfully submits the attached comments and recommendations for further revisions to the provisions of the Internal Revenue Manual regarding bond examinations and technical advice in an attempt to make those provisions more clear, efficient and useful both for the Internal Revenue Service and for municipal bond issuers. NABL recognizes and appreciates that the Office of Tax Exempt Bonds has made many helpful revisions to these provisions in the last year.

The enclosed comments were prepared by an ad hoc task force comprising those individuals listed in Exhibit A, with substantial input from individual members of the NABL Board of Directors, and were approved by the NABL Board of Directors.

If NABL can provide further assistance, please do not hesitate to call Bill Daly in our Washington, D.C. office at (202) 503-3303.

Sincerely,

Kenneth R. Artin
Enclosure

**NATIONAL ASSOCIATION OF BOND LAWYERS
COMMENTS AND SUGGESTED REVISIONS TO THE INTERNAL REVENUE
MANUAL REGARDING BOND EXAMINATIONS AND TECHNICAL ADVICE**

The National Association of Bond Lawyers (“NABL”) hereby submits its suggested revisions to certain Internal Revenue Manual sections dealing with bond examinations and technical advice as revised and transmitted through April 12, 2016 (“IRM”) and comments on the implementation of certain provisions of the IRM. We welcome the improvements the Office of Tax Exempt Bonds (“TEB”) already has made to certain sections of the IRM. We hope the comments below will be helpful in improving the clarity and effectiveness of the provisions.

1. IRM 4.81.1.4 Jurisdiction

IRM 4.81.1.4(3) provides that TEB examiners have the authority to assert civil penalties where warranted. It would be useful to list common civil penalties that might be warranted.

2. IRM 4.81.2.3(3) CPM Case Selection

Sometimes multiple bond issues of a given issuer or conduit borrower are selected for examination within a relatively short period of time, even though the selected bond issues may be similar (such as multiple issues financing the same facilities or multiple issues for the same conduit borrower where there is substantial duplication in the document review). While we are sensitive to the statistical reasons this may occur, we suggest that multiple examinations within a relatively short period of time be stated as a factor in determining whether bond issues are “inappropriate for examination within a Market Segment.” Compare IRM 4.46.3.1.2 (3) (LB&I survey to determine whether there are no large, unusual or questionable items and whether the same issues were previously present with no change or only a small change.)

3. IRM 4.81.3.3.1 Development Phase

IRM 4.81.3.3.1(2)(12) provides for the creation of a Master List of Project Participants that, under IRM 4.81.3.3.1(2)(14), will be the source of contact information. Because questionnaires sometimes are sent years after an issuer has last filed a Form 8038 series return, and because contact information and personnel change, we recommend that the Project Team contact Project Participants by telephone to determine the proper contact person and address before mailing a Compliance Check Package. Even the address and general contact information on an issuer’s website may not be appropriate for a Compliance Check Package. We have seen communications from TEB delayed in reaching appropriate officials. This creates inefficiencies and delays for issuers and for TEB, as well as an apparent lack of responsiveness on the issuer’s part. See IRM 4.81.3.3.2(2)(F)

(“Filing or IRS business system processing errors may result in inaccurate contact information for a Project Participant . . .”).

4. IRM 4.81.3.3.2 Implementation Phase

IRM 4.81.3.3.2(2)(D) provides that, before speaking with a representative of an issuer, “for example, a financial advisor,” a Team Member must obtain a Form 2848. In some circumstances, a Form 8821, Tax Information Authorization, may be more appropriate, so that option should be left open. This could be done by adding “or Form 8821” after “Form 2848.”

5. IRM 4.81.4 Examination Planning

The Manual Transmittal for IRM 4.81.4 (01-13-2016) states that previously published IRM 4.81.5.6.1, among others, is obsolete, but IRM 4.81.4.6 *Contacting the Taxpayer*, states: “[f]or procedures related to contacting the taxpayer to open an examination, see IRM 4.81.5.7.9.1.” The cross-reference was a typographical error and it is now incorrect. IRM 4.81.5.4.1.1 now contains those provisions.

6. IRM 4.81.4.1 Case Assignment

IRM 4.81.4.1(2) states: “While generally all market segment cases must be examined, there may be cases in which it is appropriate to survey the case, e.g., the examiner determines that the bonds are no longer outstanding and there are no open tax years.” In our experience, specific tax issues with respect to the same issuer or conduit borrower have been re-examined as part of different bond issue examinations, and there have been repeated examinations involving a particular facility that was financed with multiple series of bonds over time. This is not a good use of limited government resources, either those of the IRS or those of the issuer. Also see comment 2 above relating to IRM 4.81.2.3(3), CPM Case Selection, with respect to multiple examinations of the same issuer or conduit borrower after general compliance has already been established. Where these circumstances arise, the bond issue proposed to be examined should be surveyed to determine whether an examination is appropriate.

Furthermore, where the IRS and an issuer have entered into a closing agreement based on full taxpayer exposure, there is no reason for TEB to re-examine the bond issue in question.

7. IRM 4.81.4.3 Scope of the Examination

a. IRM 4.81.4.3(6) states: “Surveying a case requires approval by the group manager. While generally market segment cases should not be surveyed, if the examiner and group manager believe that surveying is appropriate, the group manager should consult with the market segment coordinator before surveying the case.” See comment 6 above.

b. IRM 4.81.4.3(7) provides that, for purposes of TEB examinations, each individual Form 8038 series return is treated as an examination. This can lead to duplication of effort where there may be multiple Form 8038 series returns for what would be a single issue but for the presence of different types of tax-advantaged bonds, or where there are multiple issuers of conduit bonds issued on a given date for a single conduit borrower, such as a hospital system, as a single issue for tax purposes. In at least one case of which we are aware, an issuer had two series of bonds issued on the same day with a common offering document that were examined by two different revenue agents and two sets of IDRs. This was very inefficient both for the IRS and the issuer. Although two types of bond issues may present some distinct tax issues, there often is significant duplication in the review of certain documents and the questions asked by the agents. Simultaneous examinations of multiple series of bonds issued on the same day with a common offering document should, at the least, be coordinated.

8. IRM 4.81.4.4 Planning the Full Scope Examination

a. IRM 4.81.4.4(3) states that, as part of the pre-audit analysis, the examiner should analyze, among other items, Form 8038 series information returns, official statements and material event notices. Agents often request copies of these items in their first IDRs, but if the examiner already has reviewed them, such requests should not be made.

b. IRM 4.81.4.4(3)(E) states that, as part of the pre-audit analysis, the examiner should review applicable Internal Revenue Code (“IRC”) sections, regulations, court cases, revenue rulings and procedures. Examiners also should review applicable private letter rulings, technical advice memoranda and Chief Counsel Advice memoranda, which, while not legal precedent, are important to understanding how the law has been applied in practice. Compare IRM 4.46.4.3 (LB&I).

9. IRM 4.81.4.6 Contacting the Taxpayer

IRM 4.81.4.6, as is stated above, cross references IRM 4.81.5.7.9.1, but the cross-reference was a typographical error and it is now incorrect. IRM 4.81.5.4.1.1 contains the applicable provisions.

10. IRM 4.81.5.4.1.1 Contacting the Taxpayer to Open an Examination

a. IRM 4.81.5.4.1.1 permits examiners to open the examination by mail, following up 14 days later to confirm receipt of the examination notice. IRM 4.81.5.4.1.1(5)(A) indicates that examiners may use the issuer’s last known address or an address taken from the issuer’s website. Because examination notices sometimes are sent years after an issuer has last filed a Form 8038 series return and because contact information and personnel change, we recommend that examiners routinely check with issuers by telephone, using the phone number on the applicable Form 8038 series return and following up with a website phone number

if necessary, to determine the proper contact person and address. Even the address and general contact information on an issuer's web site may not be appropriate for an examination notice. We have seen communications from TEB delayed in reaching appropriate officials. This creates inefficiencies and delays for issuers and for TEB, as well as an apparent lack of responsiveness on the issuer's part. See IRM 4.81.3.3.2(2)(F) ("Filing or IRS business system processing errors may result in inaccurate contact information for a Project Participant . . .")

b. IRM 4.81.5.4.1.1(9) provides that IDRs should "specify a response due date." We frequently see situations in which the stated date of the letter is significantly earlier than the postmark date and a week or more prior to its receipt by the issuer. We suspect that there are endemic delays in processing outgoing mail by certain offices of the IRS. Regardless of the reason, the due date of the response should be set with reference to an actual expected date of receipt of the IDR by the issuer. We do acknowledge that the general willingness of agents to grant extensions makes this a relatively minor point for practitioners, but it does occasionally cause distress for issuers or conduit borrowers, the latter of which do not receive IDRs until after they are first processed by the conduit issuers.

11. IRM 4.81.5.4.2.4 Bypass Procedures

We have seen circumstances in which it does not appear the bypass procedures were followed: examiners have contacted issuers directly before a Warning Letter has been sent to the representative and have made disparaging remarks about the representative to issuers. We encourage TEB management to inform examiners that such actions are not appropriate and should not occur.

12. IRM 4.81.5.4.3 Third Party Contacts

IRC section 7602(c)(2) requires the IRS to provide the taxpayer with a list of third-party contacts periodically. In our experience examiners have made third-party contacts without notifying the issuer or the issuer's representative.

13. IRM 4.81.5.5.2 Securing Records

IRM 4.81.5.5.2(3) has an incorrect cross-reference for third-party contact information.

14. IRM 4.81.5.6.2(6) Deposition (Verbatim Recordings)

IRM 4.81.5.6.2(6) (B)(A) requires group manager approval of recordings. This fact should be communicated to the taxpayer or its representative in advance of an interview, so that a request for group manager approval can be made on a timely basis.

15. IRM 4.81.5.15.1 Procedures Required Before Placing a Case in Suspense

We have experienced many occasions when examiners put examinations on hold for extended periods while specialists are reviewing cases without notifying the issuer with Letter 4563 as required by IRM 4.81.5.15.1(4).

16. IRM 4.81.6.5 Closing Agreement Terms

IRM 4.81.6.5(3) describes factors to be considered in case resolution. The factors no longer include collectability of the total taxpayer exposure from bondholders, the complexity of the transaction or hazards of litigation, all of which were factors in IRM 4.81.1.24.1(1) (01-01-2003). These are factors that will be considered by the IRS Office of Appeals. It does not appear to be a good use of IRS or issuer resources for TEB to effectively force the issuer to go to Appeals when these factors are in play. Accordingly, we recommend adding “collectability of the total taxpayer exposure from bondholders, the complexity of the transaction and hazards of litigation” to the list of factors.

In addition, while paragraphs (D) (inadvertent compliance failure or compliance failure that is a de minimis part of the transaction) and (F) (the amount of economic benefit received) allude to this concept, a clearer reference should be made to whether the failure was relatively minor – the punishment should fit the crime.

17. IRM 4.81.6.5.3.1 Computation of Taxpayer Exposure

IRM 4.81.6.5.3.1(2)(A) states that, for purposes of determining the resolution amount, TEB generally should include payment date years “within three years of the date TEB identified the compliance failure” and may increase the number of “open” years from the normal three year period up to six years if the issuer or its representative has not acted in good faith in resolving the compliance failure.

We have several concerns about these provisions. First, the statute of limitations is not based on when the IRS determines a compliance failure, but rather when the IRS assesses a tax. Second, the Office of Appeals will apply a three-year period in negotiating an agreement with the issuer, regardless of the good faith of the issuer or the representative. It does not appear to be a good use of IRS or issuer resources for TEB to effectively force the issuer to go to Appeals because of the different treatment of the statute of limitations. In addition, in some cases, representatives have been accused of not acting in good faith merely because they have been strong advocates for their clients, which they are obligated to be by applicable rules of professional responsibility.

18. IRM 4.81.6.5.3.3 Computation of Fee Amount

IRM 4.81.6.5.3.3(2)(A) refers to “the par amount of the bonds held by the issuer.” In this context, it appears that the reference should be to “the par amount of the bonds outstanding.”

19. IRM 4.81.6.5.3.4 Computation of Alternative Minimum Tax Adjustment

IRM 4.81.6.5.3.4(2)(B) uses a factor of 0.0014 in computing the adjustment. In low yield situations, the 0.0014 factor is far from an appropriate measure of the spread between AMT and non-AMT bonds. While we acknowledge that there are advantages to using constant formulae that approximate rough justice (such as the 29% deemed tax rate), in this case the formula has become extremely detached from rough justice. We do not have the statistical data needed to determine a factor, but we recommend that the calculation be based on a percentage of the interest payments rather than a percentage of the principal amount outstanding.

20. IRM 4.81.6.5.3.7 IRC Section 6700 Penalty

IRM 4.81.6.5.3.7(1) states that “the agent should determine the section 6700 penalty by treating the sale of each bond denomination as a separate activity.” While case law is divided on this interpretation of prior law, the applicable penalty now is “50 percent of the gross income derived (or to be derived) from such activity by the person on which the penalty is imposed,” see last sentence of IRC 6700(a), so the sentence partially quoted above should be deleted.

21. IRM 4.81.6.5.3.9 Computing Value as of the Closing Agreement Execution Date

IRM 4.81.6.5.3.9(3) refers to the “applicable federal rate (AFR)” and “IRC 1274(D)(1).” The references should be to the “adjusted applicable federal rate (AAFR)” and “IRC 1274(d)(1), as modified by IRC 1288(b)(1).”

22. IRM 4.81.6.6 Execution of Closing Agreements

It often occurs that the time it takes for TEB to prepare closing agreements once the settlement terms have been agreed upon is inordinately long. Perhaps some expectation of how long this process should take, particularly given the standardization of closing agreement forms, is in order. We recommend that closing agreements be prepared within 30 days, with an expectation that 14 days normally should be sufficient.

23. Exhibit 4.81.7-3 Letter 4414, Proposed Adverse Transmittal Letter

The third paragraph of this letter is somewhat misleading in that any final adverse determination with respect to the bonds after the issuer’s appeal will not be a final determination with respect to a bondholder, which is entitled to its own examination and appeal rights. We believe this should be made clear to bondholders receiving such a letter by changing the second sentence to read:

“If the issuer is unable to resolve this matter in Appeals, a final adverse determination letter will be issued to the issuer and the IRS will treat interest on the bonds as taxable. The adverse determination letter will not, however, be a final determination with respect to bondholders, who will retain their own rights to challenge the determination.”

24. IRM 4.81.11.5.4 WBO Examination Procedures

“WB SME, (‘TEB SME’),” is used three times in this IRM, but IRM 4.81.11.1.2(1)(L) defines “Functional Division WB SME or TEB SME.” IRM 4.81.11.5.4 terminology should be “Functional Division WB SME or TEB SME.”

IRM 4.81.11.1.2(1) could add a definition for “WB” (“TEB” already is defined), and “Functional Division” could be dropped throughout IRM 4.81.11.

25. IRM 4.81.14.2 Technical Assistance from CPM

IRM 4.81.14.2(2) refers to the “CPM senior manager.” The reference should be to the “Manager, CPM.”

Exhibit A
Members of IRM Revision Task Force

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