

# Request for Tax Accrual and Other Financial Audit Workpapers

## Announcement 2002-63

The Internal Revenue Service is revising its policy concerning when it will request and, if necessary, summon tax accrual and other financial audit workpapers relating to the tax reserve for deferred tax liabilities and to footnotes disclosing contingent tax liabilities (“Tax Accrual Workpapers”) appearing on audited financial statements. This limited expansion of the circumstances in which the Service will seek Tax Accrual Workpapers is necessary to allow the Service to fulfill its obligation to the public to curb abusive tax avoidance transactions and to ensure that taxpayers are in compliance with the tax laws. In all other respects, the Service’s current policy regarding requests for Tax Accrual Workpapers will continue to apply.

The Service may request Tax Accrual Workpapers in the course of examining any return filed on or after July 1, 2002, that claims any tax benefit arising out of a transaction that the Service has deter-

mined to be a listed transaction at the time of the request within the meaning of Temp. Treas. Reg. § 1.6011-4T(b)(2) (“Listed Transaction”). (Temp. Treas. Reg. § 1.6011-4T(b)(2) defines listed transactions to include substantially similar transactions.) If the Listed Transaction was disclosed under Temp. Treas. Reg. § 1.6011-4T, the Service will routinely request the Tax Accrual Workpapers pertaining only to the Listed Transaction. If the Listed Transaction was not disclosed, the Service will routinely request all Tax Accrual Workpapers. In addition, if the Service determines that tax benefits from multiple investments in Listed Transactions are claimed on a return, regardless of whether the Listed Transactions were disclosed, the Service, as a discretionary matter, will request all Tax Accrual Workpapers. Similarly, if, in connection with the examination of a return claiming tax benefits from a Listed Transaction that was disclosed, there are reported financial accounting irregularities, such as those requiring restatement of earnings, the Service, as a discretionary matter, will request all Tax Accrual Workpapers.

For a return filed prior to July 1, 2002, that claims any tax benefit arising out of a Listed Transaction, the Service may request Tax Accrual Workpapers pertaining to the Listed Transaction, if the taxpayer had an obligation to disclose the transaction under Temp. Treas. Reg. § 1.6011-4T, and failed to do so (1) on the return; (2) under Rev. Proc. 94-69, 1994-2 C.B. 804, if applicable; or (3) pursuant to Announcement 2002-2, 2002-2 I.R.B. 304 (Jan. 14, 2002).

The Supreme Court confirmed the Service’s right to obtain Tax Accrual Workpapers under its summons authority. *United States v. Arthur Young & Co.*, 465 U.S. 805 (1984). Since Tax Accrual Workpapers are not generated in connection with seeking legal or tax advice, but are developed to evaluate a taxpayer’s deferred or contingent tax liabilities in connection with a taxpayer’s disclosure to third parties of the taxpayer’s financial condition, Tax Accrual Workpapers are not privileged communications. Neither the attorney-client privilege nor the IRC § 7525 tax practitioner privilege (which is based upon, but is more limited than, the attorney-client privilege) protects Tax Accrual Workpapers from production

upon proper request by an authorized examining agent. *See also* Treasury Department Circular 230, 31 C.F.R. § 10.20 (duty of practitioner to submit information upon a proper and lawful request by the IRS).

Despite the broad scope of authority recognized by the Supreme Court, the Service has historically acted with restraint, declining to request Tax Accrual Workpapers as a standard examination technique. The Service will continue to exercise its authority to request Tax Accrual Workpapers with restraint.

The Service will continue its current policy of requesting Tax Accrual Workpapers only in unusual circumstances (1) for any returns filed prior to July 1, 2002, other than those that claim any tax benefit arising out of a Listed Transaction that has not been disclosed as mentioned above, and (2) for any returns filed on or after July 1, 2002, other than those that claim any tax benefit arising out of a Listed Transaction as described above.

### CONTACT INFORMATION

For further information regarding this announcement, contact George Bowden at 202-622-3400 (not a toll-free call).