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November 18, 2022

Via LB&I at lbi.utp.communications@irs.gov

Internal Revenue Service

RE: *Comments on Draft Uncertain Tax Positions Statement*

Ladies and Gentlemen:

On behalf of the Tax Section of the State Bar of Texas, I am pleased to submit the enclosed response to the request of the Internal Revenue Service (the "IRS" or "Service") for comments on the draft Uncertain Tax Positions Statement ("Draft Schedule UTP") issued on October 11, 2022. The Draft Schedule UTP proposes changes to the existing Schedule UTP and includes a new field to disclose the incremental dollar amount of the uncertain tax positions taken and a new column that requires taxpayers to disclose any contrary authority, including nonbinding authority such as private letter rulings or technical advice memoranda. The Draft Schedule UTP also includes examples and additional guidance as to what constitutes an adequate description of the issue.

THE COMMENTS ENCLOSED WITH THIS LETTER ARE BEING PRESENTED ONLY ON BEHALF OF THE TAX SECTION OF THE STATE BAR OF TEXAS. THE COMMENTS SHOULD NOT BE CONSTRUED AS REPRESENTING THE POSITION OF THE BOARD OF DIRECTORS, THE EXECUTIVE COMMITTEE OR THE GENERAL MEMBERSHIP OF THE STATE BAR OF TEXAS. THE TAX SECTION, WHICH HAS SUBMITTED THESE COMMENTS, IS A VOLUNTARY SECTION OF MEMBERS COMPOSED OF LAWYERS PRACTICING IN A SPECIFIED AREA OF LAW.

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THE COMMENTS ARE SUBMITTED AS A RESULT OF THE APPROVAL OF THE COMMITTEE ON GOVERNMENT SUBMISSIONS OF THE TAX SECTION AND PURSUANT TO THE PROCEDURES ADOPTED BY THE COUNCIL OF THE TAX SECTION, WHICH IS THE GOVERNING BODY OF THAT SECTION. NO APPROVAL OR DISAPPROVAL OF THE GENERAL MEMBERSHIP OF THIS SECTION HAS BEEN OBTAINED AND THE COMMENTS REPRESENT THE VIEWS OF THE MEMBERS OF THE TAX SECTION WHO PREPARED THEM.

We commend the Service for extending the opportunity to participate in this process.

Respectfully submitted,

A handwritten signature in blue ink that reads "Henry Talavera". The signature is written in a cursive style with a small flourish above the 'v' in "Talavera".

Henry Talavera, Chair
State Bar of Texas, Tax Section

Enclosure

COMMENTS ON DRAFT SCHEDULE UTP

These comments on the Draft Schedule UTP (the “Comments”) are submitted on behalf of the Tax Section of the State Bar of Texas. Lee Meyercord, Chair, Partnership and Real Estate Tax Committee, and Joshua Smeltzer, Chair, Tax Controversy Committee, primarily drafted these Comments. Abbey Garber, Chair of the CLE Committee, reviewed these Comments and provided substantive comments. Christi Mondrik, Chair of the Committee on Government Submissions, has reviewed and approved these comments. Henry Talavera, Chair of the Tax Section, reviewed the Comments.

Although members of the Tax Section who participated in preparing these Comments have clients who would be affected by the principles addressed by these Comments or have advised clients on the application of such principles, no such member (or the firm or organization to which such member belongs) has been engaged by a client to make this government submission.

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BACKGROUND

These Comments are provided in response to the IRS’s request for comments regarding the Draft Schedule UTP. Schedule UTP has been used since 2010 for certain corporations to report uncertain tax positions. Corporations that file Forms 1120, 1120-F, 1120-L, or 1120-PC must file Schedule UTP if their total assets equal or exceed \$10 million and the corporation recorded a reserve for an uncertain U.S. federal income tax position in its audited financial statements. The Schedule UTP is intended to identify uncertain tax positions to the IRS to allow it to more efficiently and effectively audit corporations.¹ At the time the Schedule UTP was initially proposed, then-Commissioner Shulman explained, “[t]he goals of our proposal are simple: to cut down the time it takes to find issues and complete an audit.”²

The Draft Schedule UTP includes a new field to disclose the amount of the uncertain tax positions and a new column that requires taxpayers to disclose any contrary authority, including nonbinding authority such as private letter rulings or technical advice memoranda. The Draft Schedule UTP also includes examples and additional guidance as to what constitutes an adequate description of the issue. We have identified two items that the IRS might consider, which we discuss below.

DISCLOSURE OF AMOUNT

The IRS states that the Draft Schedule UTP includes “a new field for the incremental dollar amount of the uncertain tax positions taken.” The instructions state that taxpayers must:

Identify the location of the tax position and amount of the unrecognized federal income tax benefits (see the definition of size earlier). Enter the form number or schedule and the line number in columns (i) and (j) and the amount of the item in column (k).

The instructions define “size” as “the amount of unrecognized U.S. federal income tax benefits recorded for that position.” The term “recorded” is used throughout the instructions to refer to the amount recorded in the audited financial statements, i.e., the taxpayer’s reserve amount. Therefore, the instructions appear to ask for the taxpayer’s reserve amount recorded in its audited financial statements.

Such a change is contrary to the “policy of restraint” in IRS Announcements 84-46, 2002-63 and 2010-9 and implicates privileged communications. The tax reserve is based on tax accrual workpapers that “pinpoint the ‘soft spots’ on a corporation’s tax return by highlighting those areas in which the corporate taxpayer has taken a position that may, at some later date, require the payment of additional taxes.”³ Tax accrual workpapers generally include a description of the

¹ IRS Announcement 2010-9, 2010-7 I.R.B. 408.

² IR-News Rel. 2010-13, 2010 I.R.B. LEXIS 52.

³ *United States v. Arthur Young*, 456 U.S. 805, 813 (1984).

issue and the reserve amount recorded in the audited financial statements. The reserve reflects the taxpayer’s assessment of the strength of the position and risk assessment.⁴

Since the early 1980s, the IRS has followed a “policy of restraint” where it would only pursue tax accrual workpapers in unusual circumstances.⁵ The policy of restraint was adopted in part because of concerns that taxpayers were no longer preparing tax accrual information or were not making full disclosures to their independent auditors.⁶ In 2002, the IRS issued Announcement 2002-63, which modified the IRS’s policy of restraint and announced that the IRS would also seek tax accrual workpapers when a taxpayer entered into a “listed transaction.”

When the IRS first announced the Schedule UTP in Announcement 2010-9, the IRS made clear that “[t]he proposal does not require the taxpayer to disclose the taxpayer’s risk assessment or tax reserve amounts” and noted that the Service is “proposing to otherwise retain its existing policy of restraint as described in Announcement 2002-63, 2002-2 C.B. 72.”⁷ Therefore, asking for the reserve amount is a dramatic departure from the policy of restraint without any formal Announcement. Further, disclosing the reserve amount may implicate privileged communications as the reserve is frequently based on counsel’s assessment of the merits. The IRS might consider whether to remove the amount requirement and reconfirm its commitment to the well-established policy of restraint.

We understand from public comments made after the Draft Schedule UTP was released that the request for an “amount” is for the amount of the tax benefit on the return.⁸ As Holly Paz (Acting Commissioner for LB&I) explained, if a taxpayer reports a \$2 million research credit on a tax return, of which \$1 million is an unrecognized tax benefit, the form is asking for that \$2 million on the line of the return.⁹ This is similar to the Schedule UTP first proposed in 2010, which asked taxpayers to disclose the maximum tax adjustment. This requirement received significant public comments and ultimately was not adopted.¹⁰ For example, practitioners expressed concern that revenue agents would decide to audit an issue based solely on the

⁴ FASB Accounting Standards Codification (ASC) Subtopic 740-10 (which incorporates most of former FASB Interpretation FIN 48).

⁵ IRS Announcement 84-46, 1984-18 I.R.B. 18 (1984). This policy was referenced in the Supreme Court’s decision in *United States v. Arthur Young*, where the Supreme Court held that tax accrual workpapers are relevant to the IRS’s examination and are not privileged. 465 U.S. 805, 816 (1984). At that time, the Supreme Court stated that privilege protections for tax accrual workpapers reflect a policy choice “best left to the Legislative Branch.” *Id.* at 821. In 1998, however, Congress enacted Section 7525, which protects communications between a taxpayer and a federally authorized tax practitioner under the tax practitioner privilege. However, because tax accrual workpapers are frequently disclosed to third-parties, they may not be protected by Section 7525.

⁶ IRS Announcement 84-46, 1984-18 I.R.B. 18 (1984).

⁷ IRS Announcement 2010-9, 2010-7 I.R.B. 408.

⁸ Kristen A. Parillo, “Misleading Instruction for Draft Schedule UTP to Be Clarified,” Tax Notes (Nov. 2, 2022).

⁹ *Id.*

¹⁰ See Comment Letter from American Bar Association Section of Taxation (May 28, 2010); Comment Letter from Tax Executives Institute, Inc. (May 28, 2010).

magnitude of tax adjustment rather than a thoughtful evaluation of the issue and the IRS's compliance concerns.¹¹ Further, practitioners noted that disclosing the amount of the tax benefit is unnecessary to the Service's stated purpose of identifying issues.¹² These prior concerns remain relevant. Therefore, the IRS might consider whether to remove the requirement to disclose an amount.

DISCLOSURE OF CONTRARY AUTHORITIES

The IRS stated that the Draft Schedule UTP includes "new columns [that] will identify the rulings or regulation sections that are contrary to positions taken on the tax return." The draft instructions for Schedule UTP include a statement that "if you are disclosing a tax position contrary to a rule...otherwise reportable on Form 8275, you must identify the rule in column (c)." Taxpayers are then given a chart of abbreviations for the authoritative sources to use that includes the following:

<u>Abbreviation</u>	<u>Authoritative Source</u>
RP	Revenue Procedure
RR	Revenue Ruling
PLR	Private Letter Ruling
TAM	Technical Advice Memorandum
NOT	Notice
CT	Court Decision
CCA	Chief Counsel Advice
FSA	Field Service Advice
GCM	General Counsel Memorandum

The current Schedule UTP only requires the listing, in column (b), of "Primary IRC Sections." Therefore, the Draft Schedule UTP and its accompanying instructions significantly expand the contrary authority required to be identified and disclosed. Also expanded is the section entitled "Coordination with Other Reporting Requirements," which previously merely noted that "a complete and accurate disclosure of a tax position. . . will be treated as if the corporation filed a Form 8275 or 8275-R (Disclosure Statement)." The additional language in the draft instructions for Schedule UTP states as follows:

For tax positions contrary to a rule otherwise reportable on Form 8275, Disclosure Statement, you must identify the statutory provision in column (b) and the revenue ruling, revenue procedure, or other guidance in column (c). . .

¹¹ See Comment Letter from American Bar Association Section of Taxation (May 28, 2010).

¹² *Id.*

The additional language in the “Coordination with Other Reporting Requirements” section also includes a “caution” icon stating that:

failure to provide a complete and accurate disclosure of the tax position on Schedule UTP will not satisfy the section 6662 adequate disclosure requirements for Form 8275, 8275-R, or tax positions reported on Schedule UTP.

Written determinations issued by the IRS may not be cited as precedent by taxpayers.¹³ For example, the draft form and instructions specifically list Private Letter Rulings (PLRs) among the “contrary authority” that must be disclosed on Schedule UTP. However, most courts have held that PLRs issued to other taxpayers are of no precedential value in deciding tax claims before them.¹⁴ Written determinations that are not taxpayer specific (e.g. Technical Advice Memoranda (TAM), Chief Counsel Advice (CCA), and Field Service Advice (FSA)) are also not allowed to be cited as precedent by taxpayers.¹⁵ Further, the IRS specifically states that requests for Chief Counsel Advice (CCA) do not represent a final determination of the IRS position even in the case requested.¹⁶ Finally, while the instructions state that the contrary authority must be identified to satisfy the adequate disclosure requirements of Form 8275 and 8275-R, written determinations are not required to be disclosed on Form 8275 or 8275-R.

To address these issues, the IRS might consider removal of the requirement for taxpayers to identify contrary authority beyond that which is binding authority. This would include the listing of the “Primary IRC Sections” required by the current version of Schedule UTP. As an alternative, the IRS might consider requiring any final regulations and applicable case law, and other legally binding authority, to be highlighted and raised as applicable. The additional authorities listed are not binding on taxpayers, have no precedential value, are not even the final legal position of the IRS, and are not required to be disclosed on Form 8275 or 8275-R.

¹³ I.R.C. § 6110(k)(3).

¹⁴ See, e.g., *Amergen Energy Co., LLC ex Rel. Exelon Generation Co., LLC v. United States*, 94 Fed. Cl. 413, 418 (2010).

¹⁵ I.R.C. § 6110(k)(3).

¹⁶ See I.R.M. § 4.8.8.12.1.3 (Feb. 11, 2021).