

## Internal Revenue Service Compliance Assurance Process

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Last fall, the IRS made permanent a new process, the Compliance Assurance Process (CAP), to assure compliance with federal tax laws. It is an elective process. A taxpayer applies to the IRS for admission into CAP. If accepted, the taxpayer advises IRS agents during the taxable year of material transactions in which the taxpayer is engaging. Further, the taxpayer advises the IRS of the reporting positions for these transactions that the taxpayer intends to take when it files its tax return.

If the IRS agrees with the taxpayer's proposed reporting positions, or if the IRS and the taxpayer resolve differences of opinion about the reporting positions, then the IRS will not audit the transactions in the tax return after it is filed. CAP thus is a real-time review of tax positions that a taxpayer proposes to take. CAP is an alternative to post-filing audits that the IRS conducts of tax returns after the end—sometimes long after the end—of the taxable year.

The objective of CAP is an agreement between the IRS and the taxpayer of intended return positions that the IRS deems worthy of review. If a CAP review is successful, it completely eliminates a need for a post-filing audit of a tax return. It also obviates the need for financial statement tax reserves and disclosures of uncertain tax positions for the obvious reason that CAP has resolved all the tax uncertainties before the taxpayer files its tax return. The essential element for CAP to work successfully is the taxpayer's disclosure of its transactions and candor concerning tax positions. Similarly, the IRS must be willing to work collaboratively with the taxpayer to resolve issues.

CAP is in stark contrast to the IRS's traditional post-filing audits of federal tax returns because CAP requires a taxpayer to volunteer disclosures of transactions to the IRS. Although volunteerism in the context of an interaction with the IRS might seem unusual to many taxpayers, currently mandated disclosures in tax returns substantially diminish any perceived advantage gained from a reactive approach in a post-filing audit.

CAP clearly is not for every taxpayer. Some taxpayers find that despite good intentions, some issues are so intractable that their resolution in CAP is unlikely. Also, some taxpayers want additional time following the filing of a tax return to analyze an issue so that they can formulate the optimal rationale to support a return position if challenged. The speed with which the IRS and a taxpayer have to deal with an issue during the taxable year in CAP deprives a taxpayer of this additional analytical time.

CAP currently has 160 participants, all of which are large corporations and many of which are automotive original equipment manufacturers and suppliers. Those who have participated find, for the most part, that the benefit of an early determination of federal tax liabilities outweighs the burden of a sometimes interminable dispute associated with traditional post-filing audits.

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