HAWKINS ADVISORY

New IRS Audit Procedures

At the National Association of Bond Lawyers annual Bond Attorneys' Workshop, held in Chicago October 4-6, practitioners learned of certain changes to the Internal Revenue Service's audit practices relating to tax-exempt and other tax-advantaged bonds. Bond issuers should be aware of the following developments:

- The initial letter sent by the IRS will be a form letter that does not identify the reason a bond issue was chosen for examination. Previously, the IRS letter described whether the bond issue was chosen in connection with a targeted compliance area or as part of a routine (random) process.
- An issuer or its legal counsel should communicate by phone, and not in writing, with an IRS examiner as soon as possible after receipt of a letter informing it of an audit.
- Once an issuer or its counsel submits a written response to an Information Document Request ("IDR"), the audit must proceed to a conclusion; i.e., the IRS field agent cannot decide not to examine the bonds. This is true even if there are no compliance concerns with the bond issue; e.g., the bonds were redeemed beyond the statute of limitations period.
- The IRS will send a Notice of Noncompliance, IRS Form 5701, to an issuer in the event a tax problem has been identified (i.e., issuers will no longer receive "adverse IDRs" that raise the question of whether interest on the bond issue is taxable); this may raise certain disclosure concerns.
- According to the IRS Work Plan for Fiscal Year 2018, the targeted compliance areas are:
  - (a) arbitrage requirements for tax-advantaged bonds with guaranteed investment contracts (GICs), hedges and investments beyond the permitted three-year temporary period;
  - (b) the rehabilitation requirement for private activity bonds used to acquire existing property;
  - (c) remedial actions taken when bond-financed facilities have an excessive amount of private business use; and
  - (d) deep discount bonds and private activity bonds that have excessive weighted average maturities.

Any questions regarding the foregoing may be addressed to a member of the Hawkins Delafield & Wood LLP Tax Department.

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