taxnotes federal
Volume 181, Number 1 ■ October 2, 2023

To Disclose or Not to Disclose (and How and When)

by Andrew R. Roberson and Mary I. Slonina

Reprinted from *Tax Notes Federal*, October 2, 2023, p. 113

To Disclose or Not to Disclose (and How and When)

Andrew R. Roberson and Mary I. Slonina

Andrew R. Roberson is a principal and Mary I. Slonina is a managing director in the tax controversy and dispute resolution group of the Washington National Tax Practice of KPMG LLP.

In this article, Roberson and Slonina explain how recently updated rules and forms affect various mandatory and voluntary disclosures on tax returns.

This article represents the views of the authors only and does not necessarily represent the views or professional advice of KPMG LLP. Any errors remain the authors' own.

The Internal Revenue Code, Treasury regulations, and Internal Revenue Bulletin guidance contain myriad rules regarding disclosures on federal tax returns. Some disclosures are mandatory while others are voluntary. For example, some corporations are required to disclose their uncertain tax positions.[1] On the other hand, taxpayers seeking to avoid penalties may voluntarily attach forms to their tax returns, disclosing the tax treatment of specific items. Similarly, eligible taxpayers that are part of the IRS large corporate compliance (LCC) program might make some disclosures at the beginning of an IRS audit (sometimes referred to as affirmative disclosures or "walk-ins").[2]

The ramifications of incomplete or missing disclosures can be dire, ranging from the imposition of penalties to the failure to start the running of the statute of limitations on assessment. On the other hand, properly made disclosures can protect against the future assertion of penalties (or preserve some penalty defenses) and ensure that the statute of limitations on assessment expires within the normal three-year period. Recent actions and guidance by the IRS reflect a trend toward sturdier and more transparent disclosures, creating challenging strategic questions for taxpayers not only as they prepare their tax returns but also when they receive notice of an IRS examination. This article touches on some of the disclosure requirements and options and provides insights for taxpayers facing questions on if, when, and how to disclose on their tax returns.

Required Disclosures

At first glance, the standard IRS federal tax return forms for individuals (Form 1040 — two pages), partnerships (Form 1065 — five pages), and corporations (Form 1120 — six pages) do not seem too daunting. However, in addition to reporting items such as income, deductions, credits, and payments on these forms, taxpayers generally must attach various other schedules and statements. Some of the additional materials are necessary to comply with mandatory reporting requirements that do not directly bear on tax liability computations but provide the IRS with other information about the taxpayer.

Examples include Schedule UTP, "Uncertain Tax Position Statement," which is used by corporations to report uncertain tax positions (that is, the recording of a liability for

[1] *See* Chandra Wallace, "Final Schedule UTP Retains Expanded Disclosure Mandates," *Tax Notes Federal*, Jan. 2, 2023, p. 117.

[2] Rev. Proc. 2022-39, 2022-49 IRB 1; IRS Form 15307, "Post-Filing Disclosures for Specific Large Business Taxpayers."

unrecognized tax benefits for a tax position in audited financial statements),[3] and Form 8886, "Reportable Transaction Disclosure Statement," which is used to disclose information for each reportable transaction in which the taxpayer participated.[4] The following discussion will focus on the disclosure requirement for uncertain tax positions, in light of recent updates to Schedule UTP.

Schedule UTP was first introduced in 2010 with the goal of providing the IRS with "more complete information earlier in the process regarding the nature and materiality of a taxpayer's uncertain tax positions."[5] In 2018 the Treasury Inspector General for Tax Administration released a report finding that Schedule UTP was "not useful" based on a polling of IRS revenue agents.[6]

TIGTA's report spurred the IRS to publish a revised draft Schedule UTP on October 11, 2022, along with corresponding instructions and requested comments on the new proposed requirements. The draft Schedule UTP and instructions required substantial additional information to be disclosed and, in a controversial move, required taxpayers to identify all "contrary authority" and provide more detail on the facts surrounding the uncertain tax position in the form's "concise description" field.

The identification of contrary authority was extremely broad, extending beyond traditional forms of authority such as court cases, regulations, and guidance published in the Internal Revenue Bulletin (for example, revenue rulings, revenue procedures, notices, and announcements) to "private guidance" such as technical advice memorandums, chief counsel advice, private letter rulings, field service advice, and general counsel memorandums.[7] And, despite the IRS indicating that the draft Schedule UTP was intended to request information similar to what taxpayers can voluntarily disclose on Form 8275, "Disclosure Statement," and Form 8275-R, "Regulation Disclosure Statement," the contrary authority requirement extended beyond what taxpayers were permitted to voluntarily disclose.

In response to taxpayer and practitioner comments on the draft Schedule UTP and instructions, the IRS scaled back its list of "contrary authority" to remove the requirements to identify private guidance in the final "revised" Schedule UTP and instructions issued in December 2022. However, in the final version, the IRS retained a more expansive view of the meaning of a concise description, modifying the prior view (including eliminating the instruction that "the description should not exceed a few sentences") to provide: "To be considered complete, a description of the relevant facts affecting the tax treatment of the position and information that can reasonably be expected to apprise the IRS of the identity of the tax position, and the nature of the issue for which the tax position is being disclosed."[8] Three paragraphs were added to the instructions that provided guidance on the terms "description of the relevant facts affecting the tax treatment of the position," "identity of the tax position," and "the nature of the issue for which the tax position is being disclosed."

Taxpayers should be aware of the implications (both good and bad) of mandatory disclosure requirements. A tax return is filed under penalties of perjury and requires the taxpayer to affirmatively acknowledge that the signatory has

[3] Reg. section 1.6012-2(a)(4) ("A corporation required to make a return under this section shall attach Schedule UTP, Uncertain Tax Position Statement, or any successor form, to such return, in accordance with forms, instructions, or other appropriate guidance provided by the IRS.").

[4] Reportable transactions encompass the following five types of transactions: (1) listed transactions; (2) confidential transactions; (3) transactions with contractual protections; (4) loss transactions; and (5) transactions of interest. Reg. section 1.6011-4.

[5] IR-2010-13. For more background on the origins and history of Schedule UTP, see comments by Baker McKenzie LLP and KPMG LLP on the draft Schedule UTP (Nov. 18, 2022).

[6] TIGTA, "The Uncertain Tax Position Statement Does Not Contain Sufficient Information to Be Useful in Compliance Efforts," 2018-30-023 (2018).

[7] *See Zimmerman v. Commissioner*, 71 T.C. 367, 371 (1978), *aff'd without published opinion*, 614 F.2d 1294 (2d Cir. 1979) ("the authoritative sources of Federal tax law are in the statutes, regulations, and judicial decisions"); section 6110(k)(3) (generally providing that written determinations — that is, rulings, determination letters, technical advice memorandums, and chief counsel advice — may not be used or cited as precedent); reg. section 1.6662-4(d)(3)(iii) (listing types of authorities that may constitute "substantial authority"); *see also* McDermott Will & Emery, "Comments on Draft Changes to Schedule UTP and Instructions" (Nov. 14, 2022) (discussing the meaning of "authorities" for federal tax purposes).

[8] The IRS also rejected comments requesting delaying implementation of the new Schedule UTP, instead making the new form effective for 2022 tax year filings.

examined the return — including accompanying schedules and statements — and that to the best of the signatory's knowledge the return is true, correct, and complete. Thus, to state the obvious, taxpayers should always make all required disclosures to comply with the jurat requirement.

The failure to submit information and make all required disclosures, even if unintentional, can have dire consequences.[9] The statute of limitations on assessment may similarly remain open for tax attributable to listed transactions if the taxpayer fails to provide required information.[10] Also, the IRS can impose penalties for the failure to disclose some information[11] — even if the information has no bearing on the taxpayer's tax liability.[12]

On the plus side, meeting mandatory disclosure requirements can provide a benefit to taxpayers. For example, a properly completed Schedule UTP can provide penalty protection for taxpayers if the taxpayer's uncertain tax position is rejected in whole or in part.

Voluntary Disclosures

Tax law is not black and white — there are often gray areas that can lead to competing interpretations of how the law applies to a set of facts. Similarly, there are situations in which taxpayers may believe that Treasury regulations are contrary to the plain language of the code or represent an unreasonable interpretation of the code.[13]

To protect against potential penalties for a position that may be challenged and ultimately disallowed by the IRS or in court, taxpayers may, as warranted, proactively disclose their reporting positions. That is usually done through the filing of a properly completed Form 8275 (to disclose items or positions that are not otherwise adequately disclosed on a tax return to avoid penalties) or Form 8275-R (to disclose positions taken on a tax return that are contrary to Treasury regulations).[14] The forms require the taxpayer to provide general information and a detailed explanation of the issue that can reasonably be expected to apprise the IRS of the identity of the item, its amount, and the nature of the controversy or potential controversy.

With some exceptions (for example, tax shelter items), as long as the taxpayer has a reasonable basis for its return position and the relevant form is properly completed, the taxpayer will not be subject to some penalties.[15] Also, some voluntary disclosure rules can negate the application of a longer statute of limitations on assessment.[16]

Another common voluntary disclosure scenario arises regarding corporate taxpayers that are part of the LCC program. Historically, taxpayers that were part of the LCC program (or its predecessor programs) could follow the procedures in Rev. Proc. 94-69, 1994-2 C.B. 804, to disclose changes in tax positions after the opening of an examination. If taxpayers complied with the procedures of Rev. Proc. 94-69, they could avoid the imposition of some penalties on any additional tax owed because of the disclosure without the need to file a qualified amended return under reg. section 1.6664-2(c)(3).

[9] For purposes of this discussion, we assume that any failure does not rise to the level of conduct that might subject a taxpayer to criminal sanctions. *See, e.g.*, sections 7201-7207.

[10] Section 6501(c)(10); *see also Blak Investments v. Commissioner*, 133 T.C. 431 (2009).

[11] *See, e.g.*, section 6707A (penalty for failure to file Form 8886).

[12] *See* Internal Revenue Manual 20.1.9 (discussing international information reporting penalties).

[13] *See Chevron U.S.A. Inc. v. NRDC*, 467 U.S. 837 (1984) (setting forth the standard for when courts will defer to an agency's interpretation of a statute). It should be noted that the Supreme Court has agreed to hear a case this coming term on whether it should overrule *Chevron*. *See Loper Bright Enterprises v. Raimondo*, No. 22-451 (S. Ct.).

[14] The recently released green book proposes to impose an affirmative requirement on taxpayers to disclose a position on a return that is contrary to a regulation. Treasury Department, "General Explanations of the Administration's Fiscal Year 2024 Revenue Proposals" (Mar. 9, 2023).

[15] As clarified and confirmed by the revised Schedule UTP and instructions, forms 8275 and 8275-R are not necessary if a properly completed Schedule UTP is attached to the tax return.

[16] *See, e.g.*, section 6501(e)(1)(B)(iii) (in determining a six-year limitations period for an omission from gross income exceeding 25 percent of the proper amount of gross income, the amount omitted from gross income (other than in the case of an overstatement of unrecovered cost or other basis) should not take into account an amount omitted if such amount is disclosed in the return, or in a statement attached to the return, in a manner adequate to apprise the secretary of the nature and amount of such item).

In November 2022 the IRS obsoleted Rev. Proc. 94-69, replacing it with Rev. Proc. 2022-39, 2022-49 IRB 1, and requiring (eligible) taxpayers[17] to submit Form 15307, "Post-Filing Disclosures for Specific Large Business Taxpayers," which would be treated as a qualified amended return if properly completed. New Form 15307 requires substantially more information than was previously required under Rev. Proc. 94-69, including (like Schedule UTP and forms 8275 and 8275-R) a detailed explanation of the item providing the necessary facts and circumstances that reasonably may be expected to apprise the IRS of the nature of the item.

Taxpayer Considerations in Making Disclosures

In complying with mandatory disclosure requirements and voluntary disclosure rules, questions often arise about the proper scope of disclosure. What constitutes proper disclosure in a given situation may depend on the language of the code, Treasury regulations, or other IRS guidance (including instructions to disclosure forms). And, whether the IRS believes that a disclosure is proper and complete may initially depend on the views of a revenue agent or other examination team member (or local IRS counsel).

In the Schedule UTP context, this issue is fast approaching given the fall deadline for 2022 tax returns being filed on extension. Taxpayers need to carefully review the revised Schedule UTP and instructions to ensure that the information they provide will be deemed complete by the IRS. This includes determining whether a position is "contrary" to any court decisions, Treasury regulations, or Internal Revenue Bulletin guidance. Given that many tax reporting positions are based on the specific facts and circumstances of a taxpayer's situation, decisions must be made regarding whether one of the above authorities truly is contrary to the taxpayer's position.

In the Forms 8275 and 8275-R context, there have not been any recent changes to the forms. However, taxpayers should revisit these voluntary disclosure options to see whether it would be beneficial to make such voluntary disclosures. If the decision is made to voluntarily disclose a position, taxpayers should take care to ensure that such disclosures will be considered complete by the IRS to obtain penalty protection. And, as always, taxpayers taking a position contrary to a Treasury regulation and filing Form 8275-R need to be aware that submitting the form will trigger review of the tax position by the IRS and likely lead to litigation given the IRS's current stance that such positions may not be settled by exam teams and are ineligible for review by the IRS Independent Office of Appeals.[18]

Finally, LCC taxpayers must be prepared for the disclosure changes in Rev. Proc. 2022-39 and consider how best to prepare and submit Form 15307.[19] The new rules require more information, and as with other disclosures, taxpayers who identify an adjustment still risk facing penalties if the rules are not followed closely. Given that taxpayers generally need to make any such disclosures at the very beginning of the examination process, it will be important to be aware of these rules and have the information to make any disclosures readily available.[20] ■

[17] The disclosure procedures, and protections, of Rev. Proc. 2022-39 are available to *some* LCC taxpayers and large partnership compliance (LPC) taxpayers. An LCC taxpayer is eligible if, on the date on which the IRS first contacts the taxpayer concerning an examination of an income tax return, at least four of the taxpayer's income tax returns for the five tax years preceding the tax year at issue are (or were) under examination under the LCC program, the coordinated industry case program, or a successor program. An LPC taxpayer is eligible if, on the date on which the IRS first contacts the partnership concerning an examination of a return of partnership income, at least four of the partnership's returns for the five tax years preceding the tax year at issue are (or were) under examination under the LPC (or a successor program).

[18] *See* prop. reg. section 301.7803(2)(c)(19), REG-125693-19 (Sept. 13, 2022).

[19] A Form 15307 must be completed and provided to the appropriate IRS personnel no later than 30 days from the date of a written request by the IRS that the form be furnished. The 30-day window may be extended by agreement, in writing, with the IRS.

[20] The foregoing information is not intended to be "written advice concerning one or more federal tax matters" subject to the requirements of section 10.37(a)(2) of Treasury Department Circular 230. The information contained herein is of a general nature and based on authorities that are subject to change. Applicability of the information to specific situations should be determined through consultation with your tax adviser. This article represents the views of the author(s) only, and does not necessarily represent the views or professional advice of KPMG LLP.