July 15, 2008

Hon. Douglas Shulman
Commissioner
Internal Revenue Service
1111 Constitution Avenue, N.W.
Washington, DC 20224

Re: Comments on Notice 2007-88: Proposed Procedural Changes for Obtaining the Commissioner’s Consent to Change a Method of Accounting

Dear Commissioner Shulman:

Enclosed are comments in response to Notice 2007-88, regarding a proposal to change the process by which taxpayers obtain the Commissioner’s consent to change a method of accounting for federal income tax purposes. These comments represent the views of the American Bar Association Section of Taxation. They have not been approved by the Board of Governors or the House of Delegates of the American Bar Association, and should not be construed as representing the policy of the American Bar Association.

Sincerely,

Stanley L. Blend
Chair, Section of Taxation

Enclosures

cc: Hon. Donald L. Korb, Chief Counsel, Internal Revenue Service
Hon. Eric Solomon, Assistant Secretary (Tax Policy), Department of the Treasury
Karen Gilbreath Sowell, Deputy Assistant Secretary (Tax Policy), Department of the Treasury
Clarissa Potter, Deputy Chief Counsel (Technical), Internal Revenue Service
George Blaine, Associate Chief Counsel (Income Tax & Accounting), Internal Revenue Service
Stephen Larson, Associate Chief Counsel, Internal Revenue Service
Steven Musher, Associate Chief Counsel, Internal Revenue Service
William O’Shea, Associate Chief Counsel, Internal Revenue Service
Eric San Juan, Deputy Tax Legislative Counsel (Tax Legislation), Department of the Treasury
Brandon Carlton, Attorney-Advisor, Department of the Treasury
Andrew Keyso, Special Counsel to the Associate Chief Counsel, Internal Revenue Service
Brenda Wilson, Technical Advisor (Income Tax & Accounting), Internal Revenue Service
The following comments ("Comments") are submitted on behalf of the American Bar Association Section of Taxation (the "Section") and have not been approved by the House of Delegates or Board of Governors of the American Bar Association. Accordingly, they should not be construed as representing the position of the American Bar Association.

Principal responsibility for preparing these Comments was exercised by Carol Conjura of the Section’s Committee on Tax Accounting (the “Committee”). Substantive contributions were made by Kenneth Kempson, Ellen McElroy, Christian Wood, and Michael Salama. The Comments were reviewed by Jody Brewster, Chair of the Committee. The Comments were further reviewed by Jack Donovan of the Section's Committee on Government Submissions and by Helen Hubbard, Council Director for the Committee.

Although the members of the Section who participated in preparing these Comments have clients or are employed by companies that might be affected by the procedures addressed by these Comments, no such member or the firm or organization to which such member belongs has been engaged by a client to make a government submission with respect to, or otherwise to influence the development or outcome of, the specific subject matter of these Comments.

Contact Person:

Carol Conjura
(202) 533-3040
cconjura@kpmg.com

July 15, 2008
EXECUTIVE SUMMARY

Notice 2007-88\(^1\) (the "Notice") requests comments from the public regarding a proposal to change the procedures under which taxpayers obtain the consent of the Commissioner of the Internal Revenue Service (the "Service") to change a method of accounting. Under the current procedures, taxpayers are generally required to obtain advance consent to change a method of accounting pursuant to Rev. Proc. 97-27,\(^2\) unless the method is specifically designated by the Service as subject to the automatic consent procedure in Rev. Proc. 2002-9.\(^3\)

In the Notice, the Service proposes to permit taxpayers to make most accounting method changes under a procedure that resembles the current automatic consent procedure. Some accounting method changes would continue to be made with advance consent. For certain other changes, taxpayers would be permitted to obtain more certainty by requesting a private letter ruling.

The Section welcomes the opportunity to comment on the proposal set forth in the Notice, and commends the Service for its continued efforts to improve the procedures for obtaining the Commissioner's consent to change a method of accounting. We believe that the proposed procedures will both increase voluntary compliance and maintain the Service's ability to effectively monitor changes in accounting methods.

Overall, the Section believes the proposal in the Notice will improve the accounting method change procedures by making useful incremental changes. We also believe the proposed changes will reduce taxpayer burden. The Section submits several additional suggestions for improving the specific procedures set forth in the Notice. Specifically, the Section suggests that:

I. The forthcoming guidance clarify the consequences of changing under the new automatic consent procedure to a method that is not specifically identified in the automatic consent procedure guidance.

II. It is appropriate for the Service to respond to the need for advance review of accounting method changes by accelerating the due date for requests made under the new automatic consent procedure for methods that are not specifically identified in guidance.

III. The Service modify the 90-day window period for taxpayers under examination to permit year-end filings of Form 3115.

IV. In the case of any Form 3115 that is determined by the National Office not to be substantially complete, a resubmission filed by the taxpayer within 30 days

---

\(^1\) 2007-46 I.R.B. 993.
\(^2\) 1997-1 C.B. 680.
\(^3\) 2002-1 C.B. 327.
of that determination should be considered solely for purposes of audit protection to have been filed on the date of the original submission.

V. Taxpayers not be required to submit a section 481(a)\(^4\) adjustment any earlier than 90 days after the beginning of the year of change.

---

\(^4\) References to a "section" are to a section of the Internal Revenue Code of 1986, as amended, unless otherwise indicated.
DISCUSSION

The Service has well established administrative authority to prescribe the procedures, terms, and conditions under which taxpayers may obtain the Commissioner’s consent to change their accounting methods pursuant to section 446(e). The Service has modified these procedures over the years to increase the efficiency and transparency of the procedures. In recent years, the Service has increasingly relied on the automatic consent procedures in lieu of the advance consent procedures.

On February 27, 2007, prior to the issuance of the Notice and in response to a request from the Associate Chief Counsel (Income Tax & Accounting), the Section submitted a proposal for revising the current accounting method change procedures. The Section's proposal addressed problems frequently encountered by taxpayers in the execution of the current procedures (both the advance and automatic consent procedures).

In the Notice, the Service proposes to permit taxpayers to obtain consent to make accounting method changes under one of three procedures. First, taxpayers would make most accounting method changes under procedures that resemble the current automatic consent procedures ("Standard Consent"). Second, taxpayers would make selected types of accounting method changes that are designated by the Service under an advance consent procedure that resembles the current advance consent procedure ("Specific Consent"). Third, taxpayers would be permitted to forgo the otherwise applicable procedure (Standard or Specific Consent) and obtain advance consent by requesting a private letter ruling ("Letter Ruling Consent"), unless the change is specifically described in Rev. Proc. 2002-9 or any other automatic consent guidance.

The Notice also clarifies the consequences of following these procedures. For example, a taxpayer receiving consent to change its method of accounting for an item under either the Specific Consent or Letter Ruling Consent procedure would not be required to change its method of accounting for that item in any tax year earlier than the applicable year of change ("audit protection"). Such a taxpayer would also be assured that any change from the new permitted method would not be applied retroactively.

---

6 See Rev. Proc. 2002-9, supra note 3 (as amended numerous times to add more accounting method changes, the automatic consent procedures therein now apply to over 100 types of accounting method changes).
8 Specifically, the Section proposed that the Service permit taxpayers to make all accounting method changes under the existing automatic procedure, except as specifically provided otherwise. The Section further proposed that the Service provide the following two alternatives to the automatic procedure: (1) the option for a taxpayer to obtain a private letter ruling when more advance certainty is desired and (2) the option for a taxpayer to obtain advance consent on a more expedited basis but with less certainty than is afforded by a private letter ruling.
A taxpayer properly changing a method of accounting under the Standard Consent procedure would receive audit protection. A taxpayer properly changing a method of accounting under the Standard Consent procedure would also receive ruling protection for a change to a method specifically identified in Rev. Proc. 2002-9 or any other automatic consent guidance, but would not receive ruling protection for a change to a method not specifically identified in that guidance (an "Other Standard Consent Method").

The Section agrees with the basic premise of the Notice—that taxpayers should make most accounting method changes under the Standard Consent procedure unless the Service specifically designates the accounting method change as subject to the Specific Consent procedure. We believe that taxpayers are likely to find the Standard Consent procedure more efficient and effective than the Letter Ruling Consent procedure and will likely use the Standard Consent procedure most often. Taxpayers will benefit, however, from having the flexibility to use the Letter Ruling Consent procedure in appropriate circumstances, as provided in the Notice.

Although the Section generally endorses the approach taken in the Notice, it would be helpful in the Section's view to include in the final guidance certain modifications that the Section believes will increase taxpayer compliance, provide greater certainty, and generally improve the overall effectiveness of the Service's monitoring of accounting method changes. Our specific suggestions in this regard are discussed below.

I. CLARIFICATION OF CONSEQUENCES OF CHANGING TO AN "OTHER STANDARD CONSENT METHOD"

As noted above, under the Notice, a taxpayer changing to a method under either of the advance consent procedures (i.e., Specific Consent or Letter Ruling Consent) would receive ruling protection for the new method. In contrast, a taxpayer changing under the Standard Consent procedure would receive ruling protection for a method specifically identified in Rev. Proc. 2002-9 or any other automatic consent guidance, but would not receive ruling protection for an "Other Standard Consent Method."
The Section agrees that ruling protection is appropriate when the Service has sufficiently reviewed the new method to determine that it is a permissible method for the taxpayer. Thus, the Section agrees with the Service's conclusion that a taxpayer should not receive ruling protection for an Other Standard Consent Method.

The Section suggests, however, that the Service clarify the consequences of changing to an Other Standard Consent Method. Specifically, it is anticipated that, on audit, an examination team ("Exam") will first determine whether the requested Other Standard Consent Method is a permissible method for the particular taxpayer. If the requested method is permissible, we suggest that the focus of the audit should shift to ensuring that the taxpayer has applied the requested method to its facts in accordance with the Service's position. On the other hand, if and only if Exam determines that the requested Other Standard Consent Method is not a permissible method for the particular taxpayer, Exam would be able to change the taxpayer's method to a permissible method (for example, to the taxpayer's prior method if that method was permissible, or to another permissible method).

We believe this clarification will encourage use of the Standard Consent procedure to change to Other Standard Consent Methods (thus, reducing the number of changes for which taxpayers will request consent under the Letter Ruling Consent procedure). We also believe that this approach appropriately takes into account the increased complexity of the tax law and the complex factual circumstances many taxpayers face. Under this approach, taxpayers will have assurance that they will be permitted to change to a permissible Other Standard Consent Method under the Standard Consent procedure notwithstanding that the taxpayer will not obtain ruling protection for the new method. At the same time, the interests of the Service will be protected because Exam will have the authority to determine the permissibility of the taxpayer's requested method and of the taxpayer's application of the requested method to its facts.

For example, assume a taxpayer has been erroneously including nontaxable deposits in taxable income upon receipt and files a request under the Standard Consent procedure to change its method of accounting to exclude nontaxable deposits from taxable income. The new method is not specifically identified in Rev. Proc. 2002-9 or any other automatic consent guidance, and thus the new method would be an Other Standard Consent Method. Also assume the taxpayer implements the new method, including a good faith determination as to which receipts are eligible to be treated as nontaxable deposits. Further assume that the new method described by the taxpayer in its Form 3115 is permissible for the taxpayer, but that the taxpayer has characterized some amounts as nontaxable deposits that should have been characterized as taxable upon receipt.

Under the Section's suggestion, Exam would have authority to determine that the requested method is permissible and to evaluate which amounts are correctly treated as nontaxable deposits under that permissible method. Under these facts, Exam would be able to change the taxpayer's application of its new method so that amounts improperly

---

treated as nontaxable deposits would be properly treated as taxable upon receipt. Exam
would not, however, be able to change the taxpayer back to its old impermissible method
or to another permissible method.

II. FORM 3115 DUE DATES

Under the existing automatic consent procedure, the Commissioner's consent is
deemed to be granted when a properly completed original Form 3115 is filed with the
taxpayer's timely filed tax return for the year of change, and a copy is filed with the
National Office on or before the due date of that return. The Notice proposes to retain
this post-year-end filing due date for changes made under the Standard Consent
procedure to a method specifically identified in Rev. Proc. 2002-9 or any other automatic
consent guidance. In contrast, in the case of method change requests made under the
Specific Consent or Letter Ruling Consent procedure, the Notice proposes to accelerate
the due date for filing the requests to the last day of the ninth month of the year of
change. The Notice requests comments on whether the due date for filing a request to
change to an Other Standard Consent Method should also be accelerated to the last day of
the ninth month of the year of change.

The proposed acceleration of the due date for method change requests made under
the Specific Consent or Letter Ruling Consent procedure is consistent with the purposes
and operational realities of the proposed new procedures. The earlier due date for such
requests would provide the Service with sufficient lead time to consider and act on each
advance consent request prior to the filing of the taxpayer's return. The Section
recognizes that accelerating the due date for requests to change to an Other Standard
Consent Method would also be appropriate from an administrative and enforcement
perspective, and the Section supports the acceleration of the due date for those requests
should the Service decide to do so.

The Section also agrees that, as stated in the Notice, any such requests filed after
the ninth month of a tax year should be treated as applications to change in the following
tax year and that this should be clearly stated in the procedural guidance.

III. WINDOW PERIODS FOR TAXPAYERS UNDER EXAMINATION

Under current procedures, a taxpayer under examination generally is precluded
from requesting a voluntary change from an impermissible method that understates
taxable income unless it requests the change in one of two window periods. Although

---

13 Under the existing advance consent procedure, a Form 3115 need only be filed within the year of change. See Rev.
Proc. 97-27, supra note 2, section 5.01(1)(a).
14 The two windows are: (1) the 120-day period beginning with the end of an examination cycle, and (2) the
first 90 days of any tax year, provided the taxpayer had been under examination for at least 12
consecutive months as of the beginning of that tax year. Rev. Proc. 97-27, supra note 2, section 6.03(2)-(3); Rev. Proc. 2002-9, supra note 3, section 6.01(2)-(3). A taxpayer otherwise precluded from using a
window period may nonetheless file a Form 3115 when the accounting method being changed is a pending
the Notice does not specifically request comments on the current Exam window periods, the Section suggests that the two window periods be retained, but that the 90-day window period be modified to permit year-end filings.

Under current procedures, the 90-day window period is the first 90 days of a taxpayer's tax year. The 90-day window thus does not permit a taxpayer under examination and seeking to change from an impermissible method near the end of a tax year to request the change prior to the end of that tax year even though the need for the change has already been identified and the taxpayer is prepared to take corrective action. This frustrates voluntary compliance by making the taxpayer wait to obtain audit protection for the change. In addition, in the taxpayer's audited financial statements for the tax year preceding the 90-day window, the taxpayer may not be allowed to anticipate that the change will be made with audit protection.

The Section suggests that the Service modify the 90-day window period so that it begins 30 days prior to the end of the tax year and ends 60 days after the beginning of the subsequent tax year. If a taxpayer files a request during the first 30 days of the revised 90-day window, the year of change will be determined by the applicable procedure. In addition, as under the current procedures, a taxpayer would qualify under the 90-day window only if the taxpayer has been under examination for at least 12 consecutive months as of the first day of the tax year that begins within the 90-day window. (Under the Section's suggested approach, the first day of the tax year that begins within the 90-day window would differ from the first day of the 90-day window.)

IV. THE REQUIREMENT OF SUBSTANTIAL COMPLETENESS

The Notice indicates that requests that are not substantially complete will be denied. The Section generally agrees with this approach. The Section suggests, however, that to preserve audit protection the Service consider granting a taxpayer changing from an impermissible method a limited ability to retain its original filing date by curing any defects within a short timeframe.

The Notice provides that the National Office will screen all method change requests for completeness and compliance with the governing procedure. If a request is not substantially complete, the Notice also provides that the taxpayer may be notified that consent is denied. The Section suggests that the procedural guidance clarify that any determination as to whether a method change request is substantially complete may only be made by the National Office in its review of such requests (as opposed to Exam in the audit process).

issue in the examination, but the taxpayer merely receives consent to change to the permissible method currently and is not protected from adjustments on audit. Rev. Proc. 2002-19, 2002-1 C.B. 696.

15 Thus, if the taxpayer uses the Standard Consent Request procedure to change to a specifically identified method, the year of change may be either the tax year of filing or the subsequent tax year. In all other cases in which a taxpayer files its Form 3115 in the first 30 days of the revised 90-day window, the year of change would be the subsequent tax year.
The Notice generally explains the meaning of substantial completeness:

For example, a Form 3115 must include sufficient information about the current and new methods of accounting to permit the IRS to understand how the methods work, and must identify legal authority (including any contrary authority) governing the new method of accounting. However, minor omissions or errors on Form 3115 would not result in the denial of consent.  

Further, the Notice states that the Service plans to provide examples of what constitutes a substantially complete Form 3115.

The Section applauds the approach to "completeness" suggested in the Notice. The Section agrees that the focus of the completeness inquiry should be on the substance of the method change, rather than inadvertent and immaterial omissions. Examples that clarify this focus will be helpful.

Further, the process proposed in the Notice permits the Service to deny incomplete requests without entering into a time-consuming and lengthy dialogue with taxpayers about the sufficiency of their requests. This recognizes the importance of substantial completeness in the consent process, and it is likely to permit the Service to focus more on the substance rather than the processing of method change requests.

We note, however, that under current procedures, the Service explicitly permits taxpayers to perfect requests that are incomplete. This policy was an informal but consistent practice long before it became explicit. The current policy is the same as the policy that applies to private letter ruling requests.

The Section is concerned that the proposal might unduly disqualify the submissions of many taxpayers who have acted in good faith to change from an impermissible method. The Section therefore suggests that the Service consider treating resubmissions by a taxpayer within 30 days of a denial for incompleteness as filed on the date of the original submission solely for purposes of audit protection. Thus, if the resubmission is filed after the due date of the original Form 3115, and the resubmission is complete, the year of change would be based on the date of the resubmission, but the taxpayer would be considered to have obtained audit protection as of the date the original submission was filed. However, if the resubmission is not substantially complete, there would be no third "bite at the apple" for audit protection.

19 The Service may wish to provide that, in the case of a method change with a positive section 481(a) adjustment, the original filing date would also determine the year of change. This would deny the taxpayer the unintended benefit of an additional tax year or years under the impermissible method.
This approach would avoid consuming National Office resources, while granting taxpayers under current or potential audit a fair chance to cure inadvertent errors. The Service need not enter into a dialogue with taxpayers regarding an incomplete request, but only need notify them of the initial denial. The Section assumes that the Service would impose other requirements to appropriately protect its interests. For example, the Service may want to consider:

- Requiring taxpayers to provide an appropriate legend at the top of the resubmitted Form 3115 noting the date of the initial, incomplete submission; and

- Not allowing any resubmission if the taxpayer did not describe its current method sufficiently well to determine if the item has previously been raised on audit.

Thus, if a taxpayer under audit filed an incomplete, good faith submission at the end of the 90-day window, the resubmission would still be considered to have been filed within the window. On the other hand, the taxpayer could not attempt to "rework" an ambiguous definition of the current method to avoid an issue raised on audit in the interim.

Coupled with the reasonable approach to substantial completeness suggested in the Notice, this limited ability to retain audit protection would strengthen the incentives for voluntary compliance already contained in the existing and proposed method-change procedures.

V. TIME FOR SUBMITTING SECTION 481(a) ADJUSTMENT

A section 481(a) adjustment for any method change is computed as of the last day of the tax year immediately prior to the year of change. Thus, in any case in which a taxpayer's request for a method change is filed prior to the year of change, it is impossible for the taxpayer to include on the Form 3115 the amount of the section 481(a) adjustment. Similarly, if a taxpayer files its method change request very early in the year of change, computation of the section 481(a) adjustment may be difficult because the prior year's financial and tax information may not yet be available.

The Section suggests that the Service clarify in procedural guidance that taxpayers are not required to submit a section 481(a) adjustment any earlier than 90 days after the beginning of the year of change. The Section assumes that the National Office also will continue its current practice of accepting and encouraging corrections to and refinements of any section 481(a) adjustment previously submitted.