



FSLG Examination Process

The following information explains what a government entity can expect during a compliance check or an examination conducted by FSLG. You may also find information with regard to adequate record keeping by government entities, disclosure constraints on the IRS and consent by government entities authorizing the IRS to disclose tax information to third parties.

- [Government Entity Compliance Toolkit](#)
This toolkit explains what a government entity can expect during a compliance check or an examination conducted by FSLG. It also provides information with regard to adequate record keeping by government entities, disclosure constraints on the IRS and consent by government entities authorizing the IRS to disclose tax information to third parties.
- [New Guides to the FSLG Exam Process](#)
Flowcharts illustrate the steps of a government entity examination.
- [FSLG Compliance Program: Compliance Checks and Examinations](#)
The purposes of compliance checks and examinations, and the differences between them.
- [What Occurs During an Examination](#)
What a government entity can expect during an examination, including the types of questions asked during an examination, the kinds of information requested, and possible outcomes of an examination.
- [What Occurs During a Compliance Check](#)
What a government entity can expect during a compliance check, including the types of questions asked during a compliance check, the kinds of information requested, and possible outcomes of a compliance check, also includes sample compliance check opening and closing letters, pro forma information document requests, etc.
- [Basic Recordkeeping for Employment Taxes and Information Return Reporting](#)
Suggestions about methods for maintaining employment tax records and vendor information. What records must be maintained by a government entity with respect to an employment tax exam.
- [Common Issues in FSLG Examinations](#)
The major tax law areas where we most frequently find compliance problems when examining government entities, and where to get more information on how to check or improve your compliance in these areas.
- [Appeals Process](#)
Information about IRS Appeals Office and the procedure for requesting review by the Office of Appeals of an adverse determination made by FSLG after an examination.

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The IRS Mission

Provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities and by applying the tax law with integrity and fairness to all.



**Department of the Treasury
Internal Revenue Service**

www.irs.gov

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The Examination Process

Introduction

The Internal Revenue Service (IRS) accepts most federal returns as filed. Some returns, however, are examined, or audited, to determine if income, expenses, and credits are reported accurately.

This publication discusses general rules and procedures we follow in examinations. It explains what happens before, during, and after an examination. It also explains appeal and payment procedures.

As a taxpayer, you have the right to fair, professional, prompt, and courteous service from IRS employees, as outlined in the Declaration of Taxpayer Rights found on page 3.

We must follow the tax rules set forth by Congress in the Internal Revenue Code. We also follow Treasury Regulations, court decisions, and other rules and procedures written to administer the tax laws.

If the examination results in a change to your tax liability, you may ask us to reconsider your case. Some reasons why we may reconsider your case include:

- You are submitting additional information that could result in a change to the additional amount we have determined that you owe;
- You are filing an original delinquent return after we have determined that you owe an additional amount, or;
- You are identifying a mathematical or processing error we made.

You must request reconsideration in writing and submit it to your local IRS office.

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? Do you have questions or need help right away? Call us. We are here to help you.

For General Information:

For information about a specific examination please contact the person named on the appointment letter.



For tax information and help:

Call the number on the bill you received or call us toll free at:

1-800-829-1040 (for 1040 filers)

1-800-829-4933 (for business filers)

1-800-829-4059 /TDD



For tax forms and publications:

1-800-829-3676

1-800-829-4059 /TDD

1-703-368-9694-Forms by Fax



Internet: www.irs.gov

FTP- [ftp.fedworld.gov/pub/](ftp://ftp.fedworld.gov/pub/)

TELENET-iris.irs.gov

You'll find answers to frequently asked tax questions, tax forms on-line, searchable publications, hot tax issues, news, and help through e-mail.



If you prefer to write to us . .

Enclose a copy of your tax bill. Print your name, social security number or taxpayer identification number, and the tax form and period shown on your bill. Write to us at the address shown on your tax bill.



You may also visit your nearest IRS Office.

You'll find the exact address in your local phone book under *U.S. Government*

Declaration of Taxpayer Rights

I. Protection of Your Rights

IRS employees will explain and protect your rights as a taxpayer throughout your contact with us.

II. Privacy and Confidentiality

The IRS will not disclose to anyone the information you give us, except as authorized by law. You have the right to know why we are asking you for information, how we will use it, and what happens if you do not provide requested information.

III. Professional and Courteous Service

If you believe that an IRS employee has not treated you in a professional, fair, and courteous manner, you should tell that employee's supervisor. If the supervisor's response is not satisfactory, you should write to the IRS Director for your Area or the Center where you file your return.

IV. Representation

You may either represent yourself or, with proper written authorization, have someone else represent you. Your representative must be a person allowed to practice before the IRS, such as an attorney, certified public accountant, or enrolled agent (a person enrolled to practice before the IRS). If you are in an interview and ask to consult such a person, then we must stop and reschedule the interview in most cases.

You can have someone accompany you at an interview. You may make sound recordings of any meetings with our examination, appeal, or collection personnel, provided you tell us in writing 10 days before the meeting.

V. Payment of Only the Correct Amount of Tax

You are responsible for paying only the correct amount of tax due under the law—no more, no less. If you cannot pay all of your tax when it is due, you may be able to make monthly payments.

VI. Help with Unresolved Tax Problems

The Taxpayer Advocate Service can help you if you have tried unsuccessfully to resolve a problem with the IRS. Your local Taxpayer Advocate can offer you special help if you have a significant hardship as a result of a tax problem. For more information, call toll-free, 1-877-777-4778 (1-800-829-4059 for TTY/TDD) or write to the Taxpayer Advocate at the IRS office that last contacted you.

VII. Appeals and Judicial Review

If you disagree with us about the amount of your tax liability or certain collection actions, you have the right to ask the Appeals Office to review your case. You may also ask a court to review your case.

VIII. Relief from Certain Penalties and Interest

The IRS will waive penalties when allowed by law if you can show you acted reasonably and in good faith or relied on the incorrect advice of an IRS employee. We will waive interest that is the result of certain errors or delays caused by an IRS employee.

Your Return Is Going To Be Examined.

Before the Examination

We accept most taxpayers' returns as filed. If we inquire about your return or select it for examination, it does not suggest that you are dishonest. The inquiry or examination may or may not result in more tax. We may close your case without change or you may receive a refund.

The process of selecting a return for examination usually begins in one of two ways. One way is to use computer programs to identify returns that may have incorrect amounts. The programs may be based on information returns, such as Forms 1099 or W-2, on studies of past examinations, or on certain issues identified by other special projects. Another way is to use information from compliance projects that indicates a return may have incorrect amounts. These sources may include newspapers, public records, and individuals. If we determine the information is accurate and reliable, we may use it to select a return for examination.

Publication 556, *Examination of Returns, Appeal Rights, and Claims for Refund*, explains the rules and procedures that we follow in examinations. The following sections give an overview of how we conduct examinations.

During the Examination

Examinations by Mail

Some examinations are conducted entirely by mail. If the examination is conducted by mail, you'll receive a letter from us asking for additional information about certain items shown on your return, such as income, expenses, and itemized deductions.

If the examination is conducted by mail, you can:

1. Act on your own behalf. (In the case of a jointly filed return, either spouse can respond or both spouses can send a joint response.)
2. Have someone represent you in correspondence with us. This person must be an attorney, accountant, enrolled agent, an enrolled actuary, or the person who prepared the return and signed it as the preparer. If you choose to have someone represent you, you must furnish us with written authorization. Make this authorization on Form 2848, *Power of Attorney and Declaration of Representative*.

Note: You may obtain any of the forms and publications referenced in this publication by calling 1-800-829-3676.

Examinations in Person

An examination conducted in person begins when we notify you that your return has been selected. We will tell you what information you need to provide at that time. If you gather the information before the examination, we may be able to complete it more easily and in a shorter time.

If the examination is conducted in person, it can take place in your home, your place of business, an IRS office, or the office of your attorney, accountant, or enrolled agent (a person enrolled to practice before the IRS). If the time or place is not convenient for you, the examiner will try to work out something more suitable.

Your Return Is Going To Be Examined. (cont.)

If the examination is conducted in person, you can:

1. Act on your own behalf. (*In the case of a jointly filed return, either spouse or both can attend the interview.*) If you are acting on your own behalf, you may leave to consult with your representative. We will suspend the interview and reschedule the examination. We cannot suspend the interview if we are conducting it as a result of your receiving an administrative summons.
2. Have someone accompany you, either to support your position or to witness to the proceedings.
3. Accompany someone who will represent you. This person must be an attorney, accountant, enrolled agent, an enrolled actuary, or the person who prepared the return and signed it as the preparer.
4. Have your representative act for you and not be present at the audit yourself. If you choose to have someone represent you in your absence, you must furnish us with written authorization. Make this authorization on **Form 2848, Power of Attorney and Declaration of Representative**.

How to Stop Interest from Accumulating

During your examination, if you think you will owe additional tax at the end of the examination, you can stop interest from accumulating by paying all or part of the amount you think you will owe. Interest will stop accumulating on the part you pay when the IRS receives your money. Interest will only be charged on the tax, penalties, and interest that are unpaid on the date they are assessed.

Consents to Extend the Statute of Limitations

We try to examine tax returns as soon as possible after they are filed, but occasionally we may request that you extend the statute of limitations of your tax return.

A return's statute of limitation generally limits the time we have to examine it and assess tax. Assessments of tax must be made within 3 years after a return is due or filed, whichever is later. We can't assess additional tax or make a refund or credit (*unless you filed a timely claim*) after the statute of limitations has expired. Also, if you disagree with the results of the examination, you can't appeal the items you disagree with unless sufficient time remains on the statute. Because of these restrictions, if there isn't much time remaining to examine your return, assess additional taxes, and/or exercise your appeal rights, you have the opportunity to extend the statute of limitations. This will allow you additional time to provide further documentation to support your position, request an appeal if you do not agree with our findings, or to claim a tax refund or credit. It also allows the Service time to complete the examination, make any additional assessment, if necessary, and provide sufficient time for processing.

A written agreement between you and the Service to extend the statutory period of a tax return is called a "consent." Consents can be used for all types of tax except estate tax.

There are two basic kinds of consent forms. One sets a specific expiration date for the extension, and the other for an indefinite period of time. Either type of consent may be limited by restrictive conditions. The use of a restricted consent is to allow the statute to expire with regard to all items on the return except those covered by the restrictive language.

If the statute of limitations for your tax return is approaching, you may be asked to sign a consent. You may:

1. Refuse to extend the statute of limitations;
2. Limit or restrict the consent to particular issues, or
3. Limit the extension to a particular period of time.

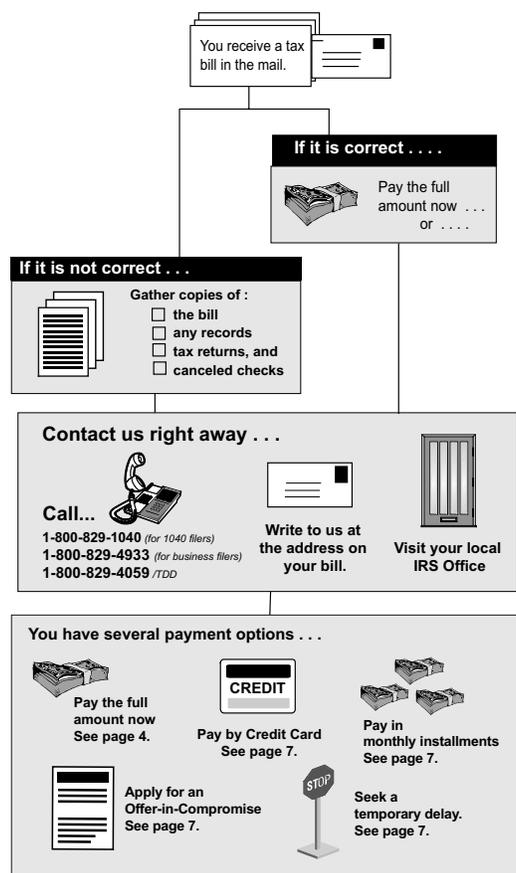
The consent will be sent or presented to you with a letter explaining this process and **Publication 1035, Extending the Tax Assessment Period**. For further information, refer to this publication.

Results of the Examination

If we accept your return as filed, you will receive a letter stating that the examiner proposed no changes to your return. You should keep this letter with your tax records.

If we don't accept your return as filed, we will explain any proposed changes to you and your authorized representative. It is important that you understand the reasons for any proposed changes; don't hesitate to ask about anything that is unclear to you.

What to Do When You Receive a Bill from the IRS



What To Do If You Agree or Disagree with the Examination Results

If You Agree

If you agree with a proposed *increase* to tax, you can sign an agreement form and pay any additional tax you may owe. You must pay interest and applicable penalties on any additional balance due. If you pay when you sign the agreement, interest is generally figured from the due date of your return to the date of your payment.

If you do not pay the additional tax and interest, you will receive a bill (See *"What To do When You Receive a Bill from the IRS" on page 4.*) If the amount due (including interest and applicable penalties) is less than \$100,000 and you pay it within 21 business days, we will not charge more interest or penalties. If the amount is \$100,000 or more, the period is reduced to 10 calendar days. If you can't pay the tax due at the end of the examination, you may pay whatever amount you can and request an installment agreement for the balance. (See *"Setting up an Installment Agreement" on page 7.*)

If you are entitled to a refund, you will receive it sooner if you sign the agreement form at the end of the examination. You will also be paid interest on the refund.

If You Do Not Agree

If you do not agree with the proposed changes, the examiner will explain your appeal rights. If your examination takes place in an IRS office, you may request an immediate meeting with the examiner's supervisor to explain your situation. You may also enter into an *Agreement to Mediate* to help resolve disputes through Fast Track Mediation services. (See *next column.*) Mediation can take place at this meeting or afterwards. If an agreement is reached, your case will be closed.

If you cannot reach an agreement with the supervisor at this meeting, or if the examination took place outside an IRS office or was conducted through correspondence with an IRS Campus employee, the examiner will prepare a report explaining your position and ours. The examiner will forward your case to the Area office for processing .

You will receive:

- A letter (known as a 30-day letter) notifying you of your rights to appeal the proposed changes within 30 days,
- A copy of the examiner's report explaining the proposed changes, and
- An agreement or a waiver form.

You generally have 30 days from the date of the 30-day letter to tell us whether you will accept the proposed changes or appeal them. The letter will explain what steps you should take, depending on what action you choose. Be sure to follow the instructions carefully. Appeal rights are explained following this section.



If you do not respond to the 30-day letter, or if you respond but do not reach an agreement with an appeals officer, we will send you a 90-day letter, also known as a *Notice of Deficiency*. This is a legal document that explains the proposed changes and the amount of the proposed tax increase. You will have 90 days (150 days if it is addressed to you outside the United States) from the date of this notice to file a petition with the Tax Court. If you do not petition the Tax Court you will receive a bill for the amount due.

Fast Track Mediation Services

If you do not agree with any or all of the IRS findings, you may request Fast Track Mediation services to help you resolve disputes resulting from the examination (audits). Fast Track Mediation offers an expedited process with a trained mediator, who will help facilitate communication, in a neutral setting. The mediator will work with you and the IRS to understand the nature of the dispute. The purpose is to help the two of you reach a mutually satisfactory resolution that is consistent with the applicable law. The mediator has no authority to require either party to accept any resolution. You may withdraw from the mediation process anytime. If any issues remain unresolved you will retain all of your usual appeal rights.

Most cases qualify for Fast Track Mediation. To begin the process, you may request the examiner or IRS representative to arrange a mediation meeting. Both you and the IRS representative must sign a simple *Agreement to Mediate* form. A mediator will then be assigned. Generally, within a week, the mediator will contact you and the IRS representative to schedule a meeting. After a brief explanation of the process, the mediator will discuss with you when and where to hold the mediation session.

For additional information, refer to Publication 3605, *Fast Track Mediation-A Process for Prompt Resolution of Tax Issues*.

How Do You Appeal a Decision?

The Appeal System

Because people sometimes disagree on tax matters, the Service has an appeal system. Most differences can be settled within this system without going to court.

Your reasons for disagreeing must come within the scope of tax laws, however. For example, you cannot appeal your case based only on moral, religious, political, constitutional, conscientious, or similar grounds.

If you do not want to appeal your case within the IRS, you may take your case directly to tax court.

Appeal Within the IRS

You may appeal our tax decision to a local appeals office, which is separate and independent of the IRS Office taking the action you disagree with. An appeals office is the only level of appeal within the IRS. Conferences with Appeals Office personnel may be conducted in person, through correspondence, or by telephone with you or your authorized representative.

If you want to have a conference with an appeals officer, follow the instructions in the letter you received. We will send your conference request letter to the appeals office to arrange for a conference at a convenient time and place. You or your qualified representative should be prepared to discuss all disputed issues at the conference. Most differences are settled at this level. Only attorneys, certified public accountants or enrolled agents are allowed to represent a taxpayer before Appeals. An unenrolled preparer may be a witness at the conference, but not a representative.

If you want to have a conference with an appeals officer, you may also need to file either a **small case request** or a **formal written protest** with the contact person named in the letter you receive.

Whether you file a small case request or a formal written protest depends on several factors.

Making a Small Case Request

You may make a **small case request** if the total amount of tax, penalties, and interest for *each* tax period involved is \$25,000 or less, and you do not meet one of the exceptions below for which a formal protest is required. If more than one tax period is involved and *any* tax period exceeds the \$25,000 threshold, you must file a formal written protest for all periods involved. The total amount includes the proposed increase or decrease in tax and penalties or claimed refund. For an *Offer-in-Compromise*, include total unpaid tax, penalty, and interest due.

To make a small case request, follow the instructions in our letter to you by sending a brief written statement requesting an appeals conference. Indicate the changes you do not agree with and the reasons you do not agree with them.



Caution

Be sure to send the protest within the time limit specified in the letter you received.

You must file a formal written protest

- If the total amount of tax, penalties, and interest for any tax period is more than \$25,000;
- In all partnership and S corporation cases, regardless of the dollar amount;
- In all employee plan and exempt organization cases, regardless of the dollar amount;
- In all other cases, unless you qualify for other special appeal procedures, such as requesting appeals consideration of liens, levies, seizures, or installment agreements. (See *Publication 1660, Collection Appeal Rights*, for more information on special collection appeals procedures.)

Filing a Formal Protest

When a **formal protest** is required, send it within the time limit specified in the letter you received. Include in your protest:

- Your name and address, and a daytime telephone number.
- A statement that you want to appeal the IRS findings to the Appeals Office.
- A copy of the letter showing the proposed changes and findings you do not agree with (*or the date and symbols from the letter.*)
- The tax periods or years involved.
- A list of the charges that you do not agree with, and why you do not agree.
- The facts supporting your position on any issue that you do not agree with.
- The law or authority, if any, on which you are relying.
- You must sign the written protest, stating that it is true, under the penalties of perjury as follows:

“Under the penalties of perjury, I declare that I examined the facts stated in this protest, including any accompanying documents, and, to the best of my knowledge and belief, they are true, correct, and complete.”

If your representative prepares and signs the protest for you, he or she must substitute a declaration stating:

- That he or she submitted the protest and accompanying documents and;
- Whether he or she knows personally that the facts stated in the protest and accompanying documents are true and correct.

We urge you to provide as much information as you can, as this will help us speed up your appeal. This will save you both time and money.

Additional information about the Appeals process may be found in **Publication 5, Your Appeals Rights and How to Prepare a Protest if you Don't Agree**.

After the Examination

Payment Options

You cannot pay all that you owe now

If you cannot pay all your taxes now, pay as much as you can. By paying now, you reduce the amount of interest and penalty you owe. Then immediately call, write, or visit the nearest IRS office to explain your situation. After you explain your situation, we may ask you to fill out a Collection Information Statement. If you are contacting us by mail or by telephone, we will mail the statement to you to complete and return to us. This will help us compare your monthly income with your expenses so we can figure the amount you can pay. We can then help you work out a payment plan that fits your situation. This is known as an installment agreement.

Payment by credit card

Individual taxpayers may make credit (*and debit*) card payments on tax liabilities (*including installment agreement* payments) by phone or Internet. Payments may be made to the United States Treasury through authorized credit card service providers.

The service providers charge a convenience fee based on the payment amount. You will be informed of the convenience fee amount before the credit card payment is authorized. This fee is in addition to any charges, such as interest, that may be assessed by the credit card issuer. Visit www.irs.gov to obtain a list of authorized service providers and to obtain updated information on credit card payment options.

Note: You can use debit cards issued by VISA and MasterCard when making tax payments through the participating service providers. However, the service providers and card issuers treat debit cards and credit cards equally for the purpose of processing electronic tax payments. Therefore, debit card users are charged the same fee traditionally associated with credit card transactions

Payment by Electronic Federal Tax Payment System (EFTPS)

EFTPS is an Electronic Federal Tax Payment System developed by the Internal Revenue Service and Financial Management Service (FMS).

The system allows federal taxes to be paid electronically. The system allows the use of the Internet at www.eftps.gov or telephone to initiate tax payments directly. EFTPS payments may also be made through your local financial institution. The service is convenient, secure and saves time.

You may enroll in EFTPS through the website at www.eftps.gov or by completing a form available from EFTPS customer service at (800) 555-4477 or (800) 945-8400.

Setting up an installment agreement

Installment agreements allow you to pay your full debt in smaller, more manageable amounts. Installment agreements generally require equal monthly payments. The amount and number of your installment payments will be based on the amount you owe and your ability to pay that amount within the time we can legally collect payment from you.

You should be aware, however, that an installment agreement is more costly than paying all the taxes you owe now. Like revolving credit arrangements, we charge interest on the unpaid portion of the debt. Penalties also continue to accumulate on installment agreements.

If you want to pay off your tax debt through an installment agreement, call the number shown on your bill. If you owe:

- \$25,000 or less in tax, we will tell you what you need to do to set up the agreement;
- More than \$25,000, we may still be able to set up an installment agreement for you, but we may also ask for financial information to help us determine your ability to pay.

Even if you set up an installment agreement, we may still file a Notice of Federal Tax Lien to secure the government's interest until you make your final payment.

Note: We cannot take any collection actions affecting your property while we consider your request for an installment agreement, while your agreement is in effect, for 30 days after we reject your request for an agreement, or for any period while you appeal the rejection.

If you arrange for an installment agreement, you may pay with:

- Personal or business checks, money orders, or certified funds (*all made payable to the U.S. Treasury*),
- Credit and debit cards,
- Payroll deductions your employer takes from your salary and regularly sends to IRS, or
- Electronic transfers from your bank account or other similar means.

Apply for an Offer-in-Compromise

In some cases, we may accept an *Offer-in-Compromise* to settle an unpaid tax account, including any penalties and interest. With this kind of arrangement, we can accept less than the full amount you owe when it is doubtful we will be able to collect the entire amount due.

Offers in compromise are also possible if collection action would create an economic hardship. You may want to discuss these options with your examiner.

Temporarily Delay the Collection Process

If we determine that you can't pay *any* of your tax debt, we may temporarily delay collection until your financial condition improves. You should know that if we delay collecting from you, your debt will increase because penalties and interest are charged until you pay the full amount. During a temporary delay, we will again review your ability to pay. We may also file a *Notice of Federal Tax Lien*, to protect the government's interest in your assets. See Publication 594, *The IRS Collection Process*.

After the Examination (cont.)

Innocent Spouse Relief

If you filed a joint tax return, you are jointly and individually responsible for the tax and any interest or penalty due on the joint return, even if you later divorce. In some cases, a spouse may be relieved of the tax, interest, and penalties on a joint return.

You can ask for relief no matter how small the liability.

Three types of relief are available.

- Innocent spouse relief - may apply to all joint filers;
- Separation of liability - may apply to joint filers who are divorced, widowed, legally separated, or have not lived together for the past 12 months;
- Equitable relief - applies to all joint filers.

Innocent spouse relief and separation of liability apply only to items incorrectly reported on the return. If a spouse does not qualify for innocent spouse relief or separation of liability, the IRS may grant equitable relief.

Each type of relief is different and each has different requirements. You must file Form 8857, *Request for Innocent Spouse Relief*, to request any of these methods of relief. Publication 971, *Innocent Spouse Relief*, explains each type of relief, who may qualify, and how to request relief.

You Must Contact Us

It is important that you contact us regarding any correspondence you receive from us. If you do not pay your bill or work out a payment plan, we are required by law to take further collection actions.

What If You Believe Your Bill is Wrong



Caution

If you believe your bill is wrong, let us know as soon as possible. Call the number on your bill, write to the IRS office that sent you the bill, call 1-800-829-1040 (for 1040 filers), 1-800-829-4933 (for business filers), 1-800-829-4059/TDD, or visit your local IRS office.

To help us correct the problem, gather a copy of the bill along with copies of any records, tax returns, and canceled checks, etc., that will help us understand why you believe your bill is wrong.

If you write to us, tell us why you believe your bill is wrong. With your letter, include copies of all the documents you gathered to explain your case. Please do not send original documents. If we find you are correct, we will adjust your account and, if necessary, send you a corrected bill.

Privacy Act Statement

The Privacy Act of 1974 says that when we ask you for information, we must first tell you our legal right to ask for the information, why we are asking for it, and how it will be used. We must also tell you what could happen if you do not provide it and whether or not you must respond under the law.

This notice applies to tax returns and any papers filed with them. It also applies to any questions we need to ask you so we can complete, correct, or process your return; figure your tax; and collect tax, interest, or penalties.

Our legal right to ask for information is found in Internal Revenue Code sections 6001, 6011, and 6012(a), and their regulations. They say that you must file a return or statement with us for any tax you are liable for. Your response is mandatory under these sections.

Code section 6109 and its regulations say that you must show your social security number or individual taxpayer identification number on what you file. You must also fill in all parts of the tax form that apply to you. This is so we know who you are, and can process your return and papers. You do not have to check the boxes for the Presidential Election Campaign Fund.

We ask for tax return information to carry out the U.S. tax laws. We need it to figure and collect the right amount of tax.

We may give the information to the Department of Justice and to other Federal agencies, as provided by law. We may also give it to cities, states, the District of Columbia, and U.S. Commonwealths or possessions to carry out their tax laws. And we may give it to certain foreign governments under tax treaties they have with the United States.

We may also disclose this information to Federal, state, or local agencies that investigate or respond to acts or threats of terrorism or participate in intelligence or counterintelligence activities concerning terrorism.

If you do not file a return, do not give us the information we ask for, or provide fraudulent information, the law says that we may have to charge you penalties and, in certain cases, subject you to criminal prosecution. We may also have to disallow the exemptions, exclusions, credits, deductions, or adjustments shown on your tax return. This could make your tax higher or delay any refund. Interest may also be charged.

Please keep this notice with your records. You may want to refer to it if we ask you for other information. If you have questions about the rules for filing and giving information, please call or visit any Internal Revenue Service office.



FSLG Toolkit

This Toolkit is designed to provide a concise guide to the basic requirements for compliance with Federal tax laws in major areas of interest to governmental organizations. The Toolkit consists of four parts:

1. A [Public Employer's Toolkit](#), which provides information to government entities and payroll officers working for government entities in meeting their federal employment tax obligations;
2. A [Compliance Toolkit](#), which provides information to help government entities and their powers of attorney understand the enforcement process;
3. [Government Retirement Plans Toolkit](#); and
4. An [International Withholding Issues Toolkit](#), addressing requirements and procedures for withholding tax from nonresident aliens.

Public Employer's Toolkit

If you are a new employer, or new to dealing with federal employment tax, the first place to go for information is IRS [Publication 15, Employer's Tax Guide](#) (Circular E). This publication is revised each year and contains the basic information employers need to be able to collect adequate information so they can determine and pay their and their employees' portion of employment tax liability, file correct tax returns, and withhold federal taxes, where necessary.

You may also want to consult the following Publications that include information specific to government entities:

[Public Employer's Tax Guide](#)
[Publication 963, Federal-State Reference Guide](#)
[Publication 15-A, Employer's Supplemental Tax Guide](#)
[Publication 15-B, Employer's Guide to Fringe Benefits](#)
[FSLG Taxable Fringe Benefits Guide](#)
[Publication 1281, Backup Withholding for Missing and Incorrect Names/TINs](#)

The following list includes most federal tax forms and instructions you are likely to need to process payroll and file necessary returns with the IRS. You can download the forms and instructions from the links. Note: Some of the forms are information copies only and cannot be used for filing. A list of all IRS forms (in fillable format) and publications is available at <http://www.irs.gov/>.

- [Form SS-4, Application for Employer Identification Number](#) ([with instructions](#)).
- [Form W-2, Wage and Tax Statement](#) ([with instructions](#)).
This form must be issued to recipients of wages and filed with the SSA.
- [Form W-3, Transmittal of Wage and Tax Statements](#).
This form is used to transmit the Form W-2 to the SSA.
- [Form W-4, Employee's Withholding Allowance Certificate](#).
This form must be furnished to each employee upon hiring to determine correct withholding. Employee may submit new certificate at any time.
- [Form W-9, Request for Taxpayer Identification Number and Certification](#) ([with instructions](#)).
This form must be furnished to each person who receives a payment from a government entity in order to verify the recipient's taxpayer identification number. Examples of such payments are interest payments made by a government entity and payments made to persons who are not employees of the government entity.
- [Form 843, Claim for Refund and Request for Abatement](#) ([with instructions](#)). This form is used to request a refund or request an abatement of certain taxes, interest and penalties, including those related to employment tax.
- [Form 941, Employer's Quarterly Federal Tax Return](#) ([with instructions](#)).
This form must be filed each quarter by an employer, including a government entity, who pays wages during a calendar quarter.
- [Form 941-X, Adjusted Employer's Quarterly Federal Tax Return or Claim for Refund](#) ([with instructions](#)).
This is an amended return to correct information reported on a previous quarter Form 941.
- [Form 944, Employer's Annual Federal Tax Return](#) ([with instructions](#)).
This form may be filed by certain employers with small payrolls who have been notified by the IRS that they can file on an annual basis, instead of filing Form 941 quarterly.
- [Form 945, Annual Income Tax Withholding Return](#) ([with instructions](#)).
This form must be filed by each employer, including a government entity, to report withholding (including back up withholding) on payments other than wages. Examples of such payments made by a government entity are pensions, annuities, and IRAs.
- [Form 1099-MISC, Miscellaneous Income](#) ([with instructions](#)).
This form must be filed by any payer, including a government entity, who makes certain payments for services to recipients who are not employees.
- [Form 1096, Annual Summary and Transmittal of U.S. Information Returns](#).
This form is used to transmit Form 1099-MISC to the IRS.

You may be required to provide the following non-tax forms to new employees. They are available from other Federal agencies:

- [Form I-9, Employment Eligibility Verification](#).

Required for all new hires. This form can be obtained from U.S. Citizenship and Immigration Services.

- [Form SSA-1945, Statement Concerning Your Employment in a Job Not Covered by Social Security](#). Employees covered under a public retirement system, as well as other categories of government workers, may not be covered by social security. State and local government employers are required to notify employees hired on or after January 1 2005, in jobs not covered by social security, of the effects of the Windfall Elimination Provision and the Government Pension Offset. The law requires newly hired public employees to sign Form SSA-1945, indicating that they are aware of a possible reduction in their future social security benefit entitlement. For more detailed information about this law, see <http://www.socialsecurity.gov/form1945>.

For further on-line information about employer responsibilities, visit the web page for [Employment Taxes for Businesses](#).

Government Entity Compliance Toolkit

The following information explains what a government entity can expect during a compliance check or an examination conducted by FSLG. It also provides information with regard to adequate record keeping by government entities, disclosure constraints on the IRS and consent by government entities authorizing the IRS to disclose tax information to third parties.

- [FSLG Compliance Program: Compliance Checks, Examinations, and the Difference Between Them](#) – The purpose of a compliance check and an examination, and the difference between the two.
- [What Occurs During an Examination](#) – What a government entity can expect during an examination, including the types of questions asked during an examination, the kinds of information requested, and possible outcomes of an examination.
- [What Occurs During a Compliance Check](#) – What a government entity can expect during a compliance check, including the types of questions asked during a compliance check, the kinds of information requested, and possible outcomes of a compliance check, also includes sample compliance check opening and closing letters, pro forma information document requests, etc.
- [Basic Recordkeeping for Employment Taxes and Information Return Reporting](#) – Suggestions about methods for maintaining employment tax records and vendor information. What records must be maintained by a government entity with respect to an employment tax exam.
- [Disclosure Laws](#) – Constraints on the IRS with regard to disclosure of tax information of a government entity to third parties. Providing consent for disclosure to the IRS, including power of attorney provisions, third party contact procedures, etc.
- [Appeals Process](#) – Information about IRS Appeals Office and procedure for requesting review by the Office of Appeals of an adverse determination made by FSLG after an examination.
- [Where To Find It](#) – A list of topics and where to go to find more information.

Government Retirement Plans Toolkit

Retirement plans established for the benefit of governmental employees generally function in ways similar to those covering private employers. However, in many cases, different sections of the Internal Revenue Code determine the tax treatment of these plans. Depending on the statutory basis for the plan and how it operates, employer and employee contributions may be subject to Federal income tax at the time of contribution, or tax-deferred until distributed; and they may be taxable or excluded from social security and Medicare taxes (FICA).

Public Retirement Systems (FICA Replacement Plans)

Effective July 2, 1991, Congress made social security coverage mandatory for state and local government employees who are neither covered by a Section 218 Agreement nor qualifying participants in a public retirement system. Under this provision, states can provide these mandatorily covered employees with membership in a public retirement system as an alternative to mandatory social security coverage. Employees may also be covered by both a public retirement system and social security under a section 218 Agreement.

A governmental retirement plan must meet certain minimum benefit or contribution standards to qualify as a public retirement system, and thereby serve as a "replacement" plan exempting the participants from mandatory social security coverage. These standards are based solely on meeting a minimum benefit level provided (defined benefit plan), or a minimum amount contributed (defined contribution plan) to the participant. Whether a plan meets the standard to exempt employees from mandatory FICA has no bearing on the rules discussed below, and a public retirement system is not necessarily a "qualified plan" within the meaning of Employee Retirement Income Security Act (ERISA). For a detailed discussion of the requirements for public retirement systems, see Chapter 6 of [Publication 963, Federal-State Reference Guide](#).

Types of Public Employer Plans

The following types of retirement plans are discussed here (sections refer to the Internal Revenue Code)

- Section 401(a) - Qualified Plan
- Section 403(b) – Annuity for public schools and 501(c)(3) organizations
- Section 457(b) – Nonqualified, eligible deferred compensation plans for state and local governments and tax-exempt organizations
- Section 457(f) – Nonqualified, ineligible deferred compensation plans

Note: After May 6, 1986, state and local governments are not eligible to adopt Section 401(k) plans except for rural cooperatives, Indian tribal entities. Under grandfather provisions, plans established prior to that date may continue to operate and add new participants.

Almost all governmental plans are covered under one of these sections. They are discussed individually below.

Key Terms and Concepts

The following are some important terms that are used in discussing the features of public employer plans.

Constructive Receipt: Under the provisions of sections 451 and 457 of the Internal Revenue Code, generally all amounts employees receive are taxable when received or made available to the employee. However, numerous code sections provide exceptions to either defer or exempt amounts from current employee income. They are discussed below as they apply to governmental plans.

Employer Contributions: Amounts credited to individual employee retirement accounts paid in addition to salary; the employee does not have the option to receive these amounts in cash. These amounts are always tax deferred, because the employee does not have constructive receipt. Except for section 457(b) deferrals and section 457(f) contributions, employer contributions are exempt from FICA.

Tax-Deferred: Refers to amounts set aside or credited to the employee retirement account are not included in gross income at the time of the transaction. They are included in income when they are distributed to or constructively received by the employee. Generally, they are subject to withholding requirements at that time also.

Salary Reduction Agreement: An arrangement that provides for amounts recognized as a cash or deferred election because the employee either (a) elects to reduce cash compensation, or (b) elects to forego an increase in cash compensation.

Mandatory Employee Contributions: Amounts deducted from employee salary and credited to a retirement account.

Employer "Pick-Up" Contributions: Section 414(h)(2) allows state or local government entities with section 401(a) plans to treat certain contributions designated as employee contributions, but which are "picked up" (paid) by the employer, to be treated as employer contributions, and therefore as exempt from income tax. This does not include contributions made under a salary reduction agreement. For purposes of FICA, the term "salary reduction" relates to amounts treated as an employer contribution under Code §414(h)(2) that would have been included in wages for FICA tax purposes, but for the employer contribution.

For more information on the requirements to treat contributions as employer pick-ups, see the article in the [January 2007 FSLG Newsletter](#). For more information on pick-up contributions and FICA, see the article in the [July 2007 FSLG Newsletter](#).

Section 401(a) Qualified Plans

Generally, any public employer may set up a 401(a) plan. Under this plan:

Employer contributions not made pursuant to a salary reduction agreement, but including employer "pick-up" contributions, are deferred from income tax until distribution, and exempt social security and Medicare tax.

Employer contributions made under a salary reduction agreement are deferred from income tax, but are subject to FICA tax.

Employee contributions pursuant to a salary reduction agreement are subject to income tax and FICA.

Section 403(b) Plans

Plans under IRC section 403(b), also called tax-sheltered annuities, are available to certain employees of public schools, employees of certain tax-exempt organizations, and certain ministers. To maintain a section 403(b) plan, a governmental employer must be a public school of a state, political subdivision of a state, or an agency or instrumentality of one or more of these. Many public school employees are covered by 403(b) plans in addition to social security coverage under section 218.

403(b) plans resemble "qualified" (i.e., 401(k)) plans in many respects. Eligible participants may defer amounts from income tax up to an annual limit (\$16,500 in 2009). This amount may be increased for certain employees with more than 15 years service. In addition, additional tax-deferred "catch-up" contributions may be made to employees age 50 or older.

Employer contributions (within dollar limitations) are tax-deferred and exempt from FICA.

Employee elective contributions to 403(b) plans that are considered employer contributions pursuant to a salary reduction agreement are deferred from income tax, but taxable for FICA.

For more information on catch-up contributions to 403(b) plans, see [Publication 571](#).

Section 457(b) Plans

Section 457 addresses nonqualified plans. Many public employees participate in nonqualified, or section 457, plans. These plans can be established by state and local governments or tax-exempt organizations. If they meet the requirements of IRC section 457(b), they are considered "eligible" plans; if not they are considered "ineligible" and are governed by IRC section 457(f).

Governmental 457(b) plans must be funded, with assets held in trust for the benefit of employees. Plan assets and income of all other eligible plans must remain the property of the employer.

Plans eligible under 457(b) may defer amounts from income tax up to an annual limit (\$16,500 in 2009). In addition, "catch-up" contributions may be made to employees age 50 or older. Social security and Medicare taxes generally apply to all employer and employee contributions. For further information regarding social security and Medicare tax withholding and reporting on amounts deferred into eligible deferred compensation plans, see [Notice 2003-20](#) and the [IRS.gov Employee Plans site](#).

Employer contributions to 457(b) plans are tax deferred up to annual limits. They are subject to FICA when no

longer subject to substantial risk of forfeiture.

Substantial risk of forfeiture. The rights of a person to compensation are subject to substantial risk of forfeiture if such person's rights to such compensation are conditioned upon the future performance of substantial services by any individual.

Section 1.83-3(c)(1) of the regulations provides that whether a risk of forfeiture is substantial or not depends upon the facts and circumstances

"A substantial risk of forfeiture exists where rights in property that are transferred are conditioned, directly or indirectly, upon the future performance (or refraining from performance) of substantial services by any person, or the occurrence of a condition related to a purpose of the transfer, and the possibility of forfeiture is substantial if such condition is not satisfied."

Section 1.83-3(c)(2) of the regulations point out that requirements that the property be returned to the employer if the employee is discharged for cause or for committing a crime will not be considered to result in a substantial risk of forfeiture.

Employee elective contributions are deferred from income tax. They are subject to FICA. However, see [IRS Notice 2003-20](#), VI B, "Timing of social security and Medicare taxes."

Section 457(f) Plans

Nonqualified state or local government plans that do not meet the tests of 457(b) are ineligible, or 457(f), plans. There is no limit on the annual deferrals on these plans, but to defer taxation all amounts must be subject to substantial risk of forfeiture (see above). Distributions are generally subject to social security and Medicare taxes at the later of the time 1) when the services giving rise to the related compensation are performed, or 2) when there is no substantial risk of forfeiture of the rights to the amounts.

Employer contributions to 457(f) plans are includible in income in the year they are no longer subject to any substantial risk of forfeiture. They are subject to income tax withholding in the year they are actually or constructively paid.

Note: IRC §457(f)(1)(A) requires that the contributions be included in the gross income of the participant in the first taxable year in which there is no substantial risk of forfeiture, whereas, IRC §3402(a)(1) requires withholding of federal income tax when the contributions are actually or constructively paid. Thus, while the contributions must be reported as income taxable wages on Form W-2 in the first year in which there is no substantial risk of forfeiture, there may be no income tax withholding requirement at that time. Contributions to funded plans (not meeting the requirements of §457(b)) are constructively paid in the "taxable year in which amounts attributable to employer contribution amounts first become nonforfeitable."

IRC 547(e)(11)(A)(i) provides exceptions to the above treatment may apply to plans involving bona fide vacation, sick leave, involuntary severance pay, disability or death benefits. For information on the treatment of severance pay plans, see [Notice 2007-62](#).

457(f) contributions are subject to FICA at the later of:

1. When the services are performed, or
2. When there is no substantial risk of forfeiture and when the amounts are reasonably ascertainable.

Form W-2 Reporting

- Box 1: Income taxable contributions.
- Box 12: Elective salary reduction deferrals to §§401(k), 403(b), 408(k)(6), 408(p); elective deferrals and employer contributions (including nonelective deferrals) to §457(b) unless subject to substantial risk of forfeiture.
- Box 14: Employer may enter the following: (a) nonelective employer contributions made on behalf of an employee, (b) voluntary after-tax contributions that are deducted from an employee's pay, (c) required employee contributions, and (d) employer matching contributions.

Resources for Further Information

[Publication 963](#), Federal-State Reference Guide
[Publication 571](#), Tax-Sheltered Annuity Plans (403(b) Plans)
[Instructions for Forms W-2 and W-3](#)

See also the following IRS web pages:

[IRC 403\(b\) Deferred Compensation Plans](#)
[IRC 457\(b\) Deferred Compensation Plans](#)

International Withholding Issues Toolkit

Federal, state and local governmental entities often act as withholding agents, and pay income to nonresident aliens. This discussion covers:

- The persons responsible for withholding (withholding agents),
- The types of income subject to withholding, and
- The information return and tax return filing obligations of withholding agents.

The discussion includes the rules that generally apply to payments of U.S. source income to nonresident aliens.

Withholding of Tax

Generally, a nonresident alien is subject to U.S. tax on its U.S. source income. Most types of U.S. source income received by a nonresident are subject to U.S. tax at a rate of 30%, unless a lower amount is prescribed by a tax treaty. An in-depth discussion of tax treaties is beyond the scope of this article, and we recommend reviewing [Publication 901, U.S. Tax Treaties](#).

The tax is generally withheld from the payment made to the nonresident alien. Nonresident alien (NRA) withholding is descriptively used to refer to withholding required under section 1441 of the Internal Revenue Code. Generally, NRA withholding describes the withholding regime that requires withholding on a payment of U.S. source income.

For general information about withholding, see [Publication 515, Withholding of Tax on Nonresident Aliens and Foreign Entities](#).

Withholding is required at the time you make a payment of an amount subject to withholding.

You are required to report payments subject to NRA withholding on [Form 1042-S](#) and to file a tax return on [Form 1042](#). Form 1042 is due March 15 of the following year. Note: Form 1042 has unique requirements to deposit tax; these differ from Form 941 tax deposits.

Withholding Agent

A withholding agent is the person responsible for withholding on payments made to a nonresident alien. You are a withholding agent if you have control, receipt, custody, disposal, or payment of any item of income of a nonresident alien that is subject to withholding.

Liability for tax

As a withholding agent, you are personally liable for any tax required to be withheld. This liability is independent of the tax liability of the nonresident alien to whom the payment is made. If you fail to withhold and the NRA fails to satisfy his or her U.S. tax liability, then both you and the nonresident alien are liable for tax, as well as interest and any applicable penalties. The applicable tax will be collected only once. If the nonresident alien satisfies the U.S. tax liability, you may still be held liable for interest and penalties for your failure to withhold.

Determination of amount to withhold

You must withhold on the gross amount subject to NRA withholding. You cannot reduce the gross amount by any deductions. If the determination of the source of the income or the amount subject to tax depends on facts that are not known at the time of payment, you must withhold an amount sufficient to ensure that at least 30% of the amount subsequently determined to be subject to withholding is withheld. In no case, however, should you withhold more than 30% of the total amount paid; if this is done because of error or inaccurate estimate of income, the excess should be refunded to the recipient.

Persons Subject to NRA Withholding

NRA withholding applies only to payments made to nonresident aliens. It does not apply to payments made to U.S. persons. Usually, you determine the payee's status as a U.S. or foreign person based on the documentation that person provides.

Nonresident Alien

A **nonresident alien** is an individual who is not a U.S. citizen or a resident alien.

A **resident alien** is an individual that is not a citizen or national of the United States and who meets either the green card test or the substantial presence test for the calendar year. Generally, resident aliens are taxed in the same way as U.S. citizens.

Green card test - An alien is a U.S. resident if the individual was a lawful permanent resident of the United States at any time during the calendar year. This is known as the "green card test" because these aliens hold immigrant visas (also known as "green cards").

Substantial presence test - An alien is considered a U.S. resident if the individual meets the substantial presence test for the calendar year. Under this test, the individual must be physically present in the United States on at least:

- 31 days during the current calendar year, and
- 183 days during the current year and the 2 preceding years, counting all the days of physical presence in the current year, but only 1/3 the number of days of presence in the first preceding year, and only 1/6 the number of days in the second preceding year.

Generally, the days the alien is in the United States as a teacher, student, or trainee on an "F, J, M, or Q" visa are not counted toward the substantial presence test. This exception is for a limited period of time. A discussion of students, scholars, teachers, researchers, exchange visitors, and cultural exchange visitors temporarily in the United States on "F, J, M, or Q" visas is beyond the scope of this article. This topic is discussed in another IRS article, [Foreign Students and Scholars](#).

For more information on resident and nonresident status, the tests for residence, and the exceptions to them, please see [Publication 519, Tax Guide for Aliens](#).

Exceptions to 30% Withholding Rule

Generally, you must withhold 30% from the gross amount paid to a nonresident alien unless you can reliably associate the payment with valid documentation that establishes either of the following.

- The payee is a U.S. person.
- The payee is a nonresident alien person that is the beneficial owner of the income and is entitled to a reduced rate of withholding.

The nonresident alien may provide you with one of the following forms. They deal with various exceptions to the

general withholding rules. You may link to these forms for further information. See [Publication 515](#).

[Form W-8BEN](#), Certificate of Foreign Status of Beneficial Owner for United States Tax Withholding
[Form W-8ECI](#), Certificate of Foreign Person's Claim That Income Is Effectively Connected With the Conduct of a Trade or Business in the United States
[Form W-8IMY](#), Certificate of Foreign Intermediary, Foreign Flow-Through Entity, or Certain U.S. Branches for United States Withholding
[Form W-8EXP](#), Certificate of Foreign Government or Other Organization for United States Tax Withholding
[Form 8233](#), Exemption From Withholding on Compensation for Independent (and Certain Dependent) Personal Services of a Nonresident Alien Individual

Source of Income

Generally, income is from a U.S. source if it is paid for personal services rendered within the United States. This is considered U.S. sourced income. Payments to a nonresident alien for personal services rendered outside the U.S. are determined to be foreign-sourced income, and are considered non-taxable and non-reportable.

Scholarships, fellowships, and grants are sourced according to the residence of the payer. Those made by entities created or domiciled in the United States are generally treated as income from sources within the United States. Scholarship, fellowship and grant income are reportable on a Form 1042S to the nonresident alien. Those made by entities created or domiciled in a foreign country are treated as income from foreign sources, and are considered nontaxable and nonreportable.

The source of pension payments is determined by the portion of the distribution that constitutes the compensation element (employer contributions) and the portion that constitutes the earnings element (the investment income). The compensation element is sourced the same as compensation from the performance of personal services. The portion attributable to services performed in the United States is U.S. source income, and the portion attributable to services performed outside the United States is foreign source income. The earnings portion of a pension payment is U.S. source income if the trust is a U.S. trust.

The information contained in this article is not to be considered an official position of the Internal Revenue Service. If you would like to obtain official written advice on an issue, please visit our website, www.irs.gov, download IRS Revenue Procedure 2007-1, and follow the instructions contained in this revenue procedure.

Page Last Reviewed or Updated: March 17, 2011



Basic Recordkeeping for Employment Taxes and Information Return Reporting

Recordkeeping

For you to be able to respond to any inquiries from the IRS about your tax forms, you should keep the following records for at least three years after the due date of the return or the date it was filed, whichever is later. In the case of quarterly (Form 941) returns, the due date is considered April 15th of the calendar year after the quarter ends. In some cases, you may want to keep the records longer.

Employment tax:

- Forms 941 or 944
- Employee copies of Forms W-2 and W-3
- Employee Forms W-4
- Employee Forms W-5
- Records of fringe benefits paid to employees, and how their value was determined
- Names, addresses, and social security numbers of all employees
- Dates of employment for each employee
- Special payments such as sick pay, lump sum leave payments
- Travel vouchers and other accounting for reimbursements to employees
- Receipts, cancelled checks, etc., for deposits made or tax paid with return

Vendor or nonemployee payments:

- Names, addresses, and taxpayer identification numbers of payees
- Dates of payment
- Forms W-9
- Payer copies of 1099-MISC and other information returns
- Forms 945
- Description and purpose of payments made
- Notices related to backup withholding

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What Occurs During an Examination

<p>What is an Examination?</p>	<p>There is no statutory or common law definition of the term "examination." However, an examination, or audit, may be described as the systematic inspection of the books and records of a taxpayer for the purpose of making a determination of the correct tax liability.</p> <p>Because government entities are generally exempt from federal income tax, our compliance efforts are generally focused on employment tax and information return reporting.</p> <p>During examinations, FSLG Specialists search for errors or omissions on employment tax and information returns. Examples of common adjustments include the following:</p> <ul style="list-style-type: none"> ● The employer discontinued the reporting of wages for FICA tax purposes before the annual wage limitation was reached. ● Compensation taxed for Federal income tax withholding purposes but not for FICA and/or Medicare tax withholding. ● Employers did not report the wages of all employees. Examples of common errors of this type include the wages of janitors, part-time or seasonal workers, etc. ● The amount of wages or income tax withheld was incorrectly reported. ● The employer did not report bonuses, vacation pay, or other payments that constitute additional wages for employment tax purposes. ● The employer did not report the fair market value of non-cash compensation. <p>In addition, the FSLG Specialist will:</p> <ul style="list-style-type: none"> ● Verify that all appropriate returns were filed timely. If not, filing deadlines and associated penalties will be discussed and assessed, and any delinquent returns will be secured. ● Verify that all deposits were made timely. If they were not, deposit requirements and failure to deposit penalties will be discussed.
<p>Scheduling the Opening Interview</p>	<p>Generally, a telephone call is used to contact the organization to schedule an appointment in the field for an employment tax interview. The FSLG Specialist will contact an authorized individual.</p> <p>An "authorized individual" is someone who has authority under the applicable state law to legally bind the entity. Usually state law, the government entity's regulations, or its charter specifies who is "authorized" to engage in certain kinds of activities. The mayor, city manager, school superintendent or comptroller/treasurer (or similar positions in other types of government entities) are other individuals who are most likely "authorized" by law to bind the organization.</p> <p>During the telephone call with the authorized government official, the FSLG Specialist will generally:</p> <ul style="list-style-type: none"> ● Set an appointment for the opening interview that is mutually agreeable, ● Discuss the tax returns and periods under audit, ● Provide information about taxpayer rights and the examination process, ● Discuss power of attorney procedures, ● Discuss the format and availability of books and records, ● Provide general information about issues initially planned to be examined and inform the taxpayer that additional issues may be examined depending upon the information obtained during the examination. <p>The FSLG Specialist will then send the taxpayer an audit confirmation letter with Publication 1 (<i>Your Rights as a Taxpayer</i>), Notice 609 (<i>Privacy Act Notice</i>), and a Form 4564 (<i>Information Document Request (IDR)</i>).</p> <p>Sometimes the initial contact is made by an appointment letter. This general occurs when the FSLG Specialist has difficulty locating a telephone number for an authorized individual.</p>
<p>Information Document Request (IDR)</p>	<p>The IDR will include requests for documents needed to support issues the FSLG plans to examine. The IDR will list the specific information and documents the taxpayer should provide to the FSLG Specialist. Although FSLG Specialists strive to phrase items in terms that are understandable to the taxpayer, sometimes terminology is unclear. If you have a question about what is requested, you should contact the Specialist for clarification.</p> <p>Items frequently requested include:</p> <ul style="list-style-type: none"> ● Books and records such as general ledger, cash disbursements journal, accounts payable ledger, etc. ● Trial balance ● Financial statements ● Forms 940, 941 or 944, 945 ● Forms W-2 ● Forms 1099 ● Employee handbooks ● Employer-provided fringe benefit packages ● Collective bargaining agreement and contracts, if any, with employees <p>Generally an IDR is sent with audit appointment letter, which will list the specific information and documents the taxpayer should have available at the initial appointment. Another IDR may be issued to the taxpayer following the initial interview to request information and documents needed to support issues that were discussed during the initial interview but not available at that time. Additional IDRs may be sent to the taxpayer until all compliance questions are resolved.</p>

	<p>IDRs will always have a deadline for information to be received. The date listed on the IDR should provide the organization a reasonable amount of time to gather and provide the information, generally between two and four weeks. If this is not sufficient, the government entity should contact the FSLG Specialist to discuss a more reasonable date.</p> <p>Examinations can be completed in a professional and timely manner when the IRS and Taxpayer/POA work cooperatively together. Time is a valuable resource for both parties and open communication will provide the framework for timely completion of the examination.</p>
Sample Interview Questions	<p>The following are a sample of questions that might be asked during the opening interview:</p> <ul style="list-style-type: none"> ● What criteria are used for each of the following categories of employees and on average how many employees are in each category: <ul style="list-style-type: none"> ○ Full-time ○ Part-time ○ Temporary ○ Seasonal ○ Other (be specific) ● Do all of the above categories of employees receive Form W-2? ● How do you file your Federal Forms W-2/W-3 and 1099/1096; i.e. manually, using magnetic media, electronically? ● For each year in question, how many Forms W-2 were filed with the Social Security Administration? ● For each year in question, how and what type of Forms 1099 were filed with the Internal Revenue Service? ● Is your payroll maintained internally or externally (if so, who is the provider)? ● If your payroll is maintained internally, is it a manual or machine sensible (computerized) system? ● Will you walk me through your payroll system and internal controls from the employee time records to the filing of Federal forms 941 and W-2? ● How are your disbursements and accounts payable records kept, manually or machine-sensitive (computerized)? ● Are completed (name, address, TIN, type of entity) and signed Forms W-9 secured from all contractors prior to the work being performed or prior to payment for services rendered? ● How do you determine who receives a Form 1099? ● Who determines and what criteria are used to determine whether a worker should be treated as an independent contractor or employee? ● Do you engage the services of former employees? If so, are they treated as employees or independent contractors? ● Will you walk me through your disbursements and accounts payable systems and internal controls? ● What employee fringe benefits do you provide? ● What classes of employees receive what benefits?
Forms 1099	<p>Forms 1099 are reviewed to identify potential issues such as:</p> <ul style="list-style-type: none"> ● Worker classification ● Backup withholding, and ● Additional wages
Taxability of wages	<p>The determination that a benefit is not "wages" must be based on a provision specifically excluding the payment from wages for employment tax purposes. Exclusion for income tax purposes is not enough.</p>
Fringe Benefits	<p>We review the organization's employee handbooks, union contracts, and employment contracts to identify fringe benefits. Then we must determine that all the fringe benefits (cash and non-cash), noted during the review have been:</p> <ul style="list-style-type: none"> ● Properly excluded from employees' income and not subject to Federal employment taxes, or, ● Properly included in employees' income and subject to all appropriate federal employment taxes, or, ● Improperly excluded from employees' income and not properly subject to all appropriate Federal employment taxes. <p>Those benefits that were <i>"improperly excluded from the employee's income and not properly subject to all appropriate Federal employment taxes"</i> will be included in the proposed adjustment.</p>
Employee Pension Plans	<p>The FSLG Specialist will ask whether the organization has employee pension plans. If the organization has a 403(b) and/or 457 plan, Specialists will consider basic eligibility rules, review Forms W-2 for excessive contributions, etc.</p>
Results of the Examination	<p>If we accept your return as filed, you will receive a letter stating that the examiner proposed no changes to your return. You should keep this letter with your tax records.</p> <p>If we don't accept your return as filed, we will explain any proposed changes to you and your authorized representative. It is important that you understand the reasons for any proposed changes; don't hesitate to ask about anything that is unclear to you.</p>
If You Agree with a Proposed Increase to Tax	<p>If you agree with a proposed increase to tax, you can sign an agreement form and pay any additional tax you may owe. You must pay interest and applicable penalties on any additional balance due. If you pay when you sign the agreement, interest is generally figured from the due date of your return to the date of your payment.</p> <p>If you do not pay the additional tax and interest, you will receive a bill</p> <p>If you are entitled to a refund, you will receive it sooner if you sign the agreement form at the end of the examination. You will also be paid interest on the refund.</p>

If You Do Not Agree with a Proposed Increase to Tax	<p>If you do not agree with the proposed changes, the examiner will explain your appeal rights. You may request an immediate meeting with the examiner's supervisor to explain your situation.</p> <p>If you cannot reach an agreement with the supervisor, the FSLG Specialist will prepare a report explaining your position and the IRS position. The examiner will forward your case to the Area office for processing.</p> <p>You will receive:</p> <ul style="list-style-type: none">• A letter (known as a 30-day letter) notifying you of your rights to appeal the proposed changes within 30 days,• A copy of the FSLG Specialist's report explaining the proposed changes, and• An agreement or a waiver form. <p>You generally have 30 days from the date of the 30-day letter to tell us whether you will accept the proposed changes or appeal them. The letter will explain what steps you should take, depending on what action you choose. Be sure to follow the instructions carefully. Appeal rights are explained in the Appeals Process article.</p> <p>If you do not respond to the 30-day letter, or if you respond but do not reach an agreement with an appeals officer, we will send you a 90-day letter, also known as a Notice of Deficiency. This is a legal document that explains the proposed changes and the amount of the proposed tax increase. You will have 90 days (150 days if it is addressed to you outside the United States) from the date of this notice to file a petition with the Tax Court. If you do not petition the Tax Court you will receive a bill for the amount due.</p>
Consents to Extend the Statute of Limitations	<p>We try to examine tax returns as soon as possible after they are filed, but occasionally we may request that you extend the statute of limitations of your tax return.</p> <p>A return's statute of limitation generally limits the time we have to examine it and assess tax. Assessments of tax must be made within 3 years after a return is due or filed, whichever is later. We can't assess additional tax or make a refund or credit (unless you filed a timely claim) after the statute of limitations has expired. Also, if you disagree with the results of the examination, you can't appeal the items you disagree with unless sufficient time remains on the statute. Because of these restrictions, if there isn't much time remaining to examine your return, assess additional taxes, and/or exercise your appeal rights, you have the opportunity to extend the statute of limitations. This will allow you additional time to provide further documentation to support your position, request an appeal if you do not agree with our findings, or to claim a tax refund or credit. It also allows the Service time to complete the examination, make any additional assessment, if necessary, and provide sufficient time for processing.</p> <p>A written agreement between you and the Service to extend the statutory period of a tax return is called a "consent."</p> <p>IRS generally utilizes Form SS-10 to extend the statute of limitations on employment tax returns.</p> <p>If the statute of limitations for your tax return is approaching, you may be asked to sign a consent. You may:</p> <ol style="list-style-type: none">1. Refuse to extend the statute of limitations;2. Limit or restrict the consent to particular issues, or3. Limit the extension to a particular period of time. <p>The consent will be sent or presented to you with a letter explaining this process and Publication 1035, Extending the Tax Assessment Period. For further information, refer to this publication.</p>



Where To Find It

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<i>Consult the publications cited as primary sources for each topic.</i>	
Accountable plans	Publication 15 (Circular E)
Bonuses and supplemental pay	Publication 15 (Circular E)
Cafeteria plans	Publication 15-B , Employer's Guide to Fringe Benefits
Characteristics of Government Entities	Publication 963 , Federal-State Reference Guide
Clothing and uniform allowances	Publication 15-B , Employer's Guide to Fringe Benefits FSLG Taxable Fringe Benefits Guide
Deposit rules	Publication 15 (Circular E)
Emergency workers	Publication 963 , Federal-State Reference Guide
Employee meals and lodging expenses	FSLG Taxable Fringe Benefits Guide Publication 463 , Travel, Entertainment, Gift and Car Expenses
Employee use of employer vehicle	Publication 15-B , Employer's Guide to Fringe Benefits FSLG Taxable Fringe Benefits Guide
Fee-based employees	Publication 963 , Federal-State Reference Guide
Filing requirements	Publication 15 (Circular E)
Information reporting	General Instructions for Forms 1099, 1098, 5498, and W-2G
Medicare coverage	Publication 963 , Federal-State Reference Guide
Nonqualified (section 457) retirement plans	Public Employer's Tax Guide Publication 963 , Federal-State Reference Guide (includes Notice 2003-20)
Public retirement systems (social security replacement plans)	Publication 963 , Federal-State Reference Guide
Section 218 social security coverage	Public Employer's Tax Guide Publication 963 , Federal-State Reference Guide
Sick pay	Publication 15-A , Employer's Supplemental Tax Guide
Volunteers	Publication 963 , Federal-State Reference Guide
Wages and items included in compensation	Publication 15-B , Employer's Guide to Fringe Benefits FSLG Taxable Fringe Benefits Guide
Who is an Employee?	Publication 15 (Circular E)
Withholding	Publication 15 (Circular E)

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