

Exam: New IRS LB&I Campaign Focuses on Success-Based Fees Paid by Taxpayers Not Electing to Use Safe Harbor

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In this article, George Hani and Mary Duffy, a Managing Director in Andersen's U.S. National Tax office and co-leader of Andersen's accounting methods team, discuss the Internal Revenue Service (IRS) Large Business & International Division (LB&I)'s recently announced compliance campaign focusing on the allocation of success-based fees in certain types of transactions for taxpayers who did not make the safe harbor election under Revenue Proc. 2011-19.1 "So-called 'facilitative' costs must be capitalized, and the Treasury Regulations provide fairly strict documentation requirements for any amount of a success-based fee to be treated as a deductible non-facilitative cost. The LB&I compliance campaign will bring increased scrutiny to the documentation required of these taxpayers, making it critical that taxpayers who engage in such transactions focus on the risks associated with not making the safe harbor election and adequately prepare for the expected documentation inquiries in an IRS audit (if no safe harbor election is made)," the authors wrote. "An IRS determination that a taxpayer has failed to properly document how success-based fees are allocated between facilitative and non-facilitative services can face significantly negative financial consequences because such fees often comprise a substantial portion of the costs incurred in an acquisition or reorganization transaction."