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HIGHLIGHTS OF THIS ISSUE

These synopses are intended only as aids to the reader in identifying the subject matter covered. They may not be relied upon as authoritative interpretations.

INCOME TAX

Notice 2016–36, page 1029.

This notice provides a safe harbor under which a transfer of property from an electricity generator to a regulated public utility, used to facilitate the transmission of electricity over the utility's transmission system, will not be treated as income under section 118. Notice 88–129, Notice 90–60, and Notice 2001–82 are modified and superseded by this notice.

EMPLOYMENT TAX

Rev. Proc. 2016–33, page 1034.

The Stephen Beck, Jr., Achieving a Better Life Experience Act of 2014 requires the establishment of a voluntary certification program for professional employer organizations. A professional employer organization, sometimes referred to as an employee leasing company, is an organization that enters into an agreement with a client to perform some or all of the federal employment tax withholding, reporting, and payment functions related to workers performing services for the client. Being certified by the IRS as a certified professional employer organization (CPEO) has certain federal employment tax consequences for both the CPEO and its clients. This revenue procedure describes the process by which a person applies for certification as a CPEO and the requirements a person must satisfy in order to become a CPEO.

Finding Lists begin on page ii.

The IRS Mission

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

Introduction

The Internal Revenue Bulletin is the authoritative instrument of the Commissioner of Internal Revenue for announcing official rulings and procedures of the Internal Revenue Service and for publishing Treasury Decisions, Executive Orders, Tax Conventions, legislation, court decisions, and other items of general interest. It is published weekly.

It is the policy of the Service to publish in the Bulletin all substantive rulings necessary to promote a uniform application of the tax laws, including all rulings that supersede, revoke, modify, or amend any of those previously published in the Bulletin. All published rulings apply retroactively unless otherwise indicated. Procedures relating solely to matters of internal management are not published; however, statements of internal practices and procedures that affect the rights and duties of taxpayers are published.

Revenue rulings represent the conclusions of the Service on the application of the law to the pivotal facts stated in the revenue ruling. In those based on positions taken in rulings to taxpayers or technical advice to Service field offices, identifying details and information of a confidential nature are deleted to prevent unwarranted invasions of privacy and to comply with statutory requirements.

Rulings and procedures reported in the Bulletin do not have the force and effect of Treasury Department Regulations, but they may be used as precedents. Unpublished rulings will not be relied on, used, or cited as precedents by Service personnel in the disposition of other cases. In applying published rulings and procedures, the effect of subsequent legislation, regulations, court decisions, rulings, and procedures must be considered, and Service personnel and others concerned are cautioned against reaching the same conclusions in other cases unless the facts and circumstances are substantially the same.

The Bulletin is divided into four parts as follows:

Part I.—1986 Code.
This part includes rulings and decisions based on provisions of the Internal Revenue Code of 1986.

Part II.—Treaties and Tax Legislation.
This part is divided into two subparts as follows: Subpart A, Tax Conventions and Other Related Items, and Subpart B, Legislation and Related Committee Reports.

Part III.—Administrative, Procedural, and Miscellaneous.
To the extent practicable, pertinent cross references to these subjects are contained in the other Parts and Subparts. Also included in this part are Bank Secrecy Act Administrative Rulings. Bank Secrecy Act Administrative Rulings are issued by the Department of the Treasury's Office of the Assistant Secretary (Enforcement).

Part IV.—Items of General Interest.
This part includes notices of proposed rulemakings, disbarment and suspension lists, and announcements.

The last Bulletin for each month includes a cumulative index for the matters published during the preceding months. These monthly indexes are cumulated on a semiannual basis, and are published in the last Bulletin of each semiannual period.

Part III. Administrative, Procedural, and Miscellaneous

Transfers of Property to Regulated Public Utilities by Electricity Generators

Notice 2016–36

I. PURPOSE

This notice provides a safe harbor for transfers of property from either an electricity generation or cogeneration facility or an energy storage facility to a regulated public utility, used to facilitate the transmission of electricity over the utility's transmission system, to be treated as a contribution to the capital of a corporation under § 118(a), and not a contribution in aid of construction (CIAC) under § 118(b). Notice 88–129, 1988–2 C.B. 541; Notice 90–60, 1990–2 C.B. 345; and Notice 2001–82, 2001–2 C.B. 619, (collectively, the "Notices") are modified and superseded.

II. BACKGROUND

A. *Law and Legislative History*

Section 61(a) of the Internal Revenue Code and § 1.61–1 of the Income Tax Regulations provide that gross income means all income from whatever source derived, unless excluded by law. Section 118(a) provides that in the case of a corporation, gross income does not include any contribution to the capital of the taxpayer. Section 118(b) provides that for purposes of § 118(a), except as provided in § 118(c), the term "contribution to the capital of taxpayer" does not include any CIAC or any other contribution as a customer or potential customer. Section 1.118–1 provides, in part, that § 118 also applies to contributions to capital made by persons other than shareholders. For example, the exclusion applies to the value of land or other property contributed to a corporation by a governmental unit or by a civic group for the purpose of enabling the corporation to expand its operating facilities. However, the exclusion does not apply to any money or property transferred to the corporation in consideration for goods or services rendered.

The legislative history to § 118 indicates that Congress added the exclusion from gross income for nonshareholder contributions to capital of a corporation to address situations in which such contributions cannot be called gifts because the contributors expect to derive indirect benefits; nor can the contributions be characterized as payments for future services because the anticipated future benefits are too intangible. The legislative history also indicates that the provision was intended to codify the existing law that had developed through court decisions on the subject. H.R. Rep. No. 1337, 83rd Cong., 2d Sess. 17 (1954); S. Rep. No. 1622, 83d Cong., 2d Sess. 18–19 (1954).

B. *Notice 88–129*

Notice 88–129, which was amplified and modified by Notice 90–60 and Notice 2001–82, provided specific guidance with respect to the treatment of transfers of property to regulated public utilities by qualifying small power producers and qualifying cogenerators (collectively, "Qualifying Facilities"), as defined in section 3 of the Federal Power Act, as amended by section 201 of the Public Utilities Regulatory Policies Act of 1978 (PURPA).

As explained in Notice 88–129, PURPA and the regulations thereunder require a utility to interconnect with a Qualifying Facility for the purpose of allowing the sale of power produced by the Qualifying Facility. These rules require the Qualifying Facility to bear the cost of the purchase and installation of any equipment required for the interconnection ("intertie"). Generally, the utility takes legal title to the intertie, which becomes part of the utility's transmission network. Qualifying Facilities generally sell electricity to utilities pursuant to long term power purchase contracts, and some of these contracts require the Qualifying Facility to construct and install the intertie and transfer it to the utility.

1. *Safe harbor*

Section 1 of Notice 88–129 provided a safe harbor under § 118 for certain transfers of interties by a Qualifying Facility to a regulated public utility. Under the safe harbor, when a Qualifying Facility transfers an intertie to a utility exclusively in connection with the sale of electricity by the Qualifying Facility to the utility, the utility would not realize income upon the transfer (a "QF transfer"). The possibility that an intertie may be used to transmit power to a utility that will in turn transmit the power across its transmission network for sale by the Qualifying Facility to another utility ("wheeling") would not cause the contribution of that intertie to be treated as a CIAC includible in income pursuant to § 118(b).

Under certain other power purchase contracts, a utility may construct and install an intertie on behalf of a Qualifying Facility, with the Qualifying Facility reimbursing or financing the construction and installation costs. A utility that constructs an intertie in exchange for a cash payment from a Qualifying Facility pursuant to a PURPA contract must recognize income from the construction in the same manner as any other taxpayer constructing similar property under contract. However, subsequent to the construction of the intertie, the Qualifying Facility will be deemed to transfer the intertie to the utility in a QF transfer that is treated in exactly the same manner as an in-kind QF transfer.

Section 2 of Notice 88–129 further explained that, in addition to transmitting power from a Qualifying Facility to a utility, an intertie may be used to transmit power from the utility for sale to the Qualifying Facility (a "dual-use intertie"). Notice 88–129 treated the contribution of a dual-use intertie to a utility as a QF transfer if it satisfied a "5% test." A contribution satisfied the 5% test if, in light of all information available to the utility at the time of transfer, it was reasonably projected that during the ten taxable years of the utility beginning with the taxable year in which the transferred intertie was placed in service, no more than 5% of the projected total power flows over the intertie would flow to the Qualifying Facility. The notice required the projection to be supported, if practicable, by a report from an independent engineer. For purposes of the 5% test, total power flows meant power flows to or from the Qual-

ifying Facility over the intertie and included power flows to a related party of the Qualifying Facility if the transmission of power to the related party was facilitated by the transfer of the intertie. Concerning the 5% test, the notice provided that transfer of an asset necessary only for sale of power by the utility to the Qualifying Facility was not a QF transfer and constituted a CIAC, even if the asset was used, in part, in connection with the transmission of power to the utility.

Section 3 of the notice provided that a transfer of an intertie by a Qualifying Facility to a utility would not be treated as a QF transfer to the extent the intertie was included in the utility's rate base or if the term of the power purchase contract was less than ten years.

2. *Termination of safe harbor*

Section 4 of Notice 88–129 provided that certain events would terminate the safe harbor and require the utility to recognize income as a consequence of the QF transfer.

Under section 4.A of Notice 88–129, if, for each of any three taxable years within any period of five consecutive taxable years, more than 5% of the total power flow over the intertie flowed from a utility to a Qualifying Facility (a "disqualification event"), then the Qualifying Facility was deemed to have made a transfer to the utility that constituted a CIAC, and a portion of the fair market value of the intertie had to be included in income by the utility.

Section 4.B of Notice 88–129 provided that, upon the termination of the power purchase contract between a Qualifying Facility and a utility, if the utility obtained or retained ownership (for tax purposes) of the intertie, then the Qualifying Facility was deemed to have made a transfer to the utility that constituted a CIAC as of the first day of the termination. The amount of the CIAC was the fair market value of the intertie, less the amount, if any, paid by the utility to obtain or retain ownership of the property for tax purposes. Absent unusual circumstances, the fair market value of a CIAC was determined under the replacement cost method.

3. *Cost recovery*

Finally, Notice 88–129 provided that the cost of property transferred in a QF transfer was required to be capitalized by the Qualified Facility as an intangible asset and recovered as appropriate. Taxpayers were not permitted to currently deduct the total amount of an expenditure that resulted in the creation of an asset having a useful life that extended substantially beyond the close of the taxable year but were required to capitalize such expenditures as assets and recover the cost of the expenditures over the useful life of the asset in question. *See, e.g.*, § 1.461–1(a)(1) and (2); Rev. Rul. 70–413, 1970–2 C.B. 103.

Notice 88–129 did not allow a utility to claim depreciation (or amortization) deductions with respect to property transferred in a QF transfer. However, if property that was the subject of a QF transfer was subsequently transferred or deemed transferred to the utility as a CIAC, the utility was allowed to take depreciation deductions with respect to the property.

C. *Notice 90–60*

Notice 90–60 amplified and modified Notice 88–129. Notice 90–60 clarified that for purposes of determining the fair market value of a CIAC under section 4.A of Notice 88–129, the replacement cost method included taking into account the condition of property deemed transferred as a CIAC in establishing its fair market value. Absent unusual circumstances, the fair market value of used CIAC property was the depreciated replacement cost.

Notice 90–60 also provided that upon the termination under section 4.B of Notice 88–129 of a power purchase contract between a Qualifying Facility and a utility, if the utility obtained or retained ownership (for tax purposes) of property transferred in a QF transfer, the Qualifying Facility was deemed to have made a transfer to the utility as of the first day of the termination. Notice 90–60 modified Notice 88–129 by providing that a deemed transfer was not treated as a CIAC, except in circumstances indicating an intention by the parties to characterize as a QF transfer a transaction that in substance constitutes a CIAC.

Finally, Notice 90–60 modified Notice 88–129 by deleting the requirement that any property that was the subject of a QF transfer be subsequently transferred or deemed transferred to the utility "as a CIAC" for the utility to be allowed to take depreciation deductions with respect to the property.

D. *Notice 2001–82*

Notice 2001–82 further amplified and modified Notice 88–129. Notice 2001–82 extended the safe harbor provisions of Notice 88–129 to include transfers of interties from both Qualifying and non-Qualifying Facilities and transfers of interties used exclusively or in part for wheeling electricity. Notice 2001–82 required that ownership of the wheeled electricity pass to the purchaser prior to its transmission on the utility's transmission grid. This ownership requirement was deemed satisfied if title passed at the busbar on the facility's end of the intertie. Further, Notice 2001–82 provided that a long-term interconnection agreement in lieu of a long-term power purchase contract could be used to satisfy the safe harbor provisions of Notice 88–129 with respect to wheeling transactions. Finally, Notice 2001–82 required that a facility capitalize the cost of transferred property as an intangible asset and recover such cost using the straight-line method over a useful life of 20 years.

E. *Industry Changes*

1. *Regional implications of interconnecting to the grid*

Since the issuance of the Notices, electricity transmission and distribution systems have evolved and become interlinked so that close coordination of operations within the major U.S. power grids is needed to maintain the various interlinked components.

Utilities across geographic regions interconnect for improved reliability and efficiency. Utilities can draw power from generator reserves in different regions to ensure continuing, reliable power and to diversify their loads. Interconnection also provides access to cheap bulk energy by allowing utilities to receive power from different sources. Further, through greater coordination, utilities can help one another maintain the frequency of oscillation

of alternating current and manage interconnections between utility regions.

In addition, utilities are responsible for maintaining the safety of their systems and planning for future customer needs. A large failure in one part of the grid can cause failures in other parts of the grid. Regional transmission operators (RTOs) measure the available transmission capacity on transmission lines and monitor the activities of parties that use space on power lines. Parties may agree to a transaction involving specific transmission lines that, in theory, are able to handle new capacity. However, the additional power delivered over those lines may overload different transmission lines in another part of the grid, as the physical and the contractual flow of power may differ. When buyers and sellers attempt to send more power over transmission lines than the system can handle, RTOs can activate procedures that enable them to stop the flow of, or in some situations, even cancel, power sales contracts (collectively, "curtailment").

To avoid curtailment, an electricity generator in one region and a utility in a different region that owns a transmission system that will be affected by power delivered by the generator may enter into an agreement in which the utility constructs upgrades to its transmission system, allowing it to handle the generator's new capacity, and the generator reimburses the utility for the costs of the upgrades. The safe harbor in Notice 88–129, as amplified and modified by Notice 2001–82, did not apply to such a transfer unless the upgrades were constructed pursuant to a long-term power purchase contract or a long-term interconnection agreement between the generator and the utility that constructed the upgrades. Electricity generators typically do not enter into long-term power purchase contracts with utilities outside of their service areas and do not enter into long-term interconnection agreements with transmission systems that are not located within their connectivity range ("neighboring transmission systems"). Therefore, contributions of transmission system upgrades to neighboring transmission systems would not qualify under the former safe harbor.

2. *Energy storage facilities*

Most sections of the U.S. power grid operate at 60 Hz. This is the frequency with which electric current oscillates. The frequency fluctuates from one second to the next as people turn on and off lights, TVs, computers, air conditioners, and other equipment that requires electricity to function. Grid operators try to keep the frequency of the electricity on the grid within a narrow band, from 59.8 to 60.2 Hz, for example. A drop in electricity demand as people turn off equipment causes the frequency to increase. A spike in demand as people turn on equipment causes the frequency to decrease. The fluctuating frequency can cause damage.

Grid frequency is becoming harder to manage as more and more intermittent wind and solar projects connect to the grid. Batteries and other storage facilities play an important role in managing grid frequency. Standalone batteries connected to the grid can allow the grid to shed electricity and call it back in very short intervals to manage frequency as well as smooth the transition to other energy sources.

III. SAFE HARBOR

A. *Explanation of Provisions*

This notice provides a new safe harbor in which a transfer of an intertie to a regulated public utility will not be treated as a CIAC under § 118(b) or give rise to gross income under § 118(a). This notice consolidates the safe harbor requirements under the Notices and removes the requirement that the generator must have a long-term power purchase contract or long-term interconnection agreement with the utility that constructs the upgrades. Because no long-term power purchase contract or long-term interconnection agreement is required under the new safe harbor, a generator (such as a solar or wind farm) may contribute an intertie to a utility that qualifies under the new safe harbor even if the generator is interconnected with a distribution system, rather than a transmission system, if all of the requirements under section III.C of this notice are met. This notice also extends the provisions of the safe harbor to transfers of interties from energy storage facilities to regulated public utilities. The Treasury Department and the Internal Revenue Service (IRS) believe that these modifications will promote reliability and economic efficiency throughout the grid and the development and interconnection of renewable energy resources.

B. *Definitions*

1. *Generator*. A *generator* is an electricity generation or cogeneration facility or an energy storage facility.

2. *Intertie*. An *intertie* includes new connecting and transmission facilities, or modifications, upgrades, or relocations of a utility's existing transmission network that enable or facilitate the interconnection of a generator with a utility or improve efficiency on the utility's transmission network**.**

3. *Dual-use intertie*. A *dual-use intertie* is an intertie that is used to transmit power from a generator to a utility and that may be used to transmit power from the utility for sale to the generator. A dual-use intertie may be used, for example, when a generator relies on the utility as a backup or supplemental power source, either sporadically or on a regular basis. A dual-use intertie includes an intertie that may be used to transmit power from a third party for sale to the generator.

4. *Utility*. A *utility* is a regulated public utility.

C. *Requirements*

A contribution of an intertie, including a dual-use intertie, by a generator to a utility will not be treated as gross income under § 118(a) or a CIAC under 118(b) if all of the following conditions are met:

1. The generator may not purchase electricity from the utility, unless the purchase satisfies the 5% test.

a. *5% Test*. If, in light of all information available to the utility at the time the intertie is contributed, it is reasonably projected that, during the ten taxable years of the utility beginning with the year in which the contributed intertie is placed in service, no more than 5% of the projected total power flows over the intertie will flow to the generator, the 5% test will be satisfied. Such a projection must be supported by appropriate documentation. Total power flows mean power flows to or

from the generator over the intertie. Power flows to a generator include power flows to a related party of the generator, if the transmission of power to the related party has been facilitated by the contribution of the intertie. For purposes of the 5% test, power flows in the taxable year in which the transferred property is placed in service may, at the option of the utility, be ignored. Power purchases by the generator from parties other than the utility are not taken into account.

b. *Example*. A utility and a generator enter into a power purchase contract with a term of twenty years, under which the generator will purchase electricity from the utility. Power flows from the utility to the generator are expected to comprise 10% of total power flows over the intertie in the first year (the taxable year in which the facility is placed in service), 1% in the second and third years, and 0.5% in each of the fourth through tenth years. Total power flows are projected to be 100 megawatt hours ("MWH") in the first and second years, and 200 MWH in the third through tenth years. The utility excludes the first year of the contract from the projection. Thus, the utility reasonably projects that power flows to the generator will be 0.59% of total power flows over the intertie for the applicable nine-year period ((1% × 100 MWH) + (1% × 200 MWH) + (7 × (0.5% × 200 MWH))/(100 MWH + (8 × 200 MWH)). The purchase of electricity by the generator satisfies the 5% test.

2. In the case of electricity wheeled over the utility's transmission system, ownership of the wheeled electricity remains with the generator prior to its transmission onto the grid. This ownership requirement is deemed to be satisfied if title to electricity wheeled passes to the purchaser at the busbar on the generator's end of the intertie.

3. The cost of the intertie is not included in the utility's rate base.

4. The intertie will be used for transmitting electricity.

5. The cost of the intertie is capitalized by the generator as an intangible asset and recovered using the straight-line method over a useful life that is treated as 20 years. A utility may not claim depreciation (or amortization) deductions with respect to the intertie. However, if the intertie is subsequently transferred or deemed transferred to the utility, the utility may be allowed to take depreciation deductions with respect to the intertie.

IV. TERMINATION OF SAFE HARBOR

The occurrence of an event specified below will terminate the safe harbor and require the utility to recognize income as a consequence of the contribution of an intertie to a utility by a generator.

A. *Proportionate Disqualification*

1. *General rule*.

If, for each of any three taxable years within any period of five consecutive taxable years, more than 5% of the total power flows over the intertie flow from the utility to the generator (a "disqualification event"), then the generator will be deemed to have made a transfer to the utility that constitutes a CIAC under § 118(b) as of the last day of the third such year. At the option of the utility, the taxable year in which the property is placed in service shall not be taken into account in determining whether there has been a disqualification event. The amount of the CIAC shall be equal to the percentage of the fair market value of the intertie as of the date of the deemed transfer that reflects the use of the intertie for the purpose of selling power to the generator, as determined by the IRS by taking into account all facts and circumstances. Relevant factors include the use of the intertie since the date it was placed in service and the reasonably anticipated use of the intertie. This proportionate disqualification does not apply to any property necessary for, and used solely to facilitate, the transmission of power by the generator to the utility.

2. *Examples*.

These principles are illustrated by the following examples.

Example 1. A generator contributes a dual-use intertie to a utility that is a calendar year taxpayer. The utility places the intertie in service in 2010 and reasonably projects that, over the ten taxable years beginning in 2010, power flows over the intertie to the generator will be less than 5% of total power flows over the intertie. Actual power flows over the intertie to the generator constitute the following percentages of total flows over the intertie: 10% in 2010; 7% in 2011; 6% in 2012; 3% in 2013; 1% in 2014; and 6% in 2015. The utility excludes 2010 (the year in which the intertie is placed in service) from the determination of whether a disqualification event has occurred. A disqualification event occurs due to power flows in 2015, the third year within the five year period from 2011 to 2015 in which more than 5% of power flows over the intertie flow to the generator. Therefore, the generator is deemed to have made a CIAC transfer to the utility as of December 31, 2015.

Example 2. A contract between a generator and a utility requires the utility to relocate a major transmission line and to construct an intertie to the generator, including protective devices that are necessary and used solely for the delivery of power to the utility. Several years into the contract, the use of the intertie by the utility for delivery of power results in a disqualification event. Payments made for the construction of the protective devices are not subject to proportionate disqualification because the protection devices were necessary for, and used solely to facilitate, the transmission of power by the generator to the utility. However, because the transmission line is used for the delivery of power over the intertie by the utility to the generator, payments made for the relocation of the transmission lines are subject to proportionate disqualification.

3. *Determination of fair market value*.

The fair market value of a CIAC generally is determined under the replacement cost method, taking into account the condition of the property deemed transferred as a CIAC. *See* Notice 87–82, 1987–2 C.B. 389. Absent unusual circumstances, the fair market value of used CIAC property will be its depreciated replacement cost (the percentage of the replacement cost that reflects the remaining economic useful life of the property). For example, a trunk line originally cost $100x to install. Ten years later, the replacement cost of the line is $150x, and 60% of its useful life remains. The depreciated replacement cost is $90x *(*60% of $150x).

B. *Termination of Power Purchase Contract*

1. *General rule*.

Upon the termination of a power purchase contract between a generator and a utility, if the utility obtains or retains ownership (for tax purposes) of the intertie, the generator will be deemed to have transferred the intertie to the utility as of the first day of such termination. Such a deemed transfer will not be treated as a

CIAC, except in circumstances that indicate an intention by the parties to characterize a contribution of an intertie as a transaction that in substance constitutes a CIAC. The utility shall include in income the fair market value of the property deemed transferred less the amount, if any, paid by the utility to obtain or retain ownership of the property for tax purposes.

The amount paid by the utility to obtain or retain ownership of the property deemed transferred shall include any "extension allowance" or similar payment by the utility to the generator during the term of the power purchase contract. For this purpose, an extension allowance is a payment to compensate the generator in consideration of the anticipated use of the property by the utility to deliver power to customers other than the generator.

2. *Determination of fair market value*. The fair market value of the property deemed transferred upon termination (except for any deemed transfer treated as a CIAC) shall be determined by taking into account all facts and circumstances, including the age and condition of the property and whether the property is needed to serve the utility's customers.

If a utility pays to a generator an amount that is determined upon termination of a power purchase contract to be the fair market value for such property under a procedure or method established or used by the relevant utility commission, such fair market value shall be presumed correct in the absence of substantial contrary evidence. For this purpose, a utility commission may take into account any relevant factors, including payments made in connection with the retention of property by a utility upon the termination of a contract and payments by the utility during the term of the contract (for example, extension allowances).

3. *Examples*. These principles are illustrated by the following examples:

Example 1. A generator contributes to a utility a circuit breaker that is installed as part of an intertie to protect the utility against damage to its system in the event of a breakdown at the generator. At the termination of the power purchase contract, the utility does not need the circuit breaker to serve its customers. The fair market value of the circuit breaker is its salvage value (less any cost of removal).

Example 2. Upon the termination of a 20-year power purchase contract, a utility retains ownership of a 50-megawatt trunk line that was transferred by a generator at the commencement of the contract. The utility will not use the trunk line other than to supply power to a 10 megawatt customer who has hooked into the trunk line. The fair market value of the trunk line is the economic value to the utility of a 20-year old 10-megawatt line, taking into account any other characteristics or factors that are relevant.

Example 3. Assume the same facts as Example 2, except that upon termination the local public utility commission requires the utility to pay $10x to the generator, which the commission has determined to be the fair market value of the trunk line. In the absence of substantial contrary evidence, the commission's finding will be presumed correct. The $10x will be treated as the fair market value for federal income tax purposes, and, because the $10x fair market value is offset by the $10x the utility paid to the generator, the utility will not be required to include any amount in income upon termination.

Example 4. A generator transfers a trunk line to a utility pursuant to a long-term power purchase agreement. The trunk line cost the generator $10x to construct. Three years later, a customer of the utility interconnects into the trunk line, and the local public utility commission requires the utility to pay to the generator an extension allowance of $5x. The following year, another customer of the utility interconnects into the line, and the commission requires another extension allowance of $4x. The commission employs a procedure under which the utility will be required to compensate the generator for the fair market value of property deemed transferred upon termination. When the contract terminates, the commission determines that the utility has, by means of the extension allowances, paid to the generator the fair market value of the property. In the absence of substantial contrary evidence, the commission's finding will be respected, and the utility will not be required to include any amount in income upon termination.

Example 5. A generator transfers a trunk line to a utility pursuant to a 20-year power purchase contract. Upon the termination of the contract, the utility commission determines the fair market value of the trunk line to be $10x, but does not require the utility to pay this amount to the generator. No presumption of correctness attaches to the utility commission's findings.

V. CHANGE IN METHOD OF ACCOUNTING

A. *In General*. A change in a utility's treatment of a transfer of an intertie, including a change to or from the safe harbor method of accounting provided in section III of this notice, is a change in method of accounting to which the provisions of §§ 446 and 481 and the regulations thereunder apply. A utility that wants to change to the methods of accounting described in this notice must use the automatic change procedures in Rev. Proc. 2015–13, 2015–5 I.R.B. 419, or its successor.

B. *Automatic Change*. Rev. Proc. 2016–29, 2016–21 I.R.B. 880, is modified to add new section 15.16 to read as follows:

15.16 *Transfers of interties under the safe harbor described in Notice 2016–36 (§ 118).*

(1) *Description of change*.

(a) *Safe harbor applicable*. This change applies to a utility that wants to change to the safe harbor method of accounting provided in section III.C of Notice 2016–36, I.R.B. 2016–25, for the treatment under § 118 of a transfer of an intertie, including a dual-use intertie, by a generator to a utility. Under this safe harbor method of accounting, such a transfer will not be treated as gross income under § 118(a) or a contribution in aid of construction (CIAC) under § 118(b) if all of the conditions specified in section III.C of Notice 2016–36 are met.

(b) *Safe harbor terminates*. This change applies to a utility that is using the safe harbor method of accounting provided in section III.C of Notice 2016–36 and is required to terminate that safe harbor method of accounting because of the occurrence of an event specified in section IV of Notice 2016–36. The occurrence of such event will require the utility to recognize income as a consequence of the transfer of an intertie, including a dual-use intertie, to the utility by a generator.

(2) *Definitions*. For purposes of this section 15.16, the terms "utility," "intertie," "dual-use intertie," and "generator" are defined in section III.B of Notice 2016–36.

(3) *Certain eligibility rules inapplicable*. The eligibility rules in sections 5.01(1)(d) and (f) of Rev. Proc. 2015–13, 2015–5 I.R.B. 419, do not apply to a utility making a change under this section 15.16.

(4) *Manner of making change*.

(a) The change in method of accounting under section 15.16(1)(a) of this revenue procedure is made with a § 481(a) adjustment.

(b) The change in method of accounting under section 15.16(1)(b) of this revenue procedure is made using a cut-off method and applies to a transfer of an intertie, including a dual-use intertie, by a generator to a utility made on or after the beginning of the taxable year in which the

safe harbor method of accounting terminates.

(5) *Concurrent automatic change*. A utility making a change under this section 15.16 for more than one transfer of an intertie, including a dual-use intertie, for the same year of change should file a single Form 3115 for all such transfers. The single Form 3115 must provide a single net § 481(a) adjustment for all changes under section 15.16(1)(a) of this revenue procedure.

(6) *Designated automatic accounting method change number*. The designated automatic accounting method change number for a change to the methods of accounting under this section 15.16 is "226."

(7) *Contact information*. For further information regarding a change under this section 15.16, contact David Selig at (202) 317-4137 (not a toll-free call).

VI. EFFECT OF THIS DOCUMENT

This document serves as an "administrative pronouncement" as that term is described in § 1.6661–3(b)(2) and may be relied upon to the same extent as a revenue ruling or a revenue procedure.

VII. EFFECT ON OTHER DOCUMENTS

Notice 88–129, 1988–2 C.B. 541; Notice 90–60, 1990–2 C.B. 345; and Notice 2001–82, 2001–2 C.B. 619, are modified and superseded. Rev. Proc. 2016–29 is modified to include the accounting method changes provided in section V of this Notice in section 15 of Rev. Proc. 2016–29.

VIII. EFFECTIVE DATE

This notice applies to transfers of interties meeting all of the requirements under this notice made on or after June 20, 2016. However, taxpayers may choose to rely on this safe harbor for transfers with respect to qualifying transfers made prior to June 20, 2016. The IRS will not issue private letter rulings involving this safe harbor.

IX. DRAFTING INFORMATION

The principal author of this notice is David Selig of the Office of the Associate Chief Counsel (Passthroughs and Special Industries). For further information regarding this notice, contact Mr. Selig at (202) 317-4137 (not a toll free number).

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26 CFR 301.7705: Applying for certification as a certified professional employer organization.

Rev. Proc. 2016–33

SECTION 1. PURPOSE

The Stephen Beck, Jr., Achieving a Better Life Experience (ABLE) Act of 2014, enacted on December 19, 2014, as part of The Tax Increase Prevention Act of 2014 (Pub. L. 113–295), added new sections 3511 and 7705 to the Internal Revenue Code (Code) relating to the federal employment tax consequences and certification requirements, respectively, of a certified professional employer organization (CPEO). The ABLE Act requires the establishment of a voluntary program for persons to apply to become certified as a CPEO. Temporary regulations under section 7705 (TD 9768) describe the certification requirements necessary for a person to become and remain a CPEO. This revenue procedure sets forth the detailed procedures for applying to be certified as a CPEO. A future revenue procedure will address requirements for a CPEO to remain certified and the procedures relating to suspension and revocation of CPEO certification.

.01 *Description of terms used in this revenue procedure*. For purposes of this revenue procedure—

(1) The term "application" means the electronic submission by a CPEO applicant and its responsible individuals of all information required by the online application form for CPEO certification (made available by the Internal Revenue Service (IRS) on *www.irs.gov*), as well as all accompanying forms and documentation required by § 301.7705–2T of the Treasury Regulations, this revenue procedure, and the instructions accompanying the application.

(2) The term "controlled group" means any controlled group of corporations or trades or businesses under common control within the meaning of sections 414(b) and (c) of the Code, and the regulations thereunder.

(3) The term "certified public accountant" ("CPA") means a certified public accountant who—

(a) With respect to a CPEO applicant, is independent of the CPEO applicant (as prescribed by the American Institute of Certified Public Accountants' Professional Standards, Code of Professional Conduct, and its interpretations and rulings);

(b) Is not currently under suspension or disbarment from practice before the IRS;

(c) Is duly qualified to practice in any state; and

(d) Files with the IRS a written declaration that he or she is currently qualified as a CPA and an authorization, in accordance with the requirements of § 601.503(a), to represent the CPEO applicant before the IRS.

(4) The term "CPEO" means a person that has been certified by the Commissioner as meeting the requirements of § 301.7705–2T, this revenue procedure, and the instructions accompanying the application and whose certification has not been revoked.

(5) The term "CPEO applicant" means a person that submits or has submitted an application to be certified as a CPEO in accordance with § 301.7705–2T, this revenue procedure, and instructions accompanying the application. A CPEO applicant remains a CPEO applicant until the CPEO applicant withdraws its application; receives a notice of certification described in section 6.01 and timely and correctly submits a proof of bond, as described in section 6.02; or receives a notice of final denial, as described in section 8.04.

(6) The term "federal employment taxes" means the taxes imposed by subtitle C of the Code.

(7) The term "precursor entity" means an entity described in § 301.7705–1T(b)(10).

(8) The term "provider of employment-related services" means a person described in § 301.7705–1T(b)(11).

(9) The term "qualified surety" means a surety that meets the requirements of § 301.7705–2T(g)(6).

(10) The term "related entity" means any person described in § 301.7705–1T(b)(12).

(11) The term "responsible individual" means an individual described in § 301.7705–1T(b)(13).

.02 *Changes and request for comments*. This revenue procedure may be updated periodically to improve the CPEO certification process. The IRS solicits comments, including suggestions, relating to this revenue procedure and the administration of the CPEO certification program. All comments will be available for public inspection and copying. Comments may be submitted in one of three ways:

(1) By mail to CC:PA:LPD:PR (Rev. Proc. 2016–33), Room 5203, Internal Revenue Service, P.O. Box 7604, Ben Franklin Station, Washington, DC 20044.

(2) Electronically to Notice.Comments@irscounsel.treas.gov. Please include "Rev. Proc. 2016–33" in the subject line of any electronic communications.

(3) By hand-delivery Monday through Friday between the hours of 8 a.m. and 4 p.m. to CC:PA:LPD:PR (Rev. Proc. 2016–33), Courier's Desk, Internal Revenue Service, 1111 Constitution Ave., NW, Washington, DC 20224.

SECTION 2. PROCEDURES FOR APPLYING FOR CERTIFICATION AS A CPEO

.01 *Method of submission*. A person seeking certification as a CPEO must electronically submit a properly completed and executed online application for CPEO certification (made available by the IRS on *www.irs.gov*) and the accompanying forms and documentation required by § 301.7705–2T, this revenue procedure, and instructions accompanying the application. Paper submissions will not be accepted and will be treated as an incomplete application as described in section 4.02. Except as otherwise provided in this revenue procedure or the instructions accompanying the application, documents required by this revenue procedure to be submitted after the application is submitted and while the application is pending must also be submitted electronically, as provided by the instructions accompanying the application. The individual submitting the online application for CPEO certification on behalf of the CPEO applicant must be authorized by section 6103(e) to inspect the return of the CPEO applicant. In addition, each of the CPEO applicant's responsible individuals must electronically submit a properly completed and executed online Responsible Individual Personal Attestation (RIPA) form and must also provide an FD–258, Fingerprint Card at the time and in the manner described in the instructions accompanying the application. Once the RIPA is submitted, the information contained in the RIPA becomes return information of the CPEO applicant and may be disclosed to the CPEO applicant if the IRS determines that such disclosure will not impair Federal tax administration.

.02 *Controlled groups*. If more than one member of a controlled group seeks to be certified as a CPEO, each such member must submit a separate application. Members of a controlled group may not apply jointly on one application. See sections 2.04, 2.05(6), and 2.06(5) for details regarding the documentation relating to the bond and financial review requirements that CPEO applicants that are members of a controlled group must submit.

.03 *User fee*. Consistent with section 7528(b)(4), upon submission of the online application for initial certification, the individual that submits the application will be automatically directed to pay a user fee in the amount of $1,000 through *www.pay.gov*. Payment confirmations are provided through the *www.pay.gov* portal. Additional information about payment submission can be found under Frequently Asked Questions at *www.pay.gov*. No CPEO application will be processed until a user fee in the amount of $1,000 is received. Once processing of the application has begun, the user fee will not be returned, even if the application is withdrawn or denied.

.04 *Proof of bond.*

(1) *Surety letter*. With its application, a CPEO applicant must submit a signed letter from a qualified surety confirming that the surety agrees to issue a bond to the CPEO applicant if and when it is certified as a CPEO (a "surety letter"). The surety letter must also state that the surety agrees to issue a bond in the amount required by § 301.7705–2T(g)(2) and pursuant to the terms set forth in Form 14751, *Certified Professional Employer Organization Surety Bond*. If a CPEO applicant is a member of a controlled group of which other members are CPEO applicants or CPEOs, the surety letter must also contain the name and EIN of each CPEO applicant and each CPEO that is or will be covered by the bond. All CPEO members of a controlled group are required to be on the same bond in the amount required by § 301.7705–2T(g)(2), applied as if all such CPEO members (and/or any of their precursor entities, if applicable) were one organization.

(2) *Form 14751*. If the IRS approves a CPEO applicant's application for certification, the CPEO applicant has 30 days from the date the IRS provides notice of certification (see section 6) to submit a properly completed and executed Form 14751 (or, in the case of a CPEO applicant that is a member of a controlled group with existing CPEOs, to post a superseding bond using a properly completed and executed Form 14751, as described in section 6.02) providing for a bond in the amount required by § 301.7705–2T(g)(2) and signed by both a qualified surety and the CPEO (or CPEOs in the case of a bond covering a controlled group).

.05 *Submission of annual audited financial statements*.

(1) *Copy of financial statements*. With its application, a CPEO applicant must submit a copy of its annual audited financial statements for the most recently completed fiscal year as of the date it submits its application, except as provided in the next sentence. If a CPEO applicant submits its application before the last day of the sixth month following its most recently completed fiscal year, and the audit of the financial statements for that fiscal year has not been completed at the time it submits its application, the CPEO applicant must provide with its application the annual audited financial statements for the immediately preceding fiscal year, and the CPEO applicant must subsequently provide to the IRS the annual audited financial statements for the most recently completed fiscal year by the last day of the sixth month after such fiscal year ends. In addition, for any fiscal year that ends after the CPEO applicant submits its application for certification and on or before the effective date of certification, if applicable, the CPEO applicant must provide the annual audited financial statements by the last day of the sixth month after such

fiscal year ends. The obligations described in this paragraph continue even if the CPEO applicant is certified as a CPEO before the IRS has received the annual audited financial statements.

(2) *CPA opinion*. With each of these required annual audited financial statements, a CPEO applicant must submit an opinion of a CPA that such financial statements—

(a) Are presented fairly and in accordance with generally accepted accounting principles (GAAP);

(b) Reflect positive working capital (as defined by GAAP) or, only if the requirements of section 2.05(4) are met, reflect negative working capital, with the opinion in either case setting forth in detail a calculation of the CPEO applicant's working capital as reflected in the financial statements; and

(c) Reflect that the CPEO applicant computes its taxable income using an accrual method of accounting.

(3) *CPA opinion must be unmodified*. The CPA opinion must be unmodified (such that it cannot be a qualified opinion, an adverse opinion, or a disclaimer of opinion) and accompanied by a written declaration, signed by the CPA, that the CPA is currently qualified as a CPA and is authorized to represent the CPEO applicant before the IRS.

(4) *Exception for negative working capital*. A CPA opinion described in section 2.05(2) may state that a CPEO applicant's annual audited financial statements reflect negative working capital, but in that case the opinion will meet the requirements of section 2.05(2) only if—

(a) The CPEO applicant has negative working capital for no more than two consecutive fiscal quarters of the fiscal year, as demonstrated by the required annual audited financial statements or the statements described in section 2.06(3), or the submission of quarterly unaudited financial statements;

(b) The CPEO applicant or its CPA provides with the CPA opinion a detailed calculation of its negative working capital and an explanation to the IRS describing the reason for the failure; and

(c) The IRS determines, in its sole discretion, that the failure does not present a material risk to the IRS's collection of federal employment taxes. The determination of whether the failure presents a material risk to the IRS's collection of federal employment taxes may depend, in part, on whether the CPEO applicant has identified facts and circumstances that will result in positive working capital in the near future.

(5) *Newly-established CPEOs*. A CPEO applicant that was not operating as a provider of employment-related services for all or part of the most recently completed fiscal year as of the date it submits its application for certification must also provide a copy of the audited financial statements of the following entity or entities, if applicable, for each applicable entity's most recently completed fiscal year, accompanied by an unmodified opinion of a CPA that such financial statements are presented fairly and in accordance with GAAP and reflect positive working capital (as defined by GAAP) or, only if the requirements of section 2.05(4) are met (as applied to such entities), reflect negative working capital, with the opinion in either case setting forth in detail a calculation of the entity's working capital as reflected in the financial statements:

(a) Any precursor entity of the CPEO applicant; or

(b) If the CPEO applicant does not have a precursor entity, any related entity described in § 301.7705–1T(b)(12)(ii)(B).

(6) *Financial statements for controlled groups*. In satisfaction of the requirement in paragraph (1), if a CPEO applicant is a member of a controlled group of which other members are CPEO applicants or CPEOs, the CPEO applicant must submit copies of combined or consolidated annual audited financial statements for all CPEO applicants and CPEOs in the controlled group, with an accompanying unmodified opinion of a CPA that such financial statements are presented fairly and in accordance with GAAP. The combined or consolidated annual audited financial statements may, but are not required to, also include all members of the controlled group that are not CPEO applicants or CPEOs. The statements and opinion must contain the name and EIN of each CPEO applicant and CPEO in the controlled group. If the statements and opinion include members of the controlled group that are not CPEOs or CPEO applicants, the name and EIN of these members must also be included. Although the CPEO applicant is not required to provide a copy of its separate financial statements as part of its application, if the financial position of a CPEO applicant is unclear from the combined or consolidated financial statements of the controlled group of which the CPEO applicant is a member, the IRS may request additional financial information that is needed to evaluate the CPEO applicant's position, such as the annual balance sheet, income statement, and statement of cash flow, of the individual CPEO applicant. Notwithstanding the foregoing, and as required by section 2.05(2), a CPEO applicant that is a member of a controlled group of which other members are CPEO applicants or CPEOs must provide an opinion of a CPA that the individual CPEO applicant's financial statements reflect positive working capital (as defined by GAAP) or, if the requirements of section 2.05(4) are met, reflect negative working capital, with the opinion in either case setting forth in detail a calculation of the individual CPEO applicant's working capital. For purposes of the requirements of section 2.05(4), if it is unclear whether the CPEO applicant has positive or negative working capital for the last quarter of the fiscal year based on the combined or consolidated financial statements of the controlled group of which the CPEO applicant is a member, the IRS may request additional financial information on an individual CPEO applicant basis. The status of other CPEO applicants and CPEOs in the controlled group is not affected if the CPEO applicant is denied certification because the annual audited financial statements reflect that the CPEO applicant has negative working capital and the CPEO applicant fails to meet the exception described in section 2.05(4).

(7) A fiscal year will be considered completed once the last day of that fiscal year has ended, regardless of whether the CPEO applicant was in operation or certified for all 12 months of the fiscal year or the fiscal year consisted of fewer than 12 months.

.06 *Submission of quarterly assertions, attestations, and working capital statements*. For the most recently completed calendar quarter as of the date of its application for certification, a CPEO applicant must provide an assertion, as de-

scribed in section 2.06(1), that it has withheld and made deposits of all federal employment taxes for which the CPEO applicant is liable for the quarter; an examination level attestation from a CPA, as described in section 2.06(2), stating that this assertion is fairly stated in all material respects; and a statement verifying that the CPEO applicant has positive working capital, as described in section 2.06(3). The CPEO applicant must continue to provide this documentation for every subsequently completed calendar quarter during which its application for certification is pending for some or all of the quarter. This documentation must be provided by the last day of the second month after the end of each such subsequent quarter, even if the CPEO applicant receives its certification before this deadline.

(1) The assertion must be signed under penalties of perjury by a responsible individual of the CPEO applicant and state that the CPEO applicant has withheld and made deposits of all federal employment taxes for the calendar quarter (except that federal employment taxes imposed by chapter 23 of the Code are not required to be included in the assertion) as required by subtitle C.

(2) The examination level attestation from a CPA must state that the assertion described in section 2.06(1) is fairly stated in all material respects and comply with the requirements of the American Institute of Certified Public Accountants' Statements of Standards for Attestation Engagements, including the specific requirements for Examination Reports. The attestation must be accompanied by a written declaration, signed by the CPA, that the CPA is currently qualified as a CPA and is authorized to represent the CPEO applicant before the IRS. A CPEO applicant will not fail to meet the requirements of this section 2.06(2) if the examination level attestation indicates that the CPEO applicant has failed to withhold or make deposits in certain immaterial respects, provided that—

(a) The attestation provides a summary of the immaterial failures that were found;

(b) The attestation states that, and explains why, the failures were immaterial and isolated and do not reflect a meaningful lapse in compliance with federal employment tax withholding and deposit requirements; and

(c) The IRS determines, in its sole discretion, that the isolated and immaterial failures identified by the CPA do not present a material risk to the IRS's collection of federal employment taxes.

(3) The statement verifying positive working capital must be signed by a responsible individual under penalties of perjury and verify that the CPEO applicant has positive working capital (as defined by GAAP) with respect to the most recently completed fiscal quarter. The statement must include a detailed calculation of the CPEO applicant's working capital and be accompanied by a copy of the CPEO applicant's unaudited financial statements for the most recently completed fiscal quarter, if such statements are available. A CPEO applicant will not fail to meet the requirements of this section 2.06(3) as a result of having negative working capital at the end of the fiscal quarter if—

(a) The CPEO applicant does not have negative working capital at the end of the two fiscal quarters immediately preceding such fiscal quarter, as demonstrated by the required annual audited financial statements described in section 2.05 or the statements described in this section 2.06(3), or the submission of quarterly unaudited financial statements;

(b) The CPEO applicant provides a detailed calculation of its negative working capital, unaudited financial statements for the quarter, if available, and an explanation to the IRS describing the reason for such negative working capital; and

(c) The IRS determines, in its sole discretion, that the negative working capital does not present a material risk to the IRS's collection of federal employment taxes. The determination of whether the failure presents a material risk to the IRS's collection of federal employment taxes may depend, in part, on whether the CPEO applicant has identified facts and circumstances that will result in positive working capital in the near future.

(4) If a CPEO applicant was not operating as a provider of employment-related services for all or part of the most recently completed calendar quarter as of the date of its application for certification or during any calendar quarter that ends while its application for certification is pending, the CPEO applicant must provide the assertion, examination level attestation, and working capital statement described in this section 2.06 with respect to any precursor entity, if applicable. The information required by this section 2.06(4) must be provided by the last day of the second month after the end of each applicable calendar quarter, beginning with the most recently completed calendar quarter as of the date of the application (or as of the date the entity became a precursor entity while the application was pending) and for all subsequent quarters while the application is pending and the CPEO applicant is not operating as a provider of employment-related services for all or any portion of a quarter.

(5) In satisfaction of the requirement in this section 2.06, if a CPEO applicant is a member of a controlled group of which other members are CPEO applicants or CPEOs, the CPEO applicant must submit the quarterly assertions and attestations described in this Section 2.06 for all CPEO applicants and CPEOs in the controlled group on a controlled group basis, rather than for the CPEO applicant individually. The quarterly assertions and attestations must contain the name and EIN of each CPEO and CPEO applicant in the controlled group. However, the quarterly working capital statement described in section 2.06(3) must relate to the CPEO applicant alone and must not be prepared on a combined or consolidated basis with other members of the controlled group. For purposes of the requirements of Section 2.06(3), if it is unclear whether the CPEO applicant has positive or negative working capital for the last quarter of the fiscal year based on the combined or consolidated financial statements of the controlled group of which the CPEO applicant is a member, the IRS may request additional financial information about the individual CPEO applicant. The status of other CPEO applicants and CPEOs in the controlled group is not affected if the CPEO applicant is denied certification because the quarterly working capital statement described in section 2.06(3) reflects negative working capital and the CPEO applicant fails to meet the exception described in section 2.06(3).

(6) If a CPEO applicant submits its CPEO application before September 1, 2016, it may include with its application the assertion, examination level attestation, and working capital statement described in this section 2.06 with respect to the first calendar quarter of 2016, provided it subsequently provides the assertion, examination level attestation, and working capital statement with respect to the second calendar quarter of 2016 by September 1, 2016.

SECTION 3. SUITABILITY AND TAX-COMPLIANCE CHECK

A CPEO applicant will be required to identify its related entities, precursor entities, and responsible individuals as part of the application for certification. The IRS will investigate the accuracy of statements and representations made by a CPEO applicant and its responsible individuals in the CPEO applicant's application by conducting background checks of the CPEO applicant, any related entities or precursor entities, and responsible individuals. These background checks may include checks on tax compliance, criminal background, professional experience, credit history, professional sanctions, and other relevant facts. By submitting an application, a CPEO applicant and its responsible individuals agree to provide the IRS with such additional information as the IRS may request to facilitate its background investigations (see section 4.03). A CPEO applicant and each of its responsible individuals must take such actions as are necessary to authorize the IRS to conduct background checks and to investigate the accuracy of statements and submissions, including waiving confidentiality and privilege in situations in which the IRS is otherwise unable to obtain information. Failure to provide such information or take such action may result in denial of certification.

SECTION 4. STANDARDS FOR GRANTING CERTIFICATION AS A CPEO

.01 *Eligibility for certification must be established in application*. A CPEO applicant will be certified as a CPEO only if its application for certification and supporting documentation establish to the satisfaction of the IRS that the CPEO applicant meets the requirements of § 301.7705–2T, this revenue procedure, and the instructions accompanying the application so as not to present a material risk to the IRS's collection of federal employment taxes.

.02 *Incomplete or inaccurate application*. An application for certification must be complete and accurate. An application is not complete and accurate if it does not contain all of the items required by § 301.7705–2T, this revenue procedure, and the instructions accompanying the application. It is anticipated that the online application system will permit the submission of an application only once it is complete. If an incomplete application is submitted, the IRS generally will request from the CPEO applicant additional information needed for a completed application. However, the IRS may deny an incomplete application without requesting additional information.

.03 *Even if application is complete, additional information may be required*. Even if an application is complete, the IRS may request additional information before approving or denying certification. For instance, if the results of a background check or tax compliance check suggest a potential failure to meet any requirement described in § 301.7705–2T, the IRS may request that the CPEO applicant provide an explanation for such results. As another example, the IRS may ask a CPEO applicant to support its representations with respect to its knowledge or experience by providing a written work history or third-party references.

.04 *CPEO applicant must notify IRS of material changes relevant to its application for certification*. Within 30 days of its occurrence, a CPEO applicant must notify the IRS of any change that materially affects the continuing accuracy of any agreement or information that was previously made or provided to the IRS as a part of its application for certification. A material change includes, but is not limited to, any change in the tax compliance, criminal background, or professional license or registration status of the CPEO applicant, or any of its precursor entities, related entities, or responsible individuals; any change to the CPEO applicant's fiscal year; and any change that results in another individual being considered a responsible individual of the CPEO applicant or another entity being considered a precursor entity or a related entity of the CPEO applicant. For this purpose, a material change also includes the discovery of significant errors in or new facts relevant to any agreement or information provided to the IRS as part of the application for certification. Additional information concerning what qualifies as a material change and how and when, once certified, a CPEO must notify the IRS of a material change will be provided in a future revenue procedure.

SECTION 5. WITHDRAWAL OF APPLICATION

.01 *Application may be withdrawn*. An application may be withdrawn only upon the written request of a responsible individual authorized to correspond with the IRS on behalf of the CPEO applicant.

.02 *May be used in subsequent examination*. When an application is withdrawn, the IRS may retain and use for tax administration the application, all supporting documents, and the information submitted in connection with the withdrawal request.

SECTION 6. NOTICE OF CERTIFICATION

.01 *Notice of certification*. The IRS will issue electronically or by mail a notice of certification to a CPEO applicant that has been approved for certification. If a CPEO applicant is a member of a controlled group and other members of the controlled group are also applying for certification, the IRS will issue a separate notice of certification to each CPEO applicant member of the controlled group that has been approved for certification. The notice of certification will specify the effective date of certification and indicate that the effective date of certification is contingent upon timely receipt by the IRS of an acceptable Form 14751 as set forth in section 6.02.

.02 *Proof of bond*. A CPEO applicant has 30 days from the date of the notice of certification to submit to the IRS proof of a bond in the form of a properly completed and executed Form 14751, signed by both a qualified surety and the CPEO (or CPEOs in the case of a controlled group), and in an amount prescribed by

§ 301.7705–2T(g)(2). If the CPEO applicant fails to provide such proof of a bond within 30 days after the date of the notice, its certification will not become effective, and the CPEO applicant will subsequently be sent a final notice of denial (with no opportunity to request review of the denial). If a CPEO applicant in a controlled group receives a notice of certification after other members of its controlled group are already certified by the IRS, the CPEO applicant (or other members of the controlled group) will be required to post a superseding bond, in the form of a properly completed and executed Form 14751, that identifies all CPEOs in the controlled group and reflects the correct bond amount for all CPEOs in the controlled group, including the CPEO applicant. If the CPEO applicant fails to submit a superseding bond on Form 14571 within the time period provided in this paragraph, the CPEO applicant's certification will not become effective, and it will subsequently be sent a final notice of denial (with no opportunity to request review of the denial). However, the status of the other CPEOs in the controlled group will remain unaffected.

.03 *Effective date of certification*. The effective date of certification will typically be the first day of the first calendar quarter following the date of the notice of certification. However, the effective date of certification for a CPEO applicant that submits a complete and accurate application before September 1, 2016, and is certified will be January 1, 2017, even if the date of its notice of certification is after January 1, 2017.

SECTION 7. DISCLOSURE OF ORGANIZATIONS CERTIFIED AS CPEOS

The IRS will publish a list of all organizations that are certified as CPEOs, and the effective date of their certification, on the IRS website at *www.irs.gov/CPEOs*, which will be updated to reflect newly certified CPEOs by the 15th day of the first month of every calendar quarter. An organization will not appear on this list until the IRS has received from it the proof of bond on Form 14751, as described in section 6.02.

SECTION 8. DENIAL OF CERTIFICATION

.01 *Notice of proposed denial*. If the IRS decides that an application for certification should be denied based on the CPEO applicant's failure to satisfy one or more of the requirements of § 301.7705–2T, the IRS will issue a notice of proposed denial (unless the circumstances in section 8.02 apply), which will—

(1) Include the reason(s) for the denial of certification; and

(2) Advise the CPEO applicant of its opportunity to request review of the proposed denial.

.02 *Circumstances in which denial is final, with no opportunity for review*. In situations in which the denial of an application is based on the CPEO applicant's failure to comply with a requirement in § 301.7705–2T, this revenue procedure, or the instructions to the application and such failure is not subject to reasonable factual or legal dispute, the IRS will not issue a notice of proposed denial, but will instead issue a notice of final denial, which will include the reason(s) for the denial of certification, but will not provide for an opportunity for review. Denials based on failures that are not subject to reasonable factual or legal dispute include, but are not limited to, denial based on the following:

(1) The CPEO applicant submits an incomplete application as described in section 4.02, or fails to respond to a request from the IRS for additional information needed for a complete application (as described in section 4.02) by the date required.

(2) The CPA opinion of annual audited financial statements submitted by the CPEO applicant is a modified opinion (which includes a qualified opinion, an adverse opinion, or a disclaimer of opinion).

(3) The annual audited financial statements submitted by the CPEO applicant or the quarterly statements submitted by a responsible individual of the CPEO applicant reflect negative working capital, and the CPEO applicant fails to meet the exceptions described in section 2.05(4) or 2.06(3), respectively.

(4) The CPEO applicant fails to provide proof of the bond required in section 2.04 within 30 days after the date of the notice of certification.

.03 *Request for review of a notice of proposed denial*. A notice of proposed denial, in accordance with section 8.01, will advise the CPEO applicant of its opportunity to request a review by the IRS Office of Professional Responsibility (OPR). To request a review, the CPEO applicant must submit to the IRS CPEO program office identified in the notice of proposed denial a written statement of the facts, law, and arguments in support of its position within 30 days from the date of the notice of proposed denial. The arguments in support of the CPEO applicant's position should focus on the factual information provided by the CPEO applicant and its responsible individuals, including whether any information provided with or subsequent to the application has changed or was incorrect. Arguments concerning the materiality of information provided or whether certain facts present a material risk to the IRS's collection of federal employment taxes are outside the scope of review and will not be considered.

.04 *Notice of final denial where no request for review of the proposed denial is submitted*. If the CPEO applicant does not submit a timely request for review of a notice of proposed denial in accordance with section 8.03, a notice of final denial will be issued to the CPEO applicant.

.05 *How the IRS handles a request for review*. If a CPEO applicant submits a request for review, the IRS CPEO program office will first review the request and accompanying written statement of supporting arguments, and, if it determines that the CPEO applicant qualifies for certification, will issue the applicant a notice of certification. If the IRS CPEO program office maintains its position regarding a proposed denial after reviewing the request, it will forward the request for review and the application case file to OPR.

.06 *Consideration by OPR*. OPR will consider the CPEO applicant's request for review. OPR will apply an abuse of discretion standard to its review, and if OPR concludes that the CPEO program office erred in denying certification, it will issue a letter notifying the CPEO applicant that notice of certification will be issued by the CPEO program office. If OPR finds no abuse of discretion, it will issue a letter of final denial.

.07 *A request for review may be withdrawn*. A CPEO applicant may withdraw its request for review of the notice of proposed denial before OPR issues its final determination. A request for review may be withdrawn only upon the written request of a responsible individual authorized to correspond with the IRS on behalf of the CPEO applicant. Upon receipt of the CPEO applicant's withdrawal request, the IRS will complete the processing of the application in the same manner as if no request for review was received.

SECTION 9. EFFECTIVE DATE

This revenue procedure is effective July 1, 2016.

SECTION 10. PAPERWORK REDUCTION ACT

The collection of information contained in this revenue procedure has been reviewed and approved by the Office of Management and Budget (OMB) in accordance with the Paperwork Reduction Act (44 U.S.C. § 3507) under control number 1545-2266.

The collection of this information in this revenue procedure relates to the information that a person must submit to the IRS to be certified as a CPEO for purposes of sections 3511 and 7705 of the Code. The collection of information burden associated with this revenue procedure is reflected in the burden estimates for Form 14737, "Request for Voluntary IRS Certification of a Professional Employer Organization"; Form 14737–A, "Responsible Individual Personal Attestation"; Form 14751, "Certified Professional Employer Organization Surety Bond"; and § 301.7705–2T, all of which are under the same control number.

An agency may not conduct or sponsor, and a person is not required to respond to, a collection of information unless the collection of information displays a valid OMB control number.

Books and records relating to the collection of information must be retained as long as their contents may become material in the administration of any internal revenue law. Generally, tax returns and tax return information are confidential, as required by section 6103.

DRAFTING INFORMATION

The principal authors of this revenue procedure are Andrew Holubeck and Melissa Duce of the Office of the Associate Chief Counsel (Tax Exempt and Government Entities). For further information regarding this revenue procedure, please contact Andrew Holubeck at (202) 317-4774 (not a toll-free number).

Definition of Terms

Revenue rulings and revenue procedures (hereinafter referred to as "rulings") that have an effect on previous rulings use the following defined terms to describe the effect:

Amplified describes a situation where no change is being made in a prior published position, but the prior position is being extended to apply to a variation of the fact situation set forth therein. Thus, if an earlier ruling held that a principle applied to A, and the new ruling holds that the same principle also applies to B, the earlier ruling is amplified. (Compare with modified, below).

Clarified is used in those instances where the language in a prior ruling is being made clear because the language has caused, or may cause, some confusion. It is not used where a position in a prior ruling is being changed.

Distinguished describes a situation where a ruling mentions a previously published ruling and points out an essential difference between them.

Modified is used where the substance of a previously published position is being changed. Thus, if a prior ruling held that a principle applied to A but not to B, and the new ruling holds that it applies to both A and B, the prior ruling is modified because it corrects a published position. (Compare with amplified and *clarified*, above).

Obsoleted describes a previously published ruling that is not considered determinative with respect to future transactions. This term is most commonly used in a ruling that lists previously published rulings that are obsoleted because of changes in laws or regulations. A ruling may also be obsoleted because the substance has been included in regulations subsequently adopted.

Revoked describes situations where the position in the previously published ruling is not correct and the correct position is being stated in a new ruling.

Superseded describes a situation where the new ruling does nothing more than restate the substance and situation of a previously published ruling (or rulings). Thus, the term is used to republish under the 1986 Code and regulations the same position published under the 1939 Code and regulations. The term is also used when it is desired to republish in a single ruling a series of situations, names, etc., that were previously published over a period of time in separate rulings. If the new ruling does more than restate the substance of a prior ruling, a combination of terms is used. For example, modified and *superseded* describes a situation where the substance of a previously published ruling is being changed in part and is continued without change in part and it is desired to restate the valid portion of the previously published ruling in a new ruling that is self contained. In this case, the previously published ruling is first modified and then, as modified, is superseded.

Supplemented is used in situations in which a list, such as a list of the names of countries, is published in a ruling and that list is expanded by adding further names in subsequent rulings. After the original ruling has been supplemented several times, a new ruling may be published that includes the list in the original ruling and the additions, and supersedes all prior rulings in the series.

Suspended is used in rare situations to show that the previous published rulings will not be applied pending some future action such as the issuance of new or amended regulations, the outcome of cases in litigation, or the outcome of a Service study.

Abbreviations

The following abbreviations in current use and formerly used will appear in material published in the Bulletin.

A—Individual.
Acq.—Acquiescence.
B—Individual.
BE—Beneficiary.
BK—Bank.
B.T.A.—Board of Tax Appeals.
C—Individual.
C.B.—Cumulative Bulletin.
CFR—Code of Federal Regulations.
CI—City.
COOP—Cooperative.
Ct.D.—Court Decision.
CY—County.
D—Decedent.
DC—Dummy Corporation.
DE—Donee.
Del. Order—Delegation Order.
DISC—Domestic International Sales Corporation.
DR—Donor.
E—Estate.
EE—Employee.
E.O.—Executive Order.
ER—Employer.
ERISA—Employee Retirement Income Security Act.
EX—Executor.
F—Fiduciary.
FC—Foreign Country.
FICA—Federal Insurance Contributions Act.
FISC—Foreign International Sales Company.
FPH—Foreign Personal Holding Company.
F.R.—Federal Register.
FUTA—Federal Unemployment Tax Act.
FX—Foreign corporation.
G.C.M.—Chief Counsel's Memorandum.
GE—Grantee.
GP—General Partner.
GR—Grantor.
IC—Insurance Company.
I.R.B.—Internal Revenue Bulletin.
LE—Lessee.
LP—Limited Partner.
LR—Lessor.
M—Minor.
Nonacq.—Nonacquiescence.
O—Organization.
P—Parent Corporation.
PHC—Personal Holding Company.
PO—Possession of the U.S.
PR—Partner.
PRS—Partnership.
PTE—Prohibited Transaction Exemption.
Pub. L.—Public Law.
REIT—Real Estate Investment Trust.
Rev. Proc.—Revenue Procedure.
Rev. Rul.—Revenue Ruling.
S—Subsidiary.
S.P.R.—Statement of Procedural Rules.
Stat.—Statutes at Large.
T—Target Corporation.
T.C.—Tax Court.
T.D.—Treasury Decision.
TFE—Transferee.
TFR—Transferor.
T.I.R.—Technical Information Release.
TP—Taxpayer.
TR—Trust.
TT—Trustee.
U.S.C.—United States Code.
X—Corporation.
Y—Corporation.
Z—Corporation.

Numerical Finding List[1]

Bulletins 2016–1 through 2016–25

Announcements:

Notices:

Notices:—Continued

Proposed Regulations:

Revenue Procedures:

Revenue Procedures:—Continued

Revenue Rulings:

Treasury Decisions:

[1]A cumulative list of all revenue rulings, revenue procedures, Treasury decisions, etc., published in Internal Revenue Bulletins 2015–27 through 2015–52 is in Internal Revenue Bulletin 2015–52, dated December 28, 2015.

Finding List of Current Actions on Previously Published Items[1]

Bulletins 2016–1 through 2016–25

Announcements:

2007-21
Modified by
Ann. 2016-1, 2016-3 I.R.B. *283*

Notices:

2001-82
Modified by
Notice 2016-36, 2016-25 I.R.B. *1029*

2001-82
Superseded by
Notice 2016-36, 2016-25 I.R.B. *1029*

2005-50
Modified by
Notice 2016-2, 2016-2 I.R.B. *265*

2007-59
Revoked by
Notice 2016-16, 2016-7 I.R.B. *318*

2013-29
Clarified by
Notice 2016-31, 2016-23 I.R.B. *1025*

2013-46
Clarified by
Notice 2016-31, 2016-23 I.R.B. *1025*

2013-54
Supplemented by
Notice 2016-17, 2016-9 I.R.B. *358*

2014-79
Superseded by
Notice 2016-1, 2016-2 I.R.B. *265*

2015-25
Modified by
Notice 2016-31, 2016-23 I.R.B. *1025*

2015-52
Supplemented by
Notice 2016-17, 2016-9 I.R.B. *358*

2015-87
Supplemented by
Notice 2016-17, 2016-9 I.R.B. *358*

2016-29
Modified by
Notice 2016-36, 2016-25 I.R.B. *1029*

Notices:—Continued

2016-60
Modified by
Notice 2016-31, 2016-23 I.R.B. *1025*

Revenue Procedures:

1987-24
Superseded by
Rev. Proc. 2016-22, 2016-15 I.R.B. *577*

2003-36
Superseded by
Rev. Proc. 2016-19, 2016-13 I.R.B. *497*

2009-14
Modified by
Rev. Proc. 2016-30, 2016-21 I.R.B. *981*

2009-14
Superseded by
Rev. Proc. 2016-30, 2016-21 I.R.B. *981*

2014-56
Superseded by
Rev. Proc. 2016-20, 2016-13 I.R.B. *499*

2014-64
Supplemented by
Rev. Proc. 2016-18, 2016-17 I.R.B. *635*

2015-1
Superseded by
Rev. Proc. 2016-2, 2016-1 I.R.B. *1*

2015-2
Superseded by
Rev. Proc. 2016-2, 2016-1 I.R.B. *102*

2015-3
Superseded by
Rev. Proc. 2016-3, 2016-1 I.R.B. *126*

2015-5
Superseded by
Rev. Proc. 2016-5, 2016-1 I.R.B. *142*

2015-7
Superseded by
Rev. Proc. 2016-7, 2016-1 I.R.B. *188*

2015-8
Superseded by
Rev. Proc. 2016-8, 2016-1 I.R.B. *200*

2015-9
Superseded by
Rev. Proc. 2016-5, 2016-1 I.R.B. *239*

Revenue Procedures:—Continued

2015-10
Superseded by
Rev. Proc. 2016-10, 2016-2 I.R.B. *270*

2015-14
Amplified by
Rev. Proc. 2016-29, 2016-21 I.R.B. *880*

2015-14
Modified by
Rev. Proc. 2016-29, 2016-21 I.R.B. *880*

2015-19
Amplified by
Rev. Proc. 2016-23, 2016-16 I.R.B. *581*

2015-19
Modified by
Rev. Proc. 2016-23, 2016-16 I.R.B. *581*

2015-22
Superseded by
Rev. Proc. 2016-8, 2016-01 I.R.B. *243*

2015-34
Modified by
Rev. Proc. 2016-27, 2016-19 I.R.B. *725*

2015-34
Supplemented by
Rev. Proc. 2016-27, 2016-19 I.R.B. *725*

2015-50
Supplemented by
Rev. Proc. 2016-18, 2016-17 I.R.B. *635*

2015-53
Modified by
Rev. Proc. 2016-11, 2016-2 I.R.B. *274*

2016-1
Modified by
Rev. Proc. 2016-30, 2016-21 I.R.B. *981*

Revenue Rulings:

2005-3
Modified by
Rev. Rul. 2016-8, 2016-11 I.R.B. *426*

2008-15
Revoked by
Rev. Rul. 2016-3, 2016-3 I.R.B. *282*

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INTERNAL REVENUE BULLETIN

The Introduction at the beginning of this issue describes the purpose and content of this publication. The weekly Internal Revenue Bulletins are available at *www.irs.gov/irb/*.

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