



Documents for Podcast 007
Listed Transactions AFIT Presentation
July 26, 2005



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This podcast is based on a presentation given at the July 26 Arizona Forum for Improvement of Taxation Annual Summer Tax Seminar held at the Downtown Arizona State University Facility. The presentation involves the required disclosures for reportable transactions (including listed transactions). In this document is included the slides from the presentation and a copy of the list of listed transactions downloaded from the IRS website.

The podcast run about one hour, while the live presentation was one hour and forty minutes.

Arizona Forum for Improvement of Taxation has members from the Arizona State Bar Association, Arizona Society of Enrolled Agents, Arizona Society of Certified Public Accountants, and Arizona Society of Practicing Accountants with liaison from the Internal Revenue Service, Arizona Department of Revenue, and City of Phoenix.

Reportable and Listed Transactions Disclosure

AFIT Conference
July 26, 2005

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Slide 1

Penalties for Failure to Disclose Reportable Transactions

- The law adds significant penalties for failing to include a required disclosure of a reportable transaction (New §6707A)
- *The provision may apply to your client—and you may not be aware of the transaction unless you ask.*
- A major trap for the unwary

Slide 2

Penalty Amounts

- General penalty for each failure to disclose a reportable transaction (§6707A(b)(1))
 - \$10,000 for an individual
 - \$50,000 for any other entity
- Increased penalty for a listed transaction (§6707A(b)(2))
 - \$100,000 for an individual
 - \$200,000 for any other entity

Slide 3

Penalty on Disclosure Issue Only

- The penalty is on the failure to disclose
- The merits of the position is not an issue in this penalty
- Taxpayer could win the issue hands down in court, and still would lose on the penalty under the law

Slide 4

Penalty Waiver

- Reportable Transactions Penalty
 - IRS has authority to rescind the *reportable transactions* penalty (§6707A(d)(1))
 - Can do so if rescinding the penalty would promote compliance with the requirements of the IRC and effective tax administration
 - No judicial review of an IRS action on rescinding the penalty is available (§6707A(d)(2))

Slide 5

Penalty Waiver

- IRS required to report on each waiver in detail (§6707A(d)(3))
- Act requires that the IRS report each year to Congress on waivers granted under this provision (Act §811(d))
- Seems likely the IRS won't grant many waivers

Slide 6

Listed Transaction Penalty Not Open to Waiver

- The IRS has no authority to waive the penalty for failure to report a listed transaction (§6707A(d)(1)(A))
- Note that in neither case is the penalty subject to the standard "reasonable cause" provisions

Slide 7

Penalty Reported to SEC

- Penalty reported in reports filed with the SEC for public companies
- Failure to report the penalty to the SEC is treated as a separate failure to report the transaction under this provision

Slide 8

Effective Date

- Effective for returns and statements whose due date is after October 22, 2004

Slide 9

What Must Be Done?

- Disclosure rules found in Reg. §1.6011-4
- Additional regulations apply these rules to tax returns other than income tax returns

Slide 10

General Rule

- Found at §1.6011-1(a)
- Reporting required if
 - Taxpayer participated (as defined in §1.6011-1(c)(3))
 - in a reportable transaction (as defined in §1.6011-1(b))
 - and is required to file a tax return

Slide 11

General Rule

- Nature of Report
 - Attach to returns for specified taxable years (defined in §1.6011-4(e))
 - A disclosure statement specified at §1.6011-4(d)
- Regulation specifies that the fact a transaction is a reportable transaction shall not affect the legal determination of whether the treatment is proper (§1.6011-4(a))

Slide 12

Reportable Transactions

- Fits into one of six categories
 - Listed transaction (§1.6011-4(b)(2))
 - Confidential transactions (§1.6011-4(b)(3))
 - Transactions with contractual protection (§1.6011-4(b)(4))
 - Loss transactions (§1.6011-4(b)(5))
 - Transactions with significant book-tax difference (§1.6011-4(b)(6))

Slide 13

Reportable Transactions

- Fits into one of six categories (cont'd)
 - Transactions involving a brief holding period (§1.6011-4(b)(7))
 - Does not fall into exceptions found at §1.6011-4(b)(8)

Slide 14

Listed Transactions

- Transaction identified by IRS as a listed transaction in
 - Notice
 - Regulation
 - Any other form of guidance
- Current list can be found on IRS website
- As well, any transaction “substantially similar” to any listed transaction

Slide 15

Listed Transactions

- Potential problem areas
 - Certain §419 & §419A plans (Notices 95-34 & 2003-24)
 - Purported multiple employer welfare trusts
 - Purportedly collectively bargained trusts
 - Certain §412(i) arrangements (Rev Rul 2004-20)
 - Premiums on policy providing for an annuity greater than the plan benefit at retirement date
 - Premiums on policy providing for a death benefit in excess of plan death benefit

Slide 16

Listed Transactions

- Potential problem areas (continued)
 - Certain Roth IRA structures (Notice 2004-8)
 - Roth IRA invests in an entity
 - Entity acquires assets from an entity controlled by taxpayer, either by purchase or otherwise, for less than fair value
 - Note potential for arguing some structures used for real estate investments in either Roth or regular IRA are “similar” if IRS attacks the price paid by IRA

Slide 17

Listed Transactions

- Potential problem areas (continued)
 - Certain S Corporation ESOP Structures (Revenue Ruling 2003-6)
 - Transfers of compensatory nonqualified stock options to a related party (Notice 2003-47)
 - S Corporation shelter involving shifting income to a tax-exempt organization (Notice 2004-30)
- The IRS can add to this list at any time

Slide 18

Listed Transactions

- Client may have been told “you don’t have to report this” and “you don’t have to tell your CPA”
- Have to inquire about these issues
- Remember, if the transaction on this list or substantially similar the penalty cannot be waived by the IRS if the transaction isn’t disclosed

Slide 19

Substantially Similar

- Defined at §1.6011-4(c)(4)
 - Transaction expected to obtain the same or similar types of tax consequences
 - Factually similar or based on the same or similar strategy
- Receipt of an opinion is not relevant to determination of “similar”
- Broadly construed in favor of disclosure

Slide 20

Confidential Transactions

- Defined as a transaction
 - Offered to taxpayer under a condition of confidentiality
 - For which the taxpayer has paid an advisor a minimum fee

Slide 21

Condition of Confidentiality

- Advisor places a limitation on disclosure by the taxpayer of the tax treatment or tax structure of the transaction and
- The limitation on disclosure protects the confidentiality of that advisor's tax strategies

Slide 22

Condition of Confidentiality

- Will still be considered a condition of confidentiality even if it turns out not to be legally binding on the taxpayer
- However, a claim that the transaction is proprietary or exclusive is not a limitation if advisor confirms to the taxpayer there is no limitation on disclosure of the tax treatment or tax structure of the transaction

Slide 23

Minimum Fee

- Fee paid to advisor is at least
 - \$250,000 if taxpayer is a corporation
 - \$50,000 for all other entities, except for partnerships or trusts where all owners or beneficiaries are corporation which go back to the \$250,000 fee
- Minimum fee calculated under expansive rules and related parties treated as one person

Slide 24

Contractual Protection

- Two ways to come under this definition
 - Taxpayer or a related party has the right to a full or partial refund of fees if all or part of the intended tax consequences are not sustained *or*
 - The fees are contingent on the taxpayer's realization of tax benefits from the transaction\
- All facts and circumstances considered in determining whether the tests are met

Slide 25

Contractual Protection

- Will consider right to reimbursement of amounts that have not technically been designated as fees as meeting test
- As well, any agreement to provide services without reasonable compensation

Slide 26

Contractual Protection Exceptions

- Exceptions
 - A transaction will not be considered to have contractual protection *solely* because one party has a right to cancel the transaction upon the happening of an event affecting the taxation of one of the parties
 - Previously reported transaction exception

Slide 27

Contractual Protection

- Revenue Procedure 2004-65, issued November 16, 2004 exempts following transactions with contingent fee related to
 - Work Opportunity Credit under § 51
 - Welfare-to-work Credit under § 51A.
 - Indian Employment Credit under § 45A(a)

Slide 28

Previously Reported Transaction

- Exception for contingent or refundable fees if
 - Advice given after the transaction has taken place and the consequences reported on a filed tax return
 - Advisor has not previously received fees from the taxpayer relating to the transaction
 - Essentially, an “after the fact” exception

Slide 29

Loss Transactions Under §165

- Any transaction resulting in a taxpayer claiming a loss under §165 of at least
 - \$10 million in any single taxable year or \$20 million in any combination of taxable years for a corporation
 - \$10 million in any single taxable year or \$20 million in any combination of taxable years for partnerships that have only corporations as partners

Slide 30

Loss Transactions Under §165

- Any transaction resulting in a taxpayer claiming a loss under §165 of at least
 - \$2 million in any single taxable year or \$4 million in any combination of taxable years for all other partnerships, individuals, S corporations or trusts
 - \$50,000 in any single taxable year for individuals or trusts with respect to 988 transaction (foreign currency transactions)

Slide 31

Loss Transactions Under §165

- Any transaction resulting in a taxpayer claiming a loss under §165 of at least
 - Note that for the 988 transactions, it counts whether or not the loss flows through from an S corporation or trust
- For cumulative loss calculation, includes only year entered into transaction and five following taxable years

Slide 32

Section 165 Loss

- Section 165 Loss adjusted for any salvage value or any insurance or other compensation received
- Does not take into account offsetting gains or other income or limitations (such as on wagering losses or capital losses)
- Full loss taken into account in year sustained, regardless of ending up in a carryover

Slide 33

Section 165 Loss

- Includes an amount deductible pursuant to another provision that treats a transaction as a sale or other disposition
 - Sale or exchange of partnership interest under §741
 - Loss resulting from §988 transaction (foreign currency)

Slide 34

Section 165 Loss

- Revenue Procedure 2004-66, issued November 16, 2004 exempts from coverage transactions if
 - Asset is not disqualified (Section .02(1))
 - Asset has a “qualifying basis” (Section .02(2))
- Check the procedure for details if it appears would otherwise meet the test

Slide 35

Significant Book-Tax Difference

- Differs by more than \$10 million on a gross basis from amount of item for book purposes
- “Book” is to be considered US GAAP basis unless entity does not maintain US GAAP books for any purpose
- Difference calculation ignores any “reserve” for taxes

Slide 36

Applicability of Book-Tax

- Entities subject to reporting under the Securities Exchange Act of 1934 and related entities
- Other entities with gross assets in excess of \$250 million at the end of the year in question
- Not generally going to be an issue for most small firm clients

Slide 37

Applicability of Book-Tax

- Revenue Procedure 2004-67, issued November 16, 2004
- List of 35 transactions that “don’t count” for this purpose
- Again, consult this list if it appears you may have a transaction that would otherwise be reportable

Slide 38

Brief Asset Holding Period

- Transaction claiming a tax credit in excess of \$250,000 (including a foreign tax credit)
- Underlying asset giving rise to the credit is held for 45 days or less
- Apply principles of §246(c)(3) and (4) to determine holding period—periods when protected from loss do not count as days held

Slide 39

Brief Asset Holding Period

- Revenue Procedure 2004-68, issued November 16, 2004
- Provides list of 4 transactions fact patterns that will be excluded from a reportable transaction
- Again, check the list if it appears you have an issue here

Slide 40

Exception Based on Ruling

- Otherwise includable item can be excluded by a determination made by the IRS
 - Must be published guidance
 - Can be done as a private letter ruling, but only applicable to the taxpayer that requests the ruling
- As noted earlier, IRS issued a set of “exclusion” rulings on November 16, 2004

Slide 41

Participation in Transaction

- A trigger for reporting
- Defined at §1.6011-4(c)(3)(i) for each type of reportable transaction, followed by examples at §1.6011-4(c)(3)(ii)
- Note that multiple “layers” of taxpayers may participate in a single transaction (can “passthrough” or both parties may have to report)

Slide 42

Participation Listed Transactions

- Return reflects tax consequences or a tax strategy of a listed transaction *or*
- Taxpayer knows, or has reason to know, taxpayers’ tax benefits are derived directly or indirectly from a listed transaction
- IRS, by published guidance, may expand the list of participants in a particular listed transaction (and they have)
- Note that it can “pass through”

Slide 43

Participation Confidential Transactions

- Taxpayer’s tax return reflects a tax benefit from a confidential transaction
- If partnership, S corporation or trust’s disclosure is limited *and* the partners’, shareholders’ or beneficiaries’ disclosure is not limited, then the entity, and not the individuals, participated in the transaction
- Both can be required to report

Slide 44

Participation Contractual Protection

- Return reflects a tax benefit and taxpayer has a right to full or partial refund or fee is contingent
- If only passthrough may get refund, entity only reports
- If there is an individual right to refund, then partner/shareholder/beneficiary would also have a reportable transaction

Slide 45

Participation Loss Transaction

- Return reflects loss and loss exceeds limits
- For pass through, measure each partner/shareholder/beneficiary's allocable share of loss (not netted or limited by other rules)
- Entity itself runs its own test

Slide 46

Participation Book-Tax Difference

- If meets the test for the book-tax difference trigger, has participated
- Ignore differences that exist solely because entity is consolidated for book, but not tax, purposes

Slide 47

Participation Brief Asset Holding Period

- Have the "reported on a return" test
- Again, for a passthrough, test independently at the partner/shareholder/beneficiary level for partner/shareholder/beneficiary reporting

Slide 48

Participation Shareholder Foreign Corporation

- Regulation §1.6011-4(c)(3)(i)(G)
- Reporting shareholder generally do a “as if” test to see if corporation would have to report if a domestic corporation for all except “book-tax” difference
- For book-tax difference, do the above but only count if it reduces or eliminates an income inclusion otherwise required under §551, §951 or §1293

Slide 49

Participation Shareholder Foreign Corporation

- Five year limit on counting participation via this provision
- Reporting shareholder is a United States shareholder in a foreign personal holding company (§552) or controlled foreign corporation (§951(b)) or a 10% shareholder (by vote or value) in a qualified electing fund (§1295)

Slide 50

Form and Content of Statement

- Found at §1.6011-4(d)
- Must use IRS Form 8886 or successor
- Must follow the form instructions
- Must attach to the appropriate return(s)
- Can't shortcut this via other disclosure—at least without risking a big buck penalty

Slide 51

When Taxpayer Discloses

- Must attach disclosure statement to return for each year the taxpayer participates in a reportable transaction
- Must attach to each amended return that reflects participation in a reportable transaction
- In first year the taxpayer reports participation in the transaction, a copy must be filed with Office of Tax Shelter Analysis as well

Slide 52

Carryback to Prior Year

- If reportable transaction results in a loss that is carried back, must attach a disclosure statement to each application for tentative refund and/or amended return filed

Slide 53

Transaction Becomes Listed After Return Filed

- Taxpayer has participated in a transaction that was not a listed transaction when return filed but
- The IRS later publishes guidance making it a listed transaction and
- The statute has not run on the final return reflecting the tax consequence of the strategy then

Slide 54

Transaction Becomes Listed After Return Filed

- A disclosure statement must be filed with the return next filed after the date the transaction is listed
- That is true even if the taxpayer does not participate in the transaction on that return (Reg. §1.6011-4(e)(2)(i))

Slide 55

Loss Transaction

- If a transaction becomes a loss transaction due to cumulative losses then
- Must attach disclosure statement to return for the year in which the threshold is crossed and
- Any subsequent return which reflects any amount of Section 165 loss from that transaction (Reg. §1.6011-4(e)(2)(ii))

Slide 56

Multiple Disclosures

- Must disclose under these rules even if the taxpayer plans to disclose the transaction under other guidance (Reg. §1.6011-4(e)(3))
- Emphasizes that this isn't horseshoes—close isn't going to be viewed as “good enough”
- That is, generally you cannot argue the IRS knew or should have known about the transaction based on other disclosures

Slide 57

Ruling Requests

- Taxpayer can request a PLR on whether the transaction is subject to disclosure (Reg. §1.6011-4(f)(1))
- Must request on or before the date when disclosure would otherwise have been required
- If do so, the obligation to report will be suspended until 60 days after issuance of the ruling or the request is withdrawn

Slide 58

Ruling Requests

- The IRS may, at its discretion, treat the ruling request as satisfying the disclosure obligation
- Remember, the PLR only applies to the taxpayer requesting the ruling—so can't “piggyback” on someone else's ruling

Slide 59

Ruling on Merits

- Taxpayer requests ruling on the merits of the transaction on or before the date disclosure otherwise would be required
- Disclosure rules satisfied so long as the request fully discloses all relevant facts relating to the transaction that would otherwise be required to be disclosed

Slide 60

Protective Disclosure

- Taxpayer can file a protective disclosure §1.6011-4(f)(2)
- Disclose in accordance with the requirements of the regulation
- Indicate unsure whether transaction required to be disclosed and statement being filed on protective basis

Slide 61



Listed Abusive Tax Shelters and Transactions

- [Revenue Ruling 90-105](#) – Certain Accelerated Deductions for Contributions to a Qualified Cash or Deferred Arrangement or Matching Contributions to a Defined Contribution Plan
 - Coordinated Issue Paper - [Deduction of Contributions to IRC section 401\(k\) Plans Attributable to Compensation Paid After Year End Under IRC section 404\(a\)\(6\)](#) - Revised 9-24-2004.
 - [Lead Executive Memorandum](#) -- Advises that settlements will not be offered on these issues
 - [Revenue Ruling 2002-46](#)– §401k Accelerators
 - [Revenue Ruling 2002-73](#) - modifies RR 2002-46 for taxpayers electing to change method of accounting.
- [Notice 95-34](#) – Certain Trusts Purported to be Multiple Employer Welfare Funds Exempted from the Lists of §§ 419 and 419A
- [ASA Investing Partnership v. Commissioner](#) -Transactions similar to that described in the ASA Investing litigation and in [ACM Partnership v. Commissioner](#), 157 F.3d 231 (3rd Cir. 1998)
- [Treasury Regulation § 1.643\(a\)-8](#) – Certain Distributions from Charitable Remainder Trusts
- [Notice 99-59](#) – Transactions involving the distributions of encumbered property in which losses claimed for capital outlays have been recovered (aka BOSS transactions).
- [Treasury Regulation § 1.7701\(l\)-3](#) – Fast Pay or Step-Down Preferred Transactions
- [Revenue Ruling 2000-12](#) – Debt Straddles
- [Notice 2000-44](#) – Inflated Partnership Basis Transactions (Son of Boss)
 - Son of Boss Settlement Initiative
 - [IRS Collects \\$3.2 Billion from Son of Boss](#)
 - [Strong response to "Son of Boss" Settlement Initiative](#) -- Over 1,500 taxpayers responded by the June 21 deadline to settle under Announcement 2004-46.
 - [IRS News Release Announcing Settlement Initiative](#)
 - [IRS Fact Sheet, Son of Boss Settlement Initiative](#)
 - [Announcement 2004-46, Son of Boss Settlement Initiative](#)
 - [FAQs](#)(updated 5-28-04 with eligibility information)
 - [Supplemental FAQs](#) (11-1-04)
 - [Form 13582, Notice of Election to Participate in Settlement Initiative](#)
 - [Form 13586, Additional Information and Documentation](#)
 - [Form 13586-A, Settlement Initiative Declaration](#)
 - [Initial RA Letter to Taxpayer](#)
 - [Rejection Letter](#)
 - [Closing Agreement Letter](#)
 - [CCN 2003-20](#) - Chief Counsel Guidance
- [Notice 2000-60](#) – Stock Compensation Transactions
- [Notice 2000-61](#) – Guam Trust
- [Notice 2001-16](#) – Intermediary Transactions
 - Coordinated Issue Paper - Intermediary Transactions
- [Notice 2001-17](#) - §351 Contingent Liability
- [Notice 2001- 45](#) – §302 Basis-Shifting Transactions
- [Notice 2002-21](#) – Inflated Basis "CARDS" Transactions
 - [Notice 2002-21 Coordinated Issue Paper](#)
 - [Appeals Settlement Guidelines \(redacted\)](#)
- [Notice 2002-35](#) – Notional Principal Contracts
- [Notice 2002-50](#)– Partnership Straddle Tax Shelter
 - [Coordinated Issue Paper on Notice 2002-50 Transactions](#)
 - [Notice 2003-54](#) - Common Trust Fund Straddle Tax Shelter
 - [Notice 2002-65](#)– Passthrough Entity Straddle Tax Shelter
 - [Coordinated Issue Paper on Notice 2002-65 Transactions](#)
- [Revenue Ruling 2002-69](#) – Lease In / Lease Out or LILO Transactions
 - [Revenue Ruling 99-14](#) – Lease-In / Lease-Out or LILO Transactions
 - [Coordinated Issue Paper - Losses Claimed and Income to be Reported from Lease In / Lease Out transactions](#)
- [Revenue Ruling 2003-6](#) - Abuses Associated with S Corp ESOPs
- [Notice 2003-22](#) - Offshore Deferred Compensation Arrangements
- [Notice 2003-24](#) - Certain Trust Arrangements Seeking to Qualify for Exception for Collectively Bargained Welfare Benefit Funds under § 419A(f)(5)

- [Notice 2003-47](#) - Transfers of Compensatory Stock Options to Related Persons
 - [Announcement 2005-39](#) - Additional Guidance relating to Announcement 2005-19
 - [Announcement 2005-19 - Stock Option Settlement Initiative](#)
 - [Frequently Asked Questions](#) - Stock Option Settlement
 - [Stock Option Settlement Press Release](#)
 - [Stock Option Settlement Fact Sheet](#)
 - [Form 13656](#) - Settlement Election For Executives and Related Parties
 - [Form 13567](#) - Settlement Election for Corporations
- [Notice 2003-55](#) - Accounting for Lease Strips and Other Stripping Transactions
 - [Notice 95-53](#) – Lease Strips - Modified and superseded by Notice 2003-55 above
- [Notice 2003-77](#) - Improper use of contested liability trusts to attempt to accelerate deductions for contested liabilities under IRC 461(f)
 - [Lead Executive Memorandum](#) -- Advises that settlements will not be offered on these issues
 - [Department of Treasury News Release](#)
 - [TD 9095](#)
 - [Regulation 136890-02](#)
 - [Revenue Procedure 2004-31](#) - Change of accounting methods for improper contested liability trust transactions described in Notice 2003-77.
 - [Treasury News Release](#) - Announcing Revenue Procedure 2004-31
- [Notice 2003-81](#) - Offsetting Foreign Currency Option Contracts
- [Notice 2004-8](#) - Abusive Roth IRA Transactions
 - [Treasury Department News Release](#)
- [Revenue Ruling 2004-04](#) -- Prohibited Allocations of Securities in an S Corporation
 - [Treasury Department Press Release](#)
- [Revenue Ruling 2004-20](#) --Abusive Transactions Involving Insurance Policies in IRC 412(i) Retirement Plans
 - [Revenue Ruling 2004-21](#)
 - [Proposed Regulation 126967-03](#)
 - [Revenue Procedure 2004-16](#)
 - [News Release IR-2004-21](#)
- [Notice 2004-20](#) -- Abusive Foreign Tax Credit Transactions
 - [Treasury Department Press Release](#)
 - [Notice 2004-19](#) -- Withdraws [Notice 98-5](#) and describes strategy to address abusive FTC transactions
- [Notice 2004-30](#) -- S Corporation Tax Shelter Involving Shifting Income to Tax Exempt Organization
 - [Lead Executive Memo regarding settlements \(4/6/05\)](#)
 - [IRS Press Release 2004-44](#)
- [Notice 2004-31](#) -- Intercompany Financing Through Partnerships
 - [Treasury Press Release dtd 4/1/04](#)
- [Notice 2005-13](#), Sale-In Lease-Out transactions
 - [Treasury Press Release](#)

"De-Listed" Transactions

- [Notice 2004-65](#) De-lists Producer Owned Reinsurance Companies (PORC) as a listed transaction
- [News Release](#) dated 09-24-2004
- [Notice 2004-64](#) Modification of exemption from tax for small property and casualty insurance companies.
- [Notice 2002-70](#) modified by Notice 2004-65.