February 7, 2005

The Honorable Mark W. Everson
Commissioner of Internal Revenue
Internal Revenue Service
Room 5226
1111 Constitution Avenue, NW
Washington, DC 20224

Re: Comments Concerning Notice 2004-80
(Interim Guidance Under IRC §§ 6111, 6112 and 6708)

Dear Commissioner Everson:

Enclosed are comments concerning Notice 2004-80 as prepared by members of the Committee on Administrative Practice, Committee on Partnerships and LLCs, Committee on Standards of Tax Practice and the Tax Shelters Task Force. These comments represent the individual views of those members who prepared them and do not represent the position of the American Bar Association or of the Section of Taxation.

Sincerely,

Kenneth W. Gideon
Chair, Section of Taxation

Enclosure

cc: Eric Solomon, Acting Deputy Assistant Secretary for Tax Policy, Treasury
    Helen Hubbard, Tax Legislative Counsel, Treasury
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COMMENTS CONCERNING NOTICE 2004-80
(INTERIM GUIDANCE UNDER I.R.C. §§ 6111, 6112 AND 6708)

The following comments represent the individual views of the members of the Section of Taxation who prepared them and do not represent the position of the American Bar Association or the Section of Taxation.

These comments were prepared as a joint project of the Section of Taxation’s Administrative Practice Committee, Partnerships and LLCs Committee, Standards of Tax Practice Committee and Tax Shelter Task Force. Principal responsibility was exercised by Ronald L. Buch, Jr., Paul Carman, R. Brent Clifton, Adam M. Cohen, Peter J. Connors, Armando Gomez, Michael B. Lang, Caroline Root and Danielle M. Smith. Substantive contributions were made by Jeffrey H. Schechter, William H. Caudill and William M. Paul. The comments were reviewed by Karen L. Hawkins of the Section’s Committee on Government Submissions and by Charles A. Pulaski, Jr., Council Director for the Committee on Administrative Practice.

All (but one) of the members who participated in this report are tax practitioners and, therefore, would be affected by the federal principles addressed herein and belong to firms or organizations who would be affected by such principles. However, no such members (or the firm or organization to which such member belongs) has been engaged by a client to make a governmental submission with respect to, or otherwise to influence the development or outcome of, the specific subject matter of these comments.

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Date: February 7, 2005
I. Executive Summary.

In Notice 2004-80, the Internal Revenue Service ("Service") and the Department of Treasury ("Treasury") requested public comment “regarding the requirements of sections 6111, 6112, and 6708, including comments on the definition of material advisor and comments on ways to reduce taxpayer burden and improve disclosure.” On January 28, 2005, the Service and Treasury issued Notice 2005-17, which stated that the Service and Treasury intend to issue further guidance on the issue of the date on which a person becomes a material advisor with respect to a reportable transaction “including whether the obligation of a material advisor arises only when a reportable transaction is entered into by a taxpayer.” The following comments will address certain issues relating to the requirements of sections 6111, 6112 or 6708 as modified by the interim guidance set forth in Notice 2004-80 and Notice 2005-17, and will offer certain suggestions for reducing taxpayer burden and improving disclosure.

These comments supplement the comments prepared by individual members of the Committee on Administrative Practice and the Tax Shelters Tax Force of the Section of Taxation of the American Bar Association and submitted by letter dated January 26, 2005 ("January 26 Submission").

A. Major Recommendations in Regard to these Comments.

We commend the Service and Treasury for promptly issuing Notice 2004-80 and Notice 2005-17 and for clarifying that only a practitioner who makes a “tax statement” may be classified as a “material advisor,” as those terms are defined in Treasury Regulations ("Regulations") under section 6112.

Our primary recommendation is that further guidance clarify that an advisor cannot “become” a material advisor until the taxpayer with respect to whom or for whose benefit the advisor has made a tax statement enters into a transaction.

We recommend that classification as a “material advisor” be based only upon the amount of fees actually received or billed, not upon an advisor’s expectations regarding future receivables.

We recommend that further guidance provide that material advisor status is limited to persons who make tax statements that constitute “material” aid, assistance or advice; casual statements and de minimis tax services should be excluded.

We recommend that further guidance provide that, for purposes of sections 6707 and 6708, the reporting and list-maintenance obligations of material advisors are limited


2 In these comments, all references to sections shall be references to sections of the Internal Revenue Code unless otherwise indicated.

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to providing information that the material advisor knows, or reasonably should know, as of the relevant date.

In addition, we also respectfully suggest that the date for the initial filing of disclosures by material advisors should be delayed until further guidance is issued addressing the issues raised by these comments.

B. Other Recommendations.

We recommend that statements that relate to financial accounting treatment be limited to statements that are made by (a) a person who is professionally qualified to advise on matters of financial statement reporting (or who holds himself or herself out as so qualified), or (b) a person who has engaged such a qualified person to advise regarding the item being addressed.

We recommend that further guidance clarify that, until the Service and Treasury issue more specific guidance regarding the allocation of fees among multiple transactions for purposes of the minimum fee threshold requirement, advisors may use any reasonable method of allocation, consistently applied, without fear of being subjected to penalties under section 6707 or 6708.

In addition, we recommend that return preparers be allowed to rely in good faith upon Forms 1099, Schedules K-1 and Forms 8886 prepared by other preparers without being viewed as having made tax statements in regard to the transactions described in such forms, absent compelling facts to the contrary.

We suggest that the Service either issue a new form for the purpose of the required disclosure of reportable transactions under section 6111 or permit material advisors to file their section 6111 disclosures on a Form 8886 modified for such purpose.

To minimize the burden of complying with section 6111 while still ensuring that the Service receives the “early warning” contemplated by the section 6111 disclosure regime, we recommend that material advisors be permitted to make section 6111 disclosures on a quarterly basis.

We respectfully request that notices describing a transaction as a “listed transaction” should give greater attention to the “tax strategy” and “tax consequences” involved.

We respectfully suggest that low-income housing credits, as well as other transactions for which Congress has provided a similar social incentive credit, should be added to the “angel” list of transactions with contractual protection.

We respectfully suggest that a material advisor’s duty to disclose and to maintain lists should be limited to information that the advisor knows or reasonably should know. Guidelines should also be provided concerning the nature and extent of the inquiries that a practitioner must make in order to establish the reasonableness of the practitioner’s
expectations or in order to establish that a given fact was not information that the practitioner reasonably should have known.

II. Discussion of Major Recommendations.

A. Disclosure Requirements Should Apply Only to Completed Transactions.

In Notice 2005-17, the Service and Treasury indicated their intent to provide further guidance regarding the date on which a person becomes a material advisor with respect to a reportable transaction. As discussed in the January 26 Submission, the section 6111 disclosure obligations should apply only with respect to transactions that actually are entered into, as opposed to hypothetical or proposed transactions. This approach is consistent with Treas. Reg. § 301.6112-1(c)(2), which defines a material advisor as an advisor who makes a tax statement to, or for the benefit of, a taxpayer who the advisor at the time the transaction is entered into knows is or reasonably expects to be required to disclose the transaction under section 6011.

The policies underlying the recent amendments to section 6111 will be fully served by a disclosure requirement that is limited to transactions that are actually entered into by the taxpayer. These are the transactions of real interest to the Service. If disclosures are required for hypothetical or proposed transactions, the Service will receive some information earlier than otherwise, but that information will necessarily be incomplete and subject to change. Disclosures will be filed for many transactions that, ultimately, never take place or that change materially before being completed, and much of the information received by the Service will be of little use when examining completed transactions. By contrast, so long as disclosures are required to be filed within a relatively short period following implementation of a transaction, the Service will receive the necessary information long before the tax returns reflecting the results of that transaction are filed. Thus, an “early warning” can be provided without imposing unnecessary burdens on potential material advisors.

The integrated system of disclosures envisioned by Treasury when it proposed revisions to section 6111 as part of its tax shelter enforcement proposals released in March 2002, is best achieved if consistent rules are established for purposes of (i) disclosures by material advisors under section 6111, (ii) list maintenance by material advisors under section 6112, and (iii) tax return disclosures by participants in reportable transactions under section 6011. There should be no doubt that tax return disclosures by participants in reportable transactions are only required for transactions that actually have been entered into. Likewise, Treas. Reg. § 301-6112-1(e)(2)(i) requires material advisors to maintain an investor list containing the names of taxpayers who actually entered into reportable transactions. Therefore, it is appropriate to limit section 6111 disclosures to transactions that actually have been entered into.

As noted in the January 26 Submission, this approach will enhance the ability of the Office of Tax Shelter Analysis ("OTSA") to efficiently allocate its resources to focus on actual transactions that warrant its oversight. A regime that requires disclosures for
hypothetical or pending transactions will distract OTSA from its true mission. Many tax-advantaged transactions are ultimately never implemented, either because of changed business circumstances or for other reasons. Nonetheless, in the absence of clarification, many practitioners are likely to file protective disclosures on hypothetical or proposed transactions which, if subsequently implemented, in modified form, may not be reportable transactions.

B. “Tax Statements” Should Be Limited To “Material” Tax Advice; Casual Statements and De Minimis Tax Services Should Be Excluded.


Section 6111(b)(1) defines a “material advisor” as any person who provides “material aid, assistance, or advice” with respect to “organizing, managing, promoting, selling, implementing, insuring, or carrying out” a reportable transaction.\(^3\) However, for the purposes of interim guidance, Notice 2004-80 imports into the statute the definition of a “material advisor” set forth in Treas. Reg. § 301.6112-1(c)(2). The Notice thereby clarifies that the “material aid, assistance, or advice” that warrants classification as a material advisor must include making a tax statement to or for the benefit of a taxpayer or other person described in Treas. Reg. § 301.6112-1(c)(2)(i)(A) through (E).

We believe this refinement of the statutory definition is authorized by the Secretary’s authority under section 6111(c)(2) and is consistent with the new statutory definition of a “disqualified advisor” under amended section 6664(d)(3)(B)(ii). We also believe that, properly applied, this refinement of the statutory definition can advance the purposes of section 6111 and 6112 without imposing unnecessary burdens or expense upon advisors or their clients. However, in this respect, we have one major concern.

For the purposes of Notice 2004-80, a “tax statement” generally means any statement, oral or written, that “relates to a tax aspect of a transaction that causes that transaction to be a reportable transaction.”\(^4\) The regulation further limits the meaning of a “tax statement” with reference to the different categories of reportable transactions. Nevertheless, there is still considerable uncertainty as to the manner in which the definition should be applied. This is largely because, by its terms, the definition of a tax statement employed by Notice 2004-80 extends to casual remarks that are not intended to be substantive advice or upon which, under the circumstances, no one would reasonably rely.

According to Treas. Reg. § 301.6112-1(c)(2)(iii), what causes a transaction to be a reportable transaction is a “tax aspect.” Any affirmative statement, oral or written, that “relates” to such a tax aspect is a “tax statement.” Thus, in the case of a listed

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\(^3\) The definition of a “material advisor” under section 6111 also defines the term “material advisor” for the purposes of section 6112 and section 6664(d)(3)(B)(ii)(I).

\(^4\) Treas. Reg. § 301.6112-1(c)(3)(iii).
transaction, for example, a person may inadvertently make a tax statement simply by commenting in some way about an aspect of the transaction that qualifies it as a listed transaction. Indeed, even telling a client that the advisor will not give a tax opinion regarding such an aspect of the transaction is arguably a tax statement under a literal interpretation of the regulatory definition.

We believe that such a broad interpretation of the term “tax statement” would be inconsistent with Congress’s intent to limit the reporting and list-maintenance regime established by sections 6111 and 6112 to only those advisors who provide material aid, assistance or advice in connection with a reportable transaction. Unless a tax statement is made under circumstances suggesting that it was intended or understood to be substantive advice, its materiality is highly suspect.

Our concern regarding casual, non-substantive tax statements is magnified because of the practical difficulty that they present for firms that are attempting to determine in good faith whether they are subject to classification as a material advisor. A firm can determine without great difficulty whether the fees earned for all services with respect to a transaction exceed the minimum fee threshold. In such a case, it is also a relatively simple matter to survey the tax professionals associated with the firm regarding the extent of the tax service that they provided. However, in many cases, outside tax advisors provide such services, and no firm tax lawyer is involved. Nevertheless, even a casual statement by a business, securities or other non-tax lawyer involved in the transaction may constitute a tax statement under Notice 2004-80, thereby classifying the firm as a material advisor. For larger firms, surveying every transaction that generated more than the minimum fee, even if no tax lawyer was involved, to determine whether any other attorney may have made an off-hand statement or remark constituting a “tax statement” is a daunting task.

Thus, we recommend the issuance of further guidance providing that statements that are not intended to constitute substantive advice upon which the recipient may rely (a subjective test) or that, under the circumstances, no person reasonably would consider to be substantive advice (an objective test) should not be classified as “tax statements” even if their content arguably relates to some tax aspect of a transaction that makes it a reportable transaction. Such factors as whether the firm had charged the taxpayer for providing tax services, whether the taxpayer had engaged a different professional or firm for tax services relating to the transaction, and whether the individual who made the tax statement held himself out as possessing tax expertise might be relevant to this inquiry.

A further rationale for this recommendation is found in Treas. Reg. § 301.6112-2(c)(iv)(A). This regulation excludes from the definition of a “tax statement” any statement regarding a transaction that is made after the first tax return reflecting the benefits of the transaction is filed with the Service. This provision demonstrates that the legitimate interests of the Service do not require the regulation of all “tax statements.” This same principle can be usefully applied to other situations in which the benefits of regulation are outweighed by the burdens involved.
For example, situations commonly arise in which an attorney transmits to a client a tax statement that was made to the attorney by another of the client’s advisors. Non-tax attorneys frequently pass on to their clients tax analyses or recommendations that were previously communicated to the attorney by the client’s tax advisor or accountant. To the extent the attorney serves as a mere conduit for a tax statement made by another, the statement of the attorney—as opposed to the statements of the tax advisor or accountant—should not be considered to be a “tax statement” for purpose of section 6111(a).

Similarly, it is common and expected for business people and non-tax advisors to include in their discussions of a transaction their understanding of the applicable tax consequences. Such discussions may occur in the course of negotiating a contract or during consultations between the client and firm representatives regarding the terms of a potential engagement. In such cases, neither the clients nor the non-tax advisors consider the discussions to be authoritative or intended to serve as substantive advice. Rather, the expectation is that tax advisors (either internal or external) will be consulted for that purpose. A client who retains a large accounting firm, for example, for tax advice and services is unlikely to rely on statements about tax consequences by a corporate lawyer from a firm that was not engaged to provide such services.

As these examples illustrate, not all statements concerning the tax aspects of a transaction that make it a reportable transaction rise to the level of materiality that warrants classification as a “tax statement.” The exception granted in the regulations for post-filing advice confirms the validity of this observation. We, therefore, recommend that statements that are not intended by the speaker to constitute substantive advice upon which the recipient should rely or that, under the circumstances, no person would reasonably consider to be substantive advice should be excluded from the definition of a “tax statement.”

2. **De Minimis Tax Services Should Also Be Excluded.**

The magnitude of the penalties potentially applicable to material advisors under section 6707 and 6708 further suggests that even some tax statements that are intended to be substantive advice are, nevertheless, too trivial or insignificant to merit application of the reporting and list-maintenance regime or its attendant penalties. That section 6111(a) only applies to practitioners who provide “material” aid, assistance, or advice with respect to a transaction implies that, in some circumstances, only “immaterial” advice or assistance may occur.

To be sure, classification as a “material advisor” presupposes receipt of more than the minimum fee. However, the minimum fee requirement is based upon gross fees earned by the firm for all services and does not distinguish between fees attributable to

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5 Such an interpretation is consistent with the deletion of the phrase “or provides” in reference to a tax statement from the definition of material advisor in Treas. Reg. § 301.6112-1(c)(2)(i) in March of 2003.
tax services and other fees. Consequently, a firm may be classified as a material advisor even if only an insignificant portion of its services related to taxes. Imposing penalties (including strict liability penalties) for very minor amounts of tax advice seems excessive, given the magnitude of the penalties involved.

Besides being limited in magnitude, tax services in connection with a transaction may also be limited in scope. Tax practitioners are often called upon to answer questions relating to narrow issues without a significant relationship to the transaction as a whole. Triggering application of the reporting and list-maintenance regime established under Notice 2004-80 in such cases serves no genuine purpose. However, under the Notice, so long as such a targeted response is deemed to “relate” to a tax aspect of the transaction that makes it a reportable transaction, compliance with section 6111 and 6112, as interpreted by the Notice, is required.

We, therefore, recommend the issuance of further guidance excluding from material advisor status those persons who provide only \textit{de minimis} tax services. Such a limitation is well within the Secretary’s authority pursuant to section 6111(c)(2). Under this proposal, whether tax services are \textit{de minimis} will depend upon the magnitude of such services and their materiality. Tax services would be \textit{de minimis} in magnitude if the fees charged for tax services represented less than five percent of total fees charged.\footnote{Treas. Reg. § 301.6112-1(c)(3)(iii).} The materiality of the tax services provided would require a qualitative judgment based upon the extent to which the tax services in question facilitated those features of the transaction that made it a reportable transaction. Advising on how the NOL carry-back rules would apply to a section 165 loss might be \textit{de minimis}; designing the strategy to generate the section 165 loss likely would not. Similarly, tax services that are limited to advising a client that a transaction is a reportable transaction and assisting the client to comply with the disclosure requirements of section 6011 should also be classified as \textit{de minimis}.

\textbf{C. Material Advisors Should Only Be Subject To Penalties Based On What They Know Or Reasonably Should Know.}

Treas. Reg. § 301.6112-1(b)(2) and (c)(2) provide that classification as a material adviser is based, in part, upon what the person knows to be true as of a specific date or what the person reasonably expects, as of that date, will be true in the future. By limiting this requirement to only those expectations that are “reasonable”, the Regulation appears to establish parameters that are manageable in the event of a future inquiry.

By contrast, the obligations of a material advisor to provide information in connection with the section 6111 reporting requirement or to produce an investor list upon written request pursuant to section 6112 appear to be absolute in scope. In effect, these obligations impose a strict liability for the failure to disclose information that may

\footnote{See section 954(b)(3).}
be unknown despite reasonable efforts to ascertain all relevant facts. For listed transactions, this strict liability obligation to disclose can trigger a non-waivable penalty of $200,000 with respect to a matter for which the advisor’s fees barely exceeded $10,000.

We recommend that Treasury and the Service should issue further guidance providing that, for purposes of section 6707 and 6708, the reporting and list-maintenance obligations of a material advisor are limited to the information that the material advisor actually knows or reasonable should know as of the relevant date. Such guidance should also indicate that, if the material advisor has provided any written advice subject to characterization as a “covered opinion” under section 10.35 of Circular 230, the determination of what information the material advisor reasonably should know will take into account the mandatory requirements of that section.

We also recommend that Treasury and the Service should establish “safe harbor” guidelines, identifying the nature and extent of the inquiries that a practitioner is required to make in order to establish the reasonableness of the practitioner’s expectations for purposes of Treas. Reg. § 301.6112-1(c)(2)(i) or in order to demonstrate that a given fact was not information that the practitioner reasonably should have known.

III. Other Recommendations.

A. Transactions with a Significant Book-Tax Difference.

We applaud Treasury and the Service for providing in Notice 2004-80 that, in order to be a section 6111 material advisor with respect to transactions with a significant book-tax difference, the advisor must make a statement that relates to the financial accounting treatment of the item(s) that gives rise to the significant book-tax difference. The use of the word “statement” as the standard for this limitation on classification as a material advisor, however, raises the same issue in connection with financial accounting treatment as it raises in regard to the tax aspects of a transaction. The word “statement” appears to include references to the subject in casual conversations by persons who do not intend their remarks to be authoritative or to be relied upon by a taxpayer.

The exception granted in the Regulations for post-filing advice\(^8\) suggests that Treasury and the Service view their interests as adequately protected without mandating the disclosure of statements that will not be relied upon in the preparation of a return. Similarly, the interests of Treasury and the Service can be adequately protected without requiring the disclosure of statements relating to financial accounting treatment that will not be relied upon as substantive accounting advice. Consistent with our recommendation regarding tax statements, we recommend that only financial accounting statements that are intended to be relied upon as substantive accounting advice should constitute statements that relate to the financial accounting treatment of an item for the purposes of classifying a person as a section 6111 material advisor.

\(^8\) Treas. Reg. § 301.6112-1(c)(iv)(A).

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More specifically, we recommend that statements that relate to financial accounting treatment should be defined to include only statements that are made by (a) a person who is professionally qualified to advise on matters of financial statement reporting (or who holds himself or herself out as so qualified) or (b) a person who has engaged such a qualified person to advise regarding the item being addressed.

B. Allocation of Fees Among Multiple Transactions.

We note that the section 6112 minimum fee threshold is applied separately for each transaction (i.e., aggregation of fees among transactions is not required). For the purposes of determining the material advisor minimum fee thresholds, however, the Regulations provide no guidance on how to allocate fees received for more than one transaction. The absence of such guidance under Treas. Reg. § 301.6112-1 raises more questions because Treas. Reg. § 301.6111-2(d) explicitly acknowledges the issue.

In light of these ambiguities, we recommend that, until the Service and Treasury issue more specific guidance regarding the allocation of fees among multiple transactions for purposes of the minimum fee threshold requirement, advisors be permitted to use any reasonable method of allocation, consistently applied, without fear of being subjected to penalties under section 6707 or 6708.

C. Reasonable Reliance on Other Practitioners.

The elasticity of the word “statement” as a part of the definition of a material advisor also requires clarification in the context of preparing returns or issuing tax information statements (such as Schedules K-1 or Forms 1099). Of course, preparing the return of an entity that participates directly in a reportable transaction and issuing Schedules K-1 or Forms 1099 to investors in respect of such entity would clearly be a “tax statement.” However, this truism begs the question: Is a return preparer who merely copies into a taxpayer’s tax return the information obtained from such Schedules K-1 or Forms 1099 also making a tax statement?

Treas. Reg. § 1.6694-2(d)(5) provides that, for the purposes of the section 6694 return preparer penalty, return preparers may rely in good faith on advice or schedules prepared by another preparer unless (i) the advice is unreasonable on its face, (ii) the preparer knew or should have known that the other preparer was not aware of all relevant facts, or (iii) the preparer knew or should have known that the advice was no longer reliable. Treas. Dec. 8392 indicates that the term “advice or schedules” is intended to include Forms K-1 prepared by another preparer.

Consistent with Treas. Reg. § 1.6694-2(d)(5), we recommend the issuance of further guidance clarifying that, absent compelling facts to the contrary, “tax statements” do not include the reporting of information on tax or information returns that the preparer

9 Treas. Reg. § 301.6112-1(c)(3)(iii).
has obtained from documents, such as Schedule K-1, Form 1099 or Form 8886, that have been prepared by another preparer upon whom the reporting preparer has relied in good faith. We also believe that the delineation of such compelling facts should take into account both the underlying purposes of sections 6111 and 6112 and the magnitude of the penalties mandated by sections 6707 and 6708.

D. Section 6111 Disclosures Should Be Made on a New Form.

We recognize that the provisions of Notice 2004-80 relating to the use of current Form 8264 to fulfill the disclosures requirements of section 6111 is merely a stopgap measure to enable advisors to comply with the statutory requirement. However, the use of the old Form 8264 (with the modifications indicted in Notice 2004-80) raises several issues or questions because of the change in focus of section 6111. To simplify the process by which material advisors disclose transactions to the Service under section 6111, and to ensure that the Service receives the information it needs, we suggest that the Service either design a new form for this purpose or permit material advisors to file their section 6111 disclosures on a Form 8886 modified for this purpose.

The Form 8264 was designed for the now repealed registration regime, which generally applied to transactions marketed to multiple investors, such as the master limited partnerships that prevailed in the early 1980s. Accordingly, the Form 8264 is designed for the disclosure of a particular tax shelter entity and the calculation of the “tax shelter ratio” under the prior version of section 6111(c). By contrast, the Form 8886, which is the form on which participants in a reportable transaction disclose such participation under section 6011, was designed with reference to the current concept of reportable transactions. As such, the Form 8886 permits ready identification of a transaction into one of the six categories of reportable transactions and calls for a description of the facts and expected tax benefits of the transaction.

With the following proposed modifications, the existing Form 8886 can be used for purposes of Section 6111 disclosures by material advisors. First, the material advisor would disclose its own name, address, and identifying information at the top of the form, but would not disclose any identifying information relating to participants in the transaction being disclosed. Second, the material advisor would be instructed to omit items 5 and 6, as those items are relevant only to participants in a reportable transaction. Third, the material advisor would be required to disclose the fees received (or expected to be received) as part of the description of facts in item 7. However, the material advisor would be instructed to not disclose identifying information relating to any participants in the transaction as part of its description of facts in item 7.

Even if the Service and Treasury choose to continue use of the Form 8264 on a stopgap basis, we believe that Notice 2004-80 should be clarified to confirm that a material advisor is not required to disclose identifying information relating to participants in reportable transactions when making a section 6111 disclosure. As we understand the current statutory framework, section 6111 is intended to provide advance notice to the Service of the types of reportable transactions with respect to which material advisors are providing material aid, assistance or advice. If the Service requires more information

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regarding specific transactions that have been disclosed under section 6111, it is authorized to obtain an investor list from the material advisor under section 6112. If that information were required as part of the section 6111 disclosure, then the investor list requirement would have no real purpose.

E. Permit Section 6111 Disclosures To Be Made on a Periodic Basis.

Notice 2004-80 requires a material advisor to file a section 6111 disclosure within 30 days of becoming a material advisor with respect to a particular reportable transaction. As discussed in the January 26 Submission, this rule effectively creates numerous filing deadlines throughout the course of any particular year. To minimize the burden of complying with section 6111 while still ensuring that the Service receives the “early warning” contemplated by the section 6111 disclosure regime, we recommend that Notice 2004-80 should be revised to permit material advisors to make section 6111 disclosures on a periodic basis. For example, a quarterly reporting system would require section 6111 disclosures to be filed before May 1, August 1, November 1, and February 1, in each case with respect to transactions completed during the immediately preceding calendar quarter.

Such a reporting system would provide clear, workable deadlines. Practitioners who are required to file disclosures under section 6111 would be able to discharge their obligations on a regular, quarter-by-quarter basis, instead of confronting multiple, transaction-specific deadlines. One can easily envision professional firms establishing procedures for quarterly reviews by their members in order to ensure compliance with these rules. Furthermore, quarterly filings will advance the purposes of section 6111 by providing the Service with timely information shortly after the transactions are implemented.

A quarterly filing requirement will also provide a useful flow of information to OTSA. For example, filings made each quarter could be analyzed to identify and evaluate emerging trends and the proliferation of new types of transactions. We would expect that this type of information will enhance the ability of OTSA to promptly target and respond to potentially abusive tax shelters.

F. Identification of Listed Transactions.

A listed transaction is a transaction that is the same as or substantially similar to one of the types of transactions that the Service has determined to be a tax avoidance transaction and has identified the transaction by notice, regulation, or other form of published guidance as a listed transaction.\(^\text{10}\) At present, approximately thirty types of transactions have been identified as listed transactions.\(^\text{11}\)

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\(^{10}\) Treas. Reg. § 1.6011-4(b)(2).

Because of their perceived potential for abuse, listed transactions are generally treated more harshly than other categories of reportable transactions. For example, if a taxpayer fails to disclose its participation in a listed transaction in accordance with section 6011, the taxpayer will be subject to greater penalties than in the case of other reportable transactions; the statute of limitations will not commence to run until the taxpayer is in compliance with its reporting obligations; and any penalties imposed upon the taxpayer pursuant to section 6707A will not be subject to rescission.

Because of these severe consequences, taxpayers and their advisors have a substantial interest in the manner in which the Service describes transactions that it decides to classify as listed transactions and in the nature of the inquiry by which other transactions are determined to be the same as or substantially similar to a listed transaction. Unfortunately, some of the notices or other forms of public guidance by which the Service has identified listed transactions do not provide sufficiently extensive guidance for the purpose of determining whether other transactions are “substantially similar.”

Such notices or other public guidance generally describe the factual background and pertinent arrangements in substantial detail. They also describe the reasons why the Service believes the described transaction should not receive the purported tax treatment. However, in these respects, a number of the notices or other published guidance are not responsive to the regulatory standards that govern the “same as or substantially similar” inquiry. These regulatory standards are set forth in Treas. Reg. § 1.6014-4(c)(4) and in Treas. Reg. § 301.6112-1(d)(2). However, while these regulations use the same terms to describe the applicable standards, the terms that each regulation employs are undefined. Both Treas. Reg. § 1.6011-4(c)(4) and Treas. Reg. § 301.6112-1(d)(2) provide that a transaction will be “substantially similar” to a listed transaction if it is expected to obtain “the same or similar type of tax consequences” and if it is either factually similar to the listed transaction or “based on the same or similar tax strategy.” In other words, even factually dissimilar transactions may be “substantially similar” if they each purport to achieve a “similar type of tax consequences” and if they are each based upon a “similar tax strategy.” Neither “tax consequence” nor “tax strategy” is defined in these regulations. Furthermore, although the prior notices identifying listed transactions describe their factual elements in some detail, they often do not explicate the “tax consequences” or the “tax strategy” to the same degree.

For example, a common M&A technique is to buy a company, which then sells off its assets because the assets of the company are worth more separately than as parts of a combined enterprise. This technique is so common that it was described at length in the

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12 I.R.C. § 6707(b)(2).
13 I.R.C. § 6501(c)(10).
movie, “Pretty Woman.” However, the Service has identified as a listed transaction an analogous arrangement involving the use of an “intermediary” with favorable tax characteristics to sell the assets of the target to the prospective buyer. Notice 2001-16 describes the abusive arrangement in some detail, but fails to provide clear guidance to distinguish a “good” split-up acquisition from the “bad” listed transaction. In both cases, the acquiring company causes the target to sell off its assets of the target and to report the gains and losses accordingly. In both cases, the tax consequences are similar, as is the strategy of acquiring the target and selling its assets. What would apparently distinguish a legitimate split-up acquisition from an abusive transaction is the absence of a pre-arrangement between buyer and seller and the intermediary, but, by its terms, Notice 2001-16 includes no such distinction. Furthermore, as noted, the absence of such a pre-arrangement would be a factual difference, but would not necessarily alter the type of tax consequences to the parties or involve a different tax strategy, as that term is commonly defined. In other words, notices that rely primarily upon fact-based criteria for distinguishing between transactions that are, or are not, “substantially similar” to a listed transaction, are of limited utility.

In light of the substantial penalties for non-compliance by taxpayers and material advisors with their respective disclosure, reporting and list-maintenance obligations, we recommend that future notices or other guidance identifying new listed transactions should include more extensive discussions of the “tax consequences” and “tax strategy” of the new listed transaction in order to facilitate the determination of whether a factually dissimilar transaction should be classified as “substantially similar” to the new listed transaction. We also request that the Service consider reviewing existing notices or other published guidance with respect to transactions currently classified as listed transactions in order to determine whether supplemental guidance, directed towards clarifying the nature and extent of the “tax consequences” and the “tax strategy” involved, might be appropriate.

IV. Comments on the “Angel” Lists.


We applaud the Service and Treasury for providing explicit exceptions to transactions with contractual protection in Notice 2004-65. We recognize that the transactions included on the list of exceptions are transactions which Congress has indicated that it wishes to encourage by providing tax as well as other economic incentives for taxpayers to undertake the transaction. There are other transactions, however, that are associated with equally strong expressions of Congressional support. For example, low-income housing credit transactions are often uneconomic without taking into consideration the credits available under section 42. The Treasury has explicitly acknowledged this in Treas. Reg. § 1.42-4(a).
return of all fees, including fees related to tax advice, if the sponsor fails to maintain qualification for the credits. We respectfully suggest that low-income housing credits, as well as other transactions for which Congress has provided a similar social incentive credit, be added to the “angel” list of transactions with contractual protection.


A repeated theme of these comments is that practitioners should be held responsible only for information that they actually know or reasonably should know, particularly with respect to their reporting obligations under section 6111. For this reason, we have requested the issuance of regulations or other interim guidance regarding the nature and extent of the inquiries in which an advisor must engaged in order to avoid the classification of unknown information as information that the advisor should have known.

In the case of loss transactions, the need for such guidance is particularly acute because, under Treas. Reg. § 1.6011-4(b)(5)(iii)(A), the magnitude of a section 165 loss is determined without taking into account offsetting gains. However, in many situations involving a sale of multiple assets that yields an over-all gain, the advisor may not know or have reason to know of the existence or amount of any gross loss embedded in the net gain or whether the underlying assets have qualifying bases for purposes of Rev. Proc. 2004-66. For example, if a practitioner provides tax advice concerning a taxpayer’s sale of 2,000 assets for $200,000,000 total with $40,000,000 of net gain, but including a gross loss of more than $10,000,000 derived from a small portion of the total assets sold, each with an individual loss well below the $10,000,000 threshold, the transaction would appear to be a reportable transaction. Consequently, if the applicable minimum fee threshold is satisfied, the advisor would be a section 6112 material advisor subject to reporting and list-maintenance obligations under sections 6111 and 6112 and Notice 2004-80.

Consistent with our other recommendations, we respectfully suggest that an advisor’s duty to disclose and to maintain lists should be limited to information that the advisor knows or reasonably should know. Similarly, to the extent that an advisor’s duty to disclose is based upon the reasonable expectation of the advisor that the transaction will be a reportable transaction in the future, we request the issuance of temporary regulations or other guidance that addresses the nature and extent of the inquiries that an advisor must undertake in order to make the advisor’s expectations “reasonable.”