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NEWSQUARTERLY

OPINION POINT

The Ethereal Angel List

By Thomas Greenaway*

In March 2010, Congress codified the economic substance doctrine by adding section 7701(o) to the Code. Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152, § 1409, 124 Stat. 1029, 1067. To pass muster, a transaction now must meaningfully change the taxpayer's economic position, and the taxpayer must have a substantial non-federal income tax purpose for the transaction. I.R.C. § 7701(o)(1). This newly-codified standard only applies to business transactions and activities engaged in for the production of income, and only if the economic substance doctrine is "relevant." The relevance determination is to be made as if Congress had not codified economic substance. I.R.C. § 7701(o)(5)(C). Congress also added new strict-liability penalties to the Code for transactions that lack economic substance. I.R.C. § 6662(b)(6).

The Staff of the Joint Committee on Taxation suggested that certain classes of transactions should not be subject to the economic substance doctrine. Staff of the Joint Committee on Taxation, *Technical Explanation of the Revenue Provisions of the "Reconciliation Act of 2010," as Amended, in Combination with the "Patient Protection and Affordable Care Act,"* JCX-18-10 (Mar. 21, 2010), http://www.jct.gov/publications.html?func=startdown&id=3673. The Joint Committee report (and the Senate Finance and House Budget Committee reports that preceded it) gave rise to the notion of an "Angel List."

Picking up on the legislative history, many taxpayers and practitioners want the Service and Treasury to issue an Angel List of transactions that will not be touched by the newly-codified economic substance doctrine and its strict liability penalties. This is not likely to happen.

For one thing, the Angel List would be very long, and even then, it would be incomplete. Second, the Service and Treasury have no incentive to publish a long list of acceptable tax-advantaged transactions. Third, in creating an Angel List, the Service and Treasury would have to wrestle with the tough questions left unanswered by the codified economic substance doctrine without the benefit of the real facts of real cases.

With Angels & Archangels

In the middle ages, St. Thomas Aquinas concluded that even though angels are immaterial substances, they must "exist in exceeding great number." *Summa Theologica,* First Part, Question 50, Article III. The same is true for acceptable tax-advantaged transactions. Several classes of tax-advantaged transactions should not be touched by the economic substance doctrine. First, and most obviously, tax credits, accelerated depreciation provisions, and lots of other Code sections deliberately encourage taxpayers to enter into transactions they otherwise would avoid. Other provisions have the same effect, even without the clear evidence of Congressional

* KPMG LLP, Boston, MA. The views and opinions are those of the author and do not necessarily represent the views of KPMG LLP. KPMG LLP does not provide legal services.

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Section Meeting Calendar

www.abanet.org/tax/calendar

ABA Tax Section meetings are a great way to get connected, get educated, and get the most from your membership! Join us for high-level CLE programming and the latest news and updates from Capitol Hill, IRS, Treasury, and other federal agencies.

September 23-25, 2010	JOINT FALL CLE MEETING	Sheraton – Toronto, ON
January 20-22, 2011	MIDYEAR MEETING	Boca Raton Resort & Club – Boca Raton, FL
May 5-7, 2011	MAY MEETING	Grand Hyatt – Washington, DC
October 20-22, 2011	JOINT FALL CLE MEETING	Hyatt Regency at Colorado Convention Center – Denver, CO
February 16-18, 2012	MIDYEAR MEETING	Manchester Grand Hyatt – San Diego, CA
May 10-12, 2012	MAY MEETING	Grand Hyatt – Washington, DC
September 13-15, 2012	JOINT FALL CLE MEETING	Westin Boston Waterfront – Boston, MA

If You Missed the Last Section Meeting

MATERIALS

As a benefit of membership, Tax Section members can view and search hundreds of papers and materials presented at the Section's Fall, Midyear, and May Meetings dating back to 1999 at: http://www.abanet.org/tax/taxiq. This service is made possible through Thomson Reuters Tax & Accounting and West, a Thomson Reuters business—a primary sponsor of the Section of Taxation.

RECORDINGS

CDs and MP3s of programs from recent Section Meetings are available from Digital Conference Providers (DCP), the Section's audio service provider. Orders can be placed through the DCP website at https://www.dcporder.com/abatx/ or by calling 630/963-8311.

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Stuart M. Lewis*

The Tax Section is a truly impressive operation. Over the last year I have come to an even greater appreciation of how well the Section functions. While many aspects of the Section's work have been impressive, the three that most caught my attention have been (1) the dedication and excellent work produced by Tax Section members and committees, (2) the impact that the Section's comments have on Congress, Treasury, and the Service, and (3) how well the Section is run.

The work of the Section all starts and largely rests with our committees and their members. The work of our committees is often outstanding and certainly impressive in the depth and breadth of its expertise. The Section's committees and their members are responsible for developing the regulatory and legislative comments that the Section submits to federal agencies and Congress, which is our most visible contribution to the tax system. The committees also are largely responsible for the success of our Section Meetings and other CLE programs. Most of the CLE, products, and services that the Section develops percolate up through the many networking and scholarship channels fostered by our committees. The committee chairs deserve our applause for orchestrating these activities and leading the Section members whose expertise and commitment make it work.

An integral part of the Section's mission, in which the members again play a critical role, is our effort to provide pro bono representation. I previously wrote about this in an earlier column. The Section has made major financial and moral commitments to this effort. Our Public Service Fellowships and other pro bono activities are some of the Section's most worthwhile endeavors.

The Section has continued its long tradition of providing detailed technical comments to the government on legislation, regulations, and other guidance. What impressed me most over the last year was the influence of these comments on the guidance or legislation in question. (A number of times we received requests from the government indicating that they were anxious to receive our input.) This is due to a number of factors, including the obvious expertise of the members, but it is also due to our rigorous (some would say bureaucratic) procedures of ensuring that our comments are only of the highest quality and objectivity while showing an appreciation of the role of the regulator as well as that of the private sector.

Over my many years of involvement with the Section, I have always thought it was well run, but I did not fully appreciate how well until the last year. Organizing meetings, dealing with the ABA and other groups, and providing services to our many members is a major task. We, as volunteers, are freed from most of these matters, allowing us to concentrate on what we can do best. We all know the fantastic work of Christine Brunswick, who is responsible for much of the Section's success. Key members of her staff are also vital to our activities, such as Anne Nicholas, Anne Dunn, Karen Dorbin, Yolanda Lee, and Janet In. They and the rest of the Tax Section staff deserve our appreciation as well.

A special thank you is due to Paul Sax who is retiring from his position as one of our Section representatives to the ABA House of Delegates. As many of you know, the Section's relationship with the ABA can be, shall we say, "interesting" and ends up taking up a lot of the chair's (as well as the other officers') time and attention. Many of the matters of interest to the ABA do not affect the Tax Section, but some do, and some potentially have great impact. Eternal vigilance is required. Our Section delegates devote a great deal of time to diplomatically dealing with these issues on our behalf. Paul has been doing this for many years with unsurpassed skill and acumen, and the Section will greatly miss his talents. Thank you, Paul, for your dedicated service. I also thank Dick Lipton who will be continuing in this role and Susan Serota who will be succeeding Paul in carrying on the Section's excellent representation.

As I leave office, I extend my thanks to the officers who have so diligently carried out their responsibilities during my term: Fred Witt (Vice-Chair, Administration) for helping us maintain our financial strength, Helen Hubbard (Vice-Chair, Government Relations) for her many contributions, not least of which is keeping us in good standing with government officials, Ellen Aprill (Vice-Chair, Communications) for maintaining and fostering our strong press relations, Peter Connors (Vice-Chair, Committee Operations) for the very difficult task of keeping our 40 (or so) committees running smoothly, Emily Parker (Vice-Chair, Professional Services) for her invaluable help in maintaining and expanding our strong CLE programs, and Doug Mancino (Vice-Chair, Publications) for his service in enhancing our quality publications. Our Secretary, Brian Trauman, and Assistant Secretary, Bahar Schippel, have also provided excellent service, and I greatly appreciate their efforts.

I want to especially thank Charlie Egerton, our Chair-Elect and soon to be Chair, for his special help over the last year. Charlie has done all and more that could be asked of a Chair-Elect. It is nice to know that the Section will carry on in such good hands. ■

* Buchanan Ingersoll & Rooney PC, Washington, DC.

Charles H. Egerton*

Experience has taught me that before charting a course for the coming year, it is important to reflect on the year that has passed. The Section has been very fortunate during the past year to have had the leadership of our outgoing Chair, Stuart Lewis. It has been my privilege as Chair-Elect to work with Stuart on an almost daily basis. Stuart established clear and concise goals at the beginning of his year and followed through on each and every one of them in a very organized fashion. He was always available when needed, and he provided level-headed and insightful guidance to all who requested it. He also never shied away from dealing with difficult issues. Stuart has set the bar very high, and I can only hope to emulate his example in the year ahead.

Health of the Section

I am pleased to report that the Section has emerged in excellent shape from a year that is best remembered as the worst economic recession in recent memory. Our membership has held steady and, although attendance at our early Section meetings was down slightly, attendance at the Washington meeting in May was up from last year and we had 150 first-time attendees. Our members are our "customers" and we intend to focus in the coming year on expanding our membership base through marketing, enhanced and improved communications, and by continuing to provide the best tax CLE that is available anywhere at a very reasonable price.

Although we have experienced some reductions in our sponsorship revenue due to the recession, our financial picture remains sound. Under the able direction of Fred Witt, our Vice-Chair of Administration, and Emily Parker, our Vice-Chair of Professional Services, we expect our revenues from CLE activities to increase in the coming year by providing more quality CLE programs. We will also renew our efforts to generate more sponsorship revenue in order to reduce the cost to our members of attending Section Meetings and CLE programs. Doug Mancino, our Vice-Chair of Publications, also has a number of innovative plans to expand the publications that the Section will offer in the coming year.

Priorities for the Coming Year

One of our goals for the coming year is to find new ways for the Section to have a meaningful voice in the tax legislative process. Our objective is to continue to promote the need for tax simplification and at the same time to provide both technical and policy input on new tax provisions that Congress may consider. This will not be an easy task. For the most part, the days of vetting tax proposals at Congressional hearings and providing reasonable opportunities for input from organizations such as the Section are largely gone. The pay-go policies currently employed by Congress may be justified, if not necessary, on a macroeconomic level, but they also yield an unfortunate by-product. In today's world tax legislation frequently takes the form of off-the-shelf revenue raisers, usually labeled as "loophole closers," that are employed by Congress to offset the cost of funding benefits or projects that Congress determines should be provided. There is often very little opportunity for input on these tax proposals. More often than not, little or no thought is given to the fact that this process also leads to increased complexity which threatens to undermine the entire framework of our self-assessment system.

How then can the Section hope to have an impact on the tax legislative process under the current system? This will be the focus of a discussion that will take place at a leadership retreat to be attended by the Section's officers, Council members, and staff together with representatives of the Section's Government Relations Committee this summer. We are hopeful that, through interaction with the staff of the House Ways and Means Committee, the Senate Finance Committee, and the Joint Committee on Taxation, and with input from members of our Government Relations Committee, many of whom are involved in various facets of the tax legislative process, we will be able to identify tax proposals at an early stage. It is our hope that the Section will then be able to provide meaningful input with respect to these proposals as they evolve.

The Section has done an outstanding job for a number of years in providing quality and timely technical comments to the Treasury and the Service. It is apparent from our courtesy call meetings with representatives of both the Service and Treasury that the Section's comments have been appreciated by them and have had an impact on final regulations and other administrative guidance that has ultimately been issued. These comments are the result of the outstanding work of the volunteers from our substantive committees with the assistance of the Council directors, COGs reviewers, and Helen Hubbard, our Vice-Chair of Government Relations, all of whom review and approve these comments. We recognize that we are an "all volunteer army" of tax professionals, and we sincerely appreciate the energy and effort of our committee officers and members who have devoted so much of

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their time to produce these comments. Our new Vice-Chair of Committee Operations, Kathy Keneally, together with our Council directors who work hand in hand with the committees, will be working hard with our committee officers to both identify appropriate regulatory and administrative proposals worthy of comment and to encourage the continued flow of quality comments.

We will also emphasize the importance in the coming year of attracting more young tax lawyers, including adding to the diversity of those who participate in Section and committee activities as well as CLE presentations. We will also continue to emphasize the pro bono activities of the Section, including our VITA and military-VITA activities as well as continuing to promote our public service fellowships. John Barrie, our new Vice-Chair of Communications, will also insure that we maintain our public face and continue our many public service announcements on timely tax topics.

The ultimate goal all of us have is for the Section to have a positive impact on the tax system. I look forward to working with each and every one of you in the coming year to make this happen. I, along with all of the other officers and Council members, welcome your comments and suggestions throughout the year. I look forward to seeing as many of you as possible at our Joint Fall Meeting with RPTE in Toronto. ■

Mark Your Calendar

Joint Fall CLE Meeting

September 23-25, 2010

Toronto, Ontario

Join the **Tax Section** and the **Trust & Estate Division of the Real Property, Trust & Estate Law Section** for the 2010 Joint Fall CLE Meeting, September 23-25, at the Sheraton Centre Toronto Hotel, Toronto, Ontario. You'll have the opportunity to attend a wide range of CLE programs, network with colleagues, and participate in high-level discussions with private practitioners and government officials on the most important issues facing tax lawyers today.

http://meetings.abanet.org/meeting/tax/fall10/

Douglas H. Shulman, *Commissioner, Internal Revenue Service* will be the Keynote Speaker at the Plenary Breakfast, Friday, September 24, 7:15 a.m.

INTERVIEW

William J. Wilkins

By Jasper L. Cummings, Jr. and Alan J.J. Swirski*

President Obama appointed Bill Wilkins to be Chief Counsel of the Internal Revenue Service, and he has served in that position since August 2009. Previously Bill was a partner with Wilmer Hale in the D.C. office. Bill served as Chair of the Section of Taxation in 2008-2009.

Q Prior to becoming Chief Counsel, had you worked for the Counsel's office or IRS in a prior life?

A No, this is my first time at IRS. My prior government experience was on the Senate Finance Committee staff back in the 1980's.

Q What has surprised you about the Office of Chief Counsel?

A There were no huge surprises. What I found was a very robust organization. In our recruiting spiel we like to say we are the largest tax law firm in the United States. In addition, there is a clear hierarchy and clear lines of authority. I have worked on the Senate Finance Committee staff and in law firms. Those are much flatter organizations than Chief Counsel and the IRS generally. The Office of Chief Counsel is very structured. People have well defined spans of control over employees, so there are a lot of ways to push tasks down into the organization and to have the results filter back up.

One other thing that struck me is that it is a very meeting intensive job. I am very heavily scheduled. Fortunately, other people do most of the meeting preparation. When I was in private practice and a big meeting was scheduled, it was likely that I was the one putting together the memo, the executive summary, the copies of the cases, and the tabbed notebooks. Here other people are doing that for the most part.

Q How do you interact with the Commissioner as Chief Counsel?

A We have regularly scheduled meetings. First, there is a leadership group of which I am a part that meets every week. I have one-on-one time scheduled with the Commissioner every week, but most of our interaction is less scheduled than that. We just handle issues as they come up. His office is right down the hall. We are in and out of each other's office a lot and we also jointly participate in meetings with other government officials. In particular, we have regular meetings with the Treasury Office of Tax Policy and we interact both to prepare for that and at the meeting itself.

Q Do you have to spend much time preparing for Hill appearances?

A I have testified once since I started here, and that was on the Foreign Account Tax Compliance Act. Steve Shay and I were on a panel together. That is the only formal testimony I have given in terms of interaction with the Hill. Other interactions are less formal—they are conference calls and the occasional in-person meetings. That has been less a part of the job than you would find with my counterparts over in the Treasury Office of Tax Policy. They have more of the tax policy end; we have more of the tax administration end.

Q Do you have much occasion to sit down with the Tax Division of the Justice Department?

A We have a regularly scheduled meeting with the Tax Division, usually every month. Also, we have a lot of interaction between times, wrestling with particular issues that are coming up. The cases that we lose present more interesting work for us than the cases that we win, so whenever that happens there is a process of consultation and figuring out next steps.

Q What portion of your attorneys are in the field as opposed to the National Office, and how does the work of the two groups differ?

A There is about a 60/40 split with the 60% being in the field and the 40% being in the National Office. The broad division of labor is that National Office attorneys are for the most part subject matter specialists. They deal with informal and formal guidance in their areas of expertise. They also handle one of the three big tasks of the Office of Chief Counsel, which is building the regulatory infrastructure that is needed to have the system work.

The second big task of Chief Counsel is dealing with conflict resolution in the tax system. That is largely handled by the field, through our Tax Court docket responsibilities. The field attorneys also work with examiners in the field on particular questions that may come up in examination, often in conjunction with National Office subject matter experts.

The third big task is working with IRS leadership on policy initiatives. That involves a combination of both groups, but it tends to be the folks that are the

* Jasper L. Cummings, Jr., Alston & Bird LLP, Washington, DC, and Raleigh, NC, and Alan J.J. Swirski, Skadden, Arps, Slater, Meagher & Flom LLP, Washington, DC.

leaders—the Division Counsel, the deputies, me, our front office people, and sometimes subject matter experts, particularly our experts on tax procedure.

Q Given the softness in the private sector for lawyers, are you seeing any changes in the type or quantity of applicants for Counsel positions?

A That is most visible in our honors hiring, which we do with the J.D. candidates at law schools. We have had that program in place for a number of years, and we are not so much seeing more applicants as we are seeing more candidates who in earlier years would look more at the law firm market, but now are looking at government service. I think this trend is partly because of softness in the law firm market, and partly because high performing law graduates are looking more at public service and government options for their careers. They are not just passively taking the law firm option like so many of us did in the 70's and 80's.

Q How many honors slots does Counsel have a year approximately?

A It is between 40 and 50. We also do hiring at the graduate level out of LL.M. programs, for which there are some additional slots. Many of the J.D. hires are people who worked in our summer program between second and third year in law school. I think with some of the good energy that Don Korb and others here have put into that program, we are very competitive with private sector firms. We have aligned our law school hiring timing and practices to be basically the same as the law firm patterns. On the lateral side, when we have openings for somebody that is more experienced, we have attracted interest from some strong candidates and that has been very encouraging.

Q Is there a hiring freeze at Chief Counsel and do you feel staffing is adequate?

A There is not a hiring freeze. We have authorized staffing levels within the organization and they are allocated within the subparts of the organization. Whenever our staffing drops below the authorized level, we can hire to get back up to the authorized level. That authorized level includes the honors hires, so that is built into the system. Every budget year we take a fresh look at the authorized staffing levels and compare them with who we have on board. What we do with hiring during the course of a fiscal year, October 1 to September 30, depends in large part on the comparison between authorized staffing levels and on-board positions on October 1st. If we have more on board than the authorized staffing level at the beginning of the year, that means we have to watch it on hiring during the course of the year. If we are a little below authorized staffing levels at the beginning of the year, that means we have more head room and actually can overshoot at the end of the year.

I am pretty happy with the resources that we have. I think there are parts within Chief Counsel where we could do a lot of good with some additional help, but that is all a system of priorities. Our budget goes hand in hand with the overall IRS. We are just a couple of percentage points of the entire budget, but I think all the budgeters inside IRS know that if certain activities get increased, generally there is a Counsel capacity that has to be increased to go along with that. This is especially true for initiatives that relate to compliance or conflict resolution.

Q What effect if any do you see of the reorganization of the IRS that occurred in 2000?

A Well, that predated me by a long time. In talking to people as I go out and visit field offices, it basically is what you would expect from having moved from a geographically organized system to an industry based or taxpayer based system. I think the IRS executives and examiners in the operating divisions have really liked having Division Counsel that are dedicated to serving them. This has improved quality of service and has improved uniform application of the law across regions in the country. So I think that has been quite a positive.

The challenges that we face are capturing again some of the good things that came from the geographic structure, such as having management responsibilities in each post of duty that are not chopped up into small pieces. That is where the matrix management idea came about, where each Counsel office does have an overall manager to deal with issues affecting that location. Another benefit of the old structure was that it made it easier to give attorneys a variety of experiences. With the new structure, we try to give people experience handling different kinds of cases by encouraging cross assignments, particularly between SBSE Counsel and LMSB Counsel. Also, we have encouraged our lawyers to be open to the idea of moving from one Division Counsel to another Division Counsel, or moving from a Division Counsel to National Office, or moving from National Office out into the field. Sometimes that is in the form of a temporary detail, and sometimes it is a complete job change.

Q Does the Chief Counsel with other parts of the government utilize a coordinated process to review and analyze the impact of significant federal court opinions?

A With our significant litigation, we engage in analysis that is strategic, and goes well beyond seeking a particular outcome in a particular case. Both IRS and Justice look at what the effect on tax administration would be of pursuing a particular line of argument, of taking a particular case on appeal, of not taking a case on appeal, of acquiescing in a case, or of not appealing a case but putting out an Action on Decision that shows we are not crazy about the case.

To the extent anybody thinks that each case is handled by its own little group

that is totally dedicated to getting the maximum amount of pennies out of that case with nobody looking at the big picture, that is not the way it works.

Q How many attorneys does LMSB have? Are they under your supervision?

A Well, the short answer is LMSB does not have any staff acting as attorneys. There is within the Office of Chief Counsel a Division Counsel for LMSB, Linda Kroening. Within that division there are about 300 attorneys. We have Division Counsel at LMSB, SBSE, and the other operating divisions. LMSB and SBSE Counsel have the bigger head count because they handle much more Tax Court litigation than the others. The total attorney count is about 1,650, to give you a point of comparison to the 300 within the LMSB Division Counsel. Each Division Counsel reports directly to Chris Sterner, who is the Deputy Chief Counsel for Operations, and Chris reports to me.

Q A surprising number of agencies, both inside and outside the government, make recommendations about the operation of the IRS in general and Chief Counsel in particular, including: (1) the National Taxpayer Advocate, (2) the U.S. Treasury Inspector General for Tax Administration, (3) OMB, (4) the IRS Oversight Board, (5) the Information Reporting Program Advisory Committee, (6) the Government Accountability Office, (7) the Transactional Records Access Clearinghouse, and (8) the Joint Committee on Taxation, which second guesses large refund claims. How do these recommendations affect the operations of Chief Counsel?

A That list could actually be longer. Obviously there are several congressional committees in addition to the Joint Tax Committee that have oversight responsibility. Oversight affects operations of parts of the IRS outside Chief Counsel more than they affect Chief Counsel. We are, however, the general counsel for the Internal Revenue Service and we have a General Legal Services division that works with the Service to the extent there are legal issues that arise from oversight. My observation on the interactions of the IRS generally with groups like the Treasury Inspector General for Tax Administration, the GAO, and the Taxpayer Advocate, is that we engage very actively on the issues that they raise. We will normally have reactions to the recommendations embedded within the final version of their reports. You will find in a lot of those reports there are areas of agreement with the overseer that some steps could be taken. Many times, by the time the report comes out, the steps are being implemented.

Q You have spoken about the need of the IRS and Chief Counsel's office to leverage private sector participants in the tax system. Can you elaborate on what that means?

A You want to try to have as few points of collection as you can possibly have. If you do everything on a retail basis, in onesies and twosies, you will get quickly overwhelmed. The tax system touches a lot of people. To the extent you can make tax administration better by having better working relationships with private sector participants, then you are doing a better job for compliance and administration without just putting more boots on the ground and increasing audit coverage.

The tax return preparer initiative is a prime example of that. There are a lot of tax returns that get filed every year. A majority of them involve some intermediation by a professional preparer. Another large chunk involves intermediation with software providers. Engaging with return preparers is a way to have contact with a group that is several hundred thousand individuals but who touch tens of millions of returns. That is leverage.

We obviously engage with all kinds of stakeholders on an informal basis. We have the ABA Tax Section coming into town this week. Clear communication with the tax bar about where we are going with things can help our programs succeed. When we put out a voluntary corrections program, that is an example of giving tax professionals a tool to bring potentially non-compliant taxpayers into compliance.

We are always on the lookout for opportunities like that to achieve our goals by touching a few hundred or a few thousand people who are key points of intersection in the tax system, with the hope of improved compliance on potentially millions of returns.

Q You are the lead singer of a well known tax-themed band which has appeared at various tax functions. Do you have any concerns that the tax law will ever cease to provide topics that your band can gently poke fun at at these meetings and band performances?

A The tax system is the gift that keeps on giving when it comes to targets for parody. There is never any shortage. We have had to retire some songs that have gotten out of date, but there are always more on the way. ■

POINTS TO REMEMBER

Correcting Code Section 409A Document Failures

By Brian A. Benko*

In general, section 409A regulates nonqualified deferred compensation plans. Under these plans, a legally binding right is created between the service recipient and the service provider (herein referred to as "employer" and "employee") to pay compensation in a subsequent taxable year. Section 409A requires, among other things, that deferred compensation is only payable upon the occurrence of certain payment events, including separation from service and change in control, and within a certain period after the occurrence of such payment events. The general purpose of section 409A is to eliminate an employee's right to control the time for receiving deferred compensation. Plan documents must formally and operationally comply with the requirements under section 409A.

Success and failure is all that matters when complying with section 409A. Success occurs when a plan complies with the requirements in form and operation. Failure occurs when a plan does not. The primary concern with success and failure is the effect of each. Success results in deferred compensation. Failure causes immediate income inclusion, if the amount is not subject to a substantial risk of forfeiture and not previously included in income, as well as the imposition of an additional 20% income tax and interest premiums.

Notice 2010-6

For some time practitioners have requested a program for correcting plan document failures. Finally, in Notice 2010-6, 2010-3 I.R.B. 275, the Service provided a program for correcting certain plan document failures. The program uses a self-correction model, allowing for the correction of a failure without gaining government approval. The program sets forth specific failures eligible for correction and certain general eligibility requirements. The program also provides specific methods for correcting failures. If a document failure is eligible for correction, then the failure must be corrected in accordance with the approved method and the employer must satisfy certain information and reporting requirements. The successful correction of a document failure eliminates or greatly reduces the penalty for failing to comply with section 409A.

The corrections program under Notice 2010-6 allows for the correction of certain types of document failures. There are generally five categories of failures that can be corrected: (1) the failure caused by using an impermissible definition for an otherwise permissible payment event; (2) the failure caused by providing for an impermissible payment period following a permissible payment event; (3) the failure caused by using certain impermissible payment events and payment schedules; (4) the failure caused by not including the six-month payment delay for specified employees; and (5) the failure caused by providing for impermissible initial and subsequent deferral elections. Within these five categories, Notice 2010-6 identifies specific document failures and correction methods. Each correction method is highly technical and thus a detailed explanation is outside the scope of this article.

These document failures can be corrected only if certain eligibility requirements are satisfied. Among the eligibility requirements, a document failure must be inadvertent and unintentional, and all other plans that have a similar failure must be identified and corrected using the prescribed method. Also, the failure cannot be for a linked plan or for stock rights, and the employer and the employee cannot be under examination with respect to nonqualified deferred compensation for any taxable year in which the document failure existed.

After using the prescribed correction method to correct a failure that is eligible for correction, employers must satisfy certain information and reporting requirements. An employer must attach an information statement to its timely filed income tax return for the taxable year during which the failure was corrected. The employer must also provide the employee with an information statement. The information statement must include certain general information about the failure. In particular, the information statement must state the name of the plan, that the failure was eligible for correction, and that the failure was timely corrected using the prescribed correction method.

Successfully correcting a document failure under Notice 2010-6 either eliminates or greatly reduces the penalties for failing to comply with section 409A. In three cases, a corrected failure results in no penalties: (1) if the document failure, and any operational failures following from such document failure, are corrected by December 31, 2010; (2) if the document failure is corrected after December 31, 2010, and the corrected provision does not affect the operation of the plan within one year following the correction; and (3) if the document failure occurs under a plan where the plan is the first type offered by the employer and the failure is corrected within a certain period of time. Beyond these cases, limited penalties still apply if, within one

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year after correcting the document failure, the correction affects the operation of the plan.

In addition to allowing the correction of certain document failures, Notice 2010-6 offers guidance on whether certain ambiguous plan terms constitute a document failure. A plan that provides for the occurrence of the payment date "as soon as practicable," or uses substantially similar language, following a permissible payment event does not have a document failure. Instead of interpreting such a provision to provide an uncertain payment date, it is interpreted as providing that the permissible payment event is the payment date. Accordingly, pursuant to the regulations, payment must be made by the later of the end of the employee's taxable year in which the permissible payment event occurs or the fifteenth day of the third calendar month following the permissible payment event.

Notice 2010-6 also provides guidance on whether a permissible payment event with either no definition or an ambiguous definition constitutes a document failure. A document failure does not occur to the extent a payment event is not interpreted as providing for payment under circumstances that would cause the plan to operationally fail to satisfy the law. The plan may be amended at any time to either include a savings clause, or add a definition for the payment event that complies with the law so long as the definition does not add an impermissible payment event or remove a permissible payment event. By promoting the use of a savings clause in these cases, the Service has clarified the positive effect of using such a plan provision.

Although the document corrections program provides some relief, certain aspects of the program raise concerns. As a result, on April 30, 2010, the Tax Section filed comments on Notice 2010-6 with the Service and the Treasury Department. These comments covered areas meriting additional relief, clarification, or guidance.

Conclusion

The document corrections program under Notice 2010-6 offers relief in several different forms and will evolve in the future. Plans with certain document failures may be corrected without penalty or with limited penalty. Plans with certain ambiguously defined payment terms and payment events may be interpreted so that no document failure occurs and may be amended to clarify that a payment event complies with the regulations. Nevertheless, as the Section's concerns indicate, additional Service guidance and relief would be welcome. ■

Academic Tracks? The Tax Attorney as Accounting Professor

By Cheryl Crespi*

If you are interested in an academic career and lifestyle, and an alternative to the 16-hour days which often typify the life of a tax attorney, then the option of an academic career in a school of business might be of interest. In point of fact, while university business school accounting departments typically look for a candidate with an M.B.A., C.P.A., and Ph.D. or D.B.A., a growing shortage of accounting faculty has created a new opportunity, particularly for the tax attorney with an M.B.A. and/or C.P.A. in addition to the J.D. In fact, according to the American Accounting Association, approximately 500 new accounting faculty will be needed annually during the next decade to compensate for retirements, with only 140 Ph.D.s graduating per year. See *Accounting Faculty in U.S. Colleges and Universities: Status and Trends, 1993-2004* (2008) published at aaahq.org. Truly, this growing shortage has created a new market niche for tax attorneys, especially because a key area in need of faculty is the area of taxation!

If you hold a J.D. or are a law student and are interested in an academic career, teaching in a law school is not the sole option. While many law school graduates interested in pursuing academic careers vie for posts in law schools, similar to how most M.D.s teach in medical schools, it is also possible for appropriately trained tax attorneys to develop an academic career path teaching undergraduate (or master's) accounting majors in various schools of business. Of course, proper credentials are still key, and a growing shortage of accounting faculty has not diminished the importance of proper training. But it is also true that a well-crafted vita (universities prefer a vita, also referred to as a curriculum vita or CV, rather than a resume), can often propel a tax attorney into candidacy for a tenure track faculty post.

With a wide range of sizes in colleges and universities, and with varying differences within schools of business, from those offering bachelor's degrees to those emphasizing master's degrees, the range of options is quite large. Many smaller colleges offering largely bachelor's degrees emphasize quality teaching, while other schools, offering master's degrees and/or Ph.D. programs, may emphasize a mix of scholarship, teaching, and service responsibilities. As such, it would be myopic to assume one type of tax attorney would have appeal in every school. Just as different law firms have different emphases and look for certain qualities with candidates, so too, applicants for academic posts should examine philosophies and emphases prior to making application.

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With few Ph.D.s in accounting graduating annually, though, this "niche" market is certainly viable. At the same time, applicants, particularly if a finalist for a campus interview, should understand that academic posts in schools of business have expectations different from those of law firms and law schools. As an example, teaching excellence is highly valued, as are expectations for undergraduate advising, service, and (similar to a law school post), scholarly presentations and publications. Because J.D.s have not completed a doctoral dissertation, committees may worry about the potential for research and publication but strong candidates can assure committees that law school faculty publish regularly, and that attorneys conduct research routinely, using models ranging from single case designs to basic descriptive research models. In fact, tax law (and case law) can serve as an outstanding base for developing scholarly endeavors.

Although J.D.s are not typically recruited into undergraduate accounting departments part-time, adjunct teaching can serve as a nice vehicle for both gaining initial teaching experience while also serving as an introduction to a local school or college. In fact, it might be viewed as parallel to a year-long clerkship in gaining critical teaching experience. At worst, such an experience simply adds supplemental income; at best, it opens a door to this new career path.

Learning About Open Positions

Intrigued? How, then, can a J.D. find out about job openings? One comprehensive on-line source is *The Chronicle of Higher Education* (http://chronicle.com/jobs). *The Chronicle* is one of the premier sources to which universities post academic openings and, as such, maintains a database of current faculty openings. Accounting openings can be located by searching in the following tab sequence: Faculty/research tab; Business/management tab; Accounting/finance tab. Individual college postings are listed chronologically with a state identification as this is a national database. A second on-line source is HigherEdJobs (http://higheredjobs.com). On one particular day, it listed 12,134 openings at 1,778 institutions. While certainly not all were accounting openings, this is a useful source for learning about accounting job openings. Like *The Chronicle*, this source also uses a sequence of tabs to locate applicable openings. At higheredjobs.com, a search can be performed on category (faculty tab, business tab, accounting tab – one search produced 155 openings), type (community college or part-time) or location (state or institution). Utilizing both databases should increase your ability to identify relevant openings.

Interested in a particular school? If you have a particular university or college in mind, such as your alma mater, or the closest university to your home, inquire directly at that university's website for current openings. These may be found on a human resources page for employment opportunities, postings, openings, careers, etc. Of course, the more limiting the search, the more limiting the available opportunities.

Elsewhere, one other important source of accounting faculty openings is with the American Accounting Association (AAA) (http://aaahq.org), a professional organization of individuals interested in accounting education. Their website includes a placement center, titled AAA Career Center, on which interested job seekers may post resumes and view jobs. Additionally, the AAA holds an annual meeting at which networking occurs and interviewing for openings is conducted. This is a practical path to discover the needs of a variety of universities. Keep in mind that the annual meeting is held annually at the beginning of August (this year in San Francisco). Of course, in academe, it is common to conduct an academic search a year in advance of an impending start date.

The Academic Interview

Applicants may need to prepare a teaching demonstration and a possible presentation covering a research and scholarly agenda. They must also demonstrate an understanding of the college and department mission and of teaching and scholarly expectations expected for the position. In many ways, of course, this is similar (if not identical) to the preparation an attorney will conduct in researching the expectations of a law firm recruiting a new associate. An understanding that academic promotions progress through the ranks of assistant, associate, and full professor is important and similar to the progress an attorney might make progressing from law clerk to associate to partner. Both progressions help in an important socialization process.

Academic interviews differ from law firm interviews in multiple ways. First, academics will typically invite the three finalists for campus interviews while law firms may conduct large numbers of interviews. Second, universities typically interview on their campus, with occasional initial interviews conducted at annual conference meetings such as the American Accounting Association's Annual Meeting Placement Center and Career Fair. Ultimately, though, you go to the campus. Third, campus interviews typically last several days, include individual interviews with all department faculty, and include interviews with deans and department chairs. Fourth, teaching and research demonstrations are conducted during this phase. Finally, scholarly and teaching objectives will be discussed in multiple arenas, with departments often reaching a final decision through a department-wide voting process. No one "partner" makes the decision.

Applicants invited for a campus interview are wise to research the college thoroughly prior to arrival. They should also examine the credentials and research and teaching interests of all faculty prior to arriving on campus.

It is also important to understand that many Ph.D.s will not view a J.D. as an equivalent degree, possibly viewing it as

a professional degree rather than a scholarly degree. Applicants need to be prepared to understand the culture which typifies academic life. At the same time, a tax attorney can bring unique mentoring skills for students, develop engaging scholarly agendas, and add balance to a department.

Course Assignments

What might the J.D. actually teach? A J.D. may be assigned to teach a variety of accounting classes. While the intricacies of debits and credits may elude a J.D., certainly individual tax, partnership tax and corporate tax would be viable courses for a J.D. to teach. Some accounting departments may provide a tax track for accounting majors or, at the least, several tax course options that the J.D. may be highly qualified to teach. And, with the emphasis for the C.P.A. license on candidates earning 150 credit hours (30 more than the norm for B.A./B.S. degrees), accounting departments have added additional courses to provide the C.P.A. candidate with sufficient opportunities to satisfy this requirement. Additionally, master's level programs may offer a tax specialty.

Aside from particular accounting classes, the J.D. would be qualified to teach business law (tested on the C.P.A. examination), which may also be offered by accounting departments. Know, however, that some schools may offer business law in another department, either within the business school or elsewhere in the university. A J.D. with a C.P.A., however, may be assigned to teach any accounting class (financial accounting, government accounting, etc.) with sufficient preparations depending upon the university or college. Given that a J.D./C.P.A did pass the C.P.A. exam, at least minimal competency has already been demonstrated!

Credentials

Business schools, which house accounting departments, may, of course, be sensitive to meeting standards created by the Association to Advance Collegiate Schools of Business (AACSB). Those standards differentiate between professionally qualified faculty and academically qualified faculty, but both may be considered as an important component of the faculty. A professionally qualified faculty member must have five years of recent work experience; therefore, work experience may be quite the marker for a faculty position, allowing the faculty member to draw upon business practice in teaching. And a J.D. who has worked for the Service, for example, would have a unique combination of experience to offer. On the other hand, an academically qualified faculty member may have a graduate degree in taxation or a combination of graduate degrees in law and accounting. Either classification may work for the J.D.; they are explained here to help interested and aspiring candidates gain some understanding of the political climate of an accounting department.

What combinations of degrees and certifications, then, are most desirable for a faculty post? With the shortage at hand, universities recognize the need to be more flexible and accepting of credentials that differ from the traditional Ph.D. As such, a J.D. armed with either an M.B.A. (obtained separately or in a joint J.D./M.B.A. program) or a C.P.A. (or ideally all three credentials) may be highly attractive to an accounting department with vacancies. Credentials other than the C.P.A. may also be valued. Credentials, such as C.I.A. (Certified Internal Auditor) and C.M.A. (Certified Managerial Accountant), can add nicely to a professional portfolio.

Conclusion

In short, for a tax attorney armed with an M.B.A. or C.P.A. in addition to the J.D., one practical career path can involve an academic career teaching accounting in a school of business. With a shortage of business school faculty, more specifically accounting faculty, the well-armed and well-prepared tax attorney can be a viable applicant. At the same time, as with any career agenda, proper planning is key. ■

FATCA Provisions of the HIRE Act: Possible Effects on International Disclosure Norms

By Vlad Frants*

On March 18, 2010, President Obama signed the Hiring Incentives to Restore Employment Act ("HIRE Act"). Pub. L. No. 111-147, 124 Stat. 71. As its title suggests, this legislation was meant to incentivize new hiring by employers in order to stimulate the U.S. economy. One of the provisions within the HIRE Act derives its popular name (FATCA) from two bills introduced in 2009, H.R. 3933 and S. 1934 (Foreign Account Tax Compliance Act of 2009). HIRE Act § 501, adding sections 1471–1474. This provision appears with other offset provisions that were added to help pay for the bill. The purpose behind FATCA was to help the government track down U.S. persons who evade taxes through the use of foreign accounts and investment vehicles. Thus, by including FATCA provisions in the HIRE Act, Congress not only gave employers incentives to create jobs but also provided for an all-out assault on tax evasion through the international channels as a means to help pay for those incentives.

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FATCA expanded the reporting obligations for U.S. individuals with respect to any interest in certain foreign financial assets, created substantial penalties for noncompliance, and extended the statute of limitations for assessment of tax on understatements of gross income attributable to those foreign financial assets. It also includes new PFIC shareholder reporting requirements, repeals bearer bond exemptions, and treats certain dividend equivalent payments on swaps as dividends for U.S. withholding tax purposes. The most stunning provisions of FATCA are the rules applicable to foreign institutions, which, essentially, affect disclosure norms by foreign entities.

FATCA presents foreign financial institutions (FFI) with the following ultimatum—enter into a reporting agreement with the U.S. Treasury or else be subject to a 30% withholding tax on all "withholdable payments." Withholdable payments include the payment of interest, dividends, and other U.S. source payments traditionally subject to U.S. withholding tax. They also include gross proceeds from sales or other dispositions of U.S. bonds, stocks or other debt instruments.

Section 1471(b)(1) imposes several reporting requirements that must be met as part of an agreement between the U.S. and an FFI. The reporting agreement would require the FFI to agree:

- To obtain information on all of its accounts to determine which accounts are U.S. accounts;
- To verify such information through required due diligence;
- To annually report information on its U.S. accounts to the Treasury;
- To withhold certain payments belonging to account holders who fail to produce the required information ("recalcitrant account holders") and to withhold payments to other foreign financial institutions that do not comply with these rules;
- To comply with any requests by the Treasury for additional information on U.S. accounts; and
- To attempt to obtain from each U.S. account holder a waiver of any foreign law that would prevent the foreign financial institution from reporting to the Treasury any required information so obtained and, if such waiver is not obtained, to close the account.

FATCA presents non-financial foreign entities (NFFE) with a different ultimatum—the NFFE receiving withholdable payments beneficially owned by it, or by another NFFE, must either disclose its substantial U.S. owners, if any, or be subject to 30% U.S. withholding tax on all withholdable payments. I.R.C. § 1472.

In the cases of both types of entities, the U.S. is basically saying: "disclose and comply with our rules or we'll require withholding." It is possible that the 30% withholding tax on all withholdable payments will "scare" foreign entities into disclosure about their accounts (when those entities either don't want to or are prohibited from disclosure under their own laws). But there is, in fact, a third possibility—foreign entities can close all U.S. accounts and avoid having dealings with U.S. persons. They will not have to worry about the 30% withholding tax or burden themselves with U.S.-imposed compliance and disclosure demands.

Because the 30% withholding requirement on withholdable payments to foreign entities goes into effect for payments made after December 31, 2012 (and there is a grandfathering exception for debt obligations outstanding on March 18, 2012), it is too soon to know how these new laws will affect disclosure. There is no such formal "induced-disclosure" mechanism currently in place. Some countries may entertain the "option" of disclosure and some may not. In any event, the FATCA provisions of the HIRE Act are of considerable importance for U.S. citizens, U.S. relations with other countries, and international disclosure norms. ■

Tax Court Invalidates New Section 6501(e) Regulations

By Steve R. Johnson*

The title of an article of mine in the Fall 2009 issue of the NewsQuarterly asked "What's Next in the Section 6501(e) Overstated Basis Controversy?" The Tax Court answered that question on May 6, 2010, in its decision *Intermountain Insurance Service of Vail, LLC v. Commissioner*, 134 T.C. No. 11. In that decision, the court invalidated two temporary regulations that had been issued on September 24, 2009: sections 301.6229(c)(2)-IT and 301.6501(e)-IT.

The Tax Court was unanimous in its result, but seriously divided as to the reasons for the result. The *Intermountain* decision is important as to both the six-year statute of limitations on assessment and the validity of tax regulations generally. It is certain, however, that the decision will not be the last word on either of these topics.

Background

There are many exceptions to the usual three-year statute of limitations on assessments. One is section 6501(e)(1)

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(A)(i), which gives the Service six years to assess income tax liabilities "[i]f the taxpayer omits from gross income an amount properly includible therein [which] is in excess of 25% of the amount of gross income stated in the return." Section 6229(c)(2) provides a similar exception for cases governed by the TEFRA partnership audit and litigation rules.

These exceptions undoubtedly apply when the taxpayer omits enough taxable receipts, but it has been controversial whether they apply when the understatement arises instead from overstated basis of sold assets. As detailed in the Fall 2009 article, the case law on the section 6501(e) overstated basis issue is divided, but the Service suffered a string of defeats in 2009 cases.

To reverse its fortunes, Treasury issued the September 24 regulations in both temporary and proposed form. Aggressively, the temporary regulations were declared to apply to tax years still open to assessment on the date of issuance, with the intention that they apply to all pending cases, including those which taxpayers had won but in which the decisions had not yet become final. *See* T.D. 9466, 2009-43 I.R.B. 551. Both the new regulations and their effective date have been highly controversial from their inception.

Intermountain

Intermountain involves what the Service considers to be an abusive tax shelter involving overstated basis. Having failed to act within the normal three years, the Service relied on the six-year limitations period. Less than a month before issuance of the temporary regulations, the Tax Court had decided the statute of limitations issue in Intermountain's favor. T.C. Memo. 2009-195. Based on the new regulations, the Service filed motions to vacate and for reconsideration of that decision.

By 13 to 0, the Tax Court held against the Service, but the 13 judges fell into three camps. Seven judges, in an opinion written by Judge Wherry, explored the possibility that, as actually drafted, the effective date provision did not effectuate Treasury's intention to reach not-yet-final cases. Although advancing a questionable "plain meaning" analysis, the majority chose not to rest the decision on that ground.

Instead, the majority examined the substantive validity of the temporary regulations. Assuming arguendo that *Chevron* provides the governing standard, the majority concluded that the regulations did not pass muster under *Chevron* Step One or *Brand X. See National Cable & Telecomm. Ass'n v. Brand X Internet Services*, 545 U.S. 967, 982 (2005); *Chevron U.S.A., Inc. v. Natural Res. Def. Council, Inc.,* 467 U.S. 837 (1984). Specifically, the majority concluded that the Supreme Court's *Colony* decision a half century ago had held that what is now section 6501(e) unambiguously precludes the position taken in the temporary regulations. *Colony, Inc. v. Commissioner,* 357 U.S. 28 (1958). The majority also noted, but felt it unnecessary to rule on, the taxpayer's argument that the temporary regulations have impermissibly retroactive effect.

Four other judges concurred in an opinion penned by Judge Cohen. This concurrence would have resolved the case on narrower grounds. Motions such as the Service's typically are granted only in unusual circumstances. An intervening statutory change can be such a circumstance. *Alioto v. Commissioner,* T.C. Memo. 2008-185, *vacating* T.C. Memo. 2006-199. The concurrence would have held, however, that an intervening regulatory change does not rise to the same level, thus is insufficient to warrant vacating or reconsidering.

Judges Halpern and Holmes concurred in another opinion. These judges rejected the majority's effective date and *Chevron* analyses but saw the temporary regulations as invalid on procedural grounds. The Administrative Procedure Act ("APA") applies to rulemaking by federal agencies, including the Treasury Department. *See* 5 U.S.C. § 551(1). Unless a stated exception applies, regulations are validly promulgated only if they go through the notice-and-comment process prescribed by 5 U.S.C. § 553. The temporary regulations were not promulgated through this process. Nonetheless, the Service defended their validity on two grounds: that the regulations fall within the APA exception for merely interpretive rules and that Congress implicitly excepted temporary tax regulations from the notice-and-comment requirement. The Halpern/Holmes concurrence rejected both contentions, and thus would hold the regulations to be procedurally invalid under the APA.

Evaluation

All three opinions in *Intermountain* reflected distaste for what the judges viewed as overly zealous use of the regulations process. The Service saw the *Intermountain* tax shelter as abusive. It is worth remembering that not just taxpayers, but the Service, too, can commit tax abuse.

Although motivated by a common impulse, the Tax Court judges differed greatly as to the doctrine by which to make that impulse legally operative. In my view, Judges Halpern and Holmes had the best view of the case. The omission of notice-and-comment is not justified by either of the grounds asserted by the Service.

The Service's "merely interpretive" argument is hopeless. The temporary regulations at issue were promulgated under the general authority of section 7805(a), not specific authority within sections 6501 or 6229. The Service and tax lawyers as a whole have long called general-authority regulations "interpretive" and specific-authority regulations "legislative." It is high time that we broke ourselves of that bad habit. "Interpretive" and "legislative" regulations have well understood meanings in administrative

law—meanings which have nothing to do with the general-authority versus specific-authority distinction. Instead, legislative regulations have "force of law" character—they make binding law or change the law—while interpretive regulations merely explain the agency's view of the statute. *E.g., Chrysler Corp. v. Brown*, 441 U.S. 281, 301-02 (1979). Tax regulations that make binding law are legislative whether they are promulgated under specific authority or general authority. The temporary regulations at issue clearly are legislative; their point was not to explain the Service's view of section 6501 but to change the law by administratively reversing the law as articulated by the adverse cases.

The Service's argument that Congress excepted temporary tax regulations from APA notice-and-comment is better but probably not good enough. The argument is based on inference, not explicit text. Yet Congress has provided that other statutes may modify APA requirements only expressly, not impliedly. 5 U.S.C. § 559.

The arguments advanced in the other *Intermountain* opinions do not strike me as persuasive. First, as pointed out by Judges Halpern and Holmes, the regulations' effective date provision is ambiguous, not plain. The provision might be read to mean "open under the normal three-year period," as the *Intermountain* majority read it, or it might mean "open under the six-year period, as that period is extended by this regulation," as Treasury and the Service intended. An agency's construction of its own ambiguous regulation is entitled to deference. *E.g., Auer v. Robbins*, 519 U.S. 452, 461 (1997); *Stinson v. United States,* 508 U.S. 36, 44-46 (1993).

Second, the majority likely is wrong as to its *Chevron* Step One analysis. *Colony* itself did not say that its result was unambiguously commanded by the statute. Moreover, *Colony* construed a predecessor of current section 6501(e), and the current statute arguably is somewhat more congenial to the Service's position. Finally, as noted in the Fall 2009 article, the Service won a number of the cases after *Colony* but before 2009. There are two possibilities. Either the courts holding for the Service failed to notice that *Colony* had settled the issue, or the *Intermountain* majority overplayed its hand in characterizing *Colony*'s holding. I think that the second of these alternatives better states the matter.

Third, the narrow ground offered by Judge Cohen and the judges joining her is dubious. Yes, a statute outranks a regulation. But a validly promulgated legislative regulation has force of law status. Thus, the distinction offered by Judge Cohen's concurrence is not a meaningful difference.

Predictions

The Tax Court's *Intermountain* decision surely is not the last shot that will be fired in the overstated basis statute of limitations battle. The Government may appeal *Intermountain*, and the validity and applicability of the new regulations will surely be tested in other cases in the future.

Based on the above analysis, the temporary regulations should continue to be invalidated. However, when they have been finalized after completion of notice-and-comment, the regulations should be upheld, particularly if applied only prospectively. Taxpayers who already have won their cases should be safe, but taxpayers whose cases have not yet been decided will be in jeopardy. ■

Social Security Benefits Formula 101: A Practical Primer

By Francine J. Lipman* and James E. Williamson†

Social Security benefits redistribute income broadly and deeply every month across America. One out of every four households and one out of every six Americans receive these critically important benefits. Almost 52 million beneficiaries receive monthly Social Security payments averaging more than $13,000 annually. While almost all seniors receive Social Security benefits, millions of children and people with disabilities also receive payments.

As these statistics demonstrate, Social Security has been one of the most successful programs in the history of America. The broad distribution of meaningful monthly benefits lifts and keeps millions out of poverty. Social Security benefits keep 40% of seniors out of poverty as well as more than one million children. These benefits are the major source of income for 52% of senior couples and 73% of senior singles and represent 90% or more of income for 21% of senior couples and 44% of senior singles (47% of senior women).

Despite the broad and deep reliance on Social Security benefits, very few of the hundreds of millions of current and future beneficiaries understand how the program works. This article will present through a hypothetical couple some of the basics of the Social Security benefits formula.

Please consider the following (perhaps all too familiar) taxpayers:

Maria and John graduated from law school in 1973 at 25 years young. As tax lawyers in love, they married and practiced tax law. After the birth of their second child, they decided that John

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Table 1

Year of Birth	FRA and Full Benefits	Age 62 Benefits As % of FRA Benefits
1937 or earlier	65	80
1938-1942	Varies (increases by 2 months for each year)	Varies (decreases by 0.83% for each year)
1943-1954	66	75
1955-1959	Varies (increases by 2 months for each year)	Varies (decreases by 0.83% for each year)
1960 and later	67	70

should quit his job and be a stay-at-home parent. Except for two maternity leaves of six months each, when the children were born, Maria has worked continuously until the present time.

Because they are now 62 years old, they have received evaluations of their Social Security retirement benefits, called the primary insurance amount (PIA). At this time they have to make their first decision about their Social Security benefits. While full retirement age (FRA) for Maria and John is age 66, they may elect a reduced Social Security benefit as early as age 62.

Had John and Maria been born a few years earlier, their age 62 benefits would have been a larger percentage of FRA benefits and their FRA would have been age 65. The Social Security Administration has implemented certain changes enacted by Congress in 2000. These changes will increase FRA from 65 to 67, while the percentage of full benefits paid to people retiring at the earliest retirement age (62) is being reduced over time from 80% to 70% of PIA. These rules are illustrated in Table 1.

PIA is the monthly benefit at FRA. If a beneficiary elects to start benefits early at age 62, she would receive 75% (70% for those born in 1960 and later) of her PIA. If she elects to defer starting her benefits until age 70, she would receive the maximum amount of Social Security benefits or 132% of PIA (8% guaranteed increase for annual deferrals beyond FRA). If she elects to defer starting her benefits to any age after 62, the PIA will be increased by any annual cost of living adjustments (COLAs).

The Basic Social Security Retirement Benefit Formula (www.ssa.gov/estimator/)

The Social Security system was designed to provide a financial retirement safety net for workers and their dependents. Accordingly, lower and middle wage earners receive a much greater percentage benefit (as compared to the cost percentage (or effective tax rate)) than higher wage earners. Social Security benefits are computed using a worker's average wage-indexed monthly earnings (AIME) on which Social Security taxes were paid during the 35 highest qualifying earning years. PIA includes 90% of the first level of AIME (up to $761 for those attaining age 62 in 2010). The second level of AIME (from bend point one to bend point two) is included in PIA at 32%. The third level of AIME is measured from bend point two to the Social Security taxable earnings ceiling. PIA includes only 15% of this amount. This calculation is illustrated for Maria, who would have the highest possible AIME of $7,948 in 2010 ($95,376, maximum average/wage-indexed annual earnings that have been subject to Social Security tax for the last 35 years).

A worker paying the maximum amount into the Social Security system for 35 years prior to 2010 would receive a monthly PIA of $2,413 ($28,956 annually). However, an average wage earner paying into the Social Security system on AIME of $4,586 ($55,032 annually) would receive a monthly benefit of $1,909 ($685 + $1,224) ($22,908 annually). These two benefit levels illustrate the cost/benefit advantage to an average wage earner. The higher wage earner receives only 23% more per month ($504) than the average wage earner while having paid 73% more in Social Security tax.

Because Maria has paid the maximum Social Security tax for more than 35 years, her PIA is $2,413. If we assume John paid in the maximum Social Security tax for each year that he worked, but only for ten years, his PIA will be based on an AIME of no more than $2,271 (10/35 x $7,948). Therefore, John's PIA is:

PIA = (761 x 0.90 = 685) + ((2,271-761) x 0.32= 483) = $1,168.

Although John paid only 27% (10/37) of the amount of Social Security tax that Maria paid, his PIA is almost 50% of her PIA. This is a result of the 90% and 32% benefits on lower amounts of AIME. The Social Security benefit formula was designed to provide an antipoverty safety net for middle and lower wage earners and their families. The Medicare system similarly provides a health care safety net. Every person who qualifies for Medicare benefits receives exactly the same benefits regardless of the amount of Medicare tax paid.

Table 2

Calculation of PIA for Workers Attaining Age 62 in 2010

	First Bend Point		Second Bend Point		Maximum AIME
	$761		$4,586		$7,948
Range	(761 x 0.90)	+	((4,586 – 761) x 0.32)	+	((7,948 – 4,586) x 0.15)
PIA	685	+	1,224	+	504 = $2,413

The Election to Start Social Security Retirement Benefits

More than 70% of recipients receive reduced benefits because they elected to start benefits before their FRA. Based on their respective PIAs, and disregarding potential COLAs, benefits at the various election dates for Maria and John would be:

Table 3

Age	62	66	70
Maria	$1,810	$2,413	$3,185
John	$ 876	$1,168	$1,542

One of the traps for the unwary in the early retirement benefits election is that, for any year in which you are younger than FRA and continue to have earned income, you must pay back $1 of your benefits for each $2 that you earn above $14,160 (indexed annually). In the year that you reach FRA, you must pay back $1 for each $3 that you earn above $37,680 (indexed annually), until the month that you reach FRA. Once you reach FRA, you may earn as much as you are capable of without a benefits payback penalty. For many workers who elect to start their Social Security benefits at 62, the sacrifice includes not only reduced benefits (75% of PIA), but also lost wages during these pre-FRA years.

Unless Maria decides to retire from practicing tax law, there would be no reason to elect to receive her benefits before her FRA. Alternatively, if John is not working in a position where he earns more than $14,160 per year, he may want to start his Social Security benefits at age 62. No matter how much Maria earns during these years, it would not affect John's benefits. Therefore, Maria and John might decide that John should start his benefits at age 62 ($876) and Maria should start her benefit at FRA ($2,413) or even at age 70 ($3,185).

Once Maria retires, John could begin collecting his spousal Social Security retirement benefits, which would be 75% of half of her benefit (0.75(0.5 x 2,413) = $905, or 0.75(0.5 x 3,185) = $1,194). If Maria and John have unmarried children (or dependent grandchildren) who are younger than age 18, full-time students (grade 12 or below) or disabled (before age 22) when they start their Social Security benefits, each child will qualify for up to half of the highest retiree's FRA benefit. However, the family cannot exceed a maximum family benefit—generally between 150% and 180% of the retiree's benefit. If a family beneficiary works, the payback penalty applies to her benefits based upon her earnings record.

Surviving Spousal Benefits

Regardless of whether John continues with his own benefits or switches to a percentage of Maria's benefit, should she die before he does, he will be able to claim 100% of her Social Security benefits as a surviving spouse. Because of this generous surviving spouse benefit, the spouse with the highest PIA should consider seriously delaying starting Social Security benefits as long as reasonably possible (up to age 70 when the benefit is capped at 132% of PIA).

Because they were married for more than 10 years, John's spousal benefits are unaffected even if Maria and John divorce. This is true even if Maria remarries. However, if John remarries before age 61, he cannot collect spousal benefits on any former wife's employment record while he is married. If John becomes single again (through divorce or death) or remarries after age 60 (50 if disabled) he will be able to collect Social Security benefits on Maria's work record.

Other Factors to Consider

The discussion in this article focuses solely on Social Security benefit levels. Decisions regarding Social Security are further complicated by the section 86 computation, which determines the percentage of benefits included in gross income. A related issue involves whether to apply for Medicare participation at 65 or continue participating in an employer-provided plan. The employer-provided premiums are generally excluded from the employee's gross income under section 106; the exclusion does not vary based on the employee's age or income. Medicare premiums, on the other hand, are an out-of-pocket cost and are means-tested. For more extensive coverage of these considerations, see Francine J. Lipman, *Shrinking Boomer Social Security Retirement Benefits*, NEWSQUARTERLY, Fall 2007, at 19.

Conclusions

As you have discovered, the Social Security benefits formula is complex and riddled with critically important decisions. Understanding how the Social Security benefits formula functions is necessary if you are to make the best decisions for your family, clients, and yourself. Millions of beneficiaries take early and substantially reduced Social Security retirement benefits. This election can result in years of regret because of inadequate cash flow to maintain an acquired or even subsistence retirement lifestyle. The worker's decisions not only affect her benefits, but the benefits of spouses, ex-spouses, and children. Because the future is so uncertain, especially given the risks in financial and real estate investment markets, a conservative approach would be best for many beneficiaries to minimize risk. Government guaranteed Social Security benefits are high return, low risk and life-saving investments for (too) many millions of beneficiaries. ■

Ronald A. Pearlman—2010 Distinguished Service Award Recipient

By Susan P. Serota*

The Section of Taxation is pleased to honor Ronald A. Pearlman, a professor of law at the Georgetown University Law Center, as our recipient of the Section of Taxation's 2010 **Distinguished Service Award** in recognition of his lifelong contributions to the tax profession and the development of tax law and policy.

Born in Hamilton, Ohio, Ron received his B.A., with honors, from Northwestern University in 1962. He attended Northwestern University School of Law where he received his J.D. *cum laude* in 1965, graduating Order of the Coif and was a member of the Northwestern University Law Review. Following the advice of one of his tax professors at Northwestern, Ron turned down offers from major law firms to become an Attorney-Advisor in the Office of Chief Counsel (Interpretive Division) of the Internal Revenue Service. Ron describes this as a "fabulous beginning to my career." While working at the Service, Ron somehow found the time to study at Georgetown Law where he received his LL.M. (Taxation). But even before his time at the Service and foreshadowing his time at the Joint Committee on Taxation, Ron was known for his budgeting skills. It is reported that when he and his wife, Hedy, went to Europe on their honeymoon, Ron made up his mind to do it on $5 a day (then very much in vogue). Apparently, Ron took it to the extreme, i.e., any day he and Hedy spent $6, the next day he insisted on spending only $4.

After leaving the Service in 1969, Ron and his family moved to St. Louis, where Hedy had grown up, to practice law for the next 16 years with the Thompson & Mitchell (now Thompson & Coburn) law firm. While in St. Louis, Ron had his first taste of teaching law when he was an Adjunct Professor at Washington University School of Law for 11 years.

Tax policy, always a great interest of Ron's, beckoned to him when in 1983 he was offered first the position of Deputy Assistant Secretary (Tax Policy) at the U.S. Department of Treasury, and then in 1984, the position of Assistant Secretary (Tax Policy). When Ron went into Government, he understood from the beginning that it was never the person but always the job that was important. He was well aware that once he left Government, the authority he previously had would be in the past and that someone else would be the decision maker. Thus, his friends and colleagues say that he never took himself too seriously.

While Ron was at the Treasury, major changes and reforms in tax law were being considered. Ron had overall responsibility for development of the Department's 1984 tax reform proposals ("Treasury I") and President Reagan's 1985 tax reform recommendations to the Congress. During the consideration of the Tax Reform Act of 1986 by the House of Representatives, he represented the Administration and was intimately involved in the tax legislative process. For his service at the Treasury, Ron was awarded the Alexander Hamilton Medal (the Treasury Department's highest award).

At the end of 1985, he left Treasury and returned to St. Louis and private practice. But Washington and tax policy beckoned once more just three years later when in 1988 he was offered the position of Chief of Staff of the Joint Committee on Taxation. Reluctant to move his family again, he at first declined, even though Sen. Lloyd Bentsen (D. Tex.) and Rep. Daniel Rostenkowski (D. Ill.), respectively Chairs of the Senate Finance Committee and the House Ways and Means Committee, both tried to convince him to take the position. However, within 24 hours, he realized that he would always regret not taking the position. Ron spent the next three years at the Joint Committee where his integrity and his commitment to sound tax policy can be seen.

Ron's agenda as Chief of Staff—and the historic agenda of the Joint Committee—was not to serve the interests of a particular person or party, but rather to help Congress develop legislation based on accurate measurement of income and conscious, explicit, and transparent decisions about the level of taxation that is applied to that income. To be effective in the legislative setting requires gaining the trust and confidence of Members of Congress with widely divergent policy perspectives, levels of knowledge, and personal priorities. Ron was extraordinarily effective in dealing with Members across the political spectrum; he knew just how to provide both effective staff support that Members could rightfully expect, while at the same time making clear to them the merits (or defects) in their proposals when measured against generally accepted norms of taxation. This is not to suggest that sound tax policy always (or even most often) guided the ultimate shape of tax

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legislation; but rather that Members were able to make well-informed decisions about the policy options they chose and that the costs and relative impacts of those decisions were made explicit and public.

Ron was also required to deal with questions and proposals across the entire Code—often with little or no time to prepare and in a very public setting. Typically the Joint Committee's revenue table for any significant piece of tax legislation includes dozens of different provisions and in a mark-up of these bills, each Member of the tax writing committees could ask questions or offer amendments about any of these provisions. As Chief of Staff, Ron was required to address literally hundreds of questions often on the spot and without any advance preparation.

Stuart Brown, Ron's Deputy Chief of Staff, remembers that Ron was very adept at responding to new ideas. On one particular occasion when a very senior member of one of the tax writing committees offered a proposal in a late night strategy meeting, "the proposal was sufficiently complex and detailed that I guessed it was being advanced at the recommendation of an outside lobbyist, but it was so poorly explained by the Member, that I had no idea what was actually being proposed. While I don't remember his exact words, Ron's response was along the lines of—a very creative and novel approach, but so different from generally accepted norms of international taxation that it could substantially affect and undermine the international competitive position of the entire U.S. economy. While I doubted that anyone else in the meeting actually understood the specific suggestion that had been offered, Ron's comment ended the discussion."

Ron's ability to provide immediate, useful, and understandable advice, about such a wide range of issues and proposals was systemically important for two reasons. First, of course, it helped determine whether particular provisions would or would not be enacted. And second, the cumulative impact of his performance served to enhance the standing of the Joint Committee and ultimately the degree to which principles of sound tax policy would have any role to play in the legislative process.

After leaving the Joint Committee, Ron became a tax partner at Covington & Burling in Washington, D.C., where he spent the next nine years until he retired from private practice. However, Ron's interest in tax law and policy was a magnet which drew him in 1999 to teach tax law as a full-time professor at Georgetown University Law Center and where he still remains a member of the faculty. From 1999-2002, he served as Director of the Law Center's Graduate Tax Program. He has also taught as the Austin Wakeman Scott Visiting Professor of Law at Harvard Law School (Fall 2002) and as a Lecturer at the Vienna University of Economics and Business Administration (June 2008), ISTAX Senior Course, Japan National Tax Administration, Tokyo, Japan (October 2003), and ESADE Law School, Barcelona, Spain (June 2000), among others.

Among Ron's many publications, the following stand out: *A Tax Reform Caveat: In the Real World, There Is No Perfect Tax System* in TOWARD FUNDAMENTAL TAX REFORM 105 (Auerbach & Hassett, eds., AEI Press 2005); *Demystifying Disclosure: First Steps*, 55 TAX L. REV. 289 (2002); *Fresh From the River Styx: The Achilles Heels of Tax Reform Proposals*, 51 NAT'L TAX J. 569 (1998) and *Transition Issues in Moving to a Consumption Tax: A Tax Lawyer's Perspective*, in ECONOMIC EFFECTS OF FUNDAMENTAL TAX REFORM 393 (Aaron & Gale, eds., Brookings Institution Press 1996). A sequel to this paper was published in COMPREHENSIVE ANALYSIS OF CURRENT CONSUMPTION TAX PROPOSALS 17 (American Bar Association 1997).

During his long career in taxation, Ron also was active in professional organizations and advisory groups, including the ABA Section of Taxation, where he served as a member of Council and Vice-Chair (Government Relations). Stef Tucker, then Chair of the Section, recalls that Ron was both pragmatic and very knowledgeable as to the real workings of the Government, both in the legislative world and in the world of regulations and rulings. Ron retained a wonderful rapport with everyone with whom he worked in his Government service and their respect for Ron's views was always apparent. Ron also was a consultant to two tax policy projects of the American Law Institute and served as President of the American Tax Policy Institute. Ron has testified before Congress more than 30 times on tax policy matters.

Ron's outstanding career in government, academia, private practice, his service to the profession, his devotion to tax policy issues, and his dedication to the development of tax law, make him an exemplary recipient of the Section of Taxation's 2010 Distinguished Service Award. ■

Laura Newland—2009 Public Service Fellow

Laura Newland received one of the first two Public Service Fellowships awarded by the Section in the program's inaugural year, 2009. She began her Fellowship after graduating from Georgetown University Law Center in the spring of 2009, and has been providing tax assistance to low-income seniors in the Washington, DC area through AARP's Legal Counsel for the Elderly program. Laura recently shared her thoughts about the Fellowship and her work at AARP's Legal Counsel for the Elderly program.

NQ: What inspired you to apply for the Tax Section's Public Service Fellowship?

LN: During law school, I became really interested in community economic development and wealth creation for low and moderate income communities. Tax practice and tax theory are really interesting from a public service perspective, but unfortunately, there aren't that many venues for a legal aid attorney to pursue tax in their practice—especially in this economic environment. The Public Service Fellowship seemed like a great opportunity to explore my interest in tax and connect me to practitioners and theorists through its networking opportunities.

NQ: How did you come to choose AARP's Legal Counsel for the Elderly as your sponsoring organization?

LN: I clerked for AARP Foundation's consumer unit during the summer after my 2L year, and one of my supervising attorneys suggested I speak with the managing attorney at Legal Counsel for the Elderly to see if they would be interested in hosting my project.

NQ: What are the types of projects on which you're working?

LN: Currently my case load is primarily composed of real property tax foreclosure defense work, but I have also had the opportunity to work on some income tax issues including garnishments and refunds, as well as tax issues related to probate.

NQ: Can you give examples of the types of issues you deal with in providing tax assistance to low-income seniors?

LN: The vast majority of my clients are on limited fixed incomes, so any unexpected event (usually health-related crises for my clients), puts my clients in untenable financial situations that their monthly income may not necessarily reflect. This can be an issue in negotiations and litigation.

NQ: What have been your biggest challenges in the position?

LN: The biggest challenges for me have mainly related to just being a new attorney and having the confidence in myself to really advocate for my clients based on my own assessment of each individual case, rather than rely solely on someone else's opinion. My employer has displayed trust in me from the beginning, and I have been fortunate in that I have been given tremendous opportunities as a new attorney, but I've really had to learn to pay attention to my reactions as I process information and to trust my instincts.

NQ: What are the most rewarding experiences you've had during the Fellowship?

LN: Working with clients and having control over the direction of my cases has been incredibly rewarding.

NQ: What, if any, influence has your Fellowship work had on your career plans?

LN: My Fellowship has given me the freedom to explore tax work exclusively as a legal aid attorney, which I very likely would have been otherwise unable to do. As a result, the Fellowship has given me confidence to pursue a public service career with a tax focus.

NQ: Do you have any advice for other lawyers or law students who may be interested in public service or pro bono work?

LN: I think it is really important to talk to people currently doing related work. Before I applied for this fellowship, I emailed and called people I thought I could learn from. Since tax is such a niche practice in the public service arena, I found that people were willing to spend time to talk with me about what they do, which helped give me a better sense of what I could expect and what I wanted in my practice.

NQ: You have attended several Tax Section meetings. Have they helped you in your work?

LN: The Tax Section meetings have been excellent educational and networking opportunities. It has been a great forum for meeting people doing work that I am interested in as well as an opportunity for me to learn from experienced practitioners.

NQ: Do you have any immediate plans after the Fellowship?

LN: I hope to stay with Legal Counsel for the Elderly continuing the work that I am currently doing, but that will depend on funding. ■

continued from page 1

purpose. For instance, interest payments on debt are deductible; payments on equity are not. All else being equal, section 163 generally encourages corporations to incur debt at the expense of equity. A business taxpayer may choose to invest in a foreign country, if only to generate foreign source income to use up expiring foreign tax credit carryforwards. Most simple transactions based on these provisions rate a spot on an Angel List—setting aside the sometimes tricky question of who owns the tax benefits.

Next year dividends will be taxed at a higher rate than capital gains (unless Congress acts). If pressed, a closely-held corporation that redeems outstanding shares for cash might struggle to satisfy the Service or a court that there was a non-tax reason for the share buyback, as opposed to a dividend. A taxpayer may trigger a capital loss solely to offset an unrelated capital gain. All of these classes of transactions—and plenty more—are strong candidates for an Angel List.

And those are just the Code-based transactions. Consider the legions of regulations and rulings that bless transactions where tax benefits drive the economics. Some of the best examples can be found in and among the elective entity regulations. There is almost no reason other than tax planning for an entity to "check the box." *E.g.*, Rev. Rul. 2003-125, 2003-2 C.B. 1243. Published guidance reveals other transactions that were structured just so in order to obtain favorable federal tax benefits. *E.g.*, Rev. Rul. 98-27, 1998-1 C.B. 1159 (transitory subsidiary respected under section 355); TAM 9748005 (leased airplane has two tax owners). All of these tax-motivated transactions—which currently work—would probably fail the subjective intent prong of the newly-codified economic substance test, if the test applied.

Finally, courts have held in favor of the taxpayer on many tax-advantaged transactions. The Supreme Court has upheld tax-driven sale-leasebacks (*Frank Lyon*) and tax-motivated debt-for-debt exchanges (*Cottage Savings*). In *John Kelley Company*, a classic debt-equity case, the court of appeals called the transaction at issue "a matter of accounting hocus-pocus, guided by a little too clever legal planning which eventuated in a rather flimsy scheme to avoid paying of taxes." *Commissioner v. John Kelley Co.*, 146 F.2d 466, 468 (7th Cir. 1944). But the Supreme Court reversed, holding for the taxpayer. 326 U.S. 521 (1946). Many other examples abound in the lower courts as well.

In short, an innumerable company of tax-advantaged transactions deserve to be on an Angel List, at least in some form or another. And each transaction turns on its own facts, with differences that could not possibly be collected and indexed.

Where Angels Fear to Tread

Even if a comprehensive list of acceptable tax-minimization transactions could be drafted, the Service and Treasury would have little incentive to publish one. With a published list, fools could rush in where angels now fear to tread. Many elements of tax law are uncertain, and the government benefits from this uncertainty (taxpayers do too, in some cases). Most rational taxpayers do not court expensive tax litigation with the Service, especially when a transaction without economic substance may now attract a strict-liability penalty of up to 40%. The raw economics of the penalty provisions means that many taxpayers will not enter into close-call transactions, which, of course, was a major reason for Congress to codify the economic substance doctrine in the first place. An Angel List (basically a set of rules) would undercut the *in terrorem* effect of the more general economic substance standard with penalties.

Instead of publishing an Angel List, the Service and taxpayers will have to build, together, a body of fresh experience around the codified economic substance provision. Of course, this process will take time. An example from another context shows how long we may have to wait. Treasury and the Service issued partnership anti-abuse regulations in 1994, but we waited until April 2010—16 years—for the government to win a case on the regulations. *Nevada Partners Fund, LLC ex rel. Sapphire II, Inc. v. United States*, 2010 WL 1795618, 105 A.F.T.R.2d 2010-2133 (S.D. Miss. April 30, 2010). This was no accident. The government only tentatively argues the partnership anti-abuse regulations. A loss hurts the government much more than the long-delayed win ended up helping the government—if it helped at all.

The government should do the same thing with the economic substance doctrine, arguing it carefully, selectively, and only as a last resort. It would help if the Service issued guidance explaining its procedures for asserting the doctrine and imposing penalties. Furthermore, the government should start with the most egregious cases, and only then work slowly back towards the middle. If a court determined that the economic substance doctrine was not "relevant"—the key word—to a close-call transaction (or reframed the Service's perspective of "the transaction") a taxpayer win might undercut the broader vitality of the doctrine.

Dancing on the Head of a Pin

Economic substance codification leaves us with hard questions that Treasury and the Service probably do not want to answer in a vacuum. Professor Joseph Bankman—a respected academic—called economic substance "dizzyingly complex" in *The Economic Substance Doctrine*, 74 S. CAL. L. REV. 5, 29 (2000). And codification did not clarify the doctrine as much as Congress might have liked. As Professor Bankman points out, the test asks a series of open-ended and unanswerable questions, and it

must apply to a wide variety of business activities and transactions, in a world with inconsistent and sometimes incoherent tax rules. *Id.* All of this complexity is still with us, and codification raises new questions.

First, as mentioned above, the new economic substance test applies to transactions only if the economic substance doctrine is "relevant." What does relevant mean in this context? Surely it cannot carry its expansive meaning over from Federal Rule of Evidence 401: "'Relevant evidence' means evidence having any tendency to make the existence of any fact that is of consequence to the determination of the action more probable or less probable than it would be without the evidence." For one thing, the economic substance doctrine is not a fact; it is an interpretative tool. Second, almost every tax position is more probable or less probable in light of the economic substance doctrine, which would mean that the doctrine is relevant in almost all cases, at least in the Rule 401 sense of the word. That cannot be. With codification, Congress did not hand the Service a unilateral option to invoke the codified economic substance doctrine in all cases, without supervision from the courts.

And the relevance determination "shall be made in the same manner as if this subsection had never been enacted." I.R.C. § 7701(o)(5)(C). This sentence means that if the government would not have made or won an economic substance argument before—at least under the old majority conjunctive standard, the codified version—it should not now, either. That makes sense. But does that mean that the current state of the law will be frozen forever, at least on the economic substance issue? For instance, could Treasury and the Service modify the check-the-box rules and attack choice-of-entity planning using the economic substance doctrine in the future, or does section 7701(o)(5)(C) foreclose that option? Put differently, should the Service hope for a different result if it re-litigated the check-and-sell issue presented in *Dover Corporation & Subsidiaries v. Commissioner*, 122 T.C. 324 (2004)?

It is plain enough that Congress resolved the lopsided circuit split on whether the general economic substance doctrine presents a conjunctive or a disjunctive test. A harder question is whether the new, uniform standard effectively overrules cases other than *Rice's Toyota World, Inc. v. Commissioner*, 752 F.2d 89 (4th Cir. 1985). For instance, under existing common law, purely tax-motivated interest deductions have economic substance if the taxpayer incurred the challenged debt to engage in "purposive activity." *Goldstein v. Commissioner*, 364 F.2d 734, 741 (2d Cir. 1966). Is that test now gone, replaced by the tougher codified standard? Likewise, has Congress implicitly overruled the lenient standard set out in *Northern Indiana Public Service Co. v. Commissioner*, 115 F.3d 506 (7th Cir. 1997), *aff'g* 105 T.C. 341 (1995)? In *NIPSCO*, the court refused to disregard a subsidiary created for tax-reduction purposes because the subsidiary conducted minimal substantive business activity. At the very least, taxpayers will continue to argue that the codified economic substance doctrine is not relevant to certain tax-driven business refinancing or reorganization cases, and courts may well agree.

Finally, what does codification mean for the various other common-law, regulatory, and statutory anti-abuse doctrines and rules? The phrase "economic substance doctrine" was not used by a court until *Georgia Cedar Corp. v. Commissioner*, T.C. Memo. 1988-213. But *Georgia Cedar* is just one in a long line of cases where the court based its decision on the substance, rather than the form, of the challenged transaction. The new section 6662(b)(6) strict liability penalty provision applies to "any disallowance of claimed tax benefits by reason of a transaction lacking economic substance …or failing to meet the requirements of any similar rule of law." Other similar rules of law might include step-transaction, substance-over-form, and sections 1.165-1(b), and 1.701-2(e) of the Income Tax Regulations.

Conclusion

In summary, the Service will want to consider how broadly it asserts the economic substance doctrine and its strict liability penalty with the benefit of real cases and real facts. Rather than arguing over the terms of the standard, taxpayers and the Service will now redouble their efforts on properly framing the transaction at issue. Taxpayers will want to broaden the perspective to place the transaction in its business context, while the Service will bear down on the technical tax planning. Penalties raise the stakes, as they always do. And we will continue to live with uncertainty. "The truth I shall not know, but live in doubt, Till my bad angel fire my good one out." William Shakespeare, *The Passionate Pilgrim*, Poem II. ■

ABA Section of Taxation CLE Calendar

www.abanet.org/tax/calendar

DATE	PROGRAM	CONTACT INFO
August 4, 2010	**Be Prepared: A [Scout's] Guide to the Coming Regulation of Federal Tax Return Preparers** CLE Teleconference & Live Audio Webcast	Tax Section www.abanet.org/tax 202/662-8670
August 5-10, 2010	**ABA Annual Meeting – Cosponsored Programs** Moscone Center West – San Francisco, CA	ABA Meetings and Travel www.abanet.org/annual/2010 800/285-2221
August 6, 2010	**Drafting an LLC Agreement to Fully Protect Your Client** *Primary Sponsor: Section of Real Property, Trust & Estate Law*	
August 6, 2010	**Entity Selection, Fringe Benefits and Retirement Plans for the Closely Held Business and Practice** *Primary Sponsor: Section of Taxation*	
August 6, 2010	**Making the Business Case for Diversity and Inclusion** *Primary Sponsor: Business Law Section*	
August 6, 2010	**Solo Day: Practicing the Practice of Law – Part I** *Primary Sponsor: General Practice, Solo and Small Firm Division*	
August 6, 2010	**Solo Day: Practicing the Practice of Law – Part II** *Primary Sponsor: General Practice, Solo and Small Firm Division*	
August 7, 2010	**Doing Deals in a Rapidly Changing Tax Environment: 2011 Rate Changes, New Strict Liability Penalties and Attacks on Privilege** *Primary Sponsor: Business Law Section*	
August 7, 2010	**Taxes and Bankruptcy: Consumer and Business Issues** *Primary Sponsor: General Practice, Solo and Small Firm Division*	
August 7, 2010	**Keeping up with the Competition and Keeping the Taxman at Bay: Employment Contracts, Severance Agreements and Sec. 409A** *Primary Sponsor: General Practice, Solo and Small Firm Division*	
August 7, 2010	**Retirement Security: Is This What's Next After Health Care Reform?** *Primary Sponsor: Section of Labor & Employment Law*	
August 8, 2010	**Health Care Reform: What Employers Need to Know Now!** *Primary Sponsor: Section of Labor & Employment Law*	
August 11, 2010	**Update on the Ongoing National Research Program Examinations** CLE Teleconference & Live Audio Webcast	Tax Section www.abanet.org/tax 202/662-8670
August 18, 2010	**Entity Selection, Fringe Benefits and Retirement Plans for the Closely Held Business and Practice** CLE Teleconference & Live Audio Webcast	Tax Section www.abanet.org/tax 202/662-8670
Sept. 30-Oct. 1, 2010	**ALI-ABA Course of Study: Consolidated Tax Return Regulations** Hilton Washington Embassy Row – Washington, DC	ALI-ABA www.ali-aba.org 800/CLE-NEWS
October 21-22, 2010	**ALI-ABA Course of Study: Tax Exempt Charitable Organizations** Washington Marriott at Metro Center – Washington, DC	ALI-ABA www.ali-aba.org 800/CLE-NEWS
October 26-27, 2010	**21st Annual Philadelphia Tax Conference** Union League of Philadelphia – Philadelphia, PA	Tax Section www.abanet.org/tax 202/662-8670

In Remembrance: Martin D. Ginsburg, 1932 – 2010

On June 27 the Section and the tax law community lost a longtime friend, leader, and colleague, Martin D. Ginsburg. Marty served on the Section Council from 1984 to 1987 and received the Section's highest award, the Distinguished Service Award, on May 5, 2006. His remarks from that day were subsequently published in the Summer 2006 issue of the *NewsQuarterly* and are reprinted here to honor his memory. To paraphrase from an essay by Pam Olson, which also appeared in the Summer 2006 issue, "Marty gave selflessly of his time, intellect, and talent. In doing so, he set an example to which all of us—especially those who benefited from his tutelage—can aspire." *–Ed*.

My very old friend Dick Loengard—we began law school together more than 50 years ago—called me to remind that at breakfast one ought not talk too long. With that excellent thought in mind, Dick proposed I speak this morning on "The Progress of Tax Simplification in My Lifetime." It would have been a very short speech. I am flattered and delighted to receive the Tax Section's Distinguished Service Award. Every prior recipient has been richly deserving. This year's selection committee, great numbers of you suspect, was drinking heavily at the selection lunch. Initially I thought so too. A disproportionate part of my professional life has been devoted to protecting the deservedly rich from the predations of the poor and downtrodden, and it is not easy to see why that deserves a medal.

But it came to me that over a fairly long life I have performed one distinguished service. I propose to use my short time this morning to recall the highlights and claim undue credit. And as this not-previously-public story involves my spouse and home and family life, I shall start there. In the 1960s I practiced law, mainly tax law, in New York City, and Ruth began her law teaching career at Rutgers Law School in Newark. One of the courses she taught was Constitutional Law, and toward the end of the decade she started looking into equal protection issues that might or might not be presented by statutes that differentiate on the basis of sex—a dismal academic undertaking because, back then, the United States Supreme Court had never invalidated any legislative classification that differentiated on the basis of sex.

Then, as now, at home Ruth and I work evenings in adjacent rooms. In my little room one evening in fall 1970, I was reading Tax Court advance sheets and came upon a pro se litigant, one Charles E. Moritz, who on a stipulated record was denied a $600 dependent care deduction under old section 214 even though, the Tax Court found, the operative facts fit the statute perfectly. Mr. Moritz was a traveling salesman for a book company, his 89-year-old dependent mother lived with him, and, in order to be gainfully employed, during the year he paid an unrelated individual at least $600 to take care of old mother whenever Charles was at work.

There was just one small problem, and in the Tax Court it served to do him in. The statute awarded its up-to-$600 deduction to a taxpayer who was a woman of any classification (divorced, widowed, or single), a married couple, a widowed man, or a divorced man. But not to a single man who had never been married. Mr. Moritz was a single man who had never married. "Deductions are a matter of legislative grace," the Tax Court quoted, and added that if the taxpayer is raising a constitutional objection, forget about it: everyone knows, the Tax Court confidently asserted, that the Internal Revenue Code is immune from constitutional attack.

I went next door, handed the advance sheets to my wife, and said, "Read this." Ruth replied with a warm and friendly snarl, "I don't read tax cases." I said, "Read this one," and returned to my room.

No more than five minutes later—it was a short opinion—Ruth stepped into my room and, with the broadest smile you can imagine, said, "Let's take it." And we did.

Ruth and I took the *Moritz* appeal pro bono, of course, but since the taxpayer was not indigent we needed a pro bono organization. We thought of the American Civil Liberties Union. Mel Wulf, the ACLU's then legal director, naturally wished to review our proposed 10th Circuit brief—which in truth was 90% Ruth's 10th Circuit brief—and when he did he was rightly bowled over.

A few months later the ACLU had its first sex discrimination/equal protection case in the United States Supreme Court—as many of you will remember it was titled *Reed v. Reed.* Recalling *Moritz*, Mel asked Ruth if she would write the ACLU's Supreme Court brief on behalf of Sally Reed. Ruth did and, reversing the decision below, the U.S. Supreme Court unanimously held for Sally. Good for Sally Reed and good for Ruth, who decided thereafter to hold down two jobs, one as a tenured professor at Columbia Law School where she had moved from Rutgers, the other as head of the ACLU's newly created Women's Rights Project.

Now back to *Moritz*. The 10th Circuit found Mr. Moritz to have been the victim of an equal protection violation and reversed the Tax Court. The Government, amazingly, petitioned for certiorari on the asserted ground that the 10th Circuit's decision cast a cloud of unconstitutionality over literally hundreds of federal statutes that, like Code section 214, contemplated differential treatment on the basis of sex.

In those pre-personal computer days, there was no easy way for us to test the Government's assertion, but the Solicitor General—Erwin Griswold, whom many of you will recall—took care of that by attaching to his petition a list—generated

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News Briefs

Thank You to VITA Volunteers

We know that many members of the Tax Section generously donate their time and energy to assisting taxpayers through the IRS Volunteer Income Tax Assistance (VITA) program each year. The programs provide a great service to low-to-moderate income taxpayers who need tax return preparation assistance.

In the 2009 filing season, the Section sent a special invitation to our members, inviting you to volunteer with VITA in your communities. We heard from nearly 90 members—and many of you were participating in VITA programs for the first time. Thank you for your help; we hope that you will continue to contribute to VITA in the future as well.

We'd like to especially thank the individuals who assisted the Military VITA 'Train the Trainer' program this filing season in Washington, D.C. The following volunteers traveled to Ft. Belvoir and Andrews AFB to train 190 military personnel, who assisted in completing nearly 4,500 income tax returns for military families in the Washington, D.C. area. Many thanks for your time and effort!

Marc Clayton, *Lockheed Martin*
Ronald Cluett, *Caplin & Drysdale Chtd.*
Catherine Engell, *DLA Piper*
Brandon Hadley, *Dewey & LeBoeuf*
Kevin Jacobs, *Ropes & Gray*
Keith Kost, *Pillsbury Winthrop Shaw Pittman LLP*
Keith Sieverding, *Steptoe & Johnson LLP*

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The American Bar Association of Taxation is pleased to announce that the application period for its Public Service Fellowship program for 2011 is now open. Applications must be received by October 4, 2010, to be considered. Applicants selected for interviews will be invited to attend the Section's meeting in Boca Raton on January 20-22, 2011, and asked to participate in interviews on January 22, 2011. For more information about the ABA Tax Section Public Service Fellowships, please visit http://www.abanet.org/tax/awards/publicservice.

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by the Department of Defense's mainframe computer—of those hundreds of suspect statutes. Cert. was denied in *Moritz*, and the computer list proved a gift beyond price. Over the balance of the decade, in Congress, the Supreme Court, and many lower courts, Ruth successfully urged the unconstitutionality of those statutes.

So Mr. Moritz's case mattered a lot. First, it fueled Ruth's early 1970s career shift from diligent academic to enormously skilled and successful appellate advocate—which in turn led to her next career on the higher side of the bench. Second, with Dean Griswold's help, *Moritz* furnished the litigation agenda Ruth actively pursued until she joined the D.C. Circuit in 1980. All in all, great achievements from a tax case with an amount in controversy that totaled exactly $296.70.

In bringing those Tax Court advance sheets to Ruth 36 years ago, I changed history. For the better. And, I shall claim, thereby rendered a uniquely distinguished service. I have decided to believe it is the service for which you have given me this great award. And even if you had something a little less cosmically significant in mind, I am immeasurably grateful to be so greatly honored by my peers. ■

BOXSCORE

Since April 2010, the Section has coordinated the following government submissions, which can be viewed and downloaded free of charge from the Section's website at www.abanet.org/tax/pubpolicy.

Submissions and Comments on Government Regulations, Administrative Rulings, Blanket Authority, and ABA Policy*

TO	DATE	CODE SECTION	TITLE	COMMITTEE	CONTACT
Internal Revenue Service	5/28/2010	n/a	Comments on Announcements 2010-9, 2010-17 and 2010-30	Administrative Practice, Standards of Tax Practice	Thomas J. Callahan
Internal Revenue Service	5/26/2010	355(b)	Comments on Proposed Regulations Regarding the Active Trade or Business Requirement Under Section 355(b)	Corporate Tax	Steven Flanagan, Derek Cain, and Brandon Hayes
House Committee on Ways & Means, Senate Committee on Finance	5/11/2010	n/a	Letter Regarding H.R. 2834 with Respect to H.R. 4213	Partnerships and LLCs	Helen Hubbard
Internal Revenue Service	5/6/2010	901	Comments on Proposed Regulations Regarding the Section 901 Compulsory Payment Requirement	Foreign Activities of U.S. Taxpayers	Dirk Suringa
Internal Revenue Service	4/30/2010	409A(a)	Comments on Relief and Guidance on Corrections of Certain Failures of a Nonqualified Deferred Compensation Plan to Comply with Section 409A(a)	Employee Benefits	Althea R. Day and Eleanor Banister
Internal Revenue Service	4/28/2010	301	Comments on Proposed Regulations Regarding Allocation of Consideration and Allocation and Recovery of Basis in Transactions Involving Corporate Stock or Securities	Corporate Tax	Neil Barr
Internal Revenue Service	4/27/2010	509(a)(3)	Comments on Proposed Regulations Under Section 509(a)(3) Regarding Type III Supporting Organizations	Exempt Organizations	LaVerne Woods
Internal Revenue Service	4/19/2010	409A	Comments on Notice 2008-115 Reporting and Wage Withholding Requirements with Respect to Amounts Includable in Income Under Section 409A	Employee Benefits	Wayne R. Luepker and Eleanor Banister
House Committee on Ways & Means, Senate Committee on Finance	4/15/2010	901(b), 2210(a), 2664, and 6166	Letter Regarding Hearings on Federal Wealth Transfer Taxes	Section of Taxation and Section of Real Property, Trust and Estate Law	Helen Hubbard
House Committee on Ways & Means, Senate Committee on Finance	4/6/2010	1374	H.R. 4169 – Technical Correction to ARRA Change in Section 1374 Built-In Gain Tax	S Corporations	Helen Hubbard
House Committee on Ways & Means, Senate Committee on Finance	4/5/2010	2210(a) and 2664	Reform of Federal Wealth Transfer Tax	Estate and Gift Taxes	Helen Hubbard
House Subcommittee on Financial Services and General Government, Senate Subcommittee on Financial Services and General Government	4/5/2010	n/a	Letter Regarding Internal Revenue Service Funding and Comments on Proposed Funding for Assistance to Low-Income Taxpayers**	Section of Taxation	Helen Hubbard

*The technical comments and blanket authority submissions listed in this index represent the views of the ABA Section of Taxation. They have not been approved by the ABA Board of Governors or the ABA House of Delegates and should not be construed as representing the policy of the ABA.

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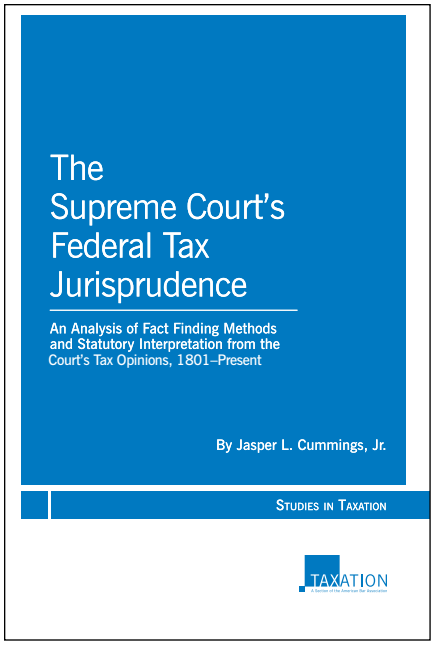

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