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Section of Taxation
NEWSQUARTERLY

## POINTS TO REMEMBER

# What Is the Value of a "Should" Opinion?

By Kathryn Morrison Sneade*

## Canal Corporation v. Commissioner

The Tax Court's August 2010 decision in *Canal Corporation v. Commissioner*, and in particular, its imposition of penalties under section 6662 despite the taxpayer's receipt of a "should" opinion from PricewaterhouseCoopers (PwC) has attracted significant commentary, much of it negative, in the blogosphere. The Tax Court (Judge Diane L. Kroupa) recharacterized the contribution of assets and liabilities by a Canal Corporation subsidiary to a newly formed limited liability company and the simultaneous receipt of a $755 million distribution under the disguised sale rules of section 707(a)(2)(B) and held that Canal Corporation was liable for a penalty of over $36 million with respect to the resulting understatement. PwC had been Canal Corporation's financial statement auditor and tax preparer for many years, assisted in negotiating and structuring the transaction, and then finally prepared the "should" opinion for the transaction that occurred in 1999.

## Scrutiny of the Fixed Fee

Critics homed in on a couple of details they found particularly problematic. In particular, they discussed the court's focus on the $800,000 fixed fee PwC received for its opinion. PwC's opinion (submitted into evidence in draft form) was, according to the court, so littered with typographical errors, so poorly organized, and so lacking legal support that the court concluded that the opinion, in light of the substantial fee, more resembled "a *quid pro quo* arrangement than a true tax advisory opinion." 135 T.C. No. 9, at 38 (emphasis added). Commentators have observed that lawyers do not always charge an hourly rate, and some clients may prefer to negotiate a fee for the job rather than pay a lawyer at an hourly rate. They have wondered, does this mean that all opinions for which there is a flat fee will be suspect?

This outrage seems disingenuous. A judge (or any person, really) naturally will inquire whether what was received was worth what was paid. When the fee paid is so dramatically larger than the fee that normal hourly-rate billing would have produced, one wonders whether what is being acquired is something more than the ordinary service. Why else would one pay the premium? In *Canal Corporation*, the court posited that the advisory opinion was an "insurance policy," and the protections provided by that insurance policy justified the high fee. Commentators have suggested that the section 6662 penalty is not appropriate in a situation where a taxpayer has a "should" opinion from a well-regarded tax advisor, at least if the transaction has economic substance (within the meaning of section 7701(o)). They seem to buy into this idea of an insurance policy. But, as in a number of other cases in which the taxpayers held "should" opinions from reputable tax advisors, the judge in *Canal Corporation*

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|---|---|---|
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| February 16-18, 2012 | MIDYEAR MEETING | Manchester Grand Hyatt – San Diego, CA |
| May 10-12, 2012 | MAY MEETING | Grand Hyatt – Washington, DC |
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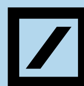

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## FROM THE CHAIR

# A Renewed Call for Tax Simplification

By Charles H. Egerton*

As I write this column, President Obama's National Commission on Fiscal Responsibility and Reform (the "Fiscal Commission") has just issued its report. Although the report failed to garner the required supermajority approval of the Fiscal Commission, its recommendations have nevertheless served the salutary purpose of focusing public attention and debate on the need to reform the nation's tax laws.

The Fiscal Commission's recommendations include the elimination of a large portion of the tax expenditures that have been woven into the fabric of the Code over the years. These tax expenditures have, in part, eroded both the efficiency and fairness of the tax system and contributed substantially to the almost inscrutable complexity of today's version of the Code.

The primary objective of the Fiscal Commission was to restore fiscal responsibility to our government in a time of ballooning national debt and a looming problem with the cost of entitlements as the baby boomer generation begins to retire. However, if prior tax reform efforts are a reliable guide, implementation of all or even a significant portion of the Commission's recommendations will most likely result in a pitched and prolonged battle that can be won only with strong leadership from both the executive and legislative branches. Every tax expenditure has a vocal and well-funded constituency that will quickly assemble an army of lobbyists to protect and preserve its favored treatment under the Code. Tax simplicity, on the other hand, has no natural constituency to support its cause. For over 30 years, the Tax Section has been the only constant, vocal proponent for tax simplification.

The Fiscal Commission's focus on retooling our tax laws as a primary means for achieving its fiscal reforms presents an opportunity for the Tax Section to renew its plea for simplification of the Code. The Section has a long-standing policy of support for simplification of our nation's tax laws. In 2009, the Section issued a white paper setting forth its call for tax simplicity, stability, and transparency. In obvious reference to the bent of Congress over the past 30 years to use the Code as a means to achieve economic and social ends, the white paper offers the following observation:

> Simplicity in income taxation requires an over-arching bias against delivery of rewards and punishments through the tax system. The core, preferred approach should be an income tax base focused on the measurement of economic income, with due regard for ease of compliance, ease of administration, economic efficiency, and similar treatment for similar taxpayers.

American Bar Association Section of Taxation, *Statement of Policy Favoring Tax Simplicity, Stability, and Transparency*, *available at* http://www.abanet.org/tax/pubpolicy/papers/whitepaper_sopfavoringtaxsimplicitystabilityandtransparency.pdf.

As a corollary to its call for simplification, the Section also has advocated that any comprehensive overhaul of the Code should include a thoughtful and comprehensive review of the entire federal civil tax penalty regime. The Tax Section issued a white paper on this topic in 2009 (American Bar Association Section of Taxation, *Statement of Policy Favoring Reform of Federal Civil Tax Penalties*, *available at* http://www.abanet.org/tax/pubpolicy/papers/whitepaper_sopfavoringreformoffederalciviltaxpenalties.pdf), and has issued a number of related reports which are referenced in the white paper. The Joint Committee on Taxation also issued an excellent three-volume report in April 2001 containing numerous suggestions for simplifying the tax laws. Joint Committee on Taxation, *Study of the Overall State of the Federal Tax System and Recommendations for Simplification, Pursuant to Section 8022(3)(B) of the Internal Revenue Code of 1986* (JCS-3-01) (April 2001), *available at* http://www.jct.gov (Publications tab). These studies as well as numerous other published reports and recommendations provide a wealth of groundwork to support any serious effort toward simplification of the Code.

President Obama has announced that he will issue a call to Congress in the coming year to reform our tax laws, perhaps in part along the lines recommended by his Fiscal Commission. A number of leaders of both political parties have also voiced support for various aspects of the Fiscal Commission's recommendations. Although the Tax Section should not embroil itself in partisan politics as the debate begins, it nevertheless provides us with an opportunity to renew our plea for tax simplification. This will most likely be a limited window of opportunity, and I urge the Section to be prepared to add our voice to those of others who seek to achieve a simpler, fairer, and more transparent tax system. ■

*Dean, Mead, Egerton, Bloodworth, Capouano & Bozarth, P.A., Orlando, FL.

INTERVIEW

# The Hon. Dan Rostenkowski

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

**Authors' Note:** Dan Rostenkowski died August 11, 2010. The interview below, reprinted from the Section of Taxation *Newsletter*, Winter 1996 issue, took place in a back office of an Illinois State legislator in Chicago shortly before Mr. Rostenkowski entered prison. That brief visit was enough to explain to the interviewers why he was such a well liked and powerful congressman: he was charming, friendly, seemingly humble, and smart. We genuinely liked Dan and he seemed to delight in telling the stories of the TRA 86, about which we had also recently interviewed Bob Packwood. Congress now faces the possibility of another dramatic rewriting of the Internal Revenue Code. Therefore it may be useful to be reminded how one of the principal actors in the last major Code revision viewed the process. As the nation faces another possible round of "tax reform," we can wish for another Dan Rostenkowski. But, alas, those were gentler times, believe it or not.

The Honorable Dan Rostenkowski served as Chairman of the Committee on Ways and Means, United States House of Representatives, 1981-1994. Mr. Rostenkowski was first elected to Congress in 1958 from the 8th District of Illinois. Before assuming Chairmanship of the Ways and Means Committee, Mr. Rostenkowski held numerous House Democratic leadership positions, including Chairman of the Democratic Caucus (90th and 91st Congresses) and Chief Deputy Majority Whip (95th and 96th Congresses). Mr. Rostenkowski was a member of the Illinois General Assembly, 1952-1954, and the Illinois Senate, 1954-1958. Mr. Rostenkowski attended Loyola University, 1948-1951, and served with the 7th Infantry Division, United States Army, 1946-1948.

**Q Many view the Tax Reform Act of 1986 as one of your major legislative achievements. Could you comment on how you got this legislation accomplished?**

A It's a pleasant reflection, now that we're in the year 1995. But in 1986, I don't think that a lot of people ever thought that they were going to see a tax bill. I often remark that the '86 Tax Bill is one piece of legislation that had a lot of wakes but never a funeral. It was a peak-and-valley experience because so many times everybody thought that it was all over.

The first turnaround that I had was the beginning of why there was a book written about Tax Reform.[1] One of the first items up before my Committee involved banks' bad debt reserves. And—in one of the first days of negotiations—they beat me so badly it was pitiful.[2] That happened in the morning.

That afternoon two of my colleagues who were sponsors of this came to see me. They said "You know, we'll move to reconsider."[3]

And I thought about that for a while, and I said, ''No, I don't think so. We're not going to take that up."

My staff was excited about the offer. "Mr. Chairman, we can do this. The Members will change their vote,"—because bad publicity was starting to evolve.

That's when I said, "No, we'll get all those people with their Gucci shoes and those pin-stripe suits. We'll let them suffer a little bit." And I did not reconvene the Committee for about seven days.

In the meantime, the unpopular bankers were getting slashed in the press. So much so, that, when we did reconvene the Committee, I think we had set the tone with the Membership: "If you're serious about eliminating tax shelters and loopholes, we can write a bill. But if you don't want to eliminate shelters, you're going to have to stand up to the public's ire and the press's investigations."

I think that was probably the first step in the direction of really working out a bill.

**Q How about your working relationship with President Reagan during this process?**

A Before we started, I went to see President Reagan. It was really a great experience. I said to Don Regan, who was Chief of Staff to the President, "I'd like to see the President."

He said, "Oh, well, I don't know that we can arrange that."

I knew Don Regan as Secretary of Treasury, and I like Don. I think he's a

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1 Jeffrey H. Birnbaum and Alan S. Murray, *Showdown at Gucci Gulch*, Random House, New York, 1987.

2 In one of its first votes on Tax Reform, the Ways and Means Committee voted to delete the Chairman's recommended cut-back of deductions for banks' bad debt reserves.

3 This means they offered to re-open the bank vote, which they were permitted to do because they had originally voted on the prevailing side.

wonderful guy. I said, "Don, I want to talk to the President. I'm not coming up there with any complicated memoranda. I just want to sit down. I want the President to know who he's dealing with."

Don Regan said, "Well, he knows *you*, by God."

I said, "Don, please let me get in to see the President."

He said, "Well, what is it about?"

"It's something that I want to talk to the President about."

He said, "Well, could I get an idea?"

"It's nothing complicated. I want 15 minutes."

"Well, Dan, I don't know. The President's going to Bittburg and we're trying to prepare him."

I said, "Don, do me a favor. Get up tomorrow morning and watch The Today Show, because I am going to be on The Today Show and I am going to tell the American people that here is the chief forecaster for where the country could be going in the tax reform process and I can't get in to see the President of the United States."

Regan said, "You wouldn't do that to me."

And I said, ''Well, Don, I'm telling you."

And he said, "Listen, slow down, I'll get you in to see him."

At any rate it was funny, because I went in the diplomatic entrance and they had me go through the back door. I went into his private quarters and I said to the President, "Mr. President, I don't know how serious you are about wanting Tax Reform, but if you want to really revise the Code, then I'll work with you. And if I can get you to agree with certain principles that I'll lay down, I'll do it. I don't know how successful we'll be. But the big thing is that I have to have a commitment from you."

And he said, "Well, Dan, what kind of a commitment do you want?"

I said, "I want you to promise me that you will not expose yourself to questions from the press about particular parts of the bill. That you will say, 'I will wait until the bill is completed and then I'll make a judgment.'"

And he said, "Why's that?"

"Mr. President, if there is something in the bill in the beginning of the mark-up, it doesn't necessarily mean that it's going to be in the bill in the end of the mark-up. But if you're going to say, 'I'll veto that' right at the beginning, then school's out—no bill! If, however, you'll say, 'I'm going to wait until I see a bill in its completed form and then I'll make a judgment as to what I'm going to do with it,' then we can work."

He put his hand out and we shook hands, and he said ''You will have my fullest cooperation. You call me any time you need me— I'll be there. I want to see a bill."

Now the President didn't say "the Administration's" fullest cooperation. He said "my" fullest cooperation.

I can still remember the President sitting there and saying, "Well, you're from Illinois aren't you, Dan?"

And I said, "Yes, Sir."

"Well, you know I was born and raised in Illinois." And he got to telling me about all of his experiences in the union that he headed. He loved to talk about the Screen Actors' Guild. And during this part of the conversation, Don Regan must have opened the sliding doors to the private quarters three times. And the President—whom I was committed to have 15 minutes with, and we were at 45 minutes by then—kept saying, ''Not yet, Don. Not yet, Don."

I don't know if I can put into words the association that I had with Don. Don Regan's a good friend, a decent person, determined and very disciplined. As I walked out, he said, "What the hell were you talking about with the President?" "You'll find out," I said.

He said, "You son of a gun."

At any rate, that was kind of that attitude that I had with the Administration. I could rib them. I could tease them. They knew that I wanted to write law and history. I knew that they wanted the credit to fall on the President of the United States. And I was never so selfish that I thought that it would be a Rostenkowski bill. The President has the pen and he has the Rose garden. Once the President goes into that Rose garden and signs that bill—it's the Reagan Administration proposal.

And I was never jealous of that. I figured that in the '86 Act I was going to prove that I could be Chairman of the Ways and Means Committee. Because I had some failures—failures in that I didn't have a united Democratic front in '81, or in '82. But, in '86 I had to prove we could get a bill out of the Committee on Ways and Means and through the House of Representatives, and get it over to the Senate.

**Q How important was public input to the process?**

**A** I think if there was anything critical that we convinced Members of the Ways and Means Committee that we had to do, it was to go into executive session.[4] It's not that you want to ignore the public. It's just that the lobbyists, the pressure groups, the trade associations—they have all their pet projects. If you put together something in public, the Members are looking over at the lobbyists, and the lobbyists are giving the "yes" and "no" signs.

I think the major stroke of writing legislation in executive session, and yet not have anybody feel that it was a covert operation, was that immediately after the day's session, we would have a press conference. I'd have the technical staff get up before the press and explain to them just what happened during that day's work. In my opinion, the press was better served by that activity than by sitting in the Committee room trying to interpret things for themselves, because the technical advisors and the people who draft the law will accurately explain what happened. There is a pride among both Members and staff that they accurately explain the intent of the law.

4 I.e., no public allowed.

Plus the fact that reporters aren't the most energetic people in the world, and they don't like to sit around all day waiting for a bit or a byte of news. This way they know that they can be doing something else and come back when the press conference is going to take place.

Now that was my idea, because I am a true believer in the fact that you can't really write law with everybody screaming and hollering in the room.

I'll never forget the first day that Jim Baker, who was then Secretary of the Treasury, walked into my office. "Danny," he said, "we'll get this bill done." This was after we reconvened in '85.[5]

And I said, "Jim, You're talking about this bill as though it was a conference report. This is the people's House, Jim. I'm going to take testimony on this for a month or two. I'm going to give everybody an opportunity to say what they have to say about it. And if you think it's a pleasure for me to be sitting in that Committee Room and taking all this testimony..."—because I always did that—"It's not. But, as Chairman, I don't want to be exposed to the claim that 'Rostenkowski isn't giving us an opportunity to be heard.'"

And that was why the health bill last year and the year before didn't go anywhere. The one thing as Chairman, in my opinion, is that you have to be patient and willing to listen. And I think, too, that if you're going to be talking to industry, to the financial giants in this country, to the corporate leaders, I think what you've got to do is assure them that—when the Chairman of the Committee says, "Tell me, what's your bottom line? What can you live with?"—if they tell you what their bottom line really is, then you will protect that confidence and you will try to work it out.

At that point in time, I think corporate America had a great deal of faith in me, and they would say, "Listen, Dan, we can do this," or "we can't do that."

5 The President sent "Tax Proposals for Fairness, Growth and Simplicity" to the Congress in early 1985.

I find the input that the business community makes, the lobbyists make, is not only necessary but extremely helpful. A good lobbyist is willing to come in and make his position known, and also tell you what the arguments against his position are. That's when I would become the court of appeals. That's when I would say, "Now wait a while, we're not going to injure this group of people. We don't want to do this," and go directly to the staff, to Joe Dowley when he worked for me, to Rob Leonard, to Janice Mays, and say "Listen, we're not in here to put people out of business." I mean, that's not the activity of government.

I think that this is the real job of a Member of the Ways and Means Committee, and it happens constantly. If I'm writing law and there are some unintended circumstances that are created by the law that I've written, I think that I have an obligation to come back in two years and have a technical corrections bill. I think we should be able to say, "Wait just a minute. This is unfair to this group of people," without the so-called discovery that Rostenkowski is "taking care of a constituency."

That is the madness in reporting today. The press wants to report so-called "smoke-filled rooms," and "midnight oil operations." That's very unfair. Because of this, we have not passed a technical corrections bill for several years. There are many, many people injured by this and it's wrong! Plus the fact that in the whole legislative process—not exclusively in the tax area—legislators have not really reinforced the steel in their tummies and taken the bitter pill and done the right thing by sacrificing a popular position in their congressional district.

**Q** **Rep. Archer says that we should "tear out the income tax system by its roots and throw it by the side of the road." Do you agree?**

**A** No. "Eliminate the tax code" is very popular to read. But what are the sacrifices that we are making? Where do we raise the revenue? What is the alternative?

**Q** **For a while after the defeat of Al Ullman, it looked as if the VAT was dead forever. Now there are a lot of VAT-type tax proposals. What do you think about the possibility of a VAT type tax?**

**A** I'd like to see the value added tax. With the world shrinking and trade becoming a large ingredient in our daily affairs, a value added tax is something that I think will come to pass. I think that it has a better chance than anything else at the present time.

By the way, my predecessor, Al Ullman, in my opinion was not defeated because he was for a value added tax. Al had other problems in his congressional district. One of them was that he didn't even have a residence there. People from Oregon just didn't appreciate that.

**Q** **Would you see the VAT as an add-on tax, or as a replacement of the income tax?**

**A** I think it would have to replace some type of tax, but I don't see it taking the place of the income tax. I just don't see how we can survive in this country without the fairness of an income tax. Whether we like it or not, sales taxes, purchase taxes, value added taxes—they're regressive as hell. And you know the legislative process. You give me in the beginning a 4% sales tax, and then that incrementally increases by a half penny, and then by a penny, and then by two cents. All that comes so easily with the legislative process, because it's hidden. And all of a sudden you're at 17, 18, 20 percent, and nobody really knows that it's happening, or how it happened.

**Q** Under the Republicans, the House has changed dramatically. Could you comment on the effects of this?

**A** I'm somewhat disappointed that the emphasis on the Committee structure isn't as great under the Gingrich Speakership as it was with the Democrats. I think the Committee system is a useful sifting process. Members don't get on Ways and Means in their first term. Members are around for two or three terms, and then they get on the Ways and Means Committee. So they have given up something else and they have learned the process.

The Gingrich leadership focuses on what they want to do, and Members of the Committees just rubber-stamp it. Now that's a two-edged sword: If you're a Chairman not willing to take responsibility for a particular piece of legislation, it's always nice to say, "Well, hell, the Speaker needs to do it."

But I don't know how long the Republicans are going to be able to control their Membership with such discipline. It's one thing, to have the discipline which Gingrich is enjoying for a short period of time, but that disintegrates. These new Members are going to have to come back and be accountable for what they are doing with respect to those billions in reductions in social services.

Members of Congress, when they loose their quality of leadership because they want to keep the job, are no longer effective. That's why the Committee system, I think, is so good. Without the Committee system, a lot of the issues that were taken to the floor of the House of Representatives in the last 20 years would never have even seen the light of day. They would not have been exposed on the floor to votes. Members on the floor want popular issues. The Committee structure protects them on the unpopular vote.

And, you know, I don't mean that governing is not always doing what your constituencies think is the right thing to do. Governing is looking at the long range effect of what your legislation is going to do. They don't elect me to represent them; they elect me to make a judgment about how I should represent them. And my judgment should be based on the outcome of the legislation that I voted on.

I also think that you get to be expert if you are on a Committee. I remember when we had to amend Social Security to save the trust funds. There was a Social Security Commission set up. All these commissions are umbrella organizations to tell the Ways and Means Committee exactly what the Ways and Means Committee knows they should do. The Chairman of the Social Security Commission would call up, and ask "What do you want us to do? What can you live with?"

I would say, "I'll tell you. I know what we can live with. We've got to postpone the COLA."

And we did that.

**Q** You mentioned lobbyists. In '93, the deductibility of business expenses for lobbying was eliminated. Did you think that was a good idea from a policy standpoint?

**A** It was definitely a political decision. I don't know that we could avoid it. The argument for it was that poor little businessmen can't afford hired guns in Washington. And that's kind of unfair.

But, you know, that's why I always thought that I was the lawyer for the 8th Congressional District. I was never embarrassed to call an agency for a business in my community. I was never embarrassed to shake up an agency.

I've got to admit that when I was Chairman of the Ways and Means Committee and I called an agency, the activity was much more fierce than when I was a freshman Member of the House of Representatives and called the agency. But I always thought that the people have a perfect right to walk in that door and to say, "Mr. Rostenkowski, I'm in small business, and I think that what you're doing here is unfair, and I think that I'm not getting the action downtown that I deserve." I'd call downtown and raise holy hell and get some activity.

Today if you did that, the newspapers would report, "Oh my God, Rostenkowski's using political pressure!" But I'm their lawyer!

I was always amazed when Chicagoans who I know on a first name basis would come in to see me in Washington, with a lobbyist. I'd say, "Mr. Jones, we played golf last week. You didn't mention this to me."

They would say, "Well, I didn't want to impose on our friendship."

I would say, "You hire these guys, and I'm not suggesting that you don't, but why wouldn't you mention it to me? I'm a Chicagoan, too! This is our city, our state. Friendship, my sister! I'm your representative! That's my job—I'm your representative!"

**Q** What do you hope to see as your legacy as Ways and Means Committee Chairman?

**A** It's known in Committee that I felt that whenever there was a difficult decision, or whenever something raised the color of a rifle shot for somebody, I didn't care so much about whether it was a rifle shot as whether it was good law—whether it was fair. Because I think that is what the Committee on Ways and Means' responsibility is. It is to write good law, and be the judge of whether people are injured by law that you write. And I've always said, when I meet my great reward, on my tombstone—because it was Rob Leonard who was more than anyone the person over my shoulder—I want it to say, "Rob, is this good law?" ■

## SPECIAL REPORT

# Update on Employee Benefits and Retirement Plans

**Editor's Note:** This issue includes David Pratt's annual update regarding employee benefit plans. William Wang and Scott McMillen address two related topics, Roth IRA conversions and in-plan Roth conversions.—Gail Levin Richmond, Nova Southeastern University, Davie, FL

# Employee Benefit Plans: Recent Developments

By David Pratt*

## Definition of Fiduciary

ERISA section 3(21)(A) provides that a person is a fiduciary with respect to an ERISA plan to the extent that, inter alia, it renders investment advice for a fee or other compensation, direct or indirect, with respect to any moneys or other property of the plan, or has any authority or responsibility to do so. In 1975, the U.S. Department of Labor (DOL) issued a regulation (§ 29 C.F.R. 2510.3-21(c)) providing that, to be a fiduciary, a person must render advice "on a regular basis" and pursuant to a mutual understanding that such services will serve as a primary basis for investment decisions. DOL also ruled that a valuation of closely-held employer securities that an ESOP would rely on in purchasing the securities would not constitute investment advice. Adv. Op. 76-65A.

In October 2010, DOL published a proposed rule expanding the definition of who is a fiduciary by virtue of providing investment advice. 75 Fed. Reg. 65263. Advice need not be provided on a "regular" basis, nor need there be the mutual understanding provided for in the existing regulation. Advice would include: advice, appraisals or fairness opinions concerning the value of securities or other property; recommendations as to the advisability of investing in, purchasing, holding, or selling securities or other property; or advice or recommendations as to the management of securities or other property. DOL requested comments on whether investment advice should encompass recommendations related to taking a plan distribution.

The proposal affects both ERISA plans and IRAs. The proposed effective date is 180 days after publication of the final regulation. The comment period ends on January 20, 2011.

It is likely that the proposal will be finalized. Attorneys, CPAs, and other advisors should refrain from inadvertently giving advice that could constitute investment advice under the expanded definition. Otherwise, they risk exposing themselves to fiduciary liability under ERISA.

## Nonqualified Deferred Compensation

Code section 409A imposes additional taxes and penalties on nonqualified plans that fail to comply, in both form and operation, with its requirements. Notice 2008-113, 2008-51 I.R.B. 1305, permits the correction of certain *operational* failures, and limits the amount includible in income for certain operational failures.

Notice 2010-6, 2010-3 I.R.B. 275, allows voluntary correction of certain *document* failures, without current income inclusion or additional taxes under section 409A, if the document failure is corrected by December 31, 2010, and any associated operational failures are also corrected, in accordance with Notice 2008-113. Notice 2010-6 also modifies Notice 2008-113. Additional relief was provided by Notice 2010-80, 2010-51 I.R.B. 853, which modifies Notices 2008-113 and 2010-6.

Although Notice 2010-6 permits corrections after December 31, 2010, the relief is more limited and penalties may apply.

## Disclosure

Under ERISA and the Code, arrangements between plans and service providers are prohibited transactions unless an exemption applies. ERISA section 408(b)(2) provides an exemption for "reasonable" service arrangements, if no more than reasonable compensation is paid to the service provider. On July 16, 2010, DOL issued an interim final regulation (75 Fed. Reg. 41600) requiring written disclosure of the services to be provided and the compensation to be received by "covered service providers" to "covered plans" before the parties enter into, renew, or extend such arrangements.

A "covered plan" means a pension plan within the meaning of ERISA section 3(2)(A) (and not exempted by ERISA section 4(b)), but does not

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include a SEP, a SIMPLE plan, or an IRA. DOL intends to develop separate disclosure requirements for health and welfare plans.

The regulation generally applies to (1) any ERISA fiduciary or registered investment adviser; (2) providers of recordkeeping or brokerage services to a participant-directed individual account plan; and (3) providers of accounting, auditing, actuarial, appraisal, banking, consulting, custodial, insurance, investment advisory (for plan or participants), legal, recordkeeping, securities or other investment brokerage, third party administration, or valuation services, if they (or affiliates or subcontractors) reasonably expect to receive indirect compensation or certain payments from related parties. Disclosure under the regulation is required only if the service provider (or an affiliate or subcontractor) reasonably expects to receive $1,000 or more in direct or indirect compensation. A service provider must also disclose any change to the required information, as soon as practicable.

Service providers must comply on or before July 16, 2011. The disclosures for new arrangements on or after that date must satisfy the rule, and prior arrangements must comply with the rule as of the effective date.

DOL noted that even arrangements that are outside the scope of the regulation must be "reasonable" to satisfy the statutory exemption. Also, ERISA section 404(a) obligates plan fiduciaries to assess the services to be provided, the reasonableness of the fees and expenses, and potential conflicts of interest.

The regulation does not supersede any state disclosure law, except to the extent that it prevents application of the regulation.

DOL has also issued a final rule on disclosure requirements under participant-directed individual account plans. (75 Fed. Reg. 64910 (Oct. 20, 2010)), effective for plan years beginning on or after November 1, 2011. Investment information must be furnished in a chart or similar format designed to facilitate comparison of the information for each investment alternative under the plan. The regulations include a model comparative chart, and note that "The cumulative effect of fees and expenses can substantially reduce the growth of your retirement savings.… Fees and expenses are only one of many factors to consider when you decide to invest in an option. You may also want to think about whether an investment in a particular option, along with your other investments, will help you achieve your financial goals."

These rules do not apply to IRAs, SEPs, or SIMPLE plans.

## Health Care Reform

President Obama signed the Patient Protection and Affordable Care Act, Pub. L. No. 111-148 (PPACA), on March 23, 2010, and the Health Care and Education Reconciliation Act of 2010, Pub. L. No. 111-152 (HCERA) on March 30, 2010 (collectively, the "Act"). For a timeline showing the changes that become effective in each year from 2010 through 2018, see http://healthreform.kff.org/timeline.aspx. This article will address only a few issues of immediate concern to tax practitioners.

Notice 2010-69, 2010-44 I.R.B. 576, provides that reporting heath care costs (required by section 6051(a)(14)), will not be required on 2011 W-2s.

DOL Technical Release 2010-02 provides a grace period through July 1, 2011, for compliance with the new claim review and appeal standards, if the plan sponsor is attempting in good faith to implement the new standards. HHS is encouraging states to provide similar grace periods for insured plans subject to state law.

Under prior law, self-insured health plans were subject to section 105(h), which prohibits discrimination in favor of "highly compensated individuals." Notice 2011-1, to be published in 2011-2 I.R.B., delays the effective date of the application of section 105(h) to insured plans until further guidance is issued. The Act also extends these rules to fully insured, non-grandfathered group plans, for plan years beginning after September 22, 2010. Notice 2010-63, 2010-41 I.R.B. 420, addresses the new requirements. Under a discriminatory *self-insured* plan, discrimination results in additional income taxation to the highly compensated individuals. A discriminatory *insured* plan may be subject to suit under ERISA, and the plan sponsor may be liable for a penalty of $100 multiplied by the number of individuals discriminated against and the number of days the plan does not comply. I.R.C. § 4980D.

The Act treats the cost of a medicine or drug as a qualified medical expense only if the medicine is insulin or a prescribed drug. This rule applies to HSA and MSA distributions paid, and to FSA and HRA expenses incurred, after December 31, 2010. I.R.C. §§ 106(f), 220(d)(2) & 223(d)(2). The Service has issued Notice 2010-59, 2010-39 I.R.B. 396, to provide guidance concerning this change. The Act increases the additional tax on distributions from HSAs and MSAs that are not used for qualified medical expenses to 20% of the amount of the distribution included in gross income; this rule applies to distributions made after December 31, 2010. I.R.C. §§ 220(f)(4)(A) & 223(f)(4)(A).

Generally, cafeteria plans may not be amended retroactively. Notice 2010-59 gives plan sponsors until June 30, 2011 to adopt conforming plan amendments. For years beginning after December 31, 2010, the Act provides a simple cafeteria plan for small employers. I.R.C. § 125(j).

The Act also added a new section 45R, providing a temporary (for tax years beginning in 2010 through 2015) tax credit to small businesses that provide health coverage to employees. The Service has issued guidance in Notice 2010-44, 2010-22 I.R.B. 717, and Notice 2010-82, 2010-51 I.R.B. 857.

## Defined Benefit Plan Funding

The Preservation of Access to Care for Medicare Beneficiaries and Pension Relief Act of 2010 (Pub. L. No.111-192) provides short term relief from the normal minimum funding requirements for defined benefit plans. The Service has issued Notice 2010-55, 2010-33 I.R.B. 253 (for single-employer plans), Notice 2010-56, 2010-33 I.R.B. 254 (for multiemployer plans), and Notice 2011-3, to be published in 2011-2 I.R.B.

## Hybrid Pension Plans

In October, 2010, the Treasury Department issued final regulations (75 Fed. Reg. 64123) providing guidance on sections 411(a)(13) and (b)(5), enacted by the Pension Protection Act of 2006 (Pub. L. No. 109-280) and amended by the Worker, Retiree, and Employer Recovery Act of 2008 (Pub. L. No. 110-458). The regulations generally apply to plan years beginning after December 31, 2010. Treasury also released proposed regulations (75 Fed. Reg. 64197), addressing issues under section 411 that were not addressed in the final regulations.

Most hybrid pension plans must be amended to reflect the new requirements. Under Notice 2009-97, 2009-52 I.R.B. 972, the amendments are due by the end of the 2010 plan year. Notice 2010-77, 2010-51 I.R.B. 851, modified Notice 2009-97 and extended the deadline to the last day of the first plan year that begins on or after January 1, 2011.

## The Small Business Jobs Act of 2010 (Pub. L. No. 111-240)

On September 27, 2010, the President signed the Small Business Jobs Act, which (1) allows 401(k) and 403(b) plans to give participants the option of transferring money from a pre-tax account to a Roth account within the plan and (2) allows governmental 457(b) plans to offer Roth accounts and Roth conversions, beginning in 2011. These changes are discussed elsewhere in this issue. *See* Scott D. McMillen, *In-Plan Roth Conversions.*

Generally, when a self-employed individual calculates net earnings for self-employment taxes, no deduction is allowed for health insurance costs. The Act permits a one-time exception to this rule for the taxable year beginning in 2010. I.R.C. § 162(l)(4).

The Act amends section 72(a) to provide rules governing the partial annuitization of an annuity, endowment, or life insurance contract, effective for amounts received in taxable years beginning after 2010.

The Act also (1) increases reporting penalties (I.R.C. §§ 6721 & 6722) for information returns required to be filed on or after January 1, 2011 (including 2010 1099s and W-2s), and (2) removes cell phones and similar telecommunication equipment from the definition of "listed property" (I.R.C. § 280F(d)(4)), effective for taxable years beginning after 2009. ■

# Some Immediate and Long-Term Advantages of a Roth IRA Conversion

By William K.S. Wang*

## Initial Analysis

Suppose I have three bank accounts, each with $100. The first two bank accounts are in traditional IRA accounts with a zero basis. (These traditional IRA accounts may have been converted from 401(k) accounts at a prior employer.) The third account I own outright.

For simplicity, assume the federal income tax rate is a flat 50% and will remain at that level forever. Further assume there will never be state income taxes. (This article could just as well have assumed some other rate, such as 33⅓%, but 50% requires an analogy to only three accounts, while 33⅓% requires an analogy to four accounts.)

In effect, the Service has a half ownership in my two traditional IRA $100 bank accounts. If I withdraw part or all of the money from the IRA, I must pay the Service half. The Service is like a 50% partner.

If I convert the $200 in the traditional IRA accounts to a Roth, I must pay $100 in income tax. In effect, for $100, I am buying out the Service's 50% partnership interest. In other words, if I give the Service the $100 bank account I own outright, the Service conveys to me its half ownership in the two traditional IRA $100 bank accounts.

I start out with $100 outright and $200 in a 50% partnership with the Service. I end up with $200 in a Roth IRA that I own outright. I give up $100 to get $100. From a net worth perspective, the result is a wash. My net worth remains $200.

Going forward, however, I have certain immediate and long-term advantages.

1. Interest on the $100 bank account that I owned outright was subject to income tax. Interest on the Roth IRA bank accounts is not subject to income tax, and all $200 of those accounts are now mine (versus only $100 earlier).

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2. Unlike the traditional IRA, my Roth IRA has no required minimum distributions starting at age 70½. I can keep the Roth IRA until I die and leave the entire amount to my child (who may take distributions over her lifetime, and never pay any income tax).
3. By paying the $100 in income taxes, I reduce my estate by $100. Before, although my net worth was really $200 (because of the $100 income tax due on the traditional IRAs), my estate was $300. (Of course, a $300 estate is not taxable, and my estate might qualify for the spousal deduction. Nevertheless, I might leave this $300 to my child and leave a sufficient amount of other assets to my child to make this $300 subject to estate tax.)

Suppose I did *not* convert and were to die upon turning age 70. Assume I did not take any distribution from my ($200 plus interest) traditional IRA and left all my assets to my child. All three bank accounts ($300 plus interest) would be in my estate. The Service would still have a half ownership in the traditional IRA accounts ($200 plus interest) that went to my child. Interest on the third ($100 plus after-tax interest) bank account would have been taxed during my lifetime and would continue to be taxed while held by my child.

Assume instead that I convert to a Roth IRA this year (at, say, age 65) and die when turning age 70. Of the original three accounts, only the two Roth IRA accounts would be in my estate ($200 plus interest). Interest on these Roth IRA accounts would never be subject to income tax (in my remaining lifetime and my daughter's).

## Alternate Analysis

Again, suppose I have three bank accounts, each with $100. The first two bank accounts are in traditional IRA accounts with a zero basis. The third account I own outright.

Again, assume the federal income tax rate is 50% and will remain 50% forever and that there will never be state income taxes. In effect, the Service has a half ownership in my two traditional IRA $100 bank accounts.

Under current law, under certain circumstances, a taxpayer whose adjusted gross income does not exceed a prescribed limit can open a Roth IRA account (and can use existing savings for that purpose). *See* I.R.C. § 408A(c)(3). What if the Code were amended to remove the income limitation and allow me to convert the third $100 bank account (the one I own outright) to a Roth IRA with no tax (and also allow me to withdraw from the Roth at any time with no tax)? Naturally, I would convert the third account to a Roth IRA.

In effect, I would have three identical bank accounts:

1. two traditional IRA $100 accounts, one "owned" by me and one "owned" by the Service.
2. one Roth IRA $100 account.

The $100 Roth IRA would cancel out the $100 account "owned" by the Service. Whenever I wanted to liquidate entirely the two traditional IRA accounts, I could also liquidate the Roth IRA and have just enough to pay the tax. The advantage of the Roth IRA over the $100 bank account I had before is that the Roth IRA would grow tax free. I would be better off.

Assume, however, that the Code does *not* allow me to convert the third bank account (the one I own outright) into a Roth IRA or even a traditional IRA. Nevertheless, I can accomplish the same result by converting my traditional IRAs into a Roth and using the third account to pay the tax on conversion. I no longer have the third account, but I also no longer have any tax liability on the traditional IRA. I have $200 that I own outright and on which I shall never owe any tax (except in very rare instances).

Of course, in both analyses above the major simplifying assumption is the constant and uniform income tax rate. In reality, rates are not constant and uniform. Conversion of a large amount to a Roth might in fact thrust me into a higher marginal income tax bracket. In addition, I do not know what my (or my child's) marginal tax rate would be at the time of withdrawal from the traditional IRA. Also unknown is the age at which I shall die. With the traditional IRA, I must start taking minimum distributions at age 70½. Nevertheless, the analysis with the simplifying assumptions demonstrates the potential advantage of a Roth IRA conversion.

## Using the Opportunity to Recharacterize the Conversion When Investing in Stocks

If I convert to a Roth, the Code allows me to recharacterize (rescind) the conversion by a certain deadline the following year. *See* I.R.C. § 408A(d)(6). If my Roth IRA is invested in stocks, the opportunity to recharacterize the conversion offers a "heads I win, tails the Service loses" opportunity.

This analysis begins with the three accounts, but with another type of asset in two of the accounts. I have three accounts, each with $100. Two are traditional IRA accounts (with a zero basis) invested in *stocks*. The third is a $100 bank account that I own outright. Again, assume federal income taxes are 50% and will remain 50% forever and that there will never be state income taxes.

If I convert the $200 in the traditional IRA accounts to Roth accounts, I must pay $100 in income tax. In effect, for $100, I am buying the Service's 50% partnership ownership. My $100

investment in stocks increases to $200 because of elimination of the tax liability.

### Stocks Increase in Value

Assume that by the deadline for recharacterization, the stocks in my Roth IRA accounts double in value from $200 to $400. By effectively increasing my $100 stock investment to $200 through the Roth conversion, I gained an extra $100, as explained in the next paragraph.

Suppose I had not converted. Ignoring bank account interest, I would have a bank account of $100. My $200 in traditional IRA stock accounts would have doubled in value to $400. Taking into account the Service's 50% ownership, my interest would be worth $200. This $200 plus the $100 bank account results in a total of $300. The conversion made me $100 better off.

If I wished, after the conversion and the increase in stock value, I could balance my investments by shifting one of the $200 Roth IRA stock accounts into a bank account. I would then have a $200 Roth IRA invested in stocks and a $200 Roth IRA in a bank account.

### Stocks Decrease in Value

Suppose that by the deadline for recharacterization, the stocks in my Roth IRA accounts *decline* 50%, from $200 to $100. I can then recharacterize my Roth conversion. In effect, I convey back to the Service a 50% interest in my IRA accounts (worth $50) and receive in return the $100 in taxes paid upon conversion. Ignoring bank account interest, my situation is the same as if I had never converted. I have traditional IRAs worth $100 (of which the Service owns 50%) and a $100 bank account.

In short, the opportunity to recharacterize my Roth conversion (by a certain deadline) enables me to invest some money in stocks and enjoy the gains but avoid the losses. If the stock market goes up, I enjoy the gains on $200 worth of stock. If the market goes down, I suffer the losses on only $100 worth of stock. I could even open numerous *separate* Roth IRA accounts in different asset classes. If some accounts appreciate and others depreciate, I can recharacterize the ones that decline.

After recharacterization, I can then *re*convert to a Roth IRA after waiting 30 days or until the tax year following the tax year of the initial Roth IRA conversion, whichever is later. *See* Treas. Reg. §§ 1.408A-5, 1.408A-9.

As before, I hypothesize a constant and uniform income tax rate. Throughout, I also assume that the Congress will not amend the Code to tax distributions from previously created Roth IRAs. ■

# In-Plan Roth Conversions

By Scott D. McMillen*

## Background

On September 27, 2010, Congress enacted the Small Business Jobs Act of 2010 (Pub. L. No. 111-240) ("the Act"). Sections 2111 through 2112 of the Act contain plan participant friendly provisions for certain types of retirement plans.

Specifically, Section 2112 of the Act amends section 402A, which allows plan participants to make Roth contributions to retirement plans. Newly enacted Act section 2112, at the most fundamental level, allows compatible plans to convert non-Roth contributions into Roth contributions within the existing retirement plan (*i.e.*, without rolling over amounts to a Roth IRA).

The Act's conversion provision was effective immediately for certain retirement plans, but did not come into effect for others (*e.g.*, section 457(b) eligible plans) until the beginning of the 2011 taxable year. However, in order to access the benefits of section 2112, most plans will need to consider and proceed upon a mixture of plan modifications to allow participants the opportunity to utilize the newly enacted provisions. This short article discusses some of the new law's nuances. It also discusses plan sponsor and plan participant considerations for Roth conversions under section 2112.

## Mechanics of Conversion

In order to take advantage of the leeway afforded by the Act, a retirement plan must satisfy a number of qualifiers. First, conversion ability is limited to section 401(k), 403(b), and 457(b) plans. Thus, money purchase plans and profit sharing plans without a CODA feature are not eligible for conversion. Second, the plan must allow participants to make Roth contributions. This requires the plan to allow participants to make Roth contributions as a prerequisite before allowing participants to execute a Roth conversion. Third, upon conversion the plan must separately account for the converted pre-tax deferrals within a separate Roth conversion account. Fourth, the conversion is applicable only for amounts that are otherwise considered eligible rollover distributions under the plan. Generally, this means that distributions upon attaining age 59½, upon a separation from service, death, or disability, or that are considered

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qualified reservist distributions are eligible for conversion. Conversely, this does not permit conversion of in-service withdrawals related to hardship. Only amounts that are eligible rollover distributions are eligible for Roth conversion.

## Payment of Taxes on Converted Deferrals

One prerequisite for participants completing any conversion of deferrals is paying income taxes on the converted amounts. In order to facilitate conversion, Act section 2112 specifically prevents the 10% excise tax under section 72(t) from applying to converted deferrals. However, beware that the 10% excise tax may apply if converted amounts are withdrawn before the completion of five taxable years. For more information on the applicability of the five-year recapture rule, see Notice 2010-84, 2010-51 I.R.B. 872.

If a participant chose to convert deferrals into Roth contributions in 2010, the default rule is that the associated federal income tax is payable ratably over a two-year period in 2011 and 2012. Thus, the gross income associated with the conversion is not taken into account on the participant's 2010 tax return but is instead taken into account ratably in 2011 and 2012.

It is not clear under the plain meaning of the Code or applicable guidance, but it appears to be a reasonable position, that participants could extinguish the entire tax liability on their 2011 tax return instead of delaying the second half of the obligation to their 2012 returns. Of course, this position would only be practical if a participant could gain an advantage from its applicability. Generally, a participant would rather defer the tax obligation until a future period.

It should be noted that section 2112 of the Act did permit participants to make an election to include the conversion-related gross income on their 2010 tax returns, instead of the default rule of spreading the income ratably over the two-year period. If this election was made, the tax obligation is due with the participant's 2010 tax return, due April 15, 2011 (without regard to any extension). Finally, unlike Roth IRAs, pursuant to section 408A(d)(6), a participant cannot unwind a Roth conversion before the filing of his or her federal income tax return.

## Benefits and Deterrents of Conversion

A large benefit of permitting conversions is mitigating the effects of widespread Roth IRA rollovers from retirement plans (so-called leakage). Under current law, the only way for a participant lacking a Roth feature in his existing retirement plan to mimic the tax effects of such a feature, is to engage in a rollover of distributable amounts into a Roth IRA. However, until last year, participants who had adjusted gross income that exceeded $100,000 were barred from engaging in a rollover to a Roth IRA. Congress, now having authorized Roth conversions, will allow retirement plans to mitigate the risk of losing money to Roth rollovers by including this conversion provision within their plan arsenal. This will presumably help preserve any asset-size-related discounts that plan sponsors are able to obtain from recordkeepers or other third-party administrators.

A few distinct advantages remain for participants of distributable age (*e.g.*, 59½) to roll over account balances to Roth IRAs. The first is the most obvious: Roth IRAs generally allow for greater investment control, including the selection of individual equities, along with significant flexibility in modifying investment allocation (*i.e.*, frequency and transparency of trades). Of course, participants come from a wide array of backgrounds and levels of sophistication, and some may not desire to have this type of command over their retirement assets.

Second, a participant may want to execute a rollover to a Roth IRA to seek shelter from the required minimum distribution ("RMD") rules applicable to qualified retirement plans (*e.g.*, 401(k) plans). At this time, even after a Roth conversion has been executed under the Act, amounts in Roth accounts are still subject to the mandatory RMD rules. The RMD rules generally require distribution at the later of retirement or age 70½. Amounts in Roth IRAs are exempt from the mandatory RMD requirements that apply to traditional IRAs and applicable qualified retirement plans. This creates a distinct advantage for Roth IRAs, even where retirement plans have the ability to convert elective deferrals to Roth contributions, because it allows participants to control their timing of asset distribution. Nonetheless, a participant can convert non-Roth accounts into Roth accounts under a qualified retirement plan and still avoid being subject to the RMD requirements. This method is more cumbersome than simply having an exemption from the requirements, but it is just as effective. To correctly avoid application of the RMD scheme, the participant can engage in a Roth conversion under the employer's retirement plan, and then must execute the rollover to a Roth IRA one year before commencing distributions under the RMD rules.

Roth conversions in retirement plans do offer at least one advantage over Roth IRAs. Allowing for Roth conversions in applicable retirement plans allows a participant to have Roth elective deferrals in excess of the IRA limit of $5,000. The participant achieves this result by deferring the maximum Roth limit within a qualified retirement plan, $16,500 (unless the participant is eligible for catch up contributions) and the maximum within a Roth IRA, $5,000 (again, absent catch up contributions).

## Service Guidance

On November 26, 2010, the Service released Notice 2010-84, 2010-51 I.R.B. 872. Using a question and answer format, this notice outlined some of the more pressing issues that required guidance before the end of 2010.

Of particular concern for practitioners was the potential remedial amendment period for adopting the obligatory amendments to provide for Roth conversions. Here, the Service indicated that sponsors of 401(k) plans could adopt the conversion amendments by the "later of the last day of the plan year in which the amendment is effective or December 31, 2011." This gives sponsors of 401(k) plans sufficient wiggle room in order to provide for conversions. On the other hand, 403(b) plan sponsors have until the end of their remedial amendment period (to be released by the Service in the near future) or the end of the plan year in the year the amendment is adopted. This will allow 403(b) plan sponsors sufficient time to meet the necessary regulatory requirements to avoid potential qualification errors.

These extensions of time to allow for amendments to meet the requirements of Act section 2112 appear to apply to any plan amendment that is adopted in order to allow for Roth conversions. In Q&A 17 the Service lists the variety of amendments that would qualify, but notes that adding a CODA feature to a qualified plan is not an amendment that relates to compliance with section 2112. Alternatively, amendments to allow Roth elective deferrals, Roth conversion availability, and acceptance of rollover contributions to a Roth account are considered to relate to compliance with Act section 2112 and are thus eligible for the remedial amendment period.

In addition, among the issues addressed was the question of whether or not section 3405(c) and 20% mandatory withholding applies to Roth conversions. Here, the Service indicated that it does not believe it is a requirement for Roth conversion amounts. However, the notice warns that a taxpayer who forgoes withholding risks being subject to an underpayment penalty. Thus, taxpayers should be cognizant of this possibility if they decide to not withhold upon executing a Roth conversion.

The Service also addressed a number of other issues, including proper reporting of conversions on Form 1099-R, notice procedures, application of the five-year recapture rule, and basis allocation under section 72.

The Service is expected to release additional guidance affecting the treatment of Roth conversions. Future guidance may contain more detailed analysis of the rules and should allow plan sponsors greater comfort in implementing conversions.

## Section 2111 and 457(b) Government Plans

It is also worth noting that Act section 2111 amends section 402A(e)(1) applicable to section 457(b) eligible plans. This amendment to section 457(b) eligible plans permits plan participants to make Roth contributions. Unlike the Roth conversion rules detailed above, this newly enacted provision did not apply until taxable years beginning after December 31, 2010. After enactment of Act section 2111, government plan participants have equivalent rights in comparison to private sector plan participants, who have had access to Roth contributions for a number of years.

Furthermore, this provision is a revenue producer for the government, with projected benefits exceeding $500 million over a 10-year period according to a summary produced by the Senate Finance Committee. Setting aside revenue projections, this is a provision that has been long awaited by many government employees, and will likely see significant activity in government plans in the foreseeable future. However, this legislation will require 457(b) plans and their record keepers to make a variety of changes going forward. Those changes are beyond the scope of this article.

## Conclusion

Congress could have pushed the legislation further to allow for Roth conversions at any point in time, including before a distributable event. This would have quelled fears that plan sponsors would terminate their 401(k) plans to move currently undistributable funds into Roth IRAs. It would also have allowed Roth conversions to become more equivalent to Roth IRAs, which currently have several advantages over Roth conversions (particularly exemption from the RMD rules). Nonetheless, this appears to be a solid start, allowing plan sponsors greater latitude within their existing plans to please participants and close the flood-gate of rollovers to Roth IRAs. ■


## Are you receiving Section of Taxation communications?

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concluded that the opinion meant very little—in other words, there is no such thing as a sure-fire insurance policy in this context.

## The Substantial Understatement Penalty

The law generally stands behind the judges in such cases. The Code and the regulations are at odds with the idea of such an insurance policy. Section 6662 creates an accuracy-related penalty for underpayments attributable to a variety of factors, including a substantial understatement of income tax. For a corporation, a substantial understatement exists if the amount of the understatement exceeds the lesser of 10% of the tax required to be shown on the return (or, if greater, $10,000) or $10 million. Under section 6664, no penalty is imposed if there was reasonable cause for, and the taxpayer acted with good faith with respect to, the underpayment. The determination of whether a taxpayer acted with reasonable cause and good faith is made on a case-by-case basis. The regulations explicitly state that reliance on a professional tax advisor does not necessarily shield a taxpayer from the penalty, but that all facts and circumstances must be considered in determining whether a taxpayer has reasonably relied in good faith on advice.

The language of the statute and the regulations seems entirely consistent with the Tax Court's holding in *Canal Corporation*, where the PwC opinion at issue was "riddled with questionable conclusions and unreasonable assumptions" (*Id.* at 34) and "tainted by an inherent conflict of interest." *Id.* at 32. Accepting those as the facts, why then the surprise? It could be that the penalties went too far, but even if they did, the case serves as an important reminder to tax professionals and tax litigators of lessons we should have learned in the past. It is possible that we have. The underlying transaction in this case occurred over a decade ago, prior to the changes to Circular 230 and prior to the enactment of Sarbanes-Oxley, and was a relative contemporary of other large penalty cases. The outcry, however, suggests that some of the practices may persist.

## Lessons Learned?

Many people likely remember *Long Term Capital Holdings v. United States*, 330 F. Supp. 2d 122 (D. Conn. 2004), which featured a hedge fund run by an all-star team of the financial elite, including two Nobel laureates. The economics of the transaction were simple: no rational investor would have invested in the shelter transaction but for its tax savings. Long Term, however, argued that it should not be subject to penalties because it had "should" opinions from two prominent law firms.

If we examine *Canal Corporation* and *Long Term Capital Holdings*, we see certain similarities. Both feature sophisticated taxpayers relying on tax advice that lacked any legal support. In *Canal Corporation*, the tax advisor wore so many hats the court became concerned about conflicts of interest. In *Long Term Capital Holdings*, the transaction was a bad deal but for the tax consequences, and witnesses for the taxpayer provided unreliable, self-serving testimony. These two cases present some of the most common pitfalls for taxpayers and tax advisors. The brief list of tips below may help tax advisors whose clients wish to avoid the imposition of penalties (and the ire of any judges who may examine the opinion).

## Tips for Avoiding the Section 6662 Penalty

1. Legal opinions should be grounded in legal analysis. That legal analysis, including careful discussion of relevant legal authorities, should be discussed in the opinion. If you can't find relevant authorities, carefully consider what that means for the level of comfort you are willing to issue.
2. Take care with your assumptions, both legal and factual. Important legal issues should not be assumed away. Are those factual assumptions really reasonable? If a reasonably diligent analysis of the facts and circumstances would reveal them to be unreasonable and/or unsupportable, the answer is no.
3. Do what you can to avoid burden of proof problems down the line.
4. Self-serving explanations and justifications will get you nowhere.
5. If the opinion serves only to avoid penalties, reconsider.
6. If you know the transaction you are blessing with a "should" is "aggressive" but another reasonable person might consider it "abusive," should you reconsider that "should"? We can all come up with examples of aggressive opinions winning the day, but if you suspect that your opinion would not be sustained by a court, then does it really warrant a "should"?
7. All taxpayers are not created equal. When a multinational company or tax attorney or hedge fund run by Nobel-prize winners is the taxpayer who relies on an opinion without substantive legal analysis, "reasonable cause" and "good faith" may be found wanting where they wouldn't for a less sophisticated taxpayer.
8. Beware the presence, or even the appearance, of conflicts of interest. If you were involved in the planning of the transaction, or your firm was, your familiarity with the transaction may make you seem like a good choice to write the opinion. In the end, you may be the right choice, but carefully consider whether it would be reasonable for a taxpayer to rely on your opinion, given your connection with the transaction. Similarly, carefully consider your fee arrangement and whether it creates, or may appear to create, a conflict of interest. ■

# Just A Matter of Fairness: Tax Consequences of the Service's Revised Community Property Treatment of California Registered Domestic Partners (RDPs)

By Francine J. Lipman* and Rebecca J. Kipper**

## A Brief History of Federal Tax Treatment of California RDPs

For Mr. Eric Rey, it was just a matter of fairness. "For the first time ever, I'm able to file federal taxes that, in a small way, acknowledges what's going on in my relationship," he exclaimed after the Service issued its historic rulings on May 28, 2010. It had been a long journey for Mr. Rey as he fought for—and ultimately won—the right to split community property income with his RDP for federal tax purposes. In 2005, when California amended its domestic partnership laws to extend community property rights to RDPs, he asked the Service for guidance on how the amendments affected the federal tax treatment. It responded with CCA 200608038, a highly criticized memorandum, which refused to recognize California's community property treatment for federal tax purposes. Because the CCA left Mr. Rey and his RDP with more questions than answers, he tried again in 2007. At that time, the Service refused to offer any additional guidance.

Still not willing to give up, Mr. Rey felt hope with the enactment of new California RDP legislation and the election of President Barack Obama. On the same day that the Service declined to grant RDPs community property tax treatment for federal purposes in 2006, California State Senator Carole Migden introduced the State Income Tax Equity Act or "the final piece" of state legislation to make California RDPs equal to spouses. The bill would require RDPs to file their state income tax returns in the same manner as married couples and would apply California community property rules to RDPs exactly as those rules apply to heterosexual married couples. Despite contentious and heated debate on the floor of the California Assembly that had to be paused to allow tempers to cool, the legislature passed the bill. On September 30, 2006, Governor Schwarzenegger signed the bill into law.

After this final piece of the California tax equality puzzle was in place, Mr. Rey once again asked the Service for guidance on the federal income and gift tax treatment of his RDP. On May 28, 2010, it responded with PLR 201021048, CCA 201021049, and CCA 201021050. These newly issued documents reversed the Service's previous position and properly applied "the principle that federal law respects state law property characterizations," and historically determined that "the federal tax treatment of community property should apply to California registered domestic partners."

## Application of the Revised Service Position on Income-Splitting for Community Property Income

### Income Allocation and Filing Status

Under the revised rules, each RDP reports one-half of community property income that is earned by either RDP, but each continues to report the full amount of his or her separate income. The Service has suggested that California RDPs follow the advice given for married heterosexual taxpayers filing their tax returns separately to determine how state community property laws apply for federal income tax reporting purposes. *See* Publication 555, *available at* www.irs.gov/pub/irs-pdf/p555.pdf, and California Franchise Tax Board Publication 737, *available at* www.ftb.ca.gov/forms/2009/09_737.pdf. These publications have not yet been updated to reflect the revised Service position.

The rules above apply to income allocation. They do not apply to filing status. Because neither RDPs nor same-sex married couples can file using the married filing jointly (or separately) federal filing status, RDPs and same-sex married couples must file separate federal income tax returns under the applicable filing status as either "unmarried/single" or "head of household." Accordingly, the advice in Publication 555 that applies to the "married filing separately filing status" rather than community property law is not applicable to RDPs.

Because this new tax treatment changes the amount of income each RDP reports as gross income, it may cause unexpected, but related tax consequences. For example, an otherwise qualifying dependent may no longer qualify as such for federal income tax reporting. Notably, self-employment

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taxes on a sole-proprietorship's net income are the sole responsibility of the sole-proprietor and should not be allocated between RDPs. However, each RDP should report one-half of the deductions and federal income tax withholdings with respect to any split community property income for federal income tax purposes. As is the case for California married couples, California RDPs can enter into written agreements to opt out of community property treatment. Given the complexity of these and related issues, California RDPs and other same-sex couples should consult their tax attorneys about their particular situations and how they should best proceed to achieve their personal goals. Lambda Legal offers online publications that can assist couples confronted by these complex and often overwhelming issues (*available at* www.lambdalegal.org/publications/take-the-power/).

### Electing Treatment for Prior Years

The Service will allow, but not require, California RDPs to amend their federal income tax returns filed for calendar years 2007, 2008 and 2009, to reflect community property income-splitting treatment, subject to any applicable statutes of limitations. The May 2010 guidance seems to indicate that community property income-splitting treatment is not required until calendar tax year 2011. Nevertheless, Lambda Legal has indicated that "Notwithstanding the language of the May 2010 IRS memorandum, however, as of November 2010, some IRS representatives have informally communicated that community property treatment will be *mandatory* for calendar year 2010 taxpayers." *The IRS Applies "Income-Splitting" Community Property Treatment to California's Registered Domestic Partners* (Q&A #12) (Oct. 20, 2010), *available at* www.lambdalegal.org/publications/factsheets/fs_the-irs-applies-income-splitting-community-property.html.

### Federal Gift Tax Consequences

Community property income-splitting operates by law so there is no taxable transfer between the parties for federal gift tax purposes. However, if the parties agree by a qualifying agreement to convert certain property from community property to separate property or from separate property to community property, the conversion may result in a federal gift tax.

### Effect on California Married Same-Sex Couples?

The CCAs and PLR issued in May 2010 refer only to California RDPs. Nevertheless, Lambda Legal stated that "the new IRS position *should* apply similarly to other situations in which community property rights exist under state law, specifically including that of married same-sex couples." *The IRS Applies "Income-Splitting" Community Property Treatment to California's Registered Domestic Partners, supra* (Q&A #14).

According to Lambda Legal, this should include any married same-sex couple residing in California who married (1) before November 5, 2008 in any country or state, including California, that permitted at the time of the marriage same-sex couples to marry; or (2) on or after November 5, 2008 outside of California in any country or state, such as Canada or Massachusetts, that permitted or permits, as the case may be, at the time of the marriage same-sex couples to marry. *Id.*

### Effect on Same-Sex Couples Outside of California?

The Service should treat taxpayers in another state the same as it treats Californians if the other state applies its community property laws to same-sex couples in a manner similar to California's treatment of RDPs. As of November 2010, according to Lambda Legal, only the states of Washington and Nevada recognize and apply community property treatment to same-sex RDPs. *Id.* (Q&A #15). Therefore, these are the only states that potentially qualify for the same federal tax treatment for their same-sex RDPs.

In Washington and Nevada the Service applies community property laws to heterosexual married couples living in these states for federal income tax purposes. While none of the May 2010 Service documents explicitly address taxpayers other than California RDPs, the principle underlying this treatment should be applied uniformly. There is no apparent basis to treat Washington or Nevada RDPs' community property income any differently than the community property income of heterosexual married couples in these states is treated. If the Service applies community property income-splitting treatment to these states' RDPs, the application should be retroactive to tax years after June 12, 2008 (Washington) and October 1, 2009 (Nevada) (the dates on which these states recognized community property ownership for their same-sex RDPs). Same-sex couples residing in Washington and Nevada, but who formed their legal relationships outside of their state of residence, must register under their respective states' laws as RDPs to be treated as such.

## Conclusions

Mr. Eric Rey, together with his attorney, heroically pursued fair answers to his basic federal tax questions. After several years Mr. Rey and similarly situated California RDPs have received some federal tax guidance. Unfortunately, the federal tax guidance for California RDPs raises many more questions than it answers. Same-sex couples across the United States, including the 18,000 couples married in California before passage of anti-marriage equality amendments, face more uncertainty and complexity as compared to their similarly situated heterosexual counterparts. The Service has stated that its revised position on community property income for California RDPs is consistent with its treatment of heterosexual married

couples filing separate tax returns. This answer ignores the obvious and glaring fact that California RDPs, as well as any same-sex legally committed couple, cannot file jointly for federal income tax purposes. As a result, the comparison is incongruous, awkward, and confusing.

Nevertheless, as the 2011 tax season is upon us, California RDPs are facing complex and time sensitive tax planning issues including whether or not they should amend their 2007, 2008, and 2009 federal income tax returns to incorporate income-splitting as well as whether they should enter into qualifying agreements to recharacterize community property and separate property income. These issues depend on a couple's particular facts and circumstances. Until the Service issues guidance on the community property income of California same-sex married couples as well as Washington and Nevada RDPs, it is unclear whether, when, and to what extent community property income-splitting applies to them. As a result, these couples must continue to consult experienced tax professionals regarding these very complicated tax issues.

Albert Einstein said it best: "The hardest thing in the world to understand is the income tax." This is especially true when state law relationships are recognized selectively based upon the sexual orientation of the parties involved. We hope that uniform and just guidance is forthcoming. Some things should be just a matter of fairness. ■



# BOXSCORE

Since October 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 | 1/10/2011 | 1471, 1472 | Comments on Grandfathering Rules in the HIRE Act and Notice 2010-60 | U.S. Activities of Foreigners and Tax Treaties | Michael Hirschfeld |
| Internal Revenue Service | 1/5/2011 | 103, 141 | Comments on Bond-Financed Grants | Tax Exempt Financing | Maxwell Solet |
| Pension Benefit Guaranty Corporation | 12/22/2010 | 415, 436 | Comments on PBGC Proposed Rule on Reportable Events | Employee Benefits | Harold Ashner, Eleanor Banister |
| Internal Revenue Service | 12/7/2010 | 6662, 6694, 7525 | Comments on Circular 230 Sections 10.2, 10.3, 10.4, 10.5, 10.6, 10.30 and 10.34 | Standards of Tax Practice | Scott Michel, Charles Muller III |
| House Committee on Ways & Means, Senate Committee on Finance | 12/1/2010 | 901, 1013, 1022, 2210, 2664 | Request for Action on Pending Estate & GST Tax Legislation | Section of Taxation, Section of Real Property, Trust and Estate Law | Charles Egerton |
| Internal Revenue Service | 11/15/2010 | 909 | Comments on the Effective Date of Section 909 | Foreign Activities of U.S. Taxpayers | Dirk Suringa |
| House Committee on Ways & Means, Senate Committee on Finance | 11/12/2010 | 894, 1563, 7852, 7874 | Letter Regarding the Treaty Override Provision in H.R. 847 | U.S. Activities of Foreigners and Tax Treaties | Joan Arnold |
| Internal Revenue Service | 11/9/2010 | 54AA, 148, 1273, 1274 | Comments on Issue Price | Tax Exempt Financing | Winnie Tsien |
| House Committee on Ways & Means, Senate Committee on Finance | 11/5/2010 | n/a | Comments on Carried Interest Proposals in Senate Amendment 4386 to H.R. 4213 | Partnerships & LLCs | Adam Cohen |
| Internal Revenue Service | 10/22/2010 | 871 | Comments on the Taxation of Dividend Equivalent | U.S. Activities of Foreigners and Tax Treaties | Matthew A. Stevens |

*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.

BOOK REVIEW

# Why Every Lawyer Needs the New Edition of Employee vs. Independent Contractor Guidebook

## Review of *Legal Guide to Independent Contractor Status* (5th ed. 2010) by Robert W. Wood

By Jonathan R. Flora*

A perennial problem for employers (and their advisors) is classifying workers. Every worker must be slotted into one of two fixed categories: employee or independent contractor. And let's face it—there's a lot of incentive for an employer to prefer the fruits of independent contractor status: no income tax withholding, no payroll or employment tax obligations, no worker's compensation—the list goes on and on. The trouble is, the stakes of misclassification are significant. They run the gamut from liability for failure to withhold income taxes and pay employment taxes to potential exposure on pension and employee benefit plans and employment claims.

Given the stakes and the frequency with which this issue arises, one might expect there would be a clear set of guideposts used for classifying a worker. Yet sadly, the opposite is the case. For example, a traditional and longstanding method used to classify a worker is the Service's so-called 20 factor test. This test is perhaps one of the least helpful the Service has provided—not one of the 20 factors is determinative, and to make planning more difficult, each factor is given different weight depending on the facts and circumstances.

It is against this backdrop that the *Legal Guide to Independent Contractor Status* by Robert W. Wood (5th ed. 2010) (the "Legal Guide") sits as an essential treatise for practitioners facing worker classification issues. Guidance is crucial in this area. Mr. Wood recently issued the fifth edition of the Legal Guide (the first edition was published in 1992). The timing could not be better. Classification of workers continues to be a front burner item for the Service—in fact, it has conducted a series of worker classification audits over the last several months.

## Scope of Work

The Legal Guide's comprehensive scope and exhaustive detail make it a resource practitioners will turn to again and again. The treatise is logically organized in a manner that a tax professional would use approaching the subject (Mr. Wood is, in fact, a prominent tax attorney who practices in San Francisco). First, it addresses the tax treatment of independent contractors and employees. Next, it analyzes how to determine classification. Finally, it lays out the stakes of misclassification. The Legal Guide also includes a chapter on how to draft independent contractor agreements and an appendix of multiple sample documents and checklists.

Worker status turns on the right of control the employer has over the worker, regardless of whether the right is exercised. The right to control is measured through numerous factors. The Service has used the 20 factor test, which looks to training, instructions, hours of work and similar components of the relationship to determine whether there is a sufficient right to control to give rise to employee status. In recent years, the Service has moved away from the 20 factor test to a three factor test (that resembles the 20 factors).

At the crux of the treatise is a chapter devoted to the issue of how to classify a worker. The Legal Guide analyzes the control tests in detail, providing examples and references to applicable rulings. It parses the components of the tests, provides discussions of relevant decisions which have applied them, and posits useful practice tips. In addition, the treatise focuses on specific types of workers to analyze the appropriate classification of each and to discuss applicable rulings and authority. The treatise, for example, examines workers labeled consultants, corporate directors and officers, employment agencies, construction workers and attorneys.

There is general consensus that the agreement between the company and worker will be a very significant factor in the event the relationship is scrutinized. The intention of the parties is a factor for determining classification, and nowhere is the intent better expressed than in the agreement between the parties. While not by itself determinative, it is nevertheless essential that the agreement consistently represent the desired worker relationship.

It is one thing to understand how to apply the relevant factors to an existing relationship. It is quite another thing to prospectively structure a relationship to successfully cope with the factors to achieve the desired classification. The Legal Guide correctly notes that practitioners rarely spend enough time on the front end structuring the relationship, which makes resolving disputes more difficult on the back end. Recognizing the importance of the agreement, the Legal Guide supplements the chapter on how to classify a worker with a separate chapter dedicated to how to draft independent contractor agreements and includes 17 sample agreements (ranging from consulting to work for hire).

* Schnader, Harrison, Segal & Lewis L.L.P., Philadelphia, PA.

## Consequences of Misclassification

Proper classification of a worker may be challenged in various ways. For example, in a well known decision, workers sued Microsoft in the 1990s claiming that they were really employees even though Microsoft treated them as independent contractors. *See Vizcaino v. Microsoft Corp.*, 97 F.3d 1187 (9th Cir. 1996), *modified en banc*, 120 F.3d 1006 (9th Cir. 1997). In that case, the Service in a routine review initially reclassified certain workers as employees, and it required Microsoft to pay withholding taxes and the employer's portion of Social Security and Medicare taxes. Following the reclassification, the workers then sued claiming they should have participated in Microsoft's employee benefit plans.

As noted in the Legal Guide, the decision demonstrates the interaction between tax controversies and other worker status inquiries. It is not uncommon for state taxing authorities also to follow a federal dispute. The stakes are high because employees typically have a much greater arsenal of substantive rights than independent contractors. There are federal labor and employment laws that apply to and protect employees. Employees also have certain rights with respect to participation in employer-sponsored retirement and employee benefit plans. Also relevant to classification is the fact that employees are generally much more likely to bind the employer with respect to tort and contract claims than an independent contractor. The Legal Guide deftly covers all of these areas in separate chapters.

## Section 530 Safe Harbor

If the Service were to challenge a classification, the employer may be able to rely on a safe harbor introduced as section 530 of the Revenue Act of 1978. When it applies, section 530 may relieve an employer of liability for unpaid taxes, as well as penalties and interest. The safe harbor is different from the traditional 20 factor test—it does not turn on control. Instead, it applies when an employer can show that it (1) consistently treated the workers as independent contractors, (2) complied with Form 1099 reporting for the tax years at issue, and (3) had a reasonable basis for treating the workers as independent contractors. The third requirement—reasonable basis—can be met through judicial precedents or administrative rulings, a prior audit, industry custom, or a catch all "other" reasonable basis.

The Legal Guide navigates the elements of the section 530 safe harbor, and it illustrates the application of the safe harbor in various cases.

Throughout the years, the Service has focused on worker status and, given the stakes and the often ambiguous nature of worker status, it will surely continue to do so in the future. The Legal Guide will prove a useful tool when confronting the thorny classification issue and its consequences.

Robert W. Wood's book, *Legal Guide to Independent Contractor Status* (5th Ed. 2010), is available at http://www.taxinstitute.com. Compression bound, including CD, 1,034 pages, $399. ■



# 10th Annual Law Student Tax Challenge

The Section of Taxation would like to congratulate all of the J.D. and LL.M. teams who participated in the 10th Annual Law Student Tax Challenge competition. A total of 95 J.D. submissions and 31 LL.M. submissions were received, making this year's Challenge the most competitive to date. The following ten teams were selected to participate in the oral rounds of the competition, which took place on January 21 at the Tax Section's 2011 Midyear Meeting in Boca Raton. The winners' names are available on the Section's website at: http://www.abanet.org/tax/lstc/.

## J.D. Semi-Finalists

**Cleveland State University College of Law**
Caryn Gross and Michael Tangry
Coach: Deborah A. Geier

**Liberty University School of Law**
Tim M. Todd, Jr. and Melissa M. Ogden
Coach: F. Philip Manns, Jr.

**University of Florida Levin College of Law**
Ben Friedman and Christopher Mikes
Coach: Charlene Luke

**University of Kentucky College of Law**
Leah Chalkley and Patrick Kern
Coach: Jennifer Bird-Pollan

**Samford University School of Law**
Wes Hill and Sims Rhyne III
Coach: Brannon Denning

**William and Mary School of Law**
Peter J. Farrell and Jonathan D. Puvak
Coach: William M. Richardson

## LL.M. Finalists

**Northwestern University School of Law**
Judson Bryant and John Goodell
Coach: Robert R. Wootton

**Temple University School of Law**
Travis Wheeler and Jeanmarie Dunn-Kane
Coach: Andrea Monroe

**University of Denver College of Law**
Jenifer Jewkes and Matthew Wiseman
Coach: Alicia Buckingham

**University of Missouri-Kansas City School of Law**
Nicholas Bracco and Samuel Burnett
Coach: Judith F. Wiseman

The Law Student Tax Challenge was established in 2001 by the Tax Section's Young Lawyers Forum to provide a unique opportunity for law students to research "real-life" tax planning issues and to demonstrate their acquired tax knowledge through their writing and oratory skills before a panel of seasoned practitioners from private practice, government, and academia.

## TAX BITES

# Tax Bites Takes Another Law School Exam

By Barry Kozak*

The Winter 2009 Tax Bites included several clever student responses to Professor Kozak's request for song lyrics with a tax theme. His 2010 summer school exam offered them a similar opportunity: "Because of Steve's stellar guitar playing skills and knowledge of federal income tax law, the chair of the American Bar Association Section of Taxation asks him to sing a song at their September 2010 meeting in Toronto that summarizes some of the tax advantages Congress can provide to taxpayers through the Internal Revenue Code." Once again his students rose to the occasion. Here are some of the more creative responses.

1. To the tune of *Don't Stop Believin'* by Journey —

Just a John Marshall kid
Living in a taxable world
He asked his attorney for some much needed help
Just an LL.M. grad ready to file taxes
She picked up the phone and cried for help

An attorney in a quiet room
The smell of paper and lack of sleep
For a few deductions they can save money
It goes on and on and on and on

Deductions waiting
Up and down the tax return
From business to personal to capital
Casualty/theft loss
Don't forget about charity
All these deductions are just hiding somewhere in the night

Don't stop deducting
Real estate and hobby losses
Don't stop deducting
But watch those limitations

2. To the tune of *Old MacDonald Had a Farm* —

Old Uncle Samuel had a code—T-A-X-E-S
And in this tax code he had a credit—T-A-X-E-S
With a tax credit here and a tax credit there, every where a tax credit—T-A-X-E-S
And in this code he had some deductions—T-A-X-E-S
Deduct business expenses here, deduct capital there, and deduct depreciation everywhere….
—T-A-X-E-S

3. To the tune of *Ring of Fire* by Johnny Cash —

I fell into an audit of my filing
Tax rates went down, down, down
as my deductions went higher
And I earned, earned, earned,
Audits of filing
Audits of filing

4. To the tune of *House of the Rising Sun* by The Animals —

Now the only thing a homeowner needs
Is a mortgage and some luck
He can deduct the interest paid

And save himself a buck

Oh, lawyer, tell your clients
To do what I have shown
Spend your future earnings
On an endless mortgage loan

* Director, Elder Law Program, John Marshall Law School, Chicago, IL.

ABA SECTION OF TAXATION

# PUBLICATIONS

Navigate a constantly changing tax landscape with the Section of Taxation.

Today more than ever, tax professionals need to be aware of new substantive administrative and procedural developments in the law and proposed changes to tax code regulations. For more than 85 years, the ABA Section of Taxation has delivered outstanding service to its members by dedicating resources to providing the most current information and analysis for tax lawyers and tax professionals.

**The Sales and Use Tax Deskbook:** A guidebook that provides in one reliable source all the information that tax managers, attorneys, and accountants are most likely to need about sales and use taxes. Organized by state, each chapter is written and updated each year by some of the most experienced state and local tax practitioners in that state. The chapters are organized in a uniform format to aid the user in quickly and easily finding guidance on particular sales/use tax issues and facilitating multi-state research.
Publication Date: May 2010
Page Count: 1000 (includes CD-ROM)
Member Price: $225

**The Property Tax Deskbook:** Like its sister publication *The Sales and Use Tax Deskbook*, this all-in-one guidebook provides all the information tax managers, attorneys, and accountants are most likely to need about property taxes. Organized by state, each chapter is written and updated each year by some of the most experienced property tax practitioners in that state.
Publication Date: September 2010
Page Count: 900 (includes CD-ROM)
Member Price: $225

**The Supreme Court's Federal Tax Jurisprudence: An Analysis of Fact Finding Methods and Statutory Interpretation from the Court's Tax Opinions, 1801-Present:** This book analyzes almost 1,000 federal tax opinions of the Supreme Court of the United States and synthesizes from them principles for applying the federal tax law, including fact finding, statutory interpretation, presumptions for and against taxpayers, and the so-called doctrines of federal taxation (including substance over form, step transactions, business purpose, sham transactions, the economic substance doctrine and its partial codification in 2010).
Publication Date: June 2010
Page Count: 514
Member Price: $125

**Effectively Representing Your Client Before the IRS:** A comprehensive, easy-to-use handbook for the general tax practitioner, this multi-volume/CD-ROM set includes sample correspondence and forms and hundreds of useful practice tips. It is an excellent resource for attorneys, accountants, and enrolled agents in all stages of representation before the IRS in controversy matters, including exam, appeals, Tax Court, refund actions, and collection matters.
Publication Date: May 2009
Page Count: 1524 (includes CD-ROM)
Member Price: $225
Additional discounts for Nonprofit/Academic/Government institutions are available. Please see the Section website below for details.

**Careers in Tax Law: Perspectives on the Tax Profession and What It Holds for You:** Designed for those considering or beginning a career in tax law, this informative guide presents a series of offerings—autobiographies in miniature—by a broad cross section of working tax professionals. Each contribution stands as a unique story of paths taken, choices made, and lessons learned. In essays divided thematically into chapters, over 75 tax professionals share their unique perspectives, knowledge, and experiences.
Publication Date: April 2009
Page Count: 308
Member Price: $55 ($25 for law students)

**Guide to Nonprofit Governance in the Wake of Sarbanes-Oxley:** Written for directors of nonprofit organizations and practitioners, this guidebook provides a complete overview of the major reforms enacted or triggered by the Sarbanes-Oxley Act, including governance reforms promulgated by the SEC and the Stock Exchanges. Also included are ten key governance principles derived from such reforms, and discussions about the potential challenges and benefits of applying such principles in the nonprofit context.
Publication Date: June 2005
Page Count: 49
Member Price: $18.95

**For more information and to purchase online, please visit www.abanet.org/tax/pubs.**

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| March 21-22, 2011 | **2011 ABA/IPT Advanced Income Tax Seminar**<br>The Ritz-Carlton New Orleans – New Orleans, LA | Tax Section<br>www.abanet.org/tax<br>202.662.8670 |
| March 22-23, 2011 | **2011 ABA/IPT Advanced Sales/Use Tax Seminar**<br>The Ritz-Carlton New Orleans – New Orleans, LA | Tax Section<br>www.abanet.org/tax<br>202.662.8670 |
| March 24-25, 2011 | **2011 ABA/IPT Advanced Property Tax Seminar**<br>The Ritz-Carlton New Orleans – New Orleans, LA | Tax Section<br>www.abanet.org/tax<br>202.662.8670 |
| Mar. 31-Apr. 1, 2011 | **ALI-ABA Advanced Course of Study: Corporate Taxation**<br>The Hilton Washington Embassy Row – Washington, DC | ALI-ABA<br>www.ali-aba.org<br>1.800.CLE.NEWS |
| April 14-15, 2011 | **Tax Planning Strategies - U.S. and Europe Conference**<br>OECD Centre – Paris, France | Tax Section<br>www.abanet.org/tax<br>202.662.8670 |
| May 13, 2011 | **Tax CLE on the Road: Tax Traps and Opportunities in Buying and Selling a Business**<br>Location TBA, Milwaukee, WI | State Bar of Wisconsin<br>www.wisbar.org<br>1.800.728.7788 |
| June 15-17, 2011 | **U.S. – Latin American Tax Planning Strategies Conference**<br>Mandarin Oriental – Miami, FL | Tax Section<br>www.abanet.org/tax<br>202.662.8670 |