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MEMORANDUM

Re: IRS Issues Guidance on Tax Shelters, Material Advisors and Reportable Transactions

From: Samuel A. Mitchell
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Date: November 18, 2004

On November 16, 2004, the IRS released guidance on the new disclosure requirements for material advisors and participants in reportable transactions. The new disclosure provisions under the American Jobs Creation Act of 2004, Pub. L. No. 108-357 ("Jobs Act") include: penalties for failure of a material advisor to file an information return regarding a reportable transaction; penalties for failure of a material advisor to produce a list of investors on request of the IRS; and penalties for failure of a participant to disclose a reportable transaction. The new guidance includes Notice 2004-80, which provides interim rules for the new reporting and list maintenance provisions to be effective until the IRS has a chance to issue regulations to implement the Jobs Act changes. Also, the IRS released four revenue procedures that narrow the reporting requirements on participants and material advisors related to four categories of reportable transactions.

I. Notice 2004-80 Provides Interim Guidance to Material Advisors

The IRS and Treasury have announced their intention to issue regulations related to the disclosure requirements in the Jobs Act. Until that time, the IRS has provided interim rules for these disclosures in Notice 2004-80, which clarifies the requirements for material advisors by providing definitions for key terms, specifying the proper forms and filing due dates and outlining the list maintenance obligations of material advisors.

A. Definitions of Reportable Transactions and Material Advisors

Notice 2004-80 specifies that, for purposes of the newly enacted I.R.C. § 6111(a), a “reportable transaction” is defined in Treas. Reg. § 1.6011-4(b), which provides six categories of reportable transactions. In addition, the rules in Reg. § 301.6112-1(b)(2) (defining transactions with potential for significant tax avoidance) and Reg. § 301.6112-1(c)(2) (defining material advisor) will generally apply for determining whether a transaction is a “reportable transaction” with regard to a material advisor. Therefore, only persons who prepare or provide a “tax statement” on a reportable transaction will be material advisors under the interim guidance. This is significant because the Jobs Act could be read more broadly than the existing regulations. A “tax statement” is defined in Reg. § 301.6112-1(c)(2)(ii) as any statement, written or oral, made to a purchaser, prospective purchaser, or certain others, that relates to a tax aspect that causes the transaction to be reportable. The Notice also clarifies that the fee thresholds in existing regulations under Reg. § 301.6112-1(c)(2), (c)(3) and (d) apply to material advisors, including the minimum fee requirement for a listed transaction (\$25,000 for a transaction with a corporation and \$10,000 for all other transactions). For transactions with significant book-tax differences, the definition of material advisor has been narrowed to apply only to individuals that make tax statements and statements related to the financial accounting treatment of the item(s) that give rise to a significant book-tax difference.

B. Material Advisors Must File Modified Form 8264

The Notice requires material advisors to use existing Form 8264, Application for Registration of a Tax Shelter, to report reportable transactions until the IRS has time to revise or replace the form. Material advisors must complete only parts I (except item 1(b)), IV and V of the form. In addition, material advisors must identify the type of reportable transaction that is being disclosed and describe the facts of the transaction and the potential tax benefits expected to result from the transaction. Material advisors may file a single Form 8264 for substantially similar transactions, and have an affirmative duty to supplement the information on the form to apprise the IRS of any changes.

C. Subject to a Transition Rule, Form 8264 is Due 30 Days After Material Advisor Status is Created

Notice 2004-80 provides that a material advisor must file Form 8264 within 30 days after the person becomes a material advisor. The Notice provides a transitional rule requiring the filing on or before February 1, 2005, for persons that become material advisors after October 22, 2004 (the date of enactment of the Jobs Act) but on or before December 31, 2004. Also, if the material advisor registered the tax shelter under former I.R.C. § 6111 prior to October 22, 2004, that registration may substitute for having to file Form 8624.

D. List Maintenance Requirements

Notice 2004-80 provides that the existing list maintenance requirements in Reg. § 301.6112-1 will apply to the list maintenance requirements imposed by the Jobs Act. New I.R.C. § 6708 imposes a penalty for the failure to provide a list, with an exception for reasonable cause. The list must be furnished within 20 business days of a written request from the IRS (without the protections of the summons procedure) or a penalty of \$10,000 per day for each day after the twentieth day applies. The list is required to be kept in a specified format and must include identification of the investors and information such as a schedule of anticipated investor tax benefits and tax opinions. The list must be maintained for seven years.

II. Revenue Procedures Narrow Requirements on Reportable Transactions

The IRS also issued four revenue procedures that eliminate certain specifically identified transactions as reportable transactions. These procedures apply to the designation of the transactions as reportable and will affect the requirements of both material advisors and participants. Guidance has been issued on the following types of reportable transactions: transactions with contractual protections (Rev. Proc. 2004-65); loss transactions (Rev. Proc. 2004-66, which supercedes prior guidance on loss transactions in Rev. Proc. 2003-24); transactions with significant book-tax differences (Rev. Proc. 2004-67, which supercedes guidance on book-tax differences in Rev. Proc. 2003-25); and transactions with brief asset holding periods (Rev. Proc. 2004-68). The guidance is effective November 16, 2004 for transactions entered into after December 31, 2002. The IRS cautioned that some transactions may still be reportable under other provisions. It is important to note that Rev. Proc. 2004-67 excludes several insurance provisions from the determination of whether there is a significant book-tax difference, including: inside buildup, death benefits or cash surrender value of life insurance or annuity contracts; insurance reserves; and capitalization of policy acquisition expenses.

Please call with questions.