

III.E.1 Mandatory IDRs for Listed Transactions

Overview

Introduction

Sample IDRs are available and are being developed specifically addressing various shelters. The OTSA website has sample IDRs available for downloading. The site for contingent liability shelter sample IDRs is:

http://lmsb.irs.gov/hq/pftg/irc351/downloads/Training/351_resource_guide/sample_IDRs/IRC_351_resource_guide_sample_idrs.htm

LMSB Mandatory IDRs

For examinations open as of April 24, 2002, and opened after April 23, 2002, a mandatory IDR must be issued in all LMSB cases. Its purpose is to determine whether a taxpayer has engaged in any listed transaction or the same as or substantially similar to the listed transactions. See the attached memorandum from Larry Langdon mandating the use of this IDR.

After the memorandum, you will see the answers to some frequently asked questions about IDR's. The IDR itself appears on pages 7-11 of the text.

MEMORANDUM FOR LARGE AND MID-SIZE BUSINESS DIVISION EXECUTIVES,
MANAGERS AND AGENTS

FROM: Larry R. Langdon s/s Debbie Nolan July 26, 2002
Commissioner, Large and Mid-Size Business
Division

SUBJECT: Abusive Tax Shelters Mandatory Information Document
Request (IDR)

In order to further strengthen our efforts to combat abusive tax shelters, the Large and Mid-Size Business Division's (LMSB) Tax Shelter Committee has approved a new revised IDR to be used in LMSB examinations, effective immediately. This IDR, developed by the Office of Tax Shelter Analysis (OTSA) and LMSB Counsel, requests appropriate information concerning Listed Transactions, as provided in IRS Notice 2001-51, 2001-34, I.R.B. 190 and subsequent notices. We will update the IDR as new transactions are added.

Use of this IDR is mandatory in all LMSB corporate examinations in process and in any new corporate examination, including limited scope examinations. The IDR may also be issued in all other LMSB examinations, including Partnerships, Trusts and other forms of enterprise.

I want to make it very clear that issuance of this IDR is not to be limited to only one cycle or one examination. The IDR must be issued at the beginning of all LMSB Corporate audits and reissued at the beginning of each subsequent cycle and each subsequent examination.

Team managers may exercise discretion in situations where the IDR should be modified or not issued, based on unique facts and circumstances. These situations should be the exception, rather than the rule and team managers are encouraged to consult with upper management and OTSA in these situations. We have attached a copy of the mandatory IDR and a list of frequently asked questions for your further guidance.

If you have any questions on this matter, please contact Frank Y. Ng, Director, PFTG, at (202) 283-8461 or David G. Harris, Manager, Office of Tax Shelter Analysis, at (202) 283-8386.

Attachments

cc: Linda Burke
Dave Robison
Joe Kehoe

**LARGE & MIDSIZE BUSINESS DIVISION (LMSB)
OFFICE OF TAX SHELTER ANALYSIS**

*Mandatory Information Document Request
FAQs – July 15, 2002*

1. Q. Should this IDR be issued to C corporations only, or does it apply to S corporations and partnerships, as well?
 - A. The IDR must be issued in all LMSB “C” Corporation examinations, including limited scope examinations. It may also be issued in examinations of “S” Corporations, Partnerships, and all other entities subject to LMSB jurisdiction. Team managers may exercise discretion in situations where the IDR should be modified or not issued, based on unique facts and circumstances, and are encouraged to consult with the Office of Tax Shelter Analysis (OTSA) at: otsa@irs.gov

2. Q. When should the IDR be issued?
 - A. The IDR must be issued at the commencement of all newly started LMSB “C” Corporation examinations and must be re-issued each subsequent cycle. It should also be issued during examination of cases already in progress. Exceptions to this latter requirement would be in situations where the examination is in its closing stages. Team managers should exercise judgement on a case by case basis regarding these exceptions.

3. Q. In a Coordinated Issue Case (CIC) just ended, I had issued the mandatory IDR and the taxpayer had indicated a negative response. I am now planning to begin auditing the subsequent cycle. Do I have to issue the Mandatory IDR again?
 - A. Yes. The mandatory IDR must be issued in every LMSB examination in each and every cycle, regardless of the taxpayer’s response in the previous cycle. Each cycle stands on its own and the IDR must be re-issued at the beginning of each new examination and in every new cycle.

4. Q. Does the Service have standard procedures for issuing a new IDR after a new listed transaction is identified?
 - A. As additional tax shelter vehicles are identified, the IDR will be updated and posted on the OTSA intranet website. The OTSA web site may be accessed at <http://lmsb.irs.gov/hq/pftg/otsa/index.htm>.

5. Q. As additional notices are issued, should examination teams be issuing additional or supplemental IDRs?

A. Yes, team managers should issue additional or supplementary IDRs whenever new notices are issued. However, in unique circumstances, team managers may also exercise discretion and not issue a supplemental or additional IDR. Any decision should be guided by the stage of the examination, the nature of the response received to the first inquiry, and other information otherwise available to the team manager. If, after weighing all the information available, the team manager has reason to believe that the taxpayer has not engaged in shelters other than those already queried, the team manager may decide not to issue additional IDRs.

6. Q. If the taxpayer accuses the agent of being on a fishing expedition due to the volume of the request and refuses to provide all of the information requested in the pro-forma IDR, how vigorously should the agent pursue the matter? If a summons is issued will counsel take enforcement action?

A. Issuance of the IDR is necessary to determine whether the taxpayer has engaged in tax shelter activities. The request is sufficiently specific to permit the taxpayer to ascertain the nature of the information requested. Should the taxpayer decline to respond or provide only a portion of the information requested, the team manager must decide if a summons will be issued. In arriving at this determination, the team manager should consider how forthcoming the taxpayer has been on other requests, the likelihood that the taxpayer is engaged in tax shelter activity and the impact of disparate treatment amongst similarly situated taxpayers.

In those situations where the taxpayer's response is unacceptable, the team manager should elevate the matter up the local chain of command and consult with local counsel regarding the issuance of a summons. As tax shelters are designated a top priority for the Service, non-compliance by the taxpayer should be dealt with urgently and aggressively.

7. Q. Following Announcement 2002-2 some taxpayers indicated they wanted to make disclosures, but were concerned that the production of certain documents and opinions might be a waiver of the attorney-client privilege. In response, the Service crafted an agreement stating it would not assert that the production of documents under the announcement caused a waiver of privilege. Are there similar procedures in place for documents provided in response to this IDR?

A. There is no similar procedure for documents furnished in response to this IDR. The response to questions raised by the taxpayer regarding attorney-client privilege should be coordinated with local counsel. [Note that the privilege

agreement referred to in the question was not a concession that a claimed privilege applied. The agreement also explicitly left open the ability of the IRS to argue that the claimed privilege did not apply for another reason.]

8. Q. If a team was already aware of specific tax shelter transactions that the taxpayer had engaged in, would it be permissible to modify the IDR to exclude those items? If not excluded, the taxpayer may accuse the team of making duplicate requests?

A. The request may be modified to exclude specific transactions that the team is aware of. This should be done either by way of a footnote to the IDR, by way of a cover letter or by way of dialogue with the taxpayer before the IDR is issued. However, the specific type of listed transaction should not be eliminated from the IDR. There is a possibility the taxpayer may have engaged in multiple transactions of a similar type.

9. Q. Should the IDR request an interview with the key players in any identified transaction because of the advantage of a face-to-face discussion over a written response? If so, who should be interviewed?

A. The IDR requests the taxpayer to provide a “list of all participants and their roles in the transaction, as well as the names and job titles of corporate officers or employees who would be available to meet with Service personnel. This request implies that the Service would like to know the identity of those individuals who have first hand knowledge of the transactions. When evaluating the transactions, the team may determine that it is advisable to conduct interviews of those involved. Whether or not the list of names is returned by the taxpayer, examiners should consider interviews of the chief financial officer, chief executive officer, board members and others who would customarily make investment decisions.

Also, when evaluating the taxpayer’s response, the team may wish to consider whether or not the taxpayer has made reasonable efforts to determine its use of, and participation in, tax shelters. The team may interview such taxpayer personnel as it deems necessary to achieve that assurance.

10. Q. The IDR requests information for “any transactions that are the same as, or substantially similar to any listed transactions”. Taxpayers appear to be interpreting any difference between their facts and those of the listed transactions as justifying the withholding of information. Is there some way to clarify what is a substantially similar transaction?

A. Some taxpayers and promoters have interpreted the “substantially similar” standard in an overly narrow manner to avoid disclosure. Some have made subtle or insignificant changes to a listed transaction in order to claim that their transactions are different and do not require disclosure. Treasury Decision 9000, issued June 14, 2002, modified regulation sections 1.6011-4T and 301.6111-2T to clarify that the term “substantially similar” includes any transaction that is expected to obtain the same or similar types of tax benefits and that either is

factually similar or based on the same or similar tax strategy. Further, taxpayers are cautioned that the term “substantially similar” must be broadly construed in favor of disclosure. The IDR has been revised to ensure that taxpayers broadly construe the term “substantially similar”.

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LISTED TRANSACTIONS

The Internal Revenue Service has identified certain transactions as "listed transactions" for purposes of §1.6011-4T(b)(2) of the temporary Income Tax Regulations. The IRS considers transactions that are the same as or substantially similar to listed transactions to be tax avoidance transactions. Attached below is a summary of the listed transactions as of the date of this IDR. The purpose of this IDR is to determine whether [Taxpayer] has directly or indirectly participated in transactions that are the same as or substantially similar to any listed transaction. Please list each transaction that is the same as or substantially similar to a listed transaction in which [Taxpayer] directly or indirectly participated and that affects [Taxpayer's] Federal income tax liability for any year under examination. The rules of §1.6011-4T apply to determine whether a taxpayer has directly or indirectly participated in a transaction and whether a transaction is the same as or substantially similar to a listed transaction. A taxpayer will have indirectly participated in a listed transaction if the taxpayer's Federal income tax liability is affected (or in the case of a partnership or S corporation, if a partner's or shareholder's Federal income tax liability is reasonably expected to be affected) by the transaction even if that taxpayer is not a direct party to the transaction. Moreover, a taxpayer will have indirectly participated in a listed transaction if the taxpayer knows or has reason to know that the tax benefits claimed from the taxpayer's transaction are derived from a listed transaction. See §1.6011-4T(a)(1) and (2). The term substantially similar includes any transaction that is expected to obtain the same or similar types of claimed tax benefits and that is either factually similar or based on the same or similar tax strategy. Receipt of an opinion concluding that the tax benefits from [Taxpayer's] transaction are allowable is not relevant to the determination of whether [Taxpayer's] transaction is the same as or substantially similar to a listed transaction. The term substantially similar must be broadly construed in favor of disclosing under this IDR. See §1.6011-4T(b)(1)(i) For each transaction identified, please provide the following:

1. A description of the transaction, including all material facts.
2. A description of [Taxpayer's] tax treatment of the transaction, including tax benefits claimed on the return. In describing the tax treatment, include all tax rules or mechanics that affect, give rise to, or result in the claimed tax benefit.
3. Information identifying the amounts involved and the General Ledger accounts affected by any part of the transaction. Please trace all identified items and amounts as line items on the tax returns.
4. All contracts and other transactional documents, including agreements, instruments, and schedules. If such information is too voluminous, then, in the alternative, provide an index that lists and describes all such contracts and transactional documents.
5. Complete copies of all documents and other materials, including legal opinions and memoranda, provided by any party that promoted, solicited, or recommended [Taxpayer's] participation in the transaction.

6. All internal documents used by [Taxpayer] in its decision making process, including, if applicable, information presented to [Taxpayer's] Board of Directors, Audit and Finance Committee, and any other committee.
7. Complete and unredacted minutes of the Board of Directors, Audit and Finance Committee, and any other committees that related, directly or indirectly, to the transaction.
8. All legal, accounting, financial, and economic opinions and memoranda secured by or on behalf of [Taxpayer] in connection with the transaction.
9. A list of all participants and their roles in the transaction.
10. The names and addresses of all parties who promoted, solicited, or recommended [Taxpayer's] participation in the transaction and to whom [Taxpayer] paid fees or other compensation in connection with [Taxpayer's] decision to participate in the transaction.

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11. The name(s) and job titles of officers and other employees of [Taxpayer] familiar with the transaction and who are available to meet with the audit team within two weeks of the date of this IDR.

Privilege

For each document withheld because of a claim of privilege, please provide the following:

- a. The name and title of the author;
- b. The date of the document;
- c. The names, titles, and addresses of all recipients of the documents;
- d. The subject matter of the document;
- e. The privilege claimed;
- f. The portions of the document for which there is no claim of privilege; and
- g. For any opinion or memoranda described in item 8 above, the conclusions reached in the opinion or memorandum.

Definitions and other instructions

- a. [Taxpayer] means all (1) entities that form a part of the consolidated group, and (2) entities over which [Taxpayer] exercises legal or effective control.
- b. Provide full and complete documents. Also, provide non-identical copies of all items requested in this IDR. Please note and explain any deviation or difference between the original and the copy.
- c. This request applies to the years [years].

Summary of listed transactions -- See Notice 2001-51, 2001-34, I.R.B. 190 (August 20, 2001) (identifying all listed transactions through Notice 2001-45). The transactions listed in Notice 2002-51 and later transactions are summarized below.

- (1) Rev. Rul. 90-105, 1990-2 C.B. 69 (transactions in which taxpayers claim deductions for contributions to a qualified cash or deferred arrangement or matching contributions to a defined contribution plan where the contributions are attributable to compensation earned by plan participants after the end of the taxable year).
- (2) Notice 95-34, 1995-1 C.B. 309 (certain trust arrangements purported to qualify as multiple employer welfare benefit funds exempt from the limits of §§ 419 and 419A of the Internal Revenue Code).
- (3) Notice 95-53, 1995-2 C.B. 334 (certain multiple-party transactions intended to allow one party to realize rental or other income from property or service contracts and to allow another party to report deductions related to that income (often referred to as "lease strips")).
- (4) Part II of Notice 98-5, 1998-1 C.B. 334 (transactions in which the reasonably expected economic profit is insubstantial in comparison to the value of the expected foreign tax credits).

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- (5) Transactions substantially similar to those at issue in *ASA Investerings Partnership v. Commissioner*, 201 F.3d 505 (D.C. Cir. 2000), and *ACM Partnership v. Commissioner*, 157 F.3d 231 (3d Cir. 1998) (transactions involving contingent installment sales of securities by partnerships in order to accelerate and allocate income to a tax-indifferent partner, such as a tax-exempt entity or foreign person, and to allocate later losses to another partner).
- (6) Treas. Reg. § 1.643(a)-8 (transactions involving distributions described in § 1.643(a)-8 from charitable remainder trusts).
- (7) Rev. Rul. 99-14, 1999-1 C.B. 835 (transactions in which a taxpayer purports to lease property and then purports to immediately sublease it back to the lessor (that is, lease-in/lease-out or LILO transactions)).
- (8) Notice 99-59, 1999-2 C.B. 761 (transactions involving the distribution of encumbered property in which taxpayers claim tax losses for capital outlays that they have in fact recovered).
- (9) Treas. Reg. § 1.7701(l)-3 (transactions involving fast-pay arrangements as defined in § 1.7701(l)-3(b)).
- (10) Rev. Rul. 2000-12, 2000-11 I.R.B. 744 (certain transactions involving the acquisition of two debt instruments the values of which are expected to change significantly at about the same time in opposite directions).
- (11) Notice 2000-44, 2000-36 I.R.B. 255 (transactions generating losses resulting from artificially inflating the basis of partnership interests).
- (12) Notice 2000-60, 2000-49 I.R.B. 568 (transactions involving the purchase of a parent corporation's stock by a subsidiary, a subsequent transfer of the purchased parent stock from the subsidiary to the parent's employees, and the eventual liquidation or sale of the subsidiary).
- (13) Notice 2000-61, 2000-49 I.R.B. 569 (transactions purporting to apply § 935 to Guamanian trusts).
- (14) Notice 2001-16, 2001-9 I.R.B. 730 (transactions involving the use of an intermediary to sell the assets of a corporation).
- (15) Notice 2001-17, 2001-9 I.R.B. 730 (transactions involving a loss on the sale of stock acquired in a purported § 351 transfer of a high basis asset to a corporation and the corporation's assumption of a liability that the transferor has not yet taken into account for federal income tax purposes).
- (16) Notice 2001-45, 2001-33 I.R.B. 129 (certain redemptions of stock in transactions not subject to U.S. tax in which the basis of the redeemed stock is purported to shift to an U.S. taxpayer).
- (17) Notice 2002-21, 2002-14 I.R.B. 730 (April 8, 2002) (transactions involving the use of a loan assumption agreement to claim an inflated basis in assets acquired from another party).
- (18) Notice 2002-35, 2002-14 I.R.B. 992 (May 28, 2002) (transactions involving a notional principal contract to claim current deductions for periodic payments while disregarding the accrual of a right to receive offsetting payments in the future).

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(19) Rev. Rul. 2002-46, 2002-29 I.R.B. 1 (June 28, 2002) (identifying as substantially similar to Rev. Rul. 90-105 a transaction in which a taxpayer makes contributions to a qualified cash or deferred arrangement under §401(k) or a defined contribution plan as matching contributions under §401(m) and the contributions are designated as satisfying a liability established before the end of the taxable year but are attributable to compensation earned by plan participants after the end of that taxable year). See Notice 2002-48, 2002-29 I.R.B. 1 (July 22, 2002) for certain variations to Rev. Rul. 90-105 that are not listed transactions.

(20) Notice 2002-50, 2002-28 I.R.B. 1 (July 15, 2002) (transactions involving economic straddles within a tiered partnership structure and a transitory partner to allocate income tax deductions to the taxpayer - often referred to as the Partnership Straddle Tax Shelter).