

The Erwin N. Griswold Lecture

Dealing With the Aggressive Corporate Tax Shelter Problem James P. Holden

I. INTRODUCTION

I am deeply honored to be invited to appear before the Fellows of this College and to deliver the 1999 Annual Erwin N. Griswold lecture. When I take account of my distinguished predecessors in this role, I am even more mindful of the great privilege it is to appear before you.

One of the perquisites of being the speaker at an event such as this is the opportunity to select the topic to be discussed. The principal constraint, of course, is the need to choose something of interest to you, the audience. I hope that I have satisfied that responsibility in having chosen to discuss the subject of aggressive corporate tax shelters, a topic that has generated considerable interest over the past several years.

II. THE NATURE OF THE AGGRESSIVE CORPORATE TAX SHELTER PROBLEM

Many of us have been concerned with the recent proliferation of tax shelter products marketed to corporations. Most tax lawyers have witnessed the promotion and sale of these products to their clients, and many tax lawyers have been asked by their clients to evaluate the products, often under conditions requiring that the lawyer extend a pledge of confidentiality for the benefit of the promoter of the product. While some such products may be based on a sound interpretation of the tax law, many are not. Many depend upon "aggressive" interpretations that distort a preference or take advantage of a structural flaw to produce an unintended tax saving to a corporate purchaser of the shelter.

The marketing of these products tears at the fabric of the tax law. Many individual tax lawyers with whom I have spoken express a deep sense of personal regret that this level of Code gamesmanship goes on. Notwithstanding their feelings on the subject, many of these lawyers regard themselves obliged by client loyalty and competitive considerations to comply with requests that they provide services that support these activities. I would like to consider with you today the avenues that are available to discourage this marketing activity and to help to restore the integrity of the tax laws.

III. AVENUES FOR DEALING WITH THE AGGRESSIVE CORPORATE TAX SHELTER PROBLEM

Four mutually complementary avenues are available to reach the goal to restrict the marketing of aggressive tax shelter products. First, the substantive law can be amended, by statute or by regulation, specifically to deny the legal interpretation that is needed for a shelter to operate. Second, penalties may be imposed on purchasers of shelters that do not survive when they are tested under the substantive law. Third, professional responsibility standards may be established for tax practitioners who advise purchasers of tax shelter products. Fourth, downside risk may be created for promoters of such products.

A. *Changing the Substantive Tax Law to Preclude Aggressive Corporate Tax Shelters*

The first avenue, changing the substantive law, is always available and always appropriate as a remedy for identified structural problems in the tax law that permit undesirable shelter activity, but it is generally effective only with respect to identified issues. Aggressive shelters may continue to be conceived in unanticipated corners of the tax law, and they will be sold and ultimately presented to the courts. If a shelter is not sustained under the substantive law, then no change in the substantive law will be required

to deal with that shelter. If instead a shelter is sustained when challenged under the substantive law, and if the result is deemed undesirable from a tax policy perspective, then the substantive law should be amended to deny the shelter existence. But this is, by its nature, a reactive process. It is also one that is both time consuming and resource intensive. In any event, a detailed discussion of the substantive law relative to aggressive corporate tax shelters is beyond the scope of my discussion today. I would like instead to turn to and evaluate the other three avenues to controlling aggressive corporate tax shelter activity, *i.e.*, imposing penalties on purchasers of such products, establishing rules of practice for practitioners who advise purchasers, and creating downside risk for promoters.

B. Imposing Penalties on Purchasers of Aggressive Corporate Tax Shelter Products that Fail Substantive Law Tests

The second avenue for controlling aggressive corporate tax shelters involves the imposition of penalties on purchasers of shelter products that fail when they are tested under the substantive law. A corporate taxpayer contemplating an aggressive tax shelter investment naturally takes into account the risk that the shelter may fail to be sustained if challenged under the substantive tax law, with consequent tax and interest liabilities. This risk may not be a significant deterrent because the tax incurred would have been required to be paid if the shelter had not been purchased, and the interest cost may be justified on use-of-money principles.¹

However, beyond the risk that failure of the shelter will produce tax and interest liabilities, the corporate officers considering an aggressive tax shelter investment must take into account the added risk that a monetary penalty may be imposed if the shelter does not prevail when challenged. The principal penalty risk lies in the twenty percent accuracy-related penalty of section 6662(d). Insofar as the language of section 6662(d) is concerned, this penalty is imposed on a no-fault basis. According to the terms of section 6662, if a corporation is determined to have a substantial understatement of income tax and the understatement is attributable to a tax shelter, the penalty is imposed without regard to any other factor.² This automatic application of the penalty for corporate tax shelters is effective for all transactions occurring after December 8, 1994, when section 6662(d) was amended to deprive corporations of the "substantial authority" and "reasonable belief" defenses that continue to be available under that section to noncorporate taxpayers.³

More important, perhaps, is the broadening of the definition of the term "tax shelter" that occurred in 1997. Effective for transactions entered into after August 5, 1997, a tax shelter includes any entity, plan, or arrangement that has as a significant purpose the avoidance or evasion of Federal income tax.⁴ This statutory definition of the term "tax shelter," which has yet to be addressed in regulations, is remarkably broad in its reach. Indeed, a distinguished tax professor recently observed in an article in *Tax Notes* that the definition sweeps in almost all corporate actions.⁵ Since corporations have an obligation to their

¹ In addition, some corporations might factor in a reduction of risk based on the possibility that the corporation might not be audited or that the issue might not be discovered. However, this discount should not be significant for the principal targets of the aggressive corporate tax shelter market. Most of the purchasers in this market are large corporations subject to continuous audit under the CEP program, and most of the shelters generate tax consequences large enough to be evident either in the reconciliation of book income to taxable income on the tax return or in some other respect.

² Disclosure of a tax shelter position does not mitigate the accuracy-related penalty.

³ Pub. L. No. 103-465, § 744(a), 108 Stat. 4809 (1994) (codified at I.R.C. § 6662(d)).

⁴ Pub. L. No. 105-34, § 1028(c)(2), 111 Stat. 788 (1997)(codified at I.R.C. § 6662(d)(2)(C)).

⁵ See Calvin Johnson, *Corporate Tax Shelters, 1997 and 1998*, *Tax Notes Today* (Sept. 28, 1998) (LEXIS, FEDTAX lib., TNT file, elec. cit. 98 TNT 187-84).

shareholders to minimize corporate expense, including Federal income tax expense, the theory is that virtually all of their actions have a significant tax-reducing objective.

Despite the fact that section 6662(d) mandates imposition of the twenty percent accuracy-related penalty on any failed corporate tax shelter, this mandate is somewhat tempered by section 6664(c). That section permits the corporation to avoid the twenty percent penalty for any underpayment if it is able to establish that there was reasonable cause for the underpayment and that the corporation acted in good faith with regard to it. However, this particular relief valve should not offer a great deal of comfort to the prospective corporate purchaser of an aggressive tax shelter product. This is so because the regulations under section 6664(c) establish a standard sufficiently high that it is unlikely to be satisfied by an aggressive tax shelter product.⁶ The regulations provide that, to escape the penalty, the corporation must establish three things. First, it must establish that there was substantial authority for the position taken. Second, it must establish that it had a reasonable belief that the position had a more than fifty percent likelihood of being sustained if challenged (based either on the corporation's own research or an unambiguous opinion of a tax professional). Third, it must establish legal justification for the position. However, even where these three factors are established, the regulations nonetheless deny relief if the corporation's participation in the shelter lacked significant business purpose, if the tax benefits claimed were unreasonable in relation to the corporation's investment in the shelter, or if the corporation agreed with the promoter to protect the confidentiality of the product.

It is reasonably clear that most of the truly aggressive tax shelter products will not be able to satisfy this regulatory standard for escaping penalty. Seldom will substantial authority exist, and seldom will the position realistically be assessed as more-likely-than-not correct; either in internal research or in an opinion from a tax practitioner. Even where substantial authority and a more-likely-than-not assessment do exist, the penalty may yet be imposed if there was not sufficient business purpose or if the corporate investment was too modest in relationship to the tax benefits sought.

The Treasury Department needs to issue regulations interpreting the term "tax shelter" under the 1997 version of section 6662(d). In this respect, it has two broad choices. On the one hand, it may define the term very broadly, sweeping a wide variety of tax reduction activity into the potential penalty box and allowing only those activities that satisfy the high standard of the section 6664(c) regulations to escape penalty. Alternatively, it can narrow the definition of tax shelter in section 6662(d), making the net less inclusive and permitting the more defensible tax saving activities to escape tax shelter classification in the first cut.

It seems to me preferable to pursue the first option, defining broadly and allowing escape only over the high hurdle of the section 6664(c) regulations. The merit of this option is that it presents greater evidence of downside risk to the potential corporate purchaser of a tax shelter product. The *in terrorem* effect of an inclusive definition, coupled with an uncertain escape route, is greater than that of a narrower definition that risks being gamed by imaginative planning.

I should note in passing that the current definition of a tax shelter, that is, any "plan" that has a substantial purpose to avoid income tax, is not limited to tax shelter products marketed by third parties. The definition is broad enough to include a plan developed by a taxpayer, with or without outside assistance. For example, a plan to utilize a particular financing technique, or a plan to utilize net operating loss carryovers in a particular way, might constitute a tax shelter if a significant purpose of the plan is to reduce Federal income tax. The consequence of tax shelter classification is to put a premium on the accuracy assessment for the plan. The taxpayer must determine whether substantial authority exists,

⁶ See Reg. § 1.6664-4(e).

whether the tax result can reasonably be viewed as more-likely-than-not correct, whether there is sufficient business purpose, and whether the tax benefits from the plan are unrealistically high. If the taxpayer has doubts as to any of these elements and yet elects to go forward, it should recognize the high risk that the accuracy-related penalty will be imposed if the plan is challenged and not sustained on its merits. But my topic today is focused on tax shelter products marketed by third parties and not on taxpayer-initiated tax planning.

Whether Treasury chooses to construe the 1997 definition of "tax shelter" broadly or narrowly, any construction that it adopts will surely be broad enough to reach all tax saving activity that can reasonably be labeled aggressive. That being so, it is apparent that existing law casts a penalty net broad enough to capture and penalize almost any activity that could be characterized as an aggressive corporate tax shelter that fails to be sustained under the substantive law. If this is true, and I believe that it is, why is there such a broad perception that aggressive corporate tax shelter sales continue unabated? Why is it that this very real penalty threat does not deter corporate purchasers of aggressive shelter products?

Perhaps corporate officers have not become aware of the wide scope of the penalty net and the narrow nature of the escape valve. Or perhaps the perception of continued sales activity is erroneous, and in fact aggressive corporate tax shelter activity has diminished in the wake of the 1997 amendment broadening the definition of tax shelter. On the other hand, if the perception of increased (or undiminished) activity is accurate, this suggests that the existing level of downside risk is not high enough to have an effect on corporate decision-making. In that case, the appropriate response would be to increase the accuracy-related penalty rate from twenty percent to some higher level, perhaps forty or fifty percent.

It may be too early to evaluate whether the 1997 legislation broadening the definition of the term "tax shelter" has had an impact, and perhaps we should wait a year or two before concluding that an increase in the penalty rate is needed. In that period, corporations may become more aware of and respond to the increased penalty risk. However, increasing the penalty rate is an option that should be kept at hand. At some level, an assured penalty that will be imposed on failed corporate tax shelters should be effective to deter potential purchasers of aggressive products.

C. *Establishing Professional Standards for Practitioners Who Advise Purchasers of Corporate Tax Shelter Products*

The third avenue for controlling aggressive corporate tax shelters involves penalties and professional standards for tax practitioners who advise purchasers of these products. The principal penalties of relevance here are the preparer penalties under section 6694. Under section 6694(a), a preparer is subject to penalty for any understatement of liability attributable to a position that is frivolous, whether or not the position is disclosed, unless the preparer is able to establish reasonable cause and good faith. Under section 6694(b), a preparer is subject to penalty for any willful attempt to understate liability or for any reckless or intentional disregard of rules and regulations.⁷

It does not seem to me that the preparer penalties are likely to play a significant role in controlling the marketing of aggressive corporate tax shelters. The definition of "preparer" in the regulations generally excludes legal advice given on a pre-transaction basis,⁸ and it excludes corporate employees who prepare their employer's return.⁹ I would not attempt to alter the preparer penalties in an effort to make them more

⁷ Section 6694(b) does not offer a reasonable cause and good faith escape option.

⁸ See Reg. § 301.7701-15.

⁹ Although corporate employees may be subject to the aiding and abetting penalty of section 6701, the high standards for the application of that penalty make it an unlikely candidate for controlling corporate tax shelter activity.

relevant to corporate tax shelters. The preparer penalties are useful and effective to influence the great army of commercial return preparers, who mainly interpret and apply tax law at the most basic personal levels. Aggressive corporate tax shelters are not marketed at these levels, and return preparers are not generally called upon to advise with respect to them.

The area more relevant to the aggressive corporate tax shelter problem is that of tax practitioner standards under Circular 230, which prescribes the regulations that govern all who practice before the Internal Revenue Service. At present, section 10.33 of Circular 230 provides standards for those who author tax shelter opinions. However, this section, which is patterned on ABA Formal Opinion 346, is targeted specifically at tax shelter opinions that are designed to be included or described in tax shelter offering materials that are publicly distributed. The rules in section 10.33 are not easily adapted for application to practitioners who advise prospective purchasers in a one-to-one relationship.

In order to provide a professional standard more directly applicable to practitioners who advise shelter purchasers, I recommend that Circular 230 be amended by adding a new section 10.35. This new section would provide standards for practitioners who are asked to furnish their clients with "more likely than not opinions" under section 6664(c) to assist in establishing the reasonable cause and good faith defense to the accuracy-related penalty.¹⁰ A draft copy of suggested language for this new section accompanies the written version of this lecture. In essence, the draft states that a practitioner providing a more-likely-than-not opinion is required to evaluate all relevant facts, to relate the law to those facts, to identify all material legal issues, to evaluate the relevance and persuasiveness of existing authority, and to determine and demonstrate that substantial authority exists for the position taken. In the absence of specific favorable authority, the opinion must conclude that the position taken is based on a well-reasoned construction of the applicable statutory provisions. The opinion is required to state unambiguously that there is a greater than fifty percent likelihood that the tax treatment of the position will be upheld if challenged by the Service. The existence of such a provision in Circular 230 would make it more likely that practitioners asked to provide their clients with opinions concerning proposed investments in aggressive tax shelters would either find the high standards satisfied or would decline to provide the opinion.

In addition, this proposed amendment of Circular 230 would make it unprofessional for a tax practitioner to agree to a confidentiality provision of the kind commonly included in the marketing of corporate tax shelter products. If a practitioner becomes aware of a construction of the tax law that might benefit his or her clients generally, it is unprofessional, and likely a conflict of interest, to agree, in the context of serving one client, that such knowledge will be restricted to the benefit of that client. If a practitioner wishes to enter into an agreement to benefit one client that will restrict service to other clients, he or she should withdraw from representing the other clients who are potentially prejudiced by the agreement. I suspect that most tax professionals would applaud the inclusion of such a rule in Circular 230. It would give them a clear and legitimate basis for declining to enter into confidentiality arrangements of this character when asked to do so by a client in order to satisfy the demands of a promoter.

I would also amend Circular 230 to make clear its wide scope of application. At the present time, Circular 230 defines "practice before the Internal Revenue Service" as essentially limited to making presentations to and communicating with the Service on behalf of taxpayers.¹¹ The definition says nothing about providing tax advice to taxpayers. Yet some important provisions of Circular 230 are inoperative unless providing tax advice constitutes practice before the Service and is subject to regulation under Circular

¹⁰ This standard would be applicable as well for opinions provided to individuals who seek to avoid the accuracy-related penalty for tax shelter understatements by establishing a reasonable belief that the position was more-likely-than-not correct under Regulation section 1.6662-4(g)(1).

¹¹ 31 C.F.R. § 10.2(e) (1994).

230. Thus, the tax shelter opinion standards established by section 10.33 could have no effect unless the provision of such opinions falls within the definition of practice before the Service. Moreover, section 10.34, which establishes the realistic possibility standard for advice related to tax return positions, could have no effect unless the providing of such advice is practice before the Service. And, new section 7525, which establishes a privilege for tax advice communications between nonlawyer practitioners and their clients, defines the term "tax advice" as advice given within the scope of one's authority to practice before the Service. Thus, if practice before the Service under Circular 230 does not include the giving of tax advice to clients, the new privilege would not apply to anything, hardly a result contemplated by Congress.

For these reasons, attention should be given to broadening the definition of practice before the Service that is now contained in Circular 230. When that is done, the desired reach of Circular 230 should be considered. Since all lawyers and all CPAs are automatically admitted to practice before the Service,¹² all lawyers and CPAs who provide tax advice should be subject to regulation in that activity under Circular 230, whether or not they ever intend to set foot in an office of the Service or to communicate with the Service on behalf of a taxpayer. And all of those lawyers and CPAs should be made aware of the fact that they may not maintain a partnership with a person who has been suspended or disbarred from practice before the Service under Circular 230.¹³ If this breadth of application were made explicit in Circular 230, I believe that it would have a salutary effect by making tax advisors more conscious of their professional obligations under Circular 230.

Having just mentioned the new tax practitioner-client privilege, I might at this point observe as an aside that section 7525 withholds the privilege from written communications between a practitioner and a corporate representative in connection with the promotion of the participation of the corporation in a tax shelter. This restriction on the application of the new privilege is not likely to have any significant effect because, in the context of penalty defense, tax advice received from a professional is ordinarily being offered to show reasonable cause and good faith. When professional advice is so offered, any privilege that might otherwise have attached to it is waived, whether it be the attorney-client privilege or the new practitioner-client privilege.

My final concern with Circular 230 does not relate to its content but to the relatively low status that the office of the Director of Practice has been accorded in recent years in the hierarchy of the Service and the Treasury. Until 1982, the Director of Practice was attached to the office of the General Counsel of the Treasury Department. That separation from the Service was judicious because, in the sometimes-adversarial relationship between the Service and tax practitioners, it is anomalous to have one's adversary in control of the disciplinary machinery. If the office of the Director of Practice is to remain within the Internal Revenue Service; it should be elevated to the level of the Taxpayer Advocate and given comparable independence from the general workings of the Service. Operationally, the Director of Practice should become far more visible in exercising regulatory responsibility. At a minimum, the office should periodically publish redacted descriptions of disciplinary actions taken in order to provide guidance to practitioners generally.

The Director of Practice is the only official who exercises disciplinary authority over all individuals who practice before the Service. Consequently, the Director of Practice should be a highly visible force, contributing to the uniformity of tax practice standards. Unfortunately, in its current operational mode, the office of the Director of Practice is essentially invisible, and it has a level of influence on professional

¹² 5 U.S.C. § 500 (1996).

¹³ 31 C.F.R. § 10.51(h) (1966).

conduct that is commensurate with that invisibility. This situation should be rectified. The Director of Practice should be a highly visible, highly respected figure within the tax community, making substantial contributions to tax administration, proposing new and better standards of practice, and enforcing existing standards. This would be beneficial not only with regard to controlling aggressive corporate tax shelters but also with regard to enhancing the respect for tax practice standards generally.

D. *Creating Downside Risk for Promoters of Corporate Tax Shelters Products*

The fourth avenue available to control the proliferation of aggressive corporate tax shelters is that of creating downside risk for those who promote them. Currently, the Code contains penalties and registration requirements that are relevant to promoters of aggressive corporate tax shelters. Section 6700 imposes a penalty on the promoter of a tax shelter that makes a false or fraudulent statement as to any material matter, and section 6701 imposes a penalty on any person who assists with a document that the person knows will understate the liability of another person. However, the standards for applying these penalties are such that they are unlikely to have any material effect in deterring aggressive corporate tax shelter products because the marketers of those products can easily avoid the proscribed conduct.

The registration requirement contained in section 6111(d) should be helpful but only to a limited degree. That section requires registration of any tax shelter marketed under conditions of confidentiality where the promoters may receive aggregate fees in excess of \$100,000.¹⁴ The registration requirement of section 6111(d) does not take effect until regulations are issued, and those regulations are expected at any time. While section 6111(d) should be effective to discourage tax shelters that are marketed under conditions of confidentiality, the common wisdom holds that, when the regulations become effective, promoters will simply cease imposing any explicit or implicit conditions of confidentiality. Thus, while this provision may put an end to the confidentiality feature of aggressive corporate tax shelters, it is not likely to provide a universal solution.

The question that I would like you to consider is whether there is any reason why an accuracy-related penalty should not be imposed on the promoter of an aggressive tax shelter product that fails to be sustained under substantive tax law. If the promoter directly markets a tax shelter product to a taxpayer, the taxpayer must take account of the accuracy-related penalty of section 6662(d). Is there any reason why the promoter should not be required to share that same downside risk? For example, the Code could provide that the promoter of a tax shelter product that fails to be sustained under the substantive law would incur an accuracy-related penalty in an amount determined by reference to the penalty assessed against the purchaser of the product. There could be a minimum fee requirement, such as the \$100,000 aggregate promoter fee requirement now contained in section 6111(d). This would serve to weed out minor transactions.

The promoter accuracy-related penalty could be set at one hundred percent or some other percentage of the penalty assessed against the taxpayer. If an accuracy-related penalty were imposed on multiple purchasers of the product, the promoter would have a separate penalty liability with respect to each such event. This penalty would be an addition to tax for the promoter for the year in which the penalty was finally determined against the taxpayer, and it would be assessed and collected as an addition to tax. One issue that would have to be carefully evaluated is whether the promoter should have the right to intervene in any administrative or judicial proceeding between shelter purchaser and the Service in which issues

¹⁴ The definition of "tax shelter" in section 6111(d) differs only slightly from that of section 6662(d), in that it requires that a significant purpose of "the structure" of the "entity, plan, arrangement, or transaction" be the evasion or avoidance of Federal income tax (emphasis added). Although the terms "structure" and "transaction" do not appear in the section 6662(d) definition, these differences are not likely to have any significant substantive effect.

related to section 6662(d) or section 6664(c) are presented and which could affect the liability of the promoter. At the other extreme, the promoter could be given the right to litigate the substantive and penalty issues *ab initio*. Finding the right balance both to protect the promoter's rights and to avoid duplicative litigation would be a difficult but surely not insurmountable problem. This kind of penalty would also place pressure on the need to identify who is a promoter, but the Code already addresses that question. Section 6111(d) defines a promoter as any person who participates in the organization, management, or sale of a tax shelter. Consequently, the need to identify promoters is not novel to the tax law.

It seems to me likely that, if promoters of tax shelter products faced an accuracy-related penalty risk commensurate with the risk faced by purchasers of tax shelters, they could be expected to exercise substantial care with respect to the quality of the products that they promote. The absence of any downside risk today effectively insulates promoters from any real concern with the quality and likely success of their products.

IV. CONCLUSION

To summarize the views that I have expressed with respect to the subject of aggressive corporate tax shelters: I believe that the existing taxpayer penalty structure is adequate to assure that a penalty will be imposed on virtually all post-1997 aggressive corporate tax shelters that fail to be sustained under the substantive tax law. Since the existing penalty net is wide enough to catch virtually all of these transactions, the remaining question is whether the existing penalty rate is high enough to deter the aggressive transactions. This question probably cannot yet be answered, but the possible need for an increase in the penalty rate should be viewed as an available option. With regard to practitioner standards, I would create a minimum practice standard in Circular 230 for more-likely-than-not opinions needed to satisfy the reasonable cause and good faith standards under section 6664(c). In addition, I would make it unprofessional for a tax practitioner to agree to a confidentiality provision; I would expand the definition of "practice" before the Service to expressly include the providing of tax advice; and I would elevate the stature and independence of the Director of Practice. With regard to promoters of aggressive tax shelter products, I would create downside risk through an accuracy-related penalty that would be imposed on any promoter of a product that caused an accuracy-related penalty to be imposed on the purchaser of that product.

In order for these steps to be optimally effective to reduce aggressive tax shelter marketing, it is essential that the Service and the Treasury make it widely known that the accuracy-related penalty will be asserted in all appropriate tax shelter cases. These would be cases in which there does not appear to be substantial authority, there is lack of business purpose, and the at-risk investment by the corporation is minimal in relationship to the tax benefit sought. In addition, Congress would have to act to extend the accuracy-related penalty to promoters of tax shelters.

I believe that, if these steps are taken, they will be effective to control and diminish the marketing of aggressive corporate tax shelters. Based on my discussions with individual members of the tax bar, I believe the bar would welcome these steps. Tax lawyers are universally proud of their professional skills, and they regard these marketing activities as demeaning to their profession.

I thank you for the opportunity to appear before you and to share with you these views on an important issue in tax policy and administration.

DRAFT OF PROPOSED AMENDMENT TO CIRCULAR 230

Add a new section 10.35 to read as follows:

§ 10.35. **Reasonable belief opinions; confidentiality agreements.**

(a) *Opinions by practitioners with respect to reasonable belief matters.* A taxpayer may seek to establish that, at the time a return was filed, the taxpayer reasonably believed that the tax treatment of an item was more likely than not the proper treatment. A taxpayer in this position may request an opinion from a practitioner in support of that determination. This section establishes minimum standards for a practitioner who provides such an opinion.

(b) *Requirements for reasonable belief opinion.* A practitioner who provides an opinion to a client for purposes of establishing that, at the time that a return was filed, the client reasonably believed that the tax treatment of an item was more likely than not the proper treatment shall comply with each of the following requirements:

(1) *Evaluate all relevant facts.* The practitioner must make inquiry as to all relevant facts and be satisfied that the practitioner's opinion takes account of all such facts. The opinion should not be based on assumed or hypothetical facts. The practitioner may, where the circumstances indicated that it would be reasonable to do so, rely upon factual representations by persons that the practitioner considers to be responsible and knowledgeable. If the information so represented appears to be incomplete or inconsistent in any material respect, the practitioner must make further investigation.

(2) *Relate the law to the facts.* The opinion must relate the applicable law to the relevant facts

(3) *Identify all material legal issues.* The opinion must identify and discuss all material legal issues.

(4) *Evaluate authorities.* The opinion must identify and discuss the relevance and persuasiveness of the legal authority pertinent to the identified facts and material legal issues.

(5) *Consider business purpose.* The opinion must take into account the taxpayer's purposes (and the relative weight of such purposes) for entering into the transaction and for structuring the transaction in a particular manner.

(6) *Substantial authority.* The opinion must assess and express a reasoned opinion on the question whether substantial authority exists for the position to be taken by the taxpayer. Such determination shall be made in the manner described in Reg. § 1.6662-4(d)(3).

(7) *More-likely-than-not assessment.* The opinion must unambiguously conclude that there is a greater than 50-percent likelihood that the tax treatment of the position will be upheld on the merits if challenged.

(c) *Effect of opinion that meets these standards.* An opinion of a practitioner that meets the above requirements will satisfy the practitioner's responsibilities under this section. The persuasiveness of the opinion with regard to the taxpayer's objective will be separately determined under applicable provisions of the law and regulations.

(d) *Confidentiality agreements.* A practitioner may not, as a condition to providing tax advice to a client, agree that knowledge of the tax law gained in the course of providing that advice will be kept confidential and not used for the benefit of other clients of the practitioner.

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