

1 **TITLE ____—TAX SHELTERS**
2 **Subtitle A—Treatment of**
3 **Participants in Tax Shelter Devices**

4 **SEC. ____.** **PENALTY FOR UNDERSTATEMENTS ATTRIB-**
5 **UTABLE TO ABUSIVE TAX SHELTER DEVICES.**

6 (a) **PENALTY.**—Part II of subchapter A of chapter
7 68 (relating to accuracy-related and fraud penalties) is
8 amended by inserting after section 6662 the following:

9 **“SEC. 6662A. PENALTY FOR PARTICIPATION IN AN ABUSIVE**
10 **TAX SHELTER DEVICE.**

11 “(a) **IMPOSITION OF PENALTY.**—If a taxpayer par-
12 ticipates directly or indirectly in an abusive tax shelter de-
13 vice, there shall be added to the taxpayer’s income tax an
14 amount equal to 40 percent of the amount of any applica-
15 ble understatement with respect to the device.

16 “(b) **ABUSIVE TAX SHELTER DEVICE.**—For pur-
17 poses of this section—

18 “(1) **IN GENERAL.**—The term ‘abusive tax shel-
19 ter device’ means any device which does not have—

20 “(A) a material nontax business purpose,
21 or

22 “(B) economic substance.

23 “(2) **DEVICE.**—The term ‘device’ means any
24 partnership or other entity, any investment plan or
25 arrangement, any other plan or arrangement, any

1 agreement, or any transaction. For purposes of the
2 preceding sentence, the Secretary may provide that
3 a series of related devices shall be treated as one de-
4 vice.

5 “(c) APPLICABLE UNDERSTATEMENT.—For pur-
6 poses of this section—

7 “(1) IN GENERAL.—The term ‘applicable un-
8 derstatement’ means any increase in a taxpayer’s in-
9 come tax which results from a difference between
10 the taxpayer’s treatment of items attributable to an
11 abusive tax shelter device as shown on the taxpayer’s
12 return of tax and the proper tax treatment of such
13 items.

14 “(2) SPECIAL RULE FOR AMENDED RE-
15 TURNS.—In no event shall any tax treatment in-
16 cluded with an amendment or supplement to a re-
17 turn of tax be taken into account if the amendment
18 or supplement is filed after the earlier of the date
19 the taxpayer is first contacted by the Secretary re-
20 garding the examination of the return or such other
21 date as is specified by the Secretary.

22 “(d) REGULATIONS.—The Secretary shall prescribe
23 such regulations as may be necessary to carry out the pro-
24 visions of this section.”

1 (b) COORDINATION WITH OTHER TAX SHELTER
2 PROVISIONS.—

3 (1) ACCURACY-RELATED PENALTY.—Section
4 6662(d) (relating to substantial understatement of
5 income tax) is amended by adding at the end the fol-
6 lowing new paragraph:

7 “(3) TREATMENT OF ABUSIVE TAX SHELTER
8 DEVICES.—

9 “(A) IN GENERAL.—This subsection shall
10 not apply to any understatement of income tax
11 to which section 6662A applies and any penalty
12 imposed under such section shall be treated as
13 imposed under subsection (b)(2) for purposes of
14 determining the applicability of any other pen-
15 alty under this section or section 6663.

16 “(B) EXCEPTION.—Any understatement
17 described in subparagraph (A) shall be taken
18 into account in determining whether paragraph
19 (1) applies to other understatements not so de-
20 scribed.”

21 (2) REASONABLE CAUSE EXCEPTION NOT TO
22 APPLY.—Section 6664(c)(1) (relating to reasonable
23 cause exception) is amended by adding at the end
24 the following: “This subsection shall not apply to a
25 penalty imposed under section 6662A.”

1 (3) TAX SHELTER DEFINITIONS.—

2 (A) Section 461(i)(3)(C) (defining tax
3 shelter) is amended by inserting “or abusive tax
4 shelter device (as defined in section 6662A(b))”
5 after “section 6662(d)(2)(C)(iii)”.

6 (B) Section 1274(b)(3)(B)(i) (defining po-
7 tentially abusive situation) is amended by in-
8 serting “or abusive tax shelter device (as de-
9 fined in section 6662A(b))” before “, and”.

10 (C) So much of section 6111(d)(1) as pre-
11 ceedes subparagraph (B) thereof is amended to
12 read as follows:

13 “(1) IN GENERAL.—For purposes of this sec-
14 tion, the term ‘tax shelter’ means any tax shelter (as
15 defined in section 6662(d)(2)(C)(iii)) or any abusive
16 tax shelter device (as defined in section 6662A(b))—

17 “(A) with respect to which a corporation is
18 a direct or indirect participant,”.

19 (c) CONFORMING AMENDMENT.—The table of sec-
20 tions for part II of subchapter A of chapter 68 is amended
21 by inserting after the item relating to section 6662 the
22 following:

“Sec. 6662A. Penalty for participation in an abusive tax shelter device.”

23 (d) EFFECTIVE DATE.—The amendments made by
24 this section shall apply to any device entered into after
25 _____.

1 **SEC. ____.** **SUBSTANTIAL UNDERSTATEMENTS OF PARTICI-**
2 **PANTS IN TAX SHELTERS OTHER THAN ABU-**
3 **SIVE TAX SHELTER DEVICES.**

4 (a) **IN GENERAL.**—Section 6662(d)(2)(C) (relating
5 to special rules involving tax shelters) is amended to read
6 as follows:

7 “(C) **SPECIAL RULES IN CASES INVOLVING**
8 **TAX SHELTERS.**—For purposes of determining
9 whether there is a substantial understatement
10 under paragraph (1)—

11 “(i) **CERTAIN ITEMS DISREGARDED.**—
12 In the case of any item of a taxpayer
13 which is attributable to a tax shelter, the
14 amount of the understatement under sub-
15 paragraph (A) shall be reduced by that
16 portion of the understatement attributable
17 to such item if—

18 “(I) there was substantial au-
19 thority for the tax treatment of such
20 item by the taxpayer,

21 “(II) the relevant facts affecting
22 the item’s tax treatment are ade-
23 quately disclosed in the return or in a
24 statement attached to the return, and

25 “(III) the taxpayer had reason-
26 able belief that the tax treatment of

1 such item by the taxpayer was more
2 likely than not the proper treatment.

3 “(ii) NO REQUIRED MINIMUM
4 AMOUNT.—Any portion of the taxpayer’s
5 understatement attributable to an item at-
6 tributable to a tax shelter shall be treated
7 as a substantial understatement without
8 regard to the amount thereof. Any portion
9 to which this clause applies shall be taken
10 into account in determining whether para-
11 graph (1) applies to any other portion of
12 the underpayment to which this clause
13 does not apply.

14 “(iii) TAX SHELTER.—For purposes
15 of this subparagraph, the term ‘tax shelter’
16 means any device (within the meaning of
17 section 6662A(b)(2)) if a significant pur-
18 pose of such device is the avoidance or eva-
19 sion of Federal income tax.”

20 (b) REASONABLE BELIEF.—Section 6662(d)(2) (de-
21 fining understatement) is amended by adding at the end
22 the following:

23 “(E) REASONABLE BELIEF.—For purposes
24 of subparagraph (C)(i)(III)—

1 “(i) IN GENERAL.—A taxpayer shall
2 be treated as having a reasonable belief
3 with respect to the tax treatment of an
4 item only if such belief—

5 “(I) is based on the facts and law
6 that exist at the time the tax shelter
7 is entered into,

8 “(II) relates solely to the tax-
9 payer’s chances of success on the mer-
10 its of such treatment and does not
11 take into account the possibility that
12 a return will not be audited, such
13 treatment will not be raised on audit,
14 or such treatment will be resolved
15 through settlement if it is raised.

16 “(ii) CERTAIN OPINIONS MAY NOT BE
17 RELIED UPON.—An opinion of a tax advi-
18 sor may not be relied upon to establish the
19 reasonable belief of a taxpayer if—

20 “(I) the tax advisor is described
21 in clause (iii), or

22 “(II) the tax opinion is described
23 in clause (iv).

1 “(iii) DISQUALIFIED TAX ADVISORS.—

2 A tax advisor is described in this clause if
3 the tax advisor—

4 “(I) is an organizer or promoter
5 of the tax shelter,

6 “(II) is compensated directly or
7 indirectly by such organizer or pro-
8 moter with respect to the tax shelter,

9 “(III) has a contingent fee ar-
10 rangement with respect to such tax
11 shelter,

12 “(IV) has any type of referral
13 agreement or other similar agreement
14 or understanding with such organizer
15 or promoter which relates to the tax
16 shelter, or

17 “(V) has any other similar char-
18 acteristic which, as determined under
19 regulations prescribed by the Sec-
20 retary, is indicative of a potential con-
21 flict of interest or compromise of inde-
22 pendence.

23 “(iv) DISQUALIFIED TAX OPINIONS.—

24 A tax opinion is described in this clause if
25 the opinion—

1 “(I) is based on unreasonable
2 factual or legal assumptions,

3 “(II) unreasonably relies on rep-
4 resentations, statements, findings, or
5 agreements of the taxpayer or any
6 other person,

7 “(III) does not identify all mate-
8 rial facts, or

9 “(IV) fails to meet any other re-
10 quirement as the Secretary may pre-
11 scribe.

12 “(v) DEFINITIONS.—For purposes of
13 this subparagraph, the terms ‘organizer’
14 and ‘promoter’ have the meanings given
15 such terms by section 6111.”

16 (c) REASONABLE CAUSE EXCEPTION NOT TO
17 APPLY.—The last sentence of section 6664(e)(1) (relating
18 to reasonable cause exception), as added by section _____,
19 is amended by inserting “to a penalty imposed under sec-
20 tion 6662 by reason of a substantial understatement of
21 tax attributable to an item described in section
22 6662(d)(2)(C) or” after “shall not apply”.

23 (d) CONFORMING AMENDMENT.—Section
24 6662(d)(2)(B) is amended by adding at the end the fol-

1 lowing: “This subparagraph does not apply to an item to
2 which subparagraph (C) applies.”

3 (e) EFFECTIVE DATE.—The amendments made by
4 this section shall apply to tax shelters entered into after
5 _____.

6 **SEC. ____ . PENALTY FOR FAILING TO DISCLOSE REPORT-**
7 **ABLE TRANSACTION.**

8 (a) IN GENERAL.—Part I of subchapter B of chapter
9 68 (relating to assessable penalties) is amended by insert-
10 ing after section 6707 the following new section:

11 **“SEC. 6707A. PENALTY FOR FAILURE TO INCLUDE TAX**
12 **SHELTER INFORMATION WITH RETURN.**

13 “(a) IMPOSITION OF PENALTY.—Any person who
14 fails to include with its return of Federal income tax any
15 information required to be included under section 6011
16 with respect to a reportable transaction shall pay a penalty
17 in the amount determined under subsection (b). No pen-
18 alty shall be imposed on any such failure if it is shown
19 that such failure is due to reasonable cause and not due
20 to willful neglect.

21 “(b) AMOUNT OF PENALTY.—

22 “(1) IN GENERAL.—The amount of the penalty
23 under subsection (a) shall be equal to the greater
24 of—

1 “(A) 5 percent of any increase in Federal
2 tax which results from a difference between the
3 taxpayer’s treatment (as shown on its return)
4 of items attributable to the reportable trans-
5 action to which the failure relates and the prop-
6 er tax treatment of such items, or

7 “(B) \$100,000.

8 For purposes of subparagraph (A), the rule of sec-
9 tion 6662A(c)(2) shall apply.

10 “(2) LISTED TRANSACTION.—If the failure
11 under subsection (a) relates to a reportable trans-
12 action which is the same as, or substantially similar
13 to, a transaction specifically identified by the Sec-
14 retary as a tax avoidance transaction for purposes of
15 section 6011, paragraph (1)(A) shall be applied by
16 substituting ‘10 percent’ for ‘5 percent’.

17 “(c) REPORTABLE TRANSACTIONS.—For purposes of
18 this section, the term ‘reportable transaction’ means any
19 transaction with respect to which information is required
20 under section 6011 to be included with a taxpayer’s return
21 of tax because, as determined under regulations prescribed
22 under section 6011, such transaction has characteristics
23 which may be indicative of a tax shelter (as defined in
24 section 6662(d)(2)(C)(iii)) or an abusive tax shelter device
25 (as defined in section 6662A(b)).

1 “(d) COORDINATION WITH OTHER PENALTIES.—
2 The penalty imposed by this section is in addition to any
3 penalty imposed under section 6662 or 6662A.”

4 (b) CONFORMING AMENDMENT.—The table of sec-
5 tions for part I of subchapter B of chapter 68 is amended
6 by inserting after the item relating to section 6707 the
7 following:

“Sec. 6707A. Penalty for failure to include tax shelter information on return.”

8 (c) EFFECTIVE DATE.—The amendments made by
9 this section shall apply to transactions entered into after
10 _____.

11 **Subtitle B—Treatment of Other** 12 **Parties to Tax Shelters**

13 **SEC. ____ . MODIFICATIONS OF PENALTIES FOR AIDING AND** 14 **ABETTING UNDERSTATEMENT OF TAX LI-** 15 **ABILITY INVOLVING TAX SHELTERS.**

16 (a) IMPOSITION OF PENALTY.—Section 6701(a) (re-
17 lating to imposition of penalty) is amended to read as fol-
18 lows:

19 “(a) IMPOSITION OF PENALTIES.—

20 “(1) IN GENERAL.—Any person—

21 “(A) who aids or assists in, procures, or
22 advises with respect to, the preparation or pres-
23 entation of any portion of a return, affidavit,
24 claim, or other document,

1 “(B) who knows (or has reason to believe)
2 that such portion will be used in connection
3 with any material matter arising under the in-
4 ternal revenue laws, and

5 “(C) who knows that such portion (if so
6 used) would result in an understatement of the
7 liability for tax of another person,
8 shall pay a penalty with respect to each such docu-
9 ment in the amount determined under subsection
10 (b).

11 “(2) CERTAIN TAX SHELTERS.—If—

12 “(A) any person—

13 “(i) aids or assists in, procures, or ad-
14 vises with respect to the creation, organiza-
15 tion, sale, implementation, management, or
16 reporting of a tax shelter (as defined in
17 section 6662(d)(2)(C)(iii)) or an abusive
18 tax shelter device (as defined in section
19 6662A(b)), and

20 “(ii) opines, advises, represents, or
21 otherwise indicates (directly or indirectly)
22 that the taxpayer’s tax treatment of items
23 attributable to such tax shelter or abusive
24 tax shelter device and giving rise to an un-
25 derstatement of tax liability would more

1 “(B) any penalty imposed by subsection
2 (a)(2),
3 the amount of the penalty shall be equal to 50 per-
4 cent of the gross proceeds derived (or to be derived)
5 by the person in connection with the tax shelter or
6 device.”

7 (c) REFERRAL AND PUBLICATION.—If a penalty is
8 imposed under section 6701(a)(2) of the Internal Revenue
9 Code of 1986 (as added by subsection (a)) on any person,
10 the Secretary of the Treasury shall—

11 (1) notify the Director of Practice of the Inter-
12 nal Revenue Service and any appropriate State li-
13 censing authority of the penalty and the cir-
14 cumstances under which it was imposed, and

15 (2) publish the identity of the person and the
16 fact the penalty was imposed on the person.

17 (d) CONFORMING AMENDMENTS.—

18 (1) Section 6701(d) is amended by striking
19 “Subsection (a)” and inserting “Subsection (a)(1)”.

20 (2) Section 6701(e) is amended by striking
21 “subsection (a)(1)” and inserting “subsection
22 (a)(1)(A)”.

23 (3) Section 6701(f) is amended by inserting “,
24 tax shelter, or device” after “document” each place
25 it appears.

1 (e) EFFECTIVE DATE.—The amendments made by
2 this section shall take effect on _____.

3 **SEC. ____ . FAILURE TO MAINTAIN LISTS.**

4 (a) FAILURE TO MAINTAIN LISTS.—Section 6708(a)
5 (relating to failure to maintain lists of investors in poten-
6 tially abusive tax shelters) is amended by adding at the
7 end the following: “In the case of a tax shelter (as defined
8 in section 6662(d)(2)(C)(iii)) or any abusive tax shelter
9 device (as defined in section 6662A(b)), the penalty shall
10 be equal to 50 percent of the gross proceeds derived (or
11 to be derived) from each person with respect to which
12 there was a failure and the limitation of the preceding sen-
13 tence shall not apply.”

14 (b) EFFECTIVE DATE.—The amendments made by
15 this section shall apply to _____.

16 **SEC. ____ . REGULATION OF INDIVIDUALS PRACTICING BE-**
17 **FORE THE DEPARTMENT OF TREASURY.**

18 (a) MONETARY PENALTIES.—Section 330(b) of title
19 31, United States Code, is amended by adding at the end
20 the following new flush sentence:

21 “The Secretary may impose a monetary penalty on any
22 representative described in the preceding sentence. If the
23 representative was acting on behalf of an employer or any
24 firm or other entity in connection with the conduct giving
25 rise to such penalty, the Secretary may impose a monetary

1 penalty on such employer, firm, or entity if it knew, or
2 reasonably should have known, of such conduct. Such pen-
3 alty shall not exceed the representative's (employer's,
4 firm's, or entity's) gross proceeds derived (or to be de-
5 rived) from the conduct giving rise to the penalty and may
6 be in addition to, or in lieu of, any suspension or disbar-
7 ment."

8 (b) REVISION OF CIRCULAR 230.—The Secretary of
9 the Treasury or his delegate shall revise Internal Revenue
10 Service Circular 230—

11 (1) to update the treatment of individuals and
12 firms involved in tax shelters and the definition of
13 tax shelters,

14 (2) to require the publication of the name of
15 any individual or firm who receives a letter of rep-
16 rimand,

17 (3) to require an automatic referral to the Di-
18 rector of Practice of the Internal Revenue Service
19 when penalties are imposed under the Internal Rev-
20 enue Code of 1986 with respect to any individual or
21 firm involved in a tax shelter, and

22 (4) to require the Director of Practice to notify
23 appropriate State licensing officials of any action
24 taken against any individual or firm.

1 **SEC. ____.** **APPROVAL PROCESS FOR TAX SHELTER ASSESS-**
2 **MENTS.**

3 (a) **IN GENERAL.**—The Commissioner of Internal
4 Revenue shall develop and implement procedures under
5 which—

6 (1) a determination by an employee to assess
7 any tax, addition to tax, or penalty involving a tax
8 shelter (as defined in section 6662(d)(2)(C)(iii) of
9 the Internal Revenue Code of 1986) or an abusive
10 tax shelter device (as defined in section 6662A(b) of
11 such Code) would, where appropriate, be required to
12 be reviewed before the assessment is made, and

13 (2) appropriate disciplinary action would be
14 taken if the procedures established under paragraph
15 (1) are not followed.

16 (b) **EFFECTIVE DATE.**—This section shall take effect
17 on _____.