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IRS Tightens Position on Abusive Tax Shelter Settlement Terms

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WASHINGTON — The Appeals Division of the Internal Revenue Service has reassessed and tightened its settlement guidelines under which it will accept offers to settle cases with taxpayers that participated in certain abusive transactions, officials said today.

Last month, the IRS Appeals Division and the Large and Mid-Size Business Division began sending letters to taxpayers involved in three abusive transactions, advising them that the settlement terms available to resolve these transactions have changed. Certain taxpayers who reported losses and deductions from lease strips, inflated-basis assets derived from lease strips, and in intermediary transactions are being notified that the Appeals position has tightened.

"As we have been doing for some time, we continue to ratchet up the pressure on those entering into abusive transactions," said IRS Commissioner Mark W. Everson. "Both Congress and the courts are supporting us in this effort."

Under the new guidelines, the IRS will not settle unless taxpayers concede 100 percent of the claimed losses or deductions, reduced by only the amount of transaction costs up to 10 percent of the claimed losses or deductions. Furthermore, taxpayers must concede 50 percent of the accuracy-related penalty at issue. If both the 40 percent gross valuation misstatement penalty and the 20 percent substantial understatement penalty were asserted, then the settlement will apply to the gross valuation misstatement penalty.

To settle these cases, taxpayers must enter into a closing agreement with the IRS. IRS agents will be able to accept these proposed agreements if they conform to the revised settlement guidelines issued by Appeals.

"Notifying taxpayers of the change in the settlement guidelines is another example of the nimbleness of the IRS," said IRS Chief Counsel Donald Korb. "This action shows that the longer a taxpayer delays in settling, the greater the risk that we will tighten our settlement ranges in response to favorable litigation."

The IRS has won an increasing number of court cases involving abusive tax transactions. In late August, the IRS won the Long Term Capital Holdings case.

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"Modifying our settlement guidelines was appropriate in light of Long Term Capital Holdings," said David Robison, chief of Appeals. "The court's careful analysis was a compelling reason to incorporate the case in our assessment of the litigating hazards for these cases."

“The court decision validated the IRS position on penalties,” said Deborah M. Nolan, LMSB commissioner. “A written tax opinion does not inoculate a taxpayer from penalties. If the facts of a specific case show that the taxpayer did not rely on the advice in good faith or that the reliance wasn’t reasonable, penalties are appropriate, the court held.”

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