



MANUAL TRANSMITTAL

Department of the Treasury
Internal Revenue Service

4.32.1

JUNE 20, 2024

EFFECTIVE DATE

(06-20-2024)

PURPOSE

- (1) This transmits revised IRM 4.32.1, Abusive Transactions, Process Guide for Combating Abusive Tax Avoidance Transactions.

MATERIAL CHANGES

- (1) Substantial changes made throughout the IRM are noted below:

Reference	Change
4.32.1.1.7 Related References - IRM 4.32.4 Citation in table	Delete Related Reference -IRM 4.32.4 was made obsolete on 1-5-2023 - Abusive Transactions - IRC 6707A Penalty for Failure to include Reportable Transaction Information with Return. Citation Reference "IRM 4.32.4" - is Obsoleted, as this information has been moved to IRM 20.1.13.3.

- (2) Changes have been made throughout to address minor editorial issues and update references.

EFFECT ON OTHER DOCUMENTS

This material supersedes IRM 4.32.1, dated 2-9-2018. This revision incorporates Interim Guidance Memorandum SB/SE 04-0321-0012, Interim Guidance on Changes to the 6707A Penalty Rescission, dated March 17, 2021 and NHQ-04-0521-0003, Interim Guidance on Designation of Cases for Litigation, dated May 24, 2021.

AUDIENCE

This section provides guidance for Small Business and Self-Employed (SB/SE) Examination area office employees, Tax Exempt and Governmental Entities (TE/GE) employees, Taxpayer Services (TS), and Large Business and International (LB&I) employees who are examining abusive transactions.

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4.32.1

Process Guide for Combating Abusive Tax Avoidance Transactions

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4.32.1.1
(10-12-2021)
Program Scope and Objectives

- (1) **Purpose:** The IRS continues to identify new types of tax transactions or promotions that are either abusive or potentially abusive requiring different levels of coordination and varying strategies. This IRM outlines operating standards for both the highly complex and technical abusive transactions and those abusive transactions that are considered scams or promotions based on the erroneous application of tax law or clearly frivolous arguments.
- (2) **Audience:** These procedures apply to examiners of abusive transactions in SB/SE, LB&I, TEGE, and TS.
- (3) **Policy Owner:** The Director, Office of Promoter Investigations, which is under the Division Commissioner, SB/SE.
- (4) **Program Owner:** The Policy and Technical Support Teams within the Office of Promoter Investigations.
- (5) **Primary Stakeholders:** The following areas can be affected by these procedures: SB/SE Field Exam, SB/SE Exam Case Selection, SB/SE Specialty Tax, Collection Division, SB/SE Counsel, SB/SE Office of Fraud Enforcement, LB&I, TS, and TE/GE.
- (6) **Program Goals:** The goal of the program is to combat abusive tax avoidance transactions.

4.32.1.1.1
(02-09-2018)
Background

- (1) This IRM provides assistance to employees who are identifying and/or examining tax transactions and tax promotions that are either abusive or potentially abusive. It also serves to promote effective communication and coordination, consistent treatment, and efficient processing.

4.32.1.1.2
(06-20-2024)
Authority

- (1) SB/SE Delegation Order SB/SE 1-23-50, Functions Related to Potential Preparer, Promoter and Tax Shelter Cases, (formerly SB/SE DO 4.60 Rev. 1), delegates the authority to approve and refer all SB/SE AT promoter investigation to the SB/SE Lead Development Center (LDC) Program Manager.

4.32.1.1.3
(10-12-2021)
Responsibilities

- (1) The Director, Office of Promoter Investigations is responsible for establishing and delivering policy and guidance that impacts the examination of potentially abusive tax avoidance transactions.
- (2) The Program Managers of the Policy and Technical Support Teams report to the Director, Office of Promoter Investigations, and are responsible for addressing abusive transactions.
- (3) All examiners and their managers working abusive transactions are responsible for familiarizing themselves with the information contained in this IRM.

4.32.1.1.4
(10-12-2021)
Program Management and Review

- (1) **Program Reports:**
 - Monthly reports detailing the current inventory of project cases by Area and their status are produced and provided to Office of Promoter Investigation staff, Counsel, and select others for monitoring purposes.
 - Ad-hoc reports are produced as requested by Exam personnel with appropriate permission.

- (2) **Program Effectiveness:** Effectiveness will be measured by analysis of compliance trends and enforcement results.

4.32.1.1.5
(10-12-2021)

Program Controls

- (1) Program controls developed to oversee the program include separation of duties, executive and Counsel oversight, and cross-functional and cross-BOD coordination on compliance strategies to address abusive transactions.

4.32.1.1.6
(10-12-2021)

Terms and Acronyms

- (1) A list of terms is given in Exhibit 4.32.1-1, Glossary of Terms.
- (2) The following table lists acronyms used throughout this IRM and their definitions:

Acronym	Definition
AT	Abusive Transactions
BOD	Business Operating Division
CCDM	Chief Counsel Directives Manual
CIP	Compliance Initiative Project/Coordinated Issue Paper
CP&C	Compliance Planning & Classification
IRC	Internal Revenue Code
LB&I	Large Business & International
LDC	Lead Development Center
LILO	Lease-In Lease-Out
OTP	Office of Tax Policy
OTSA	Office of Tax Shelter Analysis
P&SI	Pass-Throughs and Special Industries
SB/SE	Small Business/Self-Employed
TE/GE	Tax Exempt/Government Entities
TOI	Transaction of Interest
TS	Taxpayer Services

4.32.1.1.7
(06-20-2024)

Related Resources

- (1) The following table lists the primary sources of guidance for AT examiners:

IRM Section	Title
IRM 4.32.2	The Abusive Transactions (AT) Process
IRM 4.32.3	Coordination and Roles of Cross-Functional Units

IRM Section	Title
IRM 4.50.5	LB&I Compliance Integration - Office of Tax Analysis (OTSA)
IRM 20.1.13.3	Penalty Handbook, Material Advisor and Reportable Transactions Penalties
IRM 4.34.1	SB/SE Emerging Issue Process
IRM 5.2	Abusive Tax Avoidance Transactions
IRM 20.1.6	Preparer, Promoter, Material Advisor Penalties
IRM 1.2.2.5.21	Delegation Order 4-25 (Rev. 2) Supplements Delegation Order No. 97, Settlement offers, Closing Agreements, and Settlement Agreements under Section 6224(c) in Cases with Technical Advisor (TA) or Senior Program Analyst (SPA) Program Issues, and Appeals Technical Guidance Program (Compliance Coordinated and Appeals Coordinated) Issues.

4.32.1.2 (10-12-2021) Introduction

- (1) Before a recommendation for addressing abusive or potentially abusive tax transactions or promotions can be developed that is consistent with sound tax administration objectives, it is critical that the scope of the issue, transaction variations, potential case inventory, and the appropriate legal arguments are identified and explored. Because of their possible complexity and monetary significance, proper coordination of tax transactions or promotions that are either abusive or potentially abusive is vital to effective tax administration. Compliance personnel in one or more business operating divisions (BODs), Counsel, and other functions as appropriate, should be involved in coordinating efforts around each issue identified.
- (2) There are a variety of abusive transactions and promotions ranging from the highly complex transactions to the basic scams or promotions, both of which can affect either a large number of taxpayers or only a few taxpayers. To fully understand a specific transaction or promotion and to develop an effective response, it is essential that service-wide communication and coordination be clear and consistent.

4.32.1.3 (10-12-2021) Guiding Principles

- (1) The guiding principles that should be followed throughout the process of identifying and developing issues related to coordinated abusive transactions and promotions are as follows:
 - Understand the transaction.
 - Get the right people involved at the right time.
 - Respect each function's role in the administrative process.
 - Develop a service-wide strategy to address the abusive transaction or promotion.
- (2) Understanding the transaction or promotion is critical to the development of a successful strategy for addressing all tax transactions or promotions that are

either abusive or potentially abusive. Service-wide, the IRS should completely understand the transaction or promotion and its variations. It is vital that individual transactions be reviewed so that the legal positions can be properly assessed based on the facts of an actual case rather than relying solely on the facts provided as part of a legal opinion or a promoter offering. Each transaction or promotion must meet a minimum standard of factual development to ensure proper application of legal theories and to ensure design of appropriate case strategies.

- (3) It is critical to get the participation of all relevant parties for both gathering information about an identified transaction or promotion and developing strategies for addressing the abusive transactions or promotion. Depending on the specific issue, these efforts may need to include representatives from various operating divisions, Criminal Investigation, and multiple components of Counsel and Treasury.
- (4) In the case of a transaction or promotion affecting only one operating division, the operating division may determine that a strategic division-wide compliance approach is required. In the case of a transaction or promotion affecting more than one operating division, a service-wide strategy should be pursued. A wide range of available options for combating the abusive transaction or promotion should be considered and include:
 - Published Guidance
 - Audit Techniques Guides
 - Audit Resource Guides
 - Litigation Designation
 - Fast Track Process
 - Specific Resolution Strategy including Collection Strategy
 - Legislative Resolution
 - Public or Private Settlement Offers
 - Education and Marketing

4.32.1.4
(10-12-2021)
**Potentially Abusive
Transactions**

- (1) This section details information relating to potentially abusive transactions.

4.32.1.4.1
(06-20-2024)
**Initial Identification and
Development**

- (1) Potentially abusive transactions are generally identified, consolidated, and elevated as necessary within each IRS operating division (LB&I, SB/SE, and TE/GE). When an operating division determines that a potentially abusive transaction warrants review and consideration for treatment as a listed transaction or as a transaction of interest (TOI), the potentially abusive transaction is brought to the Associate Chief Counsel Office with responsibility for the issue or Code section.
- (2) Information about potentially abusive transactions is received from various sources, including but not limited to:
 - a. The LB&I Office of Tax Shelter Analysis (OTSA)—taxpayer disclosures filed under 26 CFR 1.6011-4, material advisor disclosures filed under IRC 6111, and the tax shelter hotline.
 - b. The SB/SE Lead Development Center (SB/SE LDC).

- c. Material advisor and promoter investigations with respect to penalties under IRC 6700, IRC 6701, IRC 6707, IRC 6708 and Taxpayer/investor examinations..
 - d. Taxpayer/investor examinations.
 - e. Research functions.
 - f. Associate Chief Counsel and Division Counsel offices.
 - g. Information from taxpayers, practitioners, Whistle-blowers and special interest groups and media sources.
 - h. Department of Treasury, Office of Tax Policy (Treasury OTP) and other governmental sources
 - i. Congress.
- (3) Each operating division, working with its respective Division Counsel, will review information on potentially abusive transactions and decide whether to raise specific issues with the appropriate Associate Chief Counsel. In deciding whether to raise a potentially abusive transaction with an Associate Office, consideration is given to the potential impact the issue may have from an Examination or Division Counsel perspective, such as the number of identified cases, the dollars at issue, the nature of the transaction, the nature and extent of the potential abuse, and the ease with which the transaction can be duplicated or marketed.
- (4) Each operating division has an office or group identified for handling potentially abusive transactions within its jurisdiction and is the primary contact with Counsel on these issues. All field referrals should be routed to one of these primary contacts. These offices and groups are as follows:
- TE/GE—Compliance Planning & Classification, Issue Identification
 - SB/SE—Office of Promoter Investigations, Policy and Technical Support
 - LB&I— Office of Tax Shelter Analysis
- (5) In SB/SE, potentially abusive transactions that fit the definition of an emerging issue should also be submitted to the Emerging Issue Submission Portal located on the *Emerging Issues Community of Practice* site. SB/SE defines an emerging issue as an issue that may involve a new or novel set of facts relating to the improper application of the tax law. It may also be a new technical issue or a new interpretation of existing tax law. See IRM 4.34, SB/SE Emerging Issues.

4.32.1.4.2
(10-12-2021)
**Office of Chief Counsel
Review of Potentially
Abusive Transactions**

- (1) Generally, when an operating division decides to elevate a potentially abusive transaction for Chief Counsel review, the potentially abusive transaction is referred to the operating division's respective Division Counsel on an ad hoc basis. At the request of an operating division or Division Counsel, a meeting may be held to discuss potentially abusive transactions that may be or have been referred to Counsel for review. The potentially abusive transaction meeting will include representatives from impacted business operating divisions (BODs) and their respective Division Counsels.
- (2) After receiving information on a potentially abusive transaction, the Division Counsel's office will review the information related to each issue or transaction and coordinate with the appropriate Associate Chief Counsel office(s) to determine the appropriate course of action, including whether to recommend identifying the potentially abusive transaction as a listed transaction or as a transaction of interest (TOI).

- (3) An essential part of evaluating a potentially abusive transaction is to develop transactional information. Consequently, Division Counsel and Associate Chief Counsel may request additional information from those operating divisions with the ability to provide or obtain additional information about the transaction. Additional information from internal sources such as taxpayer examinations or promoter investigations, 26 CFR 1.6011-4 disclosures, or material advisor disclosures under IRC 6111 may be requested. In certain cases, additional information from external sources such as taxpayers, promoters, or whistleblowers may be requested.
- (4) After evaluating the potentially abusive transaction, Division Counsel's office will develop a course of action that represents the office of Chief Counsel's recommendation for the potentially abusive transaction and coordinate with the BODs. These recommendations may include, but are not limited to, one or more of the following options:
 - a. Identifying the transaction as a listed transaction or TOI.
 - b. Issuing a notice (or other guidance) alerting the public that the transaction is being scrutinized by the IRS.
 - c. Issuing other guidance such as a revenue ruling, general legal advice memo, or Chief Counsel advice that states the IRS's position on the issue.
 - d. Recommending a change to a statute or regulation (if this option is selected, the appropriate Associate Chief Counsel office(s) will work directly with Treasury OTP concerning any changes recommended).
 - e. Pursuing viable issues on a case specific basis because the issues are inherently factual.
 - f. Suggesting that the transaction should no longer be pursued.
- (5) The Division Counsel (or delegate) will coordinate its proposed course of action with the BODs. The Counsel office with subject matter jurisdiction will be the Chief Counsel office responsible for developing any guidance. If a decision is made to identify the transaction as a listed transaction or a TOI, this Associate Chief Counsel Office will coordinate with the Passthroughs & Special Industries (P&SI) branch on issues related to the disclosure requirements.
- (6) While Division Counsel is considering the legal strategy for a potentially abusive transaction and determining if the transaction should be listed or identified as a TOI, representatives from the affected operating divisions will continue to identify and work inventory and assess the extent of cross-divisional impact. Many abusive tax avoidance transactions or promotions involve a significant number of taxpayers under the jurisdiction of more than one operating division, thus necessitating ongoing coordination among the operating divisions to ensure consistency of taxpayer treatment. In some cases the potentially abusive transaction under consideration involves primarily taxpayers in only one operating division. Accordingly, that operating division will be responsible for coordination and most decision-making efforts. However, the decision making process should always include input from other operating divisions (as appropriate) and Counsel (division and associate offices, as appropriate).

4.32.1.4.3
(06-20-2024)
Coordination of Listed Transactions

- (1) As potentially abusive transactions are developed, they may result in published guidance being issued officially identifying the transaction as a listed transaction. When this occurs, the listed transaction will be treated as a coordinated issue as of the date the guidance is issued.

- (2) A memorandum will be issued by the responsible Division Commissioner to affected operating units. The memorandum will contain the name of the Executive Issue Owner, the issue specialist to contact, a copy of the listing guidance, and the related plain meaning statement.
- (3) If the listed transaction surfaces during an examination, it must be raised as an issue following the guidance position. Examiners should contact the issue specialist and provide the name of the taxpayer, taxable period(s) involved, type of listed transaction, the name of the promoter, if known, the name and telephone number of the Group Manager and, if applicable, the name and telephone number of the Team Coordinator. The initial contact may be via e-mail (utilizing secure messaging), fax or telephone.
- (4) Examiners should consult with the issue specialist and Counsel on the development of the issue. Examiners must secure the concurrence of the issue specialist if their examination deviates from any mandated specific examination techniques proposed for the issue development or their proposal for adjustment deviates from any stated legal position. Examiners must also consult with and secure the concurrence of the issue specialist and Counsel before proposing any resolution other than full concession of the issue by the taxpayer. No proposals can be made without the concurrence of the Executive Issue Owner.
- (5) After the initial published guidance is released, the responsible Division and Chief Counsel staff will meet to discuss the need to further develop the issue. Discussion will include whether there is a need for Counsel to provide a thorough legal analysis of the issue or other guidance. If additional guidance is needed, an issue team should initiate work on an abbreviated coordinated issue paper (CIP). An Associate Chief Counsel office will be assigned primary responsibility for preparing the legal analysis portion of the paper. That Associate Chief Counsel office will work with the issue team on the analysis and coordinate with other Associate offices as necessary. The issue team should regularly coordinate with Chief Counsel staff during the development of the CIP.
- (6) When the draft CIP is ready for clearance, expedited 30-day clearance procedures will be used. Associate Chief Counsel should coordinate with the issue team during the review process. See *Chief Counsel Notice CC-2004-027*.

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Exhibit 4.32.1-1 (06-20-2024)

Glossary of Terms

Term	Definition
Abusive Tax Shelter	Specific tax transaction/promotion that “shelters” income from taxation by taking a tax position that is not supported by tax law or manipulates the law in a way that is not consistent with the intent of the law. The term “Abusive Tax Shelter” is commonly used to mean an abusive tax transaction or promotion that is highly technical. These transactions may sometimes be referred to as “abusive promotions.” When IRS identifies an abusive tax shelter as a listed transaction, that shelter is then subject to disclosure requirements pursuant to 26 CFR 1.6011-4. See listed transaction below in this table for a complete description. Not all abusive tax shelters are listed transactions.
Abusive Tax Avoidance Transaction/Promotion	A specific tax transaction/promotion that reduces tax liability by taking a tax position that is not supported by tax law or manipulates the law in a way that is not consistent with the intent of the law. Abusive tax avoidance transactions/promotions may be applicable to either a large number of taxpayers or a limited number of taxpayers. These strategies may be organized and marketed and, if so, are often referred to as an abusive tax shelter. See abusive tax shelter above in this table for a further description.
Emerging Issue	An issue that may involve a new or novel set of facts relating to the improper application of the tax law. It may also be a new technical issue or a new interpretation of existing tax law.
Executive Issue Owner	The executive or senior management leader who is responsible for the oversight of a particular issue.
Frivolous Tax Promotion/Scam	A transaction/promotion that is clearly not allowable or has no existing basis in law. A list of more than 40 frivolous positions is in Notice 2010-33. See <i>The Truth About Frivolous Tax Arguments Introduction</i>
Listed Transaction	A listed transaction is a type of reportable transaction subject to disclosure pursuant to 26 CFR 1.6011-4 and IRC 6111 and the regulations thereunder, and for which material advisor lists must be maintained pursuant to IRC 6112 and the regulations thereunder. A transaction is a listed transaction if it is the same as or substantially similar to a transaction the IRS has identified as a listed transaction by published guidance. A transaction is substantially similar if it is expected to obtain the same or similar types of tax consequences and is either factually similar or based on the same or similar tax strategy as that described in the published guidance. When the IRS identifies a transaction as a listed transaction, it considers the transaction to be an abusive tax avoidance transaction.
Office of the Associate Chief Counsel (Pass-throughs and Special Industries), Branch 3 (P&SI Tax Shelter Branch)	The office within Chief Counsel that evaluates potentially abusive transactions for determining if a transaction should be identified as a “listed transaction” or a “transaction of interest” in coordination with other Chief Counsel offices that may have jurisdiction over substantive legal issues with respect to the transaction.

Exhibit 4.32.1-1 (Cont. 1) (06-20-2024)

Glossary of Terms

Term	Definition
Reportable Transaction	<p>Reportable transactions include the following:</p> <ol style="list-style-type: none"> 1. Listed transactions 2. Transactions offered under conditions of confidentiality 3. Transactions subject to contractual protection 4. Loss transactions 5. Transactions of interest. <p>See 26 CFR 1.6011-4(b) for more information regarding the types of reportable transactions. Just because a transaction is a reportable transaction does not make that transaction an abusive tax shelter. Taxpayers must disclose their participation in reportable transactions as provided in 26 CFR 1.6011-4(e). If taxpayers do not disclose their participation in the reportable transaction, they will be subject to penalty pursuant to IRC 6707A. (See IRM 20.1.13.3, Penalty Handbook, Material Advisor and Reportable Transactions Penalties). In addition, material advisors must maintain and furnish lists of certain investor information with respect to reportable transactions under IRC 6112 and 26 CFR 301.6112-1 or be subject to penalty pursuant to IRC 6708. Per the American Jobs Creation Act of 2004 (Pub.L. No. 108-357), material advisors must disclose reportable transactions pursuant to IRC 6111 and 26 CFR 301.6111-3 or be subject to penalty under IRC 6707.</p>
Settlement Approach/Strategy	<p>A service-wide plan for combating a specific abusive tax transaction or promotion. Options for settlement approaches or strategies include using normal processes for case resolution or developing procedures for resolving a specific issue that deviates from normal case resolution processes. Settlement approaches or strategies are generally developed by operating division executive leadership.</p>
Tax Shelter	<p>A tax strategy or promotion that “shelters” income from normal taxation. Depending on the facts and legal analysis, a specific transaction or promotion may represent either lawful tax avoidance or unlawful tax evasion. Those tax shelters resulting in tax evasion are known as abusive tax shelters. The term “tax shelter” is sometimes used to mean “abusive tax shelter” in common parlance.</p>
Transactions of Interest (TOIs)	<p>A transaction of interest (TOI) is a reportable transaction subject to disclosure pursuant to 26 CFR 1.6011-4 and IRC 6111, and for which material advisors must maintain lists pursuant to IRC 6112. A transaction is a TOI if it is the same as or substantially similar to one of the types of transactions that the IRS has identified by published guidance as a TOI. A transaction is substantially similar to a TOI if it is expected to obtain the same or similar types of tax consequences and is either factually similar or based on the same or similar tax strategy as that described in the published guidance. TOIs are transactions that the IRS is interested in gathering more information about that could potentially be abusive tax shelters.</p>

Exhibit 4.32.1-2 (07-31-2012)

Guiding Principles for Developing Investor Penalty Resolution Strategies, Identification and Development of Issues in Cases to Designate for Litigation, and Development of the Treatment and Consideration of the Transaction Costs

This exhibit is intended for developing broad resolution strategies. Not for use in resolving individual taxpayer cases.

The purpose of any strategy should be to:

- Foster effective tax administration through overall impact on compliant and non-compliant taxpayers.
- Ensure fairness and consistency in administration of tax law.
- Maintain ethics and integrity in decision making.
- Consider the impact on future compliance risks of penalty settlement.
- Focus on changing taxpayer behavior to foster voluntary compliance.
- Address the specific transaction or promotion.
- Tailor the strategy to address the egregiousness of the taxpayer actions/non-action.
- Facilitate resolution early in the process.
- Reduce associated burden on both the IRS and the taxpayer.

Exhibit 4.32.1-3 (06-20-2024)**Criteria for Development of the Penalty Resolution****(including but not limited to)**

Consider the following when developing a strategy for integrating the applicable penalty provisions into the issue resolution strategy:

1. Periods of limitations on assessment of tax and penalties.
2. Differences in behavior, such as whether the taxpayer disclosed or concealed participation in the transaction, may justify different treatment of otherwise similarly situated taxpayers. See the list of behaviors and how each is treated below.
3. Degree of technical difficulty of the transaction or promotion.
4. Whether the transaction or promotion was marketed/promoted?
5. Sophistication of the taxpayer and their involvement in the investment decision.

TREATMENT OF INVESTORS' POSSIBLE BEHAVIORS

1) As part of an issue resolution strategy, it is reasonable to treat investors who complied with disclosure requirements differently than those who failed to comply. Different treatment may be appropriate for those taxpayers who:

- Disclosed under *Announcement 2002-2, 2002-1 C.B. 304.*, which provides that a penalty can be waived if the investor complied with the Announcement.
- Disclosed in accordance with 26 CFR 1.6011-4 in a timely manner on a return (including an amended return). As a general matter, a taxpayer must disclose their participation in a reportable transaction (such as a listed transaction or a transaction of interest) by attaching a Form 8886, Reportable Transaction Disclosure Statement, with its tax return for each year in which the taxpayer participated in the transaction and by sending a copy of that form to the Office of Tax Shelter Analysis (OTSA) at the same time that any disclosure statement is first filed by the taxpayer pertaining to a particular reportable transaction.
- Later listed transactions or Transactions of Interest: or a transaction of interest: If a transaction identified as a listed transaction or a transaction of interest is after a taxpayer filed a tax return reflecting participation in a reportable transaction and before the end of the period of limitations on assessment of tax, for any taxable year in which the taxpayer participated in the listed transaction or transaction of interest the taxpayer must disclose by filing a Form 8886 with OTSA within 90 calendar days after the date on which the transaction became a listed transaction or a transaction of interest unless the published guidance identifying the transaction as a listed transaction or transaction of interest provides otherwise.
- Voluntarily disclosed non-listed transaction to Criminal Investigation under voluntary disclosure or by filing a corrected taxable amended return.

2) For investors who were required to disclose and did not comply: No waiver of the penalty would be generally proposed as part of a resolution strategy. The penalty issue would need to be developed in each case and reasonable cause addressed for penalties to which reasonable cause is a defense.

3) For investors who received fees from other investors (promoters/advisers) for activities related to the shelter: They would be excluded from any other general categories of penalty relief as part of a resolution strategy. The penalty issue would need to be developed in each case and reasonable cause addressed for penalties to which reasonable cause is a defense.

4) For investors who were not required to disclose: It may be appropriate to provide a no waiver of penalty as part of a resolution strategy. The penalty issue would need to be developed in each case and potential reasonable cause should be addressed.

Exhibit 4.32.1-3 (Cont. 1) (06-20-2024)

Criteria for Development of the Penalty Resolution

5) When developing a resolution strategy, consider investor attempts to fully disclose the transaction or to conceal the transaction. Different actions on the part of the investor may warrant different penalty considerations.

Exhibit 4.32.1-4 (06-20-2024)**Criteria for Identification and Development of Issues in Cases to Designate for Litigation****Circumstances for Considering Designation Include, but are not limited to:**

Certain legal issues are susceptible to recurring compliance challenges that are not effectively addressed administratively or through published guidance. In limited circumstances, examination personnel may consider requesting designation of an issue in a case where sound tax administration is best served by establishing a legal precedent on the issue. Examples illustrative of situations in which sound tax administration is best served by establishing judicial precedent are where designation would:

- stem the proliferation of abusive tax transactions or other significant non-compliance (through early issue resolution),
- reduce future compliance and litigation costs of other taxpayers and the government (through early issue resolution, broad-based settlement initiatives, or other means), or
- resolve issues with respect to which published guidance has not resulted in compliance or where there is a wide divergence between IRS and taxpayer viewpoints on the law.

Examination personnel should request designation of an issue in a case in the limited circumstances where sound tax administration is best served by establishing a legal precedent on the issue and not merely to prevent Appeals' review.

While addressing whether selected issues in cases should be considered for designation for litigation as part of an overall tax shelter strategy, the following criteria should be considered:

1. If the shelter transaction includes a significant legal issue that affects a large number of taxpayers or has significant tax impact, consideration should be given to designation.
2. If the shelter transaction is still generally being used or promoted, consideration should be given to designation. However, the fact that the shelter is no longer promoted or has been closed down by legislation or regulation does not mean that designation should not be considered. There may be a significant number of cases for prior years that need resolution if the legislation or regulation is prospective only. Consider, for example, the use of a resolution in the contingent liability transactions. See Rev. Proc. 2002-67, Settlement of Section 351 Contingent Liability Tax Shelter Cases.
3. If there is a need to establish judicial precedent due to a wide divergence between IRS and taxpayer viewpoints on the law, consideration should be given to designation. Designation and a court decision would promote ultimate resolution of the issue and conserve resources for both the government and taxpayers. An example of this is lease-in, lease-out transactions ("LILOs") described in Rev. Rul. 2002-69.
4. If one or more aspects of the shelter transaction continue to be significant to other tax shelter transactions and have broader impact than the immediate shelter, e.g., issues surrounding application of IRC 351, Transfer to Corporation Controlled by Transferor, defeasance, or partnership basis, consideration should be given to designation. For example, the shelter may no longer be promoted or tax benefits from the shelter transaction may no longer be claimed by the taxpayer; however, transactions with similar structures or features may continue to be promoted or subsequent shelter transactions may utilize overstated tax basis from the prior shelter.
5. Designation may not be necessary if cases with the same or similar issue are already docketed or scheduled for trial.
6. Designation may not be necessary if the issue under examination is being conceded by many taxpayers during examination.

If a decision is made to select issues to designate for litigation, the following factors should be considered:

Several cases should be considered and developed for potential designation. Often taxpayers may concede the issue or threaten to pay the tax and file a refund suit. If the taxpayer concedes the issue, the case should not

Exhibit 4.32.1-4 (Cont. 1) (06-20-2024)**Criteria for Identification and Development of Issues in Cases to Designate for Litigation**

be designated. A threat to pay the tax and file a refund suit should not alter the decision to designate. If a taxpayer pays the tax and files a refund suit after the case is designated, the Department of Justice will be apprised of the designation and take it into consideration when handling the case.

The issue in the case recommended for litigation should result in a decision that will impact the other cases with similar transactions. Thus, cases should be selected with fact patterns that are fairly representative of the cases involved in the shelter strategy.

Designated issues in cases must be developed and resources must be committed for their complete development. When an issue in a case is identified as a potential for designation and the development of the issue is underway, a commitment must be made to follow through on the process unless the recommendation for designation is determined to be no longer appropriate. Compliance must commit its resources to the complete development of the issues, including but not limited to:

- Hiring of outside experts including appraisers, economists, etc.
- Transcribed interviews for key parties.
- Summonses of necessary taxpayer and third party documents and enforcement if necessary.

The process of designating an issue in a case is generally lengthy. The procedures for designating a case for litigation are set forth in the Chief Counsel's Directive Manual. See *CCDM 33.3.6, Other Legal Advice; Designating a Case for Litigation*. In addition, once a case is before the court, the time frame for an ultimate decision is uncertain and may be lengthy.

Full development of the penalty should be completed and the penalty analysis and decision made part of the case designation process. Designation of non-penalty issues in a case does not necessarily mean the penalty should be designated. The penalty must separately meet the criteria for designation.

The effect of the statute of limitations on case development and designation process must be considered. For example, there must be sufficient time to fully develop the case including making the recommendation and securing approval for designation.

The overall impact on the particular taxpayer must be considered. For example, if the taxpayer has carry backs, carry-overs, or credits that eliminate or significantly reduce the tax deficiency, the case may not be a good one to designate for litigation.

The positions that may have been taken on the same or a similar issue for the particular taxpayer that may affect an overall view of the case must be considered, for example, whether the issue was examined and no adjustment made on a prior examination.

Effect of Designating a Case for Litigation

When an issue under the jurisdiction of a BOD is designated for litigation, a partial agreement may be secured for the non-designated and agreed issues. The taxpayer will not receive a 30-day (or similar) letter with respect to the remaining unresolved issues in the case. Rather, the taxpayer will be issued a SNOD for the unagreed issues. Chief Counsel should be contacted to discuss the appropriate procedures to follow if the issue in question is an employment tax issue. In general, the designation of an issue in a case will not preclude the settlement of the remaining issues either before or after the case is docketed. Nor, in general, will designation preclude Appeals from considering and settling the same issue in other cases within its jurisdiction.

Exhibit 4.32.1-5 (06-20-2024)**Criteria for Development of the Treatment and Consideration of the Transaction Costs**

Transaction costs may include fees to promoters and to accommodating parties, fees for document preparation, actual losses incurred that are associated with the transaction (true economic losses), fees for legal advice and for valuations or appraisals, interest expense and similar types of expenses. These transaction costs are sometimes referred to as the “out-of-pocket costs”. As a legal matter, rarely would taxpayers be entitled to out-of-pocket costs where a transaction is a sham in fact or lacks economic substance because such transactions generally do not give rise to valid deductions or losses.

Factors that tend to support allowing transactions cost include, but not limited to:

1. The legal theory is based on a technical argument.
2. A specific transaction cost that is attributable to a separate economically substantive element that was not the centerpiece of the underlying sham transaction.

Note: It is important to considered how the transaction costs would be allowed. For example, should the costs be part of a basis determination.

Factors that tend to support disallowing transactions cost include, but not limited to:

1. Transaction costs that are an integral part of the purported benefits of the transaction. For example, if the taxpayer generates interest deductions by entering into an abusive repurchase agreement that results in payment of more interest than interest received, the payments made by the taxpayer should not be permitted as an allowable deduction because the payments constitute the principal tax benefits of the transaction. See, e.g. *United States v. Wexler*, 31 F. 3d 117 (3rd Cir. 1994).
2. Transaction costs that cannot be readily determined and, therefore, allowance will result in disparate treatment among taxpayers.
3. Transaction costs that were paid to an external party for the majority of the investors.
4. Transaction costs incurred by the taxpayer to develop the transaction costs and that were not paid to external parties, taking into account equitable treatment of taxpayers and the resources required to develop the amount of the transaction costs.

In some cases it may be appropriate to allow only partial transaction cost or only specific transaction costs.