

106TH CONGRESS
1ST SESSION

H. R. 2255

To amend the Internal Revenue Code of 1986 to curb tax abuses by disallowing tax benefits claimed to arise from transactions without substantial economic substance.

IN THE HOUSE OF REPRESENTATIVES

JUNE 17, 1999

Mr. DOGGETT (for himself, Mr. STARK, Mr. HINCHEY, Mr. TIERNEY, Mr. ALLEN, Mr. LUTHER, Mr. BONIOR, and Mr. FARR of California) introduced the following bill; which was referred to the Committee on Ways and Means

A BILL

To amend the Internal Revenue Code of 1986 to curb tax abuses by disallowing tax benefits claimed to arise from transactions without substantial economic substance.

1 *Be it enacted by the Senate and House of Representa-*
2 *tives of the United States of America in Congress assembled,*

3 **SECTION 1. SHORT TITLE.**

4 This Act may be cited as the “Abusive Tax Shelter
5 Shutdown Act of 1999”.

6 **SEC. 2. FINDINGS AND PURPOSE.**

7 (a) FINDINGS.—The Congress hereby finds that:

1 (1) Many corporate tax shelter transactions are
2 complicated ways of accomplishing nothing aside
3 from claimed tax benefits, and the legal opinions
4 justifying those transactions take an inappropriately
5 narrow and restrictive view of well-developed court
6 doctrines under which—

7 (A) the taxation of a transaction is deter-
8 mined in accordance with its substance and not
9 merely its form,

10 (B) transactions which have no significant
11 effect on the taxpayer's economic or beneficial
12 interests except for tax benefits are treated as
13 sham transactions and disregarded,

14 (C) transactions involving multiple steps
15 are collapsed when those steps have no substan-
16 tial economic meaning and are merely designed
17 to create tax benefits,

18 (D) transactions with no business purpose
19 are not given effect, and

20 (E) in the absence of a specific congres-
21 sional authorization, it is presumed that Con-
22 gress did not intend a transaction to result in
23 a negative tax where the taxpayer's economic
24 position or rate of return is better after tax
25 than before tax.

1 (2) Permitting aggressive and abusive tax shel-
 2 ters not only results in large revenue losses but also
 3 undermines the sense of voluntary compliance with
 4 the Internal Revenue Code of 1986.

5 (b) PURPOSE.—The purpose of this Act is to elimi-
 6 nate abusive tax shelters by denying tax attributes claimed
 7 to arise from transactions that do not meet a heightened
 8 economic substance requirement and by repealing the pro-
 9 vision that permits legal opinions to be used to avoid pen-
 10 alties on tax underpayments resulting from transactions
 11 without significant economic substance or business pur-
 12 pose.

13 **SEC. 3. DISALLOWANCE OF NONECONOMIC TAX AT-**
 14 **TRIBUTES.**

15 Section 7701 of the Internal Revenue Code of 1986
 16 is amended by redesignating subsection (m) as subsection
 17 (n) and by inserting after subsection (l) the following new
 18 subsection:

19 “(m) DISALLOWANCE OF NONECONOMIC TAX AT-
 20 TRIBUTES.—

21 “(1) IN GENERAL.—In determining liability for
 22 any tax under subtitle A, noneconomic tax attributes
 23 shall not be allowed.

24 “(2) NONECONOMIC TAX ATTRIBUTE.—For
 25 purposes of this subsection, a noneconomic tax at-

tribute is any deduction, loss, or credit claimed to result from any transaction unless—

“(A) the transaction changes in a meaningful way (apart from Federal income tax consequences) the taxpayer’s economic position, and

“(B)(i) the present value of the reasonably expected potential income from the transaction (and the taxpayer’s risk of loss from the transaction) are substantial in relationship to the present value of the tax benefits claimed, or

“(ii) in the case of a transaction which is in substance the borrowing of money or the acquisition of financial capital, the deductions claimed with respect to the transaction for any period are not significantly in excess of the economic return for such period realized by the person lending the money or providing the financial capital.

“(3) PRESUMPTION OF NONECONOMIC TAX ATTRIBUTES.—For purposes of paragraph (2), the following factors shall give rise to a presumption that a transaction fails to meet the requirements of paragraph (2):

1 “(A) The fact that the payments, liabil-
2 ities, or assets that purport to create a loss (or
3 other benefit) for tax purposes are not reflected
4 to any meaningful extent on the taxpayer’s
5 books and records for financial reporting pur-
6 poses.

7 “(B) The fact that the transaction results
8 in an allocation of income or gain to a tax-indif-
9 ferent party which is substantially in excess of
10 such party’s economic income or gain from the
11 transaction.

12 “(4) TREATMENT OF BUILT-IN LOSS.—The de-
13 termination of whether a transaction results in the
14 realization of a built-in loss shall be made under
15 subtitle A as if this subsection had not been enacted.
16 For purposes of the preceding sentence, the term
17 ‘built-in loss’ means any loss or deduction to the ex-
18 tent that such loss or deduction had economically
19 been incurred before such transaction is entered into
20 and to the extent that the loss or deduction was eco-
21 nomicallly borne by the taxpayer.

22 “(5) DEFINITION AND SPECIAL RULES.—For
23 purposes of this subsection—

24 “(A) TAX-INDIFFERENT PARTY.—The
25 term ‘tax-indifferent party’ means any person

1 or entity exempt from tax under subtitle A. A
2 person shall be treated as a tax-indifferent
3 party with respect to a transaction if, by reason
4 of such person's method of accounting, the
5 items taken into account with respect to the
6 transaction have no substantial impact on such
7 person's liability under subtitle A.

8 “(B) SERIES OF RELATED TRANS-
9 ACTION.—A transaction which is part of a se-
10 ries of related transactions shall be treated as
11 meeting the requirements of paragraph (2) only
12 if—

13 “(i) such transaction meets such re-
14 quirements without regard to the other
15 transactions, and

16 “(ii) such transactions, if treated as 1
17 transaction, would meet such requirements.

18 A similar rule shall apply to a multiple step
19 transaction with each step being treated as a
20 separate related transaction.

21 “(C) NORMAL BUSINESS TRANSACTIONS.—
22 In the case of a transaction which is an integral
23 part of a taxpayer's trade or business and
24 which is entered into in the normal course of
25 such trade or business, the determination of the

1 potential income from such transaction shall be
2 made by taking into account its relationship to
3 the overall trade or business of the taxpayer.

4 “(D) TREATMENT OF FEES.—In deter-
5 mining whether there is risk of loss from a
6 transaction (and the amount thereof), potential
7 loss of fees and other transaction expenses shall
8 be disregarded.

9 “(E) TREATMENT OF ECONOMIC RETURN
10 ENHANCEMENTS.—The following shall be treat-
11 ed as economic returns and not tax benefits:

12 “(i) The credit under section 29 (re-
13 lating to credit for producing fuel from a
14 nonconventional source).

15 “(ii) The credit under section 42 (re-
16 lating to low-income housing credit).

17 “(iii) The credit under section 45 (re-
18 lating to electricity produced from certain
19 renewable resources).

20 “(iv) The credit under section 1397E
21 (relating to credit to holders of qualified
22 zone academy bonds) or any similar pro-
23 gram hereafter enacted.

24 “(v) Any other tax benefit specified in
25 regulations.

1 “(F) EXCEPTIONS FOR NONBUSINESS
2 TRANSACTIONS.—

3 “(i) INDIVIDUALS.—In the case of an
4 individual, this subsection shall only apply
5 to transactions entered into in connection
6 with a trade or business or activity en-
7 gaged in for profit.

8 “(ii) CHARITABLE TRANSFERS.—This
9 subsection shall not apply in determining
10 the amount allowable as a deduction under
11 section 170, 545(b)(2), 556(b)(2), or
12 642(c).

13 “(6) ECONOMIC SUBSTANCE DOCTRINE, ETC.,
14 NOT AFFECTED.—The provisions of this subsection
15 shall not be construed as altering or supplanting any
16 rule of law referred to in section 6662(i)(2)(B) and
17 the requirements of this subsection shall be con-
18 strued as being in addition to any such rule of law.”

19 **SEC. 4. INCREASE IN SUBSTANTIAL UNDERPAYMENT PEN-**
20 **ALTY WITH RESPECT TO DISALLOWED NON-**
21 **ECONOMIC TAX ATTRIBUTES.**

22 Section 6662 of the Internal Revenue Code of 1986
23 (relating to imposition of accuracy-related penalty) is
24 amended by adding at the end the following new sub-
25 section:

1 “(i) INCREASE IN PENALTY IN CASE OF DIS-
2 ALLOWED NONECONOMIC TAX ATTRIBUTES.—

3 “(1) IN GENERAL.—In the case of the portion
4 of the underpayment to which this subsection
5 applies—

6 “(A) subsection (a) shall be applied with
7 respect to such portion by substituting ‘40 per-
8 cent’ for ‘20 percent’, and

9 “(B) subsection (d)(2)(B) and section
10 6664(c) shall not apply.

11 “(2) UNDERPAYMENTS TO WHICH SUBSECTION
12 APPLIES.—This subsection shall apply to an under-
13 payment to which this section applies by reason of
14 paragraph (1) or (2) of subsection (b) to the extent
15 that such underpayment is attributable to—

16 “(A) the disallowance of any noneconomic
17 tax attribute (determined under section
18 7701(m)), or

19 “(B) the disallowance of any other
20 benefit—

21 “(i) because of a lack of economic
22 substance or business purpose for the
23 transaction giving rise to the claimed ben-
24 efit,

1 “(ii) because the form of the trans-
2 action did not reflect its substance, or

3 “(iii) because of any other similar rule
4 of law.

5 “(3) INCREASE IN PENALTY NOT TO APPLY IF
6 COMPLIANCE WITH DISCLOSURE REQUIREMENTS.—

7 Paragraph (1)(A) shall not apply if the taxpayer—

8 “(A) discloses to the Secretary within 30
9 days after the closing of the transaction appro-
10 priate documents describing the transaction,
11 and

12 “(B) files with the taxpayer’s return of tax
13 imposed by subtitle A—

14 “(i) a statement verifying that such
15 disclosure has been made,

16 “(ii) a detailed description of the
17 facts, assumptions of facts, and factual
18 conclusions with respect to the business or
19 economic purposes or objectives of the
20 transaction that are relied upon to support
21 the manner in which it is reported on the
22 return,

23 “(iii) a description of the due dili-
24 gence performed to ascertain the accuracy

1 of such facts, assumptions, and factual
2 conclusions,

3 “(iv)(I) a statement (signed by the
4 senior financial officer of the corporation
5 under penalty of perjury) that the facts,
6 assumptions, or factual conclusions relied
7 upon in reporting the transaction are true
8 and correct as of the date the return is
9 filed, to the best of such officer’s knowl-
10 edge and belief, and

11 “(II) if the actual facts varied materi-
12 ally from the facts, assumptions, or factual
13 conclusions relied upon, a statement de-
14 scribing such variances,

15 “(v) copies of any written material
16 provided in connection with the offer of the
17 transaction to the taxpayer by a third
18 party,

19 “(vi) a full description of any express
20 or implied agreement or arrangement with
21 any advisor, or with any offeror, that the
22 fee payable to such person would be con-
23 tingent or subject to possible reimburse-
24 ment, and

1 “(vii) a full description of any express
2 or implied warranty from any person with
3 respect to the anticipated tax results from
4 the transaction.”

5 **SEC. 5. EFFECTIVE DATE.**

6 The amendments made by this Act shall apply to
7 transactions after the date of the enactment of this Act.

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