Office of Chief Counsel
Internal Revenue Service
Memorandum

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Third Party Communication: None
Date of Communication: Not Applicable

UILC: 6011.01-00, 6707.00-00, 9300.32-00

date: April 02, 2009

to: Associate Area Counsel (Kansas City)
(Small Business/Self-Employed)

from: Senior Technician Reviewer, Branch 3
(Passthroughs & Special Industries)

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subject:

This Chief Counsel Advice responds to your request for assistance. In accordance with § 6110(k)(3) of the Internal Revenue Code, this advice may not be used or cited as precedent.

LEGEND

Existing S Corporation =

Roth Corporation =

Shareholders of Existing Corporation:

Father =

Son 1 =

Son 2 =

Amount1 =

Amount2 =

Amount3 =

Amount4 =

Month1 =

Month2 =

Month3 =

Month4 =

Year1 =

Year2 =

Year3 =

ISSUES

1. Whether the transaction engaged in by Father, Son1, Son2, Existing S Corporation, and Roth Corporation is the same as, or substantially similar to, the transaction identified in Notice 2004-8, 2004-1 C.B. 333, as a listed transaction;

2. Whether Father, Son1, Son2, Existing S Corporation, and Roth Corporation participated in the transaction in Year1 and Year2 under § 1.6011-4 of the Income Tax Regulations; and

3. Whether the penalty for failure to disclose participation in a listed transaction under § 6707A applies to Father, Son1, Son2, Existing S Corporation, and Roth Corporation.

CONCLUSIONS

1. The transaction engaged in by Father, Son1, Son2, Existing S Corporation, and Roth Corporation is the same as, or substantially similar to, the transaction identified in Notice 2004-8 as a listed transaction;

2. Father, Son1, Son2, Existing S Corporation, and Roth Corporation participated in the transaction in Year1, but not in Year2; and

3. The penalty under § 6707A for failure to disclose participation in a listed transaction is effective for returns and statements the due date for which is after October 22, 2004, and which were not filed before that date. The Form 8886 disclosure statement was due when the Year1 returns were filed, and the taxpayers' returns were all filed prior to October 23, 2004. Therefore, § 6707A

does not apply to Father, Son1, Son2, Existing S Corporation, and Roth Corporation.

FACTS

Father, Son1, and Son2 are the shareholders of Existing S Corporation, an S corporation. Roth Corporation is an S corporation that was incorporated in Month1 of Year1. All parties are calendar year taxpayers.

In Month2 of Year1, Father, Son1, and Son2 each created a Roth IRA and contributed cash in the amount of the $3,000 annual contribution limit for Year1. Father, Son1, and Son2 then directed their respective Roth IRAs to purchase all of the outstanding shares of Roth Corporation.[1] Thus, Roth Corporation was initially capitalized in the amount of $9,000, and each Roth IRA owned one-third of Roth Corporation.

Existing S Corporation entered into an administrative services agreement with Roth Corporation in Month3 of Year1. Under this agreement, Existing S Corporation was required to pay to Roth Corporation a minimum annual management fee in exchange for services purportedly to be provided by Roth Corporation to Existing S Corporation.

Prior to the release of Notice 2004-8, Existing S Corporation paid Roth Corporation a total of approximately Amount1 in Month4 of Year1 pursuant to the administrative services agreement. After the release of Notice 2004-8, Roth Corporation paid a portion of that amount, Amount2, back to Existing S Corporation in Year2, claiming that Roth Corporation was overpaid in Year1. No payments were made by Existing S Corporation to Roth Corporation under the administrative services agreement in Year2.

During Month3 of Year1 through the end of Year2, Amount3 was distributed from Roth Corporation to the Roth IRAs. Roth Corporation was dissolved and liquidated in Month4 of Year2. Each of the three shareholder Roth IRAs received a liquidation distribution of Amount4.

Existing S Corporation claimed a deduction for the management fees paid to Roth Corporation on its Form 1120S for Year1 (which ultimately passed through to Father, Son1, and Son2).[2] Roth Corporation reported the receipt of the management

[1] The Roth Corporation capitalization transaction terminated Roth Corporation's S election because an IRA is not an eligible shareholder of an S corporation. This transaction may also constitute a prohibited transaction under § 4975 (potentially causing a loss of the exemption of each IRA under § 408(e) and a distribution of each IRA to its participant for such year). However, neither of these potential consequences alters the analysis with respect to whether the transaction constitutes a listed transaction for purposes of § 1.6011-4.

[2] Pursuant to § 1366, the shareholders of Existing S Corporation were required to take into account on

fees in its income for Year1. All the parties filed their Year1 returns prior to October 23, 2004. None of the parties filed Form 8886 to disclose the transaction.

In Year3, Existing S Corporation, Roth Corporation, Father, Son1, and Son2 timely elected to participate in the Global Settlement Initiative under Announcement 2005-80 with respect to the Notice 2004-8 listed transactions.

LAW

The regulations under § 6011 that are applicable to the present case are § 1.6011-4 as finalized in TD 9046, 68 CFR 10161. TD 9046 is effective for transactions entered into on or after February 28, 2003.[3]

Section 1.6011-4(a) provides that every taxpayer that has participated in a reportable transaction and who is required to file a tax return must attach to its return for the taxable year a disclosure statement in the form prescribed.

Section 1.6011-4(b)(1) provides that a reportable transaction is a transaction described in § 1.6011-4(b)(2) through (b)(7). The term transaction includes all of the factual elements relevant to the expected tax treatment of any investment, entity, plan, or arrangement, and includes any series of steps carried out as part of a plan.

Section 1.6011-4(b)(2) provides that a listed transaction is a transaction that is the same as or substantially similar to one of the types of transactions that the Internal Revenue Service (IRS) has determined to be a tax avoidance transaction and identified by notice, regulation, or other form of published guidance as a listed transaction.

Section 1.6011-4(c)(3)(i)(A) provides that a taxpayer has participated in a listed transaction if the taxpayer's tax return reflects tax consequences or a tax strategy described in the published guidance that lists the transaction under § 1.6011-4(b)(2). A taxpayer also has participated in a listed transaction if the taxpayer knows or has reason to know that the taxpayer's tax benefits are derived directly or indirectly from tax consequences or a tax strategy described in published guidance that lists a transaction under § 1.6011-4(b)(2). Published guidance may identify other types or classes of persons that will be treated as participants in a listed transaction.

Section 1.6011-4(c)(4) provides that the term substantially similar includes any transaction that is expected to obtain the same or similar types of tax consequences and that is either factually similar or based on the same or similar tax strategy. Receipt

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their individual income tax returns their pro rata share of Existing S Corporation's items of income (including tax exempt income), loss, deduction, or credit the separate treatment of which could affect the liability for tax of any shareholder, and nonseparately computed income or loss.

[3] TD 9046 was subsequently modified by TD 9108, 2004-1 C.B. 429, for transactions entered into on or after December 29, 2003, and has since been modified.

of an opinion regarding the tax consequences of the transaction is not relevant to the determination of whether the transaction is the same as or substantially similar to another transaction. Further, the term substantially similar must be broadly construed in favor of disclosure.

Section 1.6011-4(d) provides that a taxpayer required to file a disclosure statement under § 1.6011-4 must file a completed Form 8886 in accordance with the instructions to the form.

Section 1.6011-4(e)(1) provides, in part, that a disclosure statement for a reportable transaction must be attached to the taxpayer's tax return for each taxable year for which a taxpayer participates in a reportable transaction. In addition, a copy of the disclosure statement must be sent to OTSA at the same time that any disclosure statement is first filed by the taxpayer pertaining to a particular reportable transaction. In the case of a taxpayer that is a partnership or S corporation, the disclosure statement for a reportable transaction must be attached to the partnership's or S corporation's tax return for each taxable year in which the partnership or S corporation participates in the transaction under the rules of § 1.6011-4(c)(3)(i).

Section 1.6011-4(e)(2)(i) provides that if a transaction becomes a listed transaction after the filing of the taxpayer's final tax return reflecting either tax consequences or a tax strategy described in the published guidance listing the transaction (or a tax benefit derived from tax consequences or a tax strategy described in the published guidance listing the transaction) and before the end of the statute of limitations period for that return, then a disclosure statement must be filed as an attachment to the taxpayer's tax return next filed after the date the transaction is listed.

Section 6707A(a) provides that any person who fails to include on any return or statement any information with respect to a reportable transaction which is required under § 6011 to be included with such return or statement shall pay a penalty in the amount determined under § 6707A(b). Section 6707A(b)(2) provides that the amount of the penalty under § 6707A(a) with respect to a listed transaction shall be (A) $100,000 in the case of a natural person, and (B) $200,000 in any other case. Section 6707A is effective for returns and statements the due date for which is after October 22, 2004, and which were not filed before such date.

In Notice 2004-8, the Service identified transactions that are the same as, or substantially similar to, transactions described in the Notice as “listed transactions” for purposes of § 1.6011-4(b)(2) and §§ 301.6111-2(b)(2) and 301.6112-1(b)(2) of the Procedure and Administration Regulations effective December 31, 2003, the date the notice was released to the public. Transactions identified as “listed transactions” in Notice 2004-8 include arrangements in which an individual, related persons, or a business controlled by such individual or related persons, engage in one or more transactions with a corporation, including contributions of property to such corporation, substantially all the shares of which are owned by one or more Roth IRAs maintained

for the benefit of the individual, related persons, or both. The transactions are listed transactions with respect to the individuals for whom the Roth IRAs are maintained, the business (if not a sole proprietorship) that is a party to the transaction, and the corporation substantially all the shares of which are owned by the Roth IRAs. The transactions described in the Notice have been designed to avoid the statutory limits on contributions to a Roth IRA contained in § 408A.

ANALYSIS

In determining if the transaction entered into in this case is the same as, or substantially similar to, the listed transaction described in Notice 2004-8, we consider whether the transaction 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 the Notice 2004-8 transaction. We construe the term substantially similar broadly in favor of disclosure.

We have determined that the tax consequences expected to be obtained in the transaction entered into in this case are the same or of a similar type as the tax consequences obtained in the listed transaction identified in Notice 2004-8 and that the transaction is either factually similar or based on the same or similar tax strategy. In the Notice 2004-8 transaction, an individual, related persons, or a business controlled by such individual or related persons, engage in one or more transactions with a corporation, including contributions of property to such corporation, substantially all the shares of which are owned by one or more Roth IRAs maintained for the benefit of the individual, related persons, or both. The transactions described in Notice 2004-8 have been designed to avoid the statutory limits on contributions to a Roth IRA contained in § 408A. In this case, Father, Son1, and Son2 were able to transfer value, over the annual Roth IRA contribution limit, from Existing S Corporation, a business controlled by Father, Son1, and Son2, to the Roth IRAs, which were maintained for the benefit of Father, Son1, and Son2, through the use of Roth Corporation. The value transferred was in the form of payments of the annual management fee from Existing S Corporation to Roth Corporation during Year1. These payments increased the value of the shares of Roth Corporation stock held by the Roth IRAs. The increase in value of the Roth Corporation stock represents an unfair value shift from Father, Son1, and Son2 into their respective Roth IRAs. Therefore, the transaction in this case is the same as, or substantially similar to, the transaction identified as a listed transaction in Notice 2004-8.

Under § 1.6011-4(c)(3)(i)(A), a taxpayer participates in a listed transaction if the taxpayer's tax return reflects tax consequences or a tax strategy described in the published guidance that lists the transaction. Father, Son1, Son2, Existing S Corporation, and Roth Corporation participated in the listed transaction in Year1 because their respective returns reflected the tax consequences or tax strategy described in Notice 2004-8. Existing S Corporation reflected on its Year1 return a deduction for the payment of the annual management fee. Father, Son1, and Son2 also reflected on their returns a deduction for their share of the payment of the annual

management fee. Roth Corporation reflected on its Year1 return income from the annual management fee.

Father, Son1, Son2, Existing S Corporation, and Roth Corporation did not participate in the listed transaction in Year2 because their returns did not reflect the tax consequences or tax strategy described in Notice 2004-8. No payments were made to Roth Corporation from Existing S Corporation, nor were any other transfers of value made to Roth Corporation from Existing S Corporation, Father, Son1, or Son2, in Year2.

Because Father, Son1, Son2, Existing S Corporation, and Roth Corporation participated in a Notice 2004-8 listed transaction in Year1, each was required to disclose their participation by attaching Form 8886 to their respective Year1 return and sending a copy of the Form 8886 to OTSA. Father, Son1, Son2, Existing S Corporation, and Roth Corporation failed to attach Form 8886 to their respective Year1 returns and failed to send a copy to OTSA. Therefore, they each failed to comply with the requirements under § 1.6011-4 in Year1 with respect to the transaction.

Section 6707A is effective for returns and statements the due date for which is after October 22, 2004, and which were not filed before that date. Consequently, the penalty under § 6707A is not applicable to Father, Son1, Son2, Existing S Corporation, and Roth Corporation for their failures to disclose properly under § 6011 with respect to their Year1 returns because the Form 8886 disclosure statement was due when the Year1 return was filed, which was prior to October 23, 2004.

This writing may contain privileged information. Any unauthorized disclosure of this writing may undermine our ability to protect the privileged information. If disclosure is determined to be necessary, please contact this office for our views.

Please call at if you have any further questions.

/s/

By: _____

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