Regulating Corporate Tax Shelters: Seeking Certainty in a Complex World

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In 1986, Congress passed a tax-reform law that would theoretically requiring every U.S. company to pay its fair share of taxes. Presently, however, government and corporate records indicate that many companies are paying little, if any, federal income tax. Although many of these companies were small private firms, in 1995 forty percent of all companies with more than $250 million in assets or $50 million in gross receipts paid less than $100,000 in federal income tax. Although Congress's 1986 mandate has impacted the amount of corporate income tax revenue collected, corporations have discovered a wide array of new and often complex tax shelters. Some estimates indicate that corporate tax shelters cost the federal government ten billion dollars annually in lost income tax revenue.

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2. See id. (highlighting the findings of a General Accounting Office Study). From 1989 to 1995, more than half of all domestic corporations paid no federal income tax. See id.
3. See id.
4. See id. (observing that corporate income taxes comprised 10% of federal revenue in fiscal year 1999, an increase from 8% in 1986). Although corporate tax payments are up, however, they are not increasing at the same pace as corporate profits. See id. To some, the disparity between corporate tax rate increases and corporate profit increases is a result of increased globalization which creates opportunities for companies to shift profits to foreign countries with lower tax rates and still claim the corresponding deductions in the United States. See id; cf. Michael S. Powlen & Raj Tanden, Corporate Tax Shelters or Plus Ça Change, Plus C'est la Même Chose, in 1 TAX PLANNING FOR DOMESTIC & FOREIGN PARTNERSHIPS, LLCs, JOINT VENTURES & OTHER STRATEGIC ALLIANCES 1999, at 1059, 1072 (PLI Tax Law and Estate Planning Course Handbook Series No. 439, 1999) (recognizing that "Congress' desire to implement social policy through the tax code" often results in unintended loopholes as provisions are stretched beyond their original purposes by innovative taxpayers).
5. See, e.g., Curt Anderson, IRS Wins Tax Ruling Against UPS: Action Could Cost Package Carrier Millions, THE ADVOCATE (Baton Rouge), Aug. 12, 1999, at 1C. Some corporate tax executives, however, have questioned the accuracy of these estimates. See
The recent proliferation of corporate tax shelters has created a perception that corporations, through complexly structured transactions, are becoming increasingly adept at avoiding federal income taxes. Critics of corporate tax shelters believe that the increased use of corporate tax shelters threatens the effectiveness of the current tax system because of the potential drain on revenue and the threat to the integrity of the self-assessment tax system. In contrast, others contend that corporations do not violate the law by trying to minimize their taxes. Proponents of corporate tax shelters believe that the right of corporations to take advantage of the flexibility in the tax code to maximize deductions, while minimizing taxable income, is not only legitimate, but a sound business practice in an increasingly complex and competitive global business environment.


6. See STAFF OF JOINT COMM. ON TAX’N, 106TH CONG., 1ST SESS., STUDY OF PRESENT-LAW PENALTY AND INTEREST PROVISIONS AS REQUIRED BY SECTION 3801 OF THE INTERNAL REVENUE SERVICE RESTRUCTURING AND REFORM ACT OF 1998 (INCLUDING PROVISIONS RELATING TO CORP. TAX SHELTERS) 211 (Comm. Print 1999) (discussing the increasing use of sophisticated transactions to avoid federal income tax liability). This study will be referred to as JOINT COMM. REP., throughout this Comment. For a discussion of recent media revelations of complex corporate tax schemes, see Powlen & Tanden, supra note 4, at 1063-65.

7. Treasury Secretary Lawrence Summers referred to corporate tax shelters as “the most serious compliance issue threatening the American tax system today.” David Cay Johnston, U.S. Takes Aim at Tax Shelters for Companies, N.Y. TIMES, Feb. 29, 2000, at A1; see also JOINT COMM. REP., supra note 6, at 213. The characterization of the tax system as one of self-assessment refers to the requirement that taxpayers dutifully calculate and report their own tax liability each year. See id. The Joint Committee on Taxation emphasized that the IRS’s limited resources allow very few audits each year and therefore, place considerable reliance upon the good faith reporting of taxpayers. See id.

8. House Majority Leader Dick Armey has emphasized the legitimacy of corporate tax reduction strategies saying “[t]he business of a corporation is to maximize its earnings for its shareholders . . . Since tax is a very large part of their costs, anything they can do to minimize that share of their costs would be a legitimate thing.” Fawcett, supra note 5, at 9A.

9. See id.; see also Phillips, supra note 1, at A1 (suggesting that the increasingly global character of U.S. companies has contributed to the problems associated with corpo-
The tax law relating to business transactions is extremely complex. Such complexity may result from the sophistication of the economy, as well as from a desire to promote impartiality and integrity in the tax system by balancing its needs for effectiveness and flexibility. This balancing act results in ambiguous tax laws. Whether a transaction is char-

date tax shelters).

10. See Joint Comm. Rep., supra note 6, at 213; Fawcett, supra note 5, at 9A (quoting a San Francisco attorney as saying that corporate tax shelters are "predicated on complexity"); Powlen & Tanden, supra note 4, at 1066 (noting that the 1986 Tax Code "itself [was] not of one mind in defining 'tax shelters'"). The complexity of the current tax law is routinely attributed to earlier tax shelters. See id. at 1096. Judge Learned Hand addressed the complexity of the 1939 Tax Code, and wrote:

In my own case the words of such an act as the Income Tax, for example, merely dance before my eyes in a meaningless procession: cross-reference to cross-reference, exception upon exception—couched in abstract terms that offer no handle to seize hold of—leave in my mind only a confused sense of some vitally important, but successfully concealed, purport, which it is my duty to extract, but which is within my power, if at all, only after the most inordinate expenditure of time. I know that these monsters are the result of fabulous industry and ingenuity, plugging up this hole and casting out that net, against all possible evasion; yet at times I cannot help recalling a saying of William James about certain passages of Hegel: that they were no doubt written with a passion of rationality; but that one cannot help wondering whether to the reader they have any significance save that the words are strung together with syntactical correctness. Id. at 1073 n.27 (quoting The Spirit of Liberty: Papers and Addresses of Learned Hand 213 (2d ed. 1953)).

11. See Joint Comm. Rep., supra note 6, at 213; Powlen & Tanden, supra note 4, at 1069 (discussing the impact of sophisticated financial markets and the size of the international marketplace as contributing factors to the rise of modern tax shelters).

12. See Joint Comm. Rep., supra note 6, at 213-14; Powlen & Tanden, supra note 4, at 1068. The constant tug and pull that occurs between various competing interests in the formation of tax policy has been summarized as follows:

The subject of tax shelters implicates morality, politics, social policy, economic theory, legal theory, and psychology. This is why the public is so fascinated with the topic. To some, the story of a tax shelter can be a tale in which greed and hubris cloud the judgment of mighty titans who have risen to great heights, who become tempted by even greater riches and who fall to the retribution of the masses. To others, this same tax shelter can be a tale of heroic entrepreneurs who have created capital for the benefit of a society and who seek nobly to avoid having this capital impaired by a wasteful and incompetent governmental bureaucracy, and in which entrepreneurs, with the help of gifted tax planners, manage to use the system itself to preserve their capital, but ultimately fall prey to the knee-jerk decisions of a benighted judiciary. . . . To uncover the facts of an egregious tax shelter is to get a glimpse of the private moments of public figures whose public veneers are stripped away to reveal character flaws.

Id.

13. See Roby B. Sawyers, AICPA Comments on Administration's Corporate Tax Shelter Proposals, 1999 Tax Adviser 346, 347 (expressing concern regarding the lack of clear standards by which to identify abusive uses of tax laws); see also Powlen & Tanden, supra note 4, at 1070 (listing aspects of the current system that create the opportunity for
acterized as a corporate tax shelter depends on an analysis of the transaction's business purpose. If a significant purpose of the transaction avoids or evades federal income tax, it is classified as a tax shelter. It is often difficult, however, to determine with any degree of certainty a corporation's business purpose for a particular transaction. Consequently, several other characteristics of corporate tax shelters aid in making this determination.

One common characteristic of a tax shelter includes the lack of economic substance, which virtually eliminates the prospect of economic risk for the parties involved. Another characteristic of many corporate tax shelters is the participation of tax-indifferent parties. A tax-indifferent

tax shelters). Powlen and Tanden commented that the tax system involves principles that require "arbitrary line drawing," which are susceptible to manipulation, and provide no consistent basis by which to regulate the payment of taxes. Id.

14. See UPS v. Commissioner, 78 T.C.M. (CCH) 262, 293 (1999) (finding that the validity of a transaction came down to whether the taxpayer had a legitimate business purpose for engaging in it); Compaq Computer Corp. v. Commissioner, 113 T.C. 214, 224 (1999) (recognizing that business purpose requires that a taxpayer act in a "realistic and legitimate business fashion").

15. See Joint Comm. Rep., supra note 6, at 178. The Joint Committee on Taxation stated that while there is no "clear, uniform standard" as to what constitutes a corporate tax shelter, there are several statutory provisions and judicial doctrines that attempt to regulate corporate transactions in which a significant purpose is the avoidance or evasion of federal income tax. Id. (citing various sections of the tax code); see also Powlen & Tanden, supra note 4, at 1079 (recognizing that the law requires transactions to have some economic purpose besides tax savings). "[D]efining . . . [a] tax shelter is like defining moral behavior. The definition . . . depends on whether one is talking to a salesman, a customer, one's clients, opposing counsel, a judge, an IRS agent, or the mirror . . . . In the broadest sense a tax shelter is a transaction with tax benefits." Id. at 1067.

16. See U.S. Dep't of the Treasury, the Problem of Corporate Tax Shelters: Discussion, Analysis and Legislative Proposals 11-12 (1999) [hereinafter Treasury White Paper] (emphasizing that corporate tax shelters take many different forms and use many different structures); David P. Hariton, Sorting out the Tangle of Economic Substance, 52 Tax Law. 235, 240-41 (1999) (acknowledging the difficulty in distinguishing between proper and improper tax reduction strategies); Powlen & Tanden, supra note 4, at 1067.


18. See id. (quoting Professor Michael Graetz who defined tax shelters as "a deal done by very smart people that, absent tax considerations, would be very stupid"). Professor Graetz's definition highlights the lack of economic substance as a common characteristic of tax shelters. See id; Joint Comm. Rep., supra note 6, at 211 (discussing the reluctance of corporations to enter into transactions that involve substantial economic risk); Treasury White Paper, supra note 16, at 12 (maintaining that the participants in tax shelter transactions are "insulated from virtually all economic risk").

party is one that collects a fee for creating an advantageous situation for the party seeking to reduce its taxes. Finally, most corporate tax shelters involve extremely sophisticated and complex transactions. This often results in a nearly indiscernible web of provisions and steps that require regulators to spend countless hours and resources to interpret. Given the limited scope of government resources, these complex transactions may ultimately deter the government from challenging many transactions altogether.

The recent growth of corporate tax shelters is attributable to several factors. First, greater incentives exist for corporations to use tax shelters. Tax-indifferent parties are "accommodation parties who are paid a fee or an above-market return on investment for the service of absorbing taxable income or otherwise 'leasing' their tax-advantaged status." Id; see also Stanley Ruchelman & Harold L. Adrion, Check the Box Regulations: Hybrids in the International Context, in 6 Tax Planning for Domestic & Foreign Partnerships, LLCs, Joint Ventures & Other Strategic Alliances 1999, at 223, 285 (Tax Law and Estate Planning Course Handbook Series No. 444, 1999). Corporate tax shelters routinely take advantage of loopholes in the tax law, which are "exploited" with the assistance of tax-indifferent parties. Id. When this occurs, the tax-indifferent party claims the income or gain produced by the transaction, and the corporation claims the corresponding loss or deduction. See id. Tax-indifferent parties are usually offered an "accommodation fee" or an "enhanced return on investment" in exchange for their participation. Id.

A finely crafted corporate tax shelter is a marvel of financial engineering. From the outside it appears opaque, a mere shuffling of paper. But a well-executed shelter, besides protecting company assets from the tax man, requires innovation, careful planning, and some winks and nods from like-minded citizens in the corporate community.


The political system gives us the massively ambivalent, pluralistic, pop-perception-and-PAC-driven legislative process. The legislative effluvia, that is, the law, is then administered and interpreted by the Treasury and the IRS, both of which are under increasing budgetary constraints, and which are populated, in the end, by people who are only human. These constraints make the audit less of a statistical threat.

Id. (footnotes omitted); see also Joint Comm. Rep., supra note 6, at 219. The Joint Committee Report recognized the difficulty of exposing corporate tax shelters:

20. See Treasury White Paper, supra note 16, at 15-16. Tax-indifferent parties are "accommodation parties who are paid a fee or an above-market return on investment for the service of absorbing taxable income or otherwise 'leasing' their tax-advantaged status." Id; see also Stanley Ruchelman & Harold L. Adrion, Check the Box Regulations: Hybrids in the International Context, in 6 Tax Planning for Domestic & Foreign Partnerships, LLCs, Joint Ventures & Other Strategic Alliances 1999, at 223, 285 (Tax Law and Estate Planning Course Handbook Series No. 444, 1999).

21. See Treasury White Paper, supra note 16, at 17. A recent article, which attempted to illustrate the degree of creativity involved in developing current corporate tax shelters, highlighted their complexity:

A finely crafted corporate tax shelter is a marvel of financial engineering. From the outside it appears opaque, a mere shuffling of paper. But a well-executed shelter, besides protecting company assets from the tax man, requires innovation, careful planning, and some winks and nods from like-minded citizens in the corporate community.


22. See James Lardner, Corporations Sing: Gimme Tax Shelter, U.S. News & World Rep., Apr. 5, 1999, at 49 (noting that corporate tax shelters are often "artfully concealed in the minutiae of a tax return"); Phillips, supra note 1, at A1 (recognizing that today's companies indulge in extremely complex tax shelters that are not easily understood and are rarely discovered); see also Powlen & Tanden, supra note 4, at 1068-69. The difficult task faced by the IRS in uncovering corporate tax shelters has been emphasized in light of the constraints the current system places upon regulators:

The political system gives us the massively ambivalent, pluralistic, pop-perception-and-PAC-driven legislative process. The legislative effluvia, that is, the law, is then administered and interpreted by the Treasury and the IRS, both of which are under increasing budgetary constraints, and which are populated, in the end, by people who are only human. These constraints make the audit less of a statistical threat.

Id. (footnotes omitted); see also Joint Comm. Rep., supra note 6, at 219. The Joint Committee Report recognized the difficulty of exposing corporate tax shelters:
ters today than in the past. The increasingly global marketplace has created a wealth of opportunities to structure tax advantaged transactions that did not exist in a predominantly domestic market. Additionally, there is growing pressure placed upon corporate tax departments, which are increasingly viewed as "profit centers" to lower the corporation's tax liability.

Another factor contributing to the growth of corporate tax shelters includes the complex and ambiguous regulatory framework. Thus, com-

Closely related to the detection risk is the likelihood of success at the IRS and in court. Unlike the individual tax shelters of the 1970s and 1980s, which often depended on inflated valuations, artificial deductions, and other such gimmicks, the modern corporate tax shelter typically has an apparent foundation in the tax law. By taking advantage of "gliches," or the juxtaposition of unrelated Code provisions, these transactions are designed to "work." So even after the corporate tax shelter is discovered and analyzed, the IRS must factor in the possibility that it may not prevail if the matter is litigated. Most arrangements are not litigated, but rather become part of a larger settlement offer in the course of the audit. In these cases, the corporate taxpayer may settle for a percentage of the tax benefits claimed, which likely still exceed its "cost" of entering into the tax shelter.

See id.

23. See TREASURY WHITE PAPER, supra note 16, at 25-31; JOINT COMM. REP., supra note 6, at 216-25 (examining the factors contributing to the proliferation of corporate tax shelters).

24. See TREASURY WHITE PAPER, supra note 16, at 25-26. Congress intended for the Tax Reform Act of 1986 (the 1986 Act) to discourage the use of tax shelters by decreasing marginal tax rates from 46% to 34%. See id. at 25. Consequently, "a $1.00 reduction in corporate taxable income was worth twelve cents less in 1988 than it was in 1986." Id. Further, the tax rate of most corporations increased, despite the fact that marginal rates were actually reduced. See id. at 25-26. Following the passage of the 1986 Act, sheltering income from the corporate tax base become more appealing. See id. at 26; see also JOINT COMM. REP., supra note 6, at 211-17. The incentive to use corporate tax shelters is exacerbated because corporations commonly view income tax as just another manageable cost of doing business, due to the potential tax savings and the low cost of using tax shelters when weighed against the potential tax savings to be derived therefrom. See id. at 217.

25. See TREASURY WHITE PAPER, supra note 16, at 30 (citing the globalization of capital markets as a factor that contributes to the growth of corporate tax shelters); Powlen & Tanden, supra note 4, at 1069 (embracing the view that international financial markets provide greater opportunities for the use of tax shelters).

26. JOINT COMM. REP., supra note 6, at 217-20; TREASURY WHITE PAPER, supra note 16, at 7 & n.20 (recognizing that today tax departments often report to the Chief Financial Officer rather than the Corporate General Counsel); see also Powlen & Tanden, supra note 4, at 1069 n.15 (recognizing that corporate tax departments are seen as profit centers where a high tax rate is considered a manageable liability).

27. Tax shelters regulated under the current system are described as "a patchwork of laws, rules and court doctrine." John D. McKinnon, Tax Shelters Will Soon Get Tougher Rules, WALL ST. J., Feb. 25, 2000, at A3; see also TREASURY WHITE PAPER, supra note 16, at 11 (noting that practitioners exploit ambiguous provisions to create tax shelters);
panies aggressively seek legal loopholes that often reveal inconsistencies in the tax code and become the basis for corporate tax shelters. The bottomline is that corporations realize that the benefits of avoiding tax liability significantly mitigate the potential costs associated with the use of such strategies.

Finally, public opinion surveys suggest that many Americans believe that the current tax system is unfair. Complex tax planning strategies are often viewed as a justifiable self-help remedy in which any taxpayer who seeks to reduce his tax burden is merely beating an unfair system rather than adding to the burden shared by all taxpayers.

This Comment examines the current debate over the regulation of corporate tax shelters. Part I documents the historical evolution of the law applicable to corporate tax shelters. Part II discusses recent proposals for reform offered by Congress and the Clinton administration. Part III analyzes whether current proposals and existing laws provide an adequate regulatory framework for today's corporate environment. Finally, Part IV critiques the current proposals and concludes that today's economy requires a more clearly defined standard in order to avoid nega-

Powlen & Tanden, supra note 4, at 1073 ("The irony is also that the very demise of tax shelters produces new tax shelters, notably because the complexity of rules adopted to kill one generation of tax shelters creates unintended openings for new strategies.").

28. See JOINT COMM. REP., supra note 6, at 213-14 (inferring that the complexity and ambiguity of the tax law creates the opportunity for tax shelters to thrive).

29. See TREASURY WHITE PAPER, supra note 16, at 29 (emphasizing corporations' low risk of being audited); JOINT COMM. REP., supra note 6, at 220 (concluding that the current tax system is characterized by potential benefits from using tax shelters that greatly outweigh their potential risk). "Another factor contributing to the proliferation of corporate tax shelters is that, in many cases, the expected tax benefits from the tax shelter far outweigh the associated costs." Id. at 217. Many companies have realized that under the current regulatory system—even if they are caught engaging in questionable transactions—it can take the IRS several years to actually win a case. Consequently, many companies have taken the approach that the threat of getting caught and ultimately losing a case with the IRS is "an acceptable price of doing business." Fawcett, supra note 5, at 9A. But see Tax Report: A Special Summary and Forecast of Federal and State Tax Development, WALL ST. J., Apr. 7, 1999, at A1 (reporting that Treasury Secretary Lawrence Summers emphasized that regulations should simultaneously "safeguard revenues [and] protect honest taxpayers . . . . Otherwise, 'competitive pressures' stemming from suspicions that others aren't paying their fair share 'may force a race to the bottom.'").

30. See TREASURY WHITE PAPER, supra note 16, at 28 (discussing taxpayer discontent with the "complexity and perceived arbitrariness of the tax law"); see generally Joel Slemrod & Varsha Venkatesh, Public Attitudes About Taxation and the 2000 Presidential Campaign, 83 TAX NOTES 1799 (1999). In an April 1999 Gallup/CNN/USA Today poll, 65% of Americans polled felt their federal tax liability was excessive, 49% believed the amount of federal income tax they paid was unfair, and 66% said that the system was too complex. See id. at 1799 & n.4.

31. See Powlen & Tanden, supra note 4, at 1069.
tively impacting the competitive position of U.S. corporations.

I. THE HISTORICAL FOUNDATION OF THE REGULATION OF CORPORATE TAX SHELTERS

The history of tax law reveals that the use of corporate tax shelters is not a new phenomenon. The use and abuse of tax shelters are often attributed to the complex laws by which they are regulated. Therefore, any understanding of corporate tax shelters must begin with a discussion of the historical background of the laws regulating tax shelters.

A. The Evolution of the Current Statutory Framework for the Regulation of Corporate Tax Shelters

In the 1970s and 1980s, the use of tax shelters in the United States increased. This increased use of tax shelters not only decreased revenue for the Treasury Department, but also diminished taxpayer confidence in the tax system. Congress responded by enacting various forms of legislation designed to curb the exploitation of tax shelters. Beginning in 1969 and continuing to the present, Congress has attempted to make it more difficult to use tax shelters and has imposed stiffer penalties upon those found guilty of doing so.

In 1986, Congress passes a tax reform act that was hailed as the “death knell of the individual tax shelter industry.” Since the Tax Reform Act

32. See id. at 1063 n.1 (“Despite recent attention to the subject, the tax shelter industry is not new.”). Corporations have been using corporate tax shelters since the early part of the twentieth century. See id.

33. See JOINT COMM. REP., supra note 6, at 213-14 (indicating that mistaken interpretations of ambiguous tax laws have contributed to the growth of corporate tax shelters).

34. See Powlen & Tanden, supra note 4, at 1063 n.1.

35. See JOINT COMM. REP., supra note 6, at 213. In addition to a loss of nearly 10% of annual corporate income tax receipts ($10 billion), the “proliferation of corporate tax shelters causes taxpayers to question the fairness of the tax system.” Id.


38. TREASURY WHITE PAPER, supra note 16, at 60 (referring to the Tax Reform Act
of 1986, however, the use of corporate tax shelters has flourished to such a degree that once again the debate over the inherent good or evil of tax shelters is receiving considerable attention. The Tax Code broadly defines tax shelters as any transaction that has a “significant purpose” of avoiding or evading tax liability.

B. The Substance Over Form Doctrine: Gregory and its Progeny

The courts have played a role in the historical development of the law concerning tax shelters. Various judicial doctrines have emerged as useful measures to regulate the most egregious tax shelters. However, as applied by the courts and the IRS, the judicial doctrines often add to the ambiguity in the tax laws.

The “substance over form” doctrine, which originated in Gregory v. Helvering, asserts that the tax results of a specific transaction are best evaluated in light of the transaction’s substantive elements as opposed to evaluating the formal steps by which it was carried out. The Supreme Court has recognized that substance over form means that “[a] given result at the end of a straight path is not made a different result because reached by following a devious path.” Many areas of tax law have been

39. See id. at 25 (recognizing that corporate tax shelters are more prevalent today than ever before).

40. 26 U.S.C § 6111(d) (1994 & Supp. III 1997); see also TREASURY WHITE PAPER, supra note 16, at 75-76. Tax shelters are defined generally as “[a]ny investment or device purchased by a taxpayer to reduce or defer taxes on income from other sources.” WEST’S TAX LAW DICTIONARY 904 (1999). Shepard’s Tax Dictionary defines a tax shelter as “a colloquial term that usually refers to publicly or privately distributed offerings of limited partnership interests ... which offer significant tax benefits that can reduce taxes on income from other sources.” SHEPARD’S 1990-1991 TAX DICTIONARY 601 (1990); see also WG&L TAX DICTIONARY 1998-1999, at 697 (1998). An abusive tax shelter is “[a]ny tax shelter as defined in the Code and any entity, investment plan or arrangement, or other plan or arrangement which is of a type which the Secretary of the Treasury determines by regulations as having a potential for tax avoidance or evasion.” WEST’S TAX LAW DICTIONARY 3 (1999).

41. See JOINT COMM. REP., supra note 6, at 181.

42. See id.

43. See id.

44. 293 U.S. 465 (1935).

45. See JOINT COMM. REP., supra note 6, at 190 (explaining the substance over form doctrine by stating that “two transactions that achieve the same underlying result should not be taxed differently simply because they are achieved through different legal steps”); see also TREASURY WHITE PAPER, supra note 16, at 47 (stating that the substance over form doctrine originated in Gregory).

46. Minnesota Tea Co. v. Helvering, 302 U.S. 609, 613 (1938); see also JOINT COMM. REP., supra note 6, at 190.
characterized as very formalistic, which often makes it “difficult for taxpayers and courts to determine whether the application of this doctrine is appropriate.” The substance over form doctrine allows the IRS to recharacterize a transaction to correspond better with its substantive effects, while taxpayers are tied to the actual legal form of the transaction.

The “economic substance doctrine” descends from the substance over form doctrine. The economic substance doctrine contends that any transaction characterized by an absence of economic substance, independent of tax considerations, will not be recognized for purposes of claiming tax benefits. The economic substance doctrine does not question whether a transaction actually occurred, but balances the transaction’s risk and return potential in order to determine whether the transaction had any purpose beyond reducing or avoiding tax liability.

47. Joint Comm. Rep., supra note 6, at 190 (“The IRS generally has the ability to recharacterize a transaction according to its underlying substance.”). In contrast, the transaction’s initial form usually binds taxpayers and places them at a tactical disadvantage in disputes with the IRS. See id. at 191; see also William S. Blatt, Lost on a One-Way Street: The Taxpayer’s Ability to Disavow Form, 70 Or. L. Rev. 381, 384 (1991). The Supreme Court has asserted that “while a taxpayer is free to organize his affairs as he chooses, nevertheless, once having done so, he must accept the tax consequences of his choice, whether contemplated or not, and may not enjoy the benefit of some other route he might have chosen to follow but did not.” Commissioner v. National Alfalfa Dehydrating & Mill Co., 417 U.S. 134, 149 (1974); see also Humana Inc. v. Commissioner, 881 F.2d 247, 254-55 (6th Cir. 1989); Joint Comm. Rep., supra note 6, at 191.

48. See Joint Comm. Rep., supra note 6, at 190.


50. See Joint Comm. Rep., supra note 6, at 178. The Tax Court has characterized the economic substance doctrine as one that “requires that the intended transactions have economic substance separate and distinct from economic benefit achieved solely by tax reduction.” ACM Partnership v. Commissioner, 73 T.C.M. (CCH) 2189, 2215 (1997), aff’d in part, rev’d in part, 157 F.3d 231 (3d Cir. 1998), cert. denied, 119 S. Ct. 1251 (1999). The court recognized that “[t]he doctrine of economic substance becomes applicable, and a judicial remedy is warranted, where a taxpayer seeks to claim tax benefits, unintended by Congress, by means of transactions that serve no economic purpose other than tax savings.” Id. The Tax Court has stated that “the transaction must be rationally related to a useful nontax purpose that is plausible in light of the taxpayer’s conduct and economic situation.” Id. at 2217.

51. See Goldstein v. Commissioner, 364 F.2d 734, 739-40 (2d Cir. 1966); Joint Comm. Rep., supra note 6, at 184. The Joint Committee Report recognized, however, that even under the clearest articulation of the economic substance doctrine, it would still fail to adequately apply to certain sets of facts. Id. at 184 n.424.

In Gregory v. Helvering, Gregory's wholly owned corporation transferred property to a newly formed corporation, also owned by Gregory. Shortly thereafter, Gregory liquidated the new corporation and redistributed its assets to herself. Gregory subsequently sold stock that had been distributed in the liquidation, but only reported the capital gain realized after distribution. The government challenged this tax treatment, claiming that the transfer of shares between the two corporations did not constitute a tax-exempt reorganization, but a means to distribute taxable dividends. The government contended that Gregory's reorganization attempt must be disregarded because it lacked substance. The Court recognized that taxpayers have a legal right to decrease their tax liability or to avoid it altogether, "by means which the law permits." The Court emphasized that a taxpayer's motivation to escape taxation was irrelevant as long as the substance of the transaction satisfied the relevant statutory language. The Court characterized the real issue as "whether what was done, apart from the tax motive, was the thing which the statute intended." The relevant statute in Gregory referenced an asset transfer in a corporate reorganization plan and not a transfer of assets from one corporation to another without a corresponding relationship to the business of either. The Court criticized the transaction concocted by Gregory because it amounted to nothing more than a sham reorganization.

52. Gregory, 293 U.S. at 467.
53. See id.
54. See id.
55. See id. at 467-68.
56. See id. at 467.
57. Id. at 469. In the lower court opinion, Justice Learned Hand articulated that "[anyone] may so arrange his affairs that his taxes shall be as low as possible; he is not bound to choose that pattern which will best pay the Treasury; there is not even a patriotic duty to increase one's taxes." Gregory v. Helvering, 69 F.2d 809, 810 (2d Cir. 1934). Treasury Secretary Lawrence Summers recently stated that "[w]e have no quarrel with the natural desire of companies . . . to minimize their tax burden by legitimate means." Johnston, supra note 7, at A1. The Secretary continued to say that "we must draw the line at the pursuit of engineered transactions that are devoid of economic substance." Id.
58. See Gregory, 293 U.S. at 468-69. The Court referenced The Revenue Act of 1928, which exempted from taxation gains resulting from a transfer of assets by one corporation to another. See id. at 468.
59. Id. at 469.
60. Id.
than a tax avoidance scheme designed to shelter assets from tax liability.\textsuperscript{61}

2. Gilbert v. Commissioner: Clarifying the Substance Over Form Doctrine

In \textit{Gilbert v. Commissioner},\textsuperscript{62} the Court of Appeals for the Second Circuit provided a thorough analysis of the substance over form doctrine espoused in \textit{Gregory}.\textsuperscript{63} The issue in \textit{Gilbert} involved advances made by a company's stockholder-owner to the company's capital accounts, and the proper characterization of funds advanced by a shareholder to a closely held corporation.\textsuperscript{64} The court ultimately remanded this case for more explicit findings, stating that the tax court failed to explain the rationale for its decision and therefore, it was impossible to determine from the record whether the tax court applied the appropriate standards.\textsuperscript{65}

The \textit{Gilbert} court's discussion of \textit{Gregory} articulated the purpose of the substance over form doctrine.\textsuperscript{66} The court interpreted \textit{Gregory} to mean that a taxpayer's motive to avoid taxation was irrelevant because the result of the transaction constituted the crucial factor.\textsuperscript{67} The appeals court recognized the longstanding principle that legal transactions cannot be upset merely because the parties entered into them for the purpose of minimizing or avoiding taxes.\textsuperscript{68} The court reiterated that the issue was

\textsuperscript{61} See id. at 469-70. The Court stated that the transaction was: [A]n operation having no business or corporate purpose—a mere device which put on the form of a corporate reorganization as a disguise for concealing its real character, and the sole object and accomplishment of which was the consummation of a preconceived plan, not to reorganize a business or any part of a business, but to transfer a parcel of corporate shares to the petitioner. No doubt, a new and valid corporation was created. But that corporation was nothing more than a contrivance to the end last described. It was brought into existence for no other purpose . . . . When that limited function had been exercised, it immediately was put to death.

\textit{Id.} The Court concluded that Gregory's transaction was nothing more than a "devious form of conveyance masquerading as a corporate reorganization." \textit{Id.} at 470. Her tax avoidance motive was irrelevant because, on its face, the transaction lacked the substantive elements required by the language of the statute. \textit{See id.; see also} Basic Inc. v. United States, 549 F.2d 740, 743 (Ct. Cl. 1977) (recognizing that the substance of a transaction, rather than the form or timing, determines tax liability).

\textsuperscript{62} 248 F.2d 399 (2d Cir. 1957).
\textsuperscript{63} \textit{Id.} at 403-04.
\textsuperscript{64} \textit{Id.} at 400-01.
\textsuperscript{65} \textit{See id.} at 407-08.
\textsuperscript{66} \textit{Id.} at 403-06.
\textsuperscript{67} \textit{See id.} at 404.
\textsuperscript{68} \textit{See id.} at 405. In \textit{Gilbert}, the court quoted from one of its earlier decisions: "We cannot agree . . . that a taxpayer is not privileged to liquidate his security for whatever
whether the transaction under scrutiny was really what it appeared to be in form. Judge Learned Hand noted that the Gregory taxpayer adopted the customary form for creating a business, but did not intend to create a business "as the court understood that word." This contrary purpose defeated the exemption in Gregory, not the legally neutral purpose of escaping taxation. Had the taxpayers really meant to conduct business according to their respective transactions, "they would have escaped whatever other aim they might have had, whether to avoid taxes, or to regenerate the world."

C. ACM Partnership v. Commissioner and ASA Investerings Partnership v. Commissioner: Modern Applications of a Historical Standard

1. ACM Partnership v. Commissioner: Scrutinizing the Economic Substance of Business Transactions

Although Gregory was decided over sixty years ago, the business purpose analysis applied by the Gregory court is still useful in contemporary corporate tax shelter cases. In ACM Partnership v. Commissioner, the purposes he thinks most profitable, among them the reduction of his taxes." Id. (quoting Loewi v. Ryan, 229 F.2d 627, 629 (2d Cir. 1956)).

69. See id. at 406 ("In many cases in which the Gregory principle is called into play the question is whether a tax-significant transaction has occurred."). This should not be misconstrued to suggest that Gregory applies only where the issue is whether a transaction is to be disregarded for purposes of assessing tax liability. See id. Rather, Gregory applies when the legitimacy of a transaction is beyond doubt, and the issue is whether economic reality is consistent with the taxpayer's characterization. See id. Whatever the case, the court concluded, the taxpayer must prove that his characterization of the transaction does not conflict with the congressional intent. See id.

70. Chisholm v. Commissioner, 79 F.2d 14, 15 (2d Cir. 1935). Judge Learned Hand explained the Gregory holding:

[T]he question always is whether the transaction under scrutiny is in fact what it appears to be in form; a marriage may be a joke; a contract may be intended only to deceive others; an agreement may have a collateral defeasance. In such cases the transaction as a whole is different from its appearance.

Id. at 15.

71. See id.

72. Id.


IRS denied a partnership tax benefits from a purchase and sale of property. The partnership purchased private placement notes and exchanged them twenty-four days later for consideration equal to the original purchase price. The partnership contended that despite the transaction's minimal economic effect, the transaction had a substantive effect for tax purposes.

The Tax Court held, and the court of appeals affirmed, that because the transaction lacked substantive economic consequences other than the creation of tax benefits, the partnership could not claim the associated tax benefits. The court of appeals expressed concern that the transaction did not change the partnership's financial position, either before or after the acquisition and disposition of the notes. The court questioned whether the Tax Court correctly characterized the purported loss as "a phantom loss" from a transaction which lacked economic substance. The court relied upon the economic substance and substance over form doctrines to analyze the transaction, and recognized that a transaction without economic substance would most likely fail the substance over form analysis. The court, therefore, determined that it must look beyond the transaction's technical form and inquire whether the transac-

75. Id. at 244.
76. See id. at 240.
77. See id. at 245.
78. See ACM Partnership v. Commissioner, 73 T.C.M. (CCH) 2139, 2215 (1997), aff'd in part, rev'd in part by 157 F.3d 231 (3rd Cir. 1998), cert. denied, 119 S. Ct. 1251 (1999); see also Surdell, supra note 73, at 1187-94 (analyzing the decision in ACM Partnership). The Tax Court in ACM Partnership stated:

[W]e do not suggest that a taxpayer refrain from using the tax laws to the taxpayer's advantage. In this case, however, the taxpayer desired to take advantage of a loss that was not economically inherent in the object of the sale, but which the taxpayer created artificially through the manipulation and abuse of the tax laws. A taxpayer is not entitled to recognize a phantom loss from a transaction that lacks economic substance.
ACM Partnership, 73 T.C.M. (CCH) at 2215. The court identified the crucial finding to be whether the purported transaction was "rationally related to a useful nontax purpose that is plausible in light of the taxpayer's conduct and useful in light of the taxpayer's economic situation and intentions." Id. at 2217.
79. See ACM Partnership, 157 F.3d at 245.
80. Id. The appeals court explained that when "[v]iewed according to their objective economic effects rather than their form, [the taxpayer's] transactions involved . . . [an] economically inconsequential investment in and offsetting divestment from the [debt instrument] . . . [T]he transactions . . . left the ACM in the same position it had occupied before engaging in the offsetting acquisition and disposition of those notes." Id. at 250.
81. See id. at 246.
tion contained the economic substance that its form represented.82

2. ASA Investerings Partnership v. Commissioner: Looking Beyond the Formalities

More recently, in ASA Investerings Partnership v. Commissioner,83 a partnership exploited loopholes in the tax code to attribute a gain to a foreign partner and to offset loss to another partner in the United States.84 The court found that the partnership did not have sufficient economic substance to be recognized for federal tax purposes.85 The Tax Court determined that, when stripped of the formal steps, the transaction failed to comport with the economic reality of the arrangement.86 The court held that the substance of the transactions showed that the foreign partner was a separate lender who reallocated the partnership’s gains to the U.S. partner.87

Thus far, extensive case law addressing corporate tax shelters has failed to produce a consistent standard by which transactions may be judged, which compounds the problems of ambiguity and complexity.88

II. CURRENT PROPOSALS FOR REFORMING THE LAW OF CORPORATE TAX SHELTERS

A. The Joint Committee on Taxation Report

In a July 1999 study of the current provisions governing corporate tax shelters, the Joint Committee on Taxation (Joint Committee) recommended the establishment of a comprehensive framework to deter the use of corporate tax shelters.89 The Joint Committee’s report clarified

82. See id. at 247. The proper inquiry into whether a transaction has sufficient economic substance depends upon an analysis of the “objective economic substance of the transactions” and the “subjective business motivation.” Id. Accordingly, transactions that do very little to change a taxpayer’s financial position beyond reducing his taxes will usually be disallowed. See id. at 248.
83. 76 T.C.M. (CCH) 325 (1998).
84. Id. at 326.
85. See id. at 335.
86. See id.
87. See id. at 336.
88. See supra notes 10-17 and accompanying discussion.
89. See JOINT COMM. REP., supra note 6, at 1, 6. Pursuant to the IRS Reform Act of 1998, the Joint Committee on Taxation and the Department of the Treasury are required to conduct separate studies of the penalty and interest provisions of the Internal Revenue Code, and make any recommendations that would simplify the tax law and ease the compliance burden imposed upon taxpayers. See id.
the definition of corporate tax shelters through several "tax shelter indicators." This proposal classifies a transaction as a tax shelter if it exhibited one or more of the following characteristics: (1) "the reasonably expected pre-tax profit from the arrangement is insignificant relative to the reasonably expected net tax benefits," (2) "the arrangement involves a tax indifferent participant," (3) "the reasonably expected net tax benefits from the arrangement are significant," (4) "the arrangement is reasonably expected to create a 'permanent difference' for U.S. financial reporting purposes under generally accepted accounting principles," and (5) "the arrangement is designed so that the corporate participant incurs little (if any) additional economic risk as a result of entering into the arrangement."

In addition, the Joint Committee Report recommended classifying a transaction as a tax shelter—even though it did not exhibit any of the suggested tax shelter indicators—if a significant purpose of the transaction included "the avoidance or evasion of Federal income tax." The Joint Committee also endorsed stricter penalty provisions for tax shelters in the Tax Code to eliminate the requirement that an alleged understatement be substantial. The Joint Committee favored increasing the current understatement penalty rate from twenty percent to forty percent (forty-percent penalty) for any understatement "attributable to a corporate tax shelter." The Joint Committee advised that the proposed forty percent penalty be abated if the taxpayer had satisfied certain requirements. The most significant suggestion required that corporate participants determine, with at least seventy-five percent likelihood, that the transaction would be sustained if challenged by the IRS. The Joint

90. Id. at 6-7.
91. Id. at 7.
92. Id.; see also supra note 20 and accompanying text (defining a tax-indifferent participant).
93. JOINT COMM. REP., supra note 6, at 7.
94. Id.
95. Id.
96. Id.
97. See id. at 8.
98. Id. A further modification would provide that "the IRS would not have the discretion to waive the understatement penalty in settlement negotiations or otherwise for corporate tax shelters." Id.
99. See id.
100. See id. Another complete abatement requirement is a certified disclosure that verifies the accuracy of the return and is signed by the corporation's chief financial officer or another officer with sufficient knowledge of the facts to make a good faith disclosure.
Committee also recommended that the proposed forty-percent penalty be reduced to twenty percent if the corporation made certain disclosures regarding the nature and substance of the transaction. The Joint Committee would require corporations that must pay an understate-ment penalty from a corporate tax shelter of at least one million dollars to disclose the penalty to its shareholders.

B. The Proposed Abusive Tax Shelter Shutdown Act

A bill was recently introduced in the House of Representatives that would prevent tax shelter abuses by disallowing tax benefits that arise from transactions lacking substantial economic substance. The Act aims to eliminate the most abusive corporate tax shelters by denying recognition of tax benefits purported to arise from transactions that lack economic substance, and by repealing current provisions that permit legal opinions to be used "to avoid penalties on tax underpayments resulting from transactions without significant economic substance or business purpose." The bill identifies several factors that may preclude a taxpayer from claiming certain income tax deductions, losses, or credits. Similar to the Joint Committee Report, the bill would increase the

See id.

101. See id. (conditioning this reduction upon a determination that the disclosure is "attributable to a position with respect to the tax shelter for which the corporate partici-pant has substantial authority in support of such position").

102. See id. (explaining that the disclosure would reveal the amount of the penalty and detail the circumstances surrounding the penalty).


104. Id. § 2(b). This Act asserts that the legal opinions legitimizing most corporate tax shelters take an excessively narrow view of established judicial doctrines. Id. § 2(a)(1). Another purpose of the Act "send[s] a clear and unequivocal message not only to the shel-ter hustlers and tax dodgers, but also to the courts and the Administration that Congress wants this mess cleaned up." Hearing on Corporate Tax Shelters, supra note 5 (statement of Rep. Lloyd Doggett, D-Tex) <http://www.house.gov/ways_means/fullcomm/106cong/11-10-99/110dogg.htm>.

105. See H.R. 2255 § 3. The deductions, losses, and credits referred to in the Act are classified as non-economic tax attributes, defined as:

[A]ny deduction, loss, or credit claimed to result from any transaction unless [(1)] the transaction changes in a meaningful way (apart from Federal income tax con-sequences) the taxpayer's economic position, and [(2)] 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 in the case of a transaction [involving] 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 ex cess of the economic return for such period realized by the person lending the
penalties imposed for abuses and waive increased penalties if certain disclosure requirements are met.\textsuperscript{106}

C. The Clinton Administration’s Proposal

In its Fiscal Year 2000 Budget, the Clinton administration (the Administration) recommended several proposals to slow the growth of corporate tax shelters.\textsuperscript{107} The Administration would require disclosure of corporate tax shelters when a transaction exhibited any combination of the following tax shelter indicators: (1) a difference between book and tax revenues exceeding a specified amount;\textsuperscript{108} (2) the involvement of a tax-indifferent party; and (3) a disparity between the technical form of a transaction and the way it was reported.\textsuperscript{109} The Administration contends that the benefits of an increased disclosure requirement are two-fold.\textsuperscript{110} Heightened disclosure would promote self-compliance,\textsuperscript{111} and a more fact-based investigative process for suspected abuses.\textsuperscript{112}

\textsuperscript{106} See id. § 4. These provisions of the Abusive Tax Shelter Shutdown Act of 1999 mirror those proposed by the JOINT COMM. REP., supra note 6, and the TREASURY WHITE PAPER, supra note 16.

\textsuperscript{107} See TREASURY WHITE PAPER, supra note 16, at 6 (providing an overview of the Administration’s proposal); see also Ruchelman & Adrion, supra note 20, at 283 (articulating the Administration’s concern regarding the emergence of complex tax avoidance transactions).

\textsuperscript{108} See TREASURY WHITE PAPER, supra note 16, at 14, 85. A book-tax disparity refers to the difference in accounting treatment (e.g., book value) of a tax shelter as compared to its federal income tax treatment. See id. “The emergence of book-tax disparities as a hallmark of recent shelters is consistent with the trend to treat corporate in-house tax departments as profit centers . . . and the pressure to increase shareholder value and remain competitive.” Id. (footnote omitted); see also Hearing on Corporate Tax Shelters, supra note 5 (statement of Jonathan Talisman, Acting Assistant Secretary for Tax Policy, United States Dept’ of the Treasury) <http://www.house.gov/ways_means/fullcomm/106cong/11-10-99/1110tali.htm>. The alleged harm done by corporate tax shelters may not be revealed by the amount of corporate tax receipts, but by the difference between “actual tax payments and those that would be remitted absent corporate tax shelters.” Id. A recent article illustrates that corporations are increasingly reporting different amounts to their shareholders and the IRS. See Glenn Kessler, Treasury Aims to Shut Tax Shelters, WASH. POST, Feb. 29, 2000, at A1. In 1992, taxable income and profits reported by corporations were roughly the same, whereas in 1996, $119 billion less in profits was disclosed to the IRS than to shareholders. See id.

\textsuperscript{109} See TREASURY WHITE PAPER, supra note 16, at 85.

\textsuperscript{110} See id. at 80.

\textsuperscript{111} See id. The Administration’s proposal requires that a corporate officer with knowledge of the transaction, and who could be held personally liable for any reporting inaccuracies, sign the form. See id. at 85-86.

\textsuperscript{112} See id. at 80. This proposed requirement mandates that the taxpayer describe the
If the taxpayer failed to disclose the transaction, the corresponding underpayment would be subject to a forty-percent penalty. If the corporate taxpayer complies with the mandatory disclosure requirements, the resulting underpayment would only be subject to a twenty-percent penalty. If the corporate taxpayer demonstrates that it acted in good faith, and believed the transaction to be legitimate, the penalty could be avoided entirely.

The Administration addressed the issue of disallowing benefits of corporate tax shelters, acknowledging that substantive change is necessary, and suggests that such change should embrace a system of recognizable, clearly articulated standards, rather than narrow rules. Foremost among the Administration's proposals for achieving such a system is the codification of the economic substance doctrine embodied in ACM Partnership and Gregory.

In addition, concerns that the IRS may abuse a grant of broader authority are addressed by a more concise definition of an abusive tax shelter. The Administration's proposed definition classified a tax avoidance transaction as "any transaction in which the reasonably expected pre-tax profit ... of the transaction is insignificant relative to the reasonably expected net tax benefits ... of such transaction." The Administration also brings transactions involving "the improper elimin-
tion or significant reduction of tax on economic income," within the definition of a tax avoidance transaction.\textsuperscript{120} These proposals, while not considered entirely negative, have become a source of frustration to many in the business community who view them as inadequate remedies for a system that is already in disarray.\textsuperscript{121}

III. THE CURRENT SYSTEM: IN SEARCH OF A CLEAR STANDARD

As currently applied, the law governing corporate tax shelters is a patchwork of ambiguous statutory authority, which is sometimes arbitrarily applied to the detriment of legitimate business transactions.\textsuperscript{122} However, supporters of the current system contend that corporations too often manipulate the law at the expense of individual taxpayers who must ultimately make up the difference in lost treasury revenue.\textsuperscript{123} Preventing abusive corporate tax avoidance strategies while protecting legitimate business transactions has received much attention, but the success of these efforts is debatable.\textsuperscript{124}

The rules promulgated to counter corporate tax shelters are inadequate because they fail to provide a clear standard to consistently or pre-

\textsuperscript{120} Id.

\textsuperscript{121} See discussion infra part III.A. Some corporate tax executives assert that the new proposals will only "muddle" tax law, and have demanded that the Administration define the specific problem presented by corporate tax shelters rather than merely providing "anecdotal stories." Fawcett, supra note 5, at 9A.

\textsuperscript{122} See Paul J. Donahue, The Rule of Sheldon v. Commissioner: Is it an Economically Efficient Evolution of the Sham Transaction Doctrine?, 13 VA. TAX REV. 165, 167-68 (1993). Observers have interpreted Gregory as requiring "a legitimate business purpose," which does not include tax avoidance, to justify favorable tax treatment of any commercial transaction." Id. at 167. Judge Learned Hand opined that "in construing words of a tax statute which describe commercial or industrial transactions we are to understand them to refer to transactions entered upon for commercial or industrial purposes and not to include transactions entered upon for no other motive but to escape taxation." Id. at 167-68 (quoting Commissioner v. Transportation Trading and Terminal Corp., 176 F.2d 570, 572 (2d Cir. 1949)); see also Donahue, supra at 572; Hearing on Corporate Tax Shelters, supra note 5 (statement of David A. Lifson, Chair, Tax Executives Committee, American Institute of Certified Public Accountants) <http://www.house.gov/ways-means/fullcomm/106cong/11-10-99/1110lifes.htm> (emphasizing that ambiguous standards may have a "chilling effect" on legitimate business transactions).

\textsuperscript{123} See, e.g., Anderson, supra note 5, at 1C.

\textsuperscript{124} See, e.g., Calvin H. Johnson, Corporate Tax Shelters, 1997 and 1998, 80 TAX NOTES 1603, 1604 (1998) (suggesting that the current definition of tax shelter includes virtually every manner of corporate tax planning); see also, e.g., McKinnon, supra note 27, at A3 (suggesting that current laws have been ineffective because those charged with executing the law have not determined how to define tax shelters).
dictably judge alleged abuses. The doctrines espoused in Gregory and Gilbert have guided decision-makers for over seventy years, yet substantial disagreement remains concerning the distinction between abusive tax avoidance schemes and legitimate tax planning.

A. The Corporate Perspective: Pessimism Abounds

The revised proposals outlined in the Treasury White Paper are in response to criticisms from various groups and individuals. A former IRS official summarized these criticisms: "[T]here clearly are problems out there that the government ought to deal with. The question is, how do you get at the problem without interfering with legitimate business transactions." One prominent association testified before the House Committee on Ways and Means, and recognized that the Administration faces a daunting task in shutting down the most abusive tax shelters, but also expressed concern that portions of the Administration's proposal contravened legitimate corporate tax planning strategies. Other parties have commented that the current proposals fail to provide an articulate standard that clearly defines an abusive transaction, and contain broad language that could hinder legitimate tax planning activity.

125. See Donahue, supra note 122, at 182 (noting that ambiguity in the tax code creates unintended results and costs countless hours to uncover transactions beyond the contemplation of the code's drafters). The U.S. Treasury Department favors a consistent doctrine, which defines and regulates corporate tax shelters and replaces the current case-by-case approach—both are time consuming and costly. See Johnston, supra note 7, at A1.

126. See Joint Comm. Rep., supra note 6, at 181 (recognizing the precedential value of Gregory); see also Blatt, supra note 47, at 391 (suggesting that economic reality has guided federal taxation since 1921, and has been described as the cornerstone of sound taxation). "Despite this consensus, or perhaps because of it, there is no single generally accepted definition of economic reality." Id.; see also Boris L. Bitkover & Lawrence Lokken, 1 Federal Taxation of Income, Estates, and Gifts ¶ 4.3.3, at 4-35 (3d. ed. 1999) ("[I]t is almost impossible to distill useful generalizations from the welter of substance-over-form cases.").


128. Peter Stone, Gimme Shelter, Nat'l J., Apr. 10, 1999, at 94; Powien & Tanden, supra note 4, at 1103-04 (noting that the ambiguous definitions have generated outrage that the Administration's proposals "cast too wide a net" and "therefore will catch legitimate transactions"). The Joint Committee on Taxation lamented that the breadth and vagueness of the Administration's proposals could cause considerable uncertainty for parties contemplating business decisions. See id. at 1103.

129. See Sawyers, supra note 13, at 346-47.

130. See id. at 346-48. One party asked: "What standards justify the imposition of extraordinary punishment on a corporation . . . whose tax treatment of a transaction is successfully challenged by the IRS?" Id. at 347. Several panelists at an American Bar Association tax conference also expressed concern that defining tax shelters too broadly could
The corporations that will be most affected by substantive changes in the law have been encouraged by some elements of the current proposals, but remain troubled by other aspects that may be unclear and punitive. Some critics of these proposals have argued that they are unnecessary because the IRS already has the tools necessary to prevent abusive tax shelters. These critics contend that before Congress expands the IRS's authority, the IRS should demonstrate that the current enforcement provisions are ineffective.

B. Applying an Ambiguous Standard to a Complex Economy: Invitation to Conflict

In one recent case, it took the IRS fifteen years, several expert wit-
necessarily, and at least eleven attorneys to uncover and ultimately eliminate
an abusive corporate tax shelter. In *ACM Partnership*, the government
spent more than two million dollars litigating the case, and though victo-
rious, continues to face other cases involving nearly identical tax shel-
ters.

Meanwhile, the corporations who feel that they are being targeted jus-
tify their tax planning methods and strategies. General Motors (GM),
for example, emphasized that it pays considerable taxes to foreign coun-
tries, which are legitimately credited against U.S. taxes. In a complex
global economy, it is “very difficult to compare a global company like
GM to an individual company or individual person who has all of his or
her operations or income in the U.S.” because the factors that determine
the tax liabilities of each are far from analogous.

Likewise, Enron Corporation (Enron) generated $197 million in pre-
tax income in 1998, but only recognized payment of about fifteen percent
to the federal government. An Enron executive explained that “[a] com-
pany like ours that is making significant investments and is growing
substantially is going to see lower effective tax rates . . . [b]ut those in-
vestments and the growth they produce certainly add to the tax base and
create additional tax revenues in the long run.”

The illustrations drawn by GM and Enron typify the problems that to-
day’s business environment presents to the current tax law. Large cor-
porations, such as GM and Enron, engage in transactions with the inten-

135. See UPS v. Commissioner, 78 T.C.M. (CCH) 262 (1999); see also Andrea Foster,
*UPS Loses its Tax Fight as Congress Mulls Shelter Reform*, NAT'L L.J., Aug. 23, 1999, at
B5.
136. See Tom Herman, *Tax Report: A Special Summary and Forecast of Federal and
State Tax Developments*, WALL ST. J., Sept. 8, 1999, at A1; Randall Smith, *Collection
137. See Phillips, supra note 1, at A1 (citing General Motors and Enron Corporation
as examples); Powlen & Tanden, supra note 4, at 1134-35 (recognizing the disadvantage
that corporate taxpayers face when litigating with the IRS). When the IRS seeks to disal-
low an alleged abusive transaction, “it will likely scrutinize the transaction, litigate with
the taxpayer, come out with a retroactive notice denying tax benefits from participation,
even if it does not have authority for the notice, and then seek legislation providing it with
retroactive authority for the notice and regulations.” *Id.* at 1135. If the stakes are high
enough, the IRS may employ considerable resources to develop a record to show the ille-
gitimacy of a transaction. *See id.*
139. *Id.*
140. *See id.*
141. *Id.*
142. *See id.*
tition of improving their overall economic position.\(^\text{143}\) Therefore, if seeking to enhance one's economic position is a legitimate business purpose, any tax minimizing motives will be irrelevant.\(^\text{144}\) To make such a determination requires that the courts place themselves in the position of corporate management.\(^\text{145}\) Consequently, unless the courts are guided by a clearly articulated standard, they would possess a large degree of discretion in determining which transactions are legitimate and which are abusive.\(^\text{146}\)

Unlike the era of Gregory, corporations today are participants in a vast global marketplace.\(^\text{147}\) As a result, misguided decisions could come at the

\(^{143}\) See Fawcett, supra note 5, at A9. Representative Dick Armey has said that "'[T]he business of a corporation is to maximize its earnings for its shareholders . . . . Since tax is a very large part of their costs, anything they can do to minimize . . . . their costs would be a legitimate thing.'" Id.; see also Hearing on Corporate Tax Shelters, supra note 5 (statement of Danny R. Carpenter, Vice President-Finance, Kansas City Southern Industries, Inc.) <http://www.house.gov/ways_means/fullcomm/106cong/11-10-99/1110carp.htm> (indicating that transactions undertaken for business purposes strive to reduce cost, including minimizing tax liability to the furthest extent of the law).

\(^{144}\) See, e.g., Basic, Inc. v. United States, 549 F.2d 740, 745 (Ct. Cl. 1977) (recognizing that tax minimizing considerations would be irrelevant when a transaction had a business purpose); see also Surdell, supra note 73, at 1169 (articulating that the tax laws affect the form of most business transactions).

"'[T]he availability of tax benefits, or tax shelter, is often the reason the particular activity . . . is selected in preference to an activity that does not carry with it significant tax benefits. The presence, therefore, of significant tax benefits (that may even represent the investor's primary objective for entering into the transaction) should not result in the loss of the associated tax benefits if the investor, in fact, has an actual and honest profit objective apart from the tax benefits (and assuming the transaction is not a sham)."

Id. (quoting Peat Oil & Gas Assoc. v. Commissioner, 100 T.C. 271, 276 (1993)).

\(^{145}\) See Donahue, supra note 122, at 177.

\(^{146}\) See Surdell, supra note 73, at 1206 (noting that courts have not easily decided cases when the taxpayer achieves real non-tax economic benefits, but those benefits are less valuable than the tax benefits obtained). In these cases, the courts have focused on whether the transaction's economic benefits sufficiently support its tax benefits. See id. There is no judicial consensus regarding how much economic substance is required to support a larger tax benefit. See id. Such an analysis is troubling because there appears to be no clear guideline, and in the absence of a definite standard, judges could "draw the circle more broadly around those transactions which the court likes and more narrowly around those which it does not like." Id.

\(^{147}\) See Fiona Macmillan, Making Corporate Power Global, 5 INT'L TRADE L. & REG. 3, 4 (1999). Macmillan discusses the importance of recognizing that global markets change the face of corporate strategy, and that problems can be anticipated accordingly between the corporate and government sectors as each side adapts to the new environment. See id. at 5; see generally Hearing on Providing Tax Relief to Strengthen the Family and Sustain a Strong Economy Before the House Comm. on Ways and Means, 106th Cong. (1999) (Statement of Mark Bloomfield, President, American Council for Capital Forma-
expense of not only the companies involved, but individual consumers who rely on those companies.  

IV. BALANCING AN ENFORCEABLE BODY OF LAW WITH A PERCEPTION OF FAIRNESS AMONG TAXPAYERS

A. The Real World Impact of Ambiguous Tax Laws

How to avoid penalizing companies who engage in legitimate business transactions is a primary concern in considering new proposals. Failing to do so could place a burden of illegality upon all tax reduction strategies engaged in by corporations, regardless of their motives for undertaking a particular transaction.

The purpose of the Tax Code, and the penalties therein, promotes voluntary compliance with its requirements and discourages avoidance of income tax. The concern of overly broad regulations requires attention in new proposals, because broadly defined law may curtail abusive cor-

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148. See generally Dan Morgan, Congress May Target Questionable Tax Shelters, AUSTIN AM.-STATESMAN, Jan. 23, 2000, at A10. If businesses are deterred from minimizing their tax liability, consumers will make up the difference through higher prices. See id; see also Diana Ray, Waste No More, WASH. TIMES, Feb. 21, 2000, at A1.

149. See Foster, supra note 117, at B1. Representative Dick Armey expressed the opinion that in the Administration's proposal "'[t]here is sort of an implicit indictment of the corporation for doing something . . . unethical or perhaps even illegal or maybe immoral, but the fact of the matter is that we write the Tax Code, and any corporation ought to do what they can to minimize that cost.'" David Jay Johnston, Corporate Shelters Now Top Tax Dodge, SAN DIEGO UNION-TRIB., Feb. 20, 2000, at A1; see also Hearing on Corporate Tax Shelters, supra note 5 (statement of Charles W. Shewbridge, III, Chief Tax Executive, BellSouth Corp., and President, Tax Executives Institute) <http://www.house.gov/ways_means/fullcomm/106cong/11-10-99/1110shew.htm> (suggesting that a taxpayer should not be required to proceed through litigation to validate legitimate tax planning).

150. See Donahue, supra note 122, at 182.

The time of payment, the manner of payment, the quantity to be paid, ought all to be clear and plain to the contributor, and to every other person. Where it is otherwise, every person subject to the tax is put more or less in the power of the tax gatherer, who can either aggravate the tax upon any obnoxious contributor, or extort, by the terror of such aggravation, some present or perquisite to himself. The uncertainty of taxation encourages the insolence and favors the corruption of an order of men who are naturally unpopular.
porate tax shelters at the expense of legitimate business transactions.\textsuperscript{151} In addition, only through fairness will the Tax Code be able to encourage self-compliance with the law, rather than open contempt for the system.\textsuperscript{152}

Failing to recognize and give serious consideration to the concerns expressed by the business community could effectively place U.S. corporations at a competitive disadvantage in the global marketplace.\textsuperscript{153} The unintended result of failing to consider those most affected by new regulations may ultimately cause businesses to seek new homes in foreign countries or off-shore havens, where the playing field may favor competitive interests and the rules of the game are more clearly defined.\textsuperscript{154} Consequently, the United States would lose considerably more in wages, and the corresponding reintroduction of the wages back into the economy, than the revenues the Treasury would fail to collect as a

\textsuperscript{151} See Hearing on Corporate Tax Shelters, supra note 5 (statement of David A. Lifson, Chair, Tax Executives Committee, American Institute of Certified Public Accountants) <http://www.house.gov/ways_means/106cong/11-10-99/1110lifs.htm> (supporting the right of taxpayers to plan transactions under a clear standard and without “fear of draconian sanctions”); see also id. (statement of Charles W. Shewbridge, III, Chief Tax Executive, BellSouth Corp., and President, Tax Executives Institute) <http://www.house.gov/ways_means/106cong/11-10-99/1110shew.htm> (recognizing that overbroad standards ultimately harm the entire corporate community); Sawyers, supra note 13, at 348 (emphasizing that penalties should be defined in a coherent manner rather than as broad mandates designed to raise revenue).

\textsuperscript{152} See generally Hearing on Corporate Tax Shelters, supra note 5 (statement of Charles W. Shewbridge, III, Chief Tax Executive, BellSouth Corp., and President, Tax Executives Institute) <http://www.house.gov/ways_means/106cong/11-10-99/1110shew.htm> (recognizing that public confidence in the tax system is impaired by rules that are perceived to be unfair and overreaching and stating that: “While we agree that if the tax system does not respond to noncompliance or to sham transactions, public confidence in the fairness of the system will be diminished, we also believe that public confidence can be equally impaired by the enactment of overreaching or overbroad legislation.”).

\textsuperscript{153} See Hearing on Providing Tax Relief, supra note 147 (Statement of Mark Bloomfield, President, American Council for Capital Formation) <http://www.house.gov/ways_means/106cong/2-23-99/6-23bloom.htm> (discussing several features of the tax system that disadvantage U.S. companies).

\textsuperscript{154} See Phillips, supra note 1, at A1. House Ways and Means Committee Chairman, Bill Archer (R-Tx), opined that “reducing the tax burden on U.S.-based multinationals would make them less likely to merge with foreign companies and move their headquarters overseas, where they would pay even less to the IRS.” Id.; see also Macmillan, supra note 147, at 3, 7 (highlighting the importance, in a global economy, of making efforts to attract business investments by offering incentives equal to or greater than other countries). Macmillan suggests that in today’s environment, “[c]apital will go where it is wanted and stay where it is well treated. It will flee from manipulation or onerous regulation of its value or use, and no government power can restrain it for long.” Id. at 3.
result of an effective corporate tax shelter. 155

B. Reaching a Compromise Among Competing Interests

To provide a fair and enforceable system of tax laws, it is imperative that clear standards that distinguish abusive transactions from legitimate tax planning are established. 156 There is no simple answer to the complex question of how to define and, when necessary, penalize abusive corporate tax shelters. 157 The present system, assumes that a tax shelter, once discovered, will be stopped. 158 Therefore, extensive efforts are undertaken to conceal transactions that may come under scrutiny and to confuse auditors charged with untangling the web in which tax shelters are hidden. 159

In many instances, corporate tax planning involves the manipulation of ambiguities and discontinuities of the current laws to structure transactions that are so complex that the manpower and financial resources required to expose them would make enforcement both exceedingly difficult and expensive for the government. 160 Corporations have the ability to make enforcement difficult, in part, because authorities review tax

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156. See Donahue, supra note 122, at 181 (noting that certainty has been consistently recognized as a characteristic of sound tax policy); Hearing on Corporate Tax Shelters, supra note 5 (statement of Charles W. Shewbridge, III, Chief Tax Executive, BellSouth Corp., and President, Tax Executives Institute) <http://www.house.gov/ways_means/fullcomm/106cong/11-10-99/1110shew.htm>. Many members of the business community believe that under the current regulations, tax shelters are encouraged, and frequently result from the "one-sided rules that were crafted for a 'pro-government' purpose but subsequently turned on their head," by skilled tax planners. Id. It has been suggested that a consistently applied, simplified body of law may alleviate many of the evils of the current system. See id.
158. See Stone, supra note 128, at 945.
159. See id.
160. See JOINT COMM. REP., supra note 6, at 212-13; Hearing on Corporate Tax Shelters, supra note 5 (statement of Jonathan Talisman, Acting Assistant Secretary for Tax Policy, United States Dep't of the Treasury) <http://www.house.gov/ways_means/fullcomm/106cong/11-10-99/1110tali.htm> (identifying the current approach to tax shelter regulation as a factor that increases the complexity of the tax law). When tax shelters are addressed on a case-by-case basis, the multiple layers of provisions are sometimes incorrectly interpreted as meaning that there is a law for every situation. See id. A direct negative consequence may lead to the conclusion by "negative inference" that what is not specifically prohibited is allowed. Id.
shelters on a case-by-case basis.\textsuperscript{161} Case-by-case enforcement results in significant problems. First, unclear standards may actually promote the use of tax shelters that, under current guidelines, would arguably include transactions on both sides of what is considered legitimate.\textsuperscript{162} For example, the language of a recent measure considered by the House of Representatives indicates that any transaction lacking a legitimate business purpose would be disallowed.\textsuperscript{163} From \textit{Gregory} to the present the right of a taxpayer to decrease his taxes has been recognized.\textsuperscript{164} A rational purpose of all business decisions includes decreasing the financial liability incurred.\textsuperscript{165} To apply a phrase as broad as "any transaction lacking a legitimate business purpose" would require the courts to delve into an inquiry of the underlying rationales for specialized business decisions that would likely add to, rather than eliminate, inconsistencies in the application of the law.\textsuperscript{166}

Second, addressing alleged tax shelters on a case-by-case basis not only leaves gaps in the Tax Code, it also complicates matters because new

\begin{itemize}
  \item \textsuperscript{161} See \textit{TREASURY WHITE PAPER}, supra note 16, at 4-5. The current method by which tax shelters are addressed on a case-by-case basis may actually promote the growth of tax shelters because it allows for the creation of new shelters upon discovery of existing shelters. See \textit{Lardner}, supra note 22, at 49.
  \item \textsuperscript{162} See \textit{Hearing on Corporate Tax Shelters}, supra note 5 (statement of Lindy Paull, Chief of Staff, Joint Committee on Taxation) <http://www.house.gov/ways_means/fullcomm/106cong/11-10-99/1110paul.htm> (recognizing that the current law results in a cost-benefit analysis, which is skewed in favor of tax shelters due to the potential tax savings and relatively slight corresponding risk of being penalized); see also \textit{TREASURY WHITE PAPER}, supra note 16, at 5.
  \item \textsuperscript{163} See \textit{Abusive Tax Shelter Shutdown Act of 1999}, H.R. 2255, 106th Cong. § 3 (1999); see also supra note 103 and accompanying text.
  \item \textsuperscript{164} \textit{Gregory v. Helvering}, 293 U.S. 465, 469 (1935).
  \item \textsuperscript{165} See \textit{Hearing on Corporate Tax Shelters}, supra note 5 (statement of Danny R. Carpenter, Vice President-Finance, Kansas City Southern Industries, Inc.) <http://www.house.gov/ways_means/fullcomm/106cong/11-10-99/1110carp.htm> (noting that in conducting its business, his company strives to pay no more taxes than required by law).
  \item \textsuperscript{166} \textit{Donahue}, supra note 122, at 177. Where the courts are required to substitute their business judgment for that of the taxpayer, it is contended that the courts lack the expertise to assess accurately the decisions made by corporate management. An attempt at such an evaluation may lead to unpredictable and inequitable results. See \textit{id.}; see also \textit{Hearing on Corporate Tax Shelters}, supra note 5 (statement of Jonathan Talisman, Acting Assistant Secretary for Tax Policy, United States Dep’t of the Treasury) <http://www.house.gov/ways_means/fullcomm/106cong/11-10-99/1110tali.htm> (stating that reliance on judicial decisions may not be the most efficient means to regulate corporate tax shelters). Litigation frequently fails to "provide a coherent set of rules to be applied in subsequent transactions." \textit{Id.} One tax court judge recently acknowledged that judges do not make tax policy and, therefore, courts are probably equipped to provide little guidance on the level of economic substance or business purpose sufficient to find a valid transaction. See \textit{id.}
provisions are often created in response to particular transactions which add to an already voluminous body of law. A well-defined standard would deter companies from employing abusive tax shelters because the parameters identifying right and wrong would be more clearly defined. Rather than expending limited resources to keep up with new and complex schemes designed to outwit the current system, a definite standard would provide a more consistent basis by which to judge suspect transactions and offer a more efficient means to analyze these transactions.

Many critics of the Administration and Joint Committee proposals assert that they move beyond the scope necessary to reach transactions that are vaguely articulated as "the improper elimination or significant reduction of tax on economic income...." This description, regardless of its meaning, may conceivably encompass transactions that would not be considered abusive and, perhaps more troubling, may reach other trans-

168. See Hearing on Corporate Tax Shelters, supra note 5, at 3 (statement of Charles W. Shewbridge, III, Chief Tax Executive, BellSouth Corp., and President, Tax Executives Institute) <http://www.house.gov/ways_means/fullcomm/106cong/11-10-99/1110shew.htm> (asserting that complex tax laws breed opportunity). Some corporate executives have expressed frustration that Congress, the Treasury Department, and the IRS have not acknowledged the role each plays in contributing to the environment in which tax shelters thrive. See id.
169. See Donahue, supra note 122, at 182. Donahue discussed the problems created by vague standards:

The imprecisions of language and the limits of imagination mean that tax statutes will always have interpretations that their drafters did not intend. A brigade, if not an army, of some of America's most intelligent men and women work long hours attempting to ferret out transactions whose economic outcome the drafters of tax statutes did not intend to favor but which the language of the statute does in fact favor. Discovering and implementing such transactions redistributes wealth to the discoverers and their clients at the very high cost of their labor and at the additional cost of executing transactions which would not otherwise have taken place. It also increases the cost of legislation, because Congress must work after the fact to close loopholes that ingenious tax attorneys have created.

Id.; see Hearing on Corporate Tax Shelters, supra note 5 (statement of Jonathan Talisman, Acting Assistant Secretary for Tax Policy, United States Dept' of the Treasury) <http://www.house.gov/ways_means/fullcomm/106cong/11-10-99/1110tali.htm> (noting the waste of resources in the private and government sectors that result from corporate tax shelters and the manner in which they are regulated).
170. Sawyers, supra note 13, at 347. Some members of Congress have expressed a similar concern, including House Ways and Means Committee Chairman Archer who has sought a clearer distinction between abusive tax shelters and legitimate corporate tax planning. See Doggett to Offer Bill to Close Tax 'Loopholes', CONG. DAILY A.M., June 8, 1999, available in 1999 WL 18390966.
actions with legitimate business purposes. A more definitive guiding principle would provide advantages to tax administrators and taxpayers alike by promoting consistency in application and efficiency in enforcement of the tax laws.

Another concern about the current proposals contends that they suggest a significant shift in authority from Congress to the IRS. The obscure manner that the current proposals define a “tax avoidance transaction,” together with the vast range of recommended sanctions, would provide IRS auditors with excessive opportunities and incentives to find abusive tax avoidance transactions at will.

Another related and often cited concern states that the current proposals are so broad that they would negatively affect legitimate corporate tax planning. While conceding that legitimate cases of abuse and unjustified manipulation of the tax laws exist, it is still legitimate for corporations to attempt to minimize their tax liability. The current proposals broadly proscribe so many powers to the government that there is a real likelihood that, if enacted in their current form, corporate taxpayers would be discouraged from considering any tax savings measures for fear

171.  See Sawyers, supra note 13, at 347; see also discussion supra part IV.A and notes 122, 123, and 143.

172.  See Hearing on Corporate Tax Shelters, supra note 5 (statement of David A. Lifson, Chair, Tax Executives Committee, American Institute of Certified Public Accountants) <http://www.house.gov/ways_means/fullcomm/106cong/11-10-99/1110lifs.htm> (noting that an effective standard balances the powers of the IRS with the concomitant burden placed on taxpayers to comply with the regulation).

173.  See Sawyers, supra note 13, at 347 (maintaining that such a result would contradict the taxpayers' rights under the in 1998 IRS restructuring legislation). These proposals seek to grant the IRS increased authority, which some view as a grant of “virtually unbridled discretion,” only one year after Congress addressed incidents of the IRS zealously pursuing taxpayers. Id.

174.  Id. The IRS appears to have the authority to investigate an allegedly abusive transaction until the IRS ultimately prevails. See generally UPS v. Commissioner, 78 T.C.M. (CCH) 262 (1999) (discussing a case where the IRS pursued one abusive tax shelter for 15 years).

175.  See Sawyers, supra note 13, at 348; Hearing on Corporate Tax Shelters, supra note 5 (statement of Charles W. Shewbridge, III, Chief Tax Executive, BellSouth Corp., and President, Tax Executives Institute) <http://www.house.gov/ways_means/fullcomm/106cong/11-10-99/1110shew.htm> (recognizing that the desire to decrease one's tax liability is “as old as the Rosetta Stone and as legitimate as seeking shelter from the cold or rain” (footnote omitted); see also Gregory v. Helvering, 293 U.S. 465, 469 (1935). This legitimate taxpayer desire could easily be accommodated by concrete and specific proposals. See Sawyers, supra note 13, at 348.

176.  See, e.g., Granite Trust Co. v. United States, 238 F.2d 670, 675 (1st Cir. 1956); see also, e.g., Sawyers, supra note 13, at 346.
of the costly and time consuming litigation that would ensue.  

Finally, providing for increased penalty provisions, based on a vague standard would inequitably force taxpayers to overcome significant barriers to exercise their rights.  

"[P]enalties should be enacted to encourage compliance," and not to raise revenue; whether the current proposals abide by this view is open to debate.  

C. The Outlook for Reform  

There is no quick end in sight to this ongoing debate.  

It appears that neither the Joint Committee Report nor the Administration's proposals will be indoctrinated in the tax legislation currently under consideration.  

This is not to suggest that this issue simply will fade away. The abuse of corporate tax shelters continues to receive an enormous amount of attention and the high stakes involved support the conclusion that the debate over corporate tax shelters will continue well beyond current budget deliberations.  

As the debate continues over the proper approach to defining and regulating corporate tax shelters, it should be considered that perhaps the answer lies not in the details of the problem, but rather in fundamental reform. Such reform must allow corporations the tax benefits necessary to remain competitive in today's global marketplace, while eliminating the most egregious abuses.  

177. See Sawyers, supra note 13, at 348.  

178. See Gregory, 293 U.S. at 465; Sawyers, supra note 13, at 348.  

179. Sawyers, supra note 13, at 348.  

180. See Sheltering Tax Shelters, BUS. WEEK, July 26, 1999, at 43 (questioning whether the Administration's efforts to deter corporate tax shelter are dead for the year).  

181. See Archer, Roth to Defer Action on Corporate Tax Shelters, DOW JONES NEWS SERVICE, July 13, 1999 (indicating that the Chairmen of the two congressional tax writing committees, the House Ways and Means Committee and the Senate Finance Committee, planned to defer consideration of new corporate tax shelter proposals until 2000).  

182. See UK: US Attack on Corporate Tax Shelters-KPMG Tax Advisers, MONDAQ BUS. BRIEFING, July 2, 1999, available in 1999 WL 8710723 (warning against concluding that the Administration's current proposals will not be adopted). One firm advised its clients that the current attention received by corporate tax shelters has "raised the spectre of 'abusive corporate tax shelters' to new heights and there is reason to believe that they will be followed through in some form."  

183. While the verdict is still not in on the current debate regarding corporate tax shelters, some progress has been made in the form of extensive and informed debate on the subject. For example, the IRS has recently opened a new office devoted entirely to corporate tax shelters, which may provide more guidance on the specific definition of corporate tax shelters and the distinction between legitimate and abusive transactions. See John D. McKinnon, IRS, Reorganizing, to Sharpen Fight Against Abusive Corporate Tax Shelters,
V. CONCLUSION

The current body of law regulating corporate tax shelters is properly described as a model of uncertainty. There is little deterrent to prevent abuse of the system and few safeguards to prevent inadvertent interference with legitimate business activities. The current paradigm is ineffective and inefficient. Moreover, the current system may legitimately threaten the competitiveness of domestic corporations operating in a global marketplace.

As change to the current system of tax laws is discussed and alternatives are proposed, it is crucial that the actors in this debate recognize that changing circumstances require new approaches to the regulation of tax shelters. In today's global economy, the ability of U.S. companies to compete must be a priority. The objective, therefore, must be a system of taxation that balances fairness and enforceability in order to prevent abuses, but does not threaten legitimate business transactions.

The duty to pay one's fair share of the tax burden cannot be denied, but neither can a taxpayer's right to minimize his tax burden by any legal means. As currently applied, the distinction between what is abusive and what is legitimate is often difficult to ascertain. Yet, it is a distinction that will result in far reaching economic consequences whose impact will be felt far beyond corporate boardrooms. Developing a body of law that emphasizes fairness and promotes self-compliance, while also fostering competitiveness, should be the focal point as we seek an answer to the question of how best to regulate corporate tax shelters in today's complex economy.

WALL ST. J., Feb. 3, 2000, at A4. As the debate continues, solutions to the problem of corporate tax shelters may be found on roads not yet traveled. Numerous proposals have been discussed, and this dialogue must continue, as no single body or group of individuals is likely to solve the problem single handedly. See TREASURY WHITE PAPER, supra note 16, at 115-20 (discussing generally several alternative proposals, and addressing the inherent difficulty of solving the tax shelter dilemma). However, the political consequences of addressing this issue may be considered so potentially damaging that this issue will not be resolved during this crucial election year, leaving those most affected by the current system to ponder what lies ahead. See David R. Francis, Real Tax Debate: How to Spend Funds, CHRISTIAN SCI. MONITOR, Jan. 10, 2000, at 20; Howard Gleckman, Corporate Welfare: The Sound Bite and the Fury, BUS. WEEK, Jan. 17, 2000, at 80.