



State of Wisconsin
2007 - 2008 LEGISLATURE

LRB-1602/1

JK:.....

jld

DOA:.....Easton, BB0404 - Tax shelter voluntary compliance program

FOR 2007-09 BUDGET -- NOT READY FOR INTRODUCTION

*in 7-23-07
D-N*

don't gen

1 AN ACT ...; relating to: the budget.

Analysis by the Legislative Reference Bureau

TAXATION

INCOME TAXATION

This bill allows a taxpayer to report to DOR, without paying a penalty or facing criminal prosecution, certain transactions that are devised for the principal purpose of federal or state income or franchise tax and are required to be reported to the Internal Revenue Service under federal law. In order to avoid penalties and prosecution, a taxpayer must file an amended return with DOR for each taxable year beginning before January 1, 2007, in which the taxpayer participated in the transaction and pay any additional taxes. The amended return must be filed during the period beginning on October 1, 2007, and ending on December 31, 2007. Apart from the "grace period" provided under the bill, the bill, generally, requires taxpayers to report all such transactions to DOR, consistent with the reporting requirements under federal law, and pay all penalties, interest, and additional taxes.

For further information see the *state* fiscal estimate, which will be printed as an appendix to this bill.

The people of the state of Wisconsin, represented in senate and assembly, do enact as follows:

1 SECTION 1. 71.805[✓] of the statutes is created to read:

2 **71.805 Tax avoidance transactions voluntary compliance program. (1)**

3 [✓]DEFINITIONS. In this[✓] section:

4 (a) "Tax avoidance transaction"[✓] means a transaction, plan, or arrangement
5 devised for the principal purpose of avoiding federal or Wisconsin income or
6 franchise tax and that is a reportable transaction as provided under U.S. department
7 of ^{the} treasury regulations.

8 (b) "Taxpayer"[✓] means a person who is subject to the taxes imposed under this
9 chapter[✓] and who has a tax liability attributable to using a tax avoidance transaction
10 for any taxable year beginning before January 1, 2007.[✓]

11 (2)[✓] PENALTY WAIVER OR ABATEMENT. All of the following apply with regard to a
12 taxpayer who satisfies the conditions under sub. (3):[✓]

13 (a) Except as provided under sub. (4) (b),[✓] the department shall waive or abate
14 all penalties that are applicable to the underreporting or underpayment of Wisconsin
15 income or franchise taxes attributable to using a tax avoidance transaction for any
16 taxable year for which the taxpayer satisfies the conditions under sub.[✓] (3).

17 (b) The department shall not seek a criminal prosecution against the taxpayer
18 with respect to using a tax avoidance transaction for any taxable year for which the
19 taxpayer satisfies the conditions under sub. (3).[✓]

20 (3)[✓] TAXPAYER ELIGIBILITY. A taxpayer is eligible for the benefits described under
21 sub. (2) (a) and (b),[✓] if, during the period beginning on October 1, 2007, and ending
22 on December 31, 2007,[✓] the taxpayer does the following:

23 (a) Files an amended Wisconsin tax return for each taxable year for which the
24 taxpayer has previously filed a Wisconsin tax return that uses a tax avoidance
25 transaction to underreport the taxpayer's Wisconsin income or franchise tax liability

1 and the amended return reports the total Wisconsin net income and tax for the
2 taxable year, computed without regard to any tax avoidance transaction and without
3 regard to any other adjustment that is unrelated to any tax avoidance transaction.

4 (b) Pays, in full, for each taxable year for which an amended return is filed
5 under par. (a), the entire amount of Wisconsin income or franchise tax and interest
6 due that is attributable to using a tax avoidance transaction.

7 (4) LIMITATIONS AND ADMINISTRATION. (a) A taxpayer who receives the benefits
8 described under sub. (2) may not file an appeal or a claim for credit or refund with
9 respect to the tax avoidance transactions for the taxable years for which the taxpayer
10 satisfied the conditions under sub. (3).

11 (b) The department may not waive or abate a penalty as provided under sub.
12 (2) (a) if the penalty relates to an amount of Wisconsin income and franchise tax that
13 is attributable to a tax avoidance transaction and assessed or paid prior to October
14 1, 2007, or after December 31, 2007.

15 (c) For purposes of this section, a transaction does not have to be a reportable
16 transaction as provided under U.S. department of ^{the} treasury regulations in order for
17 the department to examine the transaction with regard to its principal purpose.

18 (d) A taxpayer who files an amended return under sub. (3) (a) may file a separate
19 amended return with respect to adjustments that are unrelated to any tax avoidance
20 transaction.

21 (e) The department shall promulgate rules, publish forms and instructions,
22 and take any other action necessary to implement and administer this section.

23 SECTION 2. 71.81 of the statutes is created to read:

24 **71.81 Disclosing reportable transactions.** (1) DEFINITIONS. In this section:

1 ^c
 2 ~~(a)~~ "Reportable transaction" means any transaction, plan, or arrangement,
 3 including a listed transaction, for which a taxpayer is required to submit information
 4 to the department because the taxpayer is required to disclose the transaction, plan,
 5 or arrangement for federal income tax purposes, as provided under U.S. department
 6 of ^{the} treasury regulations.

7 ^a
 8 ~~(b)~~ "Listed transaction" means any reportable transaction that is the same as,
 9 or substantially similar to, a transaction, plan, or arrangement specifically identified
 10 by the U.S. secretary of ^{the} treasury as a tax avoidance transaction for purposes of
 11 section 6011 of the Internal Revenue Code.

12 ^b
 13 ~~(c)~~ "Material advisor" means any person who provides any material aid,
 14 assistance, or advice with respect to organizing, managing, promoting, selling,
 15 implementing, insuring, or carrying out any reportable transaction and who, directly
 16 or indirectly, derives gross income from providing such aid, assistance, or advice in
 17 an amount that exceeds the threshold amount.

18 ^d
 19 ~~(d)~~ "Tax shelter" means any entity, plan, or arrangement, if avoiding or evading
 20 federal income tax or Wisconsin income or franchise tax is a significant purpose of
 21 the entity, plan, or arrangement.

22 ^e
 23 ~~(e)~~ "Threshold amount" means the following:

1. In the case of a reportable transaction, not including a listed transaction,
 from which a substantial part of the tax benefits are provided to an individual,
 \$50,000.

2. In the case of a listed transaction from which a substantial part of the tax
 benefits are provided to an individual, \$10,000.

1 3. In the case of a reportable transaction, not including a listed transaction,
2 from which a substantial part of the tax benefits are provided to an entity and not
3 an individual, \$250,000.✓

4 4. In the case of a listed transaction, from which a substantial part of the tax
5 benefits are provided to an entity and not an individual, \$25,000.✓

6 **(2) DISCLOSURE.**✓ For each taxable year in which a taxpayer has participated in
7 a reportable transaction, the taxpayer shall file with the department a copy of any
8 form prescribed by the internal revenue service✓ for disclosing a reportable
9 transaction for federal income tax purposes no later than 60✓ days after the date for
10 which the taxpayer is required to file the form for federal income tax purposes, except
11 that, if the taxpayer has filed a form with the internal revenue service on or before
12 the effective date of this subsection✓ [revisor inserts date], the taxpayer shall file
13 a copy of the form with the department no later than December✓31, 2007. The
14 department may require that forms filed with the department under this✓ subsection
15 be filed separately from this state's income or franchise tax return. This subsection
16 applies to any reportable transaction entered into after✓ January 1, 2002, for any
17 taxable year for which the transaction remains undisclosed and for which the statute
18 of limitations on assessment, including any extension provided under✓ sub. (6), has
19 not expired as of the date that is✓ 60 days after the effective date of this✓ subsection
20 [revisor inserts date].

21 **(3) PENALTY FOR FAILING TO DISCLOSE.**✓ (a) Any taxpayer who does not file the
22 form under sub. (2)✓ and who is required to file the form is subject to the following
23 penalty:

1 1. If the taxpayer participated in a reportable transaction that is not a listed
2 transaction, the lesser of \$15,000 or 10[✓] percent of the tax benefit obtained from the
3 reportable transaction.

4 2. If the taxpayer participated in a listed transaction,[✓]\$30,000.

5 (b) The penalty imposed under this subsection[✓] is assessed on the due date of
6 the Wisconsin income and franchise tax return for the period in which the
7 undisclosed reportable transaction occurred.

8 (c) The secretary of revenue may waive or abate any penalty imposed under this
9 subsection,[✓] or any portion of such penalty, related to a reportable transaction that
10 is not a listed transaction, if the waiver or abatement promotes compliance with this
11 section[✓] and effective tax administration.

12 (4) UNDERSTATEMENT PENALTY.[✓](a) If a taxpayer has a reportable transaction
13 understatement, as determined in par. (b),[✓] the taxpayer shall pay, in addition to any
14 tax owed with regard to the reportable transaction, an amount equal to either[✓] 20
15 percent of the reportable transaction understatement or, in the case of a reportable
16 transaction that is not disclosed as provided in sub. (2),[✓] 30 percent of the reportable
17 transaction understatement.

18 (b) A taxpayer has a reportable transaction understatement if the following
19 calculation results in a positive number:

20 1. Multiply the taxpayer's highest applicable tax rate under s. 71.06,[✓] 71.27,[✓] or
21 71.46,[✓] by the amount of any increase in Wisconsin taxable income that results from
22 the difference between the proper tax treatment of a reportable transaction and the
23 taxpayer's treatment of the transaction as shown on the taxpayer's tax return,
24 including any amended return the taxpayer files before the date[✓] on which the
25 department first contacts the taxpayer regarding an examination of the taxable year

1 for which the amended return is filed. For purposes of this subdivision, the amount
2 of any increase in Wisconsin taxable income for a taxable year includes any reduction
3 in the amount of loss available for carry-forward to the subsequent year.

4 2. Add the amount determined under subd. 1. to the amount of any decrease
5 in the aggregate amount of Wisconsin income or franchise tax credits that results
6 from the difference between the proper tax treatment of a reportable transaction and
7 the taxpayer's treatment of the transaction as shown on the taxpayer's tax return.

8 (c) The penalty imposed under this subsection is assessed on the due date of
9 the Wisconsin income and franchise tax return for the period that includes the
10 reportable transaction understatement for which the penalty relates.

11 (d) The secretary of revenue may waive or abate any penalty imposed under
12 this subsection, or any portion of such penalty, if the taxpayer demonstrates to the
13 department that the taxpayer had reasonable cause to act the way the taxpayer did,
14 and in good faith, with regard to the tax treatment for which the taxpayer is subject
15 to a penalty under this subsection and all facts relevant to the tax treatment are
16 adequately disclosed in the filing under sub. (2), except that, if the taxpayer does not
17 fully disclose such facts under sub. (2), the taxpayer's penalty may be waived or
18 abated under this paragraph if the taxpayer demonstrates to the department that
19 the taxpayer reasonably believed that the tax treatment for which the taxpayer is
20 subject to a penalty under this subsection was more likely than not the proper
21 treatment and substantial authority exists or existed for the tax treatment for which
22 the taxpayer is subject to a penalty under this subsection.

23 (5) ADDITIONAL UNDERSTATEMENT PENALTY. (a) 1. A taxpayer who files an
24 amended return after December 31, 2007, and before the taxpayer is contacted by the
25 internal revenue service or the department regarding a reportable transaction is

1 subject to a penalty in an amount equal to 50 percent of the interest assessed under
2 s. 71.82 on any reportable transaction understatement, as determined under sub. (4)
3 (b), for the tax period for which the taxpayer files an amended return.

4 2. If the internal revenue service or the department contacts a taxpayer after
5 December 31, 2007, regarding a reportable transaction and the taxpayer is contacted
6 before the taxpayer files an amended return with respect to that transaction, the
7 taxpayer is subject to a penalty in an amount equal to the interest assessed under
8 s. 71.82 on any reportable transaction understatement, as determined under sub. (4)
9 (b), for the tax period for which the taxpayer files an amended return.

10 (b) The penalties under sub. (a) apply to any reportable transaction
11 understatement resulting from a listed transaction entered into after January 1,
12 2002, or from any other reportable transaction entered into after the effective date
13 of this paragraph [revisor inserts date], for any taxable year for which the statute
14 of limitations on assessment, including any extension provided under sub. (6), has
15 not expired as of the effective date of this paragraph [revisor inserts date].

16 (c) The secretary of revenue may waive or abate any penalty imposed under this
17 subsection, or any portion of such penalty, if the taxpayer demonstrates to the
18 department that the taxpayer had reasonable cause to act the way the taxpayer did,
19 and in good faith, with regard to the tax treatment for which the taxpayer is subject
20 to a penalty under this subsection and all facts relevant to the tax treatment are
21 adequately disclosed in the filing under sub. (2), except that, if the taxpayer does not
22 fully disclose such facts under sub. (2), the taxpayer's penalty may be waived or
23 abated under this paragraph if the taxpayer demonstrates to the department that
24 the taxpayer reasonably believed that the tax treatment for which the taxpayer is
25 subject to a penalty under this subsection was more likely than not the proper

1 treatment and substantial authority exists or existed for the tax treatment for which
2 the taxpayer is subject to a penalty under this subsection.

3 (6) STATUTE OF LIMITATIONS EXTENSION. If a taxpayers fails to provide any
4 information regarding a reportable transaction, other than a listed transaction,
5 under sub. (2), the time for assessing any tax imposed under this chapter with
6 respect to that transaction shall expire no later than the date that is 6 years after the
7 date on which the return for the taxable year in which the reportable transaction
8 occurred was filed. If a taxpayers fails to provide any information regarding a listed
9 transaction, under sub. (2), the time for assessing any tax imposed under this chapter
10 with respect to that transaction shall expire no later than the earlier of the following:

11 (a) The date that is 6 years after the date on which the return for the taxable
12 year in which the listed transaction occurred was filed.

13 (b) The date that is 12 months after the date on which the taxpayer provides
14 information regarding the listed transaction under sub. (2).

15 (c) The date that is 12 months after the date on which the taxpayer's material
16 advisor provides, at the department's request, the list described in sub. (7) (b).

17 (7) MATERIAL ADVISOR. (a) Each material advisor who is required to disclose a
18 reportable transaction under section 6111 of the Internal Revenue Code shall file a
19 copy of the disclosure with the department no later than 60 days after the date for
20 which the material advisor is required to file the disclosure with the internal revenue
21 service, except that, if a material advisor files the disclosure with the internal
22 revenue service on or before the effective date of this paragraph ... [revisor inserts
23 date], the material advisor shall file a copy of the disclosure with the department no
24 later than December 31, 2007.

1 (b) Each material advisor shall maintain a list that identifies each Wisconsin
2 taxpayer for whom the person provided services as a material advisor, regardless of
3 whether the taxpayer is required to file the form under sub. (2). Any material advisor
4 who is required to maintain a list under this paragraph shall provide the list to the
5 department after receiving the department's written request to provide the list and
6 shall retain the information contained in the list for 7 years or for the period
7 determined by the department by rule. If 2 or more material advisors are required
8 under this paragraph to maintain identical lists, the department may provide that
9 only one of the material advisors maintain the list.

10 (c) This subsection applies to reportable transactions, not including listed
11 transactions, for which a material advisor provides services after the effective date
12 of this paragraph [revisor inserts date], and listed transactions for which a
13 material advisor provides services, and were entered into, on or after January 1,
14 2002, regardless of when the transactions became listed transactions.

15 (8) MATERIAL ADVISOR PENALTIES. (a) If a person who is required to file a
16 disclosure with the department as provided under sub. (7) (a) fails to file the
17 disclosure or files a disclosure containing false or incomplete information, the person
18 is subject to a penalty equal to the following amounts:

19 1. If the disclosure relates to a reportable transaction that is not a listed
20 transaction, \$15,000.

21 2. If the disclosure relates to a listed transaction, \$100,000.

22 (b) Any person who is required to maintain a list under sub. (7) (b) and who fails
23 to provide the list to the department no later than 20 business days after the date on
24 which the person receives the department's request to provide the list, as provided
25 under sub. (7) (b), shall pay a penalty to the department in an amount that is equal

1 to \$10,000[✓] for each day that the person does not provide the list, beginning with the
2 day that is 21[✓] business days after the date on which the person receives the
3 department's request.

4 (c) The secretary of revenue may waive or abate any penalty imposed under this
5 subsection,[✓] or any portion of such penalty, related to a reportable transaction that
6 is not a listed transaction, if the waiver or abatement promotes compliance with this
7 section[✓] and effective tax administration or, with regard to the penalty imposed under
8 par. (b),[✓] if, on each day after the time for providing the list without incurring a
9 penalty has expired, the person demonstrates to the department[✓] that the person's
10 failure to provide the list on that day is because of reasonable cause.[✓]

11 (9) TAX SHELTER PROMOTION.[✓] (a) Beginning on the effective date of this
12 paragraph[✓] [revisor inserts date], any person who organizes or assists in
13 organizing a tax shelter, or directly or indirectly participates in the sale of any
14 interest in a tax shelter, and who makes or provides or causes another person to make
15 or provide, in connection with such organization or sale, a statement that the person
16 knows or has reason to know is false or fraudulent as to any material matter
17 regarding the allowability of any tax deduction or credit, the excludability of any
18 income, the manipulation of any allocation or apportionment rule, or the securing of
19 any other tax benefit resulting from holding an interest in the entity or participating
20 in the plan or arrangement, shall pay a penalty to the department, with respect to
21 each sale or act of organization described under this paragraph,[✓] in an amount equal
22 to 50 percent[✓] of the person's gross income derived from the sale or act.

23 (b) For purposes of administering this chapter, beginning on the effective date
24 of this paragraph[✓] [revisor inserts date], a written communication between a tax
25 ~~practioner~~ and any person, director, officer, employee, agent, or representative of the

practitioner

1 person, or any other person holding a capital or profits interest in the person,
2 regarding the promotion of the person's direct or indirect participation in any tax
3 shelter is not considered a confidential or privileged communication.✓

4 (11) INJUNCTION. The department may commence an action in the circuit court
5 of Dane County✓ to enjoin a person from taking any action, or failing to take any
6 action, that is subject to a penalty under this section✓ or in violation of this section or
7 any rules that the department promulgates pursuant to this section.✓

8 (END)

d-note

DRAFTER'S NOTE
FROM THE
LEGISLATIVE REFERENCE BUREAU

LRB-1602/1dn

JK:.....

date

Jld

Darren:

Please review this draft carefully to ensure that it is consistent with your intent. I modified the language provided by DOR as necessary to remove superfluous language.

Although I do not have sufficient time to research the issue, I believe the provision related to DOR not considering written communications between "tax ~~practioner~~" and persons who promote a tax shelter to be confidential may be overly broad and, therefore, legally infirm. First, the provision conflicts with an attorney's duty to keep client communications confidential under Supreme Court Rules 20:1.6. Under the rule, an attorney may reveal any information that would otherwise be confidential to prevent the client from committing certain criminal or fraudulent acts (note the present tense). With regard to the client's past acts, however, the attorney may only reveal such information to provide a defense for the client or to rectify the consequences of any of the client's criminal or fraudulent acts for which the attorney inadvertently offered his or her assistance. In short, I'm not sure that the state can compel a tax attorney (who I assume would be a "tax ~~practioner~~" for purposes of the bill) to disclose written communications with a client who is seeking legal advice regarding a tax shelter that the client promoted in the past and for which the client may be facing legal consequences.

Second, the provision related to disclosing certain written communications could be unconstitutional to the extent that it compels a person to incriminate himself or herself with regard to the commission of a criminal act. Please contact me if you have any questions. ✓

Joseph T. Kreye
Legislative Attorney
Phone: (608) 266-2263
E-mail: joseph.kreye@legis.wisconsin.gov

DRAFTER'S NOTE
FROM THE
LEGISLATIVE REFERENCE BUREAU

LRB-1602/1dn
JK:jld:pg

January 24, 2007

Darren:

Please review this draft carefully to ensure that it is consistent with your intent. I modified the language provided by DOR as necessary to remove superfluous language.

Although I do not have sufficient time to research the issue, I believe the provision related to DOR not considering written communications between "tax practitioners" and persons who promote a tax shelter to be confidential may be overly broad and, therefore, legally infirm. First, the provision conflicts with an attorney's duty to keep client communications confidential under Supreme Court Rules 20:1.6. Under the rule, an attorney may reveal any information that would otherwise be confidential to prevent the client from committing certain criminal or fraudulent acts (note the present tense). With regard to the client's past acts, however, the attorney may only reveal such information to provide a defense for the client or to rectify the consequences of any of the client's criminal or fraudulent acts for which the attorney inadvertently offered his or her assistance. In short, I'm not sure that the state can compel a tax attorney (who I assume would be a "tax practitioner" for purposes of the bill) to disclose written communications with a client who is seeking legal advice regarding a tax shelter that the client promoted in the past and for which the client may be facing legal consequences.

Second, the provision related to disclosing certain written communications could be unconstitutional to the extent that it compels a person to incriminate himself or herself with regard to the commission of a criminal act. Please contact me if you have any questions.

Joseph T. Kreye
Legislative Attorney
Phone: (608) 266-2263
E-mail: joseph.kreye@legis.wisconsin.gov

**Department of Revenue Comments on LRB Drafts
LRB 1602/1**

1. Bill and/or LRB Number: LRB-1602/1 – Tax Shelter Voluntary Compliance Program

2. Type of Taxes Affected: (please list all that apply)

Corporation franchise and income
Individual income

3. Description of the Bill: (briefly describe the subject matter of the bill and the change/s)

This bill requires taxpayers and their advisors to file with the department copies of certain information they are already required to provide to the internal revenue service (subject to the statute of limitations) with regard to transactions the IRS has identified as potentially abusive tax avoidance transactions. These transactions are called “reportable transactions.” The bill also adopts a modified version of the penalties imposed by the internal revenue code for failure to provide this information.

To transition into these requirements, this bill provides for a voluntary compliance program in which all penalties will be waived with regard to underpayments caused by reportable transactions for which the required information is provided during the period of October 1, 2007 through December 31, 2007.

4. Statutory language problems, if any: Yes No

(If yes, describe problems and indicate suggested corrective language. Example of problem: The bill language is unclear, does not fully accomplish the desired result, or has undesirable side effects.)

The following changes are necessary to better communicate the bill's intent:

✓ **A.** In sec. 71.805(4)(c), the paragraph begins “*For purposes of this section...*” However, the intent of this paragraph is to convey that the definition of “tax avoidance transaction” in this section should not be construed to apply in any other section. A better way to communicate the intent is to begin the paragraph as follows: “*Notwithstanding the provisions of this section...*”

✓ **B.** The paragraphs 71.81(3)(b) and (4)(c) contain a provision that considers the penalty to be imposed on the due date of the Wisconsin income and franchise tax return to which the penalty applies. This is inconsistent with the way other penalties are administered because it imposes interest on the penalty amount. To simplify administration of this section, these paragraphs should be deleted.

C. Sec. 71.81(3) needs effective date language. This language is as follows:

imposed under the subsection
✓ “The penalties under sub. (a) apply to any failure to disclose a listed transaction entered into after January 1, 2002, including transactions which were not listed transactions when entered into but became listed before the effective date of this paragraph, or any other reportable transaction entered into after the effective date of this paragraph, for any taxable year for which the statute of limitations on assessment, including any extension provided under sub. (6), has not expired as of the effective date of this paragraph.”

✓ D. In sec. 71.81(5)(a)2., the additional understatement penalty language incorrectly imposes the penalty for “*the tax period for which the taxpayer files an amended return.*” This subparagraph applies to situations where the taxpayer is contacted by the IRS or the department before an amended return is filed. Therefore, penalty in (5)(a)2. should be imposed for the tax period “*for which the taxpayer is contacted by the internal revenue service or the department.*”

✓ E. The effective date language in sec. 71.81(5)(b) does not address listed transactions which became listed transactions subsequent to January 1, 2002 but before the effective date of this paragraph. To accomplish this, (5)(b) should read:

“The penalties under sub. (a) apply to any reportable transaction understatement resulting from a listed transaction entered into after January 1, 2002, including transactions which were not listed transactions when entered into but became listed before the effective date of this paragraph, or from any other reportable transaction entered into after the effective date of this paragraph, for any taxable year for which the statute of limitations on assessment, including any extension provided under sub. (6), has not expired as of the effective date of this paragraph.”

✓ F. In the last sentence of sec. 71.81(6), the “later” and “earlier” are in reverse order. The statute of limitations for an undisclosed listed transaction cannot expire earlier than 6 years after the date on which the return for the taxable year in which the listed transaction occurred was filed. Also, throughout subsection (6), “taxpayers” should be changed to “taxpayer.”

✓ G. In sec. 71.81(7)(b), clarify that the list maintenance requirement only applies to material advisors with respect to a reportable transaction. This could be done by beginning the paragraph as follows:

“Each material advisor shall maintain a list that identifies each Wisconsin taxpayer for whom the person provided services as a material advisor with respect to a reportable transaction....”

5. **Effective date problems, if any, including transitional problems:** Yes X No
(If yes, describe problem and suggested effective date or transitional language needed.)

NOTE: If the effective date is later than July 31, 2007, the time period of the voluntary compliance program may need to be adjusted to allow adequate time to publicize the program before its start date.



State of Wisconsin
2007 - 2008 LEGISLATURE

LRB-1602/1

JK:jld:pg

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Handwritten initials and a signature.

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FOR 2007-09 BUDGET -- NOT READY FOR INTRODUCTION

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INCOME TAXATION

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For further information see the *state* fiscal estimate, which will be printed as an appendix to this bill.

The people of the state of Wisconsin, represented in senate and assembly, do enact as follows:

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2 **71.805 Tax avoidance transactions voluntary compliance program. (1)**

3 DEFINITIONS. In this section:

4 (a) "Tax avoidance transaction" means a transaction, plan, or arrangement
5 devised for the principal purpose of avoiding federal or Wisconsin income or
6 franchise tax and that is a reportable transaction as provided under U.S. department
7 of the treasury regulations.

8 (b) "Taxpayer" means a person who is subject to the taxes imposed under this
9 chapter and who has a tax liability attributable to using a tax avoidance transaction
10 for any taxable year beginning before January 1, 2007.

11 **(2) PENALTY WAIVER OR ABATEMENT.** All of the following apply with regard to a
12 taxpayer who satisfies the conditions under sub. (3):

13 (a) Except as provided under sub. (4) (b), the department shall waive or abate
14 all penalties that are applicable to the underreporting or underpayment of Wisconsin
15 income or franchise taxes attributable to using a tax avoidance transaction for any
16 taxable year for which the taxpayer satisfies the conditions under sub. (3).

17 (b) The department shall not seek a criminal prosecution against the taxpayer
18 with respect to using a tax avoidance transaction for any taxable year for which the
19 taxpayer satisfies the conditions under sub. (3).

20 **(3) TAXPAYER ELIGIBILITY.** A taxpayer is eligible for the benefits described under
21 sub. (2) (a) and (b), if, during the period beginning on October 1, 2007, and ending
22 on December 31, 2007, the taxpayer does the following:

23 (a) Files an amended Wisconsin tax return for each taxable year for which the
24 taxpayer has previously filed a Wisconsin tax return that uses a tax avoidance
25 transaction to underreport the taxpayer's Wisconsin income or franchise tax liability

1 and the amended return reports the total Wisconsin net income and tax for the
2 taxable year, computed without regard to any tax avoidance transaction and without
3 regard to any other adjustment that is unrelated to any tax avoidance transaction.

4 (b) Pays, in full, for each taxable year for which an amended return is filed
5 under par. (a), the entire amount of Wisconsin income or franchise tax and interest
6 due that is attributable to using a tax avoidance transaction.

7 (4) LIMITATIONS AND ADMINISTRATION. (a) A taxpayer who receives the benefits
8 described under sub. (2) may not file an appeal or a claim for credit or refund with
9 respect to the tax avoidance transactions for the taxable years for which the taxpayer
10 satisfied the conditions under sub. (3).

11 (b) The department may not waive or abate a penalty as provided under sub.
12 (2) (a) if the penalty relates to an amount of Wisconsin income and franchise tax that
13 is attributable to a tax avoidance transaction and assessed or paid prior to October
14 1, 2007, or after December 31, 2007.

15 (c) ~~For purposes of this section,~~ *Notwithstanding the other provisions of this section* a transaction does not have to be a reportable
16 transaction as provided under U.S. department of the treasury regulations in order
17 for the department to examine the transaction with regard to its principal purpose.

18 (d) A taxpayer who files an amended return under sub. (3) (a) may file a
19 separate amended return with respect to adjustments that are unrelated to any tax
20 avoidance transaction.

21 (e) The department shall promulgate rules, publish forms and instructions,
22 and take any other action necessary to implement and administer this section.

23 SECTION 2. 71.81 of the statutes is created to read:

24 **71.81 Disclosing reportable transactions.** (1) DEFINITIONS. In this section:

1 (a) "Listed transaction" means any reportable transaction that is the same as,
2 or substantially similar to, a transaction, plan, or arrangement specifically identified
3 by the U.S. secretary of the treasury as a tax avoidance transaction for purposes of
4 section 6011 of the Internal Revenue Code.

5 (b) "Material advisor" means any person who provides any material aid,
6 assistance, or advice with respect to organizing, managing, promoting, selling,
7 implementing, insuring, or carrying out any reportable transaction and who, directly
8 or indirectly, derives gross income from providing such aid, assistance, or advice in
9 an amount that exceeds the threshold amount.

10 (c) "Reportable transaction" means any transaction, plan, or arrangement,
11 including a listed transaction, for which a taxpayer is required to submit information
12 to the department because the taxpayer is required to disclose the transaction, plan,
13 or arrangement for federal income tax purposes, as provided under U.S. department
14 of treasury regulations.

15 (d) "Tax shelter" means any entity, plan, or arrangement, if avoiding or evading
16 federal income tax or Wisconsin income or franchise tax is a significant purpose of
17 the entity, plan, or arrangement.

18 (e) "Threshold amount" means the following:

19 1. In the case of a reportable transaction, not including a listed transaction,
20 from which a substantial part of the tax benefits are provided to an individual,
21 \$50,000.

22 2. In the case of a listed transaction from which a substantial part of the tax
23 benefits are provided to an individual, \$10,000.

1 3. In the case of a reportable transaction, not including a listed transaction,
2 from which a substantial part of the tax benefits are provided to an entity and not
3 an individual, \$250,000.

4 4. In the case of a listed transaction, from which a substantial part of the tax
5 benefits are provided to an entity and not an individual, \$25,000.

6 **(2) DISCLOSURE.** For each taxable year in which a taxpayer has participated in
7 a reportable transaction, the taxpayer shall file with the department a copy of any
8 form prescribed by the internal revenue service for disclosing a reportable
9 transaction for federal income tax purposes no later than 60 days after the date for
10 which the taxpayer is required to file the form for federal income tax purposes, except
11 that, if the taxpayer has filed a form with the internal revenue service on or before
12 the effective date of this subsection [revisor inserts date], the taxpayer shall file
13 a copy of the form with the department no later than December 31, 2007. The
14 department may require that forms filed with the department under this subsection
15 be filed separately from this state's income or franchise tax return. This subsection
16 applies to any reportable transaction entered into after January 1, 2002, for any
17 taxable year for which the transaction remains undisclosed and for which the statute
18 of limitations on assessment, including any extension provided under sub. (6), has
19 not expired as of the date that is 60 days after the effective date of this subsection
20 [revisor inserts date].

21 **(3) PENALTY FOR FAILING TO DISCLOSE.** (a) Any taxpayer who does not file the
22 form under sub. (2) and who is required to file the form is subject to the following
23 penalty:

1 1. If the taxpayer participated in a reportable transaction that is not a listed
2 transaction, the lesser of \$15,000 or 10 percent of the tax benefit obtained from the
3 reportable transaction.

4 2. If the taxpayer participated in a listed transaction, \$30,000.

5 (b) The penalty imposed under this subsection is assessed on the due date of
6 the Wisconsin income and franchise tax return for the period in which the
7 undisclosed reportable transaction occurred.

8 (c) The secretary of revenue may waive or abate any penalty imposed under this
9 subsection, or any portion of such penalty, related to a reportable transaction that
10 is not a listed transaction, if the waiver or abatement promotes compliance with this
11 section and effective tax administration.

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12 (4) UNDERSTATEMENT PENALTY. (a) If a taxpayer has a reportable transaction
13 understatement, as determined in par. (b), the taxpayer shall pay, in addition to any
14 tax owed with regard to the reportable transaction, an amount equal to either 20
15 percent of the reportable transaction understatement or, in the case of a reportable
16 transaction that is not disclosed as provided in sub. (2), 30 percent of the reportable
17 transaction understatement.

18 (b) A taxpayer has a reportable transaction understatement if the following
19 calculation results in a positive number:

20 1. Multiply the taxpayer's highest applicable tax rate under s. 71.06, 71.27, or
21 71.46, by the amount of any increase in Wisconsin taxable income that results from
22 the difference between the proper tax treatment of a reportable transaction and the
23 taxpayer's treatment of the transaction as shown on the taxpayer's tax return,
24 including any amended return the taxpayer files before the date on which the
25 department first contacts the taxpayer regarding an examination of the taxable year

1 for which the amended return is filed. For purposes of this subdivision, the amount
2 of any increase in Wisconsin taxable income for a taxable year includes any reduction
3 in the amount of loss available for carry-forward to the subsequent year.

4 2. Add the amount determined under subd. 1. to the amount of any decrease
5 in the aggregate amount of Wisconsin income or franchise tax credits that results
6 from the difference between the proper tax treatment of a reportable transaction and
7 the taxpayer's treatment of the transaction as shown on the taxpayer's tax return.

8 (c) The penalty imposed under this subsection is assessed on the due date of
9 the Wisconsin income and franchise tax return for the period that includes the
10 reportable transaction understatement for which the penalty relates.

11 (d) The secretary of revenue may waive or abate any penalty imposed under
12 this subsection, or any portion of such penalty, if the taxpayer demonstrates to the
13 department that the taxpayer had reasonable cause to act the way the taxpayer did,
14 and in good faith, with regard to the tax treatment for which the taxpayer is subject
15 to a penalty under this subsection and all facts relevant to the tax treatment are
16 adequately disclosed in the filing under sub. (2), except that, if the taxpayer does not
17 fully disclose such facts under sub. (2), the taxpayer's penalty may be waived or
18 abated under this paragraph if the taxpayer demonstrates to the department that
19 the taxpayer reasonably believed that the tax treatment for which the taxpayer is
20 subject to a penalty under this subsection was more likely than not the proper
21 treatment and substantial authority exists or existed for the tax treatment for which
22 the taxpayer is subject to a penalty under this subsection.

23 (5) ADDITIONAL UNDERSTATEMENT PENALTY. (a) 1. A taxpayer who files an
24 amended return after December 31, 2007, and before the taxpayer is contacted by the
25 internal revenue service or the department regarding a reportable transaction is

The internal revenue service or the department contacts

1 subject to a penalty in an amount equal to 50 percent of the interest assessed under
2 s. 71.82 on any reportable transaction understatement, as determined under sub. (4)
3 (b), for the tax period for which the taxpayer files an amended return.

4 2. If the internal revenue service or the department contacts a taxpayer after
5 December 31, 2007, regarding a reportable transaction and the taxpayer is contacted
6 before the taxpayer files an amended return with respect to that transaction, the
7 taxpayer is subject to a penalty in an amount equal to the interest assessed under
8 s. 71.82 on any reportable transaction understatement, as determined under sub. (4)
9 (b), for the tax period for which the taxpayer files an amended return.

10 *INSERT 8-12* (b) The penalties under sub. (a) apply to any reportable transaction
11 understatement resulting from a listed transaction entered into after January 1,
12 2002, or from any other reportable transaction entered into after the effective date
13 of this paragraph [revisor inserts date], for any taxable year for which the statute
14 of limitations on assessment, including any extension provided under sub. (6), has
15 not expired as of the effective date of this paragraph [revisor inserts date].

16 (c) The secretary of revenue may waive or abate any penalty imposed under this
17 subsection, or any portion of such penalty, if the taxpayer demonstrates to the
18 department that the taxpayer had reasonable cause to act the way the taxpayer did,
19 and in good faith, with regard to the tax treatment for which the taxpayer is subject
20 to a penalty under this subsection and all facts relevant to the tax treatment are
21 adequately disclosed in the filing under sub. (2), except that, if the taxpayer does not
22 fully disclose such facts under sub. (2), the taxpayer's penalty may be waived or
23 abated under this paragraph if the taxpayer demonstrates to the department that
24 the taxpayer reasonably believed that the tax treatment for which the taxpayer is
25 subject to a penalty under this subsection was more likely than not the proper

1 treatment and substantial authority exists or existed for the tax treatment for which
2 the taxpayer is subject to a penalty under this subsection.

3 (6) STATUTE OF LIMITATIONS EXTENSION. If a taxpayer^e fails to provide any
4 information regarding a reportable transaction, other than a listed transaction,
5 under sub. (2), the time for assessing any tax imposed under this chapter with
6 respect to that transaction shall expire no later than the date that is 6 years after the
7 date on which the return for the taxable year in which the reportable transaction
8 occurred was filed. If a taxpayer^e fails to provide any information regarding a listed
9 transaction, under sub. (2), the time for assessing any tax imposed under this chapter
10 with respect to that transaction shall expire ~~no later than the earlier~~ of the following:

11 (a) The date that is 6 years after the date on which the return for the taxable
12 year in which the listed transaction occurred was filed.

13 (b) The date that is 12 months after the date on which the taxpayer provides
14 information regarding the listed transaction under sub. (2).

15 (c) The date that is 12 months after the date on which the taxpayer's material
16 advisor provides, at the department's request, the list described in sub. (7) (b).

17 (7) MATERIAL ADVISOR. (a) Each material advisor who is required to disclose a
18 reportable transaction under section 6111 of the Internal Revenue Code shall file a
19 copy of the disclosure with the department no later than 60 days after the date for
20 which the material advisor is required to file the disclosure with the internal revenue
21 service, except that, if a material advisor files the disclosure with the internal
22 revenue service on or before the effective date of this paragraph [revisor inserts
23 date], the material advisor shall file a copy of the disclosure with the department no
24 later than December 31, 2007.

dates

on the earliest

with respect to a reportable transaction

1 (b) Each material advisor shall maintain a list that identifies each Wisconsin
2 taxpayer for whom the person provided services as a material advisor, regardless of
3 whether the taxpayer is required to file the form under sub. (2). Any material advisor
4 who is required to maintain a list under this paragraph shall provide the list to the
5 department after receiving the department's written request to provide the list and
6 shall retain the information contained in the list for 7 years or for the period
7 determined by the department by rule. If 2 or more material advisors are required
8 under this paragraph to maintain identical lists, the department may provide that
9 only one of the material advisors maintain the list.

10 (c) This subsection applies to reportable transactions, not including listed
11 transactions, for which a material advisor provides services after the effective date
12 of this paragraph [revisor inserts date], and listed transactions for which a
13 material advisor provides services, and were entered into, on or after January 1,
14 2002, regardless of when the transactions became listed transactions.

15 (8) MATERIAL ADVISOR PENALTIES. (a) If a person who is required to file a
16 disclosure with the department as provided under sub. (7) (a) fails to file the
17 disclosure or files a disclosure containing false or incomplete information, the person
18 is subject to a penalty equal to the following amounts:

19 1. If the disclosure relates to a reportable transaction that is not a listed
20 transaction, \$15,000.

21 2. If the disclosure relates to a listed transaction, \$100,000.

22 (b) Any person who is required to maintain a list under sub. (7) (b) and who fails
23 to provide the list to the department no later than 20 business days after the date on
24 which the person receives the department's request to provide the list, as provided
25 under sub. (7) (b), shall pay a penalty to the department in an amount that is equal

1 to \$10,000 for each day that the person does not provide the list, beginning with the
2 day that is 21 business days after the date on which the person receives the
3 department's request.

4 (c) The secretary of revenue may waive or abate any penalty imposed under this
5 subsection, or any portion of such penalty, related to a reportable transaction that
6 is not a listed transaction, if the waiver or abatement promotes compliance with this
7 section and effective tax administration or, with regard to the penalty imposed under
8 par. (b), if, on each day after the time for providing the list without incurring a
9 penalty has expired, the person demonstrates to the department that the person's
10 failure to provide the list on that day is because of reasonable cause.

11 (9) TAX SHELTER PROMOTION. (a) Beginning on the effective date of this
12 paragraph [revisor inserts date], any person who organizes or assists in
13 organizing a tax shelter, or directly or indirectly participates in the sale of any
14 interest in a tax shelter, and who makes or provides or causes another person to make
15 or provide, in connection with such organization or sale, a statement that the person
16 knows or has reason to know is false or fraudulent as to any material matter
17 regarding the allowability of any tax deduction or credit, the excludability of any
18 income, the manipulation of any allocation or apportionment rule, or the securing of
19 any other tax benefit resulting from holding an interest in the entity or participating
20 in the plan or arrangement, shall pay a penalty to the department, with respect to
21 each sale or act of organization described under this paragraph, in an amount equal
22 to 50 percent of the person's gross income derived from the sale or act.

23 (b) For purposes of administering this chapter, beginning on the effective date
24 of this paragraph [revisor inserts date], a written communication between a tax
25 practitioner and any person, director, officer, employee, agent, or representative of

1 the person, or any other person holding a capital or profits interest in the person,
2 regarding the promotion of the person's direct or indirect participation in any tax
3 shelter is not considered a confidential or privileged communication.

4 (11) INJUNCTION. The department may commence an action in the circuit court
5 of Dane County to enjoin a person from taking any action, or failing to take any
6 action, that is subject to a penalty under this section or in violation of this section or
7 any rules that the department promulgates pursuant to this section.

8 (END)

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1 (c) The penalties imposed under this subsection apply to any failure to disclose
2 a listed transaction entered into after January 1, 2002, including transactions that
3 were not listed transactions when entered into, but became listed transactions before
4 the effective date of this paragraph [revisor inserts date], or any other reportable
5 transaction entered into after the effective date of this paragraph [revisor inserts
6 date], for any taxable year for which the statute of limitations on assessment,
7 including any extension under sub. (6), has not expired as of the effective date of this
8 paragraph [revisor inserts date].

Insert 8 - 12

9  including transactions that were not listed transactions when entered into, but
10 became listed transactions before the effective date of this paragraph [revisor
11 inserts date],

In secs. 71.81(3)(c), 71.81(5)(b), and 71.81(7)(c), "listed transaction" includes transactions entered into since 1/1/2002 that were not listed transactions when entered into, but became listed transactions before the effective date of this section. This meaning is intended for all uses of the term "listed transaction" in this section, including some not mentioned above. Also, the definition uses the term "tax avoidance transaction" in a way that has different meaning from "tax avoidance transaction" as defined in sec. 71.805. To address these issues, the recommended definition is as follows:

"...any reportable transaction that is the same as, or substantially similar to, a transaction, plan or arrangement specifically identified by the U.S. secretary of the treasury as a ~~tax~~ avoidance-listed transaction for purposes of section 6011 of the internal revenue code, which occurred on or after January 1, 2002 and which was specifically identified by the U.S. secretary of the treasury as a listed transaction on or after the date the transaction occurred."

C. "On or after" January 1, 2002 – Multiple Paragraphs

In secs. 71.81(2), (3)(c), and (5)(b), the effective dates apply to reportable transactions entered into "after January 1, 2002." To be precise, this should be changed to "on or after January 1, 2002."

D. Effective Date for Understatement Penalty – Sec. 71.81(4)(d)

This penalty does not have an effective date. The following language is recommended for a new subparagraph (4)(d):

"The penalties under sub. (a) apply to any reportable transaction understatement resulting from a reportable transaction, including a listed transaction, entered into on or after January 1, 2002, for any taxable year for which the statute of limitations on assessment, including any extension provided under sub. (6), has not expired as of the effective date of this paragraph."

E. Effective Date for Additional Understatement Penalty – Sec. 71.81(5)(b)

The effective date for the penalty in (5)(b) should be identical to (4)(d) above. (Note: The effective date for the penalty in (3)(c) is intended to be different from both of these)

F. Clarify Statute of Limitations – Sec. 71.81(6)

Currently the language does not accomplish the intent. The statute of limitations should be the latest of the dates listed in sub. (a) through sub (c), not the earliest. Also, it is unclear what happens if the taxpayer or taxpayer's material advisor never provide the information regarding the listed transaction. Further, it should be clarified that the statute of limitations may be extended by agreement between the taxpayer and the Department (as in the case of a field audit). The following language is recommended:

"(6) STATUTE OF LIMITATIONS EXTENSION. (a) If a taxpayer fails to . . . the time for assessing any tax imposed under this chapter with respect to that transaction shall expire on the ~~earliest~~ latest of the following dates:

1. The date that is 6 years . . .
4. If the taxpayer or taxpayer's material advisor do not provide the information described in subs. (2) or (7)(b) and the department subsequently discovers a listed transaction that was a listed transaction as of the date the transaction occurred, the date that is 4 years after the date of discovery by the department.

(b) The limitation periods provided in this section may be extended by written agreement between the taxpayer and the department as provided in s. 71.77(5).

5. **Effective date problems, if any, including transitional problems:** Yes No
(If yes, describe problem and suggested effective date or transitional language needed.)

NOTE: If the effective date is later than July 31, 2007, the time period of the voluntary compliance program may need to be adjusted to allow adequate time to publicize the program before its start date.