II. GENERAL FINDINGS AND RECOMMENDATIONS RELATING TO BUSINESS TAX MATTERS

A. General Findings Relating to Business Tax Matters

The Joint Committee staff believes that the transactions that are the subject of this Report demonstrate the need for strong anti-avoidance rules to combat transactions that might satisfy the technical requirements of the tax statutes and administrative rules, but that are conducted for little or no purpose other than to generate income tax or financial statement benefits. Accordingly, the Joint Committee staff makes the following findings and recommendations.

1. Cost-benefit analysis with respect to tax motivated transactions

The Joint Committee staff believes that stronger measures are necessary to discourage transactions that lack a non-tax business purpose or economic substance. Such measures, however designed, must significantly increase the economic risk to taxpayers of entering into tax-motivated transactions. Under the present system, the expected tax benefits from these transactions typically far outweigh the associated costs. Taxpayers will continue to engage in tax-motivated transactions unless and until there is a meaningful change in this cost-benefit analysis. At a minimum, taxpayers that engage in tax-motivated transactions should be subject to substantial penalties.

2. Business purpose

The Joint Committee staff believes that attainment of financial statement benefits based solely on Federal income tax savings is not a valid business purpose for purposes of evaluating a transaction or arrangement under Federal income tax laws.

3. Accommodation parties

The tax laws should not permit the use of accommodation parties such as employees, consultants, or advisors, to serve as a party in a transaction or arrangement to permit a taxpayer to achieve Federal income tax benefits. The Joint Committee staff recommends that severe penalties be imposed on the accommodation party and on the taxpayer who engages the accommodation party.

4. Tax advisors

The Joint Committee staff is concerned about the willingness of tax advisors to render opinions that rely on factual representations that the advisor knows, or has reason to believe, are incorrect, incomplete, or inconsistent with the facts. Many tax-motivated transactions cannot occur without the complicity of a tax advisor who is aware of all the relevant facts, yet chooses to ignore them and instead relies on the taxpayer's purported factual representations. The Treasury Department and IRS should have a broad array of sanctions to impose on advisors who render such opinions, and they should impose stiff sanctions on these advisors (and when appropriate, on the advisor's employer or partners). In addition, the relevant State licensing

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authority should be notified when these sanctions are imposed, and the licensing authority also should discipline the advisor as appropriate.

5. Generally accepted accounting principles relating to accounting for Federal income taxes

The Joint Committee staff is concerned that businesses are engaging in tax-motivated transactions primarily to obtain financial accounting benefits. The accounting benefits result solely from the manipulation of the Federal income tax laws to create permanent book-tax differences. The Joint Committee staff further believes that this activity may be occurring because of certain aspects of the financial accounting rules governing accounting for income tax expense. Thus, the Joint Committee staff recommends that those responsible for promulgating the accounting standards evaluate whether changes are warranted to the rules governing accounting for income taxes.

6. Disclosure of tax-motivated transactions

The Joint Committee staff is concerned that the use of multiple entities in connection with tax-motivated transactions, coupled with the inherent complexity of these transactions and the delayed timing of the tax benefits, makes it exceedingly difficult for the Treasury Department and the IRS to timely identify and properly evaluate these transactions. The Joint Committee staff believes that taxpayers should be required to make a detailed disclosure of any tax-motivated transaction on a timely basis, irrespective of whether the transaction has immediate tax return effect.

7. Continued use of certain structured transactions

The Joint Committee staff is concerned that the publication of this Report may encourage taxpayers and promoters to engage in transactions similar to those described in the Report. The Joint Committee staff recommends that the Congress and Treasury Department take appropriate action as soon as practicable.